2012

Annual Financial Report

Containing:

- Independent auditor’s opinion
- Consolidated financial statements
  as at and for the year ended December 31, 2012

www.investor.netia.pl

NETIA

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INDEPENDENT AUDITORS' OPINION

To the Shareholders and Supervisory Board of Netia S.A.

We have audited the attached consolidated financial statements of Netia Group ('the Group'), for which the holding company is Netia S.A. ('the Company'), which comprise the consolidated statement of financial position as at 31 December 2012 and the consolidated income statement, the consolidated statement of comprehensive income, the consolidated statement of changes in equity and the consolidated statement of cash flows for the year then ended, and notes to consolidated financial statements ("the attached consolidated financial statements").

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on the attached consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the attached consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the attached consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the attached consolidated financial statements present fairly, in all material respects, the financial position of the Group as of 31 December 2012, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the EU.

The convenience translations are disclosed as part of the consolidated financial statements. The convenience translation for the year ended 31 December 2012 has been presented in Euro, as a matter of arithmetic computation using the official rate of the National Bank of Poland at 31 December 2012 of PLN 4.0882 to EUR 1.00. We have not audited these translations and accordingly we do not report thereon. The Euro amounts presented in these consolidated financial statements should not be construed as a representation that the PLN amounts have been or could have been converted to Euro at this rate or at any other rate.

Ernst & Young Audit Sp zoo

Ernst &Young Audit sp. z o.o.

Warsaw, 20 February 2013

NETIA S.A.
CONSOLIDATED FINANCIAL STATEMENTS
As at and for the year ended December 31, 2012

Index to the consolidated financial statements

NETIA S.A.
CONSOLIDATED STATEMENT OF FINANCIAL POSITION
as at December 31, 2012

(All amounts in thousands, except as otherwise stated)

	Note	December 31, 2012 (PLN)	December 31, 2011 (PLN)	Convenience Translation December 31, 2012 (EUR)
ASSETS				
Non-current assets				
Property, plant and equipment	7	2,066,277	2,184,751	505,425
Intangible assets	8, 9	597,455	765,275	146,141
Investment property		-	26,399	-
Deferred income tax assets	32	101,687	111,784	24,873
Available for sale financial assets		115	115	28
Long term receivables	11	1	218	-
Prepaid expenses and accrued income	12	11,082	11,832	2,711
Total non-current assets		**2,776,617**	**3,100,374**	**679,178**
Current assets				
Inventories	10	2,094	5,314	512
Trade and other receivables	11	248,270	255,596	60,728
Current income tax receivables		518	262	127
Prepaid expenses and accrued income	12	33,660	30,091	8,233
Derivative financial instruments	15	-	2,723	-
Financial assets at fair value through profit and loss		15	16	4
Held to maturity investments		49	-	12
Restricted cash	13	2,263	2,263	554
Cash and short term deposits	13	142,702	156,509	34,906
		429,571	**452,774**	**105,076**
Assets held for sale	14	26,770	-	6,548
Total current assets		**456,341**	**452,774**	**111,624**
Total assets		**3,232,958**	**3,553,148**	**790,802**

Mirosław Godlewski
President of the Company

Jonathan Eastick
Member of the Management Board
Chief Financial Officer

Tom Ruhan
Member of the Management Board

Mirosław Suszek
Member of the Management Board

Warsaw, Poland
February 20, 2013

(All amounts in thousands, except as otherwise stated)

	Note	December 31, 2012 (PLN)	December 31, 2011 (PLN)	Convenience Translation December 31, 2012 (EUR)
EQUITY				
Share capital	16	386,281	391,602	94,487
Treasury shares	34	(106,814)	(49,582)	(26,127)
Supplementary capital		2,060,076	1,867,421	503,908
Retained earnings		(62,432)	251,012	(15,271)
Other components of equity		19,184	39,915	4,693
Equity attributable to equity owners		**2,296,295**	**2,500,368**	**561,690**
Non-controlling interests		-	5	-
Total equity		**2,296,295**	**2,500,373**	**561,690**
LIABILITIES				
Non-current liabilities				
Borrowings	18	384,452	514,584	94,039
Provisions	17	18,189	3,086	4,449
Deferred income tax liability	32	17,683	2,971	4,325
Deferred income	21	20,769	22,123	5,080
Derivative financial instruments	15	5,741	-	1,404
Other long term liabilities	19	4,232	9,392	1,035
Total non-current liabilities		**451,066**	**552,156**	**110,332**
Current liabilities				
Trade and other payables	19	260,108	263,226	63,624
Derivative financial instruments	15	7,268	84	1,778
Borrowings	18	166,197	180,593	40,653
Current income tax liabilities		1	1	-
Provisions	17	14,200	12,681	3,473
Deferred income	21	37,823	44,034	9,252
Total current liabilities		**485,597**	**500,619**	**118,780**
Total liabilities		**936,663**	**1,052,775**	**229,112**
Total equity and liabilities		**3,232,958**	**3,553,148**	**790,802**

(All amounts in thousands, except as otherwise stated)

	Note	Year ended December 31, 2012 (PLN)	Year ended December 31, 2011 (PLN)	Convenience Translation Year ended December 31, 2012 (EUR)
CONSOLIDATED INCOME STATEMENT				
Revenue	22	**2,121,356**	**1,618,803**	**518,898**
Cost of sales	23	(1,484,216)	(1,103,029)	(363,049)
Gross profit		**637,140**	**515,774**	**155,849**
Selling and distribution costs	24	(392,069)	(297,253)	(95,903)
General and administration costs	25	(207,610)	(152,473)	(50,782)
Other income	27	22,438	15,972	5,488
Other expenses	28	(5,634)	(4,204)	(1,378)
Other gains, net	29	3,974	4,205	972
Impairment losses	5	(79,203)	-	(19,374)
Reversal of impairment losses		-	220,677	-
Operating profit / (loss)		**(20,964)**	**302,698**	**(5,128)**
Finance income	30	6,271	18,288	1,534
Finance costs	30	(46,213)	(3,710)	(11,304)
Profit/ (loss) before income tax		**(60,906)**	**317,276**	**(14,898)**
Income tax charge	32	(26,798)	(68,490)	(6,555)
Profit/ (loss)		**(87,704)**	**248,786**	**(21,453)**
Profit/ (loss) attributable to:				
Owners of the Company		(87,704)	248,786	(21,453)
Non-controlling interest		-	-	-
		(87,704)	**248,786**	**(21,453)**
Earnings/ (loss) per share (expressed in PLN per share)				
- basic	33	(0.23)	0.64	(0.06)
- diluted	33	(0.23)	0.64	(0.06)

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

NETIA S.A.
CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME
for the year ended December 31, 2012

(All amounts in thousands, except as otherwise stated)

	Note	Year ended December 31, 2012 (PLN)	Year ended December 31, 2011 (PLN)	Convenience Translation Year ended December 31, 2012 (EUR)
CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME				
Profit /(loss)		**(87,704)**	**248,786**	**(21,453)**
Interest rate cash flow hedges	15	(9,421)	-	(2,304)
Foreign exchange rate cash flow hedges (acquisitions))	-	(203)	203	(50)
Foreign exchange rate cash flow hedges (equipment and construction contracts)	15	(4,195)	1,892	(1,026)
Income tax relating to components of other comprehensive income	32	2,626	(398)	642
Other comprehensive income/ (loss)		**(11,193)**	**1,697**	**(2,738)**
TOTAL COMPREHENSIVE INCOME/ (LOSS)		**(98,897)**	**250,483**	**(24,191)**
Total comprehensive income/(loss) attributable to:				
Owners of the Company		(98,897)	250,483	(24,191)
Non-controlling interest		-	-	-
		(98,897)	**250,483**	**(24,191)**

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

NETIA S.A.
CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
for the year ended December 31, 2012

(All amounts in thousands, except as otherwise stated)

				Supplementary capital			Other components of equity					
	Note	Share capital	Treasury shares	Share premium	Other supplementary capital	Retained earnings	Employee share option scheme	Hedging reserve	Other reserve	Total	Non-controlling interest	Total equity
		(PLN)	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)		
Balance as at January 1, 2012		**391,602**	**(49,582)**	**1,357,768**	**509,653**	**251,012**	**38,486**	**1,429**	**-**	**2,500,368**	**5**	**2,500,373**
Profit /(loss)for the period		-	-	-	-	(87,704)	-	-	-	(87,704)	-	(87,704)
Other comprehensive loss		-	-	-	-	-	-	(11,193)	-	(11,193)	-	(11,193)
Total comprehensive loss		-	-	-	-	(87,704)	-	(11,193)	-	(98,897)	-	(98,897)
Transfer of Netia's 2011 profit	16	-	-	-	225,004	(225,004)	-	-	-	-	-	-
Transfer of 2010 adjustment to Netia's 2009 and earlier profits		-	-	-	726	(726)	-	-	-	-	-	-
Repurchase of own shares	16	-	(106,814)	-	-	-	-	-	-	(106,814)	-	(106,814)
Redemption of own shares	16	(9,775)	49,582	(49,582)	-	-	-	-	9,775	-	-	-
Employee share option scheme:												
- value of services provided	16	-	-	-	-	-	1,774	-	-	1,774	-	1,774
- issuance of series K shares	16	4,454	-	16,633	-	-	(21,087)	-	-	-	-	-
Cost of issuance		-	-	(126)	-	-	-	-	-	(126)	-	(126)
Acquisition of non-controlling interest		-	-	-	-	(10)	-	-	-	(10)	(5)	(15)
Balance as at December 31, 2012		**386,281**	**(106,814)**	**1,324,693**	**735,383**	**(62,432)**	**19,173**	**(9,764)**	**9,775**	**2,296,295**	**-**	**2,296,295**

(All amounts in thousands, except as otherwise stated)

				Supplementary capital							
	Note	**Share capital**	**Treasury shares**	**Share premium**	**Other supplementary capital**	**Retained earnings**	**Employee share option scheme**	**Hedging reserve**	**Total**	**Non-controlling interest**	**Total equity**
		(PLN)	**(PLN)**	**(PLN)**	**(PLN)**	**(PLN)**	**(PLN)**	**(PLN)**	**(PLN)**		
Balance as at January 1, 2011		**389,459**	**-**	**1,356,678**	**242,621**	**269,258**	**39,798**	**(268)**	**2,297,546**	**-**	**2,297,546**
Profit for the period		-	-	-	-	248,786	-	-	248,786	-	248,786
Other comprehensive income		-	-	-	-	-	-	1,697	1,697	-	1,697
Total comprehensive income		-	-	-	-	248,786	-	1,697	250,483	-	250,483
Transfer of Netia's 2010 profit		-	-	-	267,032	(267,032)	-	-	-	-	-
Repurchase of own shares	16	-	(49,582)	-	-	-	-	-	(49,582)	-	(49,582)
Employee share option scheme:											
- value of services provided	16	-	-	-	-	-	1,974	-	1,974	-	1,974
- issuance of series K shares	16	2,143	-	1,143	-	-	(3,286)	-	-	-	-
Cost of issuance		-	-	(53)	-	-	-	-	(53)		(53)
Acquisition of subsidiary		-	-	-	-	-	-	-	-	5	5
Balance as at December 31, 2011		**391,602**	**(49,582)**	**1,357,768**	**509,653**	**251,012**	**38,486**	**1,429**	**2,500,368**	**5**	**2,500,373**

NETIA S.A.
CONSOLIDATED STATEMENT OF CASH FLOWS
for the year ended December 31, 2012

(All amounts in thousands, except as otherwise stated)

	Note	Year ended December 31, 2012 (PLN)	Year ended December 31, 2011 (PLN)	Convenience Translation Year ended December 31, 2012 (EUR)
Cash flows from operating activities:				
Profit/(loss)		**(87,704)**	**248,786**	**(21,453)**
Adjustments for:				
Depreciation and amortization	7, 9	482,491	308,756	118,020
Impairment loss	5	79,203	-	19,373
Reversal of impairment losses		-	(220,677)	-
Reversal of impairment charges for specific assets	7	(296)	(1,534)	(72)
Impairment charges for specific individual assets		4,611	4,122	1,128
Deferred income tax charge / (benefit)	32	27,111	16,410	6,632
Interest expense and fees charged on bank loans	30	43,185	2,491	10,563
Other interest charged/(earned)		501	(7,106)	123
Share-based compensation	16,37	1,913	3,191	468
Fair value losses /(gains) on financial assets / liabilities		1	(1)	-
Fair value losses /(gains) on derivative financial instruments		1,945	(1,464)	476
Foreign exchange losses/ (gains)		435	(970)	106
Gain on disposal of fixed assets		(21)	(2,743)	(5)
Changes in working capital	35	(11,989)	11,241	(2,933)
Tax expense relating to prior periods	32	-	58,325	-
Net cash provided by operating activities		**541,386**	**418,827**	**132,426**
Cash flows from investing activities:				
Purchase of fixed assets and computer software		(262,506)	(262,659)	(64,211)
Purchase of operational networks		-	(2,680)	-
Proceeds from sale of fixed assets		2,145	8,509	525
Purchase of ethernet operators, net of cash received	8, 35	(5,285)	(22,698)	(1,293)
Purchase of Dialog Group and Crowley, net of cash received		-	(972,287)	-
Purchase price adjustment for Crowley	8	(4,323)	-	(1,057)
Purchase of non-controlling interest		(15)	-	(4)
Proceeds from sale of investments		28	-	7
Purchase of treasury bonds / notes		(48)	(204,029)	(12)
Receipts from treasury bonds / notes		-	383,134	-
Net cash used in investing activities		**(270,004)**	**(1,072,710)**	**(66,045)**
Cash flows from financing activities:				
Government grants received		16,551	-	4,048
Proceeds from borrowings		-	700,000	-
Repurchase of own shares		(106,814)	(49,582)	(26,127)
Finance lease payments		(4,981)	(5,203)	(1,218)
Loan payments		(182,049)	(430)	(44,530)
Payments of interests, fees and interest rate swap settlements relating to bank loans		(26,212)	(8,963)	(6,412)
Net cash used in / provided by financing activities		**(303,505)**	**635,822**	**(74,239)**
Net change in cash and cash equivalents		**(32,123)**	**(18,061)**	**(7,858)**
Exchange (losses)/ gains on cash and cash equivalents		**(435)**	**970**	**(106)**
Cash and cash equivalents at beginning of period		156,509	173,600	38,283
Cash and cash equivalents at end of period	13	**123,951**	**156,509**	**30,319**

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

1. The Company and the Netia Group

Netia S.A. (the "Company" or "Netia") was formed in 1990 as a limited liability company under the laws of Poland and was transformed into a joint stock company in 1992. In 2003 a general meeting of shareholders adopted a resolution changing the Company's name from Netia Holdings S.A. to Netia S.A. The Company is incorporated and domiciled in Poland with its registered office located at ul. Poleczki 13, 02-822 Warsaw, Poland. The parent company is entered in the Register of Entrepreneurs kept by the District Court, XIII Economic Department of the National Court Register, Entry No. KRS 0000041649. The parent company was granted statistical REGON number 011566374. The parent company and other Group entities have an unlimited period of operation.

The consolidated financial statements of Netia S.A. for the year ended December 31, 2012 comprise the Company and its subsidiaries. A list of the Company's subsidiaries is set out in Note 2.

These consolidated financial statements were approved for issuance by the Company's Management Board on February 20, 2013.

The Company and its subsidiaries (together, the "Netia Group") is the largest alternative fixed-line telecommunication operator in Poland. The Netia Group provides various voice telephony and data transmission services. These services include switched, fixed-line voice telephone services (including domestic long-distance, international long-distance and fixed-to-mobile services), Integrated Services Digital Network ("ISDN"), Voice over Internet Protocol ("VoIP"), voice mail, leased lines and frame relay and MPLS services. The Netia Group also offers wholesale services (including the wholesale termination of in-bound traffic, ducts, dark fiber and co-location services), services based upon intelligent networks (free phone, split charge and premium rate services) and provides broadband Internet access with ADSL technology. These services are offered over Netia's own copper or fiber networks and, selectively, over network facilities leased from other operators.

Since 2006, the Netia Group has been providing voice and broadband services using WIMAX technology running over 3.6 – 3.8 GHz frequencies that were acquired by the Group in 2005.

Taking advantage of the opportunities arising from changes in the regulatory environment, the Company concluded a bitstream access agreement ("BSA") with Telekomunikacja Polska S.A. ("TP SA") and commercially launched its broadband Internet access services over TP SA's network in January 2007. During 2007 the Company began offering Netia voice services to TP SA customers including the arrangement whereby the customer pays a monthly fee to Netia as well as the hitherto call by call charges. Netia pays a line rental fee to TP SA under the Wholesale Line Rental (WLR) administrative decision issued by the telecommunications regulator (Urząd Komunikacji Elektronicznej, "UKE"). During 2008 Netia began to install its own equipment in the TP SA network nodes using a form of regulated access called Local Loop Unbundling (LLU) and began connecting customers using this form of regulated access.

In September 2008 the Company acquired Tele2 Polska Sp. z o.o. ("Tele2 Polska", merged with Netia in February 2009), a company providing voice and broadband services Poland-wide on the basis of regulated access to the TP SA network, including call by call, WLR and BSA.

The Netia Group is also expanding the footprint of its own network and broadband customer base by acquiring local fast ethernet operators. Since the beginning of 2007, the Netia Group has acquired 37 (not in thousands) such operators with a total of 129,808 (not in thousands) active customers. Additionally, the Netia Group has acquired 10,723 (not in thousands) customers and local access networks from other Ethernet operators.

To further broaden Netia's product offer, including convergent services, Netia started offering mobile services in September 2008. Netia provides its mobile service based on a Mobile Service Provider Agreement with P4 Sp. z o.o. ("P4"), enabling Netia to buy mobile services wholesale from P4 and resell them as Netia branded mobile services. In the third quarter of 2009, the scope of this cooperation was expanded to cover mobile broadband services as well as mobile handset based voice and data services.

Netia introduced IPTV services into its offering during 2011 and is gradually upgrading its copper and Ethernet access networks using VDSL and fibre to the building (FTTB) technology to deliver faster broadband.

The Netia Group is also engaged in the installation and supply of specialized mobile radio communication services (public trunking) in Poland through its subsidiary UNI-Net Poland Sp. z o.o. (established in May 2009 through a corporate separation from UNI-Net Sp. z o.o.).

In December 2011 Netia acquired Telefonia DIALOG S.A. ("Dialog",which was transformed into Telefonia DIALOG Sp. z o.o. on April 30, 2012) with its subsidiaries Avista Media Sp. z o.o. ("Avista", merged with Dialog in July 2012) and Petrotel Sp. z o.o. ("Petrotel") (together, the "Dialog Group") and Crowley Data Poland Sp. z o.o ("Crowley", later CDP Netia Sp. z o.o., merged with Netia in August 2012), two other Polish alternative operators, which increased materially the size of the Netia Group. Dialog and Petrotel provide a similar range of telecommunication services to Netia and serve business and residential customers. Crowley was providing telecommunications services exclusively to business customers. Avista was providing call center services mainly for Dialog but also for some third party customers.

The Company's ordinary shares have been listed on the Warsaw Stock Exchange ("WSE") since July 2000. The Company's shares are currently a component of the mWIG40 index comprising companies of medium capitalization. The Company is subject to periodic reporting requirements under the Polish regulations regarding reporting for companies listed on the WSE.

Going concern

As at December 31, 2012, the Group's equity amounted to PLN 2,296,295 and the Netia Group had net working capital of PLN 118,190 inclusive of cash available of PLN 142,702. As at December 31, 2012 the Netia Group had senior secured debt of PLN 531,898. Netia's operations were free cash flow generative in 2012 and Management expects this to continue over the medium term. Based on this position, the Management does not believe that events or conditions exist which may cast significant doubt on the Company's ability to continue as a going concern.

(All amounts in thousands, except as otherwise stated)

2. Significant subsidiaries of the Company

The consolidated financial statements include the accounts of the Company's directly or indirectly held subsidiaries:

Subsidiary	Ownership Percentage December 31, 2012	Ownership Percentage December 31, 2011
Subsidiaries held directly:		
CDP Netia Sp. z o.o.[1]	N/A	100
InterNetia Holdings Sp. z o.o.	100	100
In2Loop Sp. z o.o. in liquidation[2]	N/A	100
Netia Brand Management Sp. z o.o.	100	100
Net 2 Net Sp. z o.o.	100	100
Netia 2 Sp. z o.o.	100	100
Telefonia DIALOG Sp. z o.o.	100	100
Subsidiaries held indirectly:		
Avista Media Sp. z o.o.[3]	N/A	100
ComNet ITT Sp. z o.o.[4]	N/A	100
E-IMG Multimedia Sp. z o.o.[4]	N/A	100
Elpro-Elektronika Profesjonalna Waldemar Nitka Sp. z o.o.[4]	N/A	N/A
Internetia Sp. z o.o.	100	100
Netsystem Sp. z o.o.[4]	N/A	100
Petrotel Sp. z o.o.	100	99,99
Saite Sp. z o.o.[4]	N/A	100
Sanetja Sp. z o.o.	100	N/A
Sieci Multimedialne Intergeo Sp. z o.o.[4]	N/A	100
Silesia Multimedia Sp. z o.o.[4]	N/A	100
STI Sp. z o.o.	100	N/A
UNI-Net Poland Sp. z o.o.	100	100
ZAX.EU Sp. z o.o.[4]	N/A	100

[1] – merged with the Company
[2] – liquidated on December 28, 2012
[3] – merged with Dialog
[4] – merged with Internetia Sp. z o.o.

Shares held by Netia in its subsidiaries give the Company a corresponding share of votes at the shareholders' meetings.

All the Company's subsidiaries are incorporated in Poland.

3. Summary of significant accounting policies

Basis of preparation

Following European Union regulations, commencing January 1, 2005 Netia as a public company in Poland prepares consolidated financial statements, as required by the Accounting Act of September 29, 1994 (Journal of Laws of 2009, No. 152, item 1,223 with later amendments, "the Accounting Act") in accordance with International Financial Reporting Standards ("IFRS") as adopted by the European Union ("EU"). As of December 31, 2012, in light of the current process of IFRS endorsement in the EU and the nature of the Netia Group's activities, there is no difference between IFRS applied by the Netia Group and IFRS endorsed by the EU.

These consolidated financial statements have been prepared in accordance with IFRS as adopted by the EU, issued and effective as at the time of preparing these consolidated financial statements. The accounting policies used in the preparation of the consolidated financial statements are consistent with those used in the annual consolidated financial statements for the year ended December 31, 2011, except for new accounting standards adopted as of January 1, 2012.

Certain Group entities (acquired in 2011 and 2012) keep books of accounts in accordance with accounting policies specified in the Accounting Act and regulations issued based on that Act ("Polish Accounting Standards"). The consolidated financial statements include a number of adjustments not included in the books of account of the Group entities, which were made in order to bring the financial statements of those entities into conformity with IFRS.

The consolidated financial statements are prepared under the historic cost convention as modified by the revaluation of available-for-sale financial assets and financial assets and financial liabilities at fair value through profit and loss. However, until December 31, 1996, Poland was considered to be a hyperinflationary economy. The consolidated financial statements for the periods through that date were prepared under the historical cost convention as adjusted for the effects of inflation in accordance with IAS 29, "Financial Reporting in Hyperinflationary Economies". The inflated values in PLN at December 31, 1996 for balance sheet items became the new historical basis for subsequent periods.

The preparation of financial statements in conformity with IFRS as adopted by the EU requires the use of certain critical accounting estimates. The areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note 5.

Neither the Company's nor the Netia Group's activities are subject to any significant seasonal or cyclical trends of operations.

(All amounts in thousands, except as otherwise stated)

All Euro amounts shown as supplementary information in the consolidated financial statements have been translated from PLN only as a matter of arithmetic computation using the official rate of the National Bank of Poland at December 31, 2012 of PLN 4.0882 to EUR 1.00. These amounts are included for the convenience of the reader only. Such translation should not be construed as a representation that the PLN amounts have been or could be converted into Euros at this or any other rate.

Changes in estimates

In the year ended December 31, 2012 the Netia Group reassessed the useful lives of its property, plant and equipment and in consequence, for certain non-current assets the remaining period over which they will be depreciated was extended (in most cases) and depreciation rates were changed accordingly.

The following table summarizes main changes in these estimates:

Non-current assets	Main changes in the period of depreciation / amortization	Increase/ (decrease) in the depreciation charge recognized in current period	Relevant increase/ (decrease) in the depreciation charge for the remaining useful life
		(PLN)	(PLN)
Fixed telecommunications network	- useful lives of certain assets were extended until the end of 2015	(236)	236
Telecommunications equipment	- useful lives of certain assets were extended until the end of 2013	(372)	372
Machinery and equipment	- useful lives of certain assets were extended until the end of 2013 and 2015	(415)	415
Equipment (IT servers)	- useful lives of certain assets were extended until the end of 2013 and 2015	(19)	19
Total impact		**(1,042)**	**1,042**

New standards, interpretations and amendments to existing standards

Adoption of new accounting standards and interpretations

- Amendments to IFRS 7 "Disclosures - Transfers of Financial Assets". Amendments to the IFRS are to help users of financial statements evaluate the risk exposures relating to transfers of financial assets and the effect of those risks on an entity's financial position and will promote transparency in the reporting of transfer transactions, particularly those that involve securitization of financial assets. Entities are required to apply the amendments for annual periods beginning on or after 1 July 2011.

Standards, interpretations and amendments to published standards that are not yet effective

The following new standards, amendments to standards and interpretations have been issued but are not effective for 2012 and have not been adopted early:

- IFRS 9 "Financial Instruments" applicable for annual periods beginning on or after January 1, 2015. IFRS 9 is the Phase 1 of the Board's project to replace IAS 39. IFRS 9 improves and simplifies the approach for classification and measurement of financial assets compared with the requirements of IAS 39. This standard has not yet been endorsed by the EU.

- IFRS 10 "Consolidated Financial Statements ", which supersedes IAS 27 and SIC-12 "Consolidation – Special Purpose Entities", effective for annual periods beginning on or after 1 January 2013. IFRS 10 establishes principles for the presentation and preparation of consolidated financial statements when entity controls one or more other entities.

- IFRS 12 "Disclosure of Interests in Other Entities" effective for annual periods beginning on or after 1 January 2013. IFRS 12 applies to entities that have an interest in a subsidiary, a joint arrangement, an associate or an unconsolidated structured entity. In EU effective at the latest for annual periods beginning on or after January 1, 2014.

- IFRS 11 "Joint Arrangements" effective for annual periods beginning on or after 1 January 2013. IFRS 11 establishes principles for financial reporting by parties to a joint arrangement and supersedes IAS 31 "Interests in Joint Ventures" and SIC-13 "Jointly Controlled Entities – Non-Monetary Contributions by Venturers". In EU effective at the latest for annual periods beginning on or after January 1, 2014.

- IFRS 13 "Fair Value Measurement" applicable for annual periods beginning on or after 1 January 2013. IFRS 13 defines fair value, sets out a framework for measuring fair value and requires disclosures about fair value measurement. IFRS 13 applies to IFRSs that require or permit fair value measurement or disclosures about fair value measurements, except in specified circumstances.

- Amendments to IAS 27 reissued as IAS 27 "Separate Financial Statements", effective for annual periods beginning on or after 1 January 2013. Consolidation requirements previously forming part of IAS 27 (2008) have been revised and are now contained in IFRS 10. The amendments have not yet been endorsed by the EU. In EU effective at the latest for annual periods beginning on or after January 1, 2014.

- Amendments to IAS 28 reissued as IAS 28 " Investments in associates and Joint Ventures", effective for annual periods beginning on or after 1 January 2013. The amendments were issued for conforming changes based on the issuance of IFRS 10, IFRS 11 and IFRS 12. In EU effective at the latest for annual periods beginning on or after January 1, 2014.

- Amendments to IAS 19 "Employee Benefits", effective for annual periods beginning on or after 1 January 2013. These amendments finalise proposals in the exposure draft Defined Benefit Plans, published in April 2010 and proposals related to termination benefits in the exposure draft IAS 37 Provisions, Contingent Liabilities and Contingent Assets, published in June 2005. These amendments will make it easier for users of financial statements to understand how defined benefit plans affect an entity's financial position, financial performance and cash flows.

- IFRIC 20 "Accounting for stripping costs in the production phase of a surface mine", effective for annual periods beginning on or after 1 January 2013.

- Amendment to IAS 1 "Presentation of Financial Statements" effective for annual periods beginning on or after 1 July 2012. The amendments require entities to group items presented in Other Comprehensive Income based on whether they are potentially reclassifiable to profit or loss subsequently.

- Amendments to IFRS 7 "Financial Instruments: Disclosers: Offsetting Financial Assets and Financial Liabilities", effective for annual periods beginning on or after 1 January 2013.

- Amendments to IAS 32 "Financial Instruments: Presentation: Offsetting Financial Assets and Financial Liabilities", effective for annual periods beginning on or after 1 January 2014.

- Amendments to IFRS 1 "First–time Adoption of International Financial Reporting Standards: Government Loans" – effective for financial years beginning on or after 1 January 2013. The amendments have not yet been endorsed by the EU.

- Amendments to IFRS 10, IFRS 11 and IFRS 12 "Transition Guidance" - effective for financial years beginning on or after 1 January 2013.

- Improvements to IFRSs issued in May 2012 – effective for financial years beginning on or after 1 January 2013. The improvements have not yet been endorsed by the EU.

- Amendments to IAS 12 "Income Tax: Deferred Tax: Recovery of Underlying Assets", effective for financial years beginning on or after 1 January 2012. In EU effective at the latest for annual periods beginning on or after January 1, 2013.

- Amendments to IFRS 1 First-time Adoption of International Financial Reporting Standards: Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters, effective for financial years beginning on or after 1 July 2011. In EU effective at the latest for annual periods beginning on or after January 1, 2013.

- Amendments to IFRS 10, IFRS 12 and IAS 27 Investment Entities (issued on 31 October 2012) – effective for financial years beginning on or after 1 January 2014. The amendments have not yet been endorsed by EU.

Management is currently assessing the impact of the above standards and interpretations on the Netia Group's operations.

Consolidation

Subsidiaries

Business combinations are accounted for using the acquisition method. The cost of an acquisition is measured as the aggregate of the consideration transferred, measured at acquisition date fair value and the amount of any non-controlling interest in the acquiree. Acquisition costs incurred are expensed and included in administrative expenses.

When the Group acquires a business, it assesses the financial assets and liabilities assumed for appropriate classification and designation in accordance with the contractual terms, economic circumstances and pertinent conditions as at the acquisition date. This includes the separation of embedded derivatives in host contracts by the acquiree.

If the business combination is achieved in stages, the acquisition date fair value of the acquirer's previously held equity interest in the acquiree is remeasured to fair value at the acquisition date through profit or loss.

Any contingent consideration to be transferred by the acquirer is recognised at fair value at the acquisition date. Subsequent changes to the fair value of the contingent consideration which is deemed to be an asset or liability, is recognised in accordance with IAS 39 either in profit or loss or as a change to other comprehensive income. If the contingent consideration is classified as equity, it is not remeasured until it is finally settled within equity.

Indemnification assets and liabilities in business combinations

When an indemnification asset appears during purchase price allocation, it is treated as a separate element purchased by the Netia Group in addition to the business acquired. This asset is not offset against the contingent liability recognised during valuation of the acquired companies. Any amount received under the indemnity is treated as a realisation of that asset and is not adjusted against the cost of the business combination.

Contingent assets are recognized when it is virtually certain that inflow of economic benefits will arise. In situations where the Netia Group has agreed to share the benefits of such contingent assets with the seller, a corresponding liability is also recognized if it is probable that the outflow of future economic benefits will be required.

(All amounts in thousands, except as otherwise stated)

Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the Management Board. The Management monitors the operating results of its customer segments separately for the purpose of making decisions about resource allocation and performance assessment.

Foreign currency translation

(a) Functional and presentation currency

Items included in the financial statements of each of the Netia Group's entities are measured using the currency of the primary economic environment in which the entity operates (the "functional currency"). The consolidated financial statements are presented in Polish Złoty ("PLN"), which is the Company's functional and presentation currency.

(b) Transactions and balances

Foreign currency transactions are translated into the functional currency at the exchange rates prevailing at the date of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognized in the income statement. As at each reporting day assets and liabilities denominated in foreign currencies are revalued at average exchange rates of the National Bank of Poland prevailing at the date of financial statement.

Property, plant and equipment

Property, plant and equipment are stated at historical cost less accumulated depreciation and accumulated impairment in value, plus related inflation adjustment through December 31, 1996. Fixed assets under construction represent the accumulation of costs associated with the construction of telecommunication and data transmission networks and other tangible fixed assets. The Netia Group includes in the construction cost of its networks all eligible borrowing costs and expenditures that are directly attributable to the acquisition or bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management. Costs relating to the fixed assets under construction are transferred to the related property, plant and equipment account and depreciation begins when they are available for use.

Subsequent costs are included in the carrying amount of the asset or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Netia Group and the cost can be measured reliably. All other repairs and maintenance costs are charged to the income statement during the financial period in which they are incurred.

Upon purchase, fixed assets are divided into components, which represent items with a significant value and to which a separate useful life can be allocated.

Depreciation expense is recorded utilizing the straight-line method over the estimated useful lives of the assets. These lives are summarized as follows:

	Term
Buildings	10 to 40 years
Fixed telecommunications network	15 to 40 years
Telecommunications equipment	5 to 15 years
Machinery and equipment	5 to 12 years
Office machinery and equipment	3 to 10 years
Vehicles	5 to 8 years

Land and fixed assets under construction are not depreciated.

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

An item of property, plant and equipment is derecognized upon disposal or when no future economic benefits are expected from its use or disposal.

Gains and losses on disposals are determined by comparing proceeds with the carrying amount. These are included in the income statement.

Investment property

Investment property consists of the former head office held to earn rentals or for capital appreciation (only an insignificant portion may be held for supply of services or for administrative purposes). Investment property is measured at cost less any accumulated depreciation and impairment losses.

Depreciation expense is recorded utilizing the straight-line method over the estimated useful lives of the assets. These lives are summarized as follows:

	Term
Buildings	10 to 40 years
Fixed telecommunications network	15 to 40 years
Office machinery and equipment	3 to 10 years

Land is not depreciated.

Non-current assets classified as held for sale

Non-current assets are classified as held for sale and stated at the lower of carrying amount and fair value less costs to sell if their carrying amount is recovered principally through a sale transaction rather than through 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.

Leases

(a) Group as a lessee

Leases where the Netia Group has substantially all the risks and rewards of ownership are classified as finance leases. Finance leases are capitalised at the lease's inception at the lower of the fair value of the leased property and the present value of the minimum lease payments. Each lease payment is allocated between the liability and finance charges. The corresponding rental obligations, net of finance charges, are included in other payables. The interest element of the finance cost is charged to the income statement over the lease period. The property, plant and equipment acquired under finance leases are depreciated over the useful life of the asset. If there is no reasonable certainty that the Netia Group will obtain ownership by the end of the lease term, the asset is depreciated over the shorter of the lease term and its useful life.

Operating lease payments are recognized as an expense in the income statement on a straight line basis over the lease term.

(b) Group as a lessor

Leases where a significant portion of the risks and rewards of ownership are retained by the Group (the lessor) are classified as operating leases. Initial direct costs incurred in negotiating an operating lease are added to the carrying amount of the leased asset and recognized over the lease term on the same bases as rental income. Contingent rents are recognized as revenue in the period in which they are earned.

Intangible assets

(a) Licenses and license fee liabilities

Licenses are stated at cost less accumulated amortization and impairment losses. If payment for the license is deferred beyond normal credit terms, its cost is the net present value of the obligation. The present value of the obligation is calculated using the Netia Group's effective borrowing rates at the time the license was granted. Any differences between the nominal price of the license and its present value are treated as interest costs. Interest costs are capitalized until substantially all the activities to prepare the asset for its intended use are complete and are then recognized as interest expense over the period of the obligation. Amortization of the license also commences once the related network is capable of operating in the manner intended by management and is calculated on a straight-line basis until the end of the grant period. The amortization period is 12 to 15 years. As at December 31, 2012 the Netia Group possessed only telecommunication licenses.

(b) Goodwill

Goodwill is initially measured at cost being the excess of the aggregate of the consideration transferred and the amount recognised for non-controlling interest over the net identifiable assets acquired and liabilities assumed. If this consideration is lower than the fair value of the net assets of the subsidiary acquired, the difference is recognised in profit or loss.

After initial recognition, goodwill is measured at cost less any accumulated impairment losses. For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's cash-generating units that are expected to benefit from the combination, irrespective of whether other assets or liabilities of the acquiree are assigned to those units

Where goodwill forms part of a cash-generating unit and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured based on the relative values of the operation disposed of and the portion of the cash-generating unit retained.

(c) Computer software costs

Acquired computer software licenses are capitalized on the basis of the costs incurred to acquire and bring into use the specific software. These costs are amortized over their estimated useful lives (up to 5 years).

Costs associated with maintaining computer software programmes are recognized as an expense as incurred. Costs that are directly associated with the production of identifiable and unique software products controlled by the Netia Group and that will probably generate economic benefits, exceeding costs, beyond one year, are recognized as intangible assets. Direct costs include staff costs of the software development team and an appropriate portion of relevant overheads. Computer software development costs, recognized as assets, are amortized using the straight-line method over their estimated useful lives, not exceeding a period of 5 years.

(d) Customer relationships

Customer relationships acquired separately are measured on initial recognition at cost. The cost of customer relationship acquired in a business combination is recognized at fair value as at the date of acquisition. Customer relationships are amortized using the straight-line method over their estimated useful lives of 3 - 5 years.

Impairment of non-financial assets

Intangible assets that have an indefinite useful life are not subject to amortisation and are tested annually for impairment. Assets that are subject to amortization are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognized for the amount by which the carrying amount of the asset exceeds its recoverable amount, which is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash inflows (cash-generating units).

An assessment is made at each reporting date as to whether there is any indication that previously recognized impairment losses relating to non-financial assets other than goodwill may no longer exist or may have decreased. If such indication exists, the recoverable amount is estimated. A previously recognized impairment loss is reversed only if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognized. If this is the case, the carrying amount of the asset is increased to its recoverable amount. That increased carrying amount cannot exceed the lower of its recoverable amount and the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognized for the asset in prior years. Such a reversal is recognized in the income statement. After such a reversal the depreciation charge for the asset is adjusted in future periods to allocate the asset's revised carrying amount, less any residual value, on a systematic basis over its remaining useful life.

Financial assets

The Netia Group classifies its financial assets in the following categories: available-for-sale financial assets, financial assets at fair value through profit and loss, held-to-maturity investments and loans and receivables.

(a) Available-for-sale financial assets

Available-for-sale financial assets are non-derivative assets that are either designated in this category or not classified in any of the other categories. They are included in non-current assets unless Management intends to dispose of the financial assets within 12 months of the balance sheet date.

(b) Financial assets at fair value through profit and loss

This category has two sub-categories: financial assets held for trading, and those designated at fair value through profit or loss at inception. A financial asset is classified as held for trading if acquired principally for the purpose of selling in the short term. Financial assets, designated as at fair value through profit or loss at inception, are those that are managed and their performance is evaluated on a fair value basis, in accordance with the Netia Group's documented investment strategy. Information about these financial assets is provided internally on a fair value basis to the Netia Group's key management personnel. Derivatives are classified as held for trading unless they are designated as hedges. Assets in this category are classified as current if they are either held for trading or are expected to be realized within 12 months of the balance sheet date.

(c) Held-to-maturity investments

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that Management has the positive intention and ability to hold to maturity. Held-to-maturity financial assets are included in non-current assets, except for those with maturities less than 12 months from the balance sheet date, which are classified as current assets.

(d) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise when the Company provides money directly to a debtor with no intention of trading the receivable. They are included in current assets, except for maturities greater than 12 months after the balance sheet date. These are classified as non-current assets. Loans and receivables are classified as "trade and other receivables" in the balance sheet.

Purchase and sales of financial assets are recognized at the trade date on which the Group commits to purchase or sell the asset. Financial assets are initially recognized at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets carried at fair value through profit or loss are initially recognized at fair value and transaction costs are expensed in the income statement. Financial assets are derecognized when the rights to receive cash flows from the investments have expired or have been transferred and the Netia Group has transferred substantially all risks and rewards of ownership.

Available-for-sale financial assets and financial assets at fair value through profit and loss are subsequently carried at fair value. Loans and receivables are carried at amortized cost using the effective interest method. Realized and unrealized gains and losses arising from changes in the fair value of the financial assets at fair value through profit and loss category are included in the income statement in the period in which they arise. Unrealized gains and losses arising from changes in the fair value of securities classified as available-for-sale are recognized in other comprehensive income. When securities classified as available-for-sale are sold or impaired, the accumulated fair value adjustments recognised in equity are included in the income statement as gains and losses from investment securities.

The Netia Group assesses at each balance sheet date whether there is objective evidence that a financial asset or a group of financial assets is impaired. In the case of equity securities classified as available for sale, a significant or prolonged decline in the fair value of the security below its cost is considered in determining whether the securities are impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognized in profit or loss – is removed from equity and recognized in the income statement. Impairment losses recognized in the income statement on equity instruments are not reversed through the income statement.

Derivative financial instruments and hedging activities

Derivatives are initially recognised at fair value on the date a derivative contract is entered into and are subsequently remeasured at their fair value.

The method of recognising the resulting gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged. The Netia Group designates certain derivatives as hedges of a particular risk associated with a recognised asset or liability or a highly probable forecast transaction (cash flow hedge).

The Netia Group documents, at the inception of the transaction, the relationship between hedging instruments and hedged items, as well as its risk management objectives and strategy for undertaking various hedging transactions. The Netia Group also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in cash flows of hedged items.

The full fair value of a hedging derivative is classified as a non-current asset or liability when the remaining maturity of the hedged item is more than 12 months; it is classified as a current asset or liability when the remaining maturity of the hedged item is less than 12 months.

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges are recognised in other comprehensive income. The gain or loss relating to the ineffective portion is recognised immediately in the income statement.

Amounts accumulated in equity are recycled in the income statement in the periods when the hedged item affects profit or loss. When the forecast transaction that is hedged results in the recognition of a non-financial asset (for example, purchases of fixed assets), the gains and losses previously deferred in equity are transferred from equity and included in the initial measurement of the cost of the asset. The deferred amounts are ultimately recognised in cost of goods sold in the case of inventory, or in depreciation in case of fixed assets.

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity and is recognised when the forecast transaction is ultimately recognised in the income statement. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to the income statement.

Gains and losses arising from changes in fair value of derivatives that economically hedge commercial transactions and were not designated as hedging instruments are presented within finance income / cost.

Inventories

Inventories are stated at the lower of cost and net realizable value, determined on a first-in first-out (FIFO) basis. Net realizable value is the estimated selling price in the ordinary course of business less applicable variable selling expenses.

Trade and other receivables

Trade and other receivables are recognized initially at fair value and subsequently measured at amortized cost using the effective interest method, less provision for impairment. If it is probable that the Netia Group will not be able to collect amounts due, according to the original terms of receivables, a provision for impairment is recognized in the income statement within "Selling and distribution costs". The amount of the provision is measured as the difference between the carrying amount of receivables and the present value of expected future cash flows, discounted at the effective interest rate. Any amounts reversed during the period are presented net with the impairment provisions. The carrying amount of the asset is reduced through the use of an allowance account. When a trade receivable is uncollectible, it is written off against the allowance account for trade receivables.

Cash and short term deposits

Cash and short term deposits include cash in hand, cash at bank and short-term deposits with an original maturity of three months or less. Cash is carried in the balance sheet at nominal value.

Share capital

All shares outstanding issued by the Company are classified as equity. External costs directly attributable to the issue of new shares are shown in equity as a deduction, net of tax, from the proceeds.

Share-based compensation

In 2012 he Netia Group operated two equity-settled, share-based compensation plans. Under these plans, options are granted to employees and board members of the managing bodies of the Company. Upon exercise of the options, the Company will issue to each exercising participant the number of shares representing the value equivalent to the participant's gain from the exercise of the options. No proceeds are received when the options are exercised.

Under the terms of the 2003 Plan, which expired on December 20, 2012, options vested based on a service criteria over a period of up to 3 years. The Netia Group's New Plan, which was accepted by the Annual Shareholders' Meeting on May 26, 2010 and expires on May 26, 2020, provides for vesting over a three year service period subject also to performance against goals set by the Supervisory Board.

The fair value of the employee services received in exchange for the grant of options is recognized as an employee benefit expense with a corresponding increase in other reserves. The total amount to be expensed over the vesting period is determined by reference to the fair value of the options granted. At each balance sheet date, the Company revises its estimate of the number of options that are expected to become exercisable based on estimates of leaver rates and fulfillment of performance criteria as applicable to the relevant plan. It recognizes the impact of the revision of original estimates, if any, in the income statement, with a corresponding adjustment to other reserves.

Retirement benefits

The Netia Group makes contributions to the Government's retirement benefit scheme at the applicable rate during the period based on gross salary payments (the “State Plan”).

The State Plan is funded on a pay-as-you-go basis, i.e. the Netia Group is only obliged to pay the contributions as they fall due based upon a percentage of salary and if the Netia Group ceases to employ members of the State Plan, it will have no obligation to pay any additional benefits. The State Plan is a defined contribution plan. The expense for the contributions is charged to the income statement in the same period as the related salary expense.

Employees are entitled to severance payments, which are paid on a one-off basis on retirement. The amount of retirement severance payments is defined in the Labour Code (an average monthly remuneration). The provision recognised in the Netia Group’s balance sheet in respect of retirement severance payments is the present value of the future obligation. This provision is calculated annually by independent actuaries using the projected unit credit method. The present value of the retirement severance payments is determined by discounting the estimated future cash outflows using interest rates of long-term bonds that are denominated in the currency in which the benefits will be paid. Actuarial gains and losses are charged or credited to the income statement.

Provisions

Provisions are recognized when the Netia Group has a present legal or constructive obligation as a result of past events, it is more likely than not that an outflow of resources will be required to settle the obligation, and the amount can be reliably estimated. Netia Group has recognized provisions for loss on rental contracts, a contract related to voice termination services (onerous contracts)legal claims and restructuring. Costs related to the ongoing activities of Netia Group are not provided in advance. Provisions are not recognized for future operating losses.

Provisions for onerous contracts are recognized when the expected benefits to be derived from a contract are less than the unavoidable costs of meeting the obligations under the contract.

Provisions for claims (legal, regulatory and contractual) are recognized when, based on all available evidence, it is more likely than not that a present obligation exists at the balance sheet date, the outflow of benefits relating to the claim is probable and it is possible to estimate this reliably.

Provisions for claims are recorded at the estimated value of costs to be incurred. Provisions for onerous contracts are calculated based on the value of future net cash outflows by the termination of a contract. If a contract is concluded for a period exceeding the 12-month period from the balance sheet date, the provision is recorded based on the discounted value of net cash outflows.

Employment restructuring and termination benefits provisions comprise employee termination payments and are recognized in the period in which Netia Group becomes legally or constructively committed to payment.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessment of the time value of money and the risk specific to the obligation. The increase in the provision due to passage of time is recognized as interest expense.

Trade and other payables

Trade and other payables are recognized initially at fair value and subsequently measured at amortised cost using the effective interest method.

Borrowings

Borrowings are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest method. Corresponding borrowing costs are recognized in profit or loss in the period in which they are incurred, unless they are capitalized.

Borrowings are derecognized when the obligation under the liability is discharged or cancelled or expires. Where existing borrowings are replaced by others 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 the income statement.

Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.

Borrowing costs

Borrowing costs incurred for the construction of any qualifying asset are capitalised during the period of time that is required to complete and prepare the asset for its intended use. Other borrowing costs are expensed.

Revenue

Revenue comprises the fair value of the consideration received or receivable for the sale of goods and services in the ordinary course of the Netia Group’s activities. Revenue is shown net of value added tax, rebates and discounts and after eliminated sales within the Group.

Telecommunications revenue includes direct voice products, such as monthly charges and calling charges. Revenue from calling charges is recognized in the income statement at the time a call is made over the Netia Group’s network. Telecommunications revenue includes also services other than traditional direct voice, such as indirect voice, data transmission, interconnection, wholesale and other telecommunication services, as well as sales of goods. Other telecommunication revenue comprises intelligent network services, the provision of Internet dial-in services for Netia's indirect customers, Internet callback services, as well as other non-core revenues. Other telecommunication revenues are recognized in the income statement in the period to which the services relate.

Revenues relating to promotional offers are stated net of discounts. For certain commercial offers where customers are offered a free or significantly discounted service over a certain period in exchange for contracting for a fixed period (time-based incentives), the total revenue generated under the contract is spread over the fixed, non cancelable period of the contract, thereby creating accrued income.

Interconnection revenues are derived from calls and other traffic that originate in other domestic or foreign operators' networks but use the Netia Group's network. The Netia Group receives interconnection fees based on agreements entered into with other telecommunication operators. These revenues are recognized in the income statement in the period the services relate to.

Radio communications revenue includes revenue from specialized mobile radio service (public trunking), through the Company's subsidiary UNI-Net Poland Sp. z o.o. Service revenues are recorded when the service is provided. Revenue from the sale of equipment is recorded when the equipment is delivered to the customer.

Other services revenue includes revenues from construction services rendered by the Company's subsidiary Petrotel Sp. z o.o.

Deferred income

Deferred income is recognized when the income is invoiced during an accounting period, but for which the Netia Group has still to supply the related services. It includes deferred revenues from rental contracts and subscriptions relating to future periods. Deferred income is classified as current if the service is expected to be supplied within 12 months of the balance sheet date.

Deferred income also includes government grants relating to property, plant and equipment. Government grants are credited to the income statement on a straight-line basis over the expected lives of the related assets.

Interconnection charges

Interconnection with other telecommunication operators is required to complete calls that originate in but terminate outside of the Netia Group's network or originate outside the network and terminate within it, or are only transferred through the Netia Group's network. The Netia Group pays interconnection charges based on agreements entered into with other telecommunication operators.

Subscriber acquisition costs

Subscriber acquisition costs are recognized as an expense of the period in which they are incurred. Customer premises equipment ("CPE") sold to the customer when installed is expensed as part of the subscriber acquisition costs whereas CPE that remains the property of the Group is capitalized as a fixed asset.

Interest income

Interest income is recognized on a time-proportion basis using the effective interest method. Interest income on impaired loans is recognized either as cash is collected or on a cost-recovery basis as conditions warrant.

Interest and foreign exchange gains / (losses)

The amounts of interest and foreign exchange gains / (losses), which do not relate to debt and management of cash and cash equivalents are presented at appropriate categories of revenues and operating income/expenses.

Current and deferred income taxes

The tax expense for the period comprises current and deferred tax. Tax is recognised in the income statement, except to the extent that it relates to items recognised in other comprehensive income or directly in equity. In this case the tax is also recognised in other comprehensive income or directly in equity, respectively.

The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the balance sheet date in Poland where the company's subsidiaries operate and generate taxable income.

Deferred income tax is provided, using the liability method, on all temporary differences arising between the tax bases of assets and liabilities and their carrying values for financial reporting purposes and for tax losses. Currently enacted tax rates are used to determine deferred income tax. The principal temporary differences arise from different valuations of depreciable assets and accruals for tax and accounting purposes.

Deferred income tax assets are recognized to the extent that it is probable that future taxable profit will be available against which temporary differences can be utilized based on the estimated taxable profits to be generated over the following five years. Deferred income tax assets are also recognized for unused tax losses carried forward and unused tax credits to the extent that it is probable that future taxable profit will be available against which the unused tax losses and unused tax credits can be utilized:

- except where the deferred income tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of deductible temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, deferred income tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

Deferred income tax liabilities are recognised for all taxable temporary differences:

- except where the deferred income tax liability arises from the initial recognition of goodwill, an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, except where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred income tax assets and deferred income tax liabilities are offset if, and only if, the Company or its subsidiaries have a legally enforceable right to set off current tax assets against current tax liabilities, and the deferred income tax assets and the deferred income tax liabilities relate to income taxes levied by the same taxation authority on the same taxable base.

Value Added Tax

Revenues, expenses and assets are recognised net of the amount of value added tax except:

- where the value added tax incurred on a purchase of assets or services is not recoverable from the taxation authority, in which case value added tax is recognised as part of the cost of acquisition of the asset or as part of the expense item as applicable; and
- receivables and payables, which are stated with the amount of value added tax included.

The net amount of value added tax recoverable from, or payable to, the taxation authority is included as part of receivables or payables in the balance sheet.

Dividend distribution

Dividend distributions to the Company's shareholders are recognized as a liability in the Netia Group's consolidated financial statements in the period in which the dividends are approved by the Company's General Shareholders' Meeting.

4. Financial risk management

Financial risk factors

The Netia Group's activities expose it to a variety of financial risks: market risk (including currency risk and price risk), credit risk and liquidity risk. The Netia Group's overall risk management program focuses on minimizing potential adverse effects of those risks on the financial performance of the Netia Group. The Netia Group uses derivative financial instruments to hedge certain risk exposure. The Management Board provides written principles for overall risk management, as well as written policies covering specific areas, such as use of derivative financial instruments, credit risk and price risk.

Market risk

- Currency risk:

The Netia Group's revenues and costs are predominately denominated in Polish Złoty, other than some payments made under equipment and construction contracts, which are mainly linked to Euro and U.S. Dollars. In order to mitigate the currency risk the Netia Group sometimes holds deposits in Euro and U.S. Dollars for servicing those payments. Furthermore, in the year ended December 31, 2012 the Company entered into several forward transactions to hedge exposure against currency risk related to planned capital expenditures and expected operational expenses which are either payable in foreign currencies or priced in foreign currencies.

At December 31, 2012, if the Polish Złoty had weakened (strengthened) by 1% against the Euro with all other variables held constant, consolidated loss for the year ended December 31, 2012 would have been PLN 5 lower (higher), mainly as a result of foreign exchange gains (losses) on translation of Euro denominated Euro denominated cash deposits and trade receivables, partially offset by Euro denominated trade and investment payables. Furthermore, at December 31, 2012, the hedging reserve in shareholders' equity would have been PLN 309 higher (lower) and the consolidated loss for the year ended December 31, 2012 would have been PLN 140 lower (higher), as a result of fair value gains (losses) on Euro denominated forward contracts.

At December 31, 2011, if the Polish Złoty had weakened (strengthened) by 1% against the Euro with all other variables held constant, consolidated profit for the year ended December 31, 2011 would have been PLN 49 lower (higher) , mainly as a result of foreign exchange losses (gains) on translation of Euro denominated trade and investment payables, partially offset by Euro denominated cash deposits and trade receivables. Furthermore, at December 31, 2011, the hedging reserve in shareholders' equity would have been PLN 169 higher (lower) and the consolidated profit for the year ended December 31, 2011 would have been PLN 134 higher (lower), as a result of fair value gains (losses) on Euro denominated forward contracts.

At December 31, 2012, if the Polish Złoty had weakened (strengthened) by 1% against the U.S. Dollar with all other variables held constant, consolidated loss for the year ended December 31, 2012 would have been PLN 43 lower (higher), mainly as a result of foreign exchange gains (losses) on translation of U.S. Dollar denominated cash deposits and trade receivables, partially offset by U.S. Dollar denominated trade and investment payables. Furthermore, at December 31, 2012, the hedging reserve in shareholders' equity would have been PLN 186 higher (lower) and the consolidated loss for the year ended December 31, 2012 would have been PLN 52 lower (higher), as a result of fair value gains (losses) on U.S. Dollar denominated forward contracts.

At December 31, 2011, if the Polish Złoty had weakened (strengthened) by 1% against the U.S. Dollar with all other variables held constant, consolidated profit for the year ended December 31, 2011 would have been PLN 71 higher (lower), mainly as a result of foreign exchange gains (losses) on translation of U.S. Dollar denominated cash deposits and trade receivables, partially offset by U.S. Dollar denominated trade and investment payables. Furthermore, at December 31, 2011, the hedging reserve in shareholders' equity would have been PLN 154 higher (lower) and the consolidated profit for the year ended December 31, 2011 would have been PLN 47 higher (lower), as a result of fair value gains (losses) on U.S. Dollar denominated forward contracts.

(All amounts in thousands, except as otherwise stated)

- Interest rate risk:

The Group's exposure to the risk of changes in market interest rates relates primarily to the Group's long-term loan and finance lease obligations with floating interest rates. If the market interest rates had been 50 basis points higher (lower) during the year ended December 31, 2012, interest costs relating to bank loan and finance lease obligations would have been PLN 3,127 higher (lower). In January 2012 the Company entered into IRS contracts hedging interest rate risk associated with interest payments (See Note 15 Other financial instruments). As a result of these transactions the effect of a 50 basis point higher/ (lower) market interests rate would have decreased from PLN 3,127 higher/ (lower) to 1,630 higher/(lower).

If the market interest rates had been 50 basis points higher (lower) during the year ended December 31, 2011, interest costs relating to bank loan and finance lease obligations would have been PLN 178 higher (lower). These amounts reflect the fact that the long term loan was outstanding from December 15, 2011. If the bank loan had been drawn on January 1, 2011 and market interest rates had been 50 basis points higher (lower) during the year ended December 31, 2011, interest costs relating to the bank loan and finance lease obligations would have been PLN 3,282 higher (lower). If the IRS contracts were concluded on January 1, 2011, as a result of IRS contracts, the annualised effect of a 50 basis point higher/ (lower) market interests rate would have decreased from PLN 3,282 higher/ (lower) to 1,783 higher/(lower). The above analysis holds interests earned on the Group's deposits constant.

Credit risk

Credit risk arises from cash and cash equivalents, including deposits with banks, as well as credit exposures to customers, including outstanding receivables.

The Netia Group had no significant concentrations of credit risk throughout the year 2012. Cash deposits are limited to high credit quality financial institutions. The Netia Group has a large number of customers, nationally dispersed, and there are policies in place to ensure that sales of services to significant customers are preceded by appropriate verification of their credit history. For wholesale (in particular international carriers) and large business customers credit rating and scoring tools are used. For these customers transactions are only concluded with recognised, creditworthy counterparties or credit collaterals are established. In addition receivables from the bulk business are managed separately. Retail customers verification and dunning processes are more automatic and base on CRM and billing systems functionalities. Utilization of the usage limits, sales limits and receivables balances are monitored on an ongoing basis and if necessary further business with customer that exceeds its limit is ceased.

Liquidity risk

Management monitors rolling forecasts of the Netia Group's liquidity reserves on the basis of expected cash flow. The Company invests surplus cash in interest bearing current accounts, time deposits and marketable securities, choosing instruments with appropriate maturities or sufficient liquidity to provide sufficient cash to service forecasted payments.

The table below analyses the Netia Group's non-derivative financial liabilities into relevant maturity groupings based on the remaining period from the balance sheet to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows. Balances due within 12 months equal their nominal values as the impact of discounting is not significant.

	Less than 1 year (PLN)	Between 1 and 2 years (PLN)	Between 2 and 5 years (PLN)	Over 5 years (PLN)	Total (PLN)	Net carrying amount (PLN)
As at December 31, 2012						
Trade and other payables excluding statutory liabilities	241,092	773	1,475	-	243,340	246,915
Bank borrowings	199,181	152,020	280,107	-	631,308	550,649
Total	**440,273**	**152,793**	**281,582**	**-**	**874,648**	**797,564**

	Less than 1 year (PLN)	Between 1 and 2 years (PLN)	Between 2 and 5 years (PLN)	Over 5 years (PLN)	Total (PLN)	Net carrying amount (PLN)
As at December 31, 2011						
Trade and other payables excluding statutory liabilities	233,491	4,919	803	-	239,213	244,378
Bank borrowings	229,433	165,647	439,985	-	835,065	695,177
Total	**462,924**	**170,566**	**440,788**	**-**	**1,073,871**	**939,555**

The table below analyses the Netia Group's derivative financial instruments with a negative fair value, that will be settled on a net basis, based on their contractual maturities. The table presents the gross undiscounted cash flows and a reconciliation of those amounts to their carrying amounts.

(All amounts in thousands, except as otherwise stated)

As at December 31, 2012	Less than 1 year (PLN)	Between 1 and 2 years (PLN)	Between 2 and 5 years (PLN)	Over 5 years (PLN)
EUR forward contracts				
Inflows	45,713	-	-	-
Outflows	(47,593)	-	-	-
Net	(1,880)	-	-	-
Discounted at the applicable interbank rates	(1,851)	-	-	-
USD forward contracts				
Inflows	24,239	-	-	-
Outflows	(26,006)	-	-	-
Net	(1,767)	-	-	-
Discounted at the applicable interbank rates	(1,735)	-	-	-
IRS contracts				
Inflows	8,431	5,840	5,129	-
Outflows	(12,208)	(9,012)	(8,061)	-
Net	(3,777)	(3,172)	(2,932)	-
Discounted at the applicable interbank rates	(3,681)	(3,063)	(2,678)	-

As at December 31, 2011	Less than 1 year (PLN)	Between 1 and 2 years (PLN)	Between 2 and 5 years (PLN)	Over 5 years (PLN)
EUR forward contracts				
Inflows	11,582	-	-	-
Outflows	(11,661)	-	-	-
Net	(79)	-	-	-
Discounted at the applicable interbank rates	(76)	-	-	-
USD forward contracts				
Inflows	5,723	-	-	-
Outflows	(5,732)	-	-	-
Net	(9)	-	-	-
Discounted at the applicable interbank rates	(8)	-	-	-

Fair value estimation

Effective January 1, 2009, the Netia Group adopted the amendment to IFRS 7 for financial instruments that are measured in the balance sheet at fair value. This requires disclosure of fair value measurements by level of the following fair value measurement hierarchy:

- quoted prices (unadjusted) in active markets for identical assets or liabilities (level 1).
- 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 2).
- inputs for the asset or liability that are not based on observable market data (that is, unobservable inputs) (level 3).

The following table presents the Netia Group's assets and liabilities that are measured at fair value at December 31, 2012:

	Level 1 (PLN)	Level 2 (PLN)	Level 3 (PLN)	Total balance (PLN)
Assets				
Financial assets at fair value through profit or loss				
- Securities	15	-	-	15
- Derivatives	-	-	-	-
Derivatives used for hedging	-	-	-	-
Available-for-sale financial assets	-	-	115	115
Total assets	**15**	**-**	**115**	**130**
Liabilities				
Financial liabilities at fair value through profit or loss				
- Trading derivatives	-	946	-	946
Derivatives used for hedging	-	12,063	-	12,063
Total liabilities	**-**	**13,009**	**-**	**13,009**

(All amounts in thousands, except as otherwise stated)

The following table presents the Netia Group's assets and liabilities that are measured at fair value at December 31, 2011:

	Level 1	**Level 2**	**Level 3**	**Total balance**
	(PLN)	**(PLN)**	**(PLN)**	**(PLN)**
Assets				
Financial assets at fair value through profit or loss				
- Securities	16	-	-	16
- Derivatives		1,031		1,031
Derivatives used for hedging	-	1,692	-	1,692
Available-for-sale financial assets	-	-	115	115
Total assets	**16**	**2,723**	**115**	**2,854**
Liabilities				
Financial liabilities at fair value through profit or loss				
- Trading derivatives	-	32	-	32
Derivatives used for hedging	-	52	-	52
Total liabilities	**-**	**84**	**-**	**84**

The fair value of financial instruments traded in active markets (such as equity securities) is based on quoted market prices at the balance sheet date. The fair value of financial instruments that are not traded in an active market is determined by using valuation techniques. The fair value of forward currency contracts is determined using quoted forward exchange rates at the balance sheet date. Estimated discounted cash flows are used to determine fair value for the remaining financial instruments.

The nominal value less impairment provision of receivables and liabilities with a maturity of less than one year are assumed to approximate their fair values.

The carrying amount of the long-term borrowings approximates their fair value and the discount rate for the fair value calculation approximates the effective interest rate.

Capital risk management

The Netia Group's objectives when managing capital are to safeguard the Netia Group's ability to continue as a going concern in order to provide returns for shareholders and to maintain an optimal capital structure to reduce the cost of capital. In order to maintain or adjust the capital structure, the Netia Group may return capital to shareholders, issue new shares or sell assets to reduce debt.

Consistent with others in the industry, the Netia Group monitors capital on the basis of the gearing ratio. This ratio is calculated as net debt divided by total capital employed. Net debt is calculated as total borrowings, as shown in the consolidated balance sheet, less cash and cash equivalents. Total capital employed is calculated as equity, as shown in the consolidated balance sheet, plus net debt.

The gearing ratio as at December 31, 2012 was 14.5% as compared to 17.7% as at December 31, 2011.

Financial instruments by category

December 31, 2012	Loans and receivables	Assets at fair value through profit and loss	Derivatives used for hedging	Available for sale financial assets	Held to maturity investments	Total
	(PLN)	**(PLN)**	**(PLN)**	**(PLN)**	**(PLN)**	**(PLN)**
Financial assets						
Available-for-sale financial assets	-	-	-	115	-	115
Trade and other receivables excluding statutory receivables	245,317	-	-	-	-	245,317
Derivative financial instruments	-	-	-	-	-	-
Financial assets at fair value through profit or loss	-	15	-	-	-	15
Held to maturity investments	-	-	-	-	49	49
Restricted cash	2,263	-	-	-	-	2,263
Cash and short term deposits	142,702	-	-	-	-	142,702
Total financial assets	**390,282**	**15**	**-**	**115**	**49**	**390,461**

(All amounts in thousands, except as otherwise stated)

December 31, 2012	Liabilities at fair value through profit and loss	Derivatives used for hedging	Other financial liabilities at amortised cost	Finance leases	Total
	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)
Financial liabilities					
Finance leases	-	-	-	3,483	3,483
Trade and other payables excluding statutory liabilities	-	-	243,367	-	243,367
Derivative financial instruments	946	12,063	-	-	13,009
Borrowings	-	-	550,649	-	550,649
Other financial liabilities	-	-	66	-	66
Total financial liabilities	**946**	**12,063**	**794,082**	**3,483**	**810,574**

December 31, 2011	Loans and receivables	Assets at fair value through profit and loss	Derivatives used for hedging	Available for sale financial assets	Held to maturity investments	Total
	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)
Financial assets						
Available-for-sale financial assets	-	-	-	115	-	115
Trade and other receivables excluding statutory receivables	246,221	-	-	-	-	246,221
Derivative financial instruments	-	1,031	1,692	-	-	2,723
Financial assets at fair value through profit or loss	-	16	-	-	-	16
Restricted cash	2,263	-	-	-	-	2,263
Cash and short term deposits	156,509	-	-	-	-	156,509
Total financial assets	**404,993**	**1,047**	**1,692**	**115**	**-**	**407,847**

December 31, 2011	Liabilities at fair value through profit and loss	Derivatives used for hedging	Other financial liabilities at amortised cost	Finance leases	Total
	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)
Financial liabilities					
Finance leases	-	-	-	7,388	7,388
Trade and other payables excluding statutory liabilities	-	-	236,919	-	236,919
Derivative financial instruments	-	84	-	-	84
Borrowings	-	-	695,177	-	695,177
Other financial liabilities	-	-	-	-	-
Total financial liabilities	**-**	**84**	**932,096**	**7,388**	**939,568**

5. Critical accounting estimates and judgments

The Company makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the current or next financial year are described below.

(a) Impairment of goodwill and other non-financial assets

The Netia Group tests annually whether goodwill has suffered any impairment and assesses at each balance sheet date whether there is any indication that an asset may be impaired.

For the purpose of impairment testing of goodwill the total amount of goodwill was allocated to the following operating segments:

	Home	SOHO / SME	Corporate	Carriers	Unallocated	Total goodwill
	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)
As at December 31, 2012	216,470	51,117	68,821	15,476	8,020	359,904
As at December 31, 2011	212,540	51,117	68,821	15,476	8,020	355,974

Goodwill in Unallocated represents goodwill assigned to Petrotel. Petrotel has been assigned to the unallocated segment as it continues to operate as a separate organization.

(All amounts in thousands, except as otherwise stated)

For the purpose of impairment testing of other non-financial assets the Management identified the entire Netia Group excluding the non-current assets of UNI-Net Poland Sp. z o.o. as one cash-generating unit ("CGU").

The recoverable amount of operating segments to which goodwill was allocated and the CGU is determined based on value-in-use calculations. These calculations use cash flow projections based on assumptions underlying the budget for the next year and the approved updated business plan covering a five-year period. Only currently active projects are included in projections. As a result, cash-flows from expected future acquisitions of Ethernet operators are not included in the cash-flow projections. Cash flows beyond the five-year period are extrapolated using a long term nominal growth rate of 0.0%, which is compatible with the industry projections for the operations concerned. The discount rate used of 10.8% (13.3% in 2011) is pre-tax and reflects Management assessment of the Company's weighted average cost of capital ("WACC"). In estimating WACC, Management assesses specific risks relating to the Netia Group operations, such as regulatory and technology risks, that may increase volatility of expected cash flows. The post-tax equivalent of the WACC used in value-in-use calculations is 9.64% (11.45% in 2011).

The impairment test of non-current assets showed that the recoverable amount, before tax, of the CGU was lower by 79,203 PLN than its carrying value and any adverse change in a key assumption would result in a higher impairment loss, whilst any favorable change would result in a lower or no impairment losses. The results of the test are highly sensitive to key assumptions as illustrated in the following table:

	Total impairment charge		
	(PLN)	(PLN)	(PLN)
Change in key assumptions	*increase*	*base*	*decrease*
WACC of 9.64% after-tax			
(increase / decrease by 1 percentage point)	319,041	79,203	-
Terminal growth rate of 0.0 % per annum			
(increase / decrease by 1 percentage point)	-	79,203	252,690
Cash flow projections 2013 - 2017			
(increase / decrease by 1% in each year)	52,773	79,203	105,833
Rate of Growth in BB and TV			
(increase / decrease by 10 % in each year)	72,955	79,203	85,541
Rate of drop in voice ARPU			
(increase / decrease by 2 percentage points in each year)	134,948	79,203	23,458
Regulated access rates			
(increase / decrease by 10 %)	243,150	79,203	-
Capital investment			
(increase / decrease by 10 % in each year)	261,590	79,203	-
Unallocated operating expenses			
(increase / decrease by 10 % in each year)	202,632	79,203	-

After reflecting the impairment loss of 79,203 in the goodwill allocated to segment Home, the recoverable amount of operating segments to which goodwill was allocated is higher than their carrying amounts and as a result no additional impairment loss has been recognized, in addition to the PLN 79,203 impairment loss described above. Sensitivity of the estimated pre-tax WACC of 10.8% applied to the discounted cash flows of each operating segment is summarized in the following table:

	Home	SOHO / SME	Corporate	Carriers
The Netia Group would have to recognise an additional impairment loss on goodwill assigned to segments if pre-tax WACC of 10.8% had been increased to	12.8%	20.3%	20.6%	20.2%

As a result of the impairment test of non-current assets as of December 31, 2012 the Netia Group has recognized 79,203 PLN of impairment losses in profit and loss during the year ended December 31, 2012.

The determination of impairment of goodwill and non-current assets is based on estimates of a large number of factors, such as changes in the current competitive conditions, expectations of growth in the telecommunications industry, regulated access and interconnection rates, cost of capital, technological obsolescence and other changes in circumstances that indicate an impairment exists. While the estimation of recoverable amount is based on current assessment of telecommunication market conditions and Management's best estimates and judgment, these estimates include a considerable amount of uncertainty. The actual outcome is uncertain and Management estimates may change in the future to reflect changes in the economic, technological and competitive environment, in which the Company operates.

(b) Deferred income tax

As part of the process of preparing the consolidated financial statements, the Management is required to estimate the Netia Group's income taxes. This process involves estimating the Netia Group's actual current tax exposure together with assessing temporary differences resulting from different treatment for tax purposes compared to the accounting treatment, such as the valuation of tangible fixed assets, accruals and provisions. These differences result in deferred income tax assets and liabilities, which are recognized in the consolidated balance sheet.

The deferred income tax calculation is based on the probability that future taxable profit will be available against which temporary differences, the unused tax losses and unused tax credits can be utilized. That calculation is based upon Management's estimates, which contain a considerable amount of uncertainty.

The Management is required to assess the likelihood that deferred income tax assets will be recovered from future taxable income, and to the extent the recovery is probable the deferred income tax assets are recognized. Significant management estimates are required in the valuation of the Netia Group's deferred income tax assets. These estimates take into consideration future taxable income projections, potential volatility in those projections, historical results and ongoing tax planning strategies. Management's assessment also considered such factors as: the stability and trend of past earnings, the nature of the business and industry, the economic environment in which the Netia Group operates and the stability of local legislation.

Based on the above assumptions and Management's assessment of the Netia Group tax position as of December 31, 2012, including tax projections, deferred income tax assets of PLN 101,687 and deferred income tax liabilities of PLN 17,683 were recognized in the consolidated statement of financial position.

Because of the above and also due to results of final reviews of our tax returns by tax authorities actual results may differ and our estimates may be altered to reflect changes in the economic, technological, regulatory and competitive environment in which the Netia Group operates. Consequently, we may need to adjust the valuation of our deferred income tax assets in the future, which could potentially materially impact our financial position and results of operations.

(c) Useful lives of non-current assets

Non-current assets, consisting primarily of property, plant and equipment and intangibles, comprise a significant portion of the Netia Group's total assets. Changes in the intended use of these assets, technological development and market conditions may cause the estimated period of use or the value of these assets to change. The Netia Group perform internal studies on an annual basis to confirm the appropriateness of its estimates of the economic useful lives for each category of current property, plant and equipment and other non-current assets. In determining the initial and remaining estimated useful life of a fixed asset, Management considers:
- the physical life of the asset;
- the technological life of the asset;
- the lives for similar productive assets; and
- the expected period that benefits will be derived from the asset.

The foregoing estimates and assumptions are inherently uncertain and subject to change, including as a result of factors outside the Netia Group's control. If the estimated useful life is shortened, the Netia Group depreciates or amortizes the remaining value of the asset over the revised remaining life of the asset. Likewise, if the anticipated technological or other changes occur more slowly than expected, the life of the group could be extended based on the life assigned to new assets added to the group. This could result in a reduction of depreciation and amortization expense in future periods. Management's estimates of useful lives affect the amount of gains or losses reported on the disposal or retirement of non-current assets.

(d) Customer relationships

In 2012 and previous years the Netia Group acquired Dialog Group, Crowley, Tele2 Polska, Pro Futuro and numerous internet service providers or local networks. In the purchase price allocation process the Netia Group identified customer relationships as an intangible asset. The fair value of customer relationships was estimated using the excess earnings method. This method considers the expected present value of the future economic benefits that will flow to an owner of an intangible asset. These analyses require certain assumptions including: the expected annual cash flows, the period in which the economic benefits will flow to the owner and the risk-adjusted discount rate.

6. Segment information

For management purposes, the Netia Group is organized into business units based on their customer segments, and has four reportable operating segments, as follows:
- Home, i.e. residential clients,
- SOHO / SME, i.e. small and medium enterprises,
- Corporate, i.e. large enterprises,
- Carriers, i.e. other telecom service providers.

Management monitors the operating results of its customer segments separately for the purpose of making decisions about resource allocation and performance assessment. Segment performance is evaluated based on EBITDA (defined as operating profit / (loss) excluding depreciation and amortization) and Adjusted EBITDA (defined as operating profit / (loss) excluding depreciation and amortization as well as significant one-off transactions) which is derived from the information in the consolidated financial statements. The Netia Group financing (including finance costs and finance income) and income taxes are managed on a group basis and are not allocated to operating segments. As Netia considers its network to be a single cash generating unit, non-current assets are not acquired by individual operating segments, but shared between them. In order to produce operating profit ("EBIT") for each segment, depreciation and amortization from the shared assets also has to be allocated. The Company uses expected future cash flows from each segment as a basis to allocate depreciation and amortization. The resulting allocations can be volatile between periods, but unlike EBITDA, Management does not place reliance on these segment EBIT results for decision making purposes.

In December 2011 Netia acquired the Dialog Group and Crowley. Customers of Dialog and Crowley have been allocated into their respective customers segments whilst Petrotel has been assigned to the unallocated segment as it continues to operate as a separate organization.

No operating segments have been aggregated to form the above reportable operating segments.

(All amounts in thousands, except as otherwise stated)

The following tables present revenue and profit / (loss) information regarding the Netia Group's operating segments for the years ended December 31, 2012 and 2011, respectively:

	Home	SOHO / SME	Corporate	Carriers	Total reportable segments	Unallocated	Total
	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)
Year ended December 31, 2012							
Revenue from external customers	**1,075,145**	**290,709**	**466,315**	**252,962**	**2,085,131**	**36,225**	**2,121,356**
Adjusted EBITDA	**252,898**	**113,144**	**254,665**	**102,031**	**722,738**	**(131,572)**	**591,166**
Expenses incurred on mergers and acqusitions	-	-	-	-	-	(1,504)	(1,504)
Integration costs	-	-	-	-	-	(26,276)	(26,276)
Restructuring costs	-	-	-	-	-	(22,656)	(22,656)
Impairment losses	(79,203)	-	-	-	(79,203)	-	(79,203)
EBITDA	**173,695**	**113,144**	**254,665**	**102,031**	**643,535**	**(182,008)**	**461,527**
Depreciation and Amortization	(118,452)	(75,246)	(154,194)	(64,517)	(412,409)	(70,082)	(482,491)
Operating profit / (loss)	**55,243**	**37,898**	**100,471**	**37,514**	**231,126**	**(252,090)**	**(20,964)**
Finance income / (cost), net	-	-	-	-	-	(39,942)	(39,942)
Income tax charge	-	-	-	-	-	(26,798)	(26,798)
Profit / (Loss)	**55,243**	**37,898**	**100,471**	**37,514**	**231,126**	**(318,830)**	**(87,704)**
Capital expenditure	87,733	17,444	64,815	23,193	193,185	85,912	279,097

	Home	SOHO / SME	Corporate	Carriers	Total reportable segments	Unallocated	Total
	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)
Year ended December 31, 2011							
Revenue from external customers	**832,714**	**206,332**	**343,277**	**228,787**	**1,611,110**	**7,693**	**1,618,803**
Adjusted EBITDA	**157,165**	**68,102**	**179,542**	**106,717**	**511,526**	**(103,316)**	**408,210**
Expenses incurred on mergers and acqusitions	-	-	-	-	-	(10,434)	(10,434)
Integration costs	-	-	-	-	-	(1,097)	(1,097)
USO provision	-	-	-	-	-	(5,104)	(5,104)
Restructuring costs	-	-	-	-	-	(798)	(798)
Reversal of impairment	-	-	-	-	-	220,677	220,677
EBITDA	**157,165**	**68,102**	**179,542**	**106,717**	**511,526**	**99,928**	**611,454**
Depreciation and Amortization	(69,022)	(49,601)	(99,701)	(51,752)	(270,076)	(38,680)	(308,756)
Operating profit	**88,143**	**18,501**	**79,841**	**54,965**	**241,450**	**61,248**	**302,698**
Finance income / (cost), net	-	-	-	-	-	14,578	14,578
Income tax charge	-	-	-	-	-	(68,490)	(68,490)
Profit	**88,143**	**18,501**	**79,841**	**54,965**	**241,450**	**7,336**	**248,786**
Capital expenditure	96,253	15,855	61,630	22,047	195,785	47,934	243,719

(All amounts in thousands, except as otherwise stated)

Unallocated revenues comprise mainly revenues from Petrotel and the radio communication business. A reconciliation of earnings before interest and tax ("EBIT") for reportable segments to profit / (loss) is provided as follows:

	Year ended December 31, 2012	**Year ended December 31, 2011**
	(PLN)	(PLN)
Operating profit for reportable segments	231,126	241,450
Operating profit for Petrotel business	5,650	71
Operating profit for radio communication business	(749)	(340)
General fixed costs (incl. administration, IT, professional services)	(160,240)	(115,217)
Reorganization and restructuring costs	(22,656)	(798)
Integration costs	(26,276)	(1,097)
Other operating income / (expenses), net	14,532	(4,534)
Reversal of impairment	-	220,667
Depreciation and amortization of unallocated assets (excluding Petrotel and radio communication business)	(62,351)	(37,504)
Finance income/(costs), net	(39,942)	14,578
Income tax charge	(26,798)	(68,490)
Profit/ (Loss)	**(87,704)**	**248,786**

No single customer represented more than 10% of Netia's revenues in either 2012 or 2011. The Netia Group operates in one geographical area, which is the territory of Poland.

(All amounts in thousands, except as otherwise stated)

7. Property, plant and equipment

Current period:

	Buildings (PLN)	Land (PLN)	Fixed telecommunications network (PLN)	Telecommunications equipment (PLN)	Machinery and equipment (PLN)	Office furniture and equipment (PLN)	Vehicles (PLN)	Fixed assets under construction (PLN)	Total (PLN)
Gross book value as at January 1, 2012	114,326	8,477	2,462,104	2,229,024	127,660	84,291	4,447	107,423	5,137,752
Additions	3	-	291	1,631	534	2,851	70	243,668	249,048
Transfer to assets held for sale	-	(631)	-	-	-	-	-	(33)	(664)
Transfer from investment property (see Note 14)	283	-	156	-	-	2,078	-	-	2,517
Purchase of ethernet operators	11	12	80	31	2	74	32	5	247
Transfers	2,512	-	65,924	153,322	10,530	4,190	175	(236,653)	-
Disposals	(163)	(11)	(1,208)	(4,033)	(2,416)	(6,962)	(2,447)	(624)	(17,864)
Other movements	(347)	13	(11,668)	8,329	1,193	2,436	(171)	-	(215)
Gross book value as at December 31, 2012	116,625	7,860	2,515,679	2,388,304	137,503	88,958	2,106	113,786	5,370,821
Accumulated depreciation as at January 1, 2012	34,287	-	926,780	1,186,824	75,815	60,364	1,159	-	2,285,229
Depreciation expense	6,899	-	136,136	193,972	9,950	9,349	2,249	-	358,555
Transfer from investment property (see Note 14)	13	-	98	-	-	2,010	-	-	2,121
Disposals	(40)	-	(450)	(1,751)	(2,004)	(5,715)	(1,913)	-	(11,873)
Other movements	(39)	-	(2,767)	1,422	828	343	-	-	(213)
Accumulated depreciation as at December 31, 2012	41,120	-	1,059,797	1,380,467	84,589	66,351	1,495	-	2,633,819
Accumulated impairment as at January 1, 2012	7,301	-	359,747	277,530	13,967	5,092	18	4,117	667,772
Impairment charge for specific assets	-	-	-	-	-	-	-	4,611	4,611
Reversal of impairment charge for specific assets	-	-	-	-	-	-	-	(296)	(296)
Transfer from investment property (see Note 14)	23	-	28	-	-	68	-	-	119
Disposals	-	-	(99)	(299)	(340)	(397)	-	(346)	(1,481)
Other movements	(2)	-	(220)	(131)	353	-	-	-	-
Accumulated impairment as at December 31, 2012	7,322	-	359,456	277,100	13,980	4,763	18	8,086	670,725
Net book value as at January 1, 2012	72,738	8,477	1,175,577	764,670	37,878	18,835	3,270	103,306	2,184,751
Net book value as at December 31, 2012	**68,183**	**7,860**	**1,096,426**	**730,737**	**38,934**	**17,844**	**593**	**105,700**	**2,066,277**

(All amounts in thousands, except as otherwise stated)

7. Property, plant and equipment (cont'd)

Comparative period:

	Buildings (PLN)	Land (PLN)	Fixed telecommunications network (PLN)	Telecommunications equipment (PLN)	Machinery and equipment (PLN)	Office furniture and equipment (PLN)	Vehicles (PLN)	Fixed assets under construction (PLN)	Total (PLN)
Gross book value as at January 1, 2011	63,788	4,979	2,076,941	1,965,036	115,102	72,620	1,578	83,256	4,383,300
Additions	-	-	698	556	213	1,679	479	212,925	216,550
Transfer from investment property	26,500	-	-	-	-	-	-	-	26,500
Purchase of ethernet operators	-	-	1,294	202	43	9	39	61	1,648
Purchase of Dialog Group and Crowley	14,636	3,677	332,643	141,824	7,548	8,816	2,829	21,232	533,205
Purchase of operational networks	-	-	60	94	12	11	2	-	179
Transfers	9,595	-	59,340	131,504	6,290	3,166	1	(209,896)	-
Disposals	(125)	(179)	(8,636)	(9,489)	(2,432)	(2,131)	(483)	(988)	(24,463)
Other movements	(68)	-	(236)	(703)	884	121	2	833	833
Gross book value as at December 31, 2011	114,326	8,477	2,462,104	2,229,024	127,660	84,291	4,447	107,423	5,137,752
Accumulated depreciation as at January 1, 2011	23,686	-	868,326	1,040,579	69,602	54,902	910	-	2,058,005
Depreciation expense	5,237	-	62,721	152,411	7,514	6,776	660	-	235,319
Transfer from investment property	5,417	-	-	-	-	-	-	-	5,417
Disposals	(42)	-	(4,037)	(5,896)	(1,783)	(1,343)	(411)	-	(13,512)
Other movements	(11)	-	(230)	(270)	482	29	-	-	-
Accumulated depreciation as at December 31, 2011	34,287	-	926,780	1,186,824	75,815	60,364	1,159	-	2,285,229
Accumulated impairment as at January 1, 2011	6,491	534	510,546	308,801	15,878	5,312	18	2,033	849,613
Impairment charge for specific assets	-	-	-	-	-	67	-	3,929	3,996
Reversal of impairment charge for specific assets	-	-	-	-	-	-	-	(1,534)	(1,534)
Reversal of impairment charge	(1,006)	(496)	(149,807)	(30,214)	(1,782)	(25)	-	-	(183,330)
Transfer from investment property	1,844	-	-	-	-	-	-	-	1,844
Transfers	-	-	1	6	1	-	-	(8)	-
Disposals	(27)	(38)	(982)	(808)	(397)	(262)	-	(688)	(3,202)
Other movements	(1)	-	(11)	(255)	267	-	-	385	385
Accumulated impairment as at December 31, 2011	7,301	-	359,747	277,530	13,967	5,092	18	4,117	667,772
Net book value as at January 1, 2011	33,611	4,445	698,069	615,656	29,622	12,406	650	81,223	1,475,682
Net book value as at December 31, 2011	**72,738**	**8,477**	**1,175,577**	**764,670**	**37,878**	**18,835**	**3,270**	**103,306**	**2,184,751**

(All amounts in thousands, except as otherwise stated)

The transfers recorded in the year ended December 31, 2012 mainly relate to transfers from fixed assets under construction to fixed assets brought into use.

During the year ended December 31, 2012 the Netia Group recognized impairment charges of PLN 4,611 relating mainly to obsolete telecommunication equipment. In 2011 the Netia Group recognized specific impairment charges of PLN 3,996 for discontinued investment projects.

Subsequent costs directly attributable to the acquisition or bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by the Management amounting to PLN 16,905 and PLN 13,989 were capitalized to fixed assets under construction during the year ended December 31, 2012 and December 31, 2011, respectively. Furthermore the Company capitalized PLN 994 of net cash losses on closed forward contracts and PLN1,691 of interests costs. In the year ended December 31, 2011 the Company capitalized PLN 383 of net cash gains on closed forward contracts

The net carrying value of assets held under finance leases as at December 31, 2012 and December 31, 2011 is presented below:

	December 31, 2012 (PLN)	December 31, 2011 (PLN)
Fixed telecommunications network	1,916	1,786
Telecommunications equipment	4,996	16,201
Machinery and equipment	7	-
Vehicles	351	415
	7,270	**18,402**

8. Acquisitions

Current period

Acquisition of Ethernet operators

Elpro-Elektronika Profesjonalna Waldemar Nitka Sp. z o.o.

On February 14, 2012, Internetia Sp. z o.o. ("Internetia"), the Company's subsidiary, purchased 100% of the share capital of Elpro-Elektronika Profesjonalna Waldemar Nitka Sp. z o.o. ("Elpro"), an internet service provider offering broadband Internet access to residential clients. The total price for all Elpro shares has been set at PLN 2,202.

The Netia Group accounted for the acquisition of Elpro using the acquisition method.

If the acquisition had occurred on January 1, 2012, the Netia Group's revenue would have amounted to PLN 2,121,467 and loss would have been PLN 87,594.

The Netia Group performed a valuation of the acquired company's assets, liabilities and contingent liabilities. In the purchase price allocation process the Netia Group identified customer relationships as an intangible asset. The fair value of customer relationships was estimated using the excess earnings method. Further changes to the valuation may be introduced during the course of 12 months from the acquisition dates if additional information in respect of acquired assets, liabilities and contingent liabilities is obtained. Such additional information may include information related to pre-acquisition contingencies and calculation of the related deferred income taxes. The Netia Group will continue evaluating fair values of these assets, liabilities and contingent liabilities, which may result in further adjustments to the carrying amounts of identifiable net assets.

Details of provisional fair values of net assets acquired and goodwill as of the date of the acquisition are as follows:

	(PLN)
Purchase consideration	2,202
Provisional fair value of net assets acquired	(608)
Goodwill	**1,594**

The goodwill is based on provisional fair values of net assets acquired and is attributable to the significant synergies expected to arise after the Netia Group's acquisition. None of the recognized goodwill is expected to be deductible for income tax purposes.

The assets and liabilities recognized in the consolidated statement of financial position arising from the acquisition, as at the acquisition date, are as follows:

(All amounts in thousands, except as otherwise stated)

	Acquiree's carrying amount	Provisional fair value
	(PLN)	(PLN)
Customer relationships	-	712
Property, plant and equipment	12	12
Trade receivables	40	40
Cash and short term deposits	52	52
Prepayments	5	5
Trade liabilities	(2)	(2)
Tax and other liabilities	(76)	(76)
Deferred income tax, net	-	(135)
Net assets acquired	**31**	**608**

Fair value of the purchase consideration transferred for the acquisition:

	(PLN)
Cash paid	2,202
Total consideration	**2,202**

	(PLN)
Total purchase consideration settled in cash	(2,202)
Cash and short term deposits in the subsidiary acquired	52
Cash outflow on acquisition	**(2,150)**

The above investments are of a long-term nature.

STI Sp. z o.o.

On March 7, 2012, Internetia Sp. z o.o. purchased 100% of the share capital of STI Sp. z o.o. ("STI"), an internet service provider offering broadband Internet access to residential clients. The total purchase consideration for all STI shares has been set at PLN 1,623.

The Netia Group accounted for the acquisition of STI using the acquisition method.

If the acquisition had occurred on January 1, 2012, the Netia Group's revenue would have amounted to PLN 2,121,478 and loss would have been PLN 87,692.

The Netia Group performed a valuation of the acquired company's assets, liabilities and contingent liabilities. In the purchase price allocation process the Netia Group identified customer relationships as an intangible asset. The fair value of customer relationships was estimated using the excess earnings method. Further changes to the valuation may be introduced during the course of 12 months from the acquisition dates if additional information in respect of acquired assets, liabilities and contingent liabilities is obtained. Such additional information may include information related to pre-acquisition contingencies and calculation of the related deferred income taxes. The Netia Group will continue evaluating fair values of these assets, liabilities and contingent liabilities, which may result in further adjustments to the carrying amounts of identifiable net assets.

Details of provisional fair values of net assets acquired and goodwill as of the date of the acquisition are as follows:

	(PLN)
Purchase consideration	1,623
Provisional fair value of net assets acquired	(540)
Goodwill	**1,083**

The goodwill is based on provisional fair values of net assets acquired and is attributable to the significant synergies expected to arise after the Netia Group's acquisition. None of the recognized goodwill is expected to be deductible for income tax purposes.

The assets and liabilities recognized in the consolidated statement of financial position arising from the acquisition, as at the acquisition date, are as follows:

(All amounts in thousands, except as otherwise stated)

	Acquiree's carrying amount	Provisional fair value
	(PLN)	(PLN)
Customer relationships	-	581
Property, plant and equipment	162	162
Investments	28	28
Trade receivables	65	65
Cash and short term deposits	35	35
Prepayments	7	7
Borrowings	(61)	(61)
Trade liabilities	(76)	(76)
Tax and other liabilities	(69)	(69)
Deferred income	(22)	(22)
Deferred income tax, net	-	(110)
Net assets acquired	**69**	**540**

Fair value of the purchase consideration transferred for the acquisition:

	(PLN)
Cash paid	1,623
Total consideration	**1,623**

	(PLN)
Total purchase consideration settled in cash	(1,623)
Cash and short term deposits in the subsidiary acquired	35
Cash outflow on acquisition	**(1,588)**

The above investments are of a long-term nature.

Sanetja Sp. z o.o.

On May 29, 2012, Internetia Sp. z o.o. purchased 100% of the share capital of Sanetja Sp. z o.o. ("Sanetja"), an internet service provider offering broadband Internet access to residential clients. The total purchase consideration for all Sanetja shares has been set at PLN 1,556.

The Netia Group accounted for the acquisition of Sanetja using the acquisition method.

If the acquisition had occurred on January 1, 2012, the Netia Group's revenue would have amounted to PLN 2,121,357 and profit would have been PLN 87,705.

The Netia Group performed a valuation of the acquired company's assets, liabilities and contingent liabilities. In the purchase price allocation process the Netia Group identified customer relationships as an intangible asset. The fair value of customer relationships was estimated using the excess earnings method. Further changes to the valuation may be introduced during the course of 12 months from the acquisition dates if additional information in respect of acquired assets, liabilities and contingent liabilities is obtained. Such additional information may include information related to pre-acquisition contingencies and calculation of the related deferred income taxes. The Netia Group will continue evaluating fair values of these assets, liabilities and contingent liabilities, which may result in further adjustments to the carrying amounts of identifiable net assets.

Details of provisional fair values of net assets acquired and goodwill as of the date of the acquisition are as follows:

	(PLN)
Purchase consideration	1,556
Provisional fair value of net assets acquired	(303)
Goodwill	**1,253**

The goodwill is based on provisional fair values of net assets acquired and is attributable to the significant synergies expected to arise after the Netia Group's acquisition. None of the recognized goodwill is expected to be deductible for income tax purposes.

(All amounts in thousands, except as otherwise stated)

The assets and liabilities recognized in the consolidated statement of financial position arising from the acquisition, as at the acquisition date, are as follows:

	Acquiree's carrying amount	**Provisional fair value**
	(PLN)	(PLN)
Customer relationships	-	410
Property, plant and equipment	73	73
Trade receivables	8	8
Cash and short term deposits	10	10
Borrowings	(51)	(51)
Trade liabilities	(22)	(22)
Tax and other liabilities	(47)	(47)
Deferred income tax, net	-	(78)
Net assets acquired	**(29)**	**303**

Fair value of the purchase consideration transferred for the acquisition:

	(PLN)
Cash paid	1,556
Total consideration	**1,556**

	(PLN)
Total purchase consideration settled in cash	(1,556)
Cash and short term deposits in the subsidiary acquired	10
Cash outflow on acquisition	**(1,546)**

The above investments are of a long-term nature.

(All amounts in thousands, except as otherwise stated)

Ethernet operators: end of provisional accounting in 2012

During the year ended December 31, 2011 the Netia Group acquired several ethernet operators and performed a provisional valuation of the acquired companies' assets, liabilities and contingent liabilities. During the year ended December 31, 2012 the company adjusted provisional values of the purchase consideration and net assets of some subsidiaries acquired in 2011.
During the year ended December 31, 2011 the Netia Group purchased the following internet service providers:

Company	Date	Share capital acquired	Purchase price (PLN)
Netpro Sp. z o.o. ("Netpro")	March 30, 2011	100.0 %	600
Saite Sp. z o.o. ("Saite")	June 28, 2011	100.0 %	2,331
E-IMG Internet Multimedia Group Sp. z o.o. ("E-IMG Internet")	August 23, 2011	100.0 %	2,764
ZAX.EU Sp. z o.o. ("ZAX.EU")	September 30, 2011	100.0 %	2,960
Silesia Multimedia Sp. z o.o. ("Silesia")	November 18, 2011	100.0 %	3,712
Netsystem Sp. z o.o. ("Netsystem")	December 16, 2011	100.0 %	2,958
Sieci Multimedialne Intergeo Sp. z o.o. ("Intergeo")	December 21, 2011	100.0 %	1,206
ComNet ITT Sp. z o.o. ("ComNet")	December 29, 2011	100.0 %	6,707
Total			**23,238**

Details of provisional fair values of net assets acquired and goodwill as of the date of the acquisition estimated as at December 31, 2011 and final values as at December 31, 2012 are as follows:

	Netpro	Saite	E-IMG Internet	ZAX.EU	Silesia	Netsystem	Intergeo	ComNet	Total
Purchase price provisionally estimated as at December 31, 2011	600	2,331	2,764	2,960	3,712	2,890	1,206	6,707	23,170
Adjustments to purchase consideration made in 2012 *	-	-	-	-	-	68	-	-	68
Final purchase price as at December 31, 2012	**600**	**2,331**	**2,764**	**2,960**	**3,712**	**2,958**	**1,206**	**6,707**	**23,238**
Provisional fair value of net assets acquired estimated as at December 31, 2011	(249)	(699)	(845)	(141)	(665)	(753)	(198)	(1,990)	(5,540)
Adjustments to fair value of net assets acquired made in 2012 *	-	-	-	-	-	-	(105)	-	(105)
Final value of net assets acquired as at December 31, 2012	**(249)**	**(699)**	**(845)**	**(141)**	**(665)**	**(753)**	**(303)**	**(1,990)**	**(5,645)**
Goodwill	**351**	**1,632**	**1,919**	**2,819**	**3,047**	**2,205**	**903**	**4,717**	**17,593**

* The 2011 comparative information has been restated to reflect the above adjustments in provisional valuation.

(All amounts in thousands, except as otherwise stated)

The goodwill is based on fair values of net assets acquired and is attributable to the significant synergies expected to arise after the Netia Group's acquisition. None of the recognized goodwill is expected to be deductible for income tax purposes.

The assets and liabilities recognized in the consolidated statement of financial position arising from the acquisitions, as at the acquisitions' dates, are as follows:

Acquiree's carrying amount	**Netpro**	**Saite**	**E-IMG Internet**	**ZAX.EU**	**Silesia**	**Netsystem**	**Intergeo**	**ComNet**	**Total**
Property, plant and equipment	101	270	67	112	28	215	115	741	1,649
Other intangible assets	7	2,073							2,080
Inventories	4	1	-	64	-	-	-	9	78
Receivables	9	32	34	19	60	1	1	55	211
Prepayments	-	-	-	13	22	-	-	-	35
Cash and short term deposits	27	67	73	34	111	99	5	56	472
Borrowings	-	(106)	-	(100)	-	-	(36)	(320)	(562)
Trade liabilities	(10)	(44)	(24)	(191)	(76)	(59)	(14)	(57)	(475)
Other liabilities and accruals	(23)	(25)	(79)	(349)	(35)	(18)	(9)	(41)	(579)
Deferred income	-	-	-	(17)	-	-	-	-	(17)
Net assets acquired	**115**	**2,268**	**71**	**(415)**	**110**	**238**	**62**	**443**	**2,892**

Final fair value as at December 31, 2012	**Netpro**	**Saite**	**E-IMG Internet**	**ZAX.EU**	**Silesia**	**Netsystem**	**Intergeo**	**ComNet**	**Total**
Property, plant and equipment	101	270	67	112	28	215	115	741	1,649
Customer relationships	165	598	955	686	685	636	297	1,910	5,932
Other intangible assets	7	20							27
Inventories	4	1	-	64	-	-	-	9	78
Receivables	9	32	34	19	60	1	1	55	211
Prepayments	-	-	-	13	22	-	-	-	35
Cash and short term deposits	27	67	73	34	111	99	5	56	472
Borrowings	-	(106)	-	(100)	-	-	(36)	(320)	(562)
Trade liabilities	(10)	(44)	(24)	(191)	(76)	(59)	(14)	(57)	(475)
Other liabilities and accruals	(23)	(25)	(79)	(349)	(35)	(18)	(9)	(41)	(579)
Deferred income	-	-	-	(17)	-	-	-	-	(17)
Deferred income tax liabilities	(31)	(114)	(181)	(130)	(130)	(121)	(56)	(363)	(1,126)
Provisional fair value of net assets acquired	**249**	**699**	**845**	**141**	**665**	**753**	**303***	**1,990**	**5,645**

* Fair value of property, plant and equipment increased by PLN 115 in 2012 with corresponding decrease in fair value of customer relationship by PLN 13 in 2012. Total fair value of net assets acquired increased by PLN 105 net of tax.

Acquisition of Crowley: end of provisional accounting in 2012

On December 14, 2011 Netia purchased from Crowley Data, LLC and Crowley Poland, LLC (the "Sellers") 197,862 shares (not in thousands) in Crowley Data Poland sp. z o.o., with its registered office in Warsaw ("Crowley"), constituting 100% of the shares in the share capital of Crowley and representing 100% of the votes at the meetings of the shareholders of Crowley (the "Shares"). The total purchase price for the enterprise was USD 30,797 and comprised the purchase of a shareholder loan advanced by the Sellers to Crowley with the balancing amount paid for 100 % of the shares. The purchase price for the Shares was subject to adjustment for the difference between certain amounts stated in the balance sheet of Crowley as at 31 December 2010 and the respective amounts stated in the balance sheet of Crowley as at 30 November 2011.

On September 16, 2011, Netia executed a foreign exchange risk hedging transaction at the USD/PLN exchange rate of PLN 3.14 per USD 1.00 to mitigate the foreign currency risk associated with the acquisition.

A deposit in the amount of PLN 5,000 was paid directly after signing the share purchase agreement and this amount was treated as part of the purchase consideration. On December 14, 2011 the Company paid the outstanding (net of hedging gains) PLN 91,895 for all shares in Crowley (including purchase of the shareholder loan extended to Crowley). On March 15, 2012 the Company paid PLN 2,775 (from PLN 4,055 accrued) for the provisionally agreed adjustments to the balance sheet as at November 30, 2011. On December 13, 2012 final purchase price adjustment agreement was signed and Netia paid PLN 1,548 for additionally agreed adjustments to the balance sheet as at November 30, 2011. Consequently, Netia accounted for an additional purchase price adjustment of PLN 268.

Consequently, Netia closed the transaction at a consideration of PLN 101,218 comprising the enterprise value of PLN 97,757 and net cash and short term deposits of PLN 3,361.

The Netia Group accounted for the acquisition of Crowley using the purchase method and started consolidating the financial statements of Crowley as of December 14, 2011.

The Netia Group performed a valuation of the acquired company's assets, liabilities and contingent liabilities. In the purchase price allocation process the Netia Group identified customer relationships as an intangible asset. The fair value of customer relationships was estimated using the excess earnings method.

Details of provisional fair values as of December 31, 2011 and final fair values as of December 31, 2012 and of net assets acquired and goodwill as of the date of the acquisition are as follows:

	Provisional accounting as at December 31, 2011	Adjustments to purchase price and to fair value of net assets acquired made in 2012	Final accounting as at December 31, 2012
	(PLN)	(PLN)	(PLN)
Purchase consideration	100,950	268	101,218
Fair value of net assets acquired	(53,329)	485	(52,844)
Goodwill	**47,621**	**753**	**48,374**

The goodwill is based on fair values of net assets acquired and is attributable to the significant synergies expected to arise after the Netia Group's acquisition. None of the recognized goodwill is expected to be deductible for income tax purposes. The assets and liabilities recognized in the consolidated statement of financial position arising from the acquisition, as at the acquisition date, are as follows:

(All amounts in thousands, except as otherwise stated)

	Acquiree's carrying amount	**Provisional fair value as at December 31, 2011**	**Adjustments to fair value of net assets acquired made in 2012**	**Final fair value as at December 31, 2012**
	(PLN)	(PLN)	(PLN)	(PLN)
Customer relationships	-	30,006	-	30,006
Property, plant and equipment	40,350	31,179	(29)	31,150
Other intangible assets	2,041	2,041	-	2,041
Receivables	10,907	10,907	179	11,086
Inventory	120	120	-	120
Cash and short term deposits	3,221	3,221	-	3,221
Restricted cash	140	140	-	140
Prepayments	242	242	-	242
Trade liabilities	(6,418)	(6,418)	-	(6,418)
Tax and other liabilities	(11,143)	(11,143)	(635)	(11,778)
Provisions	(1,406)	(2,883)	-	(2,883)
Deferred income	(2,545)	(105)	-	(105)
Deferred income tax, net	(20)	(3,978)	-	(3,978)
Net assets acquired	**35,489**	**53,329**	**(485)**	**52,844**

Crowley was legally merged into Netia on August 31, 2012.

Acquisition of Dialog: end of provisional accounting in 2012

On December 16, 2011 Netia acquired 19,598,000 shares (not in thousands) in Dialog, with a nominal value of PLN 25 (not in thousands) each and the aggregate nominal value of PLN 489,950, which constitute 100% of the shares in the share capital of Dialog and represent 100% of the votes at the general meetings of Dialog. In consequence of the acquisition of the shares, Netia became an indirect owner of shares in two material subsidiaries of Dialog: Petrotel and Avista (merged with Dialog in July 2012).

The final price paid by the Company was PLN 968,927 and comprised Dialog's enterprise value of PLN 880,388 and net cash and short term deposits of PLN 88,539.

The Netia Group accounted for the acquisition of Dialog Group using the purchase method and started consolidating the financial statements of Dialog Group as of December 16, 2011.

The Netia Group performed a valuation of the acquired Dialog's Group assets, liabilities and contingent liabilities. In the purchase price allocation process the Netia Group identified customer relationships and trademarks as an intangible asset. The fair value of customer relationships was estimated using the excess earnings method.

Details of provisional fair values as of December 31, 2011 and final fair values as of December 31, 2012 of net assets acquired and goodwill as of the date of the acquisition are as follows:

	Provisional accounting as at December 31, 2011	**Adjustments to fair value of net assets acquired made in 2012**	**Final accounting as at December 31, 2012**
	(PLN)	(PLN)	(PLN)
Purchase consideration	968,927	-	968,927
Fair value of net assets acquired	(834,525)	(5,125)	(839,650)
Non-controlling interests (0,01%)	5	-	5
Goodwill	**134,407**	**(5,125)**	**129,282**

The goodwill is based on fair values of net assets acquired and is attributable to the significant synergies expected to arise after the Netia Group's acquisition. None of the recognized goodwill is expected to be deductible for income tax purposes.

The assets and liabilities recognized in the consolidated statement of financial position arising from the acquisition, as at the acquisition date, are as follows:

(All amounts in thousands, except as otherwise stated)

	Acquiree's carrying amount	Provisional fair value as at December 31, 2011	Adjustments to fair value of net assets acquired made in 2012	Final fair value as at December 31, 2012
	(PLN)	(PLN)	(PLN)	(PLN)
Customer relationships	-	102,100	-	102,100
Trademarks	-	10,900	-	10,900
Property, plant and equipment	655,499	501,544	514	502,058
Other intangible assets	35,346	35,346	(98)	35,248
Receivables	84,959	84,959	5,932	90,891
Prepayments	8,451	8,451	-	8,451
Inventory	1,013	1,013	-	1,013
Deferred income tax, net	85,060	79,165	(1,202)	77,963
Cash and short term deposits	90,314	90,314	-	90,314
Borrowings	(1,775)	(1,775)	-	(1,775)
Trade liabilities	(29,493)	(29,493)	-	(29,493)
Tax and other liabilities	(33,488)	(33,488)	-	(33,488)
Provisions	(5,387)	(6,142)	(66)	(6,208)
Deferred income	(8,369)	(8,369)	45	(8,324)
Net assets acquired	**882,130**	**834,525**	**5,125**	**839,650**

(All amounts in thousands, except as otherwise stated)

9. Intangible assets

Current period:

			Licences				Computer software costs			
	Goodwill	Trademark	Local telecommunication licenses / permits	Data communications and internet licenses / permits	Domestic long-distance licenses / permits	WiMAX licenses	Computer software	Capital work in progress	Customer relationships	Total
	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)
Gross book value as at January 1, 2012	355,974	17,477	432,823	7,417	107,354	20,329	409,856	5,959	224,529	1,581,718
Additions	-	2	-	-	-	-	6,839	23,208	-	30,049
Purchase of ethernet operators	3,930	-	-	-	-	-	-	-	1,704	5,634
Transfers	-	134	-	-	-	-	11,793	(11,927)	-	-
Disposals	-	-	-	-	-	-	(1,365)	-	-	(1,365)
Other movements	-	653	-	-	-	-	10,602	(11,040)	-	215
Gross book value as at December 31, 2012	359,904	18,266	432,823	7,417	107,354	20,329	437,725	6,200	226,233	1,616,251
Accumulated amortization as at January 1, 2012	-	3,185	242,152	1,539	61,350	6,637	257,894	-	65,238	637,995
Amortization expense	-	5,131	29,042	-	7,351	1,410	41,790	-	39,212	123,936
Disposals	-	-	-	-	-	-	(1,028)	-	-	(1,028)
Other movements	-	653					(411)	-	-	242
Accumulated amortization as at December 31, 2012	-	8,969	271,194	1,539	68,701	8,047	298,245	-	104,450	761,145
Accumulated impairment as at January 1, 2012	-	-	115,549	5,878	13,231	974	42,617	-	199	178,448
Impairment charge (see Note 5)	79,203	-	-	-	-	-	-	-	-	79,203
Disposals	-	-	-	-	-	-	-	-	-	-
Accumulated impairment as at December 31, 2012	79,203	-	115,549	5,878	13,231	974	42,617	-	199	257,651
Net book value as at January 1, 2012	355,974	14,292	75,122	-	32,773	12,718	109,345	5,959	159,092	765,275
Net book value as at December 31, 2012	**280,701**	**9,297**	**46,080**	**-**	**25,422**	**11,308**	**96,863**	**6,200**	**121,584**	**597,455**

(All amounts in thousands, except as otherwise stated)

9. Intangible assets (cont'd)

Comparative period:

			Licences				Computer software costs			
	Goodwill (PLN)	Trademark (PLN)	Local telecommunication licenses / permits (PLN)	Data communications and internet licenses / permits (PLN)	Domestic long-distance licenses / permits (PLN)	WiMAX licenses (PLN)	Computer software (PLN)	Capital work in progress (PLN)	Customer relationships (PLN)	Total (PLN)
Gross book value as at January 1, 2011	159,446	2,970	432,823	7,417	107,354	20,329	339,674	11,333	85,269	1,166,615
Additions	-	-	-	-	-	-	1,566	25,504	-	27,070
Purchase of ethernet operators	17,593	7	-	-	-	-	20	-	5,933	23,553
Purchase of Dialog Group and Crowley	177,656	13,942	-	-	-	-	26,535	7,810	132,106	358,049
Purchase of operational networks	1,279	-	-	-	-	-	-	-	1,221	2,500
Transfers	-	-	-	-	-	-	38,677	(38,677)	-	-
Disposals	-	-	-	-	-	-	(6)	(11)	-	(17)
Other movements	-	558	-	-	-	-	-	-	-	558
Gross book value as at December 31, 2011	355,974	17,477	432,823	7,417	107,354	20,329	406,466	5,959	224,529	1,578,328
Accumulated amortization as at January 1, 2011	-	2,970	222,952	1,539	55,952	5,227	224,625	-	48,561	561,826
Amortization expense	-	215	19,200	-	5,398	1,410	29,884	-	16,677	72,784
Disposals	-	-	-	-	-	-	(5)	-	-	(5)
Accumulated amortization as at December 31, 2011	-	3,185	242,152	1,539	61,350	6,637	254,504	-	65,238	634,605
Accumulated impairment as at January 1, 2011	-	-	143,739	5,878	21,547	974	42,620	385	199	215,342
Reversal of impairment charge	-	-	(28,190)	-	(8,316)	-	(3)	-	-	(36,509)
Other movements	-	-	-	-	-	-	-	(385)	-	(385)
Accumulated impairment as at December 31, 2011	-	-	115,549	5,878	13,231	974	42,617	-	199	178,448
Net book value as at January 1, 2011	159,446	-	66,132	-	29,855	14,128	72,429	10,948	36,509	389,447
Net book value as at December 31, 2011	**355,974**	**14,292**	**75,122**	**-**	**32,773**	**12,718**	**109,345**	**5,959**	**159,092**	**765,275**

(All amounts in thousands, except as otherwise stated)

As a result of the impairment test of non-current assets as of December 31, 2012 the Netia Group has recognized impairment losses amounting to 79,203 PLN during the year ended December 31, 2012 (see Note 5), which was allocated to goodwill.

Telecommunication licenses / permits

Prior to the completion of the legal merger of the Company with its operating subsidiaries on December 31, 2003, its subsidiaries held fixed-term permits for the operation of local telecommunication networks on a non-exclusive basis in specified areas throughout Poland. Those permits were obtained through their conversion from telecommunication licenses issued under the regulations of the previous Telecommunication Act. The conversion took place by virtue of the 2001 Act on January 1, 2001. Licenses for telecommunications services in Poland were issued for 15-year periods. The remaining amortization periods of the permits range between 1 and 3 years.

Domestic long-distance licenses / permits

In May 2000, one of the operating subsidiaries currently legally merged into Netia, was granted a domestic long-distance license. The license, currently converted into a permit, covers the entire territory of Poland and enables the Company to provide intercity telecommunication services. The remaining amortization period of the permit is 3 years.

Data communications and internet licenses / permits

In April 1999, one of the operating subsidiaries currently merged into Netia, obtained a data communications license covering the entire territory of Poland. This license was fully impaired in 2003.

WiMAX licenses

On October 27, 2005 the Company's subsidiaries, Netia WiMax S.A. (merged with Netia in July 2006) and Netia WiMax II S.A. (since November 2006 operating under the name "Netia WiMax S.A.", merged with Netia in October 2008), received the reservation of the 3.6-3.8 GHz frequencies, which are used to provide telecommunication services based on WiMAX technology. The license covers the entire territory of Poland and is valid for 15 years. The remaining amortization period of the permit is 8 years.

10. Inventories

	December 31, 2012 (PLN)	December 31, 2011 (PLN)
Materials	596	1,236
Goods for resale	2,847	5,147
Less provision for impairment charge	(1,349)	(1,069)
Inventories, net	**2,094**	**5,314**

During the years ended December 31, 2012 and 2011 the Netia Group recognized PLN 8,233 and PLN 10,233, respectively as the cost of inventories included in "cost of goods sold".

11. Trade and other receivables

	December 31, 2012 (PLN)	December 31, 2011 (PLN)
Trade receivables	312,808	315,413
Less provision for impairment of trade receivables	(76,648)	(72,721)
Trade receivables, net	236,160	242,692
VAT and other government receivables	2,953	6,026
Other receivables	9,236	7,628
Less provision for impairment of other receivables	(78)	(532)
Other receivables, net	9,158	7,096
	248,271	**255,814**
Of which,		
Current	248,270	255,596
Non-current	1	218

The carrying amount of non-current receivables approximates their fair value.

The provision for impairment of the Netia Group's receivables recognized during the year ended December 31, 2012 and 2011 amounted to PLN 12,664 and PLN 6,976, respectively and was included in "selling and distribution costs" in the consolidated income statement.

(All amounts in thousands, except as otherwise stated)

As of December 31, 2012 and December 31, 2011 trade and other receivables of PLN 73,809 and PLN 73,327, respectively, were past due but not fully provided for. The ageing analysis of these trade receivables is as follows:

	Less than 3 months	3 – 6 months	More than 6 months	Total
	(PLN)	(PLN)	(PLN)	(PLN)
As at December 31, 2012	52,810	5,327	15,672	73,809
As at December 31, 2011	60,991	4,037	8,299	73,327

In addition, as at December 31, 2012 and December 31, 2011 the amounts of PLN 360 and PLN 933, respectively were excluded from other receivables as they were legally reserved for spending on social purposes.

12. Prepaid expenses and accrued income

	December 31, 2012	December 31, 2011
	(PLN)	(PLN)
Accrued income relating to promotional offers	37,697	31,195
Rental costs prepaid	2,364	2,306
IT service.	1,795	1,872
Insurance.	688	1,253
Other prepaid expenses.	2,198	5,297
	44,742	**41,923**
Of which,		
Current	33,660	30,091
Non-current	11,082	11,832

13. Cash, short term deposits and restricted cash

	December 31, 2012	December 31, 2011
	(PLN)	(PLN)
Cash and short term deposits	142,702	156,509

The effective interest rate on short-term bank deposits was 4.18% and 3.8%, respectively for the year ended December 31, 2012 and the year ended December 31, 2011.

In addition, as at December 31, 2012 and December 31, 2011 the amounts of PLN 1,669 and PLN 936, respectively were excluded from cash and short term deposits as they were legally reserved for spending on social purposes.

	December 31, 2012	December 31, 2011
	(PLN)	(PLN)
Restricted cash	2,263	2,263

As at December 31, 2012 and December 31, 2011, PLN 2,110 of restricted cash represents a Court deposit and the amounts of PLN 153 were restricted as they were placed as collaterals securing payments to vendors.

For the purpose of the statement of cash flow cash and cash equivalents as at December 31, 2012 comprise the following:

	December 31, 2012	December 31, 2011
	(PLN)	(PLN)
Cash and short term deposits	142,702	156,509
Bank overdrafts (see Note 18)	(18,751)	-
Cash and cash equivalents	**123,951**	**156,509**

14. Assets held for sale

On March 23, 2012 the Company and Tilia SKA, a Company related to Ghelamco Group signed a conditional purchase agreement to sell Netia's land totalling 23,600 m2 (not in thousands) in Warsaw at Poleczki 13 and two buildings located thereon.

The Management of the Company plans to close the transaction for a value between PLN 25,920 - 32,020, depending on the size of the rentable area approved for construction by the local authorities. As an integral part of the agreement, Netia has committed to lease one of the buildings that Ghelamco plans to develop on the site, starting from 2015. Finalization of the sale depends on receipt of various authorizations from the relevant local authorities in a form satisfactory to the buyer. Management currently expects that receipt of all such authorisations will be completed in the first half of 2013 and that the sale transaction should be closed by July 31, 2013.

Consequently, as at December 31, 2012, the property of PLN 26,105 (reclassified from investment property) and land of PLN 631 and infrastructure of PLN 34 (reclassified from land) which will be sold to Tilia SKA were presented as assets held for sale.

This agreement does not relate to land and one building at the same location which houses network equipment crucial for the operation of Netia's network and is presented as property, plant and equipment as at December 31, 2012.

15. Other financial instruments

Derivative financial instruments

Derivative financial assets:	December 31, 2012	December 31, 2011
	(PLN)	(PLN)
Forward contracts	-	2,723
	-	2,723
Of which:		
Current	-	2,723
Non-current	-	-

Derivative financial liabilities:	December 31, 2012	December 31, 2011
	(PLN)	(PLN)
Forward contracts	3,588	84
Interest rate swap contracts	9,421	-
	13,009	**84**
Of which:		
Current	7,268	84
Non-current	5,741	-

Forward contracts

In order to mitigate the currency risk related to the planned payments to be made under equipment and construction contracts which are linked to foreign currencies the Company entered into several forward transactions to purchase USD and EUR for periods consistent with currency transaction exposures, generally up to 12 months. For these forward contracts hedge accounting was applied. Net fair value losses on forward contracts recognized in the hedging reserve in equity on these contracts as of December 31, 2012 amounted to PLN 4,195 (PLN 3,398, net of tax). During the year ended December 31, 2012, PLN 994 of net cash losses on closed forward contracts were capitalized, PLN 54 of net cash losses increased finance costs due to excess of the amount of closed forward contracts over purchases made and the ineffective portion of open and closed forward contracts of PLN 85 was recorded as finance costs.

Furthermore, in order to mitigate the currency risk related to the planned payments to be made under commercial contracts associated with various types of operating expense which are linked to foreign currency, the Company entered into several forward transactions to purchase USD and EUR for periods consistent with currency transaction exposures, generally up to 12 months. During the year ended December 31, 2012, PLN 1,945 of fair losses on open forward contracts were recorded as finance costs.

In year ended December 31, 2011 net fair value gains on forward contracts recognized in the hedging reserve in equity amounted to PLN 1,892 (PLN 1,532, net of tax). During the year ended December 31, 2011, PLN 383 of net cash gains on closed forward contracts were capitalized, and the ineffective portion of open and closed forward contracts of PLN 22 was recorded as finance costs.

Furthermore, in order to mitigate the currency risk related to the planned payments to be made under commercial contracts associated with various types of operating expense which are linked to foreign currency, the Company entered into several forward transactions to purchase USD and EUR for periods consistent with currency transaction exposures, generally up to 12 months. During the year ended December 31, 2011, PLN 1,486 of fair value gains on open forward contracts were recorded as finance income.

The table below presents outstanding forward transactions, related assets and liabilities and other comprehensive loss as at December 31, 2012 and for the year then ended:

	Hedged nominal amount	Hedged nominal amount	Fair value		
			Asset	Liability	Other comprehensive income/ (loss)
	(EUR)	(USD)	(PLN)	(PLN)	(PLN)
As at December 31, 2012					
Forward transactions related to equipment and construction contracts	7,590	3,410	-	(2,642)	(4,195)
Forward transactions related to commercial contracts	6,050	1,650	-	(946)	-
As at December 31, 2011					
Forward transactions related to equipment and construction contracts	3,915	4,530	1,692	(52)	1,892
Forward transactions related to commercial contracts	3,015	1,380	1,031	(32)	-

Interests rate risk hedging instruments

On January 5, 2012 and January 10, 2012, the Company entered into interest rate swap ("IRS") contracts hedging interest rate risk associated with interest payments in the amount of fifty per cent of all amounts projected to be outstanding under the Term Loan (See Note 18 Borrowings). For these IRS contracts hedge accounting was applied. As of December 31, 2012 effective portion of change in net fair value of IRS contracts recognized in the hedging reserve in equity amounted to PLN 9,421 (PLN 7,631, net of tax). During the year ended December 31, 2012, PLN 45 of net realized cash losses on IRS contracts increased interest costs.

Non-derivative hedging instruments

As of December 31, 2011, the Company held a cash balance of USD 736 purchased upon realization of a hedging forward contract and designated as a hedging instrument to mitigate foreign exchange risk associated with the planned payment of a purchase price adjustment pursuant to the Conditional Agreement to acquire shares in Crowley. For this cash balance hedge accounting was applied. A fair value gain on this instrument of PLN 21 decreased the purchase price adjustment paid by the Company on March 15, 2012.

16. Shareholders' equity

Share capital (not in thousands)

At December 31, 2011, the Company's share capital consisted of 391,601,064 ordinary shares and 1,000 series A1 shares with a par value of PLN 1 per share. Each ordinary share has one vote at the shareholders' meeting. The holder of 1,000 series A1 shares has the right to nominate one member of the Supervisory Board. The majority of votes of the Supervisory Board elect the Management Board.

In 2012 the Company issued 4,453,840 ordinary series K shares due to three current and three former Management Board members, twelve persons who hold managerial positions and two former managers (none of whom are or were management board members) exercising their rights arising from the key employee share option plan adopted by Netia's Supervisory Board in 2003 (the "2003 Plan").

At December 31, 2011, Netia held 9,775,000 own treasury shares. On December 15, 2011 the Extraordinary General Meeting of the Company resolved to redeem these treasury shares. The redemption was effective from January 30, 2012, when the decrease of the Company's share capital was registered in in the National Court Registry. The redemption of shares in January 2012 resulted in a decrease of share capital by PLN 9,775,000 and a decrease in other supplementary capital by PLN 49,582,145, from which PLN 9,775,000 was transferred to the separate reserve capital of the Company established in accordance with Article 457, §2 of the Commercial Companies Code.

As a result at December 31, 2012, the Company's share capital consisted of 386,279,904 ordinary shares and 1,000 series A1 shares with a par value of PLN 1 per share. Each share had one vote at shareholders' meetings. All shares issued by the Company were fully paid and registered in the National Court Registry by the date of signing these consolidated financial statements.

Netia held 18,935,188 own treasury shares as at December 31, 2012. See Note 34: Dividends and repurchase of own shares.

The 5,115,579 series K shares issued prior to Netia's General Meeting of Shareholders held on May 26, 2010, were redesignated in accordance with a resolution adopted by Netia's General Meeting of Shareholders, as series B shares. Following this change of the Company's Statute in 2010, up to 13,258,206 series K shares could have been issued. The total number of series K shares issued through December 31, 2012 was 6,717,551 and their nominal value was PLN 6,717,551.

According to the information provided to the Company by its shareholders, as at December 31, 2012 the following shareholders held more than 5% of the votes in the General Shareholders Meeting:

	Number of shares (not in thousands)	% of share capital
Third Avenue Management LLC	69,013,736	17.87
ING Otwarty Fundusz Emerytalny	48,010,027	12.43
SISU Capital Limited and related entities	44,336,534	11.48
Aviva OFE	20,243,646	5.24
Shares held by public and other shareholders	204,676,961	52.98
	386,280,904	**100.00**

Other supplementary capital

The Annual General Meeting of the Company held on June 19, 2012, resolved that the Company's net profit for the year 2011, in the amount of PLN 225,004 and the retained earnings of PLN 726 relating to the adjustment made in 2010 to the Company's profit from 2009 and the previous years, shall be transferred to the Company's supplementary capital.

Distributable reserves

In accordance with the Polish Code of Commercial Companies of 15 September 2000 (Journal of Laws of 2000, No. 94, item 1037 as amended) only those reserves, which relate to net profits of individual companies shown in their statutory financial statements, are available for distribution to shareholders. As at December 31, 2012, the distributable reserve amounted to PLN 480,636.

Stock options (not in thousands)

2003 Plan

As at December 31, 2011 the total number of options approved by the Supervisory Board and issued was 87,877,470. Out of these approved options 46,754,751 options were outstanding as at December 31, 2011 and exercisable until December 20, 2012.

In the year ended December 31, 2012 and 2011 the following changes took place in the number of options granted under the 2003 Plan:

	Year ended December 31, 2012		Year ended December 31, 2011 (restated)*	
Options	**Average strike price**	**Options**	**Average strike price**	**Options**
At the beginning of the period	6.22	46,754,751	5.89	54,245,436
Granted	-	-	-	-
Exercised	4,98	(23,966,937)	3.60	(6,815,685)
Forfeited / expired	7,52	(22,787,814)	6.33	(675,000)
At the end of the period	**-**	**-**	**6.22**	**46,754,751**

* in 2012 the Company found an error in its record of the number of outstanding options, which was due to a 1 mln overstatement in the number of forfeited options from 2008. The 2011 comparative information has been restated to reflect the above adjustments in number of outstanding options. The error had no impact on the Company's financial results neither in 2011 nor in earlier periods.

The Company recognizes the cost of share-based awards to employees (including share options) over the vesting period and the fair value of options is determined using a binomial pricing model. The cost of options recorded in year ended December 31, 2012 and 2011 amounted to 88 PLN thousands and PLN 1,037 thousands, respectively.

New Plan

As at December 31, 2012 and December 31, 2011, the total number of options approved by the Supervisory Board and issued under the New Plan was 7,322,000 and 3,653,000, respectively. Of these approved options 5,405,404 options were outstanding as at December 31, 2012 and 3,621,000 options were outstanding as at December 31, 2011. As at December 31, 2012, the weighted average remaining contractual life of the outstanding options was 7.5 years. The outstanding options are exercisable until May 26, 2020. Upon exercise of the options, Netia will issue to each exercising participant the number of shares representing such participant's gain resulting from the exercise of the options, being the difference between the market price of the Company's shares as of the date of exercise of the options and the strike price of the options, limited to half of one series L share for each option exercised. The participant will not be required to pay the strike price ranging from PLN 5.23 to PLN 6.16.

The Company recognizes the cost of share-based awards to employees (including share options) over the vesting period and the fair value of options is determined using a binomial pricing model and taking into account business performance criteria in the financial year in which the options were granted. The cost of options recorded in the year ended December 31, 2012 and 2011 amounted to PLN 1,686 thousands and PLN 937 thousands, respectively.

	Year ended December 31, 2012		Year ended December 31, 2011	
Options	**Average strike price**	**Options**	**Average strike price**	**Options**
At the beginning of the period	5.24	3,621,000	-	-
Granted	6.16	3,669,000	5.24	3,653,000
Forfeited/expired	5.26	(1,884,596)	5.24	(32,000)
At the end of the period	**5.86**	**5,405,404**	**5.24**	**3,621,000**

(All amounts in thousands, except as otherwise stated)

17. Provisions

	December 31, 2012 (PLN)	December 31, 2011 (PLN)
PON grants provision	16,596	45
USO provision	7,156	7,156
Loss on rental contract	2,084	1,307
Claims	3,301	4,194
Restructuring	1,482	96
Jubilee and retirement	1,157	2,356
Other	613	613
	32,389	**15,767**
Of which,		
Current	14,200	12,681
Non-current	18,189	3,086

	PON grants	Loss on rental contracts (PLN)	Claims (PLN)	Restructuring (PLN)	Jubilee and retirement (PLN)	USO provision (PLN)	Other (PLN)	Total (PLN)
As at January 1, 2012	45	1,307	4,194	96	2,356	7,156	613	15,767
Recognition and changes in estimates (charged to the income statement)	-	1,561	(224)	19,334	(968)	-	-	19,703
Used during the period	-	(892)	(669)	(17,948)	(231)	-	-	(19,740)
Discount unwinding (charged to the inco me statement)	-	108	-	-	-	-	-	108
Other movements	16,551		-	-	-	-	-	16,551
As at December 31, 2012	**16,596**	**2,084**	**3,301**	**1,482**	**1,157**	**7,156**	**613**	**32,389**

PON grants

Dialog has made significant investments in Passive Optical Networks ("PON") in recent years on the basis that a significant part of the investment will be reimbursed from European Union funds by Polish Agency for Enterprise Development ("PARP"). As at December 31, 2012 most reimbursements were recovered, however several commitments by Dialog towards PARP are still to be achieved. Given market conditions and the project of integrating with Netia, some of these requirements may not be achieved and the refunds may not be received in the amounts originally planned by Dialog. No assets have been recognized in respect to these grants in the acquisition balance sheet of Dialog and the PLN 16,596 already received has been provided for until such time that its long term retention becomes reasonably certain.

Loss on rental contracts

Provision for loss on rental contracts comprises:

- provision relating to a specific office space contract, which was recognized in 2011 upon the acquisition of Dialog Group. The loss on this rental contract is calculated as the discounted committed rental costs less discounted rental costs at estimated market level and amounts to PLN 619 as of December 31, 2012. The Netia Group expects that the cash outflows relating to this provision will be incurred through 2017;

- provision relating to the excess of office space held in certain locations in Warsaw and Wrocław following acquisitions and restructuring, some of which have been sub-leased at a loss by the Netia Group. The loss on rental contracts is calculated as discounted committed rental costs less discounted revenues expected to be received from sub-lessees. The provision amounts to PLN 1,465 as of December 31, 2012 The Netia Group expects that the cash outflows relating to this provision will be incurred through 2015.

Claims

The amounts represent provisions for legal and regulatory claims and for a contractual penalty due to delays in the performance of a contract. In the opinion of the Management the outcome of the outstanding provisions will not give rise to any significant losses beyond the amounts provided. The Netia Group is unable to determine the timing of cash outflows related to legal and regulatory claims with reasonable accuracy.

Restructuring

The balance as at December 31, 2012 comprise the provision created for those committed redundancies where the employment contract has not yet been terminated. The cash outflows relating to this provision are expected to be incurred during 2013. See also Note 26 Salaries and benefits.

(All amounts in thousands, except as otherwise stated)

Jubilee and retirement

The provision for jubilee and retirement severance payments was calculated by an independent actuary using the projected unit credit method. It represents the present value of the future obligation of the Company to make severance payments on its employee's retirement, required by the Polish Labour Code. A valuation was performed using a discount rate of 4.05% and a salary increase rate of 1.27% above inflation of 2.5%. Retirement severance payments will be paid on Netia Group employees upon their retirement.

Universal services obligation

The telecommunications law stipulates that the obligation to provide universal service should be designated by the President of UKE following completion of a tender procedure. The President of UKE issued a decision designating TP SA to provide universal service until May 8, 2011. Telecommunications undertakings, whose relevant annual revenue from telecommunications activity exceeds PLN 4,000, are obliged to participate in financing of the universal service obligation.

In May 2011 and in January 2012, the President of UKE considered the applications for awarding subsidy towards costs of universal service incurred in the period from May 8, 2006 until December 2010 that were filed by TP SA, and issued decisions by virtue of which TP SA was awarded subsidies towards incurred costs of several services falling within the scope of universal service, the total amount of which was PLN 122,096. Netia must receive individual decisions from the President of UKE as to its shares in the total amount before any amounts will be due and payable.

In view of the fact that, following the Regulator's decisions it is now possible to estimate the share of the companies of the Netia Group in the subsidy towards the incurred costs of services falling within the scope of universal service, the Management Board decided to establish a provision amounting to the value of Netia's estimated share in the awarded total subsidy.

The total share of all the companies in the Netia Group in the subsidy for this period from 2006 until 2011 inclusive was estimated at PLN 7,156 (see Note 40).

18. Borrowings

	December 31, 2012	December 31, 2011
	(PLN)	(PLN)
Bank loans	531,898	695,177
Bank overdraft	18,751	-
	550,649	**695,177**
Of which:		
Current	166,197	180,593
Non-current	384,452	514,584

Bank loans

On September 29, 2011, Netia and Internetia Sp. z o.o. (the "Borrowers") executed a loan agreement (the "Agreement") with Rabobank Polska S.A. (the "Facility Agent") and BNP Paribas S.A., BRE Bank S.A., Raiffeisen Bank Polska S.A. and Raiffeisen Bank International AG (jointly with the Facility Agent, the "Lenders"), whereunder the Lenders agreed to extend to the Borrowers a term facility maturing in five years with a total of PLN 650,000, designated for the Company to acquire 19,598,000 (not in thousands) shares Dialog, constituting 100% of its share capital, and a PLN 50,000 revolving facility for general operating purposes. The term loan was drawn on December 16, 2011 and the revolving loan was drawn on December 15, 2011. The revolving loan was repaid in full on March 15, 2012. Term loan instalments paid in 2012 amounted to PLN 130,000. As at December 31, 2012 the value of these loans at amortised cost was PLN 531,898.

The loan accrues annual interest at the rate of 3M WIBOR plus a margin established depending on the level of debt. The terms and conditions of the Agreement comply with market practice and are not different from the terms and conditions generally applied to such types of agreements. The borrowing is measured at amortized cost using an effective interest rate of 7.2%. Total transaction costs included in the calculation of the effective interest rate amounted to PLN 12,511. The carrying amount of the borrowings approximates their fair value and the discount rate for the fair value calculation approximates the effective interest rate.

To secure the Lender's claims under or related to the Agreement, the Borrowers agreed to establish in favour of the Lenders mortgages, financial and registered pledges and to make relevant representations on submission to enforcement, and to execute agreements on assignment as collateral security. The repayment of the loan is secured by the following: two capped mortgages on the right of perpetual usufruct of the Company's real estate at ul. Poleczki 13 in Warsaw, a registered pledge on a set of movables and rights of Netia and Internetia Sp. z o.o., registered pledges and financial pledges on the shares of Internetia Sp. z o.o., Netia Brand Management Sp. z o.o. and Dialog. Moreover, the Borrowers made relevant representations on submission to enforcement up to the amount of PLN 1,050,000.

On March 8, 2012, Netia entered into an overdraft credit facility agreement with BRE Bank S.A. of PLN 50,000. The facility will be disbursed for general operating purposes of the Company. The Company is entitled to become indebted under the facility agreement in the period between March 12, 2012 and December 27, 2012. On December 11, 2012, Netia signed amendment to the overdraft agreement, according to which it is entitled to become indebted until October 30, 2013. The terms and conditions of the agreement comply with market practice and are not different from the terms and conditions generally applied to such types of agreements. The outstanding balance of the overdraft credit as at December 31, 2012, amounted to PLN 18,751.

Moreover, as at December 31, 2011, the Netia Group had outstanding bank loans of PLN 1,583 drawn by the Company's subsidiary Petrotel Sp. z o.o., PLN 36 drawn by the Company's subsidiary Intergeo and PLN 319 drawn by the Company's subsidiary ComNet. The outstanding loans were repaid in full in 2012. Loans drawn by subsidiaries acquired by the Group in 2012: PLN 60 by STI and PLN 51 by Sanetja also were repaid in 2012.

(All amounts in thousands, except as otherwise stated)

19. Trade and other payables

	December 31, 2012 (PLN)	December 31, 2011 (PLN)
Trade payables	92,005	97,141
Investment payables	50,627	47,582
Accrued expenses (see Note 20)	93,803	80,816
VAT and other taxes	17,424	28,240
Crowley purchase price adjustment accrued	-	4,323
Finance lease payments	3,483	7,388
Other payables	6,998	7,128
	264,340	**272,618**
Of which,		
Current	260,108	263,226
Non-current	4,232	9,392

In addition, as at December 31, 2012 and December 31, 2011 the amounts of PLN 2,029 and PLN 1,869, respectively were excluded from other payables as they were legally reserved for social funding purposes.

20. Accrued expenses

	December 31, 2012 (PLN)	December 31, 2011 (PLN)
Construction costs	1,922	557
Uninvoiced services	34,822	31,595
Interconnection charges	22,888	21,451
Holiday accrual	5,753	6,588
Employees' bonuses and accrued salaries	20,929	15,129
Rental costs accrued	7,489	5,496
	93,803	**80,816**

21. Deferred income

	December 31, 2012 (PLN)	December 31, 2011 (PLN)
Invoiced income from subscriptions relating to future periods	33,228	33,770
Rental contracts	20,777	26,122
Government grants	445	529
Other	4,142	5,736
	58,592	**66,157**
Of which,		
Current	37,823	44,034
Non-current	20,769	22,123

(All amounts in thousands, except as otherwise stated)

22. Revenue

	Year ended December 31, 2012	Year ended December 31, 2011
	(PLN)	(PLN)
Direct voice	948,455	737,373
Monthly fees	*662,808*	*516,707*
Calling charges	*284,904*	*220,051*
Other	*743*	*615*
Indirect voice	34,976	22,469
Data	765, 658	604,188
Interconnection revenue	109,588	77,602
Wholesale services	136,242	124,375
Other telecommunication service revenue	113,789	48,014
Telecommunication revenue	**2,108,708**	**1,614,021**
Radio communication services revenue	3,540	4,352
Other services	9,108	430
Revenue	**2,121,356**	**1,618,803**

23. Cost of sales

	Year ended December 31, 2012	Year ended December 31, 2011
	(PLN)	(PLN)
Interconnection charges	(306,056)	(240,818)
Network maintenance	(647,586)	(530,240)
Cost of goods sold	(11,600)	(10,233)
Depreciation and amortization	(394,143)	(258,408)
Salaries and benefits	(41,101)	(22,034)
Restructuring	(5,608)	(384)
Taxes, frequency fees and other expenses	(78,122)	(40,912)
	(1,484,216)	**(1,103,029)**

24. Selling and distribution costs

	Year ended December 31, 2012	Year ended December 31, 2011
	(PLN)	(PLN)
Advertising and promotion	(36,663)	(46,610)
Third party commissions	(28,503)	(29,243)
Billing, mailing & logistics	(41,431)	(33,728)
Outsourced customer service	(30,034)	(32,060)
Provision for impaired receivables	(12,664)	(6,976)
Depreciation and amortization	(59,981)	(28,711)
Salaries and benefits	(118,592)	(85,638)
Restructuring	(9,619)	(164)
Other expenses	(54,582)	(34,123)
	(392,069)	**(297,253)**

25. General and administration costs

	Year ended December 31, 2012	Year ended December 31, 2011
	(PLN)	(PLN)
Professional services	(11,088)	(11,648)
Information technology services	(13,410)	(10,084)
Office and car maintenance	(18,125)	(11,771)
Depreciation and amortization	(28,367)	(21,637)
Salaries and benefits	(92,198)	(62,616)
Restructuring	(7,429)	(250)
Other expenses	(36,993)	(34,467)
	(207,610)	**(152,473)**

(All amounts in thousands, except as otherwise stated)

26. Salaries and benefits

	Year ended December 31, 2012 (PLN)	Year ended December 31, 2011 (PLN)
Wages and salaries	(214,852)	(147,495)
Social security costs and other benefits	(26,210)	(10,444)
Defined contribution plan (the State Plan)	(11,114)	(10,238)
Provision for retirement severance payment	1,199	(41)
Equity-settled share-based compensation	(1,773)	(1,974)
Cash-settled share-based compensation	(411)	(1,217)
Net change in accrual for PIT and social security costs relating to share-based compensation	1,270	1,121
Restructuring	(22,656)	(798)
	(274,547)	**(171,086)**

The Netia Group is legally required to make contributions to the Government's retirement benefit scheme in the form of social security payments. The Netia Group is not required to make any contributions in excess of this statutory rate.

Restructuring

Following the acquisition of Dialog Group and Crowley in December 2011 which significantly augmented the scale of the business, the Netia Group performed a comprehensive cost review across all functional areas of the Group and identified areas for operating cost optimization. The reorganization program includes a reduction of headcount, review of control and reporting processes, increase in work effectiveness, span of control increase and contract renegotiations. In connection with the restructuring program, in April 2012 the Netia Group announced a headcount reduction, which assumed a decrease of employment by approximately 519 full time employees and changes in terms of employment contracts of approximately 129 employees by the end of 2012.

Total reorganization costs recorded during the year period ended December 31, 2012 amounted to PLN 48,932 (out of which PLN 22,656 related to the restructuring program announced in April 2012 and PLN 26,276 related to integration costs) and were included in the following cost categories:

Year ended December 31, 2012	*Restructuring costs* (PLN)	*Integration costs* (PLN)
Cost of sales		
Salaries and benefits	(5,608)	(34)
Other	-	(207)
Selling and distribution costs		
Salaries and benefits	(9,619)	(12)
Other	-	(95)
General and administration costs		
Salaries and benefits	(7,429)	(8,870)
Other	-	(17,058)
	(22,656)	**(26,276)**

27. Other income

	Year ended December 31, 2012 (PLN)	Year ended December 31, 2011 (PLN)
Reminder fees and penalties	13,880	7,397
Forgiveness of liabilities	453	886
Reversal of impairment charges and provisions	1,398	1,534
Settlement of disputes	-	2,700
Returned VAT	1,264	1,015
Other operating income	5,443	2,440
	22,438	**15,972**

(All amounts in thousands, except as otherwise stated)

28. Other expenses

	Year ended December 31, 2012 (PLN)	Year ended December 31, 2011 (PLN)
Impairment charges for specific individual fixed assets (see Note 7)	(4,611)	(3,996)
Impairment charges for specific other assets	-	(126)
Other	(1,023)	(82)
	(5,634)	**(4,204)**

29. Other gains / (losses), net

	Year ended December 31, 2012 (PLN)	Year ended December 31, 2011 (PLN)
Gain on sale of impaired receivables	3,758	1,151
Gain on disposal of fixed assets	471	3,052
Net foreign exchange gains / (losses)	(255)	2
	3,974	**4,205**

30. Finance income and finance costs

Finance income

	Year ended December 31, 2012 (PLN)	Year ended December 31, 2011 (PLN)
Interest income on cash and cash equivalents	6,266	8,637
Amortization of held to maturity investments	1	7,488
Net foreign exchange gains	-	475
Fair value gains on open forward contracts hedging commercial exposures (see Note 15)	-	1,486
Other finance income	4	202
	6,271	**18,288**

Finance costs

	Year ended December 31, 2012 (PLN)	Year ended December 31, 2011 (PLN)
Interests and fees charged on bank loans	(43,185)	(2,503)
Interests and fees charged on overdraft	(67)	-
Amortization of finance lease liability	(394)	(307)
Amortization of provisions	(108)	(74)
Fair value loss on equity securities	(4)	(10)
Net foreign exchange losses	(82)	-
Fair value losses on open forward contracts hedging commercial exposures (see Note 15)	(1,945)	-
Excess of the amount of closed forward contracts over purchases made	(54)	-
Ineffective cash flow hedges (see Note 15)	(85)	(22)
Other finance costs	(289)	(794)
	(46,213)	**(3,710)**

31. Net foreign exchange gains / (losses)

The exchange differences credited / (charged) to the consolidated income statement are included as follows:

	Year ended December 31, 2012 (PLN)	Year ended December 31, 2011 (PLN)
Other gains / (losses), net	(255)	2
Finance income/ (costs)	(82)	475
	(337)	**477**

32. Corporate income tax

	Year ended December 31, 2012	Year ended December 31, 2011
	(PLN)	(PLN)
Current income tax charge	(1,149)	(217)
Adjustment in respect of current income tax for the year 2003	-	(34,183)
Penalty interests relating to current income tax for the year 2003	1,462	(17,680)
Deferred income tax charge, net	(27,111)	(16,410)
Income tax charge	**(26,798)**	**(68,490)**

Adjustment in respect of current income tax for the year 2003 (not in thousands)

In February 2010 the Director of the Tax Chamber in Warsaw ("Tax Chamber Director") issued a decision ("Decision") according to which Netia's corporate income tax due for the year 2003 was set at PLN 34.2 million plus penalty interest of approximately PLN 25.3 million. The decision closed proceedings related to Netia's appeal of a decision of the Director of the Tax Control Office in Warsaw ("UKS Director") according to which Netia's corporate income tax due for the year 2003 was originally set at PLN 58.7 million plus penalty interest amounting to PLN 41.3 million.

The decision of the Tax Chamber Director was issued despite legal arguments presented by the Company, which claimed that the conclusions delivered by the Tax Control Office were incorrect and groundless. According to the Tax Chamber Director and the UKS Director, Netia understated its taxable income by PLN 247.5 million by excluding from its revenues the accrued and not received interest from loans granted by Netia in earlier years to subsidiaries which subsequently merged with Netia on December 31, 2003. The Director of UKS, as the first instance tax authority, claimed in its earlier decision that Netia understated its taxable income by PLN 303 million.

The Tax Chamber Director's decision, which partially upheld the decision of the UKS Director, was enforceable as a decision of the second instance tax authority. The liability of PLN 59.6 million was settled in February 2010, from which PLN 1.3 million was returned by the tax office to Netia due to incorrect calculation of penalty interests by the Tax Authorities.

Netia received opinions from several independent tax and legal advisors, as well as tax law experts, which concluded that the claims of the Directors of the Tax Control Office and the Tax Chamber have no legal grounds. Accordingly, following the payment of the PLN 58.3 million and having recourse to two levels of independent civil court in which to obtain a positive ruling, Management took the position during 2010 that recovery through the courts is virtually certain and did not recognize the Tax Chamber's decision as a taxation expense for the financial year ended December 31, 2010 and instead treated funds paid over to the tax authorities as an overpayment of tax.

However, having heard Netia's appeal of the decision of the Tax Chamber Director, on March 15, 2011 the Voivodship Administrative Court ("WSA") in Warsaw announced a judgment with respect to the Decision and the Court dismissed the Company's claim in its entirety. On July 5, 2011 the Company received the written justification of this decision.

Following the WSA decision in favour of the tax office, Management recognizes that there is now only one instance remaining to obtain a favourable ruling and the existence of strong tax opinions is no longer sufficient to maintain the judgment that recovery is virtually certain.

Consequently, in the first quarter of 2011 the Company recognized the taxes and related penalty interest already paid in 2010 as an income tax expense relating to the year 2003 of PLN 58.3 million.

The Voivodship Administrative Court's judgment is not final. On August 3, 2011 the Company filed a cassation claim to the Supreme Administrative Court.

In November 2011 Netia claimed for return of the overpaid interests of PLN 6,462 thousand concerning penalty interests for the period between tax control proceeding and the delivery of the decision of the Tax Office Director. On December 31, 2011 Netia received the overpaid amount on the bank account. Moreover, in February 2012 a further PLN 1,462 thousand was recovered in overpaid interests.

(All amounts in thousands, except as otherwise stated)

Current income tax

The tax on the Netia Group's profit/(loss) before tax differs from the theoretical amount that would arise using the tax rate applicable to profits of the consolidated companies as follows:

	Year ended December 31, 2012 (PLN)	Year ended December 31, 2011 (PLN)
Profit/ (loss) before tax	(60,906)	317,276
Tax calculated at tax rates applicable to profit	11,572	(60,282)
Adjustments in respect of current income tax of previous years	1,462	(51,863)
Reversal of impairment loss for which no deferred tax asset had been recognised	-	20,837
Income and expense not subject / deductible for tax purposes, net	(15,992)	(6,198)
(Impairment loss)/reversal of impairment loss on assets not subject to tax	(15,049)	6,936
Recognition of previously unrecognized deferred tax asset	20,875	4,919
Derecognition of previously recognized deferred tax asset	(29,492)	-
Recognition of deferred tax assets on trademark	7,366	36,831
Derecognition of previously recognised deferred tax asset on tax losses and tax losses lost	(7,540)	(19,670)
Income tax charge	**(26,798)**	**(68,490)**

The corporate income tax rate applicable to the Company and its subsidiaries for 2012 and onwards is 19%.

Deferred income tax

The deferred income tax calculation is based upon the probability that future taxable profit will be available against which temporary differences, unused tax losses and unused tax credits can be utilized. That calculation is based upon Management's estimates, which are subject to considerable uncertainty and the actual outcome may differ. These estimates may be altered to reflect changes in the economic, technological and competitive environment in which the Netia Group operates.

As of December 31, 2012 the Management updated its previous year's assessment regarding the recognition of deferred income tax. The new assessment concluded that the Netia Group expects that future taxable profits will be generated based on the 2013 budget and long term business plan covering period until 2017. Management's assessment also considered factors such as: the stability and trend of past earnings, the nature of the business and industry, and the economic environment in which the Netia Group is located.

As at December 31, 2012 Netia Group had net deferred income tax asset of PLN 84,004. Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes relate to the same fiscal authority. Deferred income tax liabilities of PLN 17,686 presented in the consolidated statement of the financial position as of December 31, 2012 relate to net deferred income tax liabilities recognized in Netia and one of its subsidiaries (after intercompany eliminations).

	December 31, 2012 (PLN)	December 31, 2011 (PLN)
Deferred income tax assets	101,687	111,784
Deferred income tax liabilities	17,683	2,971
Deferred income tax assets, net	**84,004**	**108,813**

Deferred income tax assets and liabilities recognized on temporary deductible and taxable differences, without taking into consideration the offsetting of balances, are as follows:

	December 31, 2012 (PLN)	December 31, 2011 (PLN)
Deferred income tax assets:		
- Deferred income tax assets to be recovered after more than 12 months	90,370	126,364
- Deferred income tax assets to be recovered within 12 months	66,799	63,851
	157,169	190,215
Deferred income tax liabilities:		
- Deferred income tax liabilities to be recovered after more than 12 months	27,498	35,270
- Deferred income tax liabilities to be recovered within 12 months	45,667	46,132
	73,165	81,402
Deferred income tax assets, net	**84,004**	**108,813**

(All amounts in thousands, except as otherwise stated)

The movement in deferred income tax assets and liabilities during the period, without taking into consideration the offsetting of balances, is as follows:

Current period:

Deferred income tax assets	Tax losses	Impairment provisions for receivables	Depreciation and impairment	Accrued expenses	Interests	Forward contract	Other	Total
	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)
As at January 1, 2012	44,768	6,351	120,943	17,067	455	16	615	190,215
- Credited / (charged) to the income statement	19,842	2,568	(63,549)	3,686	1,977	2,456	(26)	(33,046)
As at December 31, 2012	**64,610**	**8,918**	**57,394**	**20,754**	**2,432**	**2,472**	**589**	**157,169**

Deferred income tax liabilities	Accrued income	Foreign exchange differences	Depreciation and impairment	Forward contract	Other	Total
	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)
As at January 1, 2012	8,690	180	66,644	517	5,371	81,402
- Charged / (credited) to the income statement	212	(180)	(9,946)	2,109	1,870	(5,935)
- Deferred income tax on acquisition	-	-	324	-	-	324
- Credited / (charged) to other comprehensive income	-	-	-	(2,626)	-	(2,626)
As at December 31, 2012	**8,902**	**-**	**57,022**	**-**	**7,241**	**73,165**

The deferred income tax recognized in equity in an amount of PLN 2,626 relates to movements in the hedging reserve.

Comparative period:

Deferred income tax assets	Tax losses	Impairment provisions for receivables	Depreciation and impairment	Accrued expenses	Foreign exchange differences	Forward contract	Other	Total
	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)
As at January 1, 2011	78,499	3,057	5,884	14,044	35	-	1,149	102,668
- Credited / (charged) to the income statement	(52,848)	301	36,929	(1,241)	417	16	(625)	(17,051)
- Deferred income tax on acquisition	19,117	2,993	78,130	4,264	2	-	92	104,596
- Credited / (charged) to other comprehensive income	-	-	-	-	-	-	-	-
As at December 31, 2011	**44,768**	**6,351**	**120,943**	**17,067**	**454**	**16**	**616**	**190,215**

Deferred income tax liabilities	Accrued income	Foreign exchange differences	Depreciation and impairment	Forward contract	Interest	Other	Total
	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)
As at January 1, 2011	11,304	10	34,301	63	805	3,423	49,906
- Charged / (credited) to the income statement	(3,925)	155	1,961	56	(805)	1,917	(641)
- Deferred income tax on acquisition	1,311	15	30,382	-	-	31	31,739
- Credited / (charged) to other comprehensive income	-	-	-	398	-	-	398
As at December 31, 2011	**8,690**	**180**	**66,644**	**517**	**-**	**5,371**	**81,402**

Deferred income tax assets are recognized for deductible temporary differences and tax loss carry-forwards to the extent that the realization of the related tax benefit through the future taxable profits is probable. As of December 31, 2012, the Netia Group had total deductible temporary differences of PLN 694,610 and unutilised tax loss carry-forwards of PLN 347,110 (total potential deferred income tax asset of PLN 197,927).

The Netia Group did not recognize deferred income tax assets of PLN 1,341 relating to tax losses of PLN 7,058 of the Company's subsidiaries, due to insufficient likelihood of future taxable profits to realize these tax losses before they expire. These unrecognized tax losses of the Netia Group available for use as at December 31, 2012 will expire in the following years: PLN 2,921 in 2013, PLN 2,737 in 2014, PLN 1,053 in 2015, PLN 289 in 2015 and PLN 58 in 2017.

Furthermore, due to the lack of conclusive evidence of future taxable profits, the Netia Group did not recognize deferred income tax assets of PLN 112,582, relating to deductible temporary differences of PLN 592,536 as follows:

	Timing differences (PLN)	Potential deferred income tax asset (PLN)
Depreciation and impairment	498,918	94,794
Trademark	77,539	14,732
Deferred income	8,958	1,702
Other	7,121	1,354
	592,536	**112,582**

The Polish tax system has restrictive provisions for grouping of tax losses for multiple legal entities under common control, such as those of the Netia Group. Thus, each of the Company's subsidiaries may only utilize its own tax losses to offset taxable income in subsequent years. Losses are not indexed to inflation. Tax losses are permitted to be utilized over five years with a 50% utilization restriction per annum.

33. Earnings per share

Basic

Basic earnings per share have been calculated based on the net profit attributable to the equity holders of the Company for each period divided by the weighted average number of shares in issue (reduced by treasury shares) during the year.

	Year ended December 31, 2012 (PLN)	Year ended December 31, 2011 (PLN)
Profit/ (loss) attributable to the equity holders of the Company	(87,704)	248,786
Weighted average number of ordinary shares in issue, excluding treasury shares (not in thousands)	379,014,108	388,558,494
Basic earnings/ (loss) per share (not in thousands)	(0.23)	0.64

Diluted

Diluted earnings per share for the net profit/ (loss) attributable to the equity holders of the Company are calculated adjusting the weighted average number of ordinary shares outstanding to assume conversion of all potentially dilutive ordinary shares. The Company had one category of potentially dilutive ordinary shares - the employees' share options (which upon their exercise trigger the issue of the series K and series L shares). For the share options a calculation was made to determine the number of shares that could have been acquired at fair value (determined as the average market share price of the Company's shares during 2012) based on the monetary value of the subscription rights attached to the outstanding share options. The number of shares outstanding was compared with the number of shares that would have been in issue assuming the exercise of the share options.

	Year ended December 31, 2012 (PLN)	Year ended December 31, 2011 (PLN)
Profit/ (loss) attributable to the equity holders of the Company	(87,704)	248,786
Weighted average number of ordinary shares in issue, excluding treasury shares (not in thousands)	379,014,108	388,558,494
Adjustments for:		
- Share options (not in thousands)	1,070,069	2,786,311
Weighted average number of ordinary shares for diluted earnings per share (not in thousands)	380,084,177	391,344,805
Diluted earnings/ (loss) per share (not in thousands)	(0.23)	0.64

34. Dividends and repurchase of own shares

No dividends have been proposed or paid in respect to the financial year ended December 31, 2011 and no proposal has been made by the Management for the year ended December 31, 2012 as at the date of these financial statements.

In accordance with the approved distribution policy, the Management Board proposed and the shareholders granted (by approval of resolution 18 at the annual General Shareholders' Meeting held on June 2, 2011) an authorisation to the Company's Management Board to purchase its own shares for the purpose of their redemption pursuant to the procedure set forth in in Art. 362 § 1 point 5 of the Commercial Companies Code (the "General Program"). The Annual General Meeting of the Company assigned the total amount of up to PLN 350,000 for the execution of the General Program, out of which the amount of up to PLN 267,032 shall be utilized from the supplementary capital created out of profits for the year 2010 and the amount of up to PLN 82,968 shall be utilized from the supplementary capitals created out of profits in the previous years. Any specific buy-back proposal within the scope of the General Program must be accepted by the Supervisory Board prior to the implementation.

The first tranche of share buy-backs approved under the General Program began on August 17, 2011. The Company allocated an amount of up to PLN 60,000 for the tranche to repurchase a maximum of 2.5% of the Company's outstanding share capital. On November 9, 2011 the Company completed the repurchase of 9,775,000 (not in thousands) own shares constituting 2.5% of the Company share capital for a total of PLN 49,582 and the tranche was completed. The repurchased shares were redeemed on January 30, 2012.

Netia obtained the relevant consent from its Supervisory Board and on May 18, 2012 commenced a further tranche of buy-backs. The Company allocated an amount of up to PLN 75,000 for the tranche to repurchase a maximum of 3.5% of the Company's outstanding share capital. On October 11, 2012 the Company completed the repurchase of 12,700,477 (not in thousands) shares constituting 3.29% of Company share capital for a total of PLN 75,000 plus transaction costs of PLN 103.

Netia obtained a third relevant consent from its Supervisory Board on June 19, 2012 and the Company commenced a third tranche of buy-backs on October 12, 2012. The Company has allocated an amount of up to PLN 50,000 for the third tranche to repurchase a maximum of 2.5% of the Company's outstanding share capital. As of December 31, 2012 the Company had repurchased 6,234,711 (not in thousands) own shares constituting 1.61% of Company share capital for a total of PLN 31,698 plus transaction costs of PLN 13.

Netia's distributable reserves are disclosed in Note 16.

35. Supplemental disclosures to the consolidated cash flow statement

Changes in working capital components:

	Year ended December 31, 2012 (PLN)	Year ended December 31, 2011 (PLN)
Receivables	7,400	(11,628)
Inventories	4,120	7,289
Prepaid expenses	(2,933)	14,920
Provisions, accruals and other payables	(12,988)	(5,380)
Deferred income	(7,588)	6,040
	(11,989)	**11,241**

Supplemental disclosures to operating activities:

	Year ended December 31, 2012 (PLN)	Year ended December 31, 2011 (PLN)
Income taxes (paid)/received	(233)	6,245
Interest received	6,267	19,259

Supplemental disclosures to investing activities:

	Year ended December 31, 2012 (PLN)	Year ended December 31, 2011 (PLN)
Subsidiaries purchased in current period	(5,285)	(994,985)
Subsidiaries purchased in previous period	(4,323)	-
Purchase of subsidiaries, net of cash received	**(9,608)**	**(994,985)**

Non-cash transactions:

During the year ended December 31, 2012 the Netia Group entered into finance lease agreements for telecommunication equipment. The carrying value of assets and liabilities recognized due to these transactions amounted to PLN 1,076 (PLN 5,500 in 2011).

36. The Management Board and Supervisory Board

Management Board

Effective January 1, 2012 Mr. Piotr Nesterowicz resigned from his position as a member of the Company's Management Board.

Effective March 16, 2012 Mr. Grzegorz Esz resigned from his position as a member of the Company's Management Board.

On April 25, 2012 the Supervisory Board of the Company appointed Mr. Mirosław Suszek as a member of the Management Board with effect from May 1, 2012.

Due to the above changes, as at December 31, 2012 the Company's Management Board consisted of the following members:

- Mirosław Godlewski – President,
- Jonathan Eastick – Chief Financial Officer,
- Tom Ruhan,
- Mirosław Suszek.

Supervisory Board

As at December 31, 2012 and December 31, 2011 the Company's Supervisory Board consisted of the following members:

- Benjamin Duster – Chairman,
- George Karaplis – Vice-Chairman,
- Stan Abbeloos,
- Raimondo Eggink,
- Nicolas Maguin,
- Ewa Pawluczuk,
- Tadeusz Radzimiński,
- Jerome de Vitry.

37. Related party transactions

Options granted to members of the Management Board (not in thousands)

On December 20, 2012 the 2003 Plan expired and 13,800,000 of unexercised options held by members of the Company's Management Board under the 2003 Plan were terminated. As at December 31, 2012 the total number of options held by members of the Company's Management Board under the New Plan was 2,402,351, none of which had vested as of that date. Strike prices for the options granted to the Management Board range between PLN 5.23 and 6.16 per share. The market price of the Company's shares at December 28, 2012 was PLN 4.28 per share.

The movements in the number of options held by Members of the Company's Management Board are presented below:

Options	2003 Plan Year ended December 31, 2012	New Plan Year ended December 31, 2012	Total Year ended December 31, 2012	Total Year ended December 31, 2011
At the beginning of the period	36,489,064	1,725,000	38,214,064	40,771,814
Granted		1,725,000	1,725,000	1,725,000
Exercised	(15,354,814)	-	(15,354,814)	(4,282,750)
Resignation from Management Board	(7,334,250)	(575,000)	(7,909,250)	-
Forfeited/terminated	(13,800,000)	(472,649)	(14,272,649)	-
At the end of the period	**-**	**2,402,351**	**2,402,351**	**38,214,064**

As at December 31, 2012 Mr. Mirosław Godlewski - the Company's President of the Management Board - held 1,028,675 options, none of which had vested. As at December 31, 2011 Mr. Mirosław Godlewski held 12,775,000 options, out of which 12,200,000 had vested.

As at December 31, 2012 Mr. Jonathan Eastick - a member of the Company's Management Board - held 514,338 options, none of which had vested. As at December 31, 2011 Mr. Jonathan Eastick held 9,859,314 options, out of which 9,571,814 had vested.

As at December 31, 2012 Mr. Tom Ruhan - a member of the Company's Management Board - held 514,338 options, none of which had vested. As at December 31, 2011 Mr. Tom Ruhan held 5,004,000 options, out of which 4,716,500 had vested.

As at December 31, 2012 Mr. Mirosław Suszek - a member of the Company's Management Board - held 345,000 options, none of which had vested

Number of shares held by members of the Management Board (not in thousands)

As at December 31, 2012 and December 31, 2011, the Company's President of the Management Board, Mr. Mirosław Godlewski, together with a company closely related to Mr. Godlewski, held 605,000 and 393,716 Netia shares respectively. During the year ended December 31, 2012, the company closely related to Mr. Godlewski, acquired 1,600,000 shares in Netia S.A. from Mr. Godlewski and subsequently disposed of 1,005,000 shares in Netia. Additionally, Mr. Godlewski directly disposed of 173,131 shares in Netia.

As at December 31, 2012 and December 31, 2011, Mr. Jonathan Eastick – a member of the Company's Management Board – held 450,000 and 499,175 shares of the Company, respectively.

As at December 31, 2012 and December 31, 2011, Mr. Tom Ruhan – a member of the Company's Management Board – and the company closely related to Mr. Tom Ruhan held 555,575 and 592,379 shares of the Company, respectively. During the year ended December 31, 2012, a company closely related to Mr. Ruhan acquired 1,057,011 shares in Netia S.A. from Mr. Ruhan and subsequently disposed of 501,436 shares in Netia S.A. Accordingly, the company closely related to Mr. Ruhan held 555,575 shares in Netia S.A. as at December 31, 2012.

Details of the changes in the number of shares held by members of the Company's Management Board during the year ended December 31, 2012 are presented below:

	December 31, 2011	Received from exercise of options	Reductions in shareholdings	December 31, 2012
Mirosław Godlewski, (including closely related company holdings	393,716	1,389,415	(1,178,131)	605,000
Jonathan Eastick	499,175	572,188	(621,363)	450,000
Tom Ruhan, (including closely related company holdings)	592,379	464,632	(501,436)	555,575
Mirosław Suszek	-	-	-	-
Total	**1,485,270**	**2,426,235**	**(2,300,930)**	**1,610,575**

Participation Units in the Change of Control Transaction Bonus Scheme (not in thousands)

On April 25, 2012, the Supervisory Board approved a new bonus plan known as the Change of Control Transaction Bonus (CoCTB) for the Company's Management Board Members. The CoCTB is a cash settled share based bonus scheme under which up to 11,400,000 Participation Units (PUs) may be issued to Management Board Members. Each PU has a strike price of 7,00 zloty per share and a term of 36 months commencing on December 31, 2012. The strike price adjusts upward over time by one percent per month from 31 January 2013 and is reduced by any dividends paid out by the Company ("the Adjusted Strike Price"). In the event that an investor or consortium of investors holds at least 90 % of Netia's equity on or prior to December 31, 2015 ("Trigger Event"), each PU shall be worth the positive difference between the acquisition price paid in a successful tender offering that secures the 90 % share-holding and the Adjusted Strike Price. For the purpose of calculating the value of the PU, the acquisition price is capped at 10 zloty per share. Should a Trigger Event occur after December 31, 2012 and prior to the expiration of the PUs on December 31, 2015, the Company shall pay the cash equivalent of the value of the PUs to each participating Management Board Member who was fulfilling his duties as at December 31, 2012 and has not resigned from his position prior to such Trigger Event. See also Note 40.

As at December 31, 2012, the members of the Management Board held Participation Units in the Change of Control Transaction Bonus Scheme as follows:

	Number of Participation Units
Mirosław Godlewski	3,800,000
Jonathan Eastick	1,900,000
Tom Ruhan	1,900,000
Mirosław Suszek	1,900,000
Total	9,500,000

A further 1,900,000 Participation Units may be assigned by the Supervisory Board.

See also Possible liabilities under the Change of Control Transaction Bonus Scheme in Note 40.

Number of shares held by members of the Supervisory Board (not in thousands)

As at December 31, 2012 and December 31, 2011, Mr. Benjamin Duster – Chairman of the Company's Supervisory Board – held nil and 21,000 shares of the Company, respectively.

As at December 31, 2012 and December 31, 2011, Mr. George Karaplis – Vice-Chairman of the Company's Supervisory Board – held nil and 20,000 shares of the Company, respectively.

As at December 31, 2012 and December 31, 2011, Mr. Raimondo Eggink – a member of the Company's Supervisory Board – held 40,000 shares of the Company.

As at December 31, 2012 and December 31, 2011, Mr. Nicolas Maguin, – a member of the Company's Supervisory Board – held 21,300 shares of the Company.

As at December 31, 2012 and December 31, 2011, Mr. Tadeusz Radzimiński – a member of the Company's Supervisory Board – held 20,001 shares of the Company.

As at December 31, 2012 and December 31, 2011, Mr. Jerome de Vitry – a member of the Company's Supervisory Board – held 20,000 shares of the Company.

As at December 31, 2012 and December 31, 2011, Mr. Stan Abbeloos– a member of the Company's Supervisory Board – held nil shares of the Company.

Restricted Stock Units (not in thousands)

As at December 31, 2012 and December 31, 2011, the total number of outstanding Restricted Stock Units ("RSU") granted to the members of the Company's Supervisory Board was 715,000 and 640,000, respectively. RSUs entitle the holder to receive additional cash remuneration equal to the value of restricted stock units, which corresponds to the market price of the Company's shares. The vesting period for the RSU ranges from 12 to 36 months after the grant date. The Company recognizes the cost of cash-settled share-based payment transactions (including RSU) over the vesting period by accruing cost provisions pro-rata to elapsed time and the market price of the Company's shares. The cost of RSUs recorded in the year ended December 31, 2012 amounted to PLN 411 thousands (PLN 1,217 thousands in the year ended December 31, 2011).

Changes in the number of RSU held by members of the Company's Supervisory Board in the year ended December 31, 2012 are presented below:

	December 31, 2011	RSU granted	RSUs exercised	December 31, 2012
Stan Abbeloos	80,000	15,000	(15,000)	80,000
Benjamin Duster	80,000	15,000	(15,000)	80,000
Raimondo Eggink	80,000	15,000	-	95,000
George Karaplis	80,000	15,000	(15,000)	80,000
Nicolas Maguin	80,000	15,000	-	95,000
Ewa Pawluczuk	80,000	15,000	-	95,000
Jerome de Vitry	80,000	15,000	-	95,000
Tadeusz Radzimiński	80,000	15,000	-	95,000
Total RSU	**640,000**	**120,000**	**(45,000)**	**715,000**

Management Board remuneration

Compensation and related costs associated with members of the Company's Management Board during year ended December 31, 2012 and December 31, 2011 amounted to PLN 7,696 and PLN 5,832, respectively. In addition, the gross cost of share-based payments in the amounts of PLN 905 and PLN 1,315 was recognized in the respective periods.

Moreover, upon exercise of the options, Management Board members received the following number of shares with a par value of PLN 1 (not in thousands) per share for which they were not required to pay (PIT and social security cost were incurred by the Company).

	Year ended December 31, 2012	**Year ended December 31, 2011**
Number of shares (not in thousands)	2,995,630	1,436,490
PIT and employee ZUS costs incurred by the Company (PLN)	1,605	770

Amounts paid and payable to former Management Board members in the course of termination of their employment relationship with the Netia Group during the year ended December 31, 2012 totalled PLN 879.

Compensation and related costs associated with members of the Management Boards of the Company's subsidiaries during the years ended December 31, 2012 and December 31, 2011 amounted to PLN 1,830 and PLN 721, respectively.

Amounts paid and payable to former members of Management Boards of the Company's subsidiaries in the course of termination of their employment relationship with the Netia Group during the year ended December 31, 2012 totalled PLN 386. These amounts were paid to certain employees and one non-employee of the Netia Group who are neither past nor present members of the Management Board of Netia S.A.

Additional to the above, termination benefits of PLN 241 and PLN 363 for the former members of the Management Board of the Company's subsidiaries were recognized as a cost in 2012 and 2011 respectively. These amounts were paid to certain employees of the Netia Group who were neither past nor present members of the Management Board of Netia S.A.

Supervisory Board remuneration

Compensation and related costs associated with members of the Company's Supervisory Board during the years ended December 31, 2012 and December 31, 2011 amounted to PLN 840 and PLN 840, respectively.

Incidental expenses of the Supervisory Board Members reimbursed by the Company amounted to PLN 342 and PLN 194 during the years ended December 31, 2012 and 2011, respectively, and mainly related to travel and accommodation.

Compensation and related costs associated with members of the Company's Supervisory Boards of the Company's subsidiaries during the years ended December 31, 2012 and December 31, 2011 amounted to PLN 76 and PLN 13, respectively. This amount was paid to persons who were neither past or present members of Netia's Management Board.

Other transactions with related parties

During the year ended December 31, 2012 the Netia Group has not been a party to any other material transactions, or proposed transactions, apart from transactions mentioned above, in which any member of the key management personnel or close members of their families, had or was to have a direct or indirect material interest.

(All amounts in thousands, except as otherwise stated)

38. Information on the registered audit company

The financial statements of Netia and the consolidated financial statements of the Netia Group for 2012 and 2011 were audited by Ernst & Young Audit Sp. z o.o. on the basis of a contract concluded on December 4, 2009.

The total fees specified in contracts with the registered audit company, payable or paid for the audit and review of the financial statements and for other services are presented below:

Item	**2012**	**2011**
Audit of stand-alone and consolidated financial statements	265	293
Review of stand-alone and consolidated financial statements	230	252
Audit of subsidiaries' financial statements	304	131
Other attest services	-	292
Total	**799**	**968**

39. Commitments

Capital commitments

Capital expenditures contracted for at the balance sheet date but not recognized in the consolidated financial statements amounted to PLN 15,536 as at December 31, 2012 and PLN 46,642 as at December 31, 2011of which, PLN 2,350 and PLN 2,841, respectively, related to the planned acquisition of intangible assets.

Operating lease commitments – where the Netia Group is the lessee

As at December 31, 2012 and December 31, 2011 the future minimum payments payable under non-cancellable operating leases were as follows:

	December 31, 2012 (PLN)	**December 31, 2011 (PLN)**
Not longer than 1 year	102,509	106,984
Longer than 1 year and not longer than 5 years	130,621	153,532
Longer than 5 years	59,666	65,506
	292,796	**326,022**

Operating lease arrangements mainly relate to the rental of buildings, land, network and vehicles. The periods of administrative building and land rentals do not exceed 30 years, network rentals range up to 20 years and vehicles are leased for 3 years. Rental costs recognized in the income statement for the years ended December 31, 2012 and December 31, 2011 amounted to PLN 578,834 and PLN 474,321, respectively. These rental costs are partially offset by income from sub-lessees in the amounts of PLN 5,518 and PLN 4,858, respectively.

Operating lease commitments – where the Netia Group is the lessor

The future minimum lease payments receivable under non-cancellable operating leases are as follows:

	December 31, 2012 (PLN)	**December 31, 2011 (PLN)**
Not longer than 1 year	16,578	22,354
Longer than 1 year and not longer than 5 years	32,595	21,991
Longer than 5 years	7,228	8,475
	56,401	**52,820**

The Netia Group has entered into several commercial leases on certain parts of its fixed telecommunications network. The periods of network rentals range up to 20 years. The relevant rents recognized in the income statement for the years ended December 31, 2012 and December 31, 2011 amounted to PLN 43,473 and PLN 33,028, respectively. The operating lease agreements do not relate to specific separate assets.

(All amounts in thousands, except as otherwise stated)

Finance lease commitments

As at December 31, 2012 and December 31, 2011 future minimum lease payments under finance leases together with the present value of net minimum lease payments were as follows:

	December 31, 2012 (PLN)	December 31, 2011 (PLN)
Not longer than 1 year	2,037	4,962
Longer than 1 year and not longer than 5 years	1,446	2,380
Longer than 5 years	-	-
Present value of minimum lease payments	**3,483**	**7,342**
Plus amount representing finance charges	368	470
Total minimum lease payments	**3,851**	**7,812**

40. Contingencies

Universal services

The telecommunications law stipulates that the obligation to provide universal service should be designated by the President of UKE following completion of a tender procedure. The President of UKE issued a decision designating TP SA to provide universal service until May 8, 2011. Telecommunications undertakings, whose relevant annual revenue from telecommunications activity exceeds PLN 4,000, are obliged to participate in financing of the universal service obligation. The exact participation amount of a telecommunications undertaking obliged to pay subsidy will be established by virtue of the President of UKE decision and cannot exceed 1% of revenues of a given telecommunications undertaking in a given calendar year.

TP SA filed with the President of UKE applications for awarding subsidy towards incurred costs of universal service provision. The applications cover subsidy towards costs incurred in the period from May 8, 2006, until May 8, 2011, i.e. the whole period of obligation to provide universal service by TP. The total amount claimed by TP SA on all applications for 2006-2011 was PLN 1,106,994. The last application was filed by TP on 29 June 2012 and included a request for subsidy for the period from January 1 to May 8, 2011 in the amount of PLN 33,837.

In May 2011, the President of UKE issued decisions by virtue of which TP SA was awarded subsidies towards incurred costs of several services falling within the scope of universal service as follows:

- in 2006 - amounting to PLN 745 - due to provision of facilities for customers with disabilities
- in 2007 - amounting to PLN 1,269 - due to provision of facilities for customers with disabilities
- in 2008 - amounting to PLN 1,830 - due to provision of facilities for customers with disabilities
- in 2009 - amounting to PLN 63,150 - due to provision of facilities for customers with disabilities as well as provision of telephone services with use of public pay phones

By virtue of a decision issued on September 7, 2011, the President of UKE upheld the decisions awarding subsidies towards incurred costs of universal service for years 2006-2009. TP SA challenged the decisions of the President of UKE before the Voivodeship Administrative Court (further "WSA"). WSA dismissed the complaints of TP SA against the decisions granting subsidy towards costs of provision of universal service in 2006 - 2009. TP appealed against sentences regarding subsidies for 2006 and 2007.

On January 10, 2012, the President of UKE issued decisions by virtue of which TP SA was awarded subsidies towards incurred costs of several services falling within the scope of universal service for 2010 amounting to PLN 55,102 due to provision of facilities for customers with disabilities as well as provision of telephone services with use of public pay phones.

This decision was upheld in decision of April 11, 2012. TP SA challenged those decisions before the WSA.

WSA dismissed the complaint of TP S.A. against the decision granting subsidy towards costs of provision of universal service in 2010.

The Management Board is convinced of the validity of the issued judgment, but cannot assure that appeal, in case of filing it by TP S.A. shall be dismissed by Supreme Administrative Court and the amounts of subsidies shall not be increased.

Jointly, TP SA was awarded the total amount of PLN 122,096 for the provision of universal service within the years 2006-2010.

Decision regarding subsidy towards costs of provision of universal service in the period from January 1, 2011 till May 8, 2012 has not been issued.

Despite the fact that in the opinion of the Management Board the application of the TP SA for reconsideration should not be admitted, and that so far the applications of TP SA for subsidies towards costs of universal service provision within 2006-2010 have been only partially admitted by the President of UKE, the Management Board is unable to assure neither that TP SA will not be finally awarded the subsidy for 2011, nor that the amount of the subsidy will not be established as higher than awarded in proportion to the sums claimed by the TP SA for the previous years.

The exact amount of share in the subsidies to costs of universal services to be payable by each telecommunications undertaking requires the President of UKE to issue individual decisions. Until the date of approval of these consolidated financial statement Companies of the Netia Group have received no such decisions.

The total amount of potential obligation of Companies of the Netia Group, estimated by the Management Board taking into account their market shares in 2006 – 2011, decisions of the President of UKE, in which the amounts of subsidies towards the costs of providing universal service in years 2006 – 2010 were granted in the total amount of PLN 122,096 and estimated amount of potential subsidy to the cost of USO for the year 2011, is PLN 7,156. In this amount, the Companies of the Netia Group have made a provision for covering potential obligations under the subsidy for universal service provided in the years 2006 – 2011.

Should TP SA prevail in any of mentioned litigation, the USO liability in respect to 2006 – 2011 could still rise materially above the amount provided to date.

On the basis of the full amount of subsidies claimed by TP SA and of the Company's estimations concerning revenues of telecommunications services providers that may participate in subsidies towards universal services, the amount of subsidy towards universal service that might conceivably be claimed by TP SA from the Netia Group amounts to approximately PLN 56,838 for the period from 2006 until 2011 inclusive as follows:

	Maximum subsidies	**Provision**
	PLN	*PLN*
2006	6,293	34
2007	10,862	63
2008	9,202	80
2009	11,964	3,199
2010	13,888	2,840
2011	4,629	940
	56,838	**7,156**

Pursuant to the decision of the President of UKE designating TP SA to provide universal service the above obligation of TP SA expired as of May 8, 2011. No undertaking obliged to provide USO as of May 8, 2011 has been designated to date and, according to the published position of the President of UKE, will not be. Nevertheless, on October 16, 2012 the President of UKE has begun consultations of new model of USO. At this stage of the Regulatory work on the model, the Management Board cannot assure that a new model of USO will not be associated with additional costs to be incurred by Netia Group.

WiMAX license requirements

On October 27, 2005 Netia WiMax S.A. (merged with Netia in 2006) and Netia WiMax II S.A. (merged with Netia in 2008) received the reservations of the 3.6-3.8 GHz frequencies, which are used to provide telecommunication services based on the WiMAX technology. The terms of licenses issued to the Company's former subsidiaries require them to meet annual connected capacity milestones in the future, as measured at the end of each year, subject to demand in the territory and population of Poland. Considering changes in the telecommunications market and, in particular, the advent of regulated access to the fixed line network of the incumbent fixed line operator, TP SA, the Company submitted applications to change future territorial and population coverage commitments for WiMax and on October 31, 2007 and on December 13, 2011 the Polish regulator issued decisions reducing the initial milestones. The milestones established for the year 2012 regarding population coverage and area coverage were achieved. In the event that reservation obligations are not met by an operator, the UKE has the power to limit or confiscate the reservation, if the entrepreneur is not able to assure effective use of possessed right. However, historically such measures have rarely been used.

Tax contingent liability

Regulations relating to value-added tax, corporate income tax, and payroll (social) taxes have radically changed in comparison to the tax regulations, which existed prior to the economic and political transformation in Poland. The lack of reference to well-established practices and the relatively short period in which these new tax regulations have been in place often results in a lack of clarity and consistency in the regulations. Frequent contradictions in legal interpretations both within government bodies and between companies and government bodies create uncertainties and conflicts. Tax settlements, together with other areas of legal compliance are subject to review and investigation by a number of authorities, which are entitled to impose severe fines, penalties and interest charges. These facts create tax risks in Poland that are substantially more significant than those typically found in countries with more developed tax systems. The tax authorities may at any time inspect the books and records of the Company and may impose additional tax assessments with penalty interest and penalties within 5 years from the end of the year when a tax is due.

Overpayment of tax (not in thousands)

On February 19, 2010 Netia received a binding and enforceable decision of the Director of the Tax Chamber according to which the Company's corporate income tax due for the year 2003 was set at PLN 34.2m plus penalty interest of approximately PLN 25.3m.

Netia executed the decision of the Tax Chamber Director, which was enforceable as a decision of the second instance tax authority, on February 23, 2010. Of the PLN 59.6m paid, PLN 1.3m was subsequently conceded by the Tax Authority as overpayment. During 2010, Netia treated the tax paid as a receivable in its accounts rather than as an expense, due to Management's expectations, based on the expert advice received, that the amounts paid will ultimately be recovered.

The Company appealed to the Voivodship Administrative Court against the decision issued by the Tax Chamber Director. However, on March 15, 2011 the Voivodship Administrative Court delivered a judgment dismissing the Company's claim in its entirety. Following the WSA decision in favour of the tax office in the first quarter of the year 2011 the Company recognized an income tax expense relating to the year 2003 of PLN 58,325 thousands.

On July 5, 2011 the Company received the written justification of this decision and the Company filed a cassation claim to the Supreme Administrative Court on August 3, 2011.

On December 30, 2011 Netia received further repayment of PLN 6.4m related to penalty interests paid previously by the Company and subsequently conceded by the Tax Authority as incorrectly claimed.

On February 22, 2012 Netia received payment of PLN 1.4m concerning penalty interests on the amount returned in December 2011.

Should the appeal to the Supreme Administrative Court be positive for the Company, the amount of unduly paid tax plus interest will be treated as an overpayment and must be returned by the tax authorities together with interest.

Netia will undertake all possible legal steps to prove that the decision of the Tax Chamber Director was groundless and reclaim the remaining net amount of PLN 51.9 m paid to tax office, together with related interest.

Possible liabilities under the Change of Control Transaction Bonus Scheme (CoCTB) (not in thousands)

Following a decision of the Supervisory Board on April 25, 2012, the current four members of Netia's Management Board have been awarded Participation Units (PUs) in a new cash paid bonus scheme known as the Change of Control Transaction Bonus Scheme (CoCTB). As of the date of these financial statements, a total of 9,500,000 from a possible 11,400,000 PUs have been allocated to the Management Board Members.

Each PU has a strike price of 7.00 zloty per share and a term of 36 months commencing on December 31, 2012. The strike price adjusts upward over time by one percent per month from January 31, 2013 and is reduced by any dividends paid out by the Company ("the Adjusted Strike Price"). In the event that an investor or consortium of investors holds at least 90 % of Netia's equity on or prior to December 31, 2015 ("Trigger Event"), each PU shall be worth the difference between the acquisition price paid in a successful tender offering that secures the 90 % share-holding and the Adjusted Strike Price. For the purpose of calculating the value of the PU, the acquisition price is capped at 10 zloty per share. Should a Trigger Event occur after December 31, 2012 and prior to the expiration of the PUs on December 31, 2015, the Company shall pay the cash equivalent of the value of the PUs to each participating Management Board Member who was fulfilling his duties as at December 31, 2012 and has not resigned from his position prior to such Trigger Event.

The PUs will expire without value if there is no Trigger Event on or prior to December 31, 2015 or if the Management Board Member to whom they are allocated resigns prior to the Trigger Event or if the Trigger Event occurs at a price below the Adjusted Strike Price. Conversely, had a Trigger Event occured for an acquisition price of 10 zloty or above occurred in January 2013 and if all four Management Board Members are still performing their duties at the Company on the day of the Trigger Event, the maximum possible liability incurred by the Company would have been 28,500,000 PLN. This amount will fall towards zero as December 31, 2015 approaches without a Trigger Event occurring and as the Adjusted Strike Price increases towards 10 zloty per share.

Given that Netia is not presently controlled by any single large investor and given that Management is not in possession of information concerning the circumstances under which existing large shareholders may consider disposing of their shares in the Company, it is not possible for Management to make a reliable estimate of the likelihood of a Trigger Event occurring during the validity period of the PUs or to reliably estimate at what price such a Trigger Event might occur. Accordingly, Management is presently unable to reliably estimate the fair value of the CoCTB contingent liability as would otherwise be required in accordance with IFRS 2, Share Based Payments.

41. Subsequent events

Repurchase of own shares

On January 23, 2013 the Company completed the third tranche of buy-bucks, under which the Company had repurchased 9,657,023 (not in thousands) shares constituting 2.5% of Company share capital for a total of PLN 47,579 plus transaction costs of PLN 20. As a result of these and earlier share buy-backs, Netia holds 22,357,500 (not in thousands) treasury shares from a total outstanding share capital of 386,280,904 (not in thousands) shares as at the date of these financial statements.

Release of a mortgage

In January 2013, one of the two capped mortgages relating to the Loan (see Note 18 Borrowings) was released by the Court. Moreover, due to the division of the other real estate into two plots and subsequent release of the mortgage on one of them, as at the date of these financial statements the loan is secured by one capped mortgage on the right of perpetual usufruct of part of the Company's real estate at ul. Poleczki 13.