DIRECTORS' REPORT
NETIA S.A. GROUP
for the year ended December 31, 2013

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This Directors' Report presents the financial results of Netia S.A. ("Netia", the "Company", the "Issuer") and the consolidated financial results for the Netia S.A. Group ("Netia Group").

1 Characteristics of the Netia Group

1.1 The Netia Group structure

The consolidated financial statements as at and for the year ended December 31, 2013 include the financial statements of the Company and the following subsidiaries:

- Centrina Sp. z o.o.
- Dianthus Sp. z o.o
- InterNetia Holdings Sp. z o.o. Group
- Net 2 Net Sp. z o.o.
- Netia 2 Sp. z o.o.
- Netia Brand Management Sp. z o.o.
- Telefonia DIALOG Sp. z o.o. Group.

The financial statements of the InterNetia Holdings Sp. z o.o. Group include the financial statements of InterNetia Holdings Sp. z o.o. ("InterNetia Holdings") and its subsidiaries:

- Internetia Sp. z o.o.,
- UNI-Net Poland Sp. z o.o.

The financial statements of the Telefonia DIALOG Sp. z o.o. Group include the financial statements of Telefonia DIALOG Sp. z o.o. and its wholly-owned subsidiary Petrotel Sp. z o.o.

Changes within the Netia Group's structure

Acquisitions

On May 10, Netia purchased from UPC Polska Sp. z o.o. and UPC Poland Holding B.V. all shares in Centrina Sp. z o.o. ("Centrina") constituting 100% of the shares in the share capital of Centrina and representing 100% of the votes at the meetings of the shareholders of Centrina and all shares in Dianthus Sp. z o.o. ("Dianthus") constituting 100% of the shares in the share capital of Dianthus and representing 100% of the votes at the meetings of the shareholders of Dianthus. Dianthus and Centrina are owners of part of the former Aster cable operator's network reaching 446,000 (not in thousands) households in Warsaw and Kraków. The network was acquired without any retail subscribers and Netia intends to integrate it with its existing network and offer similar TV, broadband and fixed voice telephony services as are offered over its copper and fiber networks. According to the agreement, the possible purchase price for Centrina and Dianthus will be between PLN 6,000 and PLN 21,000 and will depend on the number of customers Netia gains on the acquired network. At the same time Netia obtained a discount on pre-existing operational agreements with UPC with an estimated nominal value of PLN 16,412. Reflecting the substance of the transaction, the acquisition was accounted for in the consolidated accounts as a purchase of fixed assets and not as a business acquisition. The consideration transferred for the network purchased, including provision for an estimated additional payment of PLN 690 and related transaction costs, amounted to PLN 5,821. The value of fixed assets purchased is PLN 7,183 and the difference of 1,362 PLN relates to net liabilities in the purchased companies as at the acquisition date.

Mergers with subsidiaries

On September 30, 2013 Internetia Sp. z o.o. merged with its wholly-owned subsidiaries STI Sp. z o.o. and Sanetja Sp. z o.o. The merger was carried out through the transfer of the acquired company's assets to Internetia (merger by acquisition) without any increase in Internetia's share capital and without any share exchanges.

1.2 Information on basic products and services

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

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

Taking advantage of the opportunities arising from changes in the regulatory environment, the Company concluded a bitstream access agreement ("BSA") with Orange Polska S.A. (formerly Telekomunikacja Polska S.A. or "TP SA" until a name change made during 2013) and commercially launched its broadband Internet access services over Orange Polska SA's network in January 2007. During 2007 the Company began offering Netia voice services to Orange Polska SA customers including the arrangement whereby the customer pays a monthly fee to Netia as well as the hitherto call by call charges. Netia pays a line rental fee to Orange Polska SA under the Wholesale Line Rental (WLR) administrative decision issued by the telecommunications regulator (Urząd Komunikacji Elektronicznej, "UKE"). During 2008 Netia began to install its own equipment in the Orange Polska SA network nodes using a form of regulated access called Local Loop Unbundling (LLU) and began connecting customers using this form of regulated access.

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

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

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

Netia introduced IPTV services into its offering during 2011 and is gradually upgrading its copper and Ethernet access networks using VDSL and fibre to the building (FTTB) technology to deliver faster broadband. Since mid-2012 Netia has been providing streaming TV and content services based on the adaptive IP content wherever possible in preference to IPTV based services.
In December 2011 Netia acquired Telefonia DIALOG S.A. ("Dialog",which was transformed into Telefonia DIALOG Sp. z o.o. on April 30, 2012) with its subsidiaries Avista Media Sp. z o.o. ("Avista", merged with Dialog in July 2012) and Petrotel Sp. z o.o. ("Petrotel") (together, the "Dialog Group") and Crowley Data Poland Sp. z o.o ("Crowley", later CDP Netia Sp. z o.o., merged with Netia in August 2012), two other Polish alternative operators, which increased materially the size of the Netia Group. Dialog and Petrotel provide a similar range of telecommunication services to Netia and serve business and residential customers, including mobile services provided via a MVNO agreement with Polkomtel Sp. z o.o. Crowley was providing telecommunications services exclusively to business customers. Avista was providing call center services mainly for Dialog but also for some third party customers.

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

The Netia Group's revenues in 2013 and 2012 are presented below:

	Year ended December 31, 2013	Share in total revenues	Year ended December 31, 2012	Share in total revenues
	(PLN)	%	(PLN)	%
Direct voice, including:	809,188	43.1%	948,455	44.7%
Monthly fees	*588,397*	*31.4%*	*662,808*	*31.2%*
Calling charges	*220,223*	*11.7%*	*284,904*	*13.4%*
Indirect voice	19,203	1.0%	34,976	1.6%
Data	724,721	38.6%	765,658	36.1%
Interconnection revenue	85,288	4.6%	109,588	5.2%
Wholesale services	107,003	5.7%	136,242	6.4%
Other telecommunication revenue	122,189	6.5%	113,789	5.4%
Telecommunication revenues	**1,867,592**	**99.5%**	**2,108,708**	**99.4%**
Radio communication services	2,863	0.2%	3,540	0.2%
Other services	5,561	0.3%	9,108	0.4%
Total revenue	**1,876,016**	**100.0 %**	**2,121,356**	**100.0 %**

1.3 Sales market (not in thousands)

The Netia Group operates on the telecommunications services market with its predominant focus on fixed broadband, fixed telephony, FTA (free to air) and pay TV content distribution as well as mobile convergent offers. The sales market for these products has recently been becoming increasingly homogenous with multi-play integrated offers playing a major part in consumer preferences.

Following fixed telecommunications market liberalization in 2006 and introduction of services based on bit-stream access (BSA), wholesale line rental (WLR), and local loop unbundling (LLU) the Netia Group is able to offer internet access and voice services, nationwide, via the incumbent's copper network. In 2008 Netia acquired Tele2 Polska, a fixed line telephony operator mainly rendering services via WLR to its residential customers. In 2011 Netia further increased its scale through the acquisitions of Telefonia Dialog and Crowley Data Poland alternative operators, the first of which mainly operates on its own proprietary network in voice, TV and broadband segments as well as in WLR segment while the second operates mainly in corporate and SoHo/SME segment. All acquisitions contribute significantly to the Netia Group's attained scale of operations in the Polish telecommunications services market in both the residential clients and corporate customers' segments.

The fixed broadband services market increased from around 6.6 million services at 2012 year end to 6.7 million services at the end of 2013. The penetration of fixed broadband reached 48% of households in 2013 and is expected to continue to grow. Fixed line telephony services decreased from approximately 8.3 million lines at the end of 2012 to 7.9 million at the end of 2013 and is continuing to shrink. The penetration of fixed line telephony in Poland was approximately 57% of households at the end of 2013. The pay TV market in Poland is on the same level as last year (11,8 million) services, mainly dominated by cable and satellite DTH ("DTH") offerings.

Although some market share has been lost during 2013, the Netia Group maintained its position as the leading alternative for broadband services to the national telecom operator (Orange Polska SA). The Netia Group's broadband subscriber base decreased to 848,909 at December 31, 2013 from 874,778 a year earlier. The Netia Group estimates that its share of total broadband market subscribers has decreased from 13,3% to 12,7% during the past twelve months. Furthermore, at December 31, 2013 the Netia Group had 1,488,610 fixed line telephony subscribers of which 43% were connected over own proprietary networks, while 728,693 were served over WLR access and 121,312 were served over LLU voice over IP. The Netia Group estimates that its share of total fixed voice telephony market has decreased from 19.8% to 18,8% during the past twelve months. The loss of market-share is for the most part due to a 2012 Management decision to stop aggressively marketing WLR and BSA services to new customers due to falling margins caused by market retail price reductions, making such expansion no longer economically attractive. Instead Management is focused on the retention of the previously acquired WLR and BSA base plus expansion of services provided directly over the Netia Group's own access network or over LLU.

The Netia Group has its own access networks built out in areas covering approximately 16% of households in Poland. At the end of 2013, Netia served 402,140 broadband customers using the wholly owned copper, Ethernet and fiber networks. The country-wide backbone network and the ability to upgrade the existing access network allows the Group to broaden its operations, simultaneously obtaining independence from the networks of other operators and the regulatory regime. Simultaneously, the Netia Group continues to invest significant capital expenditure into a modernization of its own copper and Ethernet networks converting last miles into NGA ("Next Generation Access") standard allowing the customers to receive high speed broadband and attractive TV content. As of December 312013 the Netia Group had approximately 1,281 thousand homes passed on NGA networks including Telefonia Dialog (PON, FTTB, VDSL). Cumulatively, the Netia Group had circa 1,7 million TV ready homes passed (IPTV and streaming TV) where it can render 3play services.

As of December 31, 2013, Ethernet networks acquired by the Netia Group since mid-2007 provided broadband access to a total of 110,754 mostly residential customers with approximately 621 thousand homes passed in total. During 2013 the Netia Group hasn't acquired any Ethernet networks as Netia is currently focused on upgrading Ethernet networks to NGA standards already acquired and will therefore likely acquire new networks at a much slower rate than seen in the past.

At the end of 2013 Netia provided TV services to 120,321 customers as compared to 79,285 customers as at December 31, 2012. The Netia Group constantly expands its TV offering with new content and functionalities and additionally upgrades its own access networks, including NGA upgrades on own copper network ("VDSL") and Ethernet networks ("FTTB"), with a view to develop the offsetting revenue stream from 3play services (voice + broadband Internet + TV) for its Residential customers. The TV services are rendered by Netia both in IPTV and smooth streaming technology, which expands the availability of its 3play bundle offer outside the IPTV network, combining high quality of TV signal with lower bandwidth requirements.

Netia had over 700 unbundled nodes at December 31, 2012, passing nearly 5 million homes. Netia served 169,912 customers over LLU as at December 31, 2013 as compared to 182,726 at December 31,2012. The total LLU subscriber base includes 119,199 gross customers migrated from lower margin bit-stream ("BSA") services.

The Netia Group runs its operations within one geographical area, that is the territory of Poland.

The Netia Group renders its services both to corporate and residential customers.

1.4 Development perspectives for the Netia Group's operations

Growth prospects (not in thousands)

Following the acquisitions of Telefonia Dialog and Crowley Data Poland in December 2011, the Netia Group increased its scale of operations by over 30% in terms of revenues and more than 40% in terms of total services. Moreover, with an ambitious amount of synergies being extracted from integrating operations, the Netia Group realized significant growth in operational profitability together with capital expenditure optimization and thus a progressive free cash flow increase (as a percentage of sales) in both 2012 and 2013.

However, while the integration synergies exceeded the preliminary estimates, delivering 98 million PLN of opex and capex savings already in 2012 and 219 million PLN cumulatively for the last eight quarters, the economic slowdown observed during 2012 - 2013 alongside tougher competition and pricing pressure from the competitors, especially in the Residential market segment, resulted in a weakening outlook for revenue, margins and the number of services (RGUs – Revenue Generating Units) in 2014 and beyond. In particular, the negative market trends were visible in 2013 in the fixed-line voice telephony, which had been experiencing customer losses due to fixed-to-mobile substitution, while the fixed-broadband market became relatively stagnant. The TV product line, though growing strongly, remains subscale and will contribute to top line and margin restoration only in the medium term. Deterioration of trading conditions was particularly noticeable in the off-network services, which suffered significantly from shrinking margins and from which Netia has retreated in terms of seeking to aggressively acquire new customers. As a result, Netia Group recorded a 12% drop in sales in 2013 and is guiding for a 7.5% decline in 2014 revenue versus 2013. Due to good cost control and increasing synergies from Dialog and Crowley integration, 2013 EBITDA fell by only 10% and Management is guiding for an f 8.3% decline in Adjusted EBITDA in 2014 while only a 1.9% decline in Adjusted operating free cash flow (Adjusted OpFCF) thanks to further capex optimization.

In order to respond to the above challenges, the Company is targeting 2014 as a year of continuous focus on greater on-network sales of higher speed broadband and TV services including streaming IP. Continuing the successful implementation of this revised commercial approach has the potential to stabilize financial performance of the Residential segment in the medium term. Given the on-going strong performance of the B2B segments (combining the Corporate, SME and Carrier sub-segments), Netia expects them to be the main growth engine in the nearest future and intends to focus strongly on developing services for its business customers.

Operationally Netia Group constantly expands its TV offering with a new content and functionalities and additionally upgrades its own access networks, including NGA upgrades on own copper network ("VDSL") and Ethernet networks ("FTTB"), with a view to develop the offsetting revenue stream from 3play services (voice + broadband Internet + TV) for its Residential customers. Thanks to the ongoing infrastructure upgrade the Netia Group offers from late 2011 a competitive Internet Protocol Television ("IPTV") product and Video on Demand ("VOD") to complement the offering grid. Furthermore, in mid-2012 Netia introduced smooth streaming technology, which expands the availability of its 3play bundle offer outside the IPTV network, combining high quality of TV signal with lower bandwidth requirements. The existing backbone network together with access networks in all major Polish cities and towns country-wide empowers the Netia Group to deliver a full package of 3-play services in most locations once the NGA upgrade is completed. As at December 31, 2013, the Company covered in total 1.3 million households with its NGA networks. Moreover, Netia Group covered in total 1.7 million TV ready homes passed within its network coverage based on versatile access technologies. Combined with the recent acquisition of former-Aster cable HFC network comprising over 446k NGA and TV ready HPs, the Netia Group will reach approximately 1.7 million NGA homes passed and 2.1million TV ready homes passed in its proprietary network coverage by the end of 2014. Management's priority in this area is to increase our customer base penetration with multi-play services, including TV and over-the-top ("OTT") solutions by both targeting new customers in our coverage areas as well as cross-sell to the existing customer base.

Selective access networks upgraded to NGA standard will facilitate new service portfolio development characterized in particular by a relatively higher profitability potential in future thanks to multi-play service uptake and increased ARPUs per customer and higher penetration rates. A key priority is to continue to boost the proportion of the customer base taking more than one service from Netia, especially in 3play packages, as this drives profitability through the proportionate reduction in back office expenses.

The second cornerstone of Netia's strategy is related to maintaining, and building whenever possible, its position in the Business segment. We will focus on the most attractive areas in the Corporate segment, aiming to improve profitability while limiting incremental capital expenditure. In the future Netia aims to acquire a higher proportion of data related contracts than has been achieved in the recent past in order to accelerate growth in the Corporate and SME market segments. In the Carrier segment the goal is to increase the utilization of existing capacity and other assets by selectively pursuing projects that require limited investment and which are considered a reasonable risk for the returns available.

A critical enabler for successful accomplishment of Netia's growth plans is the organizational culture. Management has defined such corporate values, in common to all New Netia employees, as trust, audacity, excellence and pride, by which we guide our work. Thanks to those values we aim like to build such Netia brand attributes as simplicity, inventiveness, value and passion. Netia's objective is to maintain a spirit of dynamism and proactivity at Netia, which will enable the Netia Group to effectively face the challenges posed by both the market and competitors.

Given the challenges faced on the residential market and the comparative strengths of the very different business market where Netia generates two-third of its cash flows. Management took the decision to reorganize the group around two divisions, Business-to-Business ("B2B") and Business-to-Consumer ("B2C") with effect from Q2 2014. Under this reorganization, previously Group-wide functions with customer-facing relationships are to be divided between B2B and B2C, supported by single network, IT and support functions. Management believes this change should lead to more focused teams delivering stronger commercial performance in both B2B and B2C whilst finding new opportunities for efficiency gains which had been largely exhausted under the previous functional structure. This project is called N2.

Network Infrastructure (not in thousands)

Continuous changes in the telecommunication market and expansion of Netia is client base, together with acquisitions of Ethernet ISPs, Crowley and Dialog networks results in dynamic development of Netia backbone network capacity. While use of modern technology allows to fully utilize the potential of Netia's own and leased fibre infrastructure, it also makes it possible to expand geographically.

Development of broadband access networks is realized both by capacity upgrades of existing BSA and LLU points of interconnect with Orange Polska S.A. and the construction of new point of interconnect enabling access to Orange Polska S.A. IP DSLAM-s. Until the end of

2011, Netia invested heavily in BSA extension and construction of LLU access nodes in the Orange Polska S.A. network. At December 31, 2012, 713 LLU nodes had been deployed and the roll-out was completed. This LLU network give Netia access to almost 5.0 million Orange Polska S.A. access lines Poland–wide. Implementation of modern technologies in LLU nodes enables delivery of advanced services requiring broadband access (i.e TV, VoD, VoiP, MPLS). Investments in regulated access has now been slowed down as the number of customers is no longer growing and, according to Management's analysis, all potentially profitable LLU nodes have already been rolled out.

Development of Netia's own broadband access based on copper infrastructure is focused on implementation of NGA (Next Generation Access Network) based on VDSL2 technologies allowing increase of bandwidth delivered to the customer by several times, up to 80Mb/s. Acquisition of Ethernet networks is followed by gradual upgrades of their infrastructure in terms of capacity delivered to access nodes required by modern services i.e. Streaming TV and in terms of enabling remote management and automatic service provisioning of new services in these networks. As a result of upgrades Netia Ethernet networks built in FTTB (Fiber To The Building) technology are able to deliver up to 100Mb/s capacity to each customer.

Netia will continue its plan of developing new and modernizing existing infrastructure of acquired Dialog Network based on VDSL and FTTH technologies. To strengthen market position, in parallel, Netia also develops infrastructure competencies around modern, IP based multimedia and communication services such as IPTV, VoD, CDN, etc.) dedicated to residential and business market. IP/MPLS core infrastructure acts as a common denominator for all delivery scenarios, unifies deployment process and lowers development and network maintenance costs. Essential part of our network development is concentrated on delivery of CPE dedicated to Netia customers Netia Spot (WiFi router) oraz Netia Player.

A key focus for 2014 will be the completion of a project to integrate at least 400k HP from the 446k HP of CATV access network acquired from UPC Polska Sp. z o.o. into the Netia core network. This is expected to enable Netia to launch commercially 2-Play and 3-Play offerings essentially identical to those being offered over Netia's VDSL and fiber networks. Commercial launch is expected in H2 2014, and provides a major opportunity to increase Netia's TV and broadband on-net customer base in two of Poland's richest markets, Warsaw and Kraków.

2 Major factors for the activities of the Netia Group

2.1 Major risks and threats related to the operational activities

Risk of changes to the Netia Group's strategy

On January 13, 2011 the Company announced the main assumptions of its new long term strategy spanning over the period until year 2020 ("Strategy 2020"). Financial guidance regarding the Strategy 2020 was announced at the same time in order to reflect Netia's long term plans for the further roll out of Local Loop Unbundling ("LLU") as well as the upgrade of select regions of ETTH and copper network to broadband speeds of 30MB and higher (Next Generation Access "NGA"). Following Netia's acquisition of two sizeable telecom assets – Dialog Group and Crowley – in December 2011, the key assumptions of strategic financial guidance until 2020 were confirmed. However pricing pressure and falling numbers of active services in the Home segment have resulted in Management modifying its strategy to focus more on own network services and to stop targeting annual RGU growth. Following completion of the planning round for 2014, the Netia Group has decided to withdraw all long term strategic financial guidance at least until the two new B2B and B2C divisions to be created by the N2 project have had an opportunity to update their plans. Nevertheless, the strategy 2020 remains valid as the Group's strategic direction but no assurance can be given that this will not change in the future. Furthermore, Netia may seek to introduce new elements to strategy that might materially change expected cash flows or modify the risk profile of the Netia Group.

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

Currently, Netia is not controlled by any strategic investors, and its shares are held by a large number of shareholders. Neither Netia's corporate documents nor the provisions of Polish law provide for any serious restrictions to changes in control over the Company in the event of third parties acquiring a considerable number of shares. Thus, such changes of control may materially affect the composition of the Company's Supervisory Board and the Management Board and, in turn, the strategy and business activity of the Netia Group. Due to the above, the Company cannot guarantee that any adopted strategy of the Netia Group will be pursued in accordance with its initial objectives.

Risk that changes to the organization of the Polish pension system introduced by the Polish Government may have a material impact on Netia's shareholder structure

Management estimates that to the best of its knowledge as of 2013 year end no less than 40% of its equity was held by Polish pension funds ("OFE"). On December 23, 2013 President of the Republic of Poland signed an act on changes in laws governing OFE providing, among others, for free choice for individuals to transfer their pension contribution to OFE or the Polish state pension fund ("ZUS") and prohibiting OFE to invest in bonds and other types of debt instruments (the bonds which were previously under OFE's management were transferred to ZUS on February 3, 2014). On January 31, 2014 President of the Republic of Poland directed the act on changes in OFE to the Constitutional Tribunal with a motion to investigate the conformity of certain articles with the Polish constitution. These legal changes might cause some or all of the OFE currently invested in Netia to make changes to their portfolio of the equity holdings that are currently difficult to predict. If such changes include significant changes to the ownership of Netia's equity, no assurance can be given that the new owners of such equity would continue to support Netia's existing strategy, the existing Management Board or Supervisory Board or the existing systems of corporate governance.

Risk connected with the impact of potential future takeovers and acquisitions of large-scale businesses

Revenues and financial performance of the Netia Group may be materially affected by takeovers of and mergers with other entities that operate large scale telecommunications businesses. Upon the Company's takeover of another entity, the process of fully integrating this entity may carry high risks, e.g. resignation of key employees, the loss of a certain segment of its customers or high costs of the entire integration process including the lack of certain portion of contemplated synergies to be extracted from the acquisition.

The already consolidating, however still relatively fragmented market of alternative operators rendering wire line telephone services may result in continuing consolidation within the Polish market. The Company intends to evaluate potential takeovers and acquisitions whenever such possibilities arise. The performance of such transactions requires the special involvement of the Company's high-ranking managers and may entail high costs connected with the identification and evaluation of the candidates for takeover, the negotiating of agreements and integration of the entities acquired. The Netia Group may require additional funding in order to conduct such transactions.

The benefits from potential takeovers will depend mostly on the extent to which the Netia Group is able to integrate the acquired entities into its structures. Future company acquisitions may entail acquiring existing liabilities and the risk of undisclosed liabilities. The Netia Group cannot guarantee that beneficial takeover possibilities will arise in the future, nor, if such possibilities arise, that they will result in the successful integration of the acquired entities with the Netia Group. Failure to integrate the acquired entities into the structures of the Netia Group and / or the failure to generate the expected operating and strategic synergies may adversely affect the operations and financial standing of the Netia Group.

Specific risks associated with the acquisition of Dialog S.A.

In addition to general risks inherent in acquisitions of businesses of significant scale relative to the buyer, the acquisition of Dialog is associated with certain risks specific to this integration:

- Full integration will require migration of Dialog billing and customer relationship management systems onto the Netia platform. This process is expected to take until Q2 2014 and certain material operational synergies are dependent on this migration being successful. Problems with the migration might lead to problems with billing and customer service for all or a significant part of the customer base.

- Significant elements of Dialog's network are located on leased premises and notice of termination by the landlord was received during 2013. As a result, during 2014 Dialog will incur significant costs to relocate or replace the affected infrastructure and the migration process represent an increased risk of service disruption.

Management can give no assurance that one or more of the above risks may not result in the Netia Group suffering significant additional costs or reduced cash flows.

Technological risk

The telecommunications sector is an area witnessing dynamic technological changes. In designing and expanding its networks, the Netia Group uses the latest technical solutions. However, it is not possible to predict how the Netia Group's operations may be affected by technological advances in the field of wireless, mobile transmission, voice services based on cable television telephony and multimedia services provided over Internet by third-party – OTT (Over The Top). In particular, the business activities of the Netia Group may be affected by the trend to provide voice and internet access services via wireless or portable platforms, with wireless broadband access and fourth generation mobile cellular telephone systems equipped with IP. Due to the difficulties in predicting future regulatory environment and exact market potential, Netia may sometimes invest in technologies that ultimately do not deliver the expected returns. When such a situation occurs, it can have a negative impact on our results and financial condition.

Risks related to the uptake of new services and the financial returns available from investment in upgraded networks

Since 2011, Netia has been upgrading broadband speeds to its copper and Ethernet ("ETTH") networks and adding television and content services to its offering. Whilst these investments have delivered promising results, no assurance can be given that these upgrade investments will deliver a satisfactory financial reurn.

The speed of roll-out and relative performance of fast mobile broadband networks (such as HSDPA and LTE), the speed of upgrade of cable networks and the incumbent's own investment plans is likely to have a significant impact on the relative attractiveness of our broadband and television offers and sales results. Furthermore, our content services may turn out to be inferior to those of key competitors and we may not be able to meet sales targets or ARPU targets as a result.

Risk associated with property rights

In order to deliver services to its customers, Netia owns, leases or uses properties through "rights of way" easements. In some cases the property rights are unclear or Netia may be unaware of the defects in the property rights used by the Company and Management can give no assurance that legal issues or challenges will not occur from time to time. This may result in Netia incurring significant costs to protect its rights or to move its infrastructure. Similarly, the leases may unexpectedly be cancelled by lessors with the result that Netia incurs significant expenses to relocate its network elements.

Foreign currency risk

Approximately 30% of Netia's annual capital investment programme and up to 10% of typical operating expenses are either invoiced in foreign currencies or are invoiced in Polish Złoty based on price lists expressed in foreign currencies. Netia operates a Risk Management Committee that decides, from time to time, to hedge these exposures to foreign currency risks and if so, the proportion of the exposure to be hedged. Whilst Netia's hedging activities are designed always to reduce Netia's exposure to earnings volatility through changes in exchange rates (i.e. Netia does not speculate), we can give no assurance that entering into hedging transactions will result in higher earnings or cash-flows than if we had not hedged the Company's currency exposures.

Interest rate risk

Netia's long term borrowings are all Polish Zloty denominated and the interest paid depends on floating WIBOR rates and a margin that is dependent on the Netia Group's financial leverage. To mitigate the risk of higher WIBOR rates leading to worse financial results, Netia's Risk Management Comitee may decide to swap some or all interest rate risk into fixed rates coupons. Whilst Netia's hedging activities are designed always to reduce Netia's exposure to earnings volatility through changes in interest rates (i.e. Netia does not speculate), we can give no assurance that entering into hedging transactions will result in higher earnings or cash-flows than if we had not hedged the Company's interest rate exposures.

The level of profits and distributable reserves in Netia S.A. may differ materially from those of the Netia Group

With the acquisition of Dialog Group and Dialog Sp. z o.o. in particular, the Netia Group has acquired a material profitable subsidiary that Netia does not intend to merge into Netia S.A. over the medium term for operational reasons. As a result, projections show that a significant part of the Netia Group's earnings will accrue to Dialog Sp. z o.o. and that Netia S.A. operating profits shall be materially below those of Netia Group as a whole.

In these circumstances the level of distributable reserves in Netia S.A., which stood at PLN 376,937 on December 31, 2013 and the result for the year for Netia S.A. which was a profit of PLN 225,004 in 2011, a loss of PLN 94,175 in 2012 and a profit of PLN 30,724 in 2013, are likely to diverge from those of Netia Group as a whole. Whilst Netia shall take reasonable steps to ensure that profits and cash flows flow up to the parent company over time, Management can provide no assurance that Netia S.A. will always be in a position to pay a dividend or make other distributions to shareholders when the Netia Group as a whole records a net profit for a given year as the commercial code provisions regarding distributions are applicable to the issuer, Netia S.A., and not to the Group as a whole.

Netia S.A.'s earnings have historically been highly volatile and continued volatility may inhibit the Company's ability to pay dividends in predictable amounts in the future

Net profits and losses of Netia S.A. have historically been very volatile with significant profits and losses recorded in different years due to various non-cash accounting issues that depend critically on Management's judgments about the Netia Group's future prospects. These non-cash accounting issues are principally:

- Annual impairment testing net book values of goodwill and non-current assets against Management's latest cash flow projections for the business,
- Estimates of future economic lives of non-current assets, which has a direct impact on the annual depreciation and amortization charges that constitute the Netia Group's largest single expense,
- Valuation of deferred tax assets, which is also critically dependent on Management's projections of future profitability.

Changes in the business, legal or regulatory environment can lead to material changes in Management's estimates and lead to material fluctuations in the above three non-cash items between years.

If Netia S.A. records a net loss in a given year this reduces distributable reserves and this may lead to Management being unable to recommend a dividend in respect of such a year. Management has in the past sought to mitigate this risk by requesting from shareholders a multi-year authority to buy back shares, which can be done, via an attractive tender offer, as an alternative to a traditional dividend. Management may seek to use this method of distributing funds to shareholders again in the future.

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

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

We depend on third party providers to provide services to our customers.

Our commercial performance depends partly on our ability to attract and retain our customers by providing high quality services and we rely on various third party providers for important elements of the value chain such as sales, customer activation, network maintenance, information technology development and certain customer care processes. If any of these third party providers fail to maintain the capacity and quality of the services that they provide to Netia, or fail or refuse to respond quickly to Netia's changing requirements, our customers may experience poorer service which could adversely affect the perceived reliability of our services and, therefore, adversely impact our brand, reputation and market share. From time to time, in order to mitigate such risks, we may seek to change key third partner providers or to insource the services they provide, particularly where such services are provided by resources that Netia previously outsourced to a given third party provider. Changes of such scale entail significant operational risks and Management can provide no assurance that, in the event of poor performance by a thrid party provider that necessitates a significant reorganization of the way that the Netia Group delivers its services to customers, that material costs or material deterioration in commercial performance due to the disruption that results will not occur.

Risk resulting from processing personal data in ongoing activities of Netia Group's companies

In connection with providing telecommunications services and basing on the terms set in the relevant provisions, in particular in the Polish Telecommunication Law and in the The Act on the Protection of Personal Data, companies of the Netia Group process the personal data of the subscribers. Regarding authorization coming from the law and the consents of the subscribers, the processing of the personal data is a part of the ordinary activity of the companies of the Netia Group.

Despite the fact that the companies of the Netia Group use the measures to protect the client's personal data with the utmost care and in the accordance with the requirements of the applicable law, such cases as the risk of the human error, the intentional act of the third party, the technical failure or another special circumstances may occur, so it cannot be foreclosed that the data would be exposed and consequently also used inappropriately, what would lead to the breach of the law.

We cooperate with external, independent from the Netia Group, enterprises and contractors, suppliers, call centres and despite the utmost care of the companies of the Netia Group in the selection of the business partners it cannot be assured that within the scope of the supplies of that partners would not occur events which may expose and consequently, also inconsistent with the provisions of the law use of that data.

Breach of the law on the protection of the personal data of the subscribers by the companies of the Netia Group or by one of our partners may result in imposing the financial penalties, damage of the reputation and worsen the commercial results of the Netia Group.

Risk resulting from changes in the Telecommunications Law

The current Telecommunications Law came into force on September 3, 2004, except for certain regulations that came into force on January 1, 2005 in result of implementation of so-called "2002 directives package". On July 6, 2009, the act on the amendment of the Telecommunications Law and other acts entered into force. The purpose of the above-mentioned amendment was to further harmonize Polish provisions with the legal framework of the European Union.

A further amendment of the Telecommunications Law entered into force on July 20, 2010. According to this latest amendment, the definition of "subscriber" was changed, so that it now covers also users of services who have not concluded a written contract for the provision of telecommunications services. After the entry of this law into force, the obligations of telecommunications undertakings with regard to the conclusion, amendment, and performance of contracts apply to these users as well. Netia, as well as other telecommunications entrepreneurs, was obliged to adjust its standard client contracts to the new requirements within six months following the entry of the amendment into force.

On June 2, 2011, an amendment of the Telecommunications Law came into force, with regard to provisions concerning rules for verification whether fees for telecommunications access calculated by an operator with significant market power on the basis of justified or incurred costs are correct.

Pursuant to the amended law, as far as imposition of obligation to set fees on the basis of justified costs is concerned, in the absence of the auditor's opinion on the consistency of an annual regulatory accounting statement and the results of cost calculation with the binding regulations, or in case of a negative opinion or a qualified positive opinion, as well as in case of occurrence of significant discrepancies between the amount of fees calculated by an operator and established by the President of UKE on the basis of an auditor's opinion, the President of UKE establishes the amounts of fees for telecommunications access or their maximum or minimum levels, using methods specified in a decision designating an operator as holding significant market power and imposing an obligation to calculate fees for telecommunications access taking account of justified costs recovery.

As far as obligation to calculate fees on the basis of incurred costs is concerned, in a decision designating an operator as holding significant market power the President of UKE specifies methods of verification and calculation of fees. In order to verify whether the fees set by an operator on whom an obligation to calculate fees on the basis of incurred costs was imposed are correct, the President of UKE may apply the methods of fees verification specified in this decision. If the executed verification reveals that the amount of fees set by an operator is incorrect, the President of UKE establishes the amount of fees or their maximum or minimum level taking account of the promotion of efficiency and sustainable competition as well as the assurance of maximum benefits for end users. The fees shall be established in a separate decision.

Management Board is unable to assure neither that application of the amended regulations will not affect the costs of activity of the companies from the Netia Group, nor that whether – and when, as well as in what way – it will ensure the change of the amount of fees for telecommunications access to be borne by Netia after the end of this period.

On December 4, 2011, the amendment of the Telecommunications Law entered into force pursuant to which premium rate services providers were obliged, inter alia, to provide their subscribers with the right to block access to these services free of charge. On May 4, 2012 new regulations have entered into force obliging the providers of these services to inform subscribers that the limit of payments due for such services that was established by them in their contracts was exceeded. The Management Board is unable to assure that the regulations after coming into force will be uniformly interpreted by the regulatory bodies and that this interpretation will allow for provision of premium rate services without requiring increase of costs of adjustment of the companies from the Netia Group to the obligations stipulated therein.

On July 17, 2010 the act „for the support of the development of telecommunications networks and services" (hereinafter referred to as "the Act on Development") entered into force. One of the goals of the act is to improve the investment process in telecommunications infrastructure. It authorizes municipalities to construct infrastructure and telecommunications networks, to make it available, and to provide telecommunications services in areas where the demand of end users is not satisfied by commercially provided access to telecommunications services. In such a case, subject to consent of the President of UKE, Internet access services can be provided for prices lower than market prices, and even for free, if the provision of services in a given area under such preferential conditions will not lead to a distortion of effective and equal competition.

Furthermore, if in order to satisfy group needs of the municipal community, the making available of the infrastructure and provision of services is entrusted to a telecommunications entrepreneur, and due to economic conditions the performance of this activity in a given area will not be financially profitable, the entrepreneur may use the municipal infrastructure for fees that will not recover its full construction cost. The cost borne due to the provision of telecommunications services in that area can be partially co-financed by the municipality.

The Act on Development imposed the following obligations on the selected groups of entities:

- real estate owners, real estate perpetual usufructuaries and real estate administrators – the obligation to ensure access to the building as well as to the place in a building in which the cables supplied to the premises in the building are gathered; the access is to be ensured in order to ensure telecommunications and to the benefit of telecommunications entrepreneur which supplied the building with the public telecommunications network;

- owners of the telecommunications ducts situated on the real estate or in the building – the obligation to make the telecommunications ducts accessible for telecommunications undertaking which has no possibility to use another, existing telecommunications ducts;

- owner of telecommunications cable supplied to or distributed within the building – the obligation to make the whole or a part of this cable accessible for telecommunications undertaking in case the supply of another telecommunications cable to the building is not possible;

In case no agreement describing the conditions for access to the infrastructure is executed, the President of UKE may, upon a motion of any of the parties, issue a decision substituting the agreement.

The Management Board is unable to assure that the agreements on the access to infrastructure, concluded by companies from the Netia Group in the scope of ownership rights to the cable and ducts infrastructure as well as the rights concerning real estate, will be in each case established with interested telecommunications undertaking in accordance with the principle of freedom of contract, without the necessity to settle the technical or financial conditions of co-operation by the President of UKE.

Under the Act on Development the President of UKE is also authorized to issue a decision obliging an operator authorized to use assigned frequencies in an area indicated by the President of UKE in a specified manner.

The Act on Development introduces the possibility of new sources of competition for Netia from municipalities and other interested entities and the risk of overbuild of our existing networks.

On October 12, 2012 Sejm passed an amendment to the Act on Development, also amending the Telecommunications Law in the area of co-usage of infrastructure. The amendment came into force on December 16, 2012. The aim of the amendment is to streamline the process of building telecommunication networks, in particular regional broadband networks and sharing real estate and buildings in order to install telecommunication infrastructure, but the amendment introduces more rigorous conditions that determine exercising obligation of gaining access to the real estates and the existing connections and the telecommunication infrastructure in the buildings by operators. New regulation amended also other Telecommunications Law regulation, regarding access to the infrastructure.

The Management Board is unable to assure that, in spite of intentions of legislator to facilitate investment process, the changes to the provisions will not cause opposite effects and will not cause difficulties in constructing telecommunication networks and the use of infrastructure belonging to other entities.

On November 16, 2012, the Sejm passed amendments to the Telecommunications Act and some other acts including the Act on Development (hereinafter referred to as "Amendment"), aiming to implement the amendments of the 2002 Directives package, that entered into force in the EU in December 2009 and were to be transposed until May 2011. Most of the new regulations came into force on January 21, 2013. The Amendment, among other issues, forbids to enter into a first agreement to provide telecommunications services for private persons longer than 24 months and obliges telecommunications entrepreneurs to extend their offer addressed to end users to include no longer than 12 month contracts. The Amendment allowed to conclude contracts electronically using the form available on the website of the service provider. At the same time the Amendment broadens the obligatory content of contract for the provision of telecommunications services, and creates obligations with regard to network safety, including the prevention of unsolicited communications (spam).

Telecommunications undertakings were required to adjust the conditions of the contracts, including these stipulated in rules and regulations concerning the provision of publicly available telecommunications services or in price list of telecommunications services within 5 months of coming the Amendment into force, i.e. until June 21, 2013.

The Amendment regulated also specified principles of responsibility of telecommunications undertakings for delay in number portability or for number portability incompatibly with the will of the subscriber. In case of porting the number breaching the deadline established in Telecommunications Law, the undertaking that the subscriber is terminating the contract with , is obliged to pay the compensation in the amount of ¼ of the total monthly fees calculated according to the bills for the last three settlement periods, unless the impossibility to port the number occurred due to the reasons related to IT system managed by the President of UKE. In case when the porting the number has not occurred due to the reasons related to the current service provider, he is entitled to reimbursement of paid compensation in whole or in part from the entity responsible for the delay. In case of porting the number without consent of the subscriber, the subscriber is entitled to compensation from the new service provider in the amount of ½ of the average monthly fees calculated according to the bills for the last three settlement periods for each day from the activation of the number in the new network.

The Management Board is unable to assure that regulation on principles of responsibility of undertakings who take part in number portability process, will not cause the abuse of these regulations, and in effect will not became the grounds for disputes related to enforcement of claims, including recourse claims between operators or service providers, rising from possible faults in realization of subscriber right to port numbers.

The Amendment also introduces new obligations regarding protection of telecommunications secrecy, network security, including acting against distribution of unsolicited content by service users. It excludes the obligation of the President of UKE to assign undertaking obligated to provide universal service. This competence now depends on decision of the President of UKE, based on the evaluation of availability, quality and affordability of the set of universal services in a given area. In case of lack of offers which met the conditions of contest for the undertaking assigned to realize the obligation to provide universal service or individual services, the President of UKE will assign a telecommunications undertaking providing such service or services, taking into account its economic and technical ability to provide these services on given area, ensuring availability of services and the need to support the fair and effective competition. In the decision obligating to provide universal service the President of UKE can impose on assigned undertaking an obligation to apply special tariffs for this service, maximum prices or unified tariffs.

The Management Board is unable to assure that none of the companies of the Netia Group will be obligated to provide universal service on any area of Poland and, in that case, that such company will not be forced to provide such service on unprofitable conditions requiring financing the cost of provided universal services, on given area until reimbursement of such cost in the amount of subsidy determined by the President of UKE in other decision.

In addition, the Amendment granted the President of UKE new competence to establish in a decision imposing obligation to provide conditions of access to the infrastructure, set forth therein, in case of need to ensure effective competition. The Amendment obligates telecommunications undertaking being the addressee of such decision to provide access to infrastructure under conditions which cannot be worse than conditions set forth in such decision. In case when the contract for access to the infrastructure will not be concluded within 30 days of filing the motion for access to the infrastructure, the President of UKE, acting ex officio or in effect of filing the motion, can issue decision which replaces the contract, as was possible before the Amendment.

In the Management Board opinion the real market needs determined by state of development of effective competition, most of all require interference of the President of UKE in the purpose of enforcement of telecommunications access related to regulated services, provision of which is obligation the telecommunications undertaking holding SMP position on relevant markets. The Management Board is unable to assure that any of the companies of the Netia Group will not be obligated to provide access to its infrastructure under unprofitable conditions.

Moreover, the Amendment reduces the data retention period to 12 months, increases the information obligations with regard to subscribers as well as extends the obligation to transfer data concerning telecommunications activity of a given telecommunications undertaking to the President of UKE. The Amendment also extends the obligation to provide facilities for disabled persons onto all telecommunication undertakings,

On August 29, 2013 Ministry of Administration and Digitalization published draft of the "Regulation of the Minister of Administration and Digitalization on the specific requirements for providing facilities for people with disabilities by providers of the public telephone services". The draft of the Regulation provides for a number of new obligations on all of the public telephone services providers, associated with providing facilities to the people with disabilities. KIGEiT and other chambers of commerce associating telecoms indicate the redundancy of the proposed facilities, which in case of the final incorporation into the Regulation may result in increase of the cost of providing telecommunication services, also by the Netia Group. At this stage of works, the Management Board cannot foresee the final provisions of the Regulation and whether exercising obligations set in the Regulation may increase the cost of providing services, and if so in what amount, for the Netia Group.

The Amendment. also changed the rules of calculating (and provided increase) of maximum rates for the use of radio frequencies, however draft government regulation setting realistic rates do not provide a significant increase in relation of frequencies used by the companies of Netia Group.

The Management Board is unable to assure that in the future rates for the use of radio frequencies by the companies of the Netia Group will not increase by a larger amount nor that the amended rules for establishing the fees for extending the reservation of frequencies will not cause increase cost of provided services related to the frequencies used by the companies of Netia Group on the base of reservation which will require in the near future extending for the further period of time. The Management Board believes that most of the changes described above are likely to result in increased costs of running the business for the Netia Group.

In September 2013 consultations on the "Regulation of the European Parliament and of the Council laying down measures concerning the European single market for electronic communications and to achieve a Connected Continent, amending Directives 2002/20/EC, 2002/21/EC and 2002/22/EC and Regulations (EC) No 1211/2009 and (EU) No 531/2012" (the Regulation, prepared by the European Commission) were carried out in Poland. According to the draft Recommendation the aim of the proposal is creating a Single Market for the electronic communications, the development of competition and an increase in telecommunication investments in the EU. Achieving those aims is planned by: introducing "Single EU authorization", i.e. authorisation in the host Member State of the paneuropean electronic communication provider that allows to provide services in the whole EU without any additional authorization, and also introducing the new regulatory obligation of the smp electronic telecommunication provider, i.e. "European virtual access product" that, with the discretion of National Regulatory Authority, may be used in place of existing wholesale obligations of NGA networks. The Regulation also introduces, for every electronic communications provider, new obligation of providing Assured service quality (ASQ) connectivity products. The Regulation also introduces regulations protecting end-users.

The draft Regulation provides for its entering into force on July 1, 2014. In case of issuing the Regulation, it would have a direct effect in the legal systems of the EU Member States.
At this stage of work on the Regulation and other regulations concerning Single Market, including updating of the Recommendation on relevant markets, currently under preparation by the European Commission, the Management Board cannot foresee whether and when the new rules will come into force and what will be their final provisions. Consequently the Management Board cannot foresee whether the drafted regulations may cause an increase in costs or otherwise create new commercial risks for the Group and, if so, in what order of magnitude.

On January 15, 2014 The Government Committee for Digitalization adopted a draft regulation on complaints about telecommunication services.

On January 17, 2014 the Government sent to the Parliament a draft of the bill on consumers rights, changing the permissible modes of concluding contracts with consumers away from business premises.

Both abovementioned regulations, in case of their entry into force, would force all operators, including the companies from the Netia Group, to adapt to new regulations over the process of concluding contracts with consumers and formulating standard contracts. At this stage of the legislation process, the Management Board cannot foresee whether the draft regulations will come into force and whether the costs of adapting to the permissible modes of cooperation with consumers under the new regulations will be high.

The government is also working on a draft statute on the local self-government and some other regulations, amending the definition of the building in the meaning of the property tax law. These changes may result in cables constituting part of Netia's network being qualified as buildings and become subject to significant annual property taxes. Such a change, if implemented, would materially increase the taxes and fees position in Netia's operating expenditures.

At this stage of the legislation process the Management Board cannot foresee whether the draft regulations would come into force and whether they would raise operating of costs of companies of the Netia Group.

Risks resulting from the obligation to provide universal services

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

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

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

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

Following Orange Polska S.A. requesting the Regulator to reconsider cases commenced with issuing the above decisions, on September 7, 2011, the President of UKE upheld the decisions awarding subsidies towards incurred costs of universal service for years 2006-2009.

On January 10, 2012, the President of UKE issued decisions by virtue of which Orange Polska S.A. was awarded subsidies towards incurred costs of several services falling within the scope of universal service for 2010 amounting to PLN 55,102 due to provision of facilities for customers with disabilities as well as provision of telephone services with use of public pay phones. Following Orange Polska S.A. requesting the Regulator to reconsider, this decision was upheld on April 11, 2012.

Orange Polska S.A. appealed the decisions of the President of UKE to the Voivodship Administrative Court (further "WSA"). WSA dismissed the complaints of Orange Polska S.A. against the decisions granting the subsidies towards costs of provision of universal service in 2006 – 2010 and Orange Polska S.A. has appealed the WSA decisions to the Supreme Administrative Court (hereinafter "NSA").

On December 5, 2013 NSA repealed the judgments of the WSA dismissing the appeals granting Orange Polska S.A. subsidies for the years 2006 and 2007 and remanded the both cases for reconsideration to the WSA.

(All amounts in thousands, except as otherwise stated)

The Management Board is convinced of the validity of the issued decisions, but cannot assure that the Orange Polska S.A. appeals will be dismissed and that the awarded subsidies shall not be increased.

Jointly, Orange Polska S.A. was awarded the total amount of PLN 122,096 for the provision of universal service within the years 2006-2010.

On April 5, 2013, the President of UKE issued a decision dismissing the motion for granting subsidy towards costs of provision of universal service in the period from January 1, 2011 till May 8, 2011.

On June 29, 2013 Orange Polska S.A. filed for re-consideration of the case. On September 20, 2013 the President of UKE, after re-consideration of the case, issued a new decision granting Orange Polska S.A. subsidy towards costs of provision of universal service in 2011 amounting to 14,903 PLN.

On October 21, 2013 KIGEiT appealed against the abovementioned decision to the WSA. While the Management Board is convinced of the defective nature of the issued decision, it cannot assure that the decision will be repealed by the WSA and that a subsidy for 2011 shall not be finally granted.

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

The total amount of potential obligation of Companies of the Netia Group, estimated by the Management Board taking into account their market shares in 2006 – 2011, decisions of the President of UKE, in which the amounts of subsidies towards the costs of providing universal service in years 2006 – 2011 were granted in the total amount of PLN 136,999 and estimated amount of potential subsidy to the cost of USO, is PLN 7,006. The Companies of the Netia Group have made a provision for this amount to cover potential obligations under the subsidy for universal service provided in the years 2006 – 2011.

Should Orange Polska S.A. prevail in any of the aforementioned litigation, the USO liability in respect to 2006 – 2011 could still rise materially above the amount provided to date.

On the basis of the full amount of subsidies claimed by Orange Polska S.A. and of the Company's estimations concerning revenues of telecommunications services providers that may participate in subsidies towards universal services, the amount of subsidy towards universal service that might conceivably be claimed by Orange Polska S.A. from the Netia Group amounts to approximately PLN 54,002 for the period from 2006 until 2011 inclusive as follows:

	Maximum subsidies	**Provision**
	PLN	*PLN*
2006	6,293	34
2007	10,862	63
2008	9,202	80
2009	11,964	3,199
2010	13,888	2,840
2011	1,793	790
	54,002	**7,006**

Pursuant to the decision of the President of UKE designating Orange Polska S.A. to provide universal service the above obligation of Orange Polska S.A. expired as of May 8, 2011. To date no undertaking has been obliged to provide USO from May 9, 2011 onwards and, according to the published position of the President of UKE, will not be. Nevertheless, on October 16, 2012 the President of UKE began consultations on a new model of USO. At this stage of the Regulatory work on the model, the Management Board cannot assure that the President of UKE would not aim to change to a new model of USO, and in such a case that it would not be associated with additional costs to be incurred by Netia Group.

On January 28, 2014 the President of UKE commenced consultations of the Report "The status and the assessment of availability, quality of service and affordability of services included in the universal service".

No assurance can be also given that Management's best estimate of USO provision for 2006-2011 will be sufficient or that Orange Polska S.A. will not be successful in its appeal measures against decisions regarding subsidies for years 2006-2011 and the size of the subsidies will not be increased.

Risks related to holding a position of SMP

The President of the UKE issued the decision, whereby it has designated Netia, Dialog and Petrotel, as telecommunications operators holding significant market power in the market for call termination in its fixed public telephone network, in the area of the network where the termination is executed. At the same time, UKE imposed regulatory obligations that relate to:

- providing access to the network (including the use of network elements and associated facilities to the extent they are used to provide call termination services in the fixed public telephone network of Netia, Dialog and Petrotel),

- non-discrimination (obligation not to discriminate between telecommunications operators with regard to telecommunications access to the call termination services in its fixed public telecommunications network, in particular to offer the same conditions in comparable circumstances, as well as to offer the services and to provide the information on the conditions not less favorable than used within own enterprise or in relations with affiliates);
- transparency (comprising the publication of the information in matters concerning provision of telecommunications access with regard to the provision of call termination services in the fixed public telecommunications network of Netia, Dialog and Petrotel, on technical specifications of networks and telecommunications equipment, network characteristics, terms and conditions of the services and of the use of networks, as well as on the fees).

In the performance of the obligation imposed on Netia, Dialog and Petrotel, in the above mentioned decisions of the President of the UKE, Netia, Dialog and Petrotel published information on the conditions of telecommunications access with regard to call termination services in the fixed public telephone network of Netia by posting them on the internet site of Netia, at: http://www.netia.pl/files/netia_dla_korporacji/InterConnect/InterConnectoferta_ic_netii_28062013.pdf

Dialog at:
http://dialog.pl/sites/default/files/files/download/Informacja_w_sprawie_dost%C4%99pu_telekomunikacyjnego_do_sieci_Telefonii_DIALOG.pdf

and Petrotel at:
http://www.petrotel.pl/userfiles/file/regulaminy%20g%C5%82%C3%B3wne/UKE.pdf

The published documents contain information as required in the Decision of the President of the UKE, necessary for the preparation by the interested entrepreneurs of an application pertaining to the provision of telecommunications access with regard to call termination services in the fixed public telephone network of Netia, Dialog and Petrotel.

The President of UKE is obliged to notify the assessment of the market analysis to the European Commission not less often than every 3 years. Given that this period lapsed, the President initiated a procedure in the market for the termination of calls in Netia's, Dialog's and Petrotel's network, in order to evaluate whether there are reasons to uphold, amend, or waive Netia's, Petrotel's and Dialog's regulatory obligations.

No assurance can be given as to whether Netia, Dialog or Petrotel will not be obliged to perform some other duties set out in the Telecommunications Law imposed on a telecommunications operator holding significant market power in the market with respect to call termination services in the fixed public telephone network, or whether in the future a significant market power of another company of the Netia Group in this market is not determined or whether a significant market power of any company of the Netia Group in another wholesale market is not determined, as well as that any company of the Netia Group will not be subject to regulatory obligations specified in Telecommunications Law.

Interconnection rates depend on the policy of UKE

The President of UKE issued a decision amending the agreement between Netia and Orange Polska S.A. on interconnection of networks in which it established the level of asymmetry of rates for call termination on Netia's network in relation to the rates for call termination on Orange Polska S.A. 's network. According to the above-mentioned decision, rates for the services became symmetrical by January 1, 2014 in tariff period O1[1], i.e. business hours.

The President of UKE issued decision by virtue of which it established the rules of asymmetry for termination of calls in the Dialogs' network in relation to rates for termination of calls in the network Orange Polska S.A. and symmetry of those rates since January 1, 2014 in tariff period O1. Despite the fact that Dialog appealed against this decision to SOKIK, symmetrical rates for these services are applied by Dialog. Despite the fact that the Management Board is convinced of validity of the appeal, there is no certainty whether it will be accepted by the Court.

Orange Polska S.A. also appealed against this decision, demanding symmetry of termination rates or, alternatively asymmetry of termination rates differentiated in three tariff periods, instead of one tariff period. Despite the Management Board is convinced that there are no grounds for this appeal, there is no certainty whether it will be rejected by the Court.

Orange Polska S.A. filed an application to the President of UKE for amendment of rates for call termination in Netia's and Dialog's public fixed telephone networks by differentiation of the amounts of rates for each tariff period. The President of UKE by virtue of issued Decision refused the change of the Contracts pursuant to the applications of Orange Polska S.A. Despite the fact, that the decisions were issued in accordance with previous regulatory practice, the Management Board cannot assure that SOKIK will dismiss the Orange Polska S.A. appeals as well as decision refusing the change of FTR in Netia network and that the decisions will remain in force.

Orange Polska S.A. also filed with the President of UKE for the issuance of decision:
1) replacing the change of the contract on interconnection between Netia and Orange Polska S.A., by setting a flat rate for termination of calls of Netia's network in the amount symmetric to the rates of termination of calls in Orange Polska S.A.;
2) replacing the change of the contract on interconnection between Dialog and Orange Polska S.A. , by setting a flat rate for termination of calls of Dialog's network in the amount symmetric to the rates of termination of calls in Orange Polska S.A.;
3) replacing the change of the contract on interconnection between Netia and Orange Polska S.A. through making fees symmetric for use of Netia's infrastructure for the purposes of connection of the network to the fees for the use of Orange Polska S.A. infrastructure.

1 O1 – tariff period from 8:00 up to 18:00 on working days

By the virtue of decisions of June 21, 2012, the President of UKE dismissed the Orange Polska S.A. 's applications for setting flat rates for termination of calls to Netia's and Dialog's networks. Orange Polska S.A. has submited appeals against the President of UKE decisions to SOKiK. Netia and Dialog filed the court letters regarding Orange Polska S.A. appeals.

Orange Polska S.A. also submitted appeal against the decision of the President of UKE on conditions (and fees) of use of Dialog's infrastructure for the purposes of connection of the network. SOKIK dismissed Orange Polska S.A. appeal. However, the Management Board cannot assure that Orange Polska S.A. appeals shall not be successful and that the settlements rules set forth by the President of UKE will remain in force.

The Management Board believes that currently there are no grounds for application of rates for termination of calls in the networks of the companies of the Netia Group and use of their infrastructure for the purposes of the connection of the networks at the amount as claimed by Orange Polska S.A. One cannot assure, however, that the amount of these rates will not be changed in the future (by the decision of the President of UKE or court ruling).

Orange Polska S.A. has also filed with the President of UKE for the issuance of decision replacing the change of the contract on interconnection between Netia and Orange Polska S.A. which includes defining fees for number portability. Orange Polska S.A. has also filed with the President of UKE for the issuance of decision replacing the contracts for telecommunications access with Netia, Dialog and Petrotel in order to adjust interconnection rules to the current Orange Polska S.A. reference offer providing frame terms of telecommunications access with regard to calls initiation and termination, wholesale access to Orange Polska S.A. network, access to subscribers lines in the mode ensuring both full and shared access, as well as access to subscriber lines through telecommunications network loops intended for the purposes of sale of broadband data transmission services. In the course of negotiation both Netia and Dialog demanded inclusion in the negotiated contract regulatory obligations imposed on Orange Polska S.A., as well as the rules and conditions on telecommunications access which already exist on the grounds of contracts and decisions issued by the President of UKE. Finally Netia and Dialog concluded the agreement with Orange Polska S.A. ("SOR Agreements") which is limited to the Orange Polska S.A. services. The Management Board cannot assure that concluding the agreement will lead the President of UKE to the discontinuance of the proceedings.

Although the Management Board is convinced that statements filed in proceedings before the President of UKE started as a result of Orange Polska S.A. motions, were legitimate, it cannot assure that the conditions of telecommunications access related to each of regulated services, established in accordance with Orange Polska S.A. current reference offer will not be less attractive than conditions which are now in force. In particular, it cannot be assured that the President of UKE will lead to the discontinuance of the proceedings initiated by Orange Polska S.A. as groundless due to concluding the SOR Agreements and in the remaining scope will not issue decisions accepting Orange Polska S.A. motions and in such case, that terms and conditions of regulated services will not become less favorable and the costs of Orange Polska S.A. regulated services will not increase.

Risk of changes of UKE decisions and changes in UKE's approach to regulations

The conditions of performing telecommunications services by the Netia Group are in part set out in decisions issued by the President of UKE and most of them are immediately enforceable. The Management Board is unable to exclude the risk that the decisions will not be reversed or amended by the court nor that the terms of telecommunications access established therein will not be changed by the President of UKE during the period within which the Netia Group's companies make use of the regulatory conditions introduced by such decisions. The Management Board cannot assure, that in such a case, costs of providing services by the Netia Group will not increase and that operators providing wholesale services based on such decisions will not raise the claims against the Netia Group.

On February 1, 2012 a new President of UKE was appointed for a five year term of office and on April 15, 2012, a new Vice President of UKE.

On November 27, 2012 the President of UKE published the regulatory strategy for the term of office – "Regulatory Strategy until 2015" (hereinafter "Strategy"). According to the Strategy the main goal of the President of UKE is the improvement of service's quality and the development of new generation telecommunications infrastructure (NGN, NGA) of high bandwidth for the purposes of counteracting the digital exclusion and executing the Digital Agenda in relation to Poland. The President of UKE plans to execute its prerogatives stemming from Telecommunications Law, including in particular market analysis, in particular markets for call termination in each undertaking's network, the review of regulatory obligations imposed on undertakings and symmetry of fixed terminations rates (FTR) and mobile termination rates (MTR).

At this stage of realizing the strategy of the President of UKE, taking also into account the general area of interest of new President of UKE, it cannot be assured whether and to what extent in the period of time set forth in the Strategy the conditions of telecommunications access will be changed, as well as the obligations imposed on companies of Netia Group, in particular on markets for call termination on fixed networks. One cannot exclude the possibility that unless some of decisions issued by the President of UKE will lead to growth on fees for telecommunications access and new risks and challenges for the companies of Netia Group, not foreseen elsewhere in these risk factors.

Risks relating to the relationship between retail prices and regulatory access rates

On October 22, 2009 the President of UKE and Orange Polska S.A. signed an agreement laying down rules for the performance by Orange Polska S.A. of obligations with regard to telecommunications access ("The Settlement Agreement between the President of UKE and Orange Polska S.A. "). The Settlement Agreement provides that the fees for individual services in the scope of telecommunications access that follow from the applicable reference offers will be valid until December 31, 2012. This general rule in effect froze the cost of unbundled local loop services and wholesale line rental voice services.

On the basis of a draft understanding, constituting an appendix to the Settlement Agreement between the President of UKE and Orange Polska S.A., Netia and Orange Polska S.A. executed a separate understanding ("Understanding") on the December 23, 2009. The Understanding provides that the rates for specific services in the scope of telecommunications access, arising from reference offers, shall be binding until December 31, 2012. As the Understanding has not been noticed by any party, it was prolonged for unspecified period of time.

The wholesale rates for broadband access (BSA) were established at a fixed level taking account of retail prices in Orange Polska S.A. offer binding on October 10, 2009. Possible further decrease of rates established in the above manner, as well as wholesale rates paid to Orange Polska S.A. since implementation of new speeds to its BSA Offer, are controlled by a margin squeeze test („MS test") and price squeeze test („PS test"), rules for carrying out of which were established by the President of UKE ("MS/PS test").

Netia was surprised that Orange Polska S.A.'s new prices for the lowest transmission speeds somehow passed the margin squeeze tests carried out by the President of UKE. In view of the President of UKE's opinion that the Orange Polska S.A. retail offers examined with the use of the the MS test do not constitute price discrimination of Alternative Operators and may be used with the current wholesale fees for BSA services, i.e. the fees calculated on the basis of a "retail-minus" methodology but expressed in nominal values, Netia has had its costs verified by an independent auditor, and after simulating the margin squeeze test, using the audited costs. On the basis of the received outcome of the test it still seems surprising that the Orange Polska S.A. retail offers for the lowest transmission speeds should pass the margin squeeze test.

On February 9, 2011, the President of UKE published "The position of the President of UKE on the detailed methods of providing price squeeze and margin squeeze tests" (the Position) indicating amendments to the MS/PS Test procedure that were introduced after carrying out consultations with the market players.

Within the amended MS test procedure, an operator that passed his relevant cost data to the President of UKE for the purposes of carrying out of MS test is provided with access to information on average costs accepted for the test. After market launch of a retail offer that underwent the MS test, an operator that passed his relevant cost data to the President of UKE was also granted right to access data included in Orange Polska S.A. application for carrying out of the MS test, i.e.: the price accepted for the test, as well as the validity period of an agreement concluded on the basis of this offer. Upon motion of such an operator the President of UKE is obliged to carry out the MS test concerning Orange Polska S.A. retail offer one more time.

If the MS test outcome indicates that the relation between prices included in the retail offer launched into the market and wholesale rates applied by Orange Polska S.A. (regarding Orange Polska S.A. regulatory obligations) is discriminatory towards operators using wholesale services, then, according to the changed rules of MS test procedure, Orange Polska S.A. is obliged to withdraw this retail offer from the market. In case of non-performance of this obligation by Orange Polska S.A. prices set out in it will constitute a basis for calculation of wholesale rates on the basis of "retail-minus" methodology.

In the opinion of the Management Board, the amendments to the procedure of the MS test, comparing with the previously binding procedure, increase protection of operators using Orange Polska S.A. network, including Netia, against price discrimination.

Netia submitted to the President of UKE its cost data regarding the fiscal year 2010 for the purpose of MS test concerning examination of new Orange Polska S.A. retail offers. The submitted data are based on the results of the auditor's verification of the correctness of methodology applied for these costs calculation. The President of UKE considered them actual and reliable, accepted them and decided that they will be taken into account in the process of application to MS and PS tests. Similarly, Netia submitted to the President of UKE its cost data regarding the fiscal year 2011.The President of UKE considered them actual and reliable.

After having conducted with market participants subsequent agreements concerning the procedure of conduct of MS test, the President of UKE decided on January 24, 2012 not to introduce major modifications in the existing procedure. The introduced changes do not affect the rules for applying the MS test.

On June 22, 2012, the President of UKE published the Statement amending the rules of performing the PS tests. In the Statement President of UKE stated that in the process of analysis the Orange Polska S.A.'s retail offers which have no equivalent in wholesale regulated services, the Orange Polska S.A.'s wholesale costs shall be taken into account. In President of UKE opinion, such costs, as audited are reliable. KIGEiT communicated to the President of UKE that Orange Polska S.A.'s cost data relating to services that are beyond the scope of reference offer are in fact the projected costs and are not audited, while the alternative operators accessing the Orange Polska S.A. network should have guaranteed possibility at least to respond to the data projected by Orange Polska S.A. KIGEiT took legal actions to change the statement of the President of UKE, but in each and every case the President of UKE has refused to consider of KIGEiT's demands. KIGEiT has also submitted to the European Commission for intervention against changing MS/PS tests procedure without any consultation with Altnets, including Netia.

Although the Management Board is convinced of the validity of arguments taken by KIGEiT, the Management Board cannot assure that President of UKE shall amend its Statement published on June 22, 2012, and, in particular, that the President of UKE shall allow to verify the costs data used in PS test.

In January, 2013, the President of UKE launched the consultation of next amendment of statement on rules regarding MS and PS tests. The proposed amendments considered inter alia acceptable range of modification of Orange Polska S.A. retail offer tested with MS/PS test, which does not require retesting, conducting test on the grounds of Orange Polska S.A. data and deadlines for providing prices of new retail services.

KIGEiT, which participates in consultation, objects to the draft amendments of MS/PS test. The President of UKE didn't take into account KIGEiT's proposals and didn't introduce into the Statement proposals prepared by KIGEiT.

In March 22, 2013 the President of UKE published an amended Statement of the President of UKE. In the Statement the President of UKE confirmed that PS tests shall be performed basing on Orange Polska S.A. costs data. The President of UKE also accepted that Orange Polska S.A. shall not be obliged to file the motions for MS tests when the new retail offer is the modification of already existing offer. The President of UKE also stated that the PS tests result shall not be published.

Also on March 22, 2013 the President of UKE published the "Statement of the President of UKE in detailing the procedure of "Time to Market". The TTM is the process which serves in providing the new Orange Polska S.A. wholesale services, described in the Orange Polska S.A.'s reference offer. In the new TTM process the President of UKE introduced a new appeal procedure, which is applied in case when Orange Polska S.A. objects to the President of UKE statement regarding regulatory character of the new wholesale service. The President of UKE also limited the participation of alternative operators in the first phases of TTM. The President of UKE established also the dates of PS test in connection with dates of launching of Orange Polska S.A. new wholesale services to the market.

The Management Board cannot assure that TTM Process will sufficiently guarantee Netia's non-discrimination against Orange Polska S.A. regarding former Retail Arm of the Orange Polska S.A. and will allow Netia to introduce new retail services basing on Orange Polska S.A. wholesale services in the same time Orange Polska S.A. retail services are introduced into the market.

Between January 14, 2014 and January 28, 2014 the President of UKE carried out the consultation process of the Statement. A favorable draft change is being implemented by the Regulator in that only one PS test will be carried out for retail offer of the Orange Polska S.A., in case of the absence of the equivalent service in the Orange Polska S.A. reference offer, regarding the regulatory obligations which was imposed on Orange Polska S.A.

KIGEiT was active during the consultations process of the President of UKE Statement, submitting many proposals of amendments in the MS/PS test, in order to tighten up the rules of the allocation of the Orange Polska S.A. wholesale costs that are equivalent of the retail services provided in the Orange Polska S.A. bundles, including accounting rules and protection of the reasonable margin for the alternative operators.

The Management Board is also unable to assure that the MS/PS test procedures currently implemented and their possible future amendments will sufficiently guarantee Orange Polska S.A. price non-discrimination and effective protection against narrowing Netia's margin which can lead to loss of profits, cash flows or Netia market share. The Management Board is unable to assure that the President of UKE acceptance of Orange Polska S.A. retail offers on the grounds of MS/PS tests effects, and offering such services by Orange Polska S.A. will not cause loss of Netia's and Dialog' share in net connections and decrease of growth rate and thus will not cause risk of non-reaching our strategic and financial objectives.

On December 17, 2013, the President of UKE launched consultation process of the decision repealing regulatory obligations from Orange Polska S.A. (Orange Polska S.A.) on the market of providing part or the whole of the minimum set of the leased lines of 2 Mbit/s inclusive. The President of UKE draft decision is the consequence of repealing of the art. 47 of the polish Telecommunication Law which was legal basis of imposition on Orange Polska S.A. the regulatory obligations on the relevant market. The Management Board cannot assure the repealing of Orange Polska S.A. regulatory obligations won't negatively affect the conditions of the running the activity (in the providing the services with lower bit rates) by the companies of the Netia Group.

Risks related to amendments to reference offers

Beyond reach of Netia's own network, provision of telecommunications services by the Netia Group is conditional upon access to the network of Orange Polska S.A. According to the Telecommunication Law and the decisions of the President of UKE, having in mind regulatory obligations imposed on the Orange Polska S.A., Orange Polska S.A. is obliged to provide telecommunications access to telecommunications entrepreneurs, such as Netia, to its network and to offer frame terms and conditions of contracts on telecommunications access to its network for particular wholesale services, not worse than the terms and conditions specified in Orange Polska S.A. reference offers approved by the President of UKE.

On September 29, 2010, by virtue of a decision of the President of UKE, a new Reference offer providing frame terms of telecommunications access with regard to calls initiation and termination, wholesale access to Orange Polska S.A. network, access to subscribers lines in the mode ensuring both full and shared access, as well as access to subscriber lines through telecommunications network loops intended for the purposes of sale of broadband data transmission services, was introduced (hereinafter referred to as the "RO"). The RO laid down frame terms of contracts for all kinds of telecommunications services that are currently used by Netia under contracts and decisions issued upon reference offers. The RO superseded all currently valid reference offers, apart from the offer for the lease of telecommunications fibers.

The RO introduced new solutions to cooperation of network providers, so far not included in telecommunications access regulations, including:

1) unification of rules and timeframes of regulated services provision;
2) regulation of terms of broadband service access (BSA) with IP DSLAM technology;
3) introduction of electronic form of communication with Orange Polska S.A. in the form of IT System Interface into the network providers cooperation.

The RO also introduced significant increases in the fees for fixed line number portability.

KIGEiT and Orange Polska S.A. filed for re-consideration of the case concluded by issuance of RO.

Upon such reconsideration, on April 5, 2011, the President of UKE issued a decision by virtue of which it amended the RO by reducing several fees, i.e.:

a) due to LLU services provision, inter alia due to:

- connection of subscriber's line to Orange Polska S.A. network within launch of the Non-active Line - from PLN 63.4 to 39.48 (not in thousands);
- launch of service provided on the Active Line (switch-over of a pair of cables, servicing of orders for line) - from PLN 55.51 to 46.98 (not in thousands);
- service deactivation (switch-over of a pair of cables, servicing) - from PLN 21.21 to 18.28 (not in thousands);
- as well as due to number portability in such a way that its present amount remained not higher than the one binding prior to issue of the RO;

b) as well as BSA, inter alia due to:

- launch of service on the Subscriber's Line - from PLN 40.98 to 38.68 (not in thousands);
- change of Service Options – from PLN 45.22 to 34.07 (not in thousands);
- Service deactivation - from PLN 40.98 to 38.68 (not in thousands).

The RO does not provide for a fee due to cooperation between operators.
The procedure of MS/PS test was amended, according to the position of the President of UKE of February 9, 2011.

Orange Polska S.A. introduced an appeal against the decision approving RO. WSA stated that the decision is in fact decision on regulatory obligations, therefore the competent court should not be administrative court but common court. The KIGEiT, the President of UKE and Orange Polska S.A. appealed against this ruling. NSA reversed the decision of WSA, but WSA against issued the same ruling. The KIGEiT appealed again against this ruling. The WSA judgment, regarding inadmissibility of judging in the administrative courts was appealed by KIGEiT. NSA again revered WSA judgment.

By a decision of September 4, 2011, the President of UKE amended the RO with regard to conditions for BSA telecommunications access with use of VDSL technology.

The Management Board cannot assure that the conditions established in the RO by the decision of the President of UKE will not be in future amended or reversed.

Due to the fact that the RO regulates the terms and rules of co-operation of Orange Polska S.A. with other telecommunications undertakings differently than compared to the binding relations with Netia, the Management Board cannot assure that the agreed terms on which Netia uses access to the network of Orange Polska S.A. will not be changed or deteriorated in the future with the aim to ensure competitiveness comparing with other alternative operators.

In 2011 Orange Polska S.A. filed with the President of UKE a draft offer setting out frame terms of LLU services provision with regard to FTTx access. The offer that will be approved of by the President of UKE in this scope will make up frame terms of using LLU stipulated in the RO. Orange Polska S.A. also applied for amendment of the RO in the scope of BSA access including as regards application of Ethernet level, and also for modification of the BSA service in option with "up to 10 Mbit/s" and "up to 80 Mbit/s" and canceling options: 1, 2 and 6 Mbit/s. Orange Polska S.A. amended its application and withdrew it in relation to cancelation of 1, 2 and 6 Mbit/s options. The President of UKE conducted the consultation proceeding regarding the amendment of the RO in relation to BSA modification in option with "up to 10Mbit/s" without canceling options: 1, 2 and 6 Mbit/s.

In November and December of 2013 the President of UKE carried out the consultation process of the draft decision amending the reference offer. KIGEiT send position about the draft decisions. Consulted draft decisions of the President of UKE on the amending the reference offer include the increase of some fees paid to the Orange Polska S.A. and decrease of others.

At this stage of proceedings it cannot be predicted to what extent and when shall the projected conditions be adopted by the President of UKE to RO and how it will affect the conditions of doing business by Netia.

Although the Management Board is convinced that the raise of some fees for particular bandwidths (BSA service options) is groundless, it cannot be excluded that in case of issuance the decision establishing at least some of fees for broadband access higher that current fees adopted in relation between Netia and Orange Polska S.A., such decision will be reversed or amended by the court and that expenses related to access services will not rise or will not lead to loss of profitability of services provided by Netia as well as cash flows and loss of market share.

In the Understanding as of December 23, 2009, Netia and Orange Polska S.A. agreed that the amount of service rates for access to Orange Polska S.A. network will remain unchanged until December 31, 2012, which is why by that time any change to methodology of rates calculation into calculating them taking account of incurred costs would did not affect settlement rules between Netia and Orange Polska S.A. due to access to local loop and local sub-loop built according to copper technology. Despite the fact, that Understanding is still binding,, the Management Board cannot assure that no circumstances leading to increase of the amount of costs of using LLU service by Netia will not emerge in future. In particular it cannot be guaranteed that in case of issuing by the President of UKE decision setting rates for access to local loop higher than currently used by Netia and Orange Polska S.A., the decision would be repealed or changed by the court and that in case of issuing the decision increasing LLU rates, services provided by Netia would still be profitable, that cash flow would't decrease or Netia wouldn't loose market share.

The Management Board cannot assure that rules of the access to LLU service built with the fiber technology will be sufficient for ensuring Netia the opportunity the use of access to fiber local loop in Orange Polska S.A. 's network on a mass scale.

Orange Polska S.A. applied also for approval of its reference offer with regard to leased lines. Finally the President of UKE made minor modifications to an offer in the scope of using of analog lines. This change is not expected to significantly affect the conditions of doing business by Netia.

Orange Polska S.A. also filed the motion to the President of UKE to amend the leased lines reference offer on leasing lines between Ethernet nodes. At this stage of the proceeding, the Management Board cannot assure whether the amendment would affect providing services by the companies from the Netia Group.

Moreover, on January 31, 2012, the President of UKE obliged Orange Polska S.A. to change RO, i.a. in the scope of liquidation of tariff periods O1, O2, and O3 (it also concerns calculation of flat rate interconnection) and definition of fees for number portability. In consequence, the changed RO in accordance with the decision of the President of UKE may raise costs of using services of termination of calls in Orange Polska S.A.'s fixed network by companies of the Netia Group. In the proceeding regarding the amendment of the offer in relation to origination and termination in Orange Polska S.A., network, including the fees for services provided on these markets, the growth in fees for connection termination and for flat interconnection rate is provided. KIGEiT has appealed against this resolution as far as liquidation of tariff periods O1, O2 and O3 is concerned. On July 15, 2013 the President of UKE upheld the decision of January 31, 2012. On July 19, 2013 KIGEiT appealed against the decision of the President of UKE.

Orange Polska S.A. has also filed an application to the President of UKE for amendment of RO in relation to premium rate services provided within wholesale access to Orange Polska S.A. network (WLR). In Management Board opinion not every amendments proposed by Orange Polska S.A. are necessary to perform duties stemming from amendment of Telecommunications Law related to provision of premium rate services. However, the Management Board cannot assure that the President of UKE shall not approve the RO amendment in a manner that will not increase the cost of WLR.

Orange Polska S.A. has also filed an application to the President of UKE for amendment of RO in relation to Orange Polska S.A. liability, including in particular the issue of penalty clauses. According to the Orange Polska S.A. application the conditions regarding Orange Polska S.A. liability are going to became unfavorable. On October 21, 2013 the President of UKE announced consultations of the decision amending RO. The President of UKE in the draft decision partially accepted Orange Polska S.A. proposition. Although the Management Board is convinced that the Orange Polska S.A. application is not justified but it cannot assure that the President of UKE shall not amend the RO accordingly to the Orange Polska S.A. application and that in further effect the terms and conditions of regulatory services provided by Orange Polska S.A. which are used by Netia Group's companies shall not become unfavorable.

Risks related to the decisions of the President of UKE on the service of termination of calls in mobile networks (hereinafter referred to as "MTRs") (not in thousands)

In January and February 2009 the President of UKE issued temporary decisions ("Temporary decisions") amending agreements on the interconnection of networks concluded by Netia and Dialog with Polska Telefonia Cyfrowa S.A., Netia and Polkomtel Sp. z o.o. as well as Netia and Polska Telefonia Komórkowa Centertel Sp. z o.o. by lowering the mobile termination rates (MTRs) in public mobile telephone networks of the above-mentioned mobile networks operators to the level of PLN 0.2162 per minute. In June and July 2009 the President of UKE issued decisions (which replaced the above-mentioned temporary decisions) on the amendment of the interconnection agreements ("Final decisions"), concluded by Netia and Dialog with the above-mentioned operators, by setting the MTR at the level of PLN 0.1677 per minute. The same MTR was defined by President of UKE in the decision amending agreements on the interconnection of networks concluded by Petrotel with Polkomtel.

Polska Telefonia Komórkowa Centertel Sp. z o.o., Polkomtel Sp. z o.o. and Polska Telefonia Cyfrowa S.A. appealed against the temporary decisions of the President of UKE.

The following decisions were validly repealed:

1) Temporary and final decisions amending MTRs stipulated in the agreement between Polska Telefonia Cyfrowa S.A. and Netia.
2) The temporary decision changing MTR rates specified in the contract between Polska Telefonia Cyfrowa S.A. and Dialog.
3) Temporary and final decisions amending MTRs set in the Agreement between Polkomtel and Petrotel.

SOKiK repealed also but is subject to appeal: final decision amending MTRs set in the agreement between Polska Telefonia Cyfrowa S.A. and Dialog. Dialog submitted an appeal.

The Management Board cannot assure that the appeal will be successful.

In 2011 the agreements with Polska Telefonia Komórkowa Centertel Sp. z o.o., Polkomtel Sp. z o.o. and Polska Telefonia Cyfrowa S.A. (hereinafter the "MTR Agreement") were concluded. MTR Agreements were concluded by most of Alternative Operators being members of the KIGEiT, including Netia and Dialog. According to the MTR Agreement the forementioned mobile operators confirmed MTRs paid in accordance with the President of UKE decisions and limited the possibility of requesting retrospective claims. As a result of these agreements Polska Telefonia Komórkowa Centertel Sp. z o.o. and Polkomtel Sp. z o.o withdrew their appeals and these proceedings were discontinued.

Despite the fact that MTR Agreement was concluded between Netia, Dialog and Polska Telefonia Cyfrowa S.A., the Management Board cannot also assure that Polska Telefonia Cyfrowa S.A. shall not make claims related to the results of the abovementioned proceedings. The Management Board cannot predict the result of proceeding regarding such claims. Also, it cannot be excluded that Polkomtel sp. z o.o. will issue claims against Petrotel.

Along with other market participants, Netia, Dialog and Petrotel have made significant cuts in its customer tariffs for calls to mobile operators on the basis of the Regulator's MTR decision. In the event that the court raises the MTR rates once more, companies of the Netia Group will be unlikely to be able to pass on the higher costs to its customers through higher tariffs. No assurance can be given that possible damages claims against the State Treasury would be granted by the courts.

The President of UKE issued decisions stipulating the amount of MTRs to be paid to Polska Telefonia Komórkowa Centertel Sp. z o.o., Polkomtel Sp. z o.o. and Polska Telefonia Cyfrowa S.A.: as of July, 1, 2011 – at the level of PLN 0.1520 per minute and as of July 1, 2012 – at the level of PLN 0.1223 per minute, as well as the amount of MTRs to be paid to P4 Sp. z o.o., calculated on the basis of an index of asymmetry in relation to the remaining rates. Moreover, these decisions stipulate investment obligations of individual mobile networks operators in the so called "white areas", i.e. areas with low population density, excluded from GSM network coverage.

In MTR Agreements concluded by Netia and Dialog with mentioned mobile network operators the MTR provided by abovementioned decisions were confirmed.

In August 2012 the President of UKE has published to consultation the drafts of new decisions decreasing MTRs to be paid at the symmetrical level to Polska Telefonia Komórkowa Centertel Sp. z o.o., Polkomtel Sp. z o.o., Polska Telefonia Cyfrowa S.A. and P4 sp. z o.o., as of January,1, 2013 at the level of PLN 0.0826/ minute and as of July, 1, 2013 at the level of PLN 0.0429/minute.

Draft decisions were sent to the consolidation proceedings before the European Commission in September 2012.

On December 14, 2012, the President of UKE issued decisions establishing MTR (hereinafter referred to as "MTR Decisions") accordingly with consulted drafts. The new financial settlements stemming from these decisions were adopted in agreement amendments between Netia and Dialog with Polkomtel Sp. z o.o., PolskaTelefonia Komórkowa Centertel Sp. z o.o and Polska Telefonia Cyfrowa S.A. then only as regards the first of the MTR rates at the level of PLN 0,0826/minute, which is effective until June 30, 2013. The amended contract between Netia and P4 Sp. z o.o. provides also the MTR level of PLN 0,0429/minute, effective from July 1, 2013.

Finally, agreements implementing MTRs at the level of 0.0429 PLN/minute from July 1, 2013 were concluded also with Polkomtel sp. z o.o., PTK Centertel Sp. z o.o. and T-Mobile Polska S.A. (earlier Polska Telefonia Cyfrowa S.A., hereinafter "T-Mobile).

In case of suspension, repeal or change of the President of UKE decision setting the level of the MTRs of Polkomtel sp. z o.o. and in case of loss of binding force of the decision of the President of UKE setting the level of MTR of PTK Centertel sp. z o.o., the binding applicable rate with those operators would be 0,0826 PLN/minute, unless application of that rate would be impossible due to the duty of application of another rate resulting from the decisions of the President of UKE or the judgment of the court. In January 2014, the court refused to suspend the enforceability of the decision establishing the amount of the rates for call termination in the MTR Polkomel SP. z o.o. and T-Mobile.

Despite the conclusion of the agreements amending contracts with Netia and Dialog concerning MTRs from July 1, 2013 on the level of 0,0429 PLN/minute with all abovementioned mobile operators, including T-mobile S.A. proceedings started earlier before the President of UKE proceedings for the issuance of decisions amending the agreements in relation to the 0,0429 PLN/minute rate are not terminated. Netia and Dialog filed the statements underlining that SMP decision should be performed and were performed by concluding annexes instead of decisions. The Management Board is convinced that the proceeding shall be discontinued, but cannot assure that the President of UKE would terminate the proceedings in this way.

The Management Board also cannot assure that in case of filing the appeals against mentioned decisions providing MTR PLN 0,0826/minute and PLN 0,0429/minute, the court will not suspend the enforcement of these decisions at any stage of the court proceeding or will not finally reverse or change these decisions and that such suspension, reversal or change will not affect the financial settlements with mobile operators and set them differently than in the agreements with those operators and these operators will not pursue the claims against Netia and Dialog.

In case the mobile operators potentially obtain final court orders against the Netia Group's companies the Management Board cannot assure that the Netia Group's companies' regress claims against the State Treasury will be successful.

On June 19, 2013 T-Mobile asked the President of UKE to explain doubts regarding whether T-Mobile is obliged to apply regulatory obligations imposed in the MTR Decision, including the level of the MTR rate set by the President of UKE, for a calls initiated from A – catalogue subscriber number, from the number range used by states that are not members of the EU and terminated in the T-Mobile mobile network. On August 20, 2013 the President of UKE issued decision refusing to resolve T-Mobile doubts. Due to the unclear justification of the decision, KIGEiT filed with the President of UKE an application to reconsider the decision, challenging the justification of the decision. T-Mobile also filed an application to reconsider the decision. On November 29, 2013 the President of UKE issued the decision upholding the desion from August 20, 2013.

On September 4, 2013 Polkomtel asked the President of UKE to explain doubts whether the MTR Decision of the President of UKE imposing regulatory obligations on Polkomtel, including the level of the MTR, oppose applying rates for calls termination in mobile public Polkomtel network other than set in the schedule set out in that decision, in case the call terminated in the Polkomtel network was initiated outside the European Union. On December 5, 2013 the President of UKE issued the decision refusing to resolve Polkomtel doubts. Polkomtel filed to the President of UKE an application to reconsider the decision.

Although the Management Board is convinced that T-Mobile and Polkomtel questions are unjustified, the Management Board cannot assure that the final decisions of the President of UKE and their verification by the courts will not have an impact on the level of rates charged by these MNOs for calls from the number range used by the states that are not members of the EU and terminated in these operators' mobile networks. In the event that differential MTR rates are introduced, Netia may incur significant costs to enable proper management of such traffic through its network.

Risk related to reversal of President of UKE decisions stipulating conditions of the access to IN services in Netia and Dialog networks for mobile networks users

The President of UKE issued decisions stipulating conditions of access to IN services in Netia and Dialog networks for Polska Telefonia Cyfrowa S.A. and Polkomtel Sp. z o.o. users.

The Court of Appeal in Warsaw reversed these decisions stipulating access to IN services in Netia and Dialog networks for Polska Telefonia Cyfrowa S.A. users. Netia and Dialog have received the justifications of the rulings. Netia and Dialog submitted cassation complaints against the judgments of the Court of Appeal. The Supreme Court agreed to hear the cassation appeals. In Dialog case, the Supreme court asked the Court of Justice questions on the issue of the obligation to provide consultation and consolidation process during the administrative proceeding of solving operators disputes. For the time of answering that question the Supreme Court suspended Netia proceeding. The Management Board cannot assure that the ruling reversing the decision shall be issued.

Polkomtel Sp. z o.o. has also appealed against the decisions stipulating conditions of the access to IN services in Netia and Dialog networks for users of Polkomtel Sp. z o.o. network. Due to the agreement worked out between Dialog and Polkomtel Sp. z o.o., Polkomtel Sp. z o.o. withdrew the appeal and asked to terminate the proceedings. The Management Board cannot assure that the decision for Netia will not be reversed as a result of the Polkomtel Sp. z o.o. appeal.

The Management Board cannot assure that agreements stipulating conditions of the access to IN services in Netia and Dialog networks for Polska Telefonia Cyfrowa S.A. and Polkomtel Sp. z o.o. users will be concluded, and if these enterprises shall not make claims related to results of mentioned proceedings. The Management Board cannot predict the result of proceeding regarding any eventual claims.

Risks related to the analysis of relevant markets

According to the amended Telecommunications Law, the President of UKE performs an analysis of telecommunications services market („relevant market") not less often than every 3 years notifies to the European Commission the draft of the decision in which upholds, modifies or waives regulatory obligations imposed on an entrepreneur, who as a result of a previous analysis has held a significant market power.

Orange Polska S.A. holds significant market power in individual wholesale markets countrywide and is obliged, in particular, to provide telecommunications access to other entrepreneurs, under non-discriminatory terms.

On December 30, 2010, the President of UKE issued a decision defining a market, in which Orange Polska S.A. was so far obliged to provide access to local loop or a local sub-loop in copper technology, as a market of wholesale (physical) access to network infrastructure service provision (including full and shared access) in a fixed location, designated Orange Polska S.A. as holding a significant market power on the relevant market, as well as imposed regulatory obligations on Orange Polska S.A.

By virtue of the President of UKE decision Orange Polska S.A. was obliged to maintain telecommunications access to local loop and sub-local loop, as well as to provide access to the telecommunications ducts or to dark fibers, and - in case of lack of possibility of access provision for an operator applying for access to the above elements of infrastructure – to provide access to local loop and local sub-loop using fiber technology.

So far Orange Polska S.A. had an obligation to calculate costs and set telecommunications fees taking account of justified costs. This was replaced in the decision by an obligation to set fees taking account of incurred costs. The method Orange Polska S.A. is obliged to apply, allows for recovery of costs actually incurred in the process of telecommunications access provision and not justified costs i.e. costs that a hypothetical telecommunications undertaking would incur if it operated on a fully competitive market, with scope of activity and demand for its services comparable to those specific for an actually existing telecommunications undertaking obliged to run costs calculation.

In the opinion of the Management Board the amendment of the imposed obligation concerning method of calculation of costs of telecommunications access provision introduced by the President of UKE's decision is premature. No circumstances arose on the market that could justify application of the method of costs calculation taking account of incurred costs and not justified costs.

KIGEiT filed an appeal with SOKiK against the President of UKE's decision of December 30, 2010. On December 4, 2013 SOKiK repealed KIGEiT's appeal. KIGEiT still didn't receive written justification of the judgment.

On September 11, 2013 European Commission published "Commission recommendation on consistent non-discrimination obligations and costing methodologies to promote competition and enhance the broadband investment environment". One of the key elements of the Recommendation is setting month rate for access to the copper local loop on the level of 8 – 10 euro. The Management Board cannot assure how the Recommendation will affect the regulatory policy of the President of UKE and whether the implementation of the Recommendation to the polish regulatory environment will affect the costs of the Netia Group for the usage of the regulated wholesale services provided by Orange Polska S.A.

On April 28, 2011 the President of UKE issued a decision holding Orange Polska S.A. (Orange Polska S.A) as having a significant market power in the market for provision of wholesale broadband access services. The analysis of the President of UKE included the national market, within which regulatory obligations of Orange Polska S.A. in the areas of separate groups of municipalities were differentiated. The decision also provides for change of obligation to establish telecommunications access fees according to cost calculation, from the method based on justified costs to incurred costs. Eleven municipalities were excluded from the national market area. Orange Polska

S.A. appealed against the decision. On August 29, 2013 SOKiK repealed Orange Polska S.A. appeal. KIGEiT also appealed against the decision, pointing the improper deregulating of the area of the 11 municipalities. On February 4, 2014 SOKiK repealed KIGEiT's appeal. KIGEiT still didn't receive written justification of the judgment.

On July 27, 2011 the President of UKE commenced consultation and consolidation proceedings concerning a draft decision identifying a broadband access market within the administrative borders of eleven municipalities: Warszawa, Płońsk, Nowy Dwór Mazowiecki, Lublin, Zielona Góra, Bielawa, Olsztyn, Łomża, Białystok, Elbląg, Braniewo and stating that within the areas of these municipalities effective competition is present and no SMP undertaking operates.

On February 1, 2012, the President of UKE commenced consultation proceedings of the draft decision, in which it defines the relevant market as the market for provision of wholesale broadband access services, states that there is no competition on this market, Orange Polska S.A. has significant position on this market, and in this connection imposes regulatory obligations on Orange Polska S.A. Within administrative borders of four municipalities: Toruń, Lublin, Warszawa and Wrocław, in the area of which the competition distortions are in the opinion of the President of UKE significantly less important than in the rest of the country's market area, imposes on Orange Polska S.A. the obligation to assure telecommunication access along with obligation to keep realized access and obligation of non-discrimination. On March 26, 2012 within consolidation proceeding the President of UKE provided the draft of decision to the Body of European Regulators for Electronic Communications (BEREC) and national regulatory authorities in other member states.

The European Commission has started an in-depth investigation and has issued a serious doubts letter concerning the project of the decision in the scope of measures of the access to Orange Polska S.A.'s FTTH infrastructures proposed by Polish Regulator. President of UKE may work with the Commission and BEREC on regulatory rules of the access to Orange Polska S.A.'s FTTH infrastructures for three months. In the other case, President of UKE will not be allowed to issue the decision based on the project.

On August 27, 2012 the European Commission presented to the President of UKE position that decision shall be improved by imposing on Orange Polska S.A. obligation of using cost oriented rule with regard to the FTTH access or by establishing alternative measures of competition protection (an improved transparency obligation regarding FTTH, replicability requirement also for FTTH-based retail products and accounting separation obligation covering also FTTH products).

On October 8, 2013 the President of UKE issued a decision that terminated proceedings that could have led to the imposition of new obligations on Orange Polska S.A. in respect to Market 5.

On September 11, 2012 in the letter to Ms Neelie Kroes, vice-president of the European Commission, the President of UKE withdrew from a proposed regulation of the market for wholesale broadband access. Then the president of UKE presented draft of other resolution concluding the existence of effective competition and abolishing Orange Polska S.A. regulatory obligations on this market on the area of 11 polish municipalities. The European Commission notified serious doubts regarding correctness of drafted resolution and drew the attention of the President of UKE inter alia on the facts of the case contemplated under the drafted resolution, which are based on outdated data, coming from market analysis performed by the President of UKE in 2009, whereas in the moment of drafting the resolution the President of UKE had access to data from further analysis of this market. KIGEiT filed the statement to the President of UKE and the European Commission pointing the mentioned issue of outdated data and noted also other incorrectness of projected resolution, which, in the opinion of the Management Board excluded the possibility to issue the resolution in accordance to its draft. The European Commission obliged the President of UKE to withdraw the draft of the regulation. On February 8, 2013 the President of UKE published the information that the Regulatory Body has been going to conduct the new analysis of the market 5, taking into consideration the Commission's guidelines. Finally the President of UKE terminated the proceedings leading to the repeal of the regulatory obligations on the area of the 11 Polish municipalities.

In the opinion of the Management, relevant markets, including broadband access markets within the area of the municipalities comprised in the drafts of the President's of UKE decisions, are not developed sufficiently to allow for geographical or technological differentiation of Orange Polska S.A. regulatory obligations, nor are there any grounds, to hold that on the area of individual municipalities the regulatory obligations imposed on Orange Polska S.A. should be limited.

However, it cannot be said what will be the results of the new broadband market analysis and what kind of regulatory measures about access to the Orange Polska S.A. infrastructure will be set (including FTTH access). As a result, it cannot be predicted, what access conditions and on what area of Poland will be applied in the future. It also cannot be predicted how those changes will affect the existing ability of the Netia Group to offer services with the use of this type of access to the network of the Orange Polska S.A.

On October 16, 2012 the European Commission began consultation on telecoms markets Recommendation. The Management Board cannot assure that change of the telecoms markets Recommendation as a result of applying it by Regulatory Body in Poland, will not lead to an increase in the cost of telecommunications access or decrease of conditions of telecommunications access.

On December 5, 2013 BEREC began consultation of the draft Common Position on the geographical aspects of market analysis. The Management Board cannot assure that publication of the final Common Position and its implementing by the Polish Regulator would not lead to worsen of the condition of using telecommunication access services.

Risks related to Dialog's business

Orange Polska S.A. has summoned Dialog to pay the amount of PLN 667 (including interests) for account of outstanding receivables arising from the use of telecommunication access to the Orange Polska S.A.'s network by Dialog. Despite the fact that in the Management Board's opinion Orange Polska S.A.'s claims are at least partly unjustified, it cannot be assured that in case of court proceedings they will not be taken into account or that Dialog's claims for payment against Orange Polska S.A. arising from the contracts and decisions on telecommunication access or using Dialog's infrastructure by Orange Polska S.A. will be paid in the amount of exceeding the amount Orange Polska S.A.'s claims.

Moreover, Orange Polska S.A. has issued invoices for transit to ported numbers for a total amount of PLN 2,392 including interest of PLN 356. These invoices cover fees for period between January 1, 2012 and May 21, 2013. Dialog claims the invoices are unjustified because neither interconnection agreement nor agreement on number portability provide separate title for charging fees for such service, and from May 1, 2013 charging principles for transit to the NP numbers are the subject of the new Reference offer contract concluded by Dialog . Nonetheless, Orange Polska S.A. filed for payment and on October 12, 2012 an order for payment was issued, including the charge for the transit to ported numbers for the period January-June 2012, amounting to PLN 1,274 and statutory interest. The order for payment has expired on November 5, 2012 upon the submission of objections submitted by Dialog. Consequently, the case will be solved by the district court in Wrocław. On September 23, 2013 in the district court in Wroclaw the hearing was held. The district court in Wrocław announced that had no jurisdiction in that case. The case was handed over to the district court in in Warsaw.

Despite the fact that in the Management Board's opinion Orange Polska S.A.'s claims are unjustified, it cannot be assured neither that they will not be recognized by the court, also for the period until the May 1, 2013, nor that Dialog's claims for payment against Orange Polska S.A will be paid in the amount of exceeding the amount Orange Polska S.A.'s claims.

Despite the fact that in the Management Board's opinion the claim covered by Dialog's complaint, in the case of which the court has issued the order for payment by Orange Polska S.A. to Dialog amounting to PLN 40,461 and statutory interests for the penalties for not deleting failures on WLR links' on the dates described in the President's of UKE decisions, is valid, it cannot be assured that, in the light of objection submitted by Orange Polska S.A., the court will approve Dialog's claim and Orange Polska S.A. will pay Dialog the amounting covered by the order of payment in total or at least in part of it, which will be higher than potentially payable Orange Polska S.A.'s claims against Dialog.

On December 31, 2013 Dialog filed a lawsuit against Orange Polska S.A. to pay 7.852 zł contractual penalties (from the contracts between Orange Polska S.A. and Dialog) for delays of removing malfunctions of the WLR service in the year 2012. Despite the belief of the Management Board that the lawsuit is justified, the Management Board cannot assure that in case of Orange Polska S.A.'s objection, the court will approve Netia claim eventually and Orange Polska S.A. will pay Dialog the amounting covered by the order of payment in total or at least in part of it.

Risks arising from the presumption of the powers of the organizations for the collective administration of the rights of authors of neighboring rights

The Law on Copyrights and Related Rights defined (hereinafter referred to as "Law on Copyrights") a presumption, that the organizations for the collective administration of the rights of authors of neighboring rights (hereinafter referred to as "OZZ") are entitled to give consent (grant license) to rebroadcast TV channels via cable networks and are entitled to collect remuneration for the hereinabove rebroadcasting in scope of the copyrights managed by certain OZZ. Tables of remuneration of the use of works or objects of related rights covered with collective management are established on the percentage basis in relation to the gross revenue earned by the operator from the rebroadcasting of the TV channels and are approved by the Copyrights Commission (Komisja Prawa Autorskiego; hereinafter referred to as "KPA") upon the application for the approval submitted by OZZ to KPA. KPA is also entitled to settle disputes connected with concluding of the contracts between OZZ and cable network operators.

The obligation of obtaining from OZZ the channels' rebroadcasting license following from The Law on Copyrights and Related Rights is contrary to the legal regulations of the EU Directive No 93/83/EWG. EU legislator compulsory excluded the said obligation in case where the cable networks operators are granted with this license directly by the TV channels' broadcasters. According to the constitutional principle of the EU law dominance over the Polish law, there is no need to obtain the additional OZZ's license in scope of the rights already granted directly by the broadcasters. Bearing in mind the practice of dealings in Poland, the Management Boards may not guarantee that the above mentioned UE law principle shall apply to Dialog, Netia and Petrotel. However, this contradiction in law does not exclude the statutory, resulting from The Law on Copyrights and Related Rights, obligation imposed upon the rebroadcasting operators to pay the so-called additional remuneration of the use of works or objects of related rights covered with collective management for the benefit of OZZs.

As regards the TV channels' rebroadcasting, it is Polish Filmmakers Association (hereinafter referred to as "SFP") that is widely entitled to represent the producer's rights and is involved in collective copyright management. However, as long as it is not proved which works or objects of related rights are covered with collective management by Authors' Association "ZAIKS" and others OZZ, it is not possible to determine the scope of the hereinabove presumption arising from The Law on Copyrights and Related Rights and if in case of the TV channels' rebroadcasting without the agreement with Authors' Association "ZAIKS" or other OZZ, on the basis of the Polish law, OZZs shall be entitled to request abandonment of further TV channels' rebroadcasting by Netia, Dialog or Petrotel effectively and payment of the compensation in the amount of triple amount of the remuneration due OZZ.

KPA had determined the remuneration of the use of works or objects of related rights covered with collective management of SFP in the amount of 1.6% and covered with collective management of Authors' Association "ZAIKS" in the amount of 0.6% (in UPC's case) and 0.9% (in Sat-Film case), but Commission judgments were appealed. In consequence the said remunerations in amounts defined by KPA are not in force.

Polish Chamber for Electronic Communication ("PIKE") has started negotiations with certain OZZs, including SFP and ZAiKS, to conclude the general agreement. OZZs have proposed the remuneration amounting to jointly is 4% of revenues from rebroadcasting. Moreover, SFP and ZAIKS, applied jointly to KPA to approve the table of remuneration amounting to 3.3% and other OZZs taking part in negotiations with PIKE amounting to 1,1 % of revenues from rebroadcasting. KPA refused to approve these tables of OZZs' remuneration and OZZs appealed against KPA's decision to the court. At this stage, the Management Board cannot foresee the result of neither of these proceedings nor the negotiations of the general contract conducted by PIKE, in particular it is not possible to predict the amount of OZZ's remuneration, which will be defined, whether it will higher or lower than jointly 4% and whether and how this fact could influence settlement conditions between Netia, Dialog and Petrotel and OZZs.

According to the agreement currently in force, Dialog pays for the benefit of SFP the remuneration in the amount 2.2% of revenue earned by Dialog from rebroadcasting of the TV channels. The agreement between Dialog and Authors' Association "ZAIKS" is terminated, however Dialog paid in favour of Authors' Association "ZAIKS" the advance payments in the amount 0.6% of revenue earned by Dialog from rebroadcast of the TV channels and this OZZ accepted these payments till May 2012. Dialog also terminated the agreement with ZPAV (The Polish Society of the Phonographic Industry) effective on May 31, 2011. Simultaneously ZPAV didn't accept the proposed advance payments in the amount of 0.06% and in June 2012 requested to Dialog to cease all non-contractual payments as it shall be returned into Dialog's bank account. In order to avoid payment fees for rebroadcasting some works to both Artists Performing Music and Music-Verbal Works Association SAWP (hereinafter the SAWP) and Union of Performing Artist STOART (hereinafter the STOART) Dialog has served notices of termination with respect to agreements establishing current settlement rules with these organizations. Establishing the rights to represent by SAWP and STOART the property rights to works rebroadcasted by Dialog will require to point relevant organization by KPA and, in dispute cases, pursuing the mediation proceedings by KPA. In March 2012 SAWP took legal action against Dialog in order to conclude a settlement on payment of the remuneration in the amount of 48 PLN as a compensation of non-contractual use of works or objects of related rights covered with collective management during a period from 1st of September 2011 until February 29, 2012. Dialog proposed the percentage rate according to art. 110 of The Law on Copyrights and Related Rights as it takes into account the income amount of the use of works. This proposal was rejected by SAWP and as a consequence SAWP suggested the rate exclusively with reference to the number of subscribers. SAWP denied to accept the SAWP's advance payments in the amount of 25% of the expected remuneration and declared that such payments shall go toward the SAWP's claims and the lack of the SAWP's written declaration to conclude the agreement on SAWP's conditions shall be treated as the lack of will to respect the rights represented by SAWP that will force SAWP to pursue claims through the courts together with statutory interest.

In May 2013 the copy of the statement of claim of SAWP was delivered to Dialog, pursuant to the art. 105 par. 2 of the Law of the Copyrights, to provide information necessary to determine the level of remuneration and rates claimed by SAWP. Dialog submitted response to the statement of claim challenging the entire claim of SAWP. Moreover, Dialog applied for STOART to be joined to the proceedings, due to the fact that the scope of the rights represented by SAWP and STOART overlap and both these OZZ claim the right for remuneration for the use by Dialog of the same kind of works – artistic music and word-and-music performances, in the same field of exploitation (rebroadcasting). With STOART joining to the proceedings, the judgment, in case of providing information to SAWP, will have effect that in case of accepting SAWP claim in whole or in part by the court, STOART would not be able to demand satisfaction of its claim within this scope.

In the Management Board opinion, the SAWP claims in relation to the number of subscribers are not justified, in particular taking into consideration fact that during the negotiations of the general contract conducted by SAWP with other OZZ and PIKE, the OZZ, including SAWP, proposed the jointly rate of 4% of revenue received from rebroadcasting of the works, the copyrights of which they represent. At this stage, the Management Board may not foresee the amount of remuneration of OZZ and if the remuneration shall not be higher than jointly 4% of revenue received from rebroadcasting for above mentioned OZZ.

On December 31, 2013 Netia concluded with SFP the agreement on the giving Netia license to rebroadcasting of the TV programs for the payment of 2,2 % of the income for the rebroadcasting. Netia also conducts negotiations with ZAiKS in order to regulate the compensation rules for rebroadcasting of TV channel in the scope of copyrights that ZAiKS manages. The Management Board cannot assure that the negotiations will end with concluding the contract with ZAiKS concerning the rule that rebroadcasting TV channels by Netia is being done only on demand of the user of the service. This manner of providing TV services means that the subject of the settlements with SFP shall be rebroadcasting that occurs sporadically, not permanently, as in the case of CATV operators.

Even though Netia doesn't provide activity in TVC technology and Management Board is convinced of that the amounts of compensation demanded by OZZ are unjustified, it couldn't be guaranteed that Netia , Dialog and Petrotel shall not be obliged to pay to SFP such amount of compensation demanded by OZZ until KPA approves the lower rate of the remuneration or the general contract with PIKE is concluded and the settlement rules with OZZ shall be amended on one of these grounds.

At this stage of Netia's activity of TV channels' rebroadcasting, taking into account the circumstances that it is conducted via IP technology, not cable technology, and taking also under consideration the legal and the factual doubts concerning the scope of the power of each OZZ and also lack of the approved SFP's and ZAIKS's tables of remuneration of the use of works or objects of related rights covered with collective management, it couldn't be predicted what the final part of the revenue earned from providing TV services by Netia, Dialog and Petrotel, they will be obliged to pay to OZZ. However, the Management Board is convinced that, the total final amount of these receivables should be lower than paid to OZZ by cable operators. On the basis of the resolutions of the disputes between cable networks operators and OZZs and tables of remuneration of the use of works or objects of related rights to be approved by KPA, Management Board estimates that total definitive amount of the remuneration to be paid by cable network operators to OZZ may be up to 4% of revenue earned by them.

Under the cinematography law of June 30, 2005 the Polish Film Institute (Polski Instytut Sztuki Filmowej -PISF) summoned Netia and Dialog to pay the remuneration in the amount of 1,5% of revenue earned by Netia and Dialog from fees for an access to TV channels rebroadcasted by Netia and Dialog and from fees for rebroadcasting services. According to the cinematography law of June 30, 2005 the abovementioned remuneration shall be paid by two categories of entities: cable television operators and digital platform operators.

In the Management Board opinion as long as Netia and Dialog rebroadcast TV channels via IP technology both of them are not obliged to pay the abovementioned remuneration demanded by PISF. However the Management Board cannot assure that in case PISF does not share the abovementioned opinion of the Management Board and will sue Netia or Dialog for the abovementioned remuneration starting the court proceedings the court judgment in these cases will be compliant with the abovementioned opinion of the Netia's Management Board and neither Netia nor Dialog will be obliged to pay PISF the demanded remuneration.

Other regulatory risks

The President of the UKE is regularly carrying out inspections of compliance of the companies from the Netia Group with the provisions of the Telecommunications Law and using frequency and numbering conditions. In cases provided for in the Telecommunications Law, the President of UKE may fine the companies from the Netia Group with a fine up to 3% of revenues of the previous calendar year.

The President of UKE has been carrying out several inspections of the use of radio frequencies by Netia Group's companies in accordance with the conditions described in radio permits and proceedings in case of imposing a fine in connection with the irregularities (according to the President of UKE) which have been noted in this scope. On December 28, 2012 the President of UKE issued the decision imposing the fine on the Dialog in the amount of 21 PLN due to breach of the conditions of use of the frequencies stemming from the radio permission. On December 16, 2013 the President of UKE issued decision imposing fine (30 PLN) on Netia for improper work of the radio devices in three locations.

Dialog and Netia filed the appeals against the decisions, raising, inter alia, that the decisions were issued before sending post-audit recommendations. Although the Management Board is convinced of validity of the appeals it cannot assure that the appeals will be accepted and that the decisions will be reversed.

The Management Board cannot assure that the President of UKE will take into account statements submitted by the Netia's Group companies and will discontinue other inspections and proceedings in case of imposing the fine, concerning the using of radio frequencies and in the opposite case that the President of UKE will not impose the higher amount of fine than in the decision issued in Dialog's case.

The Management Board cannot assure that with regard to all inspection procedures UKE agrees that the position of Netia and the activities of the Netia Group are consistent with regulatory requirements and the law to the extent that eliminates the risk of a fine.

President of UKE is also authorized to conduct the mediation proceedings in order to find amicable solution of the disputed interests between the subscribers that are consumers and provider of telecommunication services.

Although strategic aim of Netia Group is special solicitude about comfort of subscribers using or intending to use Netia Group companies services, the Management Board cannot ensure that undertaken efforts made by Members of the Netia Group or other operators acting on their behalf, won't be evaluated by President of UKE as requiring additional benefits for the subscribers, set out in mediation proceeding. However the entering into the mediation proceeding depends on decision made by the Management Board, taking into account point of view of President of UKE justifying such need, is crucial for such decision.

The President of UOKiK is entitled, inter alia, to conduct proceedings concerning compliance of standard terms and conditions applied by the companies belonging to the Netia Group with requirements stemming from the law on protection of competition and consumers, as well as other regulations aiming at protecting consumers' interest. In cases provided for in the law on protection of competition and consumers the President of UOKiK may impose on the companies belonging to the Netia Group a fine amounting up to 10% of their income earned in the preceding calendar year.

The Management Board is unable to assure that within the scope of the explanatory proceedings the President of UOKiK will consider standard terms and conditions applied by the companies belonging to the Netia Group to be compliant with the respective legal requirements, thus excluding the risk of fine imposition.

The business conducted by the companies of the Netia Group is also subject to control by other regulatory authorities and to inspections based on the relevant laws and within the scope of the granted to such authorities. If such regulatory authorities determine that the companies of the Netia Group are not acting in compliance with the respective laws the regulatory authorities may impose various administrative sanctions on the companies of the Netia Group as prescribed in the relevant laws, including monetary fines or orders prohibiting/compelling the companies of the Netia Group to perform certain actions.

The Management Board cannot assure that with regard to all inspection procedures the authorities conducting the control agree that the position of Netia or other companies of the Netia Group and the activities of the Netia Group are consistent with regulatory requirements and the law to the extent that eliminates the risk of a fine and prohibition of performing the activity being a subject of a control.

The President of UKE is working on the implementation of the aims of the Memorandum dated October 26, 2012 on the Cooperation for Increasing Quality of Services Provided on the Telecommunications Market. The work involves the parties that signed the Memorandum, including the telecoms business associations, as well as Orange Polska S.A., MNOs, UPC, Exatel, TK Telekom, and the Netia Group. By signing the Memorandum, the President of UKE and the other Signatories obliged themselves to work together to provide to end-users reliable and comparable information on the availability and quality of provided services (Quality of Service – QoS). To date two types of indicators for fixed and mobile networks were identified: "administrative" i.e. "the average waiting time for connection with staff", "invoice correctness" on the rates for telecommunication services, and "technical" i.e. effectiveness of phone connections index and, according to the President of UKE the most important from the net neutrality point of view, the "index of data transfer speed". Other technical indicators, for example "per cent of SMS messages delivered in 10s", according to the nature of services provided in mobile networks, were defined for the MNOs.

The President of UKE sees the Memorandum as implementation of both EU directives and Polish Telecommunications Law, including the creation of uniform conditions of conducting business and using telecommunication services in the EU and also the implementation of the net neutrality principle. Work to date on the Memorandum confirms one of its objectives, i.e. creation by the Initiator (the President of UKE) a regulatory environment friendly for telecommunication operators that promotes the idea of co-regulation of the telecommunications market.

On December 17, 2013 the President of UKE announced consultation of the Final Report of the Memorandum. In the Final Report there is a list of indicators of the quality of services, methods of measurement and rules of publishing of the results of the measures and the way of providing them to the President of UKE.

Elaboration of the principles and the methods of measurement indicators of quality of services, according to the Management Board, should preclude further actions of the President of UKE for the same purpose, i.e. for example exercising powers given to the President of UKE in art. 62a of the Polish Telecommunications Law that enable the President of UKE to impose on the telecommunications operator an obligation to use specific methods of measuring data transfer speed. However, the Management Board cannot foresee what will be the policy of the President of UKE in this scope and whether the costs of measurement and publishing indicators of services provided by the Netia Group will not increase.

In August 2013 the Lower House of Parliament ("Sejm") began work on a draft resolution requesting the Minister of Administration and Digitalization to guarantee parents the right to the Internet without pornography. KIGEiT filed to the Minister of Administration and Digitalization a position paper on the case and declared cooperation of the operators from KIGEiT to publish on their websites educational information for parents on how to block access to pornography, also through available on their websites applications for blocking the access.

Netia filed for payment of PLN 49,800 against Orange Polska S.A. due to not eliminating failures on WLR links on the dates described in the President's of UKE decisions. On December 21, 2012 the court issued order for payment. The Management Board cannot assure that, in the light of objections submitted by Orange Polska S.A., the court will approve Netia's claim and Orange Polska S.A. will pay Netia the amounting covered by the order of payment in total or at least in part of it.

On December 31, 2013 Netia filed a lawsuit against Orange Polska S.A. to pay 5,232 zł contractual penalties (from the contracts between Orange Polska S.A. and Netia) for delays of removing malfunctions of the WLR service in the year 2012. Despite the belief of the Management Board that the lawsuit is justified, the Management Board cannot assure that the court will take into account the lawsuit.

Risk of collective suits

On July 19, 2010, a law on prosecution of claims in collective procedure, which provides for possibility of bringing an action to the court by a group of at least 10 people, came into force. A judgment passed as a result of such a suit regards all the members of such a group. The Management Board cannot exclude risk of bringing such actions against the Company in the future.

Risk of growth of competition as market converge

The companies of the Netia Group current core offerings are voice telephony, broadband data services and providing tv services using broandband Internet.

After the merger of PKT Certentel and TP S.A., Orange Polska S.A., being the incumbent on the both markets: fixed and mobile, is the main competitor of the Netia Group. Other competitors are alternative operators, cable operators and mobile operators Polkomtel, T-Mobile and P4.

Furthermore, during 2013 T-Mobile agreed to acquire business customer focused GTS Central Europe, whose polish subsidiary, GTS Poland, is a key competitor to Netia on the market for business customers. Should the transaction close during 2014, T-Mobile may, like Orange Polska S.A., acquire the capability to propose convergent fixed-mobile offerings to business customers more effectively than Netia and this could lead to a loss of market share and cash flows for Netia Group.

Fixed operators, including Orange Polska S.A. also offer television and content services and some cable operators now offer quadruple play bundles including mobile telephony. Certain satellite TV operators are responding to the situation by also moving into the resale of fixed telephony and/or broadband thereby further increasing the competition to Netia's core services. Companies of the Netia Group intend to respond to this competitive pressure and convergence of product offerings by itself offering television services over upgraded networks. However no assurance can be given that this tendency of operators of different types of infrastructure to offer similar multi-service bundles will not lead to the gradual erosion of margins, profitability and cash flows.

In addition, significant new operators may enter the Polish market or mergers between existing market participants may significantly alter the competitive landscape in a way that might materially deteriorate Netia's competitive position.

Risk of competition from Orange Polska S.A. and Orange Polska S.A. obedience to the UKE decisions issued in the matters of the Orange Polska S.A.

Orange Polska S.A. occupied a leading position in Poland among operators offering fixed telephony services and data transmission. After merging of PTK Centertel and Telekomunikacja Polska S.A. and changing name for Orange Polska S.A. in the scope of fixed phone services, Netia Group has to face competition from Orange Polska S.A. in all the geographic areas it operates on. Orange Polska S.A. is a much larger entity than Netia Group and in the fixed part possesses far broader backbone and access network. In the fixed market, Orange Polska S.A. is engaged in many years' relations with numerous clients that constitute a target client group of Netia Group. Fixed infrastructure exploited by Orange Polska S.A. in the main cities of the country is comparable in terms of advancement of applied technologies to the infrastructure of Netia Group. Orange Polska S.A. may also make use of the offer of its main subsidiary unit, the Orange mobile network operator, as well as of TV services, in a manner that Netia currently would not be able to copy. One cannot exclude that aggressive competition from Orange Polska S.A. will have a significant adverse effect on Netia Group revenues and its operating activities outcomes.

Orange Polska S.A. is the owner of local access networks (local loops) and offers access to these local loops networks to other operators on terms that in many cases make it unprofitable to connect client to the network. However, since 2006 the Regulator has issued decisions establishing reference offers for access to Orange Polska S.A. networks that currently is regarded by Netia to be commercially profitable, but under condition that the Regulator will protect proper relation between wholesale and retail rates. Due to the above in 2006 and in 2010 Netia signed a cooperation agreement with Orange Polska S.A. enabling Netia to offer Internet access to Orange Polska S.A. clients on the basis of regulatory Orange Polska S.A. wholesale offer called bit stream access. In June 2007 Netia and Orange Polska S.A. concluded networks interconnection agreements that complexly regulate terms of cooperation between operators. This agreement also applies to cooperation with Orange Polska S.A. in the scope previously addressed in separate agreements on networks interconnection concluded by companies from Netia Group, whose rights and obligations Netia entered into under regulations of the code of commercial partnerships and companies. By virtue of the Settlement Agreement Netia acknowledged this rule on January 22, 2010, placing with Orange Polska S.A. a binding statement on regarding the interconnection agreement between Netia and Orange Polska S.A. of June 30, 2007, as the basis for serving all of the Netia services users in the scope of networks interconnection. In January 2007 the President of UKE issued a decision on amendment of interconnection agreement between Orange Polska S.A. and Premium Internet – a company belonging to Netia Group (which in 2008 merged with Tele 2 Polska, the latter in February 2009 merged with Netia), in the scope of wholesale line rental (WLR). The decision of the President of UKE introduced a basis for a new form of access to Orange Polska S.A. network enabling Netia Group to offer voice services to Orange Polska S.A. clients. In October 2008 a WLR decision in favor of Netia was issued, as well. Moreover, in April 2007 Netia concluded an agreement with Orange Polska S.A. on full and shared local loop unbundling, with use of which Netia Group offers voice and data transmission services, interactive TV services (IPTV) and in the future plans to pay other different value-added services. Whereas the key commercial terms of these services provision laid down in the Regulator's decisions are currently attractive, still the operational cooperation with Orange Polska S.A. aiming at provision and maintenance of such services for end users will require closer cooperation than it used to be in the past.

The Settlement Agreement between the President of UKE and Orange Polska S.A. expired at the end of 2012. The Management Board is not able to guarantee that Orange Polska S.A., in the scope of previous Orange Polska S.A. activity, will cooperate on an adequate level of engagement, nor that the regulatory body will react forcing Orange Polska S.A. to realize the cooperation. Moreover, we are unable to give assurance that change of market situation, future court judgments or regulatory body decisions will not cause that currently existing possibilities of services provision for clients through use of Orange Polska S.A. access networks to be no longer profitable from the commercial point of view.

Possible future competition from new generation networks

The most modern fixed line telephony networks being deployed around Europe by incumbent operators and by cable TV operators utilize fiber to the curb (FTTC), fiber to the building (FTTB) or fiber to the home (FTTH) to significantly increase bandwidth delivered to the end user. New built Networks based on IP protocols may gradually eliminate the traditional telephony equipment and copper access cables and will replace it by fiber optic cables and new generation optical transmission systems. Moreover, many incumbents are lobbying to receive relief from regulatory obligations for a period of time in order to improve their returns from such large investments. In the future it may also become possible for public authorities or public/private partnerships to gain access to investment subsidies that could lead to new sources of competition from NGN networks. New generation networks (NGNs), if deployed in Poland, could materially deteriorate the economic returns Netia plans to earn from regulatory access products such as bitstream, WLR and LLU. The Management Board can give no assurance that NGN networks will not be deployed in Poland by entities having access to public funding not available to Netia and, if this does occur, whether the regulator will ensure alternative network operators such as Netia enjoy fair access to such a network on acceptable economic terms.

In September 2013 Orange Polska S.A. announced the commercial launch of retail services based on the FTTH network. On November 29, 2013 Orange Polska S.A. concluded the agreement with Netia on providing Netia wholesale access to the FTTx network. Managemnet Board cannot assure that Orange Polska S.A.'s obligations, which are described in the agreement, would allow Netia to provide profitable and competitive retail services on conditions in the scope of using the telecommunications access.

Competition from cellular mobile telephone operators

In recent years, services offered by cellular telephone operators have negatively affected wire line telephone operators. This stems largely from mobile substitution, whereby subscribers choose to make telephone calls using their mobile phones in preference over fixed telephones, resulting either in less traffic or disconnections for fixed line operators. Mobile substitution becomes more pronounced as mobile tariffs decline, as they have in recent years, converging with traditionally lower cost fixed line tariffs. Similar substitution effects may also apply to broadband services, given the increased take-up of mobile broadband services offered by mobile operators.

To help mitigate the losses to mobile operators, Netia has begun to offer convergent products via a wholesale mobile service provider agreement to take mobile services, both voice and broadband, from P4 that Netia may then resell under the Netia brand to Netia customers. Although Netia's sales have been among the best achieved by the many mobile virtual network operators, those sales and margins have not been sufficient to materially offset lost margins from fixed services and these services are not currently a core focus of Netia's activity.

Since 2008, certain Polish mobile operators have been marketing fixed internet access services via the fixed access network of Orange Polska S.A., on the basis of regulated bitstream access decisions. This represents a significant new source of competition for market share in the fixed broadband market.

Competition from cable operators

Over the last several years, competition for voice and Internet services has increased from cable television operators. Triple play bundles (voice telephony, Internet access and cable television) have proven to be particularly challenging. Interactive TV services (IPTV) delivered by Companies of Netia Group offers fixed line telephone operators the ability to compete directly with cable television operators. The market importance of IPTV and related services (such as video on demand) is continually being analyzed in the context of Netia's strategy to expand its share of the broadband market. The Company is working on solutions to provide profitable TV services to its customers and expects that such services should reduce churn and increase margins per customer. However no assurance can be given that Netia will be successful in implementing a profitable TV service business model. Should such services be insufficiently well received by our existing and potential customers, it may adversely affect our revenues and margins in the future.

Market consolidation

Market consolidation through acquisitions remains an effective way for fixed line operators to strengthen their market position by utilizing the effects of scale. In the past Netia has successfully acquired several telecommunications operators making it the market leader for consolidation.

Whilst acquisitions of large scale telecommunications businesses are not crucial to the Company's strategy, Netia continues to closely monitor the situation of all its main altnet competitors and may choose to try to acquire one or more of these competitors in the future if the opportunity arises. Some acquisitions may consume a considerable portion of Netia's financial resources and no assurance can be given that expected synergies from such acquisitions will be reached as planned. In particular, acquisitions of other telecommunications enterprises or infrastructure are also likely to result in new regulatory risks or Netia Group companies' legal obligations, which cannot be predicted at the moment of acquisition and may increase costs of running the business for the Netia Group.

Certain potential acquisition targets, should they become available for sale, would require Netia to raise significant amounts of financial indebtedness and / or to issue new shares or equity related instruments in order to fund a transaction. The Management Board cannot guarantee that such funding will be available when needed on acceptable terms or that such an acquisition would not significantly increase the funding risk profile of the Netia Group.

Moreover, should we be outbid by a competitor on any particular large acquisition opportunity, our position as the leading alternative operator on the Polish telecommunications market and the strategic advantages that this position creates may be materially affected.

WiMAX license requirements

On October 27, 2005 Netia WiMax S.A. (merged with Netia in 2006) and Netia WiMax II S.A. (merged with Netia in 2008) received the reservations of the 3.6-3.8 GHz frequencies, which are used to provide telecommunication services based on the WiMAX technology. The terms of licenses issued to the Company's former subsidiaries require them to meet annual connected capacity milestones in the future, as measured at the end of each year, subject to demand in the territory and population of Poland. Considering changes in the telecommunications market and, in particular, the advent of regulated access to the fixed line network of the incumbent fixed line operator, Orange Polska S.A., the Company submitted applications to change future territorial and population coverage commitments for WiMax and on October 31, 2007 and on December 13, 2011 the Polish regulator issued decisions reducing the initial milestones. The Management Board can give no assurance that there will not arise any adverse circumstances which cannot be foreseen on the current stage of the construction of base stations and that they will not impede the fulfillment of the milestones established. In the event that reservation obligations are not met by an operator, the UKE has the power to limit or confiscate the reservation, if the entrepreneur is not able to assure effective use of possessed right. However, historically such measures have rarely been used.

Possible Material Claims (not in thousands)

On June 22, 2011 the European Commission has fined Orange Polska S.A. 127 mln Euro for abuse of its dominant position by obstructing access to its wholesale broadband products which took place from August 3, 2005 until at least October 22, 2009. Orange Polska S.A. has appealed this judgment. The final judgment in this case may allow Netia to make significant follow-on claims against Orange Polska S.A. at some point in the future.

Tax regulations and their interpretation

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

Dispute over Corporate Income Tax (CIT) paid for 2003 (not in thousands)

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

The decision of the Tax Chamber Director was issued despite legal arguments presented by the Company, which claimed that the conclusions delivered by the Tax Control Office were incorrect and groundless. According to the Tax Chamber Director and the UKS

Director, Netia understated its taxable income by PLN 247.5 million by excluding from its revenues the accrued and not received interest from loans granted by Netia in earlier years to subsidiaries which subsequently merged with Netia on December 31, 2003. The Director of UKS, as the first instance tax authority, claimed in its earlier decision that Netia understated its taxable income by PLN 303 million.

According to Netia, the decisions of the UKS Director and the Tax Chamber Director are in conflict with the relevant tax regulations. In addition to major procedural faults, Netia believes that the tax authorities' decisions incorrectly interpret and apply a number of material regulations. According to the Company the following are the most important deficiencies:

1. Incorrect interpretation of art. 11 of the CIT Act (which deals with transfer pricing), especially the notion of "services" and "more favorable conditions" and assumption that the non-commencement of the execution procedure constitutes such a service of the lender towards the debtor on non-market conditions. Such interpretation of this provision and its application towards the Company is not justified in the light of the fact that in the decision issued by the tax authorities it was confirmed that loans were granted on market terms; (interest, payment terms, etc.).

2. Failure to consider the absolutely mandatory prohibition on broadening the interpretation of art. 11 of the CIT Act, which covers exceptions from the principle of taxing actual revenue, without special care and consideration of all business, legal and economic circumstances. In the case of Netia the tax authorities did not take into account issues such as:

   - Netia was not able to report interest income in 2003 because even if Netia had received interest from its subsidiaries the amount received would have been spent on the repayment of Netia's interest liabilities (and the repayment of the interest would have been a tax deductible cost);

   - the execution of interest by court enforcement proceedings, which according to the Tax Chamber Director and the UKS Director is the only proper way to proceed when debts remain unpaid, would be inefficient from a business and economic point of view and would have led to the bankruptcy of the subsidiaries. The Company chose the less expensive way, by settling its receivables through merger with its subsidiaries and thereby taking over their operating assets. In parallel to this restructuring, Netia restructured its own liabilities with the external lenders to the group;

   - to assess Netia's conduct of non-commencement of a formal execution procedure (comparable market transaction) in the case of loans granted to its subsidiaries the tax authorities considered exclusively the loan granted by Netia to Millennium Communications; in fact, Netia was involved in numerous litigations with Millennium Communications due to the unsuccessful acquisition of that company by Netia.

3. Ignoring the norms of art. 12 of the CIT Act by rejecting in the decision the rule that exclusively interest received constitutes taxable revenue (on the cash basis) and leading to the situation where the tax payer's revenue is assessed in violation of general principles relating to the mode of revenue generation.

4. Netia's taxable losses were settled incorrectly, resulting in a significant overstatement of tax being claimed. Whilst the Tax Chamber Director has recognized some of the Company's corrections to the CIT calculation in respect to 2003, reducing the claimed amount by PLN 15 million, the Company continues to claim other increases in taxable expenses that the Tax Chamber Director has not accepted.

The Tax Chamber Director's decision, which partially upheld the decision of the UKS Director, was enforceable as a decision of the second instance tax authority. The liability of PLN 59.6 million was settled in February 2010, from which PLN 1.3 million was subsequently conceded by the Tax Authority as overpayment.

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

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

Consequently, in the first quarter of the year 2011, the Company recognized the taxes and related penalty interest already paid in 2010 as an income tax expense relating to the year 2003 of PLN 58,325 thousands.

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

On December 30, 2011 and February 22, 2012 Netia received further repayments of PLN 6.4m and PLN 1.4m, respectively, related to penalty interests paid previously by the Company and subsequently conceded by Tax Authority as incorrectly claimed. Netia's claim for PLN 51.9 m plus interest is now being treated as a contingent asset in the Netia Group's accounts.

On June 25, 2013 the Supreme Administrative Court in Warsaw set aside the appealed judgment upholding the decision of the Director of the Tax Chamber in Warsaw in its entirety and remanded the case for reconsideration to the first-instance court.

On October 10, 2013, the Voivodship Administrative Court in Warsaw annulled the Decision of the Director of the Tax Chamber in its entirety. In connection with the judgment so rendered, the Tax Chamber Director is required to reconsider the Company's appeal against the Decision of the UKS Director, taking into account the legal assessment and recommendations contained in the judgments of the Voivodship Administrative Court and the Supreme Administrative Court as to how to proceed with the matter.

Having received the ruling of the Voivodship Administrative Court, on 30 December 2013, the Company has filed a cassation appeal against the judgment of the Voivodship Administrative Court in Warsaw due to the justification of the judgment of the WSA not fully reflecting the position presented by the Company during the Supreme Administrative Court proceedings. The Tax Chamber did not lodge on appeal to the Supreme Administrative Court in respect to this decision.

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

Although the Management Board is committed to taking all possible legal steps to win this claim and continues to hold the view that the Company's legal arguments are strong, the Management Board can give no assurance that any or all of these amounts will be ultimately recovered from the tax authorities nor how long it may take to finally close these proceedings with a definitive conclusion.

2.2 Factors and events having a significant influence on the operations of the Netia Group and the financial results achieved in 2013

Operational data (not in thousands)

Broadband

Broadband subscribers of Netia Group decreased to 848,909 at December 31, 2013 from 874,778 a year earlier. Netia estimates that its total fixed broadband market share was approximately 12.7% versus 13.3% at December 31, 2012. Slow market growth and tougher price competition, including cable operators offering multiplay bundles, is reflected in the performance. Management is focusing on its own network and bundled services rather than regulated access or total services sold in order to defend gross margins. Of the total broadband customers served at December 31, 2013, 47% received service over Netia's own access infrastructure as compared to 46% at December 31, 2012.

Netia Group provides its broadband services using the following technologies:

Number of broadband ports	**2013**	**2012**
xDSL and FastEthernet over Netia's own fixed-line network	386,787	382,540
Bitstream access	276,857	291,621
WiMAX Internet	15,353	17,891
LLU	169,912	182,726
Total	**848,909**	**874,778**

Broadband ARPU was PLN 56 in Q4 2013 as compared to PLN 57 in Q4 2012. Netia's conservative pricing policy and focus on higher value customer segments has resulted in a solid ARPU performance over the past year, despite deep price cuts introduced by some of Netia's competitors.

Broadband SAC was PLN 164 as compared to PLN 178 in Q4 2012.

Acquisitions of local Ethernet network operators

As of December 31, 2013, Netia's Ethernet networks provided broadband access to a total of 110,754 mostly residential customers as compared to 121,005 customers at December 31, 2012, with approximately 621,000 homes passed. Netia is currently focused on upgrading Ethernet networks already acquired and therefore will likely acquire new networks at a much slower pace than seen in the past, if at all. There were no additions of Ethernet networks completed during 2013.

NGA network development

As at December 31, 2013, Netia covered in total 1,281,000 households with its NGA networks, including 148,000 PON HPs, 897,000 VDSL HPs and 236,000 Ethernet FTTB HPs. During Q4 2013 Netia expanded its NGA coverage by approximately 41,000 HPs (being 31,000 FTTB HPs, 9,000 VDSL HPs and 1,000 PON HPs). Moreover, at December 31, 2013 Netia covered a further 172,000 TV ready HPs within its network coverage based on ADSL2+ technology. Combined with NGA ready HPs, all of which can deliver TV services, Netia had 1,453,000 TV ready HPs in its proprietary network coverage.

Netia has advanced plans to expand its NGA coverage by another 440,000 or more HPs inclusive of the recent acquisition of cable networks from UPC Polska. Once all upgrade projects are completed, Netia expects to cover in total approximately 1,720,000 NGA HPs which can be reached with 3play service bundles (TV + fixed NGA broadband + fixed voice). Furthermore, Netia has introduced smooth streaming technology, which expands the availability of its 3play bundle offer onto networks where line speeds are too slow to support IPTV and, potentially in the future, to homes where Netia does not provide the broadband connection. Management is presently focusing on optimizing sales, provisioning and maintenance processes around TV services in addition to constant development of the content offering and service functionalities in the course of 2014.

(All amounts in thousands, except as otherwise stated)

TV services

TV services totaled 120,321 at December 31, 2013 as compared to 79,285 at December 31, 2012.

Mobile services

The mobile broadband customer base totaled 26,397 at December 31, 2013 as compared to 30,281 at December 31, 2012. Mobile broadband ARPU was PLN 27 in Q4 2013 as compared to PLN 26 in Q4 2012. Mobile voice services totaled 42,120 at December 31, 2013 as compared to 60,219 at December 31, 2012.

Mobile voice ARPU was PLN 29 in Q4 2013 as compared to PLN 26 in Q4 2012. Mobile broadband has similar economics to BSA services whilst mobile voice has benefited from improved terms of MVNO agreements with partners P4 and Polkomtel.

Voice lines (own network and WLR)

Voice lines totaled 1,488,610 at December 31, 2013 as compared to 1,643,904 at December 31, 2012. In Q4 2013 Netia recorded a net decrease of 30,655 voice lines versus 33,862 voice lines in Q4 2012. The Company expects the number of fixed voice lines to continue to decline, mainly due to clients churning from traditional direct voice and WLR services.

The aggressive price competition from other providers on the market together with substitution from mobile and migrations to voice bundled with cable TV, has been putting pressure on the fixed voice subscriber base whilst Netia has been targeting higher ARPU customers and upselling unlimited fixed-line national call bundles in order to attract higher value customers. With respect to the off-net (WLR) customer base, the Company is chiefly focused on retention of clients and defending cash flows while Netia is more aggressively defending its on-net base through bundling in B2C and discounting in B2B.

Netia is steadily growing its base of relatively low cost VoIP customers, principally in the business segments. Over time, the Company expects to gradually reduce its reliance on traditional switched telephony, thereby reducing its cost base. The net decline during Q4 2013 in services was 1% on LLU voice over IP services and 4% on lower margin WLR services while higher margin own network services remained stable sequentially thanks to the more aggressive re-pricing policy.

Netia provides its voice services through the following types of access:

Number of voice lines	**2013**	**2012**
Traditional direct voice	532,639	563,753
Voice over IP*(excl. LLU)*	93,969	69,359
WiMAX voice	11,983	14,663
WLR	728,693	869,196
LLU voice over IP	121,326	126,933
Total	**1,488,610**	**1,643,904**

Voice ARPU per WLR line was PLN 45 in Q4 2013 as compared to PLN 45 in Q4 2012.

Voice ARPU per Netia network subscriber line was PLN 39 in Q4 2013 as compared to PLN 46 in Q4.

Blended voice ARPU was PLN 42 in Q4 2013 as compared to PLN 46 in Q4 2012 and PLN 43 in Q3 2013.

Indirect voice

CPS lines (carrier pre selection) totaled 55,922 at December 31, 2013 as compared to 62,241 at December 31, 2012. Netia is focused on the conversion of CPS customers to WLR and is not actively acquiring new CPS customers. CPS clients are not reflected in the total voice subscriber base of 1,488,610 clients as at December 31, 2013.

Indirect voice ARPU per CPS line was PLN 24 in Q4 2013 as compared to PLN 37 in Q4 2012. Tariff reductions, reduced call volumes and conversion of higher ARPU customers to Netia's WLR or LLU offers are responsible for the progressive ARPU decline.

2.3 Agreements essential for the Netia Group's operations

A four-year agreement with Ericsson

On August 14, 2012, Netia together with its subsidiaries signed a four-year managed services contract with Ericsson replacing the existing managed services contract signed on August 12, 2010. The contract covers the maintenance and management of the Netia Group's networks, as well as supporting the provision of services to Netia Group's residential and business customers. Whilst similar in scope to the previous agreement, the new agreement covers managed services for the Dialog Group and Crowley networks and, in addition, modifies certain pricing and operational parameters (KPIs) concerning the provision of services by Ericsson to the Netia Group. Based on the agreement 188 of the Netia Group's employees were transferred to Ericsson on the basis of art. 23' of the Labour Code. The cooperation with Ericsson will influence the reduction of maintenance and employment costs, more effective and integrated handling and management of Netia Group's networks and its service delivery. While the extended cooperation with Ericsson represents a material long term commitment on the part of Netia Group, Management does not expect it to have a material impact on profitability or cash flows of the Group over the life of the contract.

3 Financial condition of the Netia Group

3.1 Consolidated statement of financial position

As at December 31, 2013, non-current assets amounted to PLN 2,620,649 (89% of total assets) as compared to PLN 2,776,644 at the end of 2012 (86% of total assets). The main change within non-current assets relates to depreciation and amortization charge of PLN 439,994. The above change was partially offset by capital expenditures of PLN 275,772 incurred during the year ended December 31, 2013 and transfer of assets of PLN 26,770 held for sale as of the prior year end to investment property.

Current assets at December 31, 2013 in the amount of PLN 316,987 decreased by 26% as compared to PLN 429,571 at the end of 2012. The change was mainly attributable to the decrease in the Company's trade receivables and cash balance as at December 31, 2013 as compared to the end of 2012.

As at December 31, 2013, the equity amounted to PLN 2,204,504, comprising 75% of total equity and liabilities and decreased by 4% as compared to PLN 2,296,295 at the end of 2012. The main changes are the repurchase of own shares of PLN 144,198 and the consolidated total income of PLN 50,007 in the year ended December 31, 2013 (the main factors influencing the net result are described in point "Factors and events having a significant influence on the operations of the Netia Group […]").

Non-current liabilities amounted to PLN 316,738 and decreased as compared to PLN 451,066 at the end of 2012, mainly due to repayment of term loan installments of PLN 130,000 in 2013. The long-term part of the term loan as of December 31,2013 amounted to PLN 257,211 as compared to PLN 384,452 as at the end of the prior year.

As at December 31, 2013, current liabilities amounted to PLN 416,394 and decreased as compared to PLN 485,624 at the end of 2012, mainly due to lower balnce of trade and other liabilities as of December 31, 2013 and the repayment of a bank overdraft of PLN 18,751 and interests accrued on the loan of PLN 20,547 as of December 31, 2012

3.2 Consolidated income statement

Revenue decreased by 12% to PLN 1,876,016 for 2013 from PLN 2,121,356 for 2012. The B2C operating segment decreased by 12% or PLN 149,335 and the B2B segment by 11% or PLN 92,829. The decline in revenues was driven by a 6% decline in services provided (RGUs) and by falls in mobile termination rates (MTRs) which contributed approximately one third of the revenue decline. RGU declines continued to be concentrated in the B2C (Home) sub-segment and in fixed voice services and lower margin WLR services in particular. The proportion of RGUs delivered on-network has increased from 43% to 45% in the twelve months to December 31, 2013.

Telecommunications revenue decreased by 11% to PLN 1,867,592 in 2013 from PLN 2,108,708 in the prior year, driven by a 15% or PLN 139,267 decrease in direct voice revenue to PLN 809,188 from PLN 948,455 in 2012, associated with the decrease in the voice subscriber base and the drop in the number of WLR services in particular. Data revenue decreased by 5% or PLN 40,937 to PLN 724,721 from PLN 765,658 in 2012, mainly due to the lower number of BSA services. Revenues from interconnect and carrier services combined were down by 22% to PLN 192,291 from PLN 245,830 in 2012 following the introduction of lower MTRs in July 2012, in January 2013 and again in July 2013. Indirect voice services (CPS) revenue decreased by 45% or PLN 15,773 as a result of decreasing customer numbers and falling ARPUs. Other telecommunications revenue, which include TV and mobile services, increased between the compared periods by 7% or PLN 8,400 to PLN 122,189 in 2013 from PLN 113,789 in 2012 and represented 7% of total revenue versus 5% in the prior year. Direct voice revenue as a share of total telecommunications revenue declined from 45% to 43% and data revenue increased over the same period from 36% to 39%.

Cost of sales decreased by 15% to PLN 1,265,342 from PLN 1,484,216 for 2012 and represented 67% of total revenue as compared to 70% in the prior year. Lower interconnection costs following cuts to MTRs, a relatively faster decline in off-net services and synergies from Dialog Group and Crowley integration and lower depreciation and amortization expenses were the main drivers of the decreasing share of costs in relation to revenue.

Interconnection charges decreased by 34% to PLN 201,301 in 2013 as compared to PLN 306,056 for 2012, due to falling MTRs.

Network operations and maintenance cost decreased by 8% to PLN 593,399 from PLN 647,586 for the prior year due to synergies from Dialog Group and Crowley integration and less off-net RGUs, partly offset by an increase in outsourced maintenance costs after transferring Dialog and Crowley network maintenance to Ericsson.

Depreciation and amortization related to cost of sales decreased by 9% to PLN 359,562 as compared to PLN 394,143 for 2012 following the reassessment of useful lives of the Netia Group's fixed assets in Q1 2013, resulting in reduction of depreciation rates.

Taxes, frequency fees and other expenses decreased by 12% to PLN 68,893 in 2013 as compared to PLN 78,122 for 2012, due to synergies from Dialog Group and Crowley integration.

Salaries and benefits related to the cost of sales decreased by 22% to PLN 32,175 from PLN 41,101 for 2012 following the headcount reduction process started in June 2012 in connection with the integration of Netia, Dialog Group and Crowley into the New Netia Group and the transfer of Dialog and Crowley maintenance staff to Ericsson in September 2012.

Gross profit for 2013 was PLN 610,674 as compared to PLN 637,140 for 2012, a drop of just 4% despite revenue falling by 12%. Gross profit margin was 32.6% for 2013 and 30.0% for 2012. Increasing share of revenue from higher margin own-network services as well as synergies from the Dialog Group and Crowley integration, together with lower MTRs and lower depreciation charges mentioned above, are responsible for the improving percentage gross margin achieved.

Selling and distribution costs decreased by 9% YoY to PLN 358,526 from PLN 392,069 for last year and represented 19% of total revenue as compared to 18% in 2012. Synergies from Dialog Group and Crowley integration together with lower direct acquisition costs from fewer gross additions were the main drivers of the decreasing costs.

Outsourced customer service cost decreased by 52% to PLN 14,375 from PLN 30,034 due to extracting integration synergies and increased use of internal customer care resources.

Billing, mailing and logistics costs decreased by 32% YoY to PLN 28,237 from PLN 41,431 while the average number of RGUs served fell only by 6% between the two years due to integration synergies.

Depreciation and amortization related to selling and distribution cost decreased by 16% to PLN 50,519 from PLN 59,981 in 2012 following the full amortization of certain intangible assets related to computer software and telecommunications licenses.

Third party commissions decreased by 20% YoY to PLN 22,854 from PLN 28,503 due to lower gross additions, particularly in voice services.

Impairment of receivables was higher by 6% and PLN 737 as the prior year benefited from a one-off adjustment to the debt provision to reflect improving recovery rates. Provisions for doubtful debts for 2013 are nevertheless running at a moderate 0.7% of sales.

Advertising and promotion cost increased by 7% YoY to PLN 39,080 for 2013 as compared to PLN 36,663 for 2012 in connection with more intense advertising towards the year-end and introduction of a new company claim and communication platform.

Other expenses related to selling and distribution were higher by 25% and PLN 13,554 mainly on increased cost of TV content for a 52% higher base of TV customers.

General and administration costs decreased by 14% YoY to PLN 179,186 from PLN 207,610 for 2012 and represented 10% of total revenue in both 2013 and 2012. Synergies from Dialog Group and Crowley integration were the main drivers of the cost decrease.

Salaries and benefits related to general administration cost decreased by 16% to PLN 77,193m from PLN 92,198 in 2012, reflecting mainly the headcount optimization process conducted in 2012 in connection with the Dialog Group and Crowley integration into the Netia group.

Other costs related to general administration cost decreased by 21% to PLN 29,177 from PLN 36,993 in 2012, due to significantly lower integration costs as the scale of the project is reduced with most synergy initiatives now completed.

Office and car maintenance costs decreased by 15% or PLN 2,650 between the periods due to extraction of integration synergies.

Professional services costs decreased by 14% or PLN 1,589 principally due to integration synergies.

Electronic data processing cost increased by 22% or PLN 2,973 in connection with the on-going integration projects such as migration of Dialog's and Crowley's customer bases to Netia.

Adjusted EBITDA was PLN 550,855, down by 7% from PLN 591,166 for 2012 as lower revenue was partly offset by higher percentage gross margins and lower SG&A expenses. Adjusted EBITDA margin was 29.4% as compared to 27.9% in 2012. Higher Adjusted EBITDA margin reflects Dialog Group and Crowley integration synergies and lower base of both revenue and cost from MTR reductions, partially offset by falling gross profits from contracting voice services.

Including the Dialog Group and Crowley integration costs of PLN 9,500 in 2013 and PLN 26,276 in 2012, restructuring costs of PLN 3,631 in 2013 and PLN 22,656 in 2012, impairment charge of PLN 431 in 2013 and PLN 79,203 in 2012, the costs of M&A projects of PLN 618 in 2013 and PLN 1,504 in 2012, a decrease in provision for universal service obligation of PLN 150 recorded in 2013, PLN 2,603 impairment charge relating io investment property recorded in 2013, and cost reorganisation of PLN 1,469 recorded in 2013, **EBITDA** was PLN 532,753 for 2013 as compared to PLN 461,527 for 2012. EBITDA margin was 28.4% as compared to 21.8% for 2012.

Operating profit (EBIT) was PLN 92,759 as compared to an operating loss of PLN 20,964 for 2012. Excluding unusual items described above of PLN 18,102 of net costs in 2013 and PLN 129,639 of costs in 2012, Adjusted EBIT was PLN 110,861 profit for 2013 versus PLN 108,675 profit for 2012.

Net financial cost was PLN 28,339 as compared to net financial cost of PLN 39,942 for the prior year and the improvement is driven by the falls in net debt and in market interest rates between the periods.

Income tax charge of PLN 18,130 was recorded in 2013 as compared to income tax charge of PLN 26,798 for 2012.

Net profit was PLN 46,290 for 2013 versus net loss of PLN 87,704 for 2012.

3.3 Consolidated statement of cash flows

Net cash generated from operating activities by Netia Group amounted to PLN 575,271 as compared to PLN 541,386 in 2012. The increase was principally due to a fall in working capital employed.

Net cash used for the purchase of fixed assets and computer software was PLN 281,826 and was higher by 7% than PLN 262,506 in the prior year. Other significant spending on investment activities in 2012 were purchases of Ethernet operators, net of cash received of PLN 5,285 and purchase price adjustment to Crowley of PLN 4,323.

Other significant cash outflow items during 2013 in Netia Group included PLN 180,000 of loans repaid and 53,917 PLN of interests and fees paid and PLN 144,198 of repurchased own shares. As a result net cash used in financing activities in 2013 amounted to PLN 327,050 as compared to PLN 303,505 of net cash used in financing activities in 2012.

Cash and cash equivalents at the end of 2013 amounted to PLN 93,356 as compared to PLN 123,951 as of December 31, 2012.

3.4 Financial resources management and assessment of the possibility of executing the planned investments

Following its new strategy announcement in April 2007, Netia invested in broadband and other services such that free cash flows was negative in 2007 and 2008. In 2009, the Netia Group began to generate free cash flows once more and this trend of improving cash flows continued into 2012 with the acquisition of Dialog Group and Crowley and the realization of related synergies. Although synergies from integration grew further in 2013, total adjusted free cash flow in 2013 fell by 7% to PLN 311mln. Nevertheless, Management expects Netia to continue be free cash flow positive in the medium term, subject to the impact of any or all risk factors indicated in section "Major risks and threats related to the operational activities. For 2014 the Group is guiding for adjusted free cash flow of PLN 305mln. As at December 31, 2013, the Group's equity amounted to PLN 2,204,504 and the Netia Group had negative net working capital of PLN 99,407 inclusive of cash available of PLN 93,356. As at December 31, 2013 the Netia Group had senior secured debt of PLN 384,077. In addition, the Netia Group had a further PLN 200,000 of undrawn senior secured debt facilities available for the financing of capital expenditures and operating expenses of the Netia Group and for payments to shareholders of the Company. Netia's operations were free cash flow generative in 2013 and Management expects this to continue over the medium term. Based on this position, the Management does not believe that events or conditions exist which may cast significant doubt on the Company's ability to continue as a going concern.

A detailed description of risks related to the Netia Group's financial instruments has been presented in the consolidated financial statements (Note 4).

3.5 Loans Agreements

Bank loans

On September 29, 2011, Netia and Internetia Sp. z o.o. (the "Borrowers") executed a loan agreement (the "Agreement") with Rabobank Polska S.A. (the "Facility Agent"), BNP Paribas S.A., BRE Bank S.A., Raiffeisen Bank Polska S.A. and Raiffeisen Bank International AG (jointly with the Facility Agent, the "Lenders"), whereunder the Lenders agreed to extend to the Borrowers a term facility maturing in five years with a total of PLN 650,000, designated for the Company to acquire 19,598,000 (not in thousands) shares in Dialog, constituting 100% of its share capital, and a PLN 50,000 revolving facility for general operating purposes. The term loan was drawn on December 16, 2011 and the revolving loan was drawn on December 15, 2011. According to the agreement, the term loan is to be repaid in 10 equal semi-annual instalments of PLN 65,000 each. The maturity date falls on November 30, 2016. The revolving loan was repaid in full on March 15, 2012. In 2012 the Company repaid PLN 130,000 of instalments and further PLN 130,000 was repaid in 2013. On March 7, 2013 the Company again drew down the revolving loan of PLN 50,000, repaying it in full once more on July 8, 2013 and then cancelled the revolving facility on July 9, 2013.

As at December 31, 2013 the value of these outstanding loans at amortised cost was PLN 384,077.

The term loan accrue annual interest at the rate of 3M WIBOR plus a margin established depending on the level of debt relative to the Group's profitability. The terms and conditions of the Agreement comply with market practice and are not different from the terms and conditions generally applied to such types of agreements. The borrowing is measured at amortized cost using an effective interest rate, which as of December 31, 2013 was 5.7%. Total transaction costs included in the calculation of the effective interest rate amounted to PLN 10,611.

To secure the Lender's claims under or related to the Agreement, the Borrowers agreed to establish in favour of the Lenders mortgages, financial and registered pledges and to to grant relevant submissions to execution. The repayment of the loan is secured by the following the mortgage over certain Company's rights of perpetual usufruct at ul. Poleczki 13 in Warsaw, registered pledge over collection of movables and rights of the Company and registered and financial pledges over shares in Internetia sp. z o.o., Netia Brand Management sp. z o.o., Telefonia Dialog sp. z o.o. and Petrotel sp. z o.o. Additionally, Internetia sp. z o.o., Netia Brand Management Sp. z o.o. and Telefonia Dialog sp. z o.o., each of them, established security in the form of registered pledges over collection of movables and rights and granted the submission to execution for the benefit of each of the Lender. The maximum secured amount with respect to the applicable pledges, mortgages and submission to executions does not exceed PLN 1,476,750.

On March 8, 2012, Netia entered into an overdraft credit facility agreement with BRE Bank S.A. of PLN 50,000. The facility may be disbursed for general operating purposes of the Company. The Company is entitled to become indebted under the overdraft credit facility agreement in the period between March 12, 2012 and May 29, 2014. The terms and conditions of the agreement comply with market practice and are not different from the terms and conditions generally applied to such types of agreements. The Company had no outstanding balance under the overdraft credit as at December 31, 2013.

On June 20, 2013, the Company and Internetia Sp. z o.o. (the "Original Guarantor"), Netia Brand Management Sp. z o.o. (the "Additional Guarantor") and Dialog (the "Additional Guarantor") executed an annex to the Agreement with the Lenders under which the Lenders agreed to extend to the Borrower an additional PLN 200,000 amortising five year term facility, designated for the financing of capital expenditures and operating expenses of the Netia Group and for payments to shareholders of the Company (the "Additional Loan Facility"). The Additional Loan Facility can be drawn until December 20, 2014. According to the annex, the terms and conditions of the Additional Loan Facility including the interest and margin are essentially the same as set forth in the Loan Agreement. To secure the

Lenders' claims under or related to the Additional Loan Facility the Borrower and the Guarantors agreed to establish in favour of the Lenders mortgages, registered pledges and to make relevant representations on submission to enforcement.

As of December 31, 2013 and as of the date of the publication of the consolidated financial statements the Company has not drawn any loan under the Additional Loan Facility. Transactions costs and commitment fees of PLN 2,526 were deferred as of December 31, 2013.

3.6 Bonds issued and warranties and collaterals granted

Bonds issued

The Company did not issue any bonds except for those described in Note 6.1 Transactions with related parties.

Warranties and collaterals granted

Netia Group did not grant any warranties or collaterals in 2013, except for described in Note 3.5 Loans Agreements.

4 The Company's supervisory or governing authority

4.1 Rights of the Supervisory and Management Board's members

According to the Company's Statute the bodies of the Company are the General Shareholders' Meeting ("GSM"), the Supervisory Board and the Management Board.

GSM operates in accordance with the rules set forth in the Commercial Companies Code and the Company's Statute. GSM decides in matters provided for in the Commercial Companies Code, and in particular regarding decisions on the division and distribution of profit. No approval of the GSM is required for the purchase or sale of the right of real estate ownership, the right of perpetual usufruct or share in such right, without limitations upon the value of such transaction. The Company has not adopted any by-laws of the GSM. Amendments of the Company's Statute need to be adopted by 3/4 majority of the votes cast.

The Supervisory Board shall consist of up to 9 members. Members of the Supervisory Board shall be elected and dismissed by the GSM for a term of office of 5 years. One member of the Supervisory Board shall be appointed and dismissed by holders of series A1 shares. At all times at least two of the Supervisory Board members shall be "independent".

The competency of the Supervisory Board shall include general supervision of the activities of the Company. Resolutions of the Supervisory Board shall be required in matters provided for in the Commercial Companies Code and:

a) presentation to the Company's GSM of a written report on the results of the Supervisory Board's examination of the Company's financial statements, Management Board report and Management Board's recommendations with respect to the distribution of profits or coverage of losses;
b) the issuance of by-laws for the Management Board and the appointment and removal of the members of the Management Board, setting or changing the compensation and defining other terms and conditions of employment of the Management Board members, as well as setting and changing any incentive plan for the Management Board members and other key employees;
c) approval of business plans and budgets for the Company;
d) granting consent for any transaction whose value exceeds the PLN equivalent of EUR 1,250 in a single or a series of related transactions, or in the course of one year in the case of agreements entered into for unlimited duration or for periods longer than one year;
e) making any investments in or financing the activities of companies whose core and actual scope of business activity does not include telecommunications activity;
f) consent to the commencement, settlement, assignment, compromise or release of any claim of or against the Company in excess of the PLN equivalent of EUR 600 in a single or series of related acts or the equivalent amount in PLN or other currencies;
g) consent to the adoption of a performance stock option plan in accordance with § 5A of the Statute;
h) appointment of the expert auditor to audit the Company's financial statements;
i) provided that the value of the Company's obligations exceeds the PLN equivalent of EUR 100, the conclusion by the Company of any contracts with an Affiliate shall; require the approval of at least one of the independent members. For the purposes of this point, an "Affiliate" shall mean: (i) a member of the Management Board or Supervisory Board of the Company or the cousin or relative of up to the second degree of such member, or an entity controlled by such person or their cousin or relative of up to the second degree; (ii) a shareholder holding shares entitling it to at least 5% of votes at the General Meeting; or (iii) an entity controlled by, controlling or under common control with the persons listed under (i) and (ii); (iv) an entity in which the Company has, directly or indirectly, any equity stakes or voting powers. "Control" shall mean the possibility of exerting influence, whether direct or indirect, on the management or business policy of the controlled entity through holding voting shares in such entity, under a shareholders' agreement, an agreement for official receivership of votes (umowa syndykowania głosów) or in any other similar manner, even if not connected with a written agreement. For the purposes of the above definition, "control" shall not apply to any companies controlled by Netia S.A.

The Management Board of the Company shall consist of up to 10 members. The Supervisory Board shall decide on the number of Management Board members. The Management Board members shall be appointed and dismissed by the Supervisory Board for a term of office of 5 years.

The Management Board shall manage the activities of the Company, shall adopt resolutions necessary for performance of tasks and shall represent the Company before courts, authorities, offices and third parties. The Management Board shall handle the matters, which are not within the exclusive competence of the GSM or the Supervisory Board. Two members of the Management Board acting together or one member of the Management Board acting together with a commercial proxy (prokurent) shall be authorised to make declarations and to sign on behalf of the Company.

The members of the Management Board do not have any rights related to deciding about the issue or redemption of the Company's shares.

4.2 Management Board and Supervisory Board in 2013

Management Board

As at December 31, 2013 and December 31, 2012 the Company's Management Board consisted of the following members:

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

On November 21, 2013 Supervisory Board appointed Mr. Tomasz Szopa as member of the Management Board, effective February 3, 2014.

Supervisory Board

On June 28, 2013 the Annual General Meeting of the Company determined the number of the Supervisory Board members at nine persons and appointed Mr. Jerome de Vitry as member of the Supervisory Board for the next term of office and Mr. Jacek Czernuszenko as a new member of the Supervisory Board.

On 13 November 2013 Mr. Benjamin Duster resigned from his position as a Chairman and member of the Company's Supervisory Board. The resignation is effective from the date of the resignation.

Effective from November 21, 2013, Mr. George Karaplis was appointed as Chairman of the Supervisory Board.

Due to the above change as at December 31, 2013 the Company's Supervisory Board consisted of the following members:

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

On January 13, 2014 the Extraordinary General Meeting of the Company appointed Mr. Bogusław Kułakowski as an independent member of the Supervisory Board.

4.3 Supervisory board's standing committees

Two committees have been acting within the Supervisory Board since April 5, 2006: Audit Committee and the Nomination and Remuneration Committee. During the year 2013 the membership of the committees was as follows:

Audit Committee:
- Raimondo Eggink – the Chairperson of this Committee,
- Tadeusz Radzimiński,
- Ewa Pawluczuk

Nomination and Remuneration Committee:
- Jacek Czernuszenko – from December 3, 2013.
- Ben Duster – until November 13, 2013
- Mr. Nicolas Maguin – from 30 April, 2013
- Tadeusz Radzimiński
- Jerome de Vitry – until April 30, 2013

In 2009 the Supervisory Board established another standing committee – Capital Investment Committee consisting of:

- Stan Abbeloos, - the Chairperson of this Committee from March 27, 2013,
- Jacek Czernuszenko – from October 18, 2013.
- George Karaplis
- Nicolas Maguin
- Jerome de Vitry
-

On April 26, 2013 the Supervisory Board established another standing committee – Strategic Committee consisting of:

- Mr. Jerome de Vitry – the Chairperson of this Committee,
- Jacek Czernuszenko – from October 18, 2013.
- Ben Duster – until October 18, 2013
- Raimondo Eggink
- George Karaplis

Moreover, on April 26, 2013 the Supervisory Board established ad hoc Committee: Product Development Committee consisting of:

- Mr. George Karaplis – the Chairperson of this Committee,
- Ms. Ewa Pawluczuk
- Mr. Tadeusz Radzimiński

In February 2014 the following changes took place:

- Geaorge Karaplis and Jacek Czernuszenko resigned from Capital Investment Committee.
- Jacek Czernuszenko was appointed as a member of Product Development Committee.
- Stan Abbeloos was appointed as a member of Product Development Committee.
- Bogusław Kułakowski was appointed as a member of Audit Committee and Strategic Committee.
- Nicolas Maguin was appointed as a member of Product Development Committee.

Supervisory Board Members receive additional remuneration for serving on Committees (up to a limit of two committees for a Member and one for a Chairman).

The duties of the Audit Committee include advising the Supervisory Board on issues of proper implementation of the budget and financial reporting standards and internal audit of the Company and the capital group (as defined in the Accounting Act dated 29 September 1994, as amended), including the overall and comprehensive review of the Company's annual and periodic financial statements, both unconsolidated and consolidated, analysing the Company's authorised auditor's letters to the Management Board, monitoring the integrity of the financial information provided by the Company, cooperating with external and internal auditors of the Company, as well as with the Company's departments responsible for audit and checking, reviewing internal control and risk management systems. The Audit Committee meetings are held at least once every quarter prior to the Company's publication of the financial statements.

The duties of the Nominations and Remuneration Committee is to support the Company's achievement of its strategic objectives by presenting the Supervisory Board with opinions and motions related to the shaping of the management structure, including on organisation solutions, the remuneration system and selection of personnel having the qualifications required to ensure success of the Company.

The duties of the Capex Committee are, among others, monitoring key drivers of capital investment spendings within the Netia group in order to be able to properly advise the Supervisory Board on capital investments, reviewing Management's proposals for the annual capital investment budget and monitoring progress on implementation of such budget.

The Strategic Committee's tasks are to provide support to the Supervisory Board on, amongst others, the following issues:
- areas of future development for the Company,
- mergers and acquisitions,
- review of all other areas or matters which have a strategic dimension for the Company.

The principles, scope and methods of operation of the Supervisory Board Committees have been regulated in detail in the By-laws of the Supervisory Board of Netia SA.

4.4 System for controlling employee share option plans (not in thousands)

New Plan

On May 26, 2010, the Annual Shareholders Meeting resolved to adopt a set of rules, to be administered by the Company's Supervisory Board, for the issuing of up to 27,253,674 share options to the Management Board and employees of Netia, each option authorising its holder to receive, free of charge, up to ½ of a subscription warrant issued by the Company with the latest possible exercise date of May 26, 2020 (the "New Plan"). Each warrant entitles its holder to subscribe for one series L share for the nominal value of PLN 1, which shall be paid by the Company or its subsidiaries. In order to satisfy the claims arising from the exercise of the options under New Plan, the Shareholders Meeting resolved to authorize the issuance of up to 13,626,837 series L shares.

The New Plan participants are entitled to exercise their stock options on the condition that they continue their engagement with the Netia Group until the vesting date of the stock options (subject to change of control events and the termination of their engagement by the Netia Group without material cause) and the fulfilment of the business criteria set by the Supervisory Board for each year of the New Plan. In the event of termination by the Company, unvested options are retained prorata to the period worked during the vesting period. The proportion of the stock options exercised versus the number of stock options granted shall be equal to the lower of: 100% or the actual performance of the objectives set out as part of the performance criteria approved by the Supervisory Board and applicable in the financial year in which the stock options were granted. Each year within the period following the publication of the financial statements of the Company for the previous financial year and prior to the date of the Annual General Meeting of the Company, the Supervisory Board adopts a conditional resolution in which it determines the performance level of the business criteria for the previous financial year. The resolution of the Supervisory Board enters into force upon the approval of the financial statements of the Company and the Netia Group by the Annual General Meeting of the Company. Such conditional resolution of the Supervisory Board regarding the performance criteria for 2011 was taken on April 25, 2012 and the performance level was determined at 58.9%. The resolution came into force on June 19, 2012 and resulted in the cancellation of 41.1% of options granted in 2011. A conditional resolution of Supervisory Board regarding the performance criteria for the 3,669,000 options granted in 2012 was taken on February 26, 2013 and the performance level was determined at 68.6%. The resolution of the Supervisory Board came into force on June 28, 2013 and resulted in the cancellation of 31.4 % of options granted in 2012.

The amount of the reduction for the 3,669,000 options granted in 2013 is dependent on the Supervisory Board's assessment of performance against the agreed criteria for 2013. As at the date of this Directors' Report, that assessment had yet to take place.

4.5 Remuneration paid and payable to the members of the Management Board and the Supervisory Board in 2013

The compensation and related cost of remuneration (including bonuses paid or accrued) of members of the Company's Management and Supervisory Board are presented below:

	PLN
Remuneration of members of the Management Board	
Mirosław Godlewski	1,588
Jonathan Eastick	1,489
Tom Ruhan	1,177
Mirosław Suszek	1,156
	5,410

Remuneration of members of the Supervisory Board	PLN
Benjamin Duster	104
Jacek Czernuszenko	46
George Karaplis	112
Stan Abbeloos	96
Raimondo Eggink	112
Nicolas Maguin	114
Ewa Pawluczuk	112
Tadeusz Radzimiński	120
Jerome de Vitry	120
	936
Remuneration of members of management boards of subsidiaries	687
Remuneration of members of supervisory boards of subsidiaries	2
Total	**7,035**

The members of the Company's Management and Supervisory Boards do not collect any additional remuneration for being members of the authorities of the subsidiaries.

In addition, the members of the Management participate in a scheme which consists of awarding bonuses in the form of Netia's shares, under which some of them have received share options.

New Plan (not in thousands)

On May 26, 2010, the Annual Shareholders Meeting resolved to adopt a set of rules, to be administered by the Company's Supervisory Board, for the issuing of up to 27,253,674 share options to the Management Board and employees of Netia, each option authorising its holder to receive, free of charge, up to ½ of a subscription warrant issued by the Company with the latest possible exercise date of May 26, 2020 (the "New Plan"). Each warrant entitles its holder to subscribe for one series L share for the nominal value of PLN 1, which shall be paid by the Company or its subsidiaries. In order to satisfy the claims arising from the exercise of the options under New Plan, the Shareholders Meeting resolved to authorize the issuance of up to 13,626,837 series L shares.

The New Plan participants are entitled to exercise their stock options on the condition that they continue their engagement with the Netia Group until the vesting date of the stock options (subject to change of control events and the termination of their engagement by the Netia Group without material cause) and the fulfilment of the business criteria set by the Supervisory Board for each year of the New Plan. In the event of termination by the Company, unvested options are retained prorata to the period worked during the vesting period. The proportion of the stock options exercised versus the number of stock options granted shall be equal to the lower of: 100% or the actual performance of the objectives set out as part of the performance criteria approved by the Supervisory Board and applicable in the financial year in which the stock options were granted. Each year within the period following the publication of the financial statements of the Company for the previous financial year and prior to the date of the Annual General Meeting of the Company, the Supervisory Board shall adopt a conditional resolution in which it shall determine the performance level of the business criteria for the previous financial year. The resolution of the Supervisory Board shall enter into force upon the approval of the financial statements of the Company and the Netia Group by the Annual General Meeting of the Company. Such conditional resolution of Supervisory Board regarding the performance criteria for 2011 was taken on April 25, 2012 and the performance level was determined at 58.9%. The resolution came into force on June 19, 2012 and resulted in cancellation of 41.1% of options granted in 2011.

A conditional resolution of Supervisory Board regarding the performance criteria for the 1,725,000 options granted to Management Board members in 2012 was taken on February 26, 2013 and the performance level was determined at 68.6%. The resolution of the Supervisory Board came into force on June 28, 2013 and resulted in cancellation of 31.4% of options granted in 2012.

On June 28, 2013 the Supervisory Board of Netia adopted a resolution on decreasing by PLN 0.16 the strike price of all existing options issued to the Management Board members and the employees of the Company and its subsidiaries in connection with the New Plan. This decrease of the strike price of all the existing options granted to the participants of the New Plan was necessary to neutralize the impact of the acquisition by the Company on May 28, 2013 of 16,012,630 of its shares for the price of PLN 8 per share in the performance of the share buy-back program conducted by the Company. The purchase by the Company of its own shares on the terms described above had a proforma impact on the market value of the Company's shares equivalent to a dividend payment and therefore it resulted in a proforma decrease of the market value of the Company's shares and a corresponding decrease of the value of all the existing options granted to the participants of the New Plan. The plan makes specific provisions for the reduction of strike prices to neutralize the effect of dividend payments on the value of the plan and, furthermore, authorizes the Supervisory Board to make adjustments to the plan to neutralize the impact of unusual or one-off events, such as this repurchase of shares.

The new strike prices of the options granted to Management Board members range between PLN 4.54 to PLN 6.00.

Options	**New Plan Year ended December 31, 2013**
At the beginning of the period	2,402,351
Granted	1,725,000
Forfeited	(541,650)
At the end of the period	**3,585,701**

For 2013 the Supervisory Board set performance goals based on the following key performance indicators:

- B2B Data Revenue
- Number of TV services

As at the date of this Directors' Report the supervisory Board was yet to meet to decide on the proportion of 2013 granted options to be retained until vesting by the Management Board members.

The following changes in the number of options granted to members of the Management Board under New Plan occurred during the year ended December 31, 2013:

	At the beginning of the period	Granted	Forfeited	At the end of the period
Mirosław Godlewski	1,028,675	690,000	(216,660)	1,502,015
Jonathan Eastick	514,338	345,000	(108,330)	751,008
Tom Ruhan	514,338	345,000	(108,330)	751,008
Mirosław Suszek	345,000	345,000	(108,330)	581,670
Total	**2,402,351**	**1,725,000**	**(541,650)**	**3,585,701**

There were no other changes in the number of options granted to members of the Management Board as at the date of filing this report.

The Company recognizes the cost of share-based awards to employees (including share options and RSU) over the vesting period. Due to the above the cost of options granted to the members of the Management Board recorded in the year ended December 31, 2013 is as follows:

	Year ended December 31, 2013
	PLN
Mirosław Godlewski	565
Jonathan Eastick	281
Tom Ruhan	281
Mirosław Suszek	199
	1,326

Participation Units in the Value Creation Transactional Bonus Scheme, previously named the Change of Control Transaction Bonus Scheme (not in thousands)

On April 25, 2012, the Supervisory Board approved a new bonus plan known as the Change of Control Transaction Bonus Scheme (CoCTB) for the Company's Management Board Members. The plan was renamed Value Creation Transactional Bonus Scheme ("VCTB") on June 28, 2013. The VCTB is a cash settled share based bonus scheme under which up to 11,400,000 Participation Units (PUs) may be issued to Management Board Members. Each PU has a strike price of 7,00 zloty per share and a term of 36 months commencing on December 31, 2012. The strike price adjusts upward over time by one percent per month from 31 January 2013 and is reduced by any dividends or dividend equivalents paid out by the Company ("the Adjusted Strike Price"). In the event that an investor or consortium of investors holds at least 90 % of Netia's equity on or prior to December 31, 2015 ("Trigger Event"), each PU shall be worth the positive difference between the acquisition price paid in a successful tender offering that secures the 90 % share-holding and the Adjusted Strike Price. For the purpose of calculating the value of the PU, the acquisition price is capped at 10 zloty per share. Should a Trigger Event occur after December 31, 2012 and prior to the expiration of the PUs on December 31, 2015, the Company shall pay the cash equivalent of the value of the PUs to each participating Management Board Member who was fulfilling his duties and has not resigned from his position prior to such Trigger Event. See also Note 39 in consolidated financial statements.

As at December 31, 2013, the members of the Management Board held Participation Units in the Value Creation Transactional Bonus Scheme as follows:

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

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

The members of the Supervisory Board did not hold any options as at December 31, 2013 and as at the date of filing this report.

The Company's Extraordinary General Shareholders Meeting held on July 26, 2010 approved changes of the rules of remunerating the Supervisory Board members dated April 9, 2009. The change of the rules was effective from the day the resolution was adopted.

(All amounts in thousands, except as otherwise stated)

Due to the changes of rules of remunerating the Supervisory Board Members approved by the Extraordinary General Shareholders Meeting on July 26, 2010, each independent Supervisory Board Member receive an annual grant of 15,000 Restricted Stock Units ("RSU"). The first annual RSU grant was made on July 27, 2010 and subsequent grants will occur on the same date in the following years. One third of each grant vests 12, 24 and 36 months after the grant date. One RSU corresponds to one ordinary share in the Company having a value equal to the market price of the Company's shares.

Changes in the number of RSU held by members of the Company's Supervisory Board are presented below:

	December 31, 2012	RSUs granted	RSUs exercised	RSUs cancelled	December 31, 2013
Stan Abbeloos	80,000	15,000	-	-	95,000
Jacek Czernuszenko	-	65,000	-	-	65,000
Benjamin Duster	80,000	15,000	(65,000)	(30,000)	-
Raimondo Eggink	95,000	15,000	-	-	110,000
George Karaplis	80,000	15,000	(15,000)	-	80,000
Nicolas Maguin	95,000	15,000	-	-	110,000
Ewa Pawluczuk	95,000	15,000	-	-	110,000
Tadeusz Radzimiński	95,000	15,000	-	-	110,000
Jerome de Vitry	95,000	15,000	(30,000)	-	80,000
Total RSU	**715,000**	**185,000**	**(110,000)**	**(30,000)**	**760,000**

On July 27, 2013, a total of 120,000 RSUs were awarded to the Supervisory Board. Each Supervisory Board member, other than Mr. Jacek Czernuszenko, was awarded an additional 15,000 RSUs, which vest in three equal installments on the anniversary award dates over the next three years. Mr. Czernuszenko received 50,000 RSUs on the day he was appointed to the Supervisory Board, which vest on the third anniversary award date, and a further 15,000 RSUs, which vest in three equal installments on the anniversary award dates over the next three years, were awarded on the following day, June 29, 2013, in accordance with the rules of the Supervisory Board's remuneration.

On January 13, 2014 the Extraordinary General Meeting of the Company appointed Mr. Bogusław Kułakowski as the independent member of the Supervisory Board. On the day he was appointed to the Supervisory Board, Mr. Kułakowski received 50,000 RSUs which vest on the third anniversary award date.

The cost of RSUs recorded in year ended December 31, 2013 amounted to PLN 1,240 as compared to PLN 411 in 2012:

	Year ended December 31, 2013	**Year ended December 31, 2012**
Stan Abbeloos	142	62
Jacek Czernuszenko	63	-
Benjamin Duster	78	60
Raimondo Eggink	163	34
George Karaplis	130	61
Nicolas Maguin	163	34
Ewa Pawluczuk	163	34
Tadeusz Radzimiński	191	92
Jerome de Vitry	147	34
Total cost of RSU	**1,240**	**411**

Upon exercise of the RSUs in the year ended December 31,2013 and 2012, Supervisory Board members received the following gross cash payments:

	Year ended December 31, 2013	**Year ended December 31, 2012**
Stan Abbeloos	-	92
Benjamin Duster	345	90
Raimondo Eggink	-	-
George Karaplis	73	90
Nicolas Maguin	-	-
Ewa Pawluczuk	-	-
Jerome de Vitry	154	-
Tadeusz Radzimiński	-	-
Total cost of RSU	**572**	**272**

4.6 Shares held by members of the Management Board and Supervisory Board of the Netia Group

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

As at December 31, 2013 and December 31, 2012, the Company's President of the Management Board, Mr. Mirosław Godlewski, together with a company closely related to Mr. Mirosław Godlewski, held 577,385 and 605,000 shares of the Company, respectively.

As at December 31, 2013 and December 31, 2012, Mr. Jonathan Eastick, a member of the Company's Management Board, held 429,114 and 450,000 shares of the Company, respectively.

As at December 31, 2013 and December 31, 2012, Mr. Tom Ruhan, a member of the Company's Management Board, and a company closely related to Mr. Tom Ruhan held 529,790 and 555,575 shares of the Company, respectively.

Details of the changes in the number of shares held by members of the Company's Management Board during the year ended December 31, 2013 are presented below:

	December 31, 2012	Reductions in shareholdings	December 31, 2013
Mirosław Godlewski, (including closely related company holdings	605,000	(27,615)	577,385
Jonathan Eastick	450,000	(20,886)	429,114
Tom Ruhan, (including closely related company holdings)	555,575	(25,785)	529,790
Mirosław Suszek	-	-	-
Total	**1,610,575**	**(74,286)**	**1,536,289**

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

As at December 31, 2013 and December 31, 2012, Mr. Raimondo Eggink – a member of the Company's Supervisory Board – held 38,143 and 40,000 shares of the Company, respectively.

As at December 31, 2013 and December 31, 2012, Mr. Nicolas Maguin – a member of the Company's Supervisory Board – held 20,311 and 21,300 shares of the Company, respectively.

As at December 31, 2013 and December 31, 2012, Mr. Tadeusz Radzimiński – a member of the Company's Supervisory Board – held 19,072 and 20,001 shares of the Company, respectively.

As at December 31, 2013 and December 31, 2012, Mr. Jerome de Vitry – a member of the Company's Supervisory Board – held nil and 20,000 shares of the Company, respectively.

4.7 Agreements concluded by the Company and the members of the Management Board, providing for compensation in the event of their resigning or being dismissed from their positions without a sound reason or when they are dismissed or made redundant due to the Company's merging through acquisition

Under a labour contract the Supervisory Board of Netia granted one member of the Management Board compensation should that person be dismissed from his position without a justified reason. Should that member of the Management Board be dismissed, Netia will be required to pay a one-off severance payment of PLN 300 stipulated in the employment agreement. Notwithstanding the reason for separation, this Management Board Member's employment contract provided that he be released from work during a six month notice period. The above terms and conditions of separation were modified on February 19, 2014, when the Supervisory Board agreed with this Management Board Member that if he continues performing his duties and not tender his resignation until the earlier of:

i) Receiving a request from the Supervisory Board to tender his resignation, and
ii) 31 August 2014,

then, upon fulfilment of certain conditions, Netia shall pay a one-off severance payment of one year's salary of PLN 1,200 and pro rata 2014 bonus at target payout level for the period from January 1, 2014 to the de facto date of resignation.

Furthermore, an employment contract of another member of the Management Board shall not be terminated without the Supervisory Board's recommendation in the form of resolution. Otherwise the Company will be required to pay a one-off severance payment being the equivalent of the six times the monthly salary in the amount of PLN 377, as at December 31, 2013.

Upon a decision of the Supervisory Board, one of the members of the Management Board who resigns from his position and/or terminates employment and indicates a particular conflict of interest, shall be entitled to receive the severance payment equal to the aggregate amount of monetary compensation due in connection with performance of his duties as the member of the Management

Board for the period of one calendar year immediately preceding the year in which the resignation from his position or termination of employment occurred.

4.8 Changes in the basic management principles of the Netia Group

Changes in the Management Board and Supervisory Board

Changes in the Management Board and Supervisory Board were discussed in point 4.2 above.

Legal and organizational changes

There were no material legal or organizational changes made within the Netia Group during 2013 with the exception of mergers between three subsidiaries and the acquisition of companies as described in 1.1. The Netia Group structure.

On January 24, 2014 Netia announced a divisional split of its operations between two distinct Business Units: Business to Business (B2B) and Business to Consumers (B2C), with a view to best support the needs of its business and residential customers and the Company's key strategic objectives. Netia's organizational structure will be aligned accordingly, with both Business Units owning full P&L responsibility for all their operations. The B2B and B2C Business Units will be responsible for providing new, innovative and user-friendly products to their customers and constant improvement of service delivery. This organizational change is expected to results in the maximal possible simplification of internal procedures and processes, clear accountability for execution of each of strategic targets and thus the maximization further improvement of the Group's financial performance. Moreover, the change is expected to allow Netia, being the second largest fixed network operator in Poland, to take optimal advantage of its existing infrastructure, which in the medium and long term is expected to increasingly play an important role in Netia's financial performance. In addition, it should is expected to provide the flexibility necessary to take advantage of possible consolidation scenarios in the Polish telecommunications market.
This transformation is to be completed by the end of Q1 2014.

5 Major Shareholders and share capital

5.1 Shareholders holding more than 5% of the votes at the General Shareholders' Meeting of Netia (not in thousands)

Based on the most recent information presented to the Company by its shareholders, as at the date of filing this report, significant blocks of the Company's shares were held by the following entities (the ownership interest and the number of votes are calculated on the basis of the number of shares constituting the Company's share capital as at February 19, 2013):

Third Avenue Management LLC

On June 5, 2013 Third Avenue Management LLC informed that Third Avenue Management LLC had decreased its holdings of the Company's shares from 69,013,736 held by Third Avenue Management LLC on November 21, 2012 and constituting 19.84% of the Company's share capital and carrying 19.84% of the total number of votes at the General Shareholders' Meeting of the Company to 60,717,960 constituting 17.45% of the Company's share capital and carrying 17.45% of the total number of votes at the General Shareholders' Meeting of the Company.

On July 26, 2013 Third Avenue Management LLC informed that Third Avenue Management LLC had decreased its holdings of the Company's shares from 60,717,960 held by Third Avenue Management LLC on June 5, 2013 and constituting 17.45% of the Company's share capital and carrying 17.45% of the total number of votes at the General Shareholders' Meeting of the Company to 57,935,934 constituting 16.65% of the Company's share capital and carrying 16.65% of the total number of votes at the General Shareholders' Meeting of the Company.

On November 4, 2013 Third Avenue Management LLC informed that Third Avenue Management LLC had decreased its holdings of the Company's shares from 57,935,934 held by Third Avenue Management LLC on July 26, 2013 and constituting 16.65% of the Company's share capital and carrying 16.65% of the total number of votes at the General Shareholders' Meeting of the Company to 57,878,899 constituting 16.64% of the Company's share capital and carrying 16.64% of the total number of votes at the General Shareholders' Meeting of the Company.

ING Otwarty Fundusz Emerytalny and ING Dobrowolny Fundusz Emerytalny

On March 4, 2013 ING Otwarty Fundusz Emerytalny and ING Dobrowolny Fundusz Emerytalny informed that ING Otwarty Fundusz Emerytalny and ING Dobrowolny Fundusz Emerytalny had increased their holdings of the Company's shares from 57,858,758 held by ING Otwarty Fundusz Emerytalny on February 20, 2013 and constituting 16.63% of the Company's share capital and carrying 16.63% of the total number of votes at the General Shareholders' Meeting of the Company to 59,077,592 constituting 16.98% of the Company's share capital and carrying 16.98% of the total number of votes at the General Shareholders' Meeting of the Company.

Subsidiaries of SISU Capital Fund Limited

Subsidiaries of SISU Capital Fund Limited held a total of 44,336,534 of the Company's shares constituting 12.74% of the Company's share capital and representing 12.74% of the total number of votes at the General Shareholders' Meeting. The Company has received no information concerning changes in the number of shares held by Subsidiaries of SISU Capital Fund Limited since February 25, 2011.

Aviva Otwarty Fundusz Emerytalny Aviva BZ WBK

Aviva Otwarty Fundusz Emerytalny Aviva BZ WBK held a total of 20,243,646 of the Company's shares constituting 5.82% of the Company's share capital and representing 5.82% of the total number of votes at the General Shareholders' Meeting. The Company has received no information concerning changes in the number of shares held by Aviva Otwarty Fundusz Emerytalny Aviva BZ WBK since May 22, 2012.

PZU OFE „Złota Jesień"

On January 13, 2014 Otwarty Fundusz Emerytalny PZU „Złota Jesień" informed that as a result of a decrease in Netia's share capital by the redemption of 38,370,130 Netia's own shares on October 24, 2013, the ownership of Netia's shares held by Otwarty Fundusz Emerytalny PZU „Złota Jesień" has exceeded the threshold of 5% of the total number of votes at Netia's General Meeting of Shareholders. Otwarty Fundusz Emerytalny PZU „Złota Jesień"held a total of 19,266,613 of the Company's shares constituting 5.54% of the Company's share capital and representing 5.54% of the total number of votes at the General Shareholders' Meeting.

5.2 Share capital

At December 31, 2012, the Company's share capital consisted of 386,279,904 (not in thousands) ordinary shares and 1,000 (not in thousands) series A1 shares with a par value of PLN 1 (not in thousands) per share. Each ordinary share has one vote at the shareholders' meeting. The holder of 1,000 series A1 shares has the right to nominate one member of the Supervisory Board. The majority of votes of the Supervisory Board elect the Management Board.

On January 23, 2013 the Company completed the third tranche of its share buy-back program, under which the Company repurchased 9,657,023 (not in thousands) shares constituting 2.5% of Company share capital for a total of PLN 47,579 plus transaction costs of PLN 20. From these amounts, 3,422,312 (not in thousands) shares were repurchased in 2013 for a total of PLN 15,881 plus transaction costs of PLN 7.

On May 28, 2013 the Company repurchased a further 16,012,630 (not in thousands) shares constituting 4.15% of Company share capital for PLN 128,101 plus transaction costs of PLN 209.

As a result of these and earlier share buy-backs, Netia held 38,370,130 (not in thousands) treasury shares from a total outstanding share capital of 386,280,904 (not in thousands) shares. On June 28, 2013 the Annual General Meeting of the Company resolved to redeem these treasury shares and the redemption was effective from October 24, 2013 when the notice of redemption filed by the Company was registered by the National Court Registry.

The redemption of shares in October 2013 resulted in a decrease of share capital by PLN 38,370,130 (not in thousands) and a decrease in other supplementary capital by PLN 251,012,190 (not in thousands) , from which PLN 38,370,130 (not in thousands) was transferred to the separate reserve capital of the Company established in accordance with Article 457, §2 of the Commercial Companies Code.

The Company's share capital as of the date of the approval of the consolidated financial statements amounted to PLN 347,910,774 (not in thousands).

5.3 Agreements which could lead to changes in shareholding proportions in the future (not in thousands)

On the basis of the Plan 2011, the Company may issue up to 27,253,674 share options to the Management Board and employees of Netia. Each option enables the New Plan participant to receive, free of charge, up to ½ of a subscription warrant issued by the Company with the latest possible exercise date of May 26, 2020. Each warrant entitles its holder to subscribe for one series L share for the nominal value e. i PLN 1 zł, which shall be paid by the Company or its subsidiaries. In order to satisfy the claims arising from the exercise of the options under New Plan, the Shareholders Meeting resolved to authorize the issuance of up to 13,626,837 series L shares.

5.4 Holders of all securities which grant special control rights in relation to the Company

Mr. Andrzej Radzimiński holds 1,000 (not in thousands) series A1 shares which give him the right to appoint and dismiss a member of the Supervisory Board.

5.5 Limitations on the transfer of ownership rights to the Issuer's securities and limitations on exercising the voting rights carried by the Issuer's shares

Netia's corporate documents do not contain any limitations, which significantly limit changes in the control of the Issuer as a result of third parties' purchasing substantial amounts of shares.

Each Netia share carries one vote at the GSM. There are no limitations on exercising the voting rights from the Company's shares.

Mr. Andrzej Radzimiński holds 1,000 (not in thousands) series A1 shares which give him the right to appoint and dismiss a member of the Supervisory Board.

5.6 Dividends, share buybacks and distribution policy

Dividends

Management elected to propose a dividend payment in respect to the financial year ended December 31, 2013 of PLN 0.42 per share amounting to PLN 146,123.

Share buy-backs

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

Between August 17, 2011 and January 23, 2013, Netia completed three tranches of share buy-backs under the General Program, each of which was approved by the Company's Supervisory Board. As a result Netia repurchased 32,132,500 (not in thousands) shares for a total of PLN 172,141 plus transaction costs of PLN 143. Of the shares repurchased, 9,775,000 (not in thousands) shares were redeemed by the Shareholders Meeting on January 30, 2012.

On March 13, 2013 Netia, in connection with the implementation by the Company of the General Program, announced an offer to repurchase shares with respect to no more than 16,012,630 (not in thousands) own shares in the Company, which represents no more than a 4.15% of the share capital of the Company and entitles the holders thereof to exercise no more than 4.15% of the total number of votes at the general meeting of the Company. The offered purchase price of the shares amounted to PLN 8.00 (not in thousands) per share. The transaction was settled on May 28, 2013 and resulted in the repurchase of 16,012,630 (not in thousands) shares for PLN 128,101 plus transaction costs of PLN 209.

Accordingly, as a result of these share repurchases, the Company spent PLN 143,989 on 19,434,942 (not in thousands) shares plus costs of PLN 209 during 2013 and spent PLN 106,773 on 18,935,188 (not in thousands) shares plus costs of PLN 41 during 2012.

On June 28, 2013 the Annual General Meeting of the Company resolved to redeem the outstanding 38,370,130 treasury shares and the redemption was effective from October 24, 2013 when the notice of redemption filed by the Company was registered by the National Court Registry.

Distribution policy

Whilst the Netia Group is cash generative, high depreciation charges in the near term and the on-going possibility of impairment charges from annual impairment tests make net earnings of the Company relatively volatile. In these circumstances, the Management Board's intention is to make distributions to the shareholders as regularly as legally possible.

Depending on the evolution of distributable reserves in Netia, which stand at PLN 376,937 and represent the key constraint on future distributions, Management may use dividends or offers to purchase shares directed to all shareholders or capital redemptions to facilitate payments these funds to shareholders. Based on its free cash flow projections, Management estimates that the Company may distribute up to PLN 146,123, approximately PLN 0.42 per share (not in thousands), from 2014 onwards with some scope to moderately increase payments over time and Management will allow leverage to climb toward 1.0 x Adjusted EBITDA in support of this policy.

In line with this distribution policy:

i) A dividend of 42 groszy per share or PLN 146,123 is to be proposed by Management for payment in 2014.

ii) Management may seek a further multi-year share buy- back authorization from the GSM to allow for other forms of distribution via share buy-back should this be necessary.

6 Other information.

6.1 Transactions with related parties

Bonds issued

On February 15, 2013 Netia Brand Management purchased 3 EE series registered bonds issued by Netia, each of a nominal value of PLN 5.000 and of a total nominal value of PLN 15.000 and with maturity date falling on January 31, 2018.

On March 6, 2013 Dialog purchased 8 FF series registered bonds issued by Netia, each of a nominal value of PLN 10.000 and of a total nominal value of PLN 80,000 and with maturity date falling on June 6, 2013.

On June 6, 2013 Dialog purchased 8 GG series registered bonds issued by Netia, each of a nominal value of PLN 10.000 and of a total nominal value of PLN 80,000 and with maturity date falling on September 6, 2013.

On June 27, 2013 Netia Brand Management purchased 3 HH series registered bonds issued by Netia, each of a nominal value of PLN 5.000 and of a total nominal value of PLN 15.000 and with maturity date falling on June 30, 2018.

On July 3, 2013 Dialog purchased 5 II series registered bonds issued by Netia, each of a nominal value of PLN 10.000 and of a total nominal value of PLN 50,000 and with maturity date falling on October 3, 2013.

On September 6, 2013 Dialog purchased 8 JJ series registered bonds issued by Netia, each of a nominal value of PLN 10.000 and of a total nominal value of PLN 80,000 and with maturity date falling on December 6, 2013.

On October 3, 2013 Dialog purchased 5 KK series registered bonds issued by Netia, each of a nominal value of PLN 10.000 and of a total nominal value of PLN 50,000 and with maturity date falling on December 3, 2013.

On December 3, 2013 Dialog purchased 5 LL series registered bonds issued by Netia, each of a nominal value of PLN 10.000 and of a total nominal value of PLN 50,000 and with maturity date falling on March 3, 2014.

On December 6, 2013 Dialog purchased 8 MM series registered bonds issued by Netia, each of a nominal value of PLN 10.000 and of a total nominal value of PLN 80,000 and with maturity date falling on February 6, 2014.

On February 6, 2014 Dialog purchased 8 NN series registered bonds issued by Netia, each of a nominal value of PLN 10.000 and of a total nominal value of PLN 80,000 and with maturity date falling on May 6, 2014.

As a result of this bond issuance and earlier issuance, Netia S.A. had PLN 475,000 of bonds outstanding as at December 31, 2013 comprising PLN 430,000 to Dialog and PLN 45,000 to Netia Brand Management.

Other transactions with related parties

The following transactions were concluded between the Company and its subsidiaries during 2013:
- sale and purchase of telecommunications services;
- sale and purchase of other services (rental and book-keeping services) to subsidiaries;
- sale and purchase of fixed and intangible assets.

A detailed list of transactions with subsidiaries has been presented in the Company's financial statements (Note 36).

Other transactions with subsidiaries have been described in points 3.6 "Loans, warranties and collaterals granted" and 6.1 "Remuneration paid and payable to the members of the Management Board and the Supervisory Board in 2013".

6.2 Guidance for 2014 (not in thousands)

Netia today sets out its guidance for 2014.

Management expects 2014 to be a year of consolidation with a focus on providing the foundations for the B2B and B2C Business Units to deliver accelerating performance in future periods.

While Management expects to continue growth in on-net services with broadband, TV and B2B services all registering growth, the short-term priority will be to add additional product features, improve processes and reduce the cost base in order to sell more effectively in subsequent years. Accordingly, guidance is being limited to key financial measures with no RGU guidance being provided.

Guidance for 2014 is set out below:

Guidance 2014	
Revenue (PLN m)	1,735
Adjusted EBITDA (PLN m)	505
Adjusted EBITDA margin (%)	29.1%
Adjusted EBIT (PLN m)	75
Capital investment (excl. M&A and integration capex) (PLN m)	200
Capital investment (excl. M&A and integration capex) to sales (%)	11.5%
Adjusted operating free cash flow (Adj. OpFCF) (PLN m)*	305

1 Adjusted EBITDA less Capital Investments excluding acquisitions and Dialog and Crowley integration related capex

The above guidance excludes the impact of one-off integration costs and one-off integration capital investments, estimated at up to PLN 8 million and up to PLN 14 million, respectively.

(All amounts in thousands, except as otherwise stated)

The Group's medium-term strategic financial guidance, which was put under review in November 2013 at the time of publishing Q3 2013 results, is today being withdrawn. Management will await the results of the next mid-term perspective planning round together with the Company's Supervisory Board and which will be undertaken with key input from the two new, more autonomous B2B and B2C Business Units before deciding on whether to once again issue such medium-term guidance.

6.3 Information on the registered audit company

The financial statements of Netia and the consolidated financial statements of the Netia Group for 2013 and 2012 were audited by Ernst & Young Audyt Polska spółka z ograniczoną odpowiedzialnością spółka komandytowa on the basis of a contract concluded on December 4, 2009.

Item	**Year ended December 31, 2013 (PLN)**	**Year ended December 31, 2012 (PLN)**
Audit of stand-alone and consolidated financial statements	265	288
Review of stand-alone and consolidated financial statements	230	230
Audit of subsidiaries' financial statements	329	304
Other attest services	40	-
Total	**864**	**822**

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

6.4 Compliance with corporate governance rules

The Management Board of the Company represents that in 2013 the Company in principle complied with the corporate governance rules stated in the document entitled "Code of Best Practice for WSE Listed Companies". As per the Company's declaration published in the current report dated February 28, 2008 since the "Code of Best Practice for WSE Listed Companies" became effective on January 1, 2008, the Management Board of the Company declares that it appreciates the importance of corporate governance rules provides in that document and the role played by those rules in enhancing the transparency of stock exchange listed companies, and it has exercised duly diligent efforts for those rules to be observed in Netia to the greatest extent possible. With reservation of the explanation presented in the annual report on compliance with corporate governance rules, according to the Management Board's best knowledge in 2013 none of the rules stated in the "Code of Best Practice for WSE Listed Companies" was breached by the Company. All rules were applied by the Company according to the wording presented in the above mentioned document.

The Management Board of the Company is responsible for the internal control system at the Company and for the effectiveness thereof in the process of preparing financial statements and interim reports which are made and published by the Company. Therefore the Netia Group has implemented controls to ensure that financial reporting is reliable. Those controls are tested and assessed on effectiveness by internal audit, finance department managers and external auditors.

The financial department headed by the Chief Financial Officer – Management Board member, is responsible for the preparation of the financial statements and interim reports of the Company.

The financial data which is the basis for the financial statements and interim reports are taken from the Company's monthly financial and management reporting. Once the accounts for each calendar month are closed the mid level and senior management at the financial department headed by the Chief Financial Officer – Management Board member jointly analyse the financial results of the Company as compared to the assumptions made in the budget. All identified errors are corrected in the Company's books without delay in accordance with the accounting policy adopted by the Company. The Company applies the rule of independent review of the published financial reports whether or not such review or audit is required by law.

The quarterly reports, interim statements and financial data which is the basis of the reports are reviewed by the Company auditor. The review applies in particular to the adequacy of financial data and the scope of the required disclosures. The results of the quarterly review or audit are presented by the auditor to the management of the Company financial department at summary meetings and to the Audit Committee. After the review or audit is completed, the financial statements and interim reports are delivered to the members of the Company's Audit Committee. Moreover, prior to the Management Board's approval of the interim financial statements for publication, the Chief Financial Officer – Management Board member presents the Audit Committee with important aspects of a quarterly/annual financial statement, particularly with changes in the accounting principles, if any, important revaluations or accounting opinions, material disclosures and business transactions. The interim financial statements are approved for publication after acceptance by the Audit Committee. Moreover, the auditors present the Audit Committee with information on any shortcomings of the control mechanisms which they established in the course of auditing the financial statements. Any recommendations made after a review of risk management procedures and internal control mechanisms are gradually implemented.

6.5 Subsequent events *(not in thousands)*

CEO's decision to stand-down

On February 19, 2014, the President of the Company's Management Board, Mirosław Godlewski, in agreement with the Supervisory Board, decided to stand-down from his position leading the Company's Management Board and shall remain in his position while the Supervisory Board identify his replacement but not longer than until August 31, 2014.

Appointment of the Supervisory Board member and grant of RSUs (not in thousands)

On January 13, 2014 the Extraordinary General Meeting of the Company appointed Mr. Bogusław Kułakowski as the independent member of the Supervisory Board. On the day he was appointed to the Supervisory Board, Mr. Kułakowski received 50,000 RSUs which vest on the third anniversary date of his appointment.

Sale of Uni-Net

On February 6, 2014 the Company's subsidiary Internetia Holding Sp. z o.o. sold all shares in Uni-Net Poland Sp. z o.o. constituting 100% of the shares in the share capital of Uni-Net and representing 100% of the votes at the meetings of the shareholders of Uni-Net for PLN 1,476.