ANNUAL REPORT

2008

A Telefonica company

ANNUAL REPORT

2008

Champions do not become champions at the moment of their victory. They've trained for hours, day, weeks, months and years prior. To be prepared – that is the basis for success. Success will not come to us – we have to go after it to get it. Not be afraid of failure. Think of victory.

CONTENT

INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF TELEFÓNICA O2 CZECH REPUBLIC, A.S.

We have audited the consolidated financial statements of Telefónica O2 Czech Republic, a.s. and its subsidiaries ("the Group") as at 31 December 2008, presented in the annual report of Telefónica O2 Czech Republic, a.s. ("the Company") on pages 86–133, on which we have issued an auditors' report dated 20 February 2009, presented in the annual report on page 88. We have also audited the separate financial statements of the Company as at 31 December 2008, which are presented in the annual report of the Company on pages 136–183 on which we have issued an auditors' report dated 20 February 2009, presented in the annual report of the Company on page 138 (both referred further as "financial statements").

We have also audited the consistency of the annual report with the financial statements described above. The management of Telefónica O2 Czech Republic, a.s., is responsible for the accuracy of the annual report. Our responsibility is to express, based on our audit, an opinion on the consistency of the annual report with the financial statements.

We conducted our audit in accordance with International Standards on Auditing and the related implementation guidance issued by the Chamber of Auditors of the Czech Republic. Those standards require that we plan and perform the audit to obtain reasonable assurance as to whether the information presented in the annual report that describes the facts reflected in the financial statements is consistent, in all material respects, with the financial statements. We have checked that the accounting information presented in the annual report on pages 6–83 and 186–192 is consistent with that contained in the audited financial statements as at 31 December 2008. Our work as auditors was confined to checking the annual report with the aforementioned scope and did not include a review of any information other than that drawn from the audited accounting records of the Company. We believe that our audit provides a reasonable basis for our opinion.

Based on our audit, the accounting information presented in the annual report is consistent, in all material respects, with the above-mentioned financial statements.

In addition, we have reviewed the accuracy of the information contained in the report on related parties of Telefónica O2 Czech Republic, a.s., for the year ended 31 December 2008, presented in the annual report of the Company on pages 196–205. The management of Telefónica O2 Czech Republic, a.s., is responsible for the preparation of the report on related parties. Our responsibility is to issue a report based on our review.

We conducted our review in accordance with the applicable International Standard on Review Engagements and the related implementation guidance issued by the Chamber of Auditors of the Czech Republic. Those standards require that we plan and perform the review to obtain moderate assurance as to whether the report on related parties is free from material misstatement. The review is limited primarily to enquiries of company personnel, to analytical procedures applied to financial data and to examining, on a test basis, the accuracy of information, and thus provides less assurance than an audit. We have not performed an audit and, accordingly, we do not express an audit opinion.

Based on our review, nothing has come to our attention that causes us to believe that the report on related parties of Telefónica O2 Czech Republic, a.s., for the year ended 31 December 2008 is materially misstated.

Ernst & Young Audit, s.r.o.
Licence No. 401
Represented by

Brian Welsh
Partner

Radek Pav
Auditor, Licence No. 2042

15 March 2009
Prague, Czech Republic

FINANCIAL AND OPERATIONAL HIGHLIGHTS

Financial data are based on audited consolidated financial statements prepared in accordance with International Financial Reporting Standards.

All figures, unless otherwise stated, are in CZK millions as at 31 December of each year.

Financials	2008	2007
Revenues	64,709	63,196
OIBDA – Operating income before finance costs, tax, depreciation and amortization[1]	28,312	28,033
Operating income	15,380	13,598
Income before taxes	15,348	13,510
Net income	11,628	10,386
Total assets	103,623	113,552
Property, plant and equipment	63,429	71,809
Total equity	78,168	82,792
Financial debts	3,196	9,269
Capital expenditure	8,088	7,807
Operations		
Fixed telephony accesses (x 1,000)	1,893	2,069
ADSL connections (x 1,000)	631	570
Pay TV – O_2 TV (x 1,000)	115	73
Mobile registered customers in Czech Republic (x 1,000)	5,257	5,126
– of which contract	2,519	2,244
pre-paid	2,738	2,882
Mobile data customers[2] in Czech Republic (x 1,000)	229	192
Active mobile customers in Slovakia (x 1,000)	325	274
Group headcount	9,096	9,221
Ratios (in %)		
OIBDA/Business Revenues (OIBDA margin)	43.9	44.8
Net income/Revenues	18.0	16.4
Capital expenditure/Revenues	12.5	12.4
ROA (Net income/Total assets)	11.2	9.1
ROE (Net income/Equity)	14.9	12.5
Gross gearing (Financial debts/Total equity)	4.1	11.2

[1] Including impairment charge and gain from sale of non-current assets. In 2007, the Group posted an impairment charge of CZK 5 million, compared to CZK 86 million in 2008; gain from sale of non-current assets reached CZK 42 million in 2007 compared to CZK 855 million in 2008.

[2] CDMA, GPRS and UMTS.

Macroeconomic indicators[1]		
Population (in millions)	10.4	10.3
GDP growth (in %)[2]	3.1	5.9
Inflation (in %)	6.3	2.8
Unemployment (in %)	6.0	6.6
CZK/USD exchange rate – average over the period	17.0	20.3
CZK/USD exchange rate – end of period	19.3	18.1
CZK/EUR exchange rate – average over the period	24.9	27.8
CZK/EUR exchange rate – end of period	26.9	26.6

[1] Sources: Czech Statistical Office, Czech National Bank, Ministry of Labour and Social Affairs.
[2] At constant 1995 prices.

LETTER FROM THE CHAIRMAN OF THE BOARD OF DIRECTORS

SALVADOR ANGLADA GONZALEZ

To Our Shareholders

Let me use this opportunity to review the development and the results of the Telefónica O2 Czech Republic Group in 2008. I am glad that during the past year we confirmed our leadership of the Czech telecommunications market. Our successful offer of new and innovated services, which were very well received by customers, asserted our reputation as innovator in the field of telecommunications and integrated business solutions.

The solid growth in the mobile segment, together with a demonstrated improvement in our traditional fixed line services, has helped us deliver on our revenue growth targets. Our continuing efforts to improve operating efficiency sustained the high level of operating profit and delivered on the OIBDA margin growth.

As in previous years, our activities concentrated on the maximum satisfaction of customer needs. At the same time, they followed the trends of the fiercely competitive telecommunications market in the Czech Republic; those trends included an uptake in fixed line and mobile broadband services, data services, digital television over the fixed line and convergent services. We also tried to maintain the revenues from voice services in the mobile segment through the migration of customers to contract services. In the area of IT and professional solutions, we progressed further in the implementation of our strategy to integrate our operations into one professional services business unit. This has helped us reinforce our leadership among other ICT providers in the Czech Republic, and consolidate our revenues from this segment.

We launched O_2 Fér, a new, simple and attractive mobile tariff for the Slovak market. It instantly became a popular mobile choice – the market received it enthusiastically, which has led to an increase in the customer base and to improvements in the quality of the customer mix.

Now I will take a closer look at the past year's developments, our accomplishments and our expectations from 2009.

As in the previous two years, we continued in upgrading the connection speeds for O_2 Internet ADSL; from September 2008 we increased the connection speed by up to fourfold. The speeds were increased gradually, automatically and at no cost to the customer. The new basic connection speed increased to 8 Mb/s. Additionally, we abolished Fair User Policy data limits in March. The speed upgrades and the abolition of the data limits applied, as a matter of course, also to our wholesale offer to other licensed operators. Our initiative in this field helped us again to become the number one promoter of ADSL broadband internet access within the Czech telecommunications market.

We also improved the quality of our O_2 TV service. We introduced new programme bundles and added new feature films and television programmes to the TV Archive. We also brought out Multi – a new feature which allows for watching different channels on two television sets.

Both these services – O_2 TV and O_2 Internet ADSL – continued to be the key building blocks in our product bundles which combine several fixed line and mobile services, all for a flat monthly fee. The total number of customers who opted for such a bundle reached 270 thousand at the end of 2008, which means that service bundles are now subscribed by 14% of all lines. The activities aimed at improving the fixed line broadband internet and digital television offer were fully in line with our strategy to add more value to the fixed line. This resulted in a 47% slowdown in the rate of fixed line losses in 2008 compared to 2007.

With the goal to slow down the declining voice traffic generated in fixed lines, and to increase the penetration of broadband internet, we introduced the first Voice over IP service to the segment of small and medium enterprises. O_2 Neomezená linka offers maximum simplicity, comfort and flexibility.

Our innovations in the mobile segment are a clear example of the fact that we give customers the services they call for. In May, we became the first operator on the Czech market to come out with a new concept of simple and straightforward flat rate tariffs – O_2 NEON. This, together with O_2 [:kůl:], a tariff intended for our young customers, was aimed at stimulating the voice traffic in our network. Both new mobile tariffs were received with enthusiasm by the market, and almost 400 thousand customers activated them by the end of the year. Voice traffic grew 10% year on year. A similar offer was extended to customers from the small and medium business segment. Under the brand O_2 Business Unlimited we began to market a tariff with unlimited calls to all fixed line and mobile networks in the Czech Republic – all for a flat monthly fee.

We responded to the fast-growing demand for internet access via mobile handsets by introducing O_2 Internet v Mobilu, a new flat rate service which came with unlimited mobile internet access, including an e-mail service. Entrepreneurs and self-employed people were our audience for O_2 Business Mail, a virtual mobile office which, in addition to an e-mail box, also contained a shared calendar, shared workspace and an address book.

At the end of 2008 we had the broadest portfolio of mobile data access products, which gave us a considerable competitive edge over other mobile operators in the Czech Republic. In August we announced our plans to roll out our 3G network to other relevant cities by the end of 2009. During the next two to three years, our 3G network service should be available to more than 70% of the Czech population.

In 2008, we also expanded our portfolio of Managed Services that give the customer a professional ICT solution on a fee-for-service basis, without having to procure hardware, software or hire human resources. The various components of our O_2 Managed Hosting come with a dedicated server capacity and system administration, with the possibility of data backup for the eventuality of its loss. Other innovations in the segment of Managed Services included O_2 Managed Security, which keeps corporate data secure, and O_2 Managed Desktop, a comprehensive, multi-level administration of the corporate IT infrastructure.

In the first half of 2008, in line with our expectations we cleaned up our customer database in Slovakia; we deactivated inactive customers acquired at the time of the launch in 2007 who were using our services irregularly. Our new and in many ways revolutionary offer of O_2 Fér tariffs, which came with a single rate for all calls to all networks in Slovakia and which abolished the mandatory monthly fee, quickly became popular. It boosted the number of active customer in the second half of the year; their number reached 325 thousand at the end of the year, which translates into a 19% year-on-year increase.

In 2008, we also made a great progress with the construction of our proprietary GSM network in Slovakia. Our goal was to reduce the dependency on the national roaming arrangement with T-Mobile Slovensko, and to improve operating efficiency. By the end of 2008, more than 850 base stations were deployed and our network covered more than 90% of the Slovak population. The terms and conditions of the licence were also complied with.

The financial results for 2008 also delivered on our expectations for revenue and OIBDA growth and capital expenditure levels from the earlier period. The total consolidated revenues in 2008 reached CZK 64.7 billion, which is a 2.6% increase on the year before. Business revenues grew 2.9% to CZK 64.4 billion, well within the 2-4% range we expected. This growth was also supported with a solid 3.1% growth in revenues from mobile services of Telefónica O2 Czech Republic, and a 0.6% increase in fixed line revenues due to a marked improvement in the segment of traditional services. In spite of the 5.3% increase in operating expenditure, the consolidated OIBDA (Operating Income before Depreciation and Amortisation) grew 1% to CZK 28.3 billion. The result was an OIBDA margin of 43.9%, compared to 44.8% in 2007. The OIBDA margin was still high in comparison with other operators in Central and Eastern Europe. The trend of OIBDA growth, the continuing decline in depreciation, amortisation and net financial costs resulted in a 12% increase of net profit on the group consolidated basis in 2008 to CZK 11.6 billion. Our investments in 2008 continued to focus on growth areas, which, in the Czech Republic, included ADSL and IPTV technologies, and mobile and data networks. Investment activity in Slovakia focused in particular on the rollout of own network and on systems development. The total investments showed a year-on-year growth of 3.6% in 2008 and reached CZK 8.1 billion. We proved that in 2008, too, we were capable of generating a strong free cash flow; with the proceeds from the sale of no longer used properties factored in, the free cash flow level in 2008 reached CZK 19.5 billion, i.e. 6.5% more than in 2007.

In 2009, with regard to the challenging macroeconomic environment, we plan to continue with our strategy which places the customer and the satisfaction of customer needs at its core. At the same time we will concentrate on the execution of our strategic objectives and on maximising our performance. Cash flow growth by way of efficient operating and capital expenditure will be among our main priorities for 2009.

Salvador Anglada Gonzalez
Chairman of the Board of Directors

CALENDAR OF KEY EVENTS IN 2008

JANUARY

Telefónica O2 brought a new concept of state-of-the-art ICT technology to its business customers in the form of its Managed Services.

For every mobile handset turned in by people in any of the O_2 brand stores, Telefónica O2 donated CZK 25 through its O_2 Foundation towards the operations of Linka bezpečí, a helpline for children.

Telefónica O2, general partner of the highest national ice-hockey league, teamed up with all Extraliga clubs and ran a special sports result tipping contest open to all ice-hockey fans, in which the main prize was a place on the players' bench at O_2 Extraliga matches.

FEBRUARY

Telefónica O2 and BESTSPORT signed a rental agreement for an arena in Prague. The five-year contract with BESTSPORT, the owner-operator of the arena, gave Telefónica O2 not only the right to use the official name of O_2 Arena, but also a number of other benefits associated with the marketing support of the arena.

Telefónica O2 published its audited consolidated financial results prepared under International Financial Reporting Standards for the fiscal year 2007. Consolidated revenues reached CZK 63 billion. Consolidated net profit grew to CZK 10.4 billion.

Telefónica O2 Services earned the status of Preferred GOLD Partner Specialist, which confers the highest achievable standard in the comprehensive delivery of ICT products.

Jaime Smith Basterra resigned from the office of Chairman of the Board of Directors; Salvador Anglada Gonzalez, member of the Board of Directors and Chief Executive Officer of Telefónica O2, was unanimously elected to the position vacated by him.

Jaime Smith Basterra and Antonio Botas Bañuelos resigned on their membership in the Board of Directors. Peter Erskine resigned on his membership in the Supervisory Board which he chaired. Jaime Smith Basterra was co-opted by the Supervisory Board to the position vacated by him, and was later elected Chairman of the Supervisory Board.

MARCH

Telefónica O2 abolished Fair User Policy (FUP) data limits for all speed variants of O_2 Internet ADSL.

The number of visitors to O_2 brand stores exceeded the 10 million mark.

The employees of Telefónica O2 received the Křesadlo prize for volunteer work in the O_2 Foundation from the hands of Pavel Bém, the Lord Mayor of Prague.

APRIL

An Ordinary General Meeting of shareholders of Telefónica O2 Czech Republic was held. The shareholders approved a proposal of the Board of Directors for the payment of a dividend of CZK 50 per share. The previously co-opted members of the Supervisory Board were confirmed as regular members of the body. Antonio Botas Baňuelos became a member of the Supervisory Board, replacing Julio Estaban Linares López who had resigned.

The Supervisory Board of Telefónica O2 confirmed Jaime Smith Basterra as Chairman of the Supervisory Board, and elected Alfonso Alonso Durán as the First Vice-Chairman of the Supervisory Board.

A new service, Platí to Kvído, offered customers the possibility to call for one minute for free to any mobile or fixed line number in the Czech Republic.

MAY

Ramón Ros Bigeriego, Vice-President, Finance Division, left Telefónica O2 after being appointed Executive Director for Finance at Telefónica O2 UK. Jesús Pérez de Uriguen succeeded Ramón Ros both in the executive position and as a member of the Board of Directors.

Multi, a new feature of the digital television O_2 TV, let customers watch different channels on two television sets in different parts of the home.

Telefónica O2 entered into a framework agreement for the sale of a part of its real property portfolio with BOHEMIA REAL ESTATE INVESTMENTS s.r.o.

JUNE

Telefónica O2 and Apple signed a distribution agreement for iPhone enabled for the third generation network.

All five members of the Supervisory Board elected by employees were elected in employee elections for the Supervisory Board, which were held with the support of an electronic election system and were preceded by an electronic election campaign.

JULY

The Supervisory Board of Telefónica O2 co-opted Eduardo Andres Julio Zaplana Hernandéz-Soro a Anselmo Enriquez Linares as members. The new members succeeded Petr Zatloukal and Andrew Harley.

Telefónica O2 commenced a commercial pilot of two new mobile data tariffs: O_2 Internet v Mobilu and O_2 Internet v Mobilu Plus.

An open air exhibition of art using the Telefónica O2 public telephone boxes as a theme opened at Kampa in Prague.

Telefónica O2 connected more than 600 thousand customers via the ADSL technology.

AUGUST

The number of O_2 TV customers exceeded the 100 thousand mark.

Telefónica O2, the only Czech operator with a 3G network, announced its plans to significantly increase the coverage.

O_2 Internet ADSL increased the basic connection speed by up to fourfold, while preserving the same prices.

SEPTEMBER

Andrei Torriani resigned on his position of Vice-President, Consumer Division; he was succeeded by José Perdomo Lorenzo.

Telefónica O2 and its wholly owned subsidiary DELTAX Systems a.s. were voted to the TOP 10 Systems Integrators of 2008.

Telefónica O2 Slovakia introduced O_2 Fér, a new tariff which revolutionised mobile communications in Slovakia. The new proposition brought simplicity in the form of a single rate for calling all networks in Slovakia – anytime – and fairness, because of the zero monthly fee.

Telefónica O2 won a prestigious award for its long-term contribution to the fight against bullying in Czech schools.

An inspection by the Slovak Telecommunications Authority confirmed that Telefónica O2 Slovakia deployed 842 base stations of its proprietary GSM mobile network, covering 89% of the population with its signal, and thus complied with all terms and conditions of the licence which concerned the network and coverage.

OCTOBER

Telefónica O2 provided a network linking all election rooms and data and voice connectivity for the regional and Senate elections.

The Czech Ministry of Health awarded Telefónica O2 with the prestigious Healthy Company badge.

NOVEMBER

Telefónica O2 began the exclusive distribution of Emporia Life, a mobile handset designed specially for senior citizens.

Telefónica O2 launched O2 Grantový poradce, a new service which helps businesses qualify for European Union funding.

Telefónica O2 won the prestigious IT Product of the Year 2008 award, which is given every year by Computerworld magazine.

DECEMBER

Telefónica O2 became the Czech Republic's official telecommunications partner for the Czech presidency of the European Union.

The Board of Directors approved the plan to merge two wholly owned subsidiaries, DELTAX Systems a.s. and Telefónica O2 Services, spol. s r.o., in order to create a strong provider of ICT services. The corporate name of Telefónica O2 Services changed to Telefónica O2 Business Solutions spol. s r.o., in the process.

Telefónica O2 commenced the pilot operation of the new ADSL wholesale service. The pilot wholesale variant of the ADSL service did not contain the necessary component of a main telephone connection.

ABOUT TELEFÓNICA GROUP

01

Human potential is limited only by fear. Do what you fear. And keep doing it. It is the fastest and surest way how to deal with your demons. There will be nothing you will fear if you refuse to feel fear. Human life expands or shrinks with the amount of courage.

ABOUT TELEFÓNICA GROUP

In 2008, the group adopted an integrated decentralised governance model, through which it strives for maximum exploitation of the potential of all business units. Telefónica's operations are divided into three regions – Spain, Latin America and Europe. The group maintains an optimal revenue distribution in the regions, and 63% of all revenues are generated in other than the home market.

TELEFÓNICA IN FIGURES

- Presence in 25 countries
- More than 259 million customers
- 196 million mobile customers
- 43 million fixed accesses
- More than 12 million of high-speed internet connections
- 2 million of pay TV customers
- EUR 57.946 billion of revenues
- 63% of revenues generated in markets outside Spain
- EUR 4.614 billion invested in research, development and innovation
- More than 257,000 employees

CORPORATE CENTRE

The Corporate Centre is responsible for the global and organisational strategy, corporate policies, management of joint activities and coordination of business unit operations. In 2008, the Corporate Centre reinforced its relationships with the organisation units by way of a reorganisation project, which gave rise to two organisation units dedicated to innovation and transformation, respectively; the units were established to give a stronger impetus to the drive for revenues and performance.

TELEFÓNICA ESPAÑA

Telefónica was founded in 1924 in Spain, however (since 2008), the home country is no longer the main market of the company. The company's core operations are in Latin America. Telefónica España is well appointed in all main market segments; it provides fixed telephony services (including pay TV), mobile and data services, broadband internet access, and has – via its subsidiary Meditel – investments in Morocco.

TELEFÓNICA LATINOAMÉRICA

Telefónica Latinoamérica has operations in 13 countries of Latin America – Argentina, Brazil, Chile, Ecuador, El Salvador, Guatemala, Colombia, Mexico, Nicaragua, Panama, Peru, Uruguay and Venezuela, where it provides the services of mobile and fixed telecommunications, internet access and pay TV. Additionally, Telefónica International Wholesale Services provides wholesale telecommunications services to a global standard. Its portfolio spans voice, data, IP, satellite, corporate and mobile services, and its optical network connects Latin America, United States and Europe. Telefónica is also actively pursuing ancillary business in Puerto Rico and in the United States.

Mexico

Mobile Access
1,531

Fixed Wireless Access (FWA)
134

Central America

Fixed Telephony Access
437

Data and Internet Access
18

Mobile Access
5,702

Columbia

Fixed Telephony Access
2,299

Data and Internet Access
396

Mobile Access
9,963

Pay TV Connections
142

Venezuela

Mobile Access
10,584

FWA
1,313

Pay TV Connections
9

Argentina

Fixed Telephony Access
4,603

Data and Internet Access
1,284

Mobile Access
14,830

Peru

Fixed Telephony Access
2,986

Data and Internet Access
729

Mobile Access
10,613

Pay TV Connections
642

Brazil

Fixed Telephony Access
11,662

Data and Internet Access
3,626

Mobile Access
44,945

Pay TV Connections
472

Uruguay

Mobile Access
1,412

Chile

Fixed Telephony Access
2,121

Data and Internet Access
744

Mobile Access
6,875

Pay TV Connections
263

Spain

Fixed Telephony Access	15,326
Data and Internet Access	5,670
Mobile Access	23,605
Pay TV Connections	612

Portugal

9.86%
interest in Portugal Telecom[1]

United Kingdom

Mobile Access	19,470
Data and Internet Access	341

Ireland

Mobile Access	1,728

Germany

Mobile Access	14,198
Data and Internet Access	215

Italy

Telefónica has indirectly holds 10.36% of the voting rights in Telecom Italia

Morocco

Mobile Access	7,427
FWA	7

China

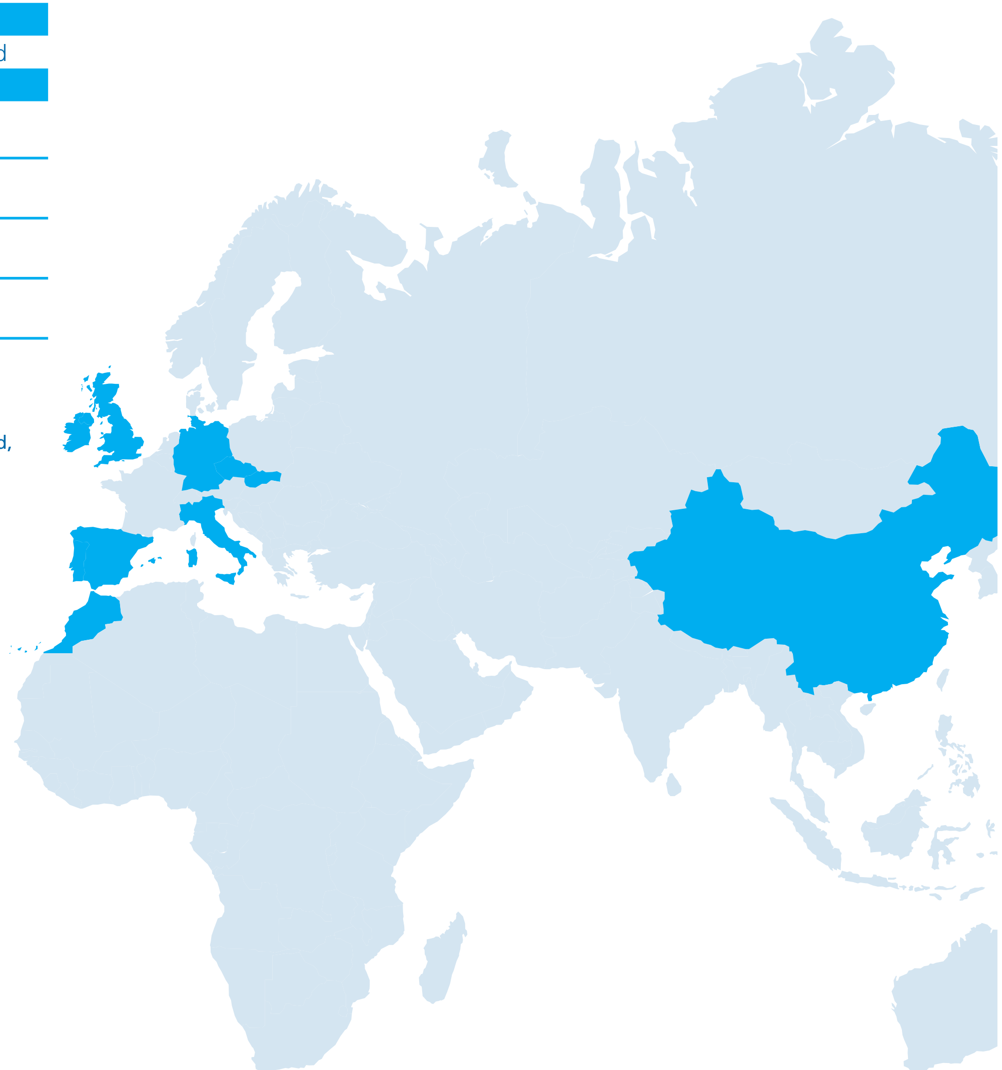
5.38% interest in China Unicom United

Czech Republic

Fixed Telephony Access	1,893
Data and Internet Access	780
Mobile Access	5,257
Pay TV Connections	114

* Data as at 31 December 2008

[1] Real interest of the Telefónica Group. With minority shareholdings disregarded, the actual ownership interest would be in the range of 10%.



TELEFÓNICA EUROPE

Telefónica O2 Europe plc changed its name to Telefónica Europe plc on 1 June 2008. The change came as an organic part of the integration process, two years after the company's integration in the group. The new corporate name structure follows the same pattern as in all the other regions – Telefónica España, Telefónica Latinoamérica and Telefónica Europe. With operations in the United Kingdom, Ireland, Germany, Czech Republic and Slovakia, Telefónica Europe provides the services of mobile and fixed telecommunications and broadband internet access.

Telefónica has an indirect presence in China and Italy through the subsidiaries China Netcom and Telecom Italia.

OTHER COMPANIES IN THE GROUP

Atento offers the services of Customer Relationship Management via its network of call centres. It has operating platforms in Spain, Argentina, Brazil, Chile, Colombia, United States, Morocco, Mexico, Peru, Puerto Rico, Czech Republic, Uruguay and Venezuela.

T-gestiona provides comprehensive administrative and financial support in the area of human resources, real property, logistics and distribution, consulting in the area of ERP processes and systems, and the services of a comprehensive back office. It operates in Spain, Argentina, Brazil, Chile and Peru.

Telefónica I+D is a research and innovation company in the field of technology. The volume of funds invested in innovation and development has made it the largest private research and development centre in Spain, and it is also the European leader in terms of participation in ICT research projects. It has operations in Spain, Brazil and Mexico.

INTEGRATED DECENTRALISED MODEL OF GOVERNANCE

It is Telefónica's goal to maximise the value of its activities at all levels – global, regional and local. The model of organisation puts the customer at the heart of the company's focus, sets out the role of innovation in revenue generation and in the transformation into a better-performing enterprise.

INTEGRATED DECENTRALISED MODEL OF GOVERNANCE

LOCAL

Spain, Argentina, Brazil, Chile, Colombia, Ecuador, El Salvador, Guatemala, Mexico, Nicaragua, Panama, Peru, Uruguay, Venezuela, Germany, Ireland, United Kingdom, Czech Republic, Slovakia

– CUSTOMER EXPERIENCE MODEL
– SINGLE POINT OF SALES MODEL
– INTEGRATED PRODUCTION MODEL

REGIONAL

Telefónica Europe
Telefónica Latinoamérica
Telefónica España

– SUPPORT, GOVERNANCE, SYNERGY

GLOBAL

Telefónica

– NEW ENGAGED CORPORATE MODEL
– INNOVATION
– TRANSFORMATION

GROUP STRUCTURE

Telefónica's organisation evolves around three regional business divisions, and builds on the strategic and industry alliances in China, Italy and Portugal.

TELEFÓNICA ESPAÑA

	Share in %
Telefónica de España	100%
Telefónica Móviles España	100%
Telyco	100%
Telefónica Telecomunic. Públicas	100%
T. Soluciones de Informática y Comunicaciones de España	100%
Iberlanda	58.94%
Medi Telecom	32.18%

TELEFÓNICA EUROPE

	Share in %
Telefónica O2 UK	100%
Telefónica O2 Germany[1]	100%
Telefónica O2 Ireland	100%
Max	100%
Be	100%
Groups 3G (Germany)[2]	100%
Telefónica O2 Czech Republic[1]	69.41%
Telefónica O2 Slovakia[3]	100%

[1] A company in which the group has a stake through Telefónica, S.A.
[2] A company in which the group has a stake through Telefónica O2 Germany.
[3] A company in which the group has a stake through Telefónica O2 Czech Republic.

TELEFÓNICA LATINOAMÉRICA

	Share in %
Telesp[1]	87.95%
Telefónica del Perú	98.18%
Telefónica de Argentina	98.20%
TLD Puerto Rico	98%
Telefónica Chile[2]	96.75%
Telefónica Telecom	52.03%
Telefónica USA	100%
T. Intern. Wholesale Serv. (TIWS)[3]	100%
Brasilcel[4]	50%
T. Móviles Argentina	100%
T. Móviles Perú	98.63%
T. Móviles Mexiko	100%
Telefónica Móviles Chile	100%
T. Móviles El Salvador	99.08%
T. Móviles Guatemala	100%
Telcel (Venezuela)	100%
T. Móviles Colombia	100%
Otecel (Ecuador)	100%
T. Móviles Panamá	100%
T. Móviles Uruguay	100%
Telefonía Celular Nicaragua	100%
T. Móviles Soluciones y Aplicac. (Chile)	100%

[1] In real terms, the ownership interest (share) is 88.01%.
[2] Telefónica Internacional de Chile, S.A., owns 44.98%, and Inversiones Telefónica Internacional Holding Ltd. owns 51.86%. On 9 January 2009, after the second acquisition was completed, the share of the Telefónica Group in the Chilean company has risen to 97.89%.
[3] Telefónica, S.A., holds 92.51%, and Telefónica DataCorp holds 7.49%.
[4] A joint venture which globally integrates the branch Vivo, S.A., through participation in Vivo Participaçoes, S.A. (63.54%).

OTHER INTERESTS

	Share in %
3G Mobile AG (Switzerland)	100%
Skupina Atento	100%
Telefónica de Contenidos – content services (Spain)	100%
Mobipay Internacional	50%
Telco SpA (Italy)[1]	42.30%
IPSE 2000 (Italy)[2]	39.92%
Mobipay España[2]	13.36%
Lycos Europe	31.10%
Hispasat	13.23%
Portugal Telecom[3]	9.86%
China Unicom Limited (Hong Kong, China)	5.38%
ZON Multimedia[4]	5.40%
BBVA	0.97%
Amper	6.10%

[1] Through Telco, Telefónica holds an indirect stake in Telecom Italia of approximately 10.36% in ordinary shares (with voting rights). After discounting saving shares (azioni di risparmio), which do not confer control rights, the indirect interest of Telefónica in Telecom Italia was 7.15%.

[2] Companies in which Telefónica Móviles España has a direct or an indirect interest.

[3] Real interest of the Telefónica Group. With minority shareholdings disregarded, Telefónica's interest would be in the range of 10%.

[4] Real interest of the Telefónica Group. With minority shareholdings disregarded, Telefónica's interest would be in the range of 5.46%.

For more information please visit: www.telefonica.es/accionistaseinversiones

BOARD OF DIRECTORS’ REPORT
ON BUSINESS ACTIVITY

02

Speed is one of the key factors in being successful. Getting through the finish line is important, but being there the first is even more important. Speed does matter.

BOARD OF DIRECTORS' REPORT ON BUSINESS ACTIVITY

TELEFÓNICA O2 CZECH REPUBLIC GROUP

OVERVIEW OF THE GROUP AND THE MAIN CHANGES IN 2008

Telefónica O2 Czech Republic Group (Telefónica O2 Group) comprises Telefónica O2 Czech Republic, a.s. (Telefónica O2, Company) and other subsidiary companies. The Group's services were provided mostly on the territory of the Czech Republic and Slovakia. Through a wholly-owned subsidiary Telefónica O2 Slovakia, the Group has expanded its business to Slovakia, where it launched the commercial operations on 2 February 2007. In line with its strategy focusing on the high growth potential areas of business and on achieving leadership in the segment of integrated ICT solutions, Telefónica O2 acquired a 100% interest in DELTAX Systems a.s. (DELTAX Systems) in 2007.

Telefónica O2 is the only integrated telecommunications operator to offer a comprehensive range of both fixed and mobile voice, data and internet services in the Czech Republic. In September 2006 it also started offering an IPTV service (O_2 TV), and in 2007 it significantly expanded its IT and ICT operations (comprehensive customer communications solutions). It also offers its network infrastructure for lease by other operators of public and private networks and services.

The retail business in the Czech Republic focused on two main customer segments – business and consumers. The business segment included corporate, business and government sub-segments. Telefónica O2 also provides wholesale services to other public telecommunications network providers and to providers of public telecommunications services both in the Czech Republic and abroad.

As at 31 December 2008, Telefónica O2 Group comprised the following subsidiary companies and associates:

On 30 November 2007, the process of liquidation of Centrade, a.s. v likvidaci, was completed. The company was deleted from the Commercial Register on 22 August 2008. During the fourth quarter of 2007, SPT TELECOM (Czech Republic) Finance B.V. initiated preparatory steps for its voluntary liquidation. The main legal steps leading to the liquidation of the company were made by the end of 2008, and the company was deleted from the Commercial Register on 9 February 2009.

In December 2008, the Board of Directors of Telefónica O2 approved the schedule of actions leading to the merger through consolidation of the wound-up undertaking DELTAX Systems a.s. with the successor undertaking Telefónica O2 Services, spol. s r.o. The merger will result in the cessation of DELTAX Systems. The assets of DELTAX Systems, its rights and obligations, including rights and obligations under the labour law, will pass to the successor company. The merger will be legally conclusive contingent on the compliance with all statutory requirements on the day of the registration of the company in the Commercial Register; the registration is now foreseen in the first half of 2009. The planned integration of both companies ties in with the Group's strategy to vest all activities in the field of ICT services and integrated business solutions in one business services unit, which will be a part of the parent company. The goal is to claim the highest position among the leading providers of ICT

Corporate name	Registered address	Object of the company	Identification number	Registered/share capital	Share of the issuer in the registered/ share capital in%
COMPANIES INCORPORATED IN THE CZECH REPUBLIC					
AUGUSTUS spol. s r.o.	Prague 10, 100 00, Na zájezdu 5	Consulting and brokerage activity in non-telecommunication disciplines	49356160	CZK 166,000	39.76%
První certifikační autorita, a.s.	Prague 9, 190 00, Podvinný mlýn 2178/6	Certification services in the area of electronic signature	26439395	CZK 20,000,000	23.25%
Telefónica O2 Business Solutions, spol. s r.o.	Prague 10, Vršovice, 100 00, Kodaňská 1392	Data services and consulting in the field of telecommunications	45797111	CZK 10,000,000	100%
DELTAX Systems a.s.	Prague 7, 170 00, Jankovcova 1569/2c	Services in the field of management systems, information systems and information technology	49241451	CZK 3,006,000	100%
COMPANIES INCORPORATED IN OTHER COUNTRIES					
SPT TELECOM (Czech Republic) Finance B.V.	Teleportboulevard 140, EJ Amsterdam 1043 Netherlands	Financing of other Group members		EUR 18,151	100%
CZECH TELECOM Austria GmbH	c/o Vienna CityTax Steuerberater GmbH, Wagramer St, Sien, 1220 Austria	Data transmission services	FN 229578s	EUR 35,000	100%
CZECH TELECOM Germany GmbH	Kennedyallee 97a, Frankfurt am Main, 60596 Germany	Data transmission services	HRB 51503	EUR 25,000	100%
Telefónica O2 Slovakia, s.r.o.	Einsteinova 24 Bratislava 851 01, Slovakia	Operation of a public telecommunications network; provision of a public telecommunications service and the service of leased lines	35848863	SKK 1,500,000,000	100%

in the Czech Republic. Telefónica O2 Business Solutions will be the only company of its kind in the Czech market offering the full scope of ICT solutions – fixed and mobile telecommunications (voice and data), terminal equipment, network infrastructure, development and implementation of proprietary software based on the customer's requirement, security, system integration, full operation and maintenance of all technologies, outsourcing of selected services, advice with the specification of new requirements and training of employees. The integration of ICT services in one organisation will simplify the management and the process model, improve efficiency and operational effectiveness. As part of the preparations for the merger, the corporate name of the successor company was changed from Telefónica O2 Services, spol. s r.o. to Telefónica O2 Business Solutions, spol. s r.o. This change was registered in the Commercial Register on 9 December 2008.

The total number of fixed telephone lines operated by Telefónica O2 in the Czech Republic as at 31 December 2008 reached 1.893 million, and the number of mobile customers registered was 5.257 million. The Company also registered 631 thousand ADSL connections and 115 thousand O_2 TV customers as at the same date. The number of Telefónica O2 Slovakia customers at the end of 2008 reached 455 thousand.

SALE OF A PART OF THE REAL ESTATE PORTFOLIO

During 2008 and in early 2009 Telefónica O2 completed a significant part of the process of its real property portfolio optimisation. In addition to other measures, the process included consolidation of staff and technology previously located in many sites, and the relocation to the new head office building, which took place in 2007. In the process, the Company identified real properties with astrategic interest and with high occupancy, which will stay in its ownership. The Company then proceeded with the sale of no longer used properties.

On 15 May 2008, Telefónica O2 and BOHEMIA REAL ESTATE INVESTMENTS signed an agreement on the sale of a part of Telefónica O2's real estate portfolio. The agreement also contained a clause providing for a long-term lease-back of some of the divested properties. The sold portfolio included administrative and technical buildings in all parts of the Czech Republic that were no longer used or optimally utilised by Telefónica O2. The total floor area of the properties for sale was 632 thousand square meters and only a small fraction of it was leased back. The sale transaction had a positive effect on the Company's 2008 bottom line.

The real properties yielded more than CZK 4 billion. The financial effect of the transaction was reflected mainly in the results for the second quarter of 2008. The profit from the transaction, after the deduction of related costs, which included primarily the net book value of the sold properties and other associated costs, reached CZK 727 million. In the third and fourth quarters, the Company collected on a significant portion of the proceeds from the sale, which positively impacted investing cash flow. In the business results of the Company from the second half of 2008 and in the following years, the transaction will cause an increase in the costs of the lease-back as well as a lower depreciation charge.

On 19 January 2009, Telefónica O2 entered into a framework agreement with Pražská správa nemovitostí and CENTRAL GROUP regarding the sale of its former headquarters in Olšanská ulice in Prague. The sale concerned a site, which is zoned for construction of 12.5 thousand of square metres and two administrative buildings of the former headquarters in Olšanská ulice – the numbers 3 and 5. The Company expects that the 2009 results will be impacted in the form of a one-off profit from the sale of the real property, amounting to more than CZK 300 million; the proceeds will be posted as incremental cash.

Telefónica O2 intends to continue in the analysis of utilisation of its assets, in order to ensure that they are beneficially employed. The completion of the sale of a part of the real estate portfolio gave a clear signal that the Company wants to efficiently use those assets that are necessary for its core telecommunications business.

TELEFÓNICA O2 SLOVAKIA

In two years from the launch of its commercial operations, Telefónica O2 Slovakia became a stable part of the Slovak mobile telecommunication market. According to customer satisfaction surveys, the company's customers rank among the most satisfied and most loyal ones. Since entering the market, Telefónica O2 Slovakia has been constantly promoting changes in the competitive environment for the benefit of the customers. Already at the beginning, it came out with a single pricing of calls, SMS and MMS to any network in the Slovak Republic, and thereby created a space for barrier-free communication in the community of 5.5 million Slovak mobile telephony users. Innovations introduced by Telefónica O2 Slovakia were adopted as a standard also by the other two Slovak mobile operators. At the same time, the company progressed in the rollout of its own mobile network; approximately 83% of the voice traffic generated by its customers was carried in the own mobile network at the end of 2008. As at the same day, the company recorded 325 thousand active customers, of which 99 thousand were users of postpaid services.

The main commercial goal of Telefónica O2 Slovakia in 2008 was to keep the customer number growth momentum, increase the proportion of active postpaid service users and to develop its base of prepaid customers through offering innovative services.

At the beginning of September 2008, Telefónica O2 Slovakia began to market a new service called O_2 Fér. The service eliminated the previously mandatory flat monthly fee, so that the customer now pays only for airtime. O2 Fér introduced single usage rate of € 0.13 (SK 3.92) per minute anytime to all numbers in Slovakia. SMS, too, was flat-billed at € 0.06 (SK 1.81). O2 Fér is completely without commitment and the customer can freely choose between receiving a bill or topping up. The offer included optional Extra top-up packages that the customers could activate if they wanted additional economically-priced airtime, SMS or data volumes. Upon launching the new O_2 Fér, the company terminated the marketing of all its previous programmes and subsidised mobile handsets.

The company also accomplished its effort to become a part of the Mobile Number Portability automated system. Previously, the service had to be effected manually because of a lack of good will on the part of the other two mobile operators.

Introduction of the new O_2 Fér offer, which was fast and very well received by the market, became one of the key growth factors in 2008. This was reflected also in a considerably increased interest in number portability. In 2008, the company recorded more than 25 thousand requests for a transfer of a number from other operators.

Prepaid service customers benefited from a simpler credit top-up in the ATM network of two largest banks in Slovakia. From July 2008, customers of Telefónica O2 Slovakia could also top-up any amount of credit on the company's website.

At the end of 2008, Telefónica O2 Slovakia customers were the most satisfied and most loyal among the customers of mobile operators in Slovakia as measured by the Customer Satisfaction Index (CSI). CSI is calculated from the responses of customers to three questions concerning their satisfaction: overall satisfaction with the operator, meeting expectations and approaching the ideal. According to the survey outcomes from the last quarter of 2008, Telefónica O2 Slovakia beat the competing operators in all three areas.

In terms of operations, the company's strategy focused on rolling out of its own network, and on using national roaming only in areas which its own network does not cover. By the end of 2008, Telefónica O2 Slovakia commissioned more than 850 base stations, and its network covered almost 90% of the Slovak population. In May 2008, Telefónica O2 Slovakia announced that it had commenced the network barring in eight largest Slovak cities. The first was Banská Bystrica, to be followed by Bratislava, Košice, Nitra, Prešov, Trenčín, Trnava and Žilina; it will lead to lesser usage of the T-Mobile network based on the national roaming agreement. At the end of 2008, Telefónica O2 Slovakia was able to carry approximately 83% of the voice traffic generated by its customers in its own network all the way. In November 2008, an inspection from the Telecommunications Office of the Slovak Republic confirmed that Telefónica O2 Slovakia had met the licence conditions which related to the number of base stations (BTS) and the coverage of population with own network. The company also expanded the operations of its call centre in Banská Bystrica.

Also in the next years, Telefónica O2 Slovakia plans to concentrate on delivering on its strategy. Its customer oriented priorities include a careful monitoring of customer needs and responding adequately to the findings. Moreover, the company will focus on the further development of its network and IT infrastructure, its strategic alternatives in the area of mobile broadband, and it will use cost structure as its competitive edge. The proactive effort to strengthen effective regulation in certain fields continues to be an integral part of the company's activities. Telefónica O2 Slovakia believes that this is an important factor for the development of the competitive environment from which the customers would benefit.

RISK MANAGEMENT

Risk management is one of the primary management tools for effective governance of companies in the Group. Its purpose is to render support in accomplishing the Company's vision and strategy. All companies in the Telefónica Group apply the same risk management model which fully conforms to the best international practice in the field of corporate governance. Close cooperation with other members of the Telefónica Group contributes to further development of the risk management system, which is an integral part of the Group's internal control system.

Risks are identified based on an assessment of the relevant management levels and suggestions made by Risk Management, Internal Audit and other units of the Group, and are evaluated in terms of their potential financial impact and likelihood of materialisation. Where the value of a risk exceeds a set limit, the risk is included in the risk catalogue of the Company. Every month, a risk management report is submitted to the governing bodies of the Group.

Also in 2008, Risk Management was responsible for the methodology and risk management system on the Group level. The governing bodies – the Board of Directors and the Supervisory Board, or, where appropriate, its Audit and Control Committee – were informed on a monthly basis of all major risks to which the Group was exposed, and of the ways the risks were mitigated.

The Company may encounter the following risks associated with the conduct of its business:

COMMERCIAL (MARKET) RISKS
Possible losses caused by market uncertainty, developments in the market or the competitive environment, changes in the legislation, which includes also regulatory intervention. Regulatory actions taken by the European Commission may have a significant bearing on the Company's bottom line.

FINANCIAL RISKS
Risks stemming from the fluctuations in the exchange rates of currencies or in the interest rates.

CREDIT RISKS
Risks of exposure to defaulting business partners or customers, e.g. receivables from customers or distributors.

OPERATING RISKS
Risks of possible losses caused by incidents relating to processes, human resources, network elements and information systems, or by external factors.

THE TELECOMMUNICATIONS MARKET IN THE CZECH REPUBLIC

Compared to the previous years, the rate of growth of the Czech telecommunications market experienced a slight slowdown in 2008. The market grew approximately 1.5% on the previous year; the rate of growth was 2.5 percentage points lower compared to 2007, which was caused mainly by the slowdown in the overall retail consumption. The total market growth as measured by revenues lagged behind the GDP growth by approximately 1.5 percentage point. The fixed market revenues were stable in year-on-year terms, whereas the mobile market revenues grew approximately 3% (compared to a growth of 6.6% in 2007). The penetration of fixed lines at the end of 2008 reached 23%, which is a continuing trend of the past years. The SIM card penetration on the other hand reached 131%, which ranks it among the highest in Europe.

The trend of fixed-to-mobile substitution continued. According to Company's own research, the proportion of mobile traffic in the total traffic grew approximately from 76% in 2007 to 81% in 2008. The trend of continuing growth in the demand for data, internet and other value-added services continued as well.

TRENDS ON THE FIXED LINE MARKET

The trends on the fixed line market in 2008 included product bundles combining voice, internet and television service, abolition of FUP (Fair User Policy) data limits, ADSL connection speed upgrades and the development of IPTV.

The revenues from the fixed line market in 2008 reached approximately CZK 52 billion, which is the same as in 2007. The decline in the revenues from data services was compensated mainly by the fast increase in the revenues from internet and television.

Competitive pressures in the fixed line segment increased. Cable operators pursued an aggressive pricing policy based on low prices and customer acquisition offers. Voice over IP telephony also experienced a growth mainly due to low prices and the growing numbers of alternative providers and internet users. The trend of fixed-to-mobile substitution continued. The number of fixed lines declined again in 2008, albeit at a slower rate.

ADSL was the area which underwent the most significant development in 2008. In March, Telekom Austria Czech Republic, which provides its services under the VOLNÝ brand, launched the so-called naked ADSL – an internet connection without the need to buy a voice tariff with a fixed line. In early April 2008, Telefónica O2 abolished its FUP data limits and let its customers download data without limitation. Other operators followed suit of Telefónica O2: the first were GTS Novera and Telekom Austria Czech Republic, joined later by České Radiokomunikace and T-Mobile, which joined the ranks of ADSL providers in 2007. At the end of summer 2008, there was a wave of ADSL speed upgrades, which largely simplified the internet tariff structure of all operators; at the end, there were two options to choose from: 8 Mb/s (or 10 Mb/s, as the case may be), and 16 Mb/s (or 20 Mb/s). The prices remained at the level of the previous 2 Mb/s and 4 Mb/s connection speeds. České Radiokomunikace, which began to offer its Premium ADSL with connection speed of up to 20 Mb/s, became the fastest ADSL provider on the Czech telecommunications market. The cable operator UPC was the last to act on this trend; UPC overhauled its internet tariff structure in September and added two new options – 10 Mb/s and 20 Mb/s. In addition to increasing the speeds of connection, operators focused on the promotion of their new internet access products through special offers, promotions, time-limited zero fees and discounts on terminal equipment.

Wi-Fi, which is rather unusually used for internet access in the Czech Republic, continued to hold a strong position. The number of Wi-Fi users grew approximately 12% year-on-year. With more than 740 thousand users (source: RT Audit), Wi-Fi has a unique position among internet access technologies in the Czech Republic compared to the rest of Europe.

IPTV, too, enjoyed a rapid growth. The number of Telefónica O2 customers who used O_2 TV reached 114,496 at the end of 2008. The Company also increase the number of television channels, expanded the choice of programme bundles and introduced O_2 TV Multi which lets customers watch television via O_2 TV at two television sets simultaneously.

Changes in the ownership structure, which started already in 2006, continued in 2008. The changes were not as evident as in the year before. UPC continued in strengthening of its leading position on the Czech cable market. In February 2008, UPC completed the acquisition of the cable, internet and telephone provider Kabelová televize Karviná. In May it acquired Forcom Net which provides its service in 13 towns of Moravia and in the east part of Prague. During 2008, UPC also concentrated on the development of its fixed line telephony business and launched a voice service in September 2008; one flat rate includes free call time also to fixed line networks to other European networks, USA and Australia. The consolidation of the cable market in 2008 also included the acquisitions made by F.C.A. and BKS Capital Partner; the two companies took over more than 40 metropolitan cable networks. Telefónica O2 distributed television content through its O_2 TV in HDTV quality. Cable operators began to offer HDTV quality during 2008.

At the beginning of December, Dial Telecom bought from Telekom Austria Group its Czech subsidiary Telekom Austria Czech Republic. Dial Telecom has a comprehensive portfolio of voice, data and internet services with guaranteed access through a proprietary optical network in all of the Czech Republic. The company is also member of the international Dial Telecom Group, which has holdings in the Czech Republic, Slovakia and Romania.

TRENDS ON THE MOBILE MARKET

The revenues generated from the mobile market in the Czech Republic in 2008 reached approximately CZK 87.5 billion, which makes for a year-on-year increase by 3%. The SIM card penetration in the Czech Republic reached 131% at the end of 2008, which is a 5 percentage point increase, ranking the Czech Republic among countries with the highest penetration in Europe. The net adds of customers in 2008 were 567 thousand customers, compared to 793 thousand in 2007. The net adds of customers declined by 28% on the year before.

The stronger competitive pressures on the mobile market became in 2008 even intense. Telefónica O2 recorded a year-on-year increase of 2.6% in the number of customers, and reached 5,257 thousand, which represents a 39% share of the market. The continuing migration of customers from the prepaid service to contracts helped the number of contract customers Telefónica O2 grow in 2008 by 12.3% on the year before; the total number of contract customers reached 2,519 thousand. The development of mobile voice services was affected by the launch of the new voice tariffs of Telefónica O2. In May, the Company introduced O_2 NEON, a new family of tariffs. Its main advantage is that the customer can call and send SMS free-of-charge within the flat monthly fee – either to other numbers within the network, or to other networks, depending on the chosen tariff. The new tariffs were joined by a brand new special tariff O_2 [:kůl:] for young people; the tariff offered free call minutes to all networks and no charge for any number of on-net SMS.

Other operators focused on community products and on making their prepaid tariffs more attractive. T-Mobile also launched new tariffs: T-Mobile Rodina, which came with free airtime between up to five "family" numbers in the T-Mobile network within the flat monthly fee, and Bav se s Mých 5, which let users send free SMS to up to five selected numbers in the Czech Republic, and call these numbers at reduced rates. Moreover, T-Mobile introduced a new prepaid tariff, T-Mobile Combi, which combined the benefits of a traditional tariff and a prepaid card. Vodafone promoted its Program kamarádi, and expanded its prepaid card offer with Vodafone Nabitá karta, which let the user call for the same lower rates as traditional tariffs if the card was topped-up monthly by a set amount.

The event of the summer was the launch of the iPhone. Telefónica O2 and T-Mobile started selling iPhone handsets in their brand stores at the midnight of 22 August 2008; Vodafone started selling the model exclusively through its e-shop. The map of the mobile market also changed as a result of the mobile operator Mobilkom which operates its network under the U:fon brand. Mobilkom launched a mobile voice service in its CDMA network in June and began to market four voice tariffs with on-net calls free-of-charge. During 2008, all mobile operators adjusted their roaming voice prices under regulatory pressure from the European Union.

In 2008, mobile operators focused largely on providing mobile data and internet access services. Telefónica O2 announced in August 2008 that it planned to expand its UMTS/HSDPA network. The Company plans to roll the network out to other relevant cities in the Czech Republic by the end of 2009. The technology should cover more than 70% of the Czech population in the next two to three years. T-Mobile announced in the summer of 2008 that it would no longer invest in its 3G UMTS (TDD) network; instead, it has plans to implement LTE, a novel technology which should be piloted in the Czech Republic. T-Mobile corrected the earlier statement at the end of 2008, adding that it planned to launch a 3G UMTS network based on the FDD technology. In the first stage, T-Mobile intends to roll the network out in the five largest Czech cities, and cover approximately 70% of the Czech population by 2010. Vodafone, which again postponed the launch of its 3G network in December 2007, commenced the construction of its UMTS network at the end of 2008. The network was partially commissioned in December 2008, with further expansion of the coverage planned for the end of the first quarter of 2009. In September, Vodafone commenced the preparation for the launch of a wireless internet service; it also built a limited network of Wi-Fi hotspots in Prague (covering selected hotels, restaurants and public institutions).

In addition to the deployment of new technologies, the areas of data tariffs and mobile internet, too, enjoyed a boom. Operators based their mobile internet offerings mainly on economical bundles, combining a notebook with internet access and terminal equipment for an attractive price. In early 2008, Vodafone launched a new data tariff, Připojení na stálo, which is an unlimited mobile data service for a flat monthly fee. In its Christmas campaign, Vodafone offered fast mobile internet free of charge for six months. Telefónica O2 introduced its mobile internet proposition to the market already in the summer. In July, the Company launched two new tariffs: O_2 Internet v mobilu and O_2 Internet v mobilu Plus. The tariffs bring the internet to the mobile without the need to have a computer or a notebook at hand.

During 2008, mobile operators continued in the development and promotion of their professional services for the business segment. T-Mobile launched ProfiNet, its integrated telecommunications solution for businesses, in April 2008. The solution combines all types of telecommunications services – mobile and fixed voice and data, including VPN. In July 2008, Vodafone began to offer a fixed line service and fixed line internet access to selected groups of its business customers. In pursuit of a stronger position in the business segment, Vodafone acquired BroadNet in September 2008; BroadNet is a fixed line telecommunications provider in the Czech Republic.

REGULATION

Several changes occurred in 2008 in the legislative environment which governs the field of electronic communications in the Czech Republic. The most material changes included the following:

- amendment of the Electronic Communications Act concerning the storage of operating and localisation data;
- passing of a government decision providing for a technical plan of the transition from the analogue to the digital television broadcasting, and of a related regulation on the demarcation of an area covered by a network signal;
- amendment to the government decision setting out the amount and method of calculation of fees for the use of radio frequencies and numbers;
- commencement of the implementation of the European Parliament and Council Regulation Audiovisual Media Directive (by way of an amendment of the Act on Radio and Television Broadcasting);
- preparation of the next amendment to the Electronic Communications Act in respect of radio frequency licences, compensation for the Universal Service, priority of emergency connection, pecuniary sanctions for the violation of statutory duties arising from the Electronic Communications Act or thereunder, storage of operating and localisation data;
- continuation of discussion of the so-called EU regulatory framework for electronic communications services in the European Parliament;
- European Commissions proposal of draft European Parliament and Council Regulation no. 717/2007/EC on roaming.

Telefónica O2 raised comments on the European Commission’s proposal for the review of the new EU regulatory framework for electronic communications services in the discussion of the European Parliament committees. The Company was also contributed to the preparation of the above legislative amendments through its involvement in the process of expert or public consultations, either directly – through industry associations of telecommunications operators, or through the parent company.

RELEVANT MARKETS ANALYSIS AND PRODUCT REGULATION

Telefónica O2 continued to meet its duties with which it was tasked based on the relevant markets analysis undertaken by the Czech Telecommunications Office (CTO) in 2006.

The CTO issued a General Provision No.1, which sets out the relevant markets in the field of electronic communications. The number of relevant markets was reduced from eighteen to seven. The CTO took over the full list of relevant markets from the European Commission recommendation in 2007.

During the whole of 2008, the CTO analysed the markets which were taken off the list of relevant markets by the European Commission. The analyses resulted in a gradual cancellation of regulatory powers, especially in the retail voice markets.

In May 2008, the CTO released a draft analysis of the wholesale high-speed internet market in the process of public consultation; the analysis was supposed to reflect the new trends in the development of the high-speed internet access market in the Czech Republic. At the end of 2008, the CTO published a final version of the analysis and nominated Telefónica O2 as the Operator with Dominant Market Position in this segment.

In the second quarter of 2008, the CTO published new regulated prices for Local Loop Unbundling which took effect from 1 July 2008. The monthly price for a fully unbundled local loop fell from CZK 360 to CZK 262 per month. The price of shared access to the local loop was reduced from CZK 92 per month to CZK 53.

In the second half of 2008, the CTO announced the commencement of the second round of the relevant markets analysis (for segments fixed line termination, mobile termination and access to the fixed line infrastructure).

In the third quarter of the year, the CTO published its price regulation decision, effectively reducing the prices of call termination in fixed line networks. The per-minute price of a call terminated in a fixed line network in the peak and off-peak was reduced from CZK 0.38 to CZK 0.36 and from CZK 0.19 to CZK 0.18, respectively. Likewise, the CTO published a proposal of the new maximum prices for call termination in mobile networks, with an outlook until 2010. The proposal details that the prices are to go down from the original level of CZK 2.99 per minute to CZK 2.65 per minute with effect from 1 February 2009 (the relevant price regulation decision providing for the lower prices effective from 1 February 2009 was published by the CTO in January 2009).

The CTO issued a price regulation decision concerning the Weighted Average Cost of Capital (WACC) in the field of electronic communications services, and the subsequent amendments to the regulated prices. The WACC rate of 11.5% for mobile and fixed line services was in effect from 1 July 2008.

REGULATION OF INTERNATIONAL ROAMING

Telefónica O2 cut its prices for SMS roaming in the countries of the European Union from CZK 10 to CZK 8.40, and introduced economical data roaming bundles. Customers have a choice of services from 2 to 250 MB, depending on their actual need. The European Commission commenced a public consultation on the evaluation of impacts of its international roaming regulation from 2007 on the market in electronic communications services. In August 2008, the Company adjusted its retail and wholesale roaming prices to heed the roaming regulation. At the end of the year, the European Commission presented its proposal for international roaming regulation after 2010.

IMPOSITION OF DUTIES RELATED TO THE PROVISION OF THE UNIVERSAL SERVICE

Telefónica O2 provided the following services during 2008 as part of meeting its duties imposed by the CTO in relation to the Universal Service provision:

a) the public payphone service;
b) access to the public telephone service, of the same quality as for other end users, for people with disabilities, namely by means of special terminal equipment;
c) special price plans for persons with disabilities, which are different from the regular price plans provided under the standard commercial terms and conditions
d) ancillary services to the service of access to the public telephone service at a fixed point of the public telephone network:
   i) payment of the charge for connection to the public telephone network in instalments – consumers only;
   ii) free-of-charge selective blocking of outgoing calls;
   iii) free-of-charge itemised billing – consumers only;
d) regular publication of directories of subscriber telephone numbers in the area of the public telephone service, and access of end users to those directories;
e) directory services.

Based on a CTO decision, the services under letters (e) and (f) were excluded from the scope of the Universal Service with effect from 22 December 2008. The services continue to be provided based on commercial terms and conditions, outside the scope of the Universal Service.

UNIVERSAL SERVICE

During the course of 2008, the CTO issued decisions concerning the loss and net costs incurred in connection with the provision of services included in the scope of the Universal Service in 2006. As at the date of this report, the decisions have not become final and conclusive.

Telefónica O2 lodged an application with the CTO for the compensation for the provision of services included in the scope of the Universal Service in 2007. The CTO lawfully decided on the compensation for the loss relating to the provision of special price plans for persons with disability, which are different from standard price plans availed under normal terms and conditions. As regards the loss incurred in the course of provision of the remaining Universal Service components, the CTO verified the loss in 2008, but it has not issued a lawful decision.

GOVERNMENT POLICY AND SUPPORT IN THE AREA OF FAST INTERNET ACCESS
In April 2008, a government policy titled Strategy for the Development of Information Society Services in the Czech Republic in 2008–2012 introduced a new action plan for the development of information technology and e-government in the Czech Republic. The document was elaborated by the Government Council for Information Society and it communicates the steps and actions that are required for bringing the government and public affairs online.

The year 2008 saw the opening of possibilities for Czech businesses to apply for grants from the Structural Funds of the European Union through the Operational Programme Enterprise and Innovation administrated by the Czech Ministry of Industry and Trade, for the development of ICT.

The Ministry of Interior published the first call for proposals of ICT projects to be funded through grants from the Integrated Operational Programme of the Structural Fund in the second half of 2008.

NETWORKS AND TECHNOLOGY

In 2008, Telefónica O2 operated the largest fixed line and mobile networks in the Czech Republic, including third generation mobile networks.

In the area of mobile networks, investments were made mainly to build up capacities to accommodate the growing traffic volumes, further develop signal coverage and to improve the quality of service. The number of base stations in the 3G mobile UMTS/HSDPA network in Prague and Brno grew to 927 in 2008, compared to 919 at the end of 2007. The contingent of base stations suffices to cover 16.5% of the population. The network roll-out and fine-tuning delivered on the objective of improving the quality of a call in progress between this and the second generation networks. The volume of data traffic in the UMTS/HSDPA network grew in 2008; in the peak times, the traffic levels were 75% higher compared to 2007. In the second half of 2008, work commenced on a major roll-out of the UMTS/HSDPA network in other regional capitals. The work on the preparation for the modernisation of the second generation GSM network continued at the same time. In December 2008, the first four base stations of the new technology were commissioned in the town of Pilsen.

In order to accommodate the growing voice traffic volumes and ensure the coverage of new developments (residential, commercial and industrial zones) and roads, 208 new base stations were commissioned in the GSM network in 2008. The total number of base stations at the end of 2008 was 4,495, with 98.9% of the population covered. During 2008, more than 1,700 base stations were reconfigured. The purpose of this exercise was to ensure the quality and capacity of radio networks during fluctuations in the density of traffic, and in response to the need to meet the network qualitative parameters. The CDMA network used for broadband data services, too, was expanded; during 2008, the network added 27 new base stations to reach a total of 455, which in turn increased the population coverage to 89.8% as at the end of 2008, compared to 88.3% the year before.

In the area of fixed line networks, Telefónica O2 directed the majority of its investment in the development of ADSL based broadband internet connection and IPTV. In 2008, the Fair User Policy data limits, previously put in place to control the monthly volumes of downloaded data, were abolished; in their stead, Deep Packet Inspection selective download speed management was implemented for the peak times. The next wave of nominal speed upgrades for ADSL connections was started – the speeds were increased to 8 Mb/s and 16 Mb/s, respectively. These facts, in combination with the steady increase in the number of active connections, have led to an increase in the IP backbone network traffic to almost a double of what it was in 2007. Backbone transmission routes were doubled up, and new data nodes were built in the backbone IP/MPLS network, in order to boost the capacity and robustness of the network.

At the end of 2008, the number of locations with ADSL access points reached 2,257 in 2008; the total number of DSLAMs was 4,625, of which 2,258 were IP DSLAMs enabled for O_2 TV via ADSL2+. The total installed capacity of ports in these locations reached 898,943, which represents a year-on-year increase of 17.5%. Access points installed at IP DSLAMs enabled for O_2 TV represented 51% of the total in 2008, compared to 43% at the end of 2007. As at the end of 2008, the total of 664,720 ports were in use (17.3% more than the year ago). During 2008, the construction of new DSLAMs brought ADSL and O_2 TV to another 17 thousand and 196 thousand prospective customers, respectively.

The access network was expanded further, especially in new residential, commercial and production developments. The core of the network consists of metallic cables covering the whole territory of the Czech Republic, with optical fibre cables and radio relay systems lending more stability and capacity to the network. The total length of the metallic cables was 301 thousand kilometres at the end of 2008 (two thousand kilometres were built in 2008). The capacity of the optical network increased further in response to the growing volumes of traffic generated by broadband customers. The total length of optical fibre cables as at 31 December 2008 reached 30,785 kilometres (a year-on-year increase of 346 kilometres). The total length of optical fibres was 946,733 kilometres (a year-on-year increase of 13,640 kilometres).

Investment in the voice technology in 2008 focused largely on maintaining the status quo as the voice network traffic, with the sole exception of international traffic, has declined and no additional capacities were needed. The telephone network comprised 138 HOST exchanges and 2,391 Remote Subscriber Units (RSU).

Other investments were made in the value-added services. The voice mail system for fixed line and mobile services was modernised and standardised in 2008.

VOICE SERVICES

The portfolio of voice services of Telefónica O2 in 2008 was built on a strategy focused mainly on stimulating mobile voice traffic. In the fixed line segment, the Company concentrated on promoting converged service bundles, which included a voice tariff with unlimited calls to all fixed line networks in the Czech Republic.

Customers of the contract mobile service were offered various promotions – free calls in the O_2 network for a period of time. This offer was extended both to existing customers who had decided to switch from the prepaid service to a contract, and to customers coming from other operators. The promotions were good for consumers as well as for small businesses and self-employed persons.

In April, Telefónica O2 introduced Platí to Kvído, a new service which offered one free minute of call to any mobile or fixed line number in the Czech Republic; all one needed to do was to dial the special number 829 829 829 beforehand and listen to a short advertising message. Afterwards, the called number is dialled and the call is free for one minute. After 45 seconds, the caller is alerted to the approaching end of the sponsored call.

For its young customers, Telefónica O2 designed a new tariff, O_2 [:kůl:], which came with free SMS to the mobile network for the duration of the subscription to the tariff – without any additional charges. The price of O_2 [:kůl:] was CZK 250 per month inclusive of VAT and, in addition to unlimited free SMS in the O_2 network, it came with 60 free call minutes to all networks per month. The free airtime could be carried over to the next month. With O_2 Pokec Nonstop, customers could call in the O_2 network and to fixed lines number after the third minute of the call for CZK 1 per minute inclusive of VAT for six months. The first three minutes of the call cost CZK 15 inclusive of VAT. If the customer preferred texting, they could get the prepaid O_2 card with the tariff O_2 TXT. With every top-up of minimum CZK 200, they could send free SMS to two numbers in the mobile O_2 network for two weeks. The higher the top-up, the more numbers could be included for free SMS; five O_2 mobile numbers were the maximum – for two weeks with a top-up of CZK 500 or more.

In May, Telefónica O2 became the first operator in the Czech market to come out with a concept of simple and straightforward flat rate tariffs – O_2 NEON. For a flat monthly fee, customers could use the benefits that came with the tariff of their choice (e.g. unlimited calls in the O_2 network or in all networks), without having to pay anything extra. With O_2 NEON XXL, for instance, the customer paid CZK 3,900 inclusive of VAT and could call numbers in any networks and regardless of the time of day, at no extra cost. Other alternatives in the O_2 NEON family were O_2 NEON SMS (free SMS and MMS in the O_2 network on weekends), O_2 NEON S (free calls in the O_2 network on weekends), O_2 NEON M (free calls and free SMS and MMS in the O_2 network on weekends), O_2 NEON L (free calls in the O_2 network on weekends and off-peak), and O_2 NEON XL (unlimited free calls in the O_2 network). Unlike the various promotions, the benefits that came as part of the tariff were a standard and could be enjoyed for the duration of the subscription. The innovative tariffs O_2 NEON and O_2 [:kůl:] have, since their launch, met with an enthusiastic reception from customers; almost 400 thousand users activated one of the tariffs by the end of the year.

A similar proposition was extended to small and medium size businesses. Under the brand O_2 Business Unlimited, Telefónica O2 began to market a tariff with unlimited free calls to all fixed line and mobile networks in the Czech Republic as part of the flat monthly fee. The flat monthly subscription fee was CZK 3,200 exclusive of VAT. O_2 Business Nonstop Max for a flat monthly fee of CZK 1,400 exclusive of VAT offered free calls in the O_2 mobile network and to all fixed line networks in the Czech Republic, as well as 200 free minutes for calls to other mobile networks in the Czech Republic.

In order to slow down the rate of decline in the fixed line traffic on one hand, and to increase the penetration of broadband internet, Telefónica O2 introduced in the first quarter of 2008 the first ever VoIP (Voice over IP) service for the transmission of voice over data lines. O_2 Neomezená linka is a service designed primarily for small and medium size business customers – offering them maximum simplicity, comfort and flexibility. Corporate customers were marketed a similar service, branded as O_2 Virtuální ústředna. The main benefit was having access to a virtual telephone exchange – no need to invest in a real one and pay for keeping it in operation.

With effect from 1 July 2008, Telefónica O2 cut the prices of roaming data packages, and the prices of outgoing SMS in the My Europe SMS tariff. Subscribers to the data package could send data while abroad for the maximum price of CZK 0.05 per 1 kB. All contract and prepaid customer who had activated Eurotarif saw the prices of outgoing and incoming calls within the European Union and from EU member states to the Czech Republic cut by more than 20%, with effect from 29 August 2008.

INTERNET, DATA AND VALUE ADDED SERVICES

In the area of fixed line internet, Telefónica O2 focused on the improvement of the service portfolio with a view to add more value to the fixed line and promote broadband ADSL internet and the digital O_2 TV. The Company abolished the Fair User Policy data limits for broadband internet via ADSL, and increased the connection speeds – completely in tune with its strategy to bring out services which are innovative and reflect what the customer demands. Telefónica O2 also expanded the programme offer for O_2 TV, the service of television over the fixed line. Both products were still the core components of the bundles of converged services; the number of customers using a service bundle as at the end of 2008 reached the 270 thousand mark.

From 1 April 2008, Telefónica O2 cancelled the data limits for data transmission – for existing customers of O_2 Internet ADSL, including those who subscribed to ADSL internet as part of one of the specially priced bundles O_2 Trio, O_2 Duo, O_2 Duo Mobil, and those who used O_2 Internet Komplet and O_2 Internet Komplet Business.

From 1 September 2008, Telefónica O2 began to gradually increase – by up to fourfold – the connection speeds for O_2 Internet ADSL while the prices remained the same. The basic download speed for O_2 Internet ADSL is now 8 Mb/s, and a premium service of 16 Mb/s was newly added to the portfolio. The upload speed, too, was increased to 512 kb/s and 768 kb/s, respectively. Existing customers of O_2 TV bundled in O_2 Trio, whose line was technically ready for the upgrade, enjoyed faster internet from 15 October 2008. Customers who subscribed to O_2 Duo and O_2 Duo Mobil bundles could apply for a speed upgrade from 1 September 2008. Other O_2 Internet ADSL customers whose lines required technical adjustments had their connection speeds increased from 1 February 2009.

In addition to the speed upgrades and the abolition of the data limits, Telefónica O2 ran several marketing campaigns designed to boost the sales of O_2 Internet ADSL. As a result, the number of ADSL retail connections grew 14% year-on-year and as at 31 December 2008 it reached 579 thousand. The number increased by 41 thousand in the last quarter of the year alone.

Telefónica O2 introduced O_2 Internet Konfigurátor – an application included with the O_2 Internet ADSL self-installation kit – which facilitates the whole service installation process; in an easy and intuitive way, the application guides the user through the whole installation process and automatically configures the modem and the PC. For the Company, the benefit comes in lesser demand for technical support during service installation.

Two new programme offers were launched for O_2 TV: O_2 TV Styl Plus for the lifestyle trend follower and for the gourmet, and O_2 TV Hudba Plus for the music fan. In February 2008, popular TV Nova programmes were added to the TV Archive. Telefónica O2 also introduced Multi, a service which let new and existing O_2 TV customers watch different channels on two television sets. O_2 TV Multi did not require a second O_2 TV subscription. Upon ordering Multi, the customer automatically received a second set-top box (for the other television set), and a new 2-port modem which is required for Multi.

In 2008, Telefónica O2 had the broadest portfolio of mobile data access, which represented a significant competitive advantage over other mobile operators in the Czech Republic. The CDMA technology covered almost 90% of the Czech population at the end of the year. Customers in Prague and Brno could use HSDPA, currently the fastest technology available on the market, while other parts of the Czech Republic were well covered with GPRS, EDGE and HSCSD. In August 2008, the Company announced that it planned to roll out 3G network to other relevant cities in the Czech Republic by the end of the year. In the next two to three years, the 3G network will cover more than 70% of the Czech population.

The addition of two new services – O_2 Internet v Mobilu and O_2 Internet v Mobilu Plus – to the portfolio of mobile data services represented a milestone in the field; they were a reaction to the dynamically growing demand for internet in the mobile telephone. With monthly subscription fee of CZK 150, O_2 Internet v Mobilu was designed namely for consumers and it contained unlimited internet in the mobile, including email. The service was intended to run especially on mobile handsets with more advanced functions; still, the data transmission capacity is still several times lower than on a PC. During one month, users could transit 150 MB of data at a speed of up to 1 Mb/s, regardless of the transmission technology. After reaching the limit, the speed was reduced to 16 kb/s. Customers who wanted to transmit larger volumes of data could use O_2 Internet v Mobilu Plus for CZK 390 per month, which came with a limit of 500 MB. The tariff was intended mainly – but not exclusively – for business customers.

From January 2008, small and medium business customers of Telefónica O2 could subscribe to O_2 Business Mail. An account at the Microsoft Exchange email server was created for every user, which – in addition to an email box – featured also a shared diary and workspace, address book and anti-virus and anti-spam filter. The virtual office could be accessed via a mail client, internet browser or from a mobile telephone. Telefónica O2 offered two alternatives of O_2 Business Mail; the basic service O_2 Business Mail Standard came with a data limit of 100 Mb, and the higher-end O_2 Business Mail Profi had a data limit of 500 Mb and came with a fully paid-up licence for a mail client for MS Outlook 2003 or 2007. The capacity could be flexibly increased and the service activation and installation were free of charge.

At the beginning of 2008, Telefónica O2 started the marketing of BlackBerry E-mail Start. BlackBerry is one of the most popular mobile office solutions. With its zero subscription, BlackBerry E-mail Start was a unique service in the Czech Republic. After activating the service, the user paid only for data they actually transmitted. Another addition to the BlackBerry range was BlackBerry Business Mail, which combines the benefits of the already existing services (BlackBerry and O_2 Business Mail) – full connectivity to corporate data – with the fact that a proprietary BlackBerry and mail server are no longer required. In principle, it was a BlackBerry ad-on to the already existing O_2 Business Mail. For the standard monthly fee charged for O_2 Business Mail Profi and for the chosen BlackBerry tariff, the customer had a professional e-mail solution running on their own domain, with full mobile synchronisation.

In addition to BlackBerry services, Telefónica O2 offered also O_2 Office Connector, which gives remote access to corporate documents. However to use it, customers did not need to buy a special mobile handset – all that was needed was to upload a simple application to the mobile. Selected mobile models already came with the application, ready to be deployed. The wide range of handsets it was compatible with made the service extremely flexible. Moreover, customers could buy mobile handsets already enabled for the service at subsidised prices with a new application.

In April, Telefónica O2 made it possible for all residents of the Czech Republic to use O_2 Hot Spot and access the websites of government organisations (e-government), regardless of whether they were or were not customers. O_2 Hot Spot is a form of data transmission which, in addition to being fast, is very easy to use. O_2 Hot Spots built in strategic locations in the Czech Republic free the user from having to look for a socket to connect to the internet. O_2 Hot Spot is also a very transparent form of data transmission and all standard protocols (HTTP, POP3, IMAP4, SMTP, FTP, IPsec, etc.) may be used with it. Telefónica O2 owns and operates the densest network of hot spots in the Czech Republic. At present, the service is available in more than 200 locations.

CONVERGENT SERVICES

Heeding its position of the leading integrated operator in the Czech telecommunications market, and in tune with its strategy of improving the quality of the fixed line service, Telefónica O2 in 2008 concentrated on advancement of its broad service portfolio combining fixed line and mobile voice, high-speed internet and television over the fixed line. The aforementioned upgrade of the broadband internet service (speed increases, elimination of the data limits) and the digital television service O_2 TV turned the convergent bundles into the primary instrument of strategy implementation.

In order to increase the numbers of users of the innovative services, in part to compensate for the declining numbers of fixed lines, Telefónica O2 ran several price promotions on the converged service bundles during the year. The end of the year clearly showed that converged services were clearly popular – the total number of customers subscribing to any of the bundles reached 270 thousand. The increase in the number of customers also helped to increase the number of retail ADSL connections and of O_2 TV users – by 14% year-on-year, to almost 580 thousand as at the end of 2008, and by 57% to 115 thousand, respectively.

ICT SERVICES, BUSINESS SOLUTIONS FOR THE GOVERNMENT

ICT services provided by Telefónica O2 combine unique experience in the field of telecommunications with IT technology, helping to combine the cost of acquisition for better efficiency, simplify the administration of IT infrastructure, flexibly adjust IT capacities to deal with the problem of the increasing cost of IT administration. They may come with a voice service, data networks, security components and hardware.

Telefónica O2 markets its ICT services as Professional Services. The solutions are made to fit the needs of the customer, and are designed in particular for the larger corporate customer. The Company also focuses on the growing of its portfolio of the so-called Managed Services. These are solutions that bring ICT to the customer on a fee-for-service basis, without the need to buy own hardware, software and hire own human capacities.

In the previous years, the Company offered Managed Services in the area of hosting and managed hosting, O_2 Kompletní kancelář (a solution delivering a local network to the customer, complete with administration, with the possibility of IP telephony and other ancillary services), O_2 Počítačové řešení (a lease of computers complete with maintenance and administration), or Managed PBX (a managed administration of a PBX exchange).

In 2008, Telefónica O2 broadened its Managed Services portfolio by adding O_2 Managed Hosting, a new service with three service components: Managed Data Storage came with a dedicated disk array for the storage of up to hundreds or thousands of gigabytes of data; Managed Server Hosting offered a server computing capacity under a guarantee of quality, for a period of time, complete with system administration to the operating system level, including change request planning and implementation; and finally, Managed Backup & Restore allowed those customers in particular, who use a hosting service of Telefónica O2, to make copies of data on a back-up medium for the event of a loss of data in the primary repository, and the restoration of the data. Managed Backup & Restore came with dedicated back-up hardware and software capacity, complete with the administration of the systems.

Other new services in the field of ICT were O_2 Managed Security/O_2 SecureNet, which provides for the security of corporate data, O_2 Managed Desktop, which is a comprehensive, multi-level professional IT infrastructure administration service, and O_2 Hosted Exchange, a professional e-mail communication solution. O_2 Managed LAN/Managed WAN ensures a full control over and administration of local and remote customer networks.

The successful service O_2 Počítačové řešení earned the distinction to use the label IT Product of the Year in the prestigious poll of the Computerworld magazine.

In 2008, Telefónica O2 also made available hardware capacity in its Nagano hosting centre for the operation of the telecommunications solution for the government (Komunikační infrastruktura informačních systémů veřejné správy) which Telefónica O2 successfully tendered in 2007. The Company also continued to render advisory services to the government and operate the central service desk. The situation of the hardware in the hosting centre helped simplify the infrastructure, improve effectiveness of communication and services and reduce the costs.

The project Operational Support to Cross – Compliance, IP/EP and ESB Communication Interface concluded at the end of November 2008 with the Czech Ministry of Agriculture followed on a 13-month long project of the building of a Cross Compliance system. The project goal was to provide for the centralisation of applications in the various information systems of the agencies supervised by the ministry.

The construction of a central data contingency warehouse for messages about the controls made and the implementation of a single ESB data communication interface were among the main supervised systems. Telefónica O2 employees guaranteed the relevant agencies of the ministry and the farmer community a real time availability of all services needed for the control activities and the processing of control reports; all ICT systems work in synchronisation with the processes governing the disbursement of agricultural subsidies. The project as a whole follows on a long-term project of Systems Integration which Telefónica O2 has been implementing for the ministry since 2005.

In November 2008, Telefónica O2 entered into an agreement with ÚZSVM (Office for the Representation of the State in Property Matters) regarding the expansion and optimisation of hosting services for application operation; the project gave ÚZSVM the support it required and provided for the future operation of ICT services, including the necessary resources. The project included hardware and software infrastructure, information systems operation, interface services and data security, proactive supervision of mission-critical parts of the ICT infrastructure, operation of a customer service desk and service management. ÚZSVM and the affiliated government agencies were guaranteed a real time availability of all systems needed for ÚZSVM operations and for information sharing with other government agencies.

In the autumn of 2008, Telefónica O2 confirmed its strong position in the government segment when it implemented a system connecting 580 election rooms in all parts of the Czech Republic during the regional government and Senate elections. The Company also supplied voice connectivity and a public telephone service, including the possibility to send and receive SMS. Telefónica O2 also operated the www.volbyhned.cz election results server with the most current election results. Independent connections with IP Connect and VPN Express Comfort services activated were installed in all election locations. O_2 SMS Connector provided for the SMS service. The overall solution also included the operation of the election server.

NATIONAL AND INTERNATIONAL WHOLESALE SERVICES

In the area of national wholesale, the year 2008 saw the continuation of many trends of the previous years. The market consolidation continued (more about market consolidation on page 29 of the Annual Report). Mobile operators pursued the strategy of convergence of mobile and fixed line services and entered the market of fixed line voice services for the business segment. The trend has led to an increased interest in the wholesale offer of SDSL access services. Telefónica O2 responded to the developments by innovating its SDSL service portfolio and by adjusting the terms and conditions for the leased lines service. In 2008, it effected changes in the reference offer for the "last mile" of leased lines. Despite the positive trend, price erosion continued, leading to the overall stagnation of the wholesale market. Despite this fact, Telefónica O2 remained the number one wholesale provider in the Czech Republic.

In the area of international data and internet services, the expansion of broadband internet service abroad for the international wholesale partners of Telefónica O2 demanded that additional capacity be procured, especially in the area of international IP connectivity. This has led to an increase in the demand and in the successful sales figures for high-capacity international leased lines (Lambda 2.5 and 10 Gb/s). A similar trend, i.e. a growing demand for international IP connectivity, was driven by the increasing needs of residential and corporate customers in the Czech Republic. Compared to 2007, the total IP connectivity of the Company grew almost threefold as a result.

In the area of international voice, Telefónica O2 reinforced its position in the region of Central and Eastern Europe. The Company increased the number of direct lines to new mobile operators in Europe and in the rest of the world, and concentrated its attention on the Middle East region. Under the global brand of Telefónica, the Company won the global auction of Vodafone for international voice service, in which it tendered with the parent company Telefónica, S.A. Compared to 2007, the volume of transit services grew 40% and reached a record of 1.4 billion minutes.

At the end of 2008, the fixed line and the mobile networks of Telefónica O2 were interconnected with 19 and 11 network operators providing the services of public electronic communications in the Czech Republic, respectively.

COMMENTS ON THE FINANCIAL RESULTS

In this section we present and comment on the consolidated financial results of the Telefónica O2 Group prepared in accordance with International Financial Reporting Standards (IFRS).

CONSOLIDATED FINANCIAL RESULTS

REVENUES, OPERATING COSTS AND OIBDA

The consolidated revenues reached CZK 64.7 billion in 2008, up 2.4% year-on-year. The consolidated business revenues grew 2.9% year-on-year to CZK 64.4 billion in 2008. Telefónica O2 Group delivered on its full year guidance of 2% to 4% growth in business revenues. Gains from the sale of non-current assets reached CZK 855 million in 2008, compared to CZK 42 million in 2007. The gain from the sale of a part of the real estate portfolio, which amounted to approximately CZK 727 million and is described on pages 24–26 of this Annual report, was the key driver of the overall gains in 2008. The total consolidated operating costs reached CZK 37.7 billion in 2008, up 5.3% year-on-year. The resulting consolidated operating income before depreciation and amortization – OIBDA – amounted to CZK 28.3 billion in 2008, up 1.0% year-on-year. OIBDA adjusted for guidance[1] grew 0.9% year-on-year to CZK 28.3 billion in 2008, which was within the guidance range of 0% to 2%. The OIBDA margin (OIBDA over Business revenues) reached 43.9% in 2008, compared to 44.8% in 2007. The Slovak operation diluted the OIBDA margin by close to 2.6 p.p. in 2008.

[1] In terms of guidance calculation, OIBDA excludes other exceptional revenues/expenses not foreseeable in 2008 (CZK 86 million of impairment charge, CZK 626 million of brand fees and CZK 727 million of a gain from real estate sale booked in 2Q). For the purpose of comparison, other equivalent exceptional revenues/expenses registered in 2007 were also deducted from the reported figures (base reported 2007 figures exclude the CZK 6 million impairment charge).

DEPRECIATION AND AMORTIZATION

The consolidated depreciation and amortization amounted to CZK 12.9 billion in 2008, resulting in a decline of 10.4% year-on-year.

OPERATING INCOME, INCOME BEFORE TAX AND NET INCOME

The consolidated operating income and consolidated income before tax went up 13.1% year-on-year and 13.6% year-on-year, and reached CZK 15.4 billion and CZK 15.3 billion, respectively, in 2008, on the back of a slight growth in OIBDA and the continuing decrease in the depreciation and amortization charge. The consolidated net income amounted to CZK 11.6 billion, up 12.0% year-on-year in 2008.

FREE CASH FLOWS

In 2008, the Group's free cash flows[1] amounted to CZK 19.5 billion, up 6.5% year-on-year. Net cash from operating activities went down 8.6% to the level of CZK 21.8 billion, and was driven mainly by an increase in the income tax paid due to the higher net income, and the CZK 2 billion payment related to the dispute with T-Mobile. In the second half of 2008, the Company received the majority portion of the proceeds from the real estate sale which was booked in 2Q 2008. The cash inflow more than compensated for the higher cash outflow related to the CAPEX accounted for in 4Q 2007 but paid in 2008, and resulted in a 60.9% decline of net cash used in investing activities.

CASH AND DEBT LEVELS

On 31 December 2008, the Group's consolidated financial debts (long-term and short-term) amounted to CZK 3.2 billion, down from CZK 9.3 billion at 2007 year-end. In July 2008, the Company repaid CZK 6 billion of its 5-year domestic bonds. The amount of cash and cash equivalents reached CZK 7.1 billion at the end of 2008, down from CZK 9.6 billion the year before. The combination of the cash and debt balances resulted in a net leverage[2] of minus 5.1% and a gross leverage[3] of 4.1% as at the end of 2008, compared to minus 0.4% and 11.2%, respectively, as at 31 December 2007.

[1] Net cash from operating activities plus cash flows from investing activities, excluding marketable securities, financial investments and dividends.
[2] Long and short term financial debts less cash and cash equivalents over equity.
[3] Long and short term financial debts over equity.

CAPITAL EXPENDITURE

The total consolidated capital expenditure amounted to CZK 8.1 billion in 2008, up 3.6% year-on-year. As in the previous years, investments selectively targeted at the growth areas of the business. Investments in the Czech Republic were directed towards increasing the capacity and coverage of the mobile broadband (mainly UMTS) and GSM networks, ADSL and IPTV, improvements of the fixed access network and upgrading of the information systems. In Slovakia, the company continued in the GSM network rollout and systems deployment. More than 850 BTS were put in operation by the end of 2008.

OVERVIEW OF CONSOLIDATED REVENUES

The total consolidated revenues in 2008 reached CZK 64.7 billion, up 2.4% year-on-year.

The total voice revenues (traffic revenues, subscription charges, interconnection revenues and connection charges) amounted to CZK 42.4 billion in 2008, down 2.2% year-on-year.

The total number of registered mobile customers in the Czech Republic increased 2.6% year-on-year to 5,257 thousand as at 31 December 2008. The total number of contract customers reached 2,519 thousand as at the same date, up 275 thousand year-on-year, which represents a 12.3% growth, and was helped by the successful strategy of active prepaid to contract migration and the good market response to the new O_2 NEON flat rate tariffs introduced in May. Contract customers accounted for 47.9% of the total customer base as at the end of December 2008, up from 43.8% the year before.

The number of prepaid registered customers in the Czech Republic decreased by 5.0% year-on-year to 2,738 thousand as at the end of December 2008. Under the methodology which defines a prepaid customer as one which generated revenue in the last 3 months, the number of active prepaid mobile customers amounted to 2,283 thousand as at 31 December 2008.

The blended monthly average churn rate reached 1.6% in 2008, which is 0.1 p.p. higher than in 2007.

The number of registered customers in Slovakia reached 455 thousand as at 31 December 2008. Applying the 3-month customer activity recognition criterion, the number of active customers reached 325 thousand as at that day, up by 18.7% year-on-year. The increase was driven mainly by the 57.2% year-on-year growth in the number of contract customers, which reached 99 thousand, while the number of active prepaid customers reached 226 thousand as at the year end, up 7.2% year-on-year. This development confirms the trend of stabilisation of the customer base, which had been seen since 3Q, after deactivations of inactive customers in the first half of 2008.

The indicator of average monthly minutes of use (MOU) per subscriber improved to 121 minutes in 2008, up from 116.9 minutes in 2007. The growing number of contract customers generating a higher average traffic per customer, coupled with the attractive O_2 NEON tariffs, which were designed to stimulate traffic and were met with a good response from the customers, were the key drivers behind the growth. By the end of December 2008, nearly 270 thousand customers subscribed to one of the O_2 NEON tariffs, and O_2 NEON customers accounted for 11% of the total voice contract customers. The voice traffic generated by fixed line customers in 2008 declined 14.3% year-on-year to 2,317 million minutes.

In 2008, the blended monthly average revenue per user (ARPU)[1] reached CZK 519, compared to CZK 524 in 2007. The monthly ARPU from contract customers reached CZK 847 in 2008, compared to CZK 907 in 2007 (- 6.7% year-on-year). The main reason for the lower contract ARPU is a dilution caused by the customer migration from the prepaid segment to contracts. The prepaid monthly ARPU decreased 2.0% year-on-year to CZK 242 in 2008, from the level of CZK 247 in 2007.

The voice (traffic) revenues (monthly fees charged to contract mobile customers, outgoing traffic revenues and roaming abroad revenues) increased marginally by 0.5% year-on-year to CZK 23.3 billion in 2008.

[1] Including inter-segment revenues

In 2008, net losses of the fixed telephony accesses operated by Telefónica O2 in the Czech Republic improved by 47.2% year-on-year. In 4Q 2008, net lines additions reached 1 thousand (including one-off adjustment of +31 thousand), compared to a loss of 45 thousand lines in 3Q08, a loss of 58 thousand in 2Q08, of 74 thousand in 1Q 2008 and of 65 thousand in 4Q 2007. This came as a result of the Company's strategy to add more value to the fixed line through an improved broadband proposition and bundled offers. The total number of the bundled product units sold (O_2 Duo, O_2 Trio and O_2 Duo Mobil) reached 270 thousand as at 31 December 2008; the number of fixed line accesses subscribed to one of the bundles represented a 14.2% share in the total accesses. The number of fixed line accesses declined 8.5% year-on-year to 1.893 thousand as at the end of 2008, which resulted in a 4.6% year-on-year decline in revenues from subscription charges, which amounted to CZK 8.4 billion.

The consolidated interconnection revenues in 2008 went down 1.9% to CZK 10.4 billion, driven mainly by higher revenues from the international fixed line transit traffic and mobile incoming traffic, which almost compensated for the declining revenues from fixed line incoming voice traffic and the revenues from roaming visitors.

The revenues from SMS & MMS & value added services increased 1.6% year-on-year to CZK 5.1 billion in 2008, as a result of the continuing growth in the total SMS and MMS. In 2008, O_2 customers in the Czech Republic sent and received in total 3,331 million SMS, which is a year-on-year increase of 8.1%.

The revenues from leased lines and data services fell 2.4% year-on-year in total, down to CZK 3.9 billion in 2008, which is attributed to the decline in leased lines revenues; the revenues from data services, on the other hand, increased as a result of the growth in the number of IP Connect and IP VPN connections.

The revenues from internet (fixed and mobile, including the revenues from IPTV) in 2008 increased 10.9% year-on-year in total to CZK 6.5 billion as a result of the revenue growth from fixed broadband services (ADSL, IPTV and content) and from mobile internet services. The total number of reported ADSL accesses (retail and wholesale) as at December 2008 reached 631 thousand, compared to 570 thousand the year before, up 10.6% year-on-year. The number of retail ADSL accesses went up 13.8% year-on-year and reached 579 thousand in this period, while the total number of reported O_2 TV customers reached 115 thousand as at the end of 2008.

The total number of mobile data customers (GPRS, CDMA and UMTS flat rate) increased 19.2% to 229 thousand as at 31 December 2008. Data ARPU improved by 2.8% year-on-year, and reached CZK 114 in 2008. Due to the growth in the number of mobile data customers, the non-SMS data ARPU represented 43.6% of the total data ARPU in 2008, compared to a share of 42.7% in 2007.

The revenues from IT and business solutions increased 18.4% year-on-year and amounted to CZK 2.3 billion in 2008 caused mainly by the growth in the revenues from ICT services for corporate and government customers.

The revenues from equipment and activation fees declined 0.6% year-on-year in total, down to CZK 2 billion in 2008, while other telecommunication revenues in 2008 reached CZK 2.3 billion, which is more than a fivefold increase compared to 2007; the increase was principally driven by the revenues from the Universal Service, which amounted to approximately CZK 1.2 billion in 2008.

OVERVIEW OF CONSOLIDATED OPERATING EXPENSES

The consolidated operating expenses of the Telefónica O2 Group increased 5.3% year-on-year and reached CZK 37.7 billion in 2008.

The interconnection and roaming expenses increased 8.9% year-on-year, to CZK 12.0 billion in 2008, and by 11.8% in the quarter. The increase was driven by a growth in the costs related to international transit (in line with the higher transit revenues) and costs incurred in Slovakia (due to a customer base growth). The cost of goods sold fell 6.9% year-on-year, down to CZK 3.3 billion, as a result of a more favourable cost of equipment. Other supplies, which comprise the costs of content, the customer loyalty program, sub-deliveries, other cost of sales and purchases, increased 27% in total and reached CZK 3.5 billion in 2008. The costs associated with the Universal Service, in the amount of approximately CZK 800 million, were the key driver of this growth in 2008.

Staff costs, including the headcount reduction costs, amounted to CZK 7.1 billion in 2008, which is a stagnating trend compared to 2007. The total number of Group employees reached 9,096 as at 31 December 2008, down 1.4% year-on-year. The headcount of Telefónica O2 Czech Republic was reduced 3.6% year-on-year, down to 8,383 as at the same date.

The marketing and sales expenses (marketing and commissions) declined 9.3% in total year-on-year, down to CZK 3.1 billion in 2008, while the network & IT repair and maintenance expenses decreased 10.1% year-on-year, down to CZK 2.3 billion, as a result of the progress in efficiency improvements (mainly in the area of processes). The rental, buildings and vehicle costs reached CZK 2.2 billion, up 14.3% year-on-year, mainly due to the higher rental and service costs of relocation to the new headquarters, the rental costs of DELTAX Systems (DELTAX Systems not consolidated in 2007) and the rental costs incurred in Slovakia. The utilities supplies went up 17.5% year-on-year to CZK 948 million, on the back of an increase in the price of electricity and the impact of the Slovak operation. Other external expenses (billing and collection, call centres, consultancy and professional fees and other external expenses, including royalty fees), and other operating expenses, reached CZK 2.3 billion in 2008, which is a year-on-year increase of 11.9%.

Taxes (other than income tax) and provisions for bad and doubtful debts and inventories increased 58.8% year-on-year and reached CZK 953 million. In 1Q 2008, Telefónica O2 Slovakia booked provisions for bad debts incurred in connection with the contract customer base acquired at the time of the commercial launch. Effective measures put in place in 2Q 2008 however led to an improvement in the credit management, which in turn reduced the bad debt ratios that are now consistent with industry standards.

THE OUTLOOK FOR 2009

With regard to the current challenging environment, the Group's strategy in 2009 will continue to focus closely on the customers and their needs, while staying firmly centred on its strategic goals. The cash flow generation through efficiencies in OPEX and CAPEX remains among our key priorities for 2009.

In 2009[1], we expect the Group's revenues[2] to be within the range from –3% to 0%, the OIBDA[3] to stay within –4% to 0%, and the Operating Cash Flow[4] to grow within the range from +2% to +5% on the situation of 2008. The Group also reiterates its medium term guidance for 2007–2010 communicated in October 2007.

The Company will continue with its active marketing of the mobile flat rate tariffs introduced in 2008, with a view to further improving the customer mix, and subsequently to accelerating usage and consumption (ARPU) of services. In line with the recently announced plans to expand the 3G coverage, the Company will focus on its improved proposition of new mobile broadband and data services. In the fixed line business, the Company's efforts will be aimed on the consolidation of its past year's performance. The Company believes that the continuing enhancement of ADSL and IPTV, as well as bundling, will further increase the value of the fixed line and will result in a deceleration of the fixed line losses. The Company will continue to concentrate its efforts on the area of ICT and integrated business solutions marketed primarily to corporate and government customers, as well as to small and medium-sized businesses and entrepreneurs. The consolidation of the activities in the field of ICT into one business unit of Professional Services, which already commenced in 2008, will further strengthen the Telefónica O2 Group's position in the ICT market, and maintain its revenues.

The Telefónica O2 Group will continue to support the gradual deployment of the Slovak operation, including the development of systems, processes and the network roll-out, while maximizing the leverage with the Czech operation. Telefónica O2 Slovakia will continue in the active marketing of its customer proposition based on "value and simplicity", which will lead to further growth and improvement in the quality of the customer base with a view to gaining a sizeable market share and strengthening our financial position.

1 The 2009 guidance excludes any changes in consolidation, assuming constant FX rates of 2008
2 In terms of 2009 guidance calculation, the revenues represent business revenues only.
3 In terms of 2009 guidance calculation, the OIBDA excludes brand fees and the impairment charge. For the purpose of comparison, the equivalent items registered in 2008 are also deducted from the reported figures (base reported 2008 figures exclude the CZK 86 million of impairment charge and brand fees amounting to CZK 626 million).
4 OIBDA minus CAPEX

CORPORATE SOCIAL RESPONSIBILITY

03

Stability comes from within, it is not something we get from outside. Only our own ability helps us cope with the environment. Being really successful requires balance.

CORPORATE SOCIAL RESPONSIBILITY

The principles of Corporate Social Responsibility (CSR) represent an integral part of the corporate philosophy of Telefónica O2. Also in 2008, the company was fully aware of the fact that it does not conduct its business in isolation from the outside world – on the contrary, that it is a part of the external environment. As far as possible, Telefónica O2 conducted its business with regard to the so-called Triple Bottom Line – not only that it concentrated on growing the business, but in doing so, the company cared about the environmental and societal aspects of its operations and on the impact they have on future generations. Telefónica O2 continued to respect the needs of the internal and the external environments, contributed to sustainable development, promoted transparency and generally assisted in the development of the society – within and beyond the scope of its commercial operations.

CORPORATE GOVERNANCE

Also in 2008, business ethics held a pivotal position in the corporate philosophy of Telefónica O2. The company implemented the group's policy in the field of ethical business conduct – the so-called Business Principles which help align the behaviour of all employees and the everyday activities in the company with the corporate values and principles. It is the responsibility of all employees to heed the purpose and the letter of this policy. The compliance with the Business Principles was supervised by Internal Audit. In the event of a suspected violation, employees could contact a specialist from Human Resources, Security and Legal Affairs, or use the confidential whistle blowing channel. The Ethics and Social Corporate Responsibility Committee, which acts as a supervisory body for CSR, received regular information about how the company handled suggestions and reports of suspected violation of the Business Principles.

Special information campaigns promoting the Business Principles among employees were ran during 2008. A course in Business Principles went online in March 2008. As at 31 December 2008, 52.5% of employees completed the course. The campaign to promote the Business Principles also employed the so-called O_2 Life Pilots (employees, unpaid volunteers, who helped with improving conditions in different areas and promoted corporate values as part of the O_2 Life programme). Every newly recruited employee received the Business Principles in print as part of their entry-level training; the text was also available online on the intranet and the website of Telefónica O2.

Ernst & Young Audit, s.r.o. performed an extensive Corporate Social Responsibility audit in 2008, focusing on key CSR activities and principal stakeholder groups. The auditors assessed the responsible behaviour of the company with respect to the environment, to its employees, how it provides for a good work-life balance of its people, how it uses feedback to improve, invests in the local community and helps where help is needed. The audit conclusions and recommendations were used to formulate CSR goals and action plans for the year ahead. The goals were presented to the Board of Directors and to the Ethics and Corporate Social Responsibility Committee for approval. CSR is an integral part of the Integrated Management System Policy of the company.

A year-long reputation tracking survey, RepTrack, was started in October 2008 in order to determine the effect of Telefónica O2's CSR activities. The survey was conducted in all countries where the Telefónica Group has presence.

In 2008, Telefónica O2 competed in European Corporate Social Responsibility Awards, a prestigious international competition, and qualified for the national finals.

In November 2008, Telefónica O2 became general partner of the 5th International Conference on Corporate Social Responsibility organised in the Prague Municipal House by the Donors Forum, the British Chamber of Commerce and the Netherlands-Czech Chamber of Commerce. The event was held under the auspices of the Chairman of the Senate of the Czech Parliament, Přemysl Sobotka, and Senator and Deputy Prime Minister for European Affairs, Alexandr Vondra. Among the five keynote speakers was the Chief Executive Officer of Telefónica O2, Salvador Anglada, who underscored the importance of CSR in business.

MARKET PRESENCE AND CUSTOMER EXPERIENCE

Telefónica O2 has built its good name on the quality of its products and services, and on the continuous improvement of customer experience. In respect of customers, Telefónica O2 strives for transparency, information and accommodation of the customers' needs and demands. What our customers tell us is very important – we used the feedback to plan our future activities which benefit the customer.

IMPROVING CUSTOMER EXPERIENCE

The best customer experience has always been one of the three pillars of Telefónica O2's strategy. The level of satisfaction of customers and their needs were tracked by a number of methods – global research, special tracking surveys and focus groups.

The outputs were used to formulate the key principles for the improvement of customer experience in 2008:
- a standardised approach to creating customer experience;
- active communication with the customer;
- improvement of customer experience at main points of contact.

To the end of delivering on the said goals, flagship projects were launched, which focused especially on the optimisation of key processes and services

Telefonica O2 responded to the demand by – among other things – introducing the tariffs O_2 NEON, in which it instilled its main values in the area of communication – simplicity, clarity and reliability, simple pricing and straightforward terms. Other achievements in 2008 in the area of improving customer experience included an upgrade of internet connection speeds, better customer care parameters at call centres, faster fixed service delivery and new business tariffs.

PRODUCTS AND SERVICES FOR PEOPLE WITH SPECIFIC NEEDS

In November 2008, Telefónica O2 introduced an exceptionally easy-to-operate mobile handset Emporia Life, designed specially for older people and for people with disabilities who would otherwise find it difficult to operate a standard mobile telephone. Emporia Life filled a gap in the previously unsaturated market for products and services for people with specific needs. The segment of older customers has been largely neglected by operators. Telefónica O2 offered its customer the possibility to buy a new handset economically bundled together – at half price – with credit or a promotionally priced version of the O2 Neon S tariff. Telefónica O2 donated CZK 100 from the sale of each Emporia Life in aid of Linka seniorů, a helpline for senior citizens.

Also in 2008 telefónica O2 continued to operate Hovor pro neslyšící (Deaf Call), a service which lets deaf customers really communicate in the case of emergency or in various life situations – when making a medical appointment, ordering a repairman or consulting directory services. A special call centre puts through calls from deaf people to the hearing, and vice versa. The service is available 24 hours a day and was used by 15,926 customers.

In 2008, the Czech government amended the laws governing the system of mandatory discounts to people with disabilities and low income. As a result, a state subsidy for people dependent on the care of other persons with degree I. dependency, and for low-income persons, was abolished with effect from 1 July 2008. Telefónica O2 decided to preserve the O2 discount on fixed line service for people with degree I. dependency in spite of the fact that the state subsidy was no longer available. Telefónica O2 also continued to rent special telephone sets to people with special requirements. In 2008, the company afforded discounts in the total value of CZK 116, 200 thousand.

Discounts for rehabilitated persons and members of the resistance movement were also preserved in 2008. Our fellow citizens who participated in the anti-fascist and anti-communist movements jointly claimed discounts on services in the total value of CZK 56.3 million.

Telefónica O2 successfully completed a project for barrier-free access to all brand shops. From 2008, all O2 shops – technical conditions allowing and subject to permission of local authorities – are barrier-free.

WE HELP TO PROTECT CHILDREN IN THE WORLD OF COMMUNICATION TECHNOLOGIES

As a provider of communications services, Telefónica O2 is committed to use all available means to help eliminate potential risks that come with modern technologies. Protecting children and creating a safe environment for them in the world of information and communication technologies has always been a key priority. Several specific actions were taken in the area of child protection. Telefónica O2 adopted a policy dealing with marketing to children, which summarises the principles respected in all its marketing activities. In 2008, a special website went online dealing with the protection and safety of children and offering useful advice and recommendations. Through its O_2 Foundation, Telefónica O2 supported the Stop Bullying project which incorporated a mass media outreach campaign. The company was also involved in the project Teachtoday.eu, where it joined the ranks of 14 European ICT leaders. The Teachtoday.eu web portal provides teachers with useful advice and guidance about internet and mobile technologies, including teaching plans, case studies and reporting procedures. Telefónica O2 also supported the Saferinternet project, an international conference on child protection and a Safe Internet Day. The company was also member of the advisory council established as part of the Safeinternet project and sent delegates to discussions and panels dedicated to the issues of child safety on the internet. The service *PC Strážce* is another example of the company's good practice in this area; the user can configure a parental lock and keep the child safe while online. Also O_2 TV has a feature which performs the same function. Telefónica O2 customers can also see the balance on their account for pre-paid and postpaid service any time.

CARING FOR EMPLOYEES AND THE WORKPLACE

In the area of human resources, the company has always strived for O2 to be "a place which is a pleasure to work at". In 2008, Telefónica O2 made a pledge to employees, in which it defined in clear terms what it intends to achieve and deliver in specific areas.

EMPLOYEE STRUCTURE

Number	As at 31 December 2008
Employees – total	8,383
Women	2,931
Men	5,452
Employees with a disability or reduced work capacity	83

EMPLOYEES BY DIVISION

Division – Unit	As at 31 December 2008
Business Division	1,154
Consumer Division	2,125
Operations Division	3,845
Wholesale Division	68
Public Affairs and Regulation	38
Strategy and Product Development	253
Human Resources and Support Services	452
Finance Division	370
Legal Affairs	40
Internal Audit and Risk Management	16
Branding and Customer Experience	19
Office of the Chief Executive Officer	3
Total	8,383

SPIRIT OF O_2

As every year, also in 2008 Telefónica O2 recognised the best employees at its annual Spirit of O_2 awards. Employees could either nominate themselves or their colleagues whose accomplishments distinguished them from the rest and who helped keep Telefónica O2 at the forefront of the telecommunications market. Winners were chosen by a special jury comprising of top executives of the company.

REFLECT

In 2008, 89% of all employees participated in the Reflect employee satisfaction survey in Telefónica O2, which is 6 percentage points more than the year before. The biggest improvement was seen in the category My Manager, which confirmed that the actions planned and implemented based on the results of the previous cycle of the survey were effective.

EMPLOYEE BENEFITS

Telefónica O2 continued to afford a wide range of employee benefits to its employees, which included financial products and services, O2 products, work-life balance promoting products and pre-school care. Employees with reduced work capacity also received a voucher in the value of CZK 10 thousand, which they could redeem against a physiotherapeutic package. In 2008, 69 employees with reduced work capacity received the voucher. The employee benefits menu is updated every year with regard to the demand. Retail partners in the Good Shopping programme offered discounts on services (e.g. restorative spa treatments, healthcare, etc.). The programme included specially-priced offerings from more than 50 partners in 2008.

STOP SMOKING CAMPAIGN

In 2008, Telefónica O2 helped employees stop smoking by means of a campaign titled We Will Help You Stop. Employees could claim one treatment cycle of Niquitin pastilles that help treat smoking addiction. Additional doses of Niquitin were handed out at Health Days which were held in Prague and in the regions. Almost two thousand employees claimed the pastilles. Employees could also have their lungs tested for CO_2 levels and consult with qualified experts on various issues, e.g. stopping smoking, the risks of continuing the habit etc.

CARING FOR THE HEALTH OF EMPLOYEES

In spring 2008, Telefónica O2 commenced a pilot project focused on employee health, called Health Days for Employees. Health Days were gradually organised in the towns of Brno, Ostrava, Prague, Kolín, České Budějovice and Ústí nad Labem. At these events, employees could use the health-oriented services available there. More than 1,500 employees used this opportunity right at the event, and many more used the special offers from our partners in the area of health and nutrition. Employees also collected presents from our partners – vitamin C, soy drink, muesli biscuits, healthy coffee, etc.

HEALTHY COMPANY

In October 2008, Telefónica O2 became again (as the only Czech telecommunications company) the proud holder of the prestigious Healthy Company award which is presented every year by the Czech Ministry of Health. Telefónica O2 received this acclaim once before in 2005; in 2008 it underwent an audit which confirmed the award. A jury of experts assessed the standard of occupational health and safety and compliance with the relevant laws of the Czech Republic.

EMPLOYER OF CHOICE

In June 2008, Telefónica O2 won the award Employer of the Year in Prague at the Employer of the Year 2008 awards presented by Jobpilot.cz. The Czech public voted Telefónica O2 as the preferred employer already for the second time running.

FAMILY-FRIENDLY COMPANY

Telefónica O2 also won the Family-friendly Company award given by the project Shared Jobs as an Instrument of Active Employment Policy.

CARING FOR THE ENVIRONMENT

The commitment of Telefónica O2 to keep the footprint of its operations on the environment is promulgated in the company's Environmental Policy. It focuses on the elimination, or at least the mitigation, of damage to or degradation of the environment – in its whole or in part; In doing so, the company uses the latest research. Telefónica O2's fundamental principles of environmental protection were coordinated across the Telefónica Group and helped to deliver on both the group and local objectives and meet the statutory and other conditions.

Telefónica O2 continually worked with its suppliers, gradually raising the bar they have to meet, in order to promote the ideas of environmental protection in its external environment. The company itself was on the vanguard – its Green Company programme involved employees in protecting the environment – economical usage of energy is only one example of how they helped to protect the environment.

The trend of reducing negative impacts on the environment continued also in 2008. In the course of its operations, Telefónica O2 in 2008 used 3.6% less natural gas compared to 2007, and the water consumption also fell by 3.2%. Compared to 2007, the volume of polluting emissions released into the air from heat or power generation and from vehicles declined; the fuel consumed for power generation in back-up power units fell 9.3% on the year before, the number of kilometres driven in company cars fell 19.2%, diesel and petrol consumption fell 7.0% and 45.3%, respectively.

The volume of waste generated was also successfully reduced by 32.15% year on year. Hazardous waste alone was reduced by 94.2%, other categories of waste by 16.9%. Another positive trend was seen in the collection of used mobile handsets whose number has risen 129.7%.

Telefónica O2 invested a lot of effort in the social area where it actively tried to implement principles of pro-active environmental protection. The most important activities included the project Let Your Old Mobile Help which benefited Linka bezpečí. The company also was one of the main partners and donated prizes for the 15th year of the recycling competition Nestlé and České sběrné suroviny Grand Prize which was organised under the auspices of the Czech Ministry of Environment. Elementary schools and kindergartens from the whole country participated in the recycling challenge. The company's positive attitude to the environment manifested itself also at Christmas time – electronic Christmas cards were given preference over printed cards and gift bags and boxes were made from recyclable material.

The activities of Telefónica O2 in the area of environmental protection were regularly audited, including those of suppliers. The standard of environmental protection is certified according to ISO 14001 international standard. Telefónica O2 is the only telecommunications operator in the Czech Republic to have this certificate.

CIVIL SOCIETY

In 2008, supporting civil society projects and philanthropy were deeply rooted in the company's CSR. Telefónica O2 strived to put its technology to use in helping to improve the quality of life. Already for the seventh year running, O_2 Foundation was the key instrument in transparent and systemic corporate donorship.

In 2008, Telefónica O2 won several prestigious awards; the most important was Via Bona which recognised the company's activities in fighting bullying in Czech schools. Telefónica O2 was also featured in TOP Corporate Philanthropist organised by the Donors Forum. The concept is based on an international model and allows for international comparison. In 2008, Telefónica O2 made cut of TOP Ten most generous corporate donors in the Czech Republic, and in the qualitative category TOP 10 Corporate Philanthropist it ranked 8th – as measured by the total invested funds. Philanthropic activities are measured using the LBG (London Benchmarking Group) Standard Responsible Company, which is a comprehensive and standardised system for the assessment of corporate philanthropy.

The total of funds, gifts and telecommunications services donated by Telefónica O2 in 2008 in aid of public benefit projects exceeded CZK 30 million.

LINKA BEZPEČÍ 116 111

In 2008, O_2 Foundation was general partner of the only national toll-free and confidential helpline for children who find themselves in difficult life situations. O_2 Foundation was involved in 2008 in the renumbering to the pan-European number 116 111. As a result, the Czech Republic joined the ranks of the first European Union member states which implemented the single number.

LINKA SENIORŮ

O_2 Foundation also became partner of Linka seniorů operated by Elpida Plus, a civil society organisation, in 2008. Senior citizens could dial the number 800 200 007 and share their concerns and joys, consult on various issues – health, legislation, psychology and welfare. The helpline answered almost 9,500 calls in 2008. Financial assistance from the O_2 Foundation helped to keep the service free of charge.

STOP BULLYING

O_2 Foundation ran an extensive anti-bullying campaign in the media in 2008. All elementary schools in the Czech Republic received information content including advice for pupils, parents and teachers. At the same time, O_2 Foundation brought online a new web portal, www.minimalizacesikany.cz, where teachers, parents and pupils found comprehensive information about this issue, as well as advice and assistance. The portal also features an online counselling service where experienced experts answer questions about relationships in the classroom.

In 2008, O_2 Foundation and Stop Bullying won the Zlatá Effie 2008 award (for the most effective socially-oriented campaign), and the Duhová kulička award presented at the International Competitive Review of Advertising to Children.

VOLUNTEERING PROGRAMMES FOR EMPLOYEES

The activities of the O_2 Foundation are based on voluntary work of employees of Telefónica O2. Departments and teams could spend a day helping a selected non-profit organisation from the many that enjoy support from the O_2 Foundation. In 2008, a total of 263 employees invested more than 5018 hours of work.

O_2 Foundation also recognised the efforts of those employees who committed their free time to active volunteering. In 2008, 18 active volunteers from the ranks of employees earned CZK 460 thousand for the benefit of the civil society organisations they had been helping.

Fundraising campaigns organised by the O_2 Foundation created many opportunities during the year for employees to make a donation to people in need or in aid of Sdružení Linka bezpečí. The amount raised through individual donations from 499 employees in 2008 amounted to more than CZK 300 thousand.

Easter and Christmas markets, which the foundation organised in ten O2 buildings in various parts of the Czech Republic, were an opportunity for sheltered workshops to sell their products made by people with disabilities. The sales at these markets in 2008 fetched CZK 500 thousand for fifty five sheltered workshops

The partnership between the O_2 Foundation and Elpida Plus made it possible for six employees to donate their time to senior citizens through teaching at a web skills course Školička internetu. Together they gave 54 hours of instruction in how to operate a mobile telephone.

Voluntary work of employees in 2008 went even beyond the borders of the Czech Republic. The year 2008 was the first year when Telefónica O2 employees participated in the volunteering programme Proniño, which the Telefónica Group's traditional programme of helping children in Latin America. The programme aims to give education to children who are underprivileged, who often have to work and stand little chance of getting an education. Twenty four volunteers from all countries where Telefónica has presence went in 2008 to Ecuador. Their mission was to find suitable after-school activities for children who would otherwise be left to their own devices out on the street, or who would have to work – often as young as seven years old.

In April 2008, Telefónica O2 kicked off Give Blood with O2, a project to promote unpaid blood donorship in the Czech Republic which has seen the numbers of voluntary donors dwindling in the past few years. Over than 300 employees participated and more than 130 litres of this life-saving liquid were collected.

Telefónica O2 was recognised for the involvement of its employees in volunteering initiatives by the Křesadlo award, which is presented by Hestia Centre for Voluntary Work under the patronage of the Lord Mayor of Prague.

PROMOTING FAIR TRADE

In 2008, Telefónica O2 started Be Fair with O2, a project whose aim is to promote Fair Trade products. The biggest accomplishment of 2008 in this area was that Fair Trade products were included in the catalogue of gifts for business partners. Employees ordered 5,500 Fair Trade gifts in the total value of CZK 3 million. Among the gifts, there were also mugs made in sheltered workshops. Employees could also buy specially-priced Fair Trade products through the e-shop, and order Fair Trade and ethnic catering for various corporate events.

CORPORATE GOVERNANCE

04

The best about cooperation is that the others are on your side. A team is strong if it is diverse, not homogeneous. You will get the best out of others if you get the best out of yourself. One man may be a key player but does not make the team. Individual effort to achieve a common goal – that makes for team spirit.

CORPORATE GOVERNANCE

CORPORATE GOVERNANCE OF THE TELEFÓNICA O2 CZECH REPUBLIC GROUP

In 2008, Telefónica O2 continued in the development and improvement of the quality of the previously implemented corporate governance model, with regard to the needs of the Company and the Telefónica O2 Czech Republic Group. The possibility of sharing and having the resources of the experience with the implementation of new procedures and best practice in the Telefónica Group – both within its European division and the parent Telefónica, S.A. – proved to be particularly useful.

Telefónica O2's ownership rights in its subsidiary companies, save for those incorporated in foreign jurisdictions, are exercised by the Board of Directors of Telefónica O2 Czech Republic acting in the capacity of the sole member. Persons with power of attorney given by the Board of Directors of the parent company exercise the ownership rights in foreign subsidiaries within the limits of the mandate approved by the Company's Board of Directors. Personnel changes in the subsidiary companies' statutory and supervisory bodies (in positions occupied by the Company's representatives) are approved by the Board of Directors of the Company and, in accordance with the Articles of Association, are also subject to prior approval by the Supervisory Board of the Company, whose decisions are made in consideration of its Nomination and Remuneration Committee.

In terms of organisation, Telefónica O2 is a part of Telefónica's European division (whose name was changed from Telefónica O2 Europe plc to Telefónica Europe plc in 2008), which holds all companies that use the O_2 commercial brand. No significant changes occurred in the ownership structure of the Company; Telefónica, S.A., holding a 69.41% stake, remains the majority owner.

SUBSIDIARIES AND ASSOCIATED COMPANIES

(as at 15 March 2008)

No principal changes occurred in the Company's structure and in the number of members of the Telefónica O2 Czech Republic Group with respect to the situation described in the 2007 Annual Report of Telefónica O2. The partial changes and motions which were initiated in the period in question are set out below.

During 2008, principal legal steps were taken to wind-up SPT TELECOM (Czech Republic) Finance B.V. with liquidation. The Board of Directors of Telefónica O2, its sole member, decided to wind-up the company in mid-2007, due to the redundancy of this dormant undertaking for the future plans of the parent company. The process of liquidation of SPT TELECOM (Czech Republic) Finance B.V. was completed in mid-February 2009.

In December 2008, the subsidiary Telefónica O2 Services, spol. s r.o., was renamed (by way of a change of the corporate name) to Telefónica O2 Business Solutions, spol. s r.o., which was a step in the already commenced project for the integration of commercial operations in the field of ICT. ICT services were previously provided by DELTAX Systems a.s. and Telefónica O2 Services, spol. s r.o. The reason for the incorporation of the new entity was to create a converged ICT provider capable of offering a comprehensive spectrum of services, while capitalising on the strengths of the parent company.

Subsidiaries and associated companies in which Telefónica O2 has direct ownership of more than 10% of the registered capital are listed in the following table.

SUBSIDIARY AND ASSOCIATED COMPANIES

(as at 15 March 2009)

Corporate name	Registered capital	Share of Telefónica O2 Czech Republic, a.s.
Telefónica O2 Slovakia, s.r.o.	SKK 1,500,000,000 (EUR 49,790,878.31)	100%
Telefónica O2 Business Solutions, spol. s r.o.	CZK 10,000,000	100%
DELTAX Systems a.s. *	CZK 3,006,000	100%
CZECH TELECOM Austria GmbH	EUR 35,000	100%
CZECH TELECOM Germany GmbH	EUR 25,000	100%
První certifikační autorita, a.s.	CZK 20,000,000	23.25%
AUGUSTUS spol. s r.o.**	CZK 166,000	39.76%

* The Board of Directors of DELTAX Systems a.s. decided in December 2008 to wind up the companies controlled by this company with liquidation, on the grounds of their redundancy within the new business model of the integrated entity Telefónica O2 Business Solutions, spol. s r.o. (see above). The process is scheduled for completion in 2009.

** Telefónica O2 Czech Republic, a.s. does not control this company.

ORGANISATION CHART OF TELEFÓNICA O2 CZECH REPUBLIC

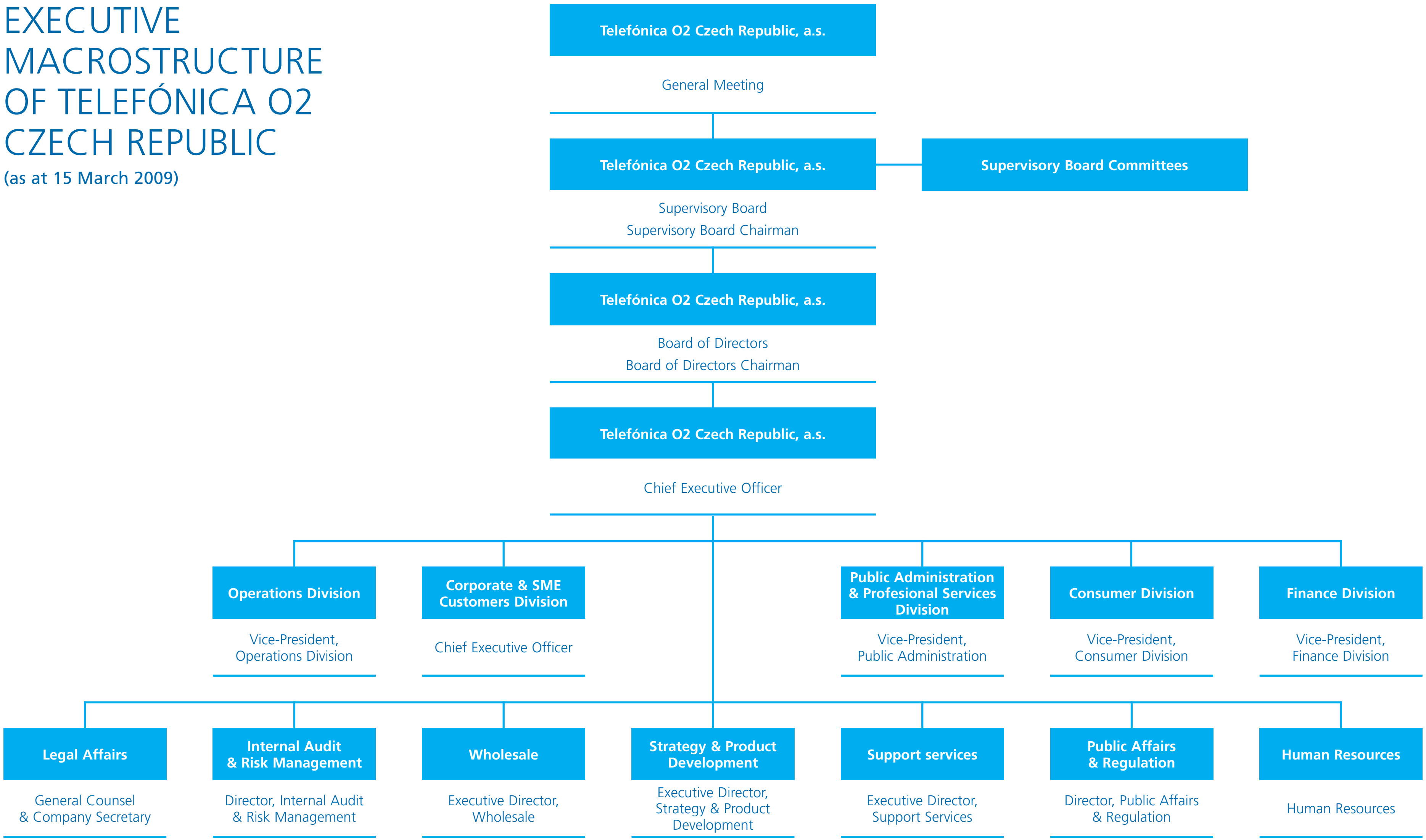
In the past period, the optimisation of the organisational and governance architecture of the Company continued, in order to make the Company function more efficiently and give it a better position – so that it is better able to meet the customer needs and exploit new growth opportunities.

The following changes from the organisation structure as shown in the 2007 Annual Report and the 2008 Half-year Report were effected:

- with effect from 1 January 2009, the Human Resources and Support Services unit was divided into an independent Human Resources unit and a Support Services unit, subordinated directly to the line of the Chief Executive Officer;
- the Branding and Customer Experience unit was transferred to the Consumer Division at the beginning of January 2009; new competences were added to this unit – consumer marketing communication, customer and business processes and market research;
- with effect from 1 February 2009, the Business Division split into two independent organisation units in the reporting line of the Chief Executive Officer: Corporate and SME Division, and Government and Professional Services unit.

EXECUTIVE MACROSTRUCTURE OF TELEFÓNICA O2 CZECH REPUBLIC

(as at 15 March 2009)



GOVERNING BODIES OF TELEFÓNICA O2 CZECH REPUBLIC

(as at 15 March 2009)

GENERAL MEETING

General Meeting, which comprises the Company's shareholders, decides on fundamental business, organisational and operating matters. Its authority and powers are determined by the Commercial Code and the Articles of Association. As a rule, the Board of Directors convenes the General Meeting once a year. Basic information on the General Meeting and its status and authority can be found in Articles 7–13 of the Company's Articles of Association.

SUPERVISORY BOARD

The Supervisory Board has fifteen members and supervises the discharge of the Board of Directors' powers and the running of the Company's business. Its composition, authority and powers are determined by the Commercial Code and the Articles of Association. As a rule, the Supervisory Board meets once in a quarter, but at least four times in the course of a calendar year. Two thirds of the Supervisory Board members are elected and recalled by the General Meeting, one third of the Supervisory Board members are elected and recalled by employees of the Company. Members of the Supervisory Board are elected for tenure of five years. Basic information about the Supervisory Board and its authority can be found in Articles 20–25 of the Company's Articles of Association.

BOARD OF DIRECTORS

The seven-member Board of Directors is a statutory body which manages the business of the Company and acts on its behalf. The Board of Directors decides on all corporate affairs which, by law or the Articles of Association, are not reserved for the General Meeting or the Supervisory Board. As a rule, the Board of Directors meets once every calendar month, but at least twelve times in the course of a calendar year. Members of the Board of Directors are elected and recalled by the Supervisory Board. The tenure of a member of the Board of Directors is five years. Basic information on the Board of Directors and its authority can be found in Articles 14–19 of the Company's Articles of Association.

COMMITTEES OF THE SUPERVISORY BOARD

Under its powers, the Supervisory Board sets up committees as its advisory and initiative bodies. Committees of the Supervisory Board are an inherent part of corporate governance. These always include an Audit and Control Committee and a Nomination and Remuneration Committee. Members of committees are elected and recalled by the Supervisory Board. The tenure of a member of a committee is two and a half years. Committees established by the Supervisory Board can comprise only members of the Supervisory Board. The scope of authority of the Supervisory Board's committees is set out in Article 26 of the Company's Articles of Association.

Company has the following committees of the Supervisory Board:
Audit and Control Committee;
Nomination and Remuneration Committee;
Ethics and Corporate Social Responsibility Committee.

BOARD OF DIRECTORS OF TELEFÓNICA O2 CZECH REPUBLIC

(as at 15 March 2009)

SALVADOR ANGLADA GONZALEZ (*1965)

CHAIRMAN

Salvador is the Chief Executive of Telefónica O2 Czech Republic, the biggest integrated operator in the Czech Republic. He was appointed CEO in June 2007 and Chairman of the Board in February 2008 and at the same time became a member of the Telefónica Europe Board as an Executive Director. Telefónica O2 Slovakia is also a part of Telefónica O2 Czech Republic. They started to operate in 2007 after gaining the third mobile license in the country in 2006. Salvador joined Telefónica group in Spain in 2002 as a Sales and Marketing Director of Telefónica Empresas, the corporate Telco and IT services subsidiary. He moved to the Czech Republic in 2005 when Telefónica acquired ČESKÝ TELECOM (the legal predecessor of Telefónica O2 Czech Republic). Salvador was fully involved in successful transformation of the Czech Telefónica business, firstly as the CEO of Eurotel, the Czech mobile subsidiary and then led the Consumer Division of the newly merged and re-branded Telefónica O2 Czech Republic. Before joining Telefónica, he held a number of executive positions in Dell Computer and Dow Jones Markets. Salvador Anglada graduated in Industrial Engineering in Madrid. He holds an MBA from Instituto de Empresa and PDG from IESE Madrid.

JURAJ ŠEDIVÝ (*1962)

1ST VICE-CHAIRMAN

Juraj graduated from the College of Mechanical Engineering in Nitra in 1984 and Comenius University in Bratislava in 1990. He worked as assistant professor and research associate in the area of vehicle mechanics until 1991. He received his MBA degree from the Rochester Institute of Technology, New York, in 1992, and joined Johnson & Johnson Consumer Products, Inc. in New Jersey where he worked as a financial analyst, then as Controller of Professional Products, Czech and Slovak Republic Division, in Prague. He gained his first experience in the telecommunications sector as the Finance Director of Globtel, a mobile subsidiary of France Telecom in the Slovak Republic (now Orange), in 1996 and 1997. In

SALVADOR ANGLADA GONZALEZ

late 1997, he joined ČESKÝ TELECOM (the legal predecessor of Telefónica O2 Czech Republic), as Executive Director of Planning and Controlling, and in 2001 became Chief Financial Officer. Since 2003 he has been the 1st Vice-Chairman of the Board of Directors of Telefónica O2 Czech Republic. In October 2006 he was appointed Chief Executive Officer of Telefónica O2 Slovakia. From 2001 to 2007 he was a member of The Supervisory Board of US Business School Prague and since 2006 he has been a member of The Academic Council of Faculty of Economics and Public Administration, High School of Economics, Prague.

JURAJ ŠEDIVÝ PETR SLOVÁČEK JAKUB CHYTIL

PETR SLOVÁČEK (*1959)

2ND VICE-CHAIRMAN

Graduated from the Technical University, Prague, with a degree in telecommunications from the Faculty of Electro-technical Engineering. Also holds a postgraduate Master of Business Telecommunications (MBT) degree from the Technical University of Delft in the Netherlands. After graduation he joined the Telecommunications Research Institution, Prague, he joined SPT TELECOM (the legal predecessor of Telefónica O2 Czech Republic) in 1989, working in switching, technical development, network management projects and OSS. In June 2008 he was re-elected 2nd Vice-Chairman of the Board of Directors of Telefónica O2 Czech Republic. He currently holds the position of Vice-President, Operations Division.

JAKUB CHYTIL (*1961)

MEMBER

Graduated from the Faculty of Law, Charles University, Prague, where he got his JUDr. degree. In 1991 – 1995, he was a junior associate and, later on, an attorney specialising in commercial and civil law, working with international law firms. In 1995 – 2000, he was a Legal Counsel for the Czech and Slovak Republic at Philip Morris ČR and Kraft Foods. In 2000–2003, he was the Senior Counsel of Philip Morris International, Lausanne, Switzerland, where he was responsible for the legal affairs of Philip Morris International's subsidiaries in various countries. Since December 2003 he has been in the position of General Counsel at ČESKÝ TELECOM (the legal predecessor of Telefónica O2 Czech Republic) and since May 2006 he has also been in the position of the Company Secretary. He is a member of the Board of Trustees of O_2 Foundation (Nadace O_2).

JESÚS PÉREZ DE URIGUEN (*1970)

MEMBER

Graduated in Business Administration at University of Maryland at College Park in 1992, expertise in Finance and Accounting, where he got his degree of Bachelor of Science in Business and Management. In 1993, he earned his MBA degree at Instituto de Empresa in Madrid. Before joining Telefónica O2 Czech Republic, a.s.

JESÚS PÉREZ DE URIGUEN JOSE SEVERINO PERDOMO LORENZO MARTIN BEK

he worked in Bank of America, Arthur Andersen, Jazz Telecom, S.A., and Telefónica Móviles, S.A. Jesús collected extensive experience in the telecommunications and finance area at these companies – he was responsible for planning, management control, etc. Lastly, he worked in the position of CFO in Telefónica Centroamérica for nearly four years. He was member Board of Directors of the operations of Telefónica Móviles in Panamá, El Salvador, Nicaragua and Guatemala. Now he holds an appointment of Vice President, Finance Division, in Telefónica O2 Czech Republic.

JOSE SEVERINO PERDOMO LORENZO (*1971)

MEMBER

José joined Telefónica in Spain in 2006, holding responsibilities in the areas of Business Intelligence and Commercial Development, until September 2008, when he moved to the Czech operation. Previously, he gained his expertise in McKinsey and Co, where, over 6 years he focused in the areas of Telecommunications and Marketing. José initiated his professional career in 1996 as an engineer in Sener (Madrid) and The Boeing Company (Los Angeles).

MARTIN BEK (*1969)

MEMBER

Studied foreign trade at University of Economics, Prague, and completed his studies at the European Business School, Paris, where he majored in Finance. He worked for ABC International, DRT International and later at Guérard Viala Prague as senior consultant and tax advisor. From 1996, he worked at ČESKÝ TELECOM (the legal predecessor of Telefónica O2 Czech Republic) as Director for Tax and Accounting, later as Executive Director for Planning and Controlling. In April 2004 he was appointed Statutory Representative of Eurotel Praha, spol. s r.o. (the legal predecessor of Telefónica O2 Czech Republic) and since September 2004 he has been Eurotel’s Chief Operating Officer. Now he holds the position Executive Director Support Services in Telefónica O2 Czech Republic. He is a member of the Board of Trustees of O2 Foundation (Nadace O2).

PERSONNEL COMPOSITION OF THE BOARD OF DIRECTORS OF TELEFÓNICA O2 CZECH REPUBLIC, A.S., AS AT 15 MARCH 2009

Name	Function	Member since
Salvador Anglada Gonzalez	Chairman of the Board of Directors	23 June 2005
Juraj Šedivý	First Vice-Chairman of the Board of Directors	14 June 2008
Petr Slováček	Second Vice-Chairman of the Board of Directors	14 June 2008
Jesús Pérez de Uriguen	Member of the Board of Directors	1 May 2008
Jose Severino Perdomo Lorenzo	Member of the Board of Directors	24 February 2009
Martin Bek	Member of the Board of Directors	27 April 2006
Jakub Chytil	Member of the Board of Directors	27 April 2006

Information about the term of office of Board of Directors members is given on page 59.

All changes in the personnel composition in the Board of Directors in 2008 were described in the 2007 Annual Report and in the 2008 Half-year Report. No changes occurred in the personnel composition of the Board of Directors in the second half of 2008.

THE FOLLOWING CHANGES OCCURRED IN THE PERSONNEL COMPOSITION OF THE BOARD OF DIRECTORS IN THE PERIOD FROM 1 JANUARY–15 MARCH 2009:

José Fernando Astiaso Laín	his office of a member of the Board of Directors was terminated upon the discussion of his resignation in the Supervisory Board on 24 February 2009,
Jose Severino Perdomo Lorenzo	elected member of the board of Directors by the Supervisory Board of 24 February 2009.

EXECUTIVE MANAGEMENT OF TELEFÓNICA O2 CZECH REPUBLIC

(as at 15 March 2009)

SALVADOR ANGLADA GONZALEZ (*1965)

CHIEF EXECUTIVE OFFICER

(resumé in section Board of Directors of Telefónica O2 Czech Republic)

JESÚS PÉREZ DE URIGUEN (*1970)

VICE-PRESIDENT, FINANCE DIVISION

(resumé in section Board of Directors of Telefónica O2 Czech Republic)

PETR SLOVÁČEK (*1959)

VICE-PRESIDENT, OPERATIONS DIVISION

(resumé in section Board of Directors of Telefónica O2 Czech Republic)

JAKUB CHYTIL (*1961)

EXECUTIVE DIRECTOR, GENERAL COUNSEL AND COMPANY SECRETARY

(resumé in section Board of Directors of Telefónica O2 Czech Republic)

MARTIN BEK (*1969)

EXECUTIVE DIRECTOR, SUPPORT SERVICES

(resumé in section Board of Directors of Telefónica O2 Czech Republic)

JOSE SEVERINO PERDOMO LORENZO (*1971)

VICE-PRESIDENT, CONSUMER DIVISION

(resumé in section Board of Directors of Telefónica O2 Czech Republic)

DAVID ŠITA (*1969)

VICE-PRESIDENT, PUBLIC ADMINISTRATION

He graduated from the University of Economy in Prague, also holds MBA at the US Business School accredited by the Rochester Institute of Technology, New York. Previously he worked in the banking and financial sectors, at GE Capital Bank and he also managed a small brokerage firm. He joined ČESKÝ TELECOM (the legal predecessor of Telefónica O2 Czech Republic, a.s.) in 2000 as a manager and later director in finance departments. In 2003 he left finance for the field of Regulation and Regulated Wholesale services as Executive Director. He continued in this role after the acquisition by the Telefónica O2 Czech Republic. In January 2008 he was appointed as Executive Director, Public Affairs and Regulation. Effective from February 1st 2009 he became Vice-president of Public Administration and Professional Services Organisation Unit. He is a Chairman of the Board of Trustees of O_2 Foundation (Nadace O_2).

JIŘÍ ŠUCHMAN (*1964)

DIRECTOR, PUBLIC AFFAIRS AND REGULATION

Graduated in Foreign Trade at the School of Economics, Prague. After gaining experience in foreign trade companies, he began to work in the telecommunications sector in 1992 and he has worked in telecommunications since; first in various management positions in SPT Telecom, France Télécom, Aliatel and T-Mobile, where he worked in 1999-2008 and was responsible for regulation and public relations. He joined Telefónica O2 Czech Republic in 2008 as Director for Public Relations. On 1 February 2009 he was appointed Director, Public Affairs and Regulation. He is on the Board of Trustees of the O_2 Foundation (Nadace O_2).

FRANTIŠEK SCHNEIDER (*1967)

VICE-PRESIDENT, CORPORATE & SME DIVISION

He joined Telefónica O2 Czech Republic, a.s., in April 2008, first as Executive Director, Corporate Sales, and later was appointed Vice-President, Corporate & SME Division. He graduated in Artificial Intelligence at the University of West Bohemia, Pilsen, and went on to start his professional career in Vikomt CZ. From 1997 he worked in Dell Computer, where started as Director for Sales to Small and Medium Enterprises, Czech and Slovak markets. In 2001 he became Business Development Manager for Eastern Europe, Middle East and Africa, where he managed development projects aimed at effective capture of the corporate market. This job took him also to Israel, Turkey, Saudi Arabia, United Arab Emirates and Russia. From May 2004 he was Managing Director of the Czech and Slovak division.

STANISLAV KŮRA (*1968)

EXECUTIVE DIRECTOR, STRATEGY AND PRODUCT DEVELOPMENT

Graduated from the Brno Technical University, School of Civil Engineering, studied project management at the Cranfield Institute of Technology, UK, and went on to earn his MBA

DAVID ŠITA JIŘÍ ŠUCHMAN FRANTIŠEK SCHNEIDER STANISLAV KŮRA PAVEL JIROUŠEK

at the London Business School. He worked in managerial positions at UNISYS in London and in Prague, at Idom, a Deloitte & Touche subsidiary, and as a junior partner responsible for telecommunications in McKinsey & Company in Prague and in Silicon Valley, California. He has 15 years of experience in the fields of telecommunications and IT. He joined Eurotel Praha, spol. s r.o. (the legal predecessor of Telefónica O2 Czech Republic) in April 2005 as Director for Broadband Services with overall responsibility for implementation of the UMTS network and services, and in October 2005 he was appointed Eurotel's Chief Strategy and Product Development Officer and Statutory Representative. After the integration of ČESKÝ TELECOM and Eurotel and inception of Telefónica O2 Czech Republic his responsibility has extended beyond strategy and product development to include operation of information and advertising-based services.

PAVEL JIROUŠEK (*1963)

EXECUTIVE DIRECTOR, WHOLESALE

Graduated from the Department of Computer Systems and Technical Cybernetics at the University of Western Bohemia in Pilsen and continued his research in the field of the Systems Control at the Academy of Science (Ph.D. programme). In 2000 he completed his MBA program at the University of Pittsburgh. From 1992 to 1995, he worked as Director for Marketing and Product Management in Eurotel and later at the same position in SPT TELECOM – NEXTEL. He joined ČESKÝ TELECOM (the legal predecessor of Telefónica O2 Czech Republic) in 1997 and after its transformation into Telefónica O2 Czech Republic, he is the new company's Executive Director for Wholesale.

CLARE RONALD CLARKE

EXECUTIVE DIRECTOR, HUMAN RESOURCES – ACTING

MAREK HAKALA

DIRECTOR, INTERNAL AUDIT & RISK MANAGEMENT – ACTING

REPORT BY THE SUPERVISORY BOARD

In keeping with the Company's Articles of Association, the Supervisory Board of Telefónica O2 Czech Republic in 2008 supervised the discharge of the Board of Directors' powers and the running of the Company's business. Supervisory Board members have the power to inspect all documents and records concerning the Company's activities; check whether the accounting records are kept to reflect the reality; determine whether the business of Telefónica O2 Czech Republic is done in compliance with the law, Articles of Association and instructions of the General Meeting.

The Supervisory Board continuously monitored the activities of Telefónica O2 Czech Republic and key decisions made by the Board of Directors and the management. Further, the Supervisory Board dealt with the suggestions raised by its committees and its members individually. The Board of Directors and the management provided the Supervisory Board with the documentation and information necessary for the discharge of its functions in accordance with the legislation and the Articles of Association.

At its meeting of 24 February 2009, the Supervisory Board examined the audited annual financial statements for 2008 (unconsolidated and consolidated) prepared under the International Financial Reporting Standards, and recommended them to the Ordinary General Meeting for approval.

In Prague on 24 February 2009

Jaime Smith Basterra
Chairman of the Supervisory Board

SUPERVISORY BOARD OF TELEFÓNICA O2 CZECH REPUBLIC

(as at 15 March 2009)

JAIME SMITH BASTERRA (*1965)

CHAIRMAN

Graduated in Economics and Business Administration (BA, Universidad Comercial Deusto, Spain) and holds an MA in Finance and Investments (Exeter University, UK). Before joining Telefónica, he worked in the financial sector for a Spanish brokerage firm, and for Banesto (BSCH Group) as Director for Global Equities in its fund management division. He joined the Telefónica Group in 1999 as Director for Financial Planning at Telefónica Internacional, and was promoted to Chief Financial Officer in December of the same year. In October 2000, he was appointed Controller of the Telefónica Group. From December 2002, he held the position of Chief Financial Officer of Telefónica de España. In June 2005, he was made Chief Executive Office and Chairman of the Board of Directors of ČESKÝ TELECOM (now Telefónica O2 Czech Republic). In June 2007, he was promoted to Chief Executive Officer of Telefónica O2 Germany GmbH. He also serves as member of the Board of Directors of Telefónica Europe plc, and Chairman of the Supervisory Board of Telefónica O2 Czech Republic.

ALFONSO ALONSO DURÁN (*1957)

1ST VICE-CHAIRMAN

Holds a BA degree in Economics from the Universidad Autónoma Madrid, and an MBA from IESE Business School Barcelona. He started his professional career in 1974 with Banco de Bilbao as manager/controller. He joined Telefónica as economist and worked in several departments: internal audit, accounts, infrastructure, international communications, financial controlling and cost management in the Spanish fixed business unit. In 1999 he left Telefónica de España for Telefónica, S.A., as Deputy Director for Planning and Management Control. In 2003, he became General Manager for Strategy, Budget and Control. In 2008 took the position of Director of Operations in the corporation and became in the same year Director of Transformation in charge of Purchases, Technology, Information systems and

JAIME SMITH BASTERRA | ALFONSO ALONSO DURÁN | LUBOMÍR VINDUŠKA | ANTONIO BOTAS BAÑUELOS | ANSELMO ENRIQUEZ LINARES

Strategy and Innovation to Transform in the scope of the operative integration of the business units of Telefónica.

LUBOMÍR VINDUŠKA (*1956)

2ND VICE-CHAIRMAN

Graduated in radio and communication from the Secondary School of Electrical Engineering. In 1974–1979 he worked as a TV repairman and later as an electrical technician at Okresní kovopodnik Praha-východ (Prague-East Regional Metal Works), then at TESLA Strašnice and Czechoslovak Radio. He has been with Telefónica O2 Czech Republic and its legal predecessors since 1979. He worked as an energy operations foreman, head of energy operations and head of territorial transport and mechanisation, Prague. At present he holds the position of Transport and Mechanisation Specialist. He is Deputy Chairman for Telecommunications of the Post, Telecommunications and Newspaper Services Employees Trade Union Deputy Chairman of the Trade Union Steering Committee at Telefónica O2 Czech Republic, and Chairman of the Prague Trade Union Steering Committee.

ANTONIO BOTAS BAÑUELOS (*1963)

MEMBER

He earned his Bachelor degree at Universidad Complutense in law and a Master degree in Economics and Business Administration (MBA) at IESE in Barcelona. He has twenty years of experience in management, operative and strategic marketing and co-ordination of large multinational teams, and he has worked in international markets, namely those in the Americas and Europe. He worked as Marketing Manager in Royal Insurance, which he joined after leaving Johnson & Johnson. He joined the Telefónica Group in 1995 and he worked for Telefónica Publicidad e Información, Doubleclick Iberoamérica, Terra and Terra Lycos in positions ranging from Chief Sales and Marketing Officer to Executive Vice-President for New Business. From 2005 until August 2007 he worked as Chief Transformation and Convergence Officer in Telefónica O2 Czech Republic. Since September 2007 he holds the position of Managing Director Product Development & Brand Management at Telefónica O2 Germany GmbH & Co. OHG. He is member of the Supervisory Board of Telefónica O2 Czech Republic since April 2008.

GUILLERMO JOSÉ FERNÁNDEZ VIDAL LUIS LADA DÍAZ DUŠAN STAREČEK MARIA PILAR LÓPEZ ÁLVAREZ ÁNGEL VILÁ BOIX

ANSELMO ENRIQUEZ LINARES (*1965)

MEMBER

Simon Linares having joined from Diageo where he was HR Director for the leading premium drinks company's Africa region, took up his position on 1 July 2008 as a new Group Human Resources Director and is responsible for the company's businesses in Europe outside of Spain, and also serves as a Member of the Board at Telefónica Europe plc. Simon has significant experience in management development at an international level thanks to his previous roles as HR Director for Africa and Iberia regions at Diageo. Prior to Diageo, Simon worked for a number of major companies in the financial services and consumer goods industries, including Barclays, Lloyds TSB and Grand Metropolitan. British born with Spanish parents, Simon is bilingual in English and Spanish. His global career experience has included responsibility for regions as diverse as Thailand, Latin America and North America. He currently resides in London.

GUILLERMO JOSÉ FERNÁNDEZ VIDAL (*1946)

MEMBER

He holds a degree in Industrial Engineering and Computer Science and in 1989 he joined Telefónica, first as a manager and later he was promoted to Commercial Director (1992–1995) and General Manager of Companies of Telefónica (1995–1999). In 1999 he was appointed Chief Executive Officer of Telefónica Data and President of Telefónica Data España. In the same year he was also a member of statutory bodies at Telefónica Móviles, Telefónica de España, Vía Digital and Portugal Telecom. In 2003 he was appointed General Manager for Subsidiaries. From 2004 to 2005 he was General Manager for Commercial Development and Affiliates at Telefónica, S.A. In 2005 he was appointed as Corporate General Manager of Telefónica, S.A. and member of the board of Telefónica Móviles de España, Telefónica de España and TPI. He is presently advisor to Telefónica, S.A.

LUIS LADA DÍAZ (*1949)

MEMBER

He holds a degree in telecommunications engineering and joined the Telefónica Group in 1973 in the Research and Development Department, rising through the ranks to hold various managerial and executive positions within the group. In 1989 he was Deputy Director for Technology, Planning and International Services. Later he joined Amper Group, a manufacturer of telecommunications system and equipment, as Director of Planning and Control. He returned to the Telefónica Group in 1993 as Chief Controller for Subsidiaries and Participated Companies. In 1994 he was appointed Chief Executive Officer of Telefónica Móviles de España, S.A., and in September 2000 he went on to become President and Chief Executive of Telefónica Móviles, S.A. until 2004, when he was named Director for Development, Planning and Regulatory Affairs of Telefónica, S.A. In 2005 he was elected Executive Chairman of Telefónica de España, S.A.U. Until he left his executive positions in Telefónica in July 2006, he had served on the Boards of Directors of Telefónica, S.A., Telefónica Móviles, S.A., Telefónica Internacional, S.A. and other Telefónica Group's corporations, and currently is a member of several foundations and think-tank Groups in Spain, Professor "Ad Honorem" of the Politechnic University of Madrid, Member of the Royal Academy of Engineering, the Scientific Advisory Board of Telefónica Research & Development (TID, S.A.) and the Telefónica Latinoamerica Advisory Board; and Member of the Boards of Directors of INDRA Sistemas S.A., Telefónica I+D, Telcel (Telefónica Venezuela), Ydilo Advanced Voice Solutions, S.A.

DUŠAN STAREČEK (*1956)

MEMBER

Qualified in Electronic and Electrical Technology at the Technical and Engineering Secondary School in Rožnov p. Radhoštěm. In 1975, he started work as a technician at Long-distance Cables Administration, Prague (the legal predecessor of ČESKÝ TELECOM). In 1992, he was promoted to the position of Head of External Maintenance in the Transmission Technology Unit (the legal predecessor of Telefónica O2 Czech Republic). At present, he works as Specialist for Operation and Maintenance of Digital Telecommunications Technology in Ostrava. He is a member of the Trade Union Steering Committee of Telefónica O2 Czech Republic, Chairman of KOV MORAVA and member of EWC (European Works Council) at Telefónica Europe plc.

MARIA PILAR LÓPEZ ÁLVAREZ (*1970)

MEMBER

A graduate of Business Studies, she joined Telefónica after working for several years at JP Morgan in London and New York where she worked her way up to Vice President. Pilar joined the Telefónica Group 1999 in Telefónica de España's Strategic Planning Department. In May 2000 she was appointed Director of Management Control at Telefónica, S.A. Two years later she joined Telefónica Móviles S.A. to head up its Management Control function. In October 2006 she was promoted to Director of Strategy and Business Development at Telefónica de España. On 1st March 2007, she was appointed Chief Financial Officer of Telefónica O2 Europe plc (now Telefónica Europe plc).

ÁNGEL VILÁ BOIX (*1964)

MEMBER

Graduated in Industrial Engineering from the Universitat Politécnica de Catalunya (1988) and holds a MBA from Columbia University (New York, 1990). After working as a financial analyst at Citibank NA and consultant at McKinsey & Co. he went to work for Ferrovial and Pacsa, two Spanish construction and service companies. In 1997 Mr. Vilá joined Telefónica as Group Controller, being promoted in 1998 to CFO at Telefónica Internacional and, subsequently, to Managing Director of Corporate Development at Group level. Mr. Vilá is Vice Chairman of the Board of Directors of Telco SpA (Italy) and member of the European Advisory Panel of Macquarie's MEIF 1, 2, 3 Funds. He previously served on the Boards of Banco Bilbao Vizcaya Argentaria (BBVA), CTC Chile, Cablevisión Argentina, Terra Lycos, Indra SSI, Telefónica Sistemas, Telefónica Data, Atento and Catalana d'Iniciatives.

PAVEL HERŠTÍK (*1951)

MEMBER

Graduated in communication technology from the Secondary Technology School of Electrotechnical Engineering. In 1972, he started working as a telephone test centre technician in Ředitelství telekomunikací Praha (Telecommunications Headquarters, Prague). For the next 20 years (1975–1995), he worked in the field of work procedure planning, evaluation and work efficiency measurement. From 1995 to 2005, he was Head of Information Management and went on to become Head of the Management, Organisation and Administration Department. At present, he is Senior

PAVEL HERŠTÍK EDUARDO ANDRES JULIO ZAPLANA HERNÁNDEZ-SORO TOMÁŠ FIRBACH PETR GAZDA ENRIQUE USED AZNAR

Specialist in the area of management and administration of management documents. In 2005 and 2009 he completed courses in international accounting standards and intra-holding relationships. In 2007 he was certified under the National Certification Programme for Corporate Ethics and Culture. He is Chairman of the Trade Union Steering Committee of Telefónica O2 Czech Republic and member of the European Works Council of the European division of the Telefónica Group. In the last five years he was not a supervisory board member in any other company.

EDUARDO ANDRES JULIO ZAPLANA HERNÁNDEZ-SORO (*1956)

MEMBER

Eduardo Zaplana has a degree in law and was the President of the regional Government of Valencia from 1995 to 2002. He has been a member of the Spanish Parliament and Senator, as well as the Spanish Minister for Labour and Social Affairs and government spokesman from 2002 to 2004. Among other official posts, he has also been President of the Commission for Regional Policy and Structural Funds, member of the Bureau and first Vice-President at the Committee of the Regions (CoR). In April 2008, Telefónica appointed Eduardo Zaplana as the Company's representative for Europe. Telefónica has an office in Brussels and operations in the UK, Germany, Ireland, the Czech Republic and Slovakia. Mr. Zaplana is a member of the Board of Directors of Telefónica Europe plc from July 2008. In December 2008, Telefónica has carried out a reorganization of its directive structure to strengthen the sections depending from the Chairman, and specifically the Technical General Secretariat, and it has created a new position of Associate to the Technical Secretary General. This position is occupied by Eduardo Zaplana, who widens in this way its field of action from his previous position related only to one of the geographical areas, Europe.

TOMÁŠ FIRBACH (*1976)

MEMBER

Graduated in Management and Economics in Transportation from the Czech Technical University, Department of Transportation. After his graduation in 1999 he worked in JSJ spol. s r.o. as information systems manager. In 2001 he joined Eurotel Praha, spol. s r.o. (the legal predecessor of Telefónica O2 Czech Republic) as network planning specialist. In 2004–2005 he worked in ČD Telekomunikace, a.s. (presently ČD Telematika, a.s.) as business consultant. He has been with Telefónica O2 Czech Republic since 2005, working as Senior Product Manager for fixed line data services. In the last five years he was not a member of any other statutory or supervisory bodies except for the Supervisory Board of Telefónica O2 Czech Republic, a.s.

PETR GAZDA (*1965)

MEMBER

Graduated in Economics and Management (BA) from the Business College Ostrava. He has been with Telefónica O2 Czech Republic (and its legal predecessors) since 2006; he presently works as Network Operations Director for Regions; previously: 1991–2006 Eurotel Praha; 1988–1991 ČESKÝ TELECOM; 1986–1988 AŽD Praha, specialist; 1983–1984 AŽD Praha, electrical engineer. In the last five years he was not a member of any other statutory or supervisory bodies except for the Supervisory Board of Telefónica O2 Czech Republic, a.s.

ENRIQUE USED AZNAR (*1941)

MEMBER

Enrique Used Aznar acts as a member of the Board of Directors of Telefónica International, Telefónica of Brasil (Telesp) and Telefónica Perú. He is also a member of the Assembly Directive of IESE of Madrid, vice-chairman of Spanish Association for Cancer Research and Patron of Cancer Science Foundation. He has also served as Executive Chairman of Telefónica Internacional S.A., Telefónica Servicios Móviles and Telefónica I+D, as executive vice-chairman of TPI Páginas Amarillas, Telefónica of Chile and Telintar (investor from Argentina), and as member of the Boards of Directors of Telefónica, Telefónica of Argentina, AT&T Network System International and Ericsson Spain. He holds a degree in telecommunications engineering from Universidad de Madrid, and a degree from IESE (Business Management).

PERSONNEL COMPOSITION OF THE SUPERVISORY BOARD OF TELEFÓNICA O2 CZECH REPUBLIC, A.S., AS AT 15 MARCH 2009

Name	Function	Member since
Jaime Smith Basterra	Chairman of the Supervisory Board	21 April 2008
Alfonso Alonso Durán	First Vice-Chairman of the Supervisory Board	23 June 2005
Lubomír Vinduška	Second Vice-Chairman of the Supervisory Board	29 June 2008
Luis Lada Díaz	Member of the Supervisory Board	23 June 2005
Maria Pilar López Álvarez	Member of the Supervisory Board	21 April 2008
Enrique Used Aznar	Member of the Supervisory Board	24 February 2009 (co-opted)
Ángel Vilá Boix	Member of the Supervisory Board	23 June 2005
Anselmo Enriquez Linares	Member of the Supervisory Board	24 July 2008 (co-opted)
Antonio Botas Bañuelos	Member of the Supervisory Board	21 April 2008
Guillermo José Fernández Vidal	Member of the Supervisory Board	23 June 2005
Eduardo Andres Julio Zaplana Hernandéz-Soro	Member of the Supervisory Board	24 July 2008 (co-opted)
Petr Gazda	Member of the Supervisory Board	29 June 2008
Pavel Herštík	Member of the Supervisory Board	29 June 2008
Tomáš Firbach	Member of the Supervisory Board	29 June 2008
Dušan Stareček	Member of the Supervisory Board	29 June 2008

Information about the term of office of Supervisory Board members is given on page 59.

ALL CHANGES IN THE PERSONNEL COMPOSITION IN THE SUPERVISORY BOARD IN THE FIRST HALF OF 2008 WERE DESCRIBED IN THE 2007 ANNUAL REPORT AND IN THE 2008 HALF-YEAR REPORT.

THE FOLLOWING CHANGES OCCURRED IN THE PERSONNEL COMPOSITION OF THE SUPERVISORY BOARD IN THE SECOND HALF OF 2008 AND IN THE PERIOD FROM 1 JANUARY–15 MARCH 2009:

Andrew Harley	his membership in the Supervisory Board ended on 24 July 2008 when his resignation was discussed by the Supervisory Board,
Anselmo Enriquez Linares	appointed (co-opted) member of the Supervisory Board on 24 July 2008,
Eduardo Andres Julio Zaplana Hernandéz-Soro	appointed (co-opted) member of the Supervisory Board on 24 July 2008,
Lubomír Vinduška	elected Second Vice-Chairman of the Supervisory Board by the Supervisory Board of 24 July 2008,
Vivek Dev	his membership in the Supervisory Board ended on 24 February 2009 when his resignation was discussed by the Supervisory Board,
Enrique Used Aznar	appointed (co-opted) member of the Supervisory Board on 24 February 2009.

PRINCIPLES OF REMUNERATION OF PERSONS WITH EXECUTIVE POWERS IN THE ISSUER

Persons with executive powers in Telefónica O2 are members of the Board of Directors, members of the Supervisory Board, the Chief Executive Officer and executive managers who are not members of the Board of Directors and are in positions at the CEO-1 level (other executives) (pages 64–65).

Changes in the way the remuneration of members of the Board of Directors and of the Supervisory Board came into effect in mid-2008. The General Meeting of 21 April 2008 approved new rules for remuneration of members of these bodies (to take effect from 1 July 2008), which are fully aligned with the best practices in the area of Corporate Governance. The change concerns the fact that the method when the General Meeting approved the annual sum of remuneration for a specific governing body for the current calendar, while the distribution of these sums among the members – on the condition that the previous rules of the remuneration of Board of Directors and Supervisory Board members were observed – was left to the discretion of the Supervisory Board (assisted in its decisions by the Nomination and Remuneration Committee), no longer applies. The new rules of remuneration provide specific amounts of remuneration for individual categories of members of the Board of Directors and of the Supervisory Board, i.e. remuneration which a regular member, vice-chair and chair of the body are entitled to, as well as other conditions for the granting of any discretionary benefits. Each member of the Board of Directors/Supervisory Board is entitled to the whole amount of remuneration on the condition that he/she makes a claim for it; if the member of the Board of Directors/Supervisory Board does not make a claim for the whole amount of remuneration, he/she will be remunerated only in the extent in which a claim was made. The basic information about the rules for remuneration of Board of Directors and Supervisory Board members and of the members of the Supervisory Board committees is given below. The full text of the new Rules for Remuneration of Members of the Governing Bodies of Telefónica O2 is published in the Czech and English languages on the Company's website.

THE BOARD OF DIRECTORS AND CHIEF EXECUTIVE OFFICER

A) REMUNERATION

In the first half of 2008, members of the Board of Directors are remunerated in accordance with the Rules for Remuneration of Members of the Telefónica O2 Board of Directors (Rules) which were approved by the Ordinary General Meeting of 27 April 2006. The principles of remuneration provided for in the Rules are explained in the 2007 Annual Report. The General Meeting approved a total sum of CZK 1.5 million for the remuneration of members of the board of Directors in the first half of 2008.

The new Rules which came into force on 1 July 2008, and whose leading principle is described above, introduced a flat monthly bonus, which comprises the following:

- an amount covering mandatory payments (e.g. taxes, health insurance contributions, etc.) which the member of the Board of Directors is liable to pay due to the fact that he/she is covered by a liability insurance for any damage arising from the performance of a member of the Board of Directors, and mandatory payments arising from the provision of the amount under this sentence. This amount depends on the amount of insurance premium attributable to the member of the Board of Directors; the overall amount is calculated using methods common in the business of insurance;
- an amount attributable to the individual categories of Board of Directors members for the number of meetings attended: (i) member of the Board of Directors: CZK 25,000; (ii) Vice-Chair of the Board of Directors: the amount as in (i) plus CZK 10,000; Chair of the Board of Directors: the amount as in (ii) plus CZK 10,000.

The Chief Executive Officer is also entitled by virtue of his/her function to additional remuneration which comprises the following components:

- basic gross salary;
- performance-related bonus;
- compensation of the balance between the health insurance benefits and 100% of the average daily wage.

The performance-related bonus is granted to the Chief Executive Officer conditional on delivering on the targets set for the CEO for the calendar year in question. These targets have a 70% direct correlation with the annual budget and business plan approved by the Board of Directors and with other targets set at the Group level. The targets represent the key performance indicators of both financial and non-financial nature (e.g. reaching the projected operating profit, reaching the revenues targets, higher customer satisfaction). The performance against these targets is evaluated by the Board of Directors and discussed by the Nomination and Remuneration Committee; the audited financial results and, in the case of customer experience, independent (external) surveys form the basis for consideration. The performance-related bonus may, in aggregate for the calendar year, reach 44% of the total annual income if the targets are achieved to a standard level.

Other non-pecuniary benefits are connected with the relocation of the executive from Spain to the Czech Republic (accommodation in Prague, flights for visiting the family, contributions towards school fees at the international school in Prague, international health insurance). In the event of temporary work incapacity, the Company will compensate to the Chief Executive Officer, for each day of the work capacity, the balance between the health insurance benefits and the 100% of the average daily salary.

B) COMPENSATION FOR THE COMMITMENT TO A NON-COMPETITION COVENANT

A member of the Board of Directors may, in their agreement for discharge of the office of a member, commit to the so-called non-competition covenant, i.e. a pledge not to do business, after the termination of the office, either individually or for the benefit of another person, in the field of telecommunications in the Czech Republic (nor in the field of advisory or consulting services related to the telecommunications industry), unless such business is done in another member of the Group. The agreement for discharge of the office of a member (including the non-competition covenant) must be approved by the General Meeting.

Compensation for commitment to the non-competition covenant is based on the following principles:

- the non-competition covenant is accepted for a period of six months as of the termination of office;
- the Company is obliged to provide to the member of the Board of Directors in question, for committing to the non-competition covenant, compensation amounting to six times the average flat remuneration as laid down in the Rules for the Remuneration of Members of the Board of Directors, in an amount attributable to one member of the Board of Directors, in the month preceding the month in which the member of the Board of Directors terminated his/her position in the Board of Directors; the fact that any member of the Board of Directors has or has not made a claim to their remuneration is not considered in the calculation of the average flat remuneration.

Upon terminating his/her employment, the Chief Executive Officer is bound by the non-competition covenant covering the whole Telefónica Group.

C) IN-KIND BENEFITS

DAMAGE LIABILITY INSURANCE

The Company, as the policy holder, contracted an insurance policy covering against damage caused in relation to the performance of designated functions; the insured persons (i.e. persons whose functions are covered by the policy) may include members of the Board of Directors. The total insurance premium paid by the Company is evenly divided amongst the insured persons and the amount calculated per insured person constitutes their income.

ENDOWMENT INSURANCE

No endowment insurance has been contracted for members of the Board of Directors in relation to their duties as members.

CAR

Members of the Board of Directors are not provided with cars for private use in connection with their duties as members. The Chief Executive Officer is provided with a car both for work and private use.

THE SUPERVISORY BOARD

A) REMUNERATION

In the first half of 2008, members of the Board of Directors are remunerated in accordance with the Rules for Remuneration of Members of the Telefónica O2 Supervisory Board (Rules) which were approved by the Ordinary General Meeting of 27 April 2006. The principles of remuneration provided for in the Rules are explained in the 2007 Annual Report. The General Meeting Board approved a total sum of CZK 4.2 million for the remuneration of members of the Board of Directors in the first half of 2008.

The new Rules which came into force on 1 July 2008, and whose leading principle is described at the beginning of this sub-section, introduced a flat monthly bonus, which comprises the following:

– an amount covering mandatory payments (e.g. taxes, health insurance contributions, etc.) which the member of the Supervisory Board is liable to pay due to the fact that he/she is covered by a liability insurance for any damage arising from the performance of a member of the Supervisory Board, and mandatory payments arising from the provision of the amount under this sentence. This amount depends on the amount of insurance premium attributable to the member of the Supervisory Board; the overall amount is calculated using methods common in the business of insurance;
– an amount attributable to the individual categories of Supervisory Board members for the number of meetings attended: (i) member of the Supervisory Board: CZK 40,000; (ii) Vice-Chair of the Supervisory Board: the amount as in (i) plus CZK 10,000; Chair of the Supervisory Board: the amount as in (ii) plus CZK 10,000.

If the member of the Supervisory Board is at the same time member of any of the committees established by the Supervisory Board, they are entitled to remuneration for working in the committee, which is construed as a bonus per meeting of the committee, as follows: (i) member of the committee: CZK 10,000; (ii) vice-chair of the committee: the amount as in (i) plus CZK 12,000; (iii) chair of the committee: the amount as in (ii) plus CZK 15,000. The said amounts attract an additional CZK 10,000 if the membership is in the Audit and Control Committee.

B) COMPENSATION FOR THE COMMITMENT TO A NON-COMPETITION COVENANT

A member of the Supervisory Board may, in their agreement for discharge of the office of a member, commit to the so-called non-competition covenant, i.e. a pledge not to do business, after the termination of the office, either individually or for the benefit of another person, in the field of telecommunications in the Czech Republic (nor in the field of advisory or consulting services related to the telecommunications industry), unless such business is done in another member of the Group. The agreement for discharge of the office of a member (including the non-competition covenant) must be approved by the General Meeting.

Compensation for commitment to the non-competition covenant is based on the following principles:

– the non-competition covenant is accepted for a period of six months as of the termination of office;

– the Company is obliged to provide to the member of the Supervisory Board in question, for committing to the non-competition covenant, compensation amounting to six times the average flat remuneration as laid down in the Rules for the Remuneration of Members of the Supervisory Board, in an amount attributable to one member of the Supervisory Board, in the month preceding the month in which the member of the Supervisory Board terminated their position in the Supervisory Board; the fact that any member of the Supervisory Board has or has not made a claim to their remuneration is not considered in the calculation of the average flat remuneration.

C) IN-KIND BENEFITS

DAMAGE LIABILITY INSURANCE

The Company, as the policy holder, contracted an insurance policy covering against damage caused in relation to the performance of designated functions; the insured persons (i.e. persons whose functions are covered by the policy) may include members of the Supervisory Board. The total insurance premium paid by the Company is evenly divided amongst the insured persons and the amount calculated per insured person constitutes their income.

ENDOWMENT INSURANCE

The Company, as the policy holder, contracted an endowment insurance policy for the benefit of selected Supervisory Board members. According to the Rules approved by the Ordinary General Meeting on 13 June 2003, the endowment insurance may be contracted for the maximum amount of twice the annual remuneration of a Supervisory Board member. The Supervisory Board lays down the specific terms and conditions of the insurance, and the following applies at present:

– the upper limit for the determination of the insurance amount is calculated as a quotient of:
  – the total annual remuneration for Supervisory Board members approved by the General Meeting, and
  – the total number of Supervisory Board members multiplied by two;
– an application for endowment insurance may be made by a person who has been a Supervisory Board member for a minimum of six months;
– the insurance contract is concluded for a minimum of five years;
– after the termination of the office of member of the Supervisory Board, the insurance policy is amended in a way that the policy holder (and premium payer) becomes the person who had been member of the Supervisory Board.

No insurance contracts for endowment insurance of Supervisory Board members were contracted in 2008.

CAR

The Supervisory Board Chairman and Vice-Chairmen are according the Rules approved by the General Meeting entitled to a higher middle class car for work and private use. This benefit has not been claimed since mid-2005.

OTHER BENEFITS

The company also granted the following benefits to members of the Board of Directors (including the Chief Executive Officer) and to members of the Supervisory Board:

– service telephone lines
– mobile telephones
– computing equipment
– VISA payment card (in the case of the Supervisory Board, only the Chairman and Vice-Chairmen are eligible; the benefit has not been claimed since mid-2005)
– health care

The benefits were given to the persons in questions in relation to their performance of the duties attached to their office.

The principles of remuneration of members of the Board of Directors and of the Supervisory Board, including discretionary benefits, are published in the full version on the Company's website.

MEMBERS OF THE EXECUTIVE MANAGEMENT (EXCLUDING THE CHIEF EXECUTIVE OFFICER)

Remuneration to which executive managers of the Company (not applicable to the Chief Executive Officer) are also entitled consists of two components. The components comprise the basic gross salary on the one hand, and a performance-related bonus which is granted upon meeting annual targets, on the other. The method of target setting, as well as performance evaluation and control are governed – for persons in the position of Vice-President – by the same rules and procedures as in the case of the Chief Executive Officer. For other members of the executive management of the Company, 30% of their annual performance-related bonus represents the achievement of specific key performance indicators set for the year in question, and 70% of it is determined on the basis of a personal assessment by the Chief Executive Officer; the sum of the bonus may, for both groups of executive managers, reach 33% of their total annual income, provided that targets are achieved to a standard level.

OTHER INFORMATION RELATING TO PERSONS WITH EXECUTIVE POWERS

INFORMATION ON ALL PECUNIARY AND IN-KIND INCOME RECEIVED IN THE ACCOUNTING PERIOD BY PERSONS WITH EXECUTIVE POWERS FROM ENTITIES CONTROLLED BY TELEFÓNICA O2

(in CZK millions)	Pecuniary income	Of which royalties	In-kind income
Board of Directors – total	103.73	0	9.12
– of which by virtue of membership in the issuer's Board of Directors[1]	0.475	0	2.15
Supervisory Board – total	11.97	0	4.68
– of which by virtue of membership in the issuer's Supervisory Board[2]	6.15	0	4.35
Executive Management[3]	49.49	0	2.87

[1] In the first half of 2008, the pecuniary income from membership in the Board of Directors of the issuer amounted to CZK 244,000.

[2] the first half of 2008, the pecuniary income from membership in the Supervisory Board of the issuer amounted to CZK 2,859,792.

[3] The Executive management category includes the shares of executives positions are included in the Executive Management of Telefónica O2 (Chief Executive Officer and executives at the CEO-1 level). Shares of those members of the Board of Directors who, at the same time, qualify as Executive Management are included in the Board of Directors total category. All income (pecuniary and in-kind) is shown in a summary form for all persons who – in the period under review – were members of a governing body or executive managers meeting the criteria of the Executive Management category.

Persons with executive powers did not receive any pecuniary or in-kind income from entities controlled by Telefónica O2 in 2008.

INFORMATION ON THE NUMBER OF SHARES ISSUED BY TELEFÓNICA O2 AND HELD BY STATUTORY BODIES OR THEIR MEMBERS, PERSONS WITH EXECUTIVE POWERS, INCLUDING PERSONS RELATED TO THESE PERSONS, INFORMATION ON OPTION AND SIMILAR AGREEMENTS, INFORMATION ON INDIVIDUAL TRANSACTIONS CONCLUDED BY THE SAID PERSONS IN THE ACCOUNTING PERIOD

	Number of shares
Board of Directors	0
Supervisory Board	100
Executive Management[1]	0
Persons related to persons with executive powers	100

[1] The Executive management category includes the shares of executives positions are included in the Executive Management of Telefónica O2 (Chief Executive Officer and executives at the CEO-1 level). Shares of those members of the Board of Directors who, at the same time, qualify as Executive Management are included in the Board of Directors total category,

No conflict of interest was found in relation to members of the Board of Directors, Supervisory Board and executive management; no member has been, in the last five years, lawfully sentenced for fraud, nor been – as a statutory or supervisory body – a party to insolvency proceedings, nor been subject to receivership or liquidation, nor charged or sanctioned by statutory or regulatory bodies.

INFORMATION ON WORK CONTRACTS AND SIMILAR CONTRACTS CONCLUDED BETWEEN MEMBERS OF THE BOARD OF DIRECTORS AND OF THE SUPERVISORY BOARD WITH THE ISSUER

In 2008, all members of the Board of Directors and of the Supervisory Board – except substitute members Eduardo Andres Julio Zaplana Hernandéz-Soro and Anselmo Enriquez Linares who were appointed (co-opted) as members of the Supervisory Board in the second half of 2008, and the Supervisory Board members elected by employees (Petr Gazda, Tomáš Firbach, Pavel Herštík, Dušan Stareček and Lubomír Vinduška) in the Supervisory Board elections in June 2008 – were bound by a valid agreement for discharge of the office of a member, which stipulates the eligibility to compensation for members who had committed to the non-competition covenant after the termination of their office.

TELEFÓNICA O2'S DECLARATION OF COMPLIANCE WITH THE CODE OF GOOD CORPORATE GOVERNANCE BASED ON OECD PRINCIPLES

Telefónica O2 made a commitment to the principles of Good Corporate Governance already in its 2001 Annual Report; it has been making regular statements in its annual reports, concerning the progress of implementation of the principles of Good Corporate Governance in its practices. The Company always aims for the maximum compliance with these principles; to this end, it makes the use of the shared experience and knowledge in the area of Corporate Governance of the parent Telefónica, S.A., and actively follows the latest Corporate Governance trends in the European Union and in other developed countries. The Board of Directors regularly oversees the good practice of Corporate Governance in the whole Telefónica O2 Czech Republic Group, i.e. in addition to Telefónica O2, also in subsidiaries controlled by it.

Telefónica O2 meets all the criteria, principles and recommendations of the updated 2004 Code of Good Corporate Governance based on OECD Principles (the Code), which the Company helped to design, with the exception of those criteria which fall outside the direct control of the Company's governing bodies and depend on the decisions of the Company's owners (namely the requirement regarding the number of independent members of the Supervisory Board).

CORPORATE GOVERNANCE

No principal changes occurred in the corporate governance model of Telefónica O2 in 2008. The model, as per the Articles of Association, is based on interaction between the executive Board of Directors, made up exclusively of executive managers of the Telefónica O2 Group, and the Supervisory Board. The Supervisory Board has powers to control key decision-making processes (using the mechanism of "prior standpoints" of the Supervisory Board to selected issues) and monitor other important aspects of the Company's operation. The powers of the Supervisory Board and their discharge make a full and active use of advisory and initiative roles of the

Supervisory Board's committees. An integral part of the model is the combination of the Chief Executive Officer's function with the function of Chairman of the Board of Directors, which the Company finds efficient and acceptable given the strong role of the Supervisory Board and the active involvement of its committees.

ORGANISATION OF CORPORATE GOVERNANCE

The model of corporate governance applied by the Telefónica O2 ensured that throughout 2008 the Company was adequately managed by the Board of Directors and that the Supervisory Board was duly exercising its oversight and controlling function.

An Ordinary **General Meeting** of the Company was held on 21 April 2008. The agenda comprised points related to the standard business of a joint-stock company, and an amendment to the Articles of Association undertaken in order to further improve and strengthen the governance processes in the Company. Full details of the conclusions of the General Meeting are given in the 2008 Half-year Report and on the Company's website. Information regarding the dividend, record date and the dividend disbursement date is on pages 189–190 of the Annual Report.

The **Board of Directors** held twenty three meetings in 2008, thus complying with the duty to hold a minimum of twelve meetings each year. As a result of the amendment of the Articles of Association, the number of members was reduced from nine to seven. An overview of the members of the Board of Directors, including their professional résumés, and the personnel changes in the Board of Directors are given on pages 60–63. The personnel changes in the Board of Directors in 2008 and in the subsequent period until 15 March 2009 occurred as a result of a promotion of the former members (Ramón Ros Bigeriego and José Fernando Astiaso Laín) to executive positions in the European division Telefónica Europe.

The **Supervisory Board** held five meetings in 2008, and thus complied in full with the Articles of Association. The practice has settled on the most effective pattern of regular quarterly meetings (February, April, July, October) dedicated, among other things, to the discussion of regular (periodic) financial statements given by the Company to its shareholders; in addition, one meeting is held primarily in preparation for the General Meeting. The Ordinary General Meeting of April 2008 approved an amendment to the Articles of Association aimed at introducing more efficiency into the governance of the Company, effectively reducing the minimum required number of Supervisory Board meetings from six to four in a calendar year. During 2008 and in the first quarter of 2009 (until 15 March 2009), several changes occurred in the personnel composition of the Supervisory Board; they were the result of personnel changes and transfers of executives within the global Telefónica Group, and of the elections of Supervisory Board members by employees. Employee elections for the Supervisory Board were held with own support of an electronic election campaign and the upgraded version of the electronic voting system (first used in 2003), whose safeguards and security mechanisms were independently audited. The progressive system allows for taking part in the elections regardless of the voter's time, technical or geographic limitations (a vote can be cast using a PDA, any computer of the Company and also remotely). An overview of the personnel changes in the Supervisory Board in the period covered by the Annual Report, including the personnel composition as at 15 March 2009 and the professional résumés of all members of the Supervisory Board, are given on pages 66–71. As at 15 March 2009, none of the Supervisory Board members meet the criterion of independence.

New members of the Board of Directors, Supervisory Board and its committees have, already at the beginning of their office, all information about the Corporate Governance rules and principles applied in Telefónica O2 and in its Group, namely the financial, commercial and other important information necessary for the due discharge of their function. The information is disseminated via the Corporate Governance Portal of the Telefónica O2 Group (CG Portal).

The discharge of duties of all governing bodies, their committees and the Internal Audit is governed by rules of procedure and charters, which are always updated after any changes are made. In 2008, the governance document of the Ethics and Corporate Social Responsibility Committee was amended, and qualitative modifications were effected also in the governance documents of Internal Audit and Risk Management (all the changes are iterated below).

The previously existing position of Company Secretary is in the new corporate governance model of Telefónica O2 combined with that of General Counsel. The Company Vice-Secretary assists in and provides for the Corporate Governance processes in the Telefónica O2 Czech Republic Group; the Company Vice-Secretary is the secretary to the Board of Directors, Supervisory Board and to the Supervisory Board Committees.

In 2008, the Internal Audit and Risk Management function was developed further, while its organisation (in one organisation unit), subordination in the line to the Chief Executive Officer and functional reporting to the Audit and Control Committee remained unchanged. Marek Hakala has been acting Executive Director of Internal Audit and Risk Management since November 2008. The previous Executive Director, Zdeněk Radil, has left Telefónica O2 at his own initiative.

Internal Audit represents an important instrument of Corporate Governance and it provides the Company's governing and executive bodies with independent and professional assessment of the Company's internal control system and the situation and trends in the given area compared to current best practice, the rules and regulations in force, and work orders and instructions issued, thus helping to continuously improve the Company's internal control system. In 2008, Internal Audit performed a total of thirty four audits and controls (including the regular audit of internal controls as per the requirements of SOX Section 404) according to the annual operative internal audit plan, or as mandated by the governing bodies and the Chief Executive Officer. In addition to performing audits and controls in Telefónica O2, the Internal Audit unit also acts as internal auditor of Telefónica O2 Slovakia. The audit conclusions were used by the management to formulate actions to redress the issues identified. Internal Audit monitors the implementation of such actions and reports to the governing bodies and the executive management.

The work of Internal Audit is monitored on a regular basis by the Audit and Control Committee. The activities of Internal Audit and its main processes are laid down in the Statue of Internal Audit of Telefónica O2 Czech Republic, which also stipulates the principle of independence of the Internal Audit function and the principle of objectiveness of internal auditors. The Internal Audit Charter was last amended in March 2008, in order to accommodate recommendations of an international quality assurance audit of our Internal Audit and Risk Management Unit. The audit was carried out in February 2007 (the detail is given in the 2007 Annual Report).

In 2008, the Company continued in the development of its **Risk Management** function and in its harmonisation with the methodology and practice in the global Telefónica Group, in order to create more space for the sharing of experience and knowledge in the area of mitigation of specific risks with the parent company and other members of the Group. The risk management system covers all areas of operations of Telefónica O2, including its subsidiary Telefónica O2 Slovakia, and provides for the identification, assessment and mitigation of risks, which it continues to monitor throughout. The Board of Directors, Supervisory Board and the Audit and Control Committee receive regular monthly reports containing information about the main risks and their development over time. For more details concerning Risk Management please refer to page 28 of the Annual Report.

An electronic platform, the so-called CG Portal, is operated and continually developed in Telefónica O2 Czech Republic. It supports the exercise of powers of all governing bodies and provides for efficient administration of Corporate Governance in Telefónica O2 Czech Republic and its group. It is a comprehensive and modern solution with archiving, distribution, organisation, education and information functions, which are used both by regular employees and the members of the governing bodies. The system supports the configuration of several levels of access privileges and has a secure remote access to all data through fixed line and mobile technology. The instrument confers equal access to archived and current documents and information to all members of the relevant governing bodies, irrespective of any local or time limitations. The document management system of the Company stores several dozens of thousand open domain and classified documents (a majority of them both in Czech and in English); in addition to the minutes of meetings, the system also stores internal audit reports and risk reports, information about the Telefónica O2 Czech Republic Group and its subsidiaries, etc. For more detail of the content and the main functions of CG Portal please refer to the 2006 Annual Report. The portal is currently used also as a platform for supporting and administrating other activities in the general sphere of Corporate Governance. In addition to the elections of employee representatives to the Supervisory Board, as mentioned above, the activities concern primarily the general agenda of the Business Principles (including the operation of a confidential whistle-blowing channel for reporting of suspected ethical malpractices), and other select priority areas of the Company's Compliance Programme. The focus of attention is on risk prevention; to this end, the Company employs online courses as a primary instrument. Depending on the subject matter in question, the courses are targeted either to all employees (Business Principles), or to a selected group of employees (e.g. the competition law course which is already online, or the personal data protection course which is in the course of preparation).

SHAREHOLDER RELATIONS

A strict compliance with all the statutory rights of shareholders, commitment to the principle of equal treatment of all shareholders of a similar standing, while respecting the specific statutory rights of minority shareholders belong among the key guiding principles of Corporate Governance of Telefónica O2. In 2008, too, the Company fully honoured its commitment to the shareholders.

The Company is scrupulous about the timely and full information to all shareholders about the developments in the Company, its financial results and business plans; in doing so, the Company has always strived and managed to exceed the scope of minimum statutory disclosure. The Company uses it website as the main platform for communication (section About Us). The Company publishes regular press releases with the quarterly financial results and announces all significant events and developments.

When organising General Meetings, the Company proceeds in a way that guarantees the compliance with all the statutory conditions and with the Articles of Association, whilst observing to the maximum extent possible the requirements of the Code which concern the rights of shareholders and their fair treatment. The Company publishes the date of the General Meeting several months prior on its website. The date, time and location of the General Meeting are chosen on the merit of ready access and availability. The Rules of Procedure of the General Meeting, despite the fact that they haven not deviated from the standard language, are approved at each meeting of the governing body. During this time, the shareholders have not made any motions to amend the Rules of Procedure. The Rules of Procedure allow shareholders to participate effectively in decision-making on fundamental changes in the Company and to ask questions and seek information on matters included on the agenda of the General Meeting. The draft Rules are available to shareholders on the Company's website and in Telefónica O2 headquarters on the day of the publication of the date of the General Meeting. All the necessary documents are available to all shareholders in print form, in two languages (Czech and English). The shareholders have the opportunity to study the principal documents (financial statements, report on the relationships with related undertakings, and any proposed amendments to the Articles of Association that may be on the agenda) within the statutory period prior to the date of the General Meeting in the premises of the Company's headquarters; upon registration for the General Meeting, they receive a full file of documents to be discussed at the meeting, including an overview of statements to be made by members of the Board of Directors in respect of the main points on the agenda. All the documents for the General Meeting and other relevant documents (e.g. the Articles of Association) are available to the shareholders also in the information centre which the Company operates for the shareholders at every General Meeting. Each point on the agenda is voted on separately, after the discussion on that point is concluded. In addition to members of the Board of Directors and of the Supervisory Board, chairpersons of committees established under the Articles of Association are also available to take questions from shareholders. A public notary is present for the whole duration of the General Meeting.

All motions (questions, requests for explanation, counterproposals and proposals) made by shareholders during the Ordinary General Meeting of 21 April 2008 (sixteen in total) were adequately addressed by the members of the Board of Directors. All questions from shareholders and the corresponding answers are noted in the Minutes of the General Meeting. Shareholders did not put any questions to Supervisory Board members, the chairpersons of the Supervisory Board committees and to representatives of the Statutory Auditor.

TRANSPARENCY AND OPEN INFORMATION POLICY

Telefónica O2 scrupulously and diligently complies with all national and community laws and the principles of the Code. In line with its mandatory duties and voluntary commitments, Telefónica O2 continually and pro-actively provides shareholders and investors with all vital information on its business, financial standing, ownership structure and governance issues. Furthermore, the Company is very scrupulous in seeing that all price-sensitive information and facts are published in a timely manner. The Company also publishes various information beyond the scope of the disclosure duties on its website, and intends to continue its open information policy toward shareholders. The Company strives to provide the shareholders and investors which everything they may need for making qualified decisions regarding the ownership of the Company stock, and in voting at General Meetings. To this end, the Company uses various information channels and instruments: print media (Commercial Bulleting, Hospodářské noviny, annual and half-year reports, etc.), but more importantly the means of electronic communications, especially the Company website. The website (particularly the section About Us) provides investors and shareholders with a broad spectrum of current and historic information about the Company in the Czech and English languages. The Company regards the electronic platform for disseminating information as key, especially since many of its shareholders are international legal and natural persons; the website facilitates access to information about the Company, especially for the international institutional investors and for small shareholders. This in turn improves their opportunities for their active, effective and valid participation in the decisions relating to the matters of the Company.

The policy of transparency dictates that the Company makes sufficient disclosure about the remuneration of members of the Board of Directors and the Supervisory Board of the Company (and of the Supervisory Board committees). This matter is addressed in detail on pages 72–76, which describes and explains the principles of the system for the remuneration of members of the Board of Directors, the Supervisory Board and other persons (with executive powers), and iterates other emoluments provided by the Company to these persons. An account of benefits claimed in the past period is also given there. The Company's website contains the current and previous versions of documents in this area (Rules for Remuneration of Members of the Board of Directors, Rules for Remuneration of Members of the Supervisory Board, Rules for the Granting of Discretionary Benefits to Members of the Supervisory Board). Members of the Board of Directors and of the Supervisory Board are entitled only to emoluments approved by the General Meeting, while the consideration of the adequacy and mechanisms of the remuneration system, and any changes thereto, are in the remit of the Nomination and Remuneration Committee of the Supervisory Board.

In line with its Business Principles, Telefónica O2 practices a zero tolerance of conflicts of interest. The procedures for the consideration and decisions in the governing bodies are aligned in a way that prevents members of the governing bodies from voting on matters which could compromise their impartiality (affiliated transactions). Potential conflicts of interests stemming from membership in the governing bodies of other companies, involvement in commercial transactions and other defined situations are subject to a regular review by the Ethics and Corporate Social Responsibility Committee (see pages 82–83 further below).

The Company is scrupulous about the prevention of insider trading; in this respect, it is compliant with the applicable community and Czech laws, as well as with rules adopted by the UK Financial Services Authority. The Company has adopted a strict internal rule, which sets the limits for the disposal of shares issued by the Company or by undertakings that it controls. Telefónica O2 keeps a regularly updated list of persons (members of governing bodies, employees, external persons) who would qualify as insiders in possession of such information.

The Company has taken measures to accommodate the principal requirements of the Sarbanes-Oxley Act (SOX); the Company is bound to comply with them implicitly, as the stock of the parent Telefónica, S.A., is traded on the US capital markets. Every year, the Company undertakes an audit of internal controls in the system of financial reporting in the scope specified in SOX Section 404, including an assessment of control mechanisms of the Company's information systems that may have a bearing on the financial statements of the Company. The audit performed in 2008 concluded that the internal controls, as applied, were of a standard which meets the SOX requirements. The quarterly declaration of the management (Chief Executive Officer and Vice-President, Finance Division) attesting to the veracity of the information contained in the financial statements, implementation and application of effective internal controls, and other matters required by SOX Section 302 (including the information about any changes in the Company's accounting policy, one-off/extraordinary or material items having an impact on the Company's results for the quarter, and the overview of material reserves created by the Company in order to cover for its contingent risks and liabilities – e.g. from litigation) form an integral part of the SOX compliance procedures in the general area of Corporate Governance. The above documents are presented internally to the Board of Directors and to the Audit and Control Committee for review and discussion.

COMMITTEES ESTABLISHED BY THE GOVERNING BODIES OF THE COMPANY

The Supervisory Board committees have been an integral part of the Company's system of Corporate Governance since 1996 and continue to play a major role in discharging the powers of the Supervisory Board. In the definition of the remit and role of the committees, the Company observes the EC Recommendation on the role of non-executive or supervisory directors of listed companies and on the committees of the (supervisory) board (Recommendation No. 2005/162/EC). An overview of all committees is shown on page 59.

The Audit and Control Committee (ACC) has five members. In April 2008, Jaime Smith Basterra became member (he succeeded Julio Esteban Linares López who resigned on his membership in the Supervisory Board), and in July 2008, Pavel Herštík, previously also a member, was confirmed in his new tenure; he had been re-elected by employees to the Supervisory Board in June 2008. At the end of 2008, the ACC had the following members: Alfonso Alonso Durán, Chairman; Ángel Vilá Boix, Vice-Chairman; Maria Pilar López Álvarez, Jaime Smith Basterra and Pavel Herštík, members. As at the end of 2008, none of the members was a chartered accountant, but all ACC members have the education, additional qualifications, professional orientation or practical experience to duly discharge the office of a member of this key committee. As per the Articles of Association, the ACC is a mandatory committee of the Supervisory Board; it co-operates also with the Board of Directors, the Statutory Auditor and with the organisation unit Internal Audit and Risk Management. It exists primarily to monitor the integrity of financial information provided by the Company, and to monitor and test the internal controlling and risk management systems. The committee is in a direct contact with the External Auditor of the Company, and assesses facts that could compromise its independence or the process of the audit of accounts; the ACC maintains a regular communication with the External Auditor. Some of the primary tasks of the committee include the discussion of audit reports submitted by Internal Audit, and, as per the Charter of Internal Audit, the ACC is obligatorily involved in the preparation and approval of the annual operative audit plan, the approval of the Internal Audit budget and the annual evaluation of Internal Audit performance. Every year, the committee gives a standpoint on the appointment of the External Auditor, and makes recommendations to the Supervisory Board in matters relating to internal and external audit and to the commissioning of the External Auditor's non-audit services for the Company. Through the CG Portal, the ACC members have a continual free access to all current and archive documents, and to all Internal Audit and Risk Management reports. The ACC held five meetings in 2008.

The Nomination and Remuneration Committee (NRC) has five members and is the second mandatory committee of the Supervisory Board. The committee reviews in particular all matters relating to personnel changes in the Board of Directors, the Supervisory Board and the Supervisory Board committees. The committee also gives a standpoint on any nomination proposals for vacancies in the governing bodies of members of the Telefónica O2 Czech Republic Group. The NRC's remit extends to reviewing the remuneration and other benefits granted to members of the Board of Directors and the Supervisory Board. The committee continually monitors and assesses the performance of members of the Board of Directors, the Supervisory Board and its committees; in this context, the NRC also considers the needs for language and professional courses on the part of the members of the governing bodies, and makes the necessary decisions. In 2008, the NRC held three meetings and the personnel changes in the composition of the committee in the covered period directly related to the personnel changes in the composition of the Supervisory Board. At the end of 2008, the NRC had the following composition: Jaime Smith Basterra, Chairman; Alfonso Alonso Durán, Vice-Chairman; Luis Lada Díaz, Guillermo José Fernández Vidal and Anselmo Enriquez Linares, members.

The Ethics and Corporate Social Responsibility Committee (ECSRC) is a voluntary committee of the Supervisory Board with six members. The reduction of the number of ECRSC members (from eight originally to the present six) was the result of the Supervisory Board resolution of July 2008, aimed at improving the efficiency of Corporate Governance, which sought to adjust the number of members in this committee to the parameters common in the mandatory Supervisory Board committees. The rule that a half of the ECSRC's members will be Supervisory Board members elected by the employees, and the other half Supervisory Board members elected by the General Meeting, remained unaffected in the process of the change. Every year, the committee addresses the issue of a potential conflict of interest; members of the Board of Directors, the Supervisory Board and members of the governing bodies in subsidiary companies are examined in this respect. The ECSRC regularly monitors compliance with the Company's Business Principles, and the functioning of the confidential whistle-blowing channel, and it is regularly informed about the activities undertaken as part of the Compliance Programme for the prevention of unethical conduct. Another primary area of interest for the ECSRC is the promotion of Corporate Social Responsibility. The committee held three meetings in 2008. The personnel composition of the ECSRC was influenced by the personnel changes in the composition of the Supervisory Board in 2008 on the one hand, and by the downsizing of the committee's membership. At the end of 2008, the ECSRC had the following composition: Pavel Herštík, Chairman; Dušan Stareček, Vice-Chairman; Jaime Smith Basterra, Tomáš Firbach, Luis Lada Díaz and Guillermo José Fernández Vidal, members.

COMPANY POLICY TOWARD STAKEHOLDERS

Telefónica O2 values Corporate Social Responsibility (CSR) as an integral part of its operations and business. Given the scope and volume of the Company's CSR endeavours, the Annual Report now contains a separate section (03) dedicated to Corporate Social Responsibility.

CONSOLIDATED FINANCIAL STATEMENTS

06

Knowing your limits makes it possible to stretch them further. Where you are is not as important as the direction you are going. It is human nature to innovate.

CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2008

including Notes

CONTENT

GENERAL INFORMATION

Telefónica O2 Czech Republic, a.s. Group (the "Group") consists of Telefónica O2 Czech Republic, a.s. (the "Company") and its subsidiaries: Telefónica O2 Business Solutions, spol s r.o. (formerly Telefónica O2 Services, spol. s r.o.), SPT TELECOM (Czech Republic) Finance B.V., DELTAX Systems a.s., CZECH TELECOM Germany GmbH, CZECH TELECOM Austria GmbH and Telefónica O2 Slovakia, s.r.o.

The Company has a form of a joint stock company and is incorporated and domiciled in the Czech Republic. The address of its registered office is Za Brumlovkou 266/2, Prague 4, 140 22, Czech Republic.

The Group is a member of the Telefónica Group of companies (the "Telefónica Group") with a parent company, Telefónica, S.A. (the "Telefónica").

The Company is the principal supplier of fixed line telecommunication services and is one of the four suppliers of mobile telephone services in the Czech Republic.

The number of employees employed with the Group amounted in average to 9,258 in 2008 (2007: 9,417).

The Company's shares are traded on the Prague Stock Exchange and London Stock Exchange (GDRs).

These consolidated financial statements were approved for issue by the Company's Board of Directors on 20 February 2009.

ACQUISITION OF DELTAX SYSTEMS A.S.

In December 2007, the purchase of 100% of the shares in DELTAX Systems a.s. was approved by the Office for the Protection of Competition. The acquisition was effective as of 1 January 2008. DELTAX Systems a.s. financial results were fully included in the Group financial statements from the effective date.

LIQUIDATION OF SUBSIDIARIES CENTRADE, A.S. IN LIQUIDATION AND SPT TELECOM (CZECH REPUBLIC) FINANCE B.V. IN LIQUIDATION

The liquidation process of CenTrade, a.s. in liquidation was effectively terminated on 30 November 2007. As of 22 August 2008 the registration of the company was cancelled from the Commercial Register. During the fourth quarter of 2007, SPT TELECOM (Czech Republic) Finance B.V. in liquidation commenced preparatory steps for the process of voluntary liquidation. Until the end of 2008, the key legal steps for dissolution of the Company have been executed. As of 9 February 2009 the registration of the company was cancelled from the Commercial Register.

MERGER OF DELTAX SYSTEMS A.S. WITH TELEFÓNICA O2 BUSINESS SOLUTIONS, SPOL. S R.O.

In December 2008, the Board of Directors of the Company approved the plan to merge Telefónica O2 Business Solutions, spol. s r.o. with DELTAX Systems a.s. This merger will become effective 1 January 2009 after the fulfillment of all legal conditions expected to be performed in the first half of 2009. Telefónica O2 Business Solutions, spol. s r.o. will become the legal successor while DELTAX Systems a.s. will be dissolved without liquidation. The assets, rights and obligations including labour rights and duties will be transferred to the successor.

PROVISION OF MOBILE TELECOMMUNICATION SERVICES IN SLOVAKIA

Telefónica O2 Slovakia, s.r.o. (Telefónica O2 Slovakia), a 100% subsidiary company of Telefónica O2 Czech Republic, a.s., was awarded the 3rd mobile license in Slovakia in September 2006.

The license allows Telefónica O2 Slovakia to use frequencies GSM 900 MHz, GSM 1800 MHz, UMTS and FS 29 GHz for the period of 20 years for providing telecommunication services in the Slovak Republic.

The operation in Slovakia is considered as an organic expansion of the Telefónica Group business in the region and is utilizing synergies with the Company operations. The leverage of the Czech operations is expected in areas of network (development, monitoring, support), IT, procurement and back office (finance, HR, legal).

Telefónica O2 Slovakia launched its commercial service in February 2007 offering prepaid voice, SMS (Short Message Service) and GPRS (General Packet Radio Service) data in the GSM (Global System for Mobile communications) spectrum. In September 2007, Telefónica O2 Slovakia launched its postpaid services. In August 2007, Telefónica O2 Slovakia also launched its UMTS (Universal Mobile Telecommunication System) network with a limited coverage.

In 2006, Telefónica O2 Slovakia signed a national roaming agreement with T-Mobile Slovensko, a.s. It provides Telefónica O2 Slovakia with the ability to offer full network coverage to its customers immediately from commercial launch even before the construction of its own network is finished. The strategy of the Telefónica O2 Slovakia is to build own network coverage in areas where it is economically feasible.

The top priority of Telefónica O2 Slovakia has been a gradual fulfilment of the license conditions, gaining a base of active customers and aiming to provide the telecommunications market with innovations and technological advances as the first company on the market.

By the end of the year 2008, Telefónica O2 Slovakia had more than 455 thousand registered customers and put in operation more than 850 BTS and thus fulfilled the licence conditions as at 31 December 2008.

INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF TELEFÓNICA O2 CZECH REPUBLIC, a.s.

We have audited the accompanying consolidated financial statements of Telefónica O2 Czech Republic, a.s. and its subsidiaries (the Group), which comprise the consolidated balance sheet as at 31 December 2008 and the consolidated income statement, consolidated statement of changes in equity and consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

MANAGEMENT'S RESPONSIBILITY FOR THE FINANCIAL STATEMENTS

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards as adoptedby the European Union. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

AUDITOR'S RESPONSIBILITY

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing and implementation guidance of the Chamber of Auditors of the Czech Republic. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

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

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

OPINION

In our opinion, the consolidated financial statements give a true and fair view of the financial position of the Group as of 31 December 2008, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union.

Ernst & Young

Ernst & Young Audit s.r.o.
Licence No. 401
Represented by

Brian Welsh
Partner

Radek Pav
Auditor, Licence No. 2042

20 February 2009
Prague, Czech Republic

CONSOLIDATED INCOME STATEMENT

For the year ended 31 December 2008

In CZK million	Notes	Year ended 31 December 2008	Year ended 31 December 2007
Revenue	2	64,709	63,196
Gains from sale of non-current assets	8	855	42
Internal expenses capitalized in fixed assets	2	484	553
Operating expenses	3	(37,650)	(35,753)
Impairment loss	8, 9, 10	(86)	(5)
Depreciation and amortisation	8, 9	(12,932)	(14,435)
Operating profit		15,380	13,598
Interest income	4	449	403
Interest expense	4	(406)	(446)
Other finance expense (net)	4	(75)	(45)
Profit before income tax		15,348	13,510
Taxes on income	5	(3,720)	(3,124)
Profit for the year		11,628	10,386
Attributable to:			
Equity holders of the Company	6	11,628	10,386
Minority interest		–	–
Earnings per share (CZK) – basic*	6	36	32

* There is no dilution of earnings as no convertible instruments have been issued by the Company.

CONSOLIDATED BALANCE SHEET

As at 31 December 2008

In CZK million	Notes	31 December 2008	31 December 2007
ASSETS			
Property, plant and equipment	8	63,429	71,809
Intangible assets	9	22,348	21,805
Investment in associate	27	11	11
Other financial assets	12	378	566
Non-current assets		86,166	94,191
Inventories	11	779	853
Receivables and prepayments	12	9,240	8,577
Income tax receivable		226	–
Held-to-maturity investments	13	–	27
Cash and cash equivalents	14	7,116	9,576
Current assets		17,361	19,033
Non-current assets classified as held for sale	8	96	328
Total assets		103,623	113,552
EQUITY AND LIABILITIES			
Ordinary shares	24	32,209	32,209
Share premium		24,374	30,816
Retained earnings, funds and reserves		21,585	19,767
		78,168	82,792
Minority interest		–	–
Total equity		78,168	82,792
Long-term financial debts	16	3,098	3,062
Deferred taxes	17	3,300	3,353
Non-current provisions for liabilities and charges	19	403	2,150
Non-current other liabilities	15	176	452
Non-current liabilities		6,977	9,017
Short-term financial debts	16	98	6,207
Trade and other payables	15	17,686	13,765
Income tax liability		9	870
Provisions for liabilities and charges	19	685	901
Current liabilities		18,478	21,743
Total liabilities		25,455	30,760
Total equity and liabilities		103,623	113,552

These consolidated financial statements were approved by the Board of Directors on 20 February 2009 and were signed on its behalf by:

Salvador Anglada Gonzales
Chairman of the Board of Directors
and Chief Executive Officer

Jesus Pérez de Uriguen
Member of the Board of Directors
and Chief Financial Officer

CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

For the year ended 31 December 2008

In CZK million	Notes	Share capital	Share premium	Hedging reserve	Foreign exchange translation reserve	Equity settled share based payments reserve	Funds*	Retained earnings	Total
At 1 January 2007		32,209	30,816	(18)	(12)	–	6,270	19,216	88,481
Fair value gains (net of tax) – cash flow hedges		–	–	(2)	–	–	–	–	(2)
Currency translation differences – amount arising in year		–	–	–	21	–	–	–	21
Changes in statutory reserves and other movements		–	–	–	–	–	182	(172)	10
Net income and expense recognised directly in equity		–	–	(2)	21	–	182	(172)	29
Net profit		–	–	–	–	–	–	10,386	10,386
Total income and expense for the year		–	–	(2)	21	–	182	10,214	10,415
Dividends declared in 2007	7	–	–	–	–	–	–	(16,104)	(16,104)
At 31 December 2007		32,209	30,816	(20)	9	–	6,452	13,326	82,792
At 1 January 2008		32,209	30,816	(20)	9	–	6,452	13,326	82,792
Fair value gains (net of tax) – cash flow hedges		–	–	20	–	–	–	–	20
Currency translation differences – amount arising in year		–	–	–	(215)	–	–	–	(215)
Net income and expense recognised directly in equity		–	–	20	(215)	–	–	–	(195)
Net profit		–	–	–	–	–	–	11,628	11,628
Total income and expense for the year		–	–	20	(215)	–	–	11,628	11,433
Equity restructuring	24	–	(6,442)	–	–	–	6,442	–	–
Transfer from reserve fund to retained earnings	24	–	–	–	–	–	(6,442)	6,442	–
Capital contribution		–	–	–	–	47	–	–	47
Dividends declared in 2008	7	–	–	–	–	–	–	(16,104)	(16,104)
At 31 December 2008		32,209	24,374	–	(206)	47	6,452	15,292	78,168

* Refer Note 24 regarding amounts not available for distribution.

CONSOLIDATED MOVEMENT OF GAINS AND LOSSES RECOGNISED IN EQUITY

In CZK million	Gains/(losses) proceeding from cash flow hedges	Translation differences	Tax effect	Total
At 1 January 2007	**(22)**	**(12)**	**4**	**(30)**
Gains/(losses) arisen in the fiscal year	(17)	21	–	4
Gains/(losses) re-classified to the profit and loss account	15	–	–	15
At 31 December 2007	**(24)**	**9**	**4**	**(11)**
Gains/(losses) arisen in the fiscal year	(52)	(215)	(4)	(271)
Gains/(losses) re-classified to the profit and loss account	76	–	–	76
At 31 December 2008	**–**	**(206)**	**–**	**(206)**

CONSOLIDATED CASH FLOW STATEMENT

For the year ended 31 December 2008

In CZK million	Notes	Year ended 31 December 2008	Year ended 31 December 2007
Net profit		11,628	10,386
Non-cash adjustments for:			
Income tax	5	3,720	3,124
Depreciation	8	10,994	12,563
Amortisation	9	1,938	1,872
Impairment loss	8, 9, 10	86	5
Disposals of obsolete assets		114	36
Profit on sale of property, plant and equipment		(840)	(51)
Net interest and other charges		(45)	42
Foreign exchange gains (net)		(239)	(123)
Fair value changes		(15)	–
Change in provisions and allowances		(828)	(641)
Operating cash flow before working capital changes		26,513	27,213
Working capital adjustments:			
Increase in trade and other receivables		(731)	(218)
Increase in inventories		(275)	(104)
Increase in trade and other payables		1,314	1,143
Cash flows from operating activities		26,821	28,034
Interest paid		(487)	(432)
Interest received		367	375
Income tax paid		(4,859)	(4,078)
Net cash from operating activities		21,842	23,899
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchase of property, plant and equipment		(4,695)	(4,060)
Purchase of intangible assets		(2,221)	(1,594)
Proceeds from sales of property, plant and equipment		4,586	74
Proceeds from marketable securities		24	53
Cash purchase of financial investments		(30)	(176)
Cash acquired from purchase of financial investments		107	–
Dividends received		2	2
Net cash used in investing activities		(2,227)	(5,701)
CASH FLOWS FROM FINANCING ACTIVITIES			
Proceeds from borrowings		650	–
Repayment of borrowings		(6,645)	–
Dividends – paid		(16,080)	(16,083)
Net cash used in financing activities		(22,075)	(16,083)
Net (decrease) / increase in cash and cash equivalents		(2,460)	2,115
Cash and cash equivalents at beginning of year		9,576	7,461
Cash and cash equivalents at the year end	14	7,116	9,576

ACCOUNTING POLICIES

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A) BASIS OF PREPARATION

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all years presented, unless otherwise stated.

The consolidated financial statements were prepared in accordance with International Financial Reporting Standards ("IFRS") and all applicable IFRSs adopted by the EU. IFRS comprise standards and interpretations approved by the International Accounting Standards Board ("IASB") and the International Financial Reporting Interpretations Committee ("IFRIC").

Effective from 1 January 2005, a change in the Czech Act on Accounting No. 563/1991 Coll. requires the Group to prepare its consolidated financial statements in accordance with IFRS adopted by the EU (Regulation (EC) No 1606/2002). At the year-end, there is no difference in the policies applied by the Group between IFRS and IFRS adopted by the EU.

The consolidated financial statements were prepared under the historical cost convention except for non-current assets held for sale, inventory held at net realizable value, financial derivatives, share based payment liability and certain assets and liabilities acquired during business combinations, as disclosed in the accounting policies below.

The preparation of financial statements in conformity with IFRS required the Group to use certain critical accounting estimates. It also required management to exercise its judgement in the process of applying the Group's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note T.

The amounts shown in these consolidated financial statements are presented in millions Czech Crowns ("CZK"), if not stated otherwise.

ADOPTION OF NEW OR REVISED IFRS STANDARDS AND INTERPRETATIONS (INCLUDES STANDARDS AND INTERPRETATIONS APPLICABLE FOR THE GROUP)

In 2008, the Group applied the below stated interpretation and amendment, which are relevant to its operations. Adoption of the interpretation and amendment did not have any effect on the financial performance or position of the Group:

IFRIC 11 IFRS 2 Group and Treasury Share Transactions (issued 2005, effective date 1 March 2007)

The interpretation provides guidance on whether share-based transactions involving treasury shares or involving group entities (for example, options over parents' shares) should be accounted for as equity-settled or cash-settled share-based payment transactions in the stand-alone financial statements of the parent and group companies. This interpretation does not have an impact on the Group's financial statements.

STANDARDS AND INTERPRETATIONS ISSUED AND ENDORSED BY THE EUROPEAN UNION BUT NOT EARLY ADOPTED BY THE GROUP (INCLUDES STANDARDS AND INTERPRETATIONS APPLICABLE FOR THE GROUP)

IFRS 8 Operating Segments (issued 2006, effective date 1 January 2009)

The standard will replace IAS 14 Segment Reporting and requires entities to disclose segment information based on the information reviewed by the entity's chief operating decision maker. The adoption of the standard will not change the current presentation of segment information.

IAS 1 Amendment (issued 2007, effective date 1 January 2009) Presentation of financial statements, Comprehensive revision including requiring a statement of comprehensive income

The amendment to the standard separates owner and non-owner changes in equity. In addition, the standard introduces a statement of comprehensive income. The Group does not expect any material effect on the Balance Sheet and the Income Statement relating to the adoption of this standard from the effective date 1 January 2009. This adoption will affect certain disclosures in the notes to the consolidated financial statements.

IAS 23 Amendment (issued 2007, effective date 1 January 2009) Borrowing Costs

The amendment requires the Group to capitalise borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset. Since the Group has already applied this policy as an allowed alternative treatment before, no impact is expected on the financial position of the Group.

IFRIC 13 Customer Loyalty Programmes (issued 2007, effective date 1 July 2008)

This interpretation addresses the accounting by entities that provide their customers with incentives to buy goods or services by providing awards as part of the sale transaction. The interpretation requires the entity that grants the awards to account for the sales transaction that gives rise to the award credits as a multiple element transaction and allocate the fair value of the consideration received or receivable between the award credits granted and the other components of the revenue transaction.

This adoption will affect current accounting policy in respect of change of the fair value awards measurement and change in the presentation in the financial statements. This will also affect certain disclosures in the notes to the consolidated financial statements. This adoption will not have material impact on the financial results in 2009.

IFRS 2 Amendment (issued 2008, effective date 1 January 2009) Share-based Payments

The amendment clarifies the definition of a vesting condition and prescribes the treatment for an award that is cancelled. The group will apply IFRS 2 (Amendment) from 1 January 2009. This amendment will not have a material impact on the Group's financial statements.

STANDARDS AND INTERPRETATIONS ISSUED BUT NOT ENDORSED BY THE EUROPEAN UNION AND NEITHER EARLY ADOPTED BY THE GROUP NOR EFFECTIVE (INCLUDES STANDARDS AND INTERPRETATIONS APPLICABLE FOR THE GROUP)

Revised IFRS 3 Business Combinations (issued 2008, effective date 1 July 2009)

The standard introduces changes in the accounting for business combination that will impact the amount of goodwill recognised, the reported results in the period that an acquisition occurs and future reported results. The Group will apply IFRS 3 (Revised) prospectively to all business combinations from 1 January 2010.

IAS 27 Consolidated and Separate Financial Statements – Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate – Amendments (issued 2008, effective date 1 January 2009)

IAS 27 is amended for the following changes in respect of the holding companies separate financial statements:

i) The deletion of the "cost method". Making the distinction between pre-and post- acquisition profits is no longer required. All dividends will be recognized in profit or loss. However, the payment of such dividends requires the entity to consider whether there is an indicator of impairment; and
ii) In case of reorganisations where a new parent is inserted above an existing parent of the group (subject to meeting specific requirements), the cost of the subsidiary is the previous carrying amount of its share of equity items in the subsidiary rather than its fair value.

The Group does not expect any material effect relating to the adoption of these amendments.

IAS 27 Consolidated and Separate Financial Statements – Amendment (issued 2008, effective date 1 July 2009)

The most significant changes to IAS 27 are as follows:

i) Change in ownership interests of a subsidiary (that do not result in a loss of control) will be accounted for as an equity transaction and will have no impact on goodwill nor will it give a rise to a gain or loss.
ii) Losses incurred by the subsidiary will be allocated between the controlling and non-controlling interests (previously referred to as "minority interests"); even if the losses exceed the non-controlling equity investment in a subsidiary.
iii) On loss of control of a subsidiary, any retained interest will be remeasured to fair value and this will impact the gain or loss recognized on disposal.

The Group does not expect any material effect relating to the adoption of this amendment.

IFRS 5 Amendment (issued 2008, effective date 1 July 2009) Non-current Assets Held for Sale and Discontinued Operations

The amendment clarifies that all of subsidiary's assets and liabilities are classified as held for sale if a partial disposal sale plan results in loss of control. Relevant disclosure should be made for this subsidiary, if the definition of a discontinued operation is met. A consequential amendment to IFRS 1 states that these amendments are applied prospectively from the date of transition to IFRS. The Group will apply the IFRS 5 (Amendment) prospectively to all partial disposals of subsidiaries from 1 January 2010.

IAS 36 Amendment (issued 2008, effective date 1 January 2009) Impairment of Assets

Where fair value less costs to sell is calculated on the basis of discounted cash flows, disclosures equivalent to those for value-in-use calculation should be made. The Group will apply the IAS 36 (Amendment) and provide the required disclosure where applicable for impairment tests from 1 January 2009.

The Group does not intend to early adopt any of those standards and interpretations before their effective dates.

B) GROUP ACCOUNTING

CONSOLIDATION
Subsidiary undertakings, which are those companies in which the Company, directly or indirectly, has an interest of more than one half of the voting rights or otherwise has power to exercise control over the operations, have been consolidated. Subsidiaries are consolidated from the date on which control is transferred to the Group and are no longer consolidated from the date when the Group ceases to have control.

A business combination is accounted for using the purchase method of accounting. An acquisition is accounted for at its cost, being the amount of cash and cash equivalents paid in exchange for control over the net assets of an acquired company, plus any costs directly attributable to the acquisition. The excess of the cost of acquisition over the fair value of the net assets of the subsidiary acquired is recorded as goodwill. For detail refer to Note E Intangible assets and also Note 9.

Intercompany transactions and balances between the Group companies are eliminated unless the transaction provides evidence of an impairment of the asset transferred. The accounting policies for subsidiaries are changed, where necessary, to ensure consistency with the policies adopted by the Group and another companies within the Group.

Intercompany transactions and balances between the Group and Telefónica companies for the period after the transfer of majority ownership to Telefónica, S.A. are not eliminated. They are identified, disclosed and measured for the disclosure purposes and elimination procedures of the majority shareholder – Telefónica, S.A.

The ultimate parent company of the Telefónica O2 Czech Republic, a.s. Group is Telefónica, S.A.

C) FOREIGN CURRENCIES

i) Functional and presentation currency
Items included in the financial statements of each entity in the Group are measured using the currency of the primary economic environment in which the entity operates ("the functional currency"). The consolidated financial statements are presented in Czech Crowns ("CZK"), which is the Group's presentation currency.

ii) Transactions and balances
Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the date of the transaction. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement, except when deferred in equity as qualifying cash flow hedges. Such balances of monetary items are translated at period-end exchange rates. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Non-monetary items that are measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

iii) Group companies
The income and cash flow statements of foreign entities are translated into the Group's reporting currency at the average exchange rates for the year and their balance sheets are translated at the exchange rates ruling on 31 December. Exchange differences arising from the translation of the net investment in foreign entities and of borrowings and other currency instruments designated as hedges of such investments are taken to shareholders' equity. When a foreign entity is sold, such exchange differences are recognised in the income statement as part of the gain or loss on sale.

D) PROPERTY, PLANT AND EQUIPMENT

All property, plant and equipment are initially recorded at cost and, except for freehold land, are subsequently carried at its cost less any accumulated depreciation and accumulated impairment losses. Freehold land is subsequently stated at cost less impairment charges.

Property, plant and equipment acquired in business combinations are stated at their acquisition costs (which are equal to their fair value at the date of acquisition) less depreciation and impairment charges.

Property, plant and equipment include all costs directly attributable to bringing the asset to working condition for its intended use. With respect to the construction of the network, this comprises every expenditure up to the customers' premises, including the cost of contractors, materials, direct labour costs and interest cost incurred during the course of construction.

Repairs and maintenance costs are expensed as incurred.

Items of property, plant and equipment that are retired are not intended for sale and are not expected to create any future economic benefits or are otherwise disposed of, are eliminated from the balance sheet, along with the corresponding accumulated depreciation. Any gain or loss arising from retirement or disposal is included in net operating income, i.e. net gain or loss is determined as the difference between the net disposal proceeds, if any, and the carrying amount of the item.

Items of property, plant and equipment, excluding freehold land, are depreciated from the time they are available for use, using the straight-line method. Depreciation ceases at the earlier of the date the asset is de-recognised or the date the asset is classified as held for sale.

Depreciation does not cease, when the asset becomes temporarily idle or retired from active use, unless the asset is fully depreciated.

Estimated useful lives adopted in these consolidated financial statements are as follows:

	Years
Freehold buildings	up to 40
Cable and other related plant	5 to 25
Exchanges and related equipment	up to 10
Other fixed assets	2 to 10

Freehold land is not depreciated as it is deemed to have an indefinite life.

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

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater then its estimated recoverable amount (refer to Note G Impairment of assets).

E) INTANGIBLE ASSETS

Intangible assets include computer software, purchased goodwill, licenses, trade names, customer base and roaming contracts. Computer software mainly represents the external acquisition costs of the Group's information systems that are intended for use within the Group. Generally, costs associated with developing or maintaining computer software programs are recognised as an expense as incurred. However, costs that are directly associated with identifiable and unique software products controlled by the Group and that have a probable economic benefit exceeding the cost beyond one year, are recognised as intangible assets. Computer software costs recognised as assets are amortised using the straight-line method over their useful lives, generally one to five years.

Intangible assets acquired in business combinations are stated at their acquisition costs (which are equal to their fair value at the date of acquisition) less amortisation and impairment charges and are amortised on a straight-line basis over their estimated useful lives. Customer bases are amortised over a period of the remaining average terms of the binding contracts.

Acquired licenses are recorded at cost and amortised on a straight-line basis over the remaining life of the license (i.e. over 15 to 20 years), from the start of commercial service, which best reflects the pattern by which the economic benefits of the intangible assets will be utilised by the Group.

Intangible assets with an indefinite useful life are not amortised. They are subject to the regular impairment reviews (see Note 9 and Note 10).

Goodwill, arising from the purchase of subsidiary undertakings and interests in associates and joint ventures, represents the excess of the fair value of the purchase consideration over the fair value of the net assets acquired. Goodwill is not amortised but is tested for impairment at least annually or anytime there are indications of a decrease in its value.

The Group reviews at least at the balance sheet date the useful lives of intangible assets that are not amortised to determine whether events and circumstances continue to support an indefinite useful life assessment for that asset. If they do not, the change in the useful life assessment from indefinite to finite is accounted for as a change in an accounting estimate.

On the balance sheet date, carrying amounts, residual values and the useful lives of assets are reviewed, revised and if necessary prospectively amended and accounted for as a change in an accounting estimate.

Intangible assets that are no longer in use and no future economic benefits are expected or that are disposed of for any other reason are de-recognised from the balance sheet together with the corresponding accumulated amortisation (for amortised assets only). All gains or losses arising in this respect are recognised in net operating income, i.e. net gain or loss is determined as the difference between net disposal proceeds, if any, and the carrying amount of the asset.

Intangible assets, with the exception of assets with an indefinite useful life, are amortised using the straight-line method from the time they are available for use. Amortisation ceases at the earlier of the date the asset is de-recognised, the date the asset is classified as having the indefinite useful life or the date the asset is classified as held for sale.

F) NON-CURRENT ASSETS CLASSIFIED AS HELD FOR SALE

The Group classifies separately in the balance sheet a non-current asset (or disposal group) as held for sale if its carrying amount will be recovered principally through a sale transaction rather than through continuing use. For this to be the case, the asset (or disposal group) is available for immediate sale in its present condition subject only to terms that are usual and customary for sales of such assets (or disposal groups), its sale is highly probable and sale is expected within one year.

The Group measures a non-current asset (or disposal group) classified as held for sale at the lower of its carrying amount and fair value less costs to sell.

The Group recognizes an impairment loss for any initial or subsequent write-down of the asset (or disposal group) to fair value less costs to sell and is accounted for as an impairment loss with impact in the income statement of the relevant period.

From the moment the asset is classified as held for sale and eventually revalued, it ceases to be depreciated/amortised and impairment is only being determined.

Any gain from any subsequent increase in fair value less costs to sell, but not in excess of the cumulative impairment loss that has been recognized, is determined and is accounted for in the income statement.

G) IMPAIRMENT OF ASSETS

Property, plant and equipment and other assets, including goodwill and intangible assets, are reviewed for impairment losses whenever events or changes in circumstances indicate that the carrying amount may not be recoverable or at least on an annual basis for goodwill and for intangibles with an indefinite useful life and for intangibles not yet in use. An impairment loss is recognised for the amount by which the carrying amount of the asset exceeds its recoverable amount, which is the higher of an asset's net selling price and value in use. For the purposes of assessing impairment, assets are grouped at the lowest level, for which there are separately identifiable cash flows (cash-generating units).

Impairment losses are recognised in expenses when incurred. A previously recognised impairment loss is reversed (except for the Goodwill impairment loss) only if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognised. If that is the case the carrying amount of the asset is increased to its recoverable amount. That increased amount cannot exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognised for the asset in prior years. Such reversal is recognised as a reduction in the expenses in the period in which the reversal occurs.

H) INVESTMENTS AND OTHER FINANCIAL ASSETS

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

Financial assets that are acquired principally for the purpose of generating a profit from short-term fluctuations in price are classified as financial assets at fair value through profit or loss and are included in current assets. During 2008 and 2007, the Group did not hold any financial assets in this category.

Investments with a fixed maturity that management has the intent and ability to hold to maturity are classified as held-to-maturity and are disclosed as current or non-current assets, depending on the period in which the settlement will take place.

Loans and receivables are financial assets with fixed or determinable payments that are not quoted in an active market and are measured at amortised cost using an effective interest rate method and are disclosed as current or non-current assets, depending on the period in which the settlement will take place.

Investments intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, are classified as available-for-sale; these are included in non-current assets unless management has expressed the intention of holding the investment for less than 12 months from the balance sheet date or unless they will need to be sold to raise operating capital, in which case they are included in current assets.

Management determines the appropriate classification of its investments at the time of the purchase and re-evaluates such designation on a regular basis, as required under IAS 39.

All purchases and sales of investments are recognised on the trade date, which is the date that the Group commits to purchase or sell the asset. The cost of purchase includes all transaction costs. Financial assets at fair value through profit or loss and available-for-sale investments are subsequently carried at fair value, whilst held-to-maturity investments are carried at amortised cost using the effective interest rate method. Realised and unrealised gains and losses arising from changes in the fair value of financial assets at fair value through profit or loss are included in the income statement in the period in which they arise. On the contrary, unrealised gains and losses arising from changes in the fair value of available-for-sale investments are included in equity in the period in which they arise, except for impairment losses, until the financial asset is de-recognised, at which time the cumulative gain or loss previously recognised in equity is recognised in the income statement.

IMPAIRMENT OF FINANCIAL ASSETS

The Group assesses at each balance sheet date whether financial assets or groups of financial assets are impaired.

1) Assets carried at amortized costs

If there is objective evidence that an impairment loss on loans and receivables or held to maturity investments carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced either directly or through use of an allowance account. The amount of the loss is recognised in the income statement.

The Group first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. If it is determined that no objective evidence of impairment exists for individually assessed financial assets, whether significant or not, it is included in a group of financial assets with similar credit risk characteristics and that group of financial assets is collectively assessed for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed. Any subsequent reversal of an impairment loss is recognised in the income statement and only to the extent that the carrying amount of the financial asset does not exceed its amortised cost at the reversal date.

In relation to trade receivables, a provision for impairment is made when there is objective evidence (such as the probability of insolvency) that the Group will not be able to collect all of the amounts due under the original terms of the invoice. The carrying amount of the receivable is reduced through use of an allowance account. Impaired debts are derecognised when they are assessed as uncollectible or sold.

2) Available-for-sale financial assets
If this asset is impaired, the cumulative loss that had been previously recognised (due to fair value revaluation) directly in equity shall be removed from equity and recognised in profit or loss even though the financial asset has not been derecognised.

The amount of the cumulative loss that is removed from equity and recognised in profit or loss shall be the difference between the acquisition cost (net of any principal repayment and amortisation) and the current fair value, less any impairment loss previously recognised in profit or loss.

Reversals of impairment losses on debt instruments are reversed through profit or loss, if the increase in fair value of the instrument can be objectively related to an event occurring after the impairment loss was recognised in the income statement.

DE-RECOGNITION OF FINANCIAL ASSETS

A financial asset is de-recognised when:

i) the rights to receive cash flow from the asset have expired,
ii) the Group retains the right to receive cash flow from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a "pass-through" arrangement, or
iii) the Group has transferred its rights to receive cash flows from the assets and either has transferred substantially all the risks and rewards of the asset, or has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

I) LEASES

The determination of whether an arrangement is, or contains a lease is based on the substance of the arrangement at inception date of whether the fulfilment of the arrangement is dependent on the use of specific asset or assets and the arrangement conveys a right to use the assets.

Leases under which a significant portion of the risks and benefits of ownership are effectively retained by the lessor are classified as operating leases. Payments made under operating leases are charged to the income statement on a straight-line basis over the period of the lease.

When an operating lease is terminated before the lease period has expired, any payment that is required to be made to the lessor by way of penalty is recognised as an expense in the period in which termination takes place.

Leases of property, plant and equipment where the Group bears substantially all the risks and rewards of ownership are classified as finance leases. Finance leases are capitalized at the inception of the lease at the lower of the fair value of the leased property or the present value of the minimum lease payments. Each lease payment is allocated between the liability and finance charges so as to achieve a constant rate on the finance balance outstanding. The corresponding lease obligations, net of finance charges, are included in other long-term payables (depending on maturity).

The interest element of the finance cost is charged to the income statement over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period. If there is a reasonable certainty that the lessee will obtain ownership by the end of the lease term, the period of expected use is the useful life of the asset; otherwise the property, plant and equipment acquired under finance leases are depreciated over the shorter of the useful life of the asset or the lease term.

A sale and lease back transaction involves the sale of an asset and the leasing back of the asset. Within the Group's operations the selling price of the asset and lease payments are independent and established at fair value. Therefore the gain from the sale of the asset and the lease payments are accounted as two separate transactions

J) INVENTORIES

Inventory is stated at the lower of cost or net realisable value. Costs of inventories include the purchase price and related costs of acquisition (transport, customs duties and insurance). The cost of inventory is determined using weighted average cost. Net realisable value is the estimate of the selling price in the ordinary course of business, less the costs of completion and selling expenses.

K) TRADE RECEIVABLES

Trade receivables are carried at original invoice amount less allowance for impairment of these receivables. Such allowance for impairment of trade receivables is established if there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of receivables. The amount of the allowance is the difference between the carrying amount and the recoverable amount, being the present value of expected cash flows, discounted at the initial market rate of interest for similar borrowers. Cash flows relating to short-term receivables are usually not discounted. The amount of the allowance is recognized in the income statement.

L) CASH AND CASH EQUIVALENTS

Cash and cash equivalents are carried in the balance sheet at cost. For the purposes of the cash flow statement, cash and cash equivalents comprise cash on hand, deposits held at call with banks, other short-term highly liquid investments with original maturities of three months or less, and bank overdrafts. Bank overdrafts are shown within borrowings in current liabilities on the balance sheet.

M) FINANCIAL DEBT

Borrowings are recognised initially at the proceeds received, net of transaction costs incurred. In subsequent periods, borrowings are stated at amortised cost using the effective interest rate method; any difference between proceeds (net of transaction costs) and the redemption value is recognised in the income statement over the period of the borrowings.

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

Interest costs on borrowings used to finance the acquisition and construction of qualifying assets are capitalized during the period of time that is required to complete and prepare the asset for its intended use. Other borrowing costs are expensed.

N) CURRENT AND DEFERRED INCOME TAXES

Taxation expense represents both current and deferred taxation, where appropriate.

Current income tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted by the balance sheet date in the relevant country.

Current income tax relating to items recognised directly in equity is recognised in equity and not in the income statement.

Deferred income taxation is calculated using the liability method applied to all temporary differences arising between the tax basis of assets and liabilities and their carrying values for financial reporting purposes. Currently enacted tax rates and laws expected to apply when the asset is realised or the liability is settled are used to determine the deferred income tax.

The principal temporary differences arise from differences in the tax and accounting values of property, plant and equipment, impairment of receivables and allowance for obsolete and slow moving inventories, non tax deductible allowances and provisions, unused tax credits and, in relation to acquisitions, on the difference between the fair values of the net assets acquired and their tax base.

Deferred income tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

The Group accounts for the tax consequences of transactions and other events in the same way that it accounts for the transactions and other events themselves. Thus, for transactions and other events recognised in the income statement, any related tax effects are also recognised in the income statement. For transactions and other events recognised directly in equity, any related tax effects are also recognised directly in equity. Similarly, the recognition of deferred tax assets and liabilities in a business combination affects the amount of goodwill.

Deferred income tax assets and tax liabilities are offset, if a legally enforceable right exists to set off current tax assets against current income tax liabilities and the deferred income taxes relate to the same taxable entity and the same taxation authority. The same applies for offsetting of current tax assets and liabilities.

O) EMPLOYEE BENEFITS

1) Pension obligations
Contributions are made to the Government's health, retirement benefit and unemployment schemes at the statutory rates applicable during the period and are based on gross salary payments. The arrangements of the Government's health, retirement benefit and unemployment schemes correspond to the arrangements for defined contribution plans. The Group has no further payment obligations once the contributions have been paid. The expense for the contributions is charged to the income statement in the same period as the related salary expense. The Group also makes contributions to defined contribution schemes operated by external pension companies. These contributions are charged to the income statement in the period to which the contributions relate.

2) Redundancy and termination benefits
Redundancy and termination benefits are payable when employment is terminated before the normal retirement or contract expiry date. The Group recognises redundancy and termination benefits when it is demonstrably committed to terminate the employment of current employees according to a detailed formal plan without possibility of withdrawal. Benefits falling due more than 12 months after the balance sheet date are discounted to present value. There are no redundancy and termination benefits falling due more than 12 months after the balance sheet date.

3) Bonus plans
The Group recognises a liability for bonuses based on a formula that takes into consideration certain performance related measures, such as turnover or free cash flow, after certain adjustments. The Group recognises a provision where the Group is contractually obliged or where there is a past practice that has created a constructive obligation.

P) SHARE-BASED COMPENSATION

During 2006, the Group introduced performance compensation systems linked to the market value of shares of the parent company, Telefónica, S.A. Certain compensation plans are settled in cash, while the others are settled via the delivery of shares.

IFRS 2 is applied to compensation schemes linked to the share price with the following accounting treatment:
Option plans that can be cash-settled or equity-settled at the option of the employee are recognized at the fair value on the grant date of the liability and equity components of the compound instrument granted.

In the cash-settled share option plan, the total cost of the rights to shares granted are expensed over the period during which the beneficiary earns the full right to exercise the options (vesting period). The total cost of the options is initially measured based on their fair value at the grant date calculated by the Black-Scholes option pricing model, taking into account the terms and conditions established in each share option plan. At each subsequent reporting date, the Group revises its estimate of fair value and the number of options it expects to vest, booking any change in the liability through the income statement for the period, if appropriate.

For the equity-settled share option plan, fair value at the grant date is measured using the binominal methodology. These plans are expensed during the vesting period with a credit to equity. At each subsequent reporting date, the Group revises its estimate of the number of options it expects to be exercised, with a corresponding adjustment to equity. As the plan will be settled by a physical delivery of equity instruments of the parent, Telefónica, S.A., to the employees, the personnel expense accrued is recognised against equity.

Q) PROVISIONS

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and a reliable estimate of the amount can be made. Where the Group expects a provision to be reimbursed, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain.

R) REVENUE RECOGNITION

Revenue, shown net of Value Added Tax and any discounts, and after eliminating sales within the Group, comprises goods sold and services provided. Revenues are measured at their fair value of the consideration received or receivable. The amount of revenue is recognised if it can be measured reliably and it is probable that the economic benefits associated with the transaction will flow to the Group. If necessary, revenue is split into separately identifiable components.

The Group offers customers free minutes for a selected price based on a chosen customer plan. Free unused minutes at the end of the month might be rolled over to the following month. The Company is not obliged to reimburse the customer for unused minutes and the option of rolling over any unused minutes is valid for only one month.

The Group recognises revenue for free minutes in the period when the related services are provided and consumed, if material. Any rollover minutes are deferred and recognised when the minutes are used or the option expires.

In assessing whether revenue should be recognised gross, i.e. with separate disclosure of costs to arrive at gross profit, or on a net basis, the Group considers these indicators of gross revenue reporting:

a) the Group is the primary obligor in the arrangement,
b) the Group has general inventory risk,
c) the Group has price latitude,
d) the Group changes the product or performs part of the service,
e) the Group has discretion in supplier selection,
f) the Group is involved in the determination of product or service specifications,
g) the Group has credit risk,
h) the Group has the ability to set the terms of the transaction,
i) the Group has the managerial control over the transaction.

The relative strength of each indicator is considered when concluding which accounting treatment to use for principal/agency arrangement.

If a transaction is considered to meet conditions of an agency arrangement, the revenue is recognised only at the amount of the commission received/realised, e.g. premium rate lines.

Revenue from fixed price construction contracts (long-term contracts) is recognised on the percentage of completion method, measured by reference to the percentage of actual cost incurred to date to estimated total costs of the contract. An expected loss on the construction contract is recognised as an expense immediately, when it is probable that total contract costs will exceed total contract revenue.

1) FIXED LINE BUSINESS REVENUES
Revenue is recognized as follows:

DOMESTIC AND INTERNATIONAL CALL REVENUES
Domestic and international call revenues are recognised in the income statement at the time the call is made.

UNIVERSAL SERVICE
The Group is obliged to render certain fixed line telephony services defined by the Act on Electronic Communications. The Group follows the accounting policy of Telefónica Group and recognises the compensation of revenues attributable to the Group using the gross principle as well as recognises the compensation when CTO approves the total compensation and decides about percentage shares and absolute amounts of other operators contributions.

SUBSCRIPTION REVENUES
Revenue is recognised in the income statement in the period in which the services are rendered.

REVENUES FROM SALES OF PREPAID CARDS
Prepaid call card sales are deferred until the customer uses the stored value on the card to pay for the relevant calls. The expiry date for prepaid cards is not longer than 36 months.

CONNECTION FEES
Connection fees, arising from the connection of the customers to the Company's network, are deferred and recognised in the income statement over the estimated average customer relationship period on the basis of the degressive accounting method.

EQUIPMENT SALES AND OTHER SALE OF GOODS
Revenue from the sale of telephone equipment and accessories and other sale of goods is recognised at the time of sale i.e. when the Group has transferred to the buyer the significant risks and rewards of ownership of the goods.

LOCAL LOOP UNBUNDLING
Revenue from access to the local loop unbundling is deferred in the income statement and recognised in the period in which the service is rendered. Regular monthly fee is recognised on the straight line basis in the period when the service is consumed. Revenue from the preparation of the location (collocation) for an alternative operator is recognized upfront in the income statement when it occurs.

2) MOBILE BUSINESS REVENUES
The Group earns mobile services revenue from customers usage of the Group's network, interconnection and roaming – collectively, "Mobile service

revenue". The Group also earns revenue from the sale of mobile telephone equipment and accessories as well as from activation fees.

AIRTIME REVENUES

Postpaid customers are billed monthly in arrears for airtime revenues. Revenue from post-paid customers is recognised as their airtime and other services are used. Prepaid customers recharge a credit, which entitles them to a certain value of airtime and other services. Revenue from prepaid customers is deferred and recognized as the airtime and other services are used. Upon termination of the customer contract or expiration of voucher (up to 14 months), all deferred revenue for unused airtime is recognized in income.

Both, post-paid and prepaid products may include deliverables such as a handset, activation and airtime and that are defined as arrangements with multiple deliverables. The arrangement consideration is allocated to each deliverable, based on its fair value. Revenue allocated to the identified deliverables in each revenue arrangement is recognized based on the same recognition criteria of the individual deliverables at the time the product or service is delivered.

EQUIPMENT SALES AND MOBILE SERVICES

Monthly service revenues and revenues from handset sales are recognized as revenue when the product or service is delivered to the distributor or to the end customer. Resulting losses from sale of handsets at a discount are recognised at the date of sale.

ROAMING REVENUES

Mobile segment derives roaming revenue as a result of airtime and other services used by the mobile segment's customers roaming on partners' networks in other countries and vice versa. Amounts receivable from and payable to roaming partners are netted and settled net on a regular basis.

COSTS

Commissions and discounts directly related to the sale of equipment, SIM cards and activations are netted against revenue in the period the product is sold to the dealer, distributor or the end customer. Other commission payments to dealers for activations, various marketing promotions and other activities are included in the costs of sales for the period.

3) INTERCONNECT REVENUES

Interconnect revenues are derived from calls and other traffic that originate in other domestic and foreign operators' network but use the Group's network. These revenues are recognised in the income statement at the time when the call is received in the Group's network. The Group pays a proportion of the call revenue it collects from its customers to other domestic and foreign operators' for calls and other traffic that originate in the Group's network but use other domestic and foreign operators' network. Amounts receivable from and payable to other domestic and foreign operators are netted and settled net on a regular basis.

4) INTERNET, IPTV AND DATA SERVICES

The Group earns revenue from providing Internet services, IPTV and other data services. Revenue from such services is recognised at the time the service is provided.

5) DIVIDEND INCOME

Dividend income is recognized when the right to receive payment is established.

6) INTEREST

Revenue is recognised as interest accrues (using the effective interest method).

S) DIVIDEND DISTRIBUTION

Dividend distribution to the Company's shareholders is recognized as a liability in the Group's financial statements in the period in which the dividends are approved by the Company's shareholders.

T) FINANCIAL INSTRUMENTS

Financial instruments carried on the balance sheet include cash and bank balances, investments, receivables, payables, borrowings and derivatives. Detailed figures are described in Note 16.

FINANCIAL RISK MANAGEMENT

The Group's is exposed to a variety of financial risks, including the effects of changes in debt market prices, foreign currency exchange rates and interest rates as a result of ordinary business, debt taken on to finance its business and net investment in foreign operations. The Group's overall risk management focuses on the unpredictability of financial markets and seeks to minimize potential adverse effects on the financial performance of the Group. The Group uses either derivative financial instruments (such as forward and swap contracts) or non-derivative instruments (such as cash instruments) to hedge certain exposures.

The Group does not conduct any speculative trading activities.

Risk management is carried out by the treasury department under approved policies. The Board of Directors provides written principles for overall risk management. In line with these principles, policies exist for specific areas, such as foreign exchange risk, interest rate risk, credit risk, liquidity risk, use of derivative financial instruments and investing excess liquidity.

i) Foreign currency risk

The Group is exposed to foreign currency risk arising from various currency exposures, primarily with respect to the Euro, partially to US Dollar and Slovak Crown:

a) balance sheet items (such as debt, receivables, payables) denominated in foreign currency,
b) probable forecasted transactions or firm commitments (such as purchases or sales) denominated in foreign currency,
c) net investment in Slovak subsidiary (functional currency differs from CZK).

The Group's objective in managing its exposure to foreign currency fluctuations is to minimize earnings and cash flow volatility associated with foreign exchange rate changes.

The Group primarily hedges the balance sheet foreign currency exposure, mainly long term debt denominated in EUR and net payables in EUR or USD. Non-derivative instruments are currently used for hedging this kind of exposure.

Additionally, the Group uses to a certain extent derivative hedging via short term forwards to buy respective foreign currency for highly probable or committed purchase transactions, primarily up to a 6 months horizon.

ii) Interest rate risk

The Group is exposed to interest rate risk arising from:

a) floating interest rate bearing cash investments and debt instruments,
b) fair value of debt on fixed interest rate.

The Group's income and operating cash flows are substantially independent of changes in market interest rates. The cash assets and short term debt are currently maintained on floating rates while long term debt instruments are on fixed rates. The Group may sometimes use interest rate swaps and forward rate agreements to manage a mix of fixed and variable rate debts.

iii) Liquidity risk

The Group's essential objective of liquidity risk management is to have ready access to cash resources sufficient to meet all its cash payment obligations as they fall due, allowing some flexibility. The cash resources consist of cash instruments, marketable securities and available committed credit facilities.

The Group is particularly focusing on the liquidity profile within the time horizon of the next 12 months considering projected cash flow from operations and maturity structure of both debt obligations and financial investments. The balance between funding continuity and flexibility is managed through maintaining the possible use of bank overdrafts or bilateral credit lines.

iv) Credit risk
Concentrations of credit risk, with respect to trade accounts receivable, are limited due to the large number of customers. However, substantially all trade receivables are concentrated within the Czech Republic. Although the Group does not currently foresee a dramatically higher credit risk associated with these receivables, repayment is significantly impacted by the financial stability of the national economy.

The Group trades only with recognized, creditworthy third parties. It is the Group's policy that all customers who wish to trade on credit terms are subject to credit verification procedures. In addition, receivable balances are monitored on an ongoing basis with the result that the Group's exposure to bad debts is not significant. The maximum exposure is the carrying amount as disclosed in Note 12. There are no significant concentrations of credit risk within the Group.

With respect to credit risk arising from the financial assets of the Group, which comprise cash and cash equivalents, available for sale investments and certain derivative instruments, the Group's exposure to credit risk arises from default of the counterparty, with a maximum exposure equal to the carrying amount of these instruments.

Credit Risk is managed by the Credit Management Department and is based on three main activities:

a) monitoring of accounts receivables: regular monitoring of payment moral of existing customers and monitoring and analyzing of the receivable aging structure (internal and external indicators of any potential bad debts),
b) prevention: scoring of new customers – checking procedures (Black Lists, External Debtors Register, other information), set up the limits or/and collection of the deposit according to customer segments, products and set up the credit limits for indirect sales partners (dealers, distributors, retailers) for purchase of our products, „securing" of credit limits (deposits, receivables insurance, bill of exchange, pledge of real estate, bank guarantee etc.). Guarantees are either in cash (deposits) or there are special procedures to collect cash for the other securing tools (insurance etc.),
c) collection: reasonable, effective and continual collection process is the additional tool of bad debts decrease and prevention as well.

NEW CREDIT MANAGEMENT ACTIVITIES DURING LAST YEARS

During last years the Group introduced new credit management activities such as:

a) implementation of the connection to the external Debtors Register Solus (sharing debtors data with other members – banks, other telecommunication operators, leasing companies etc.),
b) implementation of the credit management best practice from the merge of the fixed and mobile business in all company activities,
c) checking of the new activation by using of fixed and mobile Black Lists,
d) implementation of tight activation rules for all distribution channels.

ACCOUNTING FOR DERIVATIVE FINANCIAL INSTRUMENTS AND HEDGING ACTIVITIES

Derivative financial instruments are initially recognised in the balance sheet at cost and subsequently are re-measured at their fair value. The method of recognising the resulting gain or loss is dependent on the nature of the item being hedged. On the date a derivative contract is entered into, the Group designates certain derivatives as either:

a) hedge of the fair value of a recognised asset or liability (fair value hedge), or
b) hedge of a forecasted transaction or of a firm commitment (cash flow hedge).

Changes in the fair value of derivatives that are designated and qualify as fair value hedges and that are highly effective are recorded in the income statement, along with changes in the fair value of the hedged asset or liability that is attributable to the hedged risk.

Changes in the fair value of derivatives that are designated and qualify as cash flow hedges and that are highly effective are recognised in equity. Where the forecasted transaction or firm commitment results in the recognition of an asset or of a liability, the gains and losses previously deferred in equity are transferred from equity and included in the initial measurement of the cost of the asset or liability. Otherwise, amounts deferred in equity are transferred to the income statement and classified as revenue or expense in the same periods during which the hedged firm commitment or forecasted transaction affects the income statement.

Certain derivative transactions, while providing effective economic hedges under the Group's risk management policies, either do not qualify for hedge accounting under the specific rules in IAS 39 or the Group has elected not to apply the specific IAS 39 hedge accounting provisions. Changes in the fair value of such derivative instruments that do not qualify for hedge accounting are recognised immediately in the income statement.

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting under IAS 39, any cumulative gain or loss existing in equity at that time remains in equity and is recognised when the committed or forecasted transaction ultimately is recognised in the income statement. However, if a committed or forecasted transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to the income statement.

The Group documents at the inception of the transaction the relationship between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions. This process includes linking all derivatives designated as hedges to specific assets and liabilities or to specific firm commitments or forecast transactions. The Group also documents its assessment, both at the hedge inception and on an ongoing basis, whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items.

The fair values of various derivative instruments used for hedging purposes are disclosed in Note 20. Movements on the hedging reserve in shareholder's equity are shown in Note 25.

FAIR VALUE ESTIMATION

Except for currency options, the fair values of the derivative financial instruments reflect estimates based on calculations performed using the Group's own discounted cash flow models (using market rates). The fair value of currency options is based on information obtained from external parties, including the Group's bankers.

U) CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS

The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results.

Estimates and judgments are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

The estimates and assumptions that might have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next year are discussed below:

1) Income taxes and deferred taxes

The Group created a provision for current income taxes and in consideration of the temporary differences also for deferred tax. There are many transactions and calculations for which the ultimate tax determination is uncertain during the ordinary course of business and the measurement of deferred tax assets and liabilities reflects the tax consequences that would follow from the manner in which the Group expects to recover or settle the carrying amount of assets and liabilities. Where the final tax-deductible expenses are different from the amounts that were calculated, such differences will impact the current income and deferred tax provisions in the period in which such determination is made. As at 31 December 2008, the total amount of provision for current income taxes is CZK 3,759 million, advances paid for income taxes amount to CZK 3,976 million and the net deferred tax liability is CZK 3,300 million.

In October 2007, the new Czech legislation was enacted, by which the corporate income tax rate was reduced from 24% to 21%, 20% and 19% for the fiscal years ending in 2008, 2009 and 2010, respectively. The positive impact on the deferred tax liability amounts to CZK 798 million in 2007 (see Note 5).

2) Goodwill

The Group tests at each reporting date goodwill for an impairment. However goodwill does not generate cash flows independently of other assets or groups of assets and the assessment of its carrying value is significantly impacted by the management's assessment of the performance and expected future performance of the operation to which the goodwill relates. In accordance with the requirement of IAS 36, goodwill is tested annually for its recoverable amount, as well as when there are indications of impairment. At 31 December 2008 the carrying amount of goodwill is CZK 13,448 million (See Note 9).

3) Provisions and contingent liabilities
As set out in Note 21 the Group is a participant in several lawsuits and administrative proceedings including those related to its pricing policies. The Group's treatment of obligations with uncertain timing and amount depends on the management's estimation of the amount and timing of the obligation and probability of an outflow of resources embodying economic benefits that will be required to settle the obligation (both legal or constructive). A provision is recognised when the Group has a present obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Contingent liabilities are not recognised, because their existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Group. Contingent liabilities are assessed continually to determine whether an outflow of resource embodying economic benefits has become probable. If it becomes probable that an outflow of future economic benefits will be required for an item previously dealt with as a contingent liability, a provision is recognised in the financial statements of the period in which the change in probability occurs.

4) Interconnect
The Group provides and enters into the contracts for interconnect services and the revenue is recognised on the basis of the reasonable estimation of expected amount. Such estimation is regularly reviewed, however the final agreement and invoicing can be with some operators stated on up to a yearly basis.

5) Impairment of the fixed line business assets
The Group makes an assessment at each balance sheet date whether there is any indication that an impairment loss recognised for the fixed line business assets in prior years may no longer exist, may have decreased or may have increased. If any such indication exists, the Group estimates a recoverable amount of the assets and compares to the carrying value (net of the impairment allowance). In assessing whether there is any indication that the impairment loss recognised in the past may no longer exist, the Group considers both external and internal indicators (decline of asset's market value, changes expected in the market, including technological changes etc.). Where an estimate of recoverable amount is calculated, there is a number of management assumptions about future business performance, which may, ultimately, differ from reality.

Based on the assessment performed by the Company, no increase or decrease of the previously recognised impairment of fixed line business assets was recognised in 2008 and 2007 (see Note 8 and 10).

6) Operating lease commitments – Group as lessee
The Group changed its headquarters and moved to the new premises, where the Group has entered into the commercial property leases. The Group has determined, based on an evaluation of the terms and conditions of the arrangements, that the lessor retains all the significant risks and rewards of the ownership and therefore the Group accounts for the contract as an operating lease.

V) CHANGE IN ACCOUNTING POLICY

No significant changes in accounting policies were applied in 2008 and 2007.

W) OPERATING PROFIT

Operating profit is defined as profit before financial results and taxes and represents profit from the business operations. Financial results consist of interest income, interest expense, other financial expense (which include primarily bank charges), fair value losses and gains on financial instruments and foreign exchange gains and losses

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

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1) SEGMENT INFORMATION

Business segments recognised by the Group are as follows:

- Fixed – network communications services using a fixed network and IS/ICT services provided by the Company and other consolidated subsidiaries,
- Mobile – mobile communications services provided by the Company and by Telefónica O2 Slovakia

Year ended 31 December 2008 in CZK million	Fixed	Mobile	Group
Revenues	30,484	35,419	65,903
Inter-segment sales	(423)	(771)	(1,194)
Total consolidated revenues	30,061	34,648	64,709
Gains from sale of non-current assets	855	0	855
Internal expenses capitalised in fixed assets	338	146	484
Costs	(18,717)	(20,127)	(38,844)
Inter-segment purchases	771	423	1,194
Total consolidated costs	(17,946)	(19,704)	(37,650)
Impairment charge	(83)	(3)	(86)
Depreciation	(7,263)	(3,731)	(10,994)
Amortisation	(654)	(1,284)	(1,938)
Total consolidated depreciation and amortization	(7,917)	(5,015)	(12,932)
Operating profit	5,308	10,072	15,380
Interest and other financial costs (net)			(32)
Profit before tax			15,348
Tax			(3,720)
Profit after tax			11,628
Minority interest			–
Net profit			**11,628**
Assets (excluding goodwill and non-current assets held for sale)	37,863	52,216	90,079
Goodwill	128	13,320	13,448
Non-current assets held for sale	96	–	96
Total assets	**38,087**	**65,536**	**103,623**
Trade and other payables	6,199	11,487	17,686
Other liabilities	3,739	4,030	7,769
Total liabilities	**9,938**	**15,517**	**25,455**
Capital expenditure	**4,312**	**3,776**	**8,088**

Year ended 31 December 2007 in CZK million	Fixed	Mobile	Group
Revenues	30,500	33,934	64,434
Inter-segment sales	(455)	(783)	(1,238)
Total consolidated revenues	30,045	33,151	63,196
Gains from sale of non-current assets	42	–	42
Internal expenses capitalised in fixed assets	448	105	553
Costs	(16,973)	(20,018)	(36,991)
Inter-segment purchases	783	455	1,238
Total consolidated costs	(16,190)	(19,563)	(35,753)
Impairment charge	(5)	–	(5)
Depreciation	(8,521)	(4,042)	(12,563)
Amortisation	(684)	(1,188)	(1,872)
Total consolidated depreciation and amortization	(9,205)	(5,230)	(14,435)
Operating profit	5,135	8,463	13,598
Interest and other financial costs (net)			(88)
Profit before tax			13,510
Tax			(3,124)
Profit after tax			10,386
Minority interest			–
Net profit			**10,386**
Assets (excluding goodwill and non-current assets held for sale)	47,697	52,207	99,904
Goodwill	–	13,320	13,320
Non-current assets held for sale	328	–	328
Total assets	**48,025**	**65,527**	**113,552**
Trade and other payables	5,577	8,188	13,765
Other liabilities	8,166	8,829	16,995
Total liabilities	**13,743**	**17,017**	**30,760**
Capital expenditure	**4,263**	**3,544**	**7,807**

Revenue of the Group is predominantly derived from domestic trading activities and as a result, segment reporting is only shown on the basis of business segments. With respect to the issue of IFRS 8 Operating segments and the deep integration process from the past convergence of fixed and mobile operations, the Group has analysed criteria for segment identification. The adoption of the standard will not lead to a change in the reported segments in the next years.

Inter-segment sales and purchases represent sales and purchases to the Group companies belonging to another segment.

The inter-segment pricing rates applied in 2008 and 2007 were determined on the same basis as rates applicable for other mobile operators and are consistent with rates applied for pricing with other mobile operators.

Capital expenditures comprise additions to property, plant and equipment and intangible assets.

2) REVENUE AND INTERNAL EXPENSES CAPITALIZED IN FIXED ASSETS

Revenue in CZK million	Year ended 31 December 2008	Year ended 31 December 2007
Voice	23,269	23,147
Interconnection	10,428	10,625
Subscription charges	8,444	8,849
Connection charges	295	783
SMS & MMS & Value added services	5,080	4,998
Leased lines and data services	3,866	3,961
Internet	6,463	5,828
IT and business solutions	2,308	1,950
Equipment and activation fee	2,045	2,058
Other telecommunication revenues	2,253	437
Other revenues	258	560
Total revenues	64,709	63,196

Revenues from related parties are disclosed in Note 26.

The aggregate future minimum lease payments under non-cancellable operating leases, where the Company is a lessor, relating to the buildings and other telecommunication equipment are as follows:

In CZK million	31 December 2008	31 December 2007
No later than 1 year	185	244
Later than 1 year and not later than 5 years	754	868
Later than 5 years	198	237
Total	1,137	1,349

Internal expenses capitalized in fixed assets in CZK million	Year ended 31 December 2008	Year ended 31 December 2007
Material	79	138
Labour	405	415
Total	484	553

3) OPERATING EXPENSES

The following items have been included into the operating expenses:

In CZK million	Year ended 31 December 2008	Year ended 31 December 2007
Wages and salaries*	5,163	4,891
Redundancy payments	160	209
Social security contributions (Note 18)	1,626	1,678
Staff welfare costs	157	331
Total staff costs	7,106	7,109
Interconnection and roaming	11,989	11,012
Cost of goods sold	3,258	3,499
Contents	220	160
Customer loyalty program	363	446
Sub-deliveries	1,213	1,217
Commissions	1,213	1,203
Other cost of sales	1,127	261
Purchases	542	645
Billing and collection	399	386
Marketing	1,908	2,237
Call centres	305	245
Network & IT repairs and maintenance	2,340	2,603
Rentals, buildings and vehicles	2,168	1,897
Utilities supplies	948	807
Consultancy and professional fees	270	338
Other external services	1,242	1,043
Provision for bad and doubtful debts and inventories	530	225
Taxes (other than income tax)	423	375
Other operating expenses	86	45
Total operating expenses	37,650	35,753

* Certain Group employees (including the Board of Directors) with specialised know how, or who have access to business secrets, or who are considered important to the development of the business, are bound by non-competition restrictions, for a maximum period of 12 months from the date of termination of their employment with the Group. The Group paid CZK 11 million in relation to such non-competition clauses in 2008 (2007: CZK 7 million).

Statutory auditor's fees as at 31 December 2008 were as follows:

In CZK million	Year ended 31 December 2008	Year ended 31 December 2007
Statutory audit	23	19
Total	23	19

Purchases from related parties are disclosed in Note 26.

4) INTEREST AND OTHER FINANCE INCOME AND EXPENSE

In CZK million	Year ended 31 December 2008	Year ended 31 December 2007
FINANCIAL INCOME		
Interest income	449	403
Gain for derivatives of fair value hedges	65	–
Other financial income	1,333	749
Total financial income	1,847	1,152
FINANCIAL EXPENSES		
Interest expenses	(406)	(446)
Loss for derivatives of fair value hedges	–	(26)
Other financial expenses	(1,473)	(768)
Total financial expenses	(1,879)	(1,240)
Net financial cost (net)	(32)	(88)

5) INCOME TAX

In CZK million	Year ended 31 December 2008	Year ended 31 December 2007
Total income tax expense is made up of:		
Current income tax charge	3,777	4,240
Deferred income tax credit (Note 17)	(57)	(1,116)
Taxes on income	3,720	3,124

The tax on the Group's profit before tax differs from the theoretical amount that would arise using the basic tax rate of the home country of the Group as follows:

In CZK million	Year ended 31 December 2008	Year ended 31 December 2007
Profit before tax	15,348	13,510
Income tax charge calculated at the statutory rate of 21% (2007: 24%)	3,223	3,242
Income not subjected to tax	–	(9)
Expenses not deductible for tax purposes	164	299
Impact of change in income tax rate	–	(798)
Tax related to prior periods	22	54
Unrecognised tax losses	311	336
Taxes on income	3,720	3,124
Effective tax rate	24%	23%

6) EARNINGS PER SHARE

Basic earnings per share are calculated by dividing the net profit attributable to shareholders by the weighted average number of ordinary shares in issue during the year.

	31 December 2008	31 December 2007
Weighted number of ordinary shares in issue	322,089,900	322,089,900
Net profit attributable to shareholders (in CZK million)	11,628	10,386
Basic earnings per share (CZK)	36	32

There is no dilution of earnings as no convertible instruments have been issued by the Company.

7) DIVIDENDS

In CZK million	31 December 2008	31 December 2007
Dividends declared (including withholding tax)	16,104	16,104

Dividends include withholding tax on dividends paid by the Company to its shareholders. There has been no interim dividend paid in respect of 2008. Approval of the 2008 profit and the decision regarding the amount of any dividend payment for the 2008 financial year will take place at the Annual General Shareholders Meeting scheduled for 3 April 2009.

8) PROPERTY, PLANT AND EQUIPMENT

In CZK million	Land and buildings	Ducts, cables and related plant	Communication exchanges and related equipment	Other fixed assets	Capital work in progress including advances paid	Total
At 31 December 2008						
Opening net book amount	14,080	39,710	13,207	2,003	2,809	71,809
Additions	672	769	2,923	1,076	5,630	11,070
Disposals and other movements	24	–	(8)	(7)	(5,066)	(5,057)
Acquisition impact	–	–	–	2	–	2
Assets classified as held for sale	(3,285)	(25)	(6)	–	–	(3,316)
Depreciation charge	(678)	(4,206)	(4,927)	(1,183)	–	(10,994)
Impairment charge	(49)	(21)	(2)	–	(13)	(85)
Closing net book amount	10,764	36,227	11,187	1,891	3,360	63,429
At 31 December 2008						
Cost	17,718	99,982	91,788	10,486	3,385	223,359
Accumulated depreciation and impairment allowance	(6,954)	(63,755)	(80,601)	(8,595)	(25)	(159,930)
Net book amount	10,764	36,227	11,187	1,891	3,360	63,429
At 31 December 2007						
Opening net book amount	14,219	43,395	17,292	1,814	2,035	78,755
Additions	691	576	2,634	1,190	5,700	10,791
Disposals and other movements	(37)	(1)	(55)	(12)	(4,927)	(5,032)
Assets classified as held for sale	(132)	(10)	–	–	–	(142)
Depreciation charge	(656)	(4,250)	(6,664)	(989)	(4)	(12,563)
Impairment charge	(5)	–	–	–	5	–
Closing net book amount	14,080	39,710	13,207	2,003	2,809	71,809
At 31 December 2007						
Cost	22,838	99,696	93,126	10,557	2,839	229,056
Accumulated depreciation and impairment allowance	(8,758)	(59,986)	(79,919)	(8,554)	(30)	(157,247)
Net book amount	14,080	39,710	13,207	2,003	2,809	71,809

As at 31 December 2008, the carrying value of non-depreciated assets amounted to CZK 241 million (2007: CZK 472 million).

Land and buildings in the carrying value of CZK 8,280 million as of 31 December 2007 were pledged in respect of execution relating to the T-Mobile interconnect dispute.

In 2008 the execution was terminated (see Note 21). No property, plant and equipment were pledged as at 31 December 2008.

No borrowing costs were capitalized during the years 2008 and 2007.

The Group reports and classifies the following assets held for sale at the balance sheet date:

In CZK million	Land and buildings	Communication exchanges and related equipment	Other fixed assets	Total
At 31 December 2008				
Opening net book amount	327	1	–	328
Disposals and other movements	(3,540)	(7)	–	(3,547)
Impairment charge	(1)	–	–	(1)
Assets re-classified as held for sale	3,310	6	–	3,316
Closing net book amount	96	–	–	96
At 31 December 2008				
Cost	789	187	6	982
Accumulated depreciation and impairment allowance	(693)	(187)	(6)	(886)
Net book amount	96	–	–	96
At 31 December 2007				
Opening net book amount	202	1	–	203
Disposals and other movements	(12)	–	–	(12)
Impairment charge	(5)	–	–	(5)
Assets re-classified as held for sale	142	–	–	142
Closing net book amount	327	1	–	328
At 31 December 2007				
Cost	1,282	199	10	1,491
Accumulated depreciation and impairment allowance	(955)	(198)	(10)	(1,163)
Net book amount	327	1	–	328

Assets intended for sale in most cases represent administration buildings with land, that became vacant due to the Group's optimization process and which the Group will not use in the future and it is expected that their sale will take place within one year.

The non-current assets classified as held for sale are presented in the fixed segment.

In 2008, the Group achieved a total gain from the sale of the above fixed assets amounting to CZK 855 million (2007: CZK 42 million) and total losses in amount CZK 59 million (2007: CZK 35 million).

In 2008 and at the beginning of 2009, the Group completed the substantial part of a real estate usage optimisation process. In 2008, as part of this process, the Group sold a portfolio of administrative and technological buildings located throughout the whole Czech Republic. Net gain from the sale of the real estate portfolio amounted to 727 million CZK. A small portion of the real estate was leased back on the long term basis. In January 2009, the Group sold a construction site and two administrative buildings of the former headquarters in Olšanská street in Prague (see Note 28).

Cost of fully depreciated property, plant and equipment was CZK 59,597 million as at 31 December 2008 (2007: CZK 62,165 million).

9) INTANGIBLE ASSETS

In CZK million	Goodwill	Licences	Software	Other	Total
At 31 December 2008					
Opening net book amount	13,320	4,816	3,669	–	21,805
Additions	–	–	2,371	–	2,371
Disposals and other movements	–	15	(38)	–	(23)
Acquisition impact	128	–	5	–	133
Amortisation charge	–	(406)	(1,532)	–	(1,938)
Closing net book amount	13,448	4,425	4,475	–	22,348
At 31 December 2008					
Cost	13,448	6,226	24,601	–	44,275
Accumulated amortisation and impairment allowance	–	(1,801)	(20,126)	–	(21,927)
Net book amount	13,448	4,425	4,475	–	22,348
At 31 December 2007					
Opening net book amount	13,320	5,210	3,098	–	21,628
Additions	–	16	2,034	–	2,050
Disposals and other movements	–	–	(1)	–	(1)
Amortisation charge	–	(410)	(1,462)	–	(1,872)
Closing net book amount	13,320	4,816	3,669	–	21,805
At 31 December 2007					
Cost	13,320	6,209	22,955	2,829	45,313
Accumulated amortisation and impairment allowance	–	(1,393)	(19,286)	(2,829)	(23,508)
Net book amount	13,320	4,816	3,669	–	21,805

GOODWILL

Goodwill in amount of CZK 13,320 million resulted from the acquisition of the remaining 49% ownership interest in Eurotel Praha spol. s r.o. ("Eurotel") The initially recognized goodwill of CZK 14,087 million resulted from comparison of cost of business combination of CZK 29,215 million and fair value of net assets acquired of CZK 15,128 million. Until 31 December 2004 goodwill was amortised on a straight line basis over a period of 20 years and assessed for an indication of impairment at each balance sheet date.

Due to a revision of IFRS 3, IAS 36 and IAS 38 the Group ceased amortisation of the previously recognized goodwill from 1 January 2005. Accumulated amortisation as at 31 December 2004 was eliminated with a corresponding decrease in the cost of goodwill (767 million CZK). Since the year ending 31 December 2005 onwards, goodwill is classified as an asset with indefinite useful life which has been tested annually for the impairment, as well as when there are indications of impairment. There is no other intangible asset with indefinite useful life.

The Group performed impairment tests and as result of the test the Group did not recognize any impairment losses of goodwill in 2008 and 2007. The impairment test involves determining the recoverable amount of the mobile cash-generating unit, which corresponds to the value in use. Value in use is the present value of the future cash flows expected to be derived from a cash-generating unit.

Value in use is determined on the basis of an enterprise valuation model and is assessed from a Group internal perspective. Value in use is determined based on cash flow budgets, which are based on the medium-term business plan for a period of 3 years, which has been approved by the management and which is valid when the impairment test is performed. This business plan is based on the past experience, as well as on future market trends. Further, the business plan is based on general economic data derived from macroeconomic and financial studies. Cash flows beyond the three-year period are extrapolated using an appropriate growth rates. Key assumptions on which management has based its determination of business plan and growth rates include development of gross domestic product, interest rates, nominal wages, average revenue per user ("ARPU"), customer acquisition and retention costs, churn rates, capital expenditure, market share, growth rates and discount rates.

Any significant future changes in the market and competitive environments could have an adverse effect on the value of the cash-generating units.

The calculations of value in use for all cash-generating units are most sensitive to the following assumptions:

Estimated growth rate – the basis used to determine the value assigned to estimated growth rate is the forecast of market and regulatory environment, where the Group conduct the business.

Discount rate – discount rates reflect management's estimate of the risk specific to the cash generating unit. The basis used to determine the value assigned is weighted average of cost of capital ("WACC").

LICENCES
Acquired licences are represented by rights to operate the UMTS, GSM and NMT cellular networks in the Czech Republic. The original 450 MHz and GSM operating licenses were granted for a period of twenty years from the signing of the agreement for the original 450 MHz license in 1991 and from the granting of the GSM license in 1996 for use of the 900 spectrum. In 1999, Eurotel acquired an additional GSM 1800 spectrum under its existing GSM license. In 2002, the GSM license to both spectrums was renewed and is currently valid for the remaining period of eight years.

In 2002, Eurotel renewed its 450 MHz license; the current license enables the mobile segment to offer every internationally recognized public mobile telecommunication services on frequency of 450 MHz. Mobile segment currently provides on this frequency voice services under NMT standard and broadband Internet access services using CDMA technology. The NMT license is currently valid for the remaining period of three years.

In December 2001, Eurotel acquired the UMTS license, which has been granted for a period of twenty years. Under the license, Eurotel was provided with deferred payment terms by the Czech Telecommunication Office ("CTO") to finance the license acquisition. In December 2003, Eurotel signed an amendment to its original UMTS license agreement, by which the original launch of the service was extended by one year. According to the terms of this new amendment, Eurotel agreed to pay the UMTS obligation in full during 2004 in exchange for a forgiveness of 2003 and 2004 interest on the deferred payments provided as part of the UMTS license agreement. UMTS license was put into commercial use on 1 December 2005 when it also started to be amortized.

With respect to the operation launch in 2007, the license for GSM and UMTS networks was awarded to Telefónica O2 Slovakia on 7 September 2006 for SKK 150 million (EUR 4.1 million).

Carrying value of licences:

In CZK million	31 December 2008	31 December 2007
GSM 900 license	546	619
GSM 1800 license	440	499
NMT 450 license	33	50
UMTS license	3,268	3,518
GSM and UMTS license – TO2 Slovakia	138	130
Total	4,425	4,816

No borrowing costs were capitalized during the years 2008 and 2007.

Cost of fully amortised intangible assets was CZK 16,846 million as at 31 December 2008 (2007: CZK 17,252 million).

All of the Group's intangible assets with finite lives are amortised and are subject to an annual review of impairment indicators and revision of useful life.

10) IMPAIRMENT OF FIXED ASSETS

FIXED ASSETS OF THE FIXED LINE BUSINESS
During 2003, external factors relating to the telecommunication market and regulatory environment namely uncertainty regarding tariff rebalancing, termination charges for internet dial-up interconnection charges and other regulatory decisions in the Czech Republic led the management to assess and adjust the recoverable amount of the fixed line segment assets. The fixed line segment assets constitute one cash-generating unit (the "CGU").

Value in use has been calculated by a method of cumulated discounted cash flows for a period limited by average useful life of CGU's key assets. Primarily, the following assumptions have been used in the impairment testing model: actual business plan, estimation of consecutive development of key indicators (revenues, margin, investments etc.) in analyzed period, discount rate derived from weighted average cost of capital.

As at 31 December 2008, the management of the Company reviewed the indicators which would indicate that the impairment allowance of fixed line business assets made in 2003 is no longer relevant and should be reversed. Upon the review, a recoverable amount of the fixed line business assets (impairment test model) was estimated. Based on this assessment performed, the management believes that the value of the existing fixed network assets is fairly stated and does not differ substantially from the assets' recoverable amount as at 31 December 2008.

Value in use as at 31 December 2008 has been calculated using the same methodology as in the year 2003.

11) INVENTORIES

In CZK million	31 December 2008	31 December 2007
Construction material	114	66
Cables	47	47
Other inventory including goods for resale	607	736
Finished products and work in progress	11	4
Total	779	853

The inventories noted above are stated net of an allowance of CZK 64 million (2007: CZK 96 million), reducing the value of the inventories to their net realisable value. The total carrying amount of inventories at net realisable value amounts to CZK 31 million (2007: CZK 43 million). The amount of inventories recognised as an expense is CZK 4,059 million (2007: CZK 4,245 million).

12) RECEIVABLES AND PREPAYMENTS

In CZK million	31 December 2008	31 December 2007
Domestic trade receivables (net)	6,960	6,895
Foreign currency trade receivables (net)	834	572
Other debtors (net)	650	373
Prepayments	759	716
Other financial assets - short-term	14	17
Derivative instruments	23	4
Total	9,240	8,577

Trade receivables are stated net of an allowance for impaired receivables of CZK 3,457 million (2007: CZK 3,291 million). In order to preserve the tax-deductible status of the bad debt expense, the Group's trade receivables are not written off and removed from the primary books and records until certain statutory collection requirements have been satisfied.

Receivables from related parties are disclosed in Note 26.

Trade receivables in CZK million	Carrying amount	Neither impaired nor overdue	Not impaired but overdue			
			Less than 90 days	90 and 180 days	180 and 360 days	More than 360 days
At 31 December 2008	7,794	5,101	552	–	30	36
At 31 December 2007	7,467	4,491	321	50	–	–

Bad debt provisions in CZK million	
At 1 January 2007	3,312
Additions	117
Retirements/amount paid	(138)
At 31 December 2007	3,291
Additions	1,057
Retirements/amount paid	(891)
At 31 December 2008	3,457

The Group's historical experience regarding the collection of accounts receivable is consistent with the recorded allowances. Due to these factors, the management believes that no additional credit risk beyond the amounts provided for is inherent in the Group's trade receivables.

As at 31 December 2008 and 2007 the Group has the following non-current balances, which are classified as other financial assets:

In CZK million	31 December 2008	31 December 2007
Long-term credits	133	112
Advance payments for long-term expenses	245	247
Other financial investment	–	207
Total	378	566

Long-term trade credits include interest bearing credit (interest 5.9%) amounting to CZK 64 million (2007: CZK 71 million).

13) HELD-TO-MATURITY INVESTMENTS

Held-to-maturity investments in CZK million	31 December 2008	31 December 2007
At beginning of year	27	27
Additions	1	1
Matured	(28)	(1)
At end of year	–	27
Current	–	27
Total	–	27

Held to maturity investments category as at 31 December 2007 comprised a debt instrument – a bond held in EUR with maturity date July 2008, which was carried at amortised cost.

14) CASH AND CASH EQUIVALENTS

In CZK million	31 December 2008	31 December 2007	Interest rate
Cash at current bank accounts	330	4,130	Floating
Cash at cash-pooling structures (inter-company)	6,344	5,107	Floating
Short-term bank deposits	442	321	Fixed
Other cash equivalents	–	18	n/a
Total cash and cash equivalents	7,116	9,576	
Financial investments (held to maturity)	–	27	Fixed

As at 31 December 2008 and 2007, the Group's cash equivalents partially consisted of short-term bank promissory notes that were economically equivalent to bank term deposits and interest bearing deposits maturing in three months or less.

Since April 2006, the Group entered into mutual Telefónica Group cash-pooling, which enables the Telefónica Group good financial governance and effective operating free cash flow. The short-term deposits conditions are based on the arm's length principle. The short-term deposits are classified as cash equivalents.

At 31 December 2008, the Group had available equivalent of CZK 5,425 million (2007: CZK 12,344 million) of undrawn committed facilities.

For the purposes of the cash flow statement, the year-end cash and cash equivalents comprise the following components:

In CZK million	31 December 2008	31 December 2007
Cash and cash equivalents	7,116	9,576
Bank overdrafts and other short-term borrowings (Note 16)	–	–
Total	7,116	9,576

The amount of CZK 3,902 million kept on bank accounts was pledged as of 31 December 2007 in respect of execution relating to the T-Mobile Interconnect dispute. In 2008 the execution was terminated (Note 21). As of 31 December 2008 no cash and cash equivalents were pledged.

15) TRADE AND OTHER PAYABLES

In CZK million	31 December 2008	31 December 2007
Trade creditors in local currency (net)	4,615	4,575
Trade creditors in foreign currencies (net)	2,161	1,924
Related party loans	3,249	794
Other taxes and social security	196	518
Deferred revenue	1,054	1,254
Employee wages and benefits	794	703
VAT payable	479	162
Other creditors	406	656
Accruals	4,732	3,179
Total payables	17,686	13,765
Other non-current liabilities	176	452

In 2008 and 2007 the related party loans include an intercompany loan in amount of CZK 3,194 million (2007: CZK 794 million) provided to Telefónica O2 Slovakia, s.r.o. by the company Telfisa Global, BV (see Note 26).

Other non-current liabilities include primarily deferred revenues from connection fees, which are expected to be taken to income in more than 12 months from the balance sheet date.

16) FINANCIAL DEBTS

In CZK million	31 December 2008	31 December 2007
Bank loans in foreign currencies (a)	3,098	3,062
Bonds in local currency (b)	5	5,998
Total borrowings	3,103	9,060
Accrued interest including commitment fees	86	185
Derivatives	7	24
Other financial debt	93	209
Total financial debt	3,196	9,269
Repayable:		
Within one year	98	6,207
Between two and five years (total non-current)	3,098	3,062
Total financial debt	3,196	9,269

a) As at 31 December 2008 the Group does not utilize bank overdrafts.
In July 1997, the Company raised a private placement in the total amount of EUR 127.8 million with a maturity date on 30 July 2012. As at 31 December 2008, the outstanding amount of the foreign currency loan amounts to EUR 115 million.

b) In 2003, the Group issued CZK 6,000 million of bonds with an interest rate 3.50% p.a. and it was fully repaid at a maturity date of 9 July 2008.
For all borrowings, interest has been charged at commercial rates.

The Group's loan interest rate allocation after taking into account interest rate swaps was as follows:

In CZK million	31 December 2008	31 December 2007
At fixed rate	3,103	9,060
Total	3,103	9,060

The fair values of borrowings are based on discounted cash flows using a discount rate based upon the borrowing rate that the Board of Directors expects to be available to the Group at the balance sheet date. The carrying amounts of short-term borrowings approximate their fair value.

Effective interest rates	2008	2007
Bank loans in foreign currencies	6.64%	6.64%
Bonds in local currency	3.50%	3.50%

Loans are not secured.

The table below summarizes the maturity profile of the Group's financial liabilities at 31 December 2008 based on contractual undiscounted payments.

At 31 December 2008 in CZK million	Less than 3 months	3 to 12 months	1 to 5 years	> 5years
Interest bearing loans and borrowings	5	206	3,715	–
Trade and other payables (except for deferred revenue)	14,796	1,836	–	–
Derivatives fair value	7	–	–	–
Total	14,808	2,042	3,715	–
At 31 December 2007 in CZK million	Less than 3 months	3 to 12 months	1 to 5 years	> 5years
Interest bearing loans and borrowings	–	6,413	3,875	–
Trade and other payables (except for deferred revenue)	10,655	1,856	–	–
Other financial liabilities	3	8	–	–
Derivatives fair value	22	2	–	–
Total	10,680	8,279	3,875	–

FAIR VALUES

Set out below is a comparison by category of carrying amounts and fair values of all of the Group's financial instruments that are carried in the financial statements.

	Carrying amount		Fair value	
In CZK million	2008	2007	2008	2007
FINANCIAL ASSETS				
Cash and cash equivalents	7,116	9,576	7,116	9,576
Financial investments (held to maturity)	–	27	–	27
Derivatives	23	4	23	4
Other financial assets	378	566	378	566
	Carrying amount		Fair value	
	2008	2007	2008	2007
FINANCIAL LIABILITIES				
Interest bearing loans and borrowings				
Floating rate inter-company borrowings	3,249	794	3,249	794
Fixed rate borrowings	3,184	3,148	3,503	3,348
Issued Bonds	5	6,097	5	6,049
Derivatives	7	24	7	24

Market values have been used to determine the fair value of the above mentioned issued CZK bonds. The fair value of derivatives and borrowings has been calculated by discounting the expected future cash flows at prevailing interest rates.

FINANCIAL RISK ANALYSIS

The following table demonstrates the sensitivity to a reasonably possible change in foreign exchange rates and interest rates.

	Effect on profit before tax	
In CZK million	2008	2007
FX RISK		
Value at Risk*	(395)	(95)
Stress testing*	(76)	(46)
IR RISK		
Stress testing*	(114)	(176)

* The Value at Risk (VaR) Model enables the Group estimate the probability of maximum possible loss to the portfolio value in the given time frame which will not be exceeded given the defined reliability level. For conducting a VaR calculation, the Group uses the risk variance and covariance method using the normal distribution (e.g. parametric method). The time frame used is one month with a 95% reliability rate. Considering the importance of net open positions resulting from financial assets and financial liabilities of the Group in individual foreign currencies, the Group models VaR from a position of translation and transaction in EUR and USD.
FX risk used stress scenario represents immediate one-off change in the foreign exchange rates vs. CZK by 1% in a negative direction (in the case of short open foreign currency position, this will result in a depreciation of the foreign exchange rate and vice versa).
IR risk used stress scenario represents immediate one-off change of interest rates along the whole yield curve by 1% in an unfavourable direction. The calculation of unfavorable impact on Group cash flows (due to an increase in interest expense or drop in interest received relating to financial assets and financial liabilities) is made each month on the floating basis within a time frame of 12 months.

HEDGING

The following nominal value of foreign exchange forwards was used by the Group to hedge the currency risk:

	Nominal value in EUR million		Fair value in CZK million	
	2008	2007	2008	2007
Forward exchange contracts	19	36	16	(20)

17) DEFERRED INCOME TAXES

Deferred income taxes are calculated using currently enacted tax rates expected to apply when the asset is realized or the liability settled.

Short-term deferred taxes were calculated at 20% (21% in 2007) and long-term deferred taxes were calculated at 19% (20% and 19% in 2007 depending on the period of its expected realisation).

In CZK million	2008	2007
At 1 January	3,353	4,469
Income statement tax credit (Note 5)	(57)	(1,116)
Tax impact on changes in equity	4	–
At 31 December	3,300	3,353

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when the deferred income taxes relate to the same fiscal authority.

The following amounts, determined after offsetting, are shown in the consolidated balance sheet:

In CZK million	31 December 2008	31 December 2007
Deferred tax assets	(656)	(1,143)
Deferred tax liabilities	3,956	4,496
Total	3,300	3,353

The deferred tax asset includes CZK 423 million (2007: CZK 655 million) recoverable in less than twelve months and CZK 233 million (2007: CZK 488 million) recoverable after more than twelve months. The deferred tax liability includes CZK 494 million (2007: CZK 584 million) payable in less than twelve months and CZK 3,462 million (2007: CZK 3,912 million) payable in more than twelve months.

The deferred tax is determined by these components:

In CZK million	Consolidated balance sheet 2008	Consolidated balance sheet 2007	Consolidated income statement 2008	Consolidated income statement 2007
Temporary differences relating to:				
– property, plant and equipment and intangible assets	3,926	4,496	(570)	(575)
– trade receivables, inventories and other differences	(626)	(1,139)	513	231
Revaluations of cash flow hedges	–	(4)	–	–
Amount relating to unrecognised tax loss	–	–	–	26
Amount relating to changes in tax rates	–	–	–	(798)
Total	3,300	3,353	(57)	(1,116)

Deferred income tax related to items charged or credited directly to equity are as follows:

In CZK million	31 December 2008	31 December 2007
Revaluation of cash flow hedges	4	–
Total	4	–

Reduction of the corporate income tax rate resulted in a positive impact on deferred tax liability of CZK 798 million in 2007.

18) GOVERNMENT SOCIAL SECURITY AND PENSION SCHEMES

The Group is legally required to make contributions to government health, retirement benefit and unemployment schemes. During 2008 and 2007, the Group paid contributions at a rate of 35% of gross salaries and is not required to make any contributions in excess of this statutory rate. The total amount charged to operating expenses in respect of this scheme was CZK 1,622 million in 2008 (2007: CZK 1,678 million) (Note 3). Employees contribute 12.5% (2007: 12.5%) of their gross salaries.

The Group has a voluntary pension plan for employees under which the Group makes contributions on behalf of the Group's employees to approved pension plan providers, under defined contribution schemes. The Group's contribution depends upon the number of employees joining the scheme and their age profile. During the year the Group made contributions of CZK 59 million (2007: CZK 58 million). These contributions were charged as an operating expense.

In accordance with an annually renegotiated collective labour agreement, the Company is required to pay CZK 25,000 or CZK 90,000 on retirement depending on the length of the employee's service, who have completed not less than five years continuous service. These benefits are restricted to those employees who retire during the period for which the labour agreement is in place. The Company is not under any legal or constructive obligation to continue providing such benefits beyond the period of such agreement and therefore, no provisions beyond the period of the agreement are recognised in the financial statements. Payments made during the year 2008 relating to employee retirement amounted to CZK 0.1 million (2007: CZK 0.2 million) and were charged as an operating expense.

All amounts discussed in the above note are included in staff costs (see Note 3).

19) PROVISIONS FOR LIABILITIES AND CHARGES

In CZK million	Regulatory and court decisions	Employee redundancy costs	Employee related costs	Benefit loyalty provision	Sale of real estate portfolio provision	Other	Total
At 1 January 2008	2,110	3	303	627	0	8	3,051
Additions during the year	66	73	151	43	495	31	859
Utilised during the year	(1,781)	(63)	(287)	(418)	(235)	(13)	(2,797)
Transfers	–	–	(25)	–	–	–	(25)
At 31 December 2008	395	13	142	252	260	26	1,088
Short-term Provisions 2008	–	13	134	252	260	26	685
Long-term Provisions 2008	395	–	8	–	–	–	403
	395	13	142	252	260	26	1,088
Short-term Provisions 2007	–	3	263	627	–	8	901
Long-term Provisions 2007	2,110	–	40	–	–	–	2,150
	2,110	3	303	627	–	8	3,051

With the exception of the regulatory and court decisions and other small items for which the expected timing of payments is not certain all other provisions are expected to be utilised within next twelve months from the balance sheet date.

BENEFIT LOYALTY PROVISION

Benefit loyalty provision covers the cost of equipment, accessories, gifts and services provided to participants in the mobile segment’s loyalty program in exchange for credits awarded primarily for airtime minutes spent. The provision has been recognized based on past experience of the usage of these credits by loyalty program participants. Expected outflow of provided benefits is CZK 252 million within one year (2007: CZK 347 million within one year and CZK 280 million from one year to three years).

The future obligation of the expenditures expected to be required amounting to CZK 252 million (2007: CZK 657 million) is fully covered by the amount of the provision in its present value.

EMPLOYEE-RELATED COSTS

Provisions for employee-related costs include expected costs associated with performance bonuses and provision for termination payments.

REGULATORY AND COURT DECISIONS

Provision for regulatory and court decisions is made for legal proceedings involving the Group companies (see Note 21).

20) FINANCIAL INSTRUMENTS

NET FAIR VALUES OF DERIVATIVE FINANCIAL INSTRUMENTS

At the balance sheet date, the total net fair values of derivative financial instruments were as follows:

Forward foreign exchange contracts in CZK million	31 December 2008	31 December 2007
Cash flow hedges		
– with positive fair value	–	4
– with negative fair value	–	(24)
Instruments not qualifying as hedges		
– with positive fair value	23	–
– with negative fair value	(7)	–
Total (Note 16)	16	(20)

21) CONTINGENCIES

The Company is involved in several court proceedings which have arisen from the ordinary course of business. Significant legal matters involving the Company are listed below:

INTERCONNECT ARRANGEMENTS

I. The Company has not yet agreed a 2001 price amendment to an agreement with T-Mobile Czech Republic a.s. governing interconnect arrangements. Despite the fact that in December 2003 the Czech Telecommunication Office (CTO) effectively ruled in favor of the mobile operator (i.e. CZK 899 million for T-Mobile Czech Republic a.s., the outstanding amount is bearing interest of 0.05% per day), the management believes that the amounts are not substantiated and are without merit. The Company has subsequently brought a legal action against the decision and obtained the suspension of the executability of the decision.

Meanwhile the question of jurisdiction between the civil courts and the administrative courts has arisen. As a result of the question of jurisdiction the suspension of the executability of the CTO decision temporarily expired. T-Mobile Czech Republic a.s., initiated the execution and claimed the remuneration of the litigable amount. The Company did not agree with the execution and used all its legal instruments to the termination of the execution. After 11 months of the execution it was evident that the burden of execution will continue for another several months, therefore the management decided to pay the executed amount in April 2008 and decided to continue in the legal action, in which the executed amount is claimed. No further disclosure is deemed appropriate as it could prejudice the Company's position in the dispute.

II. On 30 June 2005, Vodafone Czech Republic, a.s. (former Český Mobil/Oskar Mobil) brought a legal action at the Municipal Court in Prague against the Company for damages in the amount of CZK 538 million with appurtenances and for returning the unjustified enrichment of CZK 117 million with appurtenances. The Company is alleged to have failed to transmit the traffic to networks operated by other mobile operators according to respective interconnection agreements.

The High Court in Prague confirmed the Company's conclusion that CTO has already issued the final decision in favour of the Company and that the company Vodafone Czech Republic, a.s. has not respected this decision. The Municipal Court in Prague therefore terminated the legal action in September 2008. Based on the current situation the Company believes that the High Court in Prague will confirm the decision and will terminate the appeal proceedings. The management is confident that all risks, which may arise as a result of the litigation, are adequately provided for in the financial statements.

OFFICE FOR THE PROTECTION OF ECONOMIC COMPETITION PROCEEDINGS

The Company was subject to administrative proceeding before the Office for the Protection of Economic Competition (UOHS) relating to the alleged abuse of the dominant position by creation of unfair barriers against development on the market through the application of certain specific price plans for residential customers. UOHS rendered resolution dated 20 April 2005 imposing a fine to the Company in the total amount of CZK 210 million, which was consequently, after the Company completed and filed a protest, reduced to CZK 205 million.

The Company lodged a legal action in January 2006 and while the suspension of the executability was not granted the fine was paid. The Regional court in Brno refused the legal action and therefore the Company lodged a complaint to the Supreme Administrative Court on 19 October 2006.

OTHER LEGAL MATTERS

I. The Company is a defendant in a case filed by TELE 2 s.r.o. on 3 February 2005 asserting causes for alleged breach of act on protection of the competition by the Company in connection by offering certain pricing plans from September 2002 to December 2004. The amount of the claim is CZK 2,142 million with appurtenances.

The Company provided to the court extensive defense along with proposed items of evidence proving the legal imperfectness of the sued court's conduct. The management is convinced that the matter is adequately reflected in the financial statements and does not believe the resolution of this legal proceeding will have a material adverse effect on net income exceeding the amount of provision already made in the financial statements. No further disclosure is deemed appropriate as it could prejudice the Company's position in the dispute.

II. The Company is prosecuted by AUGUSTUS spol. s r.o. for an alleged loss of profit in the principal amount of approximately CZK 183 million with appurtenances relating to the years 1995 – 2001. AUGUSTUS spol. s r.o. claims that the Company illegitimately cancelled a contract for issue of phone cards, which was signed for unlimited period of time. Based on court decision, the Company paid an amount of the principal of CZK 83 million and the corresponding interest in August 2006 (total approximately CZK 139 million). Both parties subsequently filed an extraordinary appeal against the court judgment. The management believes that all risks, which may arise as a result of this litigation, are adequately provided for in the financial statements. No further disclosure is deemed appropriate as it could prejudice the Company's position in the dispute.

III. Subsequently AUGUSTUS spol. s r.o. filed another action against the Company regarding the amount of approximately CZK 294 million (status in April 2008). The legal action is based on the contract on phone cards issuing signed between Telefónica O2 Czech Republic, a.s. and AUGUSTUS spol. s r.o. that was terminated 13 years ago. AUGUSTUS spol. s r.o. evocates various new requirements in the prosecution that are not underpinned by the law or contradict each other eventually. The prosecution does not enable to sum the individual claims to be able to specify the total amount. Telefónica O2 Czech Republic, a.s. takes all steps in the lawsuit to defend thoroughly this unlawful claim and believes in success in this lawsuit. However, with respect to the claimed amount the lawsuit is disclosed separately.

IV. Furthermore, the Company is a defendant in a case filed by Vodafone Czech Republic, a.s. in May 2004 asserting causes for alleged breach of the act on protection of the competition by former Eurotel Praha, spol. s r.o. (damages amounting to CZK 1,043 million). Both parties filed their expert opinions to the court. The management believes that all risks, which may arise as a result of Vodafone Czech Republic, a.s. litigations, are adequately provided for in the financial statements. Decision of the Office for the Protection of Economic Competition (UOHS) on which Vodafone Czech Republic, a.s. based its claim was on 11 July 2007 cancelled by the Constitutional court. The Municipal court in Prague dismissed the claim on 21 August 2008. Vodafone Czech Republic, a.s. appealed against that decision on the High court in Prague. No further disclosure is deemed appropriate as it could prejudice the Company's position in the dispute.

The Company is a defendant in several other legal cases. The total amount of those individual cases exceeding CZK 5 million amounts to CZK 233 million. The management believes that the risk of losing these cases is less than probable and no provision was made in the financial statements.

22) COMMITMENTS

OPERATING LEASES

The aggregate future minimum lease payments under operating leases are as follows:

In CZK million	31 December 2008	31 December 2007
No later than 1 year	1,451	1,287
Later than 1 year and not later than 5 years	4,524	4,112
Later than 5 years	6,067	3,208
Total	12,042	8,607

The total lease payments relating to operating leasing of property, plant and equipment recognised as an expense in 2008 were CZK 1,320 million (2007: CZK 1,201 million). These lease agreements may contain clauses requiring restoration of the leased site at the end of the lease term. At present, such costs do not have a material impact on the Group's consolidated results of operations, financial position, or cash flow and therefore are not accounted for.

In 2004 the Group entered into a sale and lease back transaction and now leases the majority of its car fleet under operating leases. There are no contingent rent obligations. The lease arrangements include an option to renew the lease after the initial period. Lease payments are fixed and determinable, however they may be increased to reflect inflation and other market conditions such as interest rates changes (e.g. an increase in PRIBOR by more than 2% over a half year). There are no significant restrictions imposed by these lease arrangements, such as those concerning dividends, additional debt and further leasing. Total future lease payments relating to this contract in 2008 were CZK 395 million (2007: CZK 458 million).

CAPITAL AND OTHER COMMITMENTS

In CZK million	31 December 2008	31 December 2007
Capital and other expenditure contracted but not provided for in the financial statements	646	1,877

The majority of contracted amounts relate to the telecommunications network and service contracts.

23) SERVICE CONCESSION ARRANGEMENTS

The Company performs communication activities as defined under the Act on Electronic Communications based on a notification and a certificate from the Czech Telecommunication Office num. 516 as amended by later changes num. 516/1, 516/2 and 516/3.

The communication activities include (territory of the Czech Republic):
a) public fixed network of electronic communications,
b) public network for the transfer of radio and TV signal,
c) public fixed telephone network,
d) public mobile telephone network,
e) publicly accessible telephone services,
f) other voice services – service is provided as publicly available,
g) rent of circuits – service is provided as publicly available,
h) transmission of radio and TV signal – service is provided as publicly available,
i) transfers of data – service is provided as publicly available,
j) internet access services – service is provided as publicly available,
k) other voice services – service is not provided as publicly available.

The Company provides mobile services of electronic communications in the 900 and 1800 MHz frequency bands under the Global System for Mobile Communication ("GSM") standard on the basis of radio frequency assignment from CTO valid until 7 February 2016, in the 2100 MHz frequency band under the Universal Mobile Telecommunications System ("UMTS") standard on the basis of radio frequency assignment from CTO valid until 1 January 2022 and in the 450 MHz frequency band using technology CDMA2000 (Code Division Multiple Access – "CDMA"), where on the basis of radio frequency assignment from CTO valid until 7 February 2011 is provided broadband mobile access to Internet.

Validity of radio frequency assignment is possible to prolong for next period on the basis of application submitted to CTO in accordance with the Act on Electronic Communications. Relative to the current regulatory and business environment in the Czech Republic, contractual, legal, regulatory, competitive or other economic factors may limit the period during which the Company can benefit from the use of these radio frequency assignments in the future.

No additional expenses or any limitations connected with renewal of the radio frequency assignments are expected in accordance with the existing interpretation of regulatory provisions.

PROVISION OF ELECTRONIC COMMUNICATIONS SERVICES IN SLOVAKIA

In 2006 Telefónica O2 Slovakia was granted a licence for providing of electronic communications services by the means of the public electronic communications network – GSM and UMTS mobile telephone network within the area of the Slovak Republic. The licence has been granted for 20 years, i.e. until 2026. Validity of the licence is possible to prolong for next period on the basis of application submitted to the Telecommunication Office of the Slovak Republic.

The following obligations were part of the licence:

a) putting into operation the 800 GSM base stations and to cover 45% of population by the own network,
b) launch services in respect of welcome melodies and lease of phones.

These obligations were fulfilled in year 2008.

IMPOSITION OF OBLIGATIONS RELATED TO PROVISION OF UNIVERSAL SERVICE

During the year 2008, the Company provided the partial services within CTO imposed obligations to provide universal service:

a) periodic issuance of telephone directories with numbers of participants of the publicly accessible telephone service and access of end users to these directories*,
b) information service on the numbers of participants of the publicly accessible telephone service*,
c) public pay telephones services,
d) access for disabled to the public telephone,
e) supplementary services to service of connection at a fixed location to the public telephone network and the service of access to publicly available telephone services at a fixed location:
   - phased payment of the price for the establishment of connection to the public telephone network for consumer,
   - free selective barring of outgoing calls for the subscribers, and
   - free itemised billing of the price for consumer,
f) special price schemes, which are different from the price schemes used under normal business conditions, for low income persons, persons with special social needs and disabled persons.

* Services listed under letter a) and b) above are excluded from the universal service regime on the basis of CTO decision since 22th of December 2008. Providing of these services continues in commercial regime out of universal service.

24) SHARE CAPITAL AND RESERVES

	31 December 2008	31 December 2007
Nominal value per ordinary bearer share (CZK)	100	100
Number of shares	322,089,890	322,089,890
Nominal value per ordinary registered share (CZK)*	1,000	1,000
Number of shares*	1	1
Ordinary shares (in CZK million)	32,209	32,209

* One share owned by the National Property Fund of the Czech Republic bore special decision-making rights in accordance with the statutes of the Company. These special rights included namely decisions regarding the liquidation of the Company, changes in its activities, sale or lease of the Company or of its assets. This share was assigned to Telefónica, S.A. within the transferred 51.1% stake in the Company. From this date, the share has not borne special decision-making rights.

Shareholdings in the Company were as follows:

	31 December 2008	31 December 2007
Telefónica, S.A.	69.41%	69.41%
Other shareholders	30.59%	30.59%

Funds include a statutory reserve fund of CZK 6,442 million (2007: CZK 6,442 million) that is not distributable under ruling legislation. Equity settled share based payments reserve is not distributable.

On 21 April 2008 the Annual General Shareholders Meeting approved the restructuring of equity in the form of transfer of CZK 6,442 million from share premium to statutory reserve fund. Further the opening balance of the statutory reserve fund of CZK 6,442 million was transferred to retained earnings and used for distribution of dividend.

CAPITAL MANAGEMENT

The Company is not subject to any externally imposed capital requirements.

The Company's objectives when managing its capital are:

a) to safeguard the Company's ability to continue as a going concern so that it can provide value for its shareholders, and
b) to comply with all relevant legal requirements.

The investment strategy in the light of managing capital of the Company is to focus investment activities on pro-growth areas, i.e. broadband internet, IPTV, mobile services and corporate ICT solutions and on the expansion of the mobile services in Slovakia.

At present, the approach that the Company follows is not to retain surplus cash. In the following periods, the Board of Directors will continue to evaluate and carry out an in-depth analysis of the current and anticipated results of the Company, including scheduled and potential investments and cash flow generation and will establish the most adequate capital structure for accomplishment of the plans.

There is no other specific objective.

No changes were made in the objectives, policies or processes during the years 2008 and 2007.

The equity breakdown used in the capital management is following:

In CZK million	31 December 2008	31 December 2007
Capital	78,121	82,812
Equity settled share based payment reserve	47	–
Net unrealized gains reserve (cash flow hedge)	–	(20)
Total	78,168	82,792

25) HEDGING RESERVE

In CZK million	
Balance at 1 January 2007	(18)
Fair value losses in period	(17)
Fair value losses transfer to net profit	15
Balance at 31 December 2007	(20)
Fair value losses in period	24
Fair value losses transfer to net profit	(4)
Balance at 31 December 2008	–

26) RELATED PARTY TRANSACTIONS

The Group provides services to all related parties on normal commercial terms. Sales and purchase transactions with related parties are based on contractual agreements negotiated on normal commercial terms and conditions and at market prices. Outstanding balances of assets and liabilities are unsecured, interest free (excl. financial assets used for financing) and the settlement occurs either in cash or by offsetting. The financial assets balances are tested for the impairment at the balance sheet date, and no allowance or write off was incurred.

The following transactions were carried out with related parties:

I. PARENT COMPANY

In CZK million	31 December 2008	31 December 2007
Dividend paid to Telefónica, S.A.	11,179	11,179
Royalty fees (Telefónica, S.A)	626	9

II. OTHER RELATED PARTIES – TELEFÓNICA GROUP

In CZK million	31 December 2008	31 December 2007
a) Sales of services and goods	704	651
b) Purchases of services and goods	597	443
c) Capital purchases	5	1
d) Receivables	111	45
e) Payables	4,011	838
f) Short-term receivables (interest)	14	17
g) Interest income	374	315
h) Interest expense	92	7
i) Cash equivalents	6,344	5,107

As at 31 December 2008 the payables include a loan in amount of CZK 3,194 million (2007: CZK 798 million) provided to Telefónica O2 Slovakia, s.r.o. by the company Telfisa Global, BV. The loan bears a floating interest based on 1M BRIBOR. In 2008 the total interest expense was CZK 91 million (2007: CZK 7 million). The loans conditions are based on the arm's length principle.

The list of the Telefónica companies with which the Group had any transaction in 2008 includes the following entities: Telefónica, S.A., Telefónica de Espaňa, S.A.U., O2 Germany GmbH& CO.OHG, Telefónica Deutschland GmbH, O2 (UK) Ltd., O2 Communications (Ireland) Ltd., Telefónica Móviles España, S.A.U., Telefónica Móviles Argentina, S.A., Pléyade Peninsular, O2 Holdings Ltd., Manx Telecom Ltd., Telefónica Móviles Guatemala, S.A., Telefónica Móviles El Salvador, S.A. de C.V., Telefónica Móviles Panamá, S.A., Telefónica Móviles Chile, S.A., Otecel, S.A., Telefónica Móviles Nicaragua, S.A, Telefónica Móviles Columbia, S.A., Telefónica S. de Informática y Comunicaciones de Espana, S.A.U., Telefónica Investigación y Desrrollo, S.A., Médi Telecom, S.A., Portugal Telecom, S.G.P.S., S.A., Telfisa Global, BV., Telefónica International Wholesale Services, S.L., Telefónica Gestión de Servicios Compartidos, S.A., Telefónica Factoring E.F.C., S.A., Atento Chequia, Telefónica Compras Electrónica, S.L., Telefónica Móviles Mexico, S.A, Telefónica Móviles del Uruguay, S.A, Telefónica Móviles Peru, S.A, Telefónica Venezuela, S.A., Telefónica O2 Business Solutions, spol. s r.o, DELTAX Systems a.s., CZECH TELECOM Germany GmbH, CZECH TELECOM Austria GmbH, Telefónica O2 Slovakia, s.r.o.

III. OTHER RELATED PARTIES

a) Key management compensation

Members of the Board of Directors and of the Supervisory Board of the Telefónica O2 Czech Republic, a.s., were provided with benefits as follows:

In CZK million	31 December 2008	31 December 2007
Salaries and other short-term benefits	123	153
Personal indemnification insurance	7	9
Total	130	162

b) Loans to related parties

There were no loans provided to members of Board of Directors and Supervisory Board in 2008 and 2007.

No other loan was provided to related parties by the Group.

27) PRINCIPAL SUBSIDIARY UNDERTAKINGS

	Group's interest	Cost of investment in CZK million	Country of incorporation	Activity
SUBSIDIARIES				
1. Telefónica O2 Business Solutions, spol. s r.o. (formerly Telefónica O2 Services, spol. s r.o.)	100%	30	Czech Republic	Network and consultancy services in telecommunications
2. SPT TELECOM (Czech Republic) Finance B.V. (in liquidation)	100%	1	Netherlands	Financing other entities in the Group
3. CZECH TELECOM Germany GmbH	100%	29	Germany	Data transmission services
4. CZECH TELECOM Austria GmbH	100%	11	Austria	Data transmission services
5. Telefónica O2 Slovakia, s.r.o.	100%	1,219	Slovakia	Mobile telephony, internet and data transmission services
6. DELTAX Systems a.s.	100%	207	Czech Republic	IT/ICT services
ASSOCIATES				
7. První certifikační autorita, a.s.	23%	10	Czech Republic	Rendering of certification services
8. AUGUSTUS, spol. s r.o.	40%	–	Czech Republic	Sales by auctions and advisory services

On 30 November 2007 the voluntary liquidation process of the subsidiary CenTrade, a.s., in liquidation was effectively terminated. The Group received the liquidation surplus of CZK 32 million. The cancellation of the registration from the Commercial Register was performed as of 22 August 2008.

During the fourth quarter of 2007, SPT TELECOM (Czech Republic) Finance B.V. in liquidation commenced preparatory steps for the process of voluntary liquidation. Until the end of 2008, the key legal steps for dissolution of the company have been executed. The cancellation of the registration from the Commercial Register was performed as of 9 February 2008.

In December 2008, the Board of Directors of the Company approved the plan to merge Telefónica O2 Business Solutions, spol. s r.o. with DELTAX Systems a.s. This merger will become effective 1 January 2009 after the fulfillment of all legal conditions expected to be performed in the first half of 2009. Telefónica O2 Business Solutions, spol. s r.o. will become the legal successor while DELTAX Systems a.s. will be dissolved without liquidation. The assets, rights and obligations including labour rights and duties will be transferred to the successor.

28) POST BALANCE SHEET EVENTS

In January 2009, the Group sold a construction site and two administrative buildings of the former headquarters in Olšanská Street in Prague (see Note 8). Net gain from the sale of the real estates amounted to CZK 342 million. The assets did not meet criteria for classification as assets held for sale as at 31 December 2008.

In January 2009, the Telefónica Group won a tender for providing a complete portfolio of services for DHL throughout Europe. The entire project will be managed by the dedicated Service Management Centre in Prague and is expected to start in summer 2009.

There were no other events, which have occurred subsequent to the year-end, which would have a material impact on the financial statements at 31 December 2008.

FINANCIAL STATEMENTS

06

We are rarely the only ones pursuing the same goal. Beating the strong competition requires strength, courage, speed and endurance. The key to success is to combine opportunity with readiness.

FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2008

including Notes

CONTENT

GENERAL INFORMATION

Telefónica O2 Czech Republic, a.s. (the „Company") has a form of a joint stock company and is incorporated and domiciled in the Czech Republic. The address of its registered office is Za Brumlovkou 266/2, Prague 4, 140 22, Czech Republic.

The Company is a member of the Telefónica Group of companies (the „Telefónica Group") with a parent company, Telefónica, S.A. (the „Telefónica").

The Company is the principal supplier of fixed line telecommunication services and is one of the four suppliers of mobile telephone services in the Czech Republic.

The number of employees employed with the Company amounted in average to 8,542 in 2008 (2007: 9,004).

The Company's shares are traded on the Prague Stock Exchange and London Stock Exchange (GDRs).

These financial statements were approved for issue by the Company's Board of Directors on 20 February 2009.

ACQUISITION OF DELTAX SYSTEMS A.S.

In December 2007, the purchase of 100% of the shares in DELTAX Systems a.s. was approved by the Office for the Protection of Competition. The acquisition was effective as of 1 January 2008.

LIQUIDATION OF SUBSIDIARIES CENTRADE, A.S. IN LIQUIDATION AND SPT TELECOM (CZECH REPUBLIC) FINANCE B.V. IN LIQUIDATION

The liquidation process of CenTrade, a.s. in liquidation was effectively terminated on 30 November 2007. As of 22 August 2008 the registration of the company was cancelled from the Commercial Register. During the fourth quarter of 2007, SPT TELECOM (Czech Republic) Finance B.V. in liquidation commenced preparatory steps for the process of voluntary liquidation. Until the end of 2008, the key legal steps for dissolution of the Company have been executed. As of 9 February 2009 the registration of the company was cancelled from the Commercial Register.

MERGER OF DELTAX SYSTEMS A.S. WITH TELEFÓNICA O2 BUSINESS SOLUTIONS, SPOL. S R.O.

In December 2008, the Board of Directors of the Company approved the plan to merge Telefónica O2 Business Solutions, spol. s r.o. with DELTAX Systems a.s. This merger will become effective 1 January 2009 after the fulfillment of all legal conditions expected to be performed in the first half of 2009. Telefónica O2 Business Solutions, spol. s r.o. will become the legal successor while DELTAX Systems a.s. will be dissolved without liquidation. The assets, rights and obligations including labour rights and duties will be transferred to the successor.

INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF TELEFÓNICA O2 CZECH REPUBLIC, a.s.

We have audited the accompanying financial statements of Telefónica O2 Czech Republic, a.s. (the Company), which comprise the balance sheet as at 31 December 2008 and the income statement, statement of changes in equity and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

MANAGEMENT'S RESPONSIBILITY FOR THE FINANCIAL STATEMENTS

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

AUDITOR'S RESPONSIBILITY

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing and implementation guidance of the Chamber of Auditors of the Czech Republic. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

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

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

OPINION

In our opinion, the financial statements give a true and fair view of the financial position of the Company as of 31 December 2008, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union.

Ernst & Young

Ernst & Young Audit s.r.o.
Licence No. 401
Represented by

Brian Welsh
Partner

Radek Pav
Auditor, Licence No. 2042

20 February 2009
Prague, Czech Republic

INCOME STATEMENT

For the year ended 31 December 2008

In CZK million	Notes	Year ended 31 December 2008	Year ended 31 December 2007
Revenue	2	63,613	63,035
Gains from sale of non-current assets	8	855	43
Internal expenses capitalized in fixed assets	2	341	470
Operating expenses	3	(35,232)	(34,158)
Impairment loss	8, 9,110	(85)	(5)
Depreciation and amortisation	8, 9	(12,714)	(14,375)
Operating profit		16,778	15,010
Interest income	4	446	402
Interest expense	4	(313)	(438)
Other finance (expense)/income (net)	4	(121)	3
Profit before income tax		16,790	14,977
Taxes on income	5	(3,697)	(3,083)
Profit for the year		13,093	11,894
Earnings per share (CZK) – basic*	6	41	37

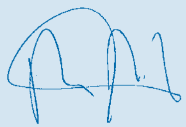
* There is no dilution of earnings as no convertible instruments have been issued by the Company.

BALANCE SHEET

As at 31 December 2008

In CZK million	Notes	31 December 2008	31 December 2007
ASSETS			
Property, plant and equipment	8	61,198	70,799
Intangible assets	9	21,702	21,467
Investment in subsidiaries and associates	27	1,507	1,300
Other financial assets	12	377	565
Non-current assets		84,784	94,131
Inventories	11	743	743
Receivables and prepayments	12	9,248	8,387
Income tax receivable		225	–
Held-to-maturity investments	13	–	27
Cash and cash equivalents	14	6,972	9,521
Current assets		17,188	18,678
Non-current assets classified as held for sale	8	96	328
Total assets		102,068	113,137
EQUITY AND LIABILITIES			
Ordinary shares	24	32,209	32,209
Share premium		24,374	30,816
Retained earnings, funds and reserves		24,896	21,400
Total equity		81,479	84,425
Long-term financial debts	16	3,098	3,062
Deferred taxes	17	3,299	3,353
Non-current provisions for liabilities and charges	19	402	2,146
Non-current other liabilities	15	175	452
Non-current liabilities		6,974	9,013
Short-term financial debts	16	98	6,207
Trade and other payables	15	12,838	11,732
Income tax liability		–	859
Provisions for liabilities and charges	19	679	901
Current liabilities		13,615	19,699
Total liabilities		20,589	28,712
Total equity and liabilities		102,068	113,137

These financial statements were approved by the Board of Directors on 20 February 2009 and were signed on its behalf by:



Salvador Anglada Gonzales
Chairman of the Board of Directors
and Chief Executive Officer

Jesus Pérez de Uriguen
Member of the Board of Directors
and Chief Financial Officer

STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

For the year ended 31 December 2008

In CZK million	Notes	Share capital	Share premium	Hedging reserve	Foreign exchange translation reserve	Equity settled share based payments reserve	Funds*	Retained earnings	Total
At 1 January 2007		32,209	30,816	(18)	(5)	–	6,269	19,344	88,615
Fair value gains (net of tax) – cash flow hedges		–	–	(2)	–	–	–	–	(2)
Currency translation differences – amount arising in year		–	–	–	5	–	–	–	5
Changes in statutory reserves and other movements		–	–	–	–	–	181	(164)	17
Net income and expense recognised directly in equity		–	–	(2)	5	–	181	(164)	20
Net profit		–	–	–	–	–	–	11,894	11,894
Total income and expense for the year		**–**	**–**	**(2)**	**5**	**–**	**181**	**11,730**	**11,914**
Dividends declared in 2007	7	–	–	–	–	–	–	(16,104)	(16,104)
At 31 December 2007		32,209	30,816	(20)	–	–	6,450	14,970	84,425
At 1 January 2008		32,209	30,816	(20)	–	–	6,450	14,970	84,425
Fair value gains (net of tax) – cash flow hedges		–	–	20	–	–	–	–	20
Net income and expense recognised directly in equity		–	–	20	–	–	–	–	20
Net profit		–	–	–	–	–	–	13,093	13,093
Total income and expense for the year		**–**	**–**	**20**	**–**	**–**	**–**	**13,093**	**13,113**
Equity restructuring	24	–	(6,442)	–	–	–	6,442	–	–
Transfer from reserve fund to retained earnings	24	–	–	–	–	–	(6,442)	6,442	–
Capital contribution		–	–	–	–	45	–	–	45
Dividends declared in 2008	7	–	–	–	–	–	–	(16,104)	(16,104)
At 31 December 2008		32,209	24,374	–	–	45	6,450	18,401	81,479

* Refer Note 24 regarding amounts not available for distribution.

MOVEMENT OF GAINS AND LOSSES RECOGNISED IN EQUITY

In CZK million	Gains/(losses) proceeding from cash flow hedges	Translation differences	Tax effect	Total
At 1 January 2007	(22)	(5)	4	(23)
Gains/(losses) arisen in the fiscal year	(17)	5	–	(12)
Gains/(losses) re-classified to the profit and loss account	15	–	–	15
At 31 December 2007	(24)	–	4	(20)
Gains/(losses) arisen in the fiscal year	(52)	–	(4)	(56)
Gains/(losses) re-classified to the profit and loss account	76	–	–	76
At 31 December 2008	–	–	–	–

CASH FLOW STATEMENT

For the year ended 31 December 2008

In CZK million	Notes	Year ended 31 December 2008	Year ended 31 December 2007
Net profit		13,093	11,894
Non-cash adjustments for:			
Income tax	5	3,697	3,083
Depreciation	8	10,838	12,522
Amortisation	9	1,876	1,853
Impairment loss	8, 9, 110	85	5
Disposals of obsolete assets		109	37
Profit on sale of property, plant and equipment		(840)	(52)
Net interest and other charges		(133)	36
Foreign exchange losses/(gains) (net)		39	(147)
Fair value changes		(15)	–
Change in provisions and allowances		(781)	(1,258)
Operating cash flow before working capital changes		27,968	27,973
Working capital adjustments:			
(Increase)/decrease in trade and other receivables		(836)	100
(Increase)/decrease in inventories		(279)	14
(Decrease)/increase in trade and other payables		(885)	55
Cash flows from operating activities		25,968	28,142
Interest paid		(392)	(428)
Interest received		367	375
Income tax paid		(4,833)	(4,074)
Net cash from operating activities		21,110	24,015

CASH FLOWS FROM INVESTING ACTIVITIES			
Purchase of property, plant and equipment		(4,070)	(3,688)
Purchase of intangible assets		(2,100)	(1,505)
Proceeds from sales of property, plant and equipment		4,585	71
Proceeds from marketable securities		24	53
Proceeds from discontinued operations		–	32
Cash purchase of financial investments		(30)	(836)
Dividends received		7	7
Grant of loan		(40)	(1,426)
Repayment of loan		40	1,583
Net cash used in investing activities		(1,584)	(5,709)
CASH FLOWS FROM FINANCING ACTIVITIES			
Proceeds from borrowings		650	–
Repayment of borrowings		(6,645)	–
Dividends – paid		(16,080)	(16,083)
Net cash used in financing activities		(22,075)	(16,083)
Net (decrease)/increase in cash and cash equivalents		(2,549)	2,223
Cash and cash equivalents at beginning of year		9,521	7,298
Cash and cash equivalents at the year end	14	6,972	9,521

ACCOUNTING POLICIES

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A) BASIS OF PREPARATION

The principal accounting policies applied in the preparation of these financial statements are set out below. These policies have been consistently applied to all years presented, unless otherwise stated.

The financial statements were prepared in accordance with International Financial Reporting Standards (“IFRS”) and all applicable IFRSs adopted by the EU. IFRS comprise standards and interpretations approved by the International Accounting Standards Board (“IASB”) and the International Financial Reporting Interpretations Committee (“IFRIC”).

Effective from 1 January 2005, a change in the Czech Act on Accounting No. 563/1991 Coll. requires the Company to prepare its financial statements in accordance with IFRS adopted by the EU (Regulation (EC) No 1606/2002). At the year-end, there is no difference in the policies applied by the Company between IFRS and IFRS adopted by the EU.

The financial statements are the separate financial statements of the Company and meet requirements of IFRS with respect to the preparation of parent’s separate financial statements. The Company also issued consolidated financial statements prepared for the same period in accordance with IFRS, which were approved for issue by the Board of Directors on 20 February 2009.

The financial statements were prepared under the historical cost convention except for non-current assets held for sale, inventory held at net realizable value, financial derivatives, share based payment liability and certain assets and liabilities acquired during business combinations, as disclosed in the accounting policies below.

The preparation of financial statements in conformity with IFRS required the Company to use certain critical accounting estimates. It also required management to exercise its judgement in the process of applying the Company’s accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed in Note T.

The amounts shown in these financial statements are presented in millions Czech Crowns ("CZK"), if not stated otherwise.

ADOPTION OF NEW OR REVISED IFRS STANDARDS AND INTERPRETATIONS (INCLUDES STANDARDS AND INTERPRETATIONS APPLICABLE FOR THE COMPANY)

In 2008, the Company applied the below stated interpretation and amendments, which are relevant to its operations. Adoption of the interpretation and amendments did not have any effect on the financial performance or position of the Company:

IFRIC 11 IFRS 2 Group and Treasury Share Transactions (issued 2005, effective date 1 March 2007)

The interpretation provides guidance on whether share-based transactions involving treasury shares or involving group entities (for example, options over parents' shares) should be accounted for as equity-settled or cash-settled share-based payment transactions in the stand-alone financial statements of the parent and group companies. This interpretation does not have an impact on the Company's financial statements.

STANDARDS AND INTERPRETATIONS ISSUED AND ENDORSED BY THE EUROPEAN UNION BUT NOT EARLY ADOPTED BY THE COMPANY (INCLUDES STANDARDS AND INTERPRETATIONS APPLICABLE FOR THE COMPANY)

IFRS 8 Operating Segments (issued 2006, effective date 1 January 2009)

The standard will replace IAS 14 Segment Reporting and requires entities to disclose segment information based on the information reviewed by the entity's chief operating decision maker. The adoption of the standard will not change the current presentation of segment information.

IAS 1 Amendment (issued 2007, effective date 1 January 2009) Presentation of financial statements, Comprehensive revision including requiring a statement of comprehensive income

The amendment to the standard separates owner and non-owner changes in equity. In addition, the standard introduces a statement of comprehensive income.

The Company does not expect any material effect on the Balance Sheet and the Income Statement relating to the adoption of this standard from the effective date 1 January 2009. This adoption will affect certain disclosures in the notes to the financial statements.

IAS 23 Amendment (issued 2007, effective date 1 January 2009) Borrowing Costs

The amendment requires the Company to capitalise borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset. Since the Company has already applied this policy as an allowed alternative treatment before, no impact is expected on the financial position of the Company.

IFRIC 13 Customer Loyalty Programmes (issued 2007, effective date 1 July 2008)

This interpretation addresses the accounting by entities that provide their customers with incentives to buy goods or services by providing awards as part of the sales transaction. The interpretation requires the entity that grants the awards to account for the sales transaction that gives rise to the award credits as a multiple element transaction and allocate the fair value of the consideration received or receivable between the award credits granted and the other components of the revenue transaction.

This adoption will affect current accounting policy in respect of change of the fair value awards measurement and change in the presentation in the financial statements. This will also affect certain disclosures in the notes to the financial statements. This adoption will not have material impact on the financial results in 2009.

IFRS 2 Amendment (issued 2008, effective date 1 January 2009) Share-based Payments

The amendment clarifies the definition of a vesting condition and prescribes the treatment for an award that is cancelled. The Company will apply IFRS 2 (Amendment) from 1 January 2009. This amendment will not have a material impact on the Company's financial statements.

STANDARDS AND INTERPRETATIONS ISSUED BUT NOT ENDORSED BY THE EUROPEAN UNION AND NEITHER EARLY ADOPTED BY THE COMPANY NOR EFFECTIVE (INCLUDES STANDARDS AND INTERPRETATIONS APPLICABLE FOR THE COMPANY)

Revised IFRS 3 Business Combinations (issued 2008, effective date 1 July 2009)

The standard introduces changes in the accounting for business combination that will impact the amount of goodwill recognised, the reported results in the period that an acquisition occurs and future reported results. The Company will apply IFRS 3 (Revised) prospectively to all business combinations from 1 January 2010.

IAS 27 Consolidated and Separate Financial Statements – Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate – Amendments (issued 2008, effective date 1 January 2009)

IAS 27 is amended for the following changes in respect of the holding companies separate financial statements:

i) The deletion of the "cost method". Making the distinction between pre-and post- acquisition profits is no longer required. All dividends will be recognized in profit or loss. However, the payment of such dividends requires the entity to consider whether there is an indicator of impairment; and
ii) In case of reorganisations where a new parent is inserted above an existing parent of the group (subject to meeting specific requirements), the cost of the subsidiary is the previous carrying amount of its share of equity items in the subsidiary rather than its fair value.

The Company does not expect any material effect relating to the adoption of these amendments.

IAS 27 Consolidated and Separate Financial Statements – Amendment (issued 2008, effective date 1 July 2009)

The most significant changes to IAS 27 are as follows:

i) Change in ownership interests of a subsidiary (that do not result in a loss of control) will be accounted for as an equity transaction and will have no impact on goodwill nor will it give a rise to a gain or loss.
ii) Losses incurred by the subsidiary will be allocated between the controlling and non-controlling interests (previously referred to as "minority interests"); even if the losses exceed the non-controlling equity investment in a subsidiary.
iii) On loss of control of a subsidiary, any retained interest will be remeasured to fair value and this will impact the gain or loss recognized on disposal.

The Company does not expect any material effect relating to the adoption of this amendment.

IFRS 5 Amendment (issued 2008, effective date 1 July 2009) Non-current Assets Held for Sale and Discontinued Operations

The amendment clarifies that all of subsidiary's assets and liabilities are classified as held for sale if a partial disposal sale plan results in loss of control. Relevant disclosure should be made for this subsidiary, if the definition of a discontinued operation is met. A consequential amendment to IFRS 1 states that these amendments are applied prospectively from the date of transition to IFRS. The Company will apply the IFRS 5 (Amendment) prospectively to all partial disposals of subsidiaries from 1 January 2010.

IAS 36 Amendment (issued 2008, effective date 1 January 2009) Impairment of Assets

Where fair value less costs to sell is calculated on the basis of discounted cash flows, disclosures equivalent to those for value-in-use calculation should be made. The Company will apply the IAS 36 (Amendment) and provide the required disclosure where applicable for impairment tests from 1 January 2009.

The Company does not intend to early adopt any of those standards and interpretations before their effective dates.

B) FOREIGN CURRENCIES

i) Functional and presentation currency
Items included in the financial statements of the Company are measured using the currency of the primary economic environment in which the Company operates ("the functional currency"). The financial statements are presented in Czech Crowns ("CZK"), which is the Company's functional and presentation currency.

ii) Transactions and balances
Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the date of the transaction. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement, except when deferred in equity as qualifying cash flow hedges. Such balances of monetary items are translated at period-end exchange rates. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Non-monetary items that are measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

C) PROPERTY, PLANT AND EQUIPMENT

All property, plant and equipment are initially recorded at cost and, except for freehold land, are subsequently carried at its cost less any accumulated depreciation and accumulated impairment losses. Freehold land is subsequently stated at cost less impairment charges.

Property, plant and equipment acquired in business combinations are stated at their acquisition costs (which are equal to their fair value at the date of acquisition) less depreciation and impairment charges.

Property, plant and equipment include all costs directly attributable to bringing the asset to working condition for its intended use. With respect to the construction of the network, this comprises every expenditure up to the customers' premises, including the cost of contractors, materials, direct labour costs and interest cost incurred during the course of construction.

Repairs and maintenance costs are expensed as incurred.

Items of property, plant and equipment that are retired are not intended for sale and are not expected to create any future economic benefits or are otherwise disposed of, are eliminated from the balance sheet, along with the corresponding accumulated depreciation. Any gain or loss arising from retirement or disposal is included in net operating income, i.e. net gain or loss is determined as the difference between the net disposal proceeds, if any, and the carrying amount of the item.

Items of property, plant and equipment, excluding freehold land, are depreciated from the time they are available for use, using the straight-line method. Depreciation ceases at the earlier of the date the asset is de-recognised or the date the asset is classified as held for sale.

Depreciation does not cease, when the asset becomes temporarily idle or retired from active use, unless the asset is fully depreciated.

Estimated useful lives adopted in these financial statements are as follows:

	Years
Freehold buildings	up to 40
Cable and other related plant	5 to 25
Exchanges and related equipment	up to 10
Other fixed assets	2 to 10

Freehold land is not depreciated as it is deemed to have an indefinite life.

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

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater then its estimated recoverable amount (refer to Note F Impairment of assets).

D) INTANGIBLE ASSETS

Intangible assets include computer software, purchased goodwill, licenses, trade names, customer base and roaming contracts. Computer software mainly represents the external acquisition costs of the Company's information systems that are intended for use within the Company. Generally, costs associated with developing or maintaining computer software programs are recognised as an expense as incurred. However, costs that are directly associated with identifiable and unique software products controlled by the Company and that have a probable economic benefit exceeding the cost beyond one year, are recognised as intangible assets. Computer software costs recognised as assets are amortised using the straight-line method over their useful lives, generally one to five years.

Intangible assets acquired in business combinations are stated at their acquisition costs (which are equal to their fair value at the date of acquisition) less amortisation and impairment charges and are amortised on a straight-line basis over their estimated useful lives. Customer bases are amortised over a period of the remaining average terms of the binding contracts.

Acquired licenses are recorded at cost and amortised on a straight-line basis over the remaining life of the license (i.e. over 15 to 20 years), from the start of commercial service, which best reflects the pattern by which the economic benefits of the intangible assets will be utilised by the Company.

Intangible assets with an indefinite useful life are not amortised. They are subject to the regular impairment reviews (see Note 9 and Note 110).

Goodwill, arising from the purchase of subsidiary undertakings and interests in associates and joint ventures, represents the excess of the fair value of the purchase consideration over the fair value of the net assets acquired. Goodwill is not amortised but is tested for impairment at least annually or anytime there are indications of a decrease in its value.

The Company reviews at least at the balance sheet date the useful lives of intangible assets that are not amortised to determine whether events and circumstances continue to support an indefinite useful life assessment for that asset. If they do not, the change in the useful life assessment from indefinite to finite is accounted for as a change in an accounting estimate.

On the balance sheet date, carrying amounts, residual values and the useful lives of assets are reviewed, revised and if necessary prospectively amended and accounted for as a change in an accounting estimate.

Intangible assets that are no longer in use and no future economic benefits are expected or that are disposed of for any other reason are de-recognised from the balance sheet together with the corresponding accumulated amortisation (for amortised assets only). All gains or losses arising in this respect are recognised in net operating income, i.e. net gain or loss is determined as the difference between net disposal proceeds, if any, and the carrying amount of the asset.

Intangible assets, with the exception of assets with an indefinite useful life, are amortised using the straight-line method from the time they are available for use. Amortisation ceases at the earlier of the date the asset is de-recognised, the date the asset is classified as having the indefinite useful life or the date the asset is classified as held for sale.

E) NON-CURRENT ASSETS CLASSIFIED AS HELD FOR SALE

The Company classifies separately in the balance sheet a non-current asset (or disposal group) as held for sale if its carrying amount will be recovered principally through a sale transaction rather than through continuing use. For this to be the case, the asset (or disposal group) is available for immediate sale in its present condition subject only to terms that are usual and customary for sales of such assets (or disposal groups), its sale is highly probable and sale is expected within one year.

The Company measures a non-current asset (or disposal group) classified as held for sale at the lower of its carrying amount and fair value less costs to sell.

The Company recognizes an impairment loss for any initial or subsequent write-down of the asset (or disposal group) to fair value less costs to sell and is accounted for as an impairment loss with impact in the income statement of the relevant period.

From the moment the asset is classified as held for sale and eventually revalued, it ceases to be depreciated/amortised and impairment is only being determined.

Any gain from any subsequent increase in fair value less costs to sell, but not in excess of the cumulative impairment loss that has been recognized, is determined and is accounted for in the income statement.

F) IMPAIRMENT OF ASSETS

Property, plant and equipment and other assets, including goodwill and intangible assets, are reviewed for impairment losses whenever events or changes in circumstances indicate that the carrying amount may not be recoverable or at least on an annual basis for goodwill and for intangibles with an indefinite useful life and for intangibles not yet in use. An impairment loss is recognised for the amount by which the carrying amount of the asset exceeds its recoverable amount, which is the higher of an asset's net selling price and value in use. For the purposes of assessing impairment, assets are grouped at the lowest level, for which there are separately identifiable cash flows (cash-generating units).

Impairment losses are recognised in expenses when incurred. A previously recognised impairment loss is reversed (except for the Goodwill impairment loss) only if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognised. If that is the case the carrying amount of the asset is increased to its recoverable amount. That increased amount cannot exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognised for the asset in prior years. Such reversal is recognised as a reduction in the expenses in the period in which the reversal occurs.

G) INVESTMENTS AND OTHER FINANCIAL ASSETS

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

Financial assets that are acquired principally for the purpose of generating a profit from short-term fluctuations in price are classified as financial assets at fair value through profit or loss and are included in current assets. During 2008 and 2007, the Company did not hold any financial assets in this category.

Investments with a fixed maturity that management has the intent and ability to hold to maturity are classified as held-to-maturity and are disclosed as current or non-current assets, depending on the period in which the settlement will take place.

Loans and receivables are financial assets with fixed or determinable payments that are not quoted in an active market and are measured at amortised cost using an effective interest rate method and are disclosed as current or non-current assets, depending on the period in which the settlement will take place.

Investments intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, are classified as available-for-sale; these are included in non-current assets unless management has expressed the intention of holding the investment for less than 12 months from the balance sheet date or unless they will need to be sold to raise operating capital, in which case they are included in current assets.

Management determines the appropriate classification of its investments at the time of the purchase and re-evaluates such designation on a regular basis, as required under IAS 39.

All purchases and sales of investments are recognised on the trade date, which is the date that the Company commits to purchase or sell the asset. The cost of purchase includes all transaction costs. Financial assets at fair value through profit or loss and available-for-sale investments are subsequently carried at fair value, whilst held-to-maturity investments are carried at amortised cost using the effective interest rate method. Realised and unrealised gains and losses arising from changes in the fair value of financial assets at fair value through profit or loss are included in the income statement in the period in which they arise. On the contrary, unrealised gains and losses arising from changes in the fair value of available-for-sale investments are included in equity in the period in which they arise, except for impairment losses, until the financial asset is de-recognised, at which time the cumulative gain or loss previously recognised in equity is recognised in the income statement.

IMPAIRMENT OF FINANCIAL ASSETS

The Company assesses at each balance sheet date whether financial assets or groups of financial assets are impaired.

1) Assets carried at amortized costs

If there is objective evidence that an impairment loss on loans and receivables or held to maturity investments carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced either directly or through use of an allowance account. The amount of the loss is recognised in the income statement.

The Company first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. If it is determined that no objective evidence of impairment exists for individually assessed financial assets, whether significant or not, it is included in a group of financial assets with similar credit risk characteristics and that group of financial assets is collectively assessed for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed. Any subsequent reversal of an impairment loss is recognised in the income statement and only to the extent that the carrying amount of the financial asset does not exceed its amortised cost at the reversal date.

In relation to trade receivables, a provision for impairment is made when there is objective evidence (such as the probability of insolvency) that the Company will not be able to collect all of the amounts due under the original terms of the invoice. The carrying amount of the receivable is reduced through use of an allowance account. Impaired debts are derecognised when they are assessed as uncollectible or sold.

2) Available-for-sale financial assets

If this asset is impaired, the cumulative loss that had been previously recognised (due to fair value revaluation) directly in equity shall be removed from equity and recognised in profit or loss even though the financial asset has not been derecognised.

The amount of the cumulative loss that is removed from equity and recognised in profit or loss shall be the difference between the acquisition cost (net of any principal repayment and amortisation) and the current fair value, less any impairment loss previously recognised in profit or loss.

Reversals of impairment losses on debt instruments are reversed through profit or loss, if the increase in fair value of the instrument can be objectively related to an event occurring after the impairment loss was recognised in the income statement.

DE-RECOGNITION OF FINANCIAL ASSETS

A financial asset is de-recognised when:

a) the rights to receive cash flow from the asset have expired,
b) the Company retains the right to receive cash flow from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a “pass-through” arrangement, or

c) the Company has transferred its rights to receive cash flows from the assets and either has transferred substantially all the risks and rewards of the asset, or has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

H) LEASES

The determination of whether an arrangement is, or contains a lease is based on the substance of the arrangement at inception date of whether the fulfilment of the arrangement is dependent on the use of specific asset or assets and the arrangement conveys a right to use the assets.

Leases under which a significant portion of the risks and benefits of ownership are effectively retained by the lessor are classified as operating leases. Payments made under operating leases are charged to the income statement on a straight-line basis over the period of the lease.

When an operating lease is terminated before the lease period has expired, any payment that is required to be made to the lessor by way of penalty is recognised as an expense in the period in which termination takes place.

Leases of property, plant and equipment where the Company bears substantially all the risks and rewards of ownership are classified as finance leases. Finance leases are capitalized at the inception of the lease at the lower of the fair value of the leased property or the present value of the minimum lease payments. Each lease payment is allocated between the liability and finance charges so as to achieve a constant rate on the finance balance outstanding. The corresponding lease obligations, net of finance charges, are included in other long-term payables (depending on maturity).

The interest element of the finance cost is charged to the income statement over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period. If there is a reasonable certainty that the lessee will obtain ownership by the end of the lease term, the period of expected use is the useful life of the asset; otherwise the property, plant and equipment acquired under finance leases are depreciated over the shorter of the useful life of the asset or the lease term.

A sale and lease back transaction involves the sale of an asset and the leasing back of the asset. Within the Company's operations the selling price of the asset and lease payments are independent and established at fair value. Therefore the gain from the sale of the asset and the lease payments are accounted as two separate transactions.

I) INVENTORIES

Inventory is stated at the lower of cost or net realisable value. Costs of inventories include the purchase price and related costs of acquisition (transport, customs duties and insurance). The cost of inventory is determined using weighted average cost. Net realisable value is the estimate of the selling price in the ordinary course of business, less the costs of completion and selling expenses.

J) TRADE RECEIVABLES

Trade receivables are carried at original invoice amount less allowance for impairment of these receivables. Such allowance for impairment of trade receivables is established if there is objective evidence that the Company will not be able to collect all amounts due according to the original terms of receivables. The amount of the allowance is the difference between the carrying amount and the recoverable amount, being the present value of expected cash flows, discounted at the initial market rate of interest for similar borrowers. Cash flows relating to short-term receivables are usually not discounted. The amount of the allowance is recognized in the income statement.

K) CASH AND CASH EQUIVALENTS

Cash and cash equivalents are carried in the balance sheet at cost. For the purposes of the cash flow statement, cash and cash equivalents comprise cash on hand, deposits held at call with banks, other short-term highly liquid investments with original maturities of three months or less, and bank overdrafts. Bank overdrafts are shown within borrowings in current liabilities on the balance sheet.

L) FINANCIAL DEBT

Borrowings are recognised initially at the proceeds received, net of transaction costs incurred. In subsequent periods, borrowings are stated at amortised cost using the effective interest rate method; any difference between proceeds (net of transaction costs) and the redemption value is recognised in the income statement over the period of the borrowings.

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

Interest costs on borrowings used to finance the acquisition and construction of qualifying assets are capitalized during the period of time that is required to complete and prepare the asset for its intended use. Other borrowing costs are expensed.

M) CURRENT AND DEFERRED INCOME TAXES

Taxation expense represents both current and deferred taxation, where appropriate. Current income tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted by the balance sheet date in the relevant country.

Current income tax relating to items recognised directly in equity is recognised in equity and not in the income statement.

Deferred income taxation is calculated using the liability method applied to all temporary differences arising between the tax basis of assets and liabilities and their carrying values for financial reporting purposes. Currently enacted tax rates and laws expected to apply when the asset is realised or the liability is settled are used to determine the deferred income tax.

The principal temporary differences arise from differences in the tax and accounting values of property, plant and equipment, impairment of receivables and allowance for obsolete and slow moving inventories, non tax deductible allowances and provisions, unused tax credits and, in relation to acquisitions, on the difference between the fair values of the net assets acquired and their tax base.

Deferred income tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

The Company accounts for the tax consequences of transactions and other events in the same way that it accounts for the transactions and other events themselves. Thus, for transactions and other events recognised in the income statement, any related tax effects are also recognised in the income statement. For transactions and other events recognised directly in equity, any related tax effects are also recognised directly in equity. Similarly, the recognition of deferred tax assets and liabilities in a business combination affects the amount of goodwill.

Deferred income tax assets and tax liabilities are offset, if a legally enforceable right exists to set off current tax assets against current income tax liabilities and the deferred income taxes relate to the same taxable entity and the same taxation authority. The same applies for offsetting of current tax assets and liabilities.

N) EMPLOYEE BENEFITS

1) Pension obligations
Contributions are made to the Government's health, retirement benefit and unemployment schemes at the statutory rates applicable during the period and are

based on gross salary payments. The arrangements of the Government's health, retirement benefit and unemployment schemes correspond to the arrangements for defined contribution plans. The Company has no further payment obligations once the contributions have been paid. The expense for the contributions is charged to the income statement in the same period as the related salary expense. The Company also makes contributions to defined contribution schemes operated by external pension companies. These contributions are charged to the income statement in the period to which the contributions relate.

2) Redundancy and termination benefits
Redundancy and termination benefits are payable when employment is terminated before the normal retirement or contract expiry date. The Company recognises redundancy and termination benefits when it is demonstrably committed to terminate the employment of current employees according to a detailed formal plan without possibility of withdrawal.

Benefits falling due more than 12 months after the balance sheet date are discounted to present value. There are no redundancy and termination benefits falling due more than 12 months after the balance sheet date.

3) Bonus plans
The Company recognises a liability for bonuses based on a formula that takes into consideration certain performance related measures, such as turnover or free cash flow, after certain adjustments. The Company recognises a provision where the Company is contractually obliged or where there is a past practice that has created a constructive obligation.

O) SHARE-BASED COMPENSATION

During 2006, the Company introduced performance compensation systems linked to the market value of shares of the parent company, Telefónica, S.A. Certain compensation plans are settled in cash, while the others are settled via the delivery of shares.

IFRS 2 is applied to compensation schemes linked to the share price with the following accounting treatment:

Option plans that can be cash-settled or equity-settled at the option of the employee are recognized at the fair value on the grant date of the liability and equity components of the compound instrument granted.

In the cash-settled share option plan, the total cost of the rights to shares granted are expensed over the period during which the beneficiary earns the full right to exercise the options (vesting period). The total cost of the options is initially measured based on their fair value at the grant date calculated by the Black-Scholes option pricing model, taking into account the terms and conditions established in each share option plan. At each subsequent reporting date, the Company revises its estimate of fair value and the number of options it expects to vest, booking any change in the liability through the income statement for the period, if appropriate.

For the equity-settled share option plan, fair value at the grant date is measured using the binominal methodology. These plans are expensed during the vesting period with a credit to equity. At each subsequent reporting date, the Company revises its estimate of the number of options it expects to be exercised, with a corresponding adjustment to equity. As the plan will be settled by a physical delivery of equity instruments of the parent, Telefónica, S.A., to the employees, the personnel expense accrued is recognised against equity.

P) PROVISIONS

Provisions are recognised when the Company has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and a reliable estimate of the amount can be made. Where the Company expects a provision to be reimbursed, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain.

Q) REVENUE RECOGNITION

Revenue, shown net of Value Added Tax and any discounts, and after eliminating sales within the Company, comprises goods sold and services provided. Revenues are measured at their fair value of the consideration received or receivable. The amount of revenue is recognised if it can be measured reliably and it is probable that the economic benefits associated with the transaction will flow to the Company. If necessary, revenue is split into separately identifiable components.

The Company offers customers free minutes for a selected price based on a chosen customer plan. Free unused minutes at the end of the month might be rolled over to the following month. The Company is not obliged to reimburse the customer for unused minutes and the option of rolling over any unused minutes is valid for only one month.

The Company recognises revenue for free minutes in the period when the related services are provided and consumed, if material. Any rollover minutes are deferred and recognised when the minutes are used or the option expires.

In assessing whether revenue should be recognised gross, i.e. with separate disclosure of costs to arrive at gross profit, or on a net basis, the Company considers these indicators of gross revenue reporting:
a) the Company is the primary obligor in the arrangement,
b) the Company has general inventory risk,
c) the Company has price latitude,
d) the Company changes the product or performs part of the service,
e) the Company has discretion in supplier selection,
f) the Company is involved in the determination of product or service specifications,
g) the Company has credit risk,
h) the Company has the ability to set the terms of the transaction,
i) the Company has the managerial control over the transaction.

The relative strength of each indicator is considered when concluding which accounting treatment to use for principal/agency arrangement.

If a transaction is considered to meet conditions of an agency arrangement, the revenue is recognised only at the amount of the commission received/realised, e.g. premium rate lines.

Revenue from fixed price construction contracts (long-term contracts) is recognised on the percentage of completion method, measured by reference to the percentage of actual cost incurred to date to estimated total costs of the contract. An expected loss on the construction contract is recognised as an expense immediately, when it is probable that total contract costs will exceed total contract revenue.

1) FIXED LINE BUSINESS REVENUES
Revenue is recognized as follows:

DOMESTIC AND INTERNATIONAL CALL REVENUES
Domestic and international call revenues are recognised in the income statement at the time the call is made.

UNIVERSAL SERVICE
The Company is obliged to render certain fixed line telephony services defined by the Act on Electronic Communications. The Company follows the accounting policy of Telefónica Group and recognises the compensation of revenues attributable to the Company using the gross principle as well as recognises the compensation when CTO approves the total compensation and decides about percentage shares and absolute amounts of other operators contributions.

SUBSCRIPTION REVENUES
Revenue is recognised in the income statement in the period in which the services are rendered.

REVENUES FROM SALES OF PREPAID CARDS
Prepaid call card sales are deferred until the customer uses the stored value in the card to pay for the relevant calls. The expiry date for prepaid cards is not longer than 36 months.

CONNECTION FEES

Connection fees, arising from the connection of the customers to the Company's network, are deferred and recognised in the income statement over the estimated average customer relationship period on the basis of the degressive accounting method.

EQUIPMENT SALES AND OTHER SALE OF GOODS

Revenue from the sale of telephone equipment and accessories and other sale of goods is recognised at the time of sale i.e. when the Company has transferred to the buyer the significant risks and rewards of ownership of the goods.

LOCAL LOOP UNBUNDLING

Revenue from access to the local loop unbundling is deferred in the income statement and recognised in the period in which the service is rendered. Regular monthly fee is recognised on the straight line basis in the period when the service is consumed. Revenue from the preparation of the location (collocation) for an alternative operator is recognized upfront in the income statement when it occurs.

2) MOBILE BUSINESS REVENUES

The Company earns mobile services revenue from customers usage of the Company's network, interconnection and roaming – collectively, "Mobile service revenue". The Company also earns revenue from the sale of mobile telephone equipment and accessories as well as from activation fees.

AIRTIME REVENUES

Postpaid customers are billed monthly in arrears for airtime revenues. Revenue from post-paid customers is recognised as their airtime and other services are used. Prepaid customers recharge a credit, which entitles them to a certain value of airtime and other services. Revenue from prepaid customers is deferred and recognized as the airtime and other services are used. Upon termination of the customer contract or expiration of voucher (up to 14 months), all deferred revenue for unused airtime is recognized in income.

Both, post-paid and prepaid products may include deliverables such as a handset, activation and airtime and that are defined as arrangements with multiple deliverables. The arrangement consideration is allocated to each deliverable, based on its fair value. Revenue allocated to the identified deliverables in each revenue arrangement is recognized based on the same recognition criteria of the individual deliverables at the time the product or service is delivered.

EQUIPMENT SALES AND MOBILE SERVICES

Monthly service revenues and revenues from handset sales are recognized as revenue when the product or service is delivered to the distributor or to the end customer. Resulting losses from sale of handsets at a discount are recognised at the date of sale.

ROAMING REVENUES

Mobile segment derives roaming revenue as a result of airtime and other services used by the mobile segment's customers roaming on partners' networks in other countries and vice versa. Amounts receivable from and payable to roaming partners are netted and settled net on a regular basis.

COSTS

Commissions and discounts directly related to the sale of equipment, SIM cards and activations are netted against revenue in the period the product is sold to the dealer, distributor or the end customer. Other commission payments to dealers for activations, various marketing promotions and other activities are included in the costs of sales for the period.

3) INTERCONNECT REVENUES

Interconnect revenues are derived from calls and other traffic that originate in other domestic and foreign operators' network but use the Company's network. These revenues are recognised in the income statement at the time when the call is received in the Company's network. The Company pays a proportion of the call revenue it collects from its customers to other domestic and foreign operators' for calls and other traffic that originate in the Company's network but use other domestic and foreign operators' network. Amounts receivable from and payable to other domestic and foreign operators are netted and settled net on a regular basis.

4) INTERNET, IPTV AND DATA SERVICES
The Company earns revenue from providing Internet services, IPTV and other data services. Revenue from such services is recognised at the time the service is provided.

5) DIVIDEND INCOME
Dividend income is recognized when the right to receive payment is established.

6) INTEREST
Revenue is recognised as interest accrues (using the effective interest method).

R) DIVIDEND DISTRIBUTION

Dividend distribution to the Company's shareholders is recognized as a liability in the Company's financial statements in the period in which the dividends are approved by the Company's shareholders.

S) FINANCIAL INSTRUMENTS

Financial instruments carried on the balance sheet include cash and bank balances, investments, receivables, payables, borrowings and derivatives. Detailed figures are described in Note 16.

FINANCIAL RISK MANAGEMENT
The Company's is exposed to a variety of financial risks, including the effects of changes in debt market prices, foreign currency exchange rates and interest rates as a result of ordinary business, debt taken on to finance its business and net investment in foreign operations.

The Company's overall risk management focuses on the unpredictability of financial markets and seeks to minimize potential adverse effects on the financial performance of the Company. The Company uses either derivative financial instruments (such as forward and swap contracts) or non-derivative instruments (such as cash instruments) to hedge certain exposures.

The Company does not conduct any speculative trading activities.

Risk management is carried out by the treasury department under approved policies. The Board of Directors provides written principles for overall risk management. In line with these principles, policies exist for specific areas, such as foreign exchange risk, interest rate risk, credit risk, liquidity risk, use of derivative financial instruments and investing excess liquidity.

i) Foreign currency risk
The Company is exposed to foreign currency risk arising from various currency exposures, primarily with respect to the Euro, partially to US Dollar and Slovak Crown:
a) balance sheet items (such as debt, receivables, payables) denominated in foreign currency,
b) probable forecasted transactions or firm commitments (such as purchases or sales) denominated in foreign currency,
c) net investment in Slovak subsidiary (functional currency differs from CZK).

The Company's objective in managing its exposure to foreign currency fluctuations is to minimize earnings and cash flow volatility associated with foreign exchange rate changes.

The Company primarily hedges the balance sheet foreign currency exposure, mainly long term debt denominated in EUR and net payables in EUR or USD. Non-derivative instruments are currently used for hedging this kind of exposure.

Additionally, the Company uses to a certain extent derivative hedging via short term forwards to buy respective foreign currency for highly probable or committed purchase transactions, primarily up to a 6 months horizon.

ii) Interest rate risk
The Company is exposed to interest rate risk arising from:
a) floating interest rate bearing cash investments and debt instruments,
b) fair value of debt on fixed interest rate.

The Company's income and operating cash flows are substantially independent of changes in market interest rates. The cash assets and short term debt are currently maintained on floating rates while long term debt instruments are on fixed rates. The Company may sometimes use interest rate swaps and forward rate agreements to manage a mix of fixed and variable rate debts.

iii) Liquidity rate risk
The Company's essential objective of liquidity risk management is to have ready access to cash resources sufficient to meet all its cash payment obligations as they fall due, allowing some flexibility. The cash resources consist of cash instruments, marketable securities and available committed credit facilities.

The Company is particularly focusing on the liquidity profile within the time horizon of the next 12 months considering projected cash flow from operations and maturity structure of both debt obligations and financial investments. The balance between funding continuity and flexibility is managed through maintaining the possible use of bank overdrafts or bilateral credit lines.

iv) Credit risk
Concentrations of credit risk, with respect to trade accounts receivable, are limited due to the large number of customers. However, substantially all trade receivables are concentrated within the Czech Republic. Although the Company does not currently foresee a dramatically higher credit risk associated with these receivables, repayment is significantly impacted by the financial stability of the national economy.

The Company trades only with recognized, creditworthy third parties. It is the Company's policy that all customers who wish to trade on credit terms are subject to credit verification procedures. In addition, receivable balances are monitored on an ongoing basis with the result that the Company's exposure to bad debts is not significant. The maximum exposure is the carrying amount as disclosed in Note 12. There are no significant concentrations of credit risk within the Company.

With respect to credit risk arising from the financial assets of the Company, which comprise cash and cash equivalents, available for sale investments and certain derivative instruments, the Company's exposure to credit risk arises from default of the counterparty, with a maximum exposure equal to the carrying amount of these instruments.

Credit Risk is managed by the Credit Management Department and is based on three main activities:
a) monitoring of accounts receivables: regular monitoring of payment moral of existing customers and monitoring and analyzing of the receivable aging structure (internal and external indicators of any potential bad debts),
b) prevention: scoring of new customers – checking procedures (Black Lists, External Debtors Register, other information), set up the limits or/and collection of the deposit according to customer segments, products and set up the credit limits for indirect sales partners (dealers, distributors, retailers) for purchase of our products, „securing" of credit limits (deposits, receivables insurance, bill of exchange, pledge of real estate, bank guarantee etc.). Guarantees are either in cash (deposits) or there are special procedures to collect cash for the other securing tools (insurance etc.),
c) collection: reasonable, effective and continual collection process is the additional tool of bad debts decrease and prevention as well.

NEW CREDIT MANAGEMENT ACTIVITIES DURING LAST YEARS
During last years the Company introduced new credit management activities such as:
a) implementation of the connection to the external Debtors Register Solus (sharing debtors data with other members – banks, other telecommunication operators, leasing companies etc.),
b) implementation of the credit management best practice from the merge of the fixed and mobile business in all company activities,
c) checking of the new activation by using of fixed and mobile Black Lists,
d) implementation of tight activation rules for all distribution channels.

ACCOUNTING FOR DERIVATIVE FINANCIAL INSTRUMENTS AND HEDGING ACTIVITIES
Derivative financial instruments are initially recognised in the balance sheet at cost and subsequently are re-measured at their fair value. The method of recognising the resulting gain or loss is dependent on the nature of the item being hedged. On the date a derivative contract is entered into, the Company designates certain derivatives as either:
a) hedge of the fair value of a recognised asset or liability (fair value hedge), or
b) hedge of a forecasted transaction or of a firm commitment (cash flow hedge).

Changes in the fair value of derivatives that are designated and qualify as fair value hedges and that are highly effective are recorded in the income statement, along with changes in the fair value of the hedged asset or liability that is attributable to the hedged risk.

Changes in the fair value of derivatives that are designated and qualify as cash flow hedges and that are highly effective are recognised in equity. Where the forecasted transaction or firm commitment results in the recognition of an asset or of a liability, the gains and losses previously deferred in equity are transferred from equity and included in the initial measurement of the cost of the asset or liability. Otherwise, amounts deferred in equity are transferred to the income statement and classified as revenue or expense in the same periods during which the hedged firm commitment or forecasted transaction affects the income statement.

Certain derivative transactions, while providing effective economic hedges under the Company's risk management policies, either do not qualify for hedge accounting under the specific rules in IAS 39 or the Company has elected not to apply the specific IAS 39 hedge accounting provisions. Changes in the fair value of such derivative instruments that do not qualify for hedge accounting are recognised immediately in the income statement.

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting under IAS 39, any cumulative gain or loss existing in equity at that time remains in equity and is recognised when the committed or forecasted transaction ultimately is recognised in the income statement. However, if a committed or forecasted transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to the income statement.

The Company documents at the inception of the transaction the relationship between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions. This process includes linking all derivatives designated as hedges to specific assets and liabilities or to specific firm commitments or forecast transactions. The Company also documents its assessment, both at the hedge inception and on an ongoing basis, whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items.

The fair values of various derivative instruments used for hedging purposes are disclosed in Note 20. Movements on the hedging reserve in shareholder's equity are shown in Note 25.

FAIR VALUE ESTIMATION
Except for currency options, the fair values of the derivative financial instruments reflect estimates based on calculations performed using the Company's own discounted cash flow models (using market rates). The fair value of currency options is based on information obtained from external parties, including the Company's bankers.

T) CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS

The Company makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results.

Estimates and judgments are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

The estimates and assumptions that might have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next year are discussed below:

1) Income taxes and deferred taxes

The Company created a provision for current income taxes and in consideration of the temporary differences also for deferred tax. There are many transactions and calculations for which the ultimate tax determination is uncertain during the ordinary course of business and the measurement of deferred tax assets and liabilities reflects the tax consequences that would follow from the manner in which the Company expects to recover or settle the carrying amount of assets and liabilities. Where the final tax-deductible expenses are different from the amounts that were calculated, such differences will impact the current income and deferred tax provisions in the period in which such determination is made. As at 31 December 2008, the total amount of provision for current income taxes is CZK 3,737 million, advances paid for income taxes amount to CZK 3,962 million and the net deferred tax liability is CZK 3,299 million.

In October 2007, the new Czech legislation was enacted, by which the corporate income tax rate will be reduced from 24% to 21%, 20% and 19% for the fiscal years ending in 2008, 2009 and 2010, respectively. The positive impact on the deferred tax liability amounts to CZK 798 million in 2007 (see Note 5).

2) Goodwill

The Company tests at each reporting date goodwill for an impairment. However goodwill does not generate cash flows independently of other assets or groups of assets and the assessment of its carrying value is significantly impacted by the management's assessment of the performance and expected future performance of the operation to which the goodwill relates. In accordance with the requirement of IAS 36, goodwill is tested annually for its recoverable amount, as well as when there are indications of impairment. At 31 December 2008 the carrying amount of goodwill is CZK 13,320 million (See Note 9).

3) Provisions and contingent liabilities

As set out in Note 21 the Company is a participant in several lawsuits and administrative proceedings including those related to its pricing policies. The Company's treatment of obligations with uncertain timing and amount depends on the management's estimation of the amount and timing of the obligation and probability of an outflow of resources embodying economic benefits that will be required to settle the obligation (both legal or constructive). A provision is recognised when the Company has a present obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Contingent liabilities are not recognised because their existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Company. Contingent liabilities are assessed continually to determine whether an outflow of resource embodying economic benefits has become probable. If it becomes probable that an outflow of future economic benefits will be required for an item previously dealt with as a contingent liability, a provision is recognised in the financial statements of the period in which the change in probability occurs.

4) Interconnect

The Company provides and enters into the contracts for interconnect services and the revenue is recognised on the basis of the reasonable estimation of expected amount. Such estimation is regularly reviewed, however the final agreement and invoicing can be with some operators stated on up to a yearly basis.

5) Impairment of the fixed line business assets

The Company makes an assessment at each balance sheet date whether there is any indication that an impairment loss recognised for the fixed line business assets in prior years may no longer exist, may have decreased or may have increased. If any such indication exists, the Company estimates a recoverable amount of the assets and compares to the carrying value (net of the impairment allowance). In assessing whether there is any indication that the impairment loss recognised in the past may no longer exist, the Company considers both external and internal indicators (decline of asset's market value, changes expected in the market, including technological changes etc.). Where an estimate of recoverable amount is calculated, there is a number of management assumptions about future business performance, which may, ultimately, differ from reality.

Based on the assessment performed by the Company, no increase or decrease of the previously recognised impairment of fixed line business assets was recognised in 2008 and 2007 (see Note 8 and 10).

6) Operating lease commitments – Company as lessee
The Company changed its headquarters and moved to the new premises, where the Company has entered into the commercial property leases. The Company has determined, based on an evaluation of the terms and conditions of the arrangements, that the lessor retains all the significant risks and rewards of the ownership and therefore the Company accounts for the contract as an operating lease.

U) INVESTMENTS IN SUBSIDIARY AND ASSOCIATED UNDERTAKINGS

A subsidiary is an enterprise that is controlled by the Company, which means that the Company has the power to govern the financial and operating policies so as to obtain benefits from its activities.

An associated undertaking is an enterprise where the Company has significant influence, which is the power to participate in the financial and operating policy decisions, but not exercise control.

Equity investments in subsidiaries and associates are recorded at cost less an allowance for diminution in value.

No consolidation of subsidiaries or associates has been performed as these financial statements are presented on a stand-alone basis. In accordance with the requirements of the Act on Accounting, the Company prepares consolidated financial statements in accordance with IFRS.

V) CHANGE IN ACCOUNTING POLICY

No significant changes in accounting policies were applied in 2008 and 2007.

W) OPERATING PROFIT

Operating profit is defined as profit before financial results and taxes and represents profit from the business operations. Financial results consist of interest income, interest expense, other financial expense (which include primarily bank charges), fair value losses and gains on financial instruments and foreign exchange gains and losses.

NOTES TO THE FINANCIAL STATEMENTS

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1) SEGMENT INFORMATION

Business segments recognised by the Company are as follows:

- Fixed - network communications services using a fixed network and IS/ICT services,
- Mobile - mobile communications services.

Year ended 31 December 2008 in CZK million	Fixed	Mobile	Company
Revenues	30,220	34,587	64,807
Inter-segment sales	(423)	(771)	(1,194)
Total revenues	29,797	33,816	63,613
Gains from sale of non-current assets	855	–	855
Internal expenses capitalised in fixed assets	261	80	341
Costs	(18,432)	(17,994)	(36,426)
Inter-segment purchases	771	423	1,194
Total costs	(17,661)	(17,571)	(35,232)
Impairment charge	(83)	(2)	(85)
Depreciation	(7,255)	(3,583)	(10,838)
Amortisation	(650)	(1,226)	(1,876)
Total depreciation and amortization	(7,905)	(4,809)	(12,714)
Operating profit	5,264	11,514	16,778
Interest and other financial income (net)			12
Profit before tax			16,790
Tax			(3,697)
Net profit			**13,093**
Assets (excluding goodwill and non-current assets held for sale)	37,880	50,772	88,652
Goodwill on purchase of additional ownership interest (Eurotel Praha, spol. s r.o.)	–	13,320	13,320
Non-current assets held for sale	96	–	96
Total assets	**37,976**	**64,092**	**102,068**
Trade and other payables	6,163	6,675	12,838
Other liabilities	3,720	4,031	7,751
Total liabilities	**9,883**	**10,706**	**20,589**
Capital expenditure	**4,271**	**2,474**	**6,745**

Year ended 31 December 2007 in CZK million	Fixed	Mobile	Company
Revenues	30,490	33,783	64,273
Inter-segment sales	(455)	(783)	(1,238)
Total revenues	30,035	33,000	63,035
Gains from sale of non-current assets	43	–	43
Internal expenses capitalised in fixed assets	448	22	470
Costs	(16,990)	(18,406)	(35,396)
Inter-segment purchases	783	455	1,238
Total costs	(16,207)	(17,951)	(34,158)
Impairment charge	(5)	–	(5)
Depreciation	(8,515)	(4,007)	(12,522)
Amortistion	(683)	(1,170)	(1,853)
Total depreciation and amortization	(9,198)	(5,177)	(14,375)
Operating profit	5,116	9,894	15,010
Interest and other financial costs (net)			(33)
Profit before tax			14,977
Tax			(3,083)
Net profit			**11,894**
Assets (excluding goodwill and non-current assets held for sale)	47,689	51,800	99,489
Goodwill on purchase of additional ownership interest (Eurotel Praha, spol. s r.o.)	–	13,320	13,320
Non-current assets held for sale	328	–	328
Total assets	**48,017**	**65,120**	**113,137**
Trade and other payables	5,631	6,101	11,732
Other liabilities	8,150	8,830	16,980
Total liabilities	**13,781**	**14,931**	**28,712**
Capital expenditure	**4,255**	**2,331**	**6,586**

Revenue of the Company is predominantly derived from domestic trading activities and as a result, segment reporting is only shown on the basis of business segments. With respect to the issue of IFRS 8 Operating segments and the deep integration process from the past convergence of fixed and mobile operations, the Company has analysed criteria for segment identification. The adoption of the standard will not lead to a change in the reported segments in the next years.

The inter-segment pricing rates applied in 2008 and 2007 were determined on the same basis as rates applicable for other mobile operators and are consistent with rates applied for pricing with other mobile operators.

Capital expenditures comprise additions to property, plant and equipment and intangible assets.

2) REVENUE AND INTERNAL EXPENSES CAPITALIZED IN FIXED ASSETS

Revenue in CZK million	Year ended 31 December 2008	Year ended 31 December 2007
Voice	22,714	22,839
Interconnection	10,128	10,625
Subscription charges	8,444	8,849
Connection charges	326	783
SMS & MMS & Value added services	4,958	4,934
Leased lines and data services	3,866	3,961
Internet	6,459	5,824
IT and business solutions	2,107	1,934
Equipment and activation fee	1,928	2,070
Other telecommunication revenues	2,182	436
Other revenues	501	780
Total revenues	63,613	63,035

Revenues from related parties are disclosed in Note 26.

The aggregate future minimum lease payments under non-cancellable operating leases, where the Company is a lessor, relating to the buildings and other telecommunication equipment are as follows:

In CZK million	31 December 2008	31 December 2007
No later than 1 year	185	244
Later than 1 year and not later than 5 years	754	868
Later than 5 years	198	237
Total	1,137	1,349

Internal expenses capitalized in fixed assets in CZK million	Year ended 31 December 2008	Year ended 31 December 2007
Material	30	138
Labour	311	332
Total	341	470

3) OPERATING EXPENSES

The following items have been included into the operating expenses:

In CZK million	Year ended 31 December 2008	Year ended 31 December 2007
Wages and salaries*	4,703	4,621
Redundancy payments	160	208
Social security contributions (Note 18)	1,504	1,612
Staff welfare costs	148	323
Total staff costs	6,515	6,764
Interconnection and roaming	11,408	10,649
Cost of goods sold	2,972	3,225
Contents	235	160
Customer loyalty program	363	446
Sub-deliveries	1,335	1,401
Commissions	1,167	1,179
Other cost of sales	1,109	258

In CZK million	Year ended 31 December 2008	Year ended 31 December 2007
Purchases	506	672
Billing and collection	399	386
Marketing	1,496	1,818
Call centres	305	231
Network & IT repairs and maintenance	2,345	2,608
Rentals, buildings and vehicles	1,973	1,802
Utilities supplies	909	790
Consultancy and professional fees	211	337
Other external services	1,163	854
Provision for bad and doubtful debts and inventories	352	171
Taxes (other than income tax)	384	362
Other operating expenses	85	45
Total operating expenses	35,232	34,158

* Certain Company employees (including the Board of Directors) with specialised know how, or who have access to business secrets, or who are considered important to the development of the business, are bound by non-competition restrictions, for a maximum period of 12 months from the date of termination of their employment with the Company. The Company paid CZK 11 million in relation to such non-competition clauses in 2008 (2007: CZK 7 million).

Purchases from related parties are disclosed in Note 26.

4) INTEREST AND OTHER FINANCE INCOME AND EXPENSE

In CZK million	Year ended 31 December 2008	Year ended 31 December 2007
FINANCIAL INCOME		
Interest income	446	402
Gain for derivatives of fair value hedges (net)	65	–
Other financial income	1,306	753
Total financial income	1,817	1,155
FINANCIAL EXPENSES		
Interest expenses	(313)	(438)
Loss for derivatives of fair value hedges (net)	–	(26)
Other financial expenses	(1,492)	(724)
Total financial expenses	(1,805)	(1,188)
Net financial income/(cost) (net)	12	(33)

5) INCOME TAX

In CZK million	Year ended 31 December 2008	Year ended 31 December 2007
Total income tax expense is made up of:		
Current income tax charge	3,755	4,224
Deferred income tax credit (Note 17)	(58)	(1,141)
Taxes on income	3,697	3,083

The tax on the Company's profit before tax differs from the theoretical amount that would arise using the basic tax rate of the home country of the Company as follows:

In CZK million	Year ended 31 December 2008	Year ended 31 December 2007
Profit before tax	16,790	14,977
Income tax charge calculated at the statutory rate of 21% (2007: 24%)	3,526	3,594
Income not subjected to tax	–	(9)
Expenses not deductible for tax purposes	149	242
Impact of change in income tax rate	–	(798)
Tax related to prior periods	22	54
Taxes on income	3,697	3,083
Effective tax rate	22%	21%

6) EARNINGS PER SHARE

Basic earnings per share are calculated by dividing the net profit attributable to shareholders by the weighted average number of ordinary shares in issue during the year.

	31 December 2008	31 December 2007
Weighted number of ordinary shares in issue	322,089,900	322,089,900
Net profit attributable to shareholders (in CZK million)	13,093	11,894
Basic earnings per share (CZK)	41	37

There is no dilution of earnings as no convertible instruments have been issued by the Company.

7) DIVIDENDS

In CZK million	2008	2007
Dividends declared (including withholding tax)	16,104	16,104

Dividends include withholding tax on dividends paid by the Company to its shareholders. There has been no interim dividend paid in respect of 2008. Approval of the 2008 profit and the decision regarding the amount of any dividend payment for the 2008 financial year will take place at the Annual General Shareholders Meeting scheduled for 3 April 2009.

8) PROPERTY, PLANT AND EQUIPMENT

In CZK million	Land and buildings	Ducts, cables and related plant	Communication exchanges and related equipment	Other fixed assets	Capital work in progress including advances paid	Total
At 31 December 2008						
Opening net book amount	14,013	39,710	12,711	1,931	2,434	70,799
Additions	508	769	2,339	1,015	4,500	9,131
Disposals and other movements	–	–	(104)	(15)	(4,375)	(4,494)
Assets classified as held for sale	(3,285)	(25)	(6)	–	–	(3,316)
Depreciation charge	(667)	(4,206)	(4,823)	(1,142)	–	(10,838)
Impairment charge	(49)	(21)	(1)	–	(13)	(84)
Closing net book amount	10,520	36,227	10,116	1,789	2,546	61,198
At 31 December 2008						
Cost	17,459	99,982	90,504	10,315	2,573	220,833
Accumulated depreciation and impairment allowance	(6,939)	(63,755)	(80,388)	(8,526)	(27)	(159,635)
Net book amount	10,520	36,227	10,116	1,789	2,546	61,198
At 31 December 2007						
Opening net book amount	14,219	43,395	17,283	1,803	1,986	78,686
Additions	622	576	2,124	1,112	4,738	9,172
Disposals and other movements	(37)	(1)	(58)	(8)	(4,291)	(4,395)
Assets classified as held for sale	(132)	(10)	–	–	–	(142)
Depreciation charge	(654)	(4,250)	(6,638)	(976)	(4)	(12,522)
Impairment charge	(5)	–	–	–	5	–
Closing net book amount	14,013	39,710	12,711	1,931	2,434	70,799
At 31 December 2007						
Cost	22,769	99,696	92,541	10,470	2,464	227,940
Accumulated depreciation and impairment allowance	(8,756)	(59,986)	(79,830)	(8,539)	(30)	(157,141)
Net book amount	14,013	39,710	12,711	1,931	2,434	70,799

As at 31 December 2008, the carrying value of non-depreciated assets amounted to CZK 241 million (2007: CZK 472 million).

Land and buildings in the carrying value of CZK 8,280 million as of 31 December 2007 were pledged in respect of execution relating to the T-Mobile interconnect dispute. In 2008 the execution was terminated (see Note 21). No property, plant and equipment were pledged as at 31 December 2008.

No borrowing costs were capitalized during the years 2008 and 2007.

The Company reports and classifies the following assets held for sale at the balance sheet date:

In CZK million	Land and buildings	Communication exchanges and related equipment	Other fixed assets	Total
At 31 December 2008				
Opening net book amount	327	1	–	328
Disposals and other movements	(3,540)	(7)	–	(3,547)
Impairment charge	(1)	–	–	(1)
Assets re-classified as held for sale	3,310	6	–	3,316
Closing net book amount	96	–	–	96
At 31 December 2008				
Cost	789	187	6	982
Accumulated depreciation and impairment allowance	(693)	(187)	(6)	(886)
Net book amount	96	–	–	96
At 31 December 2007				
Opening net book amount	202	1	–	203
Disposals and other movements	(12)	–	–	(12)
Impairment charge	(5)	–	–	(5)
Assets re-classified as held for sale	142	–	–	142
Closing net book amount	327	1	–	328
At 31 December 2007				
Cost	1,282	199	10	1,491
Accumulated depreciation and impairment allowance	(955)	(198)	(10)	(1,163)
Net book amount	327	1	–	328

Assets intended for sale in most cases represent administration buildings with land, that became vacant due to the Company's optimisation process and which the Company will not use in the future and it is expected that their sale will take place within one year.

The non-current assets classified as held for sale are presented in the fixed segment.

In 2008, the Company achieved a total gain from the sale of the above fixed assets amounting to CZK 855 million (2007: CZK 43 million) and total losses in amount CZK 58 million (2007: CZK 34 million).

In 2008 and at the beginning of 2009, the Company completed the substantial part of a real estate usage optimisation process. In 2008, as part of this process, the Company sold a portfolio of administrative and technological buildings located throughout the whole Czech Republic. Net gain from the sale of the real estate portfolio amounted to 727 million CZK. A small portion of the real estate was leased back on the long term basis. In January 2009, the Company sold a construction site and two administrative buildings of the former headquarters in Olšanská street in Prague (see Note 28)

Cost of fully depreciated property, plant and equipment was CZK 59,556 million as at 31 December 2008 (2007: CZK 62,143 million).

9) INTANGIBLE ASSETS

In CZK million	Goodwill	Licences	Software	Other	Total
At 31 December 2008					
Opening net book amount	13,320	4,686	3,461	–	21,467
Additions	–	–	2,184	–	2,184
Disposals and other movements	–	–	(73)	–	(73)
Amortisation charge	–	(399)	(1,477)	–	(1,876)
Closing net book amount	13,320	4,287	4,095	–	21,702
At 31 December 2008					
Cost	13,320	6,073	24,137	–	43,530
Accumulated amortisation and impairment allowance	–	(1,786)	(20,042)	–	(21,828)
Net book amount	13,320	4,287	4,095	–	21,702
At 31 December 2007					
Opening net book amount	13,320	5,090	3,098	–	21,508
Additions	–	–	1,814	–	1,814
Disposals and other movements	–	–	(2)	–	(2)
Amortisation charge	–	(404)	(1,449)	–	(1,853)
Closing net book amount	13,320	4,686	3,461	–	21,467
At 31 December 2007					
Cost	13,320	6,073	22,734	2,829	44,956
Accumulated amortisation and impairment allowance	–	(1,387)	(19,273)	(2,829)	(23,489)
Net book amount	13,320	4,686	3,461	–	21,467

GOODWILL

Goodwill in amount of CZK 13,320 million resulted from the acquisition of the remaining 49% ownership interest in Eurotel Praha spol. s r.o. (“Eurotel”). From the effective date of merger with Český Telecom, a.s. this goodwill is presented in the standalone financial statements of the Company. The initially recognized goodwill of CZK 14,087 million resulted from comparison of cost of business combination of CZK 29,215 million and fair value of net assets acquired of CZK 15,128 million. Until 31 December 2004 goodwill was amortised on a straight line basis over a period of 20 years and assessed for an indication of impairment at each balance sheet date.

Due to a revision of IFRS 3, IAS 36 and IAS 38 the Company ceased amortisation of the previously recognized goodwill from 1 January 2005. Accumulated amortisation as at 31 December 2004 was eliminated with a corresponding decrease in the cost of goodwill (767 million CZK). Since the year ending 31 December 2005 onwards, goodwill is classified as an asset with indefinite useful life which has been tested annually for the impairment, as well as when there are indications of impairment. There is no other intangible asset with indefinite useful life.

The Company performed impairment tests and as result of the test the Company did not recognize any impairment losses of goodwill in 2008 and 2007. The impairment test involves determining the recoverable amount of the mobile cash-generating unit, which corresponds to the value in use. Value in use is the present value of the future cash flows expected to be derived from a cash-generating unit.

Value in use is determined on the basis of an enterprise valuation model and is assessed from a Company internal perspective. Value in use is determined based on cash flow budgets, which are based on the medium-term business plan for a period of 3 years, which has been approved by the management and which is valid when the impairment test is performed. This business plan is based on the past experience, as well as on future market trends. Further, the business plan is based on general economic data derived from macroeconomic and financial studies. Cash flows beyond the three-year period are extrapolated using an appropriate growth rates. Key assumptions on which management has based its determination of business plan and growth rates include development of gross domestic product, interest rates, nominal wages, average revenue per user (ARPU), customer acquisition and retention costs, churn rates, capital expenditure, market share, growth rates and discount rates.

Any significant future changes in the market and competitive environments could have an adverse effect on the value of the cash-generating units.

The calculations of value in use for all cash-generating units are most sensitive to the following assumptions:

Estimated growth rate – the basis used to determine the value assigned to estimated growth rate is the forecast of market and regulatory environment, where the Company conduct the business.

Discount rate – discount rates reflect management's estimate of the risk specific to the cash generating unit. The basis used to determine the value assigned is weighted average of cost of capital (WACC).

LICENCES

Acquired licences are represented by rights to operate the UMTS, GSM and NMT cellular networks in the Czech Republic. The original 450 MHz and GSM operating licenses were granted for a period of twenty years from the signing of the agreement for the original 450 MHz license in 1991 and from the granting of the GSM license in 1996 for use of the 900 spectrum. In 1999, former Eurotel acquired an additional GSM 1800 spectrum under its existing GSM license. In 2002, the GSM license to both spectrums was renewed and is currently valid for the remaining period of eight years. In 2002, former Eurotel renewed its 450 MHz license; the current license enables the mobile segment to offer every internationally recognized public mobile telecommunication services on frequency of 450 MHz. Mobile segment currently provides on this frequency voice services under NMT standard and broadband Internet access services using CDMA technology. The NMT license is currently valid for the remaining period of three years.

In December 2001, former Eurotel acquired the UMTS license, which has been granted for a period of twenty years. Under the license, former Eurotel was provided with deferred payment terms by the Czech Telecommunication Office ("CTO") to finance the license acquisition. In December 2003, former Eurotel signed an amendment to its original UMTS license agreement, by which the original launch of the service was extended by one year. According to the terms of this new amendment, former Eurotel agreed to pay the UMTS obligation in full during 2004 in exchange for a forgiveness of 2003 and 2004 interest on the deferred payments provided as part of the UMTS license agreement. UMTS license was put into commercial use on 1 December 2005 when it also started to be amortized.

Carrying value of licences:

In CZK million	31 December 2008	31 December 2007
GSM 900 license	546	619
GSM 1800 license	440	499
NMT 450 license	33	50
UMTS license	3,268	3,518
Total	4,287	4,686

No borrowing costs were capitalized during the years 2008 and 2007.

Cost of fully amortised intangible assets was CZK 16,829 million as at 31 December 2008 (2007: CZK 16,947 million).

All of the Company's intangible assets with finite lives are amortised and are subject to an annual review of impairment indicators and revision of useful life.

10) IMPAIRMENT OF FIXED ASSETS

FIXED ASSETS OF THE FIXED LINE BUSINESS

During 2003, external factors relating to the telecommunication market and regulatory environment namely uncertainty regarding tariff rebalancing, termination charges for internet dial-up interconnection charges and other regulatory decisions in the Czech Republic led the management to assess and adjust the recoverable amount of the fixed line segment assets. The fixed line segment assets constitute one cash-generating unit (the "CGU").

Value in use has been calculated by a method of cumulated discounted cash flows for a period limited by average useful life of CGU's key assets. Primarily, the following assumptions have been used in the impairment testing model: actual business plan, estimation of consecutive development of key indicators (revenues, margin, investments etc.) in analyzed period, discount rate derived from weighted average cost of capital.

As at 31 December 2008, the management of the Company reviewed the indicators which would indicate that the impairment allowance of fixed line business assets made in 2003 is no longer relevant and should be reversed. Upon the review, a recoverable amount of the fixed line business assets (impairment test model) was estimated. Based on this assessment performed, the management believes that the value of the existing fixed network assets is fairly stated and does not differ substantially from the assets' recoverable amount as at 31 December 2008.

Value in use as at 31 December 2008 has been calculated using the same methodology as in the year 2003.

11) INVENTORIES

In CZK million	31 December 2008	31 December 2007
Construction material	114	66
Cables	47	47
Other inventory including goods for resale	578	626
Finished products and work in progress	4	4
Total	743	743

The inventories noted above are stated net of an allowance of CZK 57 million (2007: CZK 89 million), reducing the value of the inventories to their net realisable value. The total carrying amount of inventories at net realisable value amounts to CZK 24 million (2007: CZK 18 million). The amount of inventories recognised as an expense is CZK 3,708 million (2007: CZK 4,130 million).

12) RECEIVABLES AND PREPAYMENTS

In CZK million	31 December 2008	31 December 2007
Domestic trade receivables (net)	6,901	6,782
Foreign currency trade receivables (net)	1,061	618
Other debtors (net)	563	300
Prepayments	686	666
Other financial assets – short-term	14	17
Derivative instruments	23	4
Total	9,248	8,387

Trade receivables are stated net of an allowance for impaired receivables of CZK 3,241 million (2007: CZK 3,277 million). In order to preserve the tax-deductible status of the bad debt expense, the Company's trade receivables are not written off and removed from the primary books and records until certain statutory collection requirements have been satisfied.

Receivables from related parties are disclosed in Note 26.

Trade receivables in CZK million	Carrying amount	Neither impaired nor overdue	Not impaired but overdue			
			Less than 90 days	90 and 180 days	180 and 360 days	More than 360 days
At 31 December 2008	7,962	5,134	607	60	139	80
At 31 December 2007	7,400	4,491	321	50	–	–

Bad debt provisions in CZK million	
At 1 January 2007	3,345
Additions	103
Retirements/amount paid	(171)
At 31 December 2007	3,277
Additions	855
Retirements/amount paid	(891)
At 31 December 2008	3,241

The Company's historical experience regarding the collection of accounts receivable is consistent with the recorded allowances. Due to these factors, the management believes that no additional credit risk beyond the amounts provided for is inherent in the Company's trade receivables.

As at 31 December 2008 and 2007 the Company has the following non-current balances, which are classified as other financial assets:

In CZK million	31 December 2008	31 December 2007
Long-term credits	133	112
Advance payments for long-term expenses	244	246
Other financial investment	–	207
Total	377	565

Long-term trade credits include interest bearing credit (interest 5.9%) amounting to CZK 64 million (2007: CZK 71 million).

13) HELD-TO-MATURITY INVESTMENTS

Held-to-maturity investments in CZK million	31 December 2008	31 December 2007
At beginning of year	27	27
Additions	1	1
Matured	(28)	(1)
At end of year	–	27
Current	–	27
Total	–	27

Held to maturity investments category as at 31 December 2007 comprised a debt instrument – a bond held in EUR with maturity date July 2008, which was carried at amortised cost.

14) CASH AND CASH EQUIVALENTS

In CZK million	31 December 2008	31 December 2007	Interest rate
Cash at current bank accounts	218	4,076	Floating
Cash at cash-pooling structures (inter-company)	6,344	5,107	Floating
Short-term bank deposits	410	321	Fixed
Other cash equivalents	–	17	n/a
Total cash and cash equivalents	6,972	9,521	
Financial investments (held to maturity)	–	27	Fixed

As at 31 December 2008 and 2007, the Company's cash equivalents partially consisted of short-term bank promissory notes that were economically equivalent to bank term deposits and interest bearing deposits maturing in three months or less.

Since April 2006, the Company entered into mutual Telefónica Group cash-pooling, which enables the Telefónica Group good financial governance and effective operating free cash flow. The short-term deposits conditions are based on the arm's length principle. The short-term deposits are classified as cash equivalents.

At 31 December 2008, the Company had available equivalent of CZK 4,850 million (2007: CZK 11,453 million) of undrawn committed facilities.

For the purposes of the cash flow statement, the year-end cash and cash equivalents comprise the following components:

In CZK million	31 December 2008	31 December 2007
Cash and cash equivalents	6,972	9,521
Bank overdrafts and other short-term borrowings (Note 16)	–	–
Total	6,972	9,521

The amount of CZK 3,902 million kept on bank accounts was pledged as of 31 December 2007 in respect of execution relating to the T-Mobile

Interconnect dispute. In 2008 the execution was terminated (Note 21). As of 31 December 2008 no cash and cash equivalents were pledged.

15) TRADE AND OTHER PAYABLES

In CZK million	31 December 2008	31 December 2007
Trade creditors in local currency (net)	4,817	4,724
Trade creditors in foreign currencies (net)	1,324	1,235
Other taxes and social security	184	516
Deferred revenue	977	1,195
Employee wages and benefits	712	657
VAT payable	464	154
Other creditors	404	654
Accruals	3,956	2,597
Total payables	12,838	11,732
Other non-current liabilities	175	452

Payables to related parties are disclosed in Note 26.

Other non-current liabilities include primarily deferred revenues from connection fees, which are expected to be taken to income in more than 12 months from the balance sheet date.

16) FINANCIAL DEBTS

In CZK million	31 December 2008	31 December 2007
Bank loans in foreign currencies (a)	3,098	3,062
Bonds in local currency (b)	5	5,998
Total borrowings	3,103	9,060
Accrued interest including commitment fees	86	185
Derivatives	7	24
Other financial debt	93	209
Total financial debt	3,196	9,269
Repayable:		
Within one year	98	6,207
Between two and five years (total non-current)	3,098	3,062
Total financial debt	3,196	9,269

a) As at 31 December 2008 the Company does not utilize bank overdrafts. In July 1997, the Company raised a private placement in the total amount of EUR 127.8 million with a maturity date on 30 July 2012. As at 31 December 2008, the outstanding amount of the foreign currency loan amounts to EUR 115 million.

b) In 2003, the Company issued CZK 6,000 million of bonds with an interest rate 3.50% p.a. and it was fully repaid at a maturity date of 9 July 2008. For all borrowings, interest has been charged at commercial rates.

The Company's loan interest rate allocation after taking into account interest rate swaps was as follows:

In CZK million	31 December 2008	31 December 2007
At fixed rate	3,103	9,060
Total	3,103	9,060

The fair values of borrowings are based on discounted cash flows using a discount rate based upon the borrowing rate that the Board of Directors expects to be available to the Company at the balance sheet date. The carrying amounts of short-term borrowings approximate their fair value.

Effective interest rates	2008	2007
Bank loans in foreign currencies	6.64%	6.64%
Bonds in local currency	3.50%	3.50%

Loans are not secured.

The table below summarizes the maturity profile of the Company's financial liabilities at 31 December 2008 based on contractual undiscounted payments.

At 31 December 2008 in CZK million	Less than 3 months	3 to 12 months	1 to 5 years	> 5years
Interest bearing loans and borrowings	5	206	3,715	–
Trade and other payables (excluding deferred revenue)	10,456	1,405	–	–
Derivatives fair value	7	–	–	–
Total	10,468	1,611	3,715	–
At 31 December 2007 in CZK million	Less than 3 months	3 to 12 months	1 to 5 years	> 5years
Interest bearing loans and borrowings	–	6,413	3,875	–
Trade and other payables (excluding deferred revenue)	9,236	1,301	–	–
Other financial liabilities	3	8	–	–
Derivatives fair value	22	2	–	–
Total	9,261	7,724	3,875	–

FAIR VALUES

Set out below is a comparison by category of carrying amounts and fair values of all of the Company's financial instruments that are carried in the financial statements.

	Carrying amount		Fair value	
In CZK million	2008	2007	2008	2007
FINANCIAL ASSETS				
Cash and cash equivalents	6,972	9,521	6,972	9,521
Financial investments (held to maturity)	–	27	–	27
Derivatives	23	4	23	4
Other financial assets	377	565	377	565
FINANCIAL LIABILITIES				
Interest bearing loans and borrowings				
Floating rate borrowings	–	–	–	–
Fixed rate borrowings	3,184	3,148	3,503	3,348
Issued Bonds	5	6,097	5	6,049
Derivatives	7	24	7	24

Market values have been used to determine the fair value of the above mentioned issued CZK bonds. The fair value of derivatives and borrowings has been calculated by discounting the expected future cash flows at prevailing interest rates.

FINANCIAL RISK ANALYSIS

The following table demonstrates the sensitivity to a reasonably possible change in foreign exchange rates and interest rates.

	Effect on profit before tax	
In CZK million	2008	2007
FX RISK		
Value at Risk*	(277)	(95)
Stress testing*	(52)	(46)
IR RISK		
Stress testing*	(161)	(176)

* The Value at Risk (VaR) Model enables the Company estimate the probability of maximum possible loss to the portfolio value in the given time frame which will not be exceeded given the defined reliability level. For conducting a VaR calculation, the Company uses the risk variance and covariance method using the normal distribution (e.g. parametric method). The time frame used is one month with a 95% reliability rate. Considering the importance of net open positions resulting from financial assets and financial liabilities of the Company in individual foreign currencies, the Company models VaR from a position of translation and transaction in EUR and USD.
FX risk used stress scenario represents immediate one-off change in the foreign exchange rates vs. CZK by 1% in a negative direction (in the case of short open foreign currency position, this will result in a depreciation of the foreign exchange rate and vice versa).
IR risk used stress scenario represents immediate one-off change of interest rates along the whole yield curve by 1% in an unfavorable direction. The calculation of unfavorable impact on Company cash flows (due to an increase in interest expense or drop in interest received relating to financial assets and financial liabilities) is made each month on the floating basis within a time frame of 12 months.

HEDGING

The following nominal value of foreign exchange forwards was used by the Company to hedge the currency risk:

	Nominal value in EUR million		Fair value in CZK million	
	2008	2007	2008	2007
Forward exchange contracts	19	36	16	(20)

17) DEFERRED INCOME TAXES

Deferred income taxes are calculated using currently enacted tax rates expected to apply when the asset is realized or the liability settled.

Short-term deferred taxes were calculated at 20% (21% in 2007) and long-term deferred taxes were calculated at 19% (20% and 19% in 2007 depending on the period of its expected realisation).

In CZK million	2008	2007
At 1 January	3,353	4,494
Income statement tax credit (Note 5)	(58)	(1,141)
Tax on fair value gains	4	–
At 31 December	3,299	3,353

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when the deferred income taxes relate to the same fiscal authority.

The following amounts, determined after offsetting, are shown in the balance sheet:

In CZK million	31 December 2008	31 December 2007
Deferred tax assets	(656)	(1,143)
Deferred tax liabilities	3,955	4,496
Total	3,299	3,353

The deferred tax asset includes CZK 423 million (2007: CZK 655 million) recoverable in less than twelve months and CZK 233 million (2007: CZK 488 million) recoverable after more than twelve months. The deferred tax liability includes CZK 493 million (2007: CZK 584 million) payable in less than twelve months and CZK 3,462 million (2007: CZK 3,912 million) payable in more than twelve months.

The deferred tax is determined by these components:

In CZK million	Balance sheet 2008	Balance sheet 2007	Income statement 2008	Income statement 2007
Temporary differences relating to:				
– property, plant and equipment and intangible assets	3,925	4,496	(571)	(574)
– trade receivables, inventories and other differences	(626)	(1,139)	513	231
Revaluations of cash flow hedges	–	(4)	–	–
Amount relating to changes in tax rates	–	–	–	(798)
Total	3,299	3,353	(58)	(1,141)

Deferred income tax related to items charged or credited directly to equity are as follows:

In CZK million	2008	2007
Revaluation of cash flow hedges	4	–
Total	4	–

Reduction of the corporate income tax rate resulted in a positive impact on deferred tax liability of CZK 798 million in 2007.

18) GOVERNMENT SOCIAL SECURITY AND PENSION SCHEMES

The Company is legally required to make contributions to government health, retirement benefit and unemployment schemes. During 2008 and 2007, the Company paid contributions at a rate of 35% of gross salaries and is not required to make any contributions in excess of this statutory rate. The total amount charged to operating expenses in respect of this scheme was CZK 1,504 million in 2008 (2007: CZK 1,612 million) (see Note 3). Employees contribute 12.5% (2007: 12.5%) of their gross salaries.

The Company has a voluntary pension plan for employees under which the Company makes contributions on behalf of the Company's employees to approved pension plan providers, under defined contribution schemes. The Company's contribution depends upon the number of employees joining the scheme and their age profile. During the year the Company made contributions of CZK 58 million (2007: CZK 58 million). These contributions were charged as an operating expense.

In accordance with an annually renegotiated collective labour agreement, the Company is required to pay CZK 25,000 or CZK 90,000 on retirement depending on the length of the employee's service, who have completed not less than five years continuous service. These benefits are restricted to those employees who retire during the period for which the labour agreement is in place. The Company is not under any legal or constructive obligation to continue providing such benefits beyond the period of such agreement and therefore, no provisions beyond the period of the agreement are recognised in the financial statements. Payments made during the year 2008 relating to employee retirement amounted to CZK 0.1 million (2007: CZK 0.2 million) and were charged as an operating expense.

All amounts discussed in the above note are included in staff costs (see Note 3).

19) PROVISIONS FOR LIABILITIES AND CHARGES

In CZK million	Regulatory and court decisions	Employee redundancy costs	Employee related costs	Benefit loyalty provision	Sale of real estate portfolio	Other	Total
At 1 January 2008	2,110	3	298	627	–	9	3,047
Additions during the year	66	73	136	43	495	31	844
Utilised during the year	(1,781)	(63)	(275)	(418)	(235)	(13)	(2,785)
Transfers	–	–	(25)	–	–	–	(25)
At 31 December 2008	395	13	134	252	260	27	1,081
Short-term provisions 2008	–	13	127	252	260	27	679
Long-term provisions 2008	395	–	7	–	–	–	402
	395	13	134	252	260	27	1,081
Short-term provisions 2007	–	3	262	627	–	9	901
Long-term provisions 2007	2,110	–	36	–	–	–	2,146
	2,110	3	298	627	–	9	3,047

With the exception of the regulatory and court decisions provision and other small items for which the expected timing of payments is not certain all other provisions are expected to be utilised within next twelve months from the balance sheet date.

BENEFIT LOYALTY PROVISION

Benefit loyalty provision covers the cost of equipment, accessories, gifts and services provided to participants in the mobile segment's loyalty program in exchange for credits awarded primarily for airtime minutes spent. The provision has been recognized based on past experience of the usage of these credits by loyalty program participants. Expected outflow of provided benefits is CZK 252 million within one year (2007: CZK 347 million within one year and CZK 280 million from one year up to three years).

The future obligation of the expenditures expected to be required amounting to CZK 252 million (2007: CZK 657 million) is fully covered by the amount of the provision in its present value.

EMPLOYEE-RELATED COSTS

Provisions for employee-related costs include expected costs associated with performance bonuses and provision for termination payments.

REGULATORY AND COURT DECISIONS

Provision for regulatory and court decisions is made for legal proceedings involving the Company (see Note 21).

20) FINANCIAL INSTRUMENTS

NET FAIR VALUES OF DERIVATIVE FINANCIAL INSTRUMENTS
At the balance sheet date, the total net fair values of derivative financial instruments were as follows:

Forward foreign exchange contracts in CZK million	31 December 2008	31 December 2007
Cash flow hedges		
– with positive fair value	–	4
– with negative fair value	–	(24)
Instruments not qualifying as hedges		
– with positive fair value	23	–
– with negative fair value	(7)	–
Total (Note 16)	16	(20)

21) CONTINGENCIES

The Company is involved in several court proceedings which have arisen from the ordinary course of business. Significant legal matters involving the Company are listed below.

INTERCONNECT ARRANGEMENTS
I. The Company has not yet agreed a 2001 price amendment to an agreement with T-Mobile Czech Republic a.s. governing interconnect arrangements. Despite the fact that in December 2003 the Czech Telecommunication Office (CTO) effectively ruled in favor of the mobile operator (i.e. CZK 899 million for T-Mobile Czech Republic a.s., the outstanding amount is bearing interest of 0.05% per day), the management believes that the amounts are not substantiated and are without merit. The Company has subsequently brought a legal action against the decision and obtained the suspension of the executability of the decision.

Meanwhile the question of jurisdiction between the civil courts and the administrative courts has arisen. As a result of the question of jurisdiction the suspension of the executability of the CTO decision temporarily expired. T-Mobile Czech Republic initiated the execution and claimed the remuneration of the litigable amount. The Company did not agree with the execution and used all its legal instruments to the termination of the execution. After 11 months of the execution it was evident that the burden of execution will continue for another several months, therefore the management decided to pay the executed amount in April 2008 and decided to continue in the legal action, in which the executed amount is claimed. No further disclosure is deemed appropriate as it could prejudice the Company's position in the dispute.

II. On 30 June 2005, Vodafone Czech Republic, a.s. (former Český Mobil/Oskar Mobil) brought a legal action at the Municipal Court in Prague against the Company for damages in the amount of CZK 538 million with appurtenances and for returning the unjustified enrichment of CZK 117 million with appurtenances. The Company is alleged to have failed to transmit the traffic to networks operated by other mobile operators according to respective interconnection agreements.

The High Court in Prague confirmed the Company's conclusion that CTO has already issued the final decision in favour of the Company and that the company Vodafone Czech Republic, a.s. has not respected this decision. The Municipal Court in Prague therefore terminated the legal action in September 2008. Based on the current situation the Company believes that the High Court in Prague will confirm the decision and will terminate the appeal proceedings. The management is confident that all risks, which may arise as a result of the litigation, are adequately provided for in the financial statements.

OFFICE FOR THE PROTECTION OF ECONOMIC COMPETITION PROCEEDINGS
The Company was subject to administrative proceeding before the Office for the Protection of Economic Competition ("UOHS") relating to the alleged abuse of the dominant position by creation of unfair barriers against development on the market through the application of certain specific price plans for residential customers. UOHS rendered resolution dated 20 April 2005 imposing a fine to the Company in the total amount of CZK 210 million, which was consequently, after the Company completed and filed a protest, reduced to CZK 205 million.

The Company lodged a legal action in January 2006 and while the suspension of the executability was not granted the fine was paid. The Regional court in Brno refused the legal action and therefore the Company lodged a complaint to the Supreme Administrative Court on 19 October 2006.

OTHER LEGAL MATTERS

I. The Company is a defendant in a case filed by TELE 2 s.r.o. on 3 February 2005 asserting causes for alleged breach of act on protection of the competition by the Company in connection by offering certain pricing plans from September 2002 to December 2004. The amount of the claim is CZK 2,142 million with appurtenances.

The Company provided to the court extensive defense along with proposed items of evidence proving the legal imperfectness of the sued court's conduct. The management is convinced that the matter is adequately reflected in the financial statements and does not believe the resolution of this legal proceeding will have a material adverse effect on net income exceeding the amount of provision already made in the financial statements. No further disclosure is deemed appropriate as it could prejudice the Company's position in the dispute.

II. The Company is prosecuted by AUGUSTUS spol. s r.o. for an alleged loss of profit in the principal amount of approximately CZK 183 million with appurtenances relating to the years 1995 – 2001. AUGUSTUS spol. s r.o. claims that the Company illegitimately cancelled a contract for issue of phone cards, which was signed for unlimited period of time. Based on court decision, the Company paid an amount of the principal of CZK 83 million and the corresponding interest in August 2006 (total approximately CZK 139 million). Both parties subsequently filed an extraordinary appeal against the court judgment. The management believes that all risks, which may arise as a result of this litigation, are adequately provided for in the financial statements. No further disclosure is deemed appropriate as it could prejudice the Company's position in the dispute.

III. Subsequently AUGUSTUS spol. s r.o. filed another action against the Company regarding the amount of approximately CZK 294 million (status in April 2008). The legal action is based on the contract on phone cards issuing signed between Telefónica O2 Czech Republic, a.s. and AUGUSTUS spol. s r.o. that was terminated 13 years ago. AUGUSTUS spol. s r.o. evocates various new requirements in the prosecution that are not underpinned by the law or contradict each other eventually. The prosecution does not enable to sum the individual claims to be able to specify the total amount. Telefónica O2 Czech Republic, a.s. takes all steps in the lawsuit to defend thoroughly this unlawful claim and believes in success in this lawsuit. However, with respect to the claimed amount the lawsuit is disclosed separately.

IV. Furthermore, the Company is a defendant in a case filed by Vodafone Czech Republic, a.s. in May 2004 asserting causes for alleged breach of the act on protection of the competition by former Eurotel Praha, spol. s r.o. (damages amounting to CZK 1,043 million). Both parties filed their expert opinions to the court. The management believes that all risks, which may arise as a result of by Vodafone Czech Republic, a.s. litigations, are adequately provided for in the financial statements. Decision of the Office for the Protection of Economic Competition (UOHS) on which by Vodafone Czech Republic, a.s. based its claim was on 11 July 2007 cancelled by the Constitutional court. The Municipal court in Prague dismissed the claim on 21 August 2008. by Vodafone Czech Republic, a.s. appealed against that decision to the High court in Prague. No further disclosure is deemed appropriate as it could prejudice the Company's position in the dispute.

The Company is a defendant in several other legal cases. The total amount of those individual cases exceeding CZK 5 million amounts to CZK 233 million. The management believes that the risk of losing these cases is less than probable and no provision was made in the financial statements.

22) COMMITMENTS

OPERATING LEASES

The aggregate future minimum lease payments under operating leases are as follows:

In CZK million	31 December 2008	31 December 2007
No later than 1 year	1,275	1,196
Later than 1 year and not later than 5 years	3,963	3,809
Later than 5 years	5,720	2,976
Total	10,958	7,981

The total lease payments relating to operating leasing of property, plant and equipment recognised as an expense in 2008 were CZK 1,253 million (2007: CZK 1,112 million). These lease agreements may contain clauses requiring restoration of the leased site at the end of the lease term. At present, such costs do not have a material impact on the Company's results of operations, financial position, or cash flow and therefore are not accounted for.

In 2004 the Company entered into a sale and lease back transaction and now leases the majority of its car fleet under operating leases. There are no contingent rent obligations. The lease arrangements include an option to renew the lease after the initial period. Lease payments are fixed and determinable, however they may be increased to reflect inflation and other market conditions such as interest rates changes (e.g. an increase in PRIBOR by more than 2% over a half year). There are no significant restrictions imposed by these lease arrangements, such as those concerning dividends, additional debt and further leasing. Total future lease payments relating to this contract in 2008 were CZK 356 million (2007: CZK 458 million).

CAPITAL AND OTHER COMMITMENTS

In CZK million	31 December 2008	31 December 2007
Capital and other expenditure contracted but not provided for in the financial statements	646	1,671

The majority of contracted amounts relate to the telecommunications network and service contracts.

23) SERVICE CONCESSION ARRANGEMENTS

The Company performs communication activities as defined under the Act on Electronic Communications based on a notification and a certificate from the Czech Telecommunication Office num. 516 as amended by later changes num. 516/1, 516/2 and 516/3.

The communication activities include (territory of the Czech Republic):
a) public fixed network of electronic communications,
b) public network for the transfer of radio and TV signal,
c) public fixed telephone network,
d) public mobile telephone network,
e) publicly accessible telephone services,
f) other voice services – service is provided as publicly available,
g) rent of circuits – service is provided as publicly available,
h) transmission of radio and TV signal – service is provided as publicly available,
i) transfers of data – service is provided as publicly available,
j) internet access services – service is provided as publicly available,
k) other voice services – service is not provided as publicly available.

The Company provides mobile services of electronic communications in the 900 and 1800 MHz frequency bands under the Global System for Mobile Communication ("GSM") standard on the basis of radio frequency assignment from CTO valid until 7 February 2016, in the 2100 MHz frequency band under the Universal Mobile

Telecommunications System ("UMTS") standard on the basis of radio frequency assignment from CTO valid until 1 January 2022 and in the 450 MHz frequency band using technology CDMA2000 (Code Division Multiple Access – "CDMA"), where on the basis of radio frequency assignment from CTO valid until 7 February 2011 is provided broadband mobile access to Internet.

Validity of radio frequency assignment is possible to prolong for next period on the basis of application submitted to CTO in accordance with the Act on Electronic Communications. Relative to the current regulatory and business environment in the Czech Republic, contractual, legal, regulatory, competitive or other economic factors may limit the period during which the Company can benefit from the use of these radio frequency assignments in the future.

No additional expenses or any limitations connected with renewal of the radio frequency assignments are expected in accordance with the existing interpretation of regulatory provisions.

IMPOSITION OF OBLIGATIONS RELATED TO PROVISION OF UNIVERSAL SERVICE

During the whole year 2008, the Company provided the partial services within CTO imposed obligations to provide universal service:

a) periodic issuance of telephone directories with numbers of participants of the publicly accessible telephone service and access of end users to these directories,*
b) information service on the numbers of participants of the publicly accessible telephone service,*
c) public pay telephones services,
d) access for disabled to the public telephone,
e) supplementary services to service of connection at a fixed location to the public telephone network and the service of access to publicly available telephone services at a fixed location:
   – phased payment of the price for the establishment of connection to the public telephone network for consumer,
   – free selective barring of outgoing calls for the subscribers, and
   – free itemised billing of the price for consumer,
f) special price schemes, which are different from the price schemes used under normal business conditions, for low income persons, persons with special social needs and disabled persons.

* Services listed under letter a) and b) above are excluded from the universal service regime on the basis of CTO decision since 22th of December 2008. Providing of these services continues in commercial regime out of universal service.

24) SHARE CAPITAL AND RESERVES

	31 December 2008	31 December 2007
Nominal value per ordinary bearer share (CZK)	100	100
Number of shares	322,089,890	322,089,890
Nominal value per ordinary registered share (CZK)*	1,000	1,000
Number of shares*	1	1
Ordinary shares (in CZK million)	32,209	32,209

* One share owned by the National Property Fund of the Czech Republic bore special decision-making rights in accordance with the statutes of the Company. These special rights included namely decisions regarding the liquidation of the Company, changes in its activities, sale or lease of the Company or of its assets. This share was assigned to Telefónica, S.A. within the transferred 51.1% stake in the Company. From this date, the share has not borne special decision-making rights.

Shareholdings in the Company were as follows:

	31 December 2008	31 December 2007
Telefónica, S.A.	69.41%	69.41%
Other shareholders	30.59%	30.59%

Funds include a statutory reserve fund of CZK 6,442 million (2007: CZK 6,442 million) that is not distributable under ruling legislation. Equity settled share based payments reserve is not distributable.

On 21 April 2008 the Annual General Shareholders Meeting approved the restructuring of equity in the form of transfer of CZK 6,442 million from share premium to statutory reserve fund. Further the opening balance of the statutory reserve fund of CZK 6,442 million was transferred to retained earnings and used for distribution of dividend.

CAPITAL MANAGEMENT

The Company is not subject to any externally imposed capital requirements.

The Company's objectives when managing its capital are:

a) to safeguard the Company's ability to continue as a going concern so that it can provide value for its shareholders, and
b) to comply with all relevant legal requirements.

The investment strategy in the light of managing capital of the Company is to focus investment activities on pro-growth areas, i.e. broadband internet, IPTV, mobile services and corporate ICT solutions and on the expansion of mobile services in Slovakia.

At present, the approach that the Company follows is not to retain surplus cash. In the following periods, the Board of Directors will continue to evaluate and carry out an in-depth analysis of the current and anticipated results of the Company, including scheduled and potential investments and cash flow generation and will establish the most adequate capital structure for accomplishment of the plans.

There is no other specific objective.

No changes were made in the objectives, policies or processes during the years 2008 and 2007.

The equity breakdown used in the capital management is following:

In CZK million	31 December 2008	31 December 2007
Capital	81,434	84,445
Equity settled share based payment reserve	45	–
Net unrealized gains reserve (cash flow hedge)	–	(20)
Total	81,479	84,425

25) HEDGING RESERVE

In CZK million	
Balance at 1 January 2007	(18)
Fair value losses in period	(17)
Fair value losses transfer to net profit	15
Balance at 31 December 2007	(20)
Fair value losses in period	24
Fair value losses transfer to net profit	(4)
Balance at 31 December 2008	–

26) RELATED PARTY TRANSACTIONS

The Company provides services to all related parties on normal commercial terms. Sales and purchase transactions with related parties are based on contractual agreements negotiated on normal commercial terms and conditions and at market prices. Outstanding balances of assets and liabilities are unsecured, interest free (excl. financial assets used for financing) and the settlement occurs either in cash or by offsetting. The financial assets balances are tested for the impairment at the balance sheet date, and no allowance or write off was incurred.

The following transactions were carried out with related parties:

I. PARENT COMPANY

In CZK million	31 December 2008	31 December 2007
Dividend paid to Telefónica, S.A.	11,179	11,179
Royalty fees (Telefónica, S.A)	626	9

II. OTHER RELATED PARTIES – TELEFÓNICA GROUP

In CZK million	31 December 2008	31 December 2007
a) Sales of services and goods	1,012	982
b) Purchases of services and goods	1,041	817
c) Capital purchases	5	1
d) Receivables	480	159
e) Payables	4,336	1,001
f) Short-term receivables (interest)	14	17
g) Interest income	375	330
h) Cash equivalents	6,344	5,107

The list of the Telefónica companies with which the Company had any transaction in 2008 includes the following entities: Telefónica, S.A., Telefónica de España, S.A.U., O2 Germany GmbH& CO.OHG, Telefónica Deutschland GmbH, O2 (UK) Ltd., O2 Communications (Ireland) Ltd., Telefónica Móviles España, S.A.U., Telefónica Móviles Argentina, S.A., Pléyade Peninsular, O2 Holdings Ltd., Manx Telecom Ltd., Telefónica Móviles Guatemala, S.A., Telefónica Móviles El Salvador, S.A. de C.V., Telefónica Móviles Panamá, S.A., Telefónica Móviles Chile, S.A., Otecel, S.A., Telefónica Móviles Nicaragua, S.A, Telefónica Móviles Columbia, S.A., Telefónica S. de Informática y Comunicaciones de Espana, S.A.U., Telefónica Investigación y Desrrollo, S.A., Médi Telecom, S.A., Portugal Telecom, S.G.P.S., S.A., Telfisa Global, BV., Telefónica International Wholesale Services, S.L., Telefónica Gestión de Servicios Compartidos, S.A., Telefónica Factoring E.F.C., S.A., Atento Chequia, Telefónica Compras Electrónica, S.L., Telefónica Móviles Mexico, S.A, Telefónica Móviles del Uruguay, S.A, Telefónica Móviles Peru, S.A, Telefónica Venezuela, S.A., Telefónica O2 Business Solutions, spol. s r.o, DELTAX Systems a.s., CZECH TELECOM Germany GmbH, CZECH TELECOM Austria GmbH, Telefónica O2 Slovakia, s.r.o.

III. OTHER RELATED PARTIES

a) Key management compensation

Members of the Board of Directors and of the Supervisory Board of the Telefónica O2 Czech Republic, a.s., were provided with benefits as follows:

In CZK million	31 December 2008	31 December 2007
Salaries and other short-term benefits	123	153
Personal indemnification insurance	7	9
Total	130	162

b) Loans to related parties

There were no loans provided to members of Board of Directors and Supervisory Board in 2008 and 2007.

No other loan was provided to related parties by the Company.

27) PRINCIPAL SUBSIDIARY UNDERTAKINGS

	Company's interest	Cost of investment in CZK million	Country of incorporation	Activity
SUBSIDIARIES				
1. Telefónica O2 Business Solutions, spol. s r.o. (formerly Telefónica O2 Services, spol. s r.o.)	100%	30	Czech Republic	Network and consultancy services in telecommunications
2. SPT TELECOM (Czech Republic) Finance B.V. (in liquidation)	100%	1	Netherlands	Financing other entities in the Company
3. CZECH TELECOM Germany GmbH	100%	29	Germany	Data transmission services
4. CZECH TELECOM Austria GmbH	100%	11	Austria	Data transmission services
5. Telefónica O2 Slovakia, s.r.o.	100%	1,219	Slovakia	Mobile telephony, internet and data transmission services
6. DELTAX Systems a.s.	100%	207	Czech Republic	IT/ICT services
ASSOCIATES				
7. První certifikační autorita, a.s.	23%	10	Czech Republic	Rendering of certification services
8. AUGUSTUS spol. s r.o.	40%	–	Czech Republic	Sales by auctions and advisory services

On 30 November 2007 the voluntary liquidation process of the subsidiary CenTrade, a.s., in liquidation was effectively terminated. The Company received the liquidation surplus of CZK 32 million. The cancellation of the registration from the Commercial Register was performed as of 22 August 2008.

During the fourth quarter 2007, SPT TELECOM (Czech Republic) Finance B.V. in liquidation commenced preparatory steps for the process of voluntary liquidation. Until the end of 2008, the key legal steps for dissolution of the Company have been executed. The cancellation of the registration from the Commercial Register was performed as of 9 February 2008.

In December 2008, the Board of Directors of the Company approved the plan to merge Telefónica O2 Business Solutions, spol. s r.o. with DELTAX Systems a.s. This merger will become effective 1 January 2009 after the fulfillment of all legal conditions expected to be performed in the first half of 2009. Telefónica O2 Business Solutions, spol. s r.o. will become the legal successor while DELTAX Systems a.s. will be dissolved without liquidation. The assets, rights and obligations including labour rights and duties will be transferred to the successor.

28) POST BALANCE SHEET EVENTS

In January 2009, the Company sold a construction site and two administrative buildings of the former headquarters in Olšanská Street in Prague (see Note 8). Net gain from the sale of the real estates amounted to CZK 342 million. The assets did not meet criteria for classification as assets held for sale as at 31 December 2008.

In January 2009, the Telefónica Group won a tender for providing a complete portfolio of services for the company DHL throughout Europe. The entire project will be managed by the dedicated Service Management Centre in Prague and is expected to start in summer 2009.

There were no events, which have occurred subsequent to the year-end, which would have a material impact on the financial statements at 31 December 2008.

OTHER INFORMATION FOR SHAREHOLDERS AND INVESTORS

07

Nothing will stop a man who is trying to improve. Every obstacle along the way means a step up in the effort. It helps the drive for the goal. Talent also helps – but it will not get you as far as ambition.

OTHER INFORMATION FOR SHAREHOLDERS AND INVESTORS

BASIC INFORMATION

Corporate name:	Telefónica O2 Czech Republic, a.s. (Telefónica O2, the Company)
Registered address:	Za Brumlovkou 266/2, 140 22 Prague 4
Company identification number:	60193336
Taxpayer registration number:	CZ60193336
Date of incorporation:	16 December 1993
Legally existing from:	1 January 1994
Duration of the company:	the company was founded for an indefinite period of time
Legal form:	joint-stock company
Statute of law under which the issuer was incorporated:	provisions of Section 171 (1) and Section 172 (2) and (3) of the Commercial Code
Commercial court:	Prague Municipal Court
Commercial court record number:	Section B, Enclosure 2322

INFORMATION, WHICH ARE PART OF THE EXPLANATORY REPORT IN ACCORDANCE WITH THE REQUIREMENTS OF SECTION 118 (8), ACT NO. 256/2004 COLL., ON UNDERTAKING ON THE CAPITAL MARKET, RELATING TO THE ISSUES PURSUANT TO SECTION 118 (3) (G) – (Q), ACT ON UNDERTAKING ON THE CAPITAL MARKET:

1. Information on the structure of the issuer's equity, including securities not accepted for trading on the regulated market based in a member state of the European Union and potential determination of different types of shares, rights and duties relating to the shares of the same type and stake of each type of shares in the share capital

The structure of Telefónica O2 equity as of 31 December 2008 was as follows:

In million CZK	
Share capital	32,209
Share premium	24,374
Hedging reserve	–
Equity settled share based payments reserve	45
Funds	6,450
Retained profit	18,401
Total	81,479

The Company's share capital amounted to CZK 32,208,990,000 as of 31 December 2008, is fully paid up and is made up of the following shares.

A.	Type:	ordinary share
	Form:	bearer share
	Kind:	booked
	Number of shares:	322,089,890 shares
	Nominal value:	CZK 100
	Total issue volume:	CZK 32,208,989,000
	ISIN:	CZ0009093209

B.	Type:	ordinary share
	Form:	registered share
	Kind:	booked
	Number of shares:	1 share
	Nominal value:	CZK 1,000
	Total issue volume:	CZK 1,000

As of the effective date of the agreement on the transfer of shares between Telefónica, S.A. (Telefónica) and the National Property Fund of the Czech Republic, the registered share has lost the special rights which were attached to it pursuant to the provisions of Article IV (2) of Act no. 210/1993 Coll., amending the Act no.92/1991 Coll., on the conditions of transfer of state property to other entities, as amended.

The bearer shares in the nominal value of CZK 100 are listed for trading on the following markets:

Market	Note
Prague Stock Exchange (Burza cenných papírů Praha a.s.)	On the main market
RM-SYSTÉM, česká burza cenných papírů a.s.	
London Stock Exchange	In the form of Global Depository Receipts (GDR). The depository for the GDR is The Bank of New York Mellon, ADR Division, 101 Barclay Street, West New York, NY 10286, USA; the custodian is Komerční banka, a.s., Na Příkopě 33, čp. 906, 114 07 Prague 1.

A full wording of the Terms and Conditions of the Share Issue – the document which is the source of this summary – is available at the registered address of the security issuer.

The registered share in the nominal value of CZK 1,000 has not been listed on the regulated market seated in a member state of the European Union.

2. Information on limitations on securities transferability

The transfer of shares and Global Depository Receipts is conditional on compliance with statutory requirements. The Company's Articles of Association do not regulate the transfer of shares in any way; neither there are any other restrictions for reasons on the part of the Company.

3. Information about material direct and indirect shares in the voting rights of the issuer

Key shareholders of Telefónica O2 as at 31 December 2008:

Shareholder	Address	% of share capital
1. Telefónica, S.A.	Gran Vía 28, 28013 Madrid, the Kingdom of Spain	69.41%
2. Investment funds and individual shareholders	–	30.59%

As at 31 December 2008, the share of Telefónica, S.A., in the voting rights of Telefónica O2 Czech Republic, a.s., pursuant to the provisions of Section 122 of the Act on Undertaking on the Capital Market, was 69.41%.

4. Information on owners of securities with special rights, including description of these rights

The Company has not issued any securities with special rights, only the booked ordinary share referred to in the letter 1. above.

5. Information about restrictions of voting rights

Voting rights are attached to all shares issued by the Company and may be restricted or excluded only in instances required by the law. The Company is not aware of any such statutory restriction or exclusion of voting rights. The Company's Articles of Association do not stipulate any restriction of voting rights; neither there are any other restrictions for reasons on the part of the Company.

6. Information on contracts between shareholders which might cause worsening of transferability of shares or voting rights if the issuer is familiar with them

The Company is not aware of any information on contracts between shareholders that might cause worsening of the transferability of shares or voting rights.

7. Information on special rights defining the election and recall of members of the Board of Directors and amendment to the Company's Articles of Association

Members of the Board of Directors are elected and recalled by the Supervisory Board. The conditions of electing members of the Board of Directors are regulated by law; the Articles of Association do not contain any limitations beyond the scope of law, neither is there any limitations existing on the part of the Company.

Two thirds of members of the Supervisory Board are elected and recalled by the General Meeting; one third is elected and recalled by Company employees. The conditions of electing Supervisory Board members are regulated by law; the Articles of Association contain limitations beyond the scope of law only in respect to the fact that the Company Chief Executive Officer cannot be elected a member of the Supervisory Board. There is no other limitation existing on the part of the Company.

8. Information on special authorities of members of the Board of Directors, particularly on authorisation pursuant to Section 161 (a) and 210, the Commercial Code

Members of the Board of Directors do not have any special powers; pursuant to Article 14 (4), Articles of Association, some acts of the Board of Directors require a prior consent of the Supervisory Board.

9. Information on material contracts where the issuer is a contracting party and which will come into force, will be amended or terminate in case of the changed control of the issuer as a result of a takeover proposal and effects here from, except for those contracts the publication of which would damage the issuer seriously; the above does not limit any other duty to publish such information under this law or under special legal regulations

The Company did not conclude any contracts that will come into effect, will be amended or terminate in case of a changed control of the issuer as a result of a takeover proposal.

10. Information on contracts concluded between the issuer and members of the issuer's Board of Directors or employees through which the issuer is committed to contract performance in the case of termination of their offices or employment in relation to the takeover proposal

No contracts were concluded between the Company and members of the Company Board of Directors or Company employees that would commit the Company to any contract performance in the case of termination of their offices or employment in relation to the takeover proposal.

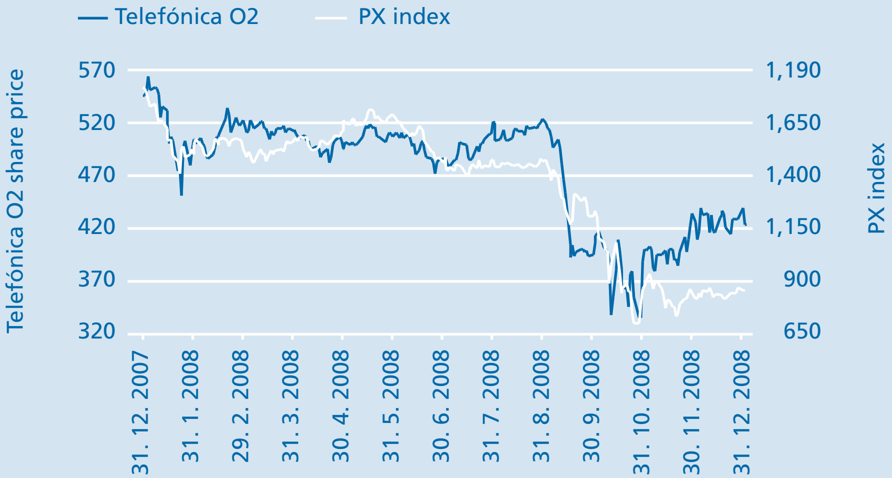
11. Information on potential programmes based on which the Company employees and members of the Board of Directors are allowed to acquire Company securities, options on these securities or other rights under favourable terms and on how the rights relating to theses securities are exercised

No programmes were developed for members of the Board of Directors or Company employees that would allow them to acquire Company securities, options on these securities or other rights relating to these securities under favourable conditions.

BONDS ISSUED BY TELEFÓNICA O2
(as at 31 December 2008)
Bond programme:
Maximum volume of unredeemed bonds: CZK 20,000,000,000
Programme duration: 2002–2012
Maturity of issues in the programme: maximum of 15 years.

On 9 July 2008, as required by the Terms and Conditions of the Bond Issue for Bond Dluhopis TELEF.O2CR 3,50% / 2008", ISIN: CZ0003501355, Telefónica O2 redeemed

Trading in Telefónica O2 shares projected over the PX index in 2008



bonds in the total value of CZK 6,000,000,000. As a result, the bond programme did not include any bonds issued as at 31 December 2008.

TRADING IN THE SHARES OF TELEFÓNICA O2 IN 2008

	2008	2007
Number of shares (in millions)	322.1	322.1
Net profit/(loss) per share (in CZK)[1]	40.6	36.9
Highest share price (in CZK)[2]	563.5	622.8
Lowest share price (in CZK)[2]	336.0	473.7
Share price at the end of period (in CZK)[2]	424.1	544.8
Market capitalization (in CZK billions)[2]	136.6	175.5

[1] unconsolidated net profit under IFRS
[2] source: Prague Stock Exchange

In 2008, Telefónica O2 once again ranked among the most important companies on the Czech capital markets according to market capitalization and trading volumes. The total volume of trades in company shares on the main stock market of the Prague Stock Exchange (PSE) in 2008 was CZK 91.1 billion compared to CZK 101.8 billion in 2007. Trading in Telefónica O2 Czech Republic shares, as measured by the total volume of shares, made up 10.9% of all trades on the PSE stock market. Telefónica O2 shares were the third most traded issue on the PSE in 2008, after ČEZ and Komerční banka. The average daily volume of trades in company shares in 2008 was CZK 359.9 million.

As at 30 December 2008 (the last trading day on the PSE in 2008), the market capitalization reached CZK 136.6 billion, ranking Telefónica O2 the second on the PSE stock market. The share price of Telefónica O2 on the last PSE trading day in 2008 reached CZK 424.1, which was a decline of 22% on the year previous, but still the second best performance out of all the blue chips traded on the PSE main market. The share price reached its maximum of CZK 563.5 on 3 January 2008, and its minimum of CZK 336 on 27 October 2008. The average share price in 2008 was CZK 475, compared to CZK 564.9 in 2007.

The above-average dividend yield, aided by the high free cash flow generation and a low level of debt, still make the shares of Telefónica O2 very attractive for investors, as was attested during the time of the general slump at the main capital markets of the world.

DIVIDENDS

At the Ordinary General Meeting of 27 April 2006 held in Prague, the shareholders approved a dividend payment from the 2005 net profit and part of the retained earnings from previous years, in the total amount of CZK 14.494 billion, i.e. CZK 45 per share of nominal value of CZK 100 and CZK 450 per share of nominal value CZK 1,000, before tax. The record day for the payment of dividends was 25 September 2006 and the disbursement date 2 October 2006.

At the Ordinary General Meeting of 27 April 2007 held in Prague, the shareholders approved a dividend payment from the 2006 net profit and part of the retained earnings from previous years, in the total amount of CZK 16.104 billion, i.e. CZK 50 per share of nominal value of CZK 100 and CZK 500 per share of nominal value CZK 1,000, before tax. The record day for the payment of dividends was 10 September 2007 and the disbursement date 3 October 2007.

At the Ordinary General Meeting of 21 April 2008 held in Prague, the shareholders approved a dividend payment from a part of the 2007 net profit and a part of the reserve fund which the Company can use at its discretion, in the total amount of CZK 16.104 billion, i.e. CZK 50 per share of nominal value of CZK 100 and CZK 500 per share of nominal value of CZK 1,000, before tax. The record day for the payment of dividends was 17 September 2008 and the disbursement date 8 October 2008.

DIVIDEND POLICY
The Company does not have an official long-term dividend policy at present. The Company has indicated several times that it did not intend to retain surplus cash. In the following periods, the Board of Directors will make annual proposals for the payment of dividend, based on a diligent analysis of the current and future performance of the Company, including the projected future cash flows and investments, development costs and acquisitions. This approach is in line with the investment strategy of directing investment into pro-growth areas, such as high-speed internet access, mobile services, ICT solutions for the corporate segment and the development of the mobile operation in Slovakia.

DETAILS OF PATENTS OR LICENSES, INDUSTRIAL, COMMERCIAL OR FINANCIAL CONTRACTS WHICH HAVE A SIGNIFICANT BEARING ON THE BUSINESS

1. PATENTS AND LICENCES
Telefónica O2 has licence agreements for the following software products: application middleware (BEA), database environment (Oracle), operating systems (Hewlett-Packard, SUN and Microsoft), workstation software (Microsoft), CRM using Siebel SW (Oracle), customer care and billing software (Amdocs and LHS) and enterprise resource planning software (SAP).

2. INDUSTRIAL AND COMMERCIAL CONTRACTS
Telefónica O2 maintains a diverse portfolio of technology suppliers. The main objective of the issuer with respect to the contracted suppliers is to have competition on the supply side. All principal technology supply contracts are awarded by tender.

In 2008, the main suppliers of technology and related services to the Company were IBM Česká republika, Alcatel Czech, AutoCont CZ, Vegacom, Siemens, Accenture Central Europe B.V., DNS, NextiraOne Czech, Amdocs Development Limited, LHS, Hewlett-Packard and Huawei Technologies Co.

3. FINANCIAL CONTRACTS
Financial liabilities as at 31 December 2008 divided into short-term and long-term (in CZK million):

Short-term (maturing within a year)	98
Long-term	3,098
Total	3,196

Loans, bonds issued and other financial liabilities:

	Currency	Outstanding in the currency as at 31 December 2008	Outstanding in CZK as at 31 December 2008	Redemption
Private Placement – debt instrument	EUR	115,040,673	3,098,045,331	2012
Other financial liabilities			98,101,519	

EUR/CZK exchange used in the table for conversion purposes (as at 31 December 2008) was CZK 26.930/EUR.

The above loan and the other financial liabilities were repaid in accordance with the relevant loan agreements or the Terms and Conditions of Issue. As at 31 December 2008, Telefónica O2 had no overdue loan obligations.

On 9 July 2008, as required by the Terms and Conditions of the Bond Issue for Bond Dluhopis TELEF.O2CR 3,50% / 2008",ISIN: CZ0003501355, Telefónica O2 redeemed bonds in the nominal value of CZK 6,000,000,000.

On 21 November 2008, the Syndicated Loan Agreement concluded on 21 November 2003 expired. Telefónica O2 last used the loan in 2005.

INVESTMENTS

Main investments made by Telefónica O2 in the last two accounting periods (in CZK million):

	2008	2007
Network & Operations	3,661	3,497
Customer Solutions	694	524
IT & Products	1,838	1,506
Property & Logistics	302	522
Point of Sale Redesign & Re-branding	53	193
Investments related to Telefónica O2 Slovakia made in the Czech Republic	197	343
Telefónica O2 Slovakia	1,302	1,213
Other subsidiaries	41	9
Total	8,088	7,807

All major investments were made in the Czech Republic and in Slovakia were financed from own capital and from borrowings.

In 2008, the Company continued to implement the standard investment policy, which clearly favours the development of progressive, customer-oriented technologies and emphasises the internal integration of the Company.

The structure of investment expenditure reflected the existing customer demands for new trends in telecommunications services with a high standard of execution, and the efforts to complete the integration processes and strengthen the primacy of the converged operator.

In the area of the fixed network, investment was aimed mainly at upgrading connection speeds, increasing the availability of ADSL, IPTV, Voice over IP and value-added services. In the mobile business, investments in the GSM network and preparatory work for the subsequent UMTS technology roll-out dominated.

Investment was primarily directed in the area of customer solutions; the volume of investment in this segment recorded a 32% year-on-year increase. An important role was played by newly developed data connectivity projects. In the area of data services, the focus was on improving the quality of the service portfolio and on customer experience, in particular with regard to the leadership in the market of converged services.

Convergent process integration was represented mainly by investment in information system; here, the common denominator was an effort to improve customer experience and offer innovative products and services.

The attention paid to the integration process was manifested in the increased investment in the information systems; customer experience was the common motto of all investment activities. The trend was also apparent in investments related to the integration of the Company's points of sale. The new headquarters also played a major role in the cultural alignment process.

In the area of regulatory compliance in the fixed line segment, investments were made in order to accommodate requirements of the Czech Telecommunications Office.

In Slovakia, the investment focused mainly on the construction of the proprietary GSM network in line with the licence obligations, and on system development. Telefónica O2 Slovakia commissioned more than 850 base stations by the end of the year, which meant that it complied with the requirements of the mobile licence in Slovakia. Its network now covers almost 90% of the population, which is approximately twice as much as what the licence requires, and it can carry approximately 83% of the voice traffic generated by users in the network.

PRINCIPAL FUTURE INVESTMENTS

In the period 2009-2010, the Company will continue to implement the standard investment policy for the telecommunications sector, which favours performance increases and the implementation of progressive technologies and customer approaches, aimed at achieving the key strategic goal – to confirm the leadership of the Czech telecommunications market and to increase the market share on the Slovak telecommunications market.

A key project in the Czech Republic is the country-wide deployment of UMTS, which will lay foundations for the later considerable expansion of technology platforms for future telecommunications and data services, delivering higher quality and more variability and choice for the customer.

INFORMATION ON FEES PAID TO AUDITORS IN THE ACCOUNTING PERIOD

Costs incurred by Telefónica O2 in connection with activities of Ernst & Young, the external auditor, in 2008:

Type of service	Fees (in CZK thousands)
Audit	18,757
Other audit-related advisory services	0
Other services	0
Total	18,757

Costs of the Telefónica O2 Group incurred in connection with the activities of Ernst & Young, the external auditor in 2008:

Type of service	Fees (in CZK thousands)
Audit	23,141
Other audit-related advisory services	0
Other services	0
Total	23,141

GENERAL MEETING

The Ordinary General Meeting of Telefónica O2 will be held on 3 April 2009 in Prague.

FINANCIAL CALENDAR

Date of release of the running financial results

For the first quarter of 2009	28 April 2009*
For the first half of 2009	28 July 2009*
For three quarters of 2009	27 October 2009*
For the year 2009	28 February 2010 at the latest instance

* subject to changes

INSTITUTIONAL INVESTORS AND SHAREHOLDERS PLEASE CONTACT

Investor Relations

Tel.: +420 271 462 076, +420 271 462 169
Fax: +420 271 463 566
E-mail: investor.relations@o2.com
URL: http://www.cz.o2.com/osobni/cz/o_nas/investor_relations/index.html
Address: Telefónica O2 Czech Republic, a.s.
Za Brumlovkou 266/2
140 22 Praha 4

INFORMATION ON PERSONS RESPONSIBLE FOR THE ANNUAL REPORT AND FOR VERIFICATION OF THE FINANCIAL STATEMENTS

Salvador Anglada Gonzalez, Chairman of the Board of Directors and Chief Executive Officer of Telefónica O2 Czech Republic, a.s.

Jesús Pérez de Uriguen, Member of the Board of Directors and Vice-President, Finance Division, Telefónica O2 Czech Republic, a.s.

hereby declare that the information contained in this Annual Report is accurate and that no significant facts which could influence the accurate and correct evaluation of the company were omitted.

Salvador Anglada Gonzalez
Chairman of the Board of Directors and
Chief Executive Officer

Jesús Pérez de Uriguen
Member of the Board of Directors and
Vice-President, Finance Division


JAPAN

APPENDIX

08

Only values without which it would be hard to live are worth risking everything. Foresight, choosing the right weapons and effective defence are key for professionalizing one’s interests.

APPENDIX

REPORT OF THE BOARD OF DIRECTORS OF TELEFÓNICA O2 CZECH REPUBLIC, A.S.

On relationships between the controlling and the controlled entity and on relationships between the controlled entity and other entities controlled by the same controlling entity for 2008 (pursuant to provisions of Section 66a of Act No. 513/1991 Coll., the Commercial Code, as amended)

TABLE OF CONTENTS

PART A APPLICABLE PERIOD

The report pursuant to Section 66a of Act No. 513/1991 Coll., the Commercial Code, as amended (Commercial Code) on relationships between the controlling and the controlled entity and on relationships between the controlled entity and other entities – interconnected entities controlled by the same controlling entity (Report) is prepared for the last accounting period, i.e. for the period started on 1 January 2008 and ended on 31 December 2008.

PART B ENTITIES FORMING A HOLDING

SECTION I. IDENTIFICATION DETAILS OF THE CONTROLLED ENTITY – TELEFÓNICA O2 CZECH REPUBLIC, A.S. (HEREINAFTER REFERRED TO AS "COMPANY")

The company is registered in the Commercial Register of the Municipal Court in Prague, Section B, Enclosure 2322.

Registration date:	1 January 1994
Corporate name:	Telefónica O2 Czech Republic, a.s.
Registered address:	Prague 4, Michle, Za Brumlovkou 266/2, PSČ 140 22
Identification number:	60 19 33 36
Legal form:	Joint-stock company

Compared to the fiscal year of 2007, there were no changes in identification data and basic legal facts.

Based on the Company's Board of Directors resolution dated 17 July 2007 adopted by virtue of the exercise of rights of the sole member, the process of liquidation of SPT TELECOM (Czech Republic) Finance B.V. continued in 2008. The liquidation was finalised in February 2009.

SECTION II. IDENTIFICATION DETAILS OF THE CONTROLLING ENTITY

Controlling entity:	Telefónica, S.A.
Registered address:	Gran Vía, 28, 28013 Madrid, Spanish Kingdom
Identification number:	A 28015865

The controlling entity held shares of the controlled entity in the aggregate nominal value of 69.41% of the registered capital of the controlled entity.

The total share in the voting rights of the controlled entity pursuant to Section 183d (1) of the Commercial Code was 69.41%.

69.41% Telefónica, S.A. Other investors 30.59%

Telefónica O2 Czech Republic, a.s.

SECTION III. INTERCONNECTED ENTITIES

Entities controlled by Telefónica, S.A.:

The list of entities controlled directly or indirectly by Telefónica, S.A. forms Appendix to this Report. The list was compiled from inputs from Telefónica, S.A. and verified using information from Commercial Registers or other available data.

PART C CONTRACTS AND AGREEMENTS BETWEEN THE CONTROLLED ENTITY AND THE CONTROLLING ENTITY AND CONTRACTS AND AGREEMENTS BETWEEN THE CONTROLLED ENTITY AND OTHER INTERCONNECTED ENTITIES INCLUDING DETAILS OF PERFORMANCE AND COUNTER-PERFORMANCE PROVIDED THEREUNDER

In the applicable period, contracts for the provision of services, credit contracts, a trademark assignment contract, a licence contract, lease contracts and insurance contracts were concluded with the controlling entity and with interconnected entities.

These contracts were entered into either with the controlling entity Telefónica, S.A. or with the interconnected entities hereunder: Telefónica de España, S.A.U., Telefónica O2 Business Solutions, spol. s r.o., O2 Germany GmbH, CZECH TELECOM Austria GmbH, CZECH TELECOM Germany GmbH, Telefónica International Wholesale Services, S.L., Telefónica Investigación y Desarollo, S.A, Atento Česká Republika, a.s., O2 Holdings Ltd., DELTAX Systems a.s., Telefónica O2 Slovakia, s.r.o., Telefónica Finanzas, S.A.

Details of contracts concluded are regarded as a trade secret by the controlled entity, according to the Commercial Code and other internal governance documents. The controlled entity has not suffered any damage in connection with contracts and agreements concluded in 2008 between the controlled entity and controlling entity and between controlled entity and other interconnected entities, under which performance and counter-performance was given, or in connection with provision of performance and counter-performance in 2008 under contracts and agreements concluded prior to 1 January 2008. Performance provided under the above contracts did not entail any advantages or disadvantages for the controlled entity.

PART D OTHER LEGAL ACTS BETWEEN HOLDING ENTITIES IN THE ACCOUNTING PERIOD 2008

In accounting period 2008, no legal acts were made by the controlled entity in the interest of or instigated by these controlling or interconnected entities, resulting in a damage or profit, advantage or disadvantage to the controlled entity.

PART E MEASURES BETWEEN HOLDING ENTITIES IN THE ACCOUNTING PERIOD 2008

In accounting period 2008, no measures were taken by the controlled entity in the interest of or instigated by these controlling or interconnected entities, resulting in a damage or profit, advantage or disadvantage to the controlled entity.

PART F CONCLUSION

a) The Report was prepared by the Board of Directors of the controlled entity, Telefónica O2 Czech Republic, a.s., and approved at the meeting of the Board of Directors held on 3 March 2009.
b) The Report was prepared using data and information obtained from the controlling entity and other interconnected entities, other available documents, and using results of examinations of relationships between the controlled entity on the one hand and the controlling entity and other interconnected entities on the other hand. The Board of Directors of the controlled entity, Telefónica O2 Czech Republic, a.s., declares that it proceeded with due professional diligence of a manager when collecting the data and information.
c) With regard to the fact that the controlled entity, Telefónica O2 Czech Republic, a.s., is obliged by law to make an Annual Report pursuant to Act No. 563/1991 Coll., on accounting, as amended, this Report will be attached to the 2008 Annual Report. Shareholders will have the opportunity to read the Report at the same time and under the same conditions as the financial statements.

In Prague, on 3rd March 2009

Telefónica O2 Czech Republic, a.s. – controlled entity

Board of Directors

APPENDIX

LIST OF COMPANIES DIRECTLY OR INDIRECTLY CONTROLLED BY TELEFÓNICA, S.A. (WITH AN OWNERSHIP INTEREST OF TELEFÓNICA GROUP OF 40–100%) IN THE PERIOD FROM 1 JANUARY 2008 UNTIL 31 DECEMBER 2008

	Share of direct controlling	Share of indirect controlling	Share of Telefónica Group
Telefónica de Contenidos, S.A.U. (SPAIN)	100.00%		100.00%
Telefónica Media Argentina, S.A. (ARGENTINA)		100.00%	100.00%
AC Inversora S.A. (ARGENTINA)		100.00%	100.00%
Atlántida Comunicaciones, S.A. (ARGENTINA)		100.00%	100.00%
ATCO I S.A. (ARGENTINA)		100.00%	100.00%
Televisión Federal S.A. – TELEFE (ARGENTINA)		100.00%	100.00%
Enfisur, S.A. (ARGENTINA)		100.00%	100.00%
Tevefe Comercialización S.A. (ARGENTINA)		100.00%	100.00%
Telefónica Servicios Audiovisuales, S.A. (SPAIN)		100.00%	100.00%
Telefónica Servicios de Música, S.A.U. (SPAIN)		100.00%	100.00%
Telefónica Europe plc (UNITED KINGDOM)	100.00%		100.00%
mmO2 plc (UNITED KINGDOM)		100.00%	100.00%
O2 Holdings Ltd. (UNITED KINGDOM)		100.00%	100.00%
O2 Communications (Ireland) Ltd. (IRELAND)		100.00%	100.00%
Manx Telecom Ltd. (ISLE OF MAN)		100.00%	100.00%
The Link Stores Ltd. (UNITED KINGDOM)		100.00%	100.00%
Be Un Limited (Be) (UNITED KINGDOM)		100.00%	100.00%
Tesco Mobile Ltd. (UNITED KINGDOM)		50.00%	50.00%
O2 (Europe) Ltd. (UNITED KINGDOM)	100.00%		100.00%
Telefónica O2 Germany GmbH & Co. OHG (GERMANY)		100.00%	100.00%
Group 3G UMTS Holding, GmbH (GERMANY)		57.20%	57.20%
Quam, GmbH (GERMANY)		100.00%	57.20%
Opco Mobile Services GmbH (GERMANY)		100.00%	57.20%
Tchibo Mobilfunk GmbH & Co. KG (GERMANY)		50.00%	50.00%
Telefónica O2 Czech Republic, a.s. (CZECH REPUBLIC)	69.41%		69.41%
SPT TELECOM (Czech Republic) Finance, B.V. in liquidation (NETHERLANDS)		100.00%	69.41%
Telefónica O2 Business Solutions, spol. s r.o. (CZECH REPUBLIC)		100.00%	69.41%
CZECH TELECOM Germany GmbH (GERMANY)		100.00%	69.41%
CZECH TELECOM Austria GmbH (AUSTRIA)		100.00%	69.41%
Telefónica O2 Slovakia, s.r.o. (SLOVAKIA)		100.00%	69.41%
DELTAX Systems a.s. (CZECH REPUBLIC)		100.00%	69.41%
LE Holding Corporation (USA)	100.00%		100.00%
Centro de Investigación y Experimentación de la Realidad Virtual, S.L. (SPAIN)	100.00%		100.00%
Corporation Real Time Team, S.L. (SPAIN)	87.96%	12.04%	100.00%

	Share of direct controlling	Share of indirect controlling	Share of Telefónica Group
Terra Networks Asociadas, S.L. (SPAIN)	100.00%		100.00%
Educaterra, S.L. (SPAIN)		100.00%	100.00%
Red Universal de Marketing y Bookings Online, S.A. (SPAIN)		50.00%	50.00%
Terra Networks Marocs, S.A.R.L. (MOROCCO)	100.00%		100.00%
Telefónica International Wholesale Services, S.L. (SPAIN)	92.51%	7.49%	100.00%
Telefónica International Wholesale Services France, S.A.S. (FRANCE)		100.00%	100.00%
Telefónica International Wholesale Services America, S.A. (URUGUAY)	80.56%	19.44%	100.00%
Telefónica International Wholesale Services Argentina, S.A. (ARGENTINA)		100.00%	100.00%
Telefónica International Wholesale Services Brasil Participacoes, Ltd. (BRAZIL)		99.99%	99.99%
Telefónica International Wholesale Services Brasil, Ltd. (BRAZIL)		99.99%	99.99%
Telefónica International Wholesale Services Chile, S.A. (CHILE)		99.99%	99.99%
Telefónica International Wholesale Services Perú, S.A.C. (PERU)		99.99%	99.99%
Telefónica International Wholesale Services USA, Inc. (USA)		100.00%	100.00%
Telefónica International Wholesale Services Guatemala, S.A. (GUATEMALA)		99.99%	99.99%
Telefónica International Wholesale Services Puerto Rico, Inc. (PUERTO RICO)		100.00%	100.00%
Telefónica International Wholesale Services Colombia, S.A. (COLOMBIA)		99.97%	99.97%
Telefónica International Wholesale Services Ecuador, S.A. (ECUADOR)		100.00%	100.00%
Telefónica Datacorp, S.A.U. (SPAIN)	100.00%		100.00%
Telefónica Datos de Venezuela, S.A. (VENEZUELA)		99.99%	99.99%
Telefónica Data Canadá, Inc. (CANADA)		100.00%	100.00%

	Share of direct controlling	Share of indirect controlling	Share of Telefónica Group
Telefónica USA Inc. (USA)		100.00%	100.00%
Katalyx, Inc. (USA)		100.00%	100.00%
Telefónica Data Caribe (SPAIN)		100.00%	100.00%
Telefónica Data Argentina, S.A. (ARGENTINA)		100.00%	100.00%
Telefónica de España, S.A.U. (SPAIN)	100.00%		100.00%
Telefónica S. de Informática y Comunicaciones de España, S.A.U. (SPAIN)		100.00%	100.00%
Telefónica Soluciones de Outsourcing, S.A. (SPAIN)		100.00%	100.00%
Telefónica Soluciones Sectoriales, S.A. (SPAIN)		100.00%	100.00%
Interdomain, S.A. (SPAIN)		100.00%	100.00%
SODETEL, Comercial de Servicios de Telecomunicaciones, S.A. (SPAIN)		50.00%	50.00%
Portel Servicios Telemáticos, S.A. (SPAIN)		49.00%	49.00%
Teleinformática y Comunicaciones, S.A. (TELYCO) (SPAIN)		100.00%	100.00%
Telyco Marruecos, S.A. (MOROCCO)		54.00%	54.00%
Telefónica Telecomunicaciones Públicas, S.A. (SPAIN)		100.00%	100.00%
Telefónica Salud, S.A. (SPAIN)		51.00%	51.00%
Iberbanda, S.A. (SPAIN)		58.94%	58.94%
Iberbanda Inversiones, S.A. (SPAIN)		100.00%	58.94%
Telefónica Cable, S.A. (SPAIN)		100.00%	100.00%
Telefónica Cable Menorca, S.A. (SPAIN)		100.00%	100.00%
Terra Networks Serviços de Acceso a Internet e Trading Ltd. (PORTUGAL)	100.00%		100.00%
Taetel, S.L. (SPAIN)	100.00%		100.00%
Lotca Servicios Integrales, S.L. (SPAIN)	100.00%		100.00%
Telefónica Ingeniería de Seguridad, S.A. (SPAIN)	100.00%		100.00%
Telefónica Engenharia de Segurança (BRAZIL)		99.99%	99.99%

	Share of direct controlling	Share of indirect controlling	Share of Telefónica Group
Telefónica Ingeniería de Seguridad México, S.A. de C.V. (MEXICO)		100.00%	100.00%
Telefónica Ingeniería de Seguridad de Argentina, S.A. (ARGENTINA)		100.00%	100.00%
Telefónica Capital, S.A. (SPAIN)	100.00%		100.00%
Fonditel Pensiones, Entidad Gestora de Fondos de Pensiones, S.A. (SPAIN)		70.00%	70.00%
Fonditel Gestión, Sociedad Gestora de Instituciones de Inversión Colectiva, S.A. (SPAIN)		100.00%	100.00%
Ateseco Comunicación, S.A. (SPAIN)	100.00%		100.00%
Atento Holding, Inversiones y Teleservicios, S.A. (SPAIN)	100.00%		100.00%
Atento Česká republika, a.s. (CZECH REPUBLIC)		100.00%	100.00%
Atento EMEA, B.V. (NETHERLANDS)		100.00%	100.00%
Atento N.V. (NETHERLANDS)		100.00%	100.00%
Woknal, S.A. (URUGUAY)		100.00%	100.00%
Atento Teleservicios España, S.A. (SPAIN)		100.00%	100.00%
Contact US Teleservices, Inc. (USA)		100.00%	100.00%
Atento Servicios Técnicos y Consultoría, S.L. (SPAIN)		100.00%	100.00%
Servicios Integrales de Asistencia yAtención, S.L. (SPAIN)		100.00%	100.00%
Atento Brasil, S.A. (BRAZIL)		100.00%	100.00%
Atento Puerto Rico, Inc. (PUERTO RICO)		100.00%	100.00%
Atento Colombia, S.A. (COLOMBIA)		100.00%	100.00%
Atento Maroc, S.A. (MOROCCO)		100.00%	100.00%
Atento Venezuela, S.A. (VENEZUELA)		100.00%	100.00%
Atento Centroamérica, S.A. (GUATEMALA)		100.00%	100.00%
Atento de Guatemala, S.A. (GUATEMALA)		100.00%	100.00%
Atento El Salvador, S.A. de C.V. (EL SALVADOR)		100.00%	100.00%

	Share of direct controlling	Share of indirect controlling	Share of Telefónica Group
Atento Holding Chile, S.A. (CHILE)		100.00%	100.00%
Centro de Contacto Salta, S.A. (ARGENTINA)		100.00%	100.00%
Mar de Plata Gestiones y Contactos, S.A. (ARGENTINA)		100.00%	100.00%
Microcentro de Contacto, S.A. (ARGENTINA)		100.00%	100.00%
Córdoba Gestiones y Contacto, S.A. (ARGENTINA)		100.00%	100.00%
Atento Argentina, S.A. (ARGENTINA)		100.00%	100.00%
Atento Chile, S.A. (CHILE)		71.16%	99.06%
CTC Marketing e Informaciones, S.A. (NEXCOM) (CHILE)		100.00%	99.06%
Atento Educación, Ltda. (CHILE)		100.00%	99.06%
Atento Recursos, Ltda. (CHILE)		100.00%	99.06%
Teleatento del Perú, S.A.C. (PERU)		100.00%	100.00%
Atento Italia, S.R.L. (ITALY)		100.00%	100.00%
Atento Mexicana, S.A. De C.V. (MEXICO)		100.00%	100.00%
Atento Atención y Servicios, S.A. De C.V. (MEXICO)		100.00%	100.00%
Atento Servicios, S.A. De C.V. (MEXICO)		100.00%	100.00%
Atento Panamá, S.A. (PANAMA)		100.00%	100.00%
Telefónica Investigación y Desarrollo, S.A. (TIDSA) (SPAIN)	100.00%		100.00%
Telefónica Investigación y Desarrollo de Mexico, S.A. de C.V. (MEXICO)		100.00%	100.00%
Telefônica Pesquisa e Desenvolvimento do Brasil, Ltda. (BRAZIL)		100.00%	100.00%
Comet, Compañía Española de Tecnología, S.A. (SPAIN)	100.00%		100.00%
Cleon, S.A. (SPAIN)		50.00%	50.00%
Casiopea Reaseguradora, S.A. (LUXEMBOURG)	99.97%	0.03%	100.00%
Pléyade Peninsular, Correduría de Seguros y Reaseguros del Grupo Telefónica, S.A. (SPAIN)	16.67%	83.33%	100.00%

	Share of direct controlling	Share of indirect controlling	Share of Telefónica Group
Pléyade Perú Corredores de Seguros, S.A.C. (PERU)		99.93%	100.00%
Pléyade Argentina, S.A. (ARGENTINA)		99.80%	99.80%
TGP Brasil Corretora de Seguros e Resseguros, Ltda. (BRAZIL)		99.90%	99.90%
Pléyade México, Agente de Seguros y de Fianzas, S.A. de C.V. (MEXICO)		99.50%	99.50%
Pléyade Chile, S.A. (CHILE)		100.00%	100.00%
Altaïr Assurances, S.A. (LUXEMBOURG)		100.00%	100.00%
Seguros de Vida y Pensiones Antares, S.A. (SPAIN)	89.99%	10.01%	100.00%
Telefónica Finanzas, S.A. (TELFISA) (SPAIN)	100.00%		100.00%
Telefónica Finanzas Perú, S.A.C. (PERU)	100.00%		100.00%
Fisatel Mexico, S.A. de C.V. (MEXICO)	100.00%		100.00%
Telfisa Global, B.V. (NETHERLANDS)	100.00%		100.00%
Venturini España, S.A. (SPAIN)	100.00%		100.00%
Venturini, S.A. (SPAIN)		100.00%	100.00%
Telefónica Participaciones, S.A. (SPAIN)	100.00%		100.00%
Telefónica Emisiones, S.A. (SPAIN)	100.00%		100.00%
Telefónica Europe, B.V. (NETHERLANDS)	100.00%		100.00%
Telefónica Internacional USA Inc. (USA)	100.00%		100.00%
Telefónica Gestión de Servicios Compartidos España, S.A. (SPAIN)	100.00%		100.00%
Tempotel, Empresa de Trabajo Temporal, S.A. (SPAIN)		100.00%	100.00%
Telefónica Gestión de Servicios Compartidos, S.A. (ARGENTINA)	4.99%	95.00%	99.99%
Cobros Serviços de Gestao, Ltda. (BRAZIL)		99.33%	99.33%
Telefónica Servicios Integrales de Distribución, S.A.U. (SPAIN)		100.00%	100.00%
Telefónica Gestión de Servicios Compartidos Mexico, S.A. de C.V. (MEXICO)		100.00%	100.00%

	Share of direct controlling	Share of indirect controlling	Share of Telefónica Group
Telefónica Gestión de Servicios Compartidos de El Salvador, S.A. de C.V. (EL SALVADOR)		100.00%	100.00%
Telefonica Gestao de Serviços Compartilhados do Brasil, Ltda. (BRAZIL)		99.99%	99.99%
Telefónica Gestión de Servicios Compartidos, S.A.C. (PERU)		100.00%	100.00%
Telefónica Centros de Cobro Perú, S.A.C. (PERU)		100.00%	100.00%
Telefónica Compras Electrónicas, S.L. (SPAIN)		100.00%	100.00%
Adquira Spain, S.A. (SPAIN)		40.00%	40.00%
Telefónica Internacional, S.A. (SPAIN)	100.00%		100.00%
Terra Networks Venezuela, S.A. (VENEZUELA)		100.00%	100.00%
Terra Networks Perú, S.A. (PERU)		99.99%	99.99%
Terra Networks Mexico Holding, S.A. De C.V. (MEXICO)		100.00%	100.00%
Terra Networks Mexico, S.A. De C.V. (MEXICO)		99.99%	99.99%
Terra Networks Guatemala, S.A. (GUATEMALA)		100.00%	100.00%
Terra Networks El Salvador, S.A. (EL SALVADOR)		99.99%	99.99%
Terra Networks Honduras, S.A. (HONDURAS)		99.99%	99.99%
Terra Networks Costa Rica, S.A. (COSTA RICA)		99.99%	99.99%
Terra Networks Nicaragua, S.A. (NICARAGUA)		99.99%	99.99%
Terra Networks Panamá, S.A. (PANAMA)		99.99%	99.99%
Terra Networks Argentina, S.A. (ARGENTINA)		100.00%	100.00%
Terra Networks Colombia , S.A. (La Ciudad.com) (COLOMBIA)		99.99%	99.99%
Servicios de Entretenimiento Holding S.A. (ARGENTINA)		100.00%	100.00%

	Share of direct controlling	Share of indirect controlling	Share of Telefónica Group
Colombia Telecomunicaciones, S.A. ESP (COLOMBIA)		52.03%	52.03%
Sao Paulo Telecomunicaçoes Participaçoes, Ltda. (BRAZIL)		100.00%	100.00%
Telecomunicaçoes de Sao Paulo, S.A. – TELESP (BRAZIL)		87.95%	87.95%
Telefonica Televisão Participações, S.A. (BRAZIL)		100.00%	87.95%
A.Telecom S.A. (BRAZIL)		100.00%	87.95%
Telefonica Sistema de Televisão, S.A. (BRAZIL)		100.00%	87.95%
Companhia AIX de Participações (BRAZIL)		50.00%	43.98%
Companhia ACT de Participações (BRAZIL)		50.00%	43.98%
Telefónica Data, S.A. (BRAZIL)		100.00%	87.95%
TS Tecnología de Informaçao, Ltd. (BRAZIL)		100.00%	87.95%
Telefónica Interactiva Brasil , Ltda. (BRAZIL)		99.99%	99.98%
Terra Networks Brasil, S.A. y subsidiarias (BRAZIL)		100.00%	99.98%
Terra Networks USA, Inc. y Filiales. (USA)		100.00%	100.00%
Telefónica del Perú, S.A.A. (PERU)	0.15%	98.03%	98.18%
Star Global Com, S.A. (PERU)		71.00%	69.70%
Telefónica Multimedia S.A.C.(PERU)		99.99%	98.17%
Telefónica Servicios Comerciales S.A.C.(PERU)		99.90%	98.08%
Media Networks Perú Latin America, S.A.C. (PERU)		99.90%	98.08%
Servicios Globales de Telecomunicaciones S.A.C. (PERU)		99.90%	98.08%
Inversiones Telefónica Móviles Holdind Ltd. (CHILE)	100.00%		100.00%
TEM Inversiones Chile Limitada (CHILE)		100.00%	100.00%
Telefónica Móviles Chile, S.A. (CHILE)		100.00%	100.00%
T.Moviles Chile Distribucion S.A. (CHILE)		100.00%	100.00%

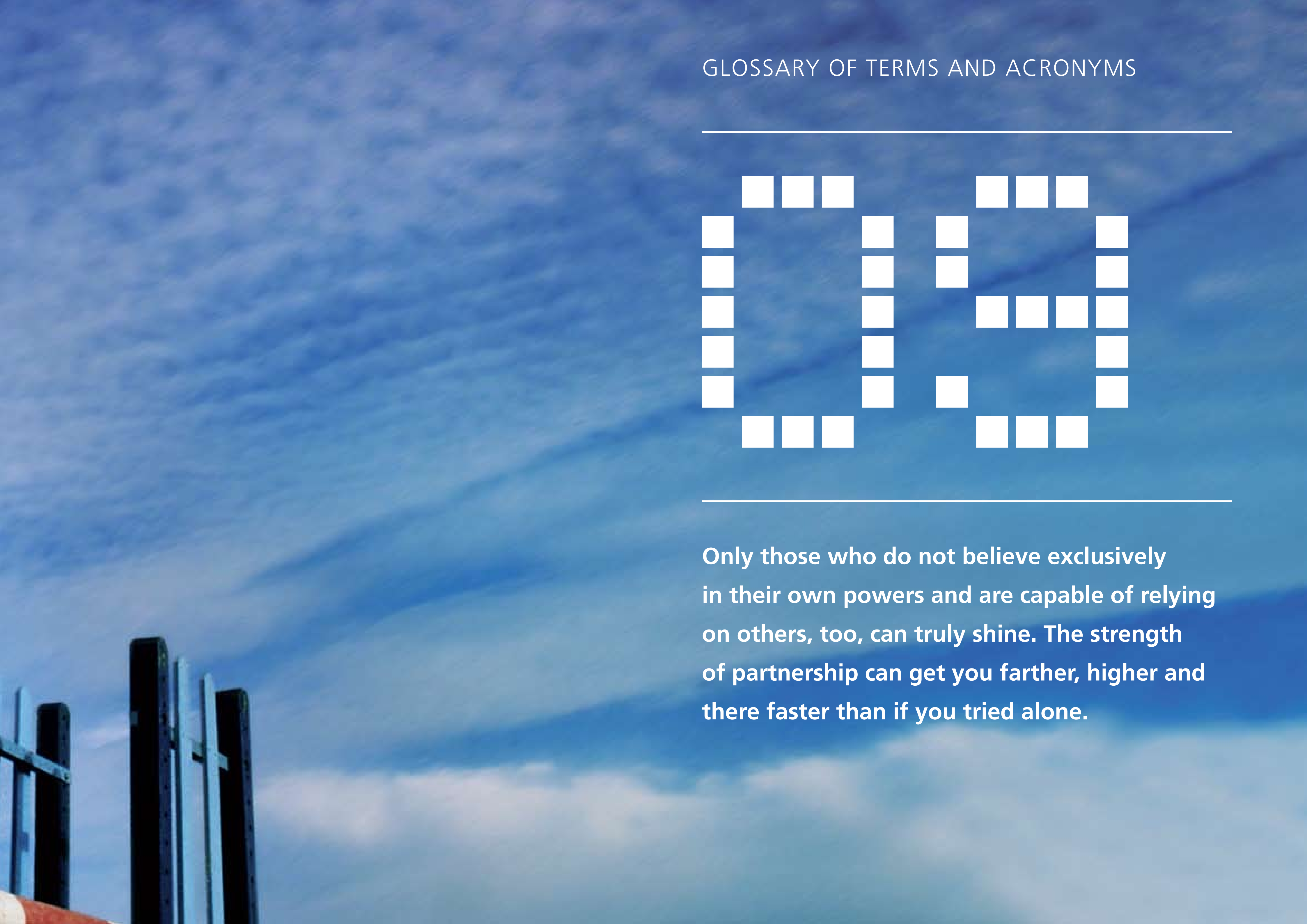
	Share of direct controlling	Share of indirect controlling	Share of Telefónica Group
Buenaventura (CHILE)		50.00%	50.00%
Telefónica Móviles Chile Inversiones. S.A. (CHILE)		100.00%	100.00%
Telefónica Móviles Chile larga Distancia, S.A. (CHILE)		100.00%	100.00%
Intertel, S.A. (CHILE)		100.00%	100.00%
Telefonica International Holding, B.V. (NETHERLANDS)		100.00%	100.00%
Telefónica Chile Holding, B.V. (NETHERLANDS)		100.00%	100.00%
Telefónica Internacional de Chile, S.A. (CHILE)		100.00%	100.00%
Inversiones telefónica Internacional Holding Limitada (CHILE)		99.99%	99.99%
Terra Networks Chile, S.A. (CHILE)		99.99%	99.99%
Compañía de Telecomunicaciones de Chile, S.A. (CHILE)		96.75%	96.75%
Telefónica Gestión de Servicios Compartidos de Chile, S.A. (CHILE)		99.99%	96.74%
Telefónica Holding de Argentina, S.A. (ARGENTINA)		99.96%	99.96%
Compañía Internacional de Telecomunicaciones, S.A. (ARGENTINA)		100.00%	99.98%
Telefónica de Argentina, S.A. (ARGENTINA)		98.20%	98.20%
Telefónica Larga Distancia de Puerto Rico, INC. (PUERTO RICO)		98.00%	98.00%
Telefonica China, B.V. (NETHERLANDS)		100.00%	100.00%
Telefónica Technologhy (Beijing) Comp Limtd (CHINA)		100.00%	100.00%
Brasilcel, N.V. (NETHERLANDS)	50.00%		50.00%
Tagilo Participaçoes, Ltda. (BRAZIL)		100.00%	50.00%
Sudestecel Participaçoes, Ltda. (BRAZIL)		100.00%	50.00%
Avista Participaçoes Ltda. (BRAZIL)		100.00%	50.00%
Telefónica Brasil Sul Celular Participaçoes, Ltda. (BRAZIL)	1.12%	98.79%	51.78%

	Share of direct controlling	Share of indirect controlling	Share of Telefónica Group
PTelecom Brasil, S.A. (BRAZIL)		100.00%	50.00%
Portelcom Participaçoes, S.A. (BRAZIL)		100.00%	50.00%
Vivo Brasil Comunicaçoes (BRAZIL)		98.00%	49.00%
Vivo Participaçoes, S.A. (BRAZIL)		63.54%	31.78%
Vivo, S.A. (BRAZIL)		100.00%	31.78%
Telefónica Móviles El Salvador Holding, S.A. de C.V. (EL SALVADOR)	100.00%		100.00%
Telefónica Móviles El Salvador, S.A. de C.V. (EL SALVADOR)		99.08%	99.08%
Telefónica Multiservicios, S.A. de C.V. (EL SALVADOR)		77.50%	76.79%
Telefónica El Salvador, S.A. de C.V. (EL SALVADOR)		100.00%	76.79%
Guatemala Cellular Holdings, B.V. (NETHERLANDS)	100.00%		100.00%
TCG Holdings, S.A. (GUATEMALA)	100.00%		100.00%
Telefónica Móviles Guatemala, S.A. (GUATEMALA)	13.60%	86.38%	99.98%
Telefónica Móviles España, S.A.U. (SPAIN)	100.00%		100.00%
Spiral Investments, B.V. (NETHERLANDS)		100.00%	100.00%
3G Mobile AG (SUIZA)		100.00%	100.00%
Solivella Investment, B.V. (NETHERLANDS)		100.00%	100.00%
Terra Mobile Brasil, Ltd. (BRAZIL)		100.00%	100.00%
Omicron Ceti, S.L. (SPAIN)	100.00%		100.00%
Telefónica Móviles Puerto Rico, Inc. (PUERTO RICO)	100.00%		100.00%
MobiPay Internacional, S.A. (SPAIN)	50.00%		50.00%
Telefónica de Centroamérica, S.L. (SPAIN)	100.00%		100.00%
Telefónica Móviles México, S.A. de C.V. (MEXICO)	100.00%		100.00%
Telefónica Finanzas México, S.A. de C.V. (MEXICO)		100.00%	100.00%
Baja Celular Mexicana, S.A. de C.V. (MEXICO)		100.00%	100.00%

	Share of direct controlling	Share of indirect controlling	Share of Telefónica Group
Movitel de Noroeste, S.A. de C.V. (MEXICO)		99.16%	99.16%
Moviservicios, S.A. de C.V. (MEXICO)		99.99%	99.99%
Telefonía Celular del Norte, S.A. de C.V. (MEXICO)		100.00%	100.00%
Celular de Telefonía, S.A. de C.V. (MEXICO)		100.00%	100.00%
Enlaces del Norte, S.A. de C.V. (MEXICO)		49.00%	49.00%
Grupo de Telecomunicaciones Mexicanas, S.A. de C.V. (MEXICO)		100.00%	97.40%
Pegaso Telecomunicaciones, S.A. de C.V. (MEXICO)		100.00%	100.00%
Pegaso Comunicaciones y Sistemas, S.A. de C.V. (MEXICO)		100.00%	100.00%
Pegaso PCS, S.A. de C.V. (MEXICO)		100.00%	100.00%
Pegaso Recursos Humanos, S.A. de C.V. (MEXICO)		100.00%	100.00%
Activos Para Telecomunicación, S.A. de C.V. (MEXICO)		100.00%	100.00%
Adquira Mexico, S.A. de C.V. (MEXICO)		50.00%	50.00%
Telefónica Telecomunicaciones México, S.A. de C.V. (MEXICO)	94.90%		94.90%
Telefónica Móviles Soluciones y Aplicaciones, S.A. (CHILE)	100.00%		100.00%
Ecuador Cellular Holdings, B.V. (NETHERLANDS)	100.00%		100.00%
Otecel, S.A. (ECUADOR)		100.00%	100.00%
Panamá Cellular Holdings, B.V. (NETHERLANDS)	100.00%		100.00%
Telefónica Móviles Panamá, S.A. (PANAMA)	56.32%	43.69%	100.00%
Latin America Cellular Holdings, B.V. (NETHERLANDS)	100.00%		100.00%
Olympic, Ltda. (COLOMBIA)		99.99%	99.99%
Telefónica Móviles Colombia, S.A. (COLOMBIA)	49.42%	50.58%	99.99%

	Share of direct controlling	Share of indirect controlling	Share of Telefónica Group
Telefónica Móviles Perú Holding, S.A.A. (PERU)		98.63%	98.31%
Telefónica Móviles Perú, S.A.C. (PERU)	0.14%	96.65%	96.79%
Telefónica Móviles del Uruguay, S.A. (URUGUAY)	32.00%	68.00%	100.00%
Telefónica Móviles Nicaragua, S.A. (NICARAGUA)		100.00%	100.00%
Telefonía Celular de Nicaragua, S.A. (NICARAGUA)		100.00%	100.00%
Doric Holding y Cía, Ltd. (NICARAGUA)		100.00%	100.00%
Kalamai Hold. Y Cía, Ltd. (NICARAGUA)		100.00%	100.00%
Comtel Comunicaciones Telefónicas, S.A. (VENEZUELA)	65.14%	34.86%	100.00%
Telcel, C.A. (VENEZUELA)	0.08%	99.92%	100.00%
Telefónica Móviles eServices Latin America, Inc. (USA)		100.00%	100.00%
Sistemas Timetrac, C.A. (VENEZUELA)		100.00%	100.00%
Corporación 271191, C.A. (VENEZUELA)		100.00%	100.00%
Telefónica Servicios Transaccionales (VENEZUELA)		100.00%	100.00%
Telefónica Móviles Argentina Holding, S.A. (ARGENTINA)	100.00%		100.00%
Telefónica Móviles Argentina, S.A. (ARGENTINA)	15.40%	84.60%	100.00%
Aliança Atlântica Holding B.V. (NETHERLANDS)	50.00%	43.99%	93.99%
Telefónica Factoring España, S.A. (SPAIN)	50.00%		50.00%
Telefónica Factoring Do Brasil, Ltd. (BRAZIL)	40.00%	10.00%	50.00%
Telefónica Factoring México, S.A. de C.V. SOFOM ENR (MEXICO)	40.50%	9.50%	50.00%

	Share of direct controlling	Share of indirect controlling	Share of Telefónica Group
Telefónica Factoring Perú, S.A.C. (PERU)	40.50%	9.50%	50.00%
Telefónica Factoring Colombia, S.A. (COLOMBIA)	40.50%	9.50%	50.00%
Telco, S.p.A. (ITALY)	42.30%		42.30%



GLOSSARY OF TERMS AND ACRONYMS

08

Only those who do not believe exclusively in their own powers and are capable of relying on others, too, can truly shine. The strength of partnership can get you farther, higher and there faster than if you tried alone.

GLOSSARY OF TERMS AND ACRONYMS

ADSL Asymmetric Digital Subscriber Line
ARPU an indicator – average monthly revenues from services per user, excluding roaming visitors
BlackBerry a mobile office solution from Telefónica O2 designed for mobile corporate customers
BTS Base Transceiver Station for relaying signal to mobile telephones
CDMA Code Division Multiple Access, a modern digital technology for wireless data and broadband internet
CSR Corporate Social Responsibility
CTO Czech Telecommunications Office
DSLAM Digital Subscriber Line Access Multiplexer; a gateway to the network of ADSL access provider
e-účet a service offering online access to the fixed line billing balance
EDGE Enhanced Data Rates for GSM Evolution, a mobile digital technology with a faster and more reliable data transmission
FTP File Transfer Protocol; a platform-independent protocol for the transfer of files between computers
GPRS General Packet Radio Service, a technology for mobile data transmission
GSM Global System for Mobile Communication; the most widely deployed digital wireless communication standard for the digital mobile system which globally uses frequencies of 450, 900, 1,800 and 1,900 MHz, and frequencies of 900 and 1,800 MHz in the Czech Republic
HSCSD High-Speed Circuit-Switched Data, a technology for mobile data transmission in the GSM network
HSDPA High Speed Downlink Packet Access, a superstructure technology for data transmission in the UMTS network, with speeds from 8 to 10 Mb/s
HTTP Hypertext Transfer Protocol; an internet protocol for exchanging hypertext documents and other HTML content
ICT Information and Communication Technologies
IFRS International Financial Reporting Standards
IMAP Internet Message Access Protocol an internet protocol for remote access to email
IP Connect a service for communication using the IP protocol
IPsec (IP security) a security enhancement to the IP protocol
IPTV Internet Protocol Television; a television signal broadcast over broadband networks using the IP protocol

IP VPN Internet Protocol Virtual Private Network, a service of intra-corporate data or voice over IP communication
LAN Local Area Network a local network for communication between computers in the network
LTE Long Term Evolution for UMTS; the latest concept of data transmission technology in the 3rd generation mobile networks
MMS a multimedia format for mobile data transmission
My Europe a mobile tariff of Telefónica O2, with free-of-charge incoming calls for roaming users
My Europe SMS a mobile tariff of Telefónica O2, with free-of-charge incoming calls for roaming users
NMT Nordic Mobile Telephony, a technology standard for mobile telephony networks using the 450 MHz frequency
O_2 Business Unlimited a tariff of Telefónica O2 for business customers, offering unlimited calls to all fixed line and mobile network free of charge, as part of the monthly subscription
O_2 Business Nonstop Max a tariff of Telefónica O2 for business customers, offering free calls within the O_2 mobile network and to all fixed line networks in the Czech Republic
O_2 Duo a converged service of Telefónica O2 combining unlimited calls to fixed line networks in the Czech Republic with O_2 Internet ADSL or O_2TV, all as part of one monthly subscription
O_2 Duo Mobil a converged service of Telefónica O2 combining, as part of one monthly subscription, O_2 Internet ADSL and a mobile voice tariff; the fixed line rental fee is already included
O_2 Fér a service of Telefónica O2 Slovakia, offering a single rate on calls and SMS for the customers of prepaid and contract services, without monthly subscription fee
O_2 Internet ADSL a broadband internet access service of Telefónica O2, formerly branded O_2 Internet Expres
O_2 Internet Komplet a service of Telefónica O2 combining fixed line and mobile services
O_2 Internet Mobil a CDMA mobile service of Telefónica O2
O_2 [:kůl:] a service of Telefónica O2 with fee SMS
O_2 Neomezená linka the first VoIP service of Telefónica O2 for business customers
O_2 Neon a family of flat rate tariffs
O_2 Trio a converged service of Telefónica O2 combining O_2 Internet ADSL, O_2 TV and unlimited calls to fixed networks in the Czech republic, all for one monthly fee
O_2 TV an IPTV service of Telefónica O2; digital television over a fixed line
O_2 TXT a mobile tariff of Telefónica O2 designed for prepaid customers who prefer to communicate via SMS and MMS
OIBDA Operating Income before Depreciation and Amortisation
Platí to Kvído a service of Telefónica O2 which lets customers call for free for a duration of one minute
POP3 Post Office Protocol version 3; an internet protocol used for downloading email messages by the client remotely from the server
RSU Remote Subscriber Unit
SMS Short Message Service; a format of short messages used in mobile telephony
UMTS Universal Mobile Telecommunications System; a standard for the so-called 3rd generation mobile networks
VoIP Voice over Internet Protocol
VPN Virtual Private Network
VPN Expres an IP VPN data service of the former ČESKÝ TELECOM; it is based on the ADSL access technology with aggregation, and the MPLS backbone network
WAN Wide Area Network; a wider computer network giving remote branches full access to data and providing for communication between the headquarters and the branches and within the branch network
WAP Wireless Application Protocol, a protocol for displaying selected web pages on a mobile telephone display
WiFi a local wireless network for accessing the internet

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