Annual Financial Report

Containing:

- Independent auditors' opinion
- Consolidated financial statements
  as at and for the year ended December 31, 2010

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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 S.A. 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 2010 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.

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ERNST & YOUNG

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 2010, 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 2010 has been presented in Euros, as a matter of arithmetic computation using the official rate of the National Bank of Poland at 31 December 2010 of PLN 3.9603 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 z o o

Ernst &Young Audit sp. z o.o.

Warsaw, 21 February 2011

NETIA S.A.
CONSOLIDATED FINANCIAL STATEMENTS
As at and for the year ended December 31, 2010

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NETIA S.A.
CONSOLIDATED STATEMENT OF FINANCIAL POSITION
as at December 31, 2010

(All amounts in thousands, except as otherwise stated)

	Note	December 31, 2009 (Restated)	December 31, 2010	Convenience Translation December 31, 2010
		(PLN)	(PLN)	(EUR)
ASSETS				
Non-current assets				
Property, plant and equipment, net	7	1,386,727	1,475,682	372,619
Intangible assets	8, 9	388,811	389,444	98,337
Investment property	10	35,574	45,084	11,384
Deferred income tax assets	34	79,400	52,762	13,323
Available for sale financial assets		10	10	3
Long term receivables	12	676	217	55
Prepaid expenses and accrued income	14	7,555	10,508	2,653
Total non-current assets		**1,898,753**	**1,973,707**	**498,374**
Current assets				
Inventories	11	3,143	11,393	2,877
Trade and other receivables	12	173,519	139,691	35,272
Tax Office receivables	13	-	58,325	14,727
Current income tax receivables		59	120	30
Prepaid expenses and accrued income	14	20,216	37,876	9,564
Derivative financial instruments	17	110	117	30
Financial assets at fair value through profit and loss	17	3,660	1	-
Held to maturity investments	15	58,489	171,616	43,334
Restricted cash	16	2,330	2,123	536
Cash and cash equivalents	16	181,203	173,600	43,835
		442,729	**594,862**	**150,205**
Assets classified as held for sale		87	-	-
Total current assets		**442,816**	**594,862**	**150,205**
Total assets		**2,341,569**	**2,568,569**	**648,579**

Mirosław Godlewski
President of the Company

Piotr Nesterowicz
Member of the Management Board

Jonathan Eastick
Member of the Management Board
Chief Financial Officer

Tom Ruhan
Member of the Management Board

Grzegorz Esz
Member of the Management Board

Warsaw, Poland
February 21, 2011

NETIA S.A.
CONSOLIDATED STATEMENT OF FINANCIAL POSITION (CONT'D)
as at December 31, 2010

(All amounts in thousands, except as otherwise stated)

	Note	December 31, 2009 (Restated)	December 31, 2010	Convenience Translation December 31, 2010
		(PLN)	(PLN)	(EUR)
EQUITY				
Share capital		389,277	389,459	98,341
Supplementary capital		1,356,652	1,599,299	403,833
Retained earnings		247,984	269,258	67,989
Other components of equity		32,264	39,530	9,982
Total equity	18	**2,026,177**	**2,297,546**	**580,145**
LIABILITIES				
Non-current liabilities				
Provisions	19	1,783	988	249
Deferred income	23	7,289	17,586	4,441
Other long term liabilities	21	12,672	8,847	2,234
Total non-current liabilities		**21,744**	**27,421**	**6,924**
Current liabilities				
Trade and other payables	21	248,791	206,768	52,210
Derivative financial instruments	17	4,423	849	214
Borrowings	20	347	31	8
Other financial liabilities		80	-	-
Current income tax liabilities		1	1	-
Provisions	19	4,893	1,855	468
Deferred income	23	35,113	34,098	8,610
Total current liabilities		**293,648**	**243,602**	**61,510**
Total liabilities		**315,392**	**271,023**	**68,434**
Total equity and liabilities		**2,341,569**	**2,568,569**	**648,579**

NETIA S.A.
CONSOLIDATED INCOME STATEMENT
for the year ended December 31, 2010

(All amounts in thousands, except as otherwise stated)

	Note	Year ended December 31, 2009 (Restated)	Year ended December 31, 2010	Convenience Translation Year ended December 31, 2010
		(PLN)	(PLN)	(EUR)
CONSOLIDATED INCOME STATEMENT				
Revenue	24	**1,505,871**	**1,569,296**	**396,257**
Cost of sales	25	(1,005,486)	(1,075,979)	(271,691)
Gross profit		**500,385**	**493,317**	**124,566**
Selling and distribution costs	26	(338,446)	(312,865)	(79,000)
General and administration costs	27	(173,458)	(142,249)	(35,919)
Other income	29	17,890	18,881	4,768
Other expenses	30	(2,068)	(1,222)	(309)
Other gains / (losses), net	31	9,965	8,709	2,199
Reversal of impairment losses	5	-	221,184	55,850
Operating profit / (loss)		**14,268**	**285,755**	**72,155**
Finance income	32	7,564	11,658	2,944
Finance costs	32	(20,707)	(8,644)	(2,183)
Profit before income tax		**1,125**	**288,769**	**72,916**
Income tax benefit / (charge)	34	87,572	(24,874)	(6,281)
Profit		**88,697**	**263,895**	**66,635**
Profit attributable to:				
Owners of the Company		88,697	263,895	66,635
Non-controlling interest		-	-	-
		88,697	**263,895**	**66,635**
Earnings per share (expressed in PLN per share)				
- basic	35	0.23	0.68	0.17
- diluted	35	0.23	0.67	0.17

(All amounts in thousands, except as otherwise stated)

	Note	Year ended December 31, 2009 (Restated)	Year ended December 31, 2010	Convenience Translation Year ended December 31, 2010
		(PLN)	(PLN)	(EUR)
CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME				
Profit		**88,697**	**263,895**	**66,635**
Cash flow hedges (acquisition of Tele2 Polska)		284	-	-
Cash flow hedges (equipment and construction contracts)	17	(2,391)	2,060	520
Income tax relating to components of other comprehensive income		454	(391)	(99)
Other comprehensive income		**(1,653)**	**1,669**	**421**
TOTAL COMPREHENSIVE INCOME		**87,044**	**265,564**	**67,056**
Total comprehensive income attributable to:				
Owners of the Company		87,044	265,564	67,056
Non-controlling interest		-	-	-
		87,044	**265,564**	**67,056**

	Note	Share capital	Supplementary capital: Share premium	Supplementary capital: Other supplementary capital	Retained earnings	Employee share option scheme	Hedging reserve	Total equity
		(PLN)	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)
Balance as at January 1, 2009		**389,277**	**1,556,489**	**-**	**(41,244)**	**24,244**	**(284)**	**1,928,482**
Changes in accounting policies	3	-	-	-	694	-	-	694
Balance as at January 1, 2009 (restated)		**389,277**	**1,556,489**	**-**	**(40,550)**	**24,244**	**(284)**	**1,929,176**
Profit for the period		-	-	-	88,697	-	-	88,697
Other comprehensive loss		-	-	-	-	-	(1,653)	(1,653)
Total comprehensive income		-	-	-	88,697	-	(1,653)	87,044
Coverage of Netia's 2008 loss		-	(199,837)	-	199,837	-	-	-
Employee share option scheme:								
- value of services provided	18	-	-	-	-	9,957	-	9,957
Balance as at December 31, 2009		**389,277**	**1,356,652**	**-**	**247,984**	**34,201**	**(1,937)**	**2,026,177**

	Note	Share capital	Supplementary capital: Share premium	Supplementary capital: Other supplementary capital	Retained earnings	Employee share option scheme	Hedging reserve	Total equity
		(PLN)	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)
Balance as at January 1, 2010 (restated)		**389,277**	**1,356,652**	**-**	**247,984**	**34,201**	**(1,937)**	**2,026,177**
Profit for the period		-	-	-	263,895	-	-	263,895
Other comprehensive income		-	-	-	-	-	1,669	1,669
Total comprehensive income		-	-	-	263,895	-	1,669	265,564
Transfer of Netia's 2009 profit		-	-	242,621	(242,621)	-	-	-
Employee share option scheme:								
- value of services provided	18	-	-	-	-	5,809	-	5,809
- issuance of series K shares	18	182	30	-	-	(212)	-	-
Cost of issuance		-	(4)	-	-	-	-	(4)
Balance as at December 31, 2010		**389,459**	**1,356,678**	**242,621**	**269,258**	**39,798**	**(268)**	**2,297,546**

(All amounts in thousands, except as otherwise stated)

	Note	Year ended December 31, 2009 (Restated)	Year ended December 31, 2010	Convenience Translation Year ended December 31, 2010
		(PLN)	(PLN)	(EUR)
Cash flows from operating activities:				
Profit		**88,697**	**263,895**	**66,635**
Adjustments for:				
Depreciation and amortization	7, 9, 10	298,566	300,684	75,925
Reversal of impairment losses	5	-	(221,184)	(55,850)
Reversal of impairment charges for specific assets	7	-	(308)	(78)
Impairment charges for specific individual assets		2,068	1,216	307
Deferred income tax charge / (benefit)	34	(88,303)	25,431	6,421
Interest expense and fees charged on bank loans	32	4,520	5,998	1,515
Other interest charged/(earned)		430	(4,146)	(1,047)
Interest accrued on loans granted		(5)	-	-
Share-based compensation	18	10,332	6,491	1,639
Fair value (gains) / losses on financial assets / liabilities		1,171	(697)	(176)
Fair value (gains) / losses on derivative financial instruments		5,018	(1,254)	(317)
Foreign exchange losses		7,249	98	25
Gain on disposal of fixed assets		(7,369)	(8,120)	(2,050)
Gain on sale of investments		(148)	881	222
Changes in working capital	37	(22,107)	(21,177)	(5,347)
Overpaid tax	13	-	(58,325)	(14,727)
Net cash provided by operating activities		**300,119**	**289,483**	**73,097**
Cash flows from investing activities:				
Purchase of fixed assets and computer software		(237,774)	(193,234)	(48,793)
Purchase of operational networks	8	(2,850)	(818)	(207)
Proceeds from sale of fixed assets		48,847	24,224	6,117
Proceeds from sale of group of assets		2,000	-	-
Purchase of subsidiaries, net of cash received	8, 37	(57,762)	(14,141)	(3,571)
Purchase of treasury bonds / notes		(107,055)	(168,482)	(42,543)
Receipts of treasury bonds / notes		50,000	60,000	15,150
Sale of investments		999	3,395	857
Receipts from loans repaid		278	-	-
Net cash used in / provided by investing activities		**(303,317)**	**(289,056)**	**(72,990)**
Cash flows from financing activities:				
Finance lease payments		(3,392)	(5,820)	(1,470)
Loan payments	20	-	(681)	(172)
Payments of fees relating to bank loans		(3,645)	(1,431)	(361)
Net cash used in / provided by financing activities		**(7,037)**	**(7,932)**	**(2,003)**
Net change in cash and cash equivalents		**(10,235)**	**(7,505)**	**(1,896)**
Exchange losses on cash and cash equivalents		**(1,247)**	**(98)**	**(25)**
Cash and cash equivalents at beginning of period		192,685	181,203	45,756
Cash and cash equivalents at end of period		**181,203**	**173,600**	**43,835**

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, 2010 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 21, 2011.

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 the third quarter of 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 26 such operators with a total of 105,030 (not in thousands) active customers. Additionally, the Netia Group has acquired 7,810 (not in thousands) customers and local 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 has been expanded to cover mobile broadband services as well as mobile handset based voice and data services.

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.).

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, 2010, the Group's equity amounted to PLN 2,297,546 and the Netia Group had working capital of PLN 351,260 inclusive of cash available of PLN 173,600 and PLN 175,000 in nominal value of treasury notes. Furthermore, Netia's operations were free cash flow generative in 2010 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.

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, 2009	December 31, 2010
Subsidiaries held directly:		
InterNetia Holdings Sp. z o.o. (previously InterNetia Sp. z o.o.)	100	100
In2Loop Sp. z o.o.	100	100
Net 2 Net Sp. z o.o. (previously Netia Corpo Sp. z o.o.)	100	100
Netia 2 Sp. z o.o.	N/A	100
Subsidiaries held indirectly:		
eTychy Sp. z o.o.	100	100
Fornet Sp. z o.o.	N/A	100
Global Connect Sp. z o.o.	100	100
Igloonet Sp. z o.o	N/A	100
Internetia Sp. z o.o (previously Air Bites Polska Sp. z o.o.)	100	100
Multiplay Polska Sp. z o.o.	N/A	100
Pronet Sp. z o.o.	N/A	100
SSI Net Sp. z o.o.	N/A	100
UNI-Net Poland Sp. z o.o	100	100

Shares held by Netia in its subsidiaries give the Company a corresponding number 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, 2010, 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, 2009, except for new accounting standards adopted as of January 1, 2010.

Certain Group entities (acquired in 2009 and 2010) 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 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, 2010 of PLN 3.9603 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, 2010 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 2010	Relevant increase / (decrease) in the depreciation charge for the remaining useful life
		(PLN)	(PLN)
Computer software	- useful lives of certain assets were extended until the end of 2010	3,582	-
Fixed telecommunications network	- useful lives of certain assets were extended until the end of 2013	(187)	187
Telecommunications equipment	- useful lives of certain assets were extended until the end of 2013	(4,061)	4,061
Machinery and equipment	- useful lives of certain assets were extended until the end of 2013	(269)	269
Total impact		**(935)**	**4,517**

Changes in presentation

The prior year financial information has been restated in respect of presentation of the long-term part of the Company's obligation resulting from rental contracts' of PLN 7,159, which previously were presented as trade and other payables. The Company's management believes that the presentation of the long-term part of the Company's obligation in respect of future rental contracts' expenditures as other long-term liabilities better reflects their character. The following adjustments were made in this respect:

As of December 31, 2009:

Net decrease in trade and other payables: PLN 7,159
Net increase in other long-term liabilities: PLN 7,159

As of January 1, 2009:

Net decrease in trade and other payables: PLN 3,894
Net increase in other long-term liabilities: PLN 3,894

New standards, interpretations and amendments to existing standards

Adoption of new accounting standards and interpretations

In 2010, the Netia Group adopted the following new standards, amendments to standards and new interpretations:

- Revised IFRS 3 "Business Combinations" and amendments to IAS 27 "Consolidated and Separate Financial Statements";
- Amendment to IAS 39 "Financial Instruments: Recognition and Measurement" - "Eligible Hedged Items";
- Amendments to IFRS 2 "Group Cash-settled Share-based Payment Transactions";
- Restructured IFRS 1 "First-time Adoption of International Financial Reporting Standards";
- Amendments to IFRS 1 "First-time Adoption of International Financial Reporting Standards: Additional Exemptions for First-time Adopters";
- Amendments to IFRS resulting from the annual improvements project;
- IFRIC 17, " Distributions of Non-cash Assets to Owners".

Amendment to IFRS 8 "Operating Segments" (included in the annual improvements project) clarified that an entity is required to disclose a measure of segment assets only if that measure is regularly reported to the chief operating decision-maker. The Netia Group do not use segment assets for internal reporting purposes and they are not used as a basis for decision making, therefore adoption of the amendment has resulted in a change in the content of related disclosures (see Note 6).

Revised IFRS 3 "Business Combinations" introduces significant changes in the accounting for business combinations occurring after January 1, 2010. Changes affect the valuation of non-controlling interest, the accounting for transaction costs, the initial recognition and subsequent measurement of contingent consideration and business combinations achieved in stages. These changes will impact the amount of goodwill recognized, the reported results in the period that an acquisition occurs and future reported results. The change in accounting policy was applied prospectively and had no material impact on the financial position of the Netia Group's operations.

Under the amendment to IAS 17 "Leases", a land lease with a lease term of several decades may be classified as a finance lease, even if at the end of the lease term title will not pass to the lessee, because in such arrangements substantially all risks and rewards are transferred to the lessee and the present value of the residual value of the leased asset is considered negligible. Prior to amendment, IAS 17 generally required a lease of land with an indefinite useful life to be classified as an operating lease. The Netia Group has reassessed the classification of land elements of unexpired leases and consequently leased land has been newly classified as a finance lease. The Netia Group recognized the assets at their fair value at the inception of those leases. The change

has been applied retrospectively. The prior year financial information has therefore been restated and the following adjustments were made:

As of January 1, 2009:

Net increase in property, plant and equipment: PLN 2,013
Net decrease in prepaid expenses: PLN 1,319
Net increase in opening retained earnings: PLN 694

As of December 31, 2009:

Net increase in property, plant and equipment: PLN 2,013
Net decrease in prepaid expenses: PLN 1,286
Net increase in opening retained earnings: PLN 694
Net decrease in cost of sales: PLN 33

Adoption of the other amendments and interpretations listed above did not have any effect on the financial position of the Netia Group's operations.

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 2010 and have not been adopted early:

- Amendment to IAS 32 "Financial Instruments: Presentation. Classification of Rights Issues" applicable for annual periods beginning on or after February 1, 2010. The amended standard clarifies the classification of rights issues;

- Revised IAS 24 "Related Party Disclosures" applicable for annual periods beginning on or after January 1, 2011. The revised standard simplifies the definition of a related party, clarifies its intended meaning and eliminates inconsistencies from the definition.

- IFRS 9 "Financial Instruments" applicable for annual periods beginning on or after January 1, 2013. IFRS 9 is the first part of 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;

- IFRIC 19, "Extinguishing Financial Liabilities with Equity Instruments", effective for annual periods beginning on or after July 1, 2010. This Interpretation addresses the accounting by an entity when the terms of a financial liability are renegotiated and result in the entity issuing equity instruments to a creditor of the entity to extinguish all or part of the financial liability.

- Amendments to IFRIC 14 "Prepayments of a Minimum Funding Requirement", effective for annual periods ending on or after January 1, 2011. The amendments apply in limited circumstances: when an entity is subject to minimum funding requirements and makes an early payment of contributions to cover those requirements. The amendments permit such an entity to treat the benefit of such an early payment as an asset.

- Amendment to IFRS 1 "Limited Exemption from Comparative IFRS 7 Disclosures for First-time Adopters" , effective for annual periods beginning on or after July 1, 2010. The amendment applies the same transition provisions for first-time adopters as for existing preparers of financial statements included in Amendments to IFRS 7 "Improving Disclosures about Financial Instruments";

- Amendments to IFRS resulting from the annual improvements project, effective for annual periods beginning the earliest on or after July 1, 2010, depending on which IFRS the amendment relates to. The amendments have not yet been endorsed by the EU.

- 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 securitisation of financial assets. Entities are required to apply the amendments for annual periods beginning on or after 1 July 2011. The amendments 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. The amendments have not yet been endorsed by the EU.

- 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. The amendments have not yet been endorsed by the 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.

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 31,2010 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 to 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 cash equivalents

Cash and cash equivalents 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

The Netia Group operates an equity-settled, share-based compensation plan. Shares 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. The vesting period for the options ranges up to three years from the date of grant or upon achieving certain specified conditions.

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. 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.

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. 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 the 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, 2010 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, 2010, if the Polish Złoty had weakened (strengthened) by 1% against Euro with all other variables held constant, consolidated profit for the year ended December 31, 2010 would have been PLN 2 higher (lower), mainly as a result of foreign exchange gains (losses) on translation of Euro denominated cash deposits and trade receivables, partially offset by Euro denominated trade and investment payables. Furthermore, at December 31, 2010, the hedging reserve in shareholders' equity would have been PLN 106 higher (lower) and the profit for the year ended December 31, 2010 would have been PLN 160 higher (lower), as a result of fair value gains (losses) on Euro denominated forward contracts.

At December 31, 2009, 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, 2009 would have been PLN 35 lower (higher), mainly as a result of foreign exchange gains (losses) on translation of Euro denominated trade, investment and other payables partially offset by Euro denominated cash deposits and trade receivables. Furthermore, at December 31, 2009, the hedging reserve in shareholders' equity would have been PLN 167 higher (lower) and the profit for the year ended December 31, 2009 would have been PLN 214 higher (lower), as a result of fair value gains (losses) on Euro denominated forward contracts.

At December 31, 2010, 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, 2010 would have been PLN 50 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, 2010, the hedging reserve in shareholders' equity would have been PLN 69 higher (lower) and the profit for the year ended December 31, 2010 would have been PLN 40 higher (lower), as a result of fair value gains (losses) on U.S. Dollar denominated forward contracts.

At December 31, 2009, 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, 2009 would have been PLN 7 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, 2009, the hedging reserve in shareholders' equity would have been PLN 114 higher (lower) and the profit for the year ended December 31, 2009 would have been PLN 48 higher (lower), as a result of fair value gains (losses) on U.S. Dollar denominated forward contracts.

- Interest rate risk:

The Netia Group's exposure to the risk of changes in market interest rates relates primarily to 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, 2010, interest costs relating to finance lease obligations would have been PLN 45 (PLN 49 for the corresponding period in 2009) higher (lower).

- Price risk:

At December 31, 2009, the Netia Group was exposed to equity securities price risk because of its investment in equity of another entity that was publicly traded. If the market price of these shares had been higher (lower) by 1% as at December 31, 2009, finance costs recognized by the Netia Group in the consolidated income statement would have been PLN 12 lower (higher).

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 2010. 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 reserve 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	Between 1 and 2 years	Between 2 and 5 years	Over 5 years
	(PLN)	(PLN)	(PLN)	(PLN)
As at December 31, 2010				
Bank borrowings	31	-	-	-
Trade and other payables excluding statutory liabilities	199,312	3,386	5,461	-
As at December 31, 2009 (restated)				
Bank borrowings	347	-	-	-
Trade and other payables excluding statutory liabilities	217,399	5,888	5,279	-
Other financial liabilities	80	-	-	-

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.

As at December 31, 2010	Less than 1 year	Between 1 and 2 years	Between 2 and 5 years	Over 5 years
	(PLN)	(PLN)	(PLN)	(PLN)
EUR forward contracts				
Inflows	25,992	-	-	-
Outflows	(26,525)	-	-	-
Net	(533)	-	-	-
Discounted at the applicable interbank rates	(525)	-	-	-
USD forward contracts				
Inflows	7,678	-	-	-
Outflows	(8,008)	-	-	-
Net	(330)	-	-	-
Discounted at the applicable interbank rates	(324)	-	-	-

As at December 31, 2009	Less than 1 year	Between 1 and 2 years	Between 2 and 5 years	Over 5 years
	(PLN)	(PLN)	(PLN)	(PLN)
EUR forward contracts				
Inflows	34,281	-	-	-
Outflows	(36,798)	-	-	-
Net	(2,517)	-	-	-
Discounted at the applicable interbank rates	(2,504)	-	-	-
USD forward contracts				
Inflows	14,971	-	-	-
Outflows	(16,904)	-	-	-
Net	(1,933)	-	-	-
Discounted at the applicable interbank rates	(1,919)	-	-	-

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, 2010:

	Level 1	Level 2	Level 3	Total balance
	(PLN)	(PLN)	(PLN)	(PLN)
Assets				
Financial assets at fair value through profit or loss				
- Trading securities	1	-	-	1
Derivatives used for hedging	-	117	-	117
Available-for-sale financial assets	-	-	10	10
Total assets	**1**	**117**	**10**	**128**
Liabilities				
Derivatives used for hedging	-	849	-	849
Total liabilities	**-**	**849**	**-**	**849**

The following table presents the Netia Group's assets and liabilities that are measured at fair value at December 31, 2009:

	Level 1	Level 2	Level 3	Total balance
	(PLN)	(PLN)	(PLN)	(PLN)
Assets				
Financial assets at fair value through profit or loss				
- Trading securities	3,060	-	-	3,060
- Trading derivatives	-	600	-	600
Derivatives used for hedging	-	110	-	110
Available-for-sale financial assets	-	-	10	10
Total assets	**3,060**	**710**	**10**	**3,780**
Liabilities				
Financial assets at fair value through profit or loss				
- Trading derivatives	-	80	-	80
Derivatives used for hedging	-	4,423	-	4,423
Total liabilities	**-**	**4,503**	**-**	**4,503**

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.

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.

As at December 31, 2010 and December 31, 2009, the Netia Group had net cash available of PLN 173,536 and PLN 181,203, respectively.

Financial instruments by category

December 31, 2010	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	-	-	-	10	-	10
Trade and other receivables excluding statutory receivables	139,421	-	-	-	-	139,421
Derivative financial instruments	-	-	117	-	-	117
Financial assets at fair value through profit or loss	-	1	-	-	-	1
Held to maturity investments	-	-	-	-	171,616	171,616
Restricted cash	2,123	-	-	-	-	2,123
Cash and cash equivalents	173,600	-	-	-	-	173,600
Total financial assets	**315,144**	**1**	**117**	**10**	**171,616**	**486,888**

December 31, 2010	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	-	-	-	7,335	7,335
Trade and other payables excluding statutory liabilities	-	-	200,825	-	200,825
Derivative financial instruments	-	849	-	-	849
Borrowings	-	-	31	-	31
Other financial liabilities	-	-	-	-	-
Total liabilities	**-**	**849**	**200,856**	**7,335**	**209,040**

December 31, 2009 (restated)	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	-	-	-	10	-	10
Trade and other receivables excluding statutory receivables	173,509	-	-	-	-	173,509
Derivative financial instruments	-	-	110	-	-	110
Financial assets at fair value through profit or loss	-	3,660	-	-	-	3,660
Held to maturity investments	-	-	-	-	58,489	58,489
Restricted cash	2,330	-	-	-	-	2,330
Cash and cash equivalents	181,203	-	-	-	-	181,203
Total financial assets	**357,042**	**3,660**	**110**	**10**	**58,489**	**419,311**

December 31, 2009 (restated)	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	-	-	-	10,591	10,591
Trade and other payables excluding statutory liabilities	-	-	217,427	-	217,427
Derivative financial instruments	-	4,423	-	-	4,423
Borrowings	-	-	347	-	347
Other financial liabilities	80	-	-	-	80
Total liabilities	**80**	**4,423**	**217,774**	**10,591**	**232,868**

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	Total goodwill
	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)
As at December 31, 2010	146,162	10,006	-	3,278	159,446
As at December 31, 2009	136,640	10,006	-	3,278	149,924

For the purpose of impairment testing of other non-financial assets the Management identified the entire Netia Group (besides non-current assets of UNI-Net Poland Sp. z o.o.) as one cash-generating unit (“CGU”). Non-current assets of UNI-Net Poland Sp. z o.o. represent a separate CGU and no indications of impairment have been identified for them.

The recoverable amount of goodwill allocated to operating segments 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. The business plan assumptions are consistent with the main strategic objectives announced by Netia in January 2011. Only currently active projects are included in projections. As a result, cash-flows from expected future acquisitions of Ethernet operators or from investments in TV services and network upgrades 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 -1.2%, which is compatible with the industry projections for the operations concerned. The discount rate used of 13.9% (in 13.2% 2009) 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 11.75% (12.1% in 2009). The pre-tax WACC increased while the post tax WACC fell due to an increasing estimate of future taxes payable between the 2009 and 2010 impairment tests.

The impairment test of non-current assets showed that the recoverable amount, before tax, of the CGU was higher by 221,184 PLN than its carrying value (before the reversal of the impairment losses) and any adverse change in a key assumption would result in a lower amount of impairment reversal or a further impairment loss, whilst any favorable change would result in a higher reversal of previously recorded impairments. The results of the test are highly sensitive to key assumptions as illustrated in the following table:

	Impairment reversal / (charge)	
Change in key assumptions	(PLN)	(PLN)
WACC of 13.9% pre-tax		
(increase / decrease by 1 percentage point)	(113,351)	129,448
Terminal growth rate of -1.2 % per annum		
(increase / decrease by 1 percentage point)	78,805	(69,019)
Cash flow projections 2011 - 2015		
(increase / decrease by 1% in each year)	18,740	(18,740)

The recoverable amount of goodwill allocated to operating segments is higher than their carrying amounts and as a result no impairment loss has been recognized. Sensitivity of the estimated pre-tax WACC of 13.9% 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 impairment loss on goodwill if pre-tax WACC of 13.9% had been increased to	15.6%	25.9%	26.8%	24%

As a result of the impairment test of non-current assets as of December 31, 2010 the Netia Group has recognized 221,184 PLN of reversal of impairment losses in profit and loss during the year ended December 31, 2010.

The reversal of the impairment loss for the CGU was allocated to the assets of the unit that had previously been impaired, except for goodwill, pro rata with the carrying amounts of these assets. In case the carrying amount of an individual asset would be increased above the lower of its recoverable amount and the carrying amount that would have been determined (net of amortization or depreciation) had no impairment loss been recognized for the asset in prior periods, the amount of the reversal of the impairment loss that would otherwise have been allocated to the asset, was allocated pro rata to the other assets of the CGU, except for goodwill. Following the reversal of 221,184 PLN of impairment losses a maximum additional amount of 261,438 of previously recognized impairment losses could be reversed as at December 31, 2010, should the results of future impairment test so require.

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, 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, 2010, including tax projections, the recognized deferred income tax assets as at December 31, 2010 amounted to PLN 52,762.

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 and competitive environment in which the Netia Group operates. Consequently, we may need to adjust the valuation of our deferred income tax assets, 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 2010 and previous years the Netia Group acquired 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 assets, 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.

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

The following tables present revenue and profit / (loss) information regarding the Netia Group's operating segments for the years ended December 31, 2010 and 2009, respectively:

	Home	SOHO / SME	Corporate	Carriers	Total reportable segments	Unallocated	Total
	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)
Year ended December 31, 2010							
Revenue from external customers	**823,761**	**184,746**	**343,823**	**209,912**	**1,562,242**	**7,054**	**1,569,296**
Adjusted EBITDA	**130,130**	**57,987**	**181,119**	**93,974**	**463,210**	**(103,716)**	**359,494**
Reversal of impairment losses	-	-	-	-	-	221,184	221,184
Profit on sale of P4 Transmission assets	-	-	-	7,298	7,298	-	7,298
Restructuring cost	-	-	-	-	-	(790)	(790)
Expenses incurred on mergers and acqusitions	-	-	-	-	-	(747)	(747)
EBITDA	**130,130**	**57,987**	**181,119**	**101,272**	**470,508**	**115,931**	**586,439**
Depreciation and Amortization	(73,842)	(51,055)	(102,247)	(39,505)	(266,649)	(34,035)	(300,684)
Operating profit / (loss)	**56,288**	**6,932**	**78,872**	**61,767**	**203,859**	**81,896**	**285,755**
Finance income / (cost), net	-	-	-	-	-	3,014	3,014
Income tax benefit / (charge)	-	-	-	-	-	(24,874)	(24,874)
Profit / (Loss)	**56,288**	**6,932**	**78,872**	**61,767**	**203,859**	**60,036**	**263,895**
Capital expenditure	72,930	16,895	58,767	16,796	165,388	34,819	200,207

(All amounts in thousands, except as otherwise stated)

	Home	SOHO / SME	Corporate	Carriers	Total reportable segments	Unallocated	Total
	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)
Year ended December 31, 2009 (Restated)							
Revenue from external customers	**772,008**	**179,448**	**349,514**	**198,249**	**1,499,219**	**6,652**	**1,505,871**
Adjusted EBITDA	**106,886**	**55,954**	**175,043**	**97,315**	**435,198**	**(131,246)**	**303,952**
Profit on sale of P4 Transmission assets	-	-	-	5,298	5,298	-	5,298
Restructuring cost	-	-	-	-	-	(11,742)	(11,742)
TP SA settlement	-	-	-	-	-	15,326	15,326
EBITDA	**106,886**	**55,954**	**175,043**	**102,613**	**440,496**	**(127,662)**	**312,834**
Depreciation and amortization	(36,126)	(24,033)	(141,664)	(65,229)	(267,052)	(31,514)	(298,566)
Operating profit / (loss)	**70,760**	**31,921**	**33,379**	**37,384**	**173,444**	**(159,176)**	**14,268**
Finance income / (cost), net	-	-	-	-	-	(13,143)	(13,143)
Income tax benefit / (charge)	-	-	-	-	-	87,572	87,572
Profit / (Loss)	**70,760**	**31,921**	**33,379**	**37,384**	**173,444**	**(84,747)**	**88,697**
Capital expenditure	78,146	15,954	87,698	31,804	213,602	32,821	246,423

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

	Year ended December 31, 2009 (Restated)	**Year ended December 31, 2010**
	(PLN)	(PLN)
EBIT for reportable segments	173,444	203,859
Radio communication segment	(220)	156
General fixed costs (incl. administration, IT, professional services)	(109,642)	(115,821)
Restructuring costs	(11,740)	(790)
Other operating (expenses) / income	(6,613)	10,757
Reversal of impairment losses	-	221,184
Depreciation and amortization of unallocated assets (excluding radio communication segment)	(30,961)	(33,590)
Finance income / (cost), net	(13,143)	3,014
Income tax benefit / (charge)	87,572	(24,874)
Profit / (Loss)	88,697	263,895

No single customer represented more than 10% of Netia's revenues in either 2009 or 2010. 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, 2010	45,526	5,127	2,026,040	1,895,760	110,263	123,778	5,993	107,791	4,320,278
Additions	685	-	172	327	410	845	71	169,442	171,952
Purchase of subsidiary	-	-	1,306	-	626	12	30	28	2,002
Purchase of operational networks	-	-	340	45	-	7	-	-	392
Transfers	17,840	-	48,714	115,005	5,917	5,009	234	(192,719)	-
Disposals	(2)	(148)	(56)	(44,841)	(3,183)	(56,971)	(4,749)	(1,286)	(111,236)
Other movements	(261)	-	425	(1,260)	1,069	(60)	(1)	-	(88)
Gross book value as at December 31, 2010	63,788	4,979	2,076,941	1,965,036	115,102	72,620	1,578	83,256	4,383,300
Accumulated depreciation as at January 1, 2010	20,203	-	794,051	910,493	64,420	100,844	3,668	-	1,893,679
Depreciation expense	3,531	-	74,494	140,272	6,833	6,289	573	-	231,992
Purchase of subsidiary	-	-	-	-	-	-	-	-	-
Disposals	(2)	-	(20)	(9,332)	(2,786)	(52,175)	(3,336)	-	(67,651)
Other movements	(46)	-	(199)	(854)	1,135	(56)	5	-	(15)
Accumulated depreciation as at December 31, 2010	23,686	-	868,326	1,040,579	69,602	54,902	910	-	2,058,005
Accumulated impairment as at January 1, 2010	7,341	1,125	631,419	368,640	18,404	10,133	30	2,780	1,039,872
Impairment charge for specific assets	-	-	-	-	-	-	-	1,216	1,216
Reversal of impairment charge for specific assets	-	-	-	-	-	-	-	(308)	(308)
Reversal of impairment charge (see Note 5)	(842)	(533)	(120,837)	(59,760)	(2,801)	(46)	(2)	-	(184,821)
Transfers	-	-	22	448	43	-	-	(513)	-
Disposals	-	(58)	(17)	(124)	(271)	(4,724)	(10)	(1,142)	(6,346)
Other movements	(8)	-	(41)	(403)	503	(51)	-	-	-
Accumulated impairment as at December 31, 2010	6,491	534	510,546	308,801	15,878	5,312	18	2,033	849,613
Net book value as at January 1, 2010	17,982	4,002	600,570	616,627	27,439	12,801	2,295	105,011	1,386,727
Net book value as at December 31, 2010	**33,611**	**4,445**	**698,069**	**615,656**	**29,622**	**12,406**	**650**	**81,223**	**1,475,682**

(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, 2009 (Restated)	36,121	5,408	1,967,921	1,774,688	107,218	123,729	9,435	100,744	4,125,264
Additions	218	-	652	321	200	925	201	219,582	222,099
Purchase of subsidiary	-	-	837	186	348	6	60	930	2,367
Purchase of operational networks	-	-	991	278	-	-	-	223	1,492
Transfers	8,092	-	43,106	150,509	6,316	4,924	-	(212,947)	-
Disposals	-	(281)	(931)	(21,960)	(470)	(2,982)	(3,703)	(741)	(31,068)
Other movements	1,095	-	13,464	(8,262)	(3,349)	(2,824)	-	-	124
Gross book value as at December 31, 2009	45,526	5,127	2,026,040	1,895,760	110,263	123,778	5,993	107,791	4,320,278
Accumulated depreciation as at January 1, 2009	17,176	-	722,284	766,238	61,793	96,268	4,457	-	1,668,216
Depreciation expense	2,878	-	72,181	144,851	6,646	6,994	1,547	-	235,097
Purchase of subsidiary	-	-	-	-	-	-	-	-	-
Disposals	-	-	(505)	(3,881)	(334)	(2,727)	(2,336)	-	(9,783)
Other movements	149	-	91	3,285	(3,685)	309	-	-	149
Accumulated depreciation as at December 31, 2009	20,203	-	794,051	910,493	64,420	100,844	3,668	-	1,893,679
Accumulated impairment as at January 1, 2009	7,313	1,238	631,450	369,263	17,837	10,372	30	1,538	1,039,041
Impairment charge for specific assets	-	-	-	-	-	-	-	1,683	1,683
Transfers	18	-	29	366	26	8	-	(447)	-
Disposals	-	(113)	(184)	(290)	(26)	(244)	-	6	(851)
Other movements	10	-	124	(699)	567	(3)	-	-	(1)
Accumulated impairment as at December 31, 2009	7,341	1,125	631,419	368,640	18,404	10,133	30	2,780	1,039,872
Net book value as at January 1, 2009	11,632	4,170	614,187	639,187	27,588	17,089	4,948	99,206	1,418,007
Net book value as at December 31, 2009	**17,982**	**4,002**	**600,570**	**616,627**	**27,439**	**12,801**	**2,295**	**105,011**	**1,386,727**

The transfers recorded in the year ended December 31, 2010 mainly relate to transfers from fixed assets under construction to fixed assets following the completion of construction.

During the year ended December 31, 2010 the Netia Group recognized impairment charges of PLN 1,216 relating to discontinued investment projects (PLN 627 in 2009). In 2009 the Netia Group recognized additionally PLN 1,056 for obsolete telecommunication equipment.

Moreover, as a result of the impairment test of non-current assets as of December 31, 2010 the Netia Group has recognized a reversal of previously recognized impairment losses amounting to 221,184 PLN during the year ended December 31, 2010 (see Note 5), 184,821 PLN of which was allocated to property, plant and equipment. In addition during the year ended December 31, 2010 the Netia Group reversed previously recognized impairment for specific assets amounting to 308 PLN.

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 12,936 and PLN 13,163 were capitalized to fixed assets under construction during the year ended December 31, 2010 and December 31, 2009, respectively. Furthermore the Company capitalized PLN 2,314 and PLN 1,117 of net cash losses on closed forward contracts during the year ended December 31, 2010 and December 31, 2009, respectively.

The net carrying value of assets held under finance leases as at December 31, 2010 and December 31, 2009 is presented below:

	December 31, 2009	December 31, 2010
	(PLN)	(PLN)
Fixed telecommunications network	44	38
Telecommunications equipment	15,245	15,087
Vehicles	-	383
	15,289	**15,508**

8. Acquisitions

Current period

Acquisition of Ethernet operators

SSI Net Sp. z o.o.

On June 15, 2010, Global Connect Sp. z o.o. ("Global Connect"), the Company's subsidiary, purchased 100% of the share capital of SSI Net Sp. z o.o. ("SSI Net"), an internet service provider offering broadband Internet access to residential clients. The total price for all SSI Net shares has been set at PLN 612.

The Netia Group accounted for the acquisition of SSI Net using the purchase method and started consolidating the financial statements of SSI Net as of June 30, 2010 adjusting the consolidated income statement and the consolidated statement of financial position for material transactions, which took place between June 15, 2010 and June 30, 2010.

If the acquisition had occurred on January 1, 2010, the Netia Group's revenue would have amounted to PLN 1,569,457, and profit would have been PLN 263,920.

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	612
Provisional fair value of net assets acquired	(283)
Goodwill	**329**

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	-	205
Receivables	81	81
Prepayments	2	2
Cash and cash equivalents	96	96
Trade liabilities	(7)	(7)
Other liabilities and accruals	(56)	(56)
Deferred income tax liabilities	-	(38)
Net assets acquired	**116**	**283**

The fair value of the trade receivables amounts to PLN 81 and corresponds to their gross amount. None of the trade receivables have been impaired and it is expected that the full contractual amount can be collected.

Fair value of the purchase consideration transferred for the acquisition:

	(PLN)
Cash paid	612
Total consideration	**612**

	(PLN)
Total purchase consideration settled in cash	(612)
Cash and cash equivalents in the subsidiary acquired	96
Cash outflow on acquisition	**(516)**

The above investments are of a long-term nature.

Multiplay Polska Sp. z o.o.

On September 30, 2010, Internetia Sp. z o.o. ("Internetia"), the Company's subsidiary, purchased 100% of the share capital of Multiplay Polska Sp. z o.o. ("Multiplay"), an internet service provider offering broadband Internet access to residential clients. The total price for all Multiplay shares has been set at PLN 7,998.

The Netia Group accounted for the acquisition of Multiplay using the purchase method and started consolidating the financial statements of Multiplay as of September 30, 2010.

If the acquisition had occurred on January 1, 2010, the Netia Group's revenue would have amounted to PLN 1,572,170 and profit would have been PLN 263,703.

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	7,998
Provisional fair value of net assets acquired	(1,992)
Goodwill	**6,006**

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:

	Acquiree's carrying amount	Provisional fair value
	(PLN)	(PLN)
Customer relationships	-	2,652
Goodwill	8,377	-
Property, plant and equipment	567	567
Receivables	119	119
Inventory	8	8
Prepayments	12	12
Cash and cash equivalents	32	32
Bank loans	(334)	(334)
Trade liabilities	(399)	(399)
Other liabilities and accruals	(202)	(202)
Deferred income tax,net	-	(463)
Net assets acquired	**8,180**	**1,992**

The fair value of the trade receivables amounts to PLN 119 and corresponds to their gross amount of PLN 338 decreased by bad debt allowance of PLN 219.

Fair value of the purchase consideration transferred for the acquisition:

	(PLN)
Cash paid	7,998
Total consideration	**7,998**

	(PLN)
Total purchase consideration settled in cash	(7,998)
Cash and cash equivalents in the subsidiary acquired	32
Cash outflow on acquisition	**(7,966)**

The above investments are of a long-term nature.

Igloonet Sp. z o.o.

On October 6, 2010, Internetia Sp. z o.o. ("Internetia"), the Company's subsidiary, purchased 100% of the share capital of Igloonet Sp. z o.o. ("Igloonet"), an internet service provider offering broadband Internet access to residential clients. The total price for all Igloonet shares has been set at PLN 3,020.

The Netia Group accounted for the acquisition of Igloonet using the purchase method and started consolidating the financial statements of Igloonet as of October 1, 2010.

If the acquisition had occurred on January 1, 2010, the Netia Group's revenue would have amounted to PLN 1,570,338 and profit would have been PLN 263,974.

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	3,020
Provisional fair value of net assets acquired	(2,387)
Goodwill	**633**

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:

	Acquiree's carrying amount	Provisional fair value
	(PLN)	(PLN)
Customer relationships	-	560
Property, plant and equipment	1,392	1,392
Trade receivables	144	144
Tax receivables	39	39
Inventory	89	89
Prepayments	11	11
Cash and cash equivalents	352	352
Trade liabilities	(47)	(47)
Tax liabilities	(47)	(47)
Deferred income tax, net	-	(106)
Net assets acquired	**1,933**	**2,387**

The fair value of the trade receivables amounts to PLN 144 and corresponds to their gross amount of PLN 183 decreased by bad debt allowance of PLN 39.

Fair value of the purchase consideration transferred for the acquisition:

	(PLN)
Cash paid	3,020
Total consideration	**3,020**

	(PLN)
Total purchase consideration settled in cash	(3,020)
Cash and cash equivalents in the subsidiary acquired	352
Cash outflow on acquisition	**(2,668)**

The above investments are of a long-term nature.

Fornet Sp. z o.o.

On December 16, 2010, Global Connect Sp. z o.o. ("Global Connect"), the Company's subsidiary, purchased 100% of the share capital of Fornet Sp. z o.o. ("Fornet"), an internet service provider offering broadband Internet access to residential clients. The total price for all Fornet shares has been set at PLN 1,368.

The Netia Group accounted for the acquisition of Fornet using the purchase method and started consolidating the financial statements of Fornet as of December 31, 2010 adjusting the consolidated income statement and the consolidated statement of financial position for material transactions, which took place between December 16, 2010 and December 31, 2010.

If the acquisition had occurred on January 1, 2010, the Netia Group's revenue would have amounted to PLN 1,569,404, and profit would have been PLN 263,913.

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	1,368
Provisional fair value of net assets acquired	(400)
Goodwill	**968**

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:

	Acquiree's carrying amount	Provisional fair value
	(PLN)	(PLN)
Customer relationships	-	298
Trade and other receivables	79	67
Cash and cash equivalents	167	167
Trade liabilities	(71)	(71)
Other liabilities and accruals	(7)	(7)
Deferred income tax liabilities	-	(54)
Net assets acquired	**168**	**400**

The fair value of the trade receivables amounts to PLN 64 and corresponds to their gross amount of PLN 76 decreased by bad debt allowance of PLN 12.

Fair value of the purchase consideration transferred for the acquisition:

	(PLN)
Cash paid	1,368
Total consideration	**1,368**

	(PLN)
Total purchase consideration settled in cash	(1,368)
Cash and cash equivalents in the subsidiary acquired	167
Cash outflow on acquisition	**(1,201)**

The above investments are of a long-term nature.

Pronet Sp. z o.o.

On December 21, 2010, Internetia Sp. z o.o. ("Internetia"), the Company's subsidiary, purchased 100% of the share capital of Pronet Sp. z o.o. ("Pronet"), an internet service provider offering broadband Internet access to residential clients. The total price for all Pronet shares has been set at PLN 1,800

The Netia Group accounted for the acquisition of Pronet using the purchase method and started consolidating the financial statements of Pronet as of December 31, 2010 adjusting the consolidated income statement and the consolidated statement of financial position for material transactions, which took place between December 21, 2010 and December 31, 2010.

If the acquisition had occurred on January 1, 2010, the Netia Group's revenue would have amounted to PLN 1,570,529, and profit would have been PLN 263,948.

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	1,800
Provisional fair value of net assets acquired	(504)
Goodwill	**1,296**

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:

	Acquiree's carrying amount	Provisional fair value
	(PLN)	(PLN)
Customer relationships	-	819
Property, plant and equipment	14	14
Receivables	27	27
Prepayments	2	2
Cash and cash equivalents	10	10
Borrowings	(31)	(31)
Trade liabilities	(95)	(95)
Other liabilities and accruals	(87)	(87)
Deferred income tax liabilities	-	(155)
Net assets acquired	**(160)**	**504**

The fair value of the trade receivables amounts to PLN 27 and corresponds to their gross amount. None of the trade receivables have been impaired and it is expected that the full contractual amount can be collected.

Fair value of the purchase consideration transferred for the acquisition:

	(PLN)
Cash paid	1,800
Total consideration	**1,800**

	(PLN)
Total purchase consideration settled in cash	(1,800)
Cash and cash equivalents in the subsidiary acquired	10
Cash outflow on acquisition	**(1,790)**

The above investments are of a long-term nature.

End of provisional accounting period

During the year ended December 31, 2009 the Netia Group acquired eTychy Sp. z o.o. and Global Connect and performed a provisional valuation of the acquired companies' assets, liabilities and contingent liabilities.

Changes in Global Connect's provisional valuation at the date of acquisition related to assets and liabilities are presented in the table below:

	Acquiree's carrying amount	Provisional fair value estimated as at December 31, 2009	Adjustments	Provisional fair value estimated as at December 31, 2010
	(PLN)	(PLN)	(PLN)	(PLN)
Property, plant and equipment	1,603	1,603	-	1,603
Customer relationships	-	3,231	-	3,231
Other intangible assets	1	1	-	1
Receivables	837	349	(87)	262
Prepayments	7	7	-	7
Cash and cash equivalents	51	51	-	51
Borrowings	(347)	(347)	-	(347)
Trade liabilities	(848)	(848)	(6)	(854)
Other liabilities and accruals	(124)	(124)	(161)	(285)
Deferred income tax liabilities	-	(614)	-	(614)
Net assets acquired	**1,180**	**3,309**	**(254)**	**3,055**

The 2009 comparative information has been restated to reflect the above adjustments in provisional valuation.

There were no adjustments to provisional valuation of assets and liabilities of eTychy Sp. o.o. as of December 31, 2009.

Operational networks

During the first quarter of 2010 the Netia Group purchased networks and customers from Ethernet operators for a total price of PLN 818. These purchases were treated as acquisitions of parts of continuing businesses. Fair values of the acquired fixed assets and customer relationships were estimated at PLN 394 and PLN 390, respectively. Total cash outflow relating to these acquisitions amounted to PLN 818. The goodwill of PLN 34 that arose on these transactions is based on the fair value of net assets acquired and is attributable to the synergies expected to arise after the Netia Group's acquisition of the above networks. The assets recognized in the consolidated statement of financial position arising from the purchase of operational networks are presented in note 7 and 9.

Registration of a new subsidiary (not in thousands)

On September 15, 2010, the Company's subsidiary, Netia 2 Sp. z o.o. ("Netia 2"), was registered in the National Court Register. Netia acquired 100 Netia 2's shares (with a par value of PLN 50 per share) constituting 100% of Netia 2's share capital and giving Netia 100% of the voting power at Netia 2's general meeting of shareholders

9. Intangible assets

Current 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, 2010 (Restated)	150,178	2,970	432,823	7,417	107,354	20,329	317,073	6,382	80,344	1,124,870
Additions	-	-	-	-	-	-	864	26,624	-	27,488
Purchase of subsidiaries	9,234	-	-	-	-	-	-	-	4,535	13,769
Purchase of operational networks	34	-	-	-	-	-	-	-	390	424
Transfers	-	-	-	-	-	-	21,673	(21,673)	-	-
Disposals	-	-	-	-	-	-	(29)	-	-	(29)
Other movements	-	-	-	-	-	-	91	-	-	91
Gross book value as at December 31, 2010	159,446	2,970	432,823	7,417	107,354	20,329	339,672	11,333	85,269	1,166,613
Accumulated amortization as at January 1, 2010	-	2,970	208,458	1,539	51,864	4,057	193,487	-	31,509	493,884
Amortization expense	-	-	14,494	-	4,088	1,170	31,079	-	17,053	67,884
Disposals	-	-	-	-	-	-	(16)	-	-	(16)
Other movements	-	-	-	-	-	-	75	-	-	75
Accumulated amortization as at December 31, 2010	-	2,970	222,952	1,539	55,952	5,227	224,625	-	48,562	561,827
Accumulated impairment as at January 1, 2010	-	-	159,788	5,878	28,511	3,408	43,998	385	207	242,175
Reversal of impairment charge (see Note 5)	-	-	(16,049)	-	(6,964)	(2,434)	(1,407)	-	(8)	(26,862)
Other movements	-	-	-	-	-	-	29	-	-	29
Accumulated impairment as at December 31, 2010	-	-	143,739	5,878	21,547	974	42,620	385	199	215,342
Net book value as at January 1, 2010	150,178	-	64,577	-	26,979	12,864	79,588	5,997	48,628	388,811
Net book value as at December 31, 2010	**159,446**	**-**	**66,132**	**-**	**29,855**	**14,128**	**72,427**	**10,948**	**36,508**	**389,444**

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, 2009 (Restated)	140,418	2,970	432,823	7,417	107,354	20,329	294,435	4,693	74,953	1,085,392
Additions	-	-	-	-	-	-	802	23,522	-	24,324
Purchase of subsidiaries	9,360	-	-	-	-	-	3	-	4,210	13,573
Purchase of operational networks	400	-	-	-	-	-	-	-	1,181	1,581
Transfers	-	-	-	-	-	-	21,833	(21,833)	-	-
Gross book value as at December 31, 2009	150,178	2,970	432,823	7,417	107,354	20,329	317,073	6,382	80,344	1,124,870
Accumulated amortization as at January 1, 2009	-	1,485	193,964	1,539	47,776	2,887	167,750	-	15,722	431,123
Amortization expense	-	1,485	14,494	-	4,088	1,170	25,669	-	15,701	62,607
Other movements	-	-	-	-	-	-	68	-	86	154
Accumulated amortization as at December 31, 2009	-	2,970	208,458	1,539	51,864	4,057	193,487	-	31,509	493,884
Accumulated impairment as at January 1, 2009	-	-	159,788	5,878	28,511	3,408	43,991	7	207	241,790
Impairment charge for specific assets	-	-	-	-	-	-	-	385	-	385
Transfers	-	-	-	-	-	-	7	(7)	-	-
Accumulated impairment as at December 31, 2009	-	-	159,788	5,878	28,511	3,408	43,998	385	207	242,175
								-		
Net book value as at January 1, 2009	140,418	1,485	79,071	-	31,067	14,034	82,694	4,686	59,024	412,479
Net book value as at December 31, 2009	**150,178**	**-**	**64,577**	**-**	**26,979**	**12,864**	**79,588**	**5,997**	**48,628**	**388,811**

As a result of the impairment test of non-current assets as of December 31, 2010 the Netia Group has recognized a reversal of previously recognized impairment losses amounting to 221,184 PLN during the year ended December 31, 2010 (see Note 5), 26,862 PLN of which was allocated to intangible assets.

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 2 and 5 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 5 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 10 years.

10. Investment property

	Year ended December 31, 2009	Year ended December 31, 2010
	(PLN)	(PLN)
Gross book value at the beginning of the period	59,649	59,952
Additions	303	816
Gross book value at the end of the period	59,952	60,768
Accumulated depreciation at the beginning of the period	(10,454)	(11,316)
Depreciation expense	(862)	(807)
Accumulated depreciation at the end of the period	(11,316)	(12,123)
Accumulated impairment at the beginning of the period	(13,062)	(13,062)
Reversal of impairment charge (see Note 5)	-	9,501
Accumulated impairment at the end of the period	(13,062)	(3,561)
Net book value at the beginning of the period	36,133	35,574
Net book value at the end of the period	**35,574**	**45,084**

Due to Management's decision to hold the Company's former head office as a long-term investment, on November 30, 2008 the Company reclassified the relating assets from assets held for sale and recognized them as investment property. The fair value of this property was estimated by an independent, professionally qualified valuer at PLN 54,620 as at February 10, 2011. This estimation has not changed materially since the date of the statement of financial position.

11. Inventories

	December 31, 2009	December 31, 2010
	(PLN)	(PLN)
Materials	103	337
Goods for resale	3,546	11,445
Less provision for impairment charge	(506)	(389)
Inventories, net	**3,143**	**11,393**

During the years ended December 31, 2010 and 2009 the Netia Group recognized PLN 19,392 and PLN 17,141, respectively as the cost of inventories included in "cost of goods sold". Moreover, during the year ended December 31, 2010 PLN 71 (PLN 4 in 2009) of previous inventory provisions were utilized.

12. Trade and other receivables

	December 31, 2009 (PLN)	December 31, 2010 (PLN)
Trade receivables	194,367	165,223
Less provision for impairment of trade receivables	(35,628)	(29,813)
Trade receivables, net	158,739	135,410
VAT and other government receivables	686	487
Other receivables	10,463	4,246
Less provision for impairment of other receivables	(243)	(235)
Other receivables, net	10,220	4,011
Indemnities received*	4,550	-
	174,195	**139,908**
Of which,		
Current	173,519	139,691
Non-current	676	217

* The asset corresponds to the part of the possible costs resulting from the pending claims against acquired companies that were reimbursable by the seller according to the relevant purchase agreement (see note 29).

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, 2010 and 2009 amounted to PLN 9,534 and PLN 8,586, respectively and was included in "selling and distribution costs" in the consolidated income statement.

As of December 31, 2010 and December 31, 2009 trade and other receivables of PLN 48,326 and PLN 53,759, respectively, were past due but not fully provided for. The ageing analysis of these trade receivables is as follows:

	Less than 3 months (PLN)	3 – 6 months (PLN)	More than 6 months (PLN)	Total (PLN)
As at December 31, 2010	40,728	5,882	1,716	48,326
As at December 31, 2009	49,362	2,903	1,494	53,759

In addition, as at December 31, 2010 and December 31, 2009 the amounts of PLN 929 and PLN 521, respectively were excluded from other receivables as they were legally reserved for spending on social purposes.

13. Tax Office receivables

Tax decision (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 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 subsequently conceded by the Tax Authority as overpayment and returned to Netia.

Netia has received opinions from several independent tax and legal advisors, as well as tax law experts, which conclude that the claims of the Directors of the Tax Control Office and the Tax Chamber have no legal grounds. Accordingly, Management has not recognised the Tax Chamber's decision as a taxation expense in either of the financial years ended December 31, 2009 and 2010 and instead treats funds paid over to the tax authorities as an overpayment of tax.

Netia has filed an appeal to the Decision with the Voivodship Administrative Court and will undertake all possible legal steps to prove that the decision of the Tax Chamber Director was groundless. The next hearing at the Voivodship Administrative Court is expected on February 22, 2011.

14. Prepaid expenses and accrued income

	December 31, 2009 (Restated)	December 31, 2010
	(PLN)	(PLN)
Accrued income relating to promotional offers	15,958	39,692
Transaction costs related to the credit facility (see Note 20)	4,567	-
Rental costs prepaid	1,867	2,850
IT service.	2,580	2,338
Insurance.	609	329
Other prepaid expenses.	2,190	3,175
	27,771	**48,384**
Of which,		
Current	20,216	37,876
Non-current	7,555	10,508

15. Investments held to maturity

		December 31, 2009		December 31, 2010	
	Maturity date	Nominal value	Carrying amount	Nominal value	Carrying amount
		(PLN)	(PLN)	(PLN)	(PLN)
52-week treasury notes	June 30, 2010	10,000	9,774	-	-
52-week treasury notes	July 14, 2010	10,000	9,788	-	-
52-week treasury notes	August 4, 2010	10,000	9,748	-	-
52-week treasury notes	August 11, 2010	10,000	9,751	-	-
52-week treasury notes	August 11, 2010	10,000	9,750	-	-
52-week treasury notes	October 27, 2010	10,000	9,678	-	-
52-week treasury notes	March 16, 2011	-	-	10,000	9,922
52-week treasury notes	March 16, 2011	-	-	10,000	9,921
52-week treasury notes	March 23, 2011	-	-	10,000	9,914
52-week treasury notes	March 23, 2011	-	-	10,000	9,914
52-week treasury notes	April 27, 2011	-	-	10,000	9,879
52-week treasury notes	June 1, 2011	-	-	10,000	9,842
52-week treasury notes	June 8, 2011	-	-	10,000	9,834
52-week treasury notes	June 15, 2011	-	-	10,000	9,823
52-week treasury notes	July 6, 2011	-	-	10,000	9,794
52-week treasury notes	August 10, 2011	-	-	10,000	9,764
52-week treasury notes	August 10, 2011	-	-	10,000	9,763
52-week treasury notes	August 10, 2011	-	-	10,000	9,765
52-week treasury notes	August 10, 2011	-	-	10,000	9,762
52-week treasury notes	August 31, 2011	-	-	10,000	9,743
52-week treasury notes	September 28, 2011	-	-	10,000	9,716
52-week treasury notes	September 28, 2011	-	-	15,000	14,580
52-week treasury notes	October 26, 2011	-	-	10,000	9,680
		60,000	**58,489**	**175,000**	**171,616**

16. Cash, cash equivalents and restricted cash

	December 31, 2009	December 31, 2010
	(PLN)	(PLN)
Cash at bank and in hand	181,203	173,600

The effective interest rate on short-term bank deposits was 3.2% and 3.5%, respectively for the year ended December 31, 2010 and the year ended December 31, 2009.

In addition, as at December 31, 2010 and December 31, 2009 the amounts of PLN 450 and PLN 722, respectively were excluded from cash and cash equivalents as they were legally reserved for spending on social purposes.

	December 31, 2009	December 31, 2010
	(PLN)	(PLN)
Restricted cash	2,330	2,123

As at December 31, 2010 and December 31, 2009, PLN 2,110 of restricted cash represents the Court's deposit and the amounts of PLN 13 and PLN 220, respectively, were restricted as they were placed as collaterals securing payments to vendors.

17. Other financial instruments

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, 2010 amounted to PLN 2,060 (PLN 1,669, net of tax). During the year ended December 31, 2010, PLN 2,314 of net cash losses on closed forward contracts were capitalized, PLN 264 of net cash losses decreased finance income due to excess of the amount of closed forward contracts over purchases made, and the ineffective portion of open forward contracts of PLN 5 was recorded as finance income.

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, 2010, PLN 1,514 of fair value gains on open forward contracts were recorded as finance income.

In year ended December 31, 2009 net fair value losses on forward contracts recognized in the hedging reserve in equity amounted to PLN 2,391 (PLN 1,937, net of tax). During year ended December 31, 2009, PLN 1,117 of net cash losses on closed forward contracts were capitalized, PLN 3,014 of net cash losses were recorded as finance cost due to excess of the amount of closed forward contracts over purchases made, and the ineffective portion of open forward contracts of PLN 89 was recorded as finance cost.

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 year ended December 31, 2009, PLN 1,915 of fair value losses on open forward contracts were recorded as finance costs.

The table below presents outstanding forward transactions as at balance sheet date:

	Hedged nominal amount	Hedged nominal amount	Fair value		
			Asset	Liability	Other comprehensive income
	(EUR)	(USD)	(PLN)	(PLN)	(PLN)
As at December 31, 2010					
Forward transactions related to equipment and construction contracts	2,700	2,380	77	(408)	2,060
Forward transactions related to commercial contracts..	4,380	1,330	40	(441)	-
As at December 31, 2009					
Forward transactions related to equipment and construction contracts	4,100	4,000	60	(2,458)	2,391
Forward transactions related to commercial contracts..	5,110	1,650	50	(1,965)	-

Equity securities

On March 19, 2008 the Netia Group sold its wholesale international voice traffic termination activities to Mediatel S.A. (“Mediatel”) for PLN 13,619, of which PLN 8,000 was settled in cash and PLN 5,619 was the estimated fair value of 440 shares issued by Mediatel and related “put” and “call” options. During the first quarter of 2010 the remaining 340 Mediatel shares were sold (100 shares were sold in 2009). In that period the Company recognized a loss of PLN 881 on disposal of shares and a gain of PLN 697 on the expiration of the related “put” and “call” options.

18. Shareholders’ equity

Share capital (not in thousands)

At December 31, 2009, the Company’s share capital consisted of 389,276,294 ordinary shares and 1,000 series A1 shares with a par value of PLN 1 per share. Each ordinary share had one vote at the shareholders' meetings. 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 2010 the Company issued 181,935 ordinary series K shares due to the exercise by certain persons (who were not Management Board members) of their rights arising from the key employee share option plan adopted by Netia’s Supervisory Board in 2003 (the “2003 Plan”). The 5,115,579 series K shares issued prior to Netia’s General Meeting of Shareholders held on May 26, 2010, including 61,059 shares issued in 2010, were redesignated, in accordance with a resolution adopted by Netia’s General Meeting of Shareholders, as series B shares. Following the change of the Company’s Statute in 2010 up to 13,258,206 series K shares may be issued. The total number of series K shares issued through December 31, 2010 was 120,876 and their nominal value was PLN 121 thousands.

As a result at December 31, 2010, the Company’s share capital consisted of 389,458,229 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.

According to the information provided to the Company by its shareholders, as at December 31, 2010 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	93,720,763	24.06
ING Otwarty Fundusz Emerytalny	48,010,027	12.33
SISU Capital Limited and related entities	39,043,006	10.02
Shares held by public and other shareholders	208,685,433	53.59
	389,459,229	**100.00**

Other supplementary capital

The Shareholders' Meeting held on May 26, 2010, resolved that the amounts of PLN 236,803 of the Company's net profit for the year 2009 and PLN 5,818 of the undistributed profit from previous years resulting from a merger of a subsidiary with the Company during the financial year 2009 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, 2010, the distributable reserve amounted to PLN 504,561.

Stock options (not in thousands)

2003 Plan

In the year ended December 31, 2010 and 2009 the following changes took place in the number of options granted under the 2003 Plan:

	Year ended December 31, 2009		Year ended December 31, 2010	
Options	**Average strike price**	**Options**	**Average strike price**	**Options**
At the beginning of the period	5.88	50,268,123	5.84	53,946,373
Granted	5.43	5,566,500	6.59	350,000
Exercised	-	-	3.50	(570,937)
Forfeited / expired	5.78	(1,888,250)	5.61	(480,000)
At the end of the period	**5.84**	**53,946,373**	**5.87**	**53,245,436**

As at December 31, 2010 the total number of options approved by the Supervisory Board and issued was 87,877,470 as compared to 87,527,470 as at December 31, 2009. Out of these approved options 53,245,436 options were outstanding as at December 31, 2010 and 53,946,373 options were outstanding as at December 31, 2009. As at December 31, 2010 and December 31, 2009 the total number of vested options was 46,788,436 and 22,718,373, respectively. The vesting period for the options is up to three years from the date of grant. As at December 31, 2010, the weighted average remaining contractual life of the outstanding options was 2 years. The outstanding options are exercisable until December 20, 2012. 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 exercise price of the Company's shares and the strike price of the options. The participant will not be required to pay the strike price ranging from PLN 3.50 to PLN 8.25.

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, 2010 and 2009 amounted to PLN 5,809 thousands and PLN 10,522 thousands, respectively, while PLN 565 thousands was derecognized in the income statement in year ended December 31, 2009.

New Plan

On May 26, 2010, the Annual Shareholders Meeting resolved to adopt a set of rules, to be administered by the Company's Supervisory Board, for the issuing of up to 27,253,674 share options to the Management Board and employees of Netia, each option authorising its holder to receive, free of charge, up to ½ of a subscription warrant issued by the Company with the latest possible exercise date of May 26, 2020 (the "New Plan"). Each warrant entitles its holder to subscribe for one series L share for the nominal value e. i PLN 1 (not in thousands), which shall be paid by the Company or its subsidiaries. In order to satisfy the claims arising from the exercise of the options under New Plan, the Shareholders Meeting resolved to authorize the issuance of up to 13,626,837 series L shares. The Supervisory Board has not granted any share options under the New Plan as at February 21, 2011.

19. Provisions

	December 31, 2009 (Restated) (PLN)	December 31, 2010 (PLN)
Loss on rental contract	1,824	869
Claims	3,780	1,223
Restructuring	685	293
Retirement	387	458
	6,676	**2,843**
Of which,		
Current	4,893	1,855
Non-current	1,783	988
	6,676	**2,843**

	Loss on rental contracts (PLN)	Claims (PLN)	Restructuring (PLN)	Retirement (PLN)	Total (PLN)
As at January 1, 2010 (Restated)	1,824	3,780	685	387	6,676
Recognition and changes in estimates (charged to the income statement)	147	(567)	-	71	(349)
Used during the period	(1,166)	(1,990)	(392)	-	(3,548)
Discount unwinding (charged to the income statement)	64	-	-	-	64
As at December 31, 2010	**869**	**1,223**	**293**	**458**	**2,843**

Loss on rental contracts

The provision was created for loss on rental contracts and relates to the excess of office space held in certain locations in Warsaw following acquisitions and restructuring, 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 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 provision for restructuring was recorded in connection with the restructuring program announced by the Netia Group in April 2009 and September 2009, which assumed a total decrease of employment by approximately 231 full time employees by the end of 2009 (see also Note 28). The remaining balance as at December 31, 2010 comprises the provision created for those committed redundancies where the employment contract has not been yet terminated. The Netia Group expects that the cash outflows relating to this provision will be incurred during 2011.

Retirement

The provision for 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 6% and a salary increase rate of 2.5% above inflation of 2.5%. Retirement severance payments will be paid on Netia Group employees upon their retirement.

20. Borrowings

Undrawn Borrowing facilities

Effective from August 5, 2010 Netia terminated its existing loan facilities totalling PLN 295,000 available under the Facility concluded on May 15, 2007 with Rabobank Polska S.A. as the arranger, Bank Millennium S.A., Bank Gospodarki Żywnościowej S.A. and Raiffeisen Bank Polska S.A.

The cumulative draw downs under the Facility made in previous years amounted to PLN 205,000 and were repaid in full in 2008. In the year ended December 31, 2010 PLN 5,998 of accumulated deferred transaction costs related to the Facility was recognized in the income statement as finance cost.

In parallel, on July 29, 2010 Netia signed a mandate letter with Rabobank, Raiffeisen Bank Polska S.A. and BRE Bank S.A. for arrangement of new financing for a potential market consolidating acquisition within the telecommunications sector in Poland.

On October 4, 2010 bank BNP Paribas, Polish branch, (BNP Paribas SA Oddział w Polsce) joined the mandate letter signed by the Company on July 29, 2010 with Rabobank Polska S.A., Raiffeisen Bank Polska S.A. and BRE Bank S.A. (the “Mandate”) for arrangement of new financing fund potential acquisitions by Netia.

The total amount of external financing which may be obtained under the Mandate is PLN 700,000.

Outstanding Bank Loans

As at December 31, 2010, the Netia Group had outstanding bank loans of total PLN 31 from Polbank EFG. The loan was drawn by the Company’s subsidiary Pronet Sp. z o.o.

21. Trade and other payables

	December 31, 2009 (Restated)	December 31, 2010
	(PLN)	(PLN)
Trade payables	75,203	61,917
Investment payables	52,919	60,344
Accrued expenses (see Note 22)	82,863	75,157
VAT and other taxes	12,298	7,391
Finance lease payments	10,591	7,335
Payables to former owners of acquired subsidiaries	4,229	-
Advance payment for the second batch of transmission equipment (see Note 31)	21,141	-
Other payables	2,219	3,471
	261,463	**215,615**
Of which,		
Current	248,791	206,768
Non-current	12,672	8,847

In addition, as at December 31, 2010 and December 31, 2009 the amounts of PLN 1,389 and PLN 1,243, respectively were excluded from other payables as they were legally reserved for funding social purposes.

22. Accrued expenses

	December 31, 2009 (Restated)	December 31, 2010
	(PLN)	(PLN)
Construction costs	4,142	270
Uninvoiced services	28,461	25,894
Interconnection charges	16,312	20,704
Holidays accrual	2,667	3,032
Employees bonuses and accrued salaries	22,300	18,096
Rental costs accrued	8,827	7,161
Other	154	-
	82,863	**75,157**

23. Deferred income

	December 31, 2009	December 31, 2010
	(PLN)	(PLN)
Invoiced income from subscriptions relating to future periods	23,704	21,395
Rental contracts	16,086	28,102
Government grants	655	574
Other	1,957	1,613
	42,402	**51,684**
Of which,		
Current	35,113	34,098
Non-current	7,289	17,586

24. Revenue

	Year ended December 31, 2009 (PLN)	Year ended December 31, 2010 (PLN)
Direct voice	743,395	741,717
Monthly fees	*457,523*	*485,186*
Calling charges	*285,541*	*256,261*
Other	*331*	*270*
Indirect voice	65,654	37,359
Data	520,460	579,850
Interconnection revenue	66,917	68,394
Wholesale services	81,592	115,561
Other telecommunication service revenue	22,489	21,553
Telecommunication revenue	**1,500,507**	**1,564,434**
Radio communication services revenue	5,364	4,862
Revenue	**1,505,871**	**1,569,296**

25. Cost of sales

	Year ended December 31, 2009 (Restated) (PLN)	Year ended December 31, 2010 (PLN)
Interconnection charges	(196,718)	(223,410)
Network maintenance	(483,969)	(525,577)
Cost of goods sold	(17,141)	(19,394)
Depreciation and amortization	(251,367)	(249,032)
Salaries and benefits	(21,526)	(19,896)
Restructuring	(2,368)	(25)
Taxes, frequency fees and other expenses	(32,397)	(38,645)
	(1,005,486)	**(1,075,979)**

26. Selling and distribution costs

	Year ended December 31, 2009 (PLN)	Year ended December 31, 2010 (PLN)
Advertising and promotion	(61,138)	(51,053)
Third party commissions	(48,247)	(39,427)
Billing, mailing & logistics	(49,722)	(36,000)
Outsourced customer service	(29,538)	(33,139)
Provision for impaired receivables	(8,586)	(9,534)
Depreciation and amortization	(30,730)	(32,564)
Salaries and benefits	(86,856)	(85,579)
Restructuring	(3,405)	(241)
Other expenses	(20,224)	(25,328)
	(338,446)	**(312,865)**

27. General and administration costs

	Year ended December 31, 2009 (PLN)	Year ended December 31, 2010 (PLN)
Professional services	(10,678)	(9,197)
Information technology services	(16,305)	(10,484)
Office and car maintenance	(18,787)	(12,213)
Depreciation and amortization	(16,469)	(19,088)
Salaries and benefits	(78,941)	(68,850)
Restructuring	(5,967)	(524)
Other expenses	(26,311)	(21,893)
	(173,458)	**(142,249)**

28. Salaries and benefits

	Year ended December 31, 2009	Year ended December 31, 2010
	(PLN)	**(PLN)**
Wages and salaries	(152,749)	(147,796)
Social security costs	(11,618)	(10,088)
Defined contribution plan (the State Plan)	(10,603)	(9,993)
Provision for retirement severance payment	394	(71)
Equity-settled share-based compensation	(9,957)	(5,809)
Cash-settled share-based compensation	(375)	(682)
Net change in accrual for PIT and social security costs relating to share-based compensation	(2,415)	114
Restructuring	(10,018)	(790)
	(197,341)	**(175,115)**

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.

Reorganization and restructuring

Following the acquisition of Tele2 Polska in September 2008 which significantly augmented the scale of the business, the Netia Group performed a comprehensive cost review across all functional areas of the Company and indentified 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 2009 and September 2009 the Netia Group announced headcount reductions, which assumed a total decrease of employment by approximately 231 full time employees by the end of 2009. Although implementation of these headcount reductions was largely completed in 2009, certain residual costs were incurred in the current period.

Total reorganization costs recorded during the periods ended December 31, 2010 and 2009 were included in the following cost categories presented in the table below:

	Year ended December 31, 2009		Year ended December 31, 2010	
	Total reorganization costs	***Out of which restructuring costs***	**Total reorganization costs**	***Out of which restructuring costs***
	(PLN)	(PLN)	**(PLN)**	(PLN)
Cost of sales				
Salaries and benefits	(2,368)	*(2,029)*	(25)	*(25)*
Selling and distribution costs				
Salaries and benefits	(3,405)	*(2,552)*	(241)	*(241)*
General and administration costs				
Salaries and benefits	(4,245)	*(3,254)*	(524)	*(524)*
Provision for rental contract	(1,104)	-	-	-
Other expenses	(618)	*(618)*	-	-
	(11,740)	***(8,453)***	**(790)**	***(790)***

29. Other income

	Year ended December 31, 2009	Year ended December 31, 2010
	(PLN)	**(PLN)**
Reminder fees and penalties	6,205	7,086
Forgiveness of liabilities	379	5,511
Reversal of impairment charges and provisions	699	1,541
Settlement with Tele2 SverigeAB	-	1,461
Settlement of disputes with TPSA	5,630	342
Receivables recovered	329	-
Other operating income	4,648	2,940
	17,890	**18,881**

On March 29, 2010 the Company and Tele2 Sverige AB signed an agreement ("Settlement Agreement") in which the parties agreed to settle all claims that they have or may have against one another under the Share Purchase Agreement ("SPA") and all ancillary agreements. In particular, the Company waived its right to the indemnities provided in the SPA (a part of any Tele2 Polska's contingent loss was indemnified by the seller) and Tele2 Sverige AB made a cash payment and waived its right to the restricted cash deposit if it is released by the Court. As a result of the Settlement Agreement, during the year ended December 31, 2010, Netia recorded an income of PLN 1,461.

30. Other expenses

	Year ended December 31, 2009	Year ended December 31, 2010
	(PLN)	(PLN)
Impairment charges for specific individual assets (see Notes 7 and 9)	(2,068)	(1,216)
Other	-	(6)
	(2,068)	**(1,222)**

31. Other gains / (losses), net

	Year ended December 31, 2009	Year ended December 31, 2010
	(PLN)	(PLN)
Gain on sale of impaired receivables	1,232	2,233
Gain on disposal of fixed assets	7,835	8,250
Net foreign exchange gains / (losses)	898	(1,774)
	9,965	**8,709**

On July 24, 2009 Netia and P4 concluded an agreement for the sale of the transmission equipment used by Netia to provide transmission services to P4. The sale agreement was entered into on the following terms and conditions:

1. The transmission equipment was purchased by P4 in three batches.
2. The total price for the transmission equipment was PLN 65,418, of which:
   a) PLN 22,832 was payable by P4 on the date of purchase of the first batch of the transmission equipment, i.e. August 1, 2009;
   b) PLN 21,141 was payable by P4 on the date of purchase of the second batch of the transmission equipment, i.e. January 1, 2010; and
   c) PLN 21,445 was payable by P4 on the date of purchase of the third batch of the transmission equipment, i.e. July 1, 2010.
3. The legal title to the given batches of the transmission equipment was transferred to P4 after P4 paid the price for a given batch.

In January 2010 and July 2010 the Company transferred to P4 the second and third batches of the transmission equipment and recognized gains on disposal of PLN 2,865 and PLN 4,433, respectively (a gain of PLN 5,298 was recognized on disposal of the first batch in the third quarter of 2009).

32. Finance income and finance costs

Finance income

	Year ended December 31, 2009	Year ended December 31, 2010
	(PLN)	(PLN)
Interest income on cash and cash equivalents	5,881	4,708
Amortization of held to maturity investments	1,434	4,645
Gain on sale of equity securities	148	-
Fair value gains on open forward contracts hedging commercial exposures (see Note 17)	-	1,514
Ineffective cash flow hedges (see Note 17)	-	5
Other finance income	101	786
	7,564	**11,658**

Finance costs

	Year ended December 31, 2009	Year ended December 31, 2010
	(PLN)	(PLN)
Fees charged on bank loans	(4,520)	(5,998)
Amortization of finance lease liability	(506)	(415)
Interest expense and amortization of other payables	(1,351)	(10)
Amortization of provisions	(7)	(85)
Fair value gain / (loss) on equity securities (see Note 8)	(929)	(881)
Fair value loss on other financial assets / liabilities (see Note 16)	(242)	-
Net foreign exchange losses	(8,134)	(991)
Excess of the amount of closed forward contracts over purchases made	(3,014)	(264)
Fair value losses on open forward contracts hedging commercial exposures	(1,915)	-
Ineffective cash flow hedges	(89)	-
Other finance costs	-	-
	(20,707)	**(8,644)**

33. Net foreign exchange gains / (losses)

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

	Year ended December 31, 2009	Year ended December 31, 2010
	(PLN)	(PLN)
Other gains / (losses), net	898	(1,774)
Finance costs	(8,134)	(991)
	(7,236)	**(2,765)**

34. Corporate income tax

	Year ended December 31, 2009	Year ended December 31, 2010
	(PLN)	(PLN)
Current income tax (charge) / benefit, net	(731)	557
Deferred income tax benefit / (charge), net	88,303	(25,431)
Income tax benefit / (charge)	**87,572**	**(24,874)**

Current income tax

The tax on the Netia Group's profit 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, 2009	Year ended December 31, 2010
	(PLN)	(PLN)
Profit before tax	1,125	288,769
Tax calculated at tax rates applicable to profit	(208)	(54,866)
Adjustments in respect of current income tax of previous year	-	718
Reversal of impairment losses for which no deferred tax asset had been recognised	-	19,638
Income and expense not subject / deductible for tax purposes, net	(1,640)	(4,312)
Reversal of impairment losses on assets not subject to tax	-	4,835
Recognition of previously unrecognized tax losses	87,837	2,846
Recognition of previously unrecognised deferred tax assets	-	6,267
Utilization of previously unrecognized tax losses	1,583	-
Income tax benefit / (charge)	**87,572**	**(24,874)**

The corporate income tax rate applicable to the Company and its subsidiaries for 2010 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, 2010 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 2011 budget and 2011-2015 long term business plan. 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.

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. The offset amounts are as follows:

	December 31, 2009	December 31, 2010
	(PLN)	(PLN)
Deferred income tax assets:		
- Deferred income tax assets to be recovered after more than 12 months	77,086	74,596
- Deferred income tax assets to be recovered within 12 months	33,512	28,072
	110,598	102,668
Deferred income tax liabilities:		
- Deferred income tax liabilities to be recovered after more than 12 months	14,902	16,390
- Deferred income tax liabilities to be recovered within 12 months	16,296	33,516
	31,198	49,906
Deferred income tax assets, net	**79,400**	**52,762**

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 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, 2010	6,245	19	19,170	21	1,532	4,211	31,198
- Charged / (credited) to the income statement	5,059	(9)	14,271	42	(727)	(788)	17,848
- Deferred income tax on acquisition	-	-	860	-	-	-	860
As at December 31, 2010	**11,304**	**10**	**34,301**	**63**	**805**	**3,423**	**49,906**

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, 2010	88,751	3,147	1,925	14,938	42	840	955	110,598
- Credited / (charged) to the income statement	(10,252)	(134)	3,959	(894)	(7)	(449)	194	(7,583)
- Deferred income tax on acquisition	-	44	-	-	-	-	-	44
- Credited / (charged) to other comprehensive income	-	-	-	-	-	(391)	-	(391)
As at December 31, 2010	**78,499**	**3,057**	**5,884**	**14,044**	**35**	**-**	**1,149**	**102,668**

Comparative period:

Deferred income tax liabilities	Deferred revenue	Foreign exchange differences	Depreciation and impairment	Forward contract	Interest	Other	Total
	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)	(PLN)
As at January 1, 2009	7,746	1,116	19,451	-	-	1,148	29,461
- Charged / (credited) to the income statement	(1,501)	(1,097)	(1,081)	9	1,532	3,063	925
- Charged / (credited) to other comprehensive income	-	-	-	12	-	-	12
- Deferred income tax on acquisition	-	-	800		-	-	800
As at December 31, 2009	**6,245**	**19**	**19,170**	**21**	**1,532**	**4,211**	**31,198**

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, 2009	-	1,881	9,520	4,032	613	-	4,858	20,904
- Credited / (charged) to the income statement	88,751	1,266	(7,595)	10,906	(571)	374	(3,903)	89,228
- Credited / (charged) to other comprehensive income	-	-	-	-	-	466	-	466
As at December 31, 2009	**88,751**	**3,147**	**1,925**	**14,938**	**42**	**840**	**955**	**110,598**

The deferred income tax recognized in equity in an amount of PLN 391 relates to movements in the hedging reserve.

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, 2010, the Netia Group had total deductible temporary differences of PLN 105,900 and unutilised tax loss carry-forwards of PLN 429,643 (total potential deferred income tax asset of PLN 101,753).

The Netia Group did not recognize deferred income tax assets of PLN 3,133 relating to tax losses of PLN 16,490 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, 2010 will expire in the following years: PLN 24 in 2011, PLN 9,993 in 2012, PLN 2,921 in 2013,PLN 2,246 in 2014 and PLN 1,306 in 2015.

Furthermore, due to the lack of conclusive evidence of future taxable profits, the Netia Group did not recognize deferred income tax assets of PLN 45,858, relating to deductible temporary differences of PLN 241,359 as follows:

	Timing differences	Potential deferred income tax asset
	(PLN)	(PLN)
Depreciation and impairment	235,079	44,665
Deferred income	6,280	1,193
	241,359	**45,858**

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.

35. 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 during the year.

	Year ended December 31, 2009	Year ended December 31, 2010
	(PLN)	(PLN)
Profit attributable to the equity holders of the Company	88,697	263,895
Weighted average number of ordinary shares in issue (not in thousands)	389,277,294	389,328,713
Basic earnings per share (not in thousands)	0.23	0.68

Diluted

Diluted earnings per share for the net profit 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 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 applicable under 2003 Plan as at December 31, 2010) 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, 2009 (PLN)	Year ended December 31, 2010 (PLN)
Profit attributable to the equity holders of the Company	88,697	263,895
Weighted average number of ordinary shares in issue (not in thousands)	389,277,294	389,328,713
Adjustments for:		
- Share options	446,332	3,501,383
Weighted average number of ordinary shares for diluted earnings per share (not in thousands)	389,723,626	392,830,096
Diluted earnings per share (not in thousands)	0.23	0.67

36. Dividends per share (not in thousands)

No dividends have been proposed or paid in respect to the financial year ended December 31, 2009 and no proposal has been made by the Management for the year ended December 31, 2010 as at the date of these financial statements. In accordance with the distribution policy published on January 13, 2011 the Management intends to propose distribution of funds in excess of a 300 mln PLN in cash and held-to-maturity investments to shareholders. Furthermore, should circumstances lead Management to conclude that transformational market consolidating acquisition opportunities are no longer feasible, then Management will also propose the return of the PLN 300 mln to shareholders.

Netia's distributable reserves are disclosed in Note 18.

37. Supplemental disclosures to the consolidated cash flow statement

Changes in working capital components:

	Year ended December 31, 2009 (Restated) (PLN)	Year ended December 31, 2010 (PLN)
Receivables	(790)	34,703
Inventories	1,917	(8,152)
Prepaid expenses	5,203	(25,157)
Restricted cash	382	207
Provisions, accruals and other payables	(41,064)	(32,060)
Deferred income	12,245	9,282
	(22,107)	**(21,177)**

Supplemental disclosures to operating activities:

	Year ended December 31, 2009 (PLN)	Year ended December 31, 2010 (PLN)
Income taxes paid	(595)	279
Interest received	6,820	4,708

Supplemental disclosures to investing activities:

	Year ended December 31, 2009 (PLN)	Year ended December 31, 2010 (PLN)
Subsidiary purchased in current period	(12,763)	(14,141)
Subsidiaries purchased in previous period	(44,999)	-
Purchase of subsidiaries, net of cash received	**(57,762)**	**(14,141)**

Non-cash transactions:

During the year ended December 31, 2010 the Netia Group entered into finance lease agreements for telecommunication equipment and vehicles. The carrying value of assets and liabilities recognized due to these transactions amounted to PLN 2,564 (PLN 9,958 in 2009).

38. The Management Board and Supervisory Board

Management Board

As at December 31, 2010 and December 31, 2009 the Company's Management Board consisted of the following members:
- Mirosław Godlewski – President,
- Jonathan Eastick – Chief Financial Officer,
- Grzegorz Esz,

- Piotr Nesterowicz,
- Tom Ruhan.

Supervisory Board

Effective May 25, 2010 Mr. Piotr Żochowski resigned from his position as Member of the Company's Supervisory Board.

Due to the above changes as at December 31, 2010 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.

39. Related party transactions

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

As at December 31, 2010, the total number of options granted to members of the Company's Management Board under the Plan, was 40,771,814 of which 35,838,564 had vested as of that date. Strike prices for the options granted to the Management Board range between PLN 3.50 and 8.25 per share. The market price of the Company's shares at December 31, 2010 was PLN 5.20 per share.

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

Options	**Year ended December 31, 2009**	**Year ended December 31, 2010**
At the beginning of the period	36,605,314	40,771,814
Granted	4,166,500	-
At the end of the period	**40,771,814**	**40,771,814**

As at December 31, 2010 and December 31, 2009 Mr. Mirosław Godlewski – the Company's President of the Management Board – held 13,334,000 options, out of which 13,334,000 had vested as at December 31, 2010.

As at December 31, 2010 and December 31, 2009 Mr. Jonathan Eastick – a member of the Company's Management Board – held 10,938,314 options, out of which 10,938,314 had vested as at December 31, 2010.

As at December 31, 2010 and December 31, 2009 Mr. Grzegorz Esz– a member of the Company's Management Board – held 4,166,500 options, out of which 1,433,250 had vested as at December 31, 2010.

As at December 31, 2010 and December 31, 2009 Mr. Piotr Nesterowicz – a member of the Company's Management – held 6,666,500 options, out of which 4,466,500 had vested as at December 31, 2010.

As at December 31, 2010 and December 31, 2009 Mr. Tom Ruhan – a member of the Company's Management Board – held 5,666,500 options, out of which 5,666,500 had vested as at December 31, 2010.

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

As at December 31, 2010 and December 31, 2009 Mr. Mirosław Godlewski – the Company's President of the Management Board – held 10,000 shares of the Company.

As at December 31, 2010 and December 31, 2009 Mr. Tom Ruhan – a member of the Company's Management Board – held 253,593 shares of the Company.

As at December 31, 2010 and December 31, 2009, Mr. Jonathan Eastick – a member of the Company's Management Board – held 50,000 and 35,500 shares of the Company, respectively.

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

As at December 31, 2010 and December 31, 2009, Mr. Raimondo Eggink – a member of the Company's Supervisory Board – held 40,000 and 20,000 shares of the Company, respectively.

As at December 31, 2010 and December 31, 2009, Mr. Tadeusz Radzimiński – a member of the Company's Supervisory Board – held 6,000 shares of the Company.

Restricted Stock Units (not in thousands)

As at December 31, 2010 the total number of Restricted Stock Units ("RSU") granted to the members of the Company's Supervisory Board was 520,000. 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 is three years from the date of grant. The Company recognizes the cost of cash-settled share-based payment transactions (including RSU) over the vesting period. The cost of RSU recorded in the year ended December 31, 2010 amounted to PLN 682 thousands (PLN 375 thousands in 2009).

Management Board remuneration

Compensation and related costs associated with members of the Company's Management Board during year ended December 31, 2010 and December 31, 2009 amounted to PLN 6,104 and PLN 6,047, respectively. In addition, the gross cost of share-based payments in the amounts of PLN 4,702 and PLN 7,575 was recognized in the respective periods.

Compensation and related costs associated with members of the Management Boards of the Company's subsidiaries during years ended December 31, 2010 and December 31, 2009 amounted to PLN 1,231 and PLN 994, respectively. Additional to the above, termination benefits of PLN 55 for the former members of the Management Board of the Company's subsidiaries were recognized as a cost in 2009. 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, 2010 and December 31, 2009 amounted to PLN 830 and PLN 795, respectively.

Incidental expenses of the Supervisory Board Members reimbursed by the Company amounted to PLN 232 and PLN 178 during the years ended December 31, 2010 and 2009, respectively, and mainly related to travel and accommodation.

Other transactions with related parties

During the year ended December 31, 2010 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.

40. Information on the registered audit company

The financial statements of Netia and the consolidated financial statements of the Netia Group for 2010 and 2009 were audited by Ernst & Young Audit Sp. z o.o. on the basis of a contract concluded on December 4, 2009 and March 30, 2007, respectively.

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	2009	2010
Audit of stand-alone and consolidated financial statements	471	358
Review of stand-alone and consolidated financial statements	423	272
Audit of subsidiaries' financial statements	137	148
Other attest services	-	350
Other services	57	-
Total	**1,088**	**1,128**

41. Commitments

Capital commitments

Capital expenditures contracted for at the balance sheet date but not recognized in the consolidated financial statements amounted to PLN 12,249 as at December 31, 2010 and PLN 14,975 as at December 31, 2009 of which, PLN 1,620 and PLN 2,294, respectively, related to the planned acquisition of intangible assets.

Operating lease commitments – where the Netia Group is the lessee

As at December 31, 2010 and December 31, 2009 the future minimum payments payable under non-cancellable operating leases were as follows:

	December 31, 2009 (PLN)	December 31, 2010 (PLN)
Not longer than 1 year	71,406	70,229
Longer than 1 year and not longer than 5 years	116,769	121,294
Longer than 5 years	45,666	51,362
	233,841	**242,885**

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, 2010 and December 31, 2009 amounted to PLN 463,542 and PLN 424,689, respectively. These rental costs are partially offset by income from sub-contractors (see also Note 18) in the amounts of PLN 2,640 and PLN 567, 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, 2009 (PLN)	December 31, 2010 (PLN)
Not longer than 1 year	16,988	21,411
Longer than 1 year and not longer than 5 years	23,891	35,240
Longer than 5 years	3,619	6,042
	44,498	**62,693**

The Netia Group has entered into several commercial leases on certain parts of the 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, 2010 and December 31, 2009 amounted to PLN 35,750 and PLN 28,147, respectively. The operating lease agreements do not relate to specific separate assets.

Finance lease commitments

In 2010 and 2009 Netia entered in new finance lease agreements for telecommunication equipment. Moreover, with the acquisition of certain internet network operators, the Netia Group has acquired finance leases for certain telecommunication equipment as well as for some vehicles. As at December 31, 2010 and December 31, 2009 future minimum lease payments under finance leases together with the present value of net minimum lease payments were as follows:

	December 31, 2009 (PLN)	December 31, 2010 (PLN)
Not longer than 1 year	5,585	5,172
Longer than 1 year and not longer than 5 years	5,006	2,163
Longer than 5 years	-	-
Present value of minimum lease payments	**10,591**	**7,335**
Plus amount representing finance charges	543	290
Total minimum lease payments	**11,134**	**7,625**

42. Contingencies

Universal services

The telecommunications law stipulates that universal service obligation will be rested on telecommunications undertaking designated in the President of UKE decision issued upon carrying out of tender procedure. The President of UKE issued a decision designating TP SA to provide universal service until May 8, 2011. Telecommunications undertakings, whose revenue from telecommunications activity exceeded PLN 4,000, are obliged to participate in financing of this obligation. The exact participation amount of a telecommunications undertaking obliged to pay subsidy will be established by virtue of the President of UKE decision, as well, although the said amount cannot exceed 1% of revenues of a given telecommunications undertaking in a given calendar year. The amount of participation in subsidy towards the universal service will constitute cost of income acquisition under law on corporate income tax. At the present stage one cannot exclude that Netia Group will be obliged to co-finance subsidy towards universal services.

TP SA filed with the President of UKE applications for awarding subsidy towards incurred costs of universal service provision. The applications regard subsidy towards costs incurred in period from May 8, 2006, until December 31, 2006. The President of UKE refused to award TP SA with a subsidy towards costs of services provided by TP SA in 2006, being a part of universal service. Upon filing a complaint by TP SA the Court repealed the President of UKE decisions. The President of UKE and KIGEiT filed cassation appeals against this judgement. The appeals were dismissed by the Supreme Administrative Court and the case was remanded to UKE for reconsideration. TP SA filed applications for subsidies towards universal service for years 2007-2009, as well.

In view of uncertainties over data included in the calculation, currently it is impossible to provide a reliable estimation of potential obligations arising from the subsidy towards universal service. On the basis of the 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 may be claimed by TP SA from Netia Group amounts to approximately PLN 27,000 for the period from 2006 until 2009 inclusive as follows:

2006	4,500
2007	7,000
2008	7,000
2009	8,500
	27,000

However, this amount may change substantially depending on (i) full or partial acceptance of TP SA applications by UKE and (ii) consistency of the Company's and UKE's estimations concerning revenues of telecommunications services providers. As Management is not aware of the size of any claim by TPSA in respect to 2010, it is still too early to estimate the related maximum amount.

The Management Board is unable to exclude the possibility of issuance of a decision, in result of which Netia will be

designated to participate in universal service provision. However, in the opinion of the Management Board the list of investments claimed by TP SA does not currently justify such subsidies. Results of an independent audit of TP SA's claims conducted by UKE have not been published and no decisions of UKE in favor of TP SA have been made to date. As a consequence no reserve due to potential participation in universal service provision was established as for the balance sheet date.

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 the Polish regulator issued a decision reducing the initial milestones. The amended milestones allotted for the years 2008 and 2009 regarding population coverage were exceeded whilst there was a marginal underperformance of the territorial coverage requirements. In the event that license obligations are not met by an operator, the UKE has the power to limit or confiscate the relevant license, if the issue is not rectified. 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 (see also Note 13).

Overpayment of tax

According to Netia, the decisions of the UKS Director and the Tax Chamber Director described in Note 13 are in conflict with the relevant tax regulations. In addition to major procedural faults, Netia believes that the tax authorities' decisions incorrectly interpret and apply a number of material regulations. Netia bases its position on opinions from several independent tax and legal advisors, as well as tax law experts, which conclude that the claims of the Directors of the Tax Control Office and the Tax Chamber have no legal grounds.

Due to the above, the Company does not treat PLN 58,325 of taxes and interest paid to the tax Authorities in February 2010, as an expense. The said amount is instead treated by Netia as a receivable from the tax authorities. Should the decision of the Voivodship Administrative Court and any subsequent appeals, be positive for the Company, the amount of unduly paid tax plus interest will be proven to be an overpayment of tax and interest and must be returned by the tax authorities together with interest, currently calculated at the annual rate of 12.5%.

Although there is a significant degree of instability in the interpretation of tax regulations by the Tax Authorities and the Courts, Management is highly confident that the merits of its arguments will prevail in the Courts and the funds will be returned by the tax office. However, should Netia lose this case and all subsequent appeals, the amount of PLN 58,325 would have to be reclassified as a taxation expense relating to prior years. The next hearing in this matter at the Voivodship Administrative Court is scheduled for February 22, 2011.

43. Subsequent events (not in thousands)

On January 14, 2011, Third Avenue Management LLC informed the Company that it had reduced its holdings of the Company's shares to 85,578,145 constituting 21.97% of the Company's share capital and carrying 21.97% of the total number of votes at the General Shareholders' Meeting of the Company.