

EUSKALTEL, S.A.

Audit report and Financial statements
for the year ended 31 December 2012





INDEPENDENT AUDITOR'S REPORT

To the Shareholders of Euskaltel, S.A.

We have audited the accompanying financial statements of Euskaltel, S.A., which comprise the balance sheet as at 31 December 2012, the income statement and the statements of comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Directors' Responsibility for the Financial Statements

The company's directors are responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards as adopted by the European Union, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

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. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about 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 auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the 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 present fairly, in all material respects, the financial position of Euskaltel, S.A. as at 31 December 2012, and 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.



Emphasis of Matter

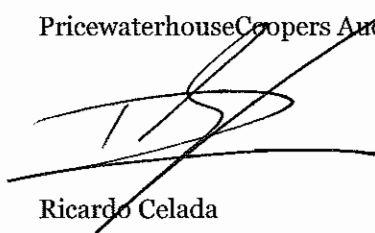
We draw attention to Notes 2.1 and 21 of the accompanying financial statements, which state that the financial statements for 2012 are the first financial statements prepared by the company's directors in accordance with International Financial Reporting Standards as adopted by the European Union, effective as at 31 December 2012, and include, for comparative purposes in each of the statements of the 2012 financial statements, the figures relating to 2011. For the purposes of a potential stock exchange listing, the Company has voluntarily prepared these financial statements under International Financial Reporting Standards as adopted by the European Union, with a transition date of 1 January 2011. Note 21 of the accompanying financial statements includes information on the criteria applied and accounting effects of the aforementioned transition. Our opinion is not qualified in respect of this matter.

Other Matters

The accompanying financial statements have been audited in accordance with International Standards on Auditing. Therefore, this report may not, under any circumstances, be understood to be an audit report issued in accordance with legislation governing the audit practice in Spain. No audit report has been issued on the comparative information as at 1 January 2011, 31 December 2011, and for the year ended 31 December 2011 prepared in accordance with International Financial Reporting Standards as adopted by the European Union.

Euskaltel S.A. has prepared a separate set of statutory annual accounts for the year ended 31 December 2012 in accordance with accounting principles generally accepted in Spain and other provisions of the financial reporting framework applicable in Spain, in respect of which we issued a separate auditor's report to the shareholders of Euskaltel, S.A. on 7 March 2013, in accordance with legislation governing the audit practice in Spain.

PricewaterhouseCoopers Auditores, S.L.



Ricardo Celada

4 June 2015





**Financial Statements
for the year ended
31 December 2012**

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EUSKALTEL, S.A.

Balance Sheets at 31 December 2012 and 2011 and at 1 January 2011

(Expressed in thousands of Euros)

ASSETS	Notes	31.12.2012	31.12.2011	01.01.2011
NON-CURRENT ASSETS		1,017,651	988,705	969,249
Intangible assets	5	15,878	20,465	17,337
Property, plant and equipment	6	827,602	780,585	807,765
Financial assets		1,157	1,356	1,384
Deferred tax assets	13	173,014	186,299	142,763
CURRENT ASSETS		45,664	133,723	122,201
Inventories	8	3,826	5,455	4,219
Trade receivables	7	40,724	70,263	71,588
Other current assets		887	1,551	1,135
Cash and cash equivalents	9	227	56,454	45,259
TOTAL ASSETS		1,063,315	1,122,428	1,091,450
EQUITY AND LIABILITIES	Notes	31.12.2012	31.12.2011	01.01.2011
EQUITY	10	572,896	464,835	567,290
Capital		379,613	325,200	325,200
Share premium		79,390	65,803	65,803
Retained earnings		113,957	73,832	176,287
Other comprehensive income		(64)	-	-
NON-CURRENT LIABILITIES		284,571	241,837	314,291
Long-term borrowings	11	284,571	241,837	314,291
CURRENT LIABILITIES		205,848	415,756	209,869
Short-term borrowings	11	126,130	72,454	48,891
Trade and other payables	4, 12	70,000	115,747	151,577
Other current liabilities	12	9,718	227,555	9,401
TOTAL EQUITY AND LIABILITIES		1,063,315	1,122,428	1,091,450

Notes 1 to 22 are an integral part of these financial statements

Derio, 1 June 2015

EUSKALTEL, S.A.

Income Statements for the years ended 31 December 2012 and 2011

(Expressed in thousands of Euros)

	Notes	2012	2011
Revenues	14	338,542	350,520
Other income		819	772
Work performed by the entity and capitalized	6	3,439	3,856
Supplies	14	(76,916)	(87,064)
Personnel expenses	14	(31,708)	(32,039)
Other operating expenses	14	(92,217)	(290,145)
Depreciation, amortization and impairment	5, 6	(75,889)	(83,762)
RESULTS FROM OPERATING ACTIVITIES		66,070	(137,862)
Finance income	14	136	1,283
Finance costs	14	(12,861)	(12,264)
NET FINANCE COST		(12,725)	(10,981)
PROFIT BEFORE INCOME TAX		53,345	(148,843)
Income tax	13	(13,220)	46,989
PROFIT FOR THE YEAR	10	40,125	(101,854)
Earnings per share:	15		
Basic earnings per share in €		7.36	(18.79)
Diluted earnings per share in €		7.36	(18.79)

Notes 1 to 22 are an integral part of these financial statements

Derio, 1 June 2015

EUSKALTEL, S.A.

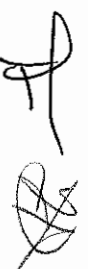
Statement of Comprehensive Income for the years ended 31 December 2012 and 2011

(Expressed in thousands of Euros)

	<u>Notes</u>	<u>2012</u>	<u>2011</u>
Profit for the year	10	40,125	(101,854)
Items that may be reclassified subsequently to profit and loss		<u>(64)</u>	<u>-</u>
Available for sale financial assets		(64)	-
TOTAL COMPREHENSIVE INCOME FOR THE YEAR		<u><u>40,061</u></u>	<u><u>(101,854)</u></u>

Notes 1 to 22 are an integral part of these financial statements

Derio, 1 June 2015



EUSKALTEL, S.A.

Statements of Changes in Equity for the years ended 31 December 2012 and 2011

(Expressed in thousands of Euros)

	Retained earnings						TOTAL
	Share capital	Share premium	Reserves and prior years' profit and loss	Treasury shares	Profit / (loss) for the year	Interim dividend	
Opening balance 2011	325,200	65,803	178,037	(1,672)	24,922	(25,000)	567,290
Total recognised income expense	-	-	-	-	(101,854)	-	(101,854)
Transactions with shareholders							
Distribution of dividends	-	-	2,727	1,672	-	(5,000)	(601)
Other changes in equity	-	-	(78)	-	(24,922)	25,000	-
Closing balance 2011	325,200	65,803	180,686	-	(101,854)	(5,000)	464,835
Total recognised income expense	-	-	-	-	40,125	-	40,061
Transactions with shareholders							
Distribution of dividends	-	-	(5,000)	-	-	5,000	-
Share capital increase	54,413	13,587	-	-	-	-	68,000
Other changes in equity	-	-	(101,854)	-	101,854	-	-
Closing balance 2012	379,613	79,390	73,832	-	40,125	-	572,896

Notes 1 to 22 are an integral part of these financial statements

Derio, 1 June 2015

EUSKALTEL, S.A.**Statements of Cash Flows for the years ended 31 December 2012 and 2011**

(Expressed in thousands of Euros)

	<u>31.12.2012</u>	<u>31.12.2011</u>
Profit for the year before tax	53,345	(148,843)
Adjustments for:	91,307	97,818
Amortization and depreciation	74,088	83,762
Impairment losses on property plant and equipment and intangible assets	2,674	-
Impairment loss on trade receivable and other financial assets	3,057	4,257
Impairment loss/(gain) on inventory	(364)	-
Gains/(losses) on disposal of property plant and equipment	(873)	-
Other income and expenses	437	(1,511)
Finance income	(132)	(902)
Finance costs	12,424	12,264
Exchange gains/(losses)	(4)	(52)
Changes in operating assets and liabilities	(226,170)	180,417
Increase in inventories	1,993	(1,236)
Increase in trade and other receivables	27,114	(3,662)
Decrease in trade payables	(255,277)	185,315
Other cash flows from operating activities	(12,335)	(11,374)
Interest paid	(12,467)	(12,221)
Dividends received	-	163
Interest received	132	739
Income tax expense	-	(55)
Cash flows from operating activities	(93,853)	118,018

Notes 1 to 22 are an integral part of these financial statements

Derio, 1 June 2015



EUSKALTEL, S.A.

Statements of Cash Flows for the years ended 31 December 2012 and 2011

(Expressed in thousands of Euros)

	<u>31.12.2012</u>	<u>31.12.2011</u>
Cash flows from investing activities		
Acquisition of other investments	(460)	(54)
Acquisition of intangible assets	(2,820)	(8,487)
Acquisition of property, plant and equipment	(123,758)	(49,449)
Proceeds from sale of other investments	254	101
Proceeds from sale of property, plant and equipment	-	-
Other...	-	-
Net cash used in investing activities	<u>(126,784)</u>	<u>(57,889)</u>
Cash flows from financing activities		
Proceeds from issue of capital	68,000	-
Proceeds from issue of loans and borrowings	168,865	-
Repayment of loans and borrowings	(72,455)	(48,934)
Other	-	-
Net cash flows from financing activities	<u>164,410</u>	<u>(48,934)</u>
Cash and cash equivalents at beginning of year	56,454	45,259
Cash and cash equivalents at year end	227	56,454
NET CASH INCREASE IN CASH AND CASH EQUIVALENTS	<u>(56,227)</u>	<u>11,195</u>

Notes 1 to 22 are an integral part of these financial statements

Derio, 1 June 2015

EUSKALTEL, S.A.

NOTES TO THE FINANCIAL STATEMENTS FOR 2012

(Expressed in thousands of Euros)

NOTE 1.- General Information

Euskaltel, S.A. (hereinafter the Company) was incorporated with limited liability on 3 July 1995. Its first product was launched on the market on 23 January 1998. Its registered office is located in Derio (Biscay) and its products are mainly sold in the Autonomous Region of the Basque Country.

The Company's statutory and principal activity since its incorporation consists of the rendering, management, installation, operation and marketing of telecommunications networks and services in accordance with prevailing legislation, as well as the marketing and sale of goods required to carry out these services. The Company's main facilities are located at the Bizkaia technology park.

NOTE 2. - Basis of Presentation

2.1 Fair presentation

The accompanying financial statements have been prepared on the basis of the accounting records of Euskaltel, S.A. The financial statements for 2012 have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union (IFRS-EU) and IFRIC interpretations, to present fairly the equity and financial position of Euskaltel, S.A. at 31 December 2012 and results of operations and changes in equity and cash flows of the Company for the year then ended.

These are the first financial statements prepared under IFRS-EU and IFRS 1, "First-time adoption of International Financial Reporting Standards" is therefore applicable. The date of first-time adoption is 31 December 2012, being 1 January 2011 the date of transition to IFRS-EU (Note 21).

Pursuant to prevailing Spanish legislation, the Company authorized for issue the statutory annual accounts for year 2012 prepared in accordance with accounting principles generally accepted in Spain and other provisions of the financial reporting framework applicable in Spain on 6 March 2013, and they were subject to audit in accordance with legislation governing the audit practice in Spain. An unqualified report was issued, on those statutory annual accounts on 7 March 2013.



The accompanying financial statements include comparative information as at 1 January 2011, 31 December 2011, and for the year ended 31 December 2011, prepared in accordance with International Financial Reporting Standards as adopted by the European Union, that are not subject to audit. The annual accounts for the year ended 31 December 2011 prepared in accordance with accounting principles generally accepted in Spain and other provisions of the financial reporting framework applicable in Spain were authorized for issue on 17 May 2012, and they were subject to audit in accordance with legislation governing the audit practice in Spain. An unqualified report was issued, on those statutory annual accounts on 31 May 2012.

The directors have prepared the accompanying financial statements for the year 2012 for the purpose of a potential listing on the stock exchange.

These financial statements were authorized for issue on 1 June 2015.

2.2 Critical issues regarding the valuation and estimation of uncertainties

Preparation of the financial statements in accordance with EU IFRS requires the use of certain critical accounting estimates and management judgements concerning the future. These are evaluated constantly and

based on historical experience and other factors, including expectations of future events and, where applicable, the justified opinion of renowned experts.

In the event that the final outcome of the estimates differed from the amounts initially recognised, or information that would modify these estimates became available, the effects of any changes in the initial estimates are accounted for in the year they are known.

The estimates and judgements that present significant risk of a material adjustment to the carrying amounts of assets and liabilities in the subsequent reporting period are as follows:

a) Corporate income tax and deferred tax assets

A major degree of judgement is required to determine the provision for income tax. There are many transactions and calculations for which the ultimate determination of the tax is uncertain during the ordinary course of business. Tax is calculated based on Management's best estimates in accordance with the current situation as regards tax legislation and taking into account expected developments in this area in the different legislations applied to the Company.

Deferred tax assets are recognised for all unused tax loss carryforwards, deductible temporary differences and available deductions to the extent that it is probable that sufficient taxable income will be available against which these assets can be utilised. In order to determine the amount of the deferred tax assets to be recognised, estimates are made of the amounts and dates on which future taxable profits will be obtained and the reversal period of temporary differences.

b) Useful lives and impairment of assets

The Company determines the estimated useful lives and related amortisation and depreciation charges of assets based on the actual decline in value due to operation and use. The Company increases amortisation and depreciation charges if the useful lives are shorter than previously estimated and writes down or writes off technically obsolete or non-strategic assets that have been abandoned or sold, or when circumstances indicate that their carrying amount might not be recoverable.

c) Provisions

The nature of the business and operations of the Company make necessary the recognition of provisions whose balances are determined according to the best estimate performed by the Society.

Provisions are subject to financial discount whenever feasible to calculate an estimate of the time that it is probable its liquidation

d) Measurements of fair values

A number of the Company's accounting policies and disclosures require the measurement of fair value, both financial and non-financial assets and liabilities. When measuring the fair value of an asset or liability, the Company uses market observable data as far as possible.

Fair values are categorised into different levels in a fair value hierarchy based on the inputs used in the fair value techniques, as follows:

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities that the Company can access at the measurement date;
- Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.
- Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

For further information about the assumptions made in measuring fair values we refer to Note 4.1.

NOTE 3.- Accounting Principles

3.1 Intangible assets

a) Computer software

Computer software mainly reflects the acquisition and development of software applications, which are recognised at cost and amortised on a straight-line basis over their estimated useful life of between three and five years.

Computer software maintenance costs are charged as expenses when incurred.

b) Other intangible assets

Licences are carried at cost less accumulated amortisation and any recognised impairment.

Licences are amortised on a straight-line basis over the term they are granted.

If the favourable situation that enabled expenses required to obtain the licence to be capitalised were to change, the portion pending amortisation is taken to profit or loss in the year the situation changed.

3.2 Property, plant and equipment

Property, plant and equipment are recognised at cost of acquisition or production, less accumulated depreciation and recognised accumulated impairment losses, where applicable.

Costs incurred to extend, modernise or improve property, plant and equipment are only recorded as an increase in the value of the asset when the capacity, productivity or useful life of the asset is increased, and provided that the carrying amounts of the items that are being replaced are known or can be reasonably estimated.

Recurring maintenance costs are charged to the income statement during the year in which they are incurred.

Depreciation of property, plant and equipment, with the exception of land that is not depreciated, is calculated systematically on a straight-line basis over the estimated useful lives of the assets based on the actual decline in value due to operation and use.

The estimated useful lives of property, plant and equipment are as follows:


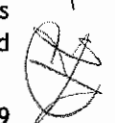
	Years
Buildings	50
Civil engineering	50
Cablings	18-40
Network equipment	10-18
Client equipment	2-15
Other installations, equipment and furniture	6-7
Other assets	5-8

The Company reviews the useful lives of the assets, as well as their classification as under construction, and makes any necessary adjustments at each reporting date. However, taking into consideration the projected utilization of the Company's fixed assets, the residual value is not expected to be significant at the closing date.

Finance costs that are directly attributable to the acquisition, construction or production of a qualifying asset form part of the cost of that asset. Other borrowing costs are recognised as an expense.

3.3 Impairment losses on non-financial assets

The Company evaluates whether there are indications of possible impairment losses on non-financial assets subject to amortisation or depreciation in order to verify whether the carrying amounts of these assets exceed

their recoverable amounts. The recoverable amount is the higher of the fair value less costs to sell and the value in use.

Impairment losses are recognized in the income statement.

The recoverable amount is determined for each individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets. If this is the case, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

At the end of each reporting period, the Company assesses whether there is any indication that an impairment loss recognized in prior periods may no longer exist or may have decreased. Impairment losses are only reversed if there has been a change in the estimates used to calculate the recoverable amount of the asset.

A reversal of an impairment loss is recognized in the income statement. The increased carrying amount of an asset attributable to a reversal of an impairment loss may not exceed the carrying amount that would have been determined, net of depreciation or amortisation, had no impairment loss been recognised.

A reversal of an impairment loss for a cash-generating-unit is allocated to the non-current assets of each unit, pro rata with the carrying amounts of those assets. An assets' carrying amount may not be increased above the lower of its recoverable amount and the carrying amount that would have been disclosed, net of amortisation or depreciation, had no impairment loss been recognised.

After an impairment loss or reversal of an impairment loss is recognised, the depreciation/amortisation charge for the asset is adjusted in future periods based on its new carrying amount.

However, if the specific circumstances of the assets indicate an irreversible loss, this is recognised directly in losses on the disposal of fixed assets in the income statement.

3.4 Inventories

Inventories are initially measured at the lower of cost (whether cost of acquisition or production) and net realisable value, and any related impairment losses or reversals are recognised in the income statement.

Cost is determined using the weighted average cost method. Net realisable value is the estimated selling price in the ordinary course of business, less estimated costs necessary to make the sale.

3.5 Financial assets

In accordance with the classification criteria established by IAS 39, Euskaltel classifies its current and non-current financial assets in the following categories:

a) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market.

These financial assets are initially carried at fair value, including directly attributable transaction costs, and are subsequently measured at amortised cost, recognising accrued interest at the effective interest rate, which is the discount rate that matches the instrument's carrying amount to all estimated cash flows to maturity. Nevertheless, trade receivables falling due in less than one year are carried at their face value at both initial recognition and subsequent measurement, provided the effect of not updating is immaterial.

The impairment loss is calculated as the difference between the carrying amount of the asset and the present value of the estimated future cash flows, discounted at the effective interest rate upon initial recognition. Impairment losses are recognised and reversed in profit or loss. Amounts covered by the provision for impairment are derecognised when their recovery is no longer expected by the Company.

b) Available-for-sale financial assets.

These are financial assets not classified in any of the aforementioned categories, nearly all of which relate to equity investments. These assets are also presented in the balance sheet at fair value which, in the case of



unlisted companies, is obtained using alternative methods, such as comparison with similar transactions or, if sufficient information is available, by discounting expected future cash flows. Changes in this market value are recognised with a charge or credit to "Unrealised Asset and Liability Revaluation Reserve" in the balance sheet until these investments are disposed of, when the accumulated balance of this heading relating to these investments is allocated in full to the income statement.

Equity investments in unlisted companies, the fair value of which cannot be measured reliably using alternative methods such as those indicated in the preceding paragraph, are measured at cost, less recognized impairments.

Management of Euskaltel decides on the most appropriate classification for each asset on acquisition and reviews the classification at each balance sheet date.

c) Derecognition of financial assets

A financial asset is derecognised from the balance sheet if all the risks and rewards of ownership are substantially transferred. In the case of receivables, this is generally understood to be when insolvency and default risks have been transferred.

3.6 Cash and cash equivalents

This heading includes cash, current bank accounts and deposits, and if appropriate, deposits and temporary acquisitions of assets which meet the following requirements:

- They are convertible into cash.
- On acquisition, they mature in less than three months.
- They are not subject to significant value fluctuation risk.
- They form part of the Company's normal cash management policy.

Bank overdrafts, if they arise, are included in borrowings in current liabilities on the balance sheet

3.7 Financial liabilities

In accordance with the classification criteria established by IAS 39, Euskaltel classifies its current and non-current financial liabilities in the following category:

Trades and other payables

Debts and payables are initially recognised at fair value, adjusted for directly attributable transaction costs, and subsequently measured at amortised cost using the effective interest method. The effective interest rate is the discount rate that matches the instrument's carrying amount with the expected future flow of payments to the maturity date of the liability.

Nevertheless, trade payables falling due in less than one year without a contractual interest rate are carried at their face value on both initial recognition and subsequent measurement, provided the effect of not discounting flows is not significant.

3.8 Current and deferred taxes

The income tax expense or tax income is recognised in the income statement each year, calculated based on the pre-tax profits disclosed in the financial statements, adjusted for permanent differences with fiscal criteria. If the profit is associated with an income or expense recognised directly in equity, the tax expense or tax income is also recognised against equity. Deferred tax assets and liabilities arising from temporary differences deriving from the application of fiscal criteria in the recognition of income and expenses, are recognised in the balance sheet until they are reversed.

The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the balance sheet date.

Deferred tax assets and unused tax credits in respect of loss carryforwards are only capitalised when their future realisation is reasonably assured.

Deferred tax is measured at the tax rates expected to be applied to temporary differences when they reversed, using tax rates enacted or substantively enacted at the reporting date.

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes assets and liabilities relate to income taxes levied by the same taxation authority on either the same taxable entity or different taxable entities where there is an intention to settle the balances on a net basis.

3.9 Provisions and contingent liabilities

Provisions are recognised, where applicable, when the Company has a present obligation (legal or constructive) as a result of a past event; 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.

Provisions expiring in one year or less, the financial effect of which is immaterial, are not discounted.

3.10 Revenue recognition

Revenue

Revenue is recognised at the fair value of the consideration receivable and reflects the amounts to be collected for goods handed over and services rendered in the ordinary course of the Company's activities, less returns, discounts and value added tax.

The Company main source of revenue comes from the individual or combined provision of fixed telephony services, pay television, broad-band internet services and mobile telephony services to retail customers and large accounts and corporations.

Commercial packages that combine different elements are analysed to determine whether it is necessary to separate the different elements identified, applying the appropriate revenue recognition policy in each specific case.

Both fixed and mobile traffic is recognised as revenue as service is provided.

If traffic or other services are sold at a fixed rate for a determined time period (flat rate), revenue is recognised on a straight-line basis over the time period covered by the rate paid by the customer.

The periodic charges for use of the network (telephony, internet and television) are credited to the income statement on a straight-line basis over the period to which they relate.

In the case of prepaid mobile telephony, the amount of unused credit is recognised as a deferred income until it is consumed or, where applicable, ultimately cancelled.

Rentals and other services are credited to the income statement as the service is provided.

Revenue from sale of goods is recognised when the significant risks and rewards of ownership of the goods have passed to the buyer, usually on delivery date.

Costs of acquiring customer, such as commissions owed to sales agents and third-party dealers, or such as handsets provided freely or heavily discounted to attract and retain customers, are recognised as an expense when the performance obligation is satisfied (the commission is rendered or the handset is delivered to the customer).

Interest income

Interest income is accrued on a time proportion basis, by reference to the principal outstanding and the effective interest rate applicable, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset's carrying amount.

3.11 Leases

a) Finance leases

Leases of property, plant and equipment where the Company has substantially assumed all the risks and rewards of ownership of leased assets are classified as finance leases. Finance leases are capitalised at the lease's inception at the lower of the fair value of the leased property and the present value of the minimum lease payments. Present value is calculated using the interest rate implicit in the lease agreement and, if this rate cannot be determined, the interest rate applied by the Company in similar transactions.

Each lease payment is distributed between the liability and finance charges. The total finance charge is apportioned over the lease term and taken to the income statement in the period of accrual, using the effective interest method. Contingent rents are expensed in the year they are incurred. Lease obligations, net of finance charges, are recognised in finance lease payables. Property, plant and equipment acquired under finance leases are depreciated over the shorter of the asset's useful life and the lease term.

b) Operating leases

Leases in which the lessor retains substantially all the risks and rewards incidental to ownership are classified as operating leases. Operating lease payments (net of any incentive received from the lessor) are recognised in profit or loss.

3.12 Foreign currency transactions

a) Functional and presentation currency

Except where otherwise stated, the figures disclosed in the financial statements are expressed in thousands of Euros, the Company's functional currency.

b) Foreign currency transactions and balances

Transactions in foreign currency are translated at the foreign exchange rate prevailing at the date of the transaction. Foreign currency gains and losses resulting from the settlement of transactions and translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currency are recognised in the income statement.

3.13 Share capital

Ordinary shares are classified as equity.

Incremental costs directly attributable to the issue of new shares or options are presented in equity as a deduction, net of taxes, from revenue obtained.

Where the Company purchases the own Company's equity share capital (treasury shares), the consideration paid, including any directly attributable incremental costs (net of income taxes), is deducted from equity attributable to equity holders of the Company until the shares are cancelled, reissued or disposed of. Where such shares are subsequently disposed of or reissued, any consideration received, net of any directly attributable incremental transaction costs and the related income tax effects, is included in equity attributable to equity holders of the Company.

3.14 Cash Flow Statement

The following terms are used in the cash flow statement with the meanings specified:

- Cash flows. Inflows and outflows of cash and cash equivalents, which are short-term, highly liquid investments that are subject to an insignificant risk of changes in value.
- Operating activities. The principal revenue-producing activities of Euskaltel and other activities that are not investing or financing activities.
- Investing activities. Activities of acquisition and disposal of long-term assets and other investments not included in cash and cash equivalents.
- Financing activities. Activities that result in changes in the size and composition of the equity and borrowings that are not operating activities.

3.15 Segment reporting

The operating segments are presented consistently with the management approach, in accordance with the information used internally at the highest decision-making level. The maximum authority for decision making is responsible for assigning resources to operating segments and evaluating the segments' performance. Segment reporting is in Note 16.

NOTE 4.- Financial instruments - Fair values and Risk Management

4.1 Accounting classification and Fair value

The main financial assets held by the Company comprise trade receivables and cash and cash equivalents. These assets are classified under assets at amortised cost and the receivables fall due in the short term, so there are no significant differences between their carrying amount and their fair value. Furthermore, the table below shows the carrying amounts and fair values of financial liabilities, including their levels in the fair value hierarchy.

	Level	31.12.12	31.12.11	01.01.11
Financial liabilities measured at amortized costs				
Loans and borrowing	2	410,631	314,291	363,182
Other financial liabilities		70	-	-
Trade and other payables & Other current liabilities		79,718	343,302	160,978
		<u>490,419</u>	<u>657,593</u>	<u>524,160</u>

The fair value of loans and borrowings is estimated by discounting contractual future cash flows at the current market interest rate available to the Company for similar financial instruments. The carrying amounts of trade and other payables are assumed to be similar to their fair values.

4.2 Financial risk management

The Company activities are exposed to various financial risks: credit risk, liquidity risk and market risk (including currency risk and fair value interest rate risk). The Company's global risk management programme focuses on uncertainty in the financial markets and aims to minimise potential adverse effects on the Company's profits.

The Company uses financial risk evaluation and mitigation methods suited to its activity and scope of operations, which are sufficient for the adequate management of risks.

A summary of the main financial risks affecting the Company, as well as the measures in place to mitigate these risks, is as follows:

- Credit risk
- Liquidity risk
- Market risk, currency risk and interest rate risk

This note presents information about the Company's exposure to each of the above risks, objectives, policies and procedures of the Company for measuring and managing risk and capital management by the Company.

Risk management framework

It is the responsibility of the Board of Directors to establish and oversee the risk management structure of the Company.

Compliance with the budget is reviewed periodically, analyzing the degree of implementation, evaluating deviations and proposing corrective measures. In this process, the managers of the various business units are involved.

The risk management policy of the Company is established in order to identify and analyze the risks assumed by the Company, set limits and appropriate risk controls, and to monitor risks and adherence to limits. Regularly, policies and risk management systems are reviewed in order to reflect changes in market conditions and the activities of the Company. The Company through its rules and administrative procedures, aims to develop an environment of disciplined and constructive control in which all employees understand their roles and obligations.

To mitigate these risks, the Company has at all times an active attitude to exogenous factors. The various departments of the Company may be affected by these factors produce specific action programs, such as those to comply with changes in national or international regulations.

The evolution of markets and changes in consumer habits are factors to which special attention is given, with departments in charge of relevant studies and analysis, relying on external collaborations in the field of market research.

The program's overall risk management of the Company is focused on minimizing the uncertainty in financial markets and the potential adverse effects on the financial performance of the Company.

a) Credit risk

Credit risk is the risk of financial loss that the Company faces if a customer or counterparty to a financial instrument fails to meet its contractual obligations and arises mainly in accounts receivable of the Company.

The Company considers customer credit risk to be mitigated by the application of different policies and specific practices to this effect, and the high level of dispersion of receivables. Among the different policies and specific practices implemented is the customer acceptance scoring policy, the long-term monitoring of customer credit, which reduces the possibility of default of significant receivables, and debt collection management

Details of the Company's ageing analysis of trade receivable are past-due but not impaired at 31 December 2012 and 2011 is as follows:

	<u>31.12.12</u>	<u>31.12.11</u>	<u>01.01.11</u>
Neither past due nor impaired	25,488	26,638	28,849
From 0-30 days	12,653	16,185	17,358
From 31-90 days	1,881	3,574	7,279
From 91-180 days	702	3,062	4,413
From 181-365 days	-	1,577	1,284
More than 365 days	-	19,227	12,405
Total	<u>40,724</u>	<u>70,263</u>	<u>71,588</u>

At 31 December 2011 and at 1 January 2011 there were relevant trade receivables matured from more than one year. They were, basically, related to pending amounts with France Telecom, which were cancelled with the final agreement with this entity in 2012 (Note 17).

The Company makes provision for impairment of trade and other receivables adding, to the total amount of balances that have exceeded a minimum period determined in accordance with pertinent legislation applicable to the sector, a percentage of past-due balances that do not exceed the aforementioned minimum period, estimated using historical data on the recovery of Company balances, as it considers that the application of this criterion represents a reasonable estimate of the impairment of the aforementioned financial assets.

Movement in the provision for impairment of trade and other receivables is as follows:

	<u>31.12.12</u>	<u>31.12.11</u>	<u>01.01.11</u>
Opening balance	28,440	30,588	28,873
Allowance account for impairment of trade receivables	3,057	4,586	7,620
Bad debts written off	<u>(9,818)</u>	<u>(6,734)</u>	<u>(5,905)</u>
Closing balance (Note 7)	<u>21,679</u>	<u>28,440</u>	<u>30,588</u>

Impairment of trade receivables is recognised and reversed under other operating expenses in the income statement, and totals Euros 3 million. Additionally, the Company has reversed provision in an amount of Euros 6.8 million as a consequence of the agreement described in Note 17. Management believes that the unimpaired amounts that are past due are still collectable based on historical payment behaviour and extensive analysis of customer credit risk. Management believes that the unimpaired amounts that are past due are still collectable based on historical payment behaviour and extensive analysis of customer credit risk. The Company does not have significant concentrations of credit risk.

The Company has cash and cash equivalents at December 31, 2012 by Euros 227 thousand (Euros 56,454 thousand Euros at December 31, 2011). Cash and cash equivalents are maintained with banks and financial institutions of high credit rating.

b) Liquidity risk

Liquidity risk is the risk that the Company would have difficulty meeting its obligations associated with its financial liabilities that are settled by delivering cash or other financial assets. The Company's approach to managing liquidity is to ensure, to the greatest extent possible, that it would always have sufficient liquidity to meet its obligations when due, under both normal and stressed conditions, without incurring unacceptable losses or risking the reputation of the Company.

The Company adjusts the maturities of its debts to its capacity to generate cash for settlement.

To do this, the Company implements three-year financing plans, which are reviewed annually, and analyses of financial position every two weeks, which include long-term projections, together with a daily monitoring of bank balances and transactions.

Therefore, although the Company's working capital, defined as the difference between current assets and current liabilities (maturing in less than 12 months in both cases), is slightly negative, it is mainly because of normal business activity, in which the average collection period is lower than the average payment period, which is normal for the Company's activity.

The following are the contractual maturities of financial liabilities, including estimated interest:

	31.12.12						Total
	Book value	2014	2015	2016	2017	Thereafter	
Long-term borrowings							
Third parties	108,706	63,916	32,577	16,057	-	-	112,550
Related parties	175,795	31,894	27,258	17,737	11,911	132,487	221,287
Other	70	-	4	9	9	48	70
Total	284,571	95,810	59,839	33,803	11,920	132,535	333,907

	31.12.11						Total
	Book value	2013	2014	2015	2016	Thereafter	
Long-term borrowings							
Third parties	179,094	68,721	64,522	48,652	16,119	-	198,014
Related parties	62,743	21,356	24,793	28,208	9,346	-	83,703
Other	-	-	-	-	-	-	-
Total	241,837	90,077	89,315	76,860	25,465	-	281,717

	01.01.11						Total
	Book value	2012	2013	2014	2015	Thereafter	
Long-term borrowings							
Third parties	242,946	69,542	67,754	63,768	32,505	16,027	249,596
Related parties	71,345	12,646	20,880	24,385	18,845	9,292	86,048
Other	-	-	-	-	-	-	-
Total	314,291	82,188	88,634	88,153	51,350	25,319	335,644

The Company has a bank loan that contains a loan covenant the breaching of which may require repayment earlier than indicated in the above tables. That covenant was related to net bank debt in comparison to share capital and share premium. As at 31 December 2012, 31 December 2011 and 1 January 2011 the Company was compliant with the required covenants. Furthermore, the interest payments on variable interest rate loans in the tables above have been calculated on the basis of conditions existing at the end of each reporting period.

The Company's credit facilities have a total limit of Euros 117 million at 31 December 2012 (Euros 89.5 million in 2011), of which Euros 78 million remains undrawn at that date (Euros 89.5 million in 2011).

On December 19, 2012 the Company signed a credit facility amounting to Euros 80 million, maturing on December 30, 2018, to secure working capital requirements of the Company. The amount is included in the limit of Euros 117 million above.

c) Market risk, currency risk and interest rate risk

Market risk is the risk that changes in market prices affect the Company's income or the value of financial instruments held. The objective of market risk management is to manage and control risk exposures within acceptable parameters, while optimizing the return.

The Company's ambit of operations barely exposes it to currency or price risks, which may arise from occasional purchases in foreign currency of insignificant amounts.

The interest rate risk arises mainly from the Company loans granted by banks and related parties at variable rates which expose the Company variability on future cash flows.

The interest rate profile of the interest-bearing for long term debt, measured at their outstanding principals due, is as follows:

	<u>31.12.12</u>	<u>31.12.11</u>	<u>01.01.11</u>
Fixed interest rate instruments	-	-	-
Variable interest rate instruments	373,500	316,833	367,000
	<u>373,500</u>	<u>316,833</u>	<u>367,000</u>

At December 31, 2012 an upturn in interest rates of 100 basis points, with other variables held constant, would have decreased the result after tax Euros 3,735 thousands (Euros 3,168 thousand in the year ended December 31, 2011).

NOTE 5.- Intangible Assets

Details of intangible assets and movement are as follows:

	Computer software	Other	Total
GROSS AMOUNT			
Balance at 01.01.11	37,893	977	38,870
Additions	5,812	2,675	8,487
Balance at 31.12.11	<u>43,705</u>	<u>3,652</u>	<u>47,357</u>
Additions	2,802	18	2,820
Balance at 31.12.12	<u>46,507</u>	<u>3,670</u>	<u>50,177</u>
ACCUMULATED AMORTISATION			
Balance at 01.01.11	(21,012)	(521)	(21,533)
Additions	(5,283)	(76)	(5,359)
Balance at 31.12.11	<u>(26,295)</u>	<u>(597)</u>	<u>(26,892)</u>
Additions	(4,675)	(58)	(4,733)
Balance at 31.12.12	<u>(30,970)</u>	<u>(655)</u>	<u>(31,625)</u>
PROVISION FOR IMPAIRMENT			
Balance at 01.01.11	-	-	-
Additions	-	-	-
Balance at 31.12.11	<u>-</u>	<u>-</u>	<u>-</u>
Additions	-	(2,674)	(2,674)
Balance at 31.12.12	<u>-</u>	<u>(2,674)</u>	<u>(2,674)</u>
NET VALUE			
Balance at 01.01.11	16,881	456	17,337
Balance at 31.12.11	<u>17,410</u>	<u>3,055</u>	<u>20,465</u>
Balance at 31.12.12	<u>15,537</u>	<u>341</u>	<u>15,878</u>

Licences, included in other intangible assets, relate to the acquisition in 2011 of two blocks of frequencies in the 2.6 GHz bandwidth (10 + 10 MHz and 5 MHz TDD) in order to be able to provide, in a future, broadband mobility last generation services (LTE) with its own network, with which complement the offer on the own fiber optic network and mobility services rendered as a mobile virtual network operator (OMV).

In 2012, the Company recognised impairment losses on licences of Euros 2.7 million, since business trends in particular and the macroeconomic climate in general meant their capacity to generate income was not reasonably ensured.

The cost of fully amortised intangible assets in use at 31 December 2012 totals Euros 19.4 million (Euros 16.3 million in 2011).

The Company has contracted sufficient insurance policies to cover the risk of damage to its intangible assets.

NOTE 6.- Property, Plant and Equipment

Details of property, plant and equipment and movement are as follows:

	Land and buildings	Civil engineering	Cabling	Network equipment	Client equipment	Other installations, equipment and furniture	Under construction and advances	Other property, plant and equipment	Total
GROSS AMOUNT									
Balance at 01.01.11	65,269	238,805	241,865	308,726	199,337	136,319	31,787	21,569	1,243,677
Additions	-	-	-	-	-	111	51,112	-	51,223
Transfers	81	4,788	9,318	14,070	22,341	3,773	(56,257)	1,886	-
Balance at 31.12.11	65,350	243,593	251,183	322,796	221,678	140,203	26,642	23,455	1,294,900
Additions	68,000	-	-	-	-	7	47,815	550	116,372
Transfers	190	9,911	12,756	15,008	14,833	3,651	(57,386)	1,037	-
Balance at 31.12.12	133,540	253,504	263,939	337,804	236,511	143,861	17,071	25,042	1,411,272
ACCUMULATED AMORTISATION									
Balance at 01.01.11	(8,678)	(35,083)	(84,560)	(138,719)	(114,435)	(38,715)	-	(15,722)	(435,912)
Additions	(1,253)	(6,484)	(15,541)	(29,348)	(15,715)	(8,642)	-	(1,420)	(78,403)
Balance at 31.12.11	(9,931)	(41,567)	(100,101)	(168,067)	(130,150)	(47,357)	-	(17,142)	(514,315)
Additions	(1,254)	(5,835)	(12,741)	(28,188)	(11,199)	(8,985)	-	(1,153)	(69,355)
Balance at 31.12.12	(11,185)	(47,402)	(112,842)	(196,255)	(141,349)	(56,342)	-	(18,295)	(583,670)
NET VALUE									
Balance at 01.01.11	56,591	203,722	157,305	170,007	84,902	97,604	31,787	5,847	807,765
Balance at 31.12.11	55,419	202,026	151,082	154,729	91,528	92,846	26,642	6,313	780,585
Balance at 31.12.12	122,355	206,102	151,097	141,549	95,162	87,519	17,071	6,747	827,602

The Basque Government-Eusko Jurlaritz, at a session held on 17 July 2012 and in compliance with the revised Equity Law of Euskadi, approved by Decree Law 2/2007 of 6 November 2007, agreed to seek the Basque Parliament's authorisation to transfer the excess telecommunications network and infrastructure owned by the Basque regional government to the Company for a sale price of Euros 68,000 thousand, based on the appraisal of an independent expert. This network, which mainly comprises underground channels, had been leased to the Company since its incorporation, and represented a rental cost of approximately Euros 3.3 million in 2012 (3.4 million in 2011).

On 13 August 2012, the Basque Parliament's Commission on Economy, Finance and Budget authorised this transfer, after which, the corresponding order for divestiture was issued by the Minister of Economy and Finance on 21 September 2012. The Company finally acquired the aforementioned telecommunications network through a deed of sale and purchase signed by both parties on 20 December 2012. This purchase was paid in full upon signing of the deed of sale and purchase, for which the Company increased its capital by Euros 54,413 thousand, with a share premium of Euros 13,587 thousand.

In 2012 the Company has capitalised Euros 259 thousand in finance costs (Euros 369 thousand in 2011) deriving from external financing obtained to roll-out the network, calculated using a capitalisation rate of 2.41% in 2012 (2011: 3.19%, equivalent to the average effective cost of the external financing during the year).

In 2012 costs of Euros 3.4 million relating to network roll-out activities have been capitalised (Euros 3.9 million in 2011).

The cost of fully depreciated property, plant and equipment in use at 31 December 2012 is Euros 202.1 million (Euros 140.2 million in 2011).

At 31 December 2012 and 2011 there are no items of property, plant and equipment pledged to secure financial liabilities and sufficient insurance policies have been taken out to cover the risk of damage to property, plant and equipment.

The heading of Under construction and advances balance included Spare parts, amounting to 4,316 thousand Euros (2011: 3,589 thousand Euros) is included, net of provision for impairment estimated based on the rotation of the elements included in this balance amounting to 8,515 thousand Euros (2011: 9,817 thousand Euros) (Note 16). In 2012 were reversed EUR 0.8 million of this provision, based on the analysis of rotation performed. In 2011 no amount was doted or reversed in this provision concepts.

NOTE 7.- Financial assets

Financial assets by category are as follows:

	<u>31.12.12</u>	<u>31.12.11</u>	<u>01.01.11</u>
Long term financial assets	1,157	1,356	1,384
Equity instruments in related entities	24	21	21
Loans and receivables	278	372	400
Available-for-sale financial assets	855	963	963
Short term financial assets			
Loans and receivables	40,776	70,347	71,657
Trade receivables (Note 7.1)	40,724	70,263	71,588
Credits and other financial assets	52	84	69
Prepayments for current assets	835	1,467	1,066

Financial assets in the long term have no defined maturity date. Long term loans and receivables are deposits due to, mainly, lease contracts, which do not have defined maturity date as the corresponding contracts have automatic renovation clauses.

At 31 December 2012 the Company held an investment in several companies, comprising eight limited liability subsidiaries (seven of which were dormant) with no material effect. At the current date, the liquidation of six of these companies had been filed at the Mercantile Registry, while the other two companies were in the process of being liquidated.

In addition, the Company held investments in associates, none of which are listed on the stock exchange, represent a 25% direct interest in Andornet, domiciled in Andorra and engaged in the transfer of data to third parties via electronic networks, and a 20% direct interest in Hamaika Telebista, domiciled in Bilbao and engaged in promoting the creation of local television stations that broadcast in the Basque language (Euskera).

7.1 Trade receivables

Details of the amounts included under this caption are shown below:

	<u>31.12.12</u>	<u>31.12.11</u>	<u>01.01.11</u>
Gross amount	62,403	98,703	102,176
Impairment	(21,679)	(28,440)	(30,588)
Total	<u>40,724</u>	<u>70,263</u>	<u>71,588</u>

The accounts receivable are stated at their nominal value, which does not differ significantly from their fair value, based on the cash flows there from discounted at market rates.

NOTE 8.- Inventories

	<u>31.12.12</u>	<u>31.12.11</u>	<u>01.01.11</u>
Customer terminals and equipment	3,264	4,585	3,861
Mobile phones	676	2,886	3,286
Digital television decoders	2,588	1,699	575
Consumables	2,593	3,219	2,711
Other inventories	489	535	531
Total gross amount	<u>6,346</u>	<u>8,339</u>	<u>7,103</u>
Impairment losses on inventories	(2,520)	(2,884)	(2,884)
Total	<u>3,826</u>	<u>5,455</u>	<u>4,219</u>

The Company has contracted sufficient insurance coverage for the risk of damage to inventories.

NOTE 9. Cash and Cash Equivalents

	<u>31.12.12</u>	<u>31.12.11</u>	<u>01.01.11</u>
Cash	227	1,071	32
Cash equivalents - third parties	-	6,646	5,678
Cash equivalents - related parties	-	48,737	39,549
Total	<u>227</u>	<u>56,454</u>	<u>45,259</u>

In 2011 the heading Other cash equivalents correspond to the balances subscription assignment of public debt, bank loans and bank borrowings of the Group, with repurchase agreement on original maturity less than 3 months and with an average yield of market.

The heading of Other cash equivalents amounting to 6,646 thousand Euros at December 31, 2011 (5,678 thousand Euros at January 1, 2011) included underwriting assignment of public debt with Caja Vital, since January 1, 2012 part of Kutxabank Group.




NOTE 10.- Equity

10.1 Capital

At 31 December 2012 the subscribed capital of the Company is represented by 6,326,890 registered shares of Euros 60 par value each, with the same rights and obligations, subscribed and fully paid (5,420,000 shares in 2011 and 2010).

Companies which hold an interest in the share capital of the Company and their percentage ownership, are as follows:

	31.12.12	31.12.11	01.01.11
	Percentage ownership	Percentage ownership	Percentage ownership
Kutxabank S.A.	30.19%	-	-
Bilbao Bizkaia Kutxa Aurrezki Kutxa eta Bahitetxea	-	35.24%	35.05%
CK Corporación Kutxa-Kutxa Korporazioa S.L.	12.64%	24.44%	24.31%
Araba Gertu S.A.	7.07%	8.25%	8.20%
Grupo Kutxabank	49.90%	67.93%	67.56%
International Cable B.V.	48.10%	-	-
Iberdrola S.A.	2.00%	11.85%	11.79%
Endesa S.A.	-	10.64%	10.58%
Euskal Irrati Telebista Herri Erakundea	-	5.32%	5.29%
Ente Vasco de la Energía	-	2.13%	2.12%
Mondragón Inversiones S.P.E. S.Coop.	-	2.13%	2.12%
Treasury Shares	-	-	0.54%
Total	100.00%	100.00%	100.00%

The Universal Extraordinary General Shareholders Meeting dated October 26, 2005 agreed unanimously, the derivative acquisition of own shares as treasury shares.

Since 1 January 2012, as a result of the spin-off of the financial businesses of Bilbao Bizkaia Kutxa, Aurrezki Kutxa eta Bahitetxea (BBK), Caja de Ahorros y Monte de Piedad de Gipuzkoa y San Sebastián - Gipuzkoa eta Donostiako Aurrezki Kutxa (Kutxa) and Caja de Ahorros de Vitoria y Álava - Araba eta Gasteizko Aurrezki Kutxa (Vital) to Kutxabank, S.A., the latter (Kutxabank) has assumed all obligations and all the rights and shares comprising the equity of BBK, Kutxa and Vital.

Consequently, since January 1, 2012, the 1,919,038 shares of the Company of which it owner BBK as of December 31, 2011 have become owned by Kutxabank and, likewise, companies CK-Kutxa Kutxa Corporation Korporazioa, S.L. and Araba Gertu, S.A. have, fully, passed belong to Kutxabank, resulting therefore that, as of January 1, 2012, shares of the Company belonging to the group are Kutxabank 3,681,931, equivalent to 67.93% of total capital.

At a meeting held on 6 March 2012, the cabinet of the Basque Government-Eusko Jaurlaritza agreed to authorise the addition of the investment held by the public entities Ente Vasco de la Energía and Euskal Irrati Telebista Herri Erakundea in the share capital of Euskaltel, S.A. to the business asset portfolio of the General Administration of the Autonomous Community of Euskadi. Consequently, as of that date, the shares held by both companies became fully owned by the Basque Government-Eusko Jaurlaritza, with the General Administration of the Autonomous Community of Euskadi assuming the legal relations, rights and obligations of the aforementioned public entities with the Company.

In December 2012 the Company increased its share capital by Euros 54,413 thousand by issuing 906,890 shares of Euros 60 par value each, with a share premium of Euros 13,587 thousand. After the shareholders renounced

their preferential right to subscription, International Cable, B.V. subscribed and fully paid the aforementioned share capital increase with share premium.

In addition, International Cable, B.V. closed individual agreements for the sale-purchase of the Company's shares with different shareholders, as a result of which, International Cable, B.V. held a 48.10% interest in the Company at 31 December 2012.

The Company manages its capital with the aim of safeguarding its capacity to continue operating as a going concern, so as to continue providing shareholder remuneration and benefiting other stakeholders, while maintaining an optimum capital structure to reduce the cost of capital.

To maintain and adjust the capital structure, the Company can adjust the amount of dividends payable to shareholders, reimburse capital, issue shares or dispose of assets to reduce debt.

Like other groups in the sector, Euskaltel controls its capital structure on a leverage ratio basis. This ratio is calculated as net debt divided by total capital. Net debt is the sum of financial debt plus trade and other payables, less cash and cash equivalents. Total capital is the sum of equity plus net debt.

During 2012 the strategy remained the same as in 2011, the ratios are calculated as follows:

	2012	2011	2010
Total debt	490,419	657,593	524,160
Less: Cash and cash equivalents	(227)	(56,454)	(45,259)
Net debt	490,192	601,139	478,901
Equity	572,896	464,835	567,290
Total capital	1,063,088	1,065,974	1,046,191
Debt ratio	0.5	0.6	0.5

The financial situation in December 2011 was affected by the resolution of the proceedings against Euskaltel, S.A. by the France Telecom Group. During 2012 there has been a positive evolution both in the results of the Company (Profit for the year: Euros 40.1 million) and the cash generation. Additionally, in December 2012 the Company increased its share capital by Euros 54.4 million with a share premium of Euros 13.6 million.

10.2 Share premium

In accordance with prevailing legislation, the share premium is a freely-distributable reserve, provided that equity exceeds share capital.




10.3 Retained earnings

Details of this caption are as follows:

	<u>31.12.12</u>	<u>31.12.11</u>	<u>01.01.11</u>
Legal reserve	22,714	22,714	19,440
Voluntary reserves	152,972	157,972	158,597
Treasury shares	-	-	(1,672)
Prior years' losses	(101,854)	-	-
Profit for the year	40,125	(101,854)	24,922
Interim dividend	-	(5,000)	(25,000)
Total	<u>113,957</u>	<u>73,832</u>	<u>176,287</u>

The legal reserve has been appropriated in compliance with article 274 of the Spanish Companies Act, which requires that companies transfer 10% of profits for the year to a legal reserve until this reserve reaches an amount equal to 20% of share capital. Until the legal reserve exceeds the above limit, it may only be applied to offset losses if no other reserves are available.

10.4 Dividends

On December 14, 2011, the Board of Directors of the Company approved the distribution of an interim dividend of profits for 2011 in the amount of 5 million Euros equivalent to 0.92 Euros per share. On the same date, all of the Company's shareholders agreed in Universal General Meeting to the materialization of such dividend in the distribution to shareholders of 28.898 own shares valued at Euros 4.4 million, together with a payment in cash of Euros 0.6 million. The acquisition cost of these treasury shares amounted to Euros 1,672 thousand and its market value was established based on the valuation of an independent expert.

NOTE 11.- Financial liabilities

The Company includes all its financial liabilities in the category of Trade and Accounts payable and financial liabilities at amortised cost. This category includes Interest bearing liabilities (Note 11.1), Trade and other payables (Note 12) and Other current liabilities (Note 12).

The Company's financial liabilities have their maturity date in the short-term, except for the interest bearing liabilities. The dates of maturity of those liabilities are detailed in Note 11.1

11.1 Interest bearing liabilities

	31.12.12	31.12.11	01.01.11
Loans and borrowings	366,336	314,291	363,579
Nominal amounts	373,500	316,834	367,000
Fees and commissions	(7,164)	(2,543)	(3,421)
Credit facilities and interest accrued	38,865	-	(397)
Arrangement expenses pending to be paid	5,500	-	-
Total	410,701	314,291	363,182

The carrying amount of the loans and borrowings and the other financial liabilities does not differ from their fair value, since they were arranged at market rates.

Details of bank loans and borrowings at 31 December 2012 are as follows:

	EIB loan 1999	Loan 2007	Loan 2009	Bilateral loan 2009	Bilateral loan 2010	Loan 2012	Thousands of Euro
Entity	European Investment Bank	7 banks, including 3 banks of Kutxabank Group	11 banks, including 3 banks of Kutxabank Group	Banco Santander	Banesto	Kutxabank	-
Contract date	17/12/1999	25/07/2007	30/06/2009	30/09/2009	18/12/2009	19/12/2012	-
Amount (in thousands of Euros)	120	150	130	4	5	130	-
Term (years)	15	8.5	5	5	5	8	-
Grace period (years)	5	6	2	2	2	4	-
Repayment	10 equal annual instalments as of 15/12/2005	6 equal half- yearly instalments as of 25/07/2013	6 equal half- yearly instalments as of 30/12/2011	6 equal half- yearly instalments as of 30/12/2011	6 equal half- yearly instalments as of 30/12/2011	8 equal half- yearly instalments as of 30/12/2016	-
Guarantees	Guarantee syndicated by 11 banks, including 3 banks of Kutxabank Group	-	-	-	-	-	-
Maturity date	15/12/2014	25/01/2016	30/06/2014	30/06/2014	30/06/2014	30/06/2020	-
Interest rate	Variables at each repayment	Variable pegged to Euribor	Variable pegged to Euribor	Variable pegged to Euribor	Variable pegged to Euribor	Variable pegged to Euribor	-
Average interest 2011	1.45%	3.72%	2.95%	2.94%	2.94%	n/a	-
Average interest 2012	0.85%	2.93%	2.18%	2.14%	2.18%	n/a	-
Outstanding principal due	24,000	150,000	65,000	2,000	2,500	130,000	373,500
Short term	12,000	25,000	43,333	1,333	1,666	-	83,332
Long term	12,000	125,000	21,667	667	834	130,000	290,168

Details of bank loans at 31 December 2011 are as follows:

	EIB loan 1999	EIB loan 2001	Loan 2007	Loan 2009	Bilateral loan 2009	Bilateral loan 2010	Thousands of Euros
Entity	European Investment Bank	European Investment Bank	7 banks, including 2 banks of Katxabank Group	11 banks, including 2 banks of Katxabank Group	Banco Santander	Banesto	-
Contract date	17/12/1999	22/06/2001	25/07/2007	30/06/2009	30/09/2009	18/12/2009	-
Amount (in thousands of Euros)	120	120	150	130	4	5	-
Term (years)	15	12	8.5	5	5	5	-
Grace period (years)	5	4	6	2	2	2	-
Repayment	10 equal annual instalments as of 15/12/2005	8 equal annual Instalments as of 15/12/2005	6 equal half- yearly instalments as of 25/07/2013	6 equal half- yearly instalments as of 30/12/2011	6 equal half- yearly instalments as of 30/12/2011	6 equal half- yearly instalments as of 30/12/2011	-
Guarantees	Guarantee syndicated by 11 banks, including 2 banks of Katxabank Group	Guarantee syndicated by 14 banks, including 2 banks of Katxabank Group	-	-	-	-	-
Maturity date	15/12/2014	15/12/2012	25/01/2016	30/06/2014	30/06/2014	30/06/2014	-
Interest rate	Variables at each repayment	Variables at each repayment	Variable pegged to Euribor	Variable pegged to Euribor	Variable pegged to Euribor	Variable pegged to Euribor	-
Average interest 2011	0.89%	0.89%	1.12%	2.33%	2.31%	2.40%	-
Average interest 2012	1.45%	1.42%	3.72%	2.95%	2.94%	2.94%	-
Outstanding principal due	36,000	15,000	150,000	108,333	3,333	4,168	316,834
Short term	12,000	15,000	-	43,333	1,333	1,667	73,333
Long term	24,000	-	150,000	65,000	2,000	2,501	243,501

Details of bank loans at 1 January 2011 are as follows:

	EIB loan 1999	EIB loan 2001	Loan 2007	Loan 2009	Bilateral loan 2009	Bilateral loan 2010	Thousands of Euros
Entity	European Investment Bank	European Investment Bank	7 banks, including 2 banks of Kutxabank Group	11 banks, including 2 banks of Kutxabank Group	Banco Santander	Banesto	-
Contract date	17/12/1999	22/06/2001	25/07/2007	30/06/2009	30/09/2009	18/12/2009	-
Amount (in thousands of Euros)	120	120	150	130	4	5	-
Term (years)	15	12	8.5	5	5	5	-
Grace period (years)	5	4	6	2	2	2	-
Repayment	10 equal annual instalments as of 15/12/2005	8 equal annual instalments as of 15/12/2005	6 equal half- yearly instalments as of 25/07/2013	6 equal half- yearly instalments as of 30/12/2011	6 equal half- yearly instalments as of 30/12/2011	6 equal half- yearly instalments as of 30/12/2011	-
Guarantees	Guarantee syndicated by 11 banks, including 2 banks of Kutxabank Group	Guarantee syndicated by 14 banks, including 2 banks of Kutxabank Group	-	-	-	-	-
Maturity date	15/12/2014	15/12/2012	25/01/2016	30/06/2014	30/06/2014	30/06/2014	-
Interest rate	Variables at each repayment	Variables at each repayment	Variable pegged to Euribor	Variable pegged to Euribor	Variable pegged to Euribor	Variable pegged to Euribor	-
Average interest 2009	2,26%	2,28%	2,37%	2,24%	2,19%	-	-
Average interest 2010	0,89%	0,89%	1,12%	2,33%	2,31%	2,40%	-
Outstanding principal due	48,000	30,000	150,000	130,000	4,000	5,000	367,000
Short term	12,000	15,000	-	21,667	667	833	50,167
Long term	36,000	15,000	150,000	108,333	3,333	4,167	316,833

On 19 December 2012 the Company signed a Euros 200 million loan contract with Kutxabank, which was broken down in two tranches as follows:

- Tranche A, of Euros 125 million, for the repayment of a short-term loan obtained in 2012 to cover cash requirements deriving from the resolution of the lawsuit involving France Telecom. The full amount of this loan has been drawn down since 31 December 2012.
- Tranche B, with a limit of Euros 75 million. A drawdown schedule for this amount has been set until 2016, based on repayments corresponding to Kutxabank's share of the 2007 and 2009 loans. Euros 5 million has been drawn down on this tranche at 31 December 2012.

The combined repayment of tranches A and B will be made in six half-yearly instalments starting in December 2016.

The contract provides for the signing in 2013 of a hedge interest rate representing 75% of the credit limit during the term hereof, the margin is at least 25 basis points. This contract also provides that any surplus cash, generated during the term of the loan and calculated in accordance with the terms of the aforementioned contract, be used to settle the amount drawn down on the credit facility.

NOTE 12.- Trade and other payables and Other current liabilities

Details of the amounts included under this caption are shown below:

	<u>31.12.12</u>	<u>31.12.11</u>	<u>01.01.11</u>
Trade payables	49,025	86,513	124,117
Suppliers of fixed assets	20,975	29,234	27,460
Total	<u><u>70,000</u></u>	<u><u>115,747</u></u>	<u><u>151,577</u></u>

Details of the amounts included under Other current liabilities are shown below:

	<u>31.12.12</u>	<u>31.12.11</u>	<u>01.01.11</u>
Accrued wages and salaries	1,863	2,287	1,962
Payable to Public Administrations	6,860	2,470	3,342
Current tax liabilities	-	-	3,508
Other payables (Note 17)	-	221,903	-
Accrual accounts	995	895	589
	<u><u>9,718</u></u>	<u><u>227,555</u></u>	<u><u>9,401</u></u>

NOTE 13.- Taxation

13.1 Income Tax and Taxation

A reconciliation of net income and expenses for 2012 with the taxable income is as follows:

	<u>31.12.12</u>			<u>31.12.11</u>		
	<u>Increases</u>	<u>Decreases</u>	<u>Total</u>	<u>Increases</u>	<u>Decreases</u>	<u>Total</u>
Profit before tax			53,345			(148,843)
Permanent differences	22	-	22	-	-	-
Temporary differences	475	(6,772)	(6,297)	2,107	(265)	1,842
Taxable income			<u><u>47,070</u></u>			<u><u>(147,001)</u></u>

Temporary differences originate mainly from differences in the accrual of expenses between the tax and accounting treatments of allowances for impairment of receivables.

The income tax expense for 2012 and 2011 reflects the following items and amounts:

	<u>31.12.12</u>	<u>31.12.11</u>
Accrued income tax expense	14,943	(41,676)
Unlimited deductions for the year	(963)	(911)
Unlimited deductions for the previous years	(695)	(3,453)
Other adjustments	(1)	(949)
Total income transferred to profit of the year	(64)	-
Total	<u>13,220</u>	<u>(46,989)</u>

Income tax (expense) / income is analysed below:

	<u>31.12.12</u>	<u>31.12.11</u>
Current tax	-	-
Deferred tax	(13,285)	43,536
Other	65	3,453
Total	<u>(13,220)</u>	<u>46,989</u>

The accrued income tax expense is the result of applying the prevailing tax rate of 28% to the sum of pre-tax profits and the amount of permanent differences originating during the year.

In 2012 the Company has used loss carryforwards of Euros 32.9 million (capitalised loss carryforwards of Euros 147.0 million in 2011). At 31 December 2012, unused loss carryforwards, incurred in 2011, amount to Euros 114.1 million (Euros 147.0 million in 2011).

In 2012 the Company has applied limited income tax deductions of Euros 3.9 million. At 31 December 2012 and 2011 the Company has unused limited on tax basis and unlimited on tax basis income tax deductions for investments and other items as follows:

Year of origin	<u>31.12.12</u>	<u>31.12.11</u>	<u>01.01.11</u>
1998	-	-	434
1999	4,072	5,456	5,022
2000	17,265	17,265	17,265
2001	23,002	23,002	23,002
2002	10,399	10,399	10,399
2003	17,310	17,310	17,310
2004	16,388	16,388	16,388
2005	12,512	12,512	12,512
2006	9,927	9,927	9,927
2007	12,760	12,760	12,760
2008	13,920	13,920	13,920
2009	773	773	773
2010	949	949	-
2011	1,063	911	-
Total	<u>140,340</u>	<u>141,572</u>	<u>139,712</u>




Euros 139.3 million of the aforementioned deductions have been capitalised at 31 December 2012 (Euros 141.6 million at 31 December 2011, Euros 139.7 million at 1 January 2011).

Estimates made by the company indicate that the Company will avail of sufficient future taxable profit to offset the tax credits capitalised at the closing date.

The tax law applicable to the corporate income returns for the year for the Company is Regional Law 11/2013, of 5 December, applicable in the Territory of Biscay. Due to that modification in the tax legislation, tax credits in respect of loss carryforwards and deductions expire in 15 years from 1 January 2014 onwards.

The Company has open to inspection all main applicable taxes for the years still open to inspection.

13.2 Deferred tax

Details of deferred taxes, which are all deferred tax assets, and movement are as follows:

	<u>Temporary differences</u>	<u>Tax credits for loss carryforwards</u>	<u>Tax deductions</u>	<u>Total deferred taxes</u>
Balance at 01.01.11	3,051	-	139,712	142,763
Application of accrued income tax	516	41,160	-	41,676
Unlimited deductions from the prior year	-	-	949	949
Other adjustments	-	-	911	911
Balance at 31.12.11	3,567	41,160	141,572	186,299
Application of accrued income tax	(1,763)	(9,226)	(3,954)	(14,943)
Unlimited deductions from the prior year	-	-	695	695
Other adjustments	-	-	963	963
Balance at 31.12.12	1,804	31,934	139,276	173,014

NOTE 14.- Income and Expenses

14.1 Revenues

Revenues total Euros 338,542 thousand, all generated in the domestic market (Euros 350,520 thousand in 2011).

For "Revenue, other income & work performed by the entity and capitalized" distributed by segments please refer to Note 16.

14.2 Supplies

	<u>31.12.12</u>	<u>31.12.11</u>
Merchandise used	23,064	28,525
Purchases	21,071	29,761
Change in inventories	1,993	(1,236)
Subcontracted work	54,216	58,539
Interconnection costs	41,589	46,839
Other supplies	12,627	11,700
Impairment of merchandise	(364)	-
Total	<u>76,916</u>	<u>87,064</u>

14.3 Personnel expenses

	<u>31.12.12</u>	<u>31.12.11</u>
Salaries and wages	25,737	25,565
Other employee benefits expense	5,971	6,474
Total	<u>31,708</u>	<u>32,039</u>

The average headcount, distributed by category, is as follows:

	<u>2012</u>	<u>2011</u>
Directors	30	31
Managers	45	45
Other professionals	473	472
Total	<u>548</u>	<u>548</u>

14.4 Other operating expenses / income

	<u>31.12.12</u>	<u>31.12.11</u>
Advertising	13,695	15,800
Repairs and maintenance	27,686	28,257
Services provided by third	36,700	36,540
Other external services	14,283	14,847
Taxes	4,098	5,440
Losses, impairment and changes in trade provisions	3,057	4,586
Other losses / (gains)	(7,302)	184,675
Total	<u>92,217</u>	<u>290,145</u>

14.5 Net finance cost/income

	<u>31.12.12</u>	<u>31.12.11</u>
Finance income	<u>136</u>	<u>1,283</u>
Investments in equity instruments	-	163
Marketable securities and other financial instruments	132	739
Exchange gains	4	52
Gains on disposal of financial instruments	-	329
Finance costs	<u>12,861</u>	<u>12,264</u>
Loans and borrowings	12,424	12,264
Impairment and loss on disposal of financial instruments	437	-

NOTE 15.- Earnings per share

Basic earnings per share are calculated by dividing the profit attributable to equity holders by the weighted average number of ordinary shares outstanding during the year, excluding own shares.

Details of the calculation of basic earnings/(loss) per share are as follows (thousands):

	<u>2012</u>	<u>2011</u>
Profit/(loss) for the year	40,125	(101,854)
Weighted average number of ordinary shares outstanding	<u>5,450</u>	<u>5,420</u>
Basic and diluted earnings/(loss) per share (in Euros)	<u>7.36</u>	<u>(18.79)</u>

The weighted average number of ordinary shares outstanding is determined as follows (thousands):

	2012	2011
Ordinary shares outstanding at 1 January	5,420	5,420
Effect of own shares	-	-
Effect of shares issued on Dec. 20th 2012	907	-
Weighted average number of ordinary shares outstanding at 31 December	5,450	5,420

There are no dilutive effects, consequently basic and dilutive earning per share are equal.

NOTE 16.- Segment information

We are the Basque fiber and convergence leader and operate in one of the most affluent regions in Spain. We offer primarily bundled services comprised of high-speed broadband, Pay TV, mobile and fixed telephony services to residential and business customers (Small Office / Home Office "SOHOs", Small and Medium-sized Enterprises "SMEs", large accounts and public sector entities), as well as the wholesale market.

The Company comprises the operating segments listed below:

Residential segment

We provide our residential customers with a combination of fixed and mobile telecommunication services, as well as other value added services, primarily through our fiber network and our MVNO (Mobile Virtual Network Operator) agreement.

We offer customers the opportunity to subscribe to a variety of "bundled" packages, which provide them with multiple services (broadband internet, Pay TV, mobile telephony and fixed telephony) charged in a single bill and at competitive prices.

Business segment

We also provide fixed and mobile telecommunication services to SOHOs, SMEs and large corporate accounts, leveraging our fiber network. For SMEs and large accounts, through our own salesforce, we are able to offer integrated and tailor-made solutions to a sophisticated and demanding customer base, which includes financial institutions, large corporates, healthcare providers and public administration bodies.

- **SOHOs:** We have a specific product offering for small businesses (under ten employees), which includes premium technical support, online presence and email services. As on the residential segment, we offer customers the opportunity to subscribe to a variety of "bundled" packages, which provide them with multiple services (broadband internet, Pay TV, mobile telephony and fixed telephony).
- **SMEs:** We provide a range of customized solutions for medium-sized businesses (ten to 40 employees) with relatively high technological requirements. These services include broadband access of up to 250Mbps, fiber access of up to 1Gbps symmetric, MPLS Network, fixed-mobile convergence ("FMC"), IP Switch and advanced IT services.
- **Large accounts:** Our large accounts customers comprise both public administration bodies and large corporates. Our large accounts customers have high technological requirements and we devise tailor-made solutions according to each customer's specific needs. These include fiber access of up to 1Gbps symmetric, FMC, SIP Trunking, MLPS networks, cloud firewall and virtual data centers. We sell these services directly through our own large accounts salesforce, which includes highly-qualified engineers across the life cycle of a project (pre-sale, implementation and post-sale).




Wholesale and Other

We provide communications services including leased lines, data and voice services to other telecommunications operators that use our facilities and infrastructure to provide services to their customers. A portion of our wholesale segment revenues is generated by a number of large telecommunication companies, most of who compete directly with us. We provide Leased Lines services in SDH (Synchronous Digital Hierarchy) and Ethernet technologies, Dark Fiber, Voice Services (that allow carriers to complete their end-user calls that originate or terminate within our territory) and Enabling Services, based in our BSS and Mobile Core Network. In addition, we offer services such as collocation and voice resale. Finally, by virtue of our agreement with RACC, we also offer mobile services in Catalonia using the "RACC M6vil" brand.

Others

We sell installation material and electronics to third-party installation companies to be used in provisioning customers and deploying and maintaining our next generation fiber network.

The Company's Senior Leadership Team reviews the internal management reports for each segment on a monthly basis. Segment performance is measured based on the income generated by each segment. The global profit generated is used as a measure of its performance because the Company considers that this is the most relevant information in the assessment of the profits generated by specific segments in relation to other groups which operate in these businesses. This information is reported from figures obtained from the accounting books. In the following table it is shown those figures, once reconciliated to NIIF, according to impacts detailed in Note 21.

A detail of the management profit and loss account broken by segments is as follows:

Revenue, other income & work performed by the entity and capitalized breakdown	2012	2011
Residential	201,286	204,079
Business	102,830	102,950
<i>o/w SoHos</i>	37,112	36,945
<i>o/w SMEs</i>	18,032	18,174
<i>o/w Large Accounts</i>	47,686	47,831
Wholesale and Other	28,889	30,603
Others*	9,795	17,516
Total	342,800	355,148
Costs breakdown		
Direct costs	(81,849)	(90,224)
Gross profit	260,951	264,924
<i>% margin</i>	76.1%	74.6%
Commercial Costs	(60,603)	(67,084)
Contribution margin	200,348	197,840
<i>% margin</i>	58.4%	55.7%
Overhead Costs	(65,691)	(67,265)
EBITDA	134,657	130,575
<i>% margin</i>	39.3%	36.8%
Depreciation and amortization	(75,889)	(83,762)
Other non recurring (costs) / income	7,302	(184,675)
Results from operating activities	66,070	(137,862)
Net Finance Cost	(12,725)	(10,981)
Profit before income tax	53,345	(148,843)
Income tax	(13,220)	46,989
Profit for the year	40,125	(101,854)

* Operations with neutral impact on profitability

Assets are not managed by segment, See information regarding intangible and tangible assets in Notes 5 and 6.

NOTE 17.- Contingences

On April 19, 2012, the Board of Civil and Criminal Superior Court of the Basque Country (hereinafter TSJPV) issued indictment with the dissenting opinion of the Chairman, for which Euskaltel, S.A. is sentenced to pay the full amount of the Award concerning the "Cease No. 15635 JRF", i.e. Euros 221.9 million, the Award is the result of proceedings against Euskaltel, S.A. dated June 2, 2008, by the France Telecom Group (hereinafter GFT) before the International Chamber of Commerce, based in Paris (hereinafter ICC), considering that the beginning of its activity Mobile Virtual Network Operator (hereinafter, OMV) was a violation of the non-competition agreement stipulated in the agreement of sale of shares of Auna Operadores de Telecomunicaciones, S.A. by Euskaltel, S.A. and other societies, GTF, the July 29, 2005, which Euskaltel accede to on October 31, 2005, and the Shareholders Agreement dated December 8, 2005.

The complaint concerning this award (named by the ICC itself as "Case No. 15653 JRF"), which, by the vote of the majority, but with a dissenting opinion diametrically opposite thereto by the only component of the Arbitral Tribunal prestige recognized and proven knowledge of Spanish law, which estimated a substantial part of the benefits of the plaintiffs, namely Euros 221.9 million (Euros 159.8 million net of tax effect) was notified to Euskaltel, SA dated July 12, 2010.

On 9 September 2010 Euskaltel raised a proceeding for annulment of that resolution on the Federal Court of Laussane, Switzerland. On 24 February 2011 it was received the dismissal of that annulment. That resolution could not be in force under Spanish legislation unless TSJPV issued the application of the same.

The reason that the intervention was necessary in the process of TSJPV is because in the Spanish legal system does not operate the automatic recognition of the effectiveness of foreign arbitral awards, but they require for their recognition and effectiveness prior judicial declaration of nature homogeneous by the competent courts, through the so-called exequatur procedure.

As a result of that Order, the accounting recognition of amounts by Euskaltel, S.A. was performed in 2011, by reformulating their financial statements, although the aforementioned order has been issued subsequent to year end, given the very significant effect posed to such financial statements and, to that date, were pending approval by the General Meeting.

On July 2, 2012, the Company signed a Settlement Agreement by which declared extinct and settled all the duties, responsibilities and liabilities in relation to this matter and other particles with GFT, accrued prior to 30 April 2012, under which the total amount payable by the Company remained minus Euros 10 million, income which is recognized under Other results of the statement of income, resulting settled and liquidated all the debts between these entities by paying Euros 215 million by Euskaltel, S.A., carried out at the signature of the Settlement Agreement.

At December 31, 2012 there are no balances with GFT arising from this litigation, or outstanding balances that do not correspond to the normal operations of the Company.

NOTE 18.- Commitments

18.1 Sale/purchase commitments

At the reporting date, the Company has signed sale-purchase contracts for the following items and amounts, all of which are related to current operations:

	<u>31.12.12</u>	<u>31.12.11</u>	<u>01.01.11</u>
Intangible assets	740	302	1,270
Property, plant and equipment	7,799	9,174	11,127
Inventories	2,330	5,868	4,812
Total	<u>10,869</u>	<u>15,344</u>	<u>17,209</u>

The Company has no firm commitments to sell assets.

18.2 Operating lease commitments

The Company mainly rents locations for its node equipment under operating leases. These contracts have a term of between 10 and 30 years, which is considered to be significantly less than the economic life of the buildings in which the aforementioned equipment is located.

Future minimum payments under operating leases are as follows:

	<u>31.12.12</u>	<u>31.12.11</u>	<u>01.01.11</u>
Less than 1 year	3,422	4,307	4,390
1-5 years	12,322	15,493	14,812
Over 5 years	24,023	25,822	24,502
Total	<u>39,767</u>	<u>45,622</u>	<u>43,704</u>

Operating lease instalments of Euros 8,287 thousand have been recognised as an expense for the year (Euros 8,653 thousand in 2011).

NOTE 19.- Related parties

19.1. Key management personnel compensation

Key management personnel compensation comprises the following:

	Board of Directors		Other key management	
	2012	2011	2012	2011
Short-term employee benefits	622	1,112	3,483	3,024
Termination payments				
Share based payments				
	<u>622</u>	<u>1,112</u>	<u>3,483</u>	<u>3,024</u>

The members of The Board of Directors of the Company have not received any remuneration as a share of profit or bonuses. Neither any shares nor share options in 2012 or 2011, and they did not exercise options or have any options to exercise. Furthermore, members of the Board of Directors of the Company have not received advances or loans during the year.

The Company has no pension or life insurance obligations with the board members.

Furthermore, the Company has no pension or life insurance commitments with its management personnel.

19.2 Other related party transactions and balances

During the years ended 31 December 2012 and 2011 the Company carried out the following transactions with their main shareholders:

	Transaction value		Balance outstanding	
	2012	2011	31.12.12	31.12.11
Service rendered	6,916	6,541	-	-
Finance income	119	652	-	-
Finance expense	6,229	3,144	51	11

The aforementioned transactions were performed with Kutxabank Group.

In addition, in 2012 a telecommunication network was acquired to the Basque Government, former Company's shareholder, as detailed in Notes 6 and 10.

Balances payable in relation with the borrowings granted by the Company's shareholders are as follows:

	2012		2011		01.01.11	
	Current	Non-current	Current	Non-current	Current	Non-current
Kutxabank Group	35,005	175,795	8,601	62,743	3,937	71,345
Total	<u>35,005</u>	<u>175,795</u>	<u>8,601</u>	<u>62,743</u>	<u>3,937</u>	<u>71,345</u>

The balances and transactions with related parties are performed on an arm's length basis.

NOTE 20.- Guarantees

The Company has extended guarantees totalling Euros 41.3 million (Euros 13.4 million in 2011), in addition to the guarantees extended to public entities for financing contracts signed as a result of legal obligations deriving from its participation in the development of the telecommunications business and for the licences to roll-out the networks.

NOTE 21.- Impact of first-time adoption

Pursuant to prevailing Spanish legislation, the Company is obliged to prepare individual financial statements in accordance with the accounting principles established in the Spanish General Chart of Accounts and other applicable regulations. In this regard, on 6 March 2013, the directors of the Company authorised for issue the annual accounts for the year ended 31 December 2012. Furthermore, within the context of the stock exchange flotation mentioned in note 2, the financial statements for the year ended 31 December 2012 were prepared in accordance with International Financial Reporting Standards as adopted by the European Union (IFRS-EU). The date of first-time adoption is 31 December 2012, being 1 January 2011 the date of transition to IFRS-EU.

These financial statements have been prepared on a historical cost basis, as modified by the revaluation of financial assets and financial assets and liabilities at fair value through profit and loss.

The preparation of these financial statements in accordance with IFRS-EU requires the application of certain significant accounting estimates. The application of IFRS also requires that management exercise judgment in the process of applying the accounting policies. In Note 2.2, the areas that require a higher level of judgment or entail greater complexity are disclosed, and the areas where assumptions and estimates are significant for the financial statements.

21.1 Application of IFRS 1

As described in note 2.1 these financial statements represent the first financial statements prepared under IFRS-EU, with 1 January 2011 as the transition date.

In accordance with IFRS 1, the Company has retrospectively applied throughout the opening balance and all periods presented all effective IFRS standards as of December 31, 2012 with the exemptions permitted by IFRS. The Company has applied the following exemptions:

- Investments in separate financial statements
- Non controlling interests
- Borrowing costs
- Disclosure about financial instruments
- Business combinations

The Company was also subject to mandatory exceptions to IFRS 1, which prohibit the retrospective application of other IFRSs relating to:

- Accounting estimates
- Derecognition of financial assets and liabilities
- Classification and measurement of previously recognized financial instruments

Investments in separate financial statements

IAS 27 Allows first time adopters to use deemed cost of either fair value or the carrying amount under previous accounting practice to measure the initial cost of investments in subsidiaries, jointly controlled entities and associates in the separate financial statements. This is the option chosen by the company



Non- controlling interests

A first-time adopter shall apply the following requirements of NIC 27 prospectively from the date of transition to IFRSs:

- a) the requirement in paragraph 28 that total comprehensive income is attributed to the owners of the parent and to the non-controlling interests even if this results in the non-controlling interests having a deficit balance;
- b) the requirements in paragraphs 30 and 31 for accounting for changes in the parent's ownership interest in a subsidiary that do not result in a loss of control; and
- c) the requirements in paragraphs 34-37 for accounting for a loss of control over a subsidiary, and the related requirements of paragraph 8A of IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*.

However, if a first-time adopter elects to apply IFRS 3 retrospectively to past business combinations, it also shall apply NIC27 in accordance with paragraph C1 of IFRS 1.

Borrowing costs

A first-time adopter can elect to apply the requirements of IAS 23 from the date of transition or from an earlier date as permitted by paragraph 28 of IAS 23. From the date on which an entity that applies this exemption begins to apply IAS 23, the entity:

- (a) shall not restate the borrowing cost component that was capitalized under previous GAAP and that was included in the carrying amount of assets at that date; and
- (b) shall account for borrowing costs incurred on or after that date in accordance with IAS 23, including those borrowing costs incurred on or after that date on qualifying assets already under construction.

The Company applies IAS 23 from the date of transition onwards.

Disclosures about financial instruments

A first-time adopter may apply the transition provisions in paragraph 44 of IFRS 7:

Disclosures—Transfers of Financial Assets (Amendments to IFRS 7), issued in October 2010, deleted paragraph 13 and added paragraphs 42A-42H and B29-B39. An entity shall apply those amendments for annual periods beginning on or after 1 July 2011. Earlier application is permitted. If an entity applies the amendments from an earlier date, it shall disclose that fact. An entity need not provide the disclosures required by those amendments for any period presented that begins before the date of initial application of the amendments.

Business combinations

The exemption provided by IFRS 1 for business combinations has been applied. As a result, it has not restated the business combinations that existed prior to the transition date of 1 January 2011.

Accounting Estimates

An entity's estimates in accordance with IFRSs at the date of transition to IFRSs shall be consistent with estimates made for the same date in accordance with previous GAAP (after adjustments to reflect any difference in accounting policies), unless there is objective evidence that those estimates were in error.

All estimates are compliant with IFRS.

Derecognition of financial assets and liabilities

The mandatory exception from full retrospective application of the derecognition rules in IAS 39 applies to all financial assets and liabilities derecognized before the date of transition to IFRS. The exception requires first-time adopters to prospectively apply the derecognition criteria for non-derivative financial assets and liabilities per IAS 39 from the date of transition to IFRS onwards. This means that: (i) non-derivative financial assets and liabilities that were derecognized under previous GAAP before the date of transition to IFRS will remain derecognized; therefore, those transactions would not have to be reconstructed; and (ii) non-derivative

financial assets and liabilities that were derecognized under previous GAAP after the date of transition to IFRS will be recognized again in the financial statements of first-time adopters, if they do not qualify for derecognition under IAS 39. Therefore, those transactions would have to be reconstructed using available information.

The Company has applied the derecognition criteria for all non-derivative financial assets and liabilities from the date of transition to onwards.

Classification and measurement of previously recognized financial instruments

IAS 39 allows a financial instrument to be designated as a financial asset or financial liability at 'fair value through profit or loss' (where permitted) or as 'available-for-sale' on initial recognition. Paragraph D19 in Appendix D of IFRS 1 allowed this designation to be made at the date of transition.

There are no changes in the classification between the previous Gaap and IFRS.

- **Assets held for sale and discontinued operations**

None of the Company's assets or discontinued activities meet the criteria for classification as held for sale during the period covered by these accounts. Therefore, no adjustment has been required.

21.2 List and summary of the standards, amended standards and interpretations published to date

a) Standards, amended standards and interpretations that are not yet effective but can be early applied in years beginning on or after 1 January 2013

At the date of authorising the financial statements for issue, the IASB and IFRS Interpretations Committee had published the following standards, amended standards and interpretations that are mandatorily applicable from 2013 and which the Company has not early applied.

- **IFRS 1 (amendment), 'Severe hyperinflation and removal of fixed dates for first-time adopters'**

Although this amendment was mandatorily applicable in annual periods beginning on or after 1 July 2011 according to the date of effectiveness established by the IASB, for European Union purposes, the amendment is effective for annual periods beginning on or after 1 January 2013.

This amendment has been early adopted and do not have an impact on the Company's financial statements.

- **IAS 1 (amendment), 'Presentation of financial statements'**

It has been applied in advance the modifications to IAS 1 regarding the presentation of the statement of comprehensive income, in force for periods after 1 July 2012.

This amendment changes the presentation of the statement of comprehensive income, requiring that the items presented in other comprehensive income (OCI) be grouped into two categories depending on whether they are potentially reclassifiable to profit or loss subsequently.

This standard is effective for annual periods beginning on or after 1 July 2012. Early application is permitted.

This amendment has been early adopted by the Company in the current financial statements.

- **IAS 19 (amendment), 'Employee benefits'**

The amended IAS 19 significantly changes how defined benefit pension and termination expenses are recognised and measured, as well as changing disclosure requirements for all employee benefits.

The amended IAS 19 is mandatorily applicable for annual periods beginning on or after 1 January 2013. Early application is allowed.

The Company is analysing the potential effects of this amendment on its financial statements.

- **IFRS 12, 'Disclosures of interests in other entities'**

IFRS 12 includes the disclosure requirements for all entities reporting under the new IFRS 10, 'Consolidated financial statements', and the new IFRS 11, 'Joint arrangements'. It additionally replaces the disclosure requirements formerly included in the old IAS 28, 'Investments in associates', and IAS 31, 'Interests in joint ventures'. Under IFRS 12, reporting entities must disclose information that allows financial statement users to assess the nature, risks and financial consequences associated with its interests in subsidiaries, associates, joint arrangements and unconsolidated structured entities.

Although this amendment was mandatorily applicable in annual periods beginning on or after 1 January 2013 according to the date of effectiveness established by the IASB, for European Union purposes, the amendment is effective for annual periods beginning on or after 1 January 2014.

Early adoption is permitted.

No impact is identified on these financial statements due to the aforementioned IFRS12.

- **IAS 27 (amendment), 'Separate financial statements'**

The requirements previously established in IAS 27 with respect to the preparation of the financial statements are included in the new IFRS 10 and therefore the former scope of application is reduced to the accounting for investments in subsidiaries, joint ventures and associates in the individual financial statements prepared under IFRS by the investing company, which have not changed with respect to existing rules (i.e. recognition at cost or fair value as per IFRS 9).

Although the amended IAS 27 was mandatorily applicable in annual periods beginning on or after 1 January 2013 according to the date of effectiveness established by the IASB, for European Union purposes, the amendment is effective for annual periods beginning on or after 1 January 2014.

It may be applied early under certain conditions.

The Company accounts its investments by the same criteria considered in the Spanish Gaap, at cost

- **IAS 28 (amendment), 'Investments in associates and joint ventures'**

IAS 28 has been updated basically to make reference to the joint ventures which under the new IFRS 11, 'Joint arrangements', must be accounted for using the equity method of consolidation.

Although the amended IAS 28 was mandatorily applicable in annual periods beginning on or after 1 January 2013 according to the date of effectiveness established by the IASB, for European Union purposes, the amendment is effective for annual periods beginning on or after 1 January 2014.

It may be applied early under certain conditions.

This amendment does not have a material impact on the Company's financial statements.

- **IFRS 13, 'Fair value measurement'**

IFRS 13 is the outcome of a joint initiative by the IASB and the FASB (the US Financial Accounting Standards Board) and is intended to explain how to value items at fair value, all with a view to improving and expanding fair value disclosures. This standard does not establish which items must be measured at fair value. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (the exit price). It is based on the perspective of market participants rather than simply that of the reporting entity. It introduces a three-level fair value hierarchy, equivalent to that established in IFRS 7, for fair value measurement.

This standard is mandatorily applicable for annual periods beginning on or after 1 January 2013. The new standard will be applied gradually from the beginning of the fiscal year in which it is applied for the first time. The disclosure requirements do not apply to the comparative information presented in respect of fiscal years prior to that of first-time application of IFRS 13.

No significant differences are identified by the Company in the application of the aforementioned IFRS13.

- **IAS 32 (amendment) and IFRS 7 (amendment), 'Offsetting financial assets and financial liabilities'**

The IASB issued an amended IAS 32, 'Offsetting financial assets and financial liabilities', and an amended IFRS 7, 'Disclosures - 'Offsetting financial assets and financial liabilities' in December 2011.

The so-amended IFRS 7 is mandatorily applicable for annual periods beginning on or after 1 January 2013 and must be applied retroactively. Early adoption is permitted.

These new standards, amended standards and interpretations do not have a material impact on the Company's financial statements.

- **Annual improvements to IFRSs, the 2009-2011 Cycle**

- **IAS 1, 'Presentation of financial statements'**

IAS 1 has been amended to clarify that the comparative information required under IAS 1 is that of a complete set of financial statements. It further clarifies the minimum comparative disclosure requirements when an entity changes accounting policy or makes retrospective restatements or reclassifications: in this instance, the reporting entity is required to present an opening statement of financial position (known as the third balance sheet); however it is not required to accompany the third balance sheet with the related notes.

This amendment must be applied retroactively and is mandatorily applicable for annual periods beginning on or after 1 January 2013. Early application is allowed. This new standard does not have a material impact on the Company's financial statements.

- **IAS 16, 'Property, plant and equipment'**

This improvement clarifies that major spare parts and servicing equipment that meet the definition of property, plant and equipment are not inventory. In the wake of this amendment, servicing equipment expected to be used for more than one year will be classified as part of property, plant and equipment rather than as inventories.

This amendment must be applied retroactively and is mandatorily applicable for annual periods beginning on or after 1 January 2013. Early application is allowed. The Company early adopted this rule.

- **IFRS 32, 'Financial instruments: Presentation'**

This amendment resolves a conflict perceived to exist between IAS 32 and IAS 12, 'Income Taxes'. It clarifies that tax credits related to distributions to equity holders and to transaction costs corresponding to any equity item must be accounted for in accordance with IAS 12. As a result, the tax incentives related to distributions to equity holders are recognised in profit or loss and the tax credits relating to transaction costs corresponding to equity instruments are recognised in equity.

This amendment must be applied retroactively and is mandatorily applicable for annual periods beginning on or after 1 January 2013. Early application is allowed. This new standard does not have a material impact on the Company's financial statements.

- **IAS 34, 'Interim financial reporting'**

IAS 34 has been amended to align the disclosure requirements stipulated by IAS 34 and IFRS 8, 'Operating segments'. The amendment clarifies that an entity that reports interim information under IAS 34 need only disclose information regarding total assets and liabilities for a particular reportable segment when the amounts are regularly provided to the chief operating decision maker and there has been a material change in the total amount disclosed in the entity's previous annual financial statements.

This amendment must be applied retroactively and is mandatorily applicable for annual periods beginning on or after 1 January 2013. Early application is allowed. This new standard does not have a material impact on the Company's financial statements.

- **Consolidated financial statements, joint arrangements and disclosure of interests in other entities: Transition guidance (amendments to IFRS 10, IFRS 11 and IFRS 12)**

The IASB has amended the transitional provisions contained in IFRS 10, 'Consolidated financial statements', IFRS 11, 'Joint arrangements', and IFRS 12, 'Disclosure of interests in other entities', in order to clarify that the date of first-time application is the first day of the first annual period in which IFRS 10 is applied for the first time.

The amendments to the above-listed standards are mandatorily applicable for annual periods beginning on or after 1 January 2013, in keeping with the dates of effectiveness of the standards so amended. Early adoption is required if the related standards (IFRS 10, IFRS 11 and IFRS 12) are also early adopted.

- **IAS 36 (Amendment) "Recoverable Amount Disclosures for Non-Financial Assets"**

This introduces a limited-scope amendment to IAS 36 "Impairment of Assets". The amendment requires detailed disclosure of how the fair value less costs of disposal has been measured when an impairment loss has been recognised or reversed.

This amendment does not have any impact on the current Company's financial statements.

- **Annual IFRS Improvements 2011-2013 Cycle**

In December 2013 the IASB issued Annual Improvements to IFRSs 2011-2013 Cycle. The amendments are effective for annual periods beginning on or after 1 January 2015, although entities are permitted to apply them earlier. The main amendments are:

- IFRS 3 "Business Combinations": Scope exceptions for joint ventures. Not applicable to the Company.
- IFRS 13 "Fair Value Measurement": Scope of the "portfolio exception" in IFRS 13.
- IAS 40 "Investment Property": Interrelationship of IAS 40 and IFRS 3 when classifying property as investment property or owner-occupied property.

These improvements do not have a material impact on the Company's financial statements.

- **Annual IFRS Improvements, 2010 - 2012**

In December 2013 the IASB issued Annual Improvements to IFRSs 2010-2012 Cycle. The amendments are effective for annual periods beginning on or after 1 February 2015, although entities are permitted to apply them earlier. The main amendments are:

- IFRS 2 "Share-Based Payment": Definition of "vesting conditions". Not applicable for the Company in 2012.
- IFRS 3 "Business Combinations": Accounting for a contingent consideration in a business combination. Not applicable to the Company.
- IFRS 8 "Operating Segments": Information to be disclosed concerning the aggregation of operating segments and reconciliation of the total of the reportable segments' assets to the entity's assets. These improvements do not have a material impact on the Company's financial statements.
- IFRS 13 "Fair Value Measurement": References to the capacity for measurement of short-term receivables and payables at nominal value when the impact of discount is not material. These improvements do not have a material impact on the Company's financial statements.
- IAS 16 "Property, Plant and Equipment" and IAS 38 "Intangible Assets": Proportionate restatement of accumulated depreciation when using the revaluation model. Not applicable for the Company.
- IAS 24 "Related-Party Disclosures": Entities providing key management personnel services in the capacity of a related party. Not applicable for the Company.

- **IAS 19 (Amendment) "Employee Benefits: Employee contributions"**

IAS 19 (as revised in 2011) distinguishes between employee contributions related to service and those not linked to service. The current amendment further distinguishes between contributions that are linked to service only in the period in which they arise and those linked to service in more than one period. The amendment allows contributions

that are linked to service, and do not vary with the length of employee service, to be deducted from the cost of benefits earned in the period that the service is provided. Contributions linked to service that vary according to the length of service must be spread over the service period using the same attribution method that is applied to the benefits. The amendment is effective for annual periods beginning on or after 1 February 2015 and retrospective application is required. Early adoption is permitted. Not applicable for the Company in 2012.

b) New standards and amendments to and interpretations of existing standards that cannot be early adopted or have not yet been adopted by the European Union

At the date of authorising the accompanying financial statements for issue, the IASB and IFRS Interpretations Committee had published the following standards, amendments and interpretations that have not yet been adopted by the European Union.

- **IFRS 9, 'Financial instruments'**

IFRS 9 addresses the classification, measurement and recognition of financial assets and financial liabilities. The complete version of IFRS 9 was published in July 2014, replacing the IAS 39 guideline to the classification and measurement of financial instruments. IFRS 9 maintains a simplified format of the combined measurement model, and establishes three main measurement categories for financial assets: amortised cost, at fair value through profit or loss, and at fair value through other comprehensive income. The classification basis depends on the entity's business model and the characteristics of the financial asset's contractual cash flows. Investments in equity instruments must be measured at fair value through profit or loss, with the irrevocable option of presenting changes to fair value through other comprehensive non-recyclable income, provided the instrument is not held for trading. IFRS9 introduces a new impairment loss model, the expected loss model, which replaces the impairment loss model in IAS 39 and will entail timely recognition of losses, as the practice was in IAS 39. IFRS 9 relaxes the requirements for effectiveness of hedges. Under IAS 39, a hedge must be highly effective, both prospectively and retrospectively. IFRS 9 requires an economic relationship between the hedged item and the hedging instrument, and for the hedged ratio to be the same as that used by the entity for risk management purposes.

IFRS 9 applies for annual periods beginning on or after 1 January 2018. Earlier application is permitted. It will be applied retrospectively, albeit with no requirement to restate the comparative figures.

This standard is applicable for annual periods beginning on or after 1 January 2015; early application is permitted.

The Company is analyzing the potential impact of this standard.

- **IFRS 15 Revenue from contracts with customers**

IFRS 15 establishes a comprehensive framework for determining whether, how much and when revenue is recognized. It replaces existing revenue recognition guidance, including IAS 18 Revenue, IAS 11 Construction Contracts and IFRIC 13 Customer Loyalty Programmes. IFRS 15 is effective for annual reporting periods beginning on or after 1 January 2017, with early adoption permitted. As informed in note 2, this financial statements has been formulated under IFRS as adopted by the EU in the context of the potential listing of company shares, consequently the analysis of the potential impact resulting from the application of IFRS 15 will depend on the successful completion of said process.



21.3. Reconciliation of IFRS to local GAAP

A reconciliation between equity in accordance with prevailing Spanish accounting principles and the equity recognised in the accompanying balance sheets for the years ended 31 December 2012 and 2011 is shown in the following table:

	<u>31.12.12</u>	<u>31.12.11</u>	<u>01.01.11</u>
Equity (SP GAAP)	572,896	464,835	56,729
Reserves	80,158	87,535	87,535
Other comprehensive income	(72,179)	(80,158)	(87,535)
Profit for the year			
Investment tax credits	(7,979)	(7,377)	-
Equity IFRS-EU	<u><u>572,896</u></u>	<u><u>464,835</u></u>	<u><u>56,729</u></u>

When preparing its first financial statements under IFRS, the Company adjusted the amounts previously recognized in its annual accounts prepared under generally accepted accounting principles in Spain. The explanation of the effects of the conversion on the balance sheet, the income statement and the statement of cash flows for the three years mentioned are detailed in the following tables and notes:




A) Balance Sheet at 31 December 2012, 2011 and 1 January 2011

	31.12.2012		
	Equity final SP Gaap	Transition Effect	Equity final IFRS
Capital and reserves	452,677	80,158	532,835
Valuation adjustments	72,115	(72,179)	(64)
Profit for the year	48,104	(7,979)	40,125
Equity	572,896	-	572,896

	31.12.2011		
	Equity final SP Gaap	Transition Effect	Equity final IFRS
Capital and reserves	479,154	87,535	566,689
Valuation adjustments	80,158	(80,158)	-
Profit for the year	(94,477)	(7,377)	(101,854)
Equity	464,835	-	464,835

	01.01.2011		
	Equity final SP Gaap	Transition Effect	Equity final IFRS
Capital and reserves	479,755	87,535	567,290
Valuation adjustments	87,535	(87,535)	-
Equity	567,290	-	567,290

B) Income Statements for the year ended 31 December 2012 and 2011

	2012		
	Transition		
	SP Gaap	Effect	IFRS
RESULTS FROM OPERATING ACTIVITIES	66,070	-	66,070
NET FINANCE COST	(12,725)	-	(12,725)
PROFIT BEFORE INCOME TAX	53,345	-	53,345
Income tax	(5,241)	(7,979)	(13,220)
PROFIT FOR THE YEAR	48,104	(7,979)	40,125

	2011		
	Transition		
	SP Gaap	Effect	IFRS
RESULTS FROM OPERATING ACTIVITIES	(137,862)	-	(137,862)
NET FINANCE COST	(10,981)	-	(10,981)
PROFIT BEFORE INCOME TAX	(148,843)	-	(148,843)
Income tax	54,366	(7,377)	46,989
PROFIT FOR THE YEAR	(94,477)	(7,377)	(101,854)

The other comprehensive income is also impacted in those periods in the same amount that the one shown in the Income statements in those periods.

In accordance with Spanish accounting principles, the investment tax credits stipulated in tax legislation can be recognised as a reduction in the current income tax expense. Alternatively, the amount of investment tax credits can be initially recorded with a charge to other comprehensive income and subsequently recognised in the income statement as a reduction in the current income tax expense. The directors of the Company used this latter criteria when preparing the annual accounts for local GAAP purposes. The accounting treatment of investment tax credits is not defined in IFRS-EU. Nevertheless, taking into account that the aforementioned tax credits are available to all entities and not associated with fulfilling additional requirements other than the investment itself, the directors of the Company consider that investments tax credits are in substance a reduction in income tax more in line with IAS 12 (Income Taxes) than with IAS 20 (Capital Grants). Consequently, reserves have been increased and other comprehensive income and income tax have been reduced by amounts of Euros 80.2 million, Euros 72.2 million and Euros 8 million, respectively (Euros 87.6 million, Euros 80.2 million and Euros 7.4 million, respectively, in 2011; Euros 87.5 million, Euros 87.5 million and zero, respectively, at 1 January 2011).

NOTE 22.- Subsequent events

The main subsequent events after the end of the year and till the date of preparation of these financial statements, which have been properly reflected in the annual accounts for the years 2013 and 2014, are as follows:

- **Share-based payments Plan:** The Company has awarded certain incentives to members of the management committee, board members and other key employees, which will entitle them to participate in any appreciation in the Company's share value between 10 July 2013 and 31 December 2025, with the possibility of extending the vesting date by another five years upon the request of the board of directors.
- **Financing plan:** On 22 March 2013, the Company signed a non-extinguishing novation addendum to the contract entered into with Kutxabank on 19 December 2012, which modifies the terms referring to the loan principal (down from Euros 200 million to Euros 130.5 million). In conjunction with this addendum, on 22 March 2013 the Company signed four long-term bilateral loans for a total of Euros 69.5 million.

In this two year period, the Company has met with the payments schedule related to the financial debt.

- **Strategic alliances:** large-scale agreements have been reached with strategic partners in the areas of information technology (with the French multinational GFI) and network management and maintenance (with the Chinese multinational ZTE). Through these agreements the Company has shared know-how and completed two externalization projects that involved the transfer of Euskaltel employees from these areas of activity, a decision that reflects the close collaboration between the companies and which will enable us to access new developments and technologies and strengthen our objective to provide innovative services of the utmost quality to our customers.
- **Business performance:** the company is the Basque Country fiber and convergence leader. It's the market leader in broadband and pay TV services, in terms of customers, and the fastest growing provider of mobile telephony services in the Basque Country.
The revenue evolution, though the decrease in the period, has been better than the market. EBITDA performance, as well, has been better than the competition, which has improved the profitability of the Company.
In terms of cash generation, the Company has generated an amount of cash in the last 2 years, that has set the financial net debt in the year 2000 levels.

- The Board of Directors at their meeting held on February 3, 2015 agreed, among others, to explore the possibility of carrying out a public offering of the company's shares on the Spanish stock market. The Board therefore agreed to contract an external advisor to help the company and coordinate all the actions required to prepare the Initial Public Offering (IPO).

The key milestones in the company since then have been the following:

- Lawyers and financial advisors have been contracted for the company
- Selection and appointment of the banks to coordinate and placement of the shares among the interested potential investors
- Adaptation of the Company to the new requirements of Corporate Government and the Stock Market regulator
- Presentations of the Company to the banks involved in the IPO and financial analysts
- Preparing the share offer explanatory leaflet
- Exploring the interest in the investment market, holding meetings with possible leading institutional investors
- Converting and preparing the financial statements of the Company for the financial years ended as of 31 December 2012, 2013 and 2014, along with those for the first quarter of 2015 (as of 31 March 2015), pursuant to international accounting standards, in order to make it easier for international investors to understand them.

It is forecast that the process that will lead to the Company's shares being traded on the stock exchange will conclude prior to mid-July 2015. In the event the stock exchange flotation goes ahead, and with the prior authorization of the Board of Directors, the Company intends to refinance its bank debt. The estimated amount of the refinancing is Euros 470 million, which would be used to cancel the financial debt existing at the time of the flotation, amounting to approximately Euros 232 million, with the remainder being used to cover certain payments relating to the public listing and refinancing expenses (between Euros 16 and 65 millions) and the possible payment of an extraordinary dividend (between Euros 173 and 223 millions, with a charge to freely-available reserves).

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Derio, 1 June 2015

In the context of a potential listing on the Madrid stock exchange, and to comply with requests of information by third parties, the directors of Euskaltel, S.A. have prepared for issue the Financial Statements comprising the balance sheet, income statement, statement of changes in equity, statement of comprehensive income, statement of cash flows and the notes thereto of the Company for the year ended 31 December 2012, at the board of directors meeting held at the above date.

The directors declare that they have signed each of the above-mentioned documents in their own hand, and in witness thereof sign below.

Signed:

Mr. Alberto García Frauzkin
(Chairman)

Mr. Richard David Alden

Ms. Alicia Vivanco González

Mr. Alfonso Basagoiti Zavala

Mr. Javier Bañón Treviño

Marebilu, S.A. I.
(Represented by Mr. John C. Mowinckel)

Ms. Bridget Cosgrave

Mr. José Ángel Corres Abasolo

Ms. Belén Amatriain Corbi

Mr. Iñaki Alzaga Etxeita

euskaltel

DILIGENCIA DEL SR. SECRETARIO: Se hace constar, conforme al artículo 253.3 de la Ley de Sociedades de Capital, que los miembros del Consejo de Administración don Javier Bañón Treviño, don John C. Mowinckel, representante de Mareblu, Sà.r.l., y doña Belén Amatriain Corbi, no han firmado los estados financieros del ejercicio 2012 por no encontrarse físicamente presentes durante la reunión del Consejo de Administración celebrado en Derio (Bizkaia) el 1 de Junio de 2015, habiendo delegado sus facultades en el Presidente del Consejo de Administración, Don Alberto García Erauzkin.

D. Francisco Javier Allende Arias

Secretario General y del Consejo