

## INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

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Report of Independent Registered Public Accounting Firm

The Supervisory Board and Stockholders  
Telekom Austria Aktiengesellschaft:

We have audited the accompanying consolidated balance sheets of Telekom Austria Aktiengesellschaft and subsidiaries as of December 31, 2005 and 2004, and the related consolidated statements of income, stockholders' equity and comprehensive income, and cash flows for each of the years in the three-year period ended December 31, 2005. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We did not audit the financial statements of mobilkom austria AG & Co KG and mobilkom austria AG and subsidiaries (collectively "mobilkom") for the year ended December 31, 2003, wholly-owned consolidated subsidiaries, which statements reflect revenues constituting 48.9 percent of total consolidated revenues for the year ended December 31, 2003. Those statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for mobilkom for the year ended December 31, 2003, is based solely on the report of the other auditor.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits and the report of the other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audits and the report of the other auditors, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Telekom Austria Aktiengesellschaft and subsidiaries as of December 31, 2005 and 2004, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2005, in conformity with U.S. generally accepted accounting principles.

As discussed in note 1 to the consolidated financial statements, the Company adopted the provisions of Statement of Financial Accounting Standards No. 123 (R) "Accounting for Stock-Based Compensation" effective January 1, 2005, Financial Accounting Standards No. 123 "Accounting for Stock-Based Compensation" effective January 1, 2004, and Statement of Financial Accounting Standards No. 143 "Accounting for Asset Retirement Obligations" effective January 1, 2003.

KPMG Wirtschaftsprüfungs- und Steuerberatungs GmbH

Vienna, Austria  
March 1, 2006

*KPMG Wirtschaftsprüfungs- und Steuerberatungs GmbH*

## **Report of Independent Registered Public Accounting Firm**

The Supervisory Board and Stockholders  
mobilkom austria AG & Co KG and  
mobilkom austria AG:

We have audited the consolidated balance sheets of mobilkom austria AG & Co KG and mobilkom austria AG and subsidiaries (collectively "mobilkom austria"), wholly-owned consolidated subsidiaries of Telekom Austria Aktiengesellschaft and the related consolidated statements of income, stockholders' equity and comprehensive income, and cash flows for the period ended December 31, 2003. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of mobilkom austria as of December 31, 2003 and the results of its operations and its cash flows in the period ended December 31, 2003 in conformity with accounting principles generally accepted in the United States of America.

As discussed in note 1 to the consolidated financial statements, mobilkom austria adopted the provisions of Statement of Financial Accounting Standards No. 143 "Accounting for Asset Retirement Obligations" effective January 1, 2003.

Grant Thornton  
Wirtschaftsprüfungs-und Steuerberatungs-GmbH



Vienna, Austria  
February 12, 2004

**TELEKOM AUSTRIA AG**  
**CONSOLIDATED BALANCE SHEETS**  
(in EUR '000s, except per share information)

	Notes No	December 31, 2005	December 31, 2004
<b>ASSETS</b>			
Current assets			
Cash and cash equivalents.....		116,756	288,195
Short-term investments.....		7,301	10,540
Accounts receivable - trade, net of allowances of EUR 104,234 and EUR 73,463 as of December 31, 2005 and December 31, 2004.....	(5)	452,878	408,820
Accounts receivable sold, net of allowances of EUR 39,820 and EUR 21,150 as of December 31, 2005 and December 31, 2004.....		228,279	173,350
Receivables due from related parties.....	(6)	66	85
Inventories.....	(7)	90,913	83,110
Deferred tax assets.....	(21)	27,803	59,939
Prepaid expenses.....		121,701	100,169
Taxes receivable.....		11,134	3,702
Assets held for sale.....	(11)	880	2,660
Other current assets.....		146,868	143,338
<b>TOTAL CURRENT ASSETS.....</b>		<b>1,204,579</b>	<b>1,273,908</b>
Property, plant and equipment, net.....	(10)	3,774,554	3,888,691
Goodwill.....	(8)	1,149,175	596,565
Other intangible assets, net.....	(9)	1,432,516	667,337
Investments in affiliates.....	(3)	3,642	3,570
Other investments.....		156,900	133,239
Deferred tax assets.....	(21)	5,385	19,436
Other assets.....		685,102	659,761
<b>TOTAL ASSETS.....</b>		<b>8,411,853</b>	<b>7,242,507</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>			
Current liabilities			
Short-term borrowings.....	(12)	785,773	751,139
Accounts payable - trade.....		529,197	534,498
Accrued liabilities.....	(13)	171,004	194,319
Payables to related parties.....		20,244	22,924
Deferred income.....	(14)	199,510	168,984
Income taxes payable.....		6,260	18,005
Other current liabilities.....		207,233	182,217
<b>TOTAL CURRENT LIABILITIES.....</b>		<b>1,919,221</b>	<b>1,872,086</b>
Long-term debt, net of current portion.....	(16)	2,557,703	1,647,171
Lease obligations, net of current portion.....	(17)	817,866	761,132
Employee benefit obligations.....	(18)	107,261	109,984
Other liabilities and deferred income.....	(19)	140,344	110,504
Stockholders' equity			
Share capital, no par value shares, 560,000,000 authorized (2004: 560,000,000), 500,000,000 issued (2004: 500,000,000), 482,502,894 outstanding (2004: 493,744,306).....		1,090,500	1,090,500
Treasury stock.....		(247,818)	(63,353)
Additional paid in capital.....		453,614	458,137
Retained earnings.....		1,565,830	1,266,551
Accumulated other comprehensive gain / (loss).....		7,332	(10,205)
<b>TOTAL STOCKHOLDERS' EQUITY.....</b>	(23)	<b>2,869,458</b>	<b>2,741,630</b>
<b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY.....</b>		<b>8,411,853</b>	<b>7,242,507</b>

see accompanying notes to consolidated  
financial statements

**TELEKOM AUSTRIA AG**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**  
(in EUR '000s, except per share information)

	Notes No	twelve months ended		
		December 31,		
		2005	2004	2003
Operating revenues (a) .....	(24)	4,377,291	4,056,268	3,969,750
Operating expenses (b)				
Materials.....		(346,504)	(324,518)	(297,084)
Employee costs, including benefits and taxes.....		(678,974)	(673,688)	(699,348)
Depreciation and amortization.....		(1,119,801)	(1,114,830)	(1,133,148)
Impairment charges.....		(17,388)	(1,334)	(6,825)
Other operating expenses.....	(25)	(1,594,632)	(1,489,224)	(1,463,521)
<b>OPERATING INCOME</b> .....		<b>619,992</b>	<b>452,674</b>	<b>369,824</b>
Other income (expense)				
Interest income (c) .....		89,084	70,016	75,167
Interest expense (d) .....		(198,151)	(188,818)	(230,979)
Equity in earnings of affiliates.....		570	552	19,112
Other, net.....	(26)	12,025	15,656	(567)
<b>INCOME BEFORE INCOME TAXES AND</b> <b>MINORITY INTERESTS</b> .....		<b>523,520</b>	<b>350,080</b>	<b>232,557</b>
Income tax expense.....	(21)	(106,372)	(122,186)	(83,036)
Minority interests .....		(2)	(631)	(3,422)
<b>INCOME BEFORE CUMULATIVE EFFECT</b> <b>OF CHANGE IN ACCOUNTING PRINCIPLE</b> .....		<b>417,146</b>	<b>227,263</b>	<b>146,099</b>
Cumulative effect of change in accounting principle, net of tax of EUR 6,071 in 2003" .....	(15)	-	-	(11,858)
<b>NET INCOME</b> .....		<b>417,146</b>	<b>227,263</b>	<b>134,241</b>
Basic and fully diluted earnings per share.....	(23)	0.85	0.46	0.27
Basic and fully diluted earnings per share excluding cumulative effect of change in accounting principle.....		0.85	0.46	0.29
a) includes revenues from related parties of .....		57,497	62,102	89,506
b) includes operating expenses from related parties of .....		117,893	124,699	128,694
c) includes interest income from related parties of .....		1	1	1
d) includes interest expense from related parties of .....		18	59	30

see accompanying notes to consolidated  
financial statements

**TELEKOM AUSTRIA AG**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(in EUR '000s, except per share information)

	Notes No	twelve months ended		
		December 31,		
		2005	2004	2003
<b>Cash generated from operations</b>				
Net income.....		417,146	227,263	134,241
Adjustments to reconcile net income to cash generated from operations				
Depreciation, amortization and impairment charges .....		1,137,189	1,116,164	1,139,973
Write-offs from investments.....		284	716	2,840
Employee benefit obligation - non cash.....		4,246	908	307
Allowance for doubtful accounts.....		43,393	23,597	30,629
Change in deferred taxes.....		67,532	62,938	59,241
Equity in earnings of affiliates in excess of dividends received.....		(73)	(15)	1,027
Stock compensation.....	(20)	13,322	4,766	-
Asset retirement obligation - non cash expense, net.....		3,087	5,829	1,336
Settlement of asset retirement obligation.....		-	(2,248)	-
Cumulative effect of change in accounting principle, net of tax.....	(15)	-	-	11,858
Gain on sale of investments.....		(4,013)	(5,163)	(17,903)
(Gain) / loss on disposal / retirement of equipment.....		(1,510)	28,788	41,571
Other.....		(5,770)	(252)	(660)
		<u>1,674,833</u>	<u>1,463,291</u>	<u>1,404,460</u>
<b>Changes in assets and liabilities, net of effect of business acquired</b>				
Accounts receivable - trade.....		(76,585)	(45,898)	(140,331)
Due from related parties.....		595	1,464	5,813
Inventories.....		(2,583)	425	5,765
Prepaid expenses and other assets.....		362	(19,526)	71,506
Accounts payable - trade.....		(19,270)	(58,814)	(58,944)
Employee benefit obligation.....		(7,276)	(46,883)	(76,649)
Accrued liabilities.....		(46,993)	(27,104)	(23,487)
Due to related parties.....		(6,767)	(731)	(13,358)
Other liabilities and deferred income.....		(2,603)	38,433	45,100
		<u>(161,120)</u>	<u>(158,634)</u>	<u>(184,585)</u>
		<u><b>1,513,713</b></u>	<u><b>1,304,657</b></u>	<u><b>1,219,875</b></u>
<b>Cash generated from operations</b>				
<b>Cash from (used in) investing activities</b>				
Capital expenditures, including interest capitalized.....		(627,639)	(548,169)	(599,684)
Acquisitions and investments, net of cash acquired.....		(1,185,652)	(2,180)	(85,989)
Final consolidation of subsidiary.....		-	-	205
Proceeds from sale of equipment.....		24,143	36,213	17,300
Purchase of investments - short-term.....		(48,918)	(51,609)	(79,750)
Purchase of investments - long-term.....		(1,660)	(1,997)	(601)
Proceeds from sale of American call options.....		-	-	957
Proceeds from sale of investments - short-term.....		57,220	51,909	80,108
Proceeds from sale of investments - long-term.....		1,605	6,502	23,599
		<u><b>(1,780,901)</b></u>	<u><b>(509,331)</b></u>	<u><b>(643,855)</b></u>
<b>Cash used in investing activities</b>				
<b>Cash from (used in) financing activities</b>				
Principal payments on bonds.....		(348,616)	(2,180)	(22,765)
Proceeds from issuance of long-term debt and bonds.....		1,168,950	-	775,948
Principal payments on long-term debt.....		(760,543)	(568,110)	(385,330)
Changes in short-term bank borrowings.....		338,717	(6,707)	(774,644)
Purchase of treasury stock.....		(184,465)	(64,161)	-
Proceeds from sale of treasury stock.....		-	808	-
Dividends paid.....		(117,866)	(64,579)	-
		<u><b>96,177</b></u>	<u><b>(704,929)</b></u>	<u><b>(406,791)</b></u>
<b>Cash provided by (used in) financing activities</b>				
<b>Effect of exchange rate changes.....</b>		<u><b>(428)</b></u>	<u><b>(4,128)</b></u>	<u><b>5,360</b></u>
<b>Net increase (decrease) in cash and cash equivalents.....</b>		<u><b>(171,439)</b></u>	<u><b>86,269</b></u>	<u><b>174,589</b></u>
Cash and cash equivalents at beginning of period.....		288,195	201,926	27,337
Cash and cash equivalents at end of period.....		<u>116,756</u>	<u>288,195</u>	<u>201,926</u>

see accompanying notes to  
consolidated financial statements

**TELEKOM AUSTRIA AG**  
**CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY**  
(in EUR '000s, except per share information)

	Common stock		Treasury stock		Additional paid in capital	Retained earnings	Accumulated other comprehensive income (loss)	Total stockholders' equity
	Number of	Par value	Number of	at cost				
	shares		shares					
Balance January 1, 2003.....	500,000,000	1,090,500	-	-	452,498	969,626	(3,084)	2,509,540
Comprehensive income								
Net income.....						134,241		134,241
Net unrealized gains on securities, net of								
EUR (1,141) deferred income tax.....							2,214	2,214
Foreign currency translation adjustment.....							(10,690)	(10,690)
Unrealized net gain on hedging activities, net of EUR (1,646) deferred income tax.....							3,195	3,195
Total comprehensive income.....								128,960
Sale of call options, net of EUR (451) income tax.....					873			873
Balance December 31, 2003.....	500,000,000	1,090,500	-	-	453,371	1,103,867	(8,365)	2,639,373
Comprehensive income								
Net income.....						227,263		227,263
Net unrealized gains on securities, net of								
EUR (565) deferred income tax.....							1,096	1,096
Net realized loss on securities, net of								
EUR 1,368 deferred income tax.....							(2,655)	(2,655)
Foreign currency translation adjustment.....							(4,581)	(4,581)
Unrealized net gain on hedging activities, net of EUR (2,077) deferred income tax.....							4,032	4,032
Realized net gain on hedging activities, net of EUR (138) deferred income tax.....							268	268
Total comprehensive income.....								225,423
Distribution of dividend.....							(64,579)	(64,579)
Stock options granted.....					4,766			4,766
Purchase of treasury shares.....			(6,345,442)	(64,161)				(64,161)
Issue of treasury shares to employees.....			89,748	808				808
Balance December 31, 2004.....	500,000,000	1,090,500	(6,255,694)	(63,353)	458,137	1,266,551	(10,205)	2,741,630
Comprehensive income								
Net income.....						417,146		417,146
Net unrealized gains on securities, net of								
EUR (201) deferred income tax.....							602	602
Net realized loss on securities, net of								
EUR 3 deferred income tax.....							(8)	(8)
Foreign currency translation adjustment, of EUR (308) deferred income tax.....							14,097	14,097
Realized net gain on hedging activities, net of EUR (1,485) deferred income tax.....							2,846	2,846
Total comprehensive income.....								434,683
Distribution of dividend.....							(117,867)	(117,867)
Modification of Stock Option Plan.....					(4,523)			(4,523)
Purchase of treasury shares.....			(11,241,412)	(184,465)				(184,465)
Balance December 31, 2005.....	500,000,000	1,090,500	(17,497,106)	(247,818)	453,614	1,565,830	7,332	2,869,458

see accompanying notes to consolidated  
financial statements

**TELEKOM AUSTRIA AG**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**(All amounts in EUR '000s)**

**(1) THE COMPANY AND SIGNIFICANT ACCOUNTING POLICIES**

**Description of business, organization and relationship with the Federal Republic of Austria**

Telekom Austria AG and its subsidiaries (the "Company" or "Telekom Austria") is engaged as a full service telecommunications provider of long distance, local and wireless services, corporate data communications services as well as internet services. The Company also provides services through pay phones and supplies telephones and technical equipment for telephone communications. These activities are conducted and operated primarily in Austria as well as in other countries of central and south-east Europe.

The Company's activities in mobile communications are performed through mobilkom austria AG & Co KG and mobilkom austria AG ("mobilkom austria") as well as through Mobiltel EAD ("Mobiltel"). mobilkom austria, together with its subsidiaries, operates mobile telecommunications networks and provides ancillary services in Austria, Croatia, Slovenia and Liechtenstein. Mobiltel operates a mobile telecommunications network and provides ancillary services in Bulgaria. The operations include wireless internet access.

The Company's activities in fixed line services are performed mainly through Telekom Austria AG and are carried out in Austria.

Telecom Italia owned 29.78% of Telekom Austria until its sale of 75,000,000 shares on November 4, 2002 in a private placement, thereby reducing its level of ownership to 14.78% as of December 31 2003. On January 21, 2004 Telecom Italia sold all of its residual shareholding of 73.9 million shares or 14.78%.

The Federal Republic of Austria, through Österreichische Industrie-Holding AG ("ÖIAG"), is a significant shareholder of the Company. In December 2004, ÖIAG sold 85 million shares of the Company in a private placement to institutional shareholders and reduced its holding from 47.17% to approximately 30.17% of voting common shares. In addition to the related party transactions described in note (6), the Federal Republic of Austria authorizes and supervises the Rundfunk und Telekom Regulierungs – GmbH ("RTR"), which regulates certain activities of the Company. The government holds the taxing authority for the Austrian operations of Telekom Austria and imposes taxes such as income and value added taxes on the Company.

**Basis of presentation**

The consolidated financial statements of Telekom Austria have been prepared in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP").

The Company has reclassified certain amounts in prior year financial statements to conform with the current year's presentation.

**TELEKOM AUSTRIA AG**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(All amounts in EUR '000s)**

In September 2003, the Austrian Supreme Court ruled that no contractual relationship exists between value-added service providers (VASP) and the Company, with the contractual relationship being established directly between the VASP and the customers. The Company is no longer considered the primary obligor and ceased reporting revenues on a gross basis as of October 1, 2003. Had the ruling been in effect for all of 2003, revenues and expenses in the accompanying consolidated statements of operations would have been lower by EUR 45,886. Had the enacted regulation and the VASP ruling been in effect for all of 2003, revenues and expenses would have been adjusted as follows:

	<b>Year ended December 31,</b>	
	<b>2003</b>	<b>2003</b>
	<b>pro-forma</b>	<b>as reported</b>
Revenues.....	3,923,864	3,969,750
Operating expenses.....	(3,554,040)	(3,599,926)
Operating income.....	369,824	369,824

**Principles of consolidation**

The consolidated financial statements include the accounts of Telekom Austria AG and all of its' subsidiaries. All intercompany transactions and balances have been eliminated in consolidation.

Investments in companies in which the Company has a significant influence, but less than a controlling financial interest, are accounted for using the equity method. Under the equity method, only the Company's investments in and net amounts due to and due from the equity investee are included in the consolidated balance sheet. The Company's share of the investee's earnings is included in the consolidated operating results and only dividends, cash distributions, loans or other cash received from or paid to the investee are included in the consolidated cash flows.

**Cash and cash equivalents**

The Company considers cash in banks and highly liquid investments with original maturities of three months or less to be cash and cash equivalents. Money market deposits with original maturities of more than three months are classified as short-term investments along with marketable securities.

**Marketable securities**

Marketable debt and equity securities, other than investments accounted for by the equity method, are classified as either available-for-sale or held-to-maturity. Securities classified as available-for-sale are reported at fair value at the balance sheet date and held-to-maturity securities are reported at amortized cost. Unrealized gains and losses on available-for-sale securities are included in accumulated other comprehensive income, net of applicable deferred tax.

**Inventories**

Inventories consist of merchandise sold in retail shops and material and spare parts used for the construction of networks, mainly for the Company's own use. Inventories are valued at the lower of cost or market, cost being determined on the basis of weighted average cost.

**TELEKOM AUSTRIA AG**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(All amounts in EUR '000s)**

**Property, plant and equipment**

Property, plant and equipment are stated at cost, which includes certain costs that are capitalized during the installation and expansion of the telecommunications network including material, payroll, direct overhead and interest costs as well as the present value of estimated asset retirement obligations. Value added tax ("VAT"), which is charged by suppliers and refunded by the tax authorities, is not included in cost. Plant and equipment under capital leases are stated at the lower of the present value of minimum lease payments or fair value.

Depreciation on plant and equipment is calculated using the straight-line method and the estimated useful lives of the assets. Plant and equipment under capital leases and leasehold improvements are amortized using the straight-line method over the lease term or the estimated useful life of the asset, whichever is shorter.

The useful lives are:

	<b>Years</b>
Transmission equipment	3 – 20
Cables and wires	10 – 20
Communications equipment	4 – 10
Software	3 – 8
Furniture, fixtures and other	3 – 10
Buildings and leasehold improvements	10 – 50

Maintenance and repairs are expensed as incurred while replacements and improvements are capitalized. The cost and accumulated depreciation of assets sold or retired are removed from the accounts, and any resulting gain or loss is reflected in other operating expenses.

**Goodwill and other intangible assets**

Goodwill and other intangible assets with indefinite useful lives are tested for impairment in accordance with Statement of Financial Accounting Standards (SFAS) No. 142, *Goodwill and Other Intangible Assets*, at least annually, but also on an interim basis if an event or circumstance indicates that an asset may be impaired. Other intangible assets with estimable useful lives are amortized over their respective useful lives to their estimated residual values and reviewed for impairment in accordance with SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*.

The goodwill impairment test is a two-step evaluation. The first step requires the Company to compare the fair value and carrying value of any reporting unit to which goodwill has been allocated. If the fair value of the reporting unit is less than its carrying value, an indication of goodwill impairment exists and the second step of the impairment test must be performed. In the second step, the implied fair value of goodwill, determined by allocating the aggregate fair value of the reporting unit to all identifiable tangible and intangible assets, is compared to its carrying amount. Any shortfall in fair value of goodwill compared to carrying value is recognized as an impairment loss.

In each reporting period, the Company is required to reevaluate its decision that a nonamortizable intangible asset has an indefinite useful life. If a nonamortizable intangible asset is subsequently determined to have a finite useful life, the intangible asset is written down to the lower of its fair value or carrying amount and amortized prospectively based on its remaining useful life. The impairment test is a comparison of the fair value of the intangible asset with its carrying value. Any excess of carrying value over fair value is recognized as an impairment loss.

**TELEKOM AUSTRIA AG**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(All amounts in EUR '000s)**

Amortizable intangible assets are stated at cost and are amortized using the straight-line method over their estimated useful lives, as shown below:

	<u>Years</u>
Wireless and wireline licenses .....	10 – 15
Patents and proprietary rights.....	4 – 20
Subscriber base.....	6 – 7
Other.....	10 – 30

**Impairment of long-lived assets and long-lived assets to be disposed of**

Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. The recoverability of assets to be held and used is measured by comparing the carrying amount of the asset to the undiscounted future net cash flows expected to be generated by the asset. If the carrying value of such assets exceeds the undiscounted cash flows, an impairment will be recognized. The amount of the impairment to be recognized is measured as the amount by which the carrying amount of the assets exceeds the fair value of the assets. Long-lived assets or disposal groups to be sold are classified as held for sale if all the criteria for reclassification in accordance with SFAS 144 are met and are reported at the lower of the carrying amount or estimated proceeds less cost to sell.

**Internally developed software**

Certain direct and indirect development costs associated with internally developed software, including direct costs of materials and services, and payroll costs for employees devoting time to the software projects, are capitalized once the project has reached the application development stage. The costs are amortized using the straight-line method over a period not exceeding four years, beginning when the asset is substantially ready for use. Costs incurred during the preliminary project stage, maintenance and training costs and research and development costs are expensed as incurred.

**Advertising and promotional costs**

Advertising and promotional costs are expensed as incurred and totaled EUR 229,580, EUR 198,138 and EUR 198,362 for the years ended December 31, 2005, 2004 and 2003, respectively.

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**Research and development costs**

Research and development costs are expensed as incurred and totaled EUR 43,031, EUR 42,387 and EUR 42,759 for the years ended December 31, 2005, 2004 and 2003, respectively, and are classified in the consolidated statement of operations according to the nature of the expense.

**Income taxes**

Income taxes are accounted for using the liability method. Deferred tax assets and liabilities are recognized for future tax consequences attributable to differences between the financial statement carrying amount of an existing asset or liability and its respective tax basis, operating losses and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which these temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of changes in tax rates is recognized as income or expense in the period of the enactment date.

Investment tax credits are recognized as a reduction of income taxes in the period in which those credits are granted.

Deferred income taxes on investments in pass-through enterprises are provided on the excess of the financial statement carrying amount of the investment, including the goodwill within the pass-through enterprise, over the tax basis of the investment.

The Company recognizes deferred tax liabilities or assets for differences between the assigned values and the tax basis of assets and liabilities recognized in a business combination. If a valuation allowance is recorded on a deferred tax asset for an acquired entity's deductible temporary differences or operating loss or tax credit carryforwards at the acquisition date, the tax benefits recognized in subsequent years due to a reassessment of that valuation allowance are applied (i) first to reduce to zero any goodwill related to the acquisition, (ii) second to reduce to zero other non-current intangible assets related to the acquisition, and (iii) third to reduce income tax expense.

**Earnings per share**

Basic earnings per share are computed by dividing consolidated net income by the weighted average number of common shares outstanding for the year.

Diluted earnings per share are calculated by dividing net income by the weighted average number of common shares outstanding for the year, adjusted by the effect of the options granted under the stock option plans.

In order to have access to shares for employee compensation purposes for the Stock option plan 2000, the Company purchased an American call option. As the American call option was written on already issued and outstanding shares, the number of potential shares outstanding was not affected by the American call option and all of these shares were already included in basic EPS. Accordingly, the call option and employee options did not have a dilutive effect.

Employee stock options under the Stock option plan 2004 were treated as potential common shares in computing diluted earnings per share under the treasury stock method in accordance with SFAS No. 128, *Earnings per Share*, as of December 31, 2004. In the year ended December 31, 2005, the Company modified the exercise terms of the Stock option plan and decided to settle the options in cash only. Accordingly, the Company adjusted the accounting for the employee stock options and recognized a liability. Therefore, the Company reported no dilutive effect of the Stock option plan as of December 31, 2005.

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**Treasury stock**

The Company accounts for the treasury stock in accordance with the cost method with acquisitions being recorded at cost and the total cost being shown in the balance sheet as a reduction of stockholders' equity.

**Asset retirement obligation**

The Company accounts for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs in accordance with SFAS No. 143, *Accounting for Asset Retirement Obligations*. The Company records the fair value of an asset retirement obligation as a liability in the period in which the legal obligation associated with the retirement of a tangible long-lived asset is incurred. An amount equal to the initial obligation is recorded as an increase to the carrying amount of the related long-lived asset and depreciated over the remaining useful life of the asset. The liability is adjusted at the end of each period to reflect the passage of time and changes in the estimated future cash flows underlying the initial fair value measurement.

**Employee benefit obligations**

The Company provides retirement benefits under both defined contribution and defined benefit plans.

In the case of defined contribution plans the Company pays contributions to publicly or privately administered pension insurance plans on a mandatory or contractual basis. Once the contributions have been paid, the Company has no further payment obligations. The regular contributions constitute net periodic costs for the year in which they are incurred.

All other retirement benefit plans are unfunded defined benefit plans for which the Company records accruals. The pension provisions are calculated using the projected unit credit method in accordance with SFAS No. 87, *Employers' Accounting for Pensions*. The future benefit obligations are valued using actuarial methods on the basis of an appropriate assessment of the discount rate, rate of compensation increase and rate of increase of pensions.

**Concentration of risks**

A portion of the Company's revenue is derived from services provided to other companies in the telecommunications industry, mainly to alternative telecommunications and cellular companies as well as internet online services. As a result, the Company has some concentration of credit risk in its customer base. The Company performs ongoing credit evaluations of the financial condition of its' large customers to support its receivables. As of the balance sheet dates, the Company does not have any significant concentrations of business transacted with a particular supplier or lender that could, if suddenly eliminated, severely impact operations. The Company also does not have a concentration of available sources of labor, services, franchises, or licenses or other rights that could, if suddenly eliminated, severely impact operations. The Company invests its cash with several high-quality credit institutions.

As a result of its expansion into the CEE-region Telekom Austria is operating in markets that have been experiencing political and economic change that has affected, and may continue to affect, the activities of enterprises operating within this environment. Consequently, operations in the CEE-region involve uncertainties, including tax uncertainties, that typically do not exist in other markets. The accompanying consolidated financial statements

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reflect management's assessment of the impact of the CEE business environment on the operations and the financial position of the Group. The future business environment may differ from management's assessment.

**Foreign currency translation**

The reporting currency of the Company is the Euro.

Foreign currency receivables and liabilities are recognized at the exchange rate applicable on the transaction date and retranslated periodically at the then applicable ruling balance sheet rate. Unrealized foreign exchange losses and gains due to exchange rate fluctuations are recognized in the statement of operations.

The functional currency for the Company's foreign operations is the applicable local currency. Assets and liabilities are translated using the current exchange rate in effect at the balance sheet date. Revenues and expenses are translated using the weighted average exchange rate during the period. Resulting translation adjustments are recorded as other comprehensive income or loss.

The following table provides the exchange rates for the currencies in which the Company conducts most of its transactions:

	<b>Balance sheet rates at</b>		<b>Average exchange rates for the</b>		
	<b>December 31</b>		<b>period ended December 31</b>		
	<b>2005</b>	<b>2004</b>	<b>2005</b>	<b>2004</b>	<b>2003</b>
Bulgarian Lev (BGN)	1.9563	1.9559	1.9558	1.9530	1.9490
Croatian Kuna (HRK) .....	7.3715	7.6712	7.4038	7.4943	7.5621
Czech Crown (CZK) .....	29.0000	30.4640	29.7803	31.9062	31.8409
Hungarian Forint (HUF) .....	252.8700	245.9700	247.9480	251.6906	253.0343
Japanese Yen (JPY) .....	138.9000	139.6500	136.8544	134.3904	130.8971
Slovak Crown (SKK) .....	37.8800	38.7450	38.5928	40.0270	41.4919
Slovenian Tolar (SIT) .....	239.5000	239.7600	239.5698	239.0826	233.8404
Swiss Franc (CHF) .....	1.5551	1.5429	1.5484	1.5442	1.5204
US Dollar (USD) .....	1.1797	1.3621	1.2446	1.2432	1.1299

**Revenue recognition**

**Wireline**

The Company generates revenues from fixed line services to individuals, to commercial and non-commercial organizations and to other national and foreign carriers. Fixed line services include access fees, domestic and long distance services, including internet, fixed to mobile calls, international traffic, voice value-added services, interconnection, call center services and public payphone services.

The Company recognizes long distance and local service revenue based upon minutes of traffic processed or contracted fee schedules when the services are rendered. Revenues due from other national and foreign carriers for incoming calls from outside the company's network are recognized in the period the call occurs.

Access fees, monthly base fees and lines leased to commercial customers are billed in advance resulting in deferred revenues. These fees are amortized over the period in which the service is provided. Cash discounts and incentives are accounted for as reductions in revenues when granted.

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Product and other service revenues are recognized when the products are delivered and accepted by customers or when services are provided in accordance with contract terms.

The installation of customer lines in residences is a separate service and the Company provides this installation service in situations where it is not providing other services. Revenue on such installation work is recognized when the installation work is completed.

The Company has entered into a limited number of agreements with other telecommunications operators outside of Austria whereby the Company grants some pre-defined access to existing capacity on its physical network in return for similar access to the physical network of the counter party. In accordance with APB No. 29, "Accounting for Nonmonetary Transactions", EITF 01-2, "Interpretation of APB Opinion No. 29", and EITF 99-17, "Accounting for Advertising Barter Transactions", no revenues and obligations (expenses) were recognized because the exchange does not result in the culmination of an earnings process due to the similarity of the assets exchanged. In addition, no gain or loss was recognized, as fair value was not considered to be determinable within reasonable limits. The Company, however, does recognize trade revenues arising from subscriber transactions under normal tariff plans. The benefits and costs of such swap agreements are reflected in the Company's results of operations in the periods in which they are realized through reduced interconnection obligations and revenues, respectively.

**Wireless**

The Company provides mobile communications services to individuals and commercial and non-commercial organizations through mobilkom austria. mobilkom austria generates revenue primarily by providing digital wireless services as well as value-added services, text and multimedia messaging, m-commerce and information services. To a lesser extent, mobilkom austria generates revenue from the sale of wireless handsets.

The Company recognizes mobile usage and roaming service revenue based upon minutes of traffic processed or contracted fee schedules when the services are rendered. Revenues due from foreign carriers for international roaming calls are included in revenues in the period in which the call occurs.

Certain prepaid usage services in the wireless segment are billed in advance and result in deferred revenues. These fees are amortized over the period in which the service is provided. Discounts and incentives are accounted for as a reduction in revenues when granted.

Revenue and related expenses associated with the sale of wireless handsets to distributors are recognized when the products are delivered and accepted, as such sales transactions are separate and distinct from the sale of wireless services to customers.

The Company also enters into multiple element arrangements which include the sale of handsets, activation fees and service contracts to customers through Company owned retail stores. These transactions include the sale of a mobile handset at a price significantly below acquisition cost (subject to a binding contract being signed), the up-front charge of non-refundable activation fees to connect the customer to the service, and the subsequent monthly fees and airtime fees charged during the contract period. The Company recognizes revenue from the sale of handsets upon delivery to the customer. The corresponding cost of sales is charged to expense when sales are recognized which results in a net loss on the sale of the handset. Activation fees charged to the customer are recognized as revenue and the related cost is expensed upon delivery and sale of the phone. Current monthly service fees are recorded as revenue from the point where the service is performed.

Other service revenues are recognized when delivered and accepted by customers and when services are provided in accordance with contract terms.

Customer acquisition costs consist primarily of commissions paid to dealers that sell wireless services to customers. Such costs are expensed ratably over the contract period as marketing expense.

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**Allowance for doubtful accounts**

The Company estimates the portion of its outstanding receivables that are uncollectible based on aging schedules. Based on historical experience, uncollectibility is estimated as an increasing percentage of each aging category. Additionally, the Company records an allowance for specific customers if circumstances indicate non-collectibility.

The estimated allowance for doubtful accounts relating to receivables sold and cash drawn under the securitizations described in note (5) are recorded as accrued liabilities. Trade accounts receivable and uncollectible loans are charged off as soon as the uncollectibility is assured.

**Stock compensation**

Until the year ended December 31, 2003, the Company accounted for stock-based employee compensation in accordance with the intrinsic value method prescribed by Accounting Principles Board Opinion (APB) No. 25, *Accounting for Stock Issued to Employees*. Specifically, the Company accounted for its combination stock option and stock appreciation rights plan under the Stock option plan 2000 (see note (20)) in accordance with the provisions of Financial Accounting Standards Board (“FASB”) Interpretation No. 28, *Accounting for Stock Appreciation Rights and Other Variable Stock Option or Award Plans*, which requires that the plan be accounted for as a stock appreciation right. The Company recognized a liability and a pro rata compensation expense in the first period in which it was probable that the target stock price criteria outlined in the plan would be met. Based on historical trends of the stock and relevant market conditions, no compensation expense has been recognized under the plan in 2003.

Effective January 1, 2004, the Company adopted SFAS No. 123, *Accounting for Stock-Based Compensation*. Because the combination stock option and stock appreciation rights plan at January 1, 2004 permitted employees to call for settlement in cash, the accounting for this plan under SFAS No. 123 was the same as in prior years under APB 25. Therefore, there was no effect of a change in accounting principle in 2004.

In 2004, the Company launched the Stock Option Plan 2004 (see note (20)), which was classified as equity awards in accordance with SFAS 123 as the Company’s management had the intention to settle the options in shares. The compensation cost was measured based on the fair value of the stock options at the grant date and recognized over the service period for the year ended December 31, 2004.

In 2005, the Company adopted the revised SFAS 123 (SFAS 123R) using the modified prospective application. As the Stock Option Plan 2004 was measured based on the fair value, there was no effect of change in accounting principle.

In March 2005, the Company modified the exercise term of the first tranche of the Stock Option Plan 2004 and elected to settle the options in cash only. As a result, amounts originally recorded in additional paid in capital were reclassified to liabilities. The liability is remeasured at fair value at each reporting date until the date of settlement. Compensation cost is based on the change in the fair value of the liability award, or a portion of the change, depending on the percentage of the requisite service that has been rendered at the reporting date.

**Derivative financial instruments**

All derivative instruments, such as interest rate swap contracts and foreign-currency exchange contracts, are recognized in the financial statements and measured at fair value regardless of the purpose or intent for holding them. Changes in the fair value of derivative financial instruments are recognized periodically either in income or

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stockholders' equity (as a component of accumulated other comprehensive income), depending on whether the derivative is being used to hedge changes in fair value or cash flows. For derivatives designated as fair value hedges, changes in the fair value of the hedged item and the derivative are recognized in earnings. For derivatives designated as cash flow hedges, fair value changes of the effective portion of the hedging instruments are recognized in accumulated other comprehensive income in the statements of changes in stockholders' equity until the hedged item is recognized in earnings. The ineffective portion of the value changes are recognized in earnings immediately. SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*, also requires that certain derivative instruments embedded in host contracts be accounted for separately as derivatives.

The Company has entered into various foreign currency forward contracts, which are accounted for as free standing derivatives. These forward contracts serve as economic hedges of the Company's operating exposure to fluctuations in foreign currencies. Changes in the fair values of such forward contracts are recorded directly in income.

**Fair value of financial instruments**

The carrying amounts of cash, accounts receivable, accounts receivable sold, accounts payable, receivables due from and payables due to related parties and accrued liabilities approximate their fair value. The fair values of securities held-to-maturity and securities available-for-sale are based on quoted market rates. The fair value of long-term debt and swap agreements is determined based on the cash flows from such financial instruments discounted at the Company's estimated current interest rate to enter into similar financial instruments.

For some investments, mainly in unconsolidated subsidiaries and equity investments, for which there are no quoted market prices ("Cost method investments"), the Company estimates the fair value to be the carrying value based on the audited financial statements, if available. Those investments are tested for impairment if losses are generated over an extended period or if the business environment changes materially.

**Use of estimates**

The preparation of financial statements in conformity with U.S. GAAP requires the use of estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from these estimates.

**New accounting pronouncements**

In March 2005, the FASB issued FIN No. 47, *Accounting for Conditional Asset Retirement Obligations—an interpretation of FASB Statement No. 143*. FIN 47 clarifies that the term conditional asset retirement obligation as used in FASB No. 143, *Accounting for Asset Retirement Obligations*, refers to legal obligations to perform an asset retirement activity in which the timing and (or) method of settlement are conditional on a future event that may or may not be within the control of the entity. This interpretation also clarified when an entity would have sufficient information to reasonably estimate the fair value of an asset retirement obligation. The provisions of FIN 47 shall be effective no later than at the end of the fiscal years ending after December 15, 2005. The Company does not expect that the adoption of FIN No. 47 will have a material impact on its consolidated financial statements.

In May 2005, the FASB issued SFAS No. 154, *Accounting Changes and Error Corrections*, which replaces APB No. 20, *Accounting Changes* and FASB No.3, *Reporting Accounting Changes in Interim Financial Statements*. Statement No. 154 requires retrospective application of changes in accounting principle to prior periods' financial statements, unless it is impracticable to determine either the period-specific effects or the cumulative effect of the

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change. The provisions of SFAS No. 154 shall be effective for the accounting changes and correction of errors made in fiscal years beginning after December 15, 2005. The Company does not expect that the adoption of SFAS No. 154 will have a material impact on the Company's consolidated financial statements.

**International Financial Reporting Standards**

In July 2002, the European Parliament adopted a regulation requiring all European Union (EU) companies to prepare their financial statements in conformity with International Financial Reporting Standards (IFRS) if their securities are traded on a regulated market within the EU. The regulation shall be applied as of the first period that begins on or after January 1, 2005. However, Member States may defer mandatory application until the first period that begins on or after January 1, 2007 for companies that already use other internationally accepted standards and that are publicly traded outside of the EU. This transitional clause applies to the Company as it is listed on the New York Stock Exchange and prepares its financial statements in accordance with US GAAP. Accordingly, the Company is not required to prepare financial statements in accordance with IFRS until the fiscal year beginning on January 1, 2007. However, the Company plans to prepare financial statements in accordance with IFRS on a voluntary basis starting for the fiscal year ending December 31, 2005.

**(2) BUSINESS COMBINATIONS**

All acquisitions have been accounted for under the purchase method, with the excess of the purchase price over the estimated fair value of the net assets acquired accounted for as goodwill. The results of operations of the acquired businesses are included in the consolidated financial statements from the dates of the acquisition.

As of June 1, 2005, the Company exercised the option and acquired 100% of Mobiltel on July 12, 2005. Consequently, the Company includes the results of operations of Mobiltel in the Company's consolidated financial statements starting from July 12, 2005. The aggregate purchase price amounted to EUR 1,214,268, including the direct costs of acquisition of EUR 7,155, option price of EUR 80,000 and a deferred consideration of EUR 181,871 that was paid in December 2005. As a result of the acquisition the Company gained a strong strategic and operating position in the Bulgarian telecommunication market.

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In November 2005, Mobiltel merged with its parent company, TAG-Tel EAD. As a result of this transaction, the majority of the accounting basis of the net assets acquired also became the new basis for tax purposes. Goodwill of EUR 565,963 is expected to be fully tax deductible. The following table summarizes the estimated fair values of the assets acquired and liabilities assumed:

Current assets .....	110,974
Tangible assets .....	274,031
Intangible assets .....	870,740
Deferred tax asset from acquisition.....	7,003
Goodwill .....	565,963
Current liabilities.....	(376,609)
Long-term liabilities .....	(237,834)
Net assets acquired.....	<u>1,214,268</u>

Mobiltel is reported in the wireless segment.

The estimated fair values, by class of the intangible assets, were as follows:

Wireless operating licenses .....	98,989
Subscriber base .....	508,682
Brand name .....	262,991
Other .....	78
Total intangible assets acquired .....	<u>870,740</u>

The brand name is classified as an intangible asset with an indefinite useful life and therefore is not subject to amortization, but is tested for impairment annually. Intangible assets recognized relating to wireless operating licenses and the subscriber base are amortized over their weighted average useful life of 10.7 and 7 years, respectively. The remaining intangible assets are subject to amortization.

The pro forma consolidated revenues, net income and earnings per share for the years ended December 31, 2005 and 2004, calculated as if Mobiltel had been acquired at the beginning of 2005 and 2004, respectively, are estimated to be:

	<u>2005</u>	<u>2004</u>
Revenues .....	4,639,271	4,530,543
Net income .....	479,696	318,756
Weighted average number of dilutive shares outstanding .....	489,050,517	496,524,827
Basic and fully diluted earnings per share .....	Euro 0.98	Euro 0.64

The pro forma results include amortization of intangible assets presented above, depreciation on fair value adjustments on property plant and equipment, the interest expense on debt assumed to finance the acquisition and income taxes as well as other adjustments including amortization on fair value adjustments to long term debts. The pro forma results of operations are not necessarily indicative of what actually would have occurred if the acquisition

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had been completed as of the beginning of each period presented, nor are they necessarily indicative of future consolidated results.

On December 31, 2004, mobilkom austria acquired the remaining 1% of VIPnet d.o.o., Zagreb, (VIPnet) for a total purchase price of EUR 1,658, thus bringing its interest to 100%.

**(3) INVESTMENTS IN AFFILIATES**

As of December 31, 2005 and 2004, the investments in affiliates included a 26.00% interest in Omnimedia Werbegesellschaft mbH ("Omnimedia") and a 25.10% interest in Output Service GmbH ("OSG").

In July 2003 the Company sold its 26.00% interest in Herold Business Data AG, the leading telephone directory provider in Austria, to PASR Vierte Beteiligungsverwaltung GmbH for EUR 22,000 and realized a gain of EUR 18,367 which was recorded in equity in earnings of affiliates.

The following table shows the roll forward of investments in affiliates:

	<b>2005</b>	<b>2004</b>
Carrying amount, January 1 .....	3,570	3,555
Changes in equity.....	72	15
Carrying amount, December 31 .....	<u>3,642</u>	<u>3,570</u>

A summary of aggregate financial information as reported by equity investees is as follows:

<b>Year ended December 31,</b>	<b>2005</b>	<b>2004</b>	<b>2003</b>
Revenues .....	6,308	6,506	35,515
Operating income.....	3,482	3,466	4,653
Net income .....	2,186	2,117	2,908
<b>At December 31,</b>	<b>2005</b>	<b>2004</b>	
Total current assets .....	39,018	31,068	
Total assets.....	39,501	31,566	
Current liabilities .....	36,167	28,590	
Long-term debt.....	1,480	1,401	
Total liabilities .....	37,647	29,991	
Total stockholders' equity .....	1,854	1,575	

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**(4) MARKETABLE SECURITIES**

Marketable securities are included in short-term investment and other investments in the balance sheet.

Debt securities originating from cross border lease transactions entered into in 1998 and 1999 (see note (17)) are classified as held-to-maturity as the Company is contractually obligated to hold these securities until maturity. The securities are bonds of triple A rated issuers and are held by a custodian. Through a further asset based swap the cash inflows from the securities are transformed into the cash flow stream required to match a specified portion of the lease payments. The securities are pledged to a counterparty in the swap agreement. No sales of securities held-to-maturity occurred in 2005, 2004 and 2003. The interest rates on the securities are fixed and range from 5.65% to 9.01%. Accrued interest is recorded as interest income. The securities will mature between 2006 and 2011.

	<b>Amortized cost</b>	<b>Gross unrealized holding gains</b>	<b>Gross unrealized holding losses</b>	<b>Fair value</b>
<b>At December 31, 2005</b>				
<i>Non-current assets</i>				
Available-for-sale				
debt securities .....	5,363	104	27	5,440
equity securities .....	119	-	1	118
mutual funds .....	10,472	442	24	10,890
Held-to-maturity .....	145,796	8,412	-	154,208
<b>At December 31, 2004</b>				
<i>Non-current assets</i>				
Available-for-sale				
debt securities .....	4,955	176	4	5,127
equity securities .....	1,658	-	-	1,658
mutual funds .....	13,342	1	472	12,871
Held-to-maturity .....	120,946	12,919	-	133,865

The contractual maturities of debt securities classified as held-to-maturity at December 31, 2005 were as follows:

	<b>Amortized cost</b>	<b>Fair value</b>
Held-to-maturity		
Due within one year.....	6,091	6,091
Due after one year through five years .....	110,714	115,949
Due after five years through ten years.....	28,991	32,168
	<u>145,796</u>	<u>154,208</u>

Proceeds from sales of available-for-sale securities amounted to EUR 6,262, EUR 8,740 and EUR 545 in 2005, 2004 and 2003, respectively. Gross realized gains from sales of available-for-sale securities were EUR 3,123, EUR 2,124 and 323 in 2005, 2004, and 2003 respectively, while gross realized losses from sales of available-for-sale securities were EUR 0, EUR 3 and EUR 0 in 2005, 2004 and 2003, respectively. The specific identification method was used to determine the cost in computing realized gains and losses.

The unrealized losses on the investment in mutual funds, corporate bonds and equity securities were caused by fluctuations in the capital markets. The Company considers the fluctuation of the fair value of these investments

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to be temporary and therefore did not record an impairment. Presented below is the fair value information for marketable securities held by the Company:

	Less than 12 months		12 months or longer		Total	
	Fair value	Gross unrealized holding losses	Fair value	Gross unrealized holding losses	Fair value	Gross unrealized holding losses
<b>At December 31, 2005</b>						
<i>Non-current assets</i>						
Available-for-sale						
debt corporate						
securities.....	1,838	27	-	-	1,838	27
equity securities.....	117	2	-	-	117	2
mutual funds.....	-	-	4,948	23	4,948	23
<hr/>						
Total temporarily impaired securities	1,955	29	4,948	23	6,903	52

**(5) ACCOUNTS RECEIVABLE - TRADE**

The roll-forward of the allowance for accounts receivable-trade and accounts receivable sold is as follows:

	2005	2004
Allowance beginning of the year .....	94,613	92,238
Foreign currency adjustment.....	24	31
Addition from acquisition of Mobiltel	27,763	-
Charged to expenses .....	43,393	24,707
Amounts written-off.....	(21,739)	(22,363)
Allowance at the end of the year.....	144,054	94,613
of which allowance for accounts receivable-trade.....	104,234	73,463
of which for accounts receivable sold.....	39,820	21,150

	December 31, 2005	December 31, 2004
Accounts receivable-trade, gross .....	557,112	482,283
Allowance for accounts receivable-trade .....	(104,234)	(73,463)
Accounts receivable-trade, net.....	452,878	408,820
Accounts receivable sold, gross.....	268,099	194,500
Allowance for accounts receivable sold.....	(39,820)	(21,150)
Accounts receivable sold, net .....	228,279	173,350
Accounts receivable, net .....	681,157	582,170

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Of accounts receivable trade, EUR 253,933 are held for sale under the securitization program described in the following paragraphs.

In January 2002, the Company entered into a revolving securitization program and sold trade receivables to a Qualifying Special Purpose Entity (QSPE) unrelated to the Company. The Company retains servicing responsibilities relating to the sold receivables. Solely for the purpose of credit enhancement from the perspective of the QSPE, the Company retains interests in the sold receivables (retained interests). These retained interests are initially measured at estimated fair values, which the Company believes approximate historical carrying values, and are subsequently measured based on a periodic evaluation of collections and delinquencies.

The Company determined that the transaction met the three sales criteria, that (a) the transferred assets have been isolated from the transferor, beyond the reach of the transferor and its creditors, even in the event of bankruptcy or receivership, (b) the transferee obtains the right, free of any conditions that constrain, to pledge or exchange the assets and (c) the transferor does not maintain effective control in accordance with SFAS No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishment of Liabilities". Additionally, the QSPE, a limited liability corporation whose shares are owned by a charitable trust fulfilled all conditions required to be a qualifying special purpose entity under SFAS No. 140.

In December 2003 the asset-backed securitization program was extended, the discounts required were reduced and the maximum program limit was increased from EUR 290,000 to EUR 350,000.

At December 31, 2005 and 2004, the Company recorded a receivable due from the QSPE of EUR 228,279 and EUR 173,350, respectively. This amount represents accounts receivable sold, net of allowance for doubtful accounts, for which the Company had not required cash settlement from QSPE.

The Company routinely evaluates its portfolio of trade receivables for risk of non-collection and records an allowance for doubtful accounts to reflect the carrying value of its trade receivables at the estimated net realizable value. Pursuant to the provisions of the revolving-period securitizations, the Company effectively bears the risk of potential delinquency or default associated with trade receivables sold or interests retained. Accordingly, in the normal course of servicing the assets sold, the Company evaluates potential collection losses and delinquencies and updates the estimated fair value of the Company's retained interest.

The allowance recorded for sold receivables, for which the company received cash settlement as of December 31, 2005, is classified as accrued liabilities. As of December 31, 2005 and 2004, respectively, the accruals totaled EUR 4,570 and EUR 19,097.

In accordance with SFAS No. 140, the Company has not recorded a servicing asset or liability as management has determined that it is not practicable to determine a fair value for the servicing.

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In the years ended December 31, 2005 and 2004, respectively, the following cash flows were received from and paid to the QSPE:

	<b>December 31,</b>	
	<b>2005</b>	<b>2004</b>
Gross trade receivables sold to QSPE.....	3,044,009	2,861,686
Collections made on behalf of and paid to the QSPE. ....	(3,105,085)	(2,806,644)
Deferred purchase price withheld. ....	1,644	(9,771)
Unearned discount (withheld) reduced. ....	(111)	(1,489)
Liquidity and program fees. ....	(2,335)	(3,110)
Retained interests. ....	9,142	(9,142)
Increase in receivable from the QSPE. ....	(73,599)	(49,140)
Net cash received from (paid to) QSPE during the period.....	(126,335)	(17,610)

Cash settlement with the QSPE takes place on a monthly basis. Gross trade receivables sold represent the fair value of billed and unbilled receivables to the QSPE during the years ended December 31, 2005 and 2004, respectively. The Company services these receivables, collecting cash from receivables previously sold on behalf of the QSPE. The Company recorded discounts, liquidity and program fees related to the securitization of trade receivables of EUR 2,270 and EUR 3,107 for the years ended December 31, 2005 and 2004, respectively. These discounts and fees are included in interest expense in the statement of operations.

**(6) RELATED PARTY TRANSACTIONS**

Disclosures of the related party transactions relate to the Company's majority shareholder ÖIAG and its subsidiary Österreichische Post AG as "ÖIAG". Transactions with other government agencies and government-owned entities, for practical reasons, are not disclosed. None of the individual accounts associated with government agencies or government-owned entities is considered significant to the Company.

Österreichische Post AG and its subsidiaries ("Post"), a subsidiary of ÖIAG which provides postal services, charged the Company for different services such as postal charges, rent, repair and administration. The Company charged Post for IT support, voice telephony, technical services, rent, repair and other services. On September 17, 2003, Postbus AG, a 100% subsidiary of Österreichische Post AG, was sold to Österreichische Bundesbahnen and is therefore no longer reported as a related party.

The terms for services provided by Telekom Austria to governmental entities are generally based on standard pricing policies. However, the Company is obligated to provide voice telephone services for disadvantaged individuals at reduced tariffs for which it is entitled to appropriate compensation from the government on a contractual basis. Beginning January 1, 2001, the contract with the government specifies the reimbursement of Euro 13.81 per customer per month, which is recorded as revenue in the service period. The total reimbursement was EUR 41,298, EUR 40,303 and EUR 41,396 in 2005, 2004 and 2003, respectively.

In 2001, a partner in a law firm which provides legal services to the Company was elected to the Supervisory Board. In 2005, 2004 and 2003, respectively, the Company was charged EUR 464, EUR 640 and EUR 560 for legal services by that law firm.

Telecom Italia and the Company charged standard rates for interconnection services provided to each other.

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**(All amounts in EUR '000s)**

The Company has entered into agreements with Telecom Italia whereby the Company grants some pre-defined access to existing capacity on its physical network in return for similar access to the physical network of Telecom Italia. The Company does not recognize revenue or an obligation under such agreements apart from the trade revenue arising from subscriber transactions under normal tariff plans. The benefits and costs of such swap agreements will be reflected in the Company's results of operations in the periods in which they are realized through reduced interconnection obligations and revenues, respectively.

**(7) INVENTORIES**

Inventories consist of:

<b>At December 31,</b>	<b>2005</b>	<b>2004</b>
Spare parts, cables and supplies .....	44,297	41,167
Merchandise .....	46,616	41,943
<b>Total .....</b>	<b>90,913</b>	<b>83,110</b>

**(8) GOODWILL**

The following tables illustrate the changes in the net book value of goodwill by segment for the years ended December 31, 2005 and 2004, respectively:

	<b>Wireline</b>	<b>Wireless</b>	<b>Total</b>
Goodwill January 1, 2005 .....	32,317	564,248	596,565
Acquisitions .....	-	565,971	565,971
Impairment .....	(16,317)	-	(16,317)
Translation adjustment .....	347	2,609	2,956
<b>Goodwill December 31, 2005 .....</b>	<b>16,347</b>	<b>1,132,828</b>	<b>1,149,175</b>

	<b>Wireline</b>	<b>Wireless</b>	<b>Total</b>
Goodwill January 1, 2004 .....	31,419	566,158	597,577
Acquisitions .....	202	-	202
Impairment .....	(211)	-	(211)
Translation adjustment .....	907	(1,910)	(1,003)
<b>Goodwill December 31, 2004 .....</b>	<b>32,317</b>	<b>564,248</b>	<b>596,565</b>

In 2005, the major addition to goodwill relates to the acquisition of Mobiltel (see note (2)).

In 2005 impairment charges in the amount of EUR 15,457 were recorded for goodwill originally recorded from the acquisition of Czech On Line a.s. ("COL"). The acquisition was based on a business plan assuming the full liberalization of the Czech market, which however remained unsatisfactory despite the privatization of the former government owned telecommunication company. Moreover, a highly competitive environment developed within the alternative telecommunication market in the Czech Republic. Due to these facts the business of COL has not

**TELEKOM AUSTRIA AG**  
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developed as expected. The value of the reporting unit in 2005 was estimated using forecasted cash flows discounted using a weighted average cost of capital of 10.8%.

Further, in 2005 the Company recorded impairment charges in the amount of EUR 860 for goodwill originally recorded from the acquisition of World-Direct. The Company expects a material decrease of the profitability of the World-Direct's market as a result of decreasing demand by customers. The value of the reporting unit in 2005 was estimated using forecasted cash flows discounted using a weighted average cost of capital of 9.2%.

**(9) OTHER INTANGIBLE ASSETS**

Other intangible assets consist of:

<b>At December 31,</b>	<b>2005</b>	<b>2004</b>
Wireless and wireline licenses .....	684,405	563,080
Patents and proprietary rights .....	73,972	78,482
Brand names.....	437,894	173,948
Subscriber base .....	731,401	138,504
Other .....	31,238	35,679
Total intangibles.....	1,958,910	989,693
Less accumulated amortization .....	(526,394)	(322,356)
Net intangibles .....	<u>1,432,516</u>	<u>667,337</u>

Interest of EUR 1,251 was capitalized on the intangible assets, with the amount predominantly relating to the UMTS licenses.

Amortization expense was EUR 114,403, EUR 74,863, and EUR 68,340 for the years 2005, 2004 and 2003, respectively.

In 2005, the major additions to intangible assets relate to the acquisition of Mobiltel (see note (2)). The following table provides granted periods, total cost incurred and possible renewal periods and renewal fees for all GSM and UMTS licenses :

	<b>GSM licenses</b>	<b>UMTS licenses</b>
Granted until .....	2013 – 2015	2020 – 2024
License cost.....	429,233	246,584
Renewal of the Croatian license until year .....	2019	2044
Onetime license fee for extension of the Croatian license .....	14,244	17,907

The Company holds licenses to operate as telecommunications service provider from the Austrian, Croatian, Slovenian, and Bulgarian commissions.

With the granting of the UMTS license for Austria, the Company has incurred the obligation to provide at least 50% degree of UMTS coverage to the population. As of December 31, 2005, the Company has fulfilled this obligation.

**TELEKOM AUSTRIA AG**  
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**(All amounts in EUR '000s)**

The gross carrying amounts and accumulated amortization of intangible assets subject to amortization, by major class, are as follows:

<b>At December 31, 2005</b>	<b>Acquisition cost</b>	<b>Accumulated amortization</b>	<b>Carrying value</b>
Wireless and wireline licenses .....	684,405	(268,966)	415,439
Subscriber base .....	731,401	(198,247)	533,154
Patents, proprietary rights and others.....	105,211	(59,182)	46,029
<b>Total .....</b>	<b>1,521,017</b>	<b>(526,395)</b>	<b>994,622</b>

<b>At December 31, 2004</b>	<b>Acquisition cost</b>	<b>Accumulated amortization</b>	<b>Carrying value</b>
Wireless and wireline licenses .....	563,080	(210,172)	352,908
Subscriber base .....	138,504	(55,149)	83,355
Patents, proprietary rights and others.....	114,161	(57,035)	57,126
<b>Total .....</b>	<b>815,745</b>	<b>(322,356)</b>	<b>493,389</b>

The following table presents expected amortization expense related to amortizable intangible assets for each of the following periods:

2006 .....	152,644
2007.. .....	151,821
2008. ....	140,000
2009. ....	125,657
2010. ....	122,832
2011. ....	109,451
Thereafter.....	192,217

The actual amortization may differ from expected amortization.

The total carrying amount of intangible assets, other than goodwill, not subject to amortization is EUR 437,894 and EUR 173,948 as of December 31, 2005 and 2004, respectively, which relates entirely to brand names. The amount as of December 31, 2005 includes a brand name of EUR 262,991 which was acquired in the course of the acquisition of Mobilтел (see note (2)).

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
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**(10) PROPERTY, PLANT AND EQUIPMENT**

Property, plant and equipment transferred to the Company by the government was recorded upon transfer at cost less accumulated depreciation as of that date. Acquisitions since then have been recorded at cost.

<b>At December 31,</b>	<b>2005</b>	<b>2004</b>
Land .....	60,031	59,172
Buildings and leasehold improvements .....	738,439	689,639
Communications network and other equipment .....	9,952,016	9,506,621
Capital leases .....	8,753	8,961
Software .....	519,308	441,223
Construction in progress, network .....	207,804	158,007
	<u>11,486,351</u>	<u>10,863,623</u>
Less accumulated depreciation (other than capital leases).....	(7,704,184)	(6,968,516)
Less accumulated depreciation, capital leases .....	(7,613)	(6,416)
Property, plant and equipment, net .....	<u>3,774,554</u>	<u>3,888,691</u>

Major additions in 2005 and 2004 related to the communications network in the wireline segment and GSM and UMTS network infrastructure in the wireless segment.

Total interest capitalized along with amortization and depreciation expenses and impairment charges for the years ended December 31, 2005, 2004 and 2003 are as follows:

	<b>2005</b>	<b>2004</b>	<b>2003</b>
Interest capitalized .....	1,123	1,557	1,605
Depreciation and amortization expense .....	1,005,398	1,039,967	1,064,808
Impairment charges.....	1,071	1,123	6,825
of which			
Amortization of software .....	77,695	81,903	79,059
Amortization of leased assets.....	1,408	1,466	3,663

In 2005, the Company reduced the estimated useful lives of certain technical equipment due to the rapid development of the technological environment in 2005 in the relevant areas. The change in estimate resulted in an increase of depreciation by EUR 17,908 in the current period.

**(11) ASSETS HELD FOR SALE**

The Company classified several buildings with carrying amount of EUR 880 as held for sale as of December 31, 2005. The assets have been accounted for at the lower of the carrying amount or each asset's estimated fair value less costs to sell.

In 2005, the Company sold the Austrian UMTS license frequency band and several buildings which were classified as held for sale and recognized a profit of EUR 7,900.

The Company recognized a gain on sale of assets of EUR 7,615 and EUR 4,762 for the years ended December 31, 2005 and 2004, respectively.

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**(12) SHORT-TERM BORROWINGS**

The Company's short-term borrowings include:

<b>At December 31,</b>	<b>2005</b>	<b>2004</b>
Current portion of long-term debt.....	296,840	653,022
Short-term debt .....	357,736	-
Lines of credit .....	8,484	2,775
Cross Border Lease .....	122,227	94,154
Current portion of lease obligations.....	486	1,188
<b>Total.....</b>	<b>785,773</b>	<b>751,139</b>

The weighted-average interest rate on lines of credit was 2.30% and 2.21% in 2005 and 2004, respectively. As of December 31, 2005 the Company had unused committed credit lines of EUR 450,000 and recorded commitment and servicing fees for these unused lines of EUR 938. The credit line commitments will expire between November 2006 and December 2007.

**(13) ACCRUED LIABILITIES**

Accrued liabilities consist of the following:

<b>At December 31,</b>	<b>2005</b>	<b>2004</b>
Taxes, other than income .....	5,623	7,643
Employee benefits.....	53,256	61,830
Customer discounts.....	48,226	42,279
Customer retention programs.....	35,486	34,712
Bad debt reserve for sold receivables .....	4,570	19,097
Other .....	23,843	28,758
<b>Total.....</b>	<b>171,004</b>	<b>194,319</b>

Other accruals relate mainly to legal fees and lawsuits, audit fees, public fees and consulting services.

In establishing accruals, management assesses different scenarios of reasonably estimated outcomes in determining the amount that the Company is expected to pay upon the resolution of a contingency. The Company records the most likely of all scenarios contemplated or, if none of the scenarios is more likely to occur, the scenario with the lowest amount is considered in establishing the accrual.

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**(14) DEFERRED INCOME**

<b>At December 31,</b>	<b>2005</b>	<b>2004</b>
Unearned income .....	192,398	162,002
Unamortized gain on sale of tax benefits .....	37,349	44,331
	<u>229,747</u>	<u>206,333</u>
Less non-current portion .....	(30,237)	(37,349)
Deferred income net of non-current portion .....	<u>199,510</u>	<u>168,984</u>

The deferred income mainly relates to prepaid access fees, monthly base fees, leased lines to commercial customers, prepaid mobile fees and rental income from site sharing. These fees are amortized over the period the service is provided.

Additional information concerning the sale of tax benefits is contained in note (17).

**(15) ASSET RETIREMENT OBLIGATION**

The Company adopted SFAS No. 143, *Accounting for Asset Retirement Obligations*, as of January 1, 2003 and recorded the following additions to long-lived assets, asset retirement obligations and a cumulative change in accounting principles:

<b>At January 1,</b>	<b>2003</b>
Addition to long-lived assets .....	6,288
Addition to accumulated depreciation .....	(2,263)
Cumulative effect of change in accounting principle .....	17,929
Asset retirement obligations .....	<u>21,954</u>

The roll-forward of asset retirement obligations is as follows:

	<b>2005</b>	<b>2004</b>
Asset retirement obligations as of January 1 .....	38,261	23,262
Foreign exchange differences .....	167	(33)
Addition from acquisition of Mobilтел .....	2,502	-
Change in estimate .....	2,558	-
Liability incurred in the current period .....	2,808	11,451
Accretion expense .....	3,087	6,173
Settlements .....	(1,274)	(2,248)
Releases .....	-	(344)
Asset retirement obligations as of December 31 .....	<u>48,109</u>	<u>38,261</u>

The Company recorded asset retirement obligations for the retirement and decommissioning of base stations, buildings, booths for public payphones and wooden masts impregnated with tar or salt.

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The Company has an obligation to operate a sufficient number of booths to assure that the Austrian population has sufficient access to telecommunications services. As long as the Company stays in business and technology does not materially change, the number of booths operated will be reduced but not eliminated completely for the foreseeable future. The Company estimated the number and timing of booths to be retired from service and estimated the asset retirement obligation based on probability-weighted cash flow estimates.

The Company has also recorded an asset retirement obligation for masts impregnated with tar or salt. Although the Company stopped setting up tar-masts in 1992, some will be in operation for approximately another 30 years. Masts impregnated with salt are currently in operation and set up for the foreseeable future. The Company has recorded an asset retirement obligation based on estimated settlement dates and expected cash flows.

Additionally, the Company recorded asset retirement obligations for buildings concerning obligations for the disposal of hazardous substances.

mobikom austria and Mobiltel situate base stations on land, rooftops and other premises under various types of rental contracts. In estimating the fair value of its retirement obligation for its base stations, the Company made a range of assumptions such as retirement dates, timing and percentage of early cancellations, development of technology and the cost of removing network equipment and remediating the sites.

Additionally, mobikom austria recorded asset retirement obligations for buildings and shops under operating leases in accordance with the obligation to refurbish the sites at the expiration of the lease contracts.

**(16) LONG-TERM DEBT**

The outstanding long-term debt, other than lease obligations, are summarized as follows:

<b>At December 31,</b>	<b>Maturity</b>	<b>2005</b>	<b>2004</b>
Face value of bonds under EMTN Programme.....	2010-2017	1,750,000	750,000
Interest rate SWAP on EMTN bonds.....	2010-2013	(5,311)	11,200
Discount and issue cost of EMTN bonds.....	2010-2017	(16,654)	(7,731)
Other bonds guaranteed by the Federal Republic of Austria .....	2005	-	149,602
Bank debt .....	2006-2009	790,312	675,296
Bank debt guaranteed by the Federal Republic of Austria .....	2006-2011	297,232	707,566
Other .....	2006-2007	38,964	14,260
		<u>2,854,543</u>	<u>2,300,193</u>
Less current portion of long-term debt .....		(296,840)	(653,022)
Long-term debt, net of current portion.....		<u>2,557,703</u>	<u>1,647,171</u>

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The interest rates on the guaranteed and unguaranteed bank debt vary between 2.3% and 7.0%. The weighted average interest rate for the years ended December 31, 2005 and 2004, respectively, was 4.32% and 5.0% for bonds and 4.5% and 4.9% for bank debt.

The year-end average interest rates for the long-term debt excluding interest rate swap agreements for 2005 and 2004 are as follows:

	<b>2005</b>	<b>2004</b>
Bonds .....	4.32%	4.56%
Bank debt .....	4.07%	4.62%

Following is a table that shows the aggregate amounts of long-term debt maturing during the next five years and thereafter:

2006 .....	296,840
2007 .....	99,689
2008 .....	235,997
2009 .....	479,415
2010 .....	495,455
Thereafter .....	1,247,147

As of December 31, 2005, the Company was in compliance with all covenants required by its loan agreements.

**Bonds under EMTN Programme**

In 2003, Telekom Austria AG and Telekom Finanzmanagement GmbH (the 100% financing subsidiary of Telekom Austria AG) initiated a Euro Medium Term Note ("EMTN") Program, which provided borrowing facilities of EUR 2,500,000 and was increased to EUR 5,000,000 in December 2005. The payments of all amounts due in respect of notes issued by Telekom Finanzmanagement GmbH under this framework agreement are unconditionally and irrevocably guaranteed by Telekom Austria AG.

Under this program, the Company launched (i) a Eurobond with face value of EUR 750,000, coupon of 5.00% and 10-year maturity in July 2003 and (ii) two Eurobonds with face value of EUR 500,000 each, with maturities of 5 and 12 years, and coupons of 3.375% and 4.250%, respectively, in January 2005. In January 2005, the bonds were issued at a discount including issue cost of EUR 4,533 and EUR 9,567, respectively, which are being amortized over the related maturities. For Eurobonds with a face value of EUR 800,000 the Company entered into fixed to floating interest rate swap agreements to reduce fluctuations of the bond's fair market value.

**Other bonds**

Other bonds issued by the Company before the privatization are guaranteed by the Federal Republic of Austria and consisted of two bonds, both of which matured and were repaid in 2005.

**Bank debt**

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Bank debt incurred by the Company after its privatization is not guaranteed by the Federal Republic of Austria. These contracts can be described in more detail as follows:

In December 2005, the Company entered into a loan agreement of EUR 180,000 with the European Investment Bank. As of December 31, 2005, the loan is outstanding in full. Under the terms of this agreement, the company must observe covenants requiring the Company to meet certain financial ratios

In March 2000, the Company entered into a loan agreement for EUR 145,000 with the European Investment Bank. As of December 31, 2005, EUR 58,000 of the loan is outstanding in accordance with the repayment terms. Under the terms of this agreement, the Company must observe covenants requiring the Company to meet certain financial ratios.

Further, in October 2000 the Company entered into a loan agreement for EUR 232,553 to fund the acquisition of COL. As of December 31, 2005 the loan is outstanding in full in accordance with the repayment terms. Under the terms of the contract the Company has to maintain a minimum equity in COL, otherwise the loan becomes due. The interest rates vary depending on the rating of the Company.

As of December 31, 2005, EUR 295,160 of a syndicated loan granted to mobilkom austria was outstanding. The original loan totaled EUR 305,000 and was guaranteed by Telekom Austria AG.

In March 1999, Si.mobil entered into a loan agreement amounting to EUR 36,000 (original currency: Deutsche Mark 71,000) to finance the construction of the GSM network in Slovenia. The loan is secured by bills of exchange, property, receivables and shares of Si.mobil. The loan is repayable through March 2007.

**Bank debt guaranteed by the Federal Republic of Austria**

Bank debt of EUR 297,232 which was entered into before the Company's privatization is guaranteed by the Federal Republic of Austria.

A bank loan denominated in Swiss Francs, which amounted to EUR 176,635 as of December 31, 2004, was repaid in 2005. As of December 31, 2005, all bank debt incurred by the Company is denominated in Euro.

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**(17) LEASING**

The Company leases equipment used in its operations. The leases are classified as either operating or capital leases, and expire on various dates through 2015.

Future minimum lease payments for noncancelable operating leases, capital leases and cross border leases as of December 31, 2005 are:

	<b>Cross border leases</b>	<b>Other Capital leases</b>	<b>Operating leases</b>
2006 .....	122,227	578	42,579
2007 .....	144,933	47	39,772
2008 .....	127,632	9	35,348
2009 .....	185,371	-	33,785
2010 .....	147,713	-	33,794
after 2010 .....	472,112	-	34,584
Total minimum lease payments.....	1,199,988	634	<u>219,862</u>
Less amount representing interest .....	(260,041)	(2)	
Present value of lease payments.....	939,947	632	
Less current portion .....	(122,227)	(486)	
Non-current lease obligations .....	<u>817,720</u>	<u>146</u>	

Total rent expense was EUR 83,534, EUR 79,204 and EUR 74,358 in 2005, 2004 and 2003, respectively.

**Cross border leases**

In 1999 and 1998, the Company entered into various cross border lease transactions whereby certain equipment items, mainly switches, were sold to a U.S.-based trust and leased back over certain terms. Concurrent with the inception, the Company entered into Payment Undertaking Agreements ("PUA") with several counterparties whereby the counterparties agreed to make lease payments on behalf of the Company in exchange for a deposit. The counterparties in the PUAs received upfront payments totaling EUR 509,285 and EUR 113,763 for a portion of the debt assumed in 1999 and 1998, respectively. Interest accruing on the cash deposits matches interest on the debt portion financed through the deposit. In addition to the cash deposits, the Company purchased debt securities, deposited those securities with a custodian and pledged the securities to one of the counterparties in the PUA; the balance is to cover the remaining portion of the present value of the lease obligation not yet covered by the cash deposit made by the Company. The Company then also entered into a swap agreement with that same counterparty swapping the entire cash flows from the securities for cash flows from the portion of the lease payments that the counterparty is obligated to pay under the PUA. As a result of the swap agreement, interest income on the securities matches interest expense on the lease.

In 1999, mobilkom austria entered into similar cross border lease transactions whereby certain equipment items (mainly transceiver stations, base station controllers and location registers) were sold to four U.S.-based trusts and leased back over certain terms.

In 2001, the Company entered into a cross border lease transaction whereby certain equipment items, mainly switches were leased to a U.S.-based trust and leased back over certain terms. Concurrent with the inception, the Company entered into PUAs with several counterparties whereby the counterparties agreed to make lease payments on behalf of the Company in exchange for the upfront lease payments received under the head lease. The counter-

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parties in the PUAs received upfront payments totaling EUR 200,526 for a portion of the debt assumed in 2001. In addition to the PUAs the Company provided a loan of EUR 66,554 to the U.S.-based trust. Interest accruing on the PUAs and the loan match interest on the debt portion.

The difference between the cash proceeds from the sale and the present value of the future minimum lease payments represents a gain on the sale of a tax benefit. The net cash effect resulting from these transactions was a gain from the sale of the tax benefits which amounted to EUR 14,547, EUR 44,437 and EUR 7,337 in 2001, 1999 and 1998, respectively. The Company is amortizing these amounts over the term of the lease. The cash deposits, the securities purchased in connection with the PUAs and the upfront payments received for the head lease and the lease obligations are recorded separately on the balance sheets as the Company has not been released from their obligation under the lease and a legal right to offset does not exist. Accordingly, interest income and expenses in an equal amount totaling EUR 62,909, EUR 58,243 and EUR 65,669 have been recognized in 2005, 2004 and 2003, respectively.

Total assets and liabilities recorded in connection with the cross border leases are as follows:

<b>At December 31,</b>	<b>2005</b>	<b>2004</b>
Securities held-to-maturity, non-current .....	139,705	115,883
Other assets .....	800,242	738,948
Total assets in connection with cross border leases .....	939,947	854,831
Of which current .....	121,145	94,297
Lease obligations .....	939,947	854,831
Of which current .....	122,227	94,154

In 2001, two banks issued letters of credit to the trust for the liabilities of the Company. As of December 31, 2005, these letters of credit totaled EUR 70,744.

**(18) EMPLOYEE BENEFIT OBLIGATIONS**

Long-term liabilities for employee benefits consist of the following:

<b>At December 31,</b>	<b>2005</b>	<b>2004</b>
Voluntary termination benefits .....	10,457	19,394
Service awards .....	49,385	44,418
Severance .....	37,424	37,096
Pensions .....	8,583	9,076
Other .....	1,412	-
Total .....	<u>107,261</u>	<u>109,984</u>

**Voluntary termination benefits**

In June 2000, June 1999 and in November 1997, the Company offered voluntary retirement incentive programs ("VRIPs") to civil servants who cannot be terminated involuntarily. Under the terms of these programs employees that accept voluntary retirement are eligible to receive these payments until the day of retirement. An obligation for VRIPs was recognized when the eligible civil servant accepted the offer. The present value of the

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obligation is determined based on current compensation levels and the law. An annual increase of 2.5% for future years and a discount rate of 4.5% are used. VRIPs are not funded.

On January 1, 2002 a law was enacted that covers civil servants over the age of 55 by a governmental retirement plan with the effect of reducing the Company's obligation under the VRIPs. As of December 31, 2005, the accrual for the VRIPs relates to 110 employees. In connection with VRIPs the Company made payments of EUR 3,436, EUR 5,365 and EUR 69,634 during 2005, 2004 and 2003, respectively.

Expenses as well as the reversals of accruals are reflected as a reduction of employee costs in the accompanying consolidated statement of operations.

**Actuarial assumptions**

The assumptions used in the measurement of obligations for service awards, severance payments and pensions are shown in the following table:

<b>At December 31,</b>	<b>2005</b>	<b>2004</b>	<b>2003</b>
Actuarial assumptions:			
Discount rate.....	4.0%	5.0%	5.0%
Rate of compensation increase – civil servants.....	5.0%	5.0%	4.0%
Rate of compensation increase – other employees.....	4.0%	4.0%	2.5%
Rate of increase of pensions.....	0.8%	1.8%	1.8%

**Service awards**

Civil servants and certain employees (together "employees") are eligible to receive service awards. Under these unfunded plans, eligible employees receive a cash bonus after a specified service period. The bonus is equal to two months salary after 25 years of service and four months salary after 40 years of service. Employees with at least 35 years of service when retiring are also eligible to receive a bonus equal to four months salary. The compensation is accrued as earned over the period of service taking into account estimates of employees whose employment will be terminated or who will retire prior to reaching the required service period. All actuarial gains and losses are recognized immediately in the period realized.

The following table provides the components and a reconciliation of the changes in service awards for the years ended December 31, 2005 and 2004, respectively:

	<b>2005</b>	<b>2004</b>
Accrual at the beginning of the year.....	44,418	46,870
Addition from acquisition of Mobilтел.....	48	-
Service cost.....	1,973	2,149
Interest cost.....	2,278	2,288
Recognized actuarial loss (gain).....	2,861	(4,191)
Benefits paid.....	(2,193)	(2,698)
Accrual at the end of the year.....	<u>49,385</u>	<u>44,418</u>

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The benefits expected to be paid are shown in the following table:

2006.....	2,521
2007.....	2,483
2008.....	2,496
2009.....	2,967
2010.....	3,409
2011-2015 .....	27,455

**Severance**

Severance benefit obligations for employees hired before January 1, 2003 are covered by defined benefit plans as described below. Following a legal change, obligations for employees starting to work for the Company in Austria after January 1, 2003 are covered by a defined contribution plan and the Company paid EUR 484 and EUR 330 to this defined contribution plan (BAWAG Allianz Mitarbeitervorsorgekasse AG) in 2005 and 2004, respectively.

Upon retirement or severance, eligible employees receive severance payments equal to a multiple of their monthly compensation which comprises fixed compensation plus variable elements such as overtime and bonuses. Maximum severance is equal to a multiple of twelve times eligible monthly compensation. Up to three months of benefits are paid upon termination, with any benefit in excess of that amount being paid in monthly installments over a period not exceeding ten months. In case of death, the heirs of an eligible employee will receive 50% of the severance benefits.

The following tables provide the components of the net periodic benefit cost and a reconciliation of the changes in severance benefit obligations for the years ended December 31, 2005, 2004 and 2003, respectively:

	<u>2005</u>	<u>2004</u>	<u>2003</u>
Service cost.....	4,914	2,853	4,218
Interest cost.....	2,140	1,467	1,784
Amortization of unrecognized net loss .....	471	96	310
Curtailment loss / settlement.....	-	-	1,090
Net periodic benefit cost.....	<u>7,525</u>	<u>4,416</u>	<u>7,402</u>

	<u>2005</u>	<u>2004</u>
Projected benefit obligation at the beginning of the year .....	40,810	29,629
Addition from acquisition of Mobiltel.....	306	-
Service cost.....	4,914	2,853
Interest cost .....	2,140	1,467
Actuarial losses.....	13,694	8,638
Benefits paid.....	(2,934)	(1,777)
Projected benefit obligation at the end of the year .....	<u>58,930</u>	<u>40,810</u>
Unrecognized net actuarial losses.....	(26,408)	(13,183)
Accrued liability at the end of the year.....	32,522	27,627
Voluntary severance obligation .....	4,902	9,469
Total accrued severance liabilities at the end of the year .....	<u>37,424</u>	<u>37,096</u>

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The benefits expected to be paid are shown in the following table:

2006.....	7,195
2007.....	3,011
2008.....	2,363
2009.....	3,045
2010.....	3,367
2011-2015 .....	15,515

The liability for voluntary severance payments relates to individuals who are generally not entitled to severance payments, but have accepted a special offer by the Company to receive severance payments for voluntary termination of employment.

The Austrian government offered to civil servants of a certain age an early retirement at reduced future pension payments. The Company offered these eligible employees additional severance payments to further encourage the acceptance of the government offer. The Company incurred a legal obligation to civil servants making use of this opportunity and recorded expenses of EUR 19,315 in the year ended December 31, 2004. In the year ended December 31, 2005, the Company released EUR 3,699 of the accrual. Telekom Austria does not expect any future liabilities in addition to these accruals. Due to this offer the Company's workforce was reduced by 470 civil servants in 2004 and 650 civil servants in 2003.

**Pensions**

*Defined contribution pension plans*

Pension benefits are generally provided by social security for employees and by the government for civil servants in Austria. The Company is required to assist in funding the Austrian government's pension and health care obligations to the Company's current and former civil servants and their surviving dependents. The Company was legally obligated to make annual contributions to the Austrian government for active civil servants. These contributions gradually increased from 27.5% in 2000 to 30.1% in 2004. Beginning in October 2005 the contribution was reduced to 28.3%. Contributions to the government, net of the share contributed by civil servants, were EUR 41,237, EUR 46,854 and EUR 51,520 in 2005, 2004 and 2003, respectively.

Further, the Company provides a defined contribution plan covering employees of Austria based group companies. The Company's contributions to this plan are based on a percentage of the compensation not exceeding 5% of the salaries. The annual cost of this plan amounted to approximately EUR 9,339, EUR 9,154 and EUR 9,082 in 2005, 2004 and 2003, respectively.

*Defined benefit pension plan*

The Company provides defined benefits for certain former employees. All of such employees are retired and were employed prior to January 1, 1975. This unfunded plan provides benefits based on a percentage of salary and on years employed, not exceeding 80% of the salary before retirement including the pension provided by social security.

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The Company uses the projected unit credit method to determine pension cost for financial reporting purposes. In conjunction with this method the Company amortizes actuarial gains and losses using the corridor method.

The pension benefits for 2005, 2004 and 2003 are shown in the following table:

	<u>2005</u>	<u>2004</u>	<u>2003</u>
Interest cost .....	334	363	396
Amortization of actuarial gain.....	(136)	(90)	(64)
Amortization of unrecognized transition obligation .....	-	-	343
Net periodic pension benefit cost.....	<u>198</u>	<u>273</u>	<u>675</u>

The following table provides a reconciliation of the changes of benefit obligations for the years ended December 31, 2005 and 2004, respectively:

	<u>2005</u>	<u>2004</u>
Projected benefit obligation at the beginning of the year .....	6,650	7,618
Interest cost .....	334	363
Actuarial (gains) losses .....	104	(582)
Benefits paid .....	(691)	(749)
Projected benefit obligation at the end of the year.....	<u>6,397</u>	<u>6,650</u>
Unrecognized net gain .....	<u>2,186</u>	<u>2,426</u>
Accrued pension liability .....	<u>8,583</u>	<u>9,076</u>

The benefits expected to be paid are shown in the following table:

2006.....	671
2007.....	674
2008.....	677
2009.....	680
2010.....	681
2011-2015 .....	3,408

**(19) OTHER LIABILITIES AND DEFERRED INCOME**

The Company's other long-term liabilities and deferred income consist of:

<u>At December 31,</u>	<u>2005</u>	<u>2004</u>
Asset retirement obligation .....	48,109	38,042
Unamortized balance on sale of tax benefit .....	30,237	37,349
Deferred tax liabilities.....	42,236	19,721
Financial Instruments .....	5,311	-
Other .....	14,451	15,392
Total .....	<u>140,344</u>	<u>110,504</u>

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**(20) STOCK BASED COMPENSATION**

In 2000, the Company launched a stock option plan (Stock Option Plan 2000), under which all exercisable options were exercised in the year ended December 31, 2004. In 2004, the company launched a succeeding stock option plan under modified conditions. The new stock option plan (Stock Option Plan 2004) consists of three tranches, of which the first tranche has been granted in the year ended December 31, 2004 and the second tranche was granted in the year ended December 31, 2005. The Company reported an overall expense of EUR 20,864 and EUR 13,257 from both plans in the year ended December 31, 2005 and 2004, respectively.

**Stock Option Plan 2000 (2000 plan)**

On October 4, 2000, the shareholders of Telekom Austria approved stock option plans for employees of the Company, which expired on February 27, 2004. Under this plan, the Company granted a total of 4,686,881 options, each of which entitled eligible grantees upon exercise of the option to receive at their choice either cash or shares equal to the difference between the average quoted price of Telekom Austria stock during the five trading days preceding the exercise and the IPO price of Euro 9. The options granted were exercisable on specific dates between May 31, 2002 and February 27, 2004, as long as the average share price during the five days prior to exercise exceeded the initial public offering price of Euro 9 by 30% or more. As the stock price in the years ended 2003 and 2002 did not exceed the hurdle, no compensation expense was recorded for these years.

However, as of February 27, 2004, the average share price had exceeded the Initial Public Offering price by more than 30% for five consecutive days. Therefore, 3,230,718 options became exercisable and compensation expense of EUR 8,736, excluding related payroll taxes and social contributions, was recorded in the year ended December 31, 2004.

The following table shows stock option activity under the 2000 Plan for the year ended December 31, 2004:

	<u>2004</u>
Outstanding as of January 1 .....	3,268,850
Granted.....	-
Forfeited.....	(38,132)
Exercised.....	(3,230,718)
Outstanding as of December 31 .....	-
of which exercisable as of December 31 .....	-

**Stock Option Plan 2004 (2004 plan)**

Based on an authorization of the Annual General Meeting, the Supervisory Board of Telekom Austria approved the 2004 plan for members of the Management Board and senior members of management on April 16, 2004. Under this plan, the Company may grant a total of 10,000,000 options in three tranches between April 2004 and April 2006. Each tranche must be approved separately by the Supervisory Board and has a vesting period of twelve months or longer and an exercise period of approximately three years. To be eligible to receive options, plan members must hold a continuous investment in Telekom Austria shares until the options are exercised. In addition, in order for the stock options to vest, certain performance must be achieved by the Company based on basic earnings per share adjusted for certain effects ("the hurdle"). The hurdle will be determined annually for each subsequent tranche of options and must be approved by the Supervisory Board. Each option entitles the holder to receive, at the Company's choice, either shares at the exercise price or cash equal to the difference between the quoted market price of the Company's shares on the date of the option's exercise and the exercise price. The exercise price is defined as

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the average quoted closing price of Telekom Austria stock during a period of twenty trading days ending two days before the granting of options. One option is convertible into one share. If one year's hurdle is not met, options will accumulate until the hurdle of the next tranche is achieved provided that it is set higher than the original hurdle. The vesting period is adjusted until the next tranche becomes exercisable.

As of December 31, 2004, the Company's management had the intention to settle the options in shares and recorded the awards as equity awards. In March 2005, the Company modified the exercise term of the first tranche and decided to settle the options in cash only. As a result, amounts originally recorded in additional paid in capital were reclassified to liabilities. The compensation expense is measured based on the fair value of the options at grant date and every subsequent reporting date and recognized over the service period on a straight-line basis.

The fair value estimation is based on the binomial option pricing model applying the following parameters:

	<b>Stock option plan</b>	
	<b>2005</b>	<b>2004</b>
Expected average dividend per share.....	Euro 0.60 – 0.66	Euro 0.25
Expected volatility .....	22.5%	25%
Risk-free interest rate range .....	2.390% – 3.450%	2.053% – 4.280%
Fair value per option first tranche.....	Euro 7.27	Euro 2.73
Fair value per option second tranche .....	Euro 5.65	-

The first exercise dates and expected expiry dates of the options granted are as follows:

First exercise date first tranche .....	April 20, 2005
Expected expiry date first tranche.....	May 30, 2008
First exercise date second tranche.....	March 16, 2006
Expected expiry date second tranche .....	May 29, 2009

On April 19, 2004 the first tranche of 2,539,480 options was offered to the eligible employees. The exercise price of the first tranche is EURO 11.92 and for every 15 options awarded an eligible employee must hold one ordinary share until exercise. Subsequent to the fulfillment of this holding condition, 2,392,925 options were granted to the eligible employees, of which 384,000 options were granted to the members of the Management Board. The first tranche has a vesting period of twelve months from the grant date and an exercise period of three years after becoming exercisable. The fair value of the options as of grant date amounted to EUR 6,340 and the Company recognized compensation expense from the first tranche amounting to EUR 7,837 and EUR 4,521, excluding related payroll taxes and social contributions, for the year ended December 31, 2005 and 2004, respectively. The fair value calculation was based on an expected forfeiture rate of 2.95% per year. The hurdle set for the first tranche was met as of December 31, 2004 and the options became exercisable on April 20, 2005.

On January 19, 2005 the second tranche of 3,398,800 options was offered to the employees. The exercise price of the second tranche is Euro 13.98 and for every 20 (15) options awarded an eligible employee (director) must hold one ordinary share until exercise. Subsequent to the fulfillment of this holding condition, 2,874,100 options were granted to the eligible employees, of which 396,400 options were granted to the members of the Management Board. The second tranche has a vesting period of twelve months from the grant date and an exercise period of three years after becoming exercisable. The fair value of the options as of grant date amounted to EUR 8,455 and the Company recognized compensation expense from the second tranche amounting to EUR 13,027 for the year ended December 31, 2005. The performance condition set for the second tranche was met as of December 31, 2005.

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The following table shows stock option activity under the 2004 plan for the years ended December 31, 2005 and 2004, respectively:

	<u>2005</u>	<u>2004</u>
Outstanding as of January 1 .....	2,363,925	-
Granted.....	2,874,100	2,392,925
Forfeited.....	(92,195)	(29,000)
Exercised.....	(1,663,350)	-
Outstanding as of December 31 .....	3,482,480	2,363,925
of which exercisable as of December 31 .....	662,680	-

**(21) INCOME TAXES**

Income before income taxes, minority interests and cumulative effect of a change in accounting principle is attributable to the following geographic locations:

	<u>2005</u>	<u>2004</u>	<u>2003</u>
Domestic .....	348,067	281,477	186,197
Foreign .....	175,453	68,603	46,360
Total .....	<u>523,520</u>	<u>350,080</u>	<u>232,557</u>

Income tax expense attributable to income before income taxes, minority interests and cumulative effect of a change in accounting principle for the years ended December 31, consisted of the following:

	<u>2005</u>	<u>2004</u>	<u>2003</u>
Current			
Domestic .....	18,523	22,266	8,899
Foreign.....	20,747	14,800	14,511
	<u>39,270</u>	<u>37,066</u>	<u>23,410</u>
Deferred			
Domestic .....	56,912	84,491	52,506
Foreign.....	10,190	629	7,120
	<u>67,102</u>	<u>85,120</u>	<u>59,626</u>
Total .....	<u>106,372</u>	<u>122,186</u>	<u>83,036</u>

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Benefits of operating loss carryforwards of EUR 131, EUR 594 and EUR 1,818 were included in the deferred tax expense for the years ended December 31, 2005, 2004 and 2003, respectively.

The table below provides information on total tax allocation in the financial statements:

	<b>2005</b>	<b>2004</b>	<b>2003</b>
Continuing operations.....	106,372	122,186	83,036
Reduction of intangible assets.....	-	(13,303)	-
Other comprehensive income.....	1,991	1,412	2,787
Additional paid in capital.....	-	-	451
	<u>108,363</u>	<u>110,295</u>	<u>86,274</u>
Tax for cumulative effect of change in accounting principle.....	-	-	(6,071)
	<u>108,363</u>	<u>110,295</u>	<u>80,203</u>

On May 6, 2004 the Austrian National Council passed a tax reform, which became effective as of January 1, 2005. Among other regulations, the reform reduces the corporate tax rate from 34 % to 25 %, which leads to an overall tax expense of EUR 21,799 from revaluation of the deferred tax assets and liabilities as of December 31, 2004. In 2004, the Company reassessed a valuation allowance that was established at the time of the 3G Mobile business combination and based on that assessment, reduced the valuation allowance by EUR 16,143. Of this amount, EUR 13,303 was used to reduce intangible assets acquired from this acquisition. The balance of EUR 2,840 net of the effect of change in tax rate of EUR 5,811 was credited to the income tax expense.

The following table shows the principle components for the difference between the reported income tax expense and the amount of income tax expense that would result from applying the Austrian statutory income tax rate to income before income taxes, minority interests and cumulative effect of a change in accounting principle:

	<b>2005</b>	<b>2004</b>	<b>2003</b>
Income tax expense at statutory rate.....	130,880	119,027	79,069
Foreign tax rate differential.....	(18,790)	(9,874)	(7,053)
Non-deductible expenses.....	3,524	2,879	3,792
Tax incentives.....	(1,923)	(3,450)	(3,673)
Tax free income from investments.....	(134)	(185)	(563)
Non-deductible impairment charges.....	4,079	-	-
Change in valuation allowance.....	(14,125)	(5,566)	7,724
Effect of change in tax rate.....	47	21,799	-
Tax expense and corrections previous years	3,048	(579)	305
Other.....	(234)	(1,865)	3,435
Income tax expense.....	<u>106,372</u>	<u>122,186</u>	<u>83,036</u>
Effective income tax rate.....	20.3%	34.9%	35.7%
Effective income tax rate excluding effect of change in tax rate.....	20.3%	28.7%	

Non-deductible expenses mainly consist of interest expenses on shareholder loans and representation expenses. Tax incentives principally consist of research and education incentives and other government grants. The effect of change in tax rate in 2005 is due to a revaluation of the tax assets of COL following a reduction of the corporate tax rate from 26% to 24 %, for 2006 and the following periods.

In 2005, the valuation allowance decreased by EUR 14,125. Changes in the amount of EUR 17,190 were primarily due to a release of valuation allowance of loss carryforwards due to changes in the tax law in Slovenia resulting in an increase of the expiration period of tax loss carryforwards and due to a change in circumstances that caused change in judgement about the realizability of the utilization of the current loss of 3G Mobile. However, this

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effect was partially offset by establishing a valuation allowance on current losses in the amount of EUR 3,715. In 2004 the valuation allowance decreased by EUR 28,075. That primarily resulted from the reduction of intangible assets of EUR 13,303, related tax benefit thereon of EUR 4,523 and the effect of a change in the tax rate of EUR 11,642. In 2003, the valuation allowance increased by EUR 65,425 of which EUR 57,868 resulted from business combinations and had no impact on the income statement.

The tax effects of temporary differences that give rise to deferred tax assets and liabilities at December 31 are shown below.

	<u>2005</u>	<u>2004</u>
Deferred tax assets		
Goodwill .....	1,398	13,510
Deferred deduction for write downs of investments in subsidiaries.....	26,142	34,565
Operating loss carryforwards.....	56,366	99,223
Accounts receivable.....	7,088	1,687
Assets held for sale .....	-	14,734
Long-term debt .....	1,027	655
Other liabilities and deferred credits.....	10,503	11,342
Accrued liabilities.....	2,784	3,173
Employee benefit obligations. ....	4,022	2,690
Other .....	8,795	10,971
Total deferred tax assets.....	<b>118,125</b>	<b>192,550</b>
Valuation allowance.....	(39,560)	(53,564)
Deferred tax assets, net of valuation allowance .....	<b>78,565</b>	<b>138,986</b>
Deferred tax liabilities		
Property, plant and equipment.....	(27,971)	(17,449)
Long-term investments.....	(83)	(84)
Goodwill Mobilitel .....	(2,076)	-
Other intangible assets.....	(55,442)	(54,693)
Other .....	(2,417)	(7,220)
Total deferred tax liabilities .....	<b>(87,989)</b>	<b>(79,446)</b>
Net deferred tax asset (liability).....	<b>(9,424)</b>	<b>59,540</b>

The net deferred tax assets decreased by EUR 68,964 and resulted in a net deferred tax liability. Of this, EUR 231 related to the acquisition of Mobilitel (see note (2)), EUR 47 related to foreign exchange differences that had no impact on the income statement. The company recorded a deferred tax expense of EUR 67,102. At December 31, 2005, the Company had approximately EUR 221,593 of operating loss carryforwards. Of these, EUR 101,881 relate to foreign subsidiaries and are not available for use in Austria. Of these loss carryforwards relating to foreign subsidiaries, EUR 92,085 have expiration dates as follows:

<u>Years</u>	<u>Amount</u>
2006	395
2007	20,236
2008	37,976
2009	24,122
2010	9,347
2012	9
Total	<u>92,085</u>

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The remaining amount of operating loss carryforwards relate to Austria and do not expire. In Austria the annual usage is limited to 75% of the taxable income for that year.

In assessing the recoverability of deferred tax assets, management considers whether it is more likely than not that all the deferred tax assets will be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income and tax planning strategies in making this assessment.

Based on the level of historical taxable income and projections for future taxable income over the periods in which the deferred tax assets are deductible, management believes it is more likely than not that the Company will realize the benefits of these deductible differences and operating loss carryforwards net of valuation allowances. The amount of deferred tax assets considered realizable, however, could be reduced in the near term if estimates of future taxable income are reduced.

**(22) FINANCIAL INSTRUMENTS**

Derivative financial instruments are used by the Company to manage its exposure to adverse fluctuations in interest and foreign exchange rates. The Company has established a control environment which includes policies and procedures for risk assessment, approval, reporting and monitoring of derivative financial instrument activities. The Company is not a party to leveraged derivatives and the policies prohibit the holding or issuing of financial instruments for speculative purposes.

The Company uses various types of financial instruments including derivative financial instruments in the normal course of business for purposes other than trading.

By their nature, all such instruments involve risk, including market risk and credit risk of nonperformance by counterparties, and the maximum potential loss may exceed the amount recognized in the balance sheets. However, at December 31, 2005 and 2004, in management's opinion the probability of nonperformance of the counterparties in these financial instruments was remote.

**Credit risk**

The Company monitors its exposure to credit risk. The Company does not have any significant exposure to any individual customer or counterparty, nor does it have any major concentration of credit risk related to any financial instrument other than noted in the section concerning the concentration of credit risk in significant accounting policies.

In order to reduce the risk of nonperformance by the other parties to swap agreements, the contracts are subject to the Swap Dealer Agreements.

**Market risk**

Market risk is monitored by using value-at-risk models for interest rate as well as currency risk for the long-term debt and derivative portfolios.

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**Information with respect to cash flow hedges**

Changes in the fair value of interest rate swaps designated as hedging instruments of variability of cash flows associated with variable rate long-term debt are reported in accumulated other comprehensive income. These amounts are subsequently classified into financial income as a yield adjustment in the same period in which the related interest on the floating-rate debt obligations affect earnings. In 2005 and 2004, respectively, no hedge ineffectiveness occurred.

**Interest rate swap agreements**

The Company entered into interest rate swaps to reduce the aggregate exposure to changes in floating interest rates and fair market value fluctuations of the debt portfolio. Fixed interest rate payments as of December 31, 2005, ranged from 3.38% to 5.00%. Floating-rate payments are based on rates tied to different inter-bank offered rates.

In line with its risk policy, the Company entered into fixed to floating interest rate swaps in 2005 and 2003. The floating rate is based on EURIBOR and enables the company to benefit from current low short-term interest rates.

The following table indicates the types of swaps in use at December 31, 2005 and 2004, and their weighted-average interest rates and the weighted-average remaining terms of the interest rate swap contracts. Average variable rates are those in effect at the reporting date and may change significantly over the lives of the contracts:

	<b>2005</b>	<b>2004</b>
<b>Variable to fixed swaps in EUR</b>		
Notional amount in EUR .....	-	145,346
Average receive rate .....	-	2.26%
Average pay rate .....	-	6.66%
Average maturity in years .....	-	0.4
<b>Fixed to variable swaps in EUR</b>		
Notional amount in EUR .....	800,000	300,000
Average receive rate .....	3.98%	5.00%
Average pay rate .....	2.62%	3.02%
Average maturity in years .....	5.38	8.5

**Foreign exchange agreements**

The Company entered into foreign currency denominated loans because of low interest rates connected to loans denominated in Swiss Francs ("CHF"). These loans were repaid in 2005. The use of cross currency swaps allowed the Company to reduce the exposure to the risk of adverse changes in exchange rates. Fixed interest rates as of December 31, 2004, ranged from 7.6% to 7.7%.

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The following table indicates the types of foreign exchange agreements in use at December 31, 2005 and 2004, and if applicable their weighted-average interest rates, the weighted-average remaining terms and the respective exchange rates of the contracts:

	<b>2005</b>	<b>2004</b>
<b>Cross Currency Swaps EUR – CHF</b>		
Notional amount in EUR .....	-	176,635
Notional amount in CHF.....	-	300,000
Average receive rate – CHF.....	-	5.47%
Average pay rate – EUR .....	-	7.65%
Average maturity in years.....	-	0.4
<b>Forward exchange contracts – US \$</b>		
Notional amount in EUR .....	2,794	4,399
Notional amount in US \$ .....	3,300	5,700
Forward exchange rate (weighted).....	1.18	1.30
Exchange rate as of the balance sheet date .....	1.18	1.36
Longest term of the contracts.....	February 2006	April 2005

The notional amounts of the derivative instruments above do not represent amounts exchanged by the parties and, therefore, are not a measure of our exposure. The Company's exposure is limited to the fair value of the contracts with a positive fair value plus interest receivable, if any, at the reporting date.

The following table summarizes the fair values of financial instruments:

	<b>2005</b>		<b>2004</b>	
	<b>Carrying amount</b>	<b>Fair value</b>	<b>Carrying amount</b>	<b>Fair value</b>
<b>Financial instruments</b>				
Cash .....	116,756	116,756	288,195	288,195
Accounts receivable – trade .....	452,878	452,878	408,820	408,820
Accounts receivable – sold .....	228,878	228,878	173,350	173,350
Balances due from related parties .....	66	66	85	85
Accounts payable –trade .....	(529,197)	(529,197)	(534,498)	(534,498)
Payables to related parties.....	(20,244)	(20,244)	(22,924)	(22,924)
Securities held-to-maturity.....	145,796	154,208	120,946	133,865
Securities available-for-sale.....	16,448	16,448	19,656	19,656
Long-term debt.....	(2,557,703)	(2,786,345)	(1,647,171)	(1,772,904)
<b>Derivative financial instruments</b>				
Interest rate swap agreements .....	(5,311)	(5,311)	(17,294)	(17,294)
Cross currency swap agreements .....	-	-	15,849	15,849
Foreign currency forward contract.....	(1)	(1)	(216)	(216)

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**(23) SHAREHOLDERS' EQUITY**

**Share Capital**

At the Annual General Meeting on June 3, 2004 the Management Board was authorized to issue convertible bonds, which grant the holders subscription and/or conversion rights of up to 90,000,000 shares. The authorization was given for a period of 5 years from the day of authorization and ends in 2009.

In addition, the Management Board was authorized to increase the share capital by up to EUR 109,050 by issuing 50,000,000 ordinary shares to holders of convertible bonds to the extent that they exercise their subscription and/or conversion rights.

**Dividend Payment**

On May 25, 2005 the shareholders approved at the Annual General Meeting a dividend distribution of Euro 0.24 per zero par value share. The overall dividend payment amounted to EUR 117,866 and was distributed on June 6, 2005.

On June 3, 2004 the shareholders approved at the Annual General Meeting of the company a dividend distribution of Euro 0.13 per share. The overall dividend payment totaled EUR 64,578 and was distributed on June 15, 2004.

The net income of Telekom Austria AG amounts to EUR 301,778 and EUR 412,683 in the year 2005 and 2004, respectively. According to Article 126 of the Stock Corporation Act, the Supervisory Board and the Management Board decided to transfer an amount of EUR 50,000 and EUR 271,931 out of Telekom Austria AG 2005 and 2004 net income of EUR 301,778 and EUR 412,683 to retained earnings, resulting in unappropriated profits of EUR 279,794 and EUR 145,882 in the years 2005 and 2004, respectively. The Management Board and Supervisory Board plan to propose to the shareholders at the Annual General Meeting to distribute from unappropriated earnings a dividend of Euro 0.55 per share.

**Treasury stock**

At the Annual General Meeting on May 25, 2005, the Management Board was authorized to acquire treasury stock to the maximum extent legally permitted at a minimum price of Euro 9 and a maximum price of Euro 21 per share during a period of 18 months, ending November, 2006. The Management Board was empowered (i) to use this treasury stock to satisfy obligations under the stock option programs described in note(20), (ii) to use it to satisfy obligations resulting from the issue of convertible bonds, (iii) to use it as consideration for acquisitions (iv) to retire it up to a maximum share capital decrease of EUR 109,050 or (v) to sell it in the stock exchange or in a public offering.

On February 27, 2004, the Company exercised its 3,326,881 American call options on treasury stock which were acquired during the Initial Public Offering in November 2000 to limit the Company's exposure under the stock option plan that expired on February 27, 2004. The strike price of each call option was Euro 9. Following the exercise of the American call option, the Company held 3,326,881 shares in treasury, 0.67% of its share capital, and available for issuance to employees under the employee stock option plan.. During the year ended December 31, 2004, 89,748 options were exercised in shares by employees at the exercise price of Euro 9. The remaining option

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holders elected to receive cash for the difference between the exercise price and the average quoted price of Telekom Austria stock.

Furthermore, the Company acquired 11,241,412 and 3,018,561 shares of treasury stock at an average purchase price of Euro 16.41 and Euro 11.34 in the years ended December 31, 2005 and 2004, respectively.

As of December 31, 2005, the Company holds 17,497,106 shares in treasury at an average purchase price of Euro 14.16 per share reported as a reduction to shareholders' equity in the amount of EUR 247,818 as a result of these transactions.

**Earnings per share**

Basic earnings per share and diluted earnings per share for the years ended December 31, 2005 and 2004 is calculated as follows:

	<u>2005</u>	<u>2004</u>
Net Income of the year ended December 31 .....	417,146	227,263
Weighted average number of common shares outstanding.....	489,050,517	496,495,378
Dilutive effect of Stock Option Plan 2004.....	-	29,449
Weighted average number of dilutive shares outstanding .....	489,050,517	496,524,827
Basic earnings per share.....	Euro 0.85	Euro 0.46
Diluted earnings per share .....	Euro 0.85	Euro 0.46

On April 19, 2004, the first tranche of 2,392,925 options was granted to eligible employees within the scope of the Stock Option Plan 2004 as described in note (20). The Company determined the dilutive effect of this transaction for periods ended June 30, September 30, and December 31, 2004. In March 2005, the Company announced its intention to settle the first tranche of the Stock Option Plan 2004 in cash. Consequently, the Company determined that the Stock Option Plan 2004 does not provide any potential common shares as of December 31, 2005.

**Shares held by members of the Management Board**

The members of the Management Board hold shares in the Company as follows:

	Number of shares			December 31, 2005
	January 1, 2005	Purchased	Sold	
Heinz Sundt	13,011	-	-	13,011
Boris Nemsic	10,110	3,000	-	13,110
Stefano Colombo	12,212	800	-	13,012
Rudolf Fischer	13,007	-	-	13,007

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**Accounting for derivative and hedging activities**

Derivative financial instruments are used by the Company to manage its exposure to adverse fluctuations in interest and foreign exchange rates. The Company has established a control environment which includes policies and procedures for risk assessment, approval, reporting and monitoring of derivative financial instrument activities. The Company is not a party to leveraged derivatives and the policies prohibit the holding or issuing of financial instruments for speculative purposes.

Changes in the time value of the derivatives are not excluded from the assessment of hedge effectiveness and are recorded in earnings. Hedge ineffectiveness, determined in accordance with SFAS No. 133, had no impact on the Company's earnings for the years ended December 31, 2005 and 2004, respectively. All cash flow hedges were realized during the years ended December 31, 2005. In the year ended December 2005 and 2004, respectively, the Company realized a gain of EUR 2,847 and EUR 268 net of income tax.

The cumulative unrealized gains and losses from hedging activities recorded in other comprehensive income are as follows:

	<b>December 31, 2005</b>	<b>December 31, 2004</b>
Unrealized Losses		
Gross.....	-	(4,313)
Less income tax .....	-	1,466
Unrealized net loss, net of income tax.....	-	<b>(2,847)</b>

**Other comprehensive income**

Other comprehensive income consists of the following items:

	<b>Unrealized gain (loss) on securities</b>	<b>Unrealized gain (loss) on hedging activities</b>	<b>Foreign currency translation</b>	<b>Accumulated other comprehensive income</b>
Balance January 1, 2003 .....	(848)	(10,342)	8,106	(3,084)
Changes, net of income tax .....	2,214	3,195	(10,690)	(5,281)
Balance December 31, 2003 .....	(2,655)	268	(414)	(3,069)
Changes, net of income tax .....	1,096	4,032	(4,167)	1,229
Balance December 31, 2004 .....	(193)	(2,847)	(7,165)	(10,205)
Realized gain (loss), net of income tax .....	(8)	2,847	1,157	3,996
Changes, net of income tax .....	602	-	12,939	13,541
Balance December 31, 2005. ....	401	-	6,931	7,332

**Sale of American call option**

The Company had classified the shares issued under this option as permanent equity, since the optional shares were registered, issued and outstanding, and the Company was under no obligation to repurchase any shares unless it desired to do so.

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On November 21, 2000, Telekom Austria purchased 3,832,248 American call options for a premium of EUR 12,527. The expiration date was February 27, 2004. The underlying shares of the American call option were the shares of Telekom Austria AG. The strike and execution price of the call option was Euro 9 and settlement was either physical delivery of the shares or cash, at the request of Telekom Austria. Since the call requires no cash settlement whatsoever by the Company, nor is the Company required to issue any additional shares as a result of exercise, the call was classified as permanent equity in accordance with EITF 00-19.

In 2003, the Company sold 610,000 American call options for an aggregate price of EUR 957. In 2002, the Company sold 717,701 American call options for an aggregate price of EUR 1,245. As the original acquisition of the options was accounted for as permanent equity under the provisions of EITF 00-19, proceeds from the sale of the options have been credited net of tax directly to additional paid in capital in the accompanying statement of changes in shareholders' equity.

On February 27, 2004, the Company exercised its 3,326,881 American call options (see Treasury stock).

**Restricted earnings**

Under the "Austrian Stock Corporation Act", retained earnings available for distribution to shareholders are based upon the unconsolidated retained earnings of Telekom Austria AG as reported in its balance sheet determined in accordance with the Austrian Commercial Code.

The net income of Telekom Austria AG under Austrian GAAP including released untaxed reserves of EUR 7,997 and EUR 48,506 amounts to EUR 301,778 and EUR 412,683 in the years ended December 31, 2005 and 2004, respectively.

**(24) REVENUES**

<b>Year ended December 31,</b>	<b>2005</b>	<b>2004</b>	<b>2003</b>
Revenues from services .....	4,093,238	3,810,891	3,726,955
Revenues from sales of merchandise .....	284,053	245,377	242,795
Total .....	<u>4,377,291</u>	<u>4,056,268</u>	<u>3,969,750</u>

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**(25) OTHER OPERATING EXPENSES**

<b>Year ended December 31,</b>	<b>2005</b>	<b>2004</b>	<b>2003</b>
Interconnection .....	489,586	452,171	421,787
Services received .....	253,125	221,952	211,445
Repairs .....	176,144	177,277	178,256
Charges from related parties .....	13,022	13,241	15,013
Advertising and marketing.....	229,580	198,138	198,362
Rental expenses.....	83,534	79,204	74,358
Legal and other consulting.....	38,862	40,354	44,451
Commission expenses .....	56,409	41,301	41,078
Bad debt expenses.....	43,393	24,707	30,629
Other support services.....	110,076	109,721	96,684
Travel expenses.....	22,777	22,302	23,696
Energy .....	23,599	21,824	21,979
Other non income taxes .....	6,185	8,023	7,201
Training expenses .....	12,928	11,657	13,129
Other .....	35,412	67,352	85,453
<b>Total .....</b>	<b>1,594,632</b>	<b>1,489,224</b>	<b>1,463,521</b>

In accordance with SFAS No. 144, as amended, the Company recorded a net gain from retirement of long-lived assets in 2005 of EUR 1,510 in 2005 and a net loss from retirement of long-lived assets in 2004 and 2003 respectively, of EUR 28,788 and EUR 41,571, which are presented in other operating expenses, other.

**(26) OTHER, net**

<b>Year ended December 31,</b>	<b>2005</b>	<b>2004</b>	<b>2003</b>
Foreign exchange losses .....	(149,996)	(103,572)	(246,883)
Foreign exchange gains.....	151,139	107,081	242,013
Dividend income .....	41	7	48
Other .....	10,841	12,140	4,255
<b>Total .....</b>	<b>12,025</b>	<b>15,656</b>	<b>(567)</b>

In other income net impairment charges recorded on investments totaling EUR 284, EUR 716 and EUR 2,840 were recorded for the years ended December 31, 2005, 2004 and 2003, respectively.

**(27) COMMITMENTS AND CONTINGENCIES**

The Company had further purchase obligations amounting to EUR 3,020,184 and EUR 1,754,300, of which EUR 866,130 and EUR 538,500 is short-term as of December 31, 2005 and 2004, respectively. These obligations include purchase commitments for property, plant and equipment as well as for intangible assets and other non-redeemable contractual commitments such as service agreements and interconnection obligations.

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In the normal course of business the Company is subject to proceedings, lawsuits and other claims, including proceedings under laws and regulations related to interconnection. Such matters are subject to many uncertainties, and outcomes are not predictable with certainty. Consequently, management is unable to ascertain the ultimate aggregate amount of monetary liability or financial impact with respect to these matters at December 31, 2005. These matters could affect the operating results or cash flows of any one quarter when resolved in future periods. However, management believes that after final disposition, any monetary liability or financial impact to the Company beyond that provided for at year end would not be material to its consolidated financial statements.

**(28) CASH FLOW STATEMENT**

Following is a summary of supplemental cash flow information:

Years ended December 31,	2005	2004	2003
<b>Cash paid for</b>			
Interest .....	145,709	161,057	182,836
Income taxes .....	57,349	23,330	16,246
<b>Cash received for</b>			
Interest .....	14,148	8,080	3,128
Tax refunds .....	-	-	-
<b>Non cash investing and financing</b>			
Dividends .....	-	-	-

**(29) SEGMENT REPORTING**

The Company organizes its operations into three segments: wireline, wireless and other activities.

Wireline includes fixed line, data communications and internet services and focuses on wholesale and retail customers. Wholesale customers including telecommunications operators and service providers are offered network-based services, while retail customers, including business and residential end-users are offered voice telephony, data communications, internet and other services.

Wireless, operated by our mobile communications segment, offers a full range of digital mobile communications services to business and residential customers.

The segment other activities contains the financing activities of the Company.

Adjusted EBITDA is defined by the Company as operating income before depreciation, amortization and impairment charges. The Company uses adjusted EBITDA to measure the performance of segments because it is commonly used in the telecommunications industry as a comparative measure of financial performance. In addition, the Company believes it is a widely accepted indicator of its ability to incur and service debt.

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The accounting policies of the segments are the same as those described in the summary of significant accounting policies (see note (1)).

For the year ended December 31, 2005 and 2004, respectively, the segment totals reconcile to the consolidated financial statements as a result of eliminating transactions and balances between consolidated segments

<b>Year ended</b>	<b>Wireline</b>	<b>Wireless</b>	<b>Other activities</b>	<b>Segment totals</b>	<b>Eliminations</b>	<b>Consolidated</b>
<b>December 2005</b>						
External revenues.....	1,973,212	2,404,032	47	4,377,291	-	4,377,291
Intersegmental revenues.....	161,956	85,156	-	247,112	(247,112)	-
Total revenues.....	2,135,168	2,489,188	47	4,624,403	(247,112)	4,377,291
adj. EBITDA (excl. Impairment charges)....	786,730	969,029	(101)	1,755,658	1,523	1,757,181
Impairment charges.....	16,317	1,071	-	17,388	-	17,388
adj. EBITDA.....	770,413	967,958	(101)	1,738,270	1,523	1,739,793
Depreciation and amortization.....	704,495	415,727	-	1,120,222	(421)	1,119,801
Operating Income.....	65,918	552,231	(101)	618,048	1,944	619,992
Total assets.....	5,421,194	4,965,138	2,713,776	13,100,108	(4,688,255)	8,411,853
Expenditures for additions to long-lived assets .....	314,145	313,494	-	627,639	-	627,639
<b>Year ended</b>	<b>Wireline</b>	<b>Wireless</b>	<b>Other activities</b>	<b>Segment totals</b>	<b>Eliminations</b>	<b>Consolidated</b>
<b>December 2004</b>						
External revenues.....	2,013,563	2,042,678	27	4,056,268	-	4,056,268
Intersegmental revenues.....	171,179	82,805	-	253,984	(253,984)	-
Total revenues.....	2,184,742	2,125,483	27	4,310,252	(253,984)	4,056,268
adj. EBITDA (excl. Impairment charges)....	814,328	765,443	(39)	1,579,732	(10,894)	1,568,838
Impairment charges.....	1,334	-	-	1,334	-	1,334
adj. EBITDA (incl. Impairment charges)....	812,994	765,443	(39)	1,578,398	(10,894)	1,567,504
Depreciation and amortization.....	757,174	358,077	-	1,115,251	(421)	1,114,830
Operating Income.....	55,820	407,366	(39)	463,147	(10,473)	452,674
Total assets.....	5,260,231	3,181,735	1,250,869	9,692,835	(2,450,328)	7,242,507
Expenditures for additions to long-lived assets .....	280,390	267,779	-	548,169	-	548,169

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Year ended	Wireline	Wireless	Other activities	Segment totals	Eliminations	Consolidated
<b>December 2003</b>						
External revenues.....	2,029,893	1,939,857	-	3,969,750	-	3,969,750
Intersegmental revenues.....	167,758	90,344	-	258,102	(258,102)	-
Total revenues.....	2,197,651	2,030,201	-	4,227,852	(258,102)	3,969,750
Adj. EBITDA (excl. Impairment charges)...	780,508	727,057	(45)	1,507,520	2,277	1,509,797
Impairment charges.....	6,825	-	-	6,825	-	6,825
Adj. EBITDA (incl. Impairment charges)....	773,683	727,057	(45)	1,500,695	2,277	1,502,972
Depreciation and amortization.....	807,935	325,620	-	1,133,555	(407)	1,133,148
Operating Income.....	(34,252)	401,437	(45)	367,140	2,684	369,824
Total assets.....	6,116,105	3,131,630	1,125,178	10,372,913	(2,476,648)	7,896,265
Expenditures for additions to long-lived assets .....	299,918	300,129	-	600,047	(363)	599,684

Adjusted EBITDA differs from consolidated net income as a result of the following differences:

	Year ended December 31,		
	2005	2004	2003
adj. EBITDA (excl. Impairment charges) - segment totals .....	1,755,658	1,579,732	1,507,520
Impairment charges.....	(17,388)	(1,334)	(6,825)
adj. EBITDA (incl. Impairment charges) - segment totals.....	1,738,270	1,578,398	1,500,695
Depreciation and amortization.....	(1,119,801)	(1,114,830)	(1,133,148)
Interest income.....	89,084	70,016	75,167
Interest expense.....	(198,151)	(188,818)	(230,979)
Equity in earnings of affiliates .....	570	552	19,112
Other.....	13,548	4,762	1,710
Income before taxes, minority interests and cumulative effect of change in accounting principle.....	523,520	350,080	232,557
Income tax expense.....	(106,372)	(122,186)	(83,036)
Minority interests.....	(2)	(631)	(3,422)
Cumulative effect of change in accounting principle, net of tax.....	-	-	(11,858)
Net income.....	417,146	227,263	134,241

In 2005, 2004 and 2003, more than 82%, 88% and 89%, respectively, of the revenues generated by the reportable segments relate to operations in Austria. As of December 31, 2005 and 2004, respectively, 68% and 90% of the long-lived assets were located in Austria.

### (30) SUBSEQUENT EVENTS

Based on the relevant approval by the Supervisory Board, the third tranche of 3,897,968 options was granted to the eligible employees under the stock option plan 2004 (see note (20)) on January 12, 2006. The exercise price of Euro 18.91 was defined as the average quoted closing price of Telekom Austria stock during a period of twenty trading days ending two days before the granting of options. The options can be settled either in cash or in shares at the Company's choice. Vesting of the stock options awarded is based on the performance of basic earnings per share

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adjusted for certain effects. The options have a vesting period of about 14 months from the grant day and an exercise period of three years after becoming exercisable.

On January 31, 2006, ÖIAG reduced its holding from 30.17% to approximately 29.99% of voting common shares through delivery of shares to investors holding exchangeable notes.

In January 2006, the Company announced resignation of CEO Mr. Heinz Sundt as of May 23, 2006. At the same time, Mr. Boris Nemsic was appointed as successor and will become Chief Executive Officer of the Company on May 24, 2006 in addition to his position as CEO of mobilkom austria. Mr. Rudolf Fischer was appointed as successor deputy CEO.

On March 1, 2006, the Company sold 16.667% of paybox austria GmbH and reduced its interest to 83.333%. The sales price amounted to EUR 200. As a consequence of participation rights given to the buyer, the Company will no longer consolidate paybox austria GmbH but will account for the investment using the equity method.