Warsaw, May 15, 2006

COMMENT ON THE FINANCIAL REPORT FOR THE FIRST QUARTER OF 2006

This Comment presents the financial results of Netia S.A. (“Netia”, the “Company”, the “Issuer”) and the consolidated financial results for the Netia S.A. Group (“Netia Group”).

1. The Netia Group’s structure

The consolidated financial statements include the financial statements of the Company and the following subsidiaries:

UNI-Net Sp. z o.o.
Regionalne Sieci Telekomunikacyjne El-Net S.A.
Polbox Sp. z o.o.
Netia WiMax II S.A. (previously operating under the name Netia Globe S.A.)
Netia WiMax S.A. Group (previously operating under the name Netia Świat S.A.)
Netia Mobile Sp. z o.o.

as well as the income and expenses of Netia Ventures Sp. z o.o. for the first quarter of 2006, i.e. until 100% of shares in Netia Ventures Sp. z o.o. were sold.

The Netia Group accounts for the investment in P4 Sp. z o.o. using the equity method.

The Netia WiMax S.A. Group’s financial statements include the financial statements of Netia WiMax S.A. and Świat Internet S.A. Group.

The Świat Internet S.A. Group’s financial statements include the financial statements of Świat Internet S.A. and the HFC Internet Sp. z o.o. Group composed of HFC Internet Sp. z o.o. and Premium Internet S.A.

2. Changes within the Netia Group’s structure

Sale of investments

On March 30, 2006 Netia transferred to P4 ownership of 100 (not in thousands) shares of Netia Ventures Sp. z o.o. (“Netia Ventures”), with a total nominal value of PLN 50, representing 100% of its share capital, for a total price of PLN 75.

3. Shareholders holding more than 5% of the votes at the General Shareholders’ Meeting of Netia as at the date of filing of this report

Based on the information presented to the Issuer by the shareholders, as at the date of filing of this report, significant blocks of the Company’s shares were held by the following entities (the interest and the number of votes calculated on the basis of the number of shares constituting the Issuer’s share capital as at May 15, 2006):

Novator Telecom Poland II S.a.r.l.

In the period from the submission of the previous quarterly report Novator Telecom Poland II S.a.r.l. increased its share in the Company’s capital and held 98,243,602 shares constituting 25.2% of the Company’s share capital and carrying 25.2% of the total number of votes at the General Shareholders’ Meeting of the Company.

Subsidiaries of SISU Capital Limited

The subsidiaries of SISU Capital Limited held a total of 23,743,225 of the Company’s shares constituting 6.1% of its share capital and carrying 6.1% of the total number of votes at the General Shareholders’ Meeting of the Company. The number of the Company’s shares held by the subsidiaries of SISU Capital Limited has not changed since February 24, 2006.

Furthermore, in the period from the submission of the previous quarterly report, the subsidiaries of Griffin Capital Management Ltd reduced their interests in the Company's share capital and, as at the date of this report being submitted, did not exceed the threshold of 5% of the total number of votes at the general Shareholders' Meeting of the Company.

4. Changes in shares and share options held by members of the Company's Management Board and Supervisory Board

Since adopting the employee share option scheme (the „Plan") on June 10, 2003 to March 31, 2006, the Supervisory Board approved for issue a total number of 14,567,347 options for members of the Management Board as well as for Netia's key employees. The options are exercisable until December 20, 2007. On March 29, 2006, the Company's General Shareholders' meeting agreed on the change of Netia's statute in relation to the extention of the period during which series K shares may be offered to members of the Management Board and key employees to execute their rights resulting from the Plan. Therefore, the Supervisory Board may extend the period when options may be exercised, up to December 20, 2012. The strike price, depending on the agreement, ranges between PLN 2.53 and PLN 5.30 per share.

In the three-month period ended March 31, 2006 the following changes took place in the number of options granted under the Plan:

Three-month period ended March 31, 2006	
At the beginning of the period	2,776,650
Exercised...	(1,817,188)
At the end of the period..................................	959,462

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

Three-month period ended March 31, 2006	Wojciech Mądalski	Paul Kearney	Piotr Czapski	Total
At the beginning of the period	906,047	362,419	543,628	1,812,094
Exercised...	(906,047)	-	-	(906,047)
At the end of the period..................................	-	362,419	543,628	906,047

The number of options held by members of the Management Board has not changed as at the date of filing of this report.

The members of Supervisory Board did not hold any options as at March 31, 2006.

In the first quarter of 2006 the following changes took place in the number of Netia's shares held by members of the Company's Supervisory Board:

Three-month period ended March 31, 2006	Andrzej Radzimiński	Nicholas Cournoyer	Raimondo Eggink	Constantine Gonticas	Total
At the beginning of the period	11,000	9,000	-	-	20,000
Resignation	-	(9,000)	-	-	(9,000)
Appointment	-	-	20,000	43,000	63,000
At the end of the period..................................	11,000	-	20,000	43,000	74,000

The number of shares held by members of the Supervisory Board has not changed as at the date of filing of this report.

The movements in the number of Netia's shares held by members of the Company's Management Board are presented below:

Three-month period ended March 31, 2006	Wojciech Mądalski
At the beginning of the period	2,043,292
Issuance of series K shares..............................	533,315
At the end of the period..................................	2,576,607

Furthermore, on April 5, 2006, Mr. Tom Ruhan was appointed the member of the Management Board and he held 253,593 Netia's shares, as of that day. There were no further changes in the number of Netia's shares held by members of the Company's Management Board until the date of filing of this report.

5. Legal proceedings

Millennium

In August and September 2000, the Company entered into certain agreements to acquire all of the outstanding equity of Millennium Communications S.A. ("Millennium"), a provider of telecommunications services in Warsaw. Certain advances were made to Millennium following the execution of the agreements, and currently a loan of EUR 2.9 million (PLN 11.4 million at the March 31, 2006 exchange rate) increased by the applicable interest is outstanding from Millennium. In December 2000, the Company brought a claim for the repayment of the loan against Millennium in the District Court in Warsaw. The matter is still pending. In 2001, a valuation allowance of PLN 17.0 million was recorded as other operating expense against the outstanding amount receivable from Millennium as a result of the events described above.

In September 2003, Newman Finance Corp. ("Newman"), Millennium's sole shareholder, filed a claim against the Company for damages of PLN 45.4 million, which is the equivalent of EUR 11.5 million plus interest accrued since the date of filing the claim until the date of payment. This claim was filed for damages incurred when a security was placed over Millennium's shares between January 4, 2000 and November 1, 2002 in connection with litigation concerning Millennium's failure to perform the agreements entered in August and September 2002. On June 8, 2005 the District Court dismissed the claim. The District Court determined that Newman neither proved the damage occurrence nor its magnitude. On July 20, 2005, Newman filed an appeal. The matter is still pending.

On April 5, 2005, Millennium filed a claim against Regionalne Sieci Telekomunikacyjne „El-Net" S.A. („El-Net") in connection with the alleged acts of unfair competition of El-Net against Millennium. Millennium sought to prohibit El-Net from submitting offers or other market proposals and conducting any commercial activities in relation to a pool of 30,000 telephone numbers held by El-Net. El-Net filed an answer to the claim on June 6, 2005 in which it requested the District Court to dismiss the claim as wholly unsubstantiated. The matter is still pending.

In May 2005, Millennium filed a motion to secure the claim against Netia in connection with the alleged acts of unfair competition of Netia against Millennium. On August 21, 2005 Millennium filed a motion against Netia in connection with the claim. Netia filed an answer to the claim on September 7, 2005 in which it rejected the claim as wholly groundless and unsubstantiated. The matter is still pending.

In July 2005, Millennium filed a motion to secure the claim against El-Net for determination that an agreement between El-Net and Millennium concerning provisions of telephone services and the use of the 30,000 telephone numbers by Millennium was not effectively terminated by El-Net. The District Court issued a decision on August 8, 2005, in which the claim was secured by an injunction prohibiting El-Net from submitting offers or other market proposals and conducting any commercial activities in relation to those 30,000 telephone numbers. The motion was delivered to El-Net on August 31, 2005, and was appealed by El-Net on September 5, 2005. On August 21, 2005, Millennium filed a motion against El-Net in connection with the claim to which the injunction pertained to. El-Net filed an answer to the claim on October 19, 2005 in which it requested the District Court to dismiss the claim as wholly unsubstantiated. The matter is still pending.

Management, having obtained legal advice, does not believe that the settlement of the matters described above will have a material adverse effect on the Netia Group's financial condition. Accordingly no liability has been recorded for the claims.

Minority shareholders

On August 1, 2002, the Company received a copy of a claim filed with the District Court in Warsaw by an individual shareholder demanding the cancellation of sections 10, 11 and 13 of Resolution No. 2 adopted by the Company's General Meeting on April 4, 2002. The individual shareholder claimed that the distribution of the Company's warrants under the financial restructuring was harmful to the minority shareholders and violated good custom. On August 14, 2002, the Company responded requesting the District Court to dismiss the claim. At the court hearing held on February 4, 2004, the District Court in Warsaw decided to forward the claim to the Regional Court for the capital city of Warsaw for its determination. At the hearing held on April 21, 2005 the Regional Court returned the claim due to the plaintiff's failure to comply with the legal claim requirements. On May 19,2005, the minority shareholders filed a complaint regarding this return. The matter is still pending.

In a second similar matter, a minority shareholder's claim was dismissed on merits by the Regional Court in Warsaw. On March 25, 2005, the minority shareholder filed an appeal. On December 8, 2005 the District Court examining the appeal overruled the judgment of the Regional Court and decided that the case has to be re-examined. The District court stated that the case is invalid in its entirety due to the fact that it should be the District Court not the Regional Court where the case should have been examined in the first resort. The matter is still pending.

Management, having obtained legal advice, does not believe that the settlement of the matters described above will have a material adverse effect on the Netia Group's financial condition. Accordingly no liability has been recorded for the claims.

6. Factors which may have an impact on the result of the Netia Group

Risk of changes to the Netia Group's strategy

The performed Restructuring has become the basis for developing a strategy which will enable the Company to pursue its mid-term and long-term objectives. In May 2003, the Supervisory Board approved the basic aims of the Netia Group's development strategy. The business plan was approved by the Supervisory Board in October 2003 and then, based on our boardening strategic scope, updated in December 2005. Currently, the business plan is being executed in accordance with the objectives. However, it is possible that the detailed solutions it includes will be modified and it cannot be predicted whether such changes may adversely affect the operating activity of the Netia Group, its financial standing or its overall performance.

Risk of changes in the shareholder structure, which may influence business activity

Currently, Netia is not controlled by any strategic investors, and its Shares are held by a large number of shareholders. In December 2005 Novator Telecom Poland II S.a.r.l. („Novator"), with its seat in Luxembourg, purchased 40,088,862 shares in the Company, thus became the majority shareholder of Netia. Moreover, as a result of the public tender for the acquisition of 52,204,740 Netia shares, dated December 19, 2005, Novator increased its stake in the Company's share capital and according to the information passed to the Company, as of April 28, 2006 it held 98,243,602 shares which represented as at the date of filing of this report, 25.2% of the Company's share capital and 25.2% of the aggregate number of votes at the Company's General Meeting of Shareholders. In addition, Novator informed the Company that it was considering increasing its holding in the aggregate number of votes in Netia within 12 months from the delivery of the notification, up to a threshold of 33% minus 1 share. Neither Netia's corporate documents nor the provisions of Polish law provide for any serious restrictions to changes in control over the Issuer in the event of third parties acquiring a considerable number of the shares. Thus, such changes of control may and may materially affect the composition of the Supervisory Board and the Management Board and, in turn, the strategy and business activity of the Netia Group. Due to the above, the Issuer cannot guarantee that the newly adopted strategy of the Netia Group will be pursued in accordance with its initial objectives. Furthermore, it is possible that the new shareholders might develop a new strategy which may materially differ from the current one.

Risk connected with the impact of potential future takeovers and acquisitions

Revenues and financial performance of the Netia Group may materially be affected by takeovers and mergers with other entities. Upon the Company's takeover of another entity, the process of fully integrating this entity may carry high risks, e.g. employment termination by key employees, the loss of a certain segment of its customers or high costs of the entire integration process.

The highly fragmented market of alternative operators rendering wireline telephone services may result in their increasing consolidation within the Polish market. The Company shall evaluate potential takeovers and acquisitions whenever such possibilities should arise. The performance of such transactions requires the special involvement of the Company's high-ranking managers and may entail high costs connected with the identification and evaluation of candidates for the takeover, the negotiating of agreements and integration of the entities acquired. The Netia Group may request additional funding in order to conduct such transactions.

The benefits from potential takeovers will depend mostly on the extent to which the Netia Group is able to integrate the acquired entities into its structures. Future company acquisitions may entail the acceptance of existing liabilities and the risk of concealed liabilities. The Netia Group cannot guarantee that beneficial takeover possibilities will arise in the future, nor, if such possibilities arise, that they will result in the successful integration of the acquired entities with the Netia Group. Failures to integrate the acquired entities into the structures of the Netia Group may adversely affect its activity and its financial standing.

Technological risk

The telecommunications sector is an area witnessing dynamic technological changes. In designing and expanding its networks, the Netia Group uses the newest technical solutions. However, what cannot be predicted is how the Netia Group's activity may be affected by technological advances in the field of fixed-line telephony, wireless transmission, and voice transmission protocol via the Internet or cable television telephony. In particular, the activity of the Netia Group may be affected by the tendency to provide telecom services via wireless or portable platforms, with wireless broadband access and third generation mobile cellular telephone systems equipped with the IP. Even if the Netia Group succeeds in adapting its activity to such technological advances, it cannot be guaranteed that other market participants with whom the Netia Group must compete will be able to adapt to these changes, at least to the same extent.

Risk of employment termination by key executives and difficulties related to the recruitment of new, competent executives

The activity of the Netia Group is dependent on the quality of work of its staff and employees in executive positions. The Management Board cannot guarantee that the possible termination of employment by some of its key executives will not adversely affect the financial standing and performance of the Netia Group, which, should some of its executives terminate their employment, may then lack executives with sufficient knowledge and experience in the field of management and operating activity. Changes in composition at the Company's executive levels may result in disruptions in the Netia Group's business activity.

Risk resulting from changes in the Telecommunications Law

The Telecommunications Law includes provisions compliant with the new package of EU directives in the field of telecommunications, i.e. "Package 2002". The Telecommunications Law entered into force on September 3, 2004, with the exception of several provisions, which entered into force on January 1, 2005.

On the basis of the Telecommunications Law, the President of the UKE may impose obligations on operators controlling access to subscribers, so as to ensure that end users are able to communicate with users of another telecom provider, including the obligation to interconnect networks. The following obligations may be imposed upon a telecommunications provider which is deemed to have a significant position on one of the telecom markets listed in the resolution of the competent Minister of Telecommunications: the obligation to grant other operators access to the network, especially with regard to its interconnection or mutual use of the local loop; the obligation to calculate costs and relate the network access tariffs to these calculations; the obligation to maintain regulatory accounts separately for each of the telecom services. The Telecommunications Law does not define the size of the area in which the market position of a telecommunications provider is evaluated. As a result, the President of the UKE may name telecommunications providers as having a significant position in a small area, in which even a small telecommunications provider can have a significant market share. This will serve as basis for imposing any other regulatory obligations upon such company, which will have to be proportional to the superior market position of the company, i.e. to the extent that it prevents effective competition on the given telecom market.

Pursuant to the Telecommunications Law, each public telecommunications network operator is obliged to conduct negotiations concerning interconnection agreements upon another telecom operator's request. However, the President of the UKE shall be obliged to resolve any disputes between the parties to the negotiations by an administrative decision, which shall replace the relevant agreement only if one of the negotiating parties is a public telecommunications network operator obliged to provide the interconnection.

The Telecommunications Law states that the obligation to provide universal services shall rest with the operator selected pursuant to a decision of the President of the UKE issued after a tender procedure. On May 5, 2006 President of the UKE passed decisions assigning TP SA as an operator obliged to provide universal services for 6 months. In the decision President of the UKE stated that next decision would oblige TP SA to provide universal service for 5 year period. Telecommunications providers whose revenues from telecom activity exceed PLN 4 million will have to co-finance the performance of this obligation, by co-financing the funding of universal services, if the funding has been assigned to the telecommunications provider selected on the basis of the decision of the President of the UKE. The share in the funding that a telecommunications provider shall be obliged to provide shall also be established by a decision of the President of the UKE; however, it may not exceed 1% of the telecommunications provider's revenues in the given calendar year. The amount of the share in the funding of the universal service shall constitute a deductible cost, as defined by the Act on Corporate Income Tax.

The present stage of development of the telecommunications market in Poland does not guarantee that the Netia Group will not be obliged to co-finance the funding of universal services on the terms described above. However, this obligation shall not arise until the end of 2006.

Before passing the decision by President of the UKE assigning TP SA as an operator obliged to provide universal services, the obligation to provide a universal services had rested with the provider deemed as having a significant position on the market for telephone services in fixed-line telephone networks on the basis of the previous regulations, i.e. also TP SA. However this operator had not been entitled to receive funding on the grounds of providing universal services.
The Telecommunications Law shall oblige telecommunications providers to pay annual telecommunications fees of up to 0.05 % of the provider's annual revenues from telecommunications activity generated in the financial year 2 years prior to the year to which the annual fee pertains, if the annual revenues exceed PLN 4 million. Pursuant to the ordinance of the Minister of Infrastructure dated December 27, 2004 referring to the amount, settlement, terms and modes of payment of the annual telecommunications fee (Journal of Law No. 285 item 2857, as amended) the fee for 2006 was fixed at the maximum statutory amount. The amount of the annual telecommunications fee shall constitute a deductible cost as defined by the Act on Corporate Income Tax.

The decisions issued by the President of the URTiP pursuant to the Telecommunications Law obligate Netia and El-Net to execute subscribers' right to retain their numbers when changing operators as from January 1, 2006. Despite Netia and El-Net's readiness to perform this obligation and arrangements with other telecommunication operators, the Management Board cannot guarantee that it will be possible to enter into an agreement with particular telecommunication operators to define the terms and conditions of cooperation between the parties to the extent required to execute the subscribers' rights to retain his/her number.

Dependence of the Company on TP SA due to interconnections

The rendering of telecommunications services by the Netia Group is dependent on the possibility of access to the telephony network of TP SA. Except for some cases, calls initiated in Netia's and El-Net's networks ending outside these networks, including the majority of international and domestic long distance calls by subscribers of Netia Group companies, are - due to technical reasons - executed via the network of TP SA. According to the provisions of the new Telecommunications Law TP SA is obligated to connect companies like Netia, El-Net to its network. Netia Group companies running operations concluded interconnection agreements with TP SA covering each area in which the Company conducted its telecommunications activities.

Delays and difficulties observed in the past and related to concluding interconnection agreements with TP SA caused the delay of the commencement of commercial activities in some areas. Problems have also emerged in relation to the closing of the interconnection agreement with TP SA relating to Netia's rendering domestic long distance telecommunications services. Currently, the decisions of the UKE President regarding interconnection tariffs for "0-20" Internet access service are not fully observed by TP SA. Further obstacles or delays in the interconnection with the TP SA network or impediments to Netia's rendering some services via the network of TP SA may limit Netia's ability to render telecommunications services and have a major negative effect on its operations and financial results.

TP SA has undertaken a range of other activities resulting in impediments to Netia and El-Net in the access to the market. These are, among other things: (a) termination or failure to execute by TP SA interconnection agreements with Netia and El-Net stipulating co-operation terms and conditions within various numbering zones, (b) impeding the rendering by Netia of audio text services through imposing onerous contractual terms and conditions, and, in particular, increasing the tariffs for such services, (c) delay in the preparation and application by TP SA of framework offers compliant with legal requirements and, thus, the failure of TP SA to guarantee other operators contractual terms and conditions within telecommunications access on conditions not worse than those set out in framework offers and referring to interconnection agreements, telecom links lease, access to the local loop, access to TP SA network nodes for the sake of the execution of "Bitstream Access" service, sharing the infrastructure. Netia and El-Net have undertaken activities aimed at the inhibiting such actions of TP SA by commencing - against TP SA - multiple court proceedings, proceedings to secure claims, antimonopoly and administration proceeding in front of the UKE President, and by defending the interests of Netia and EL-Net in court and administration proceedings commenced upon TP SA's application. The Management Board thinks that the Company's position in all pending proceeding is fully supported by current Telecommunications Law. However, the Management Board is not able to predict the outcome of the above proceedings. Any probable decisions in pending cases, which would be unfavourable for Netia or El-Net and referring to agreements with TP SA might negatively affect the financial results of the Company.

Presumptive major fee increase that Netia Group may incur in the future for the benefit of TP SA pursuant to interconnection agreements (except from renewable agreements) or the failure to decrease interconnection tariffs in the case of a probable reduction in call fees, may result in the execution of lower margins by Netia or Netia may not be able to offer telephony services at competitive prices. Additionally, the interconnection fees that Netia has to incur in relation to the execution of international or domestic long distance calls via the network of TP SA are calculated based on TP SA tariffs for such calls and not on prices collectible by Netia from its customers. Thus, a change in Netia's tariffs without a change in TP SA tariffs may have a major negative effect on the Company's financial results.

Risk of increased competition

The Netia Group's main competitors in the field of telephone services are TP SA and cellular network operators, and in some geographic areas also other operators providing wireline telephone services. Within the unregulated market for data transmission services, the main competitors are numerous providers of various sizes, the most significant of which is TP SA. Poland has witnessed a considerable increase in competition, which, as can be expected, will intensify even further, considering the lack of legal barriers in entering the market and increasing integration within the European Union. Pursuant to the Telecommunications Law, every telecommunications provider may pursue telecommunications activity on the basis of its entry into the Register of Telecommunications Providers kept by the President of the UKE. Netia is unable to evaluate the extent to which new market participants will use the availability of such rights, particularly with regard to the significantly lower costs of entering the market than those incurred by the Netia Group. The Warsaw market will probably continue to witness intense competition for customers. The Management Board is unable to evaluate the extent to which the intensification of competition will affect the Netia Group's activity.

Competition from TP SA

TP SA occupies a leading position among wireline telephone service operators in Poland. At the same time, it enjoys a stable position on the market for data transmission and indirectly, through its subsidiary on the cellular telephone market. Within the scope of wireline telephone services, the Netia Group encounters competition from TP SA in all the geographic areas in which it operates. TP SA is a much larger entity than the Netia Group and possesses much wider backbone and access networks. It enjoys long-established relationships with many customers which the Netia Group considers its target customers, including many companies operating on the territory of the Netia Group's operation. The infrastructure used by TP SA in these territories is comparable to the infrastructure of the Netia Group in terms of the technologies employed.

Moreover, TP SA still maintains a leading position among operators of domestic long-distance calls, which enables it to offer more flexible tariffs. It is difficult to predict what policies TP SA will pursue with regard to tariffs, the selection of target markets and arrangements concerning access to its infrastructure and interconnections as a reaction to the extension of the network by the Netia Group and more intense competition from the Netia Group in various areas of the country. However, the Management Board expects that TP SA will compete with the Netia Group for prices and the most attractive customers. In the past, the Netia Group was forced to lower its prices in order to attract new customers and retain the current ones, and such measures may also be necessary in the future. The Management Board expects that TP SA will maintain a strong competitive position against the Netia Group on the Warsaw market and in most geographic areas where the Netia Group provides telephone services, and will continue to compete with the Netia Group in other fields, including data transmission services and internet access. It is possible that aggressive competition from TP SA will materially and adversely affect the revenues of the Netia Group and the results of its operating activity.

TP SA owns most local loops and offers other operators access to the network of these local loops on terms that, in many cases, render the addition of a customer to the network too expensive. Even though the Telecommunications Law provides a basis for the President of the UKE to oblige operators with a dominant market share to enable other enterprises to use its network on equal terms, in many cases the Netia Group is unable to negotiate satisfactory terms with TP SA. It cannot be guaranteed that the Netia Group will be able to expand its network to urban areas, where TP SA's extensive telecommunications infrastructure already exists, unless the President of the URTiP should issue relevant decisions specifying the principles for interconnecting other operators to the local loop.

The plans of the Netia Group allow for projected revenues arising from its activity on the International Calls market. Similar to other call types, the ability to provide such services is dependent on ensuring the necessary infrastructure and executing the terms of interconnection agreements with TP SA.

As TP SA occupies a leading position on the telecommunications market in Poland and the Netia Group's areas of activity usually differ from those of other independent operators, all indirect subscribers of the Netia Group that use its domestic long-distance telephone services are subscribers of TP SA. TP SA has consistently been refusing to issue invoices to its subscribers using long-term telephone services via Netia, which forces the Netia Group to conclude separate agreements with such customers and issue separate invoices. This inconvenience discourages many potential users of the indirect services rendered by the Netia Group as part of their domestic long-distance telephone services, which, consequently, results in a decrease in potential revenues. Moreover, the necessity to conclude separate agreements and issue separate invoices entails additional costs. This situation may continue.

Competition from other independent operators

According to the regulations, which were in force before January 1, 2001, the Minister of Telecommunications granted licenses for the provision of local telecom services within a given geographic area (usually within a given number zone) to one private operator (apart from TP SA). Obtaining licenses has entailed much higher costs. As a result of the fact that obtaining a permit is significantly cheaper than obtaining a license, and the fact that the lengthy process for obtaining a license has been eliminated, since January 1, 2002 many new operators have obtained such permits. Pursuant to the New Telecommunications Law, telecommunications activity may be pursued on the basis of an entry in the Register of Telecommunications Providers kept by the President of the UKE. Therefore, the Netia Group expects the number of operators active in the areas in which it conducts its activities to increase. In 2003 there was a swap of license fee liabilities of the then-operating subsidiaries of the Netia Group, and in the case of the fees which El-Net was obliged to pay, the swap for capital expenditures took place in 2006. Part of outstanding local license fee obligations and the prolongation fees was cancelled. However, it cannot be guaranteed that the Netia Group will not be forced to pay these fees in the future, which may give new market participants a certain advantage over the Netia Group.

In some areas in which the Netia Group operates, there are large institutions with their own internal telecommunications networks (where the users of the telecom services of such institutions include, additionally, the inhabitants of the given area), which reduces the potential revenues that the Netia Group could generate in these areas, and such operators may be a potential source of competition in the future.

Competition from cellular mobile telephone operators

Cellular telephony services may currently be deemed competitive to the services of wireless telephone operators. This can be explained by the increased price competition from cellular network operators, which consequently lower their rates in relation to operators of wireline telephone services that continue to balance their tariffs. The offers of cellular telephone operators include, among others, tariff plans based on a system of prepayments for calls made, without additional subscription fees. Moreover, these operators have entered into interconnection agreements with TP SA on terms more favourable than for operators of wireline telephone services. Additionally, in the light of Polish law, mobile cellular telephone services are not universal services. Therefore, mobile cellular telephone operators are not obliged to provide services to all customers wishing to use these services.

Due to resolution of the tender for the UMTS frequency P4, Netia Group's affiliated company, intends to start providing mobile telephony services. There are significant risks pertaining to conducting this type of activity. The main risk is related to the significant saturation of the mobile telephony market and the fact that the existing operators have a well-developed radio network and customer base. Additionally, in the nearest future a tender for GSM1800 frequencies will be resolved, which may additionally increase the number of operators. In addition there is a risk that mobile virtual network operators (MVNO), competitive to P4 and its services, will appear. The pace of network development and the possibility of accessing the networks of existing operators under domestic roaming constitute important risk elements. The total value of the Netia Group's investment in P4 is limited to EUR 90 mln. The expected benefits for the Netia Group include exclusivity for direct distribution of P4 products and the related revenues, the possibility of providing outsourcing services for P4, the development of a convergent offer generating additional revenues, and limiting loss of fixed-line telephony clients, and guaranteed access to mobile telephony products while P4 holds the reservation for the UMTS frequency.

Other sources of competition

The Netia Group also encounters competition in the field of voice services from companies offering alternative forms of such services, e.g. cable network services. Moreover, in the course of the development of the data transmission and internet services, the competition from numerous providers of such services is increasing, especially with regard to voice transmission technologies via the Internet, including providers that use the broadband ADSL access. The future impact of the competition from providers of the said services on the activity of the Netia Group cannot be estimated.

Market consolidation

The highly fragmented market of alternative operators rendering wireline telephone services may result in their increasing consolidation within the Polish market. In its pursuit of one of the objectives of the approved strategy of the Netia Group, that is, the acquisitions of other entities, the Netia Group does not dismiss any methods of consolidation, and it is possible that it will continue to participate in mergers with competitors. However, the Netia Group’s role in the consolidation process may be insignificant, in particular if no additional funding can be obtained. The Management Board is unable to describe the impact of such consolidation on the financial standing of the Netia Group and its impact on the shareholders of Company.