As filed with the Securities and Exchange Commission on June 18, 2002

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

Form 20-F/A

☐ **REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (g) OF THE SECURITIES EXCHANGE ACT OF 1934**

OR

☒ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

for the fiscal year ended December 31, 2001

OR

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

Commission file number 1-14540

Deutsche Telekom AG
(Exact Name of Registrant as specified in its charter)

Germany
(Jurisdiction of Incorporation or Organization)

Friedrich-Ebert-Allee 140, 53113 Bonn, Germany
(Address of Registrant's Principal Executive Offices)

Securities registered or to be registered pursuant to Section 12(b) of the Act.

Title of each class	Name of each exchange on which registered
American Depositary Shares, each representing one Ordinary Share	New York Stock Exchange
Ordinary Shares, no par value	New York Stock Exchange*

Securities registered or to be registered pursuant to Section 12(g) of the Act.

NONE
(Title of Class)

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act.

NONE
(Title of Class)

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the annual report:

Ordinary Shares, no par value: 4,197,752,425
(as of December 31, 2001)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes ☒ No ☐

Indicate by check mark which financial statement item the registrant has elected.

Item 17 ☐ Item 18 ☒

* Not for trading, but only in connection with the registration of American Depositary Shares.

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The purpose of this amended annual report on Form 20-F dated June 18, 2002 is to add financial information concerning certain affiliates of Deutsche Telekom AG (found herein on pages A-1 to A-156) in light of the requirements of Rule 3-09 of Regulation S-X. The errata listed below are also amended. Other than these items, no part of this annual report is being amended, and the filing of this amended annual report should not be understood to mean that any statements contained herein are true or complete as of any date subsequent to April 23, 2002, the filing date of Deutsche Telekom's annual report on Form 20-F for the year 2001. This amended annual report on Form 20-F is incorporated by reference into the registration statements of Deutsche Telekom AG on Form F-3, File Nos. 333-12096, 333-13550 and 333-84510, and into each respective prospectus that forms a part of these registration statements.

Errata Notes

1. On page 5 of Deutsche Telekom's annual report on Form 20-F for the year ended December 31, 2001 filed on April 23, 2002 (the "Original Report") in the Exchange Rates table for March of the current year, the high of "0.8652" was changed to "0.8836" and the low of "0.8836" was changed to "0.8652".

2. On page 66 of the Original Report, in the carryover paragraph at the top of the page, the reference to "EUR 246 million" was changed to "EUR 224 million".

3. On page 66 of the Original Report, in the first full paragraph, the reference to "EUR 718 million" was changed to "EUR 589 million".

4. On page 69 of the Original Report in the 2001/2000 column of the table under the "T-Com revenues" heading, the percentage amounts 7.2% and 4.0% were changed to negative percentage amounts, and the "0.1%" was changed to "(0.9%)".

5. On page 79 of the Original Report, the references to "EUR 32.7 billion" and "EUR 6.2 billion" in the first full paragraph were changed to "EUR 26.2 billion" and "EUR 4.9 billion", respectively.

6. On page 86 of the Original Report, the full name of PTC is given at "Polska Telefonia Cyfrowa Sp. z.o.o.".

7. On page F-44 of the Original Report, the references to "EUR 13 billion", "EUR 5.75 billion" and "EUR 1.7 billion" in the first paragraph were changed to "EUR 12 billion", "EUR 4.5 billion" and "EUR 0.5 billion", respectively. In addition, the reference in that paragraph to "4.65%" was changed to "4.73%". Also on that page, the references to "EUR 13.95 billion", "EUR 2.2 billion" and "6.39%" in the second paragraph on page F-44 were changed to "EUR 9.6 billion", "EUR 0.9 billion" and "6.0%", respectively.

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Forward-Looking Statements

This Annual Report contains forward-looking statements. Forward-looking statements are statements that are not historical facts. Examples of forward-looking statements include:

- financial projections and estimates and their underlying assumptions;
- statements regarding plans, objectives and expectations relating to future operations, products and services;
- statements regarding the impact of regulatory initiatives on Deutsche Telekom's operations;
- statements regarding Deutsche Telekom's share of new and existing markets;
- statements regarding general industry and macroeconomic growth rates and Deutsche Telekom's performance relative to them; and
- statements regarding future performance.

Forward-looking statements generally are identified by the words ''expects'', ''anticipates'', ''believes'', ''intends'', ''estimates'' and similar expressions.

Forward-looking statements are based on current plans, estimates and projections, and therefore you should not place too much reliance on them. Forward-looking statements speak only as of the date they are made, and Deutsche Telekom undertakes no obligation to update any forward-looking statement in light of new information or future events, although Deutsche Telekom intends to continue to meet its ongoing disclosure obligations under the U.S. securities laws (such as its obligations to file annual reports on Form 20-F and reports on Form 6-K) and under other applicable laws. Forward-looking statements involve inherent risks and uncertainties, most of which are difficult to predict and generally beyond Deutsche Telekom's control. Deutsche Telekom cautions you that a number of important factors could cause actual results or outcomes to differ materially from those expressed in, or implied by, the forward-looking statements. These factors include, among other factors:

- risks and uncertainties relating to the benefits anticipated from the acquisition of VoiceStream and Powertel;
- the level of demand for telecommunications services, particularly for wireless telecommunications services, access lines, traffic and new higher value products and services;
- competitive forces, including pricing pressures, technological developments and alternative routing developments;
- Deutsche Telekom's ability to gain or retain market share in the face of competition from existing and new market entrants;
- Deutsche Telekom's ability to secure the licenses needed to offer new services and the cost of these licenses and related network infrastructure build-outs;
- the effects of tariff reduction initiatives, particularly in the fixed-line voice telephony business but also with regard to many other areas;
- regulatory developments and changes, including with respect to the levels of tariffs, terms of interconnection, customer access and international settlement arrangements;
- the outcome of litigation in which Deutsche Telekom is involved or may become involved;
- the success of new business, operating and financial initiatives, many of which involve substantial start-up costs, and of new systems and applications, particularly with regard to integration of service offerings;
- concerns over health risks associated with the use of wireless handsets and other health and safety risks related to radio frequency emissions;
- the progress of Deutsche Telekom's domestic and international investments, joint ventures and alliances;
- the impact of Deutsche Telekom's efforts to focus its business on its four strategic divisions;

- the availability, terms and deployment of capital, particularly in view of Deutsche Telekom's debt refinancing needs, and the impact of regulatory and competitive developments on Deutsche Telekom's capital outlays;
- the level of demand in the market for Deutsche Telekom's shares and for the shares of its subsidiaries, which may affect Deutsche Telekom's financing and acquisition strategies;
- Deutsche Telekom's ability to achieve cost savings and realize productivity improvements;
- Deutsche Telekom's ability to attract and retain qualified personnel;
- risks of sabotage or acts of terrorism;
- the effects of foreign exchange rate fluctuations, particularly in connection with subsidiaries operating outside the Euro zone;
- the development of the German real estate market in view of Deutsche Telekom's strategy of monetizing a significant portion of its large real estate portfolio, which had a book value of approximately EUR 13.1 billion as of December 31, 2001; and
- general economic conditions, government and regulatory policies, new legislation and business conditions in markets that Deutsche Telekom and its affiliates serve.

Exchange Rates

Effective January 1, 1999, Germany and ten other member states of the European Union adopted the Euro as their common currency. With the first quarter of 1999, Deutsche Telekom began publishing its consolidated financial statements in Euros and, unless otherwise indicated, all amounts in this document are expressed in Euros. Amounts stated in Euros appearing in this document for periods prior to December 31, 1998, have been translated from Deutsche Marks at the official fixed conversion rate of EUR 1.00 = DM 1.95583.

Where indicated, U.S. Dollar amounts have been translated from Euros at the noon buying rate in New York City for cable transfers in foreign currencies as certified for customs purposes by the Federal Reserve Bank of New York (the "Noon Buying Rate") on April 15, 2002. This rate may differ from the actual rates Deutsche Telekom used in the preparation of its consolidated financial statements as of December 31, 2001 and 2000, and for each of the years in the three year period ended December 31, 2001. Accordingly, Dollar amounts appearing in this report may differ from the actual Dollar amounts that Deutsche Telekom originally translated into Euros in the preparation of its financial statements.

Amounts appearing in this report that were translated into Euros from currencies other than the U.S. Dollar were translated in accordance with the principles described in the consolidated financial statements under "Consolidation principles — Foreign currency translation."

The following table sets forth, for the periods indicated, the average, high, low or period-end Noon Buying Rates for the Euro expressed in Dollars per EUR 1.00. Amounts for the period from 1997 through 1998 have been calculated based on Noon Buying Rates for the Deutsche Mark, converted into Euros at the official fixed conversion rate and expressed in Dollars per EUR 1.00.

Year or month	Average(1)	High	Low	Period-End
1997	1.1244			1.0871
1998	1.1120			1.1733
1999	1.0588			1.0070
2000	0.9207			0.9388
2001	0.8909			0.8901
October		0.9181	0.8893	
November		0.9060	0.8770	
December		0.9044	0.8773	
2002				
January		0.9031	0.8594	
February		0.8778	0.8613	
March		0.8836	0.8652	

(1) The average of the Noon Buying Rates on the last business day of each month during the relevant period.

On April 15, 2002, the Noon Buying Rate was \$0.8802 per €1.00.

Since January 4, 1999, the shares of Deutsche Telekom have traded on the German stock exchanges in Euro. Fluctuations in the exchange rate between the Euro and the Dollar will affect the Dollar equivalent of the Euro price of the shares on the German stock exchanges and, as a result, are likely to affect the market price of the ADSs on the New York Stock Exchange. Deutsche Telekom will declare any cash dividends in Euros, and exchange rate fluctuations will affect the Dollar amounts you receive if you are a holder of American Depositary Receipts evidencing Deutsche Telekom American Depositary Shares (“ADSs”) on conversion of cash dividends on the shares represented by your ADSs.

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PART I

ITEM 1. Identity of Directors, Senior Management and Advisors

Not applicable.

ITEM 2. Offer Statistics and Expected Timetable

Not applicable.

ITEM 3. Key Information

SELECTED FINANCIAL DATA

The following table presents selected consolidated financial information of the Deutsche Telekom group. This selected consolidated financial information should be read together with "Item 5. Operating and Financial Review and Prospects" and the consolidated financial statements of Deutsche Telekom and the notes thereto that are included elsewhere in this Annual Report. Unless otherwise indicated, all amounts are in accordance with generally accepted accounting principles ("GAAP") in Germany.

Selected financial data of the Deutsche Telekom group

	Change[1]	2001	2000	1999	1998	1997
Earnings position (billions of €)						
Net revenue	18.0%	48.3	40.9	35.5	35.1	34.5
Changes in inventories and other own capitalized costs	1.7%	0.9	0.9	0.9	1.0	1.6
Other operating income	(39.8)%	6.6	11.0	1.9	2.1	1.9
Goods and services purchased	12.8%	13.5	12.0	7.7	5.5	6.2
Personnel costs	24.7%	12.1	9.7	9.2	9.2	9.4
Depreciation and amortization	17.2%	15.2	13.0	8.4[2]	9.0[2]	9.5[2]
Other operating expenses	16.6%	12.2	10.4	6.9	6.1	5.2
Financial income (expense), net	334.8%	(5.3)	(1.2)	(2.9)	(3.3)	(4.0)
Results from ordinary business activities	(138.6)%	(2.5)	6.5	3.2	5.1	3.7
Extraordinary losses	(100.0)%	—	(0.2)	(0.2)	—	—
Taxes	154.1%	0.8	0.3	1.4	2.7	1.9
Net income (loss)	(158.3)%	(3.5)	5.9	1.3	2.2	1.7
EBITDA[3][4]	(12.8)%	18.1	20.7	14.5	17.4	17.2
Assets and liabilities (billions of €)						
Noncurrent assets	37.6%	146.7	106.6	82.0	66.5	70.0
Current assets, prepaid expenses, deferred charges	1.2%	17.8	17.6	12.6	12.8	13.2
Shareholders' equity	55.2%	66.3	42.7	35.7	25.1	24.6
Accruals	61.9%	18.4	11.4	9.3	8.3	7.7
Debt	11.1%	67.0	60.4	42.3	39.9	44.9
Other liabilities and deferred income	30.9%	12.8	9.7	7.3	6.0	6.0
Total assets	32.5%	164.5	124.2	94.6	79.3	83.2
Financing (billions of €)						
Net cash provided by operating activities	19.3%	11.9	10.0	9.6	13.5	11.6
Net cash used for investing activities	(80.6)%	(5.4)	(27.7)	(18.7)	(7.5)	(5.4)
Net cash provided by (used in) financing activities	(126.9)%	(4.8)	17.9	8.0	(6.8)	(7.0)
Capital expenditures[5]	(53.8)%	10.9	23.5	6.0	4.8	6.8
Figures in accordance with U.S. GAAP (billions of €)						
Net income	(94.4)%	0.5	9.3	1.5	2.2	1.3
Total assets	33.7%	180.7	135.2	97.5	81.5	84.9
Total long-term liabilities	26.4%	65.6	51.9	39.4	39.7	45.3
Shareholders' equity	59.9%	73.7	46.1	37.6	26.9	26.1

	Change[1]	2001	2000	1999	1998	1997
Ratios and selected data						
Employees at balance sheet date (thousands)	13.2%	257	227	196	196	210
Revenue per employee (thousands of €)[6]	(1.0)%	199	201	183	173	159
Earnings per share/ADS in accordance with German GAAP (€)[7]	(147.4)%	(0.93)	1.96	0.43	0.82	0.62
Earnings per share/ADS in accordance with U.S. GAAP — basic and diluted (€)[7]	(95.4)%	0.14	3.06	0.53	0.81	0.46
Weighted average shares outstanding under German GAAP (millions)	22.6%	3,715	3,030	2,884	2,743	2,743
Dividend per share/ADS (€)	(40.3)%	0.37[8]	0.62	0.62	0.61	0.61
Dividend per share/ADS (US$)[9]	(37.7)%	0.33	0.53	0.58	0.64	0.68
Equity ratio (%)[10]	17.6%	39%	33%	36%	30%	28%

(1) Percentage change from 2000 to 2001 on the basis of the more exact figures expressed in millions.
(2) Including depreciation of value-added tax capitalized prior to January 1, 1996.
(3) Results from ordinary business activities before financial income (expense), depreciation and amortization.
(4) EBITDA should not be viewed as an alternative to net income, operating income, net cash provided by operating activities or other financial measures prepared in accordance with German or U.S. GAAP. Since different companies may calculate EBITDA in different ways, Deutsche Telekom's EBITDA may not be directly comparable to similarly titled statistics of other companies.
(5) In accordance with the cash flow statement.
(6) Calculated on the basis of the average number of employees for the year without trainees/student interns.
(7) Based on dividing net income by the weighted average number of ordinary shares outstanding for each year. The share/ADS ratio is 1:1.
(8) Proposed dividend. Dividends per share are presented on the basis of the year in respect of which they are declared, not the year in which they are paid.
(9) Dividend amounts have been translated into dollars at the Noon Buying Rate for the relevant dividend payment date, which occured during the second quarter of the following year, except for the 2001 amount, which has been translated at the Noon Buying Rate on December 31, 2001.
(10) The ratio equals total stockholders' equity divided by total assets. Amounts proposed as dividends are treated as short-term debt rather than as equity for purposes of the calculation of this ratio.

RISK FACTORS

In addition to the other information contained in this annual report, investors in Deutsche Telekom shares should consider carefully the risks described below. Deutsche Telekom's financial condition or results of operations could be materially adversely affected by any of these risks. The risks described below are not the only risks facing Deutsche Telekom. Additional risks not currently known to Deutsche Telekom or risks that Deutsche Telekom currently regards as immaterial also could have a material adverse effect on Deutsche Telekom's financial condition or results of operations.

Intense competition could have an adverse effect on Deutsche Telekom's financial condition and results of operations.

Deutsche Telekom faces intense competition in all areas of its business. In the fixed-network voice telephony business, which has been open to competition since January 1, 1998, Deutsche Telekom has faced intense price competition that resulted in drastic declines in prices and in Deutsche Telekom's market share from 1998 through 2000, particularly in the areas of international and domestic long-distance calls. In addition, competition in the markets for regional and local calls and for access is intensifying. The level of competition is significantly influenced by decisions of the German telecommunications regulator, and the regulator could take decisions that would lead to further declines in prices, market share or both in the fixed-network voice telephony business. All of these developments may result in lower revenues and profits from fixed-network voice telephony in the future. For further information regarding competition and regulatory decisions that affect the level of competition, see ''Item 4. Information on the Company — Description of Business Segments — T-Com — Competition'' and ''Item 4. Information on the Company — Regulation.''

In the mobile communications business, Deutsche Telekom faces intense competition in all of its principal markets (Germany, the United States, the United Kingdom and Austria). Although competition based on handset subsidies has diminished in Germany, the United Kingdom and Austria, competition based on price, subscription options offered, coverage and service quality remains intense. As these markets have become increasingly saturated, the focus of competition is starting to shift from customer acquisition to customer retention. Since customer acquisition and retention expenses are substantial, significant customer defections would have an adverse effect on results of operations. Prices for mobile voice telephony have been declining over the past several years and may continue to decline in Deutsche Telekom's principal markets. In the less saturated market for mobile communications in the United States, Deutsche Telekom's mobile communications subsidiaries face significant competitive challenges, as described in greater detail below. Competition in any of Deutsche Telekom's principal markets for mobile telecommunications services may have an adverse effect on Deutsche Telekom's future financial condition and results of operations.

In the area of information technology and telecommunications systems solutions, Deutsche Telekom faces intense competition. In the information technology business, which Deutsche Telekom entered in October 2000 with its acquisition of a controlling interest in debis Systemhaus, Deutsche Telekom faces competition from a number of well-established market participants. In the telecommunications systems business, prices have been declining over the past several years as a result of intense competition and could continue to decline. Although Deutsche Telekom expects a market to develop for ''convergence'' products that combine information technology and telecommunications systems and expects to be well-positioned in this market, this market could develop more slowly than expected, which could have an adverse effect on Deutsche Telekom's future financial condition and results of operations.

Deutsche Telekom also faces intense competitive pressure in the market for Internet and multimedia services. In the market for providing of Internet access services, in addition to the challenges posed by competitors, Deutsche Telekom's competitive position may be influenced by regulation, particularly in Germany. In the market for portal services, competition is intense due to low barriers to entry.

Competition in any or all of Deutsche Telekom's principal lines of business could lead to:

- Price erosion on Deutsche Telekom's products and services;
- Inability to increase market share or loss of market share;
- Loss of existing or prospective customers and greater difficulty in retaining existing customers;
- More rapid deployment of new technologies and obsolescence of existing technologies;

and other developments that could have a material adverse effect on Deutsche Telekom's financial condition and results of operations.

Deutsche Telekom may not be able to realize the benefits expected from its investment in UMTS licenses and related capital expenditures.

Deutsche Telekom has invested more than EUR 15 billion in UMTS licenses and expects to invest substantial amounts over the next several years in the construction of UMTS networks. The economic success of these investments will depend on the availability of services based on UMTS technology that will be attractive enough to customers to generate sufficient traffic volume at sufficiently high prices. The level of demand for such UMTS services that will prevail in the future is unknown, however, and may not justify the cost of providing UMTS services. These costs include the costs of acquiring UMTS licenses, the costs of constructing, maintaining and upgrading UMTS networks, the costs of promoting demand for UMTS services through advertising, handset subsidies and other promotional measures and the costs of purchasing content for UMTS-based services in a competitive environment. The level of demand for UMTS services could be adversely affected by an early, unsuccessful launch of UMTS services by competitors. In addition, any delays in providing UMTS services, whether due to problems associated with suppliers of UMTS network components, difficulties in network construction, unavailability of adequate UMTS-compatible handsets, failure to fulfill criteria specified in UMTS licenses or other factors, could adversely affect the level or timing of revenues generated by UMTS services. Deutsche Telekom can not provide any assurance of an economic return on UMTS licenses and networks, or even that such investments will be recovered, or as to the timing of any returns on these investments. If Deutsche Telekom were to find in the future that its current expectations concerning future cash flows from UMTS services are not likely to be met, the carrying value of its UMTS licenses would be adversely affected. For further information in this regard, see "Item 5. Operating and Financial Review and Prospects — Critical Accounting Policies under German GAAP — Accounting for Long-Lived Assets." In the event that these investments do not generate significant revenue or do not do so in the time period currently envisioned, this could have a material adverse effect on Deutsche Telekom's financial condition and results of operations.

Deutsche Telekom may not be able to realize the benefits expected from its investment in VoiceStream and Powertel and other subsidiaries.

In May 2001, Deutsche Telekom acquired VoiceStream and Powertel in exchange for Deutsche Telekom shares having a market value on the acquisition date of EUR 28.7 billion plus EUR 4.9 billion in cash. Amortization of goodwill, and depreciation and amortization of assets acquired in this transaction, will have a substantial impact on Deutsche Telekom's results of operations in the coming years. In addition, Deutsche Telekom expects VoiceStream and Powertel to incur significant operating losses and to generate negative cash flows from operating activities for the foreseeable future while they continue to develop their networks and grow their subscriber bases. VoiceStream and Powertel face intense competition from other mobile communications companies that have larger U.S. market shares and significant financial resources and that are likely targeting the same customers as VoiceStream and Powertel target. Licenses that VoiceStream and Powertel need to offer planned services are limited in number, may be difficult to obtain, are currently subject to some degree of legal uncertainty and, in some cases, are owned through joint ventures that VoiceStream and Powertel do not control. VoiceStream and Powertel currently do not have licenses covering the entire United States and currently can not offer nationwide roaming in the United States due to the absence of a common mobile communications standard and the absence of commercially available dual-band handsets that permit roaming with a single handset among GSM networks and networks using different standards. In addition, mobile phone penetration rates in the United States, which currently are low relative to those in Europe, may not grow as rapidly as Deutsche Telekom anticipates, or Deutsche Telekom may fail to capture as much market share in the United States as currently is anticipated. If Deutsche Telekom were to find in the future that its current expectations concerning future cash flows from its investment in VoiceStream are not likely to be met, the carrying value of that investment would be adversely affected. For further information in this regard, see "Item 5. Operating and Financial Review and Prospects — Critical Accounting Policies under German GAAP — Accounting for Long-Lived Assets" and "— Valuation of Goodwill". These factors could have an adverse effect on VoiceStream and Powertel's success in competition in the United States and consequently on Deutsche Telekom's financial condition and results of operations.

In addition to VoiceStream and Powertel, Deutsche Telekom has made substantial investments in other subsidiaries and associates in both the telecommunications business or the information technology business during the past several years. Deutsche Telekom may not be able to recover all of the acquisition costs relating to those entities or all of the further capital expenditures made with respect to those entities.

Business may be adversely affected by inability to introduce new services to stimulate network usage.

To offset revenues lost due to increased competition and lower prices, Deutsche Telekom's strategy has been to introduce new services in both its fixed-network business and its mobile communications business in order to increase traffic on its network and to secure alternative sources of revenue. In particular, Deutsche Telekom's strategy is based on attaining strong growth rates in certain areas, particularly in mobile data communications, in services combining data communications and information technology and in the area of Internet services. If these markets do not grow as rapidly as expected, or if Deutsche Telekom is unable to win and maintain significant market share in these markets, Deutsche Telekom's future financial condition and results of operations may be adversely affected.

Deutsche Telekom operates in highly regulated markets in which its flexibility to manage its business is limited, and regulatory decisions and changes in the regulatory environment may adversely affect Deutsche Telekom's business.

Deutsche Telekom's fixed-network and mobile communications operations are subject to extensive regulatory requirements in Germany, and its international operations are subject to regulation in their host countries. In Germany, the German telecommunications regulator considers Deutsche Telekom to have a dominant position in certain markets, which imposes significant additional limits on Deutsche Telekom's flexibility to manage its business. In particular, significant parts of Deutsche Telekom's fixed-network business in Germany are subject to requirements that Deutsche Telekom:

- Submit its tariffs for prior regulatory approval or retrospective regulatory review;
- Offer competitors access to its network and to its subscriber access lines at rates that are set by the German telecommunications regulator; and
- Offer universal services in certain markets.

For detailed information regarding these requirements and other aspects of the regulatory regimes to which Deutsche Telekom's business is subject, see "Item 4. Information on the Company — Regulation." Deutsche Telekom is unable to predict the impact of any proposed or potential changes in the regulatory environment in which it operates in Germany and internationally, and any such changes could adversely affect Deutsche Telekom's business and competitiveness.

Technological change could increase competition, render existing technologies obsolete or require Deutsche Telekom to make substantial additional investments.

Deutsche Telekom's services are technology-intensive, and the development of new technologies could render Deutsche Telekom's services non-competitive and require Deutsche Telekom to write-down the book values of investments it has made in existing technologies. Deutsche Telekom is already making substantial investments, and may have to make substantial additional investments, in new technologies in order to remain competitive. New technologies that Deutsche Telekom chooses to acquire may not prove to be successful. In addition, Deutsche Telekom may not receive the necessary licenses to provide services based on new technologies in Germany or abroad. As a result, Deutsche Telekom could lose customers, fail to attract new customers or incur substantial costs to maintain its customer base.

Deutsche Telekom currently has a high level of total debt.

Deutsche Telekom's total debt amounted to EUR 67.0 billion at December 31, 2001, as shown in the consolidated financial statements. Moody's Investor Service and Standard & Poors Ratings Services downgraded their ratings of Deutsche Telekom's long-term debt in March 2002 and in April 2002, largely due to the level of Deutsche Telekom's indebtedness. Deutsche Telekom cannot offer assurances that it will be able to reduce its indebtedness as rapidly as currently is envisioned.

Alleged health risks of wireless communications devices have led to litigation affecting Deutsche Telekom and could lead to decreased wireless communications usage or increased difficulty in obtaining sites for base stations.

Media reports have suggested that radio frequency emissions from wireless handsets and cell sites may raise various health concerns, including cancer, and may interfere with various electronic medical devices, including hearing aids and pacemakers. Research and studies are ongoing. Whether or not such research or studies conclude there is a link between radio frequency emissions and health, these concerns over radio frequency emissions may discourage the use of wireless handsets and may result in significant restrictions on the location and operation of transmission facilities and antennae "base stations", either or both of which could have a material adverse effect on Deutsche Telekom's mobile communication services business.

One of Deutsche Telekom's subsidiaries, VoiceStream, is subject to current litigation relating to these health concerns. Several class action lawsuits have been filed against VoiceStream, several other wireless service operators and several wireless phone manufacturers, asserting product liability, breach of warranty and other claims relating to radio frequency transmissions to and from wireless handsets. The complaints seek substantial monetary damages as well as injunctive relief. The defense of these lawsuits may divert management's attention, and VoiceStream may be required to pay significant awards and may incur significant expenses in defending these lawsuits. In addition, VoiceStream could be subject to potential litigation, legislation or adverse publicity relating to damage caused by persons who use mobile telephones while driving.

Deutsche Telekom cannot offer assurance that legislators, regulators or private litigants will refrain from taking other actions adverse to Deutsche Telekom based on purported health-related risks associated with radio frequency emissions.

Deutsche Telekom is continuously involved in other disputes and litigation with regulators, competitors and other private parties which, if determined against Deutsche Telekom, may have material adverse effects on the company.

For information concerning litigation in which Deutsche Telekom is involved, see "Item 8. Financial Information — Litigation." For information concerning Deutsche Telekom's regulatory environment, see "Item 4. Information on the Company — Regulation."

System failures could result in reduced user traffic and reduced revenue and could harm Deutsche Telekom's reputation.

Deutsche Telekom's technical infrastructure (including its network infrastructure for fixed-network services and mobile telecommunication services) is vulnerable to damage or interruption from information technology failures, power loss, floods, windstorms, fires, intentional wrongdoing and similar events. Unanticipated problems at its facilities, system failures, hardware or software failures or computer viruses could affect the quality of Deutsche Telekom's services and cause service interruptions. Any of these occurrences could result in reduced user traffic and reduced revenue and could harm Deutsche Telekom's reputation.

Fluctuations in currency exchange rates may adversely affect Deutsche Telekom's reported results.

Deutsche Telekom has made substantial international investments outside of the Euro zone, principally in the United States, the United Kingdom and Eastern Europe. Deutsche Telekom has raised, and may in the future raise, a substantial amount of financing in currencies other than the Euro, principally the U.S. dollar and the British pound. Accordingly, the value of those liabilities will be affected by fluctuation of the Euro against the currency in which the financing is denominated.

In addition, currency risk may arise from dividends received from its international affiliates as well as cash provided by Deutsche Telekom for the needs of its affiliates.

Deutsche Telekom generally enters into a number of currency derivative transactions to manage foreign currency risk, including risk with respect to its non-Euro denominated liabilities. Deutsche Telekom can give no assurances, however, that it will be successful in managing its foreign currency risk exposure.

Loss of key personnel could weaken Deutsche Telekom's business expertise.

The loss of key personnel could significantly impede Deutsche Telekom's financial plans, marketing and other objectives. Deutsche Telekom believes that the growth and future success of its business will depend in large part on its continued ability to attract and retain highly skilled and qualified personnel at all levels. The competition for qualified personnel in the telecommunications industry is intense. Deutsche Telekom can give no assurances that it will be able to hire or retain necessary personnel.

Future sales of Deutsche Telekom shares by the government of the Federal Republic of Germany or by Deutsche Telekom may adversely affect the trading price of Deutsche Telekom shares and ADSs.

The Federal Republic of Germany (the "Federal Republic"), together with the Kreditanstalt für Wiederaufbau ("KfW"), a public-sector entity 80 percent owned by the Federal Republic, owned approximately 43 percent of the shares of Deutsche Telekom at December 31, 2001. The Federal Republic has publicly announced that it intends to further reduce its holdings of Deutsche Telekom shares as market conditions permit. Deutsche Telekom has authorized conditional capital of 195.3 million shares to be used in connection with future issuances of convertible bonds. The sale or the potential sale of further Deutsche Telekom shares by the Federal Republic of Germany or by Deutsche Telekom could have an adverse impact on the market price of Deutsche Telekom's shares and ADSs.

Changes in the composition of stock indices of which Deutsche Telekom shares are a component could cause material fluctuations in the market price of Deutsche Telekom shares.

Deutsche Telekom's shares are a component of several important stock indices, including the Deutscher Aktienindex (or "DAX"), an index of the thirty largest German companies, and Euro STOXX 50, an index of fifty large European companies. The Deutsche Börse AG has announced that by June 2002 the companies' weighting for the DAX will be based on a free float criterion. This will reduce the weighting of Deutsche Telekom shares in the DAX with effect as of September 20, 2002 as part of the regularly quarterly index rebalancing. Since a significant number of institutional investors adjust their stock portfolios to correspond to the composition of important stock indices, changes in the weighting of Deutsche Telekom shares in these indices have led to fluctuations in the Deutsche Telekom share price in the past and could cause similar fluctuations in the future.

The adoption by Deutsche Telekom of new accounting standards for purposes of U.S. GAAP may have a significant adverse effect on Deutsche Telekom's U.S. GAAP financial results.

In June 2001, the U.S. Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") 141, "Business Combinations," and SFAS 142, "Goodwill and Other Intangible Assets." SFAS 141 requires that under U.S. GAAP the purchase method of accounting be used for all business combinations initiated after June 30, 2001, and changes the criteria for recognizing intangible assets apart from goodwill. SFAS 142 addresses how purchased intangibles should be accounted for upon acquisition. The statement prescribes the necessary accounting for both identifiable intangibles and goodwill after initial recognition. SFAS 142 requires that goodwill and indefinite lived intangible assets no longer be amortized upon adoption of this statement, but instead be tested for impairment at least annually using the specific guidance and criteria described in the statement. Amortization of definite lived intangibles will continue over their useful lives. For U.S. GAAP reporting, the provisions of SFAS 141 apply to all business combinations initiated after June 30, 2001. For U.S. GAAP reporting, the provisions of SFAS 142 are required to be applied starting with fiscal years beginning after December 15, 2001, except for the nonamortization provisions for goodwill and indefinite-lived intangible assets acquired after June 30, 2001, which will be subject immediately to provisions of this statement. Deutsche Telekom is currently assessing the impact of this standard on its results of operations and financial position. Any material impairment of goodwill recognized under these standards will adversely affect Deutsche Telekom's results of operations and shareholders' equity under U.S. GAAP.

As a result of the implementation of SFAS 142, a number of major wireless carriers in the United States have concluded that the U.S. Federal Communications Commission ("FCC") wireless spectrum licenses should be considered to be intangible assets with indefinite lives under SFAS 142. Classification by Deutsche Telekom of its FCC licenses as indefinite lived would require scheduled amortization of licenses to cease commencing January 1, 2002 and trigger a number of related issues, the treatment of which is currently being evaluated. These issues include the method of testing for impairment and accounting for deferred income taxes related to the change to indefinite lives. Prior to January 1, 2002, these licenses were treated as intangibles with definite lives and the reversal of their related deferred tax liabilities was deemed to match the realization of the deferred tax assets and, as such, no valuation allowance for the deferred tax asset was necessary. If it is concluded that the FCC licenses are indefinite, however, subsequent to January 1, 2002, the deferred tax liabilities associated with these licenses would no longer be available to support the realization of the VoiceStream and Powertel deferred tax assets or future deferred tax assets because of the resulting indefinite timing of the reversal of such deferred tax liabilities. Therefore, a reassessment of the useful lives of the licenses would require Deutsche Telekom for U.S. GAAP purposes to record a valuation allowance with a corresponding charge to earnings of EUR 4.3 billion in the first quarter of 2002 relating to all of the

VoiceStream and Powertel deferred tax assets. These deferred tax assets were recorded in respect of net operating loss carryforwards assumed upon the acquisition of VoiceStream and Powertel in May 2001. Deutsche Telekom is considering whether the change in the amortization of the FCC licenses for U.S. GAAP purposes should have any implications on its net income under German GAAP as well.

ITEM 4. Information on the Company

HISTORICAL BACKGROUND

Historically, the provision of public telecommunications services in Germany was a state monopoly as formerly provided by the German constitution. In 1989, the Federal Republic began to transform the postal, telephone and telegraph services administered by the former monopoly provider into market-oriented businesses and divided the former monopoly provider into three distinct entities along lines of business, one of which was the predecessor of Deutsche Telekom. At the same time, the Federal Republic also started the progressive liberalization of the German telecommunications market. Deutsche Telekom was transformed into a private law stock corporation at the beginning of 1995.

Deutsche Telekom's most significant investment projects during the 1990's were the expansion and modernization of the telecommunications infrastructure in the former East Germany, starting with German reunification in 1990, and the digitization of its entire telecommunications network, starting in the early 1990's. Both of these projects were completed during 1997.

The telecommunications sector in Germany was fully liberalized on January 1, 1998. Deutsche Telekom now faces intense competition and is required to offer competitors access to its fixed-line network at regulated interconnection rates. The operation of networks (including cable networks) for all telecommunications services other than public fixed-line voice telephony were fully opened to competition on August 1, 1996.

Other important events in the development of Deutsche Telekom's business include:

- the formation of the Global One joint venture with France Telecom and Sprint in 1996 and the formation of a cooperation agreement with France Telecom in 1998;
- the dissolution of the Global One joint venture and the cooperation agreement with France Telecom in 2000 and the disposition of Deutsche Telekom's shares in Sprint in 2001;
- the expansion of Deutsche Telekom's business in Eastern Europe through the acquisition in 1993 of a substantial interest in MATAV, the Hungarian national telecommunications company, and the acquisition of telecommunications subsidiaries in Slovakia, Macedonia, the Czech Republic and Croatia from 2000 to 2001; and
- the acquisition of One 2 One (now T-Mobile UK) in 1999, debis Systemhaus in 2000 and VoiceStream and Powertel in 2001.

STRATEGY

Deutsche Telekom's objectives for the coming years are to build on its position as a leading telecommunications provider in Europe and to secure its place among the world's leading telecommunications companies, with the overall aim of generating attractive returns for its shareholders.

To accomplish these strategic goals, Deutsche Telekom has organized its businesses into four main divisions or "pillars": T-Com (for network access and services), T-Mobile (for mobile communications), T-Systems (for data communications and systems solutions for large business customers) and T-Online (for consumer Internet services). In its strategy, Deutsche Telekom is focused on opportunities presented by the convergence that has already begun and is expected to continue between the traditionally distinct businesses of telecommunications, information technology, media, entertainment and security services.

Assuming that current market developments continue, the evolution of technologies will be strongly influenced by the convergence of telecommunications, media and information technology. Deutsche Telekom is entering areas where such convergence is taking place and is fostering cooperation between different strategic "pillars" to reduce the time-to-market of convergent products and services, with the goal of outperforming competitors in these areas. Deutsche Telekom's principal focus in these areas will be on the convergence of:

- content/media and telecommunications;
- telecommunications and information technology; and
- fixed and mobile telecommunications.

In addition, Deutsche Telekom aims to capitalize on potential synergies generated by its recent growth, in areas such as global sourcing, billing and centralization of the carriers' carrier business.

Deutsche Telekom regularly assesses its assets to determine whether those assets fit within its ongoing business strategy and has embarked on a strategy of disposing of non-core assets, such as its cable television business and its real estate holdings.

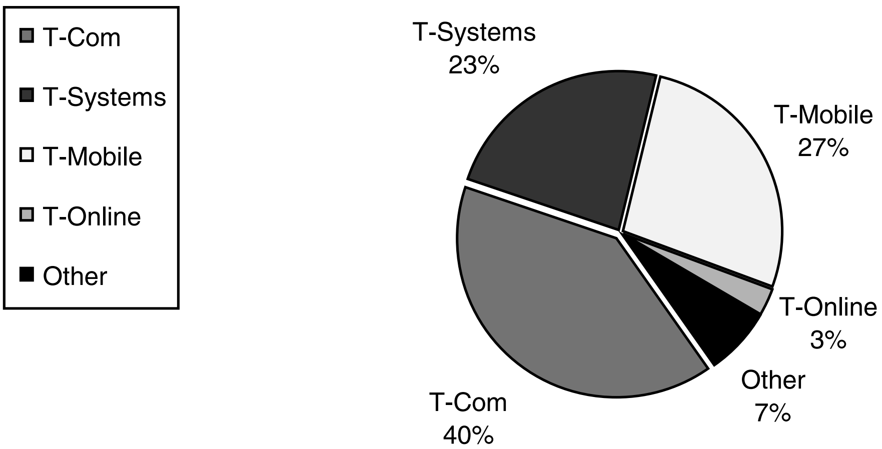
While Deutsche Telekom is focusing on the integration of businesses acquired over the past several years, it continues to evaluate business opportunities and may continue to make acquisitions and investments on a selective basis. Acquisitions and investments may be made using newly issued shares of Deutsche Telekom or its affiliates, cash or a combination of cash and shares, and may individually or in the aggregate be material to Deutsche Telekom or its affiliates. Discussions with third parties may be commenced, on-going or discontinued at any time.

DESCRIPTION OF BUSINESS SEGMENTS

Deutsche Telekom's objectives for the coming years are to build on its position as a leading telecommunications provider in Europe and to secure its place among the world's leading telecommunications companies, with the overall aim of generating attractive returns for its shareholders. To accomplish its objectives, Deutsche Telekom is developing its business with a focus on four strategic divisions:

- T-Com (Network access and services);
- T-Mobile (Mobile telecommunications);
- T-Systems (Data communications and systems solutions); and
- T-Online (Consumer Internet services).

The following chart shows revenues from each of Deutsche Telekom's divisions for 2001 expressed as a percentage of consolidated net revenues for that year.



Approximately 27.3 percent of Deutsche Telekom's revenues in 2001 were derived from activities outside Germany. For a breakdown of revenues by geographic region, see note 1 to the consolidated financial statements.

T-Com

Principal Activities

The principal services offered by T-Com are narrow and broadband access to T-Com's fixed-line telecommunications network and domestic and international public fixed-network voice telephony services for individual customers and small to medium-sized enterprises. T-Com also provides interconnection services for other domestic network operators; provides services and solutions in the field of data communications to small and medium-sized enterprises; sells, leases and services telecommunications equipment to its target customers and provides other ancillary telecommunications services. In addition, T-Com is responsible for Deutsche Telekom's cable television operations pending the planned sale of those operations. For further information in this regard, see "— Broadband Cable."

Through 2001, MATAV, Slovak Telecom and Croatian Telecom were accounted for under "other activities" of Deutsche Telekom rather than under the T-Com segment. Starting in 2002, however, these companies will be accounted for under the T-Com segment. For further information regarding these companies, see " — Other Activities – International Activities."

Network Access

T-Com offers access to its transmission network for individual customers and small to medium-sized enterprises. Typically, T-Com customers have access to the transmission network by means of a copper wire that runs from the transmission network into the home or office of a customer. These access lines can either be standard analog access lines or digital access lines. Digital access lines also are called "Integrated Services Digital Network" or "ISDN" lines. In addition, analog and digital access lines can be enhanced by means of "asymmetric digital subscriber line" or "ADSL" technology, which T-Com markets under the brand name "T-DSL". T-Com offers its customers a variety of tariff plans that generally consist of a monthly fixed payment for access and a variable, usage-based component.

Analog Access Lines. An analog access line provides a single telecommunications channel. At December 31, 2001, approximately 30 million customers were connected to T-Com's transmission network by means of standard analog access lines, marketed under the brand name "T-Net".

ISDN Access Lines. T-Com offers two types of ISDN access lines: basic and primary. Basic ISDN access lines, which provide two telecommunications channels per access line, are offered both to individual customers and to small to medium-sized enterprise customers, while primary ISDN access lines, which provide thirty telecommunications channels per access line, are offered primarily to small to medium-sized enterprise customers. At December 31, 2001, T-Com had installed approximately 8.6 million basic ISDN access lines and approximately 105,000 primary ISDN access lines, together representing approximately 20.4 million ISDN channels at that date. ISDN is marketed under the brand name "T-ISDN".

ISDN permits a single access line to be used for multiple purposes simultaneously, including voice and video telephony, data and facsimile transmission. ISDN also provides higher quality connections with faster transmission of signals and increases the capacity of the access network. T-Com offers ISDN access lines throughout Germany and has the largest ISDN network in the world, measured in terms of access lines. Increasing the ISDN penetration rate is an important part of T-Com's strategy.

T-DSL. ADSL is a telecommunications technology that permits the transmission of data at very high speeds using a standard access line. The T-Com division offers standard analog and ISDN access lines enhanced by means of ADSL technology under the brand name "T-DSL". At December 31, 2001, over 2.2 million customers had placed orders with T-Com for T-DSL, and 2.0 million customers had received T-DSL connections at that date. One of the principal benefits of ADSL technology for T-Com is that it permits customers to use their standard access lines for high-speed access to the Internet. Since Deutsche Telekom expects the Internet to grow in importance as a means of communication in the future, Deutsche Telekom considers continued growth in the number of T-DSL access lines to be an important strategic priority. For a description of regulatory proceedings that may have an impact on continued growth in the number of T-DSL access lines, see "— Regulation."

Calling Services

T-Com provides comprehensive local calling services as well as national and international long-distance calling services for customers that have access to T-Com's fixed-line network. For connecting customers to one another on its network, or connecting customers who place a call from T-Com's network to the network of another network operator, T-Com charges customers tariffs that are in general proportional to the duration of the call and to the distance traveled by the call. These tariffs generally are higher during peak calling hours than during off-peak calling hours.

Under the regulatory framework applicable to the German telecommunications sector, T-Com's tariffs for fixed-network calling services are subject to regulatory approval for so long as Deutsche Telekom is considered to be a market-dominant provider. For further information in this regard, see "— Regulation."

Following the complete liberalization of Germany's telecommunications market in 1998, Deutsche Telekom's tariffs for fixed-network calling services have declined dramatically, primarily as a result of action by the German telecommunications regulator that has significantly reduced the rate that other telecommunications providers are required to pay to T-Com for interconnection with T-Com's network. Future reductions in the interconnection rate mandated by the regulator could cause further declines in the rates that T-Com can charge for fixed-network calling services. For further information in this regard, see "— Competition" and "— Regulation."

Special Service Offerings for Business Customers

During 2001, T-Com continued its marketing efforts for virtual private network solutions for small to medium-sized business customers under the brand name "T-VPN". The T-VPN package consists of value-added modules that can be combined in different configurations to produce applications that are tailored to the needs of particular customers. T-Com also offers special tariff packages that are tailored to the needs of business customers.

Data Services

T-Com offers small and medium-sized business customers many of the data communications services that T-Systems offers to large business customers. The services include leased lines, Internet and Intranet communications applications under the brand name "T-InterConnect" and local area networks under the brand name "T-LAN". T-Com also offers, under the brand name "Telekom Designed Networks", communications solutions that are tailored to specific customer requirements. These solutions involve design and installation of communications networks, network management and ongoing services.

Carrier services

With effect as of January 1, 2002, revenues of the national carrier services business will be reflected in the revenues of the T-Com division. For periods ending on or prior to December 31, 2001, however, the revenues of the national carrier services business are reflected in the revenues of the T-Systems division, and the revenues of the T-Com division include the revenues of Deutsche Telekom's international carrier services business. For further information on the national and international carrier services businesses of Deutsche Telekom, see "— Domestic and International Carrier Services."

Broadband Cable

To begin placing its cable business on a new economic and regulatory footing, Deutsche Telekom created nine indirect regional subsidiaries in 2000 to operate the cable business of Deutsche Telekom. Deutsche Telekom sold majority interests in the regional cable companies for the German states of North Rhine-Westphalia and Hesse during 2000 and Baden-Württemberg during 2001.

At December 31, 2001, Deutsche Telekom indirectly was the 100 percent owner of six regional cable companies that offer cable television service to approximately 75 percent of the geographic area of Germany and approximately 58 percent of the population of Germany. In addition, at that date, Deutsche Telekom indirectly owned a 45 percent interest in the regional cable company that provides service to the German state of North Rhine-Westphalia, a 35 percent interest in the regional cable company that provides service to the German state of Hesse and a 40 percent interest in the regional cable company that provides service to the German state of Baden-Württemberg. In September 2001, Deutsche Telekom granted options to the majority shareholder to acquire the remaining equity interests of Deutsche Telekom in the regional companies for North Rhine-Westphalia and Baden-Württemberg. In the regions where Deutsche Telekom indirectly still owns 100 percent of the regional cable company, Deutsche Telekom directly or through its subsidiaries provides cable transmission services and markets digital program packages.

Due to objections raised by the German antitrust authority, the planned sale of the remaining six wholly-owned regional cable companies by Deutsche Telekom to Liberty Media was cancelled in February 2002, Deutsche Telekom continues to seek purchasers for controlling interests in these companies and will continue to operate these companies until purchasers are found.

Terminal Equipment

Through its terminal equipment business area, T-Com distributes an extensive range of telecommunications equipment, ranging from individual telephone sets and facsimile machines targeted at private customers to more complex telephone and facsimile terminals, private branch exchanges (PBXs) and complex network systems targeted at business customers. With most of T-Com's terminal equipment, customers have the choice of purchasing or leasing. T-Com also provides installation and repair services.

Service

Installation, maintenance, service hotlines, customer education, software installation and network management are important parts of T-Com's business activities. Standardized service levels are offered to individual customers under the brand names Compact-Service and Comfort-Service. Customized services are offered to business customers.

Other Services

Through T-Com, Deutsche Telekom offers a range of sales and service phone numbers for business and private use, provides directory assistance, has state-of-the-art call centers and offers messaging services. In addition, the value-added services business area manages Deutsche Telekom's network of public telephones and produces telephone directories as well as prepaid calling cards. This business area is also responsible for providing customers with comprehensive solutions to their telecommunications-based marketing needs.

Principal Markets

T-Com offers its services and products to individuals and small to medium-sized business enterprises located in Germany. Most of T-Com's revenues in 2001 were derived from telephony services provided within Germany. In addition, in 2001, T-Com offered wholesale products to domestic network operators as well as to carriers worldwide.

Seasonality

The business of the T-Com division is not materially affected by seasonal variations.

Suppliers

The principal goods and services purchased by the T-Com division are network components such as switching systems, transmission systems, access network components and customer premises equipment such as telephones and fax machines, T-DSL modems and similar items. Deutsche Telekom does not believe that T-Com is dependent on any single supplier, due to the multiple suppliers strategy implemented by Deutsche Telekom. Major suppliers of T-Com are Alcatel, Cisco Systems, Corning, ECI, Lucent Technologies and Siemens.

Marketing

The T-Com division markets its products and services to individual and small business customers principally through Deutsche Telekom's network of "T-Punkt" sales outlets. In 1998, T-Com began implementation of a program to redesign its T-Punkt outlets, and over 300 outlets in the new design had been opened by December 31, 2001. In addition, the number of "megastores" in the centers of major cities was increased to 16 during the year, and 68 of the planned "T-Punkt Business" outlets that are oriented primarily toward business customers had been opened by the end of the year. Deutsche Telekom expects to have completed the redesign program by the end of 2002 and to have a total of approximately 500 "T-Punkt" stores.

In addition to the T-Punkt outlets, T-Com markets its products and services through a broad range of sales partners; provides a single, toll-free number where customers can obtain information and order products and services 24 hours a day, seven days a week; and markets products and services through a catalog published semi-annually and through its homepage.

T-Com also serves small and medium-sized enterprises by a direct sales force. This sales force operates from 39 locations throughout Germany.

Dependence on Patents, Licenses, Customers, Industrial, Commercial or Financial Contracts

Deutsche Telekom does not believe that T-Com is dependent on any patent. For a description of patent infringement litigation that is relevant for T-Com's business, see "Item 8. Financial Information — Litigation — Other Proceedings."

For offering fixed line telephony and cable network services, T-Com requires and therefore is dependent on licenses for the operation of transmission lines for public telecommunication services (Class 3 licenses) and for the provision of voice telephony services to the public on the basis of self-operated telecommunication networks (Class 4 licenses). For further information on those licenses, see "— Regulation — Licensing and Notification Requirements; Allocation of Frequencies."

Deutsche Telekom does not believe that T-Com is dependent on any individual third party customer, or on any industrial, commercial or financial contract.

Competition

Fixed Network Voice Telephony and Local Access

Since the full liberalization of the German telecommunications market in January 1998, Deutsche Telekom has faced intense competition, based primarily on price, in the market for fixed-network voice telephony.

Effect of regulatory decisions. In the market for international and domestic long-distance calling services, the level of competition is influenced by the fact that Deutsche Telekom is required by law to permit other telecommunications companies to interconnect with Deutsche Telekom's fixed network at rates that are fixed by the German telecommunications regulator. As a result, decisions of the German telecommunications regulator regarding the maximum rate that Deutsche Telekom is permitted to charge for interconnection have a very significant impact on the level of competition in the market for fixed-network voice telephony. When the maximum permitted interconnection rate is below the price charged by T-Com for calling services, competitors can interconnect with T-Com's network and offer calling services for a lower price, forcing T-Com to lower its prices for calling services. The price structure for interconnection rates particularly benefits those competitors that have not made substantial investments in their own infrastructure. As a result of several decisions of the German telecommunications regulator between 1998 and 2000 that reduced the maximum permitted interconnection rate, Deutsche Telekom has reduced its tariffs substantially from 1998 through 2000, particularly in the areas of international and domestic long-distance calls. Deutsche Telekom's share of the market for international and domestic long-distance calls declined from approximately 100 percent in 1997 to approximately 60 percent in 2000. Deutsche Telekom also had to lower its prices and surrender market share in the market for domestic regional calls, although to a lesser extent. Although Deutsche Telekom's market share in these markets remained relatively stable during 2001, further decisions of the German telecommunications regulator could require Deutsche Telekom to lower its prices further, cause Deutsche Telekom to lose additional market share, or both. In October 2001, the German telecommunications regulator issued a decision that would effectively reduce the permitted interconnection rate by an average of 14 percent. For further information regarding this decision, see "— Regulation."

Regulatory decisions also play a decisive role in the level of competition in the markets for regional and local calls and for local access. T-Com is required by law to rent its subscriber access lines to competitors at prices determined by the German telecommunications regulator. Recently, Deutsche Telekom was required to permit "line sharing", which means renting to a competitor only that portion of the subscriber access line that is required for high-bandwidth services, such as high-speed Internet access. Due to a decision of the German telecommunications regulator, Deutsche Telekom also is required to offer local access and local call minutes to competitors at wholesale prices for purposes of resale. In addition, the German government has recently agreed on draft legislation that would mandate preselection and call-by-call for local calls by December 2002. T-Com expects that competitors will begin to offer those services in 2003, although no time schedule has yet been fixed. For further information in this regard, see "— Regulation — Special Network Access and Interconnection — Fixed-Fixed Interconnection."

Further regulatory initiatives of Germany or the European Union aimed at increasing competition in the markets for local calls and for access may be expected in the coming years. For further information on these regulatory requirements and initiatives, see "— Regulation." All of these decisions and initiatives are likely to cause intensified competition in the markets for local calls and for access in the coming years.

Effect of investments by other companies. Deutsche Telekom also faces significant competition in the markets for international and domestic long-distance and regional calls from competitors that have made investments in their own infrastructure, such as Arcor, Colt, MCI Worldcom and BT Ignite. In addition, national network operators, such as Arcor, and local network operators, such as Hanse Net and Net Cologne, have made substantial investments in local network infrastructure and compete with Deutsche Telekom in major urban centers throughout Germany.

Furthermore, as prices for mobile telephony decline, T-Com's local and other calling services face increasing competition from mobile telephones.

Other Services

Deutsche Telekom's decision to divide its broadband cable business into regional companies and to seek investors to assume majority ownership and operating control over those companies may in time lead to additional competition from parties seeking to provide telecommunications services, including access services, and multimedia services through a broadband cable network. Majority interests in three of these regional companies already have been sold to third party investors.

The terminal equipment sector has been open to full competition since 1990 and is characterized by falling prices, low margins, rapid technological innovation and intense competition. The basis for competition in this field is primarily price. T-Com's most significant competitors are Siemens, Alcatel, Philips and Tenovis (formerly Bosch Telecom/Telenorma). Most of these competitors are also suppliers to T-Com, since Deutsche Telekom does not manufacture its own terminal equipment.

T-Systems

Principal Activities

T-Systems is responsible for the major national and international business customers of Deutsche Telekom and offers these customers classic information technology and telecommunications services from a single source as well as integrated services involving the convergence of both of these markets. With its portfolio of services, T-Systems seeks to address all stages in the value chain of its customers, from suppliers of suppliers to customers of customers.

The activities of the T-Systems division are conducted by T-Systems International GmbH, a subsidiary of Deutsche Telekom that was created in 2000 from the business of former Deutsche Telekom group entities and the business of the former debis Systemhaus. Deutsche Telekom acquired a 50.1 percent equity interest in debis Systemhaus in October 2000 and the remaining 49.9 percent equity interest in the first quarter of 2002.

The organizational structure of T-Systems consists of "service lines" and "business lines". The service lines are grouped into the business areas "telecommunications services" and "information technology services."

Telecommunication Services

The business area telecommunications services includes the service lines "network services" and "hosting and ASP services" as well as the area "international carrier sales and services" and "global network factory." The principal tasks of the business area telecommunications services are the construction of a global network infrastructure for voice and data communications and the offering of a range of standardized services.

Network Services

Network services installs and operates customized communications networks for businesses, not-for-profit organizations and governmental agencies for voice and data communication. Projects for customers are realized on the basis of the global network of T-Systems. The solutions offered by network services thereby support communications within customers' organizations as well as customers' external communications (for example, with customers, suppliers and partners).

The services offered include the installation of networks covering a single customer location ("local area networks"), exclusive end-to-end communications lines between two customer locations ("leased lines") and complex virtual private networks, in which T-Systems uses its network to create virtual links between a number of geographically dispersed customer locations. T-Systems also offers virtual private networks based on the Internet. For a discussion of a regulatory proceeding affecting the pricing of virtual private networks, see "— Regulation."

Network services also creates customized voice communication networks for its customers and constructs complex call center solutions, that assist customers in professional management of their incoming calls, faxes and e-mails.

Contracts involving network services have an average duration of approximately three years. Voice services provided are billed on a per minute basis, while data services provided are billed in terms of bandwidth provided per month. Customers taking advantage of leased line services pay an initial connection fee based on the type of line leased and thereafter pay monthly subscription charges based on the type of line (analog or digital) and line capacity, the length of the line and the duration of the lease. Prices for leased lines have declined steadily in recent years due to intense competition.

Carrier Services

With effect as of January 1, 2002, the revenues of the international carrier services business will be reflected in the revenues of the T-Systems division. For periods ending on or prior to December 31, 2001, however, the revenues of the international carrier services business are reflected in the revenues of the T-Com division, and the revenues of the T-Systems division include the revenues of Deutsche Telekom's national carrier services business. For further information on the national and international carrier services businesses of Deutsche Telekom, see "— Domestic and International Carrier Services."

Global Network Factory

T-Systems operates an international network infrastructure called "Global Network Factory" as a platform for the telecommunications services offered to its business customers. T-Systems is actively engaged in expanding this network. Based on the progress of this expansion, Deutsche Telekom is currently in a position to offer its customers communications solutions in 40 countries.

Hosting and ASP Services

The services offered by Hosting and ASP services enable the customers of the T-Systems division to employ Internet technologies in their business processes. Hosting and ASP services arranges (or "hosts") the Internet presence of the customers by providing a reliable connection to the network and managing the customer's website. In addition, as an application service provider (or "ASP"), this service line rents to its customers the software that is needed for maintenance of an Internet presence and facilitates the updating of this software. This service line also offers electronic marketplaces and portals that enable enterprises to conduct business transactions electronically, either within a single industry or between enterprises from different industries. With these electronic marketplaces and portals, a T-Systems customer can facilitate its relationships with its suppliers ("supply chain management") or with its customers ("customer relationship management"). T-Systems thereby provides solutions that integrate its customers' trading transactions with the underlying business processes.

The services provided by Hosting and ASP services are also marketed by the T-Com division to its small and medium-sized business customers.

Contracts involving Hosting and ASP services have an average duration of approximately three years. Voice services provided are billed on a per minute basis, while data services provided are billed in terms of bandwidth provided per month.

Information Technology Services

The information technology business area possesses comprehensive expertise regarding computer software and hardware and information technology system solutions. This business area consists of computing and desktop services, systems integration and global computing factory.

Computing and Desktop Services

In the area of computing services, customers can outsource their entire information technology operations to T-Systems. The services offered in this area include the operation of data centers, application management, user support and network management and can even include the transfer of information technology assets and personnel from the customer to T-Systems. T-Systems also installs, operates and administers central computer systems (mainframes), open computer systems and business applications for customers. In the area of desktop services, T-Systems develops and implements for its customers complete office system solutions, desktop operations services, call centers and help desk services.

In general, contracts in the area of computing and desktop services have a long duration of four years or more. Customers pay for computing and desktop services based on contractually agreed service levels. These agreements describe quantities of goods to be provided and serviced (e.g., number of computers leased to the customer under the contract, computing power of the computers leased or memory capacity (in the case of large computers) and the extent of services to be provided).

T-Systems operates Europe's largest computer network, called ''Global Computing Factory'', as a platform for the information technology services offered to its customers. At the end of 2001, this network consisted of 37 computing centers and approximately 24,000 servers.

Systems Integration

Systems integration offers its customers consulting, implementation and applications support relating to system solutions in the area of communication and information technology. This service line has the expertise needed to develop software solutions customized for the needs of individual T-Systems customers and to integrate those solutions into the information technology and telecommunications structures of the customer. Examples of the services offered by the systems integration service line include solutions that assist customers in managing their business processes (e.g. supply chain management and customer relationship management solutions that enable business customers to use information technology and telecommunications to organize their relationships with suppliers and customers).

A fundamental component of the services offered are solutions that provide for security in telephone communications and electronic data transfers and for security of business data and installations.

Contracts in the area of systems integration have a duration of approximately one year on average and provide either for payment at the hourly rates of the T-Systems employees involved or for a fixed payment agreed in advance with the customer.

Media Broadcast

T-Systems offers broadcast services including traditional (analog) terrestrial broadcasting, satellite broadcasting and innovative digital applications. At December 31, 2001, the broadcast network of T-Systems included more than 8,000 analog television and radio transmitters and over 100 digital transmitters. Customers pay for media broadcast services based on fixed contracts with a duration of between four and six years.

Consulting

T-Systems offers its customers comprehensive consulting services in all service and business lines. These include management and technology consulting for customers in all lines of business regarding the use of information technology and telecommunications in all facets of their business, including supply chain management, business process optimization and modeling, customer relationship management as well as knowledge management. T-Systems' consulting services also include strategy, organization and technology consulting for companies which are primarily engaged in the information technology and telecommunications markets. Consulting services are an integral part of the service provided by each of the other service lines.

Principal Markets

At December 31, 2001, T-Systems served approximately 1,400 large business customers in the business lines of financial services, manufacturing, public and healthcare, retail and distribution, telecommunications and travel and transport. In addition, at that date, T-Systems served approximately 730 broadcasters and broadcasting content providers, as well as approximately 200 telecommunications carriers. The principal task of each of the business lines is to develop complete, customized solutions for individual T-Systems customers using the services provided by the service lines.

Financial services

The customers of the financial services business line primarily consist of banks and insurance companies. For example, the financial services business line develops solutions for bank customers that enable those customers to conduct banking transactions over the Internet and solutions for insurance company customers that enable those customers to manage their data electronically and to permit access to those data over the Internet or via mobile phone.

Manufacturing Industries

The manufacturing business line serves customers in all areas of manufacturing, including manufacturers of automobiles, aircraft and electronics and manufacturers of component parts used by other manufacturers. The services offered by this business line include, for example, electronic supply management, Internet marketplaces focused on specific industries and information technology outsourcing.

Public and Healthcare

The customers of the "public and healthcare" business line include governmental agencies, state pension funds, the armed forces of the Federal Republic of Germany, research and teaching institutions as well as international organizations such as NATO and the European Union. The services offered by this business line enable customers to establish innovative business processes. For example, this business line enables government agencies to provide services to citizens through the Internet. In the area of health care, this business line helps customers establish "health portals" for communication with their customers and manages data and voice networks for health insurers with thousands of employees.

Retail and Distribution

The customers of the retail and distribution business line come from such diverse areas of business as wholesale distribution, energy distribution, information technology service, lottery companies, print and broadcast media and the consumer goods industry. This business line offers, for example, billing solutions, shops for direct sales in the Internet and data bank systems.

Telecommunications

The customers of the telecommunications business line are other network operators and companies offering fixed-line, mobile and Internet telecommunications services. Services offered by this service line include content management systems for the organization of information on their websites and billing systems that facilitate billing transactions.

Travel and Transport

The travel and transport business line is responsible for enterprises in the areas of air transport, rail transport, logistics and tourism. Customers include airlines, airports, public transportation systems, international tour operators and logistics companies, hotel chains and rental car companies. Services offered by this service line include Internet-based reservation and booking systems and Internet portals.

Media Broadcast

The customers of the media broadcast business line include public broadcasters and private companies that provide content for broadcast media. See also "Principal Activities — Media Broadcast."

International Activities

At December 31, 2001, T-Systems was represented outside Germany by more than 10,000 employees in 20 countries, particularly in France, Italy, Spain, Austria, Switzerland, Brazil and South Africa. Of the revenues of the T-Systems division in 2001, 86% were derived from customers based in Germany, 12% from customers based in other Western European countries and 2% from customers based in other countries.

Seasonality

The business of the T-Systems division is not materially affected by seasonal variations.

Suppliers

The principal goods and services purchased by the T-Systems division are computer hardware for client server and mainframe, computer standard- and application-software, network capacity and network services, telecommunications network components and IT-Consulting services. Deutsche Telekom manages, on an enterprise level, the risk in the supplier relationship as well as quality and cost considerations. Deutsche Telekom does not believe that T-Systems is dependent on any single supplier.

Marketing

T-Systems' marketing activities are composed of account management (business line marketing) and technical management (service line marketing). The business line marketing area is organized by business sector (Financial Services, Public and Healthcare, Retail and Distribution, Travel and Transport, Manufacturing Industry, Telecommunications and Media Broadcast) and has overall responsibility for each customer. The technical management area brings specialized technical expertise to bear and is responsible for the individual products and services that serve as the basis for complete, customized solutions for individual T-Systems customers. Selling teams composed of members of both the business lines and the service lines establish and maintain close contact with the customers.

Dependence on Patents, Licenses, Customers, Industrial, Commercial or Financial Contracts

Some of the businesses of T-Systems are patent-intensive. Deutsche Telekom does not believe, however, that T-Systems is dependent on any individual patent, license or industrial, commercial or financial contracts.

DaimlerChrysler was the largest customer of the T-Systems division in 2001, accounting for approximately 5 percent of the external revenues of the division.

Competition

The principal competitors of T-Systems in the information technology area include IBM Global Services, EDS, CSC, Cap Gemini Ernst & Young, Siemens Business Service and Accenture. The principal competitors in the telecommunications area include MCI Worldcom, Cable & Wireless, AT&T, France Telecom/Equant and British Telecom. In the information technology area, competition is intense, based on price and quality of services provided. In the network services area, competition also is intense, based primarily on price. Prices for leased lines and customer telecommunications networks have been declining for the past several years as a result of this competition.

T-Mobile

Principal Activities

General

The principal services offered by the T-Mobile division are digital mobile telephony services based on the mobile telecommunications technology known as ‘‘GSM’’ (or Global System for Mobile Communications) and non-voice services such as SMS (Short Message Services) and other data services to residential and business subscribers based on WAP (Wireless Application Protocol) or GPRS (General Packet Radio Service). In addition, each of the Deutsche Telekom subsidiaries within the T-Mobile division offers international roaming services to subscribers through a large number of international roaming agreements with third-party operators, so that subscribers can access mobile services while they are outside their network service area. The T-Mobile division also sells mobile handsets to subscribers as part of packaged service offerings.

Voice telephony services are offered both on a prepay basis and on a contract (postpay) basis. Subscribers purchase contract services on the basis of fixed monthly fees and pay time-based airtime usage fees. Some contract service offerings include a limited amount of airtime in the monthly fee. Prepay services are purchased on the basis of monetary increments that are recorded on the subscribers’ airtime cards and then deducted based on time-based airtime usage fees as the cards are used. Airtime usage fees can vary according to the tariff plan selected by the customer, the day and time of day when a call is made, the destination of the call and, in some cases, other provisions applicable to the tariff plan and whether the called party is also a customer of the same network.

New Services

Deutsche Telekom offers mobile online services in Europe developed by T-Mobile Online (formerly T-Motion). These services were launched in Germany in September 2000, in the United Kingdom in February 2001 and in Austria in May 2001. In the future, Deutsche Telekom plans to further expand its mobile online services to other markets where it holds mobile communication interests. Mobile online services can be accessed through WAP-enabled handsets, and can also be accessed using ‘‘General Packet Radio Service (‘‘GPRS’’). In November 2001, VoiceStream in the U.S. launched GPRS-based services under the name iStream.

Deutsche Telekom has invested in network infrastructure relating to the GPRS mobile communications platform. GPRS is a technology that permits transmission of data at rates substantially faster than those that can be achieved using GSM technology. T-Mobile introduced GPRS for contract subscribers on a commercial basis in Germany in February 2001, in Austria in April 2001 and in the Czech Republic in August 2001.

Deutsche Telekom also has made substantial investments in the next generation mobile communications standard, known as Universal Mobile Telecommunications System or ‘‘UMTS’’. UMTS is a technology that is expected to permit transmission of data at rates even faster than those that can be achieved using GPRS technology. In February 2002, T-Mobile announced plans to cooperate with several infrastructure suppliers in the construction of UMTS mobile communications systems. Deutsche Telekom invested in UMTS licenses EUR 8.5 billion in Germany, EUR 171 million in Austria, EUR 395 million in the Netherlands and EUR 6.6 billion in Great Britain in 2000 and EUR 103 million in the Czech Republic in 2001.

Deutsche Telekom has agreements with mmO2 to jointly construct and maintain UMTS networks in Germany and the United Kingdom. Deutsche Telekom expects these arrangements to reduce its total UMTS network construction costs and operational expenditures substantially. The agreements, which are subject to regulatory approval, provide for the sharing of new and existing base stations, including sites and masts, in certain predominantly urban areas. The parties will also designate certain non-urban areas to one or the other party to construct, maintain and operate a UMTS network.

Global Branding

As part of T-Mobile's global marketing strategy to increase customer awareness of and loyalty to its brand, T-Mobile is introducing the "T-Mobile" brand. T-Mobile's operations in Germany, formerly known as "T-Mobil", began operating as "T-Mobile Deutschland" in February 2002. In April 2002, the operations in the United Kingdom, formerly known as "One 2 One", began operating as "T-Mobile UK" and the Austrian operations, formerly known as "max.mobil", began operating as "T-Mobile Austria". T-Mobile plans to begin rebranding VoiceStream's operations as "T-Mobile USA" with the rollout of its U.S. networks in California and Nevada in the third quarter of 2002 and aims to complete its rebranding of VoiceStream as T-Mobile USA throughout the United States by the end of 2002.

Principal Markets

The T-Mobile division reflects the activities of Deutsche Telekom's wholly-owned mobile communications subsidiaries in Germany, the United States, the United Kingdom, Austria and, since April 1, 2001, the Czech Republic. Through its T-Mobile division, Deutsche Telekom also holds substantial minority investments in mobile communications providers in the Netherlands, Poland, Russia and Canada.

Deutsche Telekom also directly or indirectly owns interests in mobile communications companies in Hungary, Croatia, Macedonia, Slovakia, Ukraine, Indonesia, the Philippines and Malaysia. At present, however, none of these investments is accounted for as part of the T-Mobile segment of Deutsche Telekom. For further information regarding these investments, see "Other Activities."

Germany

Through T-Mobile Deutschland, the T-Mobile division offers mobile communications services to individual and business subscribers in Germany. At December 31, 2001, T-Mobile Deutschland had approximately 23.1 million subscribers, as compared to approximately 19.1 million at year-end 2000. Of total subscribers at December 31, 2001, approximately 10.7 million were contract subscribers, as compared to 9.1 million at year-end 2000, and approximately 12.4 million were prepay subscribers, as compared to approximately 10 million at year-end 2000. At T-Mobile Deutschland, prepay subscribers are counted as continuing subscribers for the fifteen-month period since the last time they used their prepay access services.

T-Mobile Deutschland's average churn rate for 2001 was 1.4 percent per month, as compared to 1.0 percent in 2000. The churn rate for any given period represents the number of subscribers whose service was discontinued during that period, expressed as a percentage of the average number of subscribers during that period. Churn numbers are influenced by the manner in which some inactive prepay subscribers are counted as continuing subscribers. The introduction of a mobile number portability requirement could cause churn rate to rise.

United States

In May 2001, Deutsche Telekom acquired all of the outstanding equity securities of VoiceStream Wireless Corporation and of Powertel, Inc. in exchange for Deutsche Telekom shares having a market value on the acquisition date of EUR 28.7 billion plus EUR 4.9 billion in cash. From May 31, 2001 VoiceStream Wireless Corporation and Powertel, Inc. are fully consolidated within the T-Mobile division, and the name VoiceStream as used below refers to the combined entities VoiceStream Wireless Corporation and Powertel, Inc.

Through VoiceStream, the T-Mobile division offers mobile communications services to individual and business subscribers in the United States. At December 31, 2001, VoiceStream had approximately 7.0 million subscribers, as compared to approximately 4.8 million at year-end 2000. Of total subscribers at December 31, 2001, approximately 5.2 million were contract subscribers, as compared to approximately 3.3 million at year-end 2000, and approximately 1.8 million were prepay subscribers, as compared to approximately 1.5 million at year-end 2000.

VoiceStream's average churn rate for 2001 was 4.7 percent per month.

During 2001, VoiceStream entered into a 50/50 joint venture with Cingular Wireless LLC (''Cingular'') to share GSM network infrastructure in the New York area and network infrastructure that covers most of the state of California and parts of Nevada. VoiceStream and Cingular did not contribute licenses to the joint venture. Both VoiceStream and Cingular will independently market services under their respective brand names and bill and support their own subscribers in each of the markets.

The joint venture, which will operate and build out the network infrastructure in the two markets, will enable VoiceStream to enter the California market sooner and more cost effectively than would otherwise be possible. VoiceStream expects to launch services and begin adding subscribers in the California markets by 2002, provided the networks in both markets meet certain technical standards. The joint venture may be terminated under a number of circumstances, including without cause by either party starting in November, 2004. Upon termination, the joint venture agreements call for the parties to exchange certain spectrum rights and to make certain cash payments. The spectrum rights received by Deutsche Telekom in this exchange will have to be tested regularly for impairment under U.S. GAAP, and any impairment recognized could have a substantial impact on Deutsche Telekom's results of operations.

United Kingdom

In the fall of 1999, Deutsche Telekom purchased One 2 One (now T-Mobile UK), the fourth largest provider of mobile communications services in the United Kingdom, for a purchase price of EUR 10.9 billion (including the assumption of outstanding shareholder loans). In connection with the acquisition, Cable & Wireless indemnified Deutsche Telekom for certain liabilities.

Through T-Mobile UK, the T-Mobile division offers mobile communications services to individual and business subscribers in the United Kingdom. At December 31, 2001, T-Mobile UK had approximately 10.4 million subscribers, as compared to approximately 8.3 million at year-end 2000. Of total subscribers at December 31, 2001, approximately 1.7 million were contract subscribers, as compared to 1.8 at year-end 2000, and approximately 8.7 million were prepay subscribers, as compared to 6.6 million at year-end 2000.

Of the total number of T-Mobile UK subscribers at December 31, 2001, approximately 1.4 million were subscribers of the Virgin Mobile joint venture between T-Mobile UK and the Virgin Group. Virgin Mobile is a so-called mobile virtual network operator established by T-Mobile UK and the Virgin group. As a virtual network operator, Virgin Mobile purchases airtime minutes and basic mobile services from T-Mobile UK and resells these minutes and services under the ''Virgin'' brand name.

T-Mobile UK's average monthly churn rate for 2001 was 1.9 percent, as compared to 1.7 percent per month in 2000. While T-Mobile UK historically counted prepay subscribers as part of its subscriber base for 12 months after their last outbound call, after July 1, 2001 T-Mobile UK reduced this period to six months.

Austria

Through T-Mobile Austria (formerly max.mobil), the T-Mobile division offers mobile communications services to individual and business subscribers in Austria. At December 31, 2001, T-Mobile Austria had approximately 2.1 million mobile communications subscribers, largely unchanged from year-end 2000. Of the total subscribers at December 31, 2001, approximately 0.9 million were contract subscribers, largely unchanged from year-end 2000, and approximately 1.2 million were prepay subscribers, largely unchanged from year-end 2000.

T-Mobile Austria's average churn rate for 2001 was 1.6 percent per month, as compared to 1.5 percent in 2000. T-Mobile Austria counts inactive prepay subscribers as continuing subscribers for 12 months after their last outbound call or last reload of their prepay card.

Czech Republic

Through its T-Mobile division, Deutsche Telekom holds an equity interest of approximately 92 percent in a company called CMobil. Through April 2001, CMobil owned an equity interest of 49 percent in the Czech mobile communications network operator RadioMobil. In April 2001, CMobil exercised an option to increase its equity interest in RadioMobil to approximately 61 percent. As a result, Deutsche Telekom's indirect equity interest in RadioMobil increased to approximately 56 percent. RadioMobil has been consolidated in Deutsche Telekom's financial statements since April 1, 2001. At December 31, 2001, RadioMobil had approximately 2.9 million subscribers, as compared to approximately 1.9 million at year-end 2000.

The Netherlands

In October 2000, through its T-Mobile division, Deutsche Telekom acquired an equity interest of 50 percent minus one share in Ben Nederland Holding, B.V. (''Ben''), one of five operators in the Dutch mobile communications market. The acquisition of the stake in Ben took place after T-Mobile International acquired a third generation UMTS license in the Netherlands in July 2000 in a consortium with Belgacom and Tele Danmark called 3-G Blue, which subsequently merged with Ben. At December 31, 2001, Ben had approximately 1.2 million subscribers, as compared to approximately 0.8 million at year-end 2000.

T-Mobile International has a shareholders' agreement with Belgacom, Tele Danmark (''TDC Mobile'') and Gringots S.A.R.L. (''Gringots'') which gives T-Mobile International the right, from January 2002 through December 2005, to require Belgacom, TDC Mobile and Gringots to sell all or parts of their shareholdings to T-Mobile International. The call option can be exercised up to four times. Belgacom, TDC Mobile and Gringots may (collectively or individually) also put all or parts of their interests in Ben to T-Mobile International from January 2003 through December 2005, or, if in connection with an exercise of T-Mobile International's call option, at any time. The price per exercise for both options is EUR 17.23 per share. The minimum value of the shares that can be acquired at any one time is € 25 million. The maximum aggregate purchase price in connection with an acquisition of all 100 million shares held by Belgacom, TDC Mobile and Gringots is approximately € 1.7 billion, although downward adjustments may apply depending on which counterparty is selling its shares and when the exercise takes place.

Poland

Through its T-Mobile division, Deutsche Telekom holds a 45 percent equity interest in Polska Telefonia Cyfrowa Sp. z o.o.(''PTC''). At December 31, 2001, PTC had approximately 3.8 million subscribers, as compared to approximately 2.8 million at December 31, 2000. For information on an arbitral proceeding relating to Deutsche Telekom's interest in PTC, see ''Item 8. Financial Information — Litigation.'' Deutsche Telekom has a contingent obligation of EUR 153 million to acquire further shares in PTC.

Russia

Through its T-Mobile division, Deutsche Telekom holds directly and indirectly an equity interest of approximately 40 percent in OJSC Mobile TeleSystems (''MTS''), a Russian mobile telecommunications company. At year-end 2001, MTS had approximately 2.8 million subscribers, as compared to approximately 1.2 million at year-end 2000.

Seasonality

T-Mobile's business is affected by seasonal factors, with a general increase in sales of products and services in all markets during the fourth calendar quarter due to holiday purchases. As a result, T-Mobile's performance during the fourth quarter can have a significant influence on its performance for the full year.

Suppliers

T-Mobile purchases network components, as well as mobile handsets for purposes of resale, from a number of suppliers. With respect to network components, T-Mobile has in the past experienced supply delays due to the limited number of network component suppliers and could experience supply delays in the future, particularly with respect to UMTS network equipment. T-Mobile has attempted to address the risk of supply delays by using multiple suppliers and, in the case of UMTS network equipment, contractual penalties if the supplier does not deliver equipment on time. With respect to handsets, T-Mobile and other network operators have experienced delays in obtaining handsets suitable for use on GPRS networks. Deutsche Telekom does not expect the first market release of commercially viable European Standard UMTS handsets until the third quarter of 2003.

Marketing

Each of the principal subsidiaries in the T-Mobile division uses its own combination of distribution channels to market products and services to customers. In each of the principal markets, third-party distributors, who typically market the products and services of multiple mobile phone network operators, play a significant role in marketing. Deutsche Telekom's mobile communications subsidiaries use a variety of incentives to encourage third-party vendors to sell T-Mobile products and services, such as payment of marketing expenses and special commissions. In addition, T-Mobile markets its products and services to retail customers through direct sales outlets, particularly in Germany and Austria, and markets products and services to business customers through a direct sales force. Mobile telecommunications resellers (who purchase airtime and handsets at a discount from network operators, resell packaged services and handsets through their own distribution channels, charge their customers at rates that they set independently and provide customer service and technical support) are also an important distribution channel. In the United Kingdom, T-Mobile UK sells basic services to Virgin Mobile, a virtual mobile network operator established by T-Mobile UK and the Virgin Group, which resells these services under the ''Virgin'' brand name at rates that it sets independently.

Dependence on Patents, Licenses, Industrial, Commercial or Financial Contracts

T-Mobile owns a large number of registered patents and has a number of patent applications outstanding, particularly in Germany, for technical innovations in the area of mobile telecommunications applications resulting from its development activities. Deutsche Telekom does not believe that T-Mobile is dependent on any patent.

To offer mobile telecommunications services in the different jurisdictions in which it operates, Deutsche Telekom requires and therefore is dependent on licenses from the relevant authorities in each of these jurisdictions. For further information on those licenses, see ''— Regulation — Licensing and Notification Requirements; Allocation of Frequencies'' and ''— Regulation — Different Regulatory Regimes.'' Some of these licenses have limited terms which expire within the next 20 years. For example, the German GSM license expires on December 31, 2009. Although T-Mobile Deutschland expects to be able to renew this license if necessary, it has no legal entitlement in this regard. The Austrian GSM license expires on December 31, 2015 with a requirement that T-Mobile Austria comply with the European GSM standard during the last five years of the license term. Such compliance must be demonstrated no later than December 31, 2009. T-Mobile Austria believes that it will satisfy these requirements. In the United Kingdom, T-Mobile UK has an individual Public Telecommunications Operator License which cannot be revoked without cause until May 9, 2020. Otherwise, the PTO license will remain in force indefinitely unless terminated or revoked.

Deutsche Telekom does not believe that T-Mobile is dependent on any third party industrial, commercial or financial contract.

Competition

General

Competition in mobile communications is generally conducted on the basis of price, subscription options offered, offers of subsidized handsets, coverage, range of services offered, innovation and quality of service.

In the past, competition in the European mobile communications market has been conducted at the national level. Increasingly, however, competition in this market is being conducted on a more international basis than in the past.

Deutsche Telekom has not acquired a UMTS license in auction or non-public tender procedures in Italy, Spain or France. It is unclear at the present time, however, to what extent ownership of a UMTS license in each of the major markets will be advantageous in comparison to other strategies for entering those markets, such as participating as a Mobile Virtual Network Operator (MVNO). A MVNO is a provider that relies on another company for its network, focusing its efforts on marketing and customer service.

Deutsche Telekom believes that the decisions by Germany, the United Kingdom and Austria to auction UMTS licenses, as contrasted with the decisions to conduct non-public tender procedures in Spain and other countries, have created an uneven competitive playing field within the European Union that benefits incumbent telecommunications providers in countries where auctions were not conducted.

In Germany, the United Kingdom and Austria, the rate of mobile phone penetration is quite high. As a result, growth in the number of T-Mobile subscribers in these markets is expected to be significantly lower than in past years, and the focus of competition will shift from customer acquisition to customer retention and to increasing average revenues per user by stimulating demand for new products and services. In this connection, the timely introduction of new technologies that permit faster data transmission is highly significant. Churn rates could rise as mobile network operators seek to acquire subscribers of other mobile network operators. While the focus of competition is shifting, Deutsche Telekom expects that competition will continue to be intense. Large numbers of subscribers in Europe have taken advantage of prepay tariff packages. Since these prepay subscribers are not bound to T-Mobile or other operators by contract, this trend may generate additional competitive pressure in the future.

The global mobile communications industry has been undergoing consolidation in recent years, which may increase competitive pressure. Deutsche Telekom expects that the crowded markets caused by the UMTS auctions will lead to further consolidation in Europe. In the United States, Deutsche Telekom expects that pressures to consolidate will increase when spectrum ownership limits imposed by the U.S. telecommunications regulator expire in December 2002. In addition, new technologies, whether introduced by Deutsche Telekom or by others, can be expected to draw subscribers from existing technologies, including those of Deutsche Telekom. The competitive dynamics of the mobile telecommunications industry therefore could change in ways that Deutsche Telekom can not predict and that could adversely affect its results of operations.

Germany

In Germany, T-Mobile faces intense competition from the network operators Vodafone D2 (formerly Mannesmann D2), E-Plus and mmO2 (formerly Viag Interkom). T-Mobile Deutschland had a market share of approximately 41.2 percent at December 31, 2001, while Vodafone D2 had a market share of approximately 39 percent, E-Plus had a market share of approximately 13.3 percent and Viag O2 had a market share of approximately 6.5 percent at that date. The penetration rate in the German mobile communications market was approximately 68.6 percent at December 31, 2001.

In the retail market, in addition to competition from other network operators, T-Mobil faces significant competition from resellers.

The German government awarded six UMTS licenses in August 2000, including to the four existing German mobile communications network operators, the German mobile services reseller Mobilcom and a joint venture owned by Telefonica and Sonera. A significant number of subscribers on T-Mobile Deutschland's GSM network currently have customer relationships with Mobilcom, which may seek to turn those customers into subscribers of its own UMTS network. New entrants, and agreements between new entrants and existing network operators, could cause competition in the German UMTS market to be even more intense than competition in the GSM market has been, particularly as a result of the need operators will have to recoup substantial sums expended on acquiring UMTS licenses.

United Kingdom

In the United Kingdom, T-Mobile UK faces intense competition, principally from Vodafone, mmo2 (formerly BT Cellnet), and Orange, a subsidiary of France Telecom. Vodafone had a market share of approximately 28 percent at December 31, 2001, while mmo2 had a market share of approximately 23.5 percent, Orange had a market share of approximately 26.3 percent and T-Mobile UK had a market share of approximately 22.2 percent. Compared to its competitors, T-Mobile UK, including Virgin Mobile, has a lower proportion of business subscribers. The penetration rate in the British mobile communications market was approximately 80.6 percent at December 31, 2001.

In the retail market, in addition to competition from other network operators, T-Mobile UK faces significant competition from resellers and is starting to compete with virtual mobile network operators who have entered the U.K. mobile telecommunications market.

Austria

In Austria, T-Mobile Austria faces competition from Mobilkom (A1), Connect Austria (One) and tele.ring. T-Mobile Austria had a market share of approximately 32 percent at December 31, 2001, while A1 had a market share of 43.4 percent, One had a market share of 20.5 percent and tele.ring had a market share of 4.1 percent at that date. The penetration rate in the Austrian mobile communications market was approximately 75.5 percent at December 31, 2001.

Czech Republic

In the Czech Republic, RadioMobil faces competition from Eurotel and Cesky Mobil. At the end of 2001 Eurotel had a market share of 46.7 percent, RadioMobil had a market share of 41.1 percent and Cesky Radio had a market share of 12.1 percent. The penetration rate in the Czech mobile communications market was approximately 67.7 percent at December 31, 2001.

United States

In the United States, VoiceStream and Powertel together operate the smallest of the six national mobile networks. VoiceStream faces intense competition in the United States mobile communications market from the national mobile providers Verizon Wireless, Cingular, AT&T Wireless, Sprint PCS and Nextel and from some regional operators. Most of these competitors have been operating in the U.S. mobile communications market for a considerable time prior to the entry of VoiceStream and Powertel into the market.

The U.S. mobile market is quite different in a number of respects from the European mobile markets. No single communications standard is used by the nationwide network operators. At present, VoiceStream is the only U.S. operator with a nationwide GSM footprint, although Cingular Wireless and AT&T Wireless have announced that they intend to switch their networks to the GSM standard. Licenses to provide wireless services cover numerous localities, rather than the entire nation. It can be difficult for network operators to obtain the spectrum needed in some localities to expand subscriber bases, upgrade the quality of service and add new services, particularly in densely populated urban areas. On the other hand, low population density in some areas can cause problems with network efficiency and results in geographically sizeable areas with no or limited coverage. For these and other reasons, penetration levels for mobile telephony services in the United States are generally lower than penetration levels in Western European countries, with an estimated 45.7 percent mobile penetration rate as of December 31, 2001. As a result, operators in the United States market generally continue to invest heavily in order to encourage and capture rapid growth in subscriber numbers.

T-Online

Deutsche Telekom offers Internet access in Europe for residential customers and for small and medium-size business customers through its T-Online International AG subsidiary, and also offers multimedia applications and services for business customers. The T-Online segment also includes the activities of DeTeMedien, whose primary activity in terms of revenues is the publication of telephone directories.

T-Online International AG

General

T-Online had approximately 10.7 million customers at December 31, 2001 as compared to 7.9 million customers at December 31, 2000. T-Online, which is operated, developed and marketed by T-Online International AG, is one of Europe's largest online-services and internet-service providers based on revenues and number of subscribers. T-Online offers cost-effective, high-performance Internet access primarily to consumers. Average monthly usage per subscriber increased by approximately 31 percent in 2001 as compared to 2000. The average monthly usage of T-Online's portal network and services by its subscribers increased from 72 minutes in December 2000 to an average of 94 minutes in December 2001.

T-Online was first listed on the Neuer Markt segment of the Frankfurt Stock Exchange in April 2000 through a public offering of newly issued shares representing approximately ten percent of its then equity capitalization. As of December 31, 2001, Deutsche Telekom had a controlling ownership interest of approximately 81.7 percent in T-Online.

In addition to Internet access, T-Online offers customers access to a number of value-added online services. The available applications cover a spectrum that includes database research, information, entertainment and online banking.

In 2001 T-Online International AG took a significant step in the direction of becoming Europe's leading Internet Media Network. In this connection, T-Online has relaunched its portal and entered into co-operation agreements with the Axel Springer Verlag, with DaimlerChrysler, and with ZDF Heute. The goal of these measures is to increase the amount and quality of the content provided on T-Online's portals and thereby increase the time spent on its portals.

Subject to applicable regulatory constraints, T-Online's service offerings include products that bundle Internet access with services offered by other companies in the Deutsche Telekom group, such as T-DSL or access to the Internet via Deutsche Telekom's fixed-line telephone network. T-Online also seeks to promote Internet usage in Germany through special promotional offers, such as an offer of free Internet access and related software and customer service to schools in Germany.

To further its market leadership position in Germany, T-Online entered into an online banking relationship with comdirect bank AG, the online banking subsidiary of Commerzbank AG, in April 2000. As part of this relationship, T-Online agreed to take a 25 percent equity interest in comdirect, and Commerzbank took an equity stake in T-Online of approximately 2.0 percent (after giving effect to the listing of T-Online shares that took place in April 2000 and to the acquisition of Club Internet described below). As a consequence of the initial public offering in 2000 of comdirect bank AG, T-Online's interest in comdirect was diluted to 21.35 percent. In addition, T-Online also acquired a 100 percent ownership interest in Atrada Trading Network AG for EUR 26 million. This company specializes in e-commerce and was purchased in order to achieve synergies in technology.

International Internet Activities

T-Online took a significant step in the development of its international business in March 2000, when it acquired a 99.9 percent equity interest in Club Internet, the online service business of the French Lagardère group, in exchange for shares of T-Online representing an equity interest of approximately 5.8 percent in T-Online (after giving effect to the listing of T-Online shares that took place in April 2000 and to the acquisition of an interest in comdirect). T-Online has replaced the management team in France to ensure the efficient operation of its subsidiary going forward. Club Internet had approximately 778,000 customers in France at December 31, 2001.

In October 2000, T-Online acquired ya.com, a leading Spanish Internet service provider, in exchange for cash and shares of T-Online then representing an equity interest of approximately 1.25 percent in T-Online.

Ya.com had approximately 778,000 customers in Spain and Portugal at December 31, 2001.

T-Online has also launched a portal in Austria in 2001, and is planning to launch one in Switzerland in 2002.

Competition

The German and European markets for Internet access and portal services have been and will continue to be extremely competitive. In the market of providing Internet access services, particularly in Germany, strong competitors (including AOL) have pursued aggressive marketing strategies that have led to a substantial decrease in prices for Internet access. Competition in this market depends on a variety of factors, including pricing, brand recognition, network speed and reliability, customer support and time to market with new products and services. Regulation also can exert a significant influence on the level of competition in this market. In the market for portal services, competition is intense due to low barriers to entry. Deutsche Telekom faces competition in this market from websites maintained by Internet service providers, Internet information retrieval services, online community websites, home page services and shopping portals, as well as from traditional media including newspapers, magazines, radio and television.

Other Activities

The segment "Other Activities" consists mainly of foreign subsidiaries which were not assigned to a specific segment due to their activities or their customer structure. The main subsidiaries in this category are MATAV, Slovak Telekom and Croatian Telecom as well as a number of other international holdings. International activities make up about 80% of the revenue in this segment. Aside from international activities, this segment includes a variety of Deutsche Telekom units whose activities cannot be assigned directly to an individual segment. These include Deutsche Telekom's headquarters and competence centers, such as customer billing and real estate activities, as well as associated and related companies accounted for at equity or at cost.

International Activities

MATAV. Deutsche Telekom holds a 59.5 percent equity interest in MATAV, the leading full service telecommunications service provider in Hungary. In 2001, MATAV contributed EUR 2.1 billion to the consolidated revenues of Deutsche Telekom, which represented an increase in revenues of 24.6 percent over 2000. In 2001, MATAV shifted its strategic focus and reallocated human and financial resources to higher growth areas (Mobile, Internet and Data Communication).

MATAV currently has approximately one billion common shares outstanding and a single Series B share, which is held by the Hungarian Republic through the Hungarian Ministry for Transport, Telecommunications and Water Management. Although Deutsche Telekom has the power to appoint a majority of MATAV's board of directors, the Republic of Hungary retains significant influence over MATAV's activities as the holder of the Series B share, the regulator of the Hungarian telecommunications sector and MATAV's largest customer. The Series B share gives the Hungarian state certain special rights in the election of MATAV's boards and with respect to certain decisions taken at shareholders' meetings.

MATAV's monopoly in the Hungarian market for long-distance and international telecommunications services expired at the end of 2001. As a result, MATAV may face considerably intensified competition in its fixed-line business, which may adversely affect its contribution to Deutsche Telekom's consolidated net income.

Slovak Telecom. In July 2000, Deutsche Telekom acquired a 51 percent equity interest in the state-owned Slovak Telecom, the leading full-service telecommunications service provider in Slovakia, for a purchase price of EUR 1 billion. Slovak Telecom offers local, long-distance and international telephone services, data communications services, telex and telegraph services, distribution and broadcasting of radio and television signals and mobile communications services and is the leading provider of online services in Slovakia. In 2001, Slovak Telecom contributed EUR 451 million to the consolidated revenues of Deutsche Telekom.

The Slovak Telecom shares held by Deutsche Telekom are subject to substantial transfer restrictions. In addition, Deutsche Telekom has agreed to meet targets relating to fixed-line penetration and digitization of the fixed-line network and to cause Slovak Telecom to invest at least EUR 1 billion in its core business by the end of 2004.

Croatian Telecom. In October 1999, Deutsche Telekom acquired a 35 percent equity interest in the then state-owned Croatian Telecom, the leading full-service telecommunications service provider in Croatia. In October 2001, Deutsche Telekom acquired an additional 16 percent in Croatian Telecom for EUR 507 million and increased its stake to 51 percent. Croatian Telecom operates modern, largely digitized fixed-line and mobile networks and is Croatia's leading full service telecommunication provider, being the market leader not only in the fixed-line and online market but also in the mobile business. In 2001, Croatian Telecom contributed revenues of EUR 152 million to the consolidated revenues of Deutsche Telekom.

Macedonia Telecom. In January 2001, a MATAV-led consortium acquired a 51 percent equity interest in Makedonski Telekomunikacii ("Macedonia Telecom"), the state-owned telecommunications company of Macedonia, for a purchase price of EUR 302 million. Macedonia Telecom is the principal communications provider in Macedonia. The Macedonian telecommunications market is at an early stage of development in terms of penetration of services, with fixed line penetration of approximately 26 percent and mobile penetration of 11 percent at the end of 2001.

Asian Investments. Deutsche Telekom owns a 25 percent stake in Satelindo, an Indonesian mobile and international telecommunications operator, which was initially acquired by T-Mobile Deutschland in 1995. Satelindo also has a permit to operate in the field of satellite communications. Satelindo had approximately 1.8 million customers as of December 31, 2001 and generated EUR 359 million in revenues in 2001.

In Malaysia, Deutsche Telekom owns an approximate 21 percent interest in the Malaysian telecommunications provider Technology Resources Industries bhd. ("TRI") which was acquired by Deutsche Telekom in October 1996. TRI/Celcom had approximately 2 million customers as of December 31, 2001 and generated EUR 752 million in revenues in 2001. Deutsche Telekom accounts for this investment under the equity method.

In the Philippines, Deutsche Telekom owns approximately 25 percent of the common and 20 percent of the preferred shares in Globe Telecom, a leading national mobile and fixed net communications provider. Globe Telecom had approximately 4.8 million customers as of December 31, 2001 and generated EUR 774 million in revenue in 2001. Deutsche Telekom accounts for this investment under the equity method.

Other Activities

Deutsche Telekom AG's real estate holdings generated revenue with third parties in the amount of EUR 409 million, consisting of revenues from leasing activities, facility management as well as from construction management.

Domestic and International Carrier Services

Deutsche Telekom's business with other telecommunications carriers is conducted through the T-Com and T-Systems divisions. In the segment financial data for the three years ended December 31, 2001, the international carrier services business is reflected in the T-Com segment and the national carrier services business is reflected in the T-Systems business. With effect as of January 1, 2002, however, Deutsche Telekom transferred operational responsibility for the national carrier services business to the T-Com division and operational responsibility for the international carrier services business to T-Systems. This new allocation of operational responsibility for the carrier services business will be reflected in the financial data of Deutsche Telekom's segments for periods starting after December 31, 2001.

Domestic Carrier Services

The products and services provided by the domestic carrier services business area consist primarily of interconnection services for operators of fixed networks and mobile communications networks, carrier-specific transmission paths and access to the unbundled subscriber line the so-called "unbundled local loop".

The terms for interconnection of Deutsche Telekom's telephone network with networks of other national providers are contained in bilateral contracts. At December 31, 2001, Deutsche Telekom had signed 100 such agreements. The total number of leased lines provided to carriers, i.e., transmission paths that are made available to competitors in the fixed-line network, rose by 34 percent from year-end 2000 to year-end 2001.

In the national market, the terms on which Deutsche Telekom provides interconnection to competitors as well as access to the unbundled local loop so that competitors have direct access to the customers are essentially determined by the German telecommunications regulator. For further information in this regard, see "— Regulation — Special Network Access and Interconnection — Fixed-Fixed Interconnection."

International Carrier Services

The international carrier services business area provides carrier termination and transit services to other carriers for calls that originate outside Germany and are routed through Deutsche Telekom's network for termination in Germany or a third country and purchases termination services from foreign carriers for termination of Deutsche Telekom's outbound international traffic.

Since Deutsche Telekom is viewed by the German telecommunications regulator as a market-dominant provider in many markets, prices charged by Deutsche Telekom for most services provided to carriers are subject to regulatory approval. For further information on this topic, see "— Regulation — Special Requirements Applicable to Market-Dominant Providers."

Deutsche Telekom pays for the use of networks of carriers in foreign countries for outbound international calls and receives payments from other carriers for the use of its network for incoming international calls. These payments are based on settlement arrangements under the general auspices of the International Telecommunications Union. Deutsche Telekom has benefited from the lowering of settlement rates in recent years. Settlement payments are calculated using a currency basket, in which U.S. dollars have the greatest weight and settlement payments themselves are generally denominated in U.S. dollars. In 2001, Deutsche Telekom's average bilateral settlement rates per minute decreased by approximately 15 percent in comparison with the previous year.

Innovation Management (Research and Development)

Deutsche Telekom reorganized its innovation management activities in 2001 in parallel with its reorganization along the lines of its four strategic pillars. The area previously responsible for research and development was turned into a network of innovation units in the divisions and at Group headquarters. T-Systems, together with other companies and research forms the operational backbone of this work. Innovation management activities were performed within the Innovation Management central unit at the headquarters of the Deutsche Telekom group as well as within each segment. Those activities were jointly managed by the unit at group headquarters and the units within the segments.

At December 31, 2001, Deutsche Telekom had approximately 7,500 employees with research and development responsibilities in a network that combines the innovative forces within the organization. The amount spent on research and development activities amounted to EUR 0.9 billion in 2001 and EUR 0.7 billion in each of 2000 and 1999. The research and development policy of Deutsche Telekom focuses on:

- the identification of challenges and opportunities arising from the interplay of new technologies linked to emerging markets and the identification of potential synergy gains through a cross-divisional approach laid down in the innovation strategy;
- ''mega projects'' that seek to illuminate key business issues and test the feasibility of promising technologies through pilot projects; and
- product lifecycle management that, among other things, improves the cost and time to market of new product development.

Deutsche Telekom's need to safeguard ideas and project results was reflected in 479 patent applications filed in 2001. At the end of 2001, Deutsche Telekom was strategically employing over 4,200 proprietary rights.

Deutsche Telekom makes venture capital investments through its wholly-owned subsidiary T-Venture (T-Telematik Venture Holding GmbH, Bonn). At the end of 2001, the investment portfolio amounted to 63 direct investments in companies and nine indirect investments in venture capital funds in North America, Europe, Asia and Israel. The aim of these investments is to achieve synergies with Deutsche Telekom's four divisions. In this regard, Deutsche Telekom also has created T-Mobile Venture Funds (''TMVF'') and the T-Online Venture Funds (''TOVF''), each totaling EUR 100 million. In 2001, TMVF accounted for four direct investments, while TOVF accounted for two direct investments.

REGULATION

Liberalization

The legal framework for the regulation of the telecommunications sector in Germany was completely transformed through the German Telecommunications Act, which came into force on August 1, 1996. The Telecommunications Act required the complete liberalization of the German telecommunications market by January 1, 1998, as mandated by the directives of the European Commission. This represented the final step in the liberalization effort that began in 1989.

The Regulatory Framework

The Telecommunications Act allows virtually unrestricted market access by qualified entrants. The principal objectives of the Telecommunications Act are to promote competition in the telecommunications sector through regulatory measures, to guarantee appropriate and adequate telecommunications services throughout Germany and to provide for the regulation of frequencies. The Telecommunications Act aims to achieve these objectives principally by requiring licenses for the conduct of certain telecommunications activities, allocating frequencies, securing universal service and subjecting enterprises having dominant positions in particular telecommunications markets (so-called ''market-dominant providers'') to a special regulatory framework.

Regulatory Supervision

Since January 1, 1998, regulatory functions under the Telecommunications Act have been carried out by the Regulatory Authority for Telecommunications and Posts *(Regulierungsbehörde für Telekommunikation und Post*) (the ''German telecommunications regulator''), a new supervisory body established within the Federal Economics Ministry (*Bundesministerium für Wirtschaft und Technologie*) (the ''Economics Ministry''). The German telecommunications regulator has various powers under the Telecommunications Act, including the authority to grant and revoke licenses, control network access and interconnection, and approve or review the tariffs and tariff-related general business terms and conditions of market-dominant providers. It also has the authority to assign and supervise frequencies and to impose universal service obligations.

The German telecommunications regulator is supported by an Advisory Council (*Beirat*) consisting of nine representatives of each of the two houses of the German Parliament, but the matters with respect to which the Advisory Council must be consulted are very limited. The Advisory Council is involved in, among other things, decisions concerning license auctions regarding scarce frequencies and decisions obligating a licensee to provide universal service. The Advisory Council need not, however, be consulted with regard to tariff decisions. The German telecommunications regulator is headed by a president and two vice-presidents who are nominated by the German Government upon the proposal of the Advisory Council.

Licensing and Notification Requirements; Allocation of Frequencies

The Telecommunications Act establishes licensing requirements for the following activities:

- the operation of transmission lines for mobile telecommunication services for the public (Class 1 licenses),
- the operation of transmission lines for satellite services for the public (Class 2 licenses),
- the operation of transmission lines for public telecommunications services (Class 3 licenses), and
- the provision of voice telephony services to the public on the basis of self-operated telecommunication networks (Class 4 licenses).

Generally, except in the case of scarce telecommunications frequencies, the number of licenses is not limited, and each applicant satisfying basic qualification requirements is entitled to receive a license. In applying for a license, an applicant is required to specify the geographic scope and the type of activity subject to license. Conditions and obligations may at any time be attached to a license to promote the achievement of the objectives of the Telecommunications Act.

A number of telecommunications services, such as text and data transmission services over leased lines, voice services for corporate networks and closed user groups, and the simple resale of voice telephony services, are not subject to licensing requirements. However, any person providing telecommunication services has to notify the German telecommunications regulator of its operations.

By law, frequencies are to be allocated upon request on a non-discriminatory basis according to objective and verifiable criteria. Licenses may be awarded by auction or competitive bidding if the German telecommunications regulator determines that frequencies are not available in sufficient quantity for all applicants or if multiple applications are submitted for the same frequency. The German telecommunications regulator may exclude a company from taking part in an auction or competitive bid for licenses or frequencies if the success of that company in an auction or bid would endanger competition based on principles of equal opportunity. The German telecommunications regulator may also deny approval of an application to transfer a license on the same basis, regardless of whether scarce frequencies are involved.

Payment of an initial license fee or frequency fee is required of parties to whom licenses or frequencies have been granted or allocated. In addition, parties to whom frequencies have been assigned are required to make annual contributions to cover the costs incurred by the German telecommunications regulator in planning and administering efficient and interference-free frequency usage.

The level of licensing fees raised pursuant to the Licensing Fees Ordinance is presently the subject of court proceedings, which are expected to lead to lower licensing fees. On the other hand, a new fee ordinance is currently under discussion that would establish additional fees which depend on the revenues of the regulated company, to cover the costs of regulation. The details of this new fee ordinance still remain open. For further information in this regard, see "— The European Union."

In applying for a license under the Telecommunications Act, the applicant generally has considerable flexibility in choosing the scope and geographical range of the products and services it wishes to offer. Even if a licensee is granted a license covering all of Germany, it generally may choose to provide only those service and geographic combinations that offer the best business opportunities. This flexibility is limited, however, to the extent that the applicant is required to provide universal services, as described below under the heading "— Universal Services."

Special Requirements Applicable to Market-Dominant Providers

General

Market-dominant providers and their affiliates are subject to special rules and obligations, including most importantly:

- the prior approval or retrospective review of tariffs and related business terms and conditions by the German telecommunications regulator, insofar as such tariffs relate to a market in which the provider is dominant. See "— Pricing."

- the obligation to offer competitors, on the basis of unbundling, special network access (including interconnection) as well as access to essential services and facilities used by the market dominant provider internally on a non-discriminatory basis. See "— Special Network Access and Interconnection."
- potentially, the obligation to provide universal services in a market. See "— Universal Services."
- the possible inclusion of restrictive conditions in licenses, such as, in the case of scarce frequencies, a condition not to combine with another provider in the same market or the rejection of bids for licenses and frequencies in case of scarce frequency capacity to the extent that equal competition on the relevant market is endangered.

In addition, market-dominant providers must maintain segregated accounting systems to allow for transparency in dealings among their various licensed telecommunications services, and between such services and license-free services, in order to prevent, among other things, the cross-subsidization of services. In this regard, the German telecommunications regulator may specify the structure of internal accounting for particular telecommunications services subject to licenses. Furthermore, under general competition law principles, market-dominant enterprises, as a rule, are required to refrain from abuses of their dominant positions. See "— Competition Law."

Market dominance under the Telecommunications Act is determined by reference to the German Act Against Restraints on Competition (*Gesetz gegen Wettbewerbsbeschränkungen*). This Act provides, among other things, that a company is refutably presumed to have a dominant position if its share equals or exceeds one-third of a relevant market. For information regarding a proceeding on the European Union level relating to this issue, see "— The European Union." The definition of the relevant product and geographic market and the determination that a company is market-dominant under the Telecommunications Act are made by the German telecommunications regulator in agreement with the German Federal Cartel Office.

Deutsche Telekom believes that for some time to come the German telecommunications regulator is likely to view Deutsche Telekom as holding a dominant position in the German market for public voice telephony services in the fixed network and in other markets, including most of those in which it had monopoly rights in the past. As a result, Deutsche Telekom expects that the provisions of the Telecommunications Act relating to the regulation of market-dominant providers will be applied to Deutsche Telekom's activities in those markets. Considering that in many markets competitors of Deutsche Telekom are unlikely to reach dominant positions in the near future, Deutsche Telekom expects that for some period of time it will have to compete in significant markets with providers not subject to the requirements applicable to market-dominant providers. These competitors may therefore have more flexibility than Deutsche Telekom in terms of the selection of services offered and customers served, pricing and the grant of access to their networks. The definition of a market in which dominance exists requires a number of judgments, and is subject to change as competitive conditions further develop.

Deutsche Telekom has actively initiated proceedings with the German telecommunications regulator relating to the reevaluation of markets in which Deutsche Telekom is no longer dominant.

In December 2001, the German telecommunications regulator and the Monopoly Commission (*Monopolkommission*) for the second time issued reports to the German federal legislature on the development of competition in the German telecommunications market. While both reports noted an increase in the level of competition in the telecommunications market in Germany (the Monopoly Commission pointed out effective competition in the markets for international and national long-distance leased lines), the Monopoly Commission also noted a current tendency towards consolidation in the German telecommunications market. Despite those findings, the Monopoly Commission did not make any specific recommendations for a reduction of regulation.

Deutsche Telekom expects that the Telecommunications Act will be amended in 2003 to take account of the changed market conditions in Germany and the new EU legislation. For further information in this regard, see "— The European Union — New Regulatory Framework." The Federal Economics Ministry is expected to publish an outline of an official position of the German government with respect to the reports of the telecommunications regulator and the Monopoly Commission in April 2002, and the German government is expected to announce a formal position in mid-2002. The Federal Economics Ministry also is expected to publish an outline of the new telecommunications law before the parliamentary elections currently scheduled for September 2002, and a draft of the new law is expected to be discussed in the German parliament in the first half of 2003. The new telecommunications law is expected to become effective by the middle of 2003.

Pricing

Under the Telecommunications Act, tariffs and tariff-related business terms and conditions for the telecommunications services of market-dominant providers and their affiliates are subject to special regulatory oversight and control insofar as they relate to a market in which such dominance is determined to exist. Other tariffs are essentially unregulated under the Telecommunications Act. The tariffs of all providers in Germany are, however, subject to European and German law of general application, including competition and consumer protection laws and ordinances. In addition, tariffs for universal services must be set at an "affordable price". See "— Universal Services."

The Telecommunications Act distinguishes between tariffs which require prior regulatory approval and tariffs which do not require prior approval, but which are subject to retrospective review. Prior approval is required for the tariffs of a market-dominant provider in the areas of public voice telephony services, the operation of transmission lines for telecommunications services to the public, and access and interconnection services. All other tariffs including tariffs in respect of mobile telephony, subscription fees for cable transmission services and fees for satellite services may be put into effect without prior approval. However, in markets in which a provider is considered to have a market dominant position, such tariffs are subject to retrospective review to the extent that facts become known that indicate that the tariffs are inconsistent with the Telecommunications Act.

Prior Approval of Tariffs

The Telecommunications Act provides for two basic approaches to prior approvals of tariffs: a price-cap approach and an approach involving individual approvals based on an assessment of the costs of providing a particular service (the "cost-based approach"). The Tariff Regulation Ordinance (*Telekommunikations-Entgeltregulierungsverordnung*) provides that priority is to be given to the price-cap approach. The cost-based approach applies to tariffs for services which under the regulation may not be, or are not, combined in a "basket" together with other services in accordance with the price-cap approach.

Tariffs may not be approved if they (1) contain surcharges which prevail solely as a result of the applicant's market-dominant position, (2) include discounts which prejudice the competitive opportunities of other companies in a telecommunications market or (3) discriminate among customers for the same or similar services in a telecommunications market, unless such surcharges, discounts or discriminatory features are objectively justified.

Price Cap Approach. Under the price-cap approach, the German telecommunications regulator establishes baskets of services, lays down an initial price benchmark for each basket and limits tariffs for the blend of services within that basket through the use of a price cap formula. This formula allows for price increases or requires price decreases from the initial benchmark level based on the general inflation rate, reduced by an amount which reflects expected productivity improvements. In establishing the price cap formula, the German telecommunications regulator is required to consider a range of factors, including the relationship of the initial tariff levels to the costs of efficient service provision and the productivity improvements being achieved by other enterprises in similar markets. The price-cap formula has the effect of requiring the affected company to reduce, or limiting the extent to which it can increase, the aggregate tariffs for services within a basket.

The price-cap approach to tariff regulation has been applied, most notably, to voice telephony services. In 1998, the telecommunications regulator established a price cap regime that was applicable to the years 1998 through 2001 and that was divided into two two-year periods. The price-cap regime required tariff reductions in each two-year period that reflected an expected productivity improvement of 6 percent minus an estimate of consumer price inflation. In 2001, the German telecommunications regulator established a new price cap regime that is applicable to the years 2002 through 2004 that is divided into three one-year periods. The new price cap regime calls for price reductions in each one-year period reflecting productivity improvements of one percent minus a measure of inflation.

Cost-based Approach. Tariffs requiring prior approval which are not dealt with under a price cap are based on the costs of efficient provision of the relevant service. The German telecommunications regulator bases its determination of the costs of efficient service provision on the long-run incremental costs of providing a particular service, with an additional amount in respect of overhead costs (including an appropriate return on capital employed), to the extent such costs are necessary for the provision of the service. The applicant is required to submit extensive documentation as to its costs and the methods and parameters on which its determination of costs is based in respect of the service in question. The German telecommunications regulator in general has broad discretion, however, in deciding whether to accept an applicant's attribution of costs to a particular service. In recent years, in determining tariffs under the cost-based approach, the German telecommunications regulator has declined to take into account costs that Deutsche Telekom believes were properly attributed to the service in question. Discussions continue concerning the appropriate methodology to be used in the calculation of the long-run incremental cost of the services subject to cost-based pricing.

Retrospective Review of Tariffs

All tariffs of market-dominant providers in markets in which such dominance occurs are subject to retrospective regulatory examination, even if the tariffs were initially subject to prior approval. The German telecommunications regulator must initiate examination proceedings if it becomes aware of facts indicating that tariffs that were initially subject to prior approval contain discounts or discriminatory features that are not objectively justified and may ultimately object to such tariffs and declare them to be invalid. In addition, with tariffs not subject to prior approval, the German telecommunications regulator may initiate examination proceedings if it becomes aware of facts indicating that such tariffs contain surcharges, discounts or discriminatory features that are not objectively justified. The German telecommunications regulator may object to such tariffs and declare them invalid. For example, the German telecommunications regulator has initiated retrospective reviews of increases in broadband cable tariffs.

Special Network Access and Interconnection

The Telecommunications Act imposes specific obligations concerning access to networks and interconnection. The Network Access Ordinance (*Netzzugangsverordnung*) under the Telecommunications Act provides details concerning these obligations and specifies the manner in which special network access (including interconnection) is to be effected.

General Principles and Practice

Every operator of a public telecommunications network, irrespective of the operator's market position, is obligated, upon request, to make an offer to other network operators for interconnection to its network. If the parties cannot reach an agreement on such interconnection, the German telecommunications regulator will order the interconnection upon application of one of the parties. To date, numerous interconnection orders have been issued. The contents of all agreements on special network access must comply with certain requirements of the Network Access Ordinance.

Provisions Applicable to Market-Dominant Providers

A network operator that offers telecommunications services to the public and is a market-dominant provider in a particular market must allow every user access to its network or parts thereof. Such access may be granted via connections provided for all users (general network access) or via special connections (special network access), which includes the interconnection of networks. Limitations on access may be based only on the "essential requirements" set forth in the Open Network Provision Directive of the EU, which include the preservation of the security of network operations, the maintenance of network integrity, the interoperability of services and the protection of data.

A provider dominant in a market for telecommunications services to the public must also grant to competitors active in the same market access to essential services it uses internally for the provision of such services. Such access must be provided under the same conditions it applies to itself, unless the offer of different conditions can be objectively justified.

A market-dominant provider generally is required to unbundle its services for special network access, and must therefore offer its internally used essential services, including transmission, switching and operational interfaces, in such a way that other users need not purchase services they do not want. In addition, a market-dominant provider generally is obligated to allow other network operators to use transmission, switching and operational interfaces to its network on its premises on the same conditions it applies to itself.

Agreements on special network access (including interconnection) must be provided to the German telecommunications regulator immediately following their execution. Conditions in such agreements must be based on objective criteria, be comprehensible and guarantee equal access.

Fixed-Fixed Interconnection

As of December 31, 2001, Deutsche Telekom had concluded about 100 interconnection agreements with competitors offering long distance and international calling services over the fixed-line network.

The current level of interconnection pricing was approved by the German telecommunications regulator in October 2001. The interconnection tariff system that applies as of January 2002 is based on the ''element-based'' system that is the international norm. Under an element-based interconnection tariff system, the tariff for transmission of traffic is based on the number and type of network elements used in transmission and not on the distance over which the traffic is transmitted.

On October 12, 2001, the German telecommunications regulator reached a decision regarding the implementation of element-based interconnection fees. The effect of this decision in the form reached by the German telecommunications regulator would be to require Deutsche Telekom to lower its interconnection rates by an average of approximately 14 percent, which would permit competitors to lower their prices for fixed-line international and domestic long-distance calls. This decision, by its terms, took effect in January 2002. Since Deutsche Telekom believes, however, that significant aspects of this decision represent an incorrect interpretation of relevant provisions of the Telecommunications Act, Deutsche Telekom has sought a preliminary injunction against the implementation of this decision and also has challenged this decision on its merits before the courts. Other companies that have made significant investments in their own infrastructure are also challenging this decision.

In the past, in making decisions regarding interconnection rates, the German telecommunications regulator has declined to take into account costs that Deutsche Telekom believed should be taken into account. The German telecommunications regulator generally has broad discretion in this regard.

The use of Deutsche Telekom's network by other carriers that have made limited investments in their own infrastructure can, in Deutsche Telekom's view, generate atypical traffic patterns that result in inefficient use of Deutsche Telekom's network. In 1999, the German telecommunications regulator issued a decision that permits Deutsche Telekom to deny access to other carriers whose investments in their own networks do not meet a minimum standard set by the German telecommunications regulator. The European Union has, however, criticized this decision of the German telecommunications regulator.

Mobile-Fixed Interconnection

Although Deutsche Telekom takes the position that it is not a market-dominant provider in the national market for termination of traffic from mobile networks, it has in the past submitted its mobile-fixed interconnection tariffs to the German telecommunications regulator for approval as a precaution. Since January 2000, Deutsche Telekom's mobile-fixed interconnection rates match its fixed-fixed interconnection rates. Like the fixed-fixed interconnection rates, these mobile-fixed interconnection rates will be valid until the end of May 2001. See also ''— Fixed-Fixed Interconnection.'' For a discussion of developments at the EU-level, see ''— Competition Law.''

Fixed-Mobile Interconnection

In December 1999, Deutsche Telekom reached an agreement with T-Mobile Deutschland to reduce T-Mobile Deutschland's fixed-mobile interconnection rates as of February 1, 2000. As a result, Deutsche Telekom has paid lower interconnection fees to terminate calls in the digital mobile network of T-Mobile Deutschland since February 1, 2000. In February and March 2000, Deutsche Telekom also reached similar agreements with VIAG Interkom, E-Plus and Vodafone D2 (formerly Mannesmann Mobilfunk) regarding the reduction of fixed-mobile interconnection rates. As a result, the rates paid by end customers of Deutsche Telekom for the termination of calls have been reduced.

Local Loop Access

As indicated above with regard to special network access, market-dominant providers are obligated to unbundle their service offerings to the extent demanded by their competitors in a public telecommunications market unless the market-dominant provider can demonstrate that unbundling is not objectively justified under the particular circumstances. In light of this obligation, various competitors have asked Deutsche Telekom to provide unbundled access to Deutsche Telekom's subscriber lines (i.e., the local loop). By allowing competitors to connect to customer access lines in local networks, unbundling of the local loop allows competitors to gain direct access to subscribers without having to build local networks of their own. In this way, competitors are able to use Deutsche Telekom's customer access lines to offer a wide range of local services directly to the customer.

In February 1999, the German telecommunications regulator approved a monthly rate of DM 25.40 (EUR 12.99) for access to a two-wire copper line. At the same time, the German telecommunications regulator approved one-time installation fees and a fee for terminating a lease of two-wire copper line of DM 107.70 (EUR 55.07). These rates were considerably lower than the rates requested by Deutsche Telekom, since the German telecommunications regulator did not take into account a number of costs that Deutsche Telekom believed should have been taken into account. Both Deutsche Telekom and its competitors have challenged aspects of this decision in court. For further information about this legal challenge, see ''Item 8. Financial Information — Litigation''. The outcome of this legal challenge is uncertain.

On March 31, 2001, the rates that Deutsche Telekom was permitted to charge for unbundled access to the local loop expired. In a decision of March 30, 2001, the German telecommunications regulator reduced the monthly line rental charge of DM 25.40 (EUR 12.99) for the unbundled copper pair to DM 24.40 (EUR 12.48) as of April 1, 2001. This new price will be valid until March 31, 2003. In addition, in April 2002, a decrease in charges was also ordered for one-time installation charges as well as charges paid for cancellation of phone service. Decisions made on these charges will expire on June 30, 2003. Deutsche Telekom had applied for a monthly line rental charge of EUR 17.40 (DM 34.03), as Deutsche Telekom believes that actual costs incurred are higher than the costs recognized by the German telecommunications regulator.

In addition to decisions relating to the appropriate level of network access pricing, the German telecommunications regulator has also made determinations relating to the technical point in the network at which network access must be provided. In one such decision, the German telecommunications regulator took the position that Deutsche Telekom must provide unbundling in accordance with the demands of competitors to the extent technically feasible. In another decision, the German telecommunications regulator decided that Deutsche Telekom has to grant unbundled access to the part of subscriber access lines located within customers' premises. Deutsche Telekom has filed suits challenging these decisions. For further information relating to these suits, see ''Item 8. Financial Information — Litigation''. In December 1999, without recognizing a legal obligation to do so, Deutsche Telekom submitted to the German telecommunications regulator a request for approval of the one-time connection fee and the monthly rental charges that Deutsche Telekom proposed to charge third parties for direct access to the part of subscriber access lines located within customers' premises. In February 2000, the German telecommunications regulator approved the one-time connection fee proposed by Deutsche Telekom but denied approval for the proposed monthly rental charge. In addition, competitors have submitted requests to the German telecommunications regulator for further unbundling of local loop access. Deutsche Telekom has submitted comments on these requests to the German telecommunications regulator.

In December 2001, Deutsche Telekom reached an agreement regarding line sharing with the firm QS Communications (QSC) and submitted the agreement to the German telecommunications regulator for approval. Line sharing offers are offers to lease the high-frequency band of telephone access lines to carriers competing with Deutsche Telekom, who can use the leased frequency band for broadband (ADSL) Internet access for end customers. Since January 2001, Deutsche Telekom has been obligated by EU regulation to make line sharing offers. In March 2002, the telecommunications regulator issued a decision establishing a monthly price of EUR 4.77 and a one-time connection fee of EUR 85 for this offer. Deutsche Telekom had applied for regulatory approval of a monthly price of EUR 14.65 and a one-time connection fee of EUR 150, since Deutsche Telekom believes that its costs for line sharing are higher than the costs recognized by the telecommunications regulator.

In February 2001, the German telecommunications regulator opened a formal proceeding relating to potential anti-competitive discounts involved in Deutsche Telekom's offer of T-DSL (digital subscriber line) service, i.e., broad band internet access for end customers. On March 30, 2001, the German telecommunications regulator discontinued this formal proceeding. Although the telecommunications regulator opened another formal proceeding in this regard in December 2001, this additional proceeding was discontinued in January 2002 after Deutsche Telekom announced plans to raise installation and monthly fees for T-DSL.

Due to sharply increased demand of other telecommunications carriers for local loop access, a backlog had developed in Deutsche Telekom's filing of orders for collocation space for local loop access. Deutsche Telekom has been ordered by the German telecommunications regulator to make offers of local loop access to other carriers that include, among other things, a commitment to faster provision of local loop access.

Deutsche Telekom has since complied with this order and the backlog in the filing of orders for collocation space no longer exists.

Resale

In March 2001, the German telecommunications regulator issued an order requiring Deutsche Telekom to offer subscriber network services (i.e., subscriber lines, local calls and city calls) to a particular competitor of Deutsche Telekom for purposes of resale. Deutsche Telekom challenged this order on its merits before the Cologne Administrative Court and sought a preliminary injunction against the implementation of this order pending resolution of the merits. The Cologne Administrative Court decided to deny the request for a preliminary injunction, however, and in October 2001 the Appellate Administrative Court in Münster upheld this decision.

In February 2002, the Appellate Administrative Court in Münster rejected an appeal by Deutsche Telekom from another administrative proceeding, in which an obligation on the part of Deutsche Telekom to resell services to network operators was articulated. While the Appellate Administrative Court reversed other aspects of the telecommunications regulator's decision in this matter, Deutsche Telekom is now obligated as a result of this decision to make a resale offer to the companies riodata and Tele2, and to make a resale offer to other companies upon request. Negotiations with several companies that have made requests currently are in progress. The challenge to the German telecommunications regulator's order on its merits is still pending before the Cologne Administrative Court. The implementation of the German telecommunications regulator's order is likely to lead to an increase in competition in the market for subscriber lines, local calls and city calls. Deutsche Telekom currently is obligated to offer subscriber network services to switchless resellers for purposes of resale.

In two decisions published in September and November 1999, the German telecommunications regulator had decided that regulatory approval is required for Deutsche Telekom's offers of services to service providers that purchase services for purposes of resale. This position relates to offers of local, domestic, and international long-distance calls as well as local access services. Deutsche Telekom has successfully applied for a preliminary injunction against the implementation of these decisions; the decision in the main legal proceeding is still pending. For further information on these legal actions, see "Item 8. Financial Information — Litigation."

Internet Access

In January 1999, T-Online introduced a change in the pricing of its Internet access products, combining the telephone "dial-in" connection to the Internet with the Internet platform services into one product. In connection with this bundled product, Deutsche Telekom offered access to its telephone network on a wholesale basis. In April 1999, several competitors of T-Online lodged a complaint with the German telecommunications regulator alleging that, in introducing this bundled product, Deutsche Telekom and T-Online had abused their market dominant position. In June 1999, the German telecommunications regulator ruled that Deutsche Telekom could no longer offer a special volume discount to T-Online but otherwise rejected the complaints. After two price reductions in 2000 and complaints by competitors, the German telecommunications regulator ruled in November 2000 that Deutsche Telekom could no longer offer any volume discounts relating to the wholesale Internet access product. For further information on these proceedings, see "Item 8. Financial Information — Litigation."

On December 15, 2000, Deutsche Telekom began offering access to its public switched telephone network to Internet platform providers at flat ("unmetered") rates in response to a decision of the German telecommunications regulator of November 15, 2000 requiring Deutsche Telekom to offer such a flat rate product. This offer includes a number of provisions designed to limit network congestion problems that could otherwise be caused by Internet platform providers taking advantage of Deutsche Telekom's flat rate offer. In March 2001, Deutsche Telekom successfully applied for a preliminary injunction against the obligation to offer a flat rate to Internet platform providers, with the effect that Deutsche Telekom is currently not obliged to offer such a flat rate product. Nevertheless, Deutsche Telekom is still offering unmetered access to its public switched telephone network to Internet platform providers. The German telecommunications regulator may, however, require Deutsche Telekom to modify the terms of the offer or to reduce the price at which it offers unmetered access to its public switched telephone network, and either of these requirements could lead to network congestion problems or require additional investments in Deutsche Telekom's public switched telephone network, or both.

The European Commission is currently conducting an investigation into Deutsche Telekom's local loop market including ADSL. Deutsche Telekom expects to be able to show that there is no infringement of competition law in respect to local loop unbundling or ADSL.

In June 1999, the German telecommunications regulator ruled that the Internet access charges of T-Online are not subject to price regulation because the dominant feature of online services is not telecommunications, but so-called ''tele-services'' (*Teledienste*). There are indications, however, that the German telecommunications regulator may change its legal approach to regulation of prices for online services in the future.

Numbering, Number Portability and Carrier Selection

Under the Telecommunications Act, the German telecommunications regulator is assigned responsibility for developing and administering a national telephone numbering system. Upon application, each telecommunications network operator and service provider is to receive assigned ranges of telephone numbers for use by its customers. The ranges assigned are within existing area codes. Applicants are assessed fees in accordance with the Telecommunications Numbers Fees Ordinance (*Telekommunikationsnummerngebührenverordnung*), which was promulgated in August 1999, but with retroactive effect to August 1, 1996.

Since January 1, 1998, Deutsche Telekom and other telecommunications network operators have been required to allow their customers to pre-select the network operator that is to transmit their calls. In addition, customers are able to override their pre-selected carrier each time they place a call by entering another operator's numeric prefix before dialing the telephone number they wish to call. Also, since January 1, 1998, Deutsche Telekom and other telecommunications network operators have generally been required to provide number portability. This permits customers to keep their assigned telephone numbers when they choose to change their network operator as long as they do not also change the physical location from which they access the network. Number portability and the provisions on carrier selection allow customers to switch easily among competing carriers.

In February 2001, the German telecommunications regulator set the fees Deutsche Telekom is permitted to charge to a customer for carrier-preselection for a second time at a level lower than sought by Deutsche Telekom. According to another decision of the German telecommunications regulator, Deutsche Telekom currently is not permitted to charge any fee for implementing number portability requirements. Upon Deutsche Telekom's appeal, the Cologne Administrative Court has revoked both decisions. This ruling remains subject to appeal by the German telecommunications regulator.

Under the Telecommunications Act, the German telecommunications regulator is authorized to suspend the obligation to provide number portability as long as and insofar as the absence of number portability does not significantly impair competition in individual markets or adversely affect consumers. The German telecommunications regulator may also suspend this obligation as long as and in so far as this is justified on technical grounds. The German telecommunications regulator decided in August 2001 that the suspension of number portability for mobile network operators would be extended, for the last time, until the end of October 2002.

Mobile network operators are required to deliver a quarterly report to the German telecommunications regulator regarding their progress in implementing the technical measures necessary to permit number portability. T-Mobile and D2 Vodafone filed requests for injunctions against this decision of the German telecommunications regulator with the Administrative Court in Cologne in May 2000. T-Mobile's request for an injunction against the decision was rejected by the Cologne Administrative Court on April 3, 2001. T-Mobile will appeal against this court decision. It is uncertain whether or not it will be possible to introduce mobile number portability by the prescribed deadline.

With regard to the obligation to provide carrier selection in mobile networks under the current provisions of the Telecommunications Act, the German telecommunications regulator takes the view that T-Mobile Deutschland is not obliged to provide carrier selection for network-internal calls (calls that originate and terminate within Deutsche Telekom's mobile network). The manner in which the obligation to provide carrier selection for network-external calls (calls that originate in Deutsche Telekom's mobile network but terminate outside the network) is to be implemented under the current provisions of the Telecommunications Act remains open.

At the moment a proceeding on carrier selection for mobile calls is pending before the German regulatory authority. A competitor of Deutsche Telekom has requested interconnection for the purpose of carrier selection for mobile calls. The decision on this proceeding will be issued by end of April 2002. The outcome of the proceedings is yet unclear. In mid-April 2002, the German government has issued a proposal for an amendment to the Telecommunications Act that excludes mobile network operators from the obligation to provide carrier selection, subject to a re-examination of possible obligations under the new EU regulatory framework by the summer of 2003. The amendment is expected to be adopted by the German legislature before August 2002. It is not certain, however, that the German legislature will adopt an exemption for the field of mobile communications. Therefore, Deutsche Telekom cannot rule out the possibility that in the course of 2002 an obligation for carrier selection will be imposed on T-Mobile Deutschland that would adversely affect T-Mobile Deutschland's business.

The conditions for a possible obligation for mobile carrier selection will change with the adoption of the new EU regulatory framework into national law, expected to take place in June 2003. The new EU framework allows EU member states to introduce obligations for carrier selection regarding mobile calls on dominant mobile operators. Although, at present no operator in Germany is considered a dominant mobile operator, this finding may change in the course of a market analysis that may be carried out by the national regulatory authority within the next twelve months.

Universal Services

The Telecommunications Act includes provisions to ensure the availability of certain basic telecommunications services (referred to as "universal services") throughout Germany. Additional details concerning universal service requirements are provided in the Universal Service Ordinance (*Telekommunikations-Universaldienstleistungsverordnung*) and in the Telecommunications Customer Protection Ordinance (*Telekommunikations-Kundenschutzverordnung*). See "— Customer Protection Ordinance."

The Universal Service Ordinance defines "universal services" to include public fixed-network voice telephony with certain ISDN features, directory services, telephone books, public pay phones and certain categories of transmission lines. These services must be universally available to all customers at a price determined by the German telecommunications regulator to be an "affordable price".

Under the Telecommunications Act, if a universal service in a particular product and geographic market is not being appropriately and adequately provided, or where there is reason to believe that such provision will not be accomplished, each licensee with a share of at least 4 percent of the product market for such service or a dominant position in the relevant product and geographic market can be required to contribute through payments to the cost of providing such universal service. Contributions are required if the provider of a universal service proves that the long-term additional costs of providing the service efficiently in the relevant geographic market, including adequate interest on capital employed, exceed the revenues from providing that service at an "affordable price". Details concerning the manner in which this compensatory system will function remain to be determined.

Under the Universal Service Ordinance, which entered into effect at the beginning of 1998, market dominant providers in the relevant markets may be required to provide universal services. Deutsche Telekom provides customers voice telephony and other universal services within the framework of the law and Deutsche Telekom's General Terms and Conditions. Deutsche Telekom currently provides the universal services specified by the Universal Service Ordinance without compensation. If Deutsche Telekom decides to stop providing any of the services referred to in the Universal Service Ordinance, it must give at least one year's advance notice. Deutsche Telekom expects that it will, for some time to come, be the only provider considered suitable to be subjected to the obligation to offer universal services. Accordingly, it may prove difficult for Deutsche Telekom to cease providing universal services in some markets, although Deutsche Telekom may be able to claim special compensation.

If Deutsche Telekom becomes required to offer a universal service, and if the revenues from providing that service are insufficient to cover its additional costs, the compensation granted under the Telecommunications Act may be insufficient to cover the full costs to Deutsche Telekom of providing that service. This results from the fact that Deutsche Telekom, like other licensees, is required to contribute to the cost of providing these services in proportion to its market share.

Customer Protection Ordinance

The Telecommunications Customer Protection Ordinance ("Customer Protection Ordinance"), as currently in effect, covers the special rights and obligations between providers of telecommunications services to the public and their customers, who may be either end customers or competitors to the extent that they have concluded a contract or intend to conclude a contract with the respective telecommunications provider.

As a result, nearly all Deutsche Telekom products and services, with only a few exceptions, such as the marketing of telephones, are subject to the provisions of the Customer Protection Ordinance.

Under the provisions of the Customer Protection Ordinance, market-dominant providers must make their services available to everyone on the same terms. Exceptions must be objectively justified. Further, although telecommunications providers generally have some flexibility in determining whether to offer services in ''bundles'', the dominant company is required to offer individual services on an unbundled basis when there is a ''general demand'' for those individual services in the market. This requirement applies to the description of individual services and the relevant service specifications, as well as the billing for such services. Offering individually listed services as a package is, however, still allowed.

In addition, the market-dominant provider must, upon request, eliminate or repair any malfunction immediately, including at night or on Sundays or holidays. Customers can request a free itemized statement of their calls, which must be detailed enough to allow them to check and monitor the accuracy of their bills. In the event that a customer has made no other arrangements with another provider, the customer will receive a combined bill from his local carrier. In such cases, the charges for all calls which the customer has made via other providers must be listed separately. Finally, starting January 1, 2001, telecommunications service providers must ensure that any customer who has set a ceiling for his calling charges does not exceed it. The Customer Protection Ordinance also allows for certain limitations on the liability of telecommunication service providers.

In October 1999, Deutsche Telekom announced that, starting on April 1, 2000, it would no longer provide billing and collection services to its competitors other than services that are mandatory under the Customer Protection Ordinance. In Deutsche Telekom's view, these mandatory services include billing for competitors and forwarding to competitors any payments made by customers to Deutsche Telekom for calls made via those competitors, but not collection of bills on behalf of competitors. In response to a complaint submitted by a competitor, however, the German telecommunications regulator instituted proceedings against Deutsche Telekom in October 1999 alleging that the implementation of Deutsche Telekom's plans to discontinue the provision of billing and collection services for competitors would constitute an abusive practice. On February 21, 2000, the German telecommunications regulator ruled that Deutsche Telekom must continue to offer billing and collection services for dial-up voice telephony, directory inquiry, value-added services and dial-up Internet-by-Call until December 31, 2000 on the same terms and conditions as had previously prevailed. For the period thereafter, new conditions may be agreed upon. The German telecommunications regulator also ruled that, not later than June 30, 2000, Deutsche Telekom would be obligated to submit for regulatory approval proposed terms and conditions for the provision of these services after December 31, 2001. Deutsche Telekom has appealed these rulings of the German telecommunications regulator to the administrative courts. According to these rulings, however, Deutsche Telekom will no longer be obligated to manage customer complaints, send late payment warnings or enforce late payments on behalf of competitors after January 1, 2001.

Billing and Collection

In August 2000, Deutsche Telekom started to negotiate with competitors on a new contractual basis for the provision of billing and collection services. The negotiations led to an agreement on essential service elements, but they did not lead to an agreement on prices for such services until the German telecommunications regulator agreed to mediate the negotiations. The German telecommunications regulator announced the mediation results on February 28, 2001, which thereafter were accepted by all parties. The new prices (28 DM for each 1000 delivered data sets and 9 Pfennig for each bill) came into effect on March 1, 2001. Following the conclusion of a three-month test phase, the new billing system entered into effect in August 2001.

Use of Public Rights of Way

Under the pre-Telecommunications Act laws, Deutsche Telekom was entitled to utilize the Federal Republic's rights of way over public property free of charge. Pursuant to the Telecommunications Act, the Federal Republic's right to use such rights of way free of charge has been transferred to licensed operators of transmission lines for public telecommunications services. Deutsche Telekom's right to utilize such rights of way has been carried over under its license. The Telecommunications Act requires that operators of transmission lines obtain the consent of the authority responsible for the maintenance of the relevant public ways before laying new transmission lines or modifying existing transmission lines. Deutsche Telekom has agreed on a cost-saving and delay-avoiding procedure with federal associations of municipal authorities to simplify the process of obtaining the required consent.

Under the Telecommunications Act, if the establishment of new transmission lines by an operator through the use of public rights of way is not feasible or technically possible or if the cost is disproportionately high, an operator of an existing transmission line using those public rights of way may be obligated to grant to the operator of those new transmission lines the joint use of its installations, such as ducts, for adequate compensation, provided no major construction work is required and such joint use is economically feasible.

Cooperation in Construction of Mobile Networks

On June 5, 2001, the German telecommunications regulator issued an interpretation of the German UMTS license conditions stating that, subject to certain conditions, the shared use by UMTS operators of wireless sites, masts, antennas, cables, combiners and cabinets is compatible with the UMTS license award conditions. The interpretation did not allow for the shared use of frequency allocations or of certain core network elements that regulate services to customers or contain sensitive network and customer data. Deutsche Telekom believes that the interpretation will allow German UMTS licenseholders (particularly new market entrants) to achieve meaningful economies in the buildout of their UMTS networks. T-Mobile and mmO2 have concluded an agreement concerning UMTS infrastructure sharing arrangements for their respective operations in Germany and the United Kingdom. The arrangements remain subject to regulatory clearances. Similar arrangements have been put in place by T-Mobile International AG's subsidiaries max.mobil in Austria and BEN in the Netherlands. Both arrangements are subject to regulatory clearance by the relevant national competition authorities.

The European Union

General

Germany is a Member State of the EU. As such, it is required to enact EU legislation in its domestic law and to take EU legislation into account in applying its domestic law. EU legislation can take a number of forms. Regulations have general application, and are binding in their entirety and directly applicable in all Member States. Directives are binding, but national authorities may choose the form and method of implementation.

Over the past fifteen years, the European Commission has opened the telecommunications markets to competition through a series of liberalization directives that gradually abolished the monopoly rights of state-owned telecommunications operators. Public voice telephony services became open to full competition in the majority of EU member states, including Germany and Austria, with effect from January 1, 1998, and had been open to full competition in the United Kingdom before that date.

The European Union has adopted a number of directives and recommendations regarding open and efficient access to, and use of, public telecommunications networks and services. These are intended to harmonize technical interfaces, usage conditions, mandatory minimum service standards for all fixed-line users, and a general framework for tariffs throughout the European Union. Specific measures have been adopted in a number of areas including licensing and interconnection. Additional obligations in relation to special network access, interconnection charging, accounting separation and cost accounting, publication and non-discrimination are imposed on operators which are designated by the national regulatory authorities in the telecommunications sector (the "NRAs") as having significant market power in a telecommunications market.

In addition, on June 23, 1999, the European Commission adopted a directive (the "Cable Directive") amending Directive 90/388/EEC (the "Services Directive") which deals with the regulation of broadband cable networks. The amendment to the Services Directive requires that the telecommunications activities and broadband cable activities of market-dominant operators be structurally separated, i.e., dominant operators are required at least to set up a separate subsidiary for their broadband cable networks (see "— Description of Business Segments — Broadband Cable"). The amendment provides for a review after the required structural separation has been accomplished, in any event not later than December 31, 2002. The amendment further provides for a procedure whereby national regulatory authorities may request that the European Commission perform such a review. This review could lead to additional measures by the European Commission, including imposition of divestiture obligations, if it finds that European competition rules are infringed.

A new European Union regulation on unbundled access to the local loop entered into force in January 2001, containing the new obligations to provide full unbundled access to the copper paired wire and at the same time unbundled access to the high frequency spectrum (line sharing). Deutsche Telekom believes that this regulation leads to over-regulation to the disadvantage of those European Union member states, such as Germany, whose domestic laws already mandate full unbundled access to the local loop.

With regard to the implementation of European legislation, in April and in July 1999, the European Commission alleged in an official notice to the Federal Republic, which represents a first step toward an official infringement proceeding, that the Federal Republic had not sufficiently implemented some aspects of the interconnection directive and the voice telephony directive. With respect to the interconnection directive, the official infringement proceeding was then initiated in November 1999. With respect to the voice telephony directive, no official infringement proceeding has been commenced to date. In both cases, the Commission alleged in particular that the Federal Republic had not sufficiently ensured the use of appropriate cost calculation systems by market-dominant providers. In response, the German telecommunications regulator has published guidelines relating to appropriate cost calculation systems. In the proceeding concerning the interconnection directive, the European Union has also alleged that the Federal Republic has not fully implemented a European Union directive requiring that any telecommunications company that has a market share of over 25 percent in a relevant market be considered as having significant market power in that market.

In a further infringement procedure initiated in January 2000, the Commission criticized the level of licensing fees in Germany.

In April 2000, the European Commission alleged in an official notice to the Federal Republic that the Federal Republic had not fully implemented the European Union full competition-directive and the ONP voice telephony directive. This notice alleges that existing tariff approval procedures do not sufficiently ensure cost-based tariffs. In particular, the notice alleges inadequate implementation of re-balancing provisions. Re-balancing means a restructuring of monthly subscriber fees and call tariffs so as to avoid cross-subsidization. To the extent that the Commission finds a violation against European Union law, there is a possibility that the access fee charged to end customers would have to be raised or that fees charged to competitors for local loop access would have to be reduced.

On October 30, 2000, the European Commission commenced against the Federal Republic an infringement proceeding alleging that the Federal Republic has failed to fully implement the European Union interconnection directive with regard to local carrier selection, and in December 2001 the European Commission decided to open a proceeding in this regard against Germany before the European Court of Justice. The German government has recently agreed on draft legislation that would mandate carrier pre-selection and call-by-call selection for local calls. If the legislation is adopted and implemented, it could have an adverse effect on the local calling area of Deutsche Telekom's business, even though the current draft legislation also provides the German telecommunications regulator with the option to suspend this obligation for technical reasons. In any event, the German Economics Ministry has stated to the EU Commission that an obligation for local carrier selection would not enter into force before December 2002.

On July 11, 2001, the European Commission issued a statement confirming that Commission inspectors and officials from national competition authorities had started carrying out simultaneous inspections at the premises of nine European mobile telephony operators located in the United Kingdom and Germany. T-Mobile Deutschland and T-Mobile UK were among the companies inspected. The Commission asserted that an European Union-wide sector inquiry into mobile roaming has established serious competition concerns regarding pricing practices for mobile roaming that warrant further investigations, particularly in the United Kingdom and Germany. The Commission statement indicated that the inspections in the United Kingdom and Germany are to ascertain whether there is consumer price fixing by mobile operators in both countries. The statement further indicated that the inspections aim to verify whether German operators have illegally fixed the wholesale prices they charge to other operators, and whether these prices are excessive or discriminatory. While the European Commission has not yet opened formal proceedings against any of the operators, it has alluded to the fact that it may do so in the course of 2002. Deutsche Telekom is fully cooperating in the investigation. If the Commission were to establish that illegal price-setting activity has occurred, it could impose fines of up to 10 percent of prior year group global sales on each company participating in the violation, although Deutsche Telekom believes that the Commission has not as yet imposed a fine to the maximum extent permissible. Deutsche Telekom does not believe that it, T-Mobile Deutschland or T-Mobile UK has engaged in any illegal price-setting for mobile roaming services. This proceeding, however, or other regulatory action relating to mobile roaming services could have a significant impact on T-Mobile's business if determined adversely to T-Mobile.

In December 2001, the European Commission decided to open an infringement proceeding against Germany, among others, for alleged failure to implement in national law the provisions of the European

Union regulation on unbundling of the local loop. The proceeding is based in particular upon the alleged absence in Germany of an adequately published formal reference offer for access to the unbundled local loop and shared lines. In view of recent developments, in particular the approval of a relevant tariff for line sharing offer by the German telecommunications regulator on March 15, 2002, the Commission is now considering whether to end the proceedings.

In March 2002 the Commission announced the commencement of an infringement proceeding against Germany for alleged failure to implement the EU regulation on the unbundling of the local loop with regard to access to local sub-loops. Details of the Commission's allegations against Germany are not yet known. Deutsche Telekom has already published an offer for access to the sub-loop, which can in principle be approved by the German telecommunications regulator as soon as a contract with a competitor has been signed. This can be no assurance, that the German telecommunications regulator will approve Deutsche Telekom's published offer.

New Regulatory Framework

At the end of 1999, the European Commission initiated a review of the EU telecommunications regulatory framework focusing on the development of competition in the European telecommunications sector and the increasing convergence of media, telecommunications and information technology. In February 2002, legislative measures were adopted consisting of a general framework directive, three specific directives regarding (i) access to and interconnection of electronic communications networks, (ii) mandatory minimum service standards for all users (''universal service'') and users' rights, and (iii) authorization and licensing regimes, as well as a decision on a regulatory framework for radio spectrum policy in the EU. EU member states are under an obligation to implement the directives into their domestic law within 15 months from adoption. The Commission also proposed a directive on data protection, which is expected to be adopted in the first half of 2002.

The new regulatory framework, in particular:

- Sets out the rights, responsibilities, decision-making powers and procedures of the NRAs and the Commission. This includes the NRAs' obligation to submit to the Commission and the NRAs of other EU member states in draft form the regulatory measures that they intend to take with respect to market definition and significant market power, and the Commission's power to require NRAs to withdraw such drafts, if the Commission considers them to create a barrier to the single European market or to be incompatible with EU law.

- Identifies specific policy objectives that NRAs have to achieve in carrying out their responsibilities (namely, to promote an open and competitive European market for communications services, to promote the interests of European citizens and to consolidate the EU's internal market in a converging technological environment).

- Provides that operators with significant market power in relevant communications markets will be subject to certain obligations as set out in the directives on universal service and access. Significant market power, a notion that includes cases where a company has market power individually or jointly with other companies, is defined on the basis of the concept of dominance as developed in the case law of the European Court of Justice and the Court of First Instance of the European Communities.

The framework directive lists a number of markets which the European Commission will have to include in its recommendation on relevant product and services markets. The recommendation will identify certain markets the characteristics of which may justify the imposition of regulatory obligations, e.g. relating to cost-orientation of prices, transparency of information, non-discrimination between customers, accounting separation, and mandated access to, and use of, network facilities. The framework directive refers to, among others, the markets for the provision of connection to and use of the public telephone network at fixed location, the wholesale markets for call origination as well as call termination and transit in the fixed public telephone network and access to the fixed public telephone network including unbundled access to the local loop. In the area of mobile communications, the framework directive contains markets for call origination and call termination on public mobile telephone networks, the market for access to public mobile telephone networks, including carrier selection, and the national market for international roaming services on public mobile telephone networks. In addition, the European Commission is considering the possibility of defining a separate market for call termination and origination into each individual mobile network in the upcoming recommendation on relevant markets.

Deutsche Telekom cannot predict what consequences the new regulatory framework will have, but it is possible that, contrary to the stated goal, it may include additional regulation of Deutsche Telekom's telecommunications business. As the instruments of the new regulatory framework are applicable to all communications markets that the Commission has included in its recommendation and where NRAs find that there is no effective competition, an extension of sector-specific regulation to mobile markets and online communications markets cannot be ruled out. The new regulatory framework will cause NRAs to reconsider their current market analysis, and the NRAs may revise their decisions with respect to market power of Deutsche Telekom's consolidated mobile subsidiaries that are active in the EU. If Deutsche Telekom or any of its significant subsidiaries were considered to be market dominant in certain markets where market-dominance is not currently considered to exist, this could materially affect Deutsche Telekom's operations. In particular, if any of Deutsche Telekom's mobile telecommunications subsidiaries were considered to be market-dominant in its home market, and consequently an obligation were imposed on that subsidiary to provide mobile termination or international roaming services at cost-oriented prices, this could materially affect that subsidiary's operations.

In certain fields that are currently subject to sector-specific regulation, the new EU regulatory framework may lead to some reduction of regulatory burdens as a result of greater flexibility of NRAs when choosing appropriate regulatory measures to address alleged market failure and the alignment of the notion of significant market power with the concept of dominance under general EU competition law. Whether any reduction of regulatory burdens will occur will largely depend on the manner in which the directives are implemented in Member States and the concepts of the new framework are applied by the EU Commission.

Deutsche Telekom expects that in any case one result of the new framework will be an increase in cooperation between the European Commission and the NRAs, with the Commission taking a leading role in deciding key regulatory issues such as market definition and market power analysis. Further directives, recommendations, communications and measures of the EU to harmonize the telecommunications sector in European Union member states are to be expected in future.

International Obligations

Over 70 member countries of the World Trade Organization (''WTO'') representing over 90 percent of the world's basic telecommunications revenues, including European Union member states and the United States, have entered into the Basic Telecommunications Agreement (''BTA'') to provide market access to some or all of their basic telecommunications services. This agreement took effect on February 5, 1998. The BTA is part of the General Agreement on Trade in Services, which is administered by the WTO. Under the BTA, signatories have made commitments to provide ''market access'', under which they are to refrain from imposing certain quotas or other quantitative restrictions in specified telecommunications services sectors, and to provide ''national treatment'', under which they are to avoid treating foreign telecommunications service suppliers differently than national service suppliers. In addition, a number of signatories have agreed to the pro-competitive principles set forth in a reference paper relating to anti-competitive behaviour, interconnection, universal service, transparency of licensing criteria, independence of the regulator and scarce resources.

In complaints filed by three US associations in February 2002, the U.S. Trade Representative has been asked to determine whether certain aspects of the telecommunications regulatory framework in Germany comply with Germany's obligations under the BTA. The principles involved relate to, among other things, leased line provisioning, fixed-to-mobile termination rates and ADSL. On April 3, 2002 the U.S. Trade Representative published its 2002 annual review. With regard to EU Member States it focused its attention on fixed-to-mobile termination rates and leased lines. The US Trade Representative stated that progress has been made with respect to fixed-to-mobile termination rates in the EU and that it will further monitor ongoing developments.

Competition Law

Deutsche Telekom is subject to German competition law, the competition rules of the EU and the competition laws of the various jurisdictions in which it conducts its business.

The German Act Against Restraints on Competition (*Gesetz gegen Wettbewerbsbeschränkungen*) prohibits the abuse of a market-dominant position as well as the distortion of competition through horizontal agreements or collusive behavior by market participants. Agreements or behavior that impose vertical restraints on competition are generally permitted, but may be prohibited by the cartel authorities if they pose a threat of significant distortion to the relevant market. They are prohibited if they constitute price fixing.

Mergers, including the creation of joint ventures, must be notified to the Federal Cartel Office before they can be executed if the concerned undertakings' turnover reaches a certain threshold but remains below the threshold above which proposed mergers must be notified to the European Commission. The Federal Cartel Office will prohibit mergers if they create or strengthen a market-dominant position. The German competition authorities are empowered to enforce these laws and may impose sanctions if their orders are contravened. Before taking action against abuses of a market-dominant position in the telecommunication sector, the Federal Cartel Office must consult with the German telecommunications regulator. Market participants damaged by abusive practices on the part of a market-dominant provider may sue for compensation under the Telecommunications Act as well as under the German Act Against Restraints on Competition.

The EU competition rules have the force of law in the Member States and are therefore applicable to Deutsche Telekom's operations in the telecommunications market. The main principles of the EU competition rules are set forth in Articles 81 and 82 of the Treaty of Rome and in the European Merger Control Regulation.

Article 81(1) of the Treaty of Rome prohibits concerted practices or other agreements between competitors which may affect trade between Member States and which restrict, or are intended to restrict, competition within the EU. Article 82 prohibits any abuse of a market-dominant position within a substantial part of the EU that may affect trade between Member States. These rules are enforced by the European Commission in cooperation with the national competition authorities (i.e., in Germany, the Federal Cartel Office). The Federal Cartel Office may also directly enforce the competition rules of the Treaty of Rome. In addition, the national courts have jurisdiction over alleged violations of EU competition law.

In 1999 and prior years, Deutsche Telekom received numerous requests for information from the European Commission. Through inquiries of this kind, the European Commission monitors the development of competition in the telecommunication markets in all member states of the European Union. Further investigations and other measures of the European Commission aimed at promoting competition in the European telecommunications sector may be expected. Deutsche Telekom and other telecommunications providers currently are subject to sector-specific inquiries in the fields of local loop unbundling, leased lines and roaming. For further information, see "— Internet Access" and "— The European Union — General."

The European Merger Regulation requires that all mergers, acquisitions and joint ventures involving participants meeting a certain turnover threshold be submitted to the European Commission for review, rather than to national authorities. Concentrations are prohibited if they pose the risk of creating or strengthening a dominant position on a relevant market.

Different Regulatory Regimes

Deutsche Telekom also is subject to the regulatory regimes of other countries where it or its subsidiaries or affiliates are active. In the area of mobile communications, in particular, Deutsche Telekom's indirect subsidiaries are subject to the national regulatory regimes of countries in which its subsidiaries operate, primarily, in addition to Germany, the United States, the United Kingdom, the Czech Republic and Austria. Regulation in these countries includes procedures for granting or renewing licenses to use scarce frequencies, coverage conditions and other conditions contained in licenses, regulation of the terms of interconnection with the networks of other network operators, requirements to permit customers to select a different carrier for individual calls or to preselect a different carrier, mobile number portability requirements and regulation relating to potential health effects of mobile communications devices. These regulations may limit the flexibility of Deutsche Telekom's mobile communications subsidiaries to respond to market conditions. In the United Kingdom, the national regulatory authority has indicated that it is considering whether T-Mobile UK should be regarded as market-dominant. In the Czech Republic, RadioMobil is considered to have significant market power. Other national regulatory authorities could take the same view. Any finding of market-dominance could subject the affected subsidiary to additional regulation, including price regulation, that could have an adverse effect on that subsidiary's business. The new regulatory framework of the European Union will be relevant in this regard. For further information regarding this legal regime, see "— The European Union — New Regulatory Framework."

In some of the countries in which Deutsche Telekom subsidiaries or affiliated companies are active, the general legal framework and the regulatory framework relating to telecommunications are less well developed than in Western Europe, leading to legal and regulatory uncertainty that could have an impact on the operations of the Deutsche Telekom group in those countries.

Deutsche Telekom has acquired UMTS licenses or is cooperating in Great Britain, Germany, the Czech Republic and Austria. Ben has acquired a UMTS license in the Netherlands. In each country, different rights and obligations for license holders are recorded in the license conditions. This lack of uniformity is relevant particularly with regard to issues such as roaming, coverage obligations and possibilities for infrastructure sharing. The European Commission recently stated that for each national telecommunications regulator it is necessary to take these differences into consideration in order to avoid undue regulatory burdens in different member states. Non-compliance with the licensing conditions could result in additional costs to Deutsche Telekom or in the revocation of licenses, although Deutsche Telekom expects to be able to comply with all UMTS licensing conditions.

DESCRIPTION OF PROPERTY

As of December 31, 2001, Deutsche Telekom's property, plant and equipment had a total book value of EUR 58.7 billion. See note 13 to the consolidated financial statements of Deutsche Telekom.

Network Infrastructure

Deutsche Telekom has made very substantial investments in its telecommunications and cable networks since 1990, including the installation of a new network in eastern Germany after German reunification in 1990. As a result, Deutsche Telekom's fixed-line network has evolved into one of the most technologically advanced major networks in the world, with fully digital trunk switching and international trunk switching, 100 percent digital local switching and 100 percent digital transmission. Deutsche Telekom has introduced asynchronous transfer mode (ATM) technology and wavelength division multiplexing (WDM) technology on the basis of its advanced network. Deutsche Telekom also owns and operates mobile communications and Internet networks.

At December 31, 2001, Deutsche Telekom's domestic public switched telephone network and ISDN network consisted of approximately 5,200 local networks (including approximately 8,000 local exchange areas) connected by a long-distance transmission network. As of December 31, 2001, the transmission network linking Deutsche Telekom's local networks consisted of approximately 173,000 kilometers of fiber optic cable.

Deutsche Telekom's international transmission infrastructure consists of both cable and satellite transmission systems, which linked Deutsche Telekom's national network directly to approximately 350 other telecommunications service providers worldwide at December 31, 2001. In addition, at December 31, 2001, Deutsche Telekom was an investor in approximately 80 fiber-optic submarine and terrestrial cables worldwide.

At December 31, 2001, the mobile communications network of Deutsche Telekom's controlled mobile subsidiaries in Germany, the United States, the United Kingdom, Austria and the Czech Republic consisted of approximately 60,000 base station cells.

Deutsche Telekom also operates a telecommunications networks for transport of national and international Internet traffic, which featured 3.5 million access ports (0.6 million dial-in-ports and 2.9 million T-DSL Ports) in its national platform at December 31, 2001.

In March 2002, T-Mobile Deutschland entered into qualified technology equipment financing arrangements with respect to operating assets in its German GSM network. For information concerning these arrangements, see note 41(g) to the consolidated financial statements of Deutsche Telekom.

Real Estate

Approximately 87 percent of the real estate portfolio of the Deutsche Telekom group relates to Deutsche Telekom AG. The real estate portfolio of Deutsche Telekom AG consists on an unconsolidated basis of about 11,766 properties with an aggregate book value at December 31, 2001 of EUR 11.4 billion. The total area of these properties amounts to approximately 57.4 million square meters, of which approximately 46.3 million square meters are developed and approximately 11.1 million square meters are undeveloped. Substantially all of these properties are used for telecommunications installations, research centers, service outlets, computer centers and offices.

Deutsche Telekom AG's real estate portfolio is managed by its wholly owned subsidiary, Deutsche Telekom Immobilien und Service GmbH (''DeTeImmobilien''). In December 2000, as part of a broader initiative to segregate its marketing activities, facility management, and internal group leasing management, Deutsche Telekom announced plans to form a joint venture with Corpus Immobiliengruppe and Morgan

Stanley Dean Witter to aid in marketing Deutsche Telekom's real estate portfolio. This joint venture started operating in May 2001 as Sireo Real Estate Asset Management GmbH ("Sireo"). Sireo is also charged with implementing cost savings measures and the management of the development of new real estate projects. Facility management activities will continue to be operated by DeTeImmobilien whereas internal group leasing management will be provided by a GMG Generalmietgesellschaft GmbH ("GMG").

Deutsche Telekom expects that a portion of its owned and leased properties presently used in its business will no longer be required in the future given reduced technical space requirements and increased mobility of its workforce. Over time, this should allow Deutsche Telekom to terminate some existing real property leases and to relocate operations from high-cost urban centers to outlying areas. In view both of this trend and of the desire to monetize non-core assets to support investment in core growth areas and reduce net indebtedness, Deutsche Telekom set course in 2000 on a strategy to monetize its real property. Such monetization may result from various financing structures under consideration or through the sale of and terminations of leases for properties no longer needed in the business. The pace and manner of the implementation of this strategy will depend on a number of factors, including prevailing market conditions within Germany, the demand for the types of property Deutsche Telekom has available and the development of the needs within Deutsche Telekom for real property. Deutsche Telekom cannot be certain that the strategy will succeed. At this time, specific plans are in formulation. As part of its preparations related to this strategy, Deutsche Telekom conducted a property-by-property valuation of the land in its real estate property portfolio. On the basis of this valuation review, Deutsche Telekom in the fourth quarter of 2001 announced a special write-down of EUR 466 million in the book value of Deutsche Telekom's real estate portfolio.

For a discussion of this write-down and a prior special write-down of EUR 2.0 billion in the book value of the real estate portfolio recorded in respect of the fourth quarter of 2000, please refer to "Item 5. Operating and Financial Review and Prospects — Factors Affecting Deutsche Telekom's Business — Real Estate" and to notes 6, 35 and 38 to the consolidated financial statements of Deutsche Telekom.

The headquarters of Deutsche Telekom is located in a leased building in Bonn. Deutsche Telekom also leases a number of other buildings.

In addition to its real estate portfolio, Deutsche Telekom owns numerous telecommunications installations throughout Germany, including exchanges of various sizes, transmission equipment, computer installations, cable networks, base stations for cellular networks and equipment for television and radio broadcasting. The aggregate book value of the Deutsche Telekom group's technical equipment and machinery at December 31, 2001 was EUR 39.9 billion.

The Bonn public prosecutor is conducting an investigation that relates to Deutsche Telekom's real property valuations. Please refer to "Item 8. Financial Information — Litigation" for information on this investigation and related subjects.

ITEM 5. Operating and Financial Review and Prospects

You should read the following discussion in conjunction with the annual consolidated financial statements, including the notes to those financial statements. Those financial statements have been prepared in accordance with the requirements of the German Commercial Code (HGB — German GAAP), which differ in certain significant respects from U.S. GAAP. For a discussion of the principal differences between German GAAP and U.S. GAAP as they relate to Deutsche Telekom and a reconciliation of net income and total shareholders' equity to U.S. GAAP, see "— Reconciling differences between German GAAP and U.S. GAAP" and note 38 to the consolidated financial statements.

Introduction

Revenues increased by EUR 7.4 billion, or 18 percent, from 2000 to 2001. The consolidation in 2001 of companies acquired during 2000 and 2001 contributed EUR 6.2 billion to the overall increase in revenues. Revenue growth prior to the effect of acquisitions resulted primarily from the mobile communications, systems solutions and online segments.

Deutsche Telekom reported a net loss of EUR 3.5 billion for the 2001 financial year, compared with a previous year net profit of EUR 5.9 billion. This development is due in part to an increase of EUR 2.2 billion in amortization (principally amortization of goodwill and UMTS licenses) and an increase of EUR 1.8 billion in net financial expenses (without regard to the positive impact of the sale of Deutsche Telekom's indirect interest in WIND in 2000). In addition the decline in net income resulted from a high level of net income from unusual or infrequently occurring factors in 2000 that was not matched by a comparably high level of net income from such factors in 2001. For further information on these factors, see "Effects of Acquisitions and of Unusual or Infrequent Items on Deutsche Telekom's Statements of Operations for the Three Years Ended December 31, 2001 — Unusual or infrequently occurring items."

Outlook for 2002

The strategies and expectations referred to in this outlook discussion may be strongly influenced or changed by shifts in market conditions, new initiatives undertaken by Deutsche Telekom and other factors. Please refer to "Item 3. Key Information — Risk Factors" and "Forward-Looking Statements" for a description of some of the factors relevant to this discussion and other forward-looking statements in this report. Deutsche Telekom cannot guarantee that the strategies and expectations referred to in this discussion will come to fruition.

Revenues

In the T-Mobile segment, Deutsche Telekom expects an increase in revenues from 2001 to 2002, largely as a result of the fact that VoiceStream and Powertel will be consolidated for the first time for a full year in 2002. Organic revenue growth also is expected to occur in Deutsche Telekom's European mobile operations due to the expected growth in the average number of customers in those operations in 2002.

In the T-Com segment, Deutsche Telekom expects further declining revenues from call charges in 2002. Deutsche Telekom also expects, however, continued growth in revenues from access charges, due to further growth in ISDN and T-DSL. Assuming that the remaining regional cable television companies are sold in 2002, their revenues will no longer be consolidated in the revenues of Deutsche Telekom or of the T-Com segment.

In the T-Systems segment, Deutsche Telekom expects an increase in revenues, primarily due to opportunities in the areas of computing services and systems integration and increasing opportunities in the area of convergence solutions that combine information technology and telecommunications.

In the T-Online segment, Deutsche Telekom expects an increase in revenues, largely as a result of growth in the number of access customers, but to an increasing extent as a result of growth in the portal business.

Overall, Deutsche Telekom expects that, due to the impact of these developments, net revenue in 2002 will be higher than in 2001, despite the possible loss of cable revenue if cable operations are sold during the year. Price-related revenue decreases in fixed-network voice telephony in Germany should be more than offset by increases in revenues in the areas of mobile communications, data communications and systems solutions and consumer Internet services.

Costs

Costs for goods and services purchased are expected to increase moderately, largely as a result of companies newly acquired in 2001.

Personnel costs are expected to increase moderately, as increases resulting primarily from companies newly acquired in 2001 are expected to be offset to some extent by further reductions in personnel costs in companies that were part of the Deutsche Telekom group prior to 2001.

Depreciation and amortization are expected to be considerably higher in 2002 than in 2001, as depreciation and amortization at VoiceStream will be included in Deutsche Telekom's financial statements for a full year in 2002.

The development of net financial expense in 2002 will be influenced to a degree by the progress of Deutsche Telekom's debt reduction program. Unless proceeds on the disposition of assets, such as interests in regional cable television companies, and proceeds from the stock exchange listing of subsidiaries are substantial, net financial expense is likely to be higher in 2002 than in 2001, due to the impact of the first-time full-year consolidation of interest expense of VoiceStream and Powertel as well as the impact of Deutsche Telekom's purchase of the remaining interests in debis Systemhaus in 2002.

The recent downgrade in Deutsche Telekom's long-term debt ratings by Moody's and Standard & Poor's has caused an increase in the interest rate in 2002 on a portion of Deutsche Telekom's outstanding indebtedness, which will tend to increase interest expense in 2002 as compared to 2001.

Other Factors

In the event that the remaining regional cable companies, or majority interests in those companies, are sold during 2002, Deutsche Telekom expects that these sales will have a positive effect on results in 2002. Dilution gains resulting from the stock exchange listing of subsidiaries also would have a positive impact on net income in 2002, although no decision to undertake any such listing during 2002 has been reached. The sale of real estate may contribute positively to cash flows in 2002 and beyond, although the impact on net income of any such sales will depend on the specific properties that are sold. While Deutsche Telekom expects that its earnings before interest, taxes, depreciation and amortization without regard to unusual or infrequently occurring items (such as the disposition of assets or dilution effects from the stock exchange listing of subsidiaries) will increase from 2001 to 2002, net loss prior to the effect of such unusual or infrequent items is not expected to be less in 2002 than in 2001.

Factors Affecting Deutsche Telekom's Business

Deutsche Telekom's business has been affected in recent years by a number of important trends. Investments in new subsidiaries and in new technologies, sales of non-core assets, a decline in the importance of the traditional fixed-network voice telephony business, increased competition and regulatory constraints all have influenced and are expected to have significant continued influence on Deutsche Telekom's business. In addition, the rapidly expanding market for mobile and Internet communications, steady growth in data transmissions and rapid technological change are reshaping the business of telecommunications.

Investment in VoiceStream

In May 2001, Deutsche Telekom acquired VoiceStream and Powertel in exchange for Deutsche Telekom shares having a market value on the acquisition date of EUR 28.7 billion plus EUR 4.9 billion in cash. Amortization of goodwill, and depreciation and amortization of assets acquired in this transaction, will have a substantial impact on Deutsche Telekom's results of operations in the coming years. In addition, Deutsche Telekom expects VoiceStream and Powertel to incur significant operating losses and to generate negative cash flow from operating activities for the foreseeable future while they continue to develop their networks and grow their subscriber base, and these operating losses and negative cash flow from operating activities also will significantly impact Deutsche Telekom's financial statements in coming years. For further information in this regard, see "Item 3. Key Information — Risk Factors."

Investment in UMTS Licenses and Infrastructure

Deutsche Telekom has made substantial investments in UMTS licenses and is making substantial investments in the build-out of UMTS networks. The economic success of these investments will depend upon the availability of services based on UMTS technology that will be attractive enough to customers to generate sufficient traffic volume and sufficiently high prices. The level of demand for such UMTS services that will prevail in the future is unknown, however, and may not justify the cost of providing UMTS services. These costs include the costs of acquiring UMTS licenses and constructing, maintaining and upgrading UMTS networks. For further information in this regard, see "Item 3. Key Information — Risk Factors."

Effects of Acquisitions and of Unusual or Infrequent Items on Deutsche Telekom's Statements of Operations for the Three Years Ended December 31, 2001

The comparison of Deutsche Telekom's statements of operations for the years 2001, 2000 and 1999 to one another is complicated by a number of acquisitions that Deutsche Telekom has made during those years and by a number of unusual or infrequent items that affected other operating income, other operating expense, depreciation and amortization, net financial expense and tax expense in 2001 and 2000. The effects of acquisitions and of unusual or infrequently occurring items are discussed in context below under the caption "— Consolidated Results of Operations."

Unusual or infrequently occurring items

Other operating income, other operating expense, depreciation and amortization, net financial expense and tax expense of Deutsche Telekom were all influenced by one or more unusual or infrequently occurring items during 2000 and 2001.

These unusual or infrequently occurring items included the following:

Other operating income. In 2001, other operating income was influenced by gains on the sale of Deutsche Telekom's interests in Sprint (EUR 2.0 billion), gains on the sale of interests in the regional cable television company for the German state of Baden-Württemberg (EUR 912 million), gains on the sale of regional cable service companies (EUR 0.1 billion) and gains on the reversal of provisions for general real estate risks (EUR 0.3 billion) that were offset by unscheduled depreciation in an equal amount relating to buildings.

In 2000, other operating income was influenced by the sale of Deutsche Telekom's interest in the Global One joint venture (EUR 2,864 million), dilution gains from the public offerings of shares by T-Online, MTS and comdirect (EUR 2.9 billion) and gains from the sale of interests in regional cable television companies for the States of Nordrhein-Westfalen and Hessen (EUR 3.0 billion).

Personnel expense. Personnel expense in 2001 was influenced by an additional minimum pension liability (EUR 259 million).

Other operating expense. Other operating expense in 2001 was influenced by offering expenses relating to the sale of Deutsche Telekom's interests in Sprint (EUR 0.1 billion). Other operating expense in 2000 was influenced by losses on disposition of non-current assets (EUR 0.5 billion) and additions to provisions (EUR 0.4 billion).

Depreciation and amortization. Depreciation and amortization in 2001 was influenced by an unscheduled write-down of the book value of tradenames of One 2 One and max.mobil (EUR 1.0 billion) relating to a rebranding campaign conducted by T-Mobile, an unscheduled write-down of the book values of real property (EUR 466 million) and unscheduled depreciation in the amount of EUR 0.3 billion on buildings that was offset by gains in an equal amount on the reversal of provisions relating to general real estate risks. Depreciation and amortization in 2000 was influenced by an unscheduled write-down of the book values of real property (EUR 2.0 billion) and an unscheduled write-down of parts of the old copper-based long-distance cable network (EUR 1.0 billion).

Net Financial Expense. Net financial expense in 2001 was influenced by an unscheduled write-down of the book values of shares in France Telecom that are held by Deutsche Telekom (EUR 312 million) and in comdirect (EUR 0.1 billion), debenture bonds received by Deutsche Telekom in connection with the sale of regional cable companies (EUR 0.4 billion) and shares in a regional cable company (EUR 0.1 billion). Net financial expense in 2000 reflects gains from the sale of Deutsche Telekom's interest in the Italian mobile joint venture WIND (EUR 2.3 billion).

Income Tax Expense. Deutsche Telekom recognized an income tax benefit in 2001 of EUR 1.0 billion related to unusual or infrequently occurring items. Income tax expense for 2001 was positively influenced by a favorable tax ruling regarding the deductibility of a write-down recorded in the financial statements of Deutsche Telekom AG in 2000 related to the carrying value of its shareholdings in Sprint (EUR 0.9 billion).

In addition, Deutsche Telekom estimates that the aggregate tax effect of all of the unusual or infrequent items mentioned above was approximately EUR 0.1 billion for 2001 and approximately EUR 0.3 billion for 2000.

Deutsche Telekom estimates that all of the foregoing unusual or infrequent items had an aggregate positive impact on net income after taxes of approximately EUR 1.2 billion for 2001 and approximately EUR 7.4 billion for 2000.

Network Communications

One of the most important trends that has affected Deutsche Telekom since the introduction of full competition in January 1998 has been the decline in the percentage of Deutsche Telekom's revenues accounted for by the traditional fixed-network voice telephony business. That business accounted for 30.2 percent of Deutsche Telekom's external revenues in 2001, as compared to 36.8 percent in 2000. This decrease has resulted both from competition within the fixed-network voice telephony business in Germany and from the increasing popularity of mobile telephones.

Competition within the fixed-network voice telephony business has been significantly influenced by decisions of the German telecommunications regulator. On the basis of interconnection rates fixed by the German telecommunications regulator, numerous competitors are able to compete with Deutsche Telekom with minimal or modest investments in network infrastructure and with prices that often undercut Deutsche Telekom's pricing. The decision by the German telecommunications regulator to further reduce interconnection rates for 2000 led to intensified competition in this area. For further information concerning interconnection rates, see "Item 4. Information on the Company — Regulation — Special Network Access and Interconnection". This competition has led to a reduction of Deutsche Telekom's market share. According to an estimate of the German telecommunications regulator, Deutsche Telekom had an 54.3 percent share of the overall German telecommunications market in 2001, as measured in terms of minute volume. As a result of declining market share, the number of minutes of traffic carried on Deutsche Telekom's fixed network that gave rise to revenues shown under network communications decreased from 2000 to 2001, despite a higher rate of growth in the overall market.

Deutsche Telekom has begun to lose some market share in the local voice telephony market. Deutsche Telekom is required to provide competitors with unbundled access to its subscriber access lines, and the German telecommunications regulator has set a monthly tariff for this unbundled access that is substantially lower than Deutsche Telekom had sought in its tariff application. In addition, regulatory measures of the German telecommunications regulator have required Deutsche Telekom to offer access and local calling services to competitors at wholesale prices, and the German telecommunications regulator and the European Union have instituted requirements for further unbundling of the local loop. Regulatory measures affecting the degree of competition in the local voice telephony market are described in greater detail in "Item 4. Information on the Company — Regulation." Due to these and other regulatory developments, Deutsche Telekom expects that it will continue to face increasing competition on the local network level in the future.

Competition within the German fixed-line voice telephony market has also led to sharply declining tariffs. During the past three years, Deutsche Telekom has introduced several tariff reductions to address competitive challenges and, in some instances, to meet regulatory requirements imposed by the price cap regime applicable to the tariffs for Deutsche Telekom's public fixed-line voice telephony services.

Due to declining tariffs for mobile voice telephony services in Germany, which have both resulted from and contributed to increased demand for mobile telephony services, mobile phones increasingly compete with Deutsche Telekom's traditional fixed-network voice telephony business, particularly in the market for local calls.

Regulation and Litigation

Deutsche Telekom's business has been and continues to be strongly influenced by the regulatory regime applicable to telecommunications service providers in Germany. Deutsche Telekom is viewed by the German telecommunications regulator as dominant in markets that form a significant part of Deutsche Telekom's business, including the market for fixed-network voice telephony services. As a result, Deutsche Telekom is subject to regulatory requirements in various aspects of its business, including the obligation to submit tariffs charged for various services to the German telecommunications regulator for approval and universal service obligations in some areas, that do not apply to its competitors. For a description of the regulatory regime to which Deutsche Telekom is subject, see "Item 4. Information on the Company — Regulation."

Deutsche Telekom is continuously engaged in litigation and other forms of dispute resolution with regulators, competitors and other parties. For further information concerning these disputes, see ''Item 8. Financial Information — Litigation.''

Technology

In the longer term, rapid technological changes in telecommunications and information technology will continue to have a profound effect on the way Deutsche Telekom does business and give rise to new competitive challenges, particularly as the traditional businesses of telecommunications, information technology, media, entertainment and security converge. Technological advances have increased the capacity and bandwidth of telecommunications networks and led to the rise in the number of alternatives to fixed network transmission. Multiple forms of mobile communications, broadband cable and wireless transmission and Internet technology and their declining costs are increasing the sources of competition faced by Deutsche Telekom's traditional business, although they also open new opportunities arising from the convergence of information and communications technologies.

Real Estate

Deutsche Telekom is pursuing a strategy of reducing its holdings of assets that are outside the scope of its core activities. Although Deutsche Telekom makes extensive use of real property in the operation of its business, Deutsche Telekom does not view the ownership and management of real estate as one of its core activities. Accordingly, Deutsche Telekom is moving to reduce its real property holdings. As part of its preparations relating to this strategy. Deutsche Telekom conducted a property-by-property valuation of the land in its real property portfolio. On the basis of this valuation review, Deutsche Telekom in the fourth quarter of 2001 announced a special write-down of EUR 466 million in the book value of Deutsche Telekom's real estate portfolio. Deutsche Telekom had earlier recorded in the fourth quarter of 2000 EUR 2.0 billion unscheduled write-down of the book value of land in its real estate portfolio, which, together with scheduled and unscheduled depreciation in 2001, gave Deutsche Telekom at December 31, 2001 an aggregate book value of real estate on a consolidated basis of EUR 13.1 billion. The special write-downs had no effect on Deutsche Telekom's U.S. GAAP net income or shareholders' equity for the relevant years. Based on presently available information, Deutsche Telekom believes that the level of the special write-downs described below and its current provisions for risks related to real estate are appropriate. For additional information concerning Deutsche Telekom's real estate strategies, please refer to ''Item 4. Information on the Company — Description of Properties''. Please refer to notes 6 and 38 to the Consolidated Financial Statements of Deutsche Telekom for further information concerning the special write-downs.

Deutsche Telekom's real estate was recorded in the opening balance sheet at January 1, 1995 at fair market value as described in the notes to the Consolidated Financial Statements under ''Summary of accounting policies — Accounting and valuation''. At December 31, 2001, Deutsche Telekom had established reserves of EUR 168 million on its balance sheet for risks related to real estate.

In view of the size of Deutsche Telekom's real estate portfolio and the company's focus on accelerated dispositions, the development of the German real estate market, as influenced by economic growth expectations and prevailing interest rate levels, over the next few years will be among a number of significant factors that may affect the financial position and results of operation of Deutsche Telekom.

Critical Accounting Policies under German GAAP

Deutsche Telekom's discussion and analysis of its financial condition and results of operations are based upon Deutsche Telekom's consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in Germany. Reported financial condition and results of operations of Deutsche Telekom are sensitive to accounting methods, assumptions and estimates that underlie preparation of the financial statements. Deutsche Telekom bases its estimates on historical experience and on various other assumptions, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources.

The selection of critical accounting policies, the judgments and other uncertainties affecting application of those policies and the sensitivity of reported results to changes in conditions and assumptions are factors to be considered when reviewing Deutsche Telekom's financial statements. Deutsche Telekom believes the following critical accounting policies involve the most significant judgments and estimates used in the preparation of its consolidated financial statements.

Accounting for Long-lived Assets

Property, plant and equipment and purchased intangible assets other than goodwill are recorded at acquisition cost. If such assets are acquired in a business combination, the purchase price is allocated to the estimated fair value of the acquired property, plant and equipment and intangible assets. Property, plant and equipment and intangible assets are depreciated or amortized on a straight-line basis over their estimated useful lives, including UMTS licenses which are amortized over the terms of the licenses.

Property, plant and equipment are valued at acquisition or construction cost, less scheduled depreciation. Construction costs include directly allocable costs, an appropriate allocation of material and production overhead and interest accruing during the construction. However, general administration expenses are not capitalized. As permitted by Postreform II, the legislation by which the former Deutsche Bundespost Telekom was legally transformed into a stock corporation, property, plant and equipment transferred to Deutsche Telekom AG on January 1, 1995 were recorded in the opening balance sheet of Deutsche Telekom AG at fair market values at that date. However, due to the short period of time between the acquisition dates and January 1, 1995, property, plant and equipment acquired during 1993 and 1994 were valued at their remaining book value. The remaining useful lives and the depreciation methods applicable to these assets were not changed. Except as described in this paragraph, the fair market values shown in the opening balance sheet have been carried forward as the acquisition costs. Deutsche Telekom decided in late 2000 to introduce a real estate strategy oriented toward the monetization of its real estate portfolio. As a consequence, a new valuation approach based on the current replacement costs for Deutsche Telekom's individual plots of land was adopted whereby the lower of the net book value or replacement cost was recorded. The comparison of the newly calculated replacement costs with the carrying amounts resulted in downward adjustments to book value totalling EUR 2.5 billion.

Accounting for long-lived assets and intangible assets involves the use of estimates for determining the fair value at the acquisition date, especially in the case of such assets acquired in a business combination, and the useful lives of the assets over which the costs of acquiring these assets are charged to the income statement.

When an impairment in the value of assets occurs, nonscheduled write-downs are made. Deutsche Telekom assesses the impairment of identifiable intangibles and long-lived assets whenever there is reason to believe that the carrying value may exceed the fair value and where a permanent impairment in value is anticipated. The determination of impairments of long-lived and intangible assets involves the use of estimates which include but are not limited to the cause, the timing and the amount of the impairment. Impairment is based on a broad measure of factors. In evaluating assets for impairment, Deutsche Telekom applies the German commercial law principle of prudence (*Vorsichtsprinzip*) (Sec. 252 (1) (4) of the German Commercial Code) in conjunction with the individual valuation principle (*Einzelbewertungsgrundsatz*). Among other things, Deutsche Telekom typically considers technological obsolescence, discontinuance of services and other changes in circumstances that indicate an impairment.

Valuation of Goodwill

Goodwill resulting from business combinations is amortized on a straight-line basis over its useful life. The determination of goodwill is dependent on the allocation of the purchase price to the tangible and intangible assets acquired and the liabilities assumed. Such an allocation is based on management's judgment. In addition, the useful life assigned to goodwill is an estimate based on the judgment of management at the time of acquisition.

Nonscheduled write-downs are provided when an impairment in the value of goodwill occurs. Deutsche Telekom reviews, on a regular basis, the performance of its subsidiaries. When there is reason to believe that the goodwill arising from the acquisition of that subsidiary is impaired and that the impairment is of a permanent nature, Deutsche Telekom compares the carrying amount of that subsidiary to its fair value. The determination of the fair value of a subsidiary involves extensive use of estimates, depending on the method used. Significant management judgment is involved. Methods commonly used by Deutsche Telekom for valuations include discounted cash flow methods and quoted stock market prices, if available. Factors affecting estimated fair values typically include discount rates, future cash flows, market prices and control premiums. These estimates, including the methodologies used, are important in determining fair value and ultimately the amount of any goodwill write-down.

Financial Assets

Deutsche Telekom holds minority interests in companies having operations or technology in areas within its strategic focus, some of which are publicly traded and have highly volatile share prices. Deutsche Telekom records an investment impairment charge when it believes an investment has experienced a decline in value that is permanent. Determining whether an impairment is permanent involves a judgment and relies heavily on an assessment by management regarding the future development of the investee. In measuring impairments, Deutsche Telekom uses quoted market prices, if available, or other valuation methods, based on information available from the investee.

Future adverse changes in market conditions or poor operating results of underlying investments could result in losses or an inability to recover the carrying value of the investments that may not be reflected in an investment's current carrying value, thereby possibly requiring an impairment charge in the future.

Allowance for Doubtful Accounts

Management maintains an allowance for doubtful accounts for estimated losses resulting from the inability of Deutsche Telekom's customers to make required payments. Management bases its estimates on the aging of Deutsche Telekom's accounts receivable balances and Deutsche Telekom's historical write-off experience, customer credit-worthiness and changes in Deutsche Telekom's customer payment terms when evaluating the adequacy of the allowance for doubtful accounts. If the financial condition of Deutsche Telekom's customers were to deteriorate, actual write-offs may be higher than expected.

Deferred Taxes

Deutsche Telekom is required to estimate its income taxes in each of the jurisdictions in which it operates. This process involves the jurisdiction-by-jurisdiction estimation of actual current tax exposure and the assessment of temporary differences resulting from differing treatment of items, such as accruals and amortization, for tax and financial reporting purposes. These differences result in deferred tax assets and liabilities, which are included within Deutsche Telekom's consolidated balance sheet. Deutsche Telekom must assess in the course of its tax planning procedures the fiscal year of the reversal of its deferred tax assets and liabilities and if there will be future taxable profits in those periods. Deutsche Telekom reverses in the current year deferred tax assets and liabilities for timing differences that have been recorded if Deutsche Telekom anticipates that the future reversal will take place in a tax loss year. If Deutsche Telekom estimates that timing differences of a current year will be reversed in a latter tax loss year, Deutsche Telekom does not record deferred tax assets and liabilities for those timing differences.

Significant management judgment is required in determining Deutsche Telekom's provision for income taxes, deferred tax assets and liabilities. Under German GAAP, Deutsche Telekom does not record deferred tax assets consisting of net operating losses carried forward and foreign tax credits. The analysis is based on the estimates of taxable income in the jurisdictions in which the group operates and the period over which the deferred tax assets and liabilities will be recoverable. If actual results differ from these estimates, or Deutsche Telekom adjusts these estimates in future periods, Deutsche Telekom's financial position and results of operations may be affected.

Accrued Liabilities

Considerable judgment is exercised by Deutsche Telekom in recording the Company's accrued liabilities and its exposure to contingent liabilities related to pending litigation or other outstanding claims subject to negotiated settlement, mediation, arbitration or government regulation as well as other contingent liabilities. Judgment is necessary in assessing the likelihood that a pending claim will succeed or a liability will arise and to quantify the possible range of the final settlement. In case the occurrence of a contingency is more likely than not, Deutsche Telekom accrues an amount for contingent liabilities that represents management's estimate at the time of the balance sheet. Because of the inherent uncertainties in the foregoing evaluation process, actual losses may be different from the original estimated amount accrued.

Consolidated Results of Operations

The following table shows information concerning Deutsche Telekom's statements of operation for the periods indicated:

	Year ended December 31, 2001			Year ended December 31, 2000			1999
	Pre-acquisitions	Effects of acquisitions	Total	Pre-acquisitions	Effects of acquisitions	Total	Total
	(millions of euro)			(millions of euro)			(millions of euro)
Net revenue	42,061	6,248	48,309	37,514	3,425	40,939	35,470
Changes in inventories and other own capitalized costs	630	249	879	846	18	864	947
Total operating performance	42,691	6,497	49,188	38,360	3,443	41,803	36,417
Other operating income	6,457	162	6,619	10,798	204	11,002	1,871
Goods and services purchased	(11,321)	(2,156)	(13,477)	(10,295)	(1,655)	(11,950)	(7,667)
Personnel costs	(10,332)	(1,782)	(12,114)	(9,057)	(661)	(9,718)	(9,210)
Depreciation and amortization	(12,165)	(3,056)	(15,221)	(11,483)	(1,508)	(12,991)	(8,466)
Other operating expenses	(9,863)	(2,288)	(12,151)	(9,074)	(1,350)	(10,424)	(6,872)
Financial income (expense), net	(5,094)	(254)	(5,348)	(983)	(247)	(1,230)	(2,889)
Results from ordinary business activities	373	(2,877)	(2,504)	8,266	(1,774)	6,492	3,184
Extraordinary income (loss)	—	—	—	(159)	—	(159)	(240)
Taxes	(614)	(194)	(808)	(262)	(56)	(318)	(1,420)
Income (loss) after taxes	(241)	(3,071)	(3,312)	7,845	(1,830)	6,015	1,524
(Income) losses applicable to minority shareholders	(72)	(70)	(142)	(211)	122	(89)	(271)
Net income (loss)	(313)	(3,141)	(3,454)	7,634	(1,708)	5,926	1,253

Acquisitions

During the three years ended December 31, 2001, Deutsche Telekom acquired shares in a number of companies, and as a result the financial results of many of these companies were consolidated in Deutsche Telekom's financial statements for the first time during that three-year period. The principal consolidated subsidiaries acquired by Deutsche Telekom during the three years ended December 31, 2001, and the dates on which these entities became consolidated subsidiaries of Deutsche Telekom, are as follows:

- max.mobil (April 1999)
- One 2 One (October 1999)
- debis Systemhaus (October 2000)
- VoiceStream and Powertel (May 2001)

The consolidation of a newly acquired subsidiary complicates the comparison of the statements of operations for the year prior to the acquisition, the year of the acquisition and the year following the acquisition, because the newly consolidated subsidiary is not reflected in the consolidated financial statements for the year prior to the acquisition, is reflected in the consolidated financial statements for only part of the year when the acquisition takes place and is reflected in the consolidated financial statements for a full year in the year following the acquisition. To facilitate the comparison of Deutsche Telekom's statements of operations for each of the three years in the period ended December 31, 2001, the above tables summarize the effect of changes in the composition of the consolidated Deutsche Telekom group on Deutsche Telekom's statements of operations.

Net Revenues

Net revenue of Deutsche Telekom amounted to EUR 48.3 billion in 2001, representing an increase of EUR 7.4 billion, or 18 percent, over 2000. Of this increase, changes in the composition of the Deutsche Telekom group in 2001 accounted for EUR 6.2 billion, including EUR 2.8 billion relating to the first-time consolidation of VoiceStream and Powertel starting in June 2001 and EUR 2.2 billion relating to the first-time consolidation of the debis Systemhaus group starting in October 2000. Without regard to changes in the composition of the Deutsche Telekom group in 2001, revenues increased by EUR 1.1 billion, or 2.7 percent, from 2000 to 2001. This increase consisted of increased revenues in the T-Mobile and T-Systems divisions (before acquisitions) and in the T-Online division that were partially offset by decreased revenues in the T-Com division.

Net revenues of Deutsche Telekom amounted to EUR 40.9 billion in 2000, representing an increase of EUR 5.5 billion, or 15.4 percent, over 1999. Of this increase, changes in the composition of the Deutsche Telekom group accounted for EUR 3.4 billion. Without regard to changes in the composition of the Deutsche Telekom group, revenues increased by EUR 2.0 billion, or 5.8 percent, from 1999 to 2000. Again, increases in revenues of T-Mobile, T-Systems and T-Online were partially offset by decreased revenues from T-Com.

For further information on revenue trends in individual segments, see ''— Segment Analysis'' below.

Changes in Inventories and Other Own Capitalized Costs

Deutsche Telekom's statement of operations is prepared on the total-cost basis typically used in Germany. Cost line items in Germany typically include all costs incurred during the year. Total costs, however, often include expense items that are capitalized either in inventories (mainly cost of goods purchased, but not yet used) or as part of other assets (mainly personnel costs or interest relating to construction in progress). To reflect this fact and to permit the presentation of a net income/(loss) that does not include capitalized costs, the total-cost approach uses the adjusting line item ''Changes in inventories and other own capitalized costs''.

Changes in inventories and other own capitalized costs increased by EUR 15 million, or 1.7 percent, from 2000 to 2001. Inventories of work in process decreased by EUR 168 million, reflecting a mixture of offsetting effects in various companies of the Group. Own capitalized costs increased EUR 183 million, primarly due to changes in the composition of the consolidated Deutsche Telekom group and to an increase in own capitalized costs at other parts of Deutsche Telekom. Own capitalized costs relate primarily to planning and construction services. They include interest incurred during the construction period in the amount of EUR 65 million, EUR 64 million and EUR 63 million in 2001, 2000 and 1999, respectively.

Changes in inventories and other own capitalized costs decreased by EUR 83 million, or 8.8 percent, from 1999 to 2000. Inventories of work in process decreased by EUR 55 million, reflecting a mixture of offsetting effects in various companies of the group. Own capitalized costs decreased EUR 28 million, as the impact of recent acquisitions was offset almost entirely by a decrease in own capitalized cost at other parts of Deutsche Telekom.

Other Operating Income

Other operating income consists of tax refunds, reversals of allowances and accruals, cost reimbursements, gains from sales of marketable securities and assets, foreign currency gains and other miscellaneous items.

Other operating income of Deutsche Telekom amounted to EUR 6.6 billion in 2001, representing a decrease of EUR 4.4 billion, or 39.8 percent, compared to 2000. Other operating income for 2000 was positively affected by several unusual or infrequent factors, principally earnings from the sale of Deutsche Telekom's interest in Global One (EUR 2,864 million), earnings from the sale of interests in regional cable companies in Nordrhein-Westfalen and Hessen (EUR 3.0 billion) and the dilution effects resulting from the initial public offering of T-Online International AG (EUR 2.7 billion) and other investments (EUR 230 million).

Further, other operating income for 2001 was positively affected by several unusual or infrequent factors, principally gains from the sale of the Company's Sprint shares (EUR 2.0 billion) and from the sale of the regional cable company in Baden-Württemberg (EUR 912 million). Without regard to the unusual or infrequent factors discussed above, other operating income increased from EUR 2.3 billion in 2000 to EUR 3.7 billion in 2001, largely as a result of increased realized foreign currency gains and the release of accruals mainly for outstanding invoices and risks arising from property damage claims. Other operating income also was positively affected in 2001 by a reversal of general provisions for real estate related risks in the amount of EUR 350 million. This reversal of provisions was offset by an unscheduled write-down for the same amount with respect to specific properties. For further information in this regard, see ''— Depreciation and Amortization.''

Without the unusual or infrequently occurring factors described above that affected 2000, other operating income increased EUR 416 million, or 22.2 percent, from 1999 to 2000. Of this increase, EUR 204 million was due to the effects of the change in the composition of the group. An increase in other operating income from foreign currency gains and other income was offset by reduced value-added tax refunds and reduced income from a national roaming agreement between T-Mobile Deutschland and VIAG Interkom.

Pursuant to the Value-Added Tax Act (*Umsatzsteuergesetz*), Deutsche Telekom is entitled to recover a portion of the VAT incurred on assets purchased and placed into service before January 1, 1996, the date on which Deutsche Telekom became fully subject to VAT. Deutsche Telekom has reclaimed a total of EUR 2.7 billion since 1996. The refund amounted to EUR 85 million, EUR 169 million and EUR 379 million in 2001, 2000 and 1999, respectively.

Goods and Services Purchased

The following table presents information concerning goods and services purchased.

	Year ended December 31,			Year ended December 31,	
	2001	2000	1999	2001/2000	2000/1999
	(millions of euro)			(% change)	
Goods purchased	4,397	4,075	2,625	7.9	55.2
Services purchased					
Domestic network access charges	2,174	1,985	1,585	9.5	25.2
International network access charges	3,268	2,819	1,626	15.9	73.4
Total network access charges	5,442	4,804	3,211	13.3	49.6
Other services purchased	3,638	3,071	1,831	18.5	67.7
Total services purchased	9,080	7,875	5,042	15.3	56.2
Total goods and services purchased	13,477	11,950	7,667	12.8	55.9

Goods and services purchased amounted to EUR 13.5 billion in 2001, representing an increase of EUR 1.5 billion, or 12.8 percent, compared to 2000. The increase in goods and services purchased reflects changes in the composition of the Deutsche Telekom group in 2000 and 2001 of EUR 2.2 billion, principally VoiceStream and Powertel (EUR 964 million) and the debis Systemhaus group (EUR 761 million). Without regard to the effects of changes in the composition of the consolidated Deutsche Telekom group, goods and services purchased decreased by EUR 629 million, largely as a result of a decline in the number of mobile handsets purchased for resale.

Goods purchased increased from 2000 to 2001 (7.9 percent) as a result of the changes in the composition of the Deutsche Telekom group, principally VoiceStream and Powertel (EUR 621 million). Excluding the effects of the changes in the composition of the Deutsche Telekom group, the goods purchased decreased due to the decline in the number of mobile handsets purchased for resale.

Goods purchased increased from 1999 to 2000 primarily as a result of the acquisition of new subsidiaries and of increased purchases of mobile handsets for resale. Changes in the composition of the Deutsche Telekom group in 1999 and 2000 (principally One 2 One and debis Systemhaus) contributed approximately 47 percent to the increase in goods purchased. Excluding the effects of the new acquisitions, the increase in goods purchased resulted primarily from an increase in the number of mobile handsets purchased which were used as part of package offers for new subscribers in Deutsche Telekom's existing mobile businesses.

Domestic network access charges increased by 189 million, or 9.5 percent from 2000 to 2001. These charges arise principally from calls that are initiated by Deutsche Telekom's customers or routed through Deutsche Telekom's network and that are terminated in the networks of other fixed and mobile network operators in Germany. The increase in 2001 resulted primarily from increase in calls routed through Deutsche Telekom's network. An increase in the volume of these types of calls led to an increase of EUR 400 million, or 25.2 percent, in domestic network access charges from 1999 to 2000.

International network access charges increased from 2000 to 2001 primarily due to changes in the composition of the Deutsche Telekom group. International network access charges increased from 1999 to 2000 primarily due to the impact of newly consolidated companies, principally One 2 One and Siris, and the effect of increasing number of minutes of outgoing international traffic from Deutsche Telekom's mobile and fixed networks, which resulted in significantly higher network access charges. These factors were offset, to some degree, by a decline in international settlement rates.

Other services purchased consist of maintenance expenses for telecommunications hardware and software and buildings, other maintenance expenses, energy and utility costs and costs for information services provided. The increase in other services purchased from 2000 to 2001 relates primarily to increased services purchased (primarily logistic services) and changes in the composition of the Deutsche Telekom group.

The increase in other services purchased from 1999 to 2000 relates primarily to increased services purchased for value-added services, the impact of new acquisitions and services purchased in relation to a real estate development project.

Personnel Costs

The following table presents information concerning Deutsche Telekom's personnel costs.

	Year ended December 31,			Year ended December 31,	
	2001	**2000**	**1999**	**2001/2000**	**2000/1999**
	(millions of euro)			(% change)	
Wages and salaries	9,313	7,470	6,520	24.7	14.6
Other personnel costs(1)	2,801	2,248	2,690	24.6	(16.4)
Total personnel costs	12,114	9,718	9,210	24.7	5.5

(1) Other personnel costs consist primarily of social security costs, which are fixed by law generally as a percentage of wages and salaries, and of pension costs, principally for civil servant employees.

The average number of full-time equivalent employees increased from 205,032 in 2000 to 241,660 in 2001, an increase of 17.9 percent, primarily reflecting changes in the composition of the Deutsche Telekom group.

The average number of full-time equivalent employees increased from 198,006 in 1999 to 205,032 in 2000, an increase of 3.5 percent, primarily reflecting the companies that were consolidated for the first time in 2000. Without regard to changes in the composition of the Deutsche Telekom group, the average number of employees decreased by 4.6 percent due to an ongoing reduction in employee headcount at Deutsche Telekom AG.

Personnel cost increased by EUR 2.4 billion, or 24.7 percent, from 2000 to 2001. Of this increase, EUR 1.8 billion relates to changes in the composition of the Deutsche Telekom group, principally debis Systemhaus (EUR 1.0 billion), and VoiceStream and Powertel (EUR 573 million). Without regard to changes in the Deutsche Telekom group, personnel costs rose by EUR 614 million, or 6.3 percent. This increase was primarily due to pay-scale changes, which aimed at conforming salaries to market standards and encouraging high performance, as well as to changes in the structure of Deutsche Telekom's workforce. In addition, personnel expense in 2001 was influenced by an additional minimum pension liability (EUR 0.2 billion). Average personnel costs per employee (before changes in the composition of the Deutsche Telekom group) declined as a result of changes in the composition of the Deutsche Telekom's workforce.

Personnel cost increased by EUR 508 million, or 5.5 percent, from EUR 9.2 billion in 1999 to EUR 9.7 billion in 2000, as an increase in wages and salaries was partially offset by a decrease in other personnel cost. The increase in wages and salaries was due in part to the change in the composition of the group and partly due to an increase in wages and salaries under collective bargaining agreements in Germany and a change in the remuneration system. The increase in the number of employees in Deutsche Telekom's subsidiaries T-Mobile Deutschland and DeTeCSM contributed to the overall increase in personnel costs. The decline in other personnel costs is mainly attributable to a decrease of EUR 588 million in contributions to civil servant pensions that results from the rules applicable to such contributions.

Depreciation and Amortization

The following table presents information concerning depreciation and amortization.

	Year ended December 31,			Year ended December 31,	
	2001	2000	1999	2001/2000	2000/1999
	(millions of euro)			(% change)	
UMTS license amortization	724	381	0	90.0	n/a
Goodwill amortization	3,663	1,248	300	193.5	316.0
Depreciation and amortization on remaining fixed and intangible assets	10,834	11,362	8,166	(4.6)	39.1
Depreciation and amortization	15,221	12,991	8,466	17.2	53.4

Depreciation and amortization amounted to EUR 15.2 billion in 2001, representing an increase of EUR 2.2 billion, or 17.2 percent, compared to 2000. Depreciation and amortization of companies acquired by Deutsche Telekom during 2000 and 2001, principally VoiceStream, Powertel and debis Systemhaus, accounted for EUR 3.1 billion of the increase in depreciation and amortization. This amount includes goodwill amortization of EUR 882 million relating to VoiceStream and Powertel and an increase of EUR 242 million in goodwill amortization relating to debis Systemhaus, resulting from the fact that debis Systemhaus was consolidated in Deutsche Telekom's financial statements for the entire year in 2001 as opposed to only one quarter in 2000. In addition, amortization for UMTS licenses in 2001 was EUR 343 million higher than in 2000 due to the fact that UMTS licenses were acquired by T-Mobile UK, T-Mobile Deutschland and max.mobil in the later part of 2000, resulting in less than a full year of amortization for 2000. Because VoiceStream and Powertel were acquired in the middle of 2001, goodwill amortization relating to VoiceStream and Powertel in 2002 will be higher than in 2001. Deutsche Telekom also took an unscheduled write-down of EUR 466 million relating to the book values of real estate in 2001 and an unscheduled write-down of EUR 1.0 billion relating to goodwill associated with trademarks of One 2 One and max.mobil in connection with the T-Mobile rebranding campaign. For further information with respect to the unscheduled write-down relating to the book values of real estate, see notes 6, 35 and 38 to the consolidated financial statements. In addition, in 2001, an unscheduled write-down of EUR 350 million was taken with respect to buildings for which no further commercial use is expected. This write-down was offset by a gain in the same amount on the reversal of provisions for general risks. Finally, an unscheduled write-down on property, plant and equipment was taken in the amount of EUR 158 million, relating principally to parts of the mobile communications network of One 2 One (EUR 104 million).

Depreciation and amortization in 2000 was significantly influenced by several major factors. First, UMTS license amortization commenced in 2000 for the first time, relating primarily to licenses in the United Kingdom and Germany. Second, Deutsche Telekom's acquisitions during 1999 and 2000 gave rise to considerable goodwill, which contributed EUR 919 million to the increase in goodwill amortization. Goodwill primarily resulted from the acquisitions of One 2 One, max.mobil and debis Systemhaus and from the acquisition of Ameritech's interest in MATAV. The third major factor that influenced depreciation and amortization was non-scheduled depreciation of old network components (EUR 971 million) due to the introduction of advanced fiber optic transmission technology in parts of Deutsche Telekom's fixed-network. In addition, Deutsche Telekom took an unscheduled write-down of EUR 2.0 billion with respect to its real estate portfolio. For further information in this regard, see notes 6, 35 and 38 to the consolidated financial statements. The remaining increase in depreciation and amortization is primarily related to depreciation and amortization of the assets of newly acquired companies (other than goodwill and UMTS license amortization of those companies).

Goodwill relating to VoiceStream and Powertel is denominated in U.S. dollars, One 2 One goodwill is denominated in British pounds. Amortization of goodwill relating to VoiceStream, Powertel and One 2 One therefore is affected by exchange rate movements.

Other Operating Expenses

Other operating expenses consist of expenses occurring in the ordinary course of business that cannot be classified in any other line item in the statement of operations.

Other operating expenses amounted to EUR 12.2 billion in 2001, representing an increase of EUR 1.7 billion, or 16.6 percent, compared to 2000. This increase principally reflects other operating expenses for 2001 relating to VoiceStream (EUR 1.6 billion) and debis Systemhaus (EUR 339 million) and others (EUR 305 million). In addition, other operating expenses for 2001 were negatively affected by expenses and consulting fees in the amount of EUR 104 million, particularly relating to the sale of Sprint shares. Without regard to the factors discussed above, other operating expenses decreased by EUR 0.7 billion from 2000 to 2001, largely as a result of decreased losses on the disposition of noncurrent assets, decreased additions to accruals and decreased losses on derivative financial instruments. On the other hand, losses on accounts receivable and increased provisions for doubtful accounts in the amount of EUR 307 million (excluding losses and provisions relating to VoiceStream), of which EUR 224 million related to insolvencies of fixed-network competitors of Deutsche Telekom that used Deutsche Telekom's fixed network, had an upward influence on other operating expenses, as did increased maintenance costs.

Other operating expenses amounted to EUR 10.4 billion in 2000, representing an increase of EUR 3.6 billion, or 51.7 percent, compared to 1999. The impact of changes in the composition of the Deutsche Telekom group amounted to EUR 1.4 billion, relating primarily to One 2 One, debis Systemhaus and Slovenske Telekomunikacie. Of the remaining increase in other operating expenses, an increase in marketing and commission costs (other than marketing and commission costs of newly acquired companies) accounted for approximately EUR 589 million and was primarily a result of Deutsche Telekom's efforts to increase its mobile communications subscriber base. In addition, other operating expenses in 2000 included factors that had no effect on expenses in 1999. These factors were principally additional losses on disposal of assets (EUR 0.5 billion), an increase of EUR 0.4 billion in additions to accruals, relating mainly to real estate and legal proceedings, and increased provisions for doubtful accounts in the amount of EUR 0.2 billion. The remaining increase relates to increased rental and leasing expenses, higher other personnel costs and increased maintenance costs.

As indicated above, insolvencies of competitors that used Deutsche Telekom's fixed network had an upward influence on Deutsche Telekom's other operating expenses in 2001. In light of developments in the fixed-network telecommunications market in Germany, further writedowns of receivables from competitors that use Deutsche Telekom's fixed network could occur in 2002.

Financial Income (Expense), Net

The following table presents information concerning Deutsche Telekom's net financial expense.

	Year ended December 31,			Year ended December 31,	
	2001	2000	1999	2001/2000	2000/1999
	(millions of euro)			(% change)	
Results related to companies accounted for under the equity method	(547)	1,890	(265)	128.9	n/a
Other investments	(663)	(23)	(78)	n/a	70.5
Income (loss) from financial activities	(1,210)	1,867	(343)	n/a	n/a
Net interest expense	(4,138)	(3,097)	(2,546)	33.6	(21.6)
Financial income (expense), net	(5,348)	(1,230)	(2,889)	334.8	57.4

Net Interest Expense. Deutsche Telekom's debt increased during 2001 by EUR 6.7 billion to EUR 67.0 billion at year end 2001 after having increased in 2000 by EUR 18.0 billion to EUR 60.3 billion at year end 2000. The increase in debt was the primary reason for the increase of EUR 1.0 billion in net interest expense from 2000 to 2001 and increase of EUR 0.6 billion in net interest expense from 1999 to 2000. A significant portion (approximately EUR 0.5 billion) of the increase in net interest expense from 2000 to 2001 can be attributed to interest on debt incurred to finance the acquisition of UMTS licenses in 2000. The increase in interest expense was, to some extent, offset by increased interest income and income from debt securities and long-term loan receivables, primarily due to gains from specialized security funds. Net interest expense is likely to be higher in 2002 than in 2001, due to the impact of the first-time full-year consolidation of interest expense of VoiceStream and Powertel as well as the impact of Deutsche Telekom's purchase of the remaining interests in debis Systemhaus in 2002.

The effective weighted average interest rate applicable to Deutsche Telekom's outstanding indebtedness related to bonds and debentures was 6.8 percent in 2001, 6.5 percent in 2000 and 7.5 percent in 1999. The effective weighted average interest rate applicable to outstanding indebtedness related to bank liabilities was 5.8 percent in 2001, 6.7 percent in 2000 and 7.1 percent in 1999. A portion of Deutsche Telekom's debt has variable interest rates based on the Deutsche Telekom's long-term debt ratings. Deutsche Telekom's long-term debt ratings were downgraded by Moody's and Standard & Poor's in March and April of 2002, which led to an increase in the interest rate applicable to a portion of Deutsche Telekom's outstanding indebtedness. This step-up in the interest rate payable will tend to increase interest expense in 2002 as compared to 2001.

Income (Loss) from Financial Activities and Other Investments. Income (loss) from financial activities includes Deutsche Telekom's share of the income or losses on investments accounted for using the equity method. This includes the amount of annual amortization of goodwill relating to these investments, which is essentially the amortization of goodwill arising from the difference between the purchase price paid by Deutsche Telekom and Deutsche Telekom's share of the shareholders' equity for each of these investments. Income and loss from other investments consists primarily of dividends received from Deutsche Telekom's investments in various satellite service providers and from Sprint, as well as provisions for write-downs of the carrying amounts of other investments.

The decrease in results related to companies accounted for by the equity method from 2000 to 2001 was largely due to the fact that, in 2001, this line item was positively influenced by Deutsche Telekom's interest of EUR 2.3 billion in gains realized by the associated company DT-FT Italian Holding upon the sale of its interests in the Italian mobile joint venture WIND. In addition, results of other investments were negatively affected in 2001 by an unscheduled write-down in the amount of EUR 312 million in the book value of Deutsche Telekom's interest in France Telecom and an unscheduled write-down in the amount of EUR 390 million in the book value of debenture bonds received by Deutsche Telekom in the sale of interests in regional cable companies.

Results related to companies accounted for under the equity method increased from 1999 to 2000. This is mainly due, as noted above, to the gain from the sale of Deutsche Telekom's indirect interest in the Italian joint venture WIND (EUR 2.3 billion). This effect was offset to some extent by losses of associated companies, relating primarily to Deutsche Telekom's share of the results of the two broadband cable companies in Nordrhein-Westfalen and Hessen and to Deutsche Telekom's Asian subsidiaries. Deutsche Telekom started accounting for these two regional cable companies using the equity method on July 1, 2000.

Results from Ordinary Business Activities

Results from ordinary business activities decreased by EUR 9.0 billion from 2000 to 2001. Results from ordinary business activities are influenced by all of the factors described above that influenced individual statement of operations line items. The principal factor accounting for the decline in results from ordinary business activities was a substantial decline in the net contribution of unusual or infrequently occurring items to results from ordinary business activities. For a summary of the unusual or infrequently occuring items that contributed to results from ordinary business activities in 2000 and 2001, see "— Effects of Acquisitions and Unusual or Infrequent Items on Deutsche Telekom's statements of operations for the three years ended December 31, 2001." Deutsche Telekom estimates that these unusual or infrequent items had an aggregate positive impact on results from ordinary business activities of EUR 7.1 billion in 2000 and EUR 161 million in 2001. Additional factors contributing to the decline in results from ordinary business activities were losses of companies acquired in 2000 and 2001 (EUR 2.9 billion), principally VoiceStream and debis Systemhaus, amortization of goodwill relating to companies acquired in 2000 and 2001, an increase in interest expense resulting from indebtedness incurred in 2000 to finance the acquisition of UMTS licenses and the first-time inclusion of UMTS license amortization for an entire year in 2001.

Results from ordinary business activities increased by EUR 3.3 billion from 1999 to 2000. The major factors contributing to the change in results from ordinary business activities were the impact on results of losses of newly consolidated companies (EUR 1.8 billion), the positive effects from the sale of shares in Global One, regional cable companies and WIND and the capital gains from the sale of shares in subsidiaries (T-Online and others), the effects on costs of the non-scheduled write-down of the book values of real property, the non-scheduled write-down of long-distance cables and other unusual effects described above under "other operating income". The remaining change in results from ordinary business activities results from increased revenues (excluding revenues of newly acquired companies), primarily from mobile communications, carrier services and data communications and higher costs relating primarily to higher customer acquisition costs for Deutsche Telekom's German mobile communications business and higher national and international interconnection costs, primarily due to an increase in volume.

Taxes

The following table presents information concerning income taxes and other taxes.

	Year ended December 31,		
	2001	2000	1999
	(millions of euro)		
Income taxes	751	194	1,380
Other taxes	57	124	40
Taxes	808	318	1,420

Income tax expense in 2001 amounted to EUR 751 million, an increase of EUR 557 million, or more than 100 percent, compared to 2000. Due to changes in the character of the Deutsche Telekom group's income before taxes, income tax expense increased despite the decrease in results from ordinary business activities from 2000 to 2001.

Income before taxes for 2000 included significant items that were not subject to taxation, principally the proceeds of Deutsche Telekom's sale of its interest in Global One, the dilution effect resulting from the initial public offering of T-Online International AG and the proceeds of Deutsche Telekom's sale of its interest in WIND. Income before taxes for 2001 included no significant tax-free items other than the sale of Sprint shares held by Deutsche Telekom. In addition, in 2001, expenses that had to be recognized for financial accounting purposes but that were not deductible for tax purposes, principally goodwill amortization, were higher in 2001 than in 2000. Furthermore, in 2001, there was an increase in losses of subsidiaries that had to be recognized for financial reporting purposes but may be recognized for tax accounting purposes only when the related tax loss carryforwards are utilized in the future.

Income tax expense decreased from 1999 to 2000, despite increased income before taxes. This is mainly due to differences in accounting and valuation for financial reporting purposes and for tax purposes. As discussed above, a substantial part of Deutsche Telekom's income in 2000 consisted of gains that were not taxable. The increase in other taxes is primarily related to a one-time effect in 1999. Deutsche Telekom treated its unscheduled write-down of the book values of real estate in 2000 as a tax deduction in calculating its tax expense for that year. Deutsche Telekom is engaged in continuing discussions with the German tax authorities regarding the tax treatment of this write-down.

Deutsche Telekom's effective income tax rate (income taxes as a percentage of pre-tax income (loss)) was approximately (30) percent in 2001, 3.1 percent in 2000 and 47.5 percent in 1999. The German statutory income tax rate for Deutsche Telekom was approximately 39 percent in 2001 and 52 percent in 2000 and 1999 and included corporate income taxes (assuming that earnings are not distributed), trade income taxes (at a German national average rate) and the solidarity surcharge on corporate income tax (*Solidaritätszuschlag*). Due to a change in income tax law in Germany, which reduced the statutory corporate tax rate to a uniform 25 percent tax rate (for both distributed and non-distributed earnings), Deutsche Telekom's income tax rate for 2001 was significantly lower than in prior years. The change in the statutory income tax for future years affected the rate used to calculate deferred taxes. This rate has been set at 39 percent for 2001 and 2000 and 52 percent for 1999. This change in the rate used to calculate deferred taxes resulted in a one-time tax charge of EUR 188 million. The difference between the statutory rate and the effective tax rate in 1999 relates primarily to the lower income tax rate of 30 percent on the proposed dividend of EUR 1.9 billion for 1999, differentials of tax rates on income taxable outside of Germany and temporary differences and losses for which deferred taxes are not recorded under German GAAP.

Segment Analysis

The following table presents total revenues (the sum of external revenues and revenues between segments) for Deutsche Telekom's segments for the periods indicated.

	2001			2000			1999		
	Net revenue	Revenue between segments	Total revenue	Net revenue	Revenue between segments	Total revenue	Net revenue	Revenue between segments	Total revenue
	(millions of euro)								
T-Com	19,362	6,723	26,085	20,170	7,441	27,611	21,606	5,068	26,674
T-Systems	11,211	2,577	13,788	8,460	2,226	10,686	6,018	1,965	7,983
T-Mobile	12,994	1,643	14,637	8,994	1,362	10,356	5,153	1,183	6,336
T-Online	1,338	111	1,449	1,038	90	1,128	813	55	868
Other	3,404	4,583	7,987	2,277	4,834	7,111	1,880	5,300	7,180
Reconciliation	—	(15,637)	(15,637)	—	(15,953)	(15,953)	—	(13,571)	(13,571)
Group	48,309	—	48,309	40,939	—	40,939	35,470	—	35,470

T-Com

The following table presents financial information concerning the T-Com segment.

	T-Com		
	2001	2000	1999
	(millions of euro)		
Net revenue, excluding revenue between segments	19,362	20,170	21,606
Income before taxes	3,244	4,373	1,803

Revenues

T-Com revenues

The following table shows the revenues of the T-Com segment by category of activity.

	2001	2000	1999	2001/2000	2000/1999
	(in millions of euro)			(% change)	
Network communications	13,963	14,090	15,855	(0.9)	(11.1)
International Carrier Services	756	946	957	(20.1)	(1.1)
Broadband cable	1,072	1,352	1,410	(20.7)	(4.1)
Terminal Equipment	895	1,026	1,005	(12.8)	2.1
Value added services	1,396	1,376	1,353	1.5	1.7
Other	1,280	1,380	1,026	(7.2)	34.5
Total Revenues	19,362	20,170	21,606	(4.0)	(6.6)

Revenues of the T-Com segment are derived principally from network communications. To a lesser extent, the T-Com segment also derives revenues from value-added services, broadband cable, terminal equipment and carrier services.

Network Communications

Revenues from network communications consist of revenues from domestic telephone communications and from international telephone communications. Domestic telephone communications revenues include initial connection fees and monthly rental charges as well as call charges. Call charges originate from local, regional and domestic long-distance calls, calls to mobile networks and calls to Internet service providers, other than T-Online. International telephone communications revenues consist of call charges that originate from international long-distance calls.

Revenues between segments result primarily from providing of services to other segments, in particular from providing to Deutsche Telekom's fixed-network subscribers access to online services. These revenues are essentially matched by corresponding costs of providing these services.

Revenues from network communications declined from 2000 to 2001, principally as a result of declining revenues from call charges from domestic long-distance and local calls. The decline in revenues from call charges was partially offset by an increase in access charges in the areas of T-ISDN and T-DSL and by an increase in revenues from calls to mobile communications and online services.

Revenues from network communications also declined from 1999 to 2000, due to declining revenues from call charges, particularly for international and domestic long-distance calls, which resulted from reduced tariffs and decreased volume due to competition. This decline was partially offset by an increase in revenues from access charges, due to increased volume in the area of T-ISDN and due to various higher-value service packages.

Initial Connection Fees, Monthly Rental Charges and Other Network Services. Revenues from initial connection fees, monthly rental charges and other network services are primarily a function of the number and mix of standard telephone and ISDN access lines and the corresponding initial connection fees and monthly rental charges.

The average number of access channels (adjusted to reflect ISDN channels) has risen over the last three years as indicated below.

	Year ended December 31,		
	2001	2000	1999
		(millions)	
Average number of access channels	50.1	48.5	47.0

The increase in revenues from initial connection fees, monthly rental charges and other network services from 2000 to 2001 and from 1999 to 2000 resulted primarily from growth in the number of access channels.

Domestic Call Charges. Revenues from call charges are a function of the number of telephone calls, average call duration, the mix of local, regional and long distance calls as well as the time of the call and the applicable tariffs. In general, domestic telephone traffic is influenced by trends in the German telecommunications market and other market developments as described above.

The decline in domestic call charges from 2000 to 2001 resulted primarily from a reduced price level due to increased use of optional tariffs. Revenues per minute from domestic calls were on average 12 percent lower in 2001 than in 2000, as a greater decline in revenues per minute from regional long-distance calls and from calls to other services were partially offset by a smaller decline in revenues from local calls and calls to mobile. At the same time, minutes leading to revenues from domestic call charges increased 10 percent from 2000 to 2001, as a decline in minutes from local calls could be offset by increases in minutes from domestic long-distance calls and from calls to other services and mobile networks.

Revenues per minute from domestic calls were on average 15 percent lower in 2000 than in 1999, as a greater decline in revenues per minute from domestic long-distance calls was offset to some extent by a smaller decline in revenues per minute from local calls and calls to mobile networks. At the same time, minutes leading to revenues from domestic call charges increased 1.3 percent from 1999 to 2000, as a small decline in minutes from domestic long-distance calls and a larger decline in minutes from local calls were offset by increases in minutes from calls to mobile networks and calls to other services.

International Telephone Communications. Revenues from call charges for international long-distance calls are a function of tariffs and the volume, duration and mix of outgoing international traffic.

Revenues per minute from international calls declined by approximately 10 percent from 2000 to 2001 as a result of tariff measures and optional tariffs introduced in 2000 and 2001. The effects of these tariff measures were largely offset, however, by an increase of approximately 11 percent in volume of outgoing international calls.

As a consequence of the pronounced tariff reductions in 1999 and 2000, average revenues per minute decreased by 39 percent from 1999 to 2000. In addition, despite the decrease in tariffs, minute volume leading to international network communications revenues was 1.4 percent lower in 2000 than in 1999.

Other T-Com Services

International Carrier Services. For the three years ended December 31, 2001, revenues of Deutsche Telekom's international carrier services business are shown in the T-Com segment. With effect as of January 2002, however, Deutsche Telekom transferred operational responsibility for the international carrier services business to the T-Systems segment and transferred operational responsibility for the national carrier services business from the T-Systems segment to the T-Com segment. As a result, for periods after December 31, 2001, the revenues of Deutsche Telekom's international carrier services businesses will be shown in the T-Systems segment, while revenues of the national carrier services business for periods after December 31, 2001 will be shown in the T-Com segment.

From 2000 to 2001, revenues from international interconnection services decreased slightly, primarily as a result of reduced settlement rates for incoming international calls. This trend is expected to continue in the medium term due to increased liberalization of the international telecommunications markets and the resulting increase in competition.

From 1999 to 2000, revenues from international interconnection services increased mainly due to increased revenues per minute. This increase in revenues per minute, which was due to favorable exchange rate movements and higher settlement rates for calls terminating on mobile networks, was partially offset, however, by a decrease in the number of minutes carried on Deutsche Telekom's network.

Broadband Cable. Revenues from broadband cable decreased from 2000 to 2001 and from 1999 to 2000, largely as a result of the fact that the regional cable companies for Nordrhein-Westfalen and Hessen were no longer consolidated after majority interests in those companies were sold to third parties in 2000. Without regard to the effect of these sales, revenues from broadband cable increased slightly (approximately 3.5% from 2000 to 2001).

Terminal Equipment. Revenues from terminal equipment consist of revenues from the sale and rental of terminal equipment for the fixed network.

Revenues from terminal equipment declined from 2000 to 2001, due to reduced sales volume, customer cancellations in the terminal equipment rental business and continuing decline in prices for terminal equipment.

Revenues from terminal equipment declined from 1999 to 2000. Despite a strong increase in the number of units of terminal equipment sold, sales revenues declined due to the continuing decline in prices for terminal equipment. In addition, a change in the distribution channel for mobile equipment led to a reduction in external sales revenues and to a lesser extent to an increase in revenues between segments.

Value-added Services. Revenues from value-added services include revenues from public telephones, toll free lines, information services, telephone directory publishing and other directory and operator services.

External revenues from value added services remained relatively constant from 2000 to 2001, as a continued decline in revenues from the traditional public telephone business was offset by increasing revenues from other value added services, such as toll-free lines and premium rate services.

External revenues of Deutsche Telekom's value-added services business area decreased from 1999 to 2000. This can be attributed to the decline in revenues in the areas of public telephones, operator services and information services. Competition in the areas of operator and information services contributed to a decline in revenues in these areas. However, increased revenues from the areas value-added communications, premium rate services and card services offset, to some extent, the decreases in other areas.

Income Before Taxes

Income before taxes of the T-Com segment amounted to EUR 3.2 billion in 2001, which represents a decrease of EUR 1.1 billion, or 25.8 percent, as compared to 2000. Unusual or infrequently occurring factors influenced income before taxes of the T-Com segment in both years. In 2001, these factors were gains on the sale of interests in the regional cable company for Baden-Württemberg and related regional cable service companies (EUR 912 million). In 2000, these factors were gains on the sale of interests in the regional cable televisions companies for Nordrhein-Westfalen and Hessen (EUR 3.0 billion) and unscheduled depreciation on copper long-distance cables (EUR 1.0 billion). Without regard to these unusual or infrequent items, income before taxes of the T-Com segment remained relatively constant, as a decline in revenues and an increase in goods and services purchased was largely offset by reduced personnel expense and interest expense.

Income before taxes of the T-Com segment amounted to EUR 4.4 billion in 2000, which represents an increase of EUR 2.6 billion, or 142.5 percent, as compared to 1999 principally due to the unusual or infrequently occurring items mentioned above that influenced 2000.

T-Systems

The following table presents financial information concerning T-Systems:

	T-Systems						
	2001			2000			1999
	Pre-acquisitions	Effects of acquisitions	Total	Pre-acquisitions	Effects of acquisitions	Total	Total
	(millions of euro)			(millions of euro)			(millions of euro)
Net revenue, excluding revenue between segments	9,001	2,210	11,211	7,367	1,093	8,460	6,018
Income (loss) before taxes	(203)	(86)	(289)	2,658	(160)	2,498	(219)

Revenue

Revenue of the T-Systems segment is derived principally from telecommunication services and information technology services. Net revenue of the T-Systems division amounted to EUR 11.2 billion in 2001, representing an increase of EUR 2.8 billion, or 32.5 percent, compared to 2000. Of this increase, the first-time consolidation of debis Systemhaus starting in October 2000 accounted for EUR 2.2 billion. Without regard to the first-time consolidation of debis Systemhaus, revenues of the T-Systems division increased by EUR 550 million, or 6.5 percent, as a result of the developments in the telecommunication services business that are described below.

Telecommunication Services

The telecommunication services business of T-Systems consists principally of network services and, through 2001, national carrier services. For further information in this regard see "Item 4. Information on the Company — Description of Business Segments — T-Systems."

National carrier services business. For the three years ended December 31, 2001, revenues of Deutsche Telekom's national carrier services business are shown in the T-Systems segment. With effect as of January 2002, however, Deutsche Telekom transferred operational responsibility for the national carrier services business to the T-Com segment and transferred operational responsibility for the international carrier services business from the T-Com segment to the T-Systems segment. As a result, for periods after December 31, 2001, the revenues of Deutsche Telekom's national carrier services businesses will be shown in the T-Com segment, while revenues of the international carrier services business for periods after December 31, 2001 will be shown in the T-Systems segment.

Revenues from national carrier services increased from 2000 to 2001 due to increased traffic volume to online-services as well as to domestic mobile networks. The effect was partly offset by the decrease in traffic to international mobile networks due to the mobile surcharges implemented in the second half of 2000.

The increase in revenues from domestic interconnection services from 1999 to 2000 resulted from continued growth in the volume of traffic carried on Deutsche Telekom's network for other carriers. At the beginning of 2000, however, Deutsche Telekom implemented the new lower domestic interconnection rates established by the German telecommunications regulator at the end of 1999, which partially offset the effect that increased traffic volume had on revenues. For further information on the new domestic interconnection rates, see "Item 4. Information on the Company — Regulation." As the number of local loop subscriber access lines competitors which lease from Deutsche Telekom increases, these access lines are beginning to generate revenues for the national carrier services business area.

Network services. External revenues of T-Systems network services increased from 2000 to 2001 and from 1999 to 2000 due to increased volume that resulted from increased customer demand. In each year, the effects of increased volume were partially offset by decreased average prices.

Income (loss) before Taxes

Loss before taxes of the T-Systems segment amounted to EUR 0.3 billion in 2001, as compared to income before taxes of EUR 2.5 billion in 2000. Gains on the sale of Deutsche Telekom's interest in Global One contributed EUR 2.9 billion to income before taxes of the T-Systems segment for 2000. Without regard to the effect of this sale, loss before taxes of the T-Systems segment decreased by 21 percent from 2000 to 2001 due to a decrease in interest expense allocated to this segment and an improvement in profitability in the telecommunications business of the T-Systems segment. This effect was partially offset by the first-time consolidation of T-Systems ITS (formerly debis Systemhaus GmbH) starting in October 2000.

Income before taxes of the T-Systems segment amounted to EUR 2.5 billion in 2000, representing an increase of EUR 2.7 billion compared to the EUR 219 million loss in 1999. Without regard to the effect of the sale of Deutsche Telekom's interest in Global One, loss before taxes of the T-Systems segment increased by EUR 145 million from 1999 to 2000, due to the overproportional increase in depreciation and amortization resulting from goodwill amortization relating mainly to T-Systems ITS and Siris.

T-Mobile

The following table presents financial information concerning T-Mobile:

	2001			2000			1999
	Pre-acquisitions	Effects of acquisitions	Total	Pre-acquisitions	Effects of acquisitions	Total	Total
	(millions of euro)			(millions of euro)			(millions of euro)
Net Revenue, excluding revenue between segments	9,715	3,279	12,994	6,953	2,041	8,994	5,153
Income (loss) before taxes . . .	(3,656)	(2,743)	(6,399)	(1,222)	(1,128)	(2,350)	632

The mobile communications business area generates revenues from activation fees, monthly access charges and call charges paid by direct subscribers, charges paid by independent service providers, and the sale of handsets. Independent service providers purchase mobile communications services from the T-Mobile segment at a discount, resell those services and bill subscribers directly at rates they set independently.

Deutsche Telekom's mobile communications business is reflected in the activities of the subsidiaries of T-Mobile International, principally T-Mobile Deutschland in Germany, T-Mobile UK in the United Kingdom, T-Mobile Austria (formerly max.mobil) in Austria, VoiceStream and Powertel in the United States, and RadioMobil in the Czech Republic. For further information as to which of Deutsche Telekom's mobile communications investments are accounted for in the T-Mobile segment, see "Item 4. Information on the Company — Description of Business Segments — T-Mobile."

The following table shows the number of subscribers by operator.

	December 31,				
	2001	2000	1999	2001/2000	2000/1999
	(thousands)			(% change)	
T-Mobile Deutschland	23,081	19,141	9,067	20.6	111.1
T-Mobile UK	10,422	8,324	4,157	25.2	100.2
T-Mobile Austria	2,102	2,042	1,508	2.9	35.4
VoiceStream	5,819	—	—	n/a	n/a
Powertel	1,174	—	—	n/a	n/a
RadioMobil	2,850	—	—	n/a	n/a
Total subscribers	45,448	29,507	14,732	54.0	100.2

The following table presents financial information concerning revenues by geographic area in the T-Mobile segment.

	Year ended December 31,			Year ended December 31,	
	2001	2000	1999	2001/2000	2000/1999
	(millions of euro)			(% change)	
Revenues					
Germany	7,064	6,475	4,993	9.1	29.7
United Kingdom	3,277	2,883	544	13.7	430.0
United States	2,796	—	—	n/a	n/a
Austria	1,017	998	799	1.9	24.9
Czech Republic	483	—	—	n/a	n/a
Total Revenues	14,637	10,356	6,336	41.3	63.4
Revenue between segments	(1,643)	(1,362)	(1,183)	20.6	15.1
Net Revenue	12,994	8,994	5,153	44.5	74.5
Income (Loss) before Taxes	(6,399)	(2,350)	632	(172.3)	(471.8)

Revenues

Total revenue of the T-Mobile segment amounted to EUR 14.6 billion in 2001, representing an increase of EUR 4.3 billion, or 41 percent, compared to 2000. Of this increase, the first-time consolidation of VoiceStream and Powertel starting in June 2001 accounted for EUR 2.8 billion, and the first-time consolidation of the Czech mobile communications provider RadioMobil starting in April 2001 accounted for EUR 0.5 billion. Without regard to the first-time consolidation of VoiceStream, Powertel and RadioMobil, revenues of the T-Mobile division increased by EUR 1.0 billion, or 9.7 percent, largely due to further increases in the number of mobile subscribers of T-Mobile Deutschland in Germany and T-Mobile UK in the United Kingdom. The increase in the number of subscribers was partially offset by an increase in the proportion of customers that use prepay tariff packages, which generate lower revenue per subscriber than contract customers. In addition, revenues from handset sales declined due to increasing saturation of the mobile communications markets in Germany, the United Kingdom and Austria.

Revenues from mobile communications in Germany increased in all three years under review as a result of continued growth in the number of T-Mobile Deutschland's subscribers. The number of subscribers rose by 21 percent in 2001 and 111 percent in 2000, in part because of the positive response to the private customer-oriented tariff options offered by T-Mobile Deutschland to attract new customer groups. Average revenue per subscriber continued to decline substantially, however, due in part to an increase in the proportion of subscribers that use prepay tariff packages (54 percent at year-end 2001 as compared to 52 percent at year end 2000 and 20 percent at year-end 1999), which generally generate lower revenues per subscriber than contract subscribers. Reduced tariffs and a decline in minutes per subscriber also contributed to the decrease in average revenues per subscriber. Revenues from sales of mobile handsets, which are included in other mobile communications services and products, increased from 1999 to 2000 due to the growth in the mobile communications market, but declined from 2000 to 2001 due to increasing saturation of the market. Mobile handsets generally have been subsidized in order to create attractive package offers for new customers.

Revenues of T-Mobile UK increased from 2000 to 2001, although not as rapidly as the number of subscribers. While the number of subscribers that use prepay tariff packages increased, there was a slight decrease in the number of contract subscribers. These developments led to declining revenues per subscriber. The increase in revenues in the United Kingdom relating to T-Mobile UK from 1999 to 2000 is mainly due to the fact that T-Mobile UK was included in Deutsche Telekom's accounts for a full year in 2000, but only for one quarter in 1999.

Revenues of T-Mobile Austria slightly increased by 2 percent from 2000 to 2001 due to the slight increase in its subscriber base, whereas from 1999 to 2000 revenues increased by 25 percent also due to the increase in its subscriber base.

Income (Loss) Before Taxes

Loss before taxes at the T-Mobile segment amounted to EUR 6.4 billion in 2001, representing an increase in loss of EUR 4.0 billion, or 172 percent, compared to 2000. Of this decrease, the first-time consolidation of VoiceStream and Powertel starting in June 2001 accounted for EUR 2.8 billion. Depreciation and amortization of the T-Mobile segment increased substantially due to several important factors: goodwill amortization relating to VoiceStream and Powertel (EUR 882 million); unscheduled depreciation of trademarks relating to One 2 One and max.mobil which accompanied T-Mobile's rebranding campaign (EUR 1.0 billion) and the first-time inclusion of amortization of UMTS licenses in results for a full year in 2001 (EUR 0.3 billion). These effects were partially offset, however, by substantially increased revenues and by a reduction in subscriber acquisition costs (principally subsidies on mobile handsets, advertising costs and commissions for vendors of T-Mobile's services) compared to 2000.

Income (loss) before taxes of the T-Mobile segment decreased from income of EUR 0.6 billion to a loss of EUR 2.4 billion from 1999 to 2000. The decrease of EUR 3.0 billion relates to a range of factors. These factors include the increase in goodwill amortization of EUR 0.6 billion for T-Mobile UK, the amortization of UMTS licenses in the United Kingdom, Germany and Austria (EUR 0.4 billion), and the increase in interest expense allocated to Deutsche Telekom's mobile business, which reflects funding requirements relating to the acquisition of UMTS licenses. In addition, increased subscriber acquisition costs contributed to the overall decrease in income before taxes.

Deutsche Telekom expects that income before taxes of the T-Mobile segment in the coming years will be significantly affected by license amortization, goodwill amortization related to acquired companies, interest expense related to indebtedness incurred to finance UMTS licenses and the slowing of the rate of growth in the number of subscribers in increasingly saturated European markets, among other factors. For a description of additional factors that could significantly influence the net income of the T-Mobile segment in coming years, see "Item 3. Key Information — Risk Factors."

T-Online

The following table presents financial information concerning T-Online:

	T-Online						
	2001			2000			1999
	Pre-acquisitions	Effects of acquisitions	Total	Pre-acquisitions	Effects of acquisitions	Total	Total
	(millions of euro)			(millions of euro)			(millions of euro)
Net revenue, excluding revenue between segments	1,309	29	1,338	983	55	1,038	813
Income (loss) before taxes	(113)	(120)	(233)	2,781	(153)	2,628	154

Revenues

Net revenue of the T-Online segment amounted to EUR 1.3 billion in 2001, representing an increase of EUR 300 million, or 28.9 percent, compared to 2000. Of this increase, EUR 49 million is accounted for by the first-time consolidation of Club Internet in April 2000. The contribution of T-Online International AG group to the consolidated revenues of the Deutsche Telekom group increased from EUR 713 million in 2000 to EUR 1.0 billion in 2001, largely as a result of further growth in the number of subscribers and increased usage per subscriber for all products, which was supported by a change in the price structure. An increase in revenues of T-Online International AG in the portal area (advertising/e-commerce) also contributed to the increase in revenues of the T-Online division. The increase in revenues of T-Online International AG was partially offset by declining revenues of DeTeMedien in 2001, which results primarily from the disposal of certain publishing activities and a decline in revenue from the direct marketing area as compared to 2000.

The contribution of the T-Online International AG group to the consolidated revenues of Deutsche Telekom increased from EUR 412 million in 1999 to EUR 713 million in 2000, as a result of increased customer numbers and increased average usage times per customer. The effects of these factors were partially offset, however, by the introduction of a flat rate offering that reduced the relevance of minute volume for revenues. Loss before taxes of the T-Online segment amounted to EUR 233 million in 2001, as compared to income of EUR 2.7 billion in 2000. Income before taxes for 2000 included EUR 2.9 billion of dilution gains relating to the initial public offering of T-Online International AG and other investments in that segment.

Without regard to this unusual item, income before taxes of the T-Online segment remained relatively constant from 2000 to 2001 as increased depreciation and amortization resulting from acquisitions effected in 2000 (Club Internet and ya.com) was largely offset by increased interest income.

Income before taxes

Income before taxes of the T-Online segment amounted to EUR 2.6 billion in 2000, representing an increase of EUR 2.5 billion as compared to 1999 as dilution gains from the issuance of T-Online shares (EUR 2.7 billion) and increased revenues from operations were partially offset by losses of newly acquired companies and increased personnel costs.

Other Activities

Other activities consist of Deutsche Telekom's foreign subsidiaries that are not shown in any other segment, as well as Deutsche Telekom's headquarters, real estate holdings and other activities not shown in any other segment. The foreign subsidiaries shown under "other activites" in 2001 include MATAV, Siris, Slovenske Telekomunikacie, Croatian Telecom and Macedonian Telecom, a subsidiary of MATAV. Starting in 2002, these companies will be accounted for under the T-Com segment. In 2000, in addition to MATAV, other activities included Siris, Eurobell and Slovenske Telekomunikacie. Deutsche Telekom sold its shares in Eurobell in the fourth quarter of 2000. For 1999, MATAV was the only foreign subsidiary shown under other activities.

Net revenue from other activities amounted to EUR 3.4 billion in 2001, representing an increase of EUR 1.1 billion, or 49.5 percent, compared to 2000. Of this increase, EUR 244 million is accounted for by the first-time consolidation of Macedonian Telecom in the first quarter of 2001 and EUR 334 million by the first-time consolidation of Slovenske Telecomunikacije in the third quarter of 2000. Without regard to the first-time consolidation of these companies, other revenues increased by 24.1 percent, largely as a result of increased revenue from MATAV's mobile communications business, which were partially offset by a decline in revenues from MATAV's fixed-line traffic.

Revenues from other activities amounted to EUR 2.3 billion in 2000, representing an increase of EUR 397 million, or 21.1 percent, as compared to 1999. Due to the first consolidation in 2000 of the subsidiaries mentioned above, revenues of the international segment increased EUR 127 million. The remaining increase is due to increased revenues of MATAV.

Income before taxes of other activities were significantly influenced both in 2000 and 2001 by unusual or infrequently occurring factors. In 2001, these factors were gains on the sale of Sprint shares (EUR 1.9 billion) and an unscheduled write-down of the book value of France Telecom shares (EUR 312 million). In 2000, these factors were gains on the sale of Deutsche Telekom's interest in WIND (EUR 2.3 billion), losses on disposition of non-current assets and increased provisions (EUR 0.8 billion). Without regard to these factors, income before taxes of other activities amounted to EUR 134 million in 2001, representing an increase of EUR 528 million, or 134 percent, as compared to 2000. An improvement in income before taxes of MATAV, as well as the first-time full-year consolidation of Macedonia Telecom and Croatian Telecom, were primarily responsible for this development. The Hungarian telecommunications sector was opened to full competition at the end of 2001, which could have an adverse effect on MATAV's income before taxes in coming years.

The increase in income before taxes from 1999 to 2000 is attributable primarily to the first-time full-year consolidation of Siris and Eurobell in 2000. Depreciation and amortization increased primarily due to the new subsidiaries and related amortization on goodwill acquired.

Liquidity and Capital Resources

The following table provides information concerning Deutsche Telekom's cash flows.

	Year ended December 31,		
	2001	2000	1999
	(millions of euro)		
Net cash provided by operating activities	11,934	10,000	9,588
Net cash used for investing activities	(5,365)	(27,706)	(18,684)
Net cash provided by (used in) financing activities	(4,811)	17,863	7,965
Effect of foreign exchange rate changes on cash and cash equivalents	(26)	(29)	(55)
Net increase (decrease) in cash and cash equivalents[1]	1,732	128	(1,186)
Cash and cash equivalents, at beginning of year	1,006	878	2,064
Cash and cash equivalents, at end of year	2,738	1,006	878

(1) Cash and cash equivalents include cash and short-term investments with original maturities of three months or less.

Liquidity

Net Cash Provided by Operating Activities

Net cash provided by operating activities in 2001 amounted to EUR 11.9 billion, representing an increase of EUR 1.9 billion or 19.3 percent, compared to 2000.

Net cash provided from operating activities, excluding net interest paid, increased by EUR 3.3 billion, or 25.7 percent, to EUR 16.3 billion, despite the fact that net income declined from EUR 5.9 billion for 2000 to a net loss of EUR 3.5 billion for 2001. In part, this development reflects the contribution of increased depreciation and amortization to the decline in net income. In addition, net income for 2000 reflected a number of gains that did not have an impact on net cash provided by operating activities, including:

- gain from the sale of shares in Global One (EUR 2.9 billion) and gain from the sale of shares in cable companies in Nordrhein-Westfalen and Hessen (EUR 3.0 billion), the related cash effects of which are shown under net cash provided by investing activities, and
- dilution gains from the initial public offering of T-Online (EUR 2.7 billion), the cash effects of which are shown under net cash provided by financing activities.

In 2001, the gains from the sale of Sprint shares (EUR 1.9 billion) have no impact on net cash provided by operating activities while the cash proceeds (EUR 3.4 billion) are reflected as cash provided by investing activities.

Major contributors to the increase of EUR 1.9 billion in net cash provided by operating activities from 2000 to 2001 were an improvement in working capital and a tax refund received during 2001, the effects of which were partially offset by an increase in net interest paid.

Net cash provided by operating activities in 2000 amounted to EUR 10.0 billion, representing an increase of EUR 412 million, or 4.3 percent, over 1999. As described above, net income for 2000 reflected a number of gains that did not have an impact on net cash provided by operating activities. Major contributors to the increase in cash-flows of operating activities were an increase in interest received, a positive change in working capital and increased accruals. These factors were offset, however, by increased interest paid that resulted from higher debt levels and higher tax payments that were in excess of tax expense.

Net Cash Used For Investing Activities

Cash used for investing activities consists of net changes in temporary cash investments (i.e., securities with a maturity of over three months) and other cash used for investing activities such as capital expenditures, acquisitions and proceeds from sales of assets.

	Year ended December 31,		
	2001	2000	1999
	(millions of euro)		
Net change in short-term investments	4,440	401	2,328
Other cash used for investing activities	(9,805)	(28,107)	(21,012)
Net cash used for investing activities	(5,365)	(27,706)	(18,684)

Net cash used for investing activities amounted to EUR 5.4 billion in 2001, representing a decrease of EUR 22.3 billion, or 80.6 percent, as compared to 2000. This decrease is due in large part to the fact that cash expenditures for the acquisition of UMTS licenses in Germany, Great Britain and Austria in 2000 (EUR 15.3 billion) were not matched by any comparable factors in 2001. The decrease in net cash used for investing activities is also due in part to a reduction in capital expenditures for acquisitions of financial assets and acquisitions of, or investments in, fully consolidated subsidiaries. These amounted to EUR 6.2 billion in 2001, relating primarily to VoiceStream (EUR 4.1 billion), as compared to EUR 12.8 billion in 2000, relating primarily to the initial investment in VoiceStream, the acquisition of further shares in PTC and the investment in the mobile communications joint venture BEN in the Netherlands. Both in 2000 and in 2001, net cash used for investing activities was influenced by cash received from investing activities. In 2000, Deutsche Telekom received cash inflows from the disposition of shares in consolidated companies and financial assets (EUR 7.6 billion), which relate to primarily to the sale of shares in Global One and the broadband cable companies in Nordrhein-Westfalen and Hessen and to the sale of investments in non-current securities. In 2001 Deutsche Telekom received cash inflows from the disposition of shares in consolidated companies and financial assets amounting to EUR 4.5 billion, of which EUR 2.7 billion related to the sale of Deutsche Telekom's interest in WIND and EUR 912 million related to the sale of interests in the regional cable television company for Baden-Württemberg. A net change of EUR 4.4 billion in short-term investments and marketable securities, of which the sale of Deutsche Telekom's interests in Sprint accounted for EUR 3.4 billion, also had a positive effect on the development of net cash used for investing activities from 2000 to 2001, as did Deutsche Telekom's sale of receivables in an asset-backed securities transaction in 2001 (EUR 1.4 billion).

Cash used for investing activities increased from 1999 to 2000, largely as a result of the factors influencing 2000 that are described in the preceding paragraph. Deutsche Telekom's acquisition of a majority interest in debis Systemhaus had no net effect on cash used for investing activities in 2000, because Deutsche Telekom contributed EUR 4.6 billion in cash to debis Systemhaus in exchange for a 50.1 percent stake in debis Systemhaus. As debis Systemhaus is fully consolidated in Deutsche Telekom's group accounts, no cash outflow was recognized. In 1999, Deutsche Telekom received a net amount of EUR 2.3 billion from reducing its short-term investments.

Net Cash Provided By (Used For) Financing Activities

Net cash used for financing activities in 2001 amounted to EUR 4.8 billion, as compared to net cash provided by financing activities of EUR 17.9 billion in 2000. This development resulted primarily from a net increase in medium and long-term liabilities of EUR 17.3 billion in 2000, as compared to an increase of EUR 7.4 billion in medium and long-term liabilities in 2001. In 2000, cash flow provided by financing activities was significantly influenced by the issuance of a multi-currency global bond in an amount equivalent to EUR 15.4 billion, primarily to finance the cash outlays for the acquisition of UMTS licenses. In contrast, new indebtedness incurred during 2001 was used primarily to refinance bonds that were approaching maturity and thus did not result in cash provided by financing activities. In addition, net cash provided by financing activities in 2000 included EUR 3.3 billion from the initial public offering of shares of T-Online International AG and dilution effects from other investments. Dividends paid in 2001 remained unchanged from 2000.

Net cash provided by financing activities amounted to EUR 17.9 billion in 2000, representing an increase of EUR 9.9 billion, or over 100 percent, as compared to 1999, as a result of the multi-currency bond issue described above and an increase of EUR 6.3 billion in borrowings under Deutsche Telekom's existing debt issuance program. Further funds were provided by the initial public offering of shares of Deutsche Telekom's subsidiary T-Online International (EUR 3.1 billion). EUR 1.9 billion were used for the payment of dividends in 2000, as compared to EUR 1.7 billion in 1999.

Capital Resources

At December 31, 2001, the Deutsche Telekom group had credit facilities with banks totaling EUR 26.2 billion and with contractual rates of interest in a range of 0.81 percent to 9.8 percent per annum. Deutsche Telekom does not expect that the recent downgrades of its long-term debt ratings will prevent it from renewing these facilities annually. As of December 31, 2001, the credit lines under these facilities had been drawn upon in the aggregate amount of EUR 4.9 billion, of which T-Mobile UK accounted for EUR 4.0 billion. The interest rates under a substantial portion of Deutsche Telekom's credit facilities will step up in the event of certain ratings downgrades. These credit facilities contain debt covenants defining a number of events of default.

As of December 31, 2001, EUR 25.5 billion of Deutsche Telekom's liabilities were guaranteed by the Federal Republic. Indebtedness incurred by Deutsche Telekom since the beginning of 1995 is no longer guaranteed by the Federal Republic, as described above under the heading "Item 7. Major Shareholders and Related Party Transactions — Related Party Transactions — Federal Republic Guarantees." For a discussion of funding and treasury policies, see note 29 to the consolidated financial statements and "Item 11. Quantitative and Qualitative Disclosures about Market Risk."

Deutsche Telekom expects that its principal liquidity requirements for 2002 will include its expected capital expenditures budget, cash to repay indebtedness and cash to pay a dividend in respect of financial year 2001 and to acquire the remaining 49.9% of debis. Deutsche Telekom plans to fund these liquidity requirements primarily through cash flow from operations, proceeds of the sale of interests in certain subsidiaries and proceeds from the sale or other monetization of assets, including in particular assets not central to its business strategy, and through the refinancing of existing indebtedness, of which EUR 17.5 billion (including liabilities to banks) will reach maturity in 2002. Deutsche Telekom cannot offer assurances that the proceeds of asset dispositions and sales of minority interests in subsidiaries, if a decision is not made to undertake any such sales, will meet Deutsche Telekom's expectations for 2002. Following discussions with the rating agencies in March 2002, Moody's lowered Deutsche Telekom's long-term rating from A3 to Baa1 and Standard and Poor's lowered the long-term rating from A– to BBB+. These downgradings are expected to increase interest expense of Deutsche Telekom by approximately EUR 130 million per annum because the terms for part of Deutsche Telekom's current indebtedness provide for an interest rate step-up of 50 basis points upon any rating downgrade below the single-A-category. In addition, these downgrades may have the effect of increasing interest expense on future indebtedness of Deutsche Telekom. Financing and refinancing conditions will depend principally upon future market conditions, Deutsche Telekom's rating as a debtor and its future prospects. If Deutsche Telekom were to reduce its planned capital expenditures materially, this could adversely affect its ability to take full advantage of opportunities in growth areas, such as mobile telecommunications.

Capital Expenditures and Investments

The following table provides information concerning capital expenditures and investments in subsidiaries, associated companies and related companies as well as proceeds from the sales of non-current assets and investments.

	Year ended December 31,			Year ended December 31,	
	2001	2000	1999	2001/2000	2000/1999
	(millions of euro)			(% change)	
Capital expenditures	10,868	23,536	5,974	(53.8)	294.0
Investments	6,193	12,830	16,113	(51.7)	(20.4)
Proceeds from sales of non-current assets and investments	(5,872)	(8,253)	(1,075)	28.9	669.2
Other	(1,384)	(6)	—	n/a	200.0
Net cash used for investing activities(1)	9,805	28,107	21,012	(65.1)	33.8

(1) Excluding net change in short-term investments and marketable securities.

Capital Expenditures

The following table provides information concerning Deutsche Telekom's capital expenditures and related percentage changes. Other capital expenditures include intangible assets, other equipment, plant and office equipment as well as advance payments and construction in progress.

	Year ended December 31,			Year ended December 31,	
	2001	2000	1999	2001/2000	2000/1999
	(millions of euro)			(% change)	
Fixed networks	3,831	2,985	2,373	28.3	25.8
Mobile networks	1,692	873	750	93.8	16.4
Buildings	159	263	364	(39.5)	(27.7)
Other capital expenditures	5,186	19,415	2,487	(73.3)	680.7
Total capital expenditures	10,868	23,536	5,974	(53.8)	294.0

Capital expenditures in 2001 included EUR 3.1 billion, which are shown under "other capital expenditures". Such expenditures were made up primarily of advanced payments and construction in progress. Capital expenditures in 2000 included investments in UMTS licenses in Germany, the United Kingdom and Austria (EUR 15.3 billion) and work in progress for mobile networks (EUR 1.2 billion), both of which are shown under other capital expenditures.

Investments

Investments in subsidiaries, associated companies and other financial assets amounted to EUR 6.2 billion in 2001. Investments in fully consolidated companies, which accounted for EUR 5.7 billion, related primarily to VoiceStream and Powertel, RadioMobil, Croatian Telecom and Macedonia Telecom. Investments in associated and related companies and other financial assets, amounted to EUR 0.5 billion.

Investments in subsidiaries, associated companies and other financial assets amounted to EUR 12.8 billion in 2000. Investments in fully consolidated companies, which account for EUR 4.3 billion, related primarily to MATAV, Westel 900 and Slovenske Telekomunikacie. Investments in associated and related companies and other financial assets, which accounted for EUR 8.5 billion, related primarily to the initial investment in VoiceStream and to PTC in Poland and BEN in the Netherlands.

Investments in subsidiaries, associated companies and other financial assets made in 1999 totalled EUR 16.1 billion. Deutsche Telekom's investments in fully consolidated companies (principally One 2 One, max.mobil Siris) accounted for EUR 12.6 billion of this total. A further EUR 1.2 billion related to equity investments in Croatian Telecom, which accounted for EUR 0.8 billion, and in Sprint and Atlas/Global One, each of which accounted for EUR 0.2 billion. A loan of EUR 0.2 billion was granted to DETECON, an associated company. Deutsche Telekom invested a further EUR 1.3 billion in other investment securities, of which EUR 1.0 billion was invested in fixed-income securities and EUR 0.3 billion in specialized security funds (mainly fixed funds).

Research and development, patents and licenses

For a description of Deutsche Telekom's research and development activities, see "Item 4. Information on the Company — Description of Business Segments — Innovation Management (Research and Development)."

U.S. GAAP

Critical Accounting Policies under U.S. GAAP

In order to prepare the reconciliation of the Deutsche Telekom's consolidated financial statements to U.S. GAAP, the following critical accounting policies require significant judgments and estimates different from those used for German GAAP.

Impairment of intangible assets and property, plant and equipment and related goodwill

To assess impairment of intangible assets and property, plant and equipment and related goodwill under U.S. GAAP, Deutsche Telekom applies SFAS 121, "Accounting for the impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed of." If management has concluded that impairment indicators exist, Deutsche Telekom tests for impairment by comparing the sum of the future undiscounted cash flows derived from an asset or a group of assets to their carrying value. If the carrying value of the asset or the group of assets exceeds the sum of the future undiscounted cash flows, impairment is considered to exist. If an impairment is considered to exist on the basis of undiscounted cash flows, the impairment charge is measured using an estimation of the assets' fair value, typically using a discounted cash flow method. The identification of impairment indicators, the estimation of future cash flow and the determination of fair values for assets or groups of assets requires management to make significant judgments concerning the identification and validation of impairment indicators, expected cash flows and applicable discount rates. If actual results differ from these estimates, or if Deutsche Telekom adjusts these estimates in future periods, operating results could be significantly affected.

Statement of Financial Accounting Standards (''SFAS'') No. 142, ''Goodwill and Other Intangible Assets'' became effective in 2002, and as a result, Deutsche Telekom will cease to amortize goodwill. In lieu of amortization, Deutsche Telekom is required to perform an initial impairment review of its goodwill for U.S. GAAP purposes in early 2002 and an annual impairment review thereafter. Deutsche Telekom expects to complete its initial review during the first half of 2002. For further information regarding new accounting standards, including SFAS 142, refer to ''New U.S. Accounting Pronouncements'' below and ''Item 3. Key Information — Risk Factors.''

Revenue Recognition

Under U.S. GAAP, Deutsche Telekom defers the recognition of customer activation revenues and related incremental customer activation costs and amortizes them over the expected duration of the customer relationship. Deutsche Telekom assesses the estimated average duration of the relationship based on historical customer turn-over. If management's estimates are revised, material differences may result in the amount and timing of Deutsche Telekom's revenue for any period.

Deferred Taxes

Under U.S. GAAP, deferred taxes are recorded for temporary differences, including net operating loss carryforwards. In addition, under U.S. GAAP, Deutsche Telekom records a valuation allowance to reduce its deferred tax assets to the amount that is more likely than not to be realized. Deutsche Telekom has considered, for U.S. GAAP purposes, future taxable income and ongoing prudent and feasible tax planning strategies in assessing the need for the valuation allowance. In the event that Deutsche Telekom were to determine that it would be able to realize its deferred tax assets in the future in excess of their net recorded amount, an adjustment to the deferred tax asset would increase income in the period such determination were made. In the event that Deutsche Telekom were to determine that it would not be able to realize all or part of its net deferred tax asset in the future, an adjustment to the deferred tax asset would be charged to income in the period such determination were made. For further information in this regard, see ''New U.S. GAAP Accounting Pronouncements'' in note 41 to the Consolidated Financial Statements of Deutsche Telekom.

Other Accruals

Under U.S. GAAP, loss contingencies are recognized in accordance with SFAS 5, ''Accounting for Contingencies.'' Liabilities are accrued when a loss contingency is considered to exist and when a loss is considered probable and can be reasonably estimated. Management makes these estimates primarily with the support of internal specialists, if available, or with the support of outside consultants, such as actuaries or legal counsel. Revision of management's estimates of these loss contingencies may significantly effect future operating results.

Impairment of Long-term Investments

Under US GAAP, if a long-term investment's fair value declines below cost, the investor must determine whether there is adequate evidence to overcome the presumption that the decline is other than temporary. Such evidence may include:

- recoveries in fair value subsequent to the balance sheet date;
- the investee's financial performance and near-term prospects (as indicated by factors such as earnings trends, dividend payments, asset quality, and specific events), and
- the financial condition and prospects for the investee's geographic region and industry.

The evaluation of whether a decline in fair value is other than temporary may require considerable management judgment.

Reconciling differences between German GAAP and U.S. GAAP

Under U.S. GAAP, Deutsche Telekom's net income was EUR 523 million in 2001, EUR 9.3 billion in 2000 and EUR 1.5 billion in 1999, compared to a net loss of EUR 3.5 billion in 2001, and net income of EUR 5.9 billion in 2000 and EUR 1.3 billion in 1999 under German GAAP. Under U.S. GAAP, shareholders' equity was EUR 73.7 billion at December 31, 2001, and EUR 46.1 billion at December 31, 2000, compared to EUR 66.3 billion at December 31, 2001, and EUR 42.7 billion at December 31, 2000 under German GAAP.

The following section describes the significant reconciling differences between German GAAP and U.S. GAAP and the anticipated effects of these items. Other differences may arise in future years that may not have been anticipated. This discussion should be read in connection with notes 38 to 41 to the consolidated financial statements.

- Valuation adjustments of fixed assets — Under U.S. GAAP, Deutsche Telekom has recorded reconciling adjustments for differences in accounting for write-downs of fixed assets, primarily related to its real estate holdings. As of December 31, 2001 approximately EUR 3.0 billion of the cumulative reconciling adjustment is due to the reversal of write-downs of land and buildings. As a result of this difference in the basis of land and buildings between U.S. GAAP and German GAAP, should Deutsche Telekom sell portions of the related assets, the potential gain or loss to be recognized by Deutsche Telekom will be either lower (for gain) or higher (for loss) under U.S. GAAP than under German GAAP due to the higher carrying net values that will be allocated to the assets to be sold. Absent a sale, this basis difference in Deutsche Telekom's real estate properties will lead to higher depreciation expenses to be recorded under U.S. GAAP than under German GAAP. These adjustments will also result in higher depreciation expense under U.S. GAAP than under German GAAP in the future.

- Mobile communication licenses — Under U.S. GAAP, Deutsche Telekom does not amortize mobile communication licenses, primarily European UMTS licenses, that are not in use during the network build-out phase and begins amortization once the network is placed into service. Under German GAAP, amortization begins upon acquisition and continues through the expected period of use. Additionally, for U.S. GAAP, interest is capitalized during the period the mobile network is being constructed and, is subsequently amortized over the expected period of use. For U.S. GAAP net income was increased by EUR 2.1 billion and EUR 865 million for the years ended December 31, 2001 and 2000, respectively, related to the deferral of these expenses and should continue at the same level, subject to impairment considerations, over the build-out period. Once the networks are in place, capitalization of these costs will cease and related costs capitalized will be amortized into income over the remaining expected period of use.

- Effects of dilution gains — Under U.S. GAAP, reconciling adjustments for dilution gains and goodwill were recorded totaling EUR 1.9 billion for the year ended December 31, 2000, related to subsidiary shares exchanged as a part of various business combinations. This goodwill and related dilution gains were not recorded under German GAAP. Amortization of the additional goodwill recorded totaled EUR 250 million and EUR 170 million in 2001 and 2000, respectively, based on goodwill lives ranged from 7 to 15 years. In 2001, an impairment charge of EUR 146 million was recorded under U.S. GAAP to reduce the carrying value of the investment in comdirect. The charge was taken as a result of the continued losses of comdirect and the decline in the market value of the stock of comdirect. The impairment charge was calculated by comparing the book value of the investment in comdirect including goodwill with the market value of the shares owned.

- Goodwill and asset differences — Differences in accounting for business purchase combinations, goodwill and other intangible and tangible assets have resulted in differences in amortization expense for U.S. GAAP as compared to German GAAP. Effective January 1, 2002, because of the implementation of FAS 142, goodwill and indefinite lived intangible assets will no longer be amortized under U.S. GAAP, resulting in higher U.S. GAAP income. In addition, goodwill and indefinite lived intangible assets will be tested for impairment at least annually, which may result in a write-down of goodwill and indefinite lived intangible assets under U.S. GAAP.

- Write-down of tradenames — In 2001, an unscheduled write-down under German GAAP of EUR 1.0 billion related to the rebranding of T-Mobile subsidiaries, was not recorded for U.S. GAAP purposes as it did not meet the impairment criteria under U.S. GAAP. However, under U.S. GAAP, the useful lives have been shortened to one year and the remaining carrying amount will be completely amortized by December 31, 2002.
- Effects of full consolidation of debis — Under U.S. GAAP the acquisition of debis has been accounted for as a 100% acquisition effective October 20, 2000, while under German GAAP debis was considered a partially owned subsidiary consolidated at the 50.1% level. As a result of this difference, the Company recognized, in both 2000 and 2001, additional amortization expense due to increased goodwill and intangible assets, financing costs due to recognition of debt financing of the acquisition, and a portion of debis's net income which were allocated to minority interest under German GAAP. Such difference are due to recognizing 100% of debis's net income under U.S. GAAP versus recognizing only 50.1% under German GAAP and will not continue in periods after December 31, 2001, as the Company completed the acquisition of the minority interest in debis during 2002. Additionally, effective January 1, 2002, as a result of the implementation of FAS 142, goodwill and indefinite lived intangible assets will no longer be amortized under U.S. GAAP, resulting in higher income. In addition, goodwill and indefinite lived intangible assets will be tested for impairment at least annually which may result in write-down of goodwill and indefinite lived intangible assets under U.S. GAAP.
- Taxes — The tax effects of certain applicable reconciliation items described above are included in the total difference in income taxes between German GAAP and U.S. GAAP. The tax effects of the individual items are calculated by multiplying the relevant reconciliation items by the effective tax rates of the tax jurisdictions in which the entities with the reconciling items reside. These tax effects will reverse in future years as the related reconciliation items reverse the impact on net income as described in previous paragraphs.
- Deferred income — Under U.S. GAAP, the Company implemented Staff Accounting Bulletin 101 (SAB 101) in 2000. Due to the implementation of SAB 101, the Company deferred activation fees, certain one-time charges, and certain related direct incremental costs, up to the amount of revenues deferred, and is amortizing these revenues and expenses over the expected duration of the customer relationship. Additionally, the Company also deferred revenues on certain other contracts under U.S. GAAP and is amortizing these revenues over the contract lives.
- Derivatives — Under U.S. GAAP, the Company adopted SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" (SFAS 133) in 2001. Upon initial application of SFAS 133, on January 1, 2001, the Company recognized a one-time net gain of EUR 226 million (after taxes of EUR 144 million) through income and a cumulative adjustment of a net loss of EUR 22 million (after taxes of EUR 10 million) in accumulated other comprehensive income. The EUR 22 million cumulative adjustment to accumulated other comprehensive income will be reclassified into the Company's future net earnings/losses as the interest payments on certain floating-rate liabilities affect earnings. In 2001, EUR 8 million of such loss was recognized by the Company in current year losses.
- The remaining differences between German GAAP and U.S. GAAP consist primarily of capitalization of internally developed software, value added taxes, unrealized gains on marketable securities, deferral of gains on divestitures, asset backed securitization and investment in equity investees, which are historically recurring differences that should continue in future periods.

New U.S. GAAP Accounting Pronouncements

In June 2001, the FASB issued Statement of Financial Accounting Standards (SFAS) No. 141, "Business Combinations," and SFAS No. 142, "Goodwill and Other Intangible Assets," SFAS 141 supersedes APB Opinion 16, "Business Combinations," and SFAS No. 38, "Accounting for Pre-acquisition Contingencies of Purchased Enterprises." This statement requires that the purchase method of accounting be used for all business combinations initiated after June 30, 2001, and changes the criteria for recognizing intangible assets apart from goodwill. SFAS 142 supersedes APB Opinion 17, "Intangible Assets," and addresses how purchased intangibles should be accounted for upon acquisition. The statement prescribes the necessary accounting for both identifiable intangibles and goodwill after initial recognition. SFAS 142 requires that goodwill and indefinite, lived intangible assets no longer be amortized upon adoption of this statement, but instead tested for impairment at least annually. Amortization of definite lived intangibles will continue over the useful life. For U.S. GAAP reporting, the provisions of SFAS 141 apply to all business combinations initiated after June 30, 2001. The provisions of SFAS 142 are required to be applied starting with fiscal years beginning after December 15, 2001, except for the nonamortization provisions for goodwill and indefinite lived intangible assets acquired after June 30, 2001, which will be subject immediately to provisions of this statement. The Company has adopted the provisions of SFAS 141 for its acquisition of Croatian Telecom.

As a result of the implementation of SFAS 142, a number of major wireless carriers in the United States have concluded that the U.S. Federal Communications Commission (''FCC'') wireless spectrum licenses should be considered to be intangible assets with indefinite lives under SFAS 142. Classification by Deutsche Telekom of its FCC licenses as indefinite lived would require scheduled amortization of licenses to cease commencing January 1, 2002 and trigger a number of related issues, the treatment of which is currently being evaluated. These issues include the method of testing for impairment and accounting for deferred income taxes related to the change to indefinite lives. Prior to January 1, 2002 these licenses were treated as intangibles with definite lives and the reversal of their related deferred tax liabilities was deemed to match the realization of the deferred tax assets and, as such, no valuation allowance for the deferred tax asset was necessary. If it is concluded that the FCC licenses are indefinite, however, subsequent to January 1, 2002, the deferred tax liabilities associated with these licenses would no longer be available to support the realization of the VoiceStream and Powertel deferred tax assets or future deferred tax assets because of the resulting indefinite timing of the reversal of such deferred tax liabilities. Therefore, a reassessment of the useful lives of the licenses would require Deutsche Telekom for U.S. GAAP purposes to record a valuation allowance with a corresponding charge to earnings of EUR 4.3 billion in the first quarter of 2002 relating to all of the VoiceStream and Powertel deferred tax assets. These deferred tax assets were recorded in respect of net operating loss carryforwards assumed upon the acquisition of VoiceStream and Powertel in May, 2001.

Deutsche Telekom is currently assessing whether the change in the amortization of the FCC licenses for U.S. GAAP purposes should have any implications on its net income under German GAAP as well and the further impact of the implementation of SFAS 141 and 142 on its results of operations, financial position, and cash flows, except for the non-amortization provision of goodwill which was considered upon the acquisition of Croatian Telecom.

In July 2001, the FASB issued SFAS 143, ''Accounting for Asset Retirement Obligations.'' The objective of this statement is to provide accounting guidance for legal obligations associated with the retirement of long-lived assets. SFAS 143 requires that the fair value of a liability for an asset retirement obligation be recognized in the period in which it is incurred and accreted to its present value each period. The associated asset retirement costs are capitalized as part of the carrying amount of the long-lived asset and subsequently depreciated over the asset's useful life. The statement is effective for financial statements issued for fiscal years beginning after June 15, 2002. Deutsche Telekom is currently determining the impact of the adoption of SFAS 143 on its results of operations, financial position and cash flows.

In October 2001, the FASB issued SFAS 144, ''Accounting for the Impairment or Disposal of Long-Lived Assets.'' This new standard supersedes SFAS 121, ''Accounting for the Impairment of Long-Lived Assets and for the Long-Lived Assets to be Disposed Of'', providing one accounting model for the review of asset impairment. SFAS 144 retains the current requirement to recognize an impairment loss only if the carrying amounts of long-lived assets to be held and used are not recoverable from their expected undiscounted future cash flows and exceeds its fair value. However, goodwill is no longer required to be allocated to these long-lived assets when determining their carrying amounts. SFAS 144 requires that a long-lived asset to be disposed of other than by sale be considered held and used until it is disposed of, requiring the depreciable life to be adjusted as an accounting change. The criteria used to classify long-lived assets to be disposed of by sale have changed from SFAS 121. However, the statement continues to require that the amortization and depreciation of all long-lived assets to be disposed of by sale cease and that these assets be recorded at the lower of their carrying amount or fair value less cost to sell. Statement 144 also supersedes the section of the APB Opinion 30 which prescribes reporting for the effects of a disposal of a segment of a business. Discontinued operations are no longer measured on a net realizable value basis, and future operating losses are no longer recognized before they occur. The statement also broadens the definition of a discontinued operation to include a component of an entity. The provisions of SFAS 144 are effective for financial statements issued for fiscal years beginning after December 15, 2001, and interim periods within those fiscal years. The Company has assessed the impact of adopting this statement to be an asset write-down of approximately EUR 50 million, which will be recorded for U.S. GAAP during the first quarter of 2002.

Contractual Obligations and Commercial Commitments

The following table represents the contractual cash obligations and other commercial commitments of Deutsche Telekom as of December 31, 2001;

	Payments due by period			
	Total	Less than 1 year	1 to 5 years	After 5 years
	(in millions of €)			
Contractual Obligations				
Debt Bonds and debentures	58,301	12,598	28,447	17,256
Liabilities to banks	8,730	754	4,984	2,992
Total	67,031	13,352	33,431	20,248

	Payments due by period		
	Total	Less than 1 year	After 1 year
	(in millions of €)		
Other			
Present value of payments to special pension fund	9,372	845	8,527
Purchase commitments for interests in other companies other companies	6,872	5,022	1,850
Purchase commitments for capital projects in progress including obligations arising from future expenditures	3,201	3,142	59
Commitments arising from trans-actions not yet settled	444	315	129
Operating leases	6,839	1,269	5,570
Capital lease obligations	906	46	860
Total	27,634	10,639	16,995

	Total
	(in millions of €)
Guarantees and Commitments	
Liabilities arising from warranty agreements	66
Guarantees	224
Total	290

T-Mobile International AG has issued two guarantees in favor of TDC Mobile International A/S and Belgacom Services S.A., respectively. Under them, T-Mobile unconditionally and irrevocably guarantees to pay TDC and Belgacom any outstanding amounts that Ben owes to them under two loan agreements that provide credit facilities of up to EUR 128 million and EUR 297 million, respectively. As of December 31, 2001, T-Mobile International AG's combined aggregate contingent liability under these guarantees is approximately EUR 190 million.

The present value of payments required to be made by Deutsche Telekom AG on the basis of the life expectancy tables by Prof. Dr. Klaus Heubeck ("Richttafeln 1998"), in accordance with Postreform II, to the company's special pension fund for civil servants or its successor amounted to EUR 9.4 billion at December 31, 2001, of which EUR 3.9 billion relates to future payments for pensions of civil servants.

Purchase commitments for interests in other companies relate mainly to the option held by DaimlerChrysler Services AG, Berlin, to sell its remaining shareholding of 49.9 percent in T-Systems ITS GmbH (formerly debis Systemhaus GmbH, Leinfelden-Echterdingen) to Deutsche Telekom AG. Daimler-Chrysler Service AG has exercised the contractually agreed put option, effective January 1, 2002. Deutsche Telekom acquired the remaining 49.9 percent stake in T-Systems ITS GmbH in exchange for a cash payment of approximately EUR 4.7 billion.

The shareholders' agreement governing T-Mobile International's ownership interest in Ben, includes both a call option held by T-Mobile International and put options held by the other owners of Ben. Both the call and put options allow for T-Mobile International to acquire all or a portion of the shares held by the other owners in Ben. The call option is exercisable in 2002, and the put options are exercisable in 2003, each at the option of the holding party. The exercise price of these options at December 31, 2001 was EUR 17.23 per share. The purchase price for the minimum number of shares, which can be acquired under these options, is EUR 25 million. The purchase price for the maximum number of shares, which can be acquired under these options, is EUR 1.7 billion. In the event that any of these options are exercised, T-Mobile International could have a controlling interest in Ben and would therefore consolidate its operations.

Furthermore, Deutsche Telekom has committed itself to acquire further shares in PTC, Polska Telefonia Cyfrowa Sp. z o.o., Poland, for EUR 153 million.

VoiceStream has agreed to indemnify Western Wireless on an after-tax basis for any taxes, penalties, interest and various other expenses incurred by Western Wireless if it is required to recognize such a gain. The amount of such gain that Western Wireless would recognize would be equal to the difference between the fair market value of VoiceStream common shares at the time of the spin-off and Western Wireless' adjusted tax basis in such shares at the time. The estimated range of possible liability of VoiceStream, not including interest and penalties, if any, is from zero to $400 million.

ITEM 6. Directors, Senior Management and Employees

General

In accordance with the German Stock Corporation Act (*Aktiengesetz*), Deutsche Telekom AG has a Supervisory Board (*Aufsichtsrat*) and a Management Board (*Vorstand*). The two Boards are separate, and according to the German Stock Corporation Act, no individual may simultaneously be a member of both Boards. The Management Board is responsible for managing Deutsche Telekom and representing Deutsche Telekom in its dealings with third parties, while the Supervisory Board appoints and removes the members of the Management Board and oversees the management of Deutsche Telekom but is not permitted to make management decisions. The official auditor is appointed by the shareholders of the company and is engaged by the Supervisory Board.

Both the members of the Management Board and the members of the Supervisory Board owe a duty of loyalty and care to Deutsche Telekom. In carrying out their duties, members of both the Management Board and the Supervisory Board must exercise the standard of care of a prudent and diligent businessman. The interests of Deutsche Telekom are deemed to include the interests of the shareholders, the interests of the work force and, to some extent, the common interest, and both the Management Board and the Supervisory Board must take all these interests into account when taking actions or decisions. Although there is no explicit obligation to act solely in the interests of shareholders, the Management Board is required to respect their rights to equal treatment and equal information.

The Supervisory Board has comprehensive monitoring functions. To ensure that these functions are carried out properly, the Management Board must, among other things, regularly report to the Supervisory Board with regard to current business operations and future business planning. The Supervisory Board is also entitled to request special reports at any time. The Management Board is required to ensure appropriate risk management within Deutsche Telekom and has to establish an internal monitoring system.

Pursuant to the Articles of Association of Deutsche Telekom and the By-laws (*Geschäftsordnung*) of the Management Board, the Management Board must obtain the consent of the Supervisory Board for certain actions, including acquisitions or dispositions of real property having a value of more than EUR 25 million, acquisitions or dispositions of equity investments, the appointment of members of the supervisory board or other bodies having supervisory functions of direct or indirect subsidiaries with a share capital of more than EUR 2.5 million or an annual turnover of more than EUR 25 million, and actions concerning the corporate structure or the strategy of Deutsche Telekom. In addition, under the German Stock Corporation Act, the Supervisory Board is authorized to subject other actions of the Management Board to its consent.

Under German law, shareholders, like other persons, are prohibited from using their influence on Deutsche Telekom to cause a member of the Management Board or the Supervisory Board to act in a way that is harmful to Deutsche Telekom. A controlling enterprise may not cause Deutsche Telekom to take measures that are unfavorable to Deutsche Telekom unless any resulting disadvantage is compensated. An individual shareholder or any other person exerting influence on Deutsche Telekom to cause a member of the Management Board or of the Supervisory Board or holders of special proxies (*Prokuristen* or *Handlungsbevollmächtigte*) to act in a way that is unfavorable to Deutsche Telekom or its shareholders is liable for damages to Deutsche Telekom and its shareholders. Board members who have neglected their duties in taking the actions are likewise jointly and severally liable for damages.

As a general rule under German law, a shareholder has no direct recourse against the members of the Management Board or the Supervisory Board in the event that they are believed to have breached a duty to Deutsche Telekom. Only Deutsche Telekom has the right to claim damages from the members of the two boards. Deutsche Telekom may only waive such damages or settle such claims if at least three years have passed and if the shareholders so approve at a shareholders' meeting with a simple majority of the votes, provided that the opposing shareholders do not hold, in the aggregate, one tenth or more of the nominal share capital of Deutsche Telekom and do not formally express their opposition at the shareholders' meeting by having their opposition noted in the minutes of the meeting maintained by a German notary (*Notar*).

Supervisory Board

In accordance with the German Stock Corporation Act (*Aktiengesetz*), the Supervisory Board of Deutsche Telekom consists of twenty members, ten of whom represent the shareholders and ten of whom represent the employees. Members of the Supervisory Board may be elected for a term of up to five years. Re-election is permitted.

The Supervisory Board members representing the shareholders are elected at the General Meeting of the shareholders. The first election of shareholder representatives to the Supervisory Board took place at the shareholders' meeting in July 1996. The present shareholder representatives have been elected at the shareholders' meeting in May 2001. In general, the terms of office of the shareholder representatives will expire at the end of the shareholders' meeting at which the shareholders discharge the Supervisory Board members in respect of the fourth financial year following the member's commencement of tenure of office. The financial year in which tenure of office commences is not counted for this purpose. The next general election of all of the shareholders' representatives on the Supervisory Board will take place at the shareholders' meeting in 2006.

Supervisory Board members representing employees were last elected on October 2, 1997 by the employees in accordance with the provisions of the Co-Determination Act of 1976 (*Mitbestimmungsgesetz*). In this election procedure, employees elect ten representatives made up of workers, regular employees, senior management employees and three union representatives. Since October 1997, new employee representatives have been appointed by a local court pursuant to Section 104 of the German Stock Corporation Act. The terms of office of the employee representatives on the Supervisory Board expire at the end of the shareholders' meeting in May 2002. Up to the election of new employee representatives in accordance with the Co-Determination Act in late 2002, a local court will reappoint for that transitional period the current employee representatives pursuant to Section 104 of the German Stock Corporation Act. Under the law that governed the conversion of Deutsche Telekom to a stock corporation, civil servants, who are not covered by the Co-Determination Act, are included in these groups of employee representatives according to their occupations for purposes of these elections.

A member of the Supervisory Board elected by the shareholders may be removed by a shareholders' resolution by a majority of at least three quarters of the votes cast. A member of the Supervisory Board elected by the employees may be removed by a majority of at least three quarters of the votes cast by the relevant class of employees.

The Supervisory Board must meet at least twice in each half year. To achieve a quorum, at least ten of the members of the Supervisory Board must be present or cast their votes in writing. Except in situations in which a different majority is required by law, such as the appointment of Management Board members and the election of the Chairman and Co-Chairman of the Supervisory Board, the Supervisory Board takes decisions by simple majority of the votes cast. If, in the event of a deadlock, a second vote again results in a tie, the chairman of the Supervisory Board can cast a deciding vote.

Members of the Supervisory Board of Deutsche Telekom

The current members of Deutsche Telekom's Supervisory Board, the year in which they were appointed, the month in which their current term expires and their principal occupations are as follows.

Dr. Hans-Dietrich Winkhaus	Member since:	1999
Chairman	Expiration of Current Term:	May 2006
	Principal Occupation:	Member of the Shareholders' Committee of Henkel KGaA
	Supervisory Board Memberships/Directorships:	• ERGO Versicherungsgruppe AG, Düsseldorf • Degussa AG, Düsseldorf • Deutsche Lufthansa AG, Köln • Schwarz Pharma AG, Monheim, Chairman of the Supervisory Board • BMW AG, München

Rüdiger Schulze Vice-Chairman	Member since:	1999
	Expiration of Current Term:	May 2002
	Principal Occupation:	Chairman of Division 9 "Telecommunication, Information Technology and Data Processing" of the Union ver.di
	Supervisory Board Memberships/Directorships:	T-Mobile Deutschland GmbH, Bonn (previously DeTeMobil Deutsche Telekom MobilNet GmbH, Bonn), Vice Chairman of Supervisory Board
Gert Becker	Member since:	1995
	Expiration of Current Term:	May 2006
	Principal Occupation:	Former Chairman of the Management Board of Degussa AG
	Supervisory Board Memberships/Directorships:	• ALCAN Deutschland GmbH, Eschborn • Bankhaus Metzler KGaA, Frankfurt am Main, Chairman of the Supervisory Board • Bilfinger + Berger Bau AG, Mannheim, Chairman of the Supervisory Board • Degussa-Hüls AG, Frankfurt am Main (until 2001)
Josef Falbisoner	Member since:	1997
	Expiration of Current Term:	May 2002
	Principal Occupation:	Chairman of the Bavarian District of the Union ver.di
	Supervisory Board Memberships/Directorships:	PSD-Bank, München, Augsburg office
Dr. Hubertus von Grünberg	Member since:	2000
	Expiration of Current Term:	May 2006
	Principal Occupation:	Serves as member on several Supervisory Boards
	Supervisory Board Memberships/Directorships:	• Allianz-Versicherungs AG, München • Continental AG, Hannover • MAN AG, München • Schindler Holding AG, Hergiswil/ Schweiz, Administrative Board
Dr. sc. techn. Dieter Hundt	Member since:	1995
	Expiration of Current Term:	May 2006
	Principal Occupation:	Managing Shareholder of Allgaier Werke GmbH; President of the National Union of German Employers Associations
	Supervisory Board Memberships/Directorships:	• EvoBus GmbH, Stuttgart • Stauferkreis Beteiligungs-AG, Göppingen, Chairman of the Supervisory Board • Stuttgarter Hofbräu AG, Stuttgart • Stuttgarter Hofbräu Immobilien Verwaltungs-AG, Stuttgart, Chairman of the Supervisory Board • Landesbank Baden-Württemberg, Stuttgart, Administrative Board

Rainer Koch	Member since:	2000
	Expiration of Current Term:	May 2002
	Principal Occupation:	Chairman of the Central Works Council of DeTeImmobilien, Deutsche Telekom Immobilien und Service GmbH, Münster
	Supervisory Board Memberships/Directorships:	• GMG Generalmietgesellschaft mbH, Münster (previously DeTeImmobilien, Deutsche Telekom Immobilien und Service GmbH, Münster)
Dr. h.c. André Leysen	Member since:	1995
	Expiration of Current Term:	May 2006
	Principal Occupation:	Chairman of the Administrative Board of GEVAERT N.V.
	Supervisory Board Memberships/Directorships:	• Agfa-Gevaert AG, Leverkusen, Chairman of the Supervisory Board • Bayer AG, Leverkusen • E.ON AG, Düsseldorf • Schenker AG, Essen • Agfa-Gevaert N.V. Mortsel/Antwerpen, Chairman of the Administrative Board • GIB Group, Brüssel (until 2001) • Tessenderlo Chemie N.V., Tessenderlo (until 2001) • Vlaamse Uitgeversmaatschappij N.V., Groot-Bijgaarden (until 2001)
Waltraud Litzenberger	Member since:	1999
	Expiration of Current Term:	May 2002
	Principal Occupation:	Member of the Works Council of Deutsche Telekom AG, Eschborn branch office
	Supervisory Board Memberships/Directorships:	PSD-Bank e.G., Koblenz
Michael Löffler	Member since:	1995
	Expiration of Current Term:	May 2002
	Principal Occupation:	Member of the Works Council of Deutsche Telekom AG, at Dresden branch office
	Supervisory Board Memberships/Directorships:	None

Hans-W. Reich	Member since:	1999
	Expiration of Current Term:	May 2006
	Principal Occupation:	Speaker of the Management Board, Kreditanstalt für Wiederaufbau (KfW)
	Supervisory Board Memberships/Directorships:	• ALSTOM GmbH, Frankfurt am Main • DePfa Deutsche Pfandbrief Bank AG, Wiesbaden • Deutsche Energie-Agentur GmbH, Berlin • Frachtkontor Junge & Co. GmbH, Hamburg (until 2001) • Haftpflicht-Unterstützungs-Kasse kraftfahrender Beamter Deutschlands a.G., Coburg • HUK-COBURG Holding GmbH, Coburg • HUK-COBURG-Allgemeine-Versicherungs-Aktiengesellschaft, Coburg • IKB Deutsche Industriebank AG, Düsseldorf • Krankenversicherungs-Aktiengesellschaft der HUK- COBURG (HUK-COBURG-Krankenversicherung), Coburg • Lebensversicherungs-Aktiengesellschaft der HUK- COBURG (HUK-COBURG-Leben), Coburg • RAG AG, Essen • Thyssen Krupp Steel AG, Duisburg • Thyssen Krupp Werften GmbH, Emden (until 2001)
Rainer Röll	Member since:	1998
	Expiration of Current Term:	May 2002
	Principal Occupation:	Vice-Chairman of the Central Works Council at Deutsche Telekom AG
	Supervisory Board Memberships/Directorships:	None
Wolfgang Schmitt	Member since:	1997
	Expiration of Current Term:	May 2002
	Principal Occupation:	Head of Deutsche Telekom AG's Regional Directorate, South-Western District
	Supervisory Board Memberships/Directorships:	PSD-Bank, Stuttgart-Freiburg e.G.
Prof. Dr. Helmut Sihler	Member since:	1996
	Expiration of Current Term:	May 2006
	Principal Occupation:	Vice-Chairman of the Administrative Board, Novartis AG
	Supervisory Board Memberships/Directorships:	• Dr. Ing. h.c. F. Porsche AG, Stuttgart, Chairman of the Supervisory Board • max.mobil Telekommunikations Service GmbH, Vienna/Austria • Novartis AG, Basel

Michael Sommer	Member since:	2000
	Expiration of Current Term:	May 2002
	Principal Occupation:	Vice-Chairman of the Union ver.di
	Supervisory Board Memberships/Directorships:	• BHW Bausparkasse, Hameln • Postbank, Bonn, Vice-Chairman of the Supervisory Board • T-Systems International GmbH, Bonn, Vice-Chairman of the Supervisory Board
Ursula Steinke	Member since:	1995
	Expiration of Current Term:	May 2002
	Principal Occupation:	Chairwoman of the Works Council at DeTeCSM Northern District Service and Computer Center
	Supervisory Board Memberships/Directorships:	None
Prof. Dr. h.c. Dieter Stolte	Member since:	1995
	Expiration of Current Term:	May 2006
	Principal Occupation:	Director General of Zweites Deutsches Fernsehen (ZDF) TV broadcasting organization (until March 15, 2002) Publisher of the newspapers "Welt" and "Berliner Morgenpost"
	Supervisory Board Memberships/Directorships:	• Bavaria Film- und Fernsehstudios GmbH, München/Geiselgasteig, Chairman of the Supervisory Board • ZDF Enterprises GmbH, Mainz, Chairman of the Supervisory Board • Sportrechte- und Marketing-Agentur GmbH, München, Chairman of the Supervisory Board
Bernhard Walter	Member since:	1999
	Expiration of Current Term:	May 2006
	Principal Occupation:	Former Speaker of the Management Board of Dresdner Bank
	Supervisory Board Memberships/Directorships:	• Bilfinger + Berger Bau AG, Mannheim • DaimlerChrysler AG, Stuttgart • Degussa-Hüls AG, Frankfurt am Main (until 2001) • Deutsche Hyp Deutsche Hypothekenbank Frankfurt-Hamburg AG, Frankfurt am Main, Chairman of the Supervisory Board (until 2001) • Heidelberger Zement AG, Heidelberg (until 2001) • Henkel KGaA, Düsseldorf • mg technologies ag, Frankfurt am Main • Staatliche Porzellan-Manufaktur Meissen GmbH, Meissen • Thyssen Krupp AG, Düsseldorf • Wintershall AG, Kassel

Wilhelm Wegner	Member since:	1996
	Expiration of Current Term:	May 2002
	Principal Occupation:	Chairman of the Central Works Council at Deutsche Telekom AG
	Supervisory Board Memberships/Directorships:	• VPV Allgemeine Versicherungs-AG, Köln • VPV Holding AG, Stuttgart • Vereinigte Postversicherung VVaG, Stuttgart • PSD Bank Düsseldorf e.G., Düsseldorf
Prof. Dr. Heribert Zitzelsberger	Member since:	1999
	Expiration of Current Term:	May 2006
	Principal Occupation:	State Secretary in the Federal Ministry of Finance (Bundesministerium der Finanzen)
	Supervisory Board Memberships/Directorships:	None

The Supervisory Board maintains the following committees:

- The *Executive Committee (Präsidialausschuss)* is responsible for deciding the terms of the service contracts and other contractual arrangements between Deutsche Telekom AG and the Management Board. In particular, the committee determines salaries and incentive compensation awards for members of the Management Board and establishes goals for performance-based compensation plans. Members of the Executive Committee are Dr. Hans-Dietrich Winkhaus (Chairman), Dr. Andre Leysen, Rüdiger Schulze and Wilhelm Wegner.
- The *Committee for Special Matters (Ausschuss für besondere Angelegenheiten)* is responsible for reviewing and consulting on complex finance and business matters concerning the company. Those matters are delegated by the Chairman of the Supervisory Board or the Supervisory Board itself. In addition, although the Company does not have an audit committee whose functions are limited to discussions of the Company's financial statements with the Company's independent auditors, the Committee for Special Matters also reviews the annual report during a meeting with the Company's auditors in preparation for the Supervisory Board's annual meeting on the approval of the financial statements in accordance with section 171 of the German Stock Corporation Act. Members of the Committee for Special Matters are Dr. Hans-Dietrich Winkhaus (Chairman), Wolfgang Schmitt, Rüdiger Schulze, Bernhard Walter, Wilhelm Wegner and Prof. Dr. Heribert Zitzelsberger.

In addition to the two committees mentioned above, the Supervisory Board has formed a mediation committee and a personnel committee.

The committees have an equal number of shareholder representatives and employee representatives. The chairman of the Supervisory Board also serves as chairman of the Executive Committee. The chairman of the Committee for Special Matters is a representative of the shareholders. The chairman has the deciding vote in case of a tie in both committees. The chairman of the personnel committee is a representative of the employees.

Management Board

Pursuant to Deutsche Telekom's Articles of Association, the Supervisory Board determines the size of the Management Board, subject to the requirement that the Management Board must have at least two members. The Supervisory Board may appoint a chairman of the Management Board as well as a deputy chairman. The members of the Management Board are appointed by the Supervisory Board for a term of up to five years and they may be re-appointed or have their term extended for one or more terms of up to five years. Under certain circumstances, such as a material breach of duty or a bona fide vote of no confidence by the shareholders, a member of the Management Board may be removed by the Supervisory Board prior to the expiration of the five-year term. A member of the Management Board may not deal with, or vote on, matters relating to proposals, arrangements or contracts between himself and Deutsche Telekom. The Management Board takes action by simple majority unless otherwise provided by law, as in the case of a vote on the adoption of Rules of Procedure. In the event of a deadlock, the Management Board member in whose area of responsibility the resolution falls has a deciding vote. If the resolution falls in an area which is not allocated to a Management Board member, the vote of the chairman of the Management Board decides in case of a deadlock.

Members of the Management Board of Deutsche Telekom

The name, age, term of office, current position and business experience of the current members of the Management Board are set forth below. The members of the Management Board may be reached at Deutsche Telekom's registered address.

Dr. Ron Sommer, born in 1949, was appointed chairman of the Management Board in May 1995. As a result of the restructuring of the Group Board of Management effective May 1, 2001, he is responsible for the strategic management and development of the Deutsche Telekom, group communications and regulatory matters. He received a doctorate in mathematics and began his career with the Nixdorf group, first in New York and then in Paderborn and Paris. In 1980, he became managing director of Sony Deutschland and in 1986 become chairman of the Management Board of Sony Deutschland. In 1990, Dr. Sommer became president and chief operating officer of Sony USA, and in 1993, he took over the management of Sony Europe in the same capacity.

Expiration of current term: May 15, 2005

Other board memberships outside Deutsche Telekom: Münchener Rückversicherungs-Gesellschaft AG, München

Josef Brauner, born in 1950, has been Head of CS, which includes the divisions T-Com and T-Systems and the operational management of the Networks Infrastructure Group and its field organisation, since May 1, 2001. He joined Deutsche Telekom in June 1997 as head of the Main Department for Sales and became head of the Sales and Customer Care Division and a member of the Management Board in October 1998. He started his sales career with Avery as the U.S. company's branch manager for Germany, Austria and Switzerland. Mr. Brauner next joined Sony Deutschland, where he was appointed head of sales in the investment goods division and afterwards became head of that division. In 1988, Mr. Brauner became a member of the Management Board of Sony Deutschland, and in 1993 was appointed chairman of that board.

Expiration of current term: September 30, 2003

Other board memberships outside Deutsche Telekom: none

Dr. Karl-Gerhard Eick, born in 1954, was appointed head of the Finance and Controlling Division and a member of the Management Board in January 2000. After studying business administration and earning a doctorate, Dr. Eick worked in various positions for BMW AG between 1982 and 1988. From 1989 to 1991 he acted as head of Controlling at WMF AG in Geislingen. In 1991, he became head of the Controlling, Planning and IT Division for the Carl Zeiss Group. From 1993 to 1999, he held top management positions with the Haniel Group, where he was responsible for the Controlling, Business Administration and IT Division of the strategic management holding company of Franz Haniel & Cie. GmbH.

Expiration of current term: December 31, 2004

Other board memberships outside Deutsche Telekom: Dresdner Bank Luxembourg S.A., Supervisory Board

Jeffrey A. Hedberg, born in 1961, was appointed head of Deutsche Telekom's International Division and a member of the Management Board in January 1999. Mr. Hedberg, who is a U.S. citizen, joined the TVM/Matuschka group in Munich in 1985, where he was primarily involved in analyzing venture capital projects for companies with international operations. From 1990 to 1992, he worked in the international division of US West, and then as an associate at Coopers & Lybrand in international projects of the globally active telecommunications group. In 1994, Mr. Hedberg joined Swisscom, where he was in charge of international investments as Executive Vice President and member of the company's senior management.

Expiration of current term: December 31, 2006

Other board memberships outside Deutsche Telekom: none

Dr. Heinz Klinkhammer, born in 1946, was appointed head of Deutsche Telekom's Personnel and Legal Affairs Division and a member of the Management Board in April 1996. Since May 1, 2001 he has been Head of Human Resources and the newly added department Top Management Staff. Dr. Klinkhammer received a doctorate in law and began his career at the Institute for German and European Labor, Social and Business Law before becoming a Labor Court judge. From 1979 to 1990, he worked at the Ministry of

Labor, Health and Social Affairs of the state of North-Rhine/Westphalia. In 1991, he became Labor Director at Hüttenwerke Krupp Mannesmann GmbH and, in 1992, board member of Mannesmannröhren-Werke AG.

Expiration of current term: March 31, 2006

Other board memberships outside Deutsche Telekom: Federal Posts and Telecommunications Agency, Administrative Board, Bonn; Vereinigte Postversicherung VVaG, Stuttgart (until 2001)

Gerd Tenzer, born in 1943, was appointed head of the Networks Division in January 1990 and has been a member of Deutsche Telekom's Management Board since January 1995, responsible for Networks, Purchasing, and Environmental Protection. Since May 1, 2001 he is responsible for Production, Technology, Innovation Management, Purchasing and Environmental Protection. As a communications engineer, he worked in the telecommunications research department at AEG-Telefunken from 1968 to 1970. In 1970, he joined what was then the Deutsche Bundespost. In 1975, Mr. Tenzer moved to the Federal Ministry of Posts and Telecommunications, where he became head of the Telecommunications Policy Section in 1980. From 1990 to 1994, he was a member of the Management Board of Deutsche Bundespost TELEKOM.

Expiration of current term: December 31, 2004

Other board memberships outside Deutsche Telekom: VDE GmbH, Supervisory Board, Frankfurt

Dr. Max Hirschberger, born in 1956, was appointed as a member of the Management Board on April 11, 2001. Dr. Hirschberger is responsible for the Corporate Affairs Division as of May 1, 2001, which combines Legal Affairs, Strategy, Organization, Internal Auditing and Information Management. After having studied law in Regensburg and Lausanne and obtaining a Masters degree at the University of Michigan, Dr. Hirschberger joined the Legal Affairs Department at BMW AG in Munich in 1987. From 1994 he was the head of the Department for Corporate and International Law. He joined Deutsche Telekom in 1997 when he became head of the newly established Deutsche Telekom group Office. In this capacity, he was responsible for the Support Office of the chairman of the Management Board.

Expiration of current term: April 30, 2006

Other board memberships outside Deutsche Telekom: none

Kai-Uwe Ricke, born in 1961, was appointed as a new member of the Management Board on April 11, 2001. Mr. Ricke is in charge of the Group's mobile communications and online activities as of May 1, 2001. As a member of the Management Board, he is responsible for the T-Mobile and since December 2001 for the T-Online division. Mr. Ricke was Chairman of the Management Board of T-Mobil Deutschland GmbH (Deutsche Telekom MobilNet GmbH) until March 31, 2000. On February 1, 2000, he was appointed Chairman of the Management Board of T-Mobile International AG (TMO). Following bank training and studies at the European Business School at Schloss Reichartshausen, Mr. Ricke started his professional career as assistant to the Management Board chairman of Bertelsmann AG in Gütersloh, and went on to become Head of Sales and Marketing for its subsidiary, Scandinavian Music Club AG, in Malmö, Sweden. From 1990 until June 1995, Mr. Ricke was Managing Director of Talkline Verwaltungsgesellschaft mbH and Talkline PS Phone Service GmbH, both in Elmshorn near Hamburg. From July 1995 to December 1997, Mr. Ricke managed the affairs of Talkline GmbH, Elmshorn, as chairman of the Managing Board.

Expiration of current term: April 30, 2006

Other board memberships outside Deutsche Telekom: none

Compensation

Management Board Compensation

The remuneration of the Management Board of Deutsche Telekom in respect of financial year 2001 amounted to EUR 17,425,106.39. A portion of the total compensation of the Management Board is paid pursuant to a bonus arrangement. The bonus payment is determined by the Supervisory Board and is based upon three performance targets, each of which is weighted one third in determining the total bonus payment: financial performance, or the earnings of the Company as a whole; individual performance, or a Management Board member's success in meeting particular goals set for his business area; and overall performance, designed to reward intangible aspects of performance such as leadership. Financial performance targets and individual performance targets are set by the Supervisory Board at the beginning of each fiscal year. For the year ended December 31, 2001, 23.2 percent of the total remuneration was paid pursuant to this bonus arrangement.

In addition, a proposal to establish a stock option program for the members of the Management Board and key employees was approved at the shareholders' meeting in May 2001. Options in respect of a total of 1,743,908 shares have been granted to members of the Deutsche Telekom Management Board. The options have an exercise price of EUR 30 and mature on August 12, 2011. For further information on this program, see "— Share Ownership" below and Notes 26 and 40 to the Consolidated Financial Statements.

Pension accruals totaling EUR 14,771,535 have been established in the books of Deutsche Telekom AG for the members of the Management Board as of December 31, 2001. Obligations for such persons for which no reserve has been established amounted to EUR 3,393,980 as of December 31, 2001. Payments to former members for the Management Board of Deutsche Telekom or their surviving family members amounted to EUR 805,117.05 in 2000.

None of the members of the Management Board has a service contract with the Company or any of its subsidiaries providing for benefits upon termination of employment.

Supervisory Board Compensation

The Articles of Association as amended by a shareholders' resolution on May 25, 2000 provide for an annual compensation at EUR 50,000 for the chairman, EUR 37,500 for the deputy chairman and EUR 25,000 for each remaining member of the Supervisory Board. In addition, members of the Supervisory Board are entitled to reimbursement of actual out-of-pocket expenses and to receive an attendance fee amounting to EUR 200 for each meeting of the Supervisory Board or its committees. The value-added tax payable on this compensation will be borne by Deutsche Telekom. These compensation rules applied for the first time for the 1999 financial year. Remuneration for members of the Supervisory Board of Deutsche Telekom for fiscal year 2001 accrued in the amount of EUR 549,500 inclusive of meeting expenses and is subject to approval by the shareholders in the annual meeting on May 28, 2002. Remuneration for fiscal year 2001 will be paid out following shareholder approval.

None of the members of the Supervisory Board has a service contract with the Company or any of its subsidiaries providing for benefits upon termination of employment.

Share Ownership

The members of Deutsche Telekom's Management Board owned a total of approximately 8,036 Deutsche Telekom shares and options in respect of a total of 2,152,512.88 Deutsche Telekom shares as of January 10, 2002. No individual member of the Management Board beneficially owned 1 percent or more of the outstanding shares of Deutsche Telekom as of January 10, 2002.

The members of the Supervisory Board owned a total of 4,658 Deutsche Telekom shares as of January 10, 2002. No individual member of the Supervisory Board beneficially owned 1 percent or more of the outstanding shares of Deutsche Telekom as of January 10, 2002.

At the shareholders' meeting on May 25, 2000, an amendment to the Articles of Association was approved that created conditional capital of up to EUR 64 million for issuance of up to 25 million shares upon exercise of options granted to management and key employees in connection with a stock-based compensation plan adopted in May 2000 (the "Stock Option Plan 2000"). At the shareholders' meeting on May 29, 2001, an amendment to the Articles of Association was approved that cancelled the conditional capital created in May 2000, except for the nominal amount of EUR 2,621,237.76, which serves to grant subscription rights to members of the Management Board and executives of Deutsche Telekom AG, as well as members of the management boards and other executives of second-tier and lower-tier subsidiaries within the context of Deutsche Telekom's Stock Option Plan 2000. Further, the shareholders' meeting on May 29, 2001 approved the cancellation of the authorized capital for Deutsche Telekom's Stock Option Plan 2000 of up to EUR 12.8 million approved by the shareholders' meeting on May 25, 2000 for the purpose of issuing up to 5 million new shares for the Deutsche Telekom Stock Option Plan 2000.

In addition, at the shareholders' meeting on May 29, 2001 a further amendment to the Articles of Association was approved that conditionally increased Deutsche Telekom's registered share capital by up to a nominal amount of EUR 307.2 million by issuance of up to 120 million new shares. This conditional share capital may only be used if and to the extent that option rights granted pursuant to Deutsche Telekom's Stock Option Plan 2001 described in notes 26 and 40 to the consolidated financial statements are exercised and new shares are delivered upon such exercise. Option rights that have not been or may not be exercised prior to the expiration of the exercise period will expire. Shares issued from the conditional share capital generally will be entitled to any dividends paid in respect of the year in which they are issued. Shares that are issued after the end of any fiscal year, but before the ordinary general shareholders' meeting at which the activities of the Management Board for that year are approved, will be entitled to any dividends paid in respect of that year. The shareholders' resolution authorized Deutsche Telekom's Supervisory Board to grant stock options to the members of its Management Board and authorized the Management Board to grant stock options to all other eligible participants.

The shareholders' resolution authorized Deutsche Telekom's Supervisory Board to determine the detailed terms for the issuance of shares from the conditional share capital and for the grant of options as well as the other terms of the stock option plan if the Management Board is the beneficiary of the stock option plan. In all other cases, the Management Board is authorized to make these determinations.

The amendments to the Articles of Association took effect upon entry in the Commercial Register (*Handelsregister*), which occurred in June 2001.

For further information regarding the stock-based compensation plans for 2000 and 2001, including numbers of options granted, exercise prices and expiration dates, please refer to notes 26 and 40 to the consolidated financial statements. Please refer to "Item 8. Financial Information — Litigation" for a description of litigation with respect to the Stock Option Plan 2000.

Employees and Labor Relations

Employees

As of December 31, 2001, the companies within the Deutsche Telekom consolidated group employed a workforce of 257,058 people worldwide, excluding trainees and interns, which represented an increase of 13.2 percent from year-end 2000.

The table below provides a geographic breakdown of Deutsche Telekom's workforce at the dates indicated.

	December 31,		
	2001	2000	1999
Deutsche Telekom group employees	257,058	227,015	195,788
Thereof:			
Germany	178,336	179,197	172,690
European Union outside of Germany	16,538	16,577	7,521
Other European countries	43,343	29,408	15,365
North America	16,909	170	80
Rest of the world	1,932	1,663	132

The following table shows the number of employees in the Deutsche Telekom consolidated group at the date indicated, as well as a breakdown of Deutsche Telekom's workforce by category of activity.

Deutsche Telekom group employees(1)

	December 31,		
	2001	**2000**	**1999**
Deutsche Telekom AG	124,328	126,857	136,962
Thereof:			
Civil servants	54,615	59,901	71,123
Salaried employees and wage earners	69,713	66,956	65,839
Deutsche Telekom group	257,058	227,015	195,788
Thereof:			
Civil servants	54,615	59,901	71,123
Salaried employees and wage earners	202,443	167,114	124,665
Thereof:			
T-Com	116,557	117,504	124,742
T-Systems	42,931	40,253	19,316
T-Mobile	38,025	19,186	13,976
T-Online	2,960	3,010	1,236
Other activities	56,585	47,062	36,518

(1) Employees excluding trainees and interns

During fiscal year 2001, Deutsche Telekom did not employ a significant number of temporary employees.

Employee Relations

Works councils (*Betriebsräte*), whose members are elected by the employees, represent the interests of the employees vis-à-vis the employer in accordance with the Works Council Act of 1972 (*Betriebsverfassungsgesetz*), which was amended in 2001. Works councils are established locally, as well as at the level of Deutsche Telekom AG and at the group level. Works councils must be notified in advance of, and have the right to comment on, proposed employee terminations, relocations and other matters, and have codetermination rights in respect of certain social matters, including work schedules and rules of conduct. In 2001, the German Federal Government enacted amendments to the Works Council Act that increase the influence of works councils in some matters, such as the obligation to establish works councils for companies with more than 200 employees (previously 300). Furthermore, based on the requirements of the Act on European Works Councils (*Gesetz über europäische Betriebsräte*) Deutsche Telekom will establish a European works council in 2002, which will only have the right to information and consultation without participation in the decision making process.

Deutsche Telekom believes that its relations with the works council and the unions are good. Constructive relations with its employees and their representatives are of central importance to Deutsche Telekom.

Civil Servants

As of December 31, 2001, approximately 21 percent of the employees of the Deutsche Telekom group were civil servants. No employees hired after January 1, 1995 have been granted civil servant status. Pursuant to the laws that applied to the conversion of Deutsche Telekom to a stock corporation, Deutsche Telekom's civil servant employees retained their civil servant status when that conversion occurred. As such, the terms and conditions of their employment and the benefits owed to them continue to be governed by German regulations regarding civil servants. In particular, civil servant salaries are set by statute and not by Deutsche Telekom or by collective bargaining agreements. In addition, civil servants are tenured employees and may not be unilaterally terminated except in extraordinary, statutorily defined circumstances. Civil servants are not permitted to participate in work-related actions such as strikes, but are permitted to join labor unions. Although Deutsche Telekom is authorized pursuant to the law governing the privatization of Deutsche Telekom to exercise generally the rights and duties of the Federal Republic as the employer of civil servants, the Federal Postal and Telecommunications Agency (*Bundesanstalt für Post und Telekommunikation* or

"Federal Agency") has a right of consultation in the implementation of certain aspects of the terms under which Deutsche Telekom employs civil servants.

Civil servants employed by Deutsche Telekom are entitled to pension benefits provided by the Federal Government pursuant to the German Civil Servant Pension Act (*Beamtenversorgungsgesetz*). Pursuant to the law governing the privatization of Deutsche Telekom, Deutsche Telekom is required to make annual contributions to a special pension fund established to fund such pension obligations. The special pension fund was merged in 2000 with the special pension funds of Deutsche Post AG and Deutsche Postbank AG to form the joint pension fund Bundes-Pensions-Service für Post und Telekommunikation e.V. (BPS-PT). The BPS-PT works for the funds of all three companies and also handles the financial administration for the Federal Republic on a trust basis. All transactions for pension and allowance payments are made for the companies Deutsche Post AG, Deutsche Postbank AG and Deutsche Telekom AG.

In accordance with the provisions of the Post and Telecommunications Reorganization Act (*Gesetz zur Neuordnung des Postwesens und der Telekommunikation*), this pension fund makes pension and allowance payments to retired employees and their surviving dependents who are entitled to pension payments as a result of civil servant status. Deutsche Telekom AG is legally obligated as of 2000 to make an annual contribution to the special pension fund of 33 percent of the gross remuneration of active civil servants and the imputed gross remuneration of civil servants on temporary leave entitled to pension payments. These contributions amounted to EUR 845 million in 2001. A fixed annual contribution of EUR 1.5 billion was payable for the years 1995 through 1999.

The Federal Republic compensates the special pension fund for differences between the ongoing payment obligations of the special pension fund, amounts received from Deutsche Telekom AG and returns on assets, and guarantees that the special pension fund is always in a position to fulfill the obligations it has assumed. The Federal Republic cannot require reimbursement from Deutsche Telekom AG for amounts paid by it to the special fund.

Other Employees

As of December 31, 2001, approximately 79 percent of the employees of the Deutsche Telekom group were non-civil servants. In addition to being covered by collective bargaining agreements, the non-civil servant employees in Germany are in general covered by the German Termination Protection Act (*Kündigungsschutzgesetz*), which imposes various restrictions on the involuntary termination of employment.

The majority of Deutsche Telekom's employees in Germany are organized in unions, principally the union ver.di (*Vereinigte Dienstleistungsgewerkschaft*). Further, the company agrees on similar labor contracts with the organization of smaller unions (DPVKOM/CGPT). Due to Deutsche Telekom's acquisition of debis Systemhaus GmbH, the union IG Metall (*Industriegewerkschaft Metall*) also represents employees of T-Systems. The terms and conditions of employment and salary increases for non-civil servant employees are negotiated between Deutsche Telekom and the unions. Pursuant to the law governing the privatization of Deutsche Telekom, the Federal Agency is responsible for concluding collective bargaining agreements relating to certain statutorily defined non-wage benefits, rules of conduct and other general terms of employment. Such agreements only become effective with the consent of Deutsche Telekom. For further information regarding agreements among Deutsche Telekom and the Federal Postal and Telecommunications Agency, see "Item 7. Major Shareholders and Related Party Transactions — Related Party Transactions." Collective bargaining agreements between Deutsche Telekom and unions relating to remuneration typically have a term of one year.

Deutsche Telekom AG and the union ver.di concluded a new collective bargaining agreement in May 2001 that includes the introduction of a new evaluation and pay system as of July 1, 2001. As a result, Deutsche Telekom AG completed the phaseout of its old pay system, which was based on civil-service regulations. In future, employees' pay will be based solely on employees' positions and will no longer reflect criteria such as age, marital status or seniority. The new pay system will also increase the performance-based component of employee pay. Furthermore, a single collective bargaining agreement will apply throughout all of Germany, in the same manner and with the same terms. Division into "west" and "east" pay-scale areas will not continue. The collective bargaining agreement signed in May 2000 had already introduced a performance pay component for all employees. As of July 2001, the existing performance-based component of 2.15 percent of total pay will be increased to 6 percent. Deutsche Telekom's target is to increase the performance-based share of compensation up to 10 percent during the coming collective bargaining rounds. Results-based pay that depends on the achievement of individual or team goals as well as on the success of the company is initially planned only for certain categories of pay groups. Later, the results-based pay component will gradually supplant the performance component.

Collective bargaining agreements of major subsidiaries in the division T-Mobile and T-Systems already include provisions for pay based primarily on the employee's position and performance. The division T-Online is currently negotiating a new collective bargaining agreement.

For further information on the effects of these collective bargaining agreements on Deutsche Telekom's personnel expenses, see "Item 5. Operating and Financial Review and Prospects — Personnel Costs."

ITEM 7. Major Shareholders and Related Party Transactions

Major Shareholders

Historically, Deutsche Telekom formed an integral and undifferentiated part of Deutsche Bundespost, a state-owned special asset (*Sondervermögen des Bundes*). In 1989, Deutsche Bundespost was divided into three distinct entities — Deutsche Bundespost TELEKOM, Deutsche Bundespost POSTBANK and Deutsche Bundespost POSTDIENST. Deutsche Bundespost TELEKOM was transformed, with effect from January 1, 1995, into Deutsche Telekom AG, a private law stock corporation, which initially remained wholly owned by the Federal Republic.

The Federal Republic's direct ownership interest in Deutsche Telekom is approximately 30.92 percent. KfW, a development bank that is 80 percent owned by the Federal Republic and 20 percent owned by the German federal states, owns 12.13 percent.

The Federal Republic administers its shareholding and exercises its rights as a shareholder of Deutsche Telekom through the Federal Agency, which is subject to the supervision of the Finance Ministry. Except as described below, in its capacity as shareholder, the Federal Republic may exercise only those rights that it has under the German Stock Corporation Act and Deutsche Telekom's Articles of Association (*Satzung*).

For as long as the Federal Republic held, directly or indirectly or in combination with other public entities, a majority of Deutsche Telekom's voting share capital, it was entitled, under the Law on Budgetary Principles (*Haushaltsgrundsätzegesetz*), to require Deutsche Telekom to instruct its independent auditors to extend the scope of their audit of Deutsche Telekom and its subsidiaries to cover their management and certain other matters. The Federal Republic was entitled to receive copies of audit reports upon request. In addition, the Federal Audit Office (*Bundesrechnungshof*) reviews the activities of the Federal Republic regarding enterprises in which it holds interests. For as long as the Federal Republic was, directly or indirectly, the majority shareholder of Deutsche Telekom, the Federal Audit Office had the right to investigate questions arising from its review, including by inspecting Deutsche Telekom's operations as well as books and accounts. Similar rights apply with respect to those subsidiaries of Deutsche Telekom that so provide in their articles of incorporation. In reporting to the Federal Republic, Supervisory Board members who are elected on the initiative of the Federal Republic are not generally subject to the usual secrecy obligations applicable to Supervisory Board members; the Federal Republic must, however, maintain the secrecy of confidential information contained in these reports. Since the Federal Republic no longer holds a majority of Deutsche Telekom's voting share capital (either directly, indirectly or in combination with other public entities), Deutsche Telekom will no longer be subject to these requirements as of the financial year 2002.

At present, the Finance Ministry has one representative on the Supervisory Board of T-Systems International GmbH ("T-Systems"), T-Online International AG and T-Mobile International AG.

Ownership Interest of the Federal Republic in Deutsche Telekom

The table below sets forth the number of Deutsche Telekom AG ordinary shares held by holders of more than 5 percent of Deutsche Telekom ordinary shares and their percentage ownership, based on information available to Deutsche Telekom.

	12/31/2001		12/31/2000		12/31/1999	
Identity of Person or Group	**Shares owned**	**Percent**	**Shares owned**	**Percent**	**Shares owned**	**Percent**
Federal Republic of Germany	1,297,896,644	30.92%	1,297,485,401	42.83%	1,307,835,401	43.18%
Kreditanstalt für Wiederaufbau	509,164,599	12.13%	509,164,599	16.81%	654,290,599	21.60%
		43.05%		59.64%		64.78%

Due to the completion of the Deutsche Telekom/VoiceStream and the Deutsche Telekom/Powertel acquisitions, the aggregate ownership of Deutsche Telekom shares by the Federal Republic and KfW has been diluted to approximately 43 percent. The Federal Republic has publicly stated its intention to reduce substantially its ownership of Deutsche Telekom shares.

Related Party Transactions

Relationship with the Federal Republic

As is generally the case with other German corporations with a controlling shareholder, for as long as the Federal Republic is a shareholder with controlling influence (*beherrschender Einfluß*), Deutsche Telekom's Management Board is required to produce a report (*Abhängigkeitsbericht*) setting forth the relationships and the transactions entered into between Deutsche Telekom, on the one hand, and the Federal Republic or its affiliated enterprises, on the other hand. This related-party report, which is intended to protect minority shareholders and creditors, must include a declaration by the Management Board as to the fairness of transactions and dealings with the Federal Republic. Deutsche Telekom's independent auditors are required to confirm the accuracy of this report. The Supervisory Board is then required to review the related-party report and the auditor's findings thereon and to inform the shareholders as to the conclusion of both. In the 2001 related-party report, Deutsche Telekom's Management Board declared that under the circumstances known to the Management Board, at the time of performing the business transactions between Deutsche Telekom and the Federal Republic and its affiliated enterprises, including the Federal Agency, Deutsche Telekom received appropriate remuneration for these transactions, and that Deutsche Telekom did not perform or omit any actions on behalf of or on the instructions of the controlling shareholder, in its capacity as such, or any other affiliated companies. Deutsche Telekom's independent auditors have confirmed the accuracy of the 2001 related-party report regarding relationships between Deutsche Telekom and its controlling shareholder.

Coordination and Administrative Responsibilities of the Federal Agency

Pursuant to German law, the Federal Agency provides certain services to Deutsche Telekom, Deutsche Postbank and Deutsche Post and has certain rights and responsibilities with respect to the administration of the common affairs of these companies. For example, the Federal Agency is responsible for concluding general collective bargaining agreements (*Manteltarifverträge*) on behalf of these entities with employees relating only to certain non-wage benefits, rules of conduct and other general terms of employment. These agreements only become effective with the consent of the affected entity. The Federal Agency's right to conclude these agreements does not affect Deutsche Telekom's right to negotiate particular terms of employment, including wages, salaries and conditions of employment, independently on its own behalf. The Federal Agency also administers the health insurance fund for civil servants (*Postbeamtenkrankenkasse*) and the pension fund for non-civil servants (VAP) employed by Deutsche Telekom, Deutsche Postbank, Deutsche Post and others. The Federal Agency has certain additional responsibilities and rights with respect to civil servants employed by Deutsche Telekom, Deutsche Post and Deutsche Postbank. The Federal Agency has the right to provide advice concerning the coordination of the activities of Deutsche Telekom, Deutsche Postbank and Deutsche Post, particularly, with respect to their public image, issues that may arise if the business plans of these entities conflict and, upon request, with respect to certain personnel issues.

Services provided by the Federal Agency pursuant to applicable law are rendered on the basis of service agreements between Deutsche Telekom, Deutsche Postbank or Deutsche Post, on the one hand, and the Federal Agency, on the other. Since German law currently requires that each of Deutsche Telekom, Deutsche Postbank and Deutsche Post enter into a service agreement with the Federal Agency covering the services described above, Deutsche Telekom has not considered entering into arrangements with third parties for the provision of these services. Costs of the Federal Agency incurred in connection with providing these services are financed out of fees agreed upon with Deutsche Telekom, Deutsche Post and Deutsche Postbank. Deutsche Telekom paid costs of EUR 70.1 million for these services in 2001 (as compared to EUR 68.9 million in 2000).

The total costs of the Federal Agency, consisting mainly of personnel costs for its employees, are allocated pursuant to the cost attribution system of the Federal Agency in accordance with actual expenses.

Federal Republic as Regulator

The Federal Republic's role as regulator is independent and distinct from its role as shareholder. This regulatory function is exercised by the Regulatory Authority. The telecommunications licenses held in Germany by Deutsche Telekom were acquired from the Federal Republic or its agent. See "Item 4. Information on the Company — Regulation."

Federal Republic and Affiliated Entities as Customers

The Federal Republic is Deutsche Telekom's largest customer and purchases services on an arm's-length basis. Deutsche Telekom deals with the various departments and agencies of the Federal Republic of Germany as separate customers, and the provision of services to any one department or agency does not constitute a material part of Deutsche Telekom's revenues. Deutsche Telekom has also entered into contracts to provide telecommunications services to entities affiliated with the Federal Republic on an arms-length basis in the ordinary course of business.

Arrangement with Deutsche Post

Deutsche Telekom entered into an agreement with Deutsche Post AG in 2000 that calls for Deutsche Telekom to provide, among other things, information technology and corporate network services to Deutsche Post. In return, Deutsche Post provides distribution and transportation, printing, warehousing and other services. The objective of the arrangement is to allow each company to focus on its core competencies and dispose of peripheral activities. This arrangement resulted in a net transfer of around 1,500 Deutsche Telekom employees to Deutsche Post.

Federal Republic Guarantees

Under German law, all liabilities of Deutsche Telekom outstanding as of January 2, 1995, the date of Deutsche Telekom's registration in the Commercial Register (*Handelsregister*), became guaranteed by the Federal Republic. This guarantee replaced the Federal Republic's obligations with respect to Deutsche Telekom's liabilities when it was a state-owned special asset. Liabilities incurred after January 2, 1995 are not guaranteed by the Federal Republic.

Pension Contributions for Civil Servants

Civil servants (*Beamte*) employed by Deutsche Telekom are entitled to pension benefits provided by the Federal Republic. Under German law, Deutsche Telekom is required to make annual contributions to a special pension fund (*Unterstützungskasse*) established to fund these pension obligations. For further information, see "Item 6. Directors, Senior Management and Employees — Employees and Labor Relations" and "Item 5. Operating and Financial Review and Prospects — Consolidated Results of Operations — Personnel Costs."

Real Estate Investigation

Deutsche Telekom is advancing funds to cover the legal expenses being incurred by current and former board members in connection with the Bonn public prosecutors investigation of certain real estate valuation-related questions. These funds will be required to be repaid to Deutsche Telekom if there is a final determination that these individuals violated the law.

DT 3 Offering

In connection with the global offering by KfW of equity securities of Deutsche Telekom in June 2000, Deutsche Telekom agreed to bear certain offering-related expenses in view of the benefits accruing to Deutsche Telekom from the offering. Deutsche Telekom, the Federal Republic and KfW agreed to indemnify the underwriters for the offering against certain liabilities, including liabilities under the U.S. Securities Act of 1933, in the manner provided for in the underwriting agreement. The underwriting agreement allocated among Deutsche Telekom, the Federal Republic and KfW indemnification responsibility for different sections of the disclosure materials, with Deutsche Telekom taking responsibility vis-à-vis the underwriters for, among other things, the parts of the disclosure materials concerning its business and financial statements. Additionally, Deutsche Telekom agreed with KfW to assume responsibility for errors, if any, in the translation of some of the prospectuses and for certain supplementary disclosure items that were required under local law in some offering jurisdictions. As issuer of the shares that were offered, Deutsche Telekom became subject to the prospectus liabilities, if any, associated with its registering or listing the securities offered in various jurisdictions. The underwriting agreement provides that its underwriter indemnification provisions are in addition to, and do not affect, any liability that Deutsche Telekom, KfW, the Federal Republic or the underwriters may otherwise have. For a description of pending litigation and an investigation relating to the global offering, see "Item 8. Financial Information — Litigation."

Other Transactions

Deutsche Telekom provides telecommunications services to numerous companies, mainly throughout Europe, in the ordinary course of business, including firms in which it holds an ownership interest and firms with which certain members of the Supervisory Board are affiliated.

ITEM 8. Financial Information

Consolidated Financial Statements

See "Item 18. Financial Statements".

Export Sales

In 2001, EUR 13.2 billion in revenues, or 27.3 percent of total revenues, consisted of Deutsche Telekom's revenue generated with customers located in countries outside of Germany, as compared to EUR 7.8 billion, or 19 percent of total revenues, in 2000. EUR 6.1 billion of that amount was derived from customers in the European Union (other than Germany) in 2001, as compared to EUR 5.0 billion in 2000, and EUR 3.8 billion of that amount was derived from countries in the rest of Europe in 2001, as compared to EUR 2.3 billion in 2000.

Of the increase in international revenues from 2000 to 2001 companies newly acquired in 2000 and 2001 accounted for EUR 5.1 billion. VoiceStream and Powertel alone accounted for EUR 2.8 billion of the increase.

Litigation

Deutsche Telekom and its subsidiaries are involved in a number of legal proceedings in the ordinary course of their business. In addition, proceedings involving alleged abuse of a market dominant position by Deutsche Telekom and alleged antitrust violations are pending before competition and regulatory authorities.

Securities and Corporate Law-related Proceedings

A number of purported class action lawsuits have been filed and consolidated in the United States District Court for the Southern District of New York by or on behalf of purported purchasers of Deutsche Telekom ADSs issued pursuant to a registration statement on Form F-3 filed with the Securities and Exchange Commission on May 22, 2000, and pursuant to a prospectus dated June 17, 2000, and purported purchasers of Deutsche Telekom ADSs during the period from June 19, 2000 to and including February 21, 2001. The operative complaint in these consolidated actions asserts claims against Deutsche Telekom and the Chairman of its Management Board, and others, under U.S. federal securities statutes based on allegations that statements made in the registration statement and prospectus were materially false and misleading because they allegedly failed adequately to disclose detailed information relating to merger negotiations between Deutsche Telekom and VoiceStream Wireless Corporation, and allegedly overstated the value of Deutsche Telekom's real estate portfolio.

Press reports indicate that various private parties in Germany have been evaluating measures that might be taken against Deutsche Telekom, its management, or both, on the basis of allegations in the press and elsewhere that the book values recorded by Deutsche Telekom for its real property portfolio have been improperly established and maintained under applicable accounting principles. Deutsche Telekom disputes these allegations. A number of purported shareholders have written to Deutsche Telekom raising claims for damages, and more than 230 lawsuits have been filed in Germany by purported purchasers of Deutsche Telekom shares issued pursuant to a prospectus dated May 26, 2000. In many of these lawsuits, claims have been made with respect to the VoiceStream transaction analogous to those made in the purported U.S. class action lawsuits described above.

Deutsche Telekom intends to contest each of the aforementioned lawsuits vigorously. Because the lawsuits, which in the aggregate involve substantial damage claims, are in their preliminary stages, Deutsche Telekom is not in a position to predict their outcome or impact. However, Deutsche Telekom believes that the allegations in the lawsuits do not provide a basis for the recovery of damages because all required disclosures were made on a timely basis.

On June 26, 2000, two Deutsche Telekom shareholders filed a suit with the District Court in Bonn (*Landgericht Bonn*) seeking to have declared void the shareholders resolutions authorizing both the stock option plan and a related conditional capital increase. The case was dismissed by the District Court in Bonn (*Landgericht Bonn*) on February 20, 2001. The Higher Regional court Cologne (*Oberlandesgericht Köln*) dismissed the appeal against this decision.

On October 21, 1999, T-Mobile commenced arbitration proceedings in Vienna, Austria, against Elektrim S.A. and certain small shareholders of PTC. T-Mobile's claim alleges that these companies wrongfully failed to recognize Deutsche Telekom's rights of first refusal over approximately three percent of PTC, and that this failure was a material breach of the PTC shareholders' agreement. These companies have denied T-Mobile's claim, and Elektrim has filed a counterclaim against T-Mobile alleging that T-Mobile materially breached the shareholders' agreement by, among other things, attempting to purchase PTC shares from several small shareholders and obstructing Elektrim's purchase of PTC shares. T-Mobile has denied the allegations made in the counterclaim. A finding by the arbitration panel that a party has materially breached the PTC shareholders' agreement would give the non-defaulting party the right to acquire the defaulting party's PTC shares at book value, which would be substantially below their current fair market value. In December 2000, T-Mobile filed a second suit against Elektrim claiming that Elektrim breached the terms of the Deed of Foundation of PTC by transferring all but one share in PTC to Telco, a limited company under Polish law in which Elektrim has a shareholding of 51 percent and Vivendi S.A. a shareholding of 49 percent. In particular, T-Mobile claims that (i) the transfer of shares required approval by the Supervisory Board of PTC, (ii) the shareholder agreement permitted only the transfer of a party's entire interest and (iii) the consent of the Ministry of Telecommunications to the transfer was required but not obtained.

Investigations

As previously reported, the Bonn public prosecutor is conducting an investigation (*Ermittlungsverfahren*) into allegations in the press and elsewhere asserting that the book values recorded by Deutsche Telekom for its real property portfolio have been improperly established and maintained under applicable accounting principles. Recently, the prosecutor orally advised Deutsche Telekom that he has expanded his investigation to include whether Deutsche Telekom's fixed assets in general, including technical equipment and machinery, were substantially overvalued in Deutsche Telekom's 1995 opening balance sheet and possibly in later balance sheets. Deutsche Telekom believes that the book values of its fixed assets have been correctly presented in accordance with applicable accounting principles, and disputes allegations to the contrary. Deutsche Telekom has nonetheless been cooperating fully in the investigation and is interested in seeing it expeditiously resolved. Deutsche Telekom cannot offer assurances as to the timing or outcome of the prosecutor's investigations. Deutsche Telekom believes that the investigation is being conducted with regard to certain individuals and is not directed against Deutsche Telekom itself. The public prosecutor has publicly identified Deutsche Telekom's former Chief Financial Officer, the former Chairman of the company's Supervisory Board and the current Chairman of its Management Board as being among the individuals under investigation. Adverse consequences for Deutsche Telekom could follow if any of the individuals who are or who become the subject of the investigation were found to have violated the law.

The Bonn public prosecutor is conducting an investigation into whether Deutsche Telekom bore certain costs associated with the June 2000 global offering by KfW of Deutsche Telekom shares at a level not reasonably commensurate with the benefits Deutsche Telekom received. Deutsche Telekom is convinced that it acted appropriately, and is cooperating fully in the investigation.

Proceedings against Decisions of the German Telecommunications Regulator

The German telecommunications regulator issued an order in December 1999 that establishes the rates applicable to voice telephony interconnection services provided by Deutsche Telekom between January 1, 2000 and January 31, 2001. Because the decision of the German telecommunications regulator in this matter was based on an international benchmark rather than on the cost information submitted by Deutsche Telekom, Deutsche Telekom filed a complaint against this order with the Cologne Administrative Court (*Verwaltungsgericht Köln*) in January 2000.

In two decisions published in September and November 1999, the German telecommunications regulator took the position that regulatory approval is required for Deutsche Telekom's offers of services to service providers. This position relates to offers of both local calls and domestic and international long-distance calls. According to these decisions, these offers to resellers are seen as voice telephony services and Deutsche Telekom is seen as dominant in the market for those services. Deutsche Telekom's application for an injunction against the implementation of these decisions was rejected by the Cologne Administrative Court, but these decisions were reversed by the Appellate Administrative Court in Münster (*Oberverwaltungsgericht Münster*) in August and October 2000 respectively, concluding the injunction proceedings. The complaint in the main action was also rejected by the Cologne Administrative Court. Deutsche Telekom has appealed the decision.

In September 2000, the German telecommunications regulator issued an order establishing a new tariff structure for interconnection, replacing the basically distance-based tariff structure with an element-based tariff structure. Deutsche Telekom has filed a legal challenge against this order as well as an application for an injunction against the implementation of this order with the Cologne Administrative Court in October 2000. In December 2000 the Cologne Administrative Court granted the requested injunction. The German telecommunications regulator has applied for permission to appeal. The Appelate Administrative Court in Münster rejected the appeal in May 2001. The proceedings in the main action are still pending. The Cologne Administrative Court decided in favor of Deutsche Telekom. Mannesmann Arcor has appealed the decision.

In response to complaints from prospective voice telephony competitors of Deutsche Telekom, in July 1997, the predecessor of the German telecommunications regulator required Deutsche Telekom to allow the complainants unbundled access to end customer lines (the "local loop") within Deutsche Telekom's network for purposes of connecting their own customers. A motion for a temporary injunction against this order was rejected by the Cologne Administrative Court. In a hearing before the Appellate Administrative Court in Münster in September 1997, an agreement was reached substantially on the basis of the regulator's requirements, pursuant to which Deutsche Telekom now offers unbundled access to competitors. The Federal Administrative Court (*Bundesverwaltungsgericht*) in Berlin decided in April 2001 that Deutsche Telekom is obliged to offer unbundled access to competitors.

The German telecommunications regulator issued an order on March 9, 1998, rejecting in part an application by Deutsche Telekom for the approval of charges for access to the local loop. The German telecommunications regulator rejected Deutsche Telekom's cost calculations based on a purported lack of transparency in the calculations and the evaluation of the cost factors and prescribed lower charges (DM 20.65 plus VAT) than those Deutsche Telekom had sought. Deutsche Telekom filed a complaint against this order with the Cologne Administrative Court. In two decisions published in February 1999, the German telecommunications regulator reset the charge for the monthly rate at DM 25.40 plus VAT for a period ending in March 2001. Deutsche Telekom and certain competitors filed complaints against this order with the Cologne Administrative Court in March 1999. The proceedings in the main action are still pending. In March 2001, the Regulatory Authority reset the charge for the monthly rate at DM 24,40 plus VAT for a period ending in March 2003. Deutsche Telekom and certain competitors filed complaints against this decision with the Cologne Administrative Court in April 2001. The proceedings are still pending.

On November 15, 2000, the German telecommunications regulator ordered Deutsche Telekom to offer Internet service providers and other enterprises which demand Internet access, flat-rate access to its network by February 1, 2001. Additionally, the German telecommunications regulator ordered Deutsche Telekom in this context to stop providing quantity discounts and to eliminate different charges for peak/off-peak-connections. Deutsche Telekom filed a suit against this decision of the German telecommunications regulator and filed a motion for a temporary injunction, claiming that the decision of the German telecommunications regulator would not be in accordance with the relevant provisions of the Telecommunications Act. The motion for a temporary injunction against this order was rejected by the Cologne Administrative Court, but in March 2001 this decision was reversed by the Appellate Administrative Court in Münster concluding the injunction proceedings. The proceedings in the main action are still pending.

In October 2001, the German telecommunications regulator issued a decision on the charges for interconnection, replacing the distance-based tariff-structure with an element-based tariff-structure. Deutsche Telekom and certain competitors filed complaints and requests for injunction with the Cologne Administrative Court. The motions were rejected. Deutsche Telekom and the respective competitors have appealed the decision.

In March and May 2001, the German telecommunications regulator issued orders requiring Deutsche Telekom to offer certain services to Debitel AG for the purpose of reselling these services to end-users. Deutsche Telekom filed a complaint and a request for injunction with the Cologne Administrative Court. The request for injunction was rejected. The Appellate Administrative Court in Münster dismissed the appeal against this decision. The proceedings in the main action are still pending.

In March and May 2001, the German telecommunications regulator issued orders requiring Deutsche Telekom to offer shared access to end-customer lines (line-sharing). Deutsche Telekom filed a complaint and a request for injunction with the Cologne Administrative Court. The request for injunction was rejected. The Appellate Administrative Court in Muenster dismissed the appeal against this decision. The proceedings in the main action are still pending.

In October 2001, the German telecommunications regulator issued an order requiring Deutsche Telekom to apply for regulatory approval with respect to certain telecommunications services for closed user groups. Deutsche Telekom filed a complaint and a request for injunction with the Cologne Administrative Court. The court granted the requested injunction. The German telecommunications regulator has appealed the decision.

In August and September 2001, the German telecommunications regulator issued orders requiring Deutsche Telekom to offer certain services even without a regulatory approval of the respective tariffs. Deutsche Telekom filed a complaint and a request for injunction with the Cologne Administrative Court. The request for injunction was rejected. The Appellate Administrative Court in Muenster granted the requested injunction on appeal against this decision. The proceedings in the main action are still pending.

Proceedings before the European Commission

On March 17, 1999, Mannesmann Arcor filed a complaint with the European Commission against the Federal Republic and against Deutsche Telekom. The complaint primarily relates to Deutsche Telekom's prices for unbundled access to the local loop, which were set by the German telecommunications regulator in early 1999. Other competitors have jointly filed two further complaints to the European Commission containing similar reproaches. In addition, two other competitors have filed complaints alleging that Deutsche Telekom has abused a dominant position by charging long distance off-peak prices that are lower than applicable interconnection tariffs. Deutsche Telekom believes that the complaints are without merit and has submitted replies to the European Commission.

T-Online announced a plan to introduce new Internet charges as of April 1, 1999. AOL Bertelsmann filed a complaint concerning the new charges with the European Commission on February 15, 1999. The complaint alleges the abuse by Deutsche Telekom of its dominant position (in particular, the bundling of Deutsche Telekom's local telephone charges with T-Online's Internet access charges and the use by T-Online of Deutsche Telekom's billing systems). AOL Bertelsmann has also filed a complaint with the German telecommunications regulator based on essentially the same allegations.

On May 5, 1999, Mannesmann Mobilfunk filed a complaint with the European Commission alleging abuse by Deutsche Telekom of a dominant position on the fixed telephony retail market and on the market for termination services. According to the complaint, the alleged abuse consists of Deutsche Telekom's refusal to provide network services necessary for the implementation of Personal Communications Services similar to Deutsche Telekom's PCS. In addition, the price charged for this service is alleged to be abusive. Deutsche Telekom believes that the complaint is without merit and has submitted a reply to the European Commission.

Other Proceedings

In the first quarter of 2000, AOL Bertelsmann brought preliminary injunction proceedings and a respective main proceeding against T-Online and Deutsche Telekom before the Hamburg District Court (*Landgericht Hamburg*) claiming that T-Online had engaged in an anti-competitive practice by bundling its ''By-Call'' Internet access charge with Deutsche Telekom's ISDN telephone access. The Hamburg District Court decided in favor of Deutsche Telekom/T-Online in both proceedings. AOL Bertelsmann appealed to the Hamburg Court of Appeals.

On March 15, 2000, AOL Bertelsmann filed a complaint against T-Online with the German Federal Cartel Office (*Bundeskartellamt*) claiming that T-Online would engage in an anti-competitive practice by combining its ''T-Online by call'' tariff option with Deutsche Telekom ISDN access. In April 2001 the Federal Cartel Office dismissed the proceedings.

In early 1999, the U.S.-based operator Carrier 1 lodged a formal complaint with the U.S. Trade Representative against the Federal Republic alleging, among other things, that the German telecommunications regulator had failed to create a regulatory framework that guarantees competitors interconnection without unreasonable technical conditions on a timely basis and at cost-oriented prices. The complaint further alleges anti-competitive practices on the part of Deutsche Telekom (for example, delay in negotiating and implementing interconnection agreements). Deutsche Telekom believes the Carrier 1 complaint should be rejected on the merits. Two industry groups have also complained to U.S. authorities about interconnection in Germany.

In September 1998, Deutsche Post AG commenced an arbitration proceeding seeking contributions from Deutsche Telekom relating to the cost of employee housing for former Deutsche Bundespost employees, including a number of Deutsche Telekom employees. In 1995, responsibility for the housing of former employees of Deutsche Bundespost was assigned to Deutsche Post AG. The parties have different views as to the amount Deutsche Telekom is obliged to pay as cost reimbursement for the use of such employee housing for its employees. Deutsche Post AG currently is seeking payment in the amount of EUR 69.4 million from Deutsche Telekom, although Deutsche Telekom expects that Deutsche Post AG may claim further amounts in the event that its initial claim is successful. In March 2000, Deutsche Telekom raised counterclaims in the amount of EUR 62.6 million reclaiming down payments from 1995 and 1996. The outcome of the arbitration proceeding is uncertain.

In March 1999, a German consumer association filed a complaint with the Cologne Regional Court concerning telephone cards with limited validity sold by Deutsche Telekom since October 1998. The Regional Court upheld the complaint on October 27, 1999. The Cologne Higher Regional Court rejected Deutsche Telekom's appeal on August 23, 2000. Deutsche Telekom has lodged an appeal with the Federal Court of Justice (*Bundesgerichtshof*). The Federal Court rejected the appeal.

On or about April 20, 2001, the U.S. company World Access, Inc., which purports to own a substantial minority interest in the German long-distance telecommunications carrier Teldafax, reportedly filed a complaint in the U.S. District Court for the Northern District of Georgia asserting claims for alleged damages in excess of $600 million relating to, among other things, Deutsche Telekom's decision to cease providing interconnection services to Teldafax for nonpayment of invoices and alleged improper conversion by Deutsche Telekom of customers of Teldafax and World Access. Deutsche Telekom has restored interconnection services to Teldafax in accordance with a German preliminary injunction that also required Teldafax to make certain payments to a trust account and to Deutsche Telekom. Deutsche Telekom intends to oppose the complaint vigorously.

Media reports have suggested that radio frequency emissions from wireless handsets and cell sites may raise various health concerns, including cancer, and may interfere with various electronic medical devices, including hearing aids and pacemakers. Research and studies are ongoing. Whether or not such research or studies conclude there is a link between radio frequency emissions and health, these concerns over radio frequency emissions may discourage the use of wireless handsets and may result in significant restrictions on the location and operation of cell sites, either or both of which could have a material adverse effect on Deutsche Telekom or VoiceStream's results of operations. VoiceStream is subject to current, and potentially future, litigation relating to these health concerns. Several class action lawsuits have been filed against VoiceStream, several other wireless service operators and several wireless phone manufacturers, asserting products liability, breach of warranty and other claims relating to radio frequency transmissions to and from wireless handsets. The complaints seek substantial monetary damages as well as injunctive relief. The defense of these lawsuits may divert management's attention, and VoiceStream may be required to pay significant awards or settlement and may incur significant expenses in defending these lawsuits. In addition, VoiceStream could be subject to potential litigation, legislation or adverse publicity relating to damage caused by persons who use mobile telephones while driving.

In April 2001, QPSX Europe GmbH filed suit for a permanent injunction with the District Court in Munich (*Landgericht München*) against Deutsche Telekom and Siemens AG, alleging that these companies are infringing plaintiff's patent by providing services using Asynchronous Transfer Mode (ATM) technology. Since ATM technology is used in a number of products and services offered by Deutsche Telekom, an adverse outcome in this proceeding could have a substantial adverse effect on Deutsche Telekom's business.

VoiceStream and a joint venture in which VoiceStream holds an interest were both high bidders for certain U.S. mobile telecommunications licenses in FCC Auction No. 35. Those licenses had been repossessed and reauctioned by the FCC after the original purchaser of the licenses declared bankruptcy. The original purchaser of those licenses has challenged the FCC's repossession of the licenses in court, and a U.S. federal appellate court has ruled in favor of the original purchaser. The U.S. Supreme Court has agreed to hear the case during its 2002-2003 term.

In January 2002, the telecommunications carrier Global Crossing filed for bankruptcy protection. Previously, Deutsche Telekom had purchased from Global Crossing indefeasible rights to use certain network infrastructure in Western Europe that had a carrying value as of December 31, 2001, of less than EUR 300 million. Deutsche Telekom is assessing the situation, but at this stage can offer no assurance that its investment will be unaffected by Global Crossing's bankruptcy. If for any reason Deutsche Telekom became unable to avail itself of its indefeasible rights of use, Deutsche Telekom likely would need to incur costs to secure alternative capacity in the market.

Dividend Policy

The following table sets forth the annual dividends paid per share with respect to each of the financial years indicated:

Year Ended December 31,	Dividend Paid per Ordinary Share		
	DM	Euro	US$(1)
1998	1.20	—	0.64
1999	—	0.62	0.58
2000	—	0.62	0.53

(1) Dividend amounts have been translated into dollars at the Noon Buying Rate for the relevant dividend payment date, which occurred during the second quarter of the following year.

Shareholders determine the declaration, amount and timing of dividends based on the year-end unconsolidated stand-alone financial statements of Deutsche Telekom AG in respect of each fiscal year at their annual general meeting in the following year, upon the joint recommendation of the Management Board and the Supervisory Board. The annual general meeting is usually convened during the second quarter of each year.

Due to the completion of the Deutsche Telekom/VoiceStream merger and the Deutsche Telekom/Powertel merger in 2001, the Federal Republic and KfW no longer own a majority of Deutsche Telekom's voting share capital. However, because approval of dividend distributions requires only a majority of votes present at a shareholders' meeting, the Federal Republic and KfW may be able to determine the level of dividends even after their combined interests in Deutsche Telekom have fallen below 50 percent. Deutsche Telekom may declare and pay dividends only from distributable balance sheet profits (*Bilanzgewinn*) of Deutsche Telekom AG, as adjusted to reflect losses or gains carried over from prior years as well as transfers to or from retained earnings. Deutsche Telekom AG's retained earnings in its unconsolidated, stand-alone financial statements as of December 31, 2001 were EUR 8.1 billion. Certain reserves (*Rücklagen*) are required by law to be made and deducted in calculating distributable balance sheet profits available for distribution as dividends.

The payment of future dividends depends on Deutsche Telekom's earnings, its financial condition and other factors, including cash requirements, the future prospects of Deutsche Telekom and tax, regulatory and other legal considerations. Although Deutsche Telekom expects to pay annual dividends on its shares, you should not assume that any dividend will actually be paid or make any assumption about the amount that will be paid in any given year. To the extent necessary to implement Deutsche Telekom's dividend policy, Deutsche Telekom will consider drawing upon its retained earnings, as it has done with respect to the proposed dividend for 2001. Deutsche Telekom's ability to pay dividends is determined by reference to the unconsolidated financial statements of Deutsche Telekom AG, which are prepared in accordance with German GAAP. In financial year 2001, Deutsche Telekom's net loss on a consolidated German-GAAP basis was EUR 3.3 billion, while the net gain of Deutsche Telekom AG on an unconsolidated basis in accordance with German GAAP was EUR 6.6 billion. The difference was primarily caused by net loss from subsidiaries and associates as well as amortization and impairment of intangible assets (e.g. goodwill and trademarks), recognized in the consolidated balance sheet through consolidation.

The Management Board has recommended a dividend allocation in respect of 2001, which would be payable in 2002, of approximately EUR 1.6 billion, or EUR 0.37 per share (assuming approximately 4.2 billion shares outstanding). Dividends paid will be subject to German withholding tax. For further information on German withholding tax and related United States refund procedures, see "Item 10. Additional Information — Taxation."

Significant changes

Except as discussed elsewhere in this Annual Report, no significant change has occurred since the date of the annual financial statements included in this Annual Report.

ITEM 9. The Offer and Listing

Trading Markets

The principal trading market for Deutsche Telekom's shares is the Frankfurt Stock Exchange. The shares also trade on the other German stock exchanges in Berlin, Bremen, Düsseldorf, Hamburg, Hannover, Munich and Stuttgart and on the Tokyo Stock Exchange. Options on the shares trade on the German options exchange (*Eurex Deutschland*) and other exchanges. Originally, Deutsche Telekom issued all its shares in bearer form. With effect from January 24, 2001, the shares were converted from bearer form to registered form.

American Depositary Shares ("ADSs"), each representing one share, are listed on the New York Stock Exchange (NYSE) and trade under the symbol "DT". The depositary for the ADSs is Citibank N.A. For information on securities held in the United States see "— Trading on the New York Stock Exchange."

Trading on the Frankfurt Stock Exchange

Deutsche Börse AG operates the Frankfurt Stock Exchange, which is the most significant of the eight German stock exchanges. It accounts for the vast majority of the turnover in exchange-traded shares in Germany. As of December 31, 2001, the shares of 5,777 companies traded on the official, regulated and unregulated markets and the Neuer Markt Segment of the Frankfurt Stock Exchange. Of these, 912 were German companies and 4,865 were non-German companies.

Trading on the floor of the Frankfurt Stock Exchange begins every business day at 9:00 a.m. and ends at 8:00 p.m., Central European Time. Securities listed on the Frankfurt Stock Exchange generally trade in the auction market, but also change hands in interbank dealer markets both on and off the Frankfurt Stock Exchange. Publicly commissioned stock brokers who are members of the Frankfurt Stock Exchange, but who do not as a rule deal with the public, note prices, which are determined by out-cry. The prices of actively traded securities, including the shares of large corporations, are continuously quoted during trading hours.

Deutsche Telekom's shares are traded on Xetra (Exchange Electronic Trading) in addition to being traded on the auction market. Xetra is an electronic exchange trading platform operated by rules and regulations. Xetra is available daily between 9:00 a.m. and 8:00 p.m. to brokers and banks that have been admitted to Xetra by the Frankfurt Stock Exchange. Private investors can trade on Xetra through their banks or brokers.

Deutsche Börse publishes a daily list of quotations containing the Xetra prices for all traded securities. The list is available on the Internet at http://www.exchange.de under the heading "Market Data — Price Overview."

Transactions on the Frankfurt Stock Exchange (including transactions through the Xetra system) settle on the second business day following the trade. Transactions off the Frankfurt Stock Exchange (such as, for example, large trades or transactions in which one of the parties is foreign) generally also settle on the second business day following the trade, although a different period may be agreed to by the parties. Under standard terms and conditions for securities transactions employed by German banks, customers' orders for listed securities must be executed on a stock exchange unless the customer gives specific instructions to the contrary.

The Frankfurt Stock Exchange can suspend a quotation if orderly trading is temporarily endangered or if a suspension is deemed to be necessary to protect the public.

The trading supervisory offices (*Handelsüberwachungsstellen*) at the stock exchanges and the exchange supervisory authorities (*Börsenaufsichtsbehörden*) of the German federal states monitor trading activities on the German stock exchanges. The Federal Supervisory Authority for Securities Trading (*Bundesaufsichtsamt für den Wertpapierhandel*) (as of May 1, 2002, Federal Agency for Financial Services Supervision (*Bundesanstalt für Finanzdienstleistungsaufsicht*)) monitors compliance with the insider trading rules.

The table below sets forth, for the periods indicated, the high and low closing sales prices for the shares of Deutsche Telekom on the Frankfurt Stock Exchange, as reported by the Frankfurt Stock Exchange Xetra trading system, together with the highs and lows of the DAX (*Deutscher Aktienindex*).

	Price Per Ordinary Share		DAX(1)	
	High	Low	High	Low
	Euro(2)			
Yearly highs and lows				
1997	22.599	15.267	4,438.93	2,848.77
1998	28.617	15.947	6,171.43	3,896.08
1999	71.00	31.35	6,958.14	4,678.72
2000	103.50	31.48	8,064.97	6,200.71
2001	38.75	14.50	6,795.14	3,787.23
Quarterly highs and lows				
2000				
First Quarter	103.50	61.00	8,064.97	6,474.92
Second Quarter	80.40	55.80	7,555.92	6,834.88
Third Quarter	61.35	38.40	7,480.14	6,682.92
Fourth Quarter	45.11	31.48	7,136.30	6,200.71
2001				
First Quarter	38.75	24.15	6,795.14	5,388.02
Second Quarter	30.30	23.30	6,278.90	5,553.46
Third Quarter	27.56	14.50	6,109.50	3,787.23
Fourth Quarter	20.50	16.50	5,271.29	4,239.97
2002				
First Quarter	20.16	15.00	5,462.55	4,745.58
Monthly highs and lows				
2001				
July	27.56	23.92	6,109.50	5,582.76
August	24.36	16.29	5,835,25	5,162.40
September	17.20	14.50	5,208.10	3,787.23
October	19.25	16.50	4,820.26	4,239.97
November	20.45	16.87	5,185.10	4,583.31
December	20.50	18.68	5,271.29	4,239.97
2002				
January	20.16	16.68	5,318.73	4,984.20
February	16.65	15.00	5,097.06	4,745.58
March	17.71	16.60	5,462.55	5,097.41
April (through April 15, 2002)	16.86	15.79	5,311.08	5,162.96

(1) The DAX is a weighted performance index of the shares of thirty large German corporations. The calculation of the DAX did not change upon the introduction of the Euro. The composition of the DAX and the weighting of different corporations in the DAX has changed in the period covered by this table and may change in the future. For further information in this regard, see "Item 3. Key Information — Risk Factors."

(2) Effective January 1, 1999, Germany and ten other member states of the European Union adopted the Euro as their common currency. From January 4, 1999, all shares on German stock exchanges have traded in Euros. For consistency of presentation, Deutsche Telekom has translated amounts in Deutsche Marks for prior periods into Euros at the official fixed conversion rate of EUR 1.00 = DM 1.95583. The translation of all Deutsche Mark amounts into Euros at the official fixed conversion rate does not affect the trends discussed above. However, the amounts appearing above for dates or periods prior to January 4, 1999 will not be comparable to share prices for other companies to the extent that those prices were denominated in a currency other than the Deutsche Mark.

On April 15, 2002, the closing sales price per ordinary share on the Frankfurt Stock Exchange was EUR 16.21, which was equivalent to US$14.27 per share, translated into U.S. dollars using the noon buying rate in New York City for cable transfers in Euros as certified for customs purposes by the Federal Reserve

Bank of New York for April 15, 2002. On April 15, 2002, the noon buying rate was 0.8802 U.S. dollar per Euro.

Trading on the New York Stock Exchange

American Depositary Shares (ADSs), each representing one Deutsche Telekom ordinary share, are listed on the New York Stock Exchange and trade under the symbol "DT". The depositary for the ADSs is Citibank N.A.

The table below sets forth, for the periods indicated, the high and low closing sales prices for the Deutsche Telekom ADSs on the NYSE:

	Price per ADS	
	High	**Low**
	US$	
Yearly highs and lows		
1997	$24\frac{7}{8}$	$16\frac{3}{8}$
1998	$33\frac{1}{2}$	$17\frac{1}{16}$
1999	71	$36\frac{1}{16}$
2000	$98\frac{5}{8}$	$29\frac{1}{4}$
2001	36.5625	13.39
Quarterly highs and lows		
2000		
First Quarter	$98\frac{5}{8}$	$63\frac{1}{16}$
Second Quarter	$76\frac{1}{4}$	$49\frac{3}{16}$
Third Quarter	$58\frac{115}{256}$	$33\frac{29}{64}$
Fourth Quarter	$38\frac{3}{16}$	$29\frac{1}{4}$
2001		
First Quarter	36.5625	22.11
Second Quarter	26.76	19.5
Third Quarter	23.12	13.39
Fourth Quarter	18.14	15.08
2002		
First Quarter	18.01	13.15
Monthly highs and lows		
2001		
July	23.12	21.26
August	21.62	15.24
September	15.62	13.39
October	17.02	15.08
November	18.08	15.15
December	18.14	16.55
2002		
January	18.01	14.25
February	14.18	13.15
March	16.65	14.44
April (through April 15, 2002)	15.14	13.91

On April 15, 2002, the closing sales price per ADS on the NYSE was US$14.20.

Based on the share register, as of April 15, 2002, Deutsche Telekom AG had approximately 2,854,250 registered holders of Deutsche Telekom ordinary shares, including 3,130 holders of record of Deutsche Telekom ordinary shares with addresses in the U.S.

As of April 15, 2002, there were 192,747,388 Deutsche Telekom ADSs outstanding, with 1,545 holders of record of Deutsche Telekom ADSs with addresses in the United States and 61 holders of record of ADSs with addresses outside the United States.

ITEM 10. Additional Information

Articles of Association

This section provides information about Deutsche Telekom's Articles of Association and about German law as these relate to the rights of holders of the shares of Deutsche Telekom. Set forth below is a summary of certain information relating to Deutsche Telekom's share capital and of certain provisions of Deutsche Telekom's Articles of Association and German law. This summary is not complete and is qualified by reference to Deutsche Telekom's Articles of Association and German law as in effect at the date of this filing. Copies of the Articles of Association are publicly available at the Commercial Register in Bonn, and an English translation has been filed as an exhibit to this Annual Report on Form 20-F.

Organization and Register

Deutsche Telekom AG is a stock corporation organized in the Federal Republic of Germany under the German Stock Corporation Act (*Aktiengesetz*). Deutsche Telekom AG is registered in the Commercial Register (*Handelsregister*) maintained by the local court in Bonn, Germany, under the entry number "HRB 6794".

Purpose and Object of Deutsche Telekom

According to the Articles of Association, the object of the Company is activity in all areas of telecommunications and in related areas in Germany and abroad. The Company is entitled to enter into all other transactions and take all other measures deemed appropriate to serve the object of the enterprise. It may also set up, acquire and participate in other undertakings of the same or similar kind in Germany and abroad, as well as run such undertakings or confine itself to the administration of its participations. It may spin off its operations wholly or partly to affiliated undertakings.

Information relating to Supervisory Board and Management Board Members

A Supervisory Board member may not receive a loan from Deutsche Telekom AG unless approved by the Supervisory Board. A Management Board member may only receive a loan from Deutsche Telekom AG upon prior approval by the Supervisory Board. For further information with respect to the Supervisory Board and the Management Board, see also "Item 6. Directors, Senior Management and Employees."

Class of Stock

The capital stock of Deutsche Telekom consists of ordinary shares in registered form with no par value (*Stückaktien*). The individual shares do not have a par value as such, but they do have a notional par value that can be determined by dividing the share capital amount by the number of shares.

Voting Rights and Shareholders' Meetings

Each share entitles its holder to one vote at Deutsche Telekom's general meeting of the shareholders. Shareholders may pass resolutions at a general meeting by a majority of the votes cast, unless a higher vote is required by law or by Deutsche Telekom's Articles of Association. Neither the German Stock Corporation Act nor the Articles of Association provide for minimum quorum requirements for shareholders' meetings. The German Stock Corporation Act and the Articles of Association require that significant resolutions be passed by a majority of the votes cast and with at least three-quarters of the share capital represented at a meeting.

These significant resolutions include:

- capital increases which provide for an exclusion of preemptive rights;
- capital decreases;
- the creation of authorized capital (*genehmigtes Kapital*) or conditional capital (*bedingtes Kapital*);
- dissolution of Deutsche Telekom;
- merger of Deutsche Telekom into or consolidation of Deutsche Telekom with another corporation;
- split-off or spin-off; transfer of all Deutsche Telekom's assets;

- conclusion of intercompany agreements (*Unternehmensverträge*), including, in particular, control and profit and transfer agreements (*Beherrschungs- und Gewinnabführungsverträge*);
- amendments to the corporate purpose of Deutsche Telekom; and
- a change in Deutsche Telekom's corporate form.

A general meeting of the shareholders of Deutsche Telekom may be called by the Management Board or by shareholders holding in the aggregate at least 5 percent of Deutsche Telekom's issued share capital. If required in the interest of Deutsche Telekom, the Supervisory Board must call a shareholders' meeting. The annual general meeting must take place within the first eight months of the fiscal year and is called by the Management Board upon the receipt of the Supervisory Board's report on the annual financial statements. Under the Articles of Association, the right to participate in and to vote at a shareholders' meeting will only be given to those shareholders who have timely registered for the shareholders' meeting in writing or by fax with the Management Board at the seat of the company and who are included in the share register when their registration for the shareholders' meeting is received. There must be at least six days between receipt of the registration and the date of the shareholders' meeting, unless the Management Board shorten the time period. Following receipt of a shareholder's registration, Deutsche Telekom will not enter a transfer of the related shares in the share register until after the conclusion of the general shareholders' meeting. Deutsche Telekom must publish notice of shareholders' meetings in the Federal Gazette (*Bundesanzeiger*) at least one month prior to the date by which shareholders have to register for the shareholders' meeting. The day of publication and the last date by which shareholders have to register for the shareholders' meeting are not counted for this purpose. In addition, Deutsche Telekom must publish a notice in a national authorized stock exchange journal.

Holders of shares (but not holders of ADSs) are required to provide to Deutsche Telekom their names, addresses and birthdates (or, in the case of business entities, their names, business addresses and registered seats) as well as the number of shares held, so that they can be entered into the share register maintained by Deutsche Telekom. ADEUS Aktienregister-Service-GmbH (a joint venture of Dresdner Bank AG, Allianz AG, Münchner Rückversicherungs-Gesellschaft AG in München and CSC Ploenzke AG) is the transfer agent and registrar of the registered shares in Germany.

Dividends And Other Distributions

Deutsche Telekom may pay dividends immediately following the resolution by the general meeting of shareholders on the distribution of profits. Shareholders participate in profit distributions in proportion to the notional value of their shares.

Under German law, Deutsche Telekom may declare and pay dividends only from balance sheet profits as shown in the unconsolidated annual financial statements of Deutsche Telekom. In determining the distributable balance sheet profits, the Deutsche Telekom Management Board and the Deutsche Telekom Supervisory Board may allocate to profit reserves (*andere Gewinnrücklagen*), either in whole or in part, the annual surplus (*Jahresüberschuss*) that remains after allocation to statutory reserves and losses carried forward. Under the Deutsche Telekom Articles of Association, transferring more than one-half of the annual surplus to profit reserves is not permissible if, following the transfer, the accumulated reserves out of surplus would exceed one-half of Deutsche Telekom's share capital. The shareholders, in determining the distribution of profits, may allocate additional amounts to profit reserves and may carry forward profits in part or in full.

Dividends approved at a shareholders' meeting are payable on the first stock exchange trading day after that meeting, unless otherwise decided at the shareholders' meeting. Details regarding paying agents are published in the Federal Gazette (*Bundesanzeiger*). Shareholders holding ordinary shares through Clearstream Banking AG will receive dividends by credit to their respective accounts.

Record Dates

In accordance with the German Stock Corporation Act, the record date for determining which holders of Deutsche Telekom ordinary shares are entitled to the payment of dividends or other distributions, whether in cash, stock or property, will be the date of the general meeting of shareholders at which such dividends or other distributions are declared. The record date for determining which holders of Deutsche Telekom ordinary shares are entitled to vote at a general meeting will be the date of such general meeting, provided that holders of Deutsche Telekom ordinary shares who are registered in the share register (*Aktienbuch*) on the date of the meeting will be entitled to attend and vote at the meeting only if such holders have given Deutsche Telekom notice of their desire to attend early enough that there are at least six days between the day the notice is given and the day of the shareholders' meeting, unless the Management Board shortens the time period.

Requirement to Disclose Shareholdings

The German Securities Trading Act (*Wertpapierhandelsgesetz*) requires each person whose shareholding reaches, exceeds or, after exceeding, falls below the 5%, 10%, 25%, 50% or 75% voting rights thresholds of a listed company to notify the company and the Federal Supervisory Authority for Securities Trading in writing within seven calendar days after they have reached, exceeded or fallen below such a threshold. In their notification, they must among other things state the number of votes they have and the relative voting power which the number of shares they hold represent. Such holders cannot exercise any rights, including voting rights and the rights to receive dividends from those shares, until they have satisfied this disclosure requirement. Failure to notify may also trigger a penalty provided for by law. In addition, the German Securities Trading Act contains various rules designed to ensure the attribution of shares to the person who has effective control over the exercise of the voting rights attached to those shares.

Repurchase of Shares

Under the German Stock Corporation Act, Deutsche Telekom may not purchase its own shares, subject to certain limited exceptions.

The general shareholders' meeting on May 29, 2001 approved a resolution that authorizes Deutsche Telekom pursuant to Section 71(1) no. 8 of the German Stock Corporation Act to purchase its own shares in an amount representing up to ten percent of its registered share capital of EUR 7.76 billion through November 19, 2002. The purchase price for the shares (excluding purchasing costs) must not exceed or fall below the market price by more than five percent, in the case of a purchase on the stock exchange, or twenty percent, in the case of an offer to purchase made to all shareholders. The relevant market price for this purpose would be the opening auction price in the Xetra system of the Frankfurt Stock Exchange on the day of the purchase, in the case of a purchase on the stock exchange, or the closing price in the Xetra system on the day prior to the publication of the offer, in the case of an offer to purchase made to all shareholders.

Pursuant to the resolution, Deutsche Telekom's Management Board is authorized, with the approval of the Supervisory Board, to:

(1) list the acquired shares on foreign stock exchanges on which they are not listed;

(2) offer the acquired shares to third parties in the context of mergers with and acquisitions of other companies and acquisitions of interests in other companies; and

(3) to cancel the acquired shares without further shareholder approval. This cancellation option can be exercised in whole or in part.

Shareholders' preemptive rights are excluded for the purposes listed in clauses (1) and (2) above. The price for any sale on a stock exchange or use in a merger or acquisition transaction would not be permitted to fall more than five percent below the opening auction price of Deutsche Telekom's shares in the Xetra system of the Frankfurt Stock Exchange on the day of the sale on the stock exchange or the definitive agreement with a third party, as applicable.

Preemptive Rights

Under the German Stock Corporation Act, every shareholder generally has preemptive rights with respect to an issuance of new shares (including securities convertible into shares, securities with warrants to purchase shares, profit-sharing certificates and securities with a profit participation). Preemptive rights are freely transferable and may be traded on the German stock exchanges for a limited number of days prior to the final date for the exercise of the rights. Shareholders may exclude preemptive rights through a resolution passed by a majority of votes cast and a majority of at least three quarters of the share capital represented in the shareholders' meeting. In addition, an exclusion of preemptive rights requires a report by the Management Board, which must justify the exclusion by establishing that Deutsche Telekom's interest in the exclusion outweighs the shareholders' interest in exercising their preemptive rights. Preemptive rights related to the issuance of new shares may be excluded without justification if:

- Deutsche Telekom increases share capital for cash contributions; and
- the amount of the increase does not exceed 10 percent of the issued share capital; and
- the shares are sold at a price not substantially lower than the current quoted share price.

Rights upon Liquidation

In accordance with the German Stock Corporation Act, upon a liquidation of Deutsche Telekom, shareholders will receive, in proportion to the ordinary shares held, any liquidation proceeds remaining after paying off all of Deutsche Telekom's liabilities.

Material Contracts

VoiceStream Acquisition

On July 24, 2000 Deutsche Telekom entered into a contract with VoiceStream Wireless Corporation that provided for VoiceStream to merge with and into a wholly-owned subsidiary of Deutsche Telekom AG. In connection with this merger, which closed in May 31, 2001 former VoiceStream shareholders received EUR 4.9 billion in cash and newly issued Deutsche Telekom shares having a market value on that date of approximately EUR 28.7 billion.

Exchange Controls

At present, German law does not restrict the movement of capital between Germany and other countries or individuals, except with respect to investments in Iraq and with certain persons in other countries such as Serbia and Afghanistan. Germany imposed these restrictions in order to comply with applicable United Nations and European Union resolutions.

For statistical purposes corporations or individuals residing in Germany are required to report to the German Central Bank (*Deutsche Bundesbank*) any payment received from, or made to or for the account of, a non-resident corporation or individual that exceeds € 12,500 (or the equivalent in a foreign currency).

At the end of every month, corporations or individuals residing in Germany, except financial institutions, must also report to the German Central Bank any claims against or liabilities payable to a non-resident corporation or individual that in the aggregate exceed € 1.5 million (or the equivalent in foreign currency).

Taxation

The following is a summary of material U.S. federal income tax and German tax considerations relating to the ownership and disposition of ADSs or Ordinary shares in Deutsche Telekom AG (the "Company") by a U.S. holder. In general, a "U.S. Holder" is any beneficial owner of ADSs or Ordinary shares (1) who is resident of the United States for the Purposes of the Income Tax Treaty between the United States and Germany (the "Treaty"), (2) who is not also a resident of the Federal Republic of Germany for the purposes of the Treaty, (3) who owns the ADSs or Ordinary Shares as capital assets, (4) who does not hold shares or ADSs as part of a permanent establishment or a fixed base used for the performance of independent personal services in Germany, and (5) who is entitled to benefits under the Treaty with respect to income and gain derived in connection with the ADSs or Ordinary Shares.

The summary does not purport to be a comprehensive description of all tax considerations that may be relevant to the ownership of ADSs or Ordinary Shares, and, in particular, it does not address U.S. federal taxes other than income tax and German taxes other than income tax, gift and inheritance taxes. Moreover, the discussion does not consider the tax treatment of shareholders that are subject to special rules, such as fiduciaries of pension, profit-sharing or other employee benefit plans, banks, insurance companies, dealers in securities or currencies, persons that hold the ADSs or Ordinary shares in a hedging transaction or other integrated transaction, persons that own, directly or indirectly, 10 percent or more of our voting stock and persons whose functional currency is not the U.S. dollar.

Investors are strongly urged to consult their own tax advisers regarding the United States Federal Income and German tax consequences of the purchase, ownership and disposition of ADSs or Ordinary Shares in light of their particular circumstances, including the effect of any state, local, or other national laws.

Taxation of the Company

On January 1, 2001, the German Tax Reduction Act repealed the corporate imputation tax system with a classic corporate income tax system. The prior German tax rules continued to apply to dividends paid by Deutsche Telekom AG on or before December 31, 2001, provided that the underlying earnings were generated by the end of the calendar year 2000. The change in the system is facilitated by a number of transitional rules.

Under the new legislation, the Company's income is generally subject to German corporate income tax at a flat rate of 25 percent, regardless of whether such income is distributed or not. A solidarity surcharge of 5.5 percent is imposed on the corporate income tax liability, resulting in an aggregate effective German corporate income tax charge of 26.375 percent (i.e., not including German local trade tax). Generally, dividends and capital gains from the sale of shares received by Deutsche Telekom are tax-free beginning in 2002. However, this applies for trade tax purposes only if Deutsche Telekom has at least a 10% holding in the share capital of the entity.

In addition, a German resident company is also subject to profit-related trade tax, which is levied on the Company's trade income. The effective rate of the trade tax depends on the rate set out by each municipality where the company is resident. It generally ranges from 15 percent to 21 percent. In computing the corporate income tax of a corporation, the trade tax on income is deductible as a business expense.

Generally, losses can be accumulated for corporate income tax as well as for trade tax purposes. To the extent losses cannot be offset against taxable income, the remaining portion can be carried forward without time limit. For corporate income tax there is an optional carryback to the previous year of up to € 511,500.

German Taxation of Dividends

Under German law, the full amount of a dividend distributed by the Company from January 2002 onwards is generally subject to German withholding tax at the domestic rate of 20 percent (plus a solidarity surcharge of 5.5 percent, effectively 1.1 percent of the dividend before taxes, resulting in an aggregate rate of withholding of 21.1 percent). This withholding tax rate may be reduced under the Treaty to 15% of the gross amount of the dividend. The reduction can be obtained by U.S. Holders by way of a partial refund from the German tax authorities in the amount of 6.1% of the gross dividend equalling the difference between the amount withheld at the German domestic dividend withholding rate (plus solidarity surcharge) and the amount computed under the applicable treaty rate. (21.1% aggregate German withholding tax minus 15% Treaty withholding tax rate)

As a result of the changes in the German tax treatment of dividend income received by a German domestic taxpayer, and which also affect the benefits available for U.S. Holders under the treaty, the previously granted further reduction of the German withholding tax rate to 10 percent will no longer be available for U.S. Holders.

At the level of a German resident shareholder, the so-called half-income system (*Halbeinkünfteverfahren*) replaced the imputation system (*Anrechnungsverfahren*). Accordingly, for dividends paid in 2002, only half of the income distributed is taxable for individual taxpayers resident in Germany (this is also valid for foreign investors that hold shares or ADSs as part of a permanent establishment or fixed place of business in Germany). Likewise, only half of the expenses related to the taxable dividend income is deductible for personal income tax purposes. It is important to note that, nevertheless, the withholding tax is withheld from the full amount of dividends.

German Taxation of Capital Gains

Under the Treaty, a U.S. Holder will not be liable for German tax on capital gains realized or accrued on the sale or other disposition of shares or ADSs provided that the shares or ADSs subject to such transfer are not held as part of a permanent establishment or a fixed base in Germany.

German Inheritance and Gift Tax

Under the United States-Germany estate tax treaty a transfer of shares or ADSs by gift or at death is generally not subject to German inheritance or gift tax, if the donor or the transferor is domiciled in the United States. However, this does not apply if the heir, donee or other beneficiary is domiciled in Germany. In this case, the transferred shares or ADSs are subject to German inheritance or gift tax. However, the amount of federal estate tax paid in the United States with respect to the transferred shares or ADSs will be credited against the German inheritance or gift tax liability pursuant to the United States-Germany estate tax treaty.

Other German Taxes

No German transfer, stamp or other similar taxes apply to the purchase, sale or other disposition of shares or ADSs by a U.S. Holder.

German Taxation of Bonus Shares

According to a notice of the Federal Ministry of Finance dated December 10, 1999, the bonus shares which have been credited to the investor's depositary account in January 2002 with respect to shares purchased in the third public offering in 2000 will be taxed as taxable dividend income to the shareholders although no withholding tax is to be retained. A U.S. Holder must file a tax return and report this income to the German tax authorities.

In the case of a German Nonresident Holder's sale or other disposition of the bonus shares or ADSs representing such bonus shares, the rules described above under the heading ''Capital Gains'' apply.

United States Federal Income Taxation

In general, for U.S. federal income tax purposes and for purposes of the Treaty, beneficial owners of ADSs will be treated as the beneficial owners of the shares represented by those ADSs.

Taxation of Dividends

2002 dividends are subject to German withholding tax at an aggregate rate of 21.1 percent (consisting of a 20 percent withholding tax and a 1.1 percent solidarity surcharge).

Under the Treaty, a U.S. holder will be entitled to claim a refund to the extent the amount withheld exceeds the 15 percent rate provided under the Treaty, but will not be entitled to the additional payment associated with 2001 dividends. Accordingly, a U.S. holder who complies with procedures for claiming Treaty benefits will receive total cash payments of 85 in respect of a dividend of 100, and will incur a net German withholding tax cost of 15. For U.S. tax purposes, the U.S. holder will be deemed to have received dividend income of 100.

The gross amount of dividends that a U.S. holder receives (prior to the deduction of German withholding tax), generally will be subject to U.S. federal income taxation as foreign source dividend income, and will not be eligible for the dividends received deduction generally allowed to U.S. corporations. German withholding tax at the 15 percent rate provided under the Treaty will be treated as a foreign income tax that, subject to generally applicable limitations under U.S. tax law, is eligible for credit against a U.S. holder's U.S. federal income tax liability or, at the holder's election, may be deducted in computing taxable income. A U.S. holder will not be able to claim credits for German taxes that would have been refunded if the holder had filed a claim for a refund. For foreign tax credit purposes, dividends paid by Deutsche Telekom AG will be foreign source ''passive income'' or, in the case of certain U.S. holders, ''financial services income''. Foreign tax credits will not be allowed for withholding taxes imposed in respect of certain short-term or hedged positions in securities or in respect of arrangements in which a U.S. holder's expected economic profit, after non-U.S. taxes, is insubstantial. U.S. holders should consult their own advisers concerning the implications of these rules in light of their particular circumstances.

Dividends will be paid in Euros and will be included in the income of a U.S. holder in a U.S. dollar amount calculated by reference to the exchange rate in effect on the date of receipt by the holder or, in the case of ADSs, by the Depositary, regardless of whether the payment is in fact converted into U.S. dollars. If such a dividend is converted into U.S. dollars on the date of receipt, a U.S. holder generally should not be required to recognize foreign currency gain or loss in respect of the dividend income. A U.S. holder may be required to recognize foreign currency gain or loss on the receipt of a refund in respect of German withholding tax to the extent the U.S. dollar value of the refund differs from the U.S. dollar equivalent of that amount on the date of receipt of the underlying dividend.

Bonus Shares

Certain holders who acquired shares or ADSs at the time they were offered in the third public offering in 2000 have been entitled to receive bonus shares if they continued to hold their shares or ADSs up to a specified date. The receipt of bonus shares will be treated differently for U.S. and German tax purposes. From a U.S. tax perspective, the receipt of bonus shares should be treated as a purchase price adjustment. Accordingly, a U.S. holder would not include any amount in income upon the receipt of bonus shares, and instead should reallocate its tax basis between its prior shareholding and the bonus shares.

From a German tax perspective, the receipt of bonus shares will be treated as a taxable dividend. Although the delivery of bonus shares will not be subject to German withholding tax, a recipient who is a U.S. holder would in principle still be liable for German tax at the 15 percent rate applicable to dividend income under the Treaty. For purposes of the U.S. foreign tax credit limitation, it is possible that any German taxes paid with respect to bonus shares may be allocated to general limitation income. In that event, a U.S. holder that does not receive sufficient foreign-source general limitation income from other sources may not be able to derive effective foreign tax credit benefits in respect of those German taxes.

Refund Procedures

Pursuant to administrative procedures introduced on a trial basis (and which therefore could be amended or revoked at any time), a simplified refund procedure currently is available to certain U.S. holders of ADSs that are held through brokers participating in the Depository Trust Company (“DTC”). Under these procedures, the DTC provides the German tax authorities with electronic certification of the U.S. taxpayer status of such U.S. Holders based on information it receives from its broker participants, and claims a refund on behalf of those U.S. Holders. This combined claim need not include evidence of a U.S. holder’s entitlement to Treaty benefits. The German tax authorities will issue refunds to DTC, which in turn will issue corresponding refund checks to the participating brokers. Under audit procedures that apply for up to 4 years, the German tax authorities may require brokers to provide evidence regarding the entitlement of their clients to Treaty benefits. In the event of such an audit, brokers must submit to the German tax authorities a list containing names and addresses of the relevant holders of ADSs, and official certifications on IRS Form 6166 of the last filed United States federal income tax return of such holders (discussed below). Brokers participating in the DTC arrangements may require that holders provide documentation establishing their eligibility for Treaty benefits.

Claims for Treaty refunds by U.S. holders of ADSs who do not participate in the DTC procedures discussed above may be submitted to German tax authorities by the Depositary on behalf of those holders. Holders who are entitled to refunds in excess of € 153,39 for the calendar year normally must file their refund claim on an individual basis; however, the Depositary may be in a position to make a refund claim on behalf of such holders. Details of the refund procedures for holders of ADSs can be obtained from the Depositary.

If a U.S. holder does not submit a claim for a Treaty refund pursuant to the collective refund procedures described above, then it must submit a claim for refund on an individual basis on a special German form which must be filed with the German tax authorities at the following address: Bundesamt für Finanzen, Friedhofstrasse 1, 53221 Bonn, Germany. Copies of the required form may be obtained from the German tax authorities at that address, from the Embassy of the Federal Republic of Germany, 4645 Reservoir Road, N.W., Washington, D.C. 20007-1998 or from the Office of International Operations, Internal Revenue Service, 1325 K Street, N.W., Washington, D.C. 20225, Attention: Taxpayer Service Division, Room 900.

As part of the individual refund claim, a U.S. holder must submit to the German tax authorities the original bank voucher (or certified copy thereof) issued by the paying entity documenting the tax withheld, and an official certification on IRS Form 6166 of its last filed U.S. federal income tax return. IRS Form 6166 may be obtained by filing a request with the Internal Revenue Service Center in Philadelphia, Pennsylvania, Foreign Certificate Request, P.O. Box 16347, Philadelphia, PA 19114-0447. (Additional information, including IRS Publication 686, can be obtained from the Internal Revenue Service website at *www.irs.gov*). Requests for certification must be in writing and must include the U.S. holder’s name, Social Security number or employer identification number and tax return form number, and tax period for which the certification is requested. Requests for certification can include a request to the Internal Revenue Service to send the certification directly to the German tax authorities. If no such request is made, the Internal Revenue Service will send a certificate on IRS Form 6166 to the U.S. holder, which then must submit the certification with its claim for refund. A certification is valid for three years and need only be resubmitted in a fourth year in the event of a subsequent application for refund.

All claims for refund must be filed within four years of the end of the calendar year in which the dividend was received.

Refunds under the Treaty are not available in respect of shares or ADSs held in connection with a permanent establishment or fixed base in Germany.

Capital Gains

Under the Treaty, a U.S. holder will not be subject to German income tax on capital gains in respect of a sale or other disposition of shares or ADSs, so long as the shares or ADSs were not held as part of a permanent establishment or fixed base in Germany.

For U.S. federal income tax purposes, gain or loss realized by a U.S. holder on the sale or disposition of shares or ADSs will be capital gain or loss, and will be long-term capital gain or loss if the shares or ADSs were held for more than one year. The net amount of long-term capital gain recognized by an individual holder generally is subject to taxation at a maximum rate of 20 percent. A U.S. holder's ability to offset capital losses against income is subject to limitations. Deposits and withdrawals of shares in exchange for ADSs will not result in the recognition of gain or loss for U.S. federal income tax purposes.

Inheritance and Gift Tax

Under the estate, inheritance and gift tax treaty between the United States and Germany (''the Estate Tax Treaty''), a transfer of shares or ADSs generally will not be subject to German gift or inheritance tax so long as neither the donor or decedent, nor heir, donee or other beneficiary, was domiciled in Germany for purposes of the Estate Tax Treaty at the time of the transfer, and the shares or ADSs were not held as part of a permanent establishment or fixed base in Germany.

The Estate Tax Treaty provides a credit against U.S. federal gift and estate tax liability for the German inheritance and gift tax paid subject to certain limitations.

Information Reporting and Backup Withholding

Dividends on shares or ADSs, and payments of the proceeds of a sale of shares or ADSs, paid within the United States or through certain U.S.-related financial intermediaries are subject to information reporting and may be subject to backup withholding at a 30 percent rate (for calendar years 2002 and 2003) unless the U.S. Holder (1) is a corporation or other exempt recipient or (2) provides a taxpayer identification number and certifies that no loss of exemption from backup withholding has occurred.

Documents on Display

Deutsche Telekom is subject to the informational requirements of the Securities Exchange Act of 1934, as amended. In accordance with these requirements, Deutsche Telekom files Annual Reports on Form 20-F and furnishes periodic reports on Form 6-K with the Securities and Exchange Commission. These materials, including this annual report and the exhibits thereto, may be inspected and copied at the Commission's Public Reference Room at 450 Fifth Street, N.W., Washington, D.C. 20549 and at the Commission's regional offices at 500 West Madison Street, Suite 1400, Chicago, Illinois 60661-2511, and 233 Broadway, New York, New York 10274. Copies of the materials may be obtained from the Public Reference Room of the Commission at 450 Fifth Street, N.W. Washington, D.C. 20549 at prescribed rates. The public may obtain information on the operation of the Commission's Public Reference Room by calling the Commission in the United States at 1-800-SEC-0330. The Commission also maintains a web site at http://www.sec.gov that contains reports and proxy information regarding registrants that file electronically with the Commission. In addition, material filed by Deutsche Telekom can be inspected at the offices of the New York Stock Exchange at 20 Broad Street, New York, New York 10005.

ITEM 11. Quantitative and Qualitative Disclosures About Market Risk

The following discussion should be read in conjunction with "Summary of Accounting Principles" in the notes to the consolidated financial statements and in conjunction with note 34 to the consolidated financial statements, which provides a summarized comparison of the nominal amounts, book values and market values of derivative and non-derivative financial instruments and other information relating to those instruments.

Risk Identification and Analysis

The activities of the Deutsche Telekom Central Treasury are subject to policies approved by the Management Board and are monitored by the Supervisory Board. The Central Treasury's policies address the use of derivative financial instruments, including the approval of counterparties, and the investment of excess liquidity. These policies are intended to minimize financial risks and to generate financial advantages for the entire group such as central management of cash resources and needs, cost reduction and the improvement of results from financial transactions. The Management Board is regularly informed by the Central Treasury of the level and value of current market risk exposures. Certain transactions require prior approval by the Management Board. Deutsche Telekom regards effective market risk management as an important element of its treasury function. Simulations are carried out using market and worst case scenarios in order to evaluate the effects of different market situations on the financial position of Deutsche Telekom. The Central Treasury, operating as a service center, supplies financial services to individual Deutsche Telekom group entities appropriate to their requirements and local circumstances.

As with any risk management system, the results are based on individual assessments that may be subject to error. There is no guarantee that this system will consistently identify all of the important risks or provide an adequate assessment of their impact.

Deutsche Telekom is exposed to market risks primarily from changes in foreign exchange rates, interest rates and share prices associated with assets, liabilities or anticipated transactions which may affect its operating results and financial condition. Deutsche Telekom seeks to minimize market risk through its regular operating and financing activities and, following the evaluation of the exposures, selectively enters into derivative or nonderivative hedging instruments. Hedging instruments are entered into as a rule with major financial institutions with at least a single A credit rating, thereby minimizing the risk of credit loss. Furthermore, for certain derivative instruments Deutsche Telekom provides and receives cash collaterals. Deutsche Telekom does not enter into derivative financial instruments for trading purposes or other speculative purposes.

The following discussion and tables, which constitute forward-looking statements that involve risk and uncertainties, summarize Deutsche Telekom's market-sensitive financial instruments and include fair values, maturity and contract terms.

Foreign Exchange Rate Risk

Currency risks arise from Deutsche Telekom's investing, financing and operating activities. Since Deutsche Telekom's corporate objective is pursued through its commercial operations — meaning the sale of telecommunications services — unwanted foreign currency exposures are normally hedged, provided the risks would affect Deutsche Telekom's cash flows. Therefore, foreign currency risks that do not affect Deutsche Telekom's cash flows (such as risks resulting from the translation of Deutsche Telekom's foreign entities assets and liabilities into Deutsche Telekom's reporting currency) generally remain unhedged. However, in specific circumstances, Deutsche Telekom seeks to hedge the foreign currency translation risk inherent in certain foreign entities.

For purposes of managing foreign currency risks, a distinction is made in principle between investing, financing and operating activities:

Foreign currency transaction risks in the investment area arise from the acquisition and sale of investments in foreign entities. The Central Treasury hedges these exposures to the extent approved by the Management Board. In addition, the increase, reduction and termination of foreign currency derivative and non-derivative hedging instruments related to existing net investments in foreign entities require approval by the Management Board. At December 31, 2001, hedging instruments used in the investment area consisted primarily of USD forward sales contracts to hedge Deutsche Telekom's investment in shares of preferred stock in VoiceStream and of certain cross-currency interest rate swaps to hedge a portion of Deutsche Telekom's net investment in One 2 One. The translation risk inherent in Deutsche Telekom's remaining net investments in VoiceStream and One 2 One and in its investments in other foreign entities was unhedged at

December 31, 2001. Effects from currency fluctuations on the translation of the net investments are reflected in Deutsche Telekom's consolidated equity position. Deutsche Telekom was not subject to material transaction risk in the investment area at December 31, 2001.

Foreign currency risks in the financing area are hedged to the extent practicable by Central Treasury. Deutsche Telekom uses cross-currency interest rate swaps and foreign currency forward contracts to effectively convert foreign currency denominated financial assets and liabilities into the group companies' functional currencies (primarily Euro, U.S. dollar and British pound). At December 31, 2001, hedged foreign currency denominated liabilities consisted primarily of Deutsche Telekom's multi-currency global bond which was issued in July 2000, bonds issued in February 2001 that are denominated in Japanese yen, certain medium term notes and commercial paper. Hedged foreign currency denominated assets consisted primarily of U.S. dollar denominated short term intercompany loans. As a result its hedging activities, Deutsche Telekom was not subject to material foreign exchange risk in the financing area at December 31, 2001.

In the operating area, individual Deutsche Telekom's group entities conduct most of their activities in their respective functional currencies. Therefore, Deutsche Telekom considers its foreign currency transaction risk from its ongoing operations to be low. Some group entities are, however, exposed to foreign currency transaction risk related to certain anticipated foreign exchange payments. These anticipated foreign exchange payments relate primarily to capital expenditures and expense payments to international telecommunications carriers for completing international calls made by Deutsche Telekom's domestic customers. These anticipated foreign currency denominated payments are small compared to the group's consolidated cash flows and did not expose the group to material foreign currency risk at December 31, 2001. However, based on Deutsche Telekom's estimate of future foreign exchange spot rates, it selectively enters into foreign currency forward contracts or buys foreign currency options to hedge these anticipated payments up to a maximum of one year. There can be no assurance that actual foreign currency denominated payments will conform to Deutsche Telekom's expectations or to historical payment patterns.

The table below provides information about foreign currency derivative instruments. The nonderivative foreign currency denominated assets and liabilities are indicated in the interest rate tables below.

December 31, 2001
Derivative Instruments Subject to Foreign Exchange Risk

	Maturities							
	2002	2003	2004	2005	2006	Thereafter	Total	Fair Value
	(euro in millions)							
Foreign currency forward contracts								
Buy USD/sell EUR	38	12	12	11	11	21	104	3
Average contractual exchange rate (EUR/USD)	0.90	0.90	0.91	0.92	0.93	0.94	0.91	
Buy GBP/sell EUR	35	—	—	—	—	—	35	1
Average contractual exchange rate (EUR/GBP)	0.63						0.63	
Buy JPY/sell EUR	76	—	—	—	—	—	76	(7)
Average contractual exchange rate (EUR/JPY)	105.56						105.56	
Buy CHF/sell EUR	14	—	—	—	—	—	14	0
Average contractual exchange rate (EUR/CHF)	1.48						1.48	
Buy USD/sell GBP	0.27	0.35	—	—	—	—	1	0
Average contractual exchange rate (USD/GBP)	1.41	1.40					1.40	
Sell USD/buy EUR	10,669	37	33	—	—	—	10,759	(136)
Average contractual exchange rate (EUR/USD)	0.89	1.03	0.92				0.89	
Sell GBP/buy EUR	735	408	—	—	—	—	1,142	(13)
Average contractual exchange rate (EUR/GBP)	0.62	0.62					0.62	
Sell JPY/buy EUR	3	—	—	—	—	—	3	0
Average contractual exchange rate (EUR/JPY)	115.00						115.00	
Sell CHF/buy EUR	139	—	—	7	—	—	146	1
Average contractual exchange rate (EUR/CHF)	1.46			1.44			1.46	
Sell HUF/buy EUR	5	—	—	—	—	—	5	0
Average contractual exchange rate (EUR/HUF)	270.69						270.69	
Sell CZK/buy EUR	105	176	—	—	—	—	281	(97)
Average contractual exchange rate (EUR/CZK)	42.21	44.13					43.42	
Foreign currency options								
Buy USD-Call/EUR-Put	9	—	—	—	—	—	9	0
Average strike rate (EUR/USD)	0.89						0.89	
Buy USD-Put/EUR-Call	6	—	—	—	—	—	6	0
Average strike rate (EUR/USD)	0.89						0.89	

	Maturities							Fair
	2002	2003	2004	2005	2006	Thereafter	Total	Value
	(euro in millions)							
Cross currency interest rate swaps								
Receive variable USD, pay variable GBP(2)	—	—	—	2,463	—	3,940	6,403	286
Average pay rate (%)(1)				4.08		4.06	4.07	
Average receive rate (%)(1)				1.92		1.92	1.92	
Receive fixed JPY, pay variable EUR(2)	2,552	—	—	—	—	—	2,552	(271)
Average pay rate (%)(1)	3.61						3.61	
Average receive rate (%)(1)	0.44						0.44	
Receive variable USD, pay variable EUR(2)	—	—	—	785	—	1,845	2,629	141
Average pay rate (%)(1)				3.22		3.29	3.27	
Average receive rate (%)(1)				1.92		1.96	1.95	
Receive variable JPY, pay variable EUR(2)	155	359	—	892	—	—	1,407	(153)
Average pay rate (%)(1)	3.86	3.38		3.22			3.33	
Average receive rate (%)(1)	0.58	0.08		(0.04)			0.06	
Receive fixed JPY, pay fixed EUR(2)	240	—	326	—	233	93	893	(92)
Average pay rate (%)(1)	4.68		5.92		6.36	6.81	5.79	
Average receive rate (%)(1)	0.39		1.50		1.95	2.40	1.41	
Receive variable JPY, pay fixed EUR(2)	—	—	831	—	—	—	831	(78)
Average pay rate (%)(1)			5.88				5.88	
Average receive rate (%)(1)			1.18				1.18	
Receive fixed GBP, pay variable EUR(2)	—	237	—	—	—	—	237	11
Average pay rate (%)(1)		3.35					3.35	
Average receive rate (%)(1)		5.75					5.75	
Receive variable GBP, pay variable EUR(2)	—	37	—	—	—	—	37	(1)
Average pay rate (%)(1)		4.06					4.06	
Average receive rate (%)(1)		3.40					3.40	
Receive variable EUR, pay fixed SKK(2)	12	20	—	—	—	—	32	(3)
Average pay rate (%)(1)	16.99	9.15					12.04	
Average receive rate (%)(1)	2.85	4.18					3.69	
Receive fixed USD, pay variable EUR(2)	—	—	—	—	—	19	19	5
Average pay rate (%)(1)						3.88	3.88	
Average receive rate (%)(1)						7.05	7.05	
Receive variable CZK, pay variable EUR(2)	—	—	—	—	—	57	57	(2)
Average pay rate (%)(1)						4.77	4.77	
Average receive rate (%)(1)						3.38	3.38	
Receive fixed USD, pay fixed EUR(2)	—	—	—	—	—	21	21	5
Average pay rate (%)(1)						5.17	5.17	
Average receive rate (%)(1)						6.56	6.56	
Receive fixed EUR, pay fixed SKK(2)	10	—	—	—	—	—	10	0
Average pay rate (%)(1)	11.20						11.20	
Average receive rate (%)(1)	4.47						4.47	

(1) Weighted average settlement rates applicable to the current settlement period.
(2) Represents notional amounts.

Interest Rate Risk

Deutsche Telekom is exposed to market risk arising from changing interest rates, primarily in the European Union, in the United Kingdom and in the United States. Interest rate risk management currently is performed separately for Euro and British pounds, and separate interest rate risk management for U.S. dollars started in 2002. Once a year, Deutsche Telekom's Management Board specifies a desired mixture of fixed- and floating-rate net debt in each currency. Central Treasury then enters into interest rate derivatives to modify the interest payments on bonds, other liabilities and cash investments to adjust their risk profile to the defined target mixture. Interest rate swaps are used, as well as bought interest rate options (such as caps and collars) to a lesser extent. As a result of these hedging activities, approximately 75 percent of the EUR denominated net debt and 85 percent of the GBP denominated net debt effectively represented a fixed-rate debt exposure at December 31, 2001, assuming the due performance by our hedge counterparties of their obligations.

The following tables summarize the principal amounts and fair values, maturity and other contract terms of the interest rate sensitive derivative and nonderivative financial instruments that were held by Deutsche Telekom at December 31, 2001.

December 31, 2001
Assets and Related Derivative Instruments Subject to Interest Rate Risk

	Maturities							
	2002	2003	2004	2005	2006	Thereafter	Total	Fair Value
	(euro in millions)							
ASSETS								
Long-term loans								
Fixed rate, EUR	106	114	2	2	2	9	235	235
Average interest rate (%)	7.0	7.0	3.5	3.5	3.5	3.5	6.8	
Variable rate, EUR	—	15	—	—	—	—	15	15
Average interest rate (%)		3.6					3.6	
Fixed rate, HRK	—	—	—	—	—	6	6	6
Average interest rate (%)						0.8	0.8	
Variable rate, HUF	—	10	—	8	—	—	18	18
Average interest rate (%)		0.0		0.0			0.0	
Fixed rate, USD	3	—	—	—	11	—	14	14
Average interest rate (%)	12.0				7.6		8.5	
Variable rate, USD	246	—	—	—	—	—	246	246
Average interest rate (%)	2.4						2.4	
Investments in non-current securities								
Fixed rate, EUR	292	102	2	—	—	2	398	401
Average interest rate (%)	6.3	4.5	3.4			0	5.8	
Variable rate, EUR	—	—	—	—	—	1	1	1
Average interest rate (%)						3.5	3.5	
Fixed rate, GBP	—	445	—	—	—	—	445	445
Average interest rate (%)		5.0					5.0	
Fixed rate, HRK	5	5	—	6	—	—	16	16
Average interest rate (%)	3.0	8.0		8.4			6.6	
Fixed rate, SKK	2	—	—	—	—	—	2	2
Average interest rate (%)	11.5						11.5	
Fixed rate, USD	6	—	—	—	—	—	6	6
Average interest rate (%)	9.5						9.5	
Investments in marketable securities								
Fixed rate, EUR	191	102	363	—	1	—	657	657
Average interest rate (%)	6.0	8.8	5.3		4.5		6.0	
Variable rate, EUR	7	—	—	—	—	3	10	10
Average interest rate (%)	3.1					3.5	3.2	
Fixed rate, HRK	20	—	—	—	—	—	20	20
Average interest rate (%)	3.3						3.3	
Variable rate, HRK	7	—	—	—	—	—	7	7
Average interest rate (%)	5.4						5.4	
Fixed rate, MKD	1	—	—	—	—	—	1	1
Average interest rate (%)	0.0						0.0	

	Maturities 2002	2003	2004	2005	2006	Thereafter	Total	Fair Value
	(euro in millions)							
LIQUID ASSETS								
Fixed rate, EUR	1,380	119	—	—	—	—	1,499	1,499
Average interest rate (%)	0.7	4.5					1.0	
Variable rate, EUR	672	—	—	—	—	—	672	672
Average interest rate (%)	3.4						3.4	
Variable rate, CZK	38	—	—	—	—	—	38	38
Average interest rate (%)	4.8						4.8	
Variable rate, GBP	85	—	—	—	—	—	85	85
Average interest rate (%)	4.5						4.5	
Fixed rate, HRK	47	—	—	—	—	—	47	47
Average interest rate (%)	5.3						5.3	
Variable rate, HRK	46	—	—	—	—	—	46	46
Average interest rate (%)	5.0						5.0	
Variable rate, HUF	41	—	—	—	—	—	41	41
Average interest rate (%)	10.2						10.2	
Variable rate, JPY	2	—	—	—	—	—	2	2
Average interest rate (%)	0.4						0.4	
Variable rate, SGD	8	—	—	—	—	—	8	8
Average interest rate (%)	0.7						0.7	
Variable rate, SKK	292	—	—	—	—	—	292	292
Average interest rate (%)	3.5						3.5	
Fixed rate, USD	2	—	—	—	—	—	2	2
Average interest rate (%)	1.2						1.2	
Variable rate, USD	136	—	—	—	—	—	136	136
Average interest rate (%)	1.1						1.1	
EUR interest rate swaps								
Receive fixed, pay variable(2)	500	—	—	—	—	—	500	10
Average pay rate (%)(1)	3.26						3.26	
Average receive rate (%)(1)	3.79						3.79	

(1) Weighted average settlement rates applicable to the current settlement period.
(2) Represents notional amounts.

December 31, 2001
Liabilities and Related Derivative Instruments Subject to Interest Rate Risk

	Maturities 2002	2003	2004	2005	2006	Thereafter	Total	Fair Value
	(euro in millions)							
LIABILITIES								
Bonds and debentures, EUR								
Fixed rate	9,326	3,787	9,280	2,249	4,560	7,334	36,536	34,419
Average interest rate (%)	7.3	5.6	7.4	6.1	5.8	6.3	6.7	
Variable rate	200	1,000	—	—	128	—	1,328	1,327
Average interest rate (%)	4.0	3.7			4.8		3.9	
Bonds and debentures, GBP								
Fixed rate	36	237	—	1,003	—	481	1,757	1,551
Average interest rate (%)	3.5	5.8		7.1		7.1	6.9	
Bonds and debentures, USD								
Fixed rate	6	—	—	3,376	—	9,347	12,729	10,399
Average interest rate (%)	3.6			7.8		9.3	8.9	
Bonds and debentures, CZK								
Fixed rate	—	—	156	—	—	—	156	143
Average interest rate (%)			8.1				8.1	
Bonds and debentures, JPY								
Fixed rate	2,908	—	326	827	234	93	4,388	4,320
Average interest rate (%)	0.5		1.5	1.5	2.0	2.4	0.9	
Variable rate	108	360	831	—	—	—	1,299	1,278
Average interest rate (%)	0.4	0.4	1.1				0.8	
Bonds and debentures, CHF								
Fixed rate	13	—	—	—	—	—	13	13
Average interest rate (%)	3.4						3.4	

	Maturities 2002	2003	2004	2005	2006	Thereafter	Total	Fair Value
	(euro in millions)							
Bonds and debentures, HUF								
Fixed rate	—	53	—	—	—	—	53	53
Average interest rate (%)		9.3					9.3	
Variable rate	—	41	—	—	—	—	41	41
Average interest rate (%)		0.5					0.5	
Bonds and debentures, PLN								
Variable rate	1	—	—	—	—	—	1	1
Average interest rate (%)	0.0						0.0	
Liabilities to banks, EUR								
Fixed rate	428	504	332	150	8	686	2,108	1,940
Average interest rate (%)	5.8	6.6	5.6	6.4	10.5	6.5	6.2	
Variable rate	41	171	3	3	1	262	481	469
Average interest rate (%)	7.4	4.9	4.5	4.5	4.5	4.2	4.7	
Liabilities to banks, GBP								
Fixed rate	104	—	37	345	118	731	1,335	1,276
Average interest rate (%)	4.3		5.9	6.5	5.9	6.5	6.3	
Variable rate	25	37	41	2,912	21	1,133	4,169	4,169
Average interest rate (%)	4.9	3.8	3.8	4.7	3.8	4.5	4.6	
Liabilities to banks, USD								
Fixed rate	5	5	5	5	4	22	46	42
Average interest rate (%)	6.8	6.8	6.8	6.8	6.8	6.8	6.8	
Variable rate	27	9	30	21	25	141	253	251
Average interest rate (%)	5.2	5.3	5.5	8.3	8.7	8.1	7.5	
Liabilities to banks, HUF								
Fixed rate	—	1	52	1	1	2	57	56
Average interest rate (%)		0.0	11.5	0.0	0.0	0.0	10.5	
Variable rate	109	80	21	25	3	3	241	240
Average interest rate (%)	10.0	9.9	9.9	9.9	10.0	10.0	9.9	
Liabilities to banks, JPN								
Variable rate	3	—	—	—	—	—	3	3
Average interest rate (%)	0.4						0.4	
Liabilities to banks, NLG								
Fixed rate	2	2	2	2	2	5	15	13
Average interest rate (%)	7.3	7.3	7.3	7.3	7.3	7.3	7.3	
Liabilities to banks, FRF								
Fixed rate	1	1	1	1	2	7	13	12
Average interest rate (%)	7.7	7.7	7.7	7.7	7.7	7.7	7.7	
Liabilities to banks, CZK								
Variable rate	9	—	—	—	—	—	9	9
Average interest rate (%)	4.8						4.8	
EUR interest rate swaps								
Receive variable, pay fixed(2)	15	82	—	1,492	—	1,662	3,252	(243)
Average pay rate (%)(1)	4.94	4.26		5.65		5.88	5.73	
Average receive rate (%)(1)	3.56	3.31		3.22		3.28	3.25	
EUR interest rate swaps								
Receive fixed pay variable(2)	1,236	3,731	2,556	—	—	1,662	9,186	187
Average pay rate (%)(1)	3.87	3.49	4.34			3.28	3.74	
Average receive rate (%)(1)	4.83	4.56	4.66			5.17	4.74	
GBP interest rate swaps								
Receive variable, pay fixed(2)	41	862	49	3,940	410	3,940	9,243	(633)
Average pay rate (%)(1)	7.05	6.39	5.09	6.43	5.53	6.40	6.37	
Average receive rate (%)(1)	4.48	4.48	4.48	4.23	4.50	4.08	4.20	
Forward GBP interest rate swaps								
Receive variable, pay fixed(2)	—	—	328	1,313	—	—	1,642	(9)
Average pay rate (%)(1)			6.11	6.05			6.06	
Average receive rate (%)			LIBOR 6M	LIBOR 6M			LIBOR 6M	
JPY interest rate swaps								
Receive fixed, pay variable(2)	—	—	—	778	—	—	778	26
Average pay rate (%)(1)				0.34			0.34	
Average receive rate (%)(1)				1.50			1.50	
USD interest rate swaps								
Receive fixed, pay variable(2)	34	79	—	3,485	—	7,651	11,249	1,221
Average pay rate (%)(1)	1.87	3.20		2.41		1.92	2.08	
Average receive rate (%)(1)	5.90	5.83		7.70		8.05	7.92	

	Maturities 2002	2003	2004	2005	2006	Thereafter	Total	Fair Value
	(euro in millions)							
USD interest rate swaps								
Receive variable, pay fixed(2)	79	147	—	85	—	283	595	(27)
Average pay rate (%)(1)	5.33	5.40		5.92		6.23	5.86	
Average receive rate (%)(1)	2.18	2.84		3.10		2.09	2.44	
CZK interest rate swaps								
Receive fixed, pay variable(2)	—	—	13	—	—	—	13	1
Average pay rate (%)(1)			4.88				4.88	
Average receive rate (%)(1)			8.14				8.14	
EUR interest rate caps purchased								
Contract amount	153	—	—	—	—	—	153	0
Premium paid	9						9	
Average strike rate (%)	3.83						3.83	
GBP interest rate caps (collars) purchased								
Contract amount	205	41	—	—	—	—	246	(3)
Average cap strike rate (%)	8.50	7.50					8.33	
Average floor strike rate (%)	6.04	4.50					5.79	

(1) Weighted average settlement rates applicable to the current settlement period.
(2) Represents notional amounts.

Equity Price Risk

Deutsche Telekom continuously evaluates investment opportunities in order to meet its business and strategic goals. With limited exceptions, it is Deutsche Telekom's intention not to hedge fair value changes of its equity investments arising from fluctuations in quoted share prices. The table below presents the cost and fair value of those marketable equity securities comprising investments in start-up companies as well as other participations held by Deutsche Telekom at December 31, 2001 which are sensitive to changes in share prices. The securities are carried at cost.

	December 31, 2001 Assets subject to equity price risk Cost	Fair Value
	(in millions of euro)	
Investments in equity securities	415	994

Changes in Market Risk Exposure in 2001 Compared to 2000

As a result of the acquisition of VoiceStream and Powertel in May 2001, Deutsche Telekom now has a third principal currency to be managed in accordance with the principles governing management of the existing principal currencies, the Euro and the British pound. Deutsche Telekom's Central Treasury expects to start separate interest management for the U.S. dollar in 2002. At December 31, 2001, approximately 22 percent of Deutsch Telekom's U.S. dollar-denominated net debt was fixed-rate debt. Furthermore, as a result of the acquisition of VoiceStream and Powertel, Deutsche Telekom is exposed to a higher foreign currency translation risk compared to 2000. At December 31, 2001, the translation risk inherent in the net investments in VoiceStream and Powertel was hedged to the extent it relates to the shares of redeemable preferred stock in VoiceStream held by T-Mobile International AG.

An increase in Deutsche Telekom's long-term fixed-rate Euro-denominated bonds by almost EUR 4.0 billion compared with December 31, 2000 and the associated deviation from the desired mixture of fixed-rate and variable-rate debt, was counteracted by entering into EUR 5 billion in receive fixed, pay variable interest rate swaps.

MTN drawings predominantly denominated in Japanese yen and the issue of a yen-denominated bond in 2001 did not lead to any material increase in foreign currency transaction exposure, as these foreign currency items were converted into Euro exposures using cross-currency interest rate swaps.

Because the VoiceStream merger occurred in 2001, it is no longer possible to convert the initial investment in shares of convertible voting preferred stock of VoiceStream into shares of VoiceStream's common stock. VoiceStream is now a fully consolidated subsidiary. Other equity price risk decreased due to the sale of Deutsche Telekom's investment in Sprint.

ITEM 12. Description of Securities Other than Equity Securities

Not applicable.

PART II

ITEM 13. Defaults, Dividend Arrearages and Delinquencies

None.

ITEM 14. Material Modifications to the Rights of Security Holders and Use of Proceeds

None.

ITEM 15. [Reserved]

ITEM 16. [Reserved]

PART III

ITEM 17. Financial Statements

Not applicable.

ITEM 18. Financial Statements

See pages F-1 through F-82.

See pages A-1 through A-156 regarding the financial statements of certain equity method investees (requirements of Rule 3-09 of Regulation S-X).

ITEM 19. Exhibits

Documents filed as exhibits to this Annual Report.

1.1 Memorandum and Articles of Association (*Satzung*) of Deutsche Telekom AG as amended to date (English translation included).*

2.1 Indenture dated as of July 6, 2000 relating to debt securities of Deutsche Telekom International Finance B.V. (incorporated by reference to Deutsche Telekom's Registration Statement on Form F-3, File No. 333-12096).

2.2 Except as noted above, the total amount of long-term debt securities of Deutsche Telekom AG authorized under any instrument does not exceed 10 percent of the total assets of the Group on a consolidated basis. Deutsche Telekom AG hereby agrees to furnish to the Commission, upon its request, a copy of any instrument defining the rights of holders of long-term debt of Deutsche Telekom AG or of its subsidiaries for which consolidated or unconsolidated financial statements are required to be filed.

4.1 Agreement and Plan of Merger dated as of July 23, 2000, as amended and restated on February 8, 2001 and as amended on April 13, 2001 between Deutsche Telekom AG and VoiceStream Wireless Corporation and Bega, Inc. (incorporated by reference to Deutsche Telekom's registration statement on Form F-4, File No. 333-47306, as amended through February 9, 2001).

4.2 Amendment No. 1 dated as of April 13, 2001, to the Merger Agreement among Deutsche Telekom AG, VoiceStream and a Delaware corporation formed by Deutsche Telekom AG (incorporated herein by reference to Exhibit 29 to Deutsche Telekom AG's Amendment No. 4 to Schedule 13D in respect to VoiceStream filed on May 1, 2001).

8.1 Significant subsidiaries as of the end of the year covered by this report.*

10.1 Consent of Ernst & Young and PwC Deutsche Revision.

10.2 Consent of PwC Deutsche Revision.

10.3 Consent of PricewaterhouseCoopers N.V.

10.4 Consent of PwC Deutsche Revision.

10.5 Consent of Arthur Andersen Sp. zo.o.

10.6 Consent of Arthur Andersen ZAO.

10.7 Consent of Arthur Andersen.

10.8 Representation from Deutsche Telekom regarding quality control letters received from Arthur Andersen.

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* Previously filed.

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INDEX TO FINANCIAL STATEMENTS

REPORT OF INDEPENDENT ACCOUNTANTS

To the Board of Management and Shareholders of Deutsche Telekom AG

We have audited the accompanying consolidated balance sheet of Deutsche Telekom AG as of December 31, 2001, and the related consolidated statements of operations, shareholders' equity, and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Deutsche Telekom AG as of December 31, 2001, and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in Germany.

Accounting principles generally accepted in Germany vary in certain important respects from accounting principles generally accepted in the United States of America. The application of the latter would have affected the determination of consolidated net income for the year ended December 31, 2001, and the determination of consolidated shareholders' equity and consolidated financial position at December 31, 2001 to the extent summarized in Note (38) Reconciliation to U.S. GAAP to the consolidated financial statements.

March 18, 2002, except for Note (41c), as to which the date is June 14, 2002

Ernst & Young
Deutsche Allgemeine Treuhand AG
Wirtschaftsprüfungsgesellschaft
Stuttgart

(Prof. Dr. Pfitzer) Wirtschaftsprüfer	(Hollweg) Wirtschaftsprüfer

PwC Deutsche Revision
Aktiengesellschaft
Wirtschaftsprüfungsgesellschaft
Frankfurt am Main

(Frings) Wirtschaftsprüfer	(Laue) Wirtschaftsprüfer

REPORT OF INDEPENDENT ACCOUNTANTS

To the Board of Management and Shareholders of Deutsche Telekom AG

We have audited the accompanying consolidated balance sheet of Deutsche Telekom AG and its subsidiaries as of December 31, 2000 and the related consolidated statements of operations, of shareholders' equity and of cash flows for each of the two years in the period ended December 31, 2000. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Deutsche Telekom AG and its subsidiaries as of December 31, 2000, and the results of their operations and their cash flows for each of the two years in the period ended December 31, 2000 in conformity with accounting principles generally accepted in Germany.

Accounting principles generally accepted in Germany vary in certain important respects from accounting principles generally accepted in the United States of America. The application of the latter would have affected the determination of consolidated net income for each of the two years in the period ended December 31, 2000 and the determination of consolidated shareholders' equity and consolidated financial position at December 31, 2000 to the extent summarized in Note 38 to the consolidated financial statements.

Frankfurt am Main, March 26, 2001,
except for Notes 38, 39, 40 and 41 as to which the date is February 13, 2002

PwC Deutsche Revision
Aktiengesellschaft
Wirtschaftsprüfungsgesellschaft

(Frings)	(Laue)
Wirtschaftsprüfer	Wirtschaftsprüfer

CONSOLIDATED STATEMENTS OF OPERATIONS

	Note	2001	2000	1999
		millions of €	millions of €	millions of €
Net revenue	(1)	48,309	40,939	35,470
Change in inventories and other own capitalized costs	(2)	879	864	947
Total operating performance		**49,188**	**41,803**	**36,417**
Other operating income	(3)	6,619	11,002	1,871
Goods and services purchased	(4)	(13,477)	(11,950)	(7,667)
Personnel costs	(5)	(12,114)	(9,718)	(9,210)
Depreciation and amortization	(6)	(15,221)	(12,991)	(8,466)
Other operating expenses	(7)	(12,151)	(10,424)	(6,872)
Financial income (expense), net	(8)	(5,348)	(1,230)	(2,889)
Results from ordinary business activities		**(2,504)**	**6,492**	**3,184**
Extraordinary income (loss)	(9)	—	(159)	(240)
Taxes	(10)	(808)	(318)	(1,420)
Income (loss) after taxes		**(3,312)**	**6,015**	**1,524**
(Income) loss applicable to minority shareholders	(11)	(142)	(89)	(271)
Net income (loss)		**(3,454)**	**5,926**	**1,253**
Earnings (loss) per share in €		(0.93)	1.96	0.43

The accompanying notes are an integral part of the consolidated financial statements.

CONSOLIDATED BALANCE SHEETS

	Note	Dec. 31, 2001 millions of €	Dec. 31, 2000 millions of €
Assets			
Noncurrent assets			
Intangible assets	(12)	80,051	35,754
Property, plant and equipment	(13)	58,708	54,137
Financial assets	(14)	7,957	16,715
		146,716	106,606
Current assets			
Inventories, materials and supplies	(15)	1,671	1,587
Receivables	(16)	6,826	7,159
Other assets	(17)	4,966	3,671
Marketable securities	(18)	702	2,370
Liquid assets	(19)	2,868	1,893
		17,033	16,680
Prepaid expenses, deferred charges and deferred taxation	(20)	813	956
Total assets		164,562	124,242
Shareholders' equity and liabilities			
Shareholders' equity	(21)		
Capital stock	(22)	10,746	7,756
Additional paid-in capital	(23)	49,994	24,290
Retained earnings	(24)	3,607	398
Unappropriated net income carried forward from previous year		101	44
Net income (loss)		(3,454)	5,926
Minority interest	(25)	5,307	4,302
		66,301	42,716
Accruals			
Pensions and similar obligations	(27)	3,661	3,330
Other accruals	(28)	14,766	8,055
		18,427	11,385
Liabilities	(29)		
Debt		67,031	60,357
Other		12,020	9,130
		79,051	69,487
Deferred income		783	654
Total shareholders' equity and liabilities		164,562	124,242

The accompanying notes are an integral part of the consolidated financial statements.

CONSOLIDATED NONCURRENT ASSETS

millions of €	Acquisition or production cost							Depreciation, amortization and write-downs								Net carrying amount	
	Jan. 1, 2001	Translation adjustment	Changes in the composition of the Deutsche Telekom Group	Additions	Disposals	Reclassi-fications	Dec. 31, 2001	Jan. 1, 2001	Translation adjustment	Changes in the composition of the Deutsche Telekom Group	Additions	Disposals	Reclassi-fications	Reinstated depreciation	Dec. 31, 2001	Dec. 31, 2001	Dec. 31, 2000
Intangible assets																	
Concessions, industrial and similar rights and assets, and licences in such rights and assets	18,791	314	23,554	1,178	814	145	43,168	2,385	22	51	2,080	622	(2)	0	3,914	39,254	16,406
Goodwill statements	20,957	485	(21)	24,683	399	370	46,075	1,694	80	(20)	3,663	68	129	0	5,478	40,597	19,263
Advance payments	85	1	8	198	3	(89)	200	0	0	0	0	0	0	0	0	200	85
	39,833	800	23,541	26,059	1,216	426	89,443	4,079	102	31	5,743	690	127	0	9,392	80,051	35,754
Property, plant and equipment																	
Land and equivalent rights, and buildings including buildings on land owned by third parties	19,910	40	439	159	948	301	19,901	5,494	4	28	1,473	165	4	0	6,838	13,063	14,416
Technical equipment and machinery	73,313	397	4,588	5,523	3,854	1,938	81,905	37,792	105	296	6,805	3,042	2	0	41,958	39,947	35,521
Other equipment, plant and office equipment	5,534	69	392	1,221	529	268	6,955	3,402	33	40	1,199	458	(4)	0	4,212	2,743	2,132
Advance payments and construction in progress	2,073	29	1,096	2,950	105	(3,088)	2,955	5	0	0	1	6	0	0	0	2,955	2,068
	100,830	535	6,515	9,853	5,436	(581)	111,716	46,693	142	364	9,478	3,671	2	0	53,008	58,708	54,137
Financial assets																	
Investments in unconsolidated subsidiaries	171	0	(6)	124	8	16	297	18	0	0	51	0	0	0	69	228	153
Loans to unconsolidated subsidiaries	57	0	0	130	105	0	82	0	0	0	0	0	0	0	0	82	57
Investments in associated companies	7,341	171	(384)	520	3,524	652	4,776	678	11	0	303	31	(129)	0	832	3,944	6,663
Other investments in related companies	7,540	0	(5,605)	457	73	(16)	2,303	84	0	0	332	8	0	0	408	1,895	7,456
Long-term loans to associated and related companies	803	1	213	398	1	(544)	870	85	0	0	390	0	0	0	475	395	718
Other investments in noncurrent securities	1,130	1	20	81	329	0	903	24	0	0	0	0	0	0	24	879	1,106
Other long-term loans	563	1	14	76	166	47	535	1	0	0	0	0	0	0	1	534	562
	17,605	174	(5,748)	1,786	4,206	155	9,766	890	11	0	1,076	39	(129)	0	1,809	7,957	16,715
	158,268	1,509	24,308	37,698	10,858	0	210,925	51,662	255	395	16,297	4,400	0	0	64,209	146,716	106,606

CONSOLIDATED STATEMENTS OF CASH FLOWS

	2001	2000	1999
	millions of €	millions of €	millions of €
Net income (loss)	(3,454)	5,926	1,253
Income (loss) applicable to minority shareholders	142	89	271
Income (loss) after taxes	**(3,312)**	**6,015**	**1,524**
Depreciation and amortization	15,221	12,991	8,466
Income tax expense	751	194	1,380
Net interest expense	4,138	3,097	2,546
Results from the disposition of noncurrent assets	(1,106)	(4,796)	540
Results from associated companies	547	(1,890)	265
Other noncash transactions	(1,146)	(2,661)	28
Change in capitalized working capital*	428	(1,791)	(1,399)
Change in accruals	(136)	1,078	478
Change in other working capital carried as liability**	761	1,391	243
Income taxes (paid)received	10	(871)	(2,040)
Dividends received	115	189	172
Cash generated from operations	**16,271**	**12,946**	**12,203**
Interest paid	(4,779)	(3,873)	(3,100)
Interest received	442	927	485
Net cash provided by operating activities	**11,934**	**10,000**	**9,588**
Cash outflows from investments in			
— intangible assets	(1,021)	(15,980)	(881)
— property, plant and equipment	(9,847)	(7,556)	(5,093)
— financial assets	(498)	(8,487)	(3,480)
— consolidated companies	(5,695)	(4,343)	(12,633)
Cash inflows from disposition of			
— intangible assets	208	10	14
— property, plant and equipment	1,146	655	171
— financial assets	3,514	4,474	888
— shareholdings in consolidated companies and business units	1,004	3,114	2
Net change in short-term investments and marketable securities	4,440	401	2,328
Other	1,384	6	—
Net cash used for investing activities	**(5,365)**	**(27,706)**	**(18,684)**
Net change in short-term debt	(10,266)	(780)	(1,077)
Issuances of medium and long-term debt	13,949	19,708	1,833
Repayments of medium and long-term debt	(6,589)	(2,408)	(1,687)
Dividends	(1,905)	(1,914)	(1,718)
Proceeds from share offering	—	3,255	10,613
Changes in minority interests	—	2	1
Net cash provided by (used in) financing activities	**(4,811)**	**17,863**	**7,965**
Effect of foreign exchange rate changes on cash and cash equivalents	(26)	(29)	(55)
Net increase (decrease) in cash and cash equivalents	**1,732**	**128**	**(1,186)**
Cash and cash equivalents, at beginning of year	**1,006**	**878**	**2,064**
Cash and cash equivalents, at end of year	**2,738**	**1,006**	**878**

* Change in receivables, liabilities, other assets, inventories, materials and supplies and prepaid expenses and deferred charges.

** Change in other liabilities (which do not relate to financing activities) and deferred income.

The accompanying notes are an integral part of the consolidated financial statements.

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

millions of €	Shares issued and outstanding (in thousands)	Capital stock nominal value	Additional paid-in capital	Retained earnings: Difference from currency translation	Retained earnings: Treasury stock	Retained earnings: Other retained earnings (deficit)	Retained earnings: Total	Unappropriated net income carried forward from previous year	Net income	Minority interest	Total
Balance at Jan. 1, 1999	2,743,700	7,014	14,250	(503)	1	1,288	786	6	2,243	765	25,064
Changes in the composition of the Deutsche Telekom group										(1)	(1)
Dividends for 1998 0.62 € per share									(1,683)	(41)	(1,724)
Unappropriated net income carried forward from previous year								7	(7)		
Transfer to retained earnings						553	553		(553)		
Increase in nominal value of capital stock		10	(10)								
Proceeds from share offering	285,904	732	9,881								10,613
Transfer to reserve for treasury stock					13	(13)					
Net income/Net Loss									1,253	271	1,524
Difference from currency translation				219			219			(6)	213
Balance at Dec. 31, 1999	3,029,604	7,756	24,121	(284)	14	1,828	1,558	13	1,253	988	35,689
Changes in the composition of the Deutsche Telekom group						(31)	(31)			3,259	3,228
Dividends for 1999 0.62 € per share						(621)	(621)		(1,253)	(25)	(1,899)
Unappropriated net income carried forward from previous year						(31)	(31)	31			
Increase in nominal value of capital stock			169								169
Transfer from reserve for treasury stock					(7)	7					
Net income/Net Loss									5,926	89	6,015
Difference from currency translation				(477)			(477)			(9)	(486)
Balance at Dec. 31, 2000	3,029,604	7,756	24,290	(761)	7	1,152	398	44	5,926	4,302	42,716
Changes in the composition of the Deutsche Telekom group										808	808
Dividends for 1999 0.62 € per share								(1,877)		(33)	(1,910)
Unappropriated net income carried forward from previous year						3,992	3,992	1,934	(5,926)		
Increase in nominal value of capital stock	1,168,148	2,990	25,704								28,694
Net income/Net Loss									(3,454)	142	(3,312)
Difference from currency translation				(811)		28	(783)			88	(695)
Balance at Dec. 31, 2001	4,197,752	10,746	49,994	(1,572)	7	5,172	3,607	101	(3,454)	5,307	66,301

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Description of business and relationship with the Federal Republic of Germany

Since January 1, 2001 the Deutsche Telekom group's (referred to as the Company, Deutsche Telekom or Group below) business has been structured in four divisions: T-Com, T-Systems, T-Mobile and T-Online. "Other" contains not only Group headquarters and central service areas, but also certain foreign subsidiaries.

T-Com is responsible for serving the 41 million residential customers and approximately 420,000 small and medium-sized business customers in Germany. Furthermore, the entire international interconnection business, the remaining broadband cable business, a major portion of the value-added services and the entire terminal equipment business are assigned to T-Com.

T-Systems is responsible for serving domestic and international named accounts. T-Systems offers comprehensive services in the convergence field of information technology (IT) and telecommunications (TC). The acquisition of T-Systems ITS GmbH (formerly debis Systemhaus GmbH) made Deutsche Telekom the second largest systems company in Europe, and in a position to provide its customers with IT/TC packages and e-business systems solutions all from under one roof.

T-Mobile is Deutsche Telekom's mobile communications division. It combines the Group's main mobile communications activities. T-Mobile currently offers mobile communications services via subsidiaries in Germany, the United Kingdom, the United States of America, Austria and the Czech Republic and has holdings in mobile communications companies in Poland, the Netherlands and Russia. T-Mobile will be able to offer the new mobile communications standard UMTS in many countries via its subsidiaries.

T-Online is the business segment for the Internet mass market. Measured by subscriber numbers and revenue, T-Online is one of the largest Internet service providers in Europe with service offerings in Germany, France, Spain, Portugal and Austria. T-Online concentrates on the areas of Internet access and portals (advertising/e-commerce). For this reason, Deutsche Telekom includes in the T-Online division not only the business of T-Online International AG, but also the business of DeTeMedien.

"Other" combines a variety of Group units whose activities cannot be allocated to an individual division. These include Deutsche Telekom group headquarters and competence centers, such as customer billing, and real estate. This segment also includes those foreign subsidiaries and shareholdings which cannot be clearly assigned to another segment because of their activities or customer structure. The most significant of these are the foreign companies MATAV, Slovenské Telekomunikácie (referred to as Slovenské below) and Croatian Telecom.

The Company, Deutsche Telekom AG, was registered with the Commercial Registry of the Bonn District Court (Amtsgericht – HRB 6794) on January 2, 1995.

The Company's capital stock was increased on May 31, 2001 as a result of the acquisition of VoiceStream and Powertel in the form of a share exchange and a cash payment. The number of Deutsche Telekom authorized shares increased to 4.2 billion. The Federal Republic's direct and indirect shareholding in Deutsche Telekom as of December 31, 2001 amounts to 43.05%. The direct shareholding amounts to 30.92%; a further 12.13% of the shares are held by a federal corporation, the Kreditanstalt für Wiederaufbau (KfW). The Federal Republic administers its shareholding and exercises its rights as a shareholder through a public law entity, the Bundesanstalt für Post und Telekommunikation Deutsche Bundespost (the Federal Agency), which is subject to supervision by the Federal Ministry of Finance (BMF).

In accordance with § 21 paragraph 1 of the Security Trading Act (WpHG), the Federal Agency informed Deutsche Telekom in its letter of June 5, 2001 that its share of the voting rights in Deutsche Telekom had fallen below the 50% threshold on May 31, 2001, to 43.05%. According to a letter of February 13, 2002, the Federal Agency held 1,297,896,644 shares in Deutsche Telekom as at December 31, 2001, a shareholding of 30.92%. In accordance with § 21 paragraph 1 of the WpHG, the KfW informed Deutsche Telekom in its letter of December 22, 1997 that its share of the voting rights in Deutsche Telekom had exceeded the 10% threshold to 13.47%. As reported in a letter of January 22, 2002, the KfW held 509,164,599 shares in Deutsche Telekom as at December 31, 2001, a shareholding of 12.13%.

The Regulatory Authority for Telecommunications and Posts (the Regulatory Authority) commenced its activities on January 1, 1998. The Regulatory Authority, which is under the authority of the Federal Ministry of Economics, has thus taken the place of the dissolved Federal Ministry of Posts and Telecommunications in supervising the telecommunications sector in Germany, and in this capacity regulates the business activities of Deutsche Telekom.

The Federal Republic and various government departments and agencies are collectively Deutsche Telekom's largest customer. Charges for services provided to the Federal Republic and such departments and agencies are based on Deutsche Telekom's commercial pricing policies. Services provided to any one department or agency do not represent a significant component of Deutsche Telekom's net revenues.

Summary of significant accounting policies

The annual financial statements and the management report of the Deutsche Telekom group have been prepared in accordance with the requirements of the German Commercial Code (Handelsgesetzbuch – HGB) and German Stock Corporation Law (Aktiengesetz – AktG).

German GAAP differs in certain respects from generally accepted accounting principles in the United States of America (U.S. GAAP). Application of U.S. GAAP would have affected the balance sheets as of December 31, 2001 and 2000 and the results of operations for each of the three years in the period ended December 31, 2001. The material differences between German GAAP and U.S. GAAP as they related to the Company are discussed in further detail in footnote (38).

The consolidated balance sheets and the consolidated statements of operations are prepared in accordance with the classification requirements of § 298 HGB, in combination with § 266 and § 275 HGB. The statement of operations is prepared using the total cost method. All amounts shown are in millions of Euros (€/EUR). Certain items have been combined for presentation purposes in the statements of operations and the balance sheets in order to enhance the informative value and understanding of the financial statements. These items are disclosed separately in the notes. In case of changes in presentation, prior-year amounts are reclassified to conform with the current-year presentation. In accordance with § 297 paragraph 1 sentence 2 HGB, the consolidated accounts also include a consolidated statement of cash flows and a segment report; in addition, the consolidated accounts also include a consolidated statement of shareholders' equity. In conformity with international practice, reporting begins with the statements of operations followed by the balance sheets, the statements of cash flows and the statements of shareholders' equity, which precede the notes to the consolidated financial statements.

The consolidated financial statements are prepared in accordance with uniform accounting and valuation principles. The accounting policies used in the consolidated financial statements differ from those used in the unconsolidated financial statements of the parent company. Such differences, mostly applied to conform with U.S. GAAP, include the following:

- Property, plant and equipment leased under contracts for which the risks and rewards of ownership have been assumed are capitalized. Scheduled depreciation is recorded over the useful economic life of the asset or over the term of the lease. The present value of payment obligations resulting from future lease payments is included as liabilities.

- Interest incurred while items included in property, plant and equipment were under construction has been added to construction costs.

- Direct pension obligations are measured in accordance with Statement of Financial Accounting Standards (SFAS) No. 87, using valuation methods consistent with those used for indirect pension obligations in the unconsolidated financial statements of Deutsche Telekom AG. The increase in the average life expectancy is taken into account in the measurement of all pension obligations in the consolidated financial statements.

- In the measurement of the compensation obligations to the Civil Service Health Insurance Fund (*Postbeamtenkrankenkasse*), the additional accruals required according to the new 1998 life expectancy tables by Prof. Dr. Klaus Heubeck ("Richttafeln 1998") were recorded in the 1998 financial year, thus fully affecting net income in that year. In contrast, in the unconsolidated financial statements of Deutsche Telekom AG, the accruals are spread over four financial years.

- Accruals for the internal costs of preparing the annual financial statements are not recorded.

- Investment grants received are recorded as reductions of the acquisition costs of assets.

Consolidated group

The consolidated financial statements are comprised of the accounts of Deutsche Telekom AG and its subsidiaries.

The subsidiaries, associated companies and other related companies have been included in the consolidated financial statements in accordance with the following criteria:

- Subsidiaries are companies in which Deutsche Telekom directly or indirectly has majority voting rights or management control.
- Associated companies are companies in which Deutsche Telekom directly or indirectly holds between 20% and 50% of the voting rights and exercises significant influence. Such companies are generally included in the consolidated financial statements using the equity method.
- Companies in which Deutsche Telekom holds less than 20% of the voting rights are carried in the consolidated financial statements at the lower of acquisition cost or market value and classified as other investments in related companies.

The changes in the composition of the Deutsche Telekom group in 2001 are presented in the following table:

	Domestic	International	Total
Consolidated subsidiaries			
January 1, 2001	80	129	209
Additions	16	129	145
Disposals	(10)	(12)	(22)
Reclassifications	18	7	25
December 31, 2001	104	253	357
Associated companies included at equity			
January 1, 2001	24	28	52
Additions	2	10	12
Disposals	(1)	(4)	(5)
Reclassifications	(4)	(5)	(9)
December 31, 2001	21	29	50
Other unconsolidated subsidiaries and other investments in related companies (greater than 5%)			
January 1, 2001	90	54	144
Additions	27	13	40
Disposals	(12)	(17)	(29)
Reclassifications	(14)	(2)	(16)
December 31, 2001	91	48	139
Total			
January 1, 2001	194	211	405
Additions	45	152	197
Disposals	(23)	(33)	(56)
Reclassifications	—	—	—
December 31, 2001	216	330	546

The consolidated financial statements include the individual company financial statements of the parent company, Deutsche Telekom AG, as well as 104 and 80 domestic and 253 and 129 foreign subsidiaries in 2001 and 2000, respectively in which Deutsche Telekom AG has a direct or indirect controlling interest.

At December 31, 2001 and 2000, 83 and 84 subsidiaries, respectively, were not included in the calculation because they were not material to the net worth, financial position and results of the Deutsche Telekom group. These subsidiaries accounted for less than 1% of consolidated revenue, results and balance sheet total of the Deutsche Telekom group.

In accordance with § 311 paragraph 1 HGB, 50 and 52 companies in 2001 and 2000 over which Deutsche Telekom exercises significant influence have been classified as associated companies and are accounted for using the equity method. The remaining 56 and 60 associated companies in 2001 and 2000, which have little or no effect on the net worth, financial position and results of the T-Mobile International Group, were classified as other investments in related companies at acquisition cost less applicable write-downs.

The full list of investment holdings is filed with the Commercial Registry of the Bonn District Court (HRB 6794). It is available upon request from Deutsche Telekom AG, Bonn, Investor Relations. Furthermore, the list of investment holdings includes a full list of all subsidiaries which exercise the disclosure simplification option in accordance with § 264 paragraph 3 HGB.

The most significant subsidiaries consolidated for the first time in 2001 are VoiceStream and Powertel including their subgroup financial statements. The changes in the composition of the Deutsche Telekom group had the following effects on the consolidated financial statements:

Effects on the consolidated statement of operations (in millions of EUR):

Revenue	6,248
Goods and services purchased	(2,156)
Personnel costs	(1,782)
Depreciation and amortization	(3,056)
Other income/(expenses)	(2,395)
Net loss	(3,141)

Effects on the consolidated balance sheet (in millions of EUR):

Assets		**Shareholders' equity and liabilities**	
Noncurrent assets	54,621	Shareholders' equity	26,032
Current assets, prepaid expenses, deferred charges and deferred taxation	2,461	Accruals	7,019
		Liabilities and deferred income	24,031
	57,082		57,082

On January 15, 2001, Deutsche Telekom acquired 51% of the shares in the Macedonian telecommunications company Makedonski Telekommunikacii A.D., Skopje (referred to as Maktel below) via a subsidiary of MATAV, the Deutsche Telekom Hungarian telecom subsidiary. The purchase price amounted to EUR 301.5 million. Maktel was included in the subgroup financial statements of MATAV for the first time in the first quarter of 2001. The goodwill of EUR 180.3 million will be amortized over a period of 20 years.

In April 2001, Deutsche Telekom increased its shareholding in the Czech mobile communications company RadioMobil a.s., Prague (''RadioMobil'') via Cmobil B.V., Amsterdam, a subsidiary of T-Mobile International. The purchase price for this additional stake amounted to EUR 598 million. This increased CMobil's stake in RadioMobil from 49% to 60.77%. The additional goodwill of EUR 444 million, will be amortized over a period of 12 years. RadioMobil was consolidated in full for the first time on April 1, 2001. Prior to April 1, 2000, RadioMobil was accounted for under the equity method.

On May 31, 2001 Deutsche Telekom acquired 100% of the outstanding shares in VoiceStream Wireless Corporation (''VoiceStream'') and Powertel, Inc. (''Powertel'') for a total purchase price of EUR 39.4 billion including a cash component of EUR 4.9 billion and the initial investment in VoiceStream preferred stock amounting to EUR 5.6 billion, which Deutsche Telekom had made in September 2000 and the issuance of 1.2 billion Deutsche Telekom shares.

VoiceStream provides mobile communications services for private households in urban areas of the United States through its GSM (Global System for Mobile Communications) network. Powertel Inc. provides mobile communications services for private households, mainly in urban areas in the southeastern United States thru its GSM network. VoiceStream shareholders received for each share of VoiceStream common stock either 3.6693 Deutsche Telekom shares and US$ 15.7262 in cash, 3.6683 Deutsche Telekom shares and US$ 15.9062 in cash or 3.7647 Deutsche Telekom shares. Each Powertel shareholder received 2.6353 Deutsche Telekom shares for each Powertel share. The consolidation of VoiceStream and Powertel generated goodwill totaling EUR 23.6 billion. This is scheduled to be amortized over a period of up to 20 years. VoiceStream and Powertel were consolidated in full for the first time on May 31, 2001. In conjunction with the acquisition of VoiceStream and Powertel as described above, Deutsche Telekom exchanged VoiceStream and Powertel warrants, options and obligations pursuant to exchange right agreements (Cook Inlet Exchange Rights, Eliska Wireless Exchange Rights) into warrants, options and exchange rights to acquire 1,767,509 and 37,627,149 and 4,224,603 Deutsche Telekom ordinary shares, respectively.

Deutsche Telekom AG acquired an additional 16% stake in the capital of the Croatian telecommunications company Croatian Telecom, Zagreb, on October 25, 2001 for a purchase price of EUR 507 million. Deutsche Telekom AG is therefore now the majority shareholder with a stake of 51% and includes the company in full in its consolidated financial statements from November 1, 2001. The goodwill generated, a total of EUR 240 million, is scheduled to be amortized over periods up to 20 years.

In the first quarter of 2000, through the acquisition of the Netherlands-based Mediaone holding company for a total purchase price of EUR 2.1 billion, Deutsche Telekom increased its shareholdings in the Hungarian mobile communications company Westel 900 from 15.2% to 64.2% and the Polish mobile communications company Polska Telefonia Cyfrowa (PTC) from 22.2% to 45%. The resulting goodwill amounts to EUR 0.9 billion for Westel 900 and EUR 1.1 billion for PTC, which is scheduled to be amortized over a period of 15 years. At the same time, MATAV was granted an option to acquire the remaining 49% in Westel 900. Matav exercised its option during the fourth quarter of 2001.

In April 2000, the subsidiary T-Online International AG acquired 99.9% of the shares in the French Internet service provider Grolier Interactive Europe Online Groupe S.A. (renamed T-Online France SAS (Club Internet)) from the Lagardère group. The total consideration paid by the Company was approximately EUR 1,880 million, consisting of 69,633,116 shares of T-Online issued as part of a capital increase against non-cash contributions. This resulted in goodwill in Deutsche Telekom's consolidated financial statements of EUR 0.5 billion, which will be amortized over a period of 7 years. T-Online France was consolidated for the first time in the second quarter of 2000.

Ameritech exercised its right effective June 30, 2000 to offer and transfer its 50% stake in MagyarCom to Deutsche Telekom. As a result, Deutsche Telekom became the sole shareholder of MagyarCom. The purchase price was EUR 2.3 billion; this resulted in further goodwill of EUR 1.9 billion, which is scheduled to be amortized over a period of 15 years. MagyarCom holds shares (59.52%) in the publicly traded company MATAV.

In October 2000, Deutsche Telekom acquired a shareholding through T-Systems GmbH of 50.1% in debis Systemhaus GmbH (now T-Systems ITS GmbH), including its subsidiaries, for a cash contribution of EUR 4.6 billion. The group operates in the field of information technology. The acquisition of debis Systemhaus in the fourth quarter of 2000 generated goodwill of EUR 2.6 billion, which is scheduled to be amortized over periods ranging from 3 and 12 years. Deutsche Telekom AG has granted DaimlerChrysler Services AG, Berlin, an option valid until January 1, 2005, under which DaimlerChrysler Services AG has the right to sell its shares in debis Systemhaus GmbH (now T-Systems ITS GmbH) (49.9%) to Deutsche Telekom AG. In addition, Deutsche Telekom AG has an option valid from January 1, 2002 to January 1, 2005 to acquire debis Systemhaus (now T-Systems ITS GmbH) in full. DaimlerChrysler Service AG has exercised the contractually agreed put option effective January 1, 2002. Deutsche Telekom AG acquired the remaining 49.9% stake in exchange for a cash payment of approximately EUR 4.7 billion on March 4, 2002.

At the end of the third quarter 2000, Deutsche Telekom AG acquired a total of 51% of the shares in the Slovakian telecommunications company Slovenské (''Slovek Telekom'') for EUR 1.0 billion through the purchase of shares issued by Slovek Telekom through a capital increase. The resulting goodwill of EUR 0.5 billion will be amortized over a period of 15 years. The company was consolidated for the first time on September 30, 2000.

The following table presents significant pro forma financial data as if the significant subsidiaries acquired in 2000 and 2001 had been consolidated into Deutsche Telekom as of January 1, 2000.

Unaudited pro forma information

	2001	2000
Net revenue (billions of €)		
Actual	48.3	40.9
Pro forma	51.1	47.9
Net income/(loss) under German GAAP (millions of €)		
Actual	(3.5)	5.9
Pro forma	(6.0)	(1.4)
Earnings (loss) per share under German GAAP (in €)		
Actual	(0.93)	1.96
Pro forma	(1.61)	(0.47)

Principal subsidiaries and associated companies

The principal subsidiaries and associated companies whose revenues and results, together with Deutsche Telekom AG, account for more than 90% of the Group are shown in the table below:

Name and registered office	Deutsche Telekom share Dec. 31, 2001	Shareholders' equity Dec. 31, 2001	Revenue 2001	Income (loss) after taxes 2001	Employees 2001 annual average
	%	millions of €	millions of €	millions of €	
Subsidiaries					
DeTeMobil Deutsche Telekom MobilNet GmbH, Bonn(5)	100.00	1,447	7,076	1,123	9,488
Deutsche Telekom Mobile Holdings Ltd., London, United Kingdom(1)(5)	100.00	13,989	3,279	(1,587)	6,784
max.mobil Telekommunikation Service GmbH, Wien, Österreich(1)(5)	100.00	367	1,052	1	2,858
VoiceStream Wireless Corporation, Bellevue, Washington, USA/**Powertel Inc.**, Bellevue, USA(1)(2)(5)	100.00	33,365	2,798	(2,795)	9,098
RadioMobil a.s., Prague(2)(7)	60.77	298	487	48	1,755
T-Online International AG, Darmstadt(1)	81.71	5,814	1,140	(804)	1,810
T-Systems ITS GmbH, Leinfelden-Echterdingen(1)(6)	50.10	4,559	996	(147)	20,967
T-Systems CSM GmbH, Darmstadt(6)	100.00	243	1,969	189	6,766
T-Systems Nova GmbH, Bonn(6)	100.00	70	830	46	5,083
T-Systems SIRIS S.A.S., Paris, France(6)	100.00	82	241	(155)	594
GMG Generalmietgesellschaft mbH, Münster	100.00	153	3,764	(48)	7,828
T-Data Gesellschaft für Datenkommunikation mbH, Bonn(1)	100.00	502	573	15	1,248
Kabel Deutschland GmbH, Bonn(1)	100.00	3,801	1,095	508	2,461
MATAV Magyar, Távközlési Rt., Budapest, Hungary(1)(4)	59.52	2,074	2,138	438	16,819
Slovenské Telekomunikácie, a.s., Bratislava, Slovakia	51.00	1,053	462	94	12,089
Croatian Telecom, Zagreb, Croatia(1)(2)	51.00	1,546	154	5	1,871
Associated companies					
MTS, OJSC Mobile TeleSystems, Moscow, Russia(3)(5)(8)	36.20	661	604	191	2,340
Other companies					
France Télécom S.A., Paris, France(1)(3)	1.78	33,157	33,674	3,660	188,866

(1) Consolidated subgroup financial statements
(2) Revenue and net income since being included in the Deutsche Telekom group
(3) 2000 financial year
(4) Held via MagyarCom Holding GmbH, Bonn (Deutsche Telekom AG share: 100%)
(5) Indirect shareholding via T-Mobile International AG, Bonn (Deutsche Telekom share: 100%)

(6) Indirect shareholding via T-Systems International GmbH, Bonn (Deutsche Telekom share: 100%)
(7) Indirect shareholding via Cmobil B.V., Amsterdam (Deutsche Telekom indirect share: 92.14%)
(8) Indirect shareholding via DeTEMobil Deutsche Telekom Mobil Net GmbH, Bonn, (Deutsche Telekom share: 100%)

Consolidation principles

Capital consolidation is performed following the book value method under German GAAP. Under this method, the purchase consideration for an acquisition is allocated to the assets and liabilities acquired based on their fair values. Any resulting excess of the purchase consideration over the parent's interest in the fair value of net assets acquired is capitalized as goodwill and amortized over its useful life. Negative goodwill from capital consolidation is included under other accruals.

Profits or losses generated by subsidiaries during their period of affiliation with the Group are included in retained earnings; furthermore, they include the effects of consolidation and the net income (loss) of subsidiaries.

If, in the course of capital increases of subsidiaries and associated and related companies, shares are issued to third-party shareholders, without the involvement of Deutsche Telekom, the resulting added value for Deutsche Telekom is shown, in cases of cash capital increases, as income in the statement of operations; in cases of capital increases for non-cash contributions, it is only shown as such if the added value exceeds a given level of goodwill acquired by the subsidiary or associated or related company in the course of the capital increase.

Revenue, income and expenses as well as receivables and liabilities between the consolidated companies are eliminated. **Intercompany profits and losses** and income effects from the **consolidation of intercompany debt** are eliminated in the consolidated financial statements.

The consolidated balance sheets include deferred taxes resulting from the effects of consolidation, provided the tax expense is expected to reverse in later years, except where the effects of consolidation relate to the parent company during the periods prior to the end of 1995, when it was essentially exempt from taxation.

The investments in associated companies included **at equity** are accounted for using the book value method. This method is similar to the method described above for consolidated subsidiaries. The principles used for full consolidation are also applied in treating the differences resulting from the initial consolidation.

Joint ventures are included in the consolidated financial statements using the equity method.

Foreign currency translation

In the individual company financial statements, foreign currency receivables, cash in banks and liabilities are translated at the exchange rate applicable on the transaction date. Unrealized foreign currency losses due to exchange rate fluctuations through the balance sheet date are recognized in the statement of operations while unrealized foreign currency gains are not recognized. Where foreign currency items have been hedged by forward exchange contracts, they are valued at the corresponding hedge rate.

Currency translation of foreign subsidiaries is made in accordance with the functional currency method. Thus, the functional currency is the currency in which the foreign subsidiary performs its principal operations. The activities and financial structure as reported in this currency should be reflected in the group accounts. Generally, the functional currency of dependent subsidiaries is identical with that of the parent company. Dependent subsidiaries are translated according to the temporal method. On the other hand, the functional currency of independent subsidiaries is the local currency. Currently all consolidated foreign subsidiaries of Deutsche Telekom conduct their operations independently of the parent company; the financial statements are therefore translated according to the modified current rate method. Therefore, in the consolidated financial statements, the translation of all items shown in balance sheets of foreign subsidiaries from foreign currencies into Euros is performed using middle rates on the balance sheet date and, for Member States of the European Monetary Union, the official Euro conversion rates. Gains and losses resulting from translation are recorded, without affecting net income, in retained earnings. The income statements of foreign subsidiaries are translated at the average annual exchange rates.

The exchange rates of certain significant currencies are as follows:

	Annual average rate			Rate at balance sheet date	
	2001	2000	1999	Dec. 31, 2001	Dec. 31, 2000
	€	€	€	€	€
100 Swiss Francs (CHF)	66.2063	64.2701	62.5317	67.5494	65.6859
100 Czech Coruna (CZK)	2.9092	2.8011	2.7133	3.1309	2.8547
1 Pound Sterling (GBP)	1.6076	1.6423	1.5181	1.6418	1.6044
100 Croatian Kuna (HRK)	13.3685	13.0896	13.0640	13.6055	13.1924
100 Hungarian Forints (HUF)	0.3904	0.3850	0.3958	0.4079	0.3775
100 Indonesian Rupiah (IDR)	0.0109	0.0130	0.0121	0.0109	0.0111
100 Japanese Yen (JPY)	0.9170	1.0050	0.8292	0.8644	0.9361
100 Malaysian Ringgit (MYR)	29.3934	28.5882	24.7594	29.8263	28.2907
100 Philippine Pesos (PHP)	2.1913	2.4585	2.4049	2.1973	2.1521
100 Polish Zloty (PLN)	27.2201	24.9595	23.7013	28.6050	25.9876
1 Russian Rubel (RUB)	0.0383	0.0386	0.0378	0.0372	0.0376
100 Singapore Dollars (SGD)	62.5594	62.9966	55.4866	61.2145	66.0721
100 Slovak Koruna (SKK)	2.3099	2.1282	2.2700	2.3377	2.2773
1 U.S. Dollar (USD)	1.1168	1.0863	0.9388	1.1334	1.0750

Accounting and valuation

Net revenues consist of goods and services sold in connection with the ordinary business activities of Deutsche Telekom. Net revenues are recorded net of VAT and sales-related reductions and recorded in the period realized. Revenues due from foreign carriers for international incoming calls are included in revenues in the period in which the calls occur. Revenues from other operating activities are recognized in the period when earned by the delivery of goods or the rendering of services.

Research and development costs are expensed as incurred and amounted to approximately EUR 0.9 billion, EUR 0.7 billion, and EUR 0.7 billion for the years ended December 31, 2001, 2000 and 1999, respectively.

Pension costs for defined benefit plans are actuarially computed and shown using the Projected Unit Credit Method, which is consistent with SFAS No. 87. This method presupposes the total present value of the benefit obligations accumulated during the reporting period and takes into consideration the expected increases in wages and salaries and in retirement benefits. By contrast, the minimum accrual method in accordance with § 6a of the German Income Tax Act (Einkommensteuergesetz, EStG) is aimed at the recognition of the expense over the employees' entire working lives and does not take the expected increases in wages and salaries and retirement benefits into account (cf. Note 27 accruals for pensions and similar obligations).

Pension costs include current service cost, interest cost, return on plan assets and amortization of actuarial gains/losses. Calculation of pension obligations according to SFAS No. 87 may result in an additional minimum liability which is recorded as an expense in the consolidated financial statements.

The pension costs are accrued in the balance sheet consistent with SFAS No. 87, whereby the accrual is increased by the expense recognized and decreased by payments made during the year.

Deutsche Telekom is required to make contributions to a pension fund for current and former civil servant employees in annual amounts established by Postreform II, which came into force in 1995, rather than by annual actuarial valuations. The amounts currently due in each period are recognized as an expense in that period.

Advertising costs are charged to expense as incurred.

Income tax expense includes current payable taxes on income as well as deferred income taxes. Deferred income taxes are recorded for the expected future tax effects attributable to temporary differences in the balance sheets prepared for tax reporting and for financial reporting purposes, except for the effects of those differences that are not expected to reverse in the foreseeable future. Such differences may arise at the individual taxable entity level as well as in consolidation. Deferred taxes on temporary differences relating to Deutsche Telekom AG have not been included in the consolidated financial statements for periods prior to

January 1, 1996 as Deutsche Telekom AG was not taxable prior to January 1, 1995 and benefited from an essentially complete exemption from tax in 1995.

Earnings per share for each period is calculated by dividing net income/loss by the weighted average number of ordinary shares outstanding during that period. The weighted average number of ordinary shares in 2001 was ascertained after giving effect to the issuance of shares as part of the acquisition of VoiceStream and Powertel from the date these shares began trading in Frankfurt am Main, which was June 4, 2001.

Purchased **intangible assets** are valued at acquisition cost and are amortized on a straight-line basis over their estimated useful lives, except for UMTS licenses which are amortized over the terms of the licenses. Acquired goodwill, including goodwill resulting from capital consolidation, is amortized on a straight-line basis over its useful life.

As permitted by Postreform II, **property, plant and equipment** transferred to Deutsche Telekom AG on January 1, 1995 was recorded in the opening balance sheet of Deutsche Telekom AG at fair market values at that date. However, due to the short period of time between the acquisition dates and January 1, 1995, property, plant and equipment acquired during 1993 and 1994 was valued at its remaining book value. The remaining useful lives and the depreciation methods applicable to these assets were not changed. The fair market values shown in the opening balance sheet have been carried forward as the acquisition costs.

Other property, plant and equipment is valued at acquisition or construction cost, less scheduled depreciation. Construction costs include directly allocable costs, an appropriate allocation of material and production overhead and interest accruing during construction. General administration expenses are not capitalized.

Property, plant and equipment includes nondeductible capitalized German VAT amounts at the level of expected refunds from VAT adjustments pursuant to § 15a of the German Value-Added Tax Act (Umsatzsteuergesetz – UStG) resulting from Deutsche Telekom's full liability for VAT as of 1996. Capitalized VAT was depreciated over a period of four years, starting in 1996 and ending in 1999.

When an impairment in the value of assets occurs, non-scheduled write-downs are made. Deutsche Telekom assesses the impairment of identifiable intangibles and long-lived assets whenever there is reason to believe that the carrying value may materially exceed the fair value and where a permanent impairment in value is anticipated. Determination of impairments of long-lived and intangible assets also involves the use of estimates which include but are not limited to the cause, the timing and the amount of the impairment. Impairment is based on a broad measure of factors. In evaluating assets for impairment the Company applies the German commercial law principle of prudence (*Vorsichtsprinzip*) (Sec. 252 (1)(4) of the German Commercial Code) in conjunction with the individual valuation principle (*Einzelbewertungsgrundsatz*). Among others, the company typically considers technological obsolescence, discontinuance of services and other changes in circumstances that indicate an impairment.

Nonscheduled write-downs related to goodwill are provided when an impairment in the value occurs. Deutsche Telekom reviews, on a regular basis, the performance of its subsidiaries. When there is reason to believe that the goodwill arising from the acquisition of that subsidiary is impaired and that the impairment is of permanent nature, Deutsche Telekom compares the carrying amount of that subsidiary to its fair value. The determination of the fair value of a subsidiary involves extensive use of estimates, depending on the method used, to determine the fair value. Methods commonly used by Deutsche Telekom for valuations include discounted cash flow methods and quoted stock market prices, if available. Factors affecting estimated fair values typically include discount rates, future cash flows, market prices and control premiums. These estimates, including the methodologies used, are important in determining fair value and ultimately the amount of any goodwill write-down.

To increase the informative value of the financial statements, accelerated depreciation recorded in the individual company financial statements for tax purposes has not been recognized in the consolidated financial statements.

Depreciation of noncurrent assets is carried out using the straight-line method over the following useful lives:

	years
Intangible assets	3 to 22
Goodwill	3 to 20
Buildings	25 to 30
Shop improvements and window displays	8
Telephone facilities and terminal equipment	3 to 10
Data communications equipment, telephone network and ISDN switching equipment, transmission equipment, radio transmission equipment and technical equipment for broadband distribution networks	4 to 10
Broadband distribution networks, outside plant networks and cable conduit lines	15 to 35
Telecommunications power facilities and other	3 to 10
Other equipment, plant and office equipment	3 to 20

Additions to real estate property are depreciated beginning in the month the building is placed into service. For assets other than buildings acquired in the first half of a year, a full year of depreciation is provided in the year of acquisition and, for those assets acquired in the second half of the year, a half year of depreciation is provided.

Items with a low acquisition cost are expensed in the year of purchase.

Maintenance and repairs are charged to expense when incurred.

Upon sale or disposal of **noncurrent assets**, the related cost and accumulated depreciation are removed from the balance sheet, and a gain or loss is recognized for the difference between the proceeds from the sale and the net carrying amount of the assets.

Financial assets are valued at the lower of cost or market value. Low-interest or non-interest bearing loan receivables are recorded at net present value. Nonscheduled write-downs are provided only if impairment of financial assets is assumed to be permanent. In measuring impairments, Deutsche Telekom uses the quoted market prices, if available, or other valuation methods, based on information available from the investee.

Raw materials and supplies, and **merchandise** purchased and held for resale are valued at acquisition cost, while **work in process and finished goods** are stated at production cost using average cost. Based on normal capacity utilization, production cost includes directly allocable costs such as material and labor costs as well as special production costs plus an appropriate allocation of material and production overhead and straight-line depreciation. General administration and selling costs, social amenities expenses as well as voluntary benefits to personnel including pensions are not included in production cost. The carrying amount of inventories is reduced to the lower of cost or market value at the balance sheet date. To the extent that inventory values are impaired, obsolescence provisions are made.

Receivables and other assets are shown at their nominal value. Known individual risks are accounted for through appropriate individual valuation allowances, and general credit risks through general valuation adjustments of receivables. Low-interest and non-interest bearing items with more than one year remaining to maturity are discounted.

Marketable securities are stated at the lower of cost or market value at the balance sheet date.

Effects of Stock options granted by way of a contingent capital increase are recognized only in the balance sheet at the date the options are exercised, not at the date they are granted. At the time the options are exercised, the amount received by the company from its employees is recorded at the value of the corresponding nominal capital increase in the capital stock and at the value of an additional amount in additional paid-in capital, in accordance with § 272 paragraph 2 No. 1 HGB.

Pension obligations are calculated using actuarial methods in accordance with the internationally accepted Projected Unit Credit Method, which is consistent with U.S. GAAP (SFAS No. 87), and are shown in accordance with SFAS No. 132.

Provisions for taxes and other accruals, including those for loss contingencies and environmental liabilities are recorded using best estimates. Sufficient allowance was made for all perceivable risks when assessing these provisions and accruals.

Deferred taxes are recorded for the expected tax effects of temporary differences between the balance sheets prepared for financial reporting and tax reporting purposes, as well as for the temporary differences arising from consolidation entries. Deferred taxes are netted and either a net deferred tax asset or net deferred tax liability is recorded separately under tax accruals. For purposes of computing deferred taxes, Deutsche Telekom used the German income tax rate for undistributed earnings for domestic companies until and including 1999 — and from 2000 the uniform corporate income tax rate — and the respective local tax rate for foreign companies.

Cost accruals are only made by Deutsche Telekom when there is an obligation to carry such liabilities on the balance sheet pursuant to § 249 paragraph 1 HGB. This refers mainly to accruals for costs of maintenance recorded in the financial year, but actually incurred within the first three months of the following year.

Major **accruals**, with the exception of pensions and similar obligations as well as Civil Service Health Insurance Fund accruals for future shortfalls, are not discounted.

Liabilities are recorded at their repayment amount. In instances where the repayment amount of a liability is greater than the principal amount, the difference is recorded as an asset and recognized as an adjustment to interest expense over the term of the liability.

Unrealized losses relating to **derivative financial instruments** which do not qualify for hedge accounting are recognized when incurred whereas unrealized gains are deferred until realized.

The preparation of consolidated financial statements in accordance with German GAAP requires the Company to make estimates and assumptions that affect the reported carrying amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the amounts of revenues and expenses recognized during the reporting period. Actual results could differ from those estimates.

NOTES TO THE CONSOLIDATED STATEMENT OF OPERATIONS

(1) Net revenue(1)

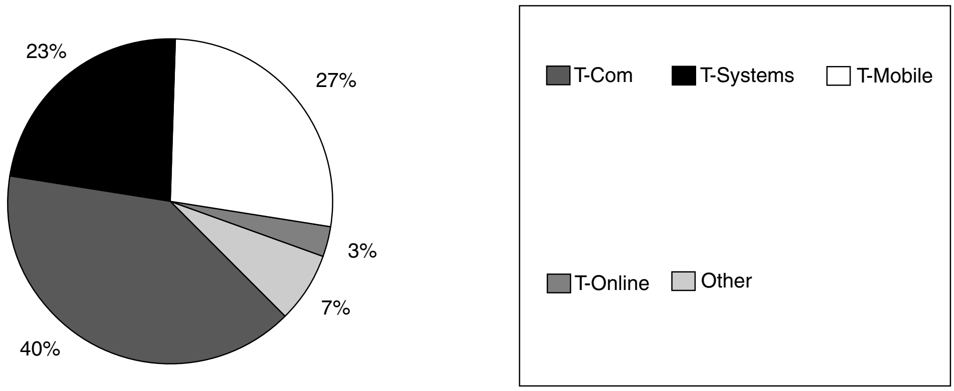
	2001	2000	1999
	millions of €	millions of €	millions of €
T-Com	19,362	20,170	21,606
T-Systems	11,211	8,460	6,018
T-Mobile	12,994	8,994	5,153
T-Online	1,338	1,038	813
Other	3,404	2,277	1,880
	48,309	40,939	35,470

(1) Deutsche Telekom focused its business activities on its four-pillar strategy in the 2001 financial year and has managed its activities in 2001 in four divisions. "Other" contains not only Group headquarters and central service areas, but also certain foreign subsidiaries (MATAV, Slovenské, Croatian Telecom). The figures for previous years have been adjusted accordingly.

Revenue by geographic area:

	2001	2000	1999
	millions of €	millions of €	millions of €
Domestic	35,107	33,178	31,411
International	13,202	7,761	4,059
	48,309	40,939	35,470
Breakdown of international revenues:			
European Union (excluding Germany)	6,088	5,023	1,906
Rest of Europe	3,787	2,266	1,817
North America	3,066	231	161
Latin America	85	43	17
Other	176	198	158
	13,202	7,761	4,059

The percentage of the individual revenue segments in relation to net revenue for 2001 is as follows:



Net revenue increased by EUR 7,370 million or 18% over the previous year. The changes in the composition of the Deutsche Telekom group resulted in a revenue increase of EUR 6,248 million or 15.3%.

The increase in revenue at T-Systems was attributable in particular to the consolidation for the full year of T-Systems ITS and business with national carriers.

T-Mobile generated increased revenue, in particular as a result of the consolidation of VoiceStream and Powertel since June 1, 2001 and the increased mobile communications subscriber numbers at T-Mobile Deutschland and DT Mobile Holdings (referred to as One 2 One).

The increase at T-Online is attributable to the strong customer growth in the access area and the increased usage across all the main tariffs. The increased roll-out of the portal business also had a positive effect.

The main causes for the revenue decrease at T-Com, besides price changes, were the substitution in the fixed network of long-distance calls by mobile calls in the city region and the influence of competition.

The increase in revenue in the segment "Other" is mainly due to the fact that Maktel, Croatian Telecom and Slovenské were not consolidated in the previous year, or not consolidated for the full financial year. Furthermore, increased revenue from MATAV's mobile communications activities due to growth in subscriber numbers also contributed to the revenue growth.

(2) Changes in inventories and other own capitalized costs

	2001 millions of €	2000 millions of €	1999 millions of €
Change in inventories of work in process	(7)	161	216
Own capitalized costs	886	703	731
	879	864	947

Own capitalized costs relate primarily to planning and construction services. They include interest incurred during the construction period in the amount of EUR 65 million, EUR 64 million and EUR 63 million in 2001, 2000 and 1999, respectively.

(3) Other operating income

	2001 millions of €	2000 millions of €	1999 millions of €
Income from disposition of marketable securities	1,967	—	—
Income from the disposition of noncurrent assets (including sales of investments)	1,584	5,928	89
Reversal of accruals	1,139	386	506
Foreign currency transaction gains	533	309	89
Income from reversal of valuation adjustments	288	125	106
Cost reimbursements	255	305	248
Refund of value-added tax (§ 15a UStG)	85	169	379
Insurance compensation	46	51	55
Income from the national roaming agreement	5	95	154
Income from capital increases of subsidiaries and associated companies	—	2,887	—
Other income	717	747	245
	6,619	11,002	1,871

Of the income from the disposition of marketable securities, EUR 1,954 million relates to income from the sale of Sprint shares.

Income from the disposition of noncurrent assets amounted to EUR 1,584 million. Of this amount, EUR 912 million relates to the sale of the regional cable company in Baden-Württemberg. A further EUR 75 million was generated by the sale of Isla Communications Co., Inc. shares. The decrease in comparison with the previous year is attributable to the non-recurrence of the proceeds from the sale in 2000 of Global One and the cable companies in North-Rhine Westphalia and Hesse.

Of the increase in the reversal of accruals, EUR 350 million relates to the reversal of accruals for real estate risks which were previously calculated as lump sums. This risk is now taken into account in a nonscheduled write-down on real estate for the same value.

Of the total amount of other operating income, EUR 1,897 million, EUR 611 million and EUR 701 million, in 2001, 2000 and 1999, respectively, relates to other financial years.

(4) Goods and services purchased[1]

	2001 millions of €	2000 millions of €	1999 millions of €
Goods purchased	4,397	4,075	2,625
Services purchased	9,080	7,875	5,042
of which: network access charges, Germany	2,174	1,985	1,585
of which: international network access charges	3,268	2,819	1,626
of which: other services	3,638	3,071	1,831
	13,477	11,950	7,667

(1) Since the beginning of the 2000 financial year, certain expenses (mainly relating to maintenance) have been shown as other operating expenses, rather than other services purchased. EUR 737 million was reclassified for the 1999 financial year.

The level of goods and services purchased increased by EUR 1,527 million compared to 2000. Of this increase, EUR 2,156 million is attributable to changes in the composition of the Deutsche Telekom group. Without taking into consideration the changes in the composition of the Deutsche Telekom group, this results in a decrease which is mainly attributable to the lower level of terminal equipment purchased and the decrease in network access charges in the international carrier sector.

(5) Personnel costs/Average number of employees

	2001 millions of €	2000 millions of €	1999 millions of €
Wages and salaries:			
Civil servants	1,874	2,287	2,535
Salaried employees (excl. civil servants)[1]	7,439	5,183	3,985
	9,313	7,470	6,520
Social security contributions and expenses for pension plans and benefits:			
Social security costs	1,147	861	730
Expenses for pension plans for civil servants	845	895	1,483
Expenses for pension plans for salaried employees[2]	607	310	265
Pension costs	1,452	1,205	1,748
Active civil servant healthcare costs	151	164	193
Other employee benefits	51	18	19
	2,801	2,248	2,690
	12,114	9,718	9,210

Number of employees (average for the year)

	2001	2000	1999
Civil servants	56,707	65,217	76,223
Salaried employees (excl. civil servants)[1]	184,953	139,815	121,783
Total Deutsche Telekom group	241,660	205,032	198,006
Trainees/student interns	8,147	6,826	6,354

(1) Since the new Deutsche Telekom AG collective agreement came into force on July 1, 2001, there is no longer any differentiation between salaried employees and wage earners; a single figure is shown for employees.

(2) Expenses are incurred from net periodic pension costs which includes an additional minimum liability amounting to EUR 259 million in 2001.

Personnel costs increased by EUR 2,396 million or 24.7% in 2001 to EUR 12,114 million. Of this amount, EUR 1,782 million related to newly consolidated companies. Furthermore, collectively agreed adjustments of wages and salaries to bring them in line with market conditions and to promote performance, and the structural change with the assignment of personnel in higher value positions contributed to the increase in personnel costs. Further, an additional minimum pension liability of EUR 259 million had the effect of increasing expense in the consolidated financial statements under German GAAP.

The average number of employees increased by 36,628 or 17.9% to 241,660. Changes in the composition of the Deutsche Telekom group in the course of the year led to an increase of 15,327 in the average number of employees (mainly attributable to the new acquisitions, VoiceStream and Powertel and Maktel). The remainder of the increase is mainly attributable to the acquisitions made in the course of the previous year, in particular T-Systems ITS and Slovenské, which in 2000 were only included in the calculation of the average for the period they belonged to the Group and are included in full in 2001.

(6) Depreciation and amortization

	2001	2000	1999
	millions of €	millions of €	millions of €
Amortization of intangible assets	5,743	2,233	801
of which: amortization of goodwill	3,663	1,248	300
of which: amortization of UMTS licenses	724	381	0
Depreciation of property, plant and equipment	9,478	10,758	7,665
	15,221	12,991	8,466

Depreciation and amortization increased during 2001 by EUR 2,230 million or 17.2% to EUR 15,221 million. Besides the full year's amortization of UMTS licenses, the inclusion of companies consolidated for the first time had a considerable impact of EUR 3,056 million on this development. This amount includes EUR 1.4 billion of amortization of goodwill, relating in particular to VoiceStream and Powertel with approximately EUR 0.9 billion and T-Systems ITS with EUR 0.2 billion.

In December 2001, T-Mobile International implemented a global rebranding program to migrate all brands to the "T-Mobile" brand. As a result of this decision, nonscheduled write-downs of EUR 1,040 million were made on the goodwill of One 2 One and max.mobil, which includes the existing old company names as components, in 2001.

Further nonscheduled write-downs of intangible assets amounted to approximately EUR 63 million.

The nonscheduled write-downs for real estate in the form of a valuation adjustment amounting to EUR 2,018 million made in 2000 have been allocated in 2001 to individual items of real estate, based on a detailed survey, as part of Deutsche Telekom's changed real estate strategy. This survey resulted in further nonscheduled write-downs during 2001 of EUR 466 million. An additional non-scheduled write-down was also made in 2001 in the form of a valuation adjustment amounting to EUR 350 million for buildings for which business use is no longer planned. This write-down corresponds to income in the same amount from the reversal of accruals for risks previously calculated as a lump sum.

Furthermore, non-scheduled write-downs of EUR 158 million were made on property, plant and equipment, in particular EUR 104 million for technical equipment of mobile communications networks of One 2 One.

(7) Other operating expenses

	2001	2000	1999(1)
	millions of €	millions of €	millions of €
Marketing expenses	1,896	1,967	1,148
Advertising, gifts and commissions	1,329	794	381
Losses on accounts receivable and provision for doubtful accounts	1,225	723	514
Rental and leasing expenses	1,213	766	513
Maintenance, repairs and damage reparation	1,133	843	730
Legal and consulting fees	695	591	499
Other employee-related costs	598	493	349
Postal charges	486	481	438
Losses on disposition of noncurrent assets (including sale of investments)	478	1,132	629
Provisions	391	611	238
Foreign currency transaction losses	333	241	275
Administrative expenses	314	217	184
Travel and transport expenses	290	241	192
License and concession expenses	197	116	85
Loan employment and temporary employment expenses	145	122	50
Utilities	129	77	34
Telephone charges	94	15	7
Losses relating to derivative financial instruments	73	194	134
Other expenses	1,132	800	472
	12,151	10,424	6,872

(1) Prior-year figures have been adjusted to reflect the changed reporting structure in the 2000 financial year. Various expenses (mainly relating to maintenance) were shown under goods and services purchased until 1999. A total of EUR 737 million has been reclassified for the 1999 financial year.

Other operating expenses decreased by EUR 561 million before the effects of the changes in the composition of the Deutsche Telekom group (EUR 2,288 million) are taken into account.

The increase in advertising, gifts and commissions relates mainly to the inclusion of VoiceStream and Powertel in 2001. The losses on accounts receivable and provisions for doubtful accounts are mostly attributable to bad debt losses with carriers. The increase in rental and leasing expenses results mainly from the changes in the composition of the Deutsche Telekom group, in particular the consolidation of VoiceStream and Powertel and T-Systems ITS GmbH. Maintenance, repairs and damage reparation expenses increased at Deutsche Telekom AG in particular as a result of more extensive modernization measures.

This was offset by a decrease in losses from dispositions. The losses on disposition of noncurrent assets in the previous year mainly related to the scrapping of outside plant equipment and the sale of Eurobell (Holdings) Plc, Crawley.

Of the total amount of other operating expenses, EUR 534 million, EUR 1,208 million and EUR 687 million in 2001, 2000 and 1999, respectively, relates to other accounting periods.

(8) Financial income (expense), net

	2001 millions of €	2000 millions of €	1999 millions of €
Dividend income from investments	107	147	166
Results related to companies accounted for under the equity method (including amortization of goodwill)	(547)	1,890	(265)
Income (loss) related to associated and related companies	(440)	2,037	(99)
Income from debt securities and long-term loan receivables	152	487	83
Other interest and similar income	408	511	420
Interest and similar expense	(4,698)	(4,095)	(3,049)
Net interest expense	(4,138)	(3,097)	(2,546)
Write-downs on financial assets and marketable securities	(770)	(170)	(244)
	(5,348)	(1,230)	(2,889)

The increase in the net financial expense in the 2001 financial year is a consequence of several items. The income (loss) related to subsidiaries, associated and related companies decreased by EUR 2,477 million compared with the high positive level of the previous year at EUR 2,037 million, mainly as a consequence of the non-recurrence of a one-time gain recorded in 2000, totaling EUR 2,358 million relating to the sale of WIND by the associated company DT-FT Italian Holding GmbH. Net interest expense increased partly due to the newly issued bonds for financing the UMTS licenses (EUR 603 million), and partly by the reduced income from debt securities and long-term loan receivables (EUR 335 million) due to the sale of specialized security funds in the first half of 2000. The increase in write-downs on financial assets and marketable securities by EUR 600 million to EUR 770 million is primarily a result of the valuation adjustment of the net carrying amount of Deutsche Telekom's shareholding in France Telecom (EUR 312 million) and increased valuation adjustments for loans to subsidiaries of Kabel Deutschland GmbH (EUR 317 million).

(9) Extraordinary income (losses)

In 2000, this item related to the share offering costs for the initial public offering of T-Online International AG and expenses for the planned initial public offering of T-Mobile International AG. In 1999 this item showed exclusively the costs from Deutsche Telekom AG's second share offering.

(10) Taxes

Breakdown of income before taxes:

	2001 millions of €	2000 millions of €	1999 millions of €
Germany	2,953	8,291	2,910
International	(5,457)	(1,958)	34
	(2,504)	6,333	2,944

Breakdown of tax expense:

	2001 millions of €	2000 millions of €	1999 millions of €
Income taxes	751	194	1,380
Other taxes	57	124	40
	808	318	1,420

Breakdown of the Group's income taxes, Germany and international:

	2001	2000	1999
	millions of €	millions of €	millions of €
Current taxes			
Germany	686	207	1,471
International	91	35	34
Deferred income taxes			
Germany	(30)	(57)	(121)
International	4	9	(4)
	751	194	1,380

In 2001, the combined statutory income tax rate, currently 39%, includes corporate income taxes at a rate of 25%, trade taxes at an average German national rate and the solidarity surcharge (Solidaritätszuschlag) of 5.5% on corporate income tax. In 2000 and 1999, the combined statutory income tax rate of 52%, including corporate income taxes at a rate of 40% for undistributed earnings, trade taxes at an average German national rate and the solidarity surcharge (Solidaritätszuschlag) of 5.5% on corporate income tax, was used. When earnings were distributed, the corporate income tax imposed on such earnings was reduced to 30%. Due to the change in taxation of corporations effective in 2001, the deferred taxes at the end of 2000 were calculated under the new tax law reflecting the reduced rate.

Although the Group's results under HGB are considerably lower than in the previous year, the taxable result is higher than the comparable figure for the previous year. This is attributable to the differing composition of income and expense with and without tax effects.

There was no income tax expense despite the increased basis for tax calculation due to existing net operating loss carryforwards.

Differences between actual tax expense of EUR 751 million and EUR 194 million for 2001 and 2000 and the expected corporate income tax expense (computed using 39% for 2001, the statutory corporate income tax rate for the parent company) are as follows:

	2001	2000
	millions of €	millions of €
Expected corporate income tax (benefit)/expense at the tax rate applicable for the parent company	(977)	2,723
Increase (decrease) in income tax due to:		
Tax-free gains/losses	(795)	(1,252)
Reduction of the Group's results without tax effect	2,896	1,497
Increase in the Group's results without tax effect	(171)	(2,324)
Discounted taxation, including taxation differences abroad	(491)	(546)
Permanent and semi-permanent differences between the balance sheets prepared for financial reporting and tax reporting purposes	611	(640)
Trade tax (long-term debt)	216	180
Utilization of net operating loss carryforwards	(1,186)	370
Effective changes in taxation recalculations	676	167
Other	(28)	19
Income taxes	751	194
Effective income tax rate	(30%)	3.1%

In its tax return, Deutsche Telekom AG has reported a goodwill (residual difference between the market value of the Company and the fair value of the individual assets) that is — based on § 7 paragraph 1 EStG — amortized over a period of 15 years. In line with the principle of prudence, as in previous years, goodwill amortization has not been recognized for accounting purposes in the year under review until this approach has been fully approved.

Deferred taxes result primarily from temporary differences between income determined under German GAAP and under applicable tax law. On the basis of the existing net operating loss carryforwards in the

Deutsche Telekom tax consolidation group, the parent company will not show any income taxes on the current taxable result until the net operating loss carryforwards have been utilized in full. The deferred taxes of the parent company and the integrated companies which will offset each other in the short term, i.e. over the period of utilization of the net operating loss carryforwards, were released in 2001.

At December 31, 2001, Deutsche Telekom had net operating loss carryforwards affecting corporate income tax and similar carryforwards amounting to approximately EUR 17,633 million, as compared to EUR 547 million in 2000, and trade tax net operating loss carryforwards amounting to approximately EUR 4,580 million, as compared to EUR 753 million in 2000. With the exception of net operating loss carryforwards of EUR 10,442 million in the United States, which will start to expire in 2008 and additional net operating loss carryforwards of EUR 644 million in certain tax jurisdictions which expire at varying dates, these net operating loss carryforwards have an unlimited carry forward period under German and local tax law.

(11) (Income) loss applicable to minority shareholders

(Income) loss applicable to minority shareholders includes EUR 322 million, EUR 189 million and EUR 274 million in 2001, 2000 and 1999, respectively, in gains and EUR 180 million, EUR 100 million and EUR 3 million in 2001, 2000 and 1999, respectively, in losses. The gains in 2001 relate mainly to MATAV and T-Systems ITS. The losses relate mainly to T-Online International AG.

NOTES TO THE CONSOLIDATED BALANCE SHEET

(12) Intangible assets

	Dec. 31, 2001 Net carrying amount	Dec. 31, 2000 Net carrying amount
	millions of €	millions of €
Concessions, industrial and similar rights and assets, and licenses in such rights and assets	39,254	16,406
Goodwill	40,597	19,263
Advance payments	200	85
	80,051	35,754

The increase in concessions and industrial and similar rights is mainly due to the changes in the composition of the Deutsche Telekom group, EUR 23,455 million of which relates to VoiceStream and Powertel, mostly for mobile communications licenses. The EUR 21,334 million increase in goodwill is also a result of the consolidation for the first time of VoiceStream and Powertel, which accounted for EUR 23,598 million. This is offset by amortization of EUR 3,663 million.

The development of intangible assets is shown in the table of consolidated noncurrent assets.

(13) Property, plant and equipment

	Dec. 31, 2001 Net carrying amount	Dec. 31, 2000 Net carrying amount
	millions of €	millions of €
Land and equivalent rights, and buildings including buildings on land owned by third parties	13,063	14,416
Technical equipment and machinery	39,947	35,521
Other equipment, plant and office equipment	2,743	2,132
Advance payments and construction in progress	2,955	2,068
	58,708	54,137

The development of property, plant and equipment is the result of offsetting effects. On the one hand, investments were made amounting to EUR 9,853 million which relate mainly to technical equipment and machinery. Furthermore, property, plant and equipment increased as a result of the changes in the composition of the Deutsche Telekom group — particularly relating to the inclusion of VoiceStream and Powertel and Croatian Telecom. Finally, the partial sale of cable activities decreased property, plant and equipment by EUR 433 million.

The development of property, plant and equipment is shown in the table of consolidated noncurrent assets.

Leasing

Minimum lease payments under leases expiring subsequent to December 31, 2001 are shown below.

Year	Capital Leases	Operating Leases
	millions of €	millions of €
2002	46	1,269
2003	48	1,012
2004	48	856
2005	51	754
2006	51	684
after 2006	662	2,264
Total minimum lease payments	906	6,839
Imputed interest	(384)	
Present value of net minimum lease payments	522	

Capital leases are primarily for office buildings and have terms of up to 25 years.

(14) Financial assets

	Dec. 31, 2001 Net carrying amount	Dec. 31, 2000 Net carrying amount
	millions of €	millions of €
Investments in subsidiaries	228	153
Loans to subsidiaries	82	57
Investments in associated companies	3,944	6,663
Other investments in related companies	1,895	7,456
Long-term loans to associated and related companies	395	718
Other investments in noncurrent securities	879	1,106
Other long-term loans	534	562
	7,957	16,715

The decrease of EUR 2,719 million in the net carrying amount of investments in associated companies relates mainly to a dividend payment of DT-FT Italian Holding GmbH, Bonn to Deutsche Telekom, amounting to EUR 2,759 million and a reclassification of the shares in Croatian Telecom, Zagreb, as a result of its full consolidation for the first time in 2001. Furthermore, the decrease is marked by negative operating results and the amortization of goodwill. These developments were partially offset by increases in various related companies of the VoiceStream Wireless Corporation, Bellevue, amounting to EUR 290 million.

The net carrying amounts of other investments in related companies also decreased by EUR 5,561 million, as the initial investment of EUR 5,590 million in VoiceStream preferred shares made in 2000 as part of the acquisition costs has now been eliminated in the full consolidation of the company. Furthermore, the valuation adjustment of the shareholding in France Telecom reduced its net carrying amount. These decreases were offset by other investments in related companies including EUR 254 million through the forgiveness of shareholder loans.

Long-term loans primarily include loans to associated and related companies. The decrease is mainly attributable to valuation allowances for loans to cable companies.

Other investments in noncurrent securities mainly include fixed-interest securities. The decrease is attributable to the sale of part of the fixed-interest securities from the portfolio of Deutsche Telekom Holding B.V., Amsterdam. This is offset by the acquisition of additional fixed-interest securities by Deutsche Telekom AG for EUR 74 million.

The development of financial assets is shown in the table of consolidated noncurrent assets. The full list of investment holdings is filed under HRB 6794 with the Commercial Registry of the Bonn District Court. It is available upon request from Deutsche Telekom AG, Bonn, Investor Relations.

Significant investments in associated companies are shown below:

	Dec. 31, 2001			Dec. 31, 2000		
Name	Deutsche Telekom share	Net carrying amount	of which: Net difference between carrying value and equity in net assets	Deutsche Telekom share	Net carrying amount	of which: Net difference between carrying value and equity in net assets
	%	millions of €	millions of €	%	millions of €	millions of €
PTC	45.00	1,232	1,114	45.00	1,165	1,088
Ben Holding[1]	50.00	871	584	50.00	1,036	638
GSM Facilities	24.00	516	—	—	—	—
MTS[2]	36.20	435	16	36.20	327	17
Cook Inlet/VS GSM IV	83.56	360	—	—	—	—
Other		530	101		4,135	574
		3,944	1,815		6,663	2,317

(1) Shareholding: 50% minus 1 share
(2) Proportional market value on December 31, 2001: EUR 1,459 million

(15) Inventories, materials and supplies

	Dec. 31, 2001	Dec. 31, 2000
	millions of €	millions of €
Raw materials and supplies	597	201
Work in process	458	612
Finished goods and merchandise	606	763
Advance payments	10	11
	1,671	1,587

Inventories, materials and supplies increased compared with 2000 by EUR 84 million or 5.3%. The effect from the consolidation for the first time of VoiceStream and Powertel, Maktel, RadioMobil and Croatian Telecom amounted to EUR 354 million.

Raw materials and supplies include spare parts for data communications equipment, transmission equipment and other telecommunications, components and cable. Work in process is mainly related to projects which have not yet been completed, such as the installation of private automatic branch exchanges (PABXs) and the implementation of IT systems solutions.

Finished goods and merchandise relate mainly to inventories of terminal equipment held both for resale and leasing as well as existing rights of use for submarine cables.

Advance payments relate mainly to orders for terminal equipment.

(16) Receivables

	Dec. 31, 2001	Dec. 31, 2000
	millions of €	millions of €
Trade accounts receivable	6,173	6,852
Receivables from subsidiaries	423	149
Receivables from associated and related companies	230	158
	6,826	7,159

In December 2001, Deutsche Telekom AG sold certain trade accounts receivable to a special purpose vehicle in a global assignment of debtors as part of its asset-backed securities transaction. This explains to a great extent the decrease in trade accounts receivable compared with the previous year. The contract explicitly rules out the retransfer of the receivables sold. The credit risks accepted by the purchaser are compensated by a corresponding discount. The remaining outstanding contract risk for Deutsche Telekom was agreed in a further discount. The contract provides for an interest bonus for both discounts if the risks covered by the discounts are ultimately not realized to the detriment of the purchaser. The receivables sold are still collected by Deutsche Telekom on behalf of the purchaser.

All receivables, with the exception of EUR 183 million, are due within one year.

The allowance for doubtful accounts and changes therein are as follows:

years	January 1	Charged to costs and expenses	Amounts written off/ released	December 31
	millions of €	millions of €	millions of €	millions of €
2001	790	821	(623)	988
2000	493	379	(82)	790
1999	371	173	(51)	493

Valuation allowances at Deutsche Telekom have increased due to bad debt losses, mainly as a result of the increase in doubtful accounts receivable in the carrier sector.

The Company directly wrote off accounts receivable balances of EUR 391 million and EUR 344 million in 2001 and 2000.

(17) Other assets

	Dec. 31, 2001	Dec. 31, 2000
	millions of €	millions of €
Tax receivables	3,287	2,262
Accrued interest	352	289
Receivables from employees	34	56
Receivables from reimbursements and loans receivable	221	286
Miscellaneous other assets	1,072	778
	4,966	3,671

The increase in other assets relates mainly to tax receivables, which consist mainly of income taxes. The change compared with the previous year is mainly due to a claim for reimbursement of corporate income tax resulting from the dividend payment of T-Mobile International AG to Deutsche Telekom AG.

The increase in miscellaneous receivables mainly relates to the capitalization of fair values of derivative transactions which qualify for hedges.

(18) Marketable securities

	Dec. 31, 2001 millions of €	Dec. 31, 2000 millions of €
Treasury shares	7	7
Other marketable securities	695	2,363
	702	2,370

The amount of treasury shares at the balance sheet date, 2,670,828, unchanged from the balance sheet date of the previous year, is made up as follows:

1996 Employee Stock Purchase Plan	459,900
1999 Employee Stock Purchase Plan	5,185,278
Decrease as a result of the 2000 Employee Stock Purchase Plan	(2,988,980)
Shares acquired from the KfW, not yet issued	14,630
	2,670,828

The shares are recorded in the balance sheet at acquisition cost of EUR 2.56 per share. The shares not purchased by employees in 2000 year (14,630) were initially shown in the balance sheet at acquisition cost of EUR 0.9 million and written down to the lower market trading price applicable at the balance sheet date. The total proportion of treasury shares in capital stock is 0.07%.

The decrease in other marketable securities compared with the previous year is mainly attributable to the sale of shares in Sprint Corporation, Kansas City.

Other marketable securities are primarily own bonds held (EUR 275 million) to maintain favorable trading conditions, callable step-up bonds (EUR 322 million) and Portuguese government bonds (EUR 55 million).

(19) Liquid assets

	Dec. 31, 2001 millions of €	Dec. 31, 2000 millions of €
Checks	47	12
Petty cash and deposits at the Bundesbank	25	41
Cash in banks (including deposits at Deutsche Postbank AG)	2,796	1,840
	2,868	1,893

	Dec. 31, 2001 millions of €	Dec. 31, 2000 millions of €
Cash and cash equivalents		
Original maturity less than 3 months	2,738	1,006
Temporary cash investments (original maturity longer than 3 months)	130	887
	2,868	1,893

Cash and cash equivalents with original maturity of less than 3 months consist primarily of fixed-term bank deposits, checking account balances, deposits at the Bundesbank and Deutsche Postbank AG and petty cash. Temporary cash investments consist almost exclusively of fixed-term bank deposits.

The change in the composition of the Deutsche Telekom group has an impact of EUR 381 million. The increase in cash in banks is mainly attributable to Deutsche Telekom's fixed-term bank deposit (EUR 1,069 million).

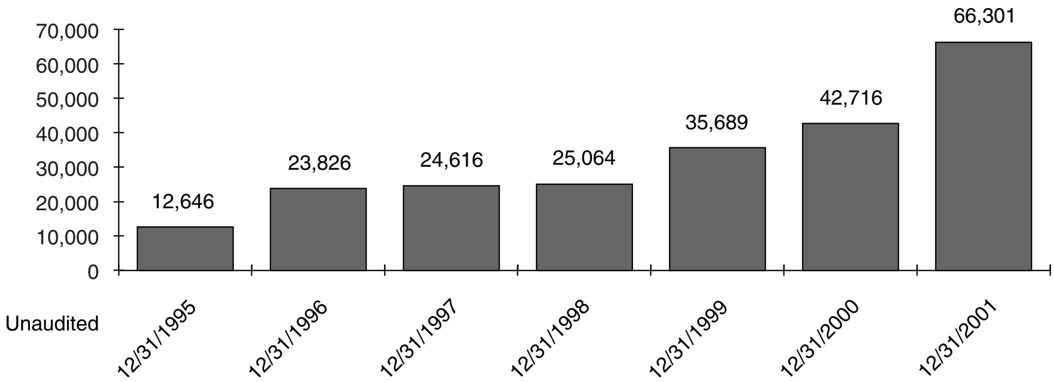
(20) Prepaid expenses, deferred charges and deferred taxation

Prepaid expenses and deferred charges of EUR 813 million and EUR 956 million in 2001 and 2000 include discounts on loans of EUR 351 million and EUR 59 million in 2001 and 2000 which are amortized on a straight line basis over the terms of the respective liabilities. Of the total amount, EUR 151 million relates to the consolidation of VoiceStream for the first time and EUR 146 million to DeTe International Finance B.V. Other prepaid expenses and deferred charges are also shown for advance personnel costs and lease payments. In the previous year, a deferred tax asset of EUR 475 million was shown here after netting against deferred tax liabilities. In 2001 this item is shown — after netting against the higher deferred tax liabilities — under other accruals.

(21) Shareholders' equity

A detailed account of the development of the consolidated shareholders' equity for the years 2001, 2000 and 1999 is presented in a separate table before the notes to the consolidated financial statements.

The development of the consolidated shareholders' equity from December 31, 1995 to December 31, 2001 is as follows (millions of €):



(22) Capital stock

In accordance with Article 5 paragraph 1 of the Articles of Incorporation, Deutsche Telekom AG's capital stock totaled EUR 10,746 million at December 31, 2001, representing 4,197.8 million registered ordinary no par value shares. Each share entitles the holder to one vote.

The Federal Republic's direct shareholding in Deutsche Telekom, represented by the Federal Agency, was 30.92% at December 31, 2001; the KfW's shareholding was 12.13% at December 31, 2001. A total of 1,298 million individual no-par value shares of the capital stock were therefore held by the Federal Republic at December 31, 2001 and 509 million by the KfW. The remaining shares are widely held.

In the course of the acquisition of VoiceStream and Powertel, Deutsche Telekom granted options on Deutsche Telekom shares in exchange for the warrants in circulation between Deutsche Telekom and VoiceStream and Powertel at the time of the acquisition. The number of still outstanding options granted to VoiceStream and Powertel employees amounted to 24,593,297 at December 31, 2001.

The Board of Management has been authorized to increase the capital stock (share capital) with the approval of the Supervisory Board by up to a nominal € 3,865,093,163.52 and has exercised the authorization to the extent of 1,509,802,017 ordinary registered shares for non-cash contributions in the period up to May 25, 2005. The authorization may be used for partial amounts. The subscription right of shareholders is precluded. The Board of Management is authorized to determine the future content of share rights and the conditions for issuing shares with the approval of the Supervisory Board.

In connection with the Merger of Deutsche Telekom with VoiceStream and Powertel, the board of management has exercised this authorization to the extent of 1,168,148,391 Deutsche Telekom shares.

The Deutsche Telekom shareholders' meeting on May 29, 2001 passed the following resolutions:

1. The contingent capital increase of up to € 64,000,000 approved by the Shareholders' Meeting on May 25, 2000, for the purpose of issuing up to 25,000,000 new individual no par value registered shares was cancelled with respect to the nominal amount of € 61,378,762.24 and therefore continues to apply to the nominal amount of € 2,621,237.76. This contingent capital increase exclusively serves the purpose of issuing up to 1,023,921 new individual no par value registered shares in respect of which subscription rights were granted pursuant to the Deutsche Telekom Stock Option Plan (SOP) 2000 during the financial year then ended.

2. The Board of Management was authorized to conditionally increase the capital stock by up to EUR 500,000,000, divided into up to 195,312,500 shares (contingent capital). The contingent capital increase shall be implemented only to the extent that the holders and creditors of conversion rights or warrants exercise their conversion or option rights or holders or creditors obligated to convert convertible bonds fulfill their conversion obligation.

3. The capital stock (share capital) of the company was conditionally increased by up to € 307,200,000 by issuing up to 120,000,000 new individual no par value registered shares to enable the granting of stock options as part of the SOP 2001. The contingent capital increase exclusively serves the purpose of granting up to 120,000,000 options pursuant to the Deutsche Telekom Stock Option Plan 2001 to members of the Board of Management and other executives of the Company and second- and lower-tier affiliated companies.

4. Deutsche Telekom was empowered to purchase shares of the Company up to a maximum of 10% of the share capital, i.e., a total of no more than 302,960,403 shares. This may be done in order to introduce shares of the Company to foreign stock exchanges, to be able to offer shares to third parties in the context of mergers or acquisitions or acquiring interests therein, or to withdraw shares. The authorization may be exercised as a whole or in partial amounts and applies until November 19, 2002.

(23) Additional paid-in capital

The additional paid-in capital of the consolidated group exceeds by EUR 25,690 million the EUR 24,304 million additional paid-in capital of Deutsche Telekom AG. This is due to the recording of the new Deutsche Telekom shares issued in the course of the acquisition of VoiceStream and Powertel at their market value (EUR 28,680 million) instead of their nominal value (EUR 2,990 million), which is permitted in the consolidated financial statements.

(24) Retained earnings

In addition to the transfers made from Deutsche Telekom AG's net income from prior years, retained earnings include the consolidated group's share of the consolidated subsidiaries' net income or losses, provided they were generated by such subsidiaries since being included in the consolidated group, as well as a reserve for treasury shares held by the Company in accordance with § 272 paragraph 4 HGB. This item also includes the cumulative effects of consolidation entries from prior years. Translation adjustments are recorded in a separate component of retained earnings.

(25) Minority interest

Minority interest represents the minority shareholders' proportionate share of the equity of the consolidated subsidiaries and relates primarily to T-Systems ITS, T-Online International AG, Croatian Telecom, MATAV and Slovenské.

(26) Stock-based compensation

Deutsche Telekom AG

In 2000, Deutsche Telekom, for the first time, granted stock options to certain employees. On July 19, 2000, Deutsche Telekom used its authority under shareholders' resolutions adopted in May 2000 to grant 1,023,920.54 options in respect of 1,023,920.54 shares of its stock to participants in its stock option plan at an exercise price of EUR 62.69. The quoted fair market value of Deutsche Telekom's common stock as quoted on Frankfurt am Main Xetra on the grant date was EUR 60.40 per share. The options have an expiration date of July 19, 2005.

The option rights may not be exercised before the end of the qualifying period on July 19, 2002. The options may only be exercised when and if both the absolute and the relative performance target have each been exceeded at least once in the period from July 20, 2002 to July 18, 2005.

The absolute performance target is deemed achieved when the moving thirty-day average closing Frankfurt Xetra share price exceeds the exercise price by more than 20%.

The relative performance target is linked to the performance of the shares relative to the performance of the Dow Jones Euro Stoxx 50© Total Return index. The options may only be exercised if, following expiration of the two-year lock-up period, the performance of the shares, adjusted for dividends, options and other special rights (total shareholder return), exceed the performance of the Euro Stoxx 50© Total Return index measured on a moving thirty-day average basis.

Deutsche Telekom reserved the right, at its election, to settle the options through the payment of a cash amount (stock appreciation rights – SAR) instead of issuing new shares. The exercise of an SAR cancels the related option and the exercise of an option cancels the related SAR. No conversion decision to this effect was taken at December 31, 2001.

The weighted average remaining contractual life as of December 31, 2001 was 3.5 years.

In 2001, Deutsche Telekom granted additional stock options to certain employees. On August 13, 2001, Deutsche Telekom used its authority under the shareholders' resolutions adopted in May 2001 to grant 8,220,803.00 further options in respect of 8,220,803.00 shares of its stock to participants in its stock option plan at an exercise price of EUR 30.00. The quoted fair market value of Deutsche Telekom's common stock as quoted on Frankfurt am Main Xetra on the grant date was EUR 19.10 per share. The options have an expiration date of August 12, 2011.

Of the options granted, 50% may only be exercised after a period of two years, calculated from the day the options were granted. The remaining 50% of the options granted may only be exercised after period of three years after the day the options are granted.

The exercise price is payable upon exercise of the options. The exercise price per share is 120% of the reference price. The reference price corresponds to the non-weighted average of the closing prices of the T-Share in Xetra trading on the Deutsche Börse AG stock exchange in Frankfurt am Main (or a subsequent system in place of the Xetra system) over the last 30 trading days before granting of the options. If the average closing price calculated by this method is lower than the closing price of the T-Share in Xetra trading on the Deutsche Börse AG stock exchange (or a subsequent system) on the day of granting of the options, this closing price shall be taken as the reference price. The exercise price may not be lower than the lowest proportionate share in the capital stock per share. The reference price is the performance target.

The options are not transferable. A total of 120 million shares were reserved for future issuance under the plan. The weighted average remaining contractual life as of December 31, 2001 was 9.5 years.

The activities relating to the share options granted by Deutsche Telekom are as follows:

	Stock option plan 2000			
	2001		2000	
	Stock options (in thousands)	Weighted-average exercise price (€)	Stock options (in thousands)	Weighted-average exercise price (€)
Outstanding at beginning of year	1,022	62.69	n/a	n/a
Granted	0	—	1,024	62.69
Exercised	0	—	0	—
Forfeited	21	62.69	2	62.69
Outstanding at end of year	1,001	62.69	1,022	62.69
Exercisable at year-end	0	—	0	—

	Stock option plan 2001	
	Stock options (in thousands)	Weighted-average exercise price (€)
Outstanding at beginning of year	n/a	n/a
Granted	8,221	30.00
Exercised	0	—
Forfeited	2	—
Outstanding at end of year	8,219	30.00
Exercisable at year-end	0	—

Furthermore, Deutsche Telekom AG granted 169,695 Stock Appreciation Rights (SAR) to employees in countries in which it was not legally possible to grant stock options under terms similar to its stock option plan. Of these, all SARs granted remained outstanding at December 31, 2001.

VoiceStream

Before its acquisition on May 31, 2001, VoiceStream had granted stock options to its employees. On May 31, 2001, as a consequence of the acquisition, all unvested, outstanding options of VoiceStream employees were converted from VoiceStream options into Deutsche Telekom options at a conversion rate of 3.7647 per unvested, outstanding VoiceStream option. The Deutsche Telekom shares linked to these options are administered in a trust deposit account which has been set up for the benefit of holders of VoiceStream stock options. The exercise price for each share of Deutsche Telekom common stock corresponds to the applicable exercise price per share of VoiceStream common stock divided by 3.7647. Furthermore, no more options will be granted under any other VoiceStream stock option plans.

At December 31, 2001, 22.1 million shares were available for outstanding options for the 1999 Management Incentive Stock Option Plan (“MISOP”), which was changed as a consequence of the acquisition on May 31, 2001. The MISOP provides for the issue of up to 8 million shares of Deutsche Telekom common stock, either as non-qualified stock options or as incentive stock options, plus the number of shares of common stock deliverable upon the exercise of the VoiceStream rollover options in accordance with the Agreement and Plan of Merger between Deutsche Telekom and VoiceStream. The vesting period and option term relating to the option plan are determined by the MISOP administrator. The options typically vest for a period of four years and have a term of up to 10 years.

The activities relating to the share options granted since the acquisition of VoiceStream are as follows:

	June 1 to December 31, 2001	
	Stock options (in thousands)	Weighted-average exercise price (US$)
Outstanding at the time of consolidation	24,278	15.36
Granted	—	—
Exercised	1,639	3.21
Forfeited	555	17.47
Outstanding at end of year	22,084	16.21
Exercisable at year-end	6,299	9.88

	Outstanding options			Exercisable options	
Ranges of the exercise prices in US$	Number (in thousands)	Weighted average remaining contractual life in years	Weighted-average exercise price in US$	Number (in thousands)	Weighted-average exercise price (US$)
0.00 - 7.60	7,515	6.0	2.66	3,828	2.44
7.61 - 15.20	2,875	6.3	8.47	953	8.60
15.21 - 22.80	85	7.7	17.58	38	17.59
22.81 - 30.39	10,056	8.5	26.26	1,100	29.34
30.40 - 37.99	1,553	8.3	30.98	380	30.98
0.00 - 37.99	22,084	7.4	16.21	6,299	9.88

Powertel

Before its acquisition on May 31, 2001, Powertel had granted stock options to its employees. On May 31, 2001, as a consequence of the acquisition, all unvested, outstanding Powertel options were converted into Deutsche Telekom options at a conversion rate of 2.6353. The Deutsche Telekom shares linked to these options are administered in a trust deposit account set up for the benefit of holders of Powertel stock options. The exercise price for each share of Deutsche Telekom common stock corresponds to the applicable exercise price per share of Powertel common stock divided by 2.6353. Furthermore, no more options will be granted under any other Powertel stock option plans.

The Powertel 2000 Stock Plan had 660,310 shares available at December 31, 2001. This plan was changed as a consequence of the acquisition. Under the terms of this plan, all employees, managers, directors, consultants and advisors may be eligible for the allocation of options, conditional share allocations or other allocations within the framework of the 2000 Stock Plan.

A total of 1,821,943 Deutsche Telekom shares were available for outstanding options at December 31, 2001 for the Powertel Employee Stock Option Plan in force since 1991 (''1991 Option Plan''). The Powertel Board of Directors has decided not to grant any further options in the 1991 Option Plan.

At December 31, 2001, 26,560 shares were available for outstanding options for the Non-employee Stock Option Plan (''Non-employee Plan''). The Powertel Board of Directors has decided not to grant any further options in the Non-employee Plan.

The activities relating to the share options granted since the acquisition of Powertel are as follows:

	June 1 to December 31, 2001	
	Stock options (in thousands)	Weighted-average exercise price (US$)
Outstanding at the time of consolidation	5,323	20.04
Granted	—	—
Exercised	1,200	6.29
Forfeited	1,614	31.42
Outstanding at end of year	2,509	19.50
Exercisable at year-end	883	8.76

	Outstanding options			Exercisable options	
Ranges of the exercise prices in US$	Number (in thousands)	Weighted average remaining contractual life in years	Weighted-average exercise price in US$	Number (in thousands)	Weighted-average exercise price (US$)
0.02 - 7.60	994	5.9	5.42	663	5.32
7.61 - 15.20	175	6.4	9.94	108	9.46
15.21 - 22.80	32	7.9	19.52	10	18.85
22.81 - 30.39	627	8.3	26.84	67	26.34
30.40 - 38.00	681	8.0	35.74	35	35.52
0.02 - 38.00	2,509	7.1	19.50	883	8.76

T-Online International AG

Stock option plan 2000

In 2000, T-Online, for the first time, granted stock options to certain employees in the Group. On July 6, 2000, T-Online used its authority under shareholders' resolutions adopted in March 2000 to grant 214,472.52 options in respect of 214,472.52 shares of its stock to participants in its stock option plan at an exercise price of EUR 37.65. The options have an expiration date of July 6, 2005. At December 31, 2000 a total of 20,000,000 million shares were reserved as contingent capital for future issuance under the plan. This contingent capital increase was reduced to EUR 214,473.00 at the shareholders' meeting on May 30, 2001. The weighted average remaining contractual life as of December 31, 2001 was 3.5 years.

The option rights may not be exercised before the end of the qualifying period on July 6, 2002. The options may only be exercised when and if both the absolute and the relative performance target are each exceeded at least once in the period from July 7, 2002 to July 6, 2005. The absolute performance target is deemed achieved when the moving thirty-day average closing Frankfurt Xetra share price exceeds the exercise price by more than 40%.

The relative performance target is linked to the performance of the shares relative to the performance of the Dow Jones Euro Stoxx Telecom© index. The options may only be exercised if, following expiration of the two year lock-up period, the performance of the shares, adjusted for dividends, options and other special rights (total shareholder return), exceed the performance of the Euro Stoxx Telecom© index by more than 20% measured on a moving thirty-day average basis.

The activities relating to the share options granted by T-Online International AG as part of the 2000 Stock Option Plan (in thousands) are as follows:

	Stock option plan 2000			
	2001		2000	
	Stock options	Weighted-average exercise price	Stock options	Weighted-average exercise price
	(in thousands)	(€)	(in thousands)	(€)
Outstanding at beginning of year	2,041	3.27	n/a	n/a
Granted	—	—	214	37.65
Granted in conjunction with the Ya.com acquisition*	—	—	1,864	0.00
Exercised	692	0.00	—	—
Forfeited	148	15.26	37	37.65
Outstanding at end of year	1,201	3.67	2,041	3.27
Exercisable at year-end	—	—	280	0.00

* In addition to the shares issued in connection with the purchase business combination of Ya.com Internet Factory, S.A. (Ya.com), T-Online agreed to issue an additional 1,863,886 T-Online options to Ya.com employees. Under the terms of the purchase agreement, 15% vested immediately upon closing. An additional 41.1% vest ratably over a three-year period from the closing date (1/3 at each anniversary date). The remaining 42.8% vest in the event that certain performance obligations have been met. In the event employees leave Ya.com, they forfeit all unvested options.

Stock option plan 2001

The T-Online shareholders' meeting on May 30, 2001 conditionally increased the capital stock of T-Online International AG by EUR 51,000,000 for the 2001 plan and authorized the Supervisory Board to grant options to the members of the Board of Management of T-Online International AG and authorized the Board of Management to grant options to managers below the Board of Management. These include directors, senior managers, selected specialists at T-Online International AG and members of the Board of Management, members of the management and other directors, senior managers and selected specialists at Group companies within and outside Germany in which T-Online International AG directly or indirectly holds a majority shareholding.

The stock option plan is structured as a "premium priced plan". The exercise price is payable upon exercise of the options. The exercise price per share is 125% of the reference price. The reference price corresponds to the non-weighted average of the closing prices of the T-Online share in Xetra trading on the Deutsche Börse AG stock exchange in Frankfurt am Main (or a subsequent system in place of the Xetra system) over the last 30 trading days before granting of the options. If the average closing price calculated by this method is lower than the closing price of the T-Share in Xetra trading on the Deutsche Börse AG stock exchange (or a subsequent system) on the day of granting of the options, this closing price shall be taken as the reference price.

Options are granted in annual tranches for periods of five years; stock options can be granted for last time in 2005.

50% of the options granted may only be exercised after period of two years — calculated from the day the options are granted. The remaining 50% of the options granted may only be exercised three years after the day the options are granted. The options have a life of ten years from the date of granting, meaning that the options are forfeit without replacement or compensation on August 12, 2011 at the latest. The weighted average remaining contractual life as of December 31, 2001 was 9.5 years.

Based on this authorization, the first tranche was granted on August 13, 2001. The exercise price as the performance target is EUR 10.35 (125% of the reference price of EUR 8.281).

The activities relating to the share options granted by T-Online International AG as part of the 2001 Stock Option Plan are as follows:

	Stock option plan 2001	
	2001	2001
	Stock options	Weighted-average exercise price
	(in thousands)	(€)
Outstanding at beginning of the year	—	—
Granted	2,369	10.35 €
Exercised	—	—
Forfeited	21	10.35 €
Outstanding at end of year under review	2,348	10.35 €
Exercisable at year-end	—	—

Stock options granted in the course of a contingent capital increase are shown in the balance sheet at the date the options are exercised, not at the date they are granted. No share options had been exercised at the balance sheet date. This therefore incurred no personnel costs for the company in the 2001 financial year. This does not apply for shares which were transferred to Ya.com employees in the course of the acquisition of Ya.com.

(27) Pensions and similar obligations

The pension obligations of Deutsche Telekom for non-civil servants are provided for by a range of defined benefit plans; there are further obligations under Article 131 of the Basic Law (Grundgesetz – GG). Deutsche Telekom's indirect pension obligations were made to its employees via the Versorgungsanstalt der Deutschen Bundespost (VAP) and the Deutsche Telekom Betriebsrenten-Service e.V. (DTBS).

The VAP provides pension services for pensioners who were employed as salaried workers by Deutsche Telekom. The VAP benefits, which supplement national social security retirement benefits up to the level specified in the pension benefits formula, are generally calculated on the basis of the level of employee compensation during specific periods of employment. Within the scope of negotiations on the realignment of the company pension plan, the employer and the trade unions agreed in 1997 on arrangements for the protection of vested VAP benefits. Pursuant to this agreement, the benefit obligations due to retirees and employees approaching retirement will remain unchanged. In the case of younger employees with vested benefits, the obligations were converted into an initial amount reflecting the number of years covered. This amount will be credited to a capital account held by the employer (cash balance plan). Deutsche Telekom credits further amounts to this account; when the insured event occurs, the account balance will be paid out in full, in installments or converted into a pension. If the relevant employees had not reached the age of 35 and had been insured for less than ten years, their benefit obligations are due directly from Deutsche Telekom. The DTBS was founded for processing the remaining obligations.

A new regulation of VAP benefits was made by collective agreement in the year 2000 without affecting obligations. The pensioners covered by this collective agreement no longer receive their pension payments directly from the VAP as the provider of pension services, but, since November 2000, directly and with a legal claim from Deutsche Telekom. The obligations of the VAP are thus suspended (parallel obligation). The VAP provides pension services for and on behalf of Deutsche Telekom. Pension accruals are made in the balance sheet for financial reporting purposes for the now direct pension obligations in accordance with U.S. GAAP SFAS 87. Due to the direct nature of the parallel obligation, these pension accruals have been shown in the balance sheet for tax reporting purposes, valued according to § 6a of the Income Tax Act. Those pensioners remaining in the VAP continue to receive their benefits directly from the VAP as the provider of pension services.

Benefits relating to other direct pension plans are generally determined on the basis of salary levels and years of service; these benefit obligations are also usually determined by the amounts credited by Deutsche Telekom to its capital accounts.

The following table shows the composition of pension obligations:

	Dec. 31, 2001 millions of €	Dec. 31, 2000 millions of €
Pension obligations:		
— Direct	2,683	2,497
— Indirect	966	820
Obligations under Article 131 GG	12	13
	3,661	3,330

The obligation amount shown for 2001 contains an "additional minimum liability" for individual pension plans. An additional minimum liability is a step-up amount for pension obligations relating to individual pension plans, to be shown under HGB as affecting net income, but under U.S. GAAP these amounts are reflected as a component of shareholders' equity. Excluding the additional minimum liability, the accrual for pensions amounts to EUR 3,402 million.

	Dec. 31, 2001 millions of €	Dec. 31, 2000 millions of €
Actuarial present value of benefits:		
Vested	3,701	3,227
Nonvested	342	415
Accumulated benefit obligation	4,043	3,642
Effect of projected future salary increases	121	122
Projected benefit obligation	4,164	3,764
Plan assets at fair value	(405)	(379)
Projected benefit obligations in excess of plan assets	3,759	3,385
Unrecognized net (losses) gains	(357)	(55)
Unfunded Accrued Pension Cost	3,402	3,330
Additional minimum liability	259	—
Total obligation	3,661	3,330

Taking into consideration the assets transferred to other entities, the pension obligations were recorded in full in the balance sheet.

The corresponding pension accruals measured in accordance with § 6a of the Income Tax Act (Einkommensteuergesetz – EStG) are EUR 2,995 and 3,119 million in 2001 and 2000, respectively.

The amount of pension obligations was determined using actuarial principles that are consistent with U.S. GAAP SFAS No. 87 and using the assumptions at the respective balance sheet dates as shown in the following table:

	2001	2000	1999
Discount rate	6.00%	6.25%	6.25%
Projected salary increase	2.75%-3.50%	2.75%-3.50%	2.75%-3.50%
Expected return on assets	6.00%	6.00%-6.50%	4.50%-6.00%
Projected pension increase	1.50%	1.50%	1.50%

Development of the projected benefit obligation:

	2001	2000
	millions of €	millions of €
Projected benefit obligation, beginning of year	3,764	3,389
Service cost	144	119
Interest cost	228	208
Change in obligations	(6)	179
Actuarial (gains)/losses	280	87
Total benefits actually paid	(246)	(218)
Projected benefit obligation, end of year	4,164	3,764

Development of plan assets at fair value:

	2001	2000
	millions of €	millions of €
Plan assets at fair value, beginning of year	379	320
Actual return on plan assets	2	9
Contributions by employer	73	232
Benefits actually paid through pension funds	(49)	(182)
Plan assets at fair value, end of year	405	379

Net periodic pension cost is summarized as follows:

	2001	2000	1999
	millions of €	millions of €	millions of €
Service cost	144	119	83
Interest cost	228	208	194
Expected return on assets			
Return on plan assets	(24)	(17)	(12)
Net periodic pension cost	348	310	265

Civil servant retirement arrangements

In accordance with the provisions of the Posts and Telecommunications Reorganization Act (PTNeuOG), Deutsche Telekom makes pension and allowance payments via a pension fund to retired employees and their surviving dependents who are entitled to pension payments as a result of civil servant status. The level of Deutsche Telekom AG's payment obligations to this special pension fund is defined under § 16 of the Law concerning the Legal Provisions for the Former Deutsche Bundespost Staff (PostPersRG). Deutsche Telekom AG is legally obligated as of 2000 to make an annual contribution to the special pension fund of 33% of the gross remuneration of active civil servants and the gross remuneration of civil servants on temporary leave entitled to pension payments. These contributions amounted to EUR 845 million, EUR 895 million and EUR 1.5 billion in 2001, 2000 and 1999, respectively. A fixed annual contribution of EUR 1.5 billion was payable for the years 1995 through 1999, see footnote (33).

Under PTNeuOG, the Federal Republic compensates the special pension fund for differences between the ongoing payment obligations of the special pension fund, amounts received from Deutsche Telekom AG and returns on assets, and guarantees that the special pension fund is always in a position to fulfill the obligations it has assumed. The Federal Republic cannot require reimbursement from Deutsche Telekom AG for amounts paid by it to the special fund.

Until 2000, Deutsche Telekom AG maintained a special pension fund (Unterstützungskasse) for its active and former civil servants, which was merged with the special pension funds of Deutsche Post AG and Deutsche Postbank AG by notarized agreement on December 7, 2000 to form the joint pension fund Bundes-Pensions-Service für Post und Telekommunikation e.V. (BPS-PT). The fund was entered in the Register of Associations on January 11, 2001, backdated to July 1, 2000. The BPS-PT works for the funds of all three companies and also handles the financial administration for the Federal Republic on a trust basis. All transactions for pension and allowance payments are made for the companies Deutsche Post AG, Deutsche Postbank AG and Deutsche Telekom AG.

(28) Other accruals

	Dec. 31, 2001	Dec. 31, 2000
	millions of €	millions of €
Taxes	1,938	1,470
Provisions for deferred taxes	5,348	0
Accruals other than taxes		
Employee benefits		
Civil Service Health Insurance Fund	1,079	1,028
Personnel restructuring	209	149
Other obligations	959	803
	2,247	1,980
Outstanding invoices	2,218	1,855
Loss contingencies	514	94
Unused telephone units on phone cards sold	422	363
Advertising cost subsidies/commissions	270	168
Litigation risks	266	293
Restoration commitments	265	239
Risks related to real estate	168	508
Investment risks	145	355
Refunds to be granted	132	131
Loss contingencies, subletting	89	88
Deferred maintenance	56	49
Other	688	462
	7,480	6,585
	14,766	8,055

Intangible assets for mobile communications licenses were realized upon first consolidation of VoiceStream and Powertel with the accounting of the purchase price. This generated a provision for deferred taxes of EUR 5,812 million. As a result of this considerable increase in deferred taxes, the consolidated financial statements show a balance of deferred taxes on the liabilities side under provisions for deferred taxes of EUR 5,348 million. Deferred tax assets of EUR 475 million were shown in 2000.

The increase in accruals (excluding deferred taxes) is mainly attributable to the changes in the composition of the Deutsche Telekom group, in particular the consolidation for the first time of VoiceStream and Powertel, RadioMobil and Croatian Telecom. These three companies recorded other accruals of EUR 1,088 million at December 31, 2001.

The Civil Service Health Insurance Fund (PbeaKK) provides healthcare and medical benefits for its members and their relatives employed by Deutsche Telekom along with Deutsche Post AG and Deutsche Postbank AG. When Postreform II came into effect, the PbeaKK was closed to new members. Due to the aging of the group of people insured, there is an expected shortfall between the fund's sources of regular income and benefits paid. Deutsche Telekom AG is obligated under the Post Reform II Act to pay for any operating cost shortfalls of the PbeaKK related to its civil servants and has accrued the actuarially determined present value of this future deficit which Deutsche Telekom has to cover, taking the new 1998 life expectancy tables by Prof. Dr. Klaus Heubeck (''Richttafeln 1998'') into account, which primarily reflect the increase in average life expectancy. Deutsche Telekom expensed EUR 70 million, EUR 142 million and EUR 137 million for costs incurred related to the PbeaKK in 2001, 2000 and 1999, respectively.

Deutsche Telekom had, in response to competition, announced its intention to reduce its workforce by approximately 60,000 to 170,000 full-time equivalent employees by the end of the year 2000 (excluding employees of subsidiaries first consolidated after January 1, 1995) through natural attrition, early retirement and other programs. The planned reductions included an estimated 38,300 non-civil servants expected to leave under voluntary separation agreements. The personnel restructuring program has now been completed. There are, however, still contracts originating from this time which have to be completed. On the other hand, collective agreements in particular are still used for bridging allowances and old-age part time work and lead to the establishment of new accruals when a concrete contractual relationship is entered into.

In 2000, as was the case in prior years, civil servants as well as non-civil servants accepted the Company's offer for early retirement and severance. The early retirement program for civil servants and natural attrition do not result in incremental costs for Deutsche Telekom AG. In 2001, unpaid restructuring costs amounting to EUR 209 million are included in accruals and EUR 6 million are included in other accounts payable.

The table below sets forth the payments made and the related accruals/payables for future payments in respect of these staff reduction measures for the years 2001 and 2000:

	2001	2000
	millions of €	millions of €
Accruals/payables, beginning of year	150	261
Payments made (including payments made against accruals/payables)	(125)	(156)
Establishment of new accruals/payables	190	45
Accruals/payables, end of year	215	150

Of the increase in accruals for loss contingencies, EUR 325 million relates to accruals for debt premiums at VoiceStream and Powertel, which result from the difference between the repayment amount and the higher fair value of bonds.

The accruals for unused telephone units on phone cards sold are made for payments received for telephone services but for which services have not yet been performed. The increase compared with 2000 is a result of the consolidation of VoiceStream and Powertel.

(29) Liabilities

	Dec. 31, 2001				Dec. 31, 2000			
		of which due				of which due		
	Total	within one year	in one to five years	after five years	Total	within one year	in one to five years	after five years
		millions of €				millions of €		
Debt								
Bonds and debentures	58,301	12,598	28,447	17,256	51,344	12,774	27,669	10,901
Liabilities to banks	8,730	754	4,984	2,992	9,013	2,438	1,772	4,803
	67,031	13,352	33,431	20,248	60,357	15,212	29,441	15,704
Other								
Advances received	371	357	14	—	297	297	—	—
Trade accounts payable	4,827	4,792	35	—	4,029	3,936	93	—
Liabilities on bills accepted and drawn	1	1	—	—	1	1	—	—
Payables to subsidiaries	104	103	1	—	24	24	—	—
Liabilities to other companies in which an equity interest is held	152	152	—	—	74	65	—	9
Other liabilities	6,565	5,243	355	967	4,705	3,642	199	864
of which: from taxes	(2,200)	(2,200)	—	—	(679)	(679)	—	—
of which: from social security	(131)	(131)	—	—	(109)	(109)	—	—
	12,020	10,648	405	967	9,130	7,965	292	873
Total liabilities	79,051	24,000	33,836	21,215	69,487	23,177	29,733	16,577

The main items under bonds and debentures are old bonds issued by Deutsche Bundespost amounting to EUR 25.5 billion and a global bond issued in the second half of 2000. This bond, issued by Deutsche Telekom International Finance B.V. Amsterdam (DT Finance), amounting to EUR 15.4 billion, is structured as follows:

Tranche	Nominal amount in currency	Nominal amounts in €	Interest rate	Maturity
EUR	2,250,000,000	2,250,000,000	6.125%	2005
EUR	750,000,000	750,000,000	6.625%	2010
GBP	625,000,000	1,026,104,088	7.125%	2005
GBP	300,000,000	492,529,962	7.125%	2030
USD	3,000,000,000	3,400,242,551	7.750%	2005
USD	3,000,000,000	3,400,242,551	8.000%	2010
USD	3,500,000,000	3,966,949,642	8.250%	2030
JPY	90,000,000,000	777,944,681	1.500%	2005

DT Finance issued a eurobond for EUR 8 billion in 2 tranches in 2001:

Tranche 1 for EUR 4.5 billion (5.875%) has a maturity of 5 years and is to repay medium-term notes (MTN) in the DT Finance debt issuance program and to repay other bond obligations of Deutsche Telekom AG.

Tranche 2 for EUR 3.5 billion (6.625%) has a maturity of 10 years. If Deutsche Telekom AG is downgraded by the rating agencies S&P and Moody's to BBB level, the coupon of the global bond and the eurobond will increase by 0.5% for the next interest period. In the same way, the coupon will be reduced to the original interest rate if Deutsche Telekom AG is promoted back to A– level.

DT Finance is a wholly owned finance subsidiary of Deutsche Telekom and the bonds issued by DT Finance are fully and unconditionally guaranteed by Deutsche Telekom.

Breakdown of bonds and debentures in millions of Euros as follows:

Effective interest rate	up to 6%	up to 7%	up to 8%	up to 9%	over 9%	Total
Due in						
2002	4,726	—	5,317	2,555	—	12,598
2003	2,828	2,556			94	5,478
2004	1,157	3,068	6,212	156	—	10,593
2005	778	2,250	4,427	—	—	7,455
2006	4,921	—	—	—	—	4,922
after 2006	2,104	4,456	4,422	3,967	2,307	17,255
	16,514	12,330	20,378	6,678	2,401	58,301

Liabilities to banks (mainly loan notes and short-term loans) due in the next 5 years and thereafter are in millions of Euros as follows:

Due in	Amounts
2002	754
2003	810
2004	524
2005	3,465
2006	185
after 2006	2,992
	8,730

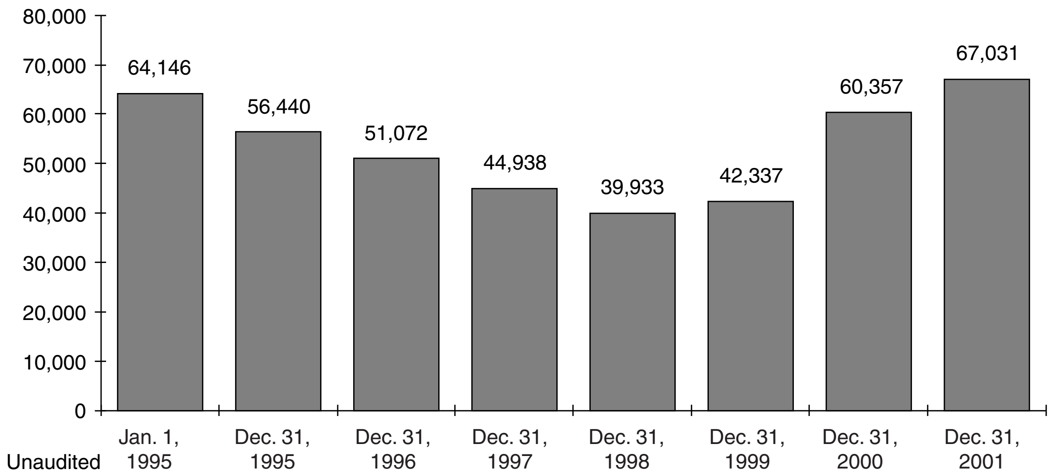
The average effective interest rate of total debt is for:

Bonds and debentures	6.81% p.a. (2000: 6.50% p.a.)
Liabilities to banks	5.82% p.a. (2000: 6.70% p.a.)

Deutsche Telekom and One 2 One entered into syndicated loan facilities in the amount of EUR 12 billion (the ''DT Syndicated Loan'') and EUR 4.5 billion (the ''DTMH Syndicated Loan''), respectively. Deutsche Telekom serves as guarantor of both syndicated loans. The interest rates and commitment fees on the syndicated loans vary based on Deutsche Telekom's debt rating and the respective syndicated loan's borrowing level and are based on LIBOR plus applicable margin ranging from 0.30% to 0.425%. At December 31, 2001, there were no borrowings outstanding on the DT Syndicated Loan. At December 31, 2001, EUR 4.01 billion was outstanding on the DTMH Syndicated Loan, due in the first quarter of 2002, and bearing an average interest rate and commitment fee of 4.73% representing LIBOR plus 0.38%, and 0.15%, respectively. The syndicated loans expire at various dates through October 2, 2007. Covenants in the syndicated loans include a limitation on Deutsche Telekom's ratio of EBITDA to Net Interest Payable. At December 31, 2001, approximately EUR 12 billion and EUR 0.5 billion of additional borrowings were available under the DT Syndicated Loan and the DTMH Syndicated Loan, respectively. An amount of EUR 5 billion of the DT Syndicated Loan supports a commercial paper arrangement.

Deutsche Telekom has committed lines of credit totaling EUR 9.6 billion through several unsecured revolving credit agreements with a group of banks. Borrowings under these revolving credit agreements at December 31, 2001 amounted to EUR 0.9 billion and bore a weighted average interest rate of 6.0%. The interest on borrowings is based upon the terms of each specific borrowing and is subject to market conditions. The majority of these agreements expire during the third quarter of 2002.

The development of debt from January 1, 1995 to December 31, 2001 is shown in millions of Euro as follows:



The Company's original debt was raised principally to finance the development of the communications networks in eastern Germany.

The reasons for the increase in debt in 2000 include the payments for UMTS licenses, the initial investment in VoiceStream and Powertel, the increase in the shareholding in MATAV and the acquisition of Slovenské and T-Systems ITS.

The increase in debt in 2001 is mainly attributable to the acquisition and consolidation for the first time of VoiceStream and Powertel.

Certain debt agreements contain affirmative and negative covenants, including financial covenants, and provide for various events of default. As of December 31, 2001, Deutsche Telekom and its subsidiaries were in compliance with these covenants. Additionally, certain subsidiaries of Deutsche Telekom are or may be subject to debt covenants that restrain the payment of dividends or the making of loans to Deutsche Telekom AG. With regard to non-wholly owned subsidiaries, agreements with minority shareholders or generally applicable principles of law relating to the rights of minority shareholders may in some instances inhibit the ability of Deutsche Telekom to compel the payment of dividends or making of loans to Deutsche Telekom AG. The ability of subsidiaries to pay dividends may be subject to limitations relating to the availability of sufficient retained earnings or other local law requirements of general applicability.

Other liabilities

	Dec. 31, 2001	Dec. 31, 2000
	millions of €	millions of €
Interest	1,586	1,558
Rental and leasing obligations	569	451
Loan notes	659	658
Liabilities to employees	153	183
Other	3,598	1,855
	6,565	4,705

Other liabilities include taxes of EUR 2,200 million and EUR 679 million in 2001 and 2000 and social security liabilities of EUR 131 million and EUR 109 million in 2001 and 2000.

Liabilities include borrowings of EUR 17,799 million and EUR 13,818 million in 2001 and 2000 for foreign currency liabilities.

Liabilities in the amount of EUR 5,234 million and EUR 28 million in 2001 and 2000 payable by subsidiary companies to banks and third parties are collateralized. Deutsche Telekom AG has provided no collateral against these liabilities.

In accordance with Postreform II (§ 2 paragraph 4 of the Stock Corporation Transformation Act — Postumwandlungsgesetz), the Federal Republic is guarantor of all Deutsche Telekom AG's liabilities which were outstanding at January 1, 1995.

Notes to the consolidated statement of cash flows

The consolidated statement of cash flows has been prepared in conformity with International Accounting Standard (IAS) No. 7, Cash Flow Statements. Besides IAS 7, German Accounting Standard (DRS) No. 2, cash flow, as approved by the German Standardization Council (DSR), is also used in preparing the consolidated statement of cash flows.

Liquid assets and short-term investments with original maturities of less than 3 months at the date of purchase are considered cash equivalents in drawing up the consolidated statement of cash flows. These current cash and cash equivalents increased by EUR 1,732 million to EUR 2,738 million in 2001.

(30) Net cash provided by operating activities

Net cash provided by operating activities amounted to EUR 11,934 million in 2001. This represents an increase of EUR 1,934 million over the previous year. Taking into consideration the increase in net interest payments of EUR 1,391 million, cash generated from operations increased by EUR 3,325 million or 25.7% to EUR 16,271 million. The result for the Group is EUR 9,327 million lower than in the previous year, but the positive result in 2000 was influenced to a considerable extent by transactions which are assigned to net cash provided by financing activities (proceeds from the acquisition of new shareholders in the course of the initial public offering of T-Online of approximately EUR 2.7 billion) or net cash used for investing activities (sale of shares in Global One (EUR 2.9 billion) and the sale of shares in the cable companies in North-Rhine Westphalia and Hesse (EUR 3.0 billion)) or had not yet had any effect on cash flows (proceeds from the sale of WIND for EUR 2.3 billion).

Correspondingly, the proceeds from the sale of Sprint shares in 2001 (EUR 1.9 billion), the sale of the cable business in Baden Württemberg (EUR 0.9 billion) and the sale of receivables (ABS transactions) for EUR 1.4 billion are allocated to net cash used for investing activities and thus also have no effect on net cash provided by operating activities. In addition, the Group's results were burdened by an increase of EUR 2,230 million in depreciation and amortization compared with the previous year, which have no effect on cash flows. Furthermore, in contrast to 2000, no income taxes were paid in 2001 although income tax expense was considerably higher than in the previous year.

(31) Net cash used for investing activities

Net cash used for investing activities decreased in 2001 by EUR 22.3 billion to EUR 5.4 billion. The considerably higher level of net cash used for investing activities in the previous year was mainly attributable to the large payment for the acquisition of UMTS licenses in the United Kingdom, Germany and Austria amounting to a total of EUR 15.3 billion and the acquisition of shareholdings. Payments totaling EUR 5.7 billion were made in 2001 for the acquisition of fully consolidated companies, in particular VoiceStream and Powertel.

	Purchase price	Acquired liquid Assets	Net outflow
		(billions of €)	
VoiceStream and Powertel	5.1	(1.0)	4.1
RadioMobil	0.6	—	0.6
Croatian Telecom	0.5	(0.1)	0.4
Maktel	0.3	—	0.3
Other	0.3	—	0.3
			5.7

In addition, Deutsche Telekom invested EUR 11.4 billion in noncurrent assets. This is offset by divestments of EUR 4.9 billion, of which EUR 2.7 billion relates to the sale of shares in WIND. The Group also received EUR 1.0 billion from the sale of fully consolidated companies, EUR 0.9 billion of which related to the sale of cable activities in Baden Württemberg alone. The sale of receivables (EUR 1.4 billion) and the change in cash and cash equivalents (greater than three months to maturity) and marketable securities (EUR 4.4 billion) also had a positive effect on net cash used for investing activities, of which EUR 3.4 billion relates to the sale of shares in Sprint. The issue of 1.2 billion new T-Shares (market value of EUR 28.7 billion) as part of the purchase price for the acquisition of VoiceStream and Powertel is to be reported as a major transaction which did not lead to a change in the cash levels (cash-less transaction).

(32) Net cash provided by (used in) financing activities

Net cash provided by (used in) financing activities shows a net cash outflow of EUR 4.8 billion, compared with an inflow of EUR 17.9 billion in the previous year. Debt was decreased in the period under review by EUR 2.9 billion, compared with an increase of EUR 16.5 billion in 2000. Whereas there were no equivalent inflows from capital increases in 2001, the Group also received liquid assets of EUR 3.1 billion from the initial public offering of T-Online alone in 2000. There was an outflow of liquid assets of EUR 1.9 billion from the payment of dividends in 2001, unchanged from the previous year.

Other information

(33) Guarantees and commitments and other financial obligations

Guarantees and commitments

	Dec. 31, 2001	Dec. 31, 2000
	millions of €	millions of €
Guarantees	224	35
Liabilities arising from warranty agreements	66	81
Collateral granted against third party liabilities	—	49
	290	165

The increase relates mainly to guarantees given by T-Mobile International AG for Belgacom N.V./S.A., Belgium (EUR 134 million), and Tele Danmark A/S, Denmark (EUR 56 million) to hedge loans granted to Ben Nederland Holding B.V., Netherlands.

Otherwise, guarantees and commitments serve Deutsche Telekom’s day-to-day business activities.

Other financial obligations

	Dec. 31, 2001			Dec. 31, 2000		
		of which due			of which due	
	Total	in the following financial year	from second year after the balance sheet date	Total	in the following financial year	from the second year after the balance sheet date
	millions of €	millions of €	millions of €	millions of €	millions of €	millions of €
Present value of payments to special pension fund	9,372	845	8,527	9,935	912	9,023
Purchase commitments for interests in other companies	6,872	5,022	1,850	8,345	1,144	7,201
Obligations under rental and lease agreements	6,839	1,269	5,570	5,607	1,020	4,587
Purchase commitments for capital projects in progress including obligations arising from future expenditure	3,201	3,142	59	3,911	2,017	1,894
Commitments arising from transactions not yet settled	444	315	129	473	192	281
Total other financial obligations	26,728	10,593	16,135	28,271	5,285	22,986

The present value of payments required to be made by Deutsche Telekom AG on the basis of the life expectancy tables by Prof. Dr. Klaus Heubeck (“Richttafeln 1998”), in accordance with Postreform II, to the special pension fund for civil servants or its successor amounted to EUR 9,372 million at December 31, 2001, of which EUR 3.9 billion relates to the future payments for pensions of civil servants.

Purchase commitments for interests in other companies relate mainly to the option of Daimler-Chrysler AG, Stuttgart, to sell Deutsche Telekom the remainder of its shares in T-Systems ITS GmbH, Leinfelden-Echterdingen, (EUR 4.7 billion); this option was exercised at the beginning of 2002.

The Shareholders’ agreement governing T-Mobile International’s ownership interest in Ben, includes both a call option held by T-Mobile International and put options held by the other owners of Ben. Both the call and put options allow for T-Mobile International to acquire all or a portion of the shares held by the other owners in Ben. The call option is exercisable in 2002, and the put options are exercisable in 2003, each at the option of the holding party. The exercise price of these options at December 31, 2001 was EUR 17.23 per share. The purchase price for the minimum number of shares, which can be acquired under these options, is EUR 25 million. The purchase price for the maximum number of shares, which can be acquired under these options, is EUR 1.7 billion. In the event that any of these options are exercised, T-Mobile International could have a controlling interest in Ben and would therefore consolidate its operations.

The Shareholders’ agreement governing T-Mobile International’s ownership interest in PTC Sp.z.o.o., includes a call option, whereby if a shareholder in PTC materially defaults on its responsibility under the shareholders’ agreement, the other shareholders may exercise an option to acquire the defaulting shareholder’s interest in PTC. Additionally, if a shareholder desires to sell its shares in PTC, the Shareholders’ Agreement provides for all shareholders to participate pro-rata to their then current shareholding in the PTC in the purchase of those shares. In 1999, a minority shareholder in PTC sold its shares. T-Mobile International’s pro-rata portion of the sold shares amounted to an additional 3.1269% ownership interest in PTC. T-Mobile International is currently in arbitration with another PTC shareholder over whether a default occurred relative to the sale of these shares. In the event the court of arbitration rules that a default has occurred in favor of T-Mobile International, T-Mobile International will have the ability to acquire the remaining outstanding shares in PTC, at PTC’s book value. In the event T-Mobile seeks to acquire only the additional 3.1269% interest in PTC, the cost of the incremental shares would be EUR 153 million at December 31, 2001.

The increase in obligations under rental and lease agreements relates mainly to the obligations of VoiceStream and Powertel, USA, which are consolidated for the first time.

The decrease in purchase commitments for capital projects in progress is mainly attributable to the decrease in purchase commitments.

The commitments arising from transactions not yet settled relate mainly to contractual obligations of T-Mobile International AG.

Litigation, Claims and Assessments

As previously reported, the Bonn public prosecutor is conducting an investigation (*Ermittlungsverfahren*) into allegations in the press and elsewhere asserting that the book values recorded by Deutsche Telekom for its real property portfolio have been improperly established and maintained under applicable accounting principles. Recently, the prosecutor orally advised Deutsche Telekom that he has expanded his investigation to include whether Deutsche Telekom's fixed assets in general, including technical equipment and machinery, were substantially overvalued in Deutsche Telekom's 1995 opening balance sheet and possibly in later balance sheets. Deutsche Telekom believes that the book values of its fixed assets have been correctly presented in accordance with applicable accounting principles, and disputes allegations to the contrary. Deutsche Telekom has nonetheless been cooperating fully in the investigation and is interested in seeing it expeditiously resolved. Deutsche Telekom cannot offer assurances as to the timing or outcome of the prosecutor's investigations. Deutsche Telekom believes that the investigation is being conducted with regard to certain individuals and is not directed against Deutsche Telekom itself. The public prosecutor has publicly identified Deutsche Telekom's former Chief Financial Officer, the former Chairman of the company's Supervisory Board and the current Chairman of its Management Board as being among the individuals under investigation. Adverse consequences for Deutsche Telekom could follow if any of the individuals who are or who become the subject of the investigation were found to have violated the law.

A number of purported class action lawsuits have been filed and consolidated in the United States District Court for the Southern District of New York by or on behalf of purported purchasers of Deutsche Telekom ADSs issued pursuant to a registration statement on Form F-3 filed with the Securities and Exchange Commission on May 22, 2000, and pursuant to a prospectus dated June 17, 2000, and purported purchasers of Deutsche Telekom ADSs during the period from June 19, 2000 to and including February 21, 2001. The operative complaint in these consolidated actions asserts claims against Deutsche Telekom and the Chairman of its Management Board, and others, under U.S. federal securities statutes based on allegations that statements made in the registration statement and prospectus were materially false and misleading because they allegedly failed adequately to disclose detailed information relating to merger negotiations between Deutsche Telekom and VoiceStream Wireless Corporation, and allegedly overstated the value of Deutsche Telekom's real estate portfolio.

Press reports indicate that various private parties in Germany have been evaluating measures that might be taken against Deutsche Telekom, its management, or both, on the basis of allegations in the press and elsewhere that the book values recorded by Deutsche Telekom for its real property portfolio have been improperly established and maintained under applicable accounting principles. Deutsche Telekom disputes these allegations. A number of purported shareholders have written to Deutsche Telekom raising claims for damages, and more than 230 lawsuits have been filed in Germany by purported purchasers of Deutsche Telekom shares issued pursuant to a prospectus dated May 26, 2000. In many of these lawsuits, claims have been made with respect to the VoiceStream transaction analogous to those made in the purported U.S. class action lawsuits described above.

Deutsche Telekom intends to contest each of the aforementioned lawsuits vigorously. Because the lawsuits, which in the aggregate involve substantial damage claims, are in their preliminary stages, Deutsche Telekom is not in a position to predict their outcome or impact. However, Deutsche Telekom believes that the allegations in the lawsuits do not provide a basis for the recovery of damages because all required disclosures were made on a timely basis.

Media reports have suggested that radio frequency emissions from wireless handsets and cell sites may raise various health concerns, including cancer, and may interfere with various electronic medical devices, including hearing aids and pacemakers. Research and studies are ongoing. Whether or not such research or studies conclude there is a link between radio frequency emissions and health, these concerns over radio frequency emissions may discourage the use of wireless handsets and may result in significant restrictions on the location and operation of cell sites, either or both of which could have a material adverse effect on VoiceStream's results of operations. VoiceStream is also subject to current, and potentially future, litigation relating to these health concerns. Several class action lawsuits have been filed against VoiceStream, several other wireless service operators and several wireless phone manufacturers, asserting products liability, breach of warranty and other claims relating to radio frequency transmissions to and from wireless handsets. The complaints seek substantial monetary damages as well as injunctive relief. The defense of these lawsuits may divert management's attention, and VoiceStream may be required to pay significant awards or settlement and may incur significant expenses in defending these lawsuits. In addition, VoiceStream could be subject to potential litigation, legislation or adverse publicity relating to damage caused by persons who use mobile telephones while driving.

In April 2001, QPSX Europe GmbH filed suit for a permanent injunction with the District Court in Munich (Landgericht München) against Deutsche Telekom AG and Siemens AG, alleging that these companies are infringing plaintiff's patent by providing services using Asynchronous Transfer Mode (ATM) technology. Since ATM technology is used in a number of products and services offered by Deutsche Telekom, an adverse outcome in this proceeding could have a substantial adverse effect on Deutsche Telekom's business.

On May 3, 1999, Western Wireless distributed its entire 80.1% interest in VoiceStream's common shares to its stockholders. Prior to this "spin-off," Western Wireless obtained a favorable ruling from the IRS indicating that the spin-off would not result in the recognition of gain or taxable income to Western Wireless or its stockholders. However, Western Wireless could still recognize gain upon the spin-off, notwithstanding the favorable IRS ruling, if it is determined that the spin-off was part of a "prohibitive plan," that is, a plan or series of related transactions in which one or more persons acquire, directly or indirectly, 50% or more of VoiceStream's stock. Acquisitions of 50% or more of VoiceStream's stock occurring during the four year period beginning two years before the spin-off could give rise to a rebuttable presumption that the spin-off was part of a prohibited plan. Although it is not assured, VoiceStream believes that the spin-off, the subsequent Omnipoint and Aerial mergers, certain investments by Hutchison and Sonera Corporation ("Sonera") and the T-Mobile merger were not pursuant to a "prohibitive plan."

(34) Financial instruments

Fair value

The fair value of a financial instrument is the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. The following is a summary of the estimated fair value of Deutsche Telekom's financial instruments:

	Dec. 31, 2001		Dec. 31, 2000	
	Fair value	Net carrying amount	Fair value	Net carrying amount
	millions of €	millions of €	millions of €	millions of €
Assets				
Other investments in related companies	2,024	1,895	8,325	7,456
Other long-term loans	534	534	562	562
Other investments in noncurrent securities	880	879	1,094	1,106
Receivables	6,826	6,826	7,159	7,159
Liquid assets	2,868	2,868	1,893	1,893
Other investments in marketable securities	702	702	3,963	2,370
Liabilities				
Bonds and debentures	59,171	58,301	52,203	51,344
Liabilities to banks	8,730	8,730	9,013	9,013
Other	12,020	12,020	9,130	9,130
Derivative financial instruments(1)				
Interest rate swaps	532	(34)	296	(46)
Interest rate caps/collars purchased	(3)	(1)	1	1
Cross currency interest rate swaps sold	(152)	270	(373)	44
Foreign currency forward contracts	(250)	(81)	163	(4)
Foreign currency options contracts	—	—	17	138

(1) Non-bracketed amounts represent assets, bracketed amounts represent liabilities.

Fair values were determined as follows:

The fair value of other investments in noncurrent securities and in marketable securities is based on quoted market prices for those instruments or similar instruments. The net carrying amount of other investments in marketable securities is adjusted to market value where market value is less than the original investment. The net carrying amounts of trade accounts receivable approximate their fair values, due to the short period to maturity. The net carrying amounts of liquid assets also reflect reasonable estimates of fair value due to the relatively short period to maturity of the instruments.

The fair value of debt which is publicly traded, primarily bonds and debentures, is estimated based on quoted market prices at year end. The book values of liabilities to banks, and other liabilities, approximate their fair values.

The fair value of off-balance sheet financial instruments generally reflects the estimated amount the Company would receive or pay to terminate the contracts at the reporting date, thereby taking into account the current unrealized gains and losses of open contracts. The estimated fair values of derivatives used to hedge or modify the Company's risk will vary substantially with future changes in interest rates or with fluctuations in foreign exchange rates. These fair values should not be viewed in isolation, but rather in relation to the fair values of the underlying hedged transactions and the overall reduction in the Company's exposure to adverse fluctuations in interest and foreign exchange rates.

The fair values of investments in associated and related companies, which have carrying values of EUR 2,372 million and EUR 8,231 million at December 31, 2001 and 2000, respectively, were not practicably determinable, except for the investments in New Skies Satellite, VocalTec and Secunet, because they are not publicly traded and cannot be sold due to contractual restrictions at this point in time. New Skies Satellite, VocalTec and Secunet are valued at their market values based on share prices.

Derivative financial instruments

The Company uses derivative financial instruments for the purpose of hedging interest rate and currency exposures which arise from its ongoing business operations. The Company's policy is to hold or issue derivative financial instruments to reduce or eliminate risk exposures instead of creating new risk. Derivative financial instruments are subject to internal controls.

Derivatives classified as hedging instruments are those entered into for the purpose of offsetting or eliminating risk from potential movements in interest rates and foreign exchange rates inherent in the Company's assets and liabilities. A derivative is designated as a hedge where there is an offset between the effects of potential movements in the derivative and designated underlying asset, liability or position being hedged. Such derivatives are reviewed regularly for their effectiveness as hedge instruments. Derivative instruments designated as hedges are accounted for on the same basis as the hedged item.

The Company uses interest rate swaps and cross currency interest rate swaps in particular to reduce its exposure to interest rate and market value volatility on certain debt issues and deposit instruments and to manage its interest expense by setting an agreed mix of floating and fixed-rate debt and deposit instruments per currency. Interest rate swaps are designated as hedging instruments for specific liabilities or groups of similar liabilities. Cross currency interest rate swaps usually swap foreign currency bonds or Medium-Term Notes in required target currencies.

Gains or losses related to changes in the value of interest rate swaps are generally not recognized. Interest rate swaps related to deposit instruments are marked to market and resulting negative values are accrued and included as a component of net interest expense; gains are recognized upon realization. Interest rate swaps which are not designated as hedging instruments for balance sheet assets and liabilities (which are mainly hedges of planned future transactions) are assigned to the interest instrument valuation portfolio. Unrealized gains and losses from changes in market value are netted currency for currency and resultant net losses are recognized as a component of net interest expense. The interest differential to be paid or received on interest rate swaps is recognized in the statement of operations, as incurred, as a component of net interest expense. Gains or losses on interest rate swaps terminated prior to their maturity are recognized currently in net interest expense.

The Company uses foreign currency forward contracts and foreign currency options purchased as well as cross currency interest rate swaps to reduce fluctuations in foreign currency cash flows related to capital expenditures and financial liabilities. Foreign currency forward contracts hedging firm commitments to invest in a foreign entity are not recognized at the balance sheet date. The investment in the purchased entity is capitalized using the foreign exchange rate fixed by the foreign currency forward contract. The Company purchases options to hedge firm commitments to invest in a foreign entity. A purchased option is included in other assets and measured at historical cost. Upon exercise of the option, the premium is included in the purchase cost of the asset.

Gains and losses resulting from foreign currency forward contracts, cross currency interest rate swaps and foreign currency financing which relate to the net investments in foreign entities are recorded in the cumulative translation adjustment account.

Foreign currency forward contracts hedging other payments and receipts are assigned to foreign currency portfolios categorized by foreign currency type with the related financial instruments. These portfolios are marked to market at the balance sheet date and resultant negative portfolio values are accrued under other liabilities. Valuation gains and losses are netted portfolio for portfolio. An accrual for loss contingencies is established for each portfolio for the amount of the excess loss. Excess gains are not recognized until the transaction is settled.

The forward foreign exchange contracts fix amounts the Company is required to pay in the future in EUR for a contractually fixed amount of foreign currency forward contracts and currency options.

The following is a summary of the contract or notional principal amounts outstanding at December 31, 2001 and 2000:

	Dec. 31, 2001		Dec. 31, 2000	
	Maturity	Notional Amount millions of €	Maturity	Notional Amount millions of €
Interest rate swaps (EUR)				
Receive fixed/pay variable	2002-2010	9,686	2001-2008	3,112
Receive variable/pay fixed	2002-2010	3,251	2005-2010	3,154
Interest rate swaps (US$)				
Receive fixed/pay variable	2002-2030	11,249	2002-2030	10,670
Receive variable/pay fixed	2002-2008	595	2002-2008	457
Interest rate swaps (GBP)				
Receive variable/pay fixed	2002-2030	9,243	2002-2030	10,517
Forward receive variable/pay fixed	2004-2005	1,642	—	—
Interest rate swaps (JPY)				
Receive fixed/pay variable	2005	778	2005	842
Interest rate swaps (CZK)				
Receive fixed/pay variable	2004	13	—	—
Interest rate caps/collars purchased	2002-2003	400	2002-2003	434
Cross currency interest rate swaps sold	2002-2030	15,129	2001-2030	16,243
Foreign currency forward contracts				
Forward purchases	2002-2008	229	2001	754
Forward sales	2002-2004	12,336	2001-2003	8,434
Currency options	2002	15	2001-2002	4,845

The terms of the EUR-receive fixed, pay variable interest rate swaps provide for Deutsche Telekom to receive interest at fixed rates (weighted average 4.7% per annum) and pay interest at variable rates (generally based on the six-month EURIBOR rate). The terms of the EUR-receive variable, pay fixed interest rate swaps provide for Deutsche Telekom to receive interest at variable rates (generally based on the six-month EURIBOR rate) and pay interest at fixed rates (weighted average of 5.7% per annum).

The terms of the GBP-receive variable, pay fixed interest rate swaps provide for Deutsche Telekom to receive interest at variable rates (generally based on the six-month GBP-LIBOR rate) and pay interest at fixed rates (weighted average of 6.4% per annum for the GBP receive variable, pay fixed interest rate swaps and 6.1% per annum for the forward contracts.)

The terms of the JPY-receive fixed, pay variable interest rate swaps provide for Deutsche Telekom to receive interest at fixed rates of 1.5% per annum which are swapped for variable rates (generally based on the six-month JPY-LIBOR rate).

The terms of the USD-receive fixed, pay variable interest rate swaps provide for Deutsche Telekom to receive interest at fixed rates (weighted average of 7.9% per annum) which are swapped for variable rates (generally based on the six-month and the three-month USD-LIBOR rate). The terms of the USD-receive variable, pay fixed interest rate swaps provide for Deutsche Telekom to pay interest at fixed rates (weighted average of 6.2% per annum) which are swapped for variable rates (generally based on the six-month and the three-month USD-LIBOR rate).

The terms of the CZK-receive fixed, pay variable interest rate swaps provide for Deutsche Telekom to receive interest at fixed rates of 8.1% per annum which are swapped for variable rates (generally based on the six-month PRIBOR rate).

The terms of the cross currency interest rate swaps provide for Deutsche Telekom to receive and pay interest at variable rates.

Amounts received and paid under all these interest rate swaps and cross currency interest rate swaps, which are dependent on the notional amounts and the contractual interest rates, are settled annually, semi-annually or quarter-annually.

The interest rate caps purchased have one to two-year terms and provide for Deutsche Telekom to receive excesses over a specified reference interest rate. For some of the caps, option contracts were written in order to reduce the premium (purchase of interest rate collars).

The notional amounts of the derivative financial instruments do not generally represent amounts exchanged by the parties and, therefore, are not a direct measure of the exposure of the Company through its use of derivatives. The amounts exchanged are calculated by reference to the notional amounts and by the other terms of the derivatives, such as interest rates, exchange rates or other indices.

(35) Segment information by divisions

Deutsche Telekom applies Statement of Financial Accounting Standards No. 131, ''Disclosures about Segments of an Enterprise and Related Information'' (SFAS 131) and the German Accounting Standard No. 3 ''Segment Reporting'' (DRS 3) for the calculation of segment information. In accordance with the aforementioned, companies must disclose information on their operational segments in accordance with their internal reporting structures. Under SFAS No. 131 and DRS 3, Deutsche Telekom has the following operational segments for which reporting is required: T-Com, T-Systems, T-Mobile and T-Online. The segments for which reporting is required are strategic divisions which differ in their products and services, their relevant sub-markets, the profile of their customers and their regulatory environment.

Deutsche Telekom has focused its strategy on the strongest growth segments of global telecommunications. The Group is thus represented on all the important T.I.M.E.S. markets: telecommunications, information technology, multimedia, entertainment and security services. As a universal provider, Deutsche Telekom is thus responding to the trend across the industry for the convergence of technologies, networks, products and services. In order to be able to serve the T.I.M.E.S. markets in the best possible way, Deutsche Telekom has been structured into four divisions in 2001.

The valuation methods used for the group segment reporting correspond mainly to those used in the German consolidated financial statements. Deutsche Telekom evaluates the segments' performance based on their income before taxes including extraordinary income (loss). No single matter in the 2001 financial year was shown in the Deutsche Telekom group's extraordinary income/loss; the expenses for the initial public offering of T-Online and the planned initial public offering of T-Mobile International AG accounted for the extraordinary loss of EUR 159 million in 2000.

Revenues generated and goods and services exchanged between segments are, as far as possible, calculated on the basis of market prices. Income taxes and taxes chargeable as expense are not assigned to individual segments. With the exception of depreciation and amortization, no major non-cash items are shown in the segments. The income (loss) related to associated and related companies relates to income from investments and associated companies, as well as write-downs of financial assets and marketable securities.

Segment assets under segment reporting include the remaining book value of property, plant and equipment, intangible assets and financial assets. Segment investments are defined as increases in these areas. In addition, the segment assets and segment investments are shown by geographical regions; assignment to the individual regions is generally by the location of the asset. Please refer to footnote (1) in the notes to the consolidated financial statements for the presentation of revenue by regions. In accordance with DRS 3, liabilities have been assigned to the segments since the 2000 financial year. As part of Group segment reporting, these include debt and other liabilities, excluding tax liabilities.

		Net revenue	Revenue between segments	Depreciation and amortization	Net interest expense	Income (loss) related to associated and related companies	Income (loss) before taxes	Segment assets	Segment investments	Segment liabilities	Employees[1]
		millions of €									
T-Com	2001	19,362	6,723	(4,789)	(260)	(525)	3,244	28,375	5,094	11,357	117,655
	2000	20,170	7,441	(6,036)	(737)	(239)	4,373	29,446	3,783	15,807	121,514
	1999	21,606	5,068	(5,077)	(1,406)	2	1,803	—	—	—	—
T-Systems	2001	11,211	2,577	(1,313)	(2)	13	(289)	5,045	1,289	4,260	41,528
	2000	8,460	2,226	(754)	(114)	15	2,498	5,259	3,536	5,669	23,695
	1999	6,018	1,965	(494)	(108)	(53)	(219)	—	—	—	—
T-Mobile	2001	12,994	1,643	(6,324)	(3,008)	(204)	(6,399)	86,704	28,418	21,657	30,124
	2000	8,994	1,362	(2,337)	(1,370)	(127)	(2,350)	40,230	25,483	31,421	16,757
	1999	5,153	1,183	(850)	(78)	(134)	632	—	—	—	—
T-Online	2001	1,338	111	(189)	168	(134)	(233)	983	118	258	3,008
	2000	1,038	90	(93)	127	(9)	2,628	1,208	1,212	464	2,162
	1999	813	55	(25)	3	—	154	—	—	—	—
Other	2001	3,404	4,583	(2,160)	(1,088)	(359)	1,629	25,733	2,888	41,891	49,345
	2000	2,277	4,834	(1,758)	(1,074)	2,213	1,154	30,644	9,149	16,984	40,904
	1999	1,880	5,300	(2,042)	(974)	(165)	497	—	—	—	—
Reconciliation	2001	—	(15,637)	(446)	52	(1)	(456)	(124)	(109)	(2,572)	—
	2000	—	(15,953)	(2,013)	71	14	(1,970)	(181)	(95)	(1,537)	—
	1999	—	(13,571)	22	17	7	77	—	—	—	—
Group	2001	48,309	—	(15,221)	(4,138)	(1,210)	(2,504)	146,716	37,698	76,851	241,660
	2000	40,939	—	(12,991)	(3,097)	1,867	6,333	106,606	43,068	68,808	205,032
	1999	35,470	—	(8,466)	(2,546)	(343)	2,944	—	—	—	—

(1) Average figures for the year, and nominal number.

Segments by geographic area

	Segment assets		Segment investments	
	Dec. 31, 2001	Dec. 31, 2000	Dec. 31, 2001	Dec. 31, 2000
	millions of €	millions of €	millions of €	millions of €
Germany	55,490	59,021	7,669	16,404
European Union (excluding Germany)	26,499	31,962	1,908	15,402
Rest of Europe	12,218	9,188	1,952	5,458
North America	51,527	5,668	25,519	5,618
Other	982	767	650	186
Group	146,716	106,606	37,698	43,068

T-Com

Within the "four-pillar strategy", T-Com is responsible in particular for Deutsche Telekom's fixed network business. This also includes the provision of network platforms and the creation, expansion and support of appropriate network infrastructures. This range of services is complemented by special additional services such as public telecommunications, directory inquiries, call centers and free call and shared-cost numbers, the terminal equipment business, which is managed by T-Com Sales, services with international carriers and a broad range of products and services for data communications. T-Com provides this wide range of services for 41 million residential and small business customers and around 420,000 medium-sized business customers.

The decrease in net revenue of EUR 808 million to EUR 19,362 million is mainly attributable to the partial sale of the cable business (in Hesse and North-Rhine Westphalia in the third quarter of 2000 and Baden-Württemberg in the third quarter of 2001). Substitution effects in the City region from fixed network to mobile calls continued to contribute to the decrease in revenue, as well as price measures which were implemented as a result of directives from the Regulatory Authority and the continued intense price pressure from competitors in the domestic long-distance sector in particular. The decrease in revenue from call charges is offset by higher earnings from line installation and rental charges, which are mainly attributable to the increase in the number of ISDN channels and T-DSL lines. The decrease in net revenue in the T-Com segment is also attributable to price reductions for international traffic terminating in the mobile and fixed networks.

Revenue from business with other segments amounting to EUR 6,723 million relates mainly to network and support services billed by T-Com to other segments and the provision of fixed-network terminal equipment for other segments.

The depreciation and amortization item reflects the depreciation on the noncurrent assets assigned to this segment. The decrease in depreciation and amortization is attributable to the sale of part of the cable network and a nonscheduled write-down in the previous year on parts of the copper cable long-distance network and telecommunications equipment amounting to EUR 971 million. There were no comparable write-downs in 2001. The positive development of net interest expense is attributable in particular to lower debts in this segment. The decrease in the result related to associated and related companies in the period under review relates mainly to write-downs on financial assets and a poorer result related to associated and related companies at Kabel Deutschland.

Income before taxes in this segment of EUR 3,244 million was lower than last year. Besides the aforementioned changes in revenue, depreciation and amortization, results related to associated and related companies and net interest expense, this development is particularly attributable to the high level of other operating income relating to the sale of the cable companies in North-Rhine Westphalia and Hesse in 2000 for EUR 2,964 million. The only comparable development in the period under review relates to the proceeds from the sale of the cable companies in Baden Württemberg and the regional Kabel service companies in North-Rhine Westphalia and Baden Württemberg amounting to EUR 997 million.

The decrease in segment assets from EUR 29,466 million to EUR 28,375 million relates in particular to a decrease in property, plant and equipment at T-Com. This is mainly attributable to the sale of parts of the cable network and scheduled depreciation of property, plant and equipment. The investments in T-Com's segment assets were mainly made in technical equipment and advance payments and construction in progress. The decrease in segment liabilities is primarily a consequence of lower debts.

T-Systems

T-Systems is responsible for serving Deutsche Telekom's domestic and international named accounts. T-Systems offers comprehensive services from the field of information technology (IT) and telecommunications (TC) as well as e-business solutions from the IT/TC convergence sector. Together with T-Systems ITS, acquired in the fourth quarter of 2000 as debis Systemhaus (now: T-Systems ITS GmbH), Deutsche Telekom has grown into the second largest systems house in Europe.

As in the previous year, the net revenue in the T-Systems segment increased further in 2001 to EUR 11,211 million. The increase is predominantly attributable to the consolidation of the T-Systems ITS group for the full financial year. Furthermore, DeTe System generated increased revenues from systems solutions, such as with the Deutsche Post project. The business area Carrier Services National continued to contribute to the increase in revenue. The area Carrier Services National will be part of the T-Com division beginning January 1, 2002. In return, the area Carrier Services International, previously part of T-Com, is being reassigned to the T-Systems segment.

Revenue from business with other segments also increased slightly to EUR 2,577 million. T-Systems CSM and T-Systems Nova in particular contributed to the increase in revenue. T-Systems CSM and T-Systems Nova mainly bill IT/development services to the other segments.

The increase in depreciation and amortization and the positive development of the net interest expense relate mainly to the inclusion of T-Systems ITS for the full twelve months. This led, above all, to increased amortization of goodwill. The decrease in income before taxes is furthermore attributable to the high level of proceeds from the sale of Global One (EUR 2,864 million) in early 2000. There was no income comparable with these proceeds in 2001. Excluding the sale of these shares, income before taxes improved slightly in 2001 compared with the previous year. The loss before taxes of EUR 289 million was also influenced by losses on written-off receivables from national carriers.

Segment assets amounting to EUR 5,045 million consist mainly of intangible assets, in particular goodwill relating to T-Systems ITS. Segment liabilities are influenced mainly by the level of debts.

T-Mobile

The business of T-Mobile combines all the activities of the T-Mobile International group. Via its subsidiaries, T-Mobile currently offers a transatlantic GSM mobile communications network and thus the advantages of a uniform technical platform, mainly for a broad range of customers in Germany, the United Kingdom, the United States of America, Austria and the Czech Republic. T-Mobile also holds stakes in companies in Poland, the Netherlands, Russia and Canada. Besides T-Mobile International AG as the parent company, the companies fully consolidated include T-Mobile Deutschland GmbH, One 2 One, VoiceStream and Powertel, max.mobil, RadioMobil and T-Motion.

The increase in net revenue by EUR 4,000 million to EUR 12,994 million reflects in particular the increase in the number of subscribers in the mobile communications networks under T-Mobile's majority control. VoiceStream and Powertel and RadioMobil, consolidated for the first time in 2001, also had an impact on revenue. It should be noted, however, that VoiceStream and Powertel were only consolidated for 7 months and RadioMobil for 9 months.

Revenue from business with other segments amounting to EUR 1,643 million relates mainly to domestic network interconnection services (so-called mobile-terminated calls). These services made a considerable contribution to the increase in revenue between segments.

The increased depreciation and amortization in 2001 is due not only to changes in the composition of the TMO Group (EUR 2,258 million), but also in particular to nonscheduled write-downs. The measures approved in December 2001 to standardize the brand names of the individual mobile communications operators with the aim of establishing the name T-Mobile as a global brand for mobile communications resulted in nonscheduled write-downs on goodwill of EUR 1,040 million. In addition, the increase also relates to the amortization of UMTS licenses, included for the full year for the first time in 2001. Scheduled amortization and depreciation relates in particular to goodwill (EUR 1,802 million), mobile communications licenses (EUR 1,445 million), and technical equipment for GSM mobile communications networks (EUR 1,419 million).

The net interest expense of EUR 3,008 million is attributable, besides the change in the composition of the Group, mainly to interest expense from loans taken out by Deutsche Telekom AG — in particular as a result of the inclusion of VoiceStream and Powertel — and DT Finance. Also included in interest expense is an early repayment penalty of EUR 569 million arising from the conversion of loans from Deutsche Telekom AG to shareholders' equity in 2001.

The increase in segment assets relates mainly to the acquisition of VoiceStream and Powertel. While both intangible assets and property, plant and equipment increased, financial assets decreased as the initial investment in VoiceStream and Powertel made in 2000 was included in the acquisition costs and was thus eliminated by the full consolidation of the company. The considerable decrease in segment liabilities is a result in particular of the conversion of loans from Deutsche Telekom AG to shareholders' equity. The increase in bonds due to the changes in the composition of the Group and the increase in the syndicated loan for One 2 One had an offsetting effect.

T-Online

The T-Online segment is one of the largest online providers in Europe, measured in terms of subscriber numbers and revenue. It is represented with companies in France, Spain, Portugal, Austria and Switzerland. T-Online is the business area for the Internet consumer market and focuses on the growth areas of access and portal business (advertising/e-commerce). Besides the T-Online Group, the T-Online segment also includes DeTeMedien.

The net revenue of the T-Online segment increased further in 2001 by EUR 300 million to EUR 1,338 million and thus continued the trend of 1999 and 2000. The positive developments in both the access and portal business areas make particular contributions to the revenue growth in 2001. The reasons for the increase in revenue are the increased subscriber numbers in the access area and increased portal revenues and the inclusion of Ya.com for the full year in the non-access area. The decreased revenues from DeTeMedien, a result of the spin off of the media publishing house and the card business to DeTe Card, only had a minor impact on the revenue of the T-Online segment.

T-Online also recorded a slight increase in revenue to EUR 111 million from the internal provision of services between segments. The revenue between segments relates mainly to portal revenues for the use of the T-Online homepage.

The marked decrease in income before taxes in mainly attributable to the fact that high level of proceeds relating to the initial public offering of T-Online International AG and the capital increase of comdirect were recorded in the previous year. There were no comparable activities in 2001. Excluding these one-time effects in 2000, the income before taxes is at approximately the same level as in the previous year. T-Online's increased revenues are offset by increased amortization of goodwill, particularly on companies in the T-Online subgroup acquired in 2000, and the decreased results from associated and related companies due to the negative development of results from comdirect and T-Motion.

Assets of the T-Online segment decreased, which is mainly attributable to the amortization of goodwill. The decrease in segment liabilities relates mainly to liabilities to subsidiaries.

Other

"Other" includes Deutsche Telekom group headquarters, competence centers (including customer billing), real estate and several foreign companies such as the Hungarian company MATAV and Slovenské, which was consolidated for the first time in the fourth quarter of 2000. Croatian Telecom, fully consolidated since the fourth quarter of 2001, is also shown here. MATAV, Slovenské and Croatian Telecom have been assigned to the T-Com segment since January 1, 2002.

The increase in net revenue to EUR 3,404 million was influenced considerably by the inclusion for the first time of Croatian Telecom and the Macedonian company Maktel and the full-year consolidation of Slovenské. Besides these consolidation effects, increased net revenue at MATAV, particularly in the areas of mobile communications and access and call charges, also had a positive effect.

Revenue from business with other segments amounting to EUR 4,583 million relates mainly to revenues from real estate business with T-Com.

The increase in depreciation and amortization mainly relates to a non-scheduled write-down on real estate which, however, is offset by proceeds in the same amount from the reversal of accruals for risks previously calculated as a lump sum. The decrease in the result related to associated and related companies is primarily attributable to the non-recurrence of the high proceeds of the equity stake relating to DT-FT Italian Holding of EUR 2,328 million in the previous year, generated by the sale of shares in WIND, and the valuation allowance of EUR 312 million for the stake in France Telecom.

The development of results was also marked by proceeds from the sale of Sprint FON and PCS shares and one-time expenses (totaling EUR 1,850 million) relating mainly to the sale of these shares.

The decrease in segment assets to EUR 25,733 million is attributable in particular to the decrease in financial assets. The dividend payment of DT-FT Italian Holding in particular led to a lower net carrying value of the equity stake. Furthermore, the sale of Mediaone to T-Mobile International AG led to a decrease in the assets of this segment in the 2001 financial year. The considerable increase in segment liabilities in the period under review is attributable to the reclassification of liabilities from the T-Mobile segment to the segment "Other". The reason for this is the conversion of a considerable proportion of the loans to T-Mobile International AG into shareholders' equity.

Reconciliation

The items to be reconciled relate mainly to consolidation measures. As part of its strategy to separate itself more quickly from a considerable proportion of its real estate portfolio, Deutsche Telekom has made a nonscheduled write-down in the form of a valuation adjustment on the asset side using average prices per square meter for groups of properties to determine individual fair values amounting to EUR 2,018 million for the 2000 financial year. The valuation of real estate, completed in the period under review, led to a further nonscheduled write-down of EUR 466 million. These valuation adjustments, which do not affect the operational segments, have no effect on the internal operation of the segments; they are almost exclusively an element of the depreciation and amortization shown in the reconciliation line.

(36) Information on the Board of Management and the Supervisory Board of Deutsche Telekom AG

The Supervisory Board has received no Supervisory Board remuneration or meeting attendance fees so far for the 2001 financial year. After the shareholders' meeting on May 29, 2002, Supervisory Board remuneration and meeting fees amounting to approximately EUR .5 million will be paid for the 2001 financial year.

Provided that the 2001 financial statements of Deutsche Telekom AG are approved in their current form, the remuneration of the Board of Management of Deutsche Telekom will amount to approximately EUR 17.4 million. Deutsche Telekom granted approximately 1.7 million stock options to the members of the Board of Management in 2001.

The remuneration to be paid to former members of the Board of Management of Deutsche Telekom AG and their surviving dependents amounts to approximately EUR .8 million. Accruals approximating EUR 16.5 million have been established for current and future pensions of this group of persons at December 31, 2001. Pension obligations to such persons for which no accrual had to be established amounted to approximately EUR 3.4 million.

The members of the Board of Management and former members of the Board of Management, respectively, have not received any loans from the Company.

(37) Proposal for appropriation of net income of Deutsche Telekom AG

The statement of operations of Deutsche Telekom AG reflects income after taxes of EUR 6.6 billion. Of this income, approximately EUR 3.3 billion has been transferred to retained earnings in accordance with § 22 paragraph 3 of the Articles of Incorporation. Following inclusion of the unappropriated net income of approximately EUR 100.5 million, carried forward from 2000, this gives rise to cumulative unappropriated net income of approximately EUR 3.4 billion.

Under the German corporation law (Aktiengesetz), the amount of dividends available for distribution to shareholders is based upon the unappropriated accumulated earnings of Deutsche Telekom AG (parent company only) as reported in its statutory financial statements determined in accordance with the German commercial code (Handelsgesetzbuch). The Supervisory Board and the Board of Management will propose to the shareholders' meeting to pay a dividend of EUR 0.37 per individual no par value share, to transfer an amount of EUR 850 million to other retained earnings, and to carry forward the remaining balance of approximately EUR 7.2 million as part of unappropriated net income.

(38) Reconciliation to U.S. GAAP

The consolidated financial statements of Deutsche Telekom AG have been prepared in accordance with German GAAP, which differs in certain respects from generally accepted accounting principles in the United States (U.S. GAAP). Application of U.S. GAAP would have affected the results of operations for each of the years in the three-year period ended December 31, 2001 and the balance sheets as of December 31, 2001 and 2000 to the extent described below.

Reconciliation of net income (loss) from German GAAP to U.S. GAAP:

		2001	2000	1999
		millions of €	millions of €	millions of €
Net income (loss) as reported in the consolidated financial statements under German GAAP		(3,454)	5,926	1,253
U.S. GAAP reconciling adjustments				
Valuation adjustments of fixed assets	(a)	443	2.792	—
Mobile communications licenses	(b)	2,098	865	—
Internally developed software	(c)	166	95	163
Effects of dilution gains	(d)	(396)	1,741	—
Goodwill and asset differences	(e)	(285)	(97)	5
Write-down of tradenames	(f)	1,040	—	—
Value-added tax	(h)	(27)	(169)	288
Derivatives and related foreign exchange differences	(i)	(31)	(146)	68
Implementation of SFAS 133	(i)	370	—	—
Accruals for personnel restructuring	(j)	10	(125)	(97)
Financing of fixed assets	(k)	(42)	—	—
Deferral of gains on divestitures	(l)	27	(348)	—
Deferred income	(m)	(168)	48	(129)
Implementation of SAB 101, cumulative to December 31, 1999	(m)	—	(869)	—
Capital raising and financing costs	(n)	—	120	238
Asset-backed securitization	(o)	(71)	—	—
Investments in equity investees	(p)	(182)	62	—
Effects of full consolidation of debis, net of tax	(q)	(294)	(116)	—
Other differences	(r)	253	(28)	(32)
Income taxes	(s)	1,066	(482)	(244)
Net income in accordance with U.S. GAAP		523	9,269	1,513

Reconciliation of shareholders' equity from German GAAP to U.S. GAAP:

		Dec. 31, 2001	Dec. 31, 2000
		millions of €	millions of €
Shareholders' equity as reported in the consolidated financial statements under German GAAP		66,301	42,716
U.S. GAAP reconciling adjustments			
Valuation adjustments of fixed assets	(a)	3,235	2,792
Mobile communications licenses	(b)	2,963	865
Internally developed software	(c)	438	272
Effects of dilution gains	(d)	1,345	1,741
Goodwill and asset differences	(e)	2,672	1,001
Write-down of tradenames	(f)	1,062	—
Unrealized gains on marketable securities	(g)	580	2,503
Value-added tax	(h)	—	27
Derivatives and related foreign exchange differences	(i)	29	(154)
Implementation of SFAS 133	(i)	338	—
Accruals for personnel restructuring	(j)	22	12
Financing of fixed assets	(k)	(42)	—
Deferral of gains on divestitures	(l)	(321)	(348)
Deferred income	(m)	(1,144)	(88)
Implementation of SAB 101, cumulative to December 31, 1999	(m)	—	(869)
Asset-backed securitization	(o)	(71)	—
Investments in equity investees	(p)	(117)	56
Effects of full consolidation of debis, net of tax	(q)	(410)	(116)
Other differences	(r)	82	40
Income taxes	(s)	2,049	(40)
Minority interest	(t)	(5,307)	(4,302)
Shareholders' equity in accordance with U.S. GAAP		73,704	46,108

Changes in shareholders' equity in accordance with U.S. GAAP:

	2001	2000
	millions of €	millions of €
Shareholders' equity in accordance with U.S. GAAP, on January 1	46,108	37,611
Net income in accordance with U.S. GAAP	523	9,269
Other Comprehensive Income		
Net change in unrealized gains on marketable securities, net of tax	(1,904)	1,458
Foreign currency translation	(684)	(480)
Additional minimum pension liability, net of tax	(158)	—
Derivatives, net of tax	(14)	—
	(2,760)	978
Capital increase due to shares issued for VoiceStream and Powertel	31,614	—
Other changes	96	124
Dividends for 2000 and 1999, respectively	(1,877)	(1,874)
Shareholders' equity in accordance with U.S. GAAP, on December 31	73,704	46,108

As permitted by Postreform II, certain property, plant and equipment on hand as of December 31, 1992 were valued at fair values rather than at historical cost less depreciation, which is required by U.S. GAAP. The Company has not been able to quantify the effect of the difference in accounting treatment because, prior to January 1, 1993, the predecessor company did not maintain sufficiently detailed historical cost records. The fair market values recorded in the opening balance sheet of Deutsche Telekom AG at January 1, 1995 have been carried forward as the historical acquisition or construction costs.

(a) Valuation adjustments of fixed assets

(i) In the fourth quarter of 2001, the Company recorded an additional write-down for land in the amount of EUR 466 million under German GAAP. This amount represents the difference between the final valuation adjustment completed in the fourth quarter 2001 of EUR 2,484 million and a preliminary estimate of EUR 2,018 million which had been recorded in 2000. These charges were made in connection with the new disposal-oriented real estate concept in which management has developed a strategy of reducing its holdings of assets that are outside the scope of its core activities. This plan provided sufficient justification under German GAAP to allow the Company to perform an evaluation of the current market value of land and record a write-down for those properties whose book values exceeded their fair values. Under U.S. GAAP, the Company's plan did not have the characteristics as described in Staff Accounting Bulletin 100 to consider the land to be in the category of ''Assets to Be Disposed Of'' under SFAS No. 121*, Accounting for the Impairment of Long-Lived Assets and Long-Lived Assets to Be Disposed of* (SFAS 121). Accordingly, under U.S. GAAP, these assets would be considered ''Assets to Be Held and Used'' and were not impaired under SFAS 121. Accordingly, the write-downs have not been recorded under U.S. GAAP.

(ii) The Company historically capitalized ISDN boxes relating to digital telephony services under both German and U.S. GAAP. Due to the decrease in the per unit replacement cost, the Company began expensing the newly acquired ISDN boxes as they no longer exceeded the Company's minimum capitalization threshold. As new assets no longer met the criteria for capitalization, the Company expensed EUR 204 million in 2000 relating to the remaining book values of the ISDN boxes previously capitalized under German GAAP. Under U.S. GAAP, the fact that new assets do not meet the criteria for capitalization does not result in the write-off of assets that were previously capitalized in accordance with the Company's accounting policy. Accordingly, this entry was not recorded and the costs are capitalized under U.S. GAAP. As of December 31, 2001, the remaining net book value was EUR 153 million.

(iii) The carrying values of land and buildings acquired prior to 1995 were determined on the basis of fair values per square meter. During 2000, the Company remeasured the square meters of its land and buildings currently held and originally included in the opening balance sheet of the Company at January 1, 1995 (see summary of accounting principles). The Company determined that certain land and buildings had more square meters and other land and buildings had less square meters than originally utilized to calculate the values recorded in the fixed asset records in 1995. Overall, the remeasurement process indicated that there were more square meters than originally recorded. However, under German GAAP, the Company adjusted only the land and buildings in which there was a decrease in square meters and such adjustment is recorded in the year determined. As a result, the carrying values of land and buildings were reduced by EUR 220 million and expensed in 2000. Under U.S. GAAP, this adjustment did not meet the impairment criteria under SFAS 121, and therefore was not recorded. As of December 31, 2001, the remaining net book value was EUR 209 million. Furthermore, the assignment of fair values to land and buildings requires the use of estimates and assumptions. The net increase represented approximately 1% of the original value ascribed to land and buildings. This difference is insignificant, and the Company believes that for purposes of U.S. GAAP, the values originally assigned were appropriate.

(iv) Under German GAAP, at December 31, 2000, the Company accrued EUR 350 million relating to the carrying value of certain empty building space, on the basis of the ''prudence'' principle. Under U.S. GAAP, such accruals do not meet the impairment criteria under SFAS 121, and, therefore, were not recorded. During 2001, under German GAAP, this accrual was reversed and a corresponding EUR 350 million write-down of the carrying value of the fixed assets was recorded. As the adjustments were offsetting, there was no impact on the German GAAP statement of operations in 2001. For U.S. GAAP purposes, such a write-down still did not meet the impairment criteria. Therefore it continues to be a reconciling item for U.S. GAAP.

(v) Under German GAAP, the capitalization of interest related to fixed assets under construction is based on the allocated interest expense given the financial structure of the Company. Under U.S. GAAP, the capitalization of interest related to fixed assets under construction does not take into account the Company's financial structure, but capitalizes the interest expense which could have theoretically been avoided if the assets had not been constructed (i.e. assumes the entire expenditure was financed). As a result, in 2001 the Company capitalized an additional EUR 39 million of interest expense related to assets under construction for U.S. GAAP.

(b) Mobile communications licenses

Under German GAAP, the acquisition costs of the licenses purchased in the United Kingdom, Germany and Austria in 2000 and licenses obtained in the acquisition of VoiceStream and Powertel are amortized as scheduled from the time of acquisition over the expected period of usage. The interest on borrowings made to finance the acquisitions of the licenses is recognized immediately as an expense. Under U.S. GAAP, amortization is from the beginning of the economic use of the licenses, considered to be the start of operation of the networks, over the expected period of usage. This resulted in a decrease in amortization expense of EUR 863 million and EUR 377 million in 2001 and 2000, respectively. The interest accumulated on borrowings through the start of network operation represents part of the acquisition costs under U.S. GAAP, resulting in a decrease in interest expense of EUR 1.2 billion and EUR 488 million in 2001 and 2000, respectively.

(c) Internally developed software

In accordance with Statement of Position 98-1, *Accounting for the Costs of Computer Software Developed or Obtained for Internal Use*, in contrast to German GAAP, certain internal and external expenses incurred during the internal project development stage of computer software for internal use are to be capitalized and amortized over its expected useful life.

(d) Effects of dilution gains

In 2000, T-Online, comdirect bank AG (“comdirect”) and OJSC Mobile TeleSystems (“MTS”) entered into transactions in which their shares were either sold for cash or exchanged as part of a purchase business combination. As a result of these transactions, the Company’s ownership interest in the subsidiary or affiliate changed resulting in a “dilution gain”. For German GAAP, the Company recognized dilution gains resulting from cash sales of subsidiary or affiliate shares as a credit to income. However, under German GAAP, the Company does not recognize changes in interest transactions when cash proceeds are not received. Under U.S. GAAP, all such transactions, including those related to purchase business combinations, are reflected as dilution gains. The following transactions generated dilution gains in 2000:

Cash transactions:

- As described in footnote (3), in April 2000 T-Online issued 114,100,000 ordinary shares in an initial public offering (“IPO”) at EUR 27 per share for cash consideration totaling EUR 3,080 million. This reduced the Company’s ownership in T-Online from 100% to 89.76%, resulting in a dilution gain of EUR 2,657 million.
- In June 2000, MTS, a Russian mobile telephone company, issued 345,244,080 shares for cash consideration totaling EUR 364 million in an IPO. This reduced the Company’s ownership percentage in MTS from 44.1% to 36.2%, resulting in a dilution gain of EUR 111 million.
- In June 2000, comdirect, an on-line bank, issued 20,500,000 shares at EUR 31 per share for cash consideration totaling EUR 636 million in an IPO. This reduced T-Online’s ownership percentage in comdirect from 25% to 21.35%, resulting in a dilution gain of EUR 119 million. For U.S. GAAP the dilution gain is EUR 57 million lower because the equity investment balance was higher for U.S. GAAP at the date of the IPO.

Non-cash transactions:

- In April 2000, T-Online acquired all of the shares outstanding of Club Internet, a French Internet provider, in exchange for 69,633,116 of T-Online ordinary shares at EUR 27 per share. Consideration totaled EUR 1,880 million and decreased the Company’s ownership percentage in T-Online from 89.76% to 84.48%. Under U.S. GAAP, the dilution gain of EUR 1,355 million has been recognized as income with a corresponding increase to goodwill.
- In April 2000, T-Online acquired a 25% interest in comdirect in exchange for 24,875,189 of T-Online ordinary shares at EUR 27 per share. Consideration totaled EUR 671 million and decreased the Company’s ownership percentage in T-Online from 84.48% to 82.74%. Under U.S. GAAP, the dilution gain of EUR 391 million has been recognized as income with a corresponding increase to goodwill.

- In October 2000, T-Online acquired all of the outstanding shares of ya.com, a Spanish Internet service provider, in exchange for 12,387,280 ordinary shares of T-Online at EUR 32.42 per share. Consideration totaled EUR 402 million and decreased the Company's ownership percentage in T-Online from 82.87% to 81.71%. Under U.S. GAAP, the dilution gain of EUR 222 million has been recognized as income with a corresponding increase in goodwill.

Dilution gains related to sales of shares for cash totaled EUR 2,887 million in fiscal 2000 and have been recorded as income for German GAAP. For U.S. GAAP this amount was reduced by EUR 57 million due to reasons explained above. Dilution gains related to purchase business combinations totaling EUR 1,968 million have been recorded as income for U.S. GAAP purposes but not recognized for German GAAP purposes. For both German and U.S. GAAP, no deferred taxes have been provided as under the currently enacted German tax law the above transactions will not give rise to any taxable event. Amortization of the additional goodwill recorded totaled EUR 250 million and EUR 170 million in 2001 and 2000, respectively, based on goodwill lives ranging from 7 to 15 years. In 2001, an impairment charge was recorded to reduce the carrying value of the investment in comdirect to fair value. As the carrying basis for comdirect under U.S. GAAP exceeded the carrying basis under German GAAP due to the dilution gains described above, an additional write-down for EUR 146 million was recorded under U.S. GAAP. The charge was taken as a result of the continued losses of comdirect and the decline in the market value of the stock of comdirect. The impairment charge was calculated by comparing the book value of the investment in comdirect including goodwill with the market value of the shares owned.

(e) Goodwill and asset differences

Purchase price differences between German and U.S. GAAP are generated from business combinations due to net assets acquired, valuation of shares and stock options issued, valuation of underlying assets and liabilities (including deferred taxes), dates used to calculate consideration, paid as well as the date at which an acquisition is considered completed. The acquisitions resulting in the majority of the differences between German GAAP and U.S. GAAP are discussed beneath the tables.

The following table quantifies the differences for goodwill and intangible amortization expense as well as fixed asset depreciation related to these assets for the years ended December 31, 2001, 2000, and 1999.

U.S. GAAP Reconciling Adjustments to the Statement of Operations

	2001	2000	1999
	millions of €	millions of €	millions of €
U.S. GAAP Adjustments to German GAAP, income (loss)			
Goodwill amortization expense	466	326	5
Intangible asset amortization expense	(727)	(413)	—
Fixed asset depreciation expense	(24)	(10)	—
Net effect	(285)	(97)	5

The following table quantifies the differences between U.S. GAAP and German GAAP for goodwill, intangible assets, and fixed assets resulting from the Company's acquisitions.

U.S. GAAP Reconciling Adjustments to Shareholders' Equity

	Dec. 31, 2001 millions of €	Dec. 31, 2000 millions of €
U.S. GAAP Adjustments to German GAAP, increase (decrease)		
Goodwill	(2,563)	(3,468)
Goodwill accumulated amortization	779	313
Intangible assets	5,422	4,371
Intangible asset accumulated amortization	(1,140)	(413)
Fixed assets	208	208
Fixed asset accumulated depreciation	(34)	(10)
Net effect	2,672	1,001

(i) In 2001, the Company acquired VoiceStream and Powertel. The Powertel acquisition was a 100% stock acquisition with a predetermined stock conversion rate which was not subject to adjustment. Under APB 16, the acquirer is required to use the stock price based on the date of the acquisition agreement to determine the acquisition price. This resulted in an increase in the U.S. GAAP purchase price, as compared to German GAAP. Based on a third party valuation, the purchase price was then allocated to certain intangible assets as well as differences in deferred taxes which reduced the net effect on goodwill related to the purchase price differences. The purchase price and purchase price allocation differences related to the VoiceStream and Powertel acquisitions resulted in increases in goodwill of EUR 888 million and intangibles of EUR 1.1 billion under U.S. GAAP as compared to German GAAP as of the date of acquisition.

(ii) In 2000, the Company completed its purchase price allocation for One 2 One. The differences between German GAAP and U.S. GAAP primarily relate to the allocations made from goodwill to intangible assets for U.S. GAAP purposes, mainly related to licenses, tradename and customer lists. The allocation from goodwill to intangible assets was offset by the applicable deferred taxes under U.S. GAAP.

(f) Write-down of Tradenames

At the end of 2001, the Company made the decision to re-brand its foreign mobile subsidiaries operating in the T-Mobile business segment under a common "T-Mobile" name by the end of 2002. For German GAAP purposes, this resulted in an immediate write-down of the respective portion of goodwill attributable to tradenames for the projected net book value on December 31, 2002, assuming normal amortization in 2002. This adjustment resulted in a net book value at the end of 2001 equivalent to one-year's normal amortization. For U.S. GAAP purposes, the decision was considered a triggering event resulting in an impairment analysis under SFAS 121. Based on this analysis, no impairment existed and the asset is considered to be in use through the end of 2002. Accordingly, the write-down recorded under German GAAP was reversed. However, under U.S. GAAP, the useful lives have been shortened to one year and the remaining carrying amount will be completely amortized by December 31, 2002.

(g) Unrealized gains on marketable securities

Under German GAAP, marketable debt and equity securities (including certain securities classified as other investments) are generally carried at historical cost. Under U.S. GAAP, marketable debt and equity securities, other than investments accounted for by the equity method, are categorized as either trading, available for sale, or held to maturity. Securities classified as trading or available for sale are reported at fair value at the balance sheet date and held to maturity securities are reported at historical cost. Unrealized gains and losses on trading securities are recorded in net income while unrealized gains and losses on securities categorized as available for sale are recorded, net of income tax, in shareholders' equity. The change in 2001 as compared to 2000 primarily relates to the Company's sale of its holdings in Sprint.

(h) Value-added tax

The nondeductible capitalized VAT (capitalized prior to 1996) was recorded as property, plant and equipment. German GAAP requires the capitalized VAT to be depreciated and the VAT recoveries to be recorded as other operating income. Under U.S. GAAP, the capitalized VAT is treated as a long-term receivable rather than property, plant and equipment. As VAT recoveries are received, they are offset against the receivable and neither depreciation nor other operating income are recognized.

(i) Derivatives and related foreign exchange differences

Significant differences arise relating to accounting for derivatives under U.S. GAAP as compared to German GAAP. These result from fair value recognition under U.S. GAAP, whereas under German GAAP the cost basis is generally used, unless losses have occurred. In addition, there are classification differences between foreign currency translation adjustments reflected as part of the shareholders' equity section of the balance sheet and the statement of operations. See additional discussion related to derivatives under German GAAP in footnote (34) and under U.S. GAAP in footnote (41 d).

(j) Accruals for personnel restructuring

Under German GAAP, the estimated costs of employee separations have been accrued on the basis of the Company's announced intention to reduce its workforce. Under U.S. GAAP, these costs are accrued in the period that the employee accepts the offer of termination. The Company has agreed pursuant to its collective bargaining agreements with the unions that it will not unilaterally terminate the employment of its non-civil servant employees due to business reasons before the end of the year 2004. Civil servants may not be involuntarily terminated under the terms of their conditions of employment.

(k) Financing of fixed assets

In December 2001, the Company completed a sale-leaseback transaction for certain properties. Under German GAAP, this was recognized as a legal sale with a separate leaseback accounted for as an operating lease. Under U.S. GAAP, transactions with continuing involvement in sold properties due to participation in potential future gains are accounted for as a financing. Therefore, under U.S. GAAP, the proceeds from the sale of EUR 562 million are recorded as a liability, and the net book value of the sold assets of EUR 492 million remain recorded as assets. Additionally, EUR 28 million has been capitalized as other assets related to costs of the financing and will be amortized over the 18-year life of the contract. The future payments are approximately EUR 48 million in each of the first five years and EUR 715 million thereafter. Under German GAAP, these amounts are included as minimum lease payments under operating leases in footnote (13).

(l) Deferral of gains on divestitures

During 2001 the Company sold its shareholdings in certain broadband cable operations located in Baden Württemberg ("BW"). The total sales price was EUR 1,320 million, consisting of cash in the amount of EUR 914 million, a 40% interest valued at EUR 106 million in the newly formed entity that acquired BW broadband cable and a senior deferred note in the amount of EUR 300 million (the "BW Note"). The BW Note is due in 2011 and bears an interest rate of EURIBOR plus 7.5% until 2004 and 15% thereafter. Interest on the BW Note is accrued semiannually until September 2006. Subsequently, cash interest, which is calculated on the total accrued interest and principal of the BW Note, will become payable semiannually beginning March 2007. All interest accrued prior to and including September 2006 will be payable on maturity of the note.

During 2000, the Company sold its shareholdings in the broadband cable operations located in the North Rhine-Westphalia ("NRW") and Hesse regions to two investor groups in two separate transactions. The total sales price for the two transactions amounted to EUR 4,542 million, consisting of cash in the amount of EUR 3,269 million, a 45% interest valued at EUR 676 million in the newly formed entity that acquired NRW broadband cable, a 35% interest valued at EUR 197 million in the newly formed entity that acquired the Hesse broadband cable business, a senior deferred note in the amount of EUR 250 million related to the NRW sale (the "NRW Note"), and a preference interest of EUR 150 million related to the Hesse sale (the "Hesse Preference Interest"). The NRW Note is due in 2010 and bears an interest rate of EURIBOR plus 7.5%. Interest on the NRW Note is accrued semiannually until July 2006. Subsequently, cash interest, which is calculated on the total accrued interest and principal of the NRW Note, will become payable semiannually beginning January 2007. All interest accrued prior to January 2007 will be payable on maturity of the note. The Hesse Preference Interest is redeemable in 2011 and bears an interest rate which increases from 12% in the first year to 21% at redemption date. Interest on the Hesse Preference Interest is accrued semiannually and becomes payable upon redemption.

Under German GAAP, the non-cash proceeds represented by the senior deferred note and the preference interest were included in the calculation of gains recognized on the divestiture of the regional cable companies. Under U.S. GAAP, due to the high leverage of the acquiring entities and the uncertainty of the cash flows available to service the debt, the Company applied Staff Accounting Bulletin (''SAB'') Topic 5:U ''*Gain Recognition on the Sale of Business or Operating Assets to a Highly Leveraged Entity*'' in evaluating and accounting for the NRW and Hesse transactions. Based on the guidance provided in SAB Topic 5:U, for U.S. GAAP, the EUR 300 million related to the 2001 BW transaction along with the EUR 400 million relating to the 2000 transactions for the non-cash proceeds will not be recognized until the collection becomes reasonably assured.

In 2001 and 2000, the Company recognized EUR 62 million and EUR 21 million of interest income, respectively in relation to the senior deferred notes and the preference interest along with provisions totaling EUR 389 million and EUR 73 million, respectively (in order to reflect the approximate fair market value of these instruments). Under U.S. GAAP, the senior deferred notes and the preference interest had not been recorded and accordingly the provisions recorded under German GAAP were reversed.

(m) Deferred income

During the fourth quarter of 2000, the Company implemented Staff Accounting Bulletin 101 (SAB 101) which establishes guidelines with respect to certain revenue recognition reporting practices. As required by SAB 101, the Company retroactively adopted this accounting change effective January 1, 2000. As a result of the implementation of SAB 101, Deutsche Telekom has deferred activation fees and certain other one-time charges and is amortizing them over the average life of the related service. Related direct incremental costs, up to the amount of revenues, are also deferred and subsequently amortized. This is in contrast to German GAAP, under which the revenue and incremental direct costs are recognized immediately. All other direct costs associated with customer activation are expensed as incurred. The Company also has certain other contracts with differing revenue recognition periods. One type of contract is accounted for under German GAAP with the revenue being recognized in accordance with the economic useful life, whereas under U.S. GAAP the revenue is to be distributed over the duration of the agreement. A second type of contract relates to indefeasible rights of use. Under German GAAP, the sales of sub-leasing of capacity on certain fiber optic networks are recognized immediately, whereas, under U.S. GAAP, the sales do not constitute sales as defined by FASB Interpretation 43 (FIN 43), ''*Real Estate Sales*'', and were recorded as deferred income, which will be recognized as income over the contract lives, ranging from 20 to 25 years.

(n) Capital raising and financing costs

Under German GAAP, the costs incurred in connection with share offerings are recorded as extraordinary expenses in the statement of operations. Under U.S. GAAP, specific incremental costs directly attributable to an offering are charged against the proceeds of the offering.

(o) Asset-backed securitization

In December 2001, the Company entered into an asset-backed securitization of certain receivables. Under German GAAP, the transaction is accounted for based on contractual values. For U.S. GAAP, the transaction is accounted for based on the fair values of the assets sold and related retained interests. See footnote (41 b) for additional information regarding this transaction.

(p) Investments in equity investees

For German GAAP purposes, the investment in Telesens has been recorded at cost. Under U.S. GAAP, this investment is accounted for as an equity investment as required by APB 18. As a result of accounting for this investment under the equity method, the Company recognized an EUR 62 million loss and EUR 10 million loss in 2001 and 2000, respectively.

In 2000, as a result of an initial public offering by Telesens as well as Telesens issuing shares for an acquisition, the Company's interest was diluted from 38% to 25%. Under U.S. GAAP, these transactions resulted in the Company recognizing an EUR 72 million gain. No dilution gain was recorded for German GAAP as the investment is accounted for at cost.

Additionally, in 2001, the Company restructured its DeTeAsia operation's equity investments, including exchanging its shares in Islacom for shares in Globe Telecom, which resulted in gains under German GAAP, as these transactions were recorded as individual transactions based on the legal contracts signed. For U.S. GAAP purposes, these transactions were recorded as primarily one transaction and accounted for as a non-monetary transaction with no gains or losses recognized. As a result, gains totaling EUR 123 million under German GAAP were recorded as a reduction of the carrying basis under U.S. GAAP.

The remaining differences result from investments in other equity investees.

(q) Effects of full consolidation of debis, net of tax

As described in the Summary of Significant Accounting Policies, on October 20, 2000, the Company acquired a 50.1% interest in debis Systemhaus GmbH (debis) by purchasing newly issued shares for EUR 4.6 billion. The Company has granted DaimlerChrysler Services AG an option to sell the 49.9% of the remaining shares in debis to the Company. In turn, the Company has an option to acquire the 49.9% of the debis shares owned by DaimlerChrysler. The put option was immediately exercisable, and the call option is exercisable starting January 1, 2002. Both options expire in 2005. The exercise price for the option is EUR 4.6 billion. Under German GAAP, the Company accounted for this transaction as the acquisition of a 50.1% interest in debis, the 49.9% interest of DaimlerChrysler Service AG was shown as minority interest within equity.

Under U.S. GAAP, the Company followed the guidance in EITF 00-04 "*Majority Owner's Accounting for a Transaction in the Shares of a Consolidated Subsidiary and a Derivative Indexed to the Minority Interest in That Subsidiary*". Under this guidance, the put and the call options are viewed on a combined basis with DaimlerChrysler's interest and are accounted for as a financing for the purchase by the Company. As a result, for U.S. GAAP purposes, net income attributable to the remaining 49.9% interest is allocated to Deutsche Telekom, rather than to the minority interest. Accordingly, the Company consolidated 100% of debis with an offsetting liability to purchase the remaining 49.9% interest owned by DaimlerChrysler.

As a result of the differences in accounting, amortization expense increased by EUR 360 million and EUR 86 million, financing costs increased by EUR 60 million and EUR 48 million and net income allocated to minority interest of EUR 94 million and EUR 18 million is eliminated under U.S. GAAP in 2001 and 2000, respectively. The tax benefit was EUR 32 million in 2001, primarily due to the deferred tax income attributable to the amortization of intangibles. In 2001 the financing charge reflects the EUR 60 million guaranteed dividend payable to DaimlerChrysler for the year 2001. The financing charge in 2000 reflects (i) EUR 10 million guaranteed dividend payable to DaimlerChrysler for the year 2000 and (ii) the fact that the remaining 49.9% of the shares could be immediately put back to the Company for EUR 38 million more than the price paid by the Company to acquire 50.1% of the shares.

In January 2002, DaimlerChrysler exercised its put option whereby the Company acquired the remaining 49.9% of debis on March 4, 2002.

(r) Other differences

Other differences consist of the different accounting and valuation approaches between German GAAP and U.S. GAAP that are not individually significant, including the treatment of unrealized gains on foreign currency receivables and payables that are recognized under U.S. GAAP but not under German GAAP, accruals for maintenance, and contract accounting. Under German GAAP, accruals have to be made for maintenance that is carried out within three months after the balance sheet date. Under U.S. GAAP, maintenance expenditures are reflected in the period in which a liability has been incurred. The contract accounting differences are a result of the application of the percentage of completion method under U.S. GAAP, as opposed to the completed contract method under German GAAP.

In the current year, a minimum liability related to certain pension plans was recognized as an expense under German GAAP. Under U.S. GAAP, this liability is recorded through other comprehensive income and resulted in a reconciling difference that resulted in an increase in net income under U.S. GAAP of EUR 156 million, net of tax, as compared to German GAAP.

(s) Income taxes

The determination of income tax expense under German GAAP differs from U.S. GAAP as follows:

— Under U.S. GAAP, in contrast to German GAAP, deferred tax assets are recognized for the estimated future tax effects attributable to tax loss carryforwards.

— Under German GAAP, deferred taxes are not recorded for temporary differences that arose during tax-free periods. Under U.S. GAAP, the estimated future tax effects related to those temporary differences are recognized.

— Under German GAAP, deferred taxes have not been recognized for those temporary differences that are not expected to reverse in the foreseeable future. Under U.S. GAAP, deferred taxes are generally recognized for all temporary differences.

Deferred taxes are also provided for the income tax effects of valuation differences between U.S. GAAP and German GAAP. Deferred tax assets are measured based on enacted tax law and reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized. Additionally, existing deferred tax assets and liabilities recognized under U.S. GAAP are adjusted when there is an enacted change of future tax rates.

The following table shows the differences between income tax benefit (expense) determined in accordance with U.S. GAAP and German GAAP:

	2001	2000	1999
	Mio. €	Mio. €	Mio. €
Deferred taxes from the application of U.S. GAAP	2,570	(561)	(14)
Deferred taxes on U.S. GAAP/German GAAP Differences	(1,472)	79	(230)
	1,098*	(482)	(244)

* The difference between the amount reported in the above reconciliation of income tax benefit (expense) and the amount reported in the Reconciliation of net income (loss) from German GAAP to U.S. GAAP in line (s) results from the consolidation effects of debis, which are presented net of tax in the net income (loss) table.

(t) Minority interest

Under U.S. GAAP, minority interest is not included in shareholders' equity.

(39) Deferred taxes in accordance with U.S. GAAP:

Deferred tax assets and liabilities arising from temporary differences and net operating losses are as follows:

	2001 Mio. €	2000 Mio. €
Deferred tax assets in accordance with U.S. GAAP		
Current deferred tax assets		
Net operating loss carryforwards	280	50
Accruals for loss contingencies	404	68
Other	91	75
Noncurrent deferred tax assets		
Net operating loss carryforwards	6,959	1,652
Financial assets	435	—
Personnel restructuring accruals	16	29
Pension accruals	341	364
Civil servant health insurance accruals	421	401
Accruals for risk related to real estate	—	167
Other accruals	223	245
Deferred income	381	361
Deferred gains on divestitures	125	136
Foreign exchange transaction differences	—	83
Other	177	27
Deferred tax assets in accordance with U.S. GAAP	9,853	3,658
Deferred tax liabilities in accordance with U.S. GAAP		
Current deferred tax liabilities		
Derivatives	(112)	(24)
Accruals	(389)	(234)
Noncurrent deferred tax liabilities		
Intangible assets	(9,173)	(1,640)
Property, plant and equipment	(883)	(1,458)
Other	(226)	(2)
Deferred tax liabilities in accordance with U.S. GAAP	(10,783)	(3,358)
Net current deferred tax asset (liability)	274	(65)
Net noncurrent deferred tax asset (liability)	(1,204)	365
Valuation allowance	(468)	(110)
Net deferred tax asset (liability) under U.S. GAAP	(1,398)	190

The following table shows the development of deferred taxes from German GAAP to U.S. GAAP:

	2001 Mio. €	2000 Mio. €
Net deferred taxes under German GAAP	(5,348)	475
U.S. GAAP adjustments		
Application of U.S. GAAP	8,304	1,670
U.S./German GAAP differences	(4,354)	(1,955)
Net deferred taxes under U.S. GAAP	(1,398)	190

(40) Additional information on the financial statements in accordance with U.S. GAAP

Consolidated statements of income

The consolidated statements of income and the earnings per share in accordance with U.S. GAAP are presented below.

	2001	2000	1999
	Mio. €	Mio. €	Mio. €
Results from ordinary business activities/Income (loss) before income taxes	(144)	10,882	3,409
Income tax benefit (expense)	504	(1,106)	(1,624)
Income before income applicable to minority shareholders	360	9,776	1,785
Income applicable to minority shareholders	(63)	(70)	(272)
Income in accordance with U.S. GAAP before effect of implementation of SFAS 133 and cumulative effect of SAB 101, in 2001 and 2000, respectively	297	9,706	1,513
Effect due to implementation of SFAS 133/SAB 101, net of tax	226	(437)	—
Net income in accordance with U.S. GAAP	523	9,269	1,513
Basic and diluted earnings per share/ADS under U.S. GAAP (in €)			
Earnings per share before implementation of SFAS 133/SAB 101	0.08	3.21	0.53
Cumulative effect from implementation of SFAS 133/SAB 101	0.06	(0.15)	—
Total earnings per share in accordance with U.S. GAAP	0.14	3.06	0.53
Weighted average shares outstanding — basic (in millions)	3,676	3,030	2,884
Weighted average shares outstanding — diluted (in millions)	3,689	3,030	2,884
Pro forma information: backdated implementation of SAB 101			
Pro forma net income in accordance with U.S. GAAP (in millions)			1,481
Pro forma earnings per share in accordance with U.S. GAAP			0.51

The following table sets forth the computation of weighted average shares outstanding for basic and diluted under U.S. GAAP:

	2001
	(in millions)
Weighted average shares outstanding German GAAP	3,715
Adjustments[(1)]	(39)
Weighted average shares outstanding U.S. GAAP — basic	3,676
Dilutive effect of options, warrants and exchange rights[(2)]	13
Weighted average shares outstanding — diluted	3,689

(1) Under U.S. GAAP, the weighted average shares outstanding has been adjusted to eliminate 39 million shares held in a trust, which are considered issued and outstanding for German GAAP but not for U.S. GAAP.

(2) Stock options, warrants and exchange rights issued in connection with the acquisition of VoiceStream and Powertel.

A reconciliation is not provided for 2000 and 1999, as the weighted average shares outstanding for both basic and diluted were the same under U.S. GAAP and German GAAP.

Consolidated statements of comprehensive income (loss)

In addition to the contents of the financial statements which must be disclosed in accordance with German GAAP, comprehensive income (loss) must be disclosed under U.S. GAAP. Other comprehensive income (loss) covers certain changes to the shareholders' equity not affecting net income (loss) and not related to capital payments, dividend payments or similar transactions with the shareholders.

	2001	2000	1999
	Mio. €	Mio. €	Mio. €
Net income in accordance with U.S. GAAP	523	9,269	1,513
Other comprehensive income (loss)			
Foreign currency translation	(684)	(480)	177
Unrealized gains on marketable securities, net of tax (€ 0 million in 2001 and 2000, € 196 million in 1999)	67	1,312	176
Reclassification of realized gains included in net income (loss), net of tax (€ 19 million in 2001, € 154 million in 2000 and € 60 million in 1999)	(1,971)	146	56
	(1,904)	1,458	232
Additional minimum pension liability, net of tax (€ 101 million in 2001)	(158)	—	—
Derivatives, net of tax (€ 10 million in 2001)	(14)	—	—
Other comprehensive income (loss)	(2,760)	978	409
Total comprehensive income (loss)	(2,237)	10,247	1,922

Development of comprehensive income

	Foreign currency translation	Unrealized gains on marketable securities	Other developments	Cumulative other comprehensive income (loss)
	Mio. €	Mio. €	Mio. €	Mio. €
December 31, 1998	(541)	345	—	(196)
Changes	177	232	—	409
December 31, 1999	(364)	577	—	213
Changes	(480)	1,458	—	978
December 31, 2000	(844)	2,035	—	1,191
Changes	(684)	(1,904)	(172)	(2,760)
December 31, 2001	(1,528)	131	(172)	(1,569)

Balance sheet presentation under U.S. GAAP

German GAAP does not require presentation of a classified balance sheet. Under U.S. GAAP, all receivables due after one year and all liabilities payable after one year are classified as noncurrent. Summarized balance sheet information measured and classified in accordance with U.S. GAAP is as follows:

	2001	2000
	Mio. €	Mio. €
Assets		
Current assets		
Cash and cash equivalents	2,622	1,014
Other current assets	15,291	16,259
	17,913	17,273
Noncurrent assets	162,811	117,903
Total assets	180,724	135,176
Shareholders' equity and liabilities		
Current liabilities		
Short-term debt	13,753	15,213
Other liabilities	13,308	9,103
Accruals	6,489	5,881
Deferred purchase price debis	4,609	4,609
	38,159	34,806
Long-term liabilities		
Long-term debt	52,654	45,092
Other noncurrent liabilities	12,914	6,794
	65,568	51,886
Minority interest	3,293	2,376
Shareholders' equity		
Capital stock	10,746	7,756
Additional paid-in capital	52,726	24,006
Retained earnings, unappropriated net income carried forward from previous year and net income	11,808	13,162
Total other comprehensive income	(1,569)	1,191
Treasury shares	(7)	(7)
	73,704	46,108
Total shareholders' equity and liabilities	180,724	135,176

(41) Other information

(a) Stock-based compensation

The Company has elected to account for employee stock options under U.S. GAAP in accordance with Accounting Principles Board Opinion No. 25 (APB 25), *Accounting for Stock Issued to Employees* and related interpretations and to furnish the pro forma disclosures required under SFAS No. 123, *Accounting for Stock-Based Compensation*.

APB 25 requires recognition of compensation expense for variable award plans (Deutsche Telekom and T-Online) over the vesting period of such plans, based upon the then-current market values of the underlying stock. In contrast, SFAS 123 requires recognition of compensation expense for grants of stock options over the vesting period of such grants, based on the estimated grant-date fair values of those grants.

Under APB 25, the 2001 stock option for plans for both Deutsche Telekom AG and T-Online International AG were considered fixed plans. The 2000 plans for both companies were considered variable plans. As the exercise price of Deutsche Telekom AG's and T-Online International AG's employee stock options was higher than the market price of the underlying stock at the end of both years, no compensation expense was recognized in 2001 or 2000. Another one of Deutsche Telekom's subsidiaries has a stock-based compensation program which is not disclosed since it was deemed immaterial to the Company's financial statements.

Pro forma fair value disclosures

SFAS 123 requires presentation of pro forma information as if the company had accounted for its employee stock based compensation under the fair value method of that statement. The alternative fair value accounting provided for under SFAS 123 requires use of option valuation models that were not developed for use in valuing employee stock options. The fair value of the stock options issued in conjunction with the 2001 and 2000 stock option plans were calculated at the grant date based on a Black-Scholes option pricing model for 2001 and based on a Monte-Carlo option pricing model for 2000. The fair values were calculated in accordance with the terms of the issuance. The Monte-Carlo option pricing model was used for 2000, as the plan was considered a variable compensation plan. This model simulates multiple paths for the stock and the index between Year 2 and Year 5 (3.5) given their initial levels and takes the expected value of the payoff.

Both the Black-Scholes and Monte-Carlo option valuation models were developed for use in estimating the fair value of traded options which have no vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions including the expected stock price volatility. Because the Company's employee stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion, the existing models do not necessarily provide a reliable single measure of the fair value of its employee stock options.

At the grant dates, the underlying assumptions and the resulting fair values per option of the respective companies were as follows:

Deutsche Telekom AG	2001	2000
Expected dividend yield	3.25%	1.00%
Expected stock volatility	47.0%	44.0%
Risk-free interest rate	4.65%	5.73%
Expected lives (in years)	5	5
Employee stock options fair value (in €)	4.87	25.08

T-Online International AG	2001	2000
Expected dividend yield	0%	0%
Expected stock volatility	60.0%	60.0%
Risk-free interest rate	4.65%	5.475%
Expected lives (in years)	5	3.5
Employee stock options fair value (in €)	3.72	13.10

For purposes of pro forma disclosure, the estimated fair value of the options at the date of grant is amortized to expense over the vesting period. Under the fair value method, the Company's net income (loss) and earnings (loss) per share would have been as follows:

	2001	2000	1999
Net income (millions of €)			
As reported under U.S. GAAP	523	9,247	1,513
Pro forma under SFAS No. 123	498	9,244	*
Basic earnings per share (€)			
As reported under U.S. GAAP	0.14	3.05	0.53
Pro forma under SFAS No. 123	0.14	3.05	*
Diluted earnings per share (€)			
As reported under U.S. GAAP	0.14	n/a	*
Pro forma under SFAS No. 123	0.13	n/a	*

* There were no stock-based compensation plans in the Deutsche Telekom group in 1999.

(b) Asset-backed securitization

In December 2001, the Company began selling certain customer accounts receivable to a Qualifying Special Purpose Entity (QSPE) in a securitization. The contractual arrangement to sell these receivables expires in December 2006. Under German GAAP, the determination of the gain or loss on the sale of receivables is based upon contractual estimates for the credit and dilution discounts. In accordance with SFAS No. 140, "*Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*" for U.S. GAAP purposes, the gain or loss on sale of the receivables depends in part on the previous carrying amount of the financial assets involved in the transfer, allocated between the assets sold and the interests and obligations retained, based on their relative fair values at the date of transfer.

Solely for purposes of credit enhancement from the perspective of the QSPE, the Company retains an interest in the sold receivables (retained interests). The retained interests represent the cash flows resulting from the difference between the contractual credit loss and dilution discounts and the performance of the receivables. These retained interests are initially measured at the contractual discounts applied in the transaction, and are subsequently measured based on a periodic evaluation of actual collections and delinquencies. These assumptions are updated periodically based on actual credit loss experience and market interest rates. The contractual discount rate in 2001 was 6.5%, which includes a 3.5% credit loss rate. The estimated credit loss and dilution discount rates utilized are materially consistent with historical performance. The difference resulting from the fair value concept under U.S. GAAP and contract value under German GAAP results in an EUR 21 million reduction of the retained interest under U.S. GAAP as compared to German GAAP.

The Company retains servicing responsibility related to the sold receivables and has estimated the servicing liability for future costs to be incurred on the sold receivables to be EUR 50 million. This estimate is based on internal costs and is not recognized under German GAAP.

During 2001, the following cash flows were received from and paid to the QSPE:

	2001
	(millions of €)
Gross trade receivables sold to QSPE	2,962
Collections made on behalf of QSPE	(1,456)
Discounts	(71)
Increase in retained interest	(51)
Net cash received from QSPE	1,384

Cash settlement with the QSPE takes place monthly on a net basis and occurs during the following month. Gross trade receivables sold represent the face value of all receivables sold during the year to the QSPE. As the Company services the receivables, collections of the receivables previously sold is made on behalf of the QSPE. Under U.S. GAAP, the Company records all applicable program fees and other transaction costs at the point of sale of receivables to the QSPE.

At December 31, 2001, the face value of gross trade receivables held by the QSPE was EUR 1,482 million. Under U.S. GAAP, the retained interests included in other assets was EUR 51 million and sales of receivables resulted in a loss of approximately EUR 79 million, which includes recognition of the service liability and the difference between the face value and the contract value of the receivables.

(c) Equity method investments

Deutsche Telekom has numerous investments, ranging from 20% to 50%, in companies that operate in similar lines of business. Deutsche Telekom's investments in equity method affiliates under U.S. GAAP amounted to EUR 4.1 billion and EUR 7.1 billion at December 31, 2001 and December 2000, respectively. Deutsche Telekom's equity in net earnings (losses) of its equity method affiliates under U.S. GAAP was EUR (653) million, EUR 2.7 billion and EUR (265) million for the years 2001, 2000 and 1999, respectively.

Deutsche Telekom received dividends based on its equity interests in these companies of EUR 2,768 million, EUR 29 million and EUR 7 million for the years 2001, 2000 and 1999, respectively.

The schedules below present summarized statement of operations and balance sheet information of the investments that are accounted for under the equity method that were significant in 2001. Comparable information for 2000 and 1999 is also presented. This information is presented on a U.S. GAAP basis and presents the various adjustments that Deutsche Telekom records to reflect its accounting for the investments.

Statements of Operations

	For the year ended December 31, 2001							
	MTS	PTC	Ben	Virgin Mobile	Telesens	comdirect	Other Equity Investments	Total Equity Investments
					millions of €			
Net revenue	998	1,187	448	264	82	236	1,422	4,637
Total expenses	(632)	(1,044)	(633)	(367)	(304)	(387)	(1,561)	(4,928)
Income/(loss) before income taxes and minority interest	366	143	(185)	(103)	(222)	(151)	(139)	(291)
Income Taxes	(109)	(9)	—	—	(23)	(10)	(80)	(231)
Minority interest	(7)	—	—	—	—	—	—	(7)
Income before effect of change in accounting principle and extraordinary gain (loss)	250	134	(185)	(103)	(245)	(161)	(219)	(529)
Cumulative effect of change in accounting principle, net of income taxes	(20)	(1)	—	(1)	—	—	—	(22)
Extraordinary gain (loss), net of income taxes	2	—	—	—	—	—	—	2
U.S. GAAP net income/(loss)	232	133	(185)	(104)	(245)	(161)	(219)	(549)
Deutsche Telekom's percentage of ownership in investee	36.20%	45.00%	49.99%	50.00%	25.92%	21.35%		
Deutsche Telekom's equity in net earnings (losses) of equity investees under U.S. GAAP	84	60	(92)	(52)	(64)	(34)	(26)	(124)
Consolidation adjustments:								—
Goodwill amortization	(2)	(80)	(54)	—	—	(33)	—	(169)
Intangible asset amortization	—	(12)	—	—	—	—	—	(12)
Impairment charges	—	—	—	—	(13)	(226)	—	(239)
Other	8	(27)	(7)	(2)	2	(4)	(79)	(109)
Deutsche Telekom's equity in net earnings (losses) of equity investees, including consolidating adjustments, under U.S. GAAP	90	(59)	(153)	(54)	(75)	(297)	(105)	(653)

	For the year ended December 31, 2000							
	MTS	PTC	Ben (Acquired in Oct 2000)	Virgin Mobile	Telesens	comdirect	Other Equity Investments	Total Equity Investments
				millions of €				
Net revenue	582	879	246	113	42	314	5,533(a)	7,709
Total expenses	(435)	(841)	(470)	(290)	(84)	(288)	(796)	(3,204)
Income/(loss) before income taxes and minority interest	147	38	(224)	(177)	(42)	26	4,737	4,505
Income Taxes	(56)	(8)	—	—	12	(23)	(84)	(159)
Minority interest	7	—	—	—	—	—	—	7
U.S. GAAP net income/(loss)	98	30	(224)	(177)	(30)	3	4,653	4,353
Deutsche Telekom's percentage of ownership in investee	36.20%	45.00%	49.99%	50.00%	25.92%	21.35%		
Deutsche Telekom's equity in net earnings (losses) of equity investees under U.S. GAAP	35	14	(19)	(89)	(8)	1	2,282	2,216
Consolidation adjustments:								
Goodwill amortization	(3)	(55)	(9)	—	—	(25)	—	(92)
Intangible asset amortization	—	(5)	—	—	—	—	—	(5)
Dilution gains	111	—	—	—	72	449	—	632
Other	16	(6)	(1)	8	4	(1)	(103)	(83)
Deutsche Telekom's equity in net earnings (losses) of equity investees, including consolidating adjustments, under U.S. GAAP	159	(52)	(29)	(81)	68	424	2,179	2,668

(a) Net revenue for the year ended December 31, 2000 include EUR 4.6 billion in proceeds from the sale by DT-FT Italian Holding GmbH of its 49% ownership interest in WIND Telecomunicazioni S.p.A.

	For the year ended December 31, 1999							
	MTS	PTC	Ben	Virgin Mobile	Telesens	comdirect	Other Equity Investments	Total Equity Investments
				millions of €				
Net revenue	337	614	—	14	5	—	524	1,494
Total expenses	(241)	(638)	—	(55)	(27)	—	(564)	(1,525)
Income/(loss) before income taxes and minority interest	96	(24)	—	(41)	(22)	—	(40)	(31)
Income Taxes	(18)	(9)	—	—	8	—	(5)	(24)
Minority interest	2							2
U.S. GAAP net income/(loss)	80	(33)	—	(41)	(14)	—	(45)	(53)
Deutsche Telekom's percentage of ownership in investee	45.90%	22.50%	—	50.00%	39.00%			
Deutsche Telekom's equity in net earnings (losses) of equity investees under U.S. GAAP	37	(8)	—	(21)	(5)	—	(229)	(226)
Consolidation adjustments:								
Goodwill amortization	(1)	—	—	—	—	—	—	(1)
Other	22	(1)	—	6	5	—	(70)	(38)
Deutsche Telekom's equity in net earnings (losses) of equity investees, including consolidating adjustments, under U.S. GAAP	58	(9)	—	(15)	—	—	(299)	(265)

Balance Sheets

	December 31, 2001							
	MTS	PTC	Ben	Virgin Mobile	Telesens	comdirect	Other Equity Investments	Total Equity Investments
	millions of €							
Current assets	543	300	126	80	34	2,017	712	3,812
Non-current assets	1,398	1,823	1,032	41	101	957	4,449	9,801
Total assets	1,941	2,123	1,158	121	135	2,974	5,161	13,613
Current liabilities	341	248	526	105	39	2,394	1,390	5,043
Non-current liabilities	439	1,591	10	282	30	2	2,120	4,474
Minority interest	15	—	—	—	—	—	12	27
Shareholders' equity/(deficit)	1,146	284	622	(266)	66	578	1,639	4,069
Total liabilities and shareholders' equity/(deficit)	1,941	2,123	1,158	121	135	2,974	5,161	13,613
Deutsche Telekom's investment in and advances to equity investees at cost plus equity in undistributed earnings (losses) since acquisition	435	1,215	888	—	9	328	1,223	4,098
Deutsche Telekom's percentage of ownership in investee	36.20%	45.00%	49.99%	50.00%	25.92%	21.35%		

	December 31, 2000							
	MTS	PTC	Ben	Virgin Mobile	Telesens	comdirect	Other Equity Investments	Total Equity Investments
	millions of €							
Current assets	351	235	120	45	97	1,580	5,981	8,409
Non-current assets	822	1,572	897	45	265	1,295	1,431	6,327
Total assets	1,173	1,807	1,017	90	362	2,875	7,412	14,736
Current liabilities	195	562	198	111	51	2,134	635	3,886
Non-current liabilities	125	1,088	12	143	4	1	1,077	2,450
Minority interest	—	—	—	—	—	—	20	20
Shareholders' equity/(deficit)	853	157	807	(164)	307	740	5,680	8,380
Total liabilities and shareholders' equity/(deficit)	1,173	1,807	1,017	90	362	2,875	7,412	14,736
Deutsche Telekom's investment in and advances to equity investees at cost plus equity in undistributed earnings (losses) since acquisition	327	1,160	1,041	—	81	624	3,824	7,057
Deutsche Telekom's percentage of ownership in investee	36.20%	45.00%	49.99%	50.00%	25.92%	21.35%		

(d) Derivatives

Accounting Standard

In June 1998, the Financial Accounting Standards Board (FASB) issued SFAS No. 133, ''Accounting for Derivative Instruments and Hedging Activities (SFAS 133).'' This statement became effective for Deutsche Telekom on January 1, 2001 and establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts, (collectively referred to hereafter as derivatives) and for hedging activities. It requires recognition of all derivatives on the balance sheet at fair value, regardless of the hedging relationship designation. Derivative instruments must be classified as hedging transactions (either fair value hedges, cash flow hedges, foreign currency fair value hedges, foreign currency cash flow hedges or hedges of the net investment in a foreign operation) or non-hedging transactions, and the accounting treatment of derivative instruments and hedged items depends on this classification. Changes in the fair value of derivatives designated as highly effective in fair value hedging relationships are recognized in current period earnings along with fair value changes of the hedged item attributable to the hedged risk. Changes in the fair value of derivatives designated in cash flow hedging relationships are recorded in other comprehensive income and are recognized in earnings when the hedged item affects earnings. Any hedge ineffectiveness is recorded in current-period earnings. Changes in the fair value of a derivative that is designated and qualifies as a foreign-currency hedge is recorded in either current-period earnings or other comprehensive income, depending on whether the hedging relationship satisfies the criteria for a fair-value or cash-flow hedge. If a derivative is used as a hedge of a net investment in a foreign operation, the changes in the derivative's fair value, to the extent that the derivative is effective as a hedge, are recorded in other comprehensive income (outside earnings) as part of the cumulative translation adjustment. Changes in the fair value of derivative instruments that are not designated as hedging instruments are recognized in earnings when they occur.

Risk Management Policies

Deutsche Telekom is exposed to foreign currency risks, interest rate risks and equity price risks arising from fluctuations in exchange rates, interest rates and quoted share prices. The Company's risk policy generally only takes into account risks affecting the Group's cash flows. Therefore, fair value changes of investments arising from fluctuations in quoted share prices as well as foreign currency translation risks inherent in Telekom's net investments in foreign entities are not normally hedged. Deutsche Telekom does not enter into derivative financial instruments for trading purposes or other speculative purposes.

Deutsche Telekom is exposed to interest rate risks, primarily in the European Union, in Great Britain and in the United States. Interest management is performed separately for each of the main currencies. Once a year Deutsche Telekom's Management Board specifies a desired mixture of fixed- and floating-rate net debt in each main currency. Consequently, the Company's Central Treasury Group enters into interest rate derivatives to modify the interest payments on bonds, other liabilities and cash investments to adjust their risk profile to the defined target mixture. Interest rate swaps in particular are used as well as purchased interest rate options (such as caps and collars).

Foreign currency risks arise from Telekom's investing, financing and operating activities. Since Telekom's corporate objective is pursued through its commercial operations — meaning the sale of telecommunications services — unwanted foreign currency exposures are normally hedged, provided the risks would affect the Group's cash flows. Foreign currency risks that do not affect the Group's cash flows (risks resulting from the translation of Deutsche Telekom's foreign entities' assets and liabilities to the Group's reporting currency) generally remain unhedged. However, in specific circumstances, Deutsche Telekom seeks to hedge the foreign currency translation risk inherent in certain foreign entities.

Initial Application of SFAS 133

On January 1, 2001, Deutsche Telekom recognized all freestanding derivative instruments as either assets or liabilities and measured them at fair value under U.S. GAAP. The differences between the derivatives' previous carrying amounts and their fair values were reported as transition adjustments. Because Deutsche Telekom's foreign currency forward contracts, foreign currency options and cross-currency interest rate swaps were already recognized at fair value at December 31, 2000, transition adjustments were only required for certain interest rate derivatives.

The majority of Deutsche Telekom's interest rate derivatives entered into before January 1, 2001 were used to create synthetic financial instruments (mostly synthetic debt). Thus, for example, Deutsche Telekom sold 30 year fixed-rate U.S. dollar notes and simultaneously entered into a combination of interest rate swaps and cross-currency interest swaps to effectively create a 10 year fixed-rate British pound borrowing. Adjusting the interest rate swaps' previous carrying amounts (accrued interest payables and receivables) to their fair values resulted in a net gain of EUR 226 million (after taxes of EUR 144 million) on January 1, 2001, which was reported as a cumulative-effect-type adjustment of net income.

A smaller number of interest rate swaps as well as interest rate collars entered into before January 1, 2001 were used to reduce the cash flow exposure of floating-rate British pound liabilities. The transition adjustments for these derivatives resulted in a loss of EUR 22 million (after taxes of 10 million) which was reported as a cumulative-effect-type adjustment of accumulated other comprehensive income on January 1, 2001 and will be reclassified into earnings in future fiscal years when interest payments on the floating-rate liabilities affect earnings. The derivatives were not redesignated as hedging instruments at January 1, 2001.

Deutsche Telekom's other interest rate derivatives were already recognized at fair value on December 31, 2000 and no transition adjustments for these derivatives were therefore required.

No derivative or nonderivative hedging instrument entered into before January 1, 2001 was designated anew as a hedging instrument at January 1, 2001 except for a British pound denominated borrowing that hedged the foreign currency exposure of a portion of Deutsche Telekom's net investment in One 2 One.

Post-Transition-Date Accounting under SFAS 133

Using financial analysis, such as Value-at-Risk analysis, to identify the extent of a derivative's potential gain or loss, Deutsche Telekom Central Treasury decides on the date that it enters into a derivative contract whether it is efficient to seek hedge accounting for the derivative. If Central Treasury elects to apply hedge accounting, it puts in place the appropriate hedge documentation and effectiveness testing routine at inception of the hedge.

Fair value hedges

In the middle of 2001, Deutsche Telekom entered into pay-variable, receive-fixed interest rate swaps to hedge the fair value risk of fixed rate Euro debt. These interest rate swaps were designated as fair value hedging instruments. They meet all the required criteria of SFAS 133 for the assumption of perfect hedge effectiveness. Accordingly, gains from adjusting the carrying amounts of the interest rate swaps to their fair values of EUR 68 million and from adjusting the carrying amount of the debt (resulting in losses of EUR 68 million) completely offset each other.

Cash flow hedges

There were no new derivatives designated as cash flow hedging instruments during 2001. However, losses on interest rate derivatives of EUR 22 million (after taxes of 10 million) were reported in accumulated other comprehensive income on January 1, 2001 as a result from the initial application of SFAS 133. Losses of EUR 8 million (after taxes of 3 million) associated with this transition adjustment were reclassified into earnings during 2001. The same amount is expected to be reclassified as earnings within the next twelve months.

Net investment hedges

Deutsche Telekom continued to hedge the foreign currency translation risk inherent in a portion of its net investment in One 2 One with British pound denominated borrowings through 2001. At June 1, 2001 Telekom designated U.S. dollar forward sale contracts (U.S. dollar versus Euro sales) as hedges of the foreign currency translation risk inherent in shares of the preferred stock in VoiceStream, which form a part of Deutsche Telekom's net investment in VoiceStream. Gains and losses on these derivative and nonderivative financial instruments were reported in other comprehensive income (shareholders' equity) along with gains and losses resulting from the translation of the net assets of the mentioned foreign subsidiaries at current spot rates. When using derivatives as hedging instruments, Deutsche Telekom measures hedge effectiveness of such hedges based on the changes in forward rates. Between January 1, and December 31, 2001, a net gain of EUR 78 million (after taxes of zero) on the derivative and nonderivative hedging instruments was reported in other comprehensive income as part of the cumulative translation adjustment. No hedge ineffectiveness occurred during the respective period.

All other derivatives

Certain derivative transactions, while providing effective economic hedges under the Group's risk management policies, do not qualify for hedge accounting under the specific rules in SFAS 133. Thus, for example, Deutsche Telekom uses forward foreign currency contracts and foreign currency options to hedge the transaction risk arising from the forecasted purchase of a foreign subsidiary that will be fully consolidated after the acquisition. Hedge accounting is not permissible for such hedging relationships under SFAS 133.

For derivatives that hedge the foreign currency transaction risk of recognized foreign currency denominated assets or liabilities, a special hedge accounting is not necessary, because the transaction gain or loss on the hedged foreign currency denominated asset or liability will be reported in earnings along with the gain or loss on the undesignated derivative.

Furthermore, for certain derivatives Deutsche Telekom Central Treasury did not elect to apply hedge accounting on the date that it entered into the derivative.

As of December 31, 2001, Deutsche Telekom reported the fair value of derivative instrument assets of EUR 1.9 billion in other non-current assets and derivative instrument liabilities of EUR 1.8 billion in other current liabilities for the purpose of a balance sheet presentation in accordance with U.S. GAAP. These amounts reflect no netting of derivative instrument assets and liabilities.

(e) Related Party Transactions

Coordination and Administrative Responsibilities of the Federal Agency

Pursuant to German law, the Federal Agency provides certain services to Deutsche Telekom, Deutsche Postbank and Deutsche Post and has certain rights and responsibilities with respect to the administration of the common affairs of these companies. For example, the Federal Agency is responsible for concluding general collective bargaining agreements (*Manteltarifverträge*) on behalf of these entities with employees relating only to certain non-wage benefits, rules of conduct and other general terms of employment. These agreements only become effective with the consent of the affected entity. The Federal Agency's right to conclude these agreements does not affect Deutsche Telekom's right to negotiate particular terms of employment, including wages, salaries and conditions of employment, independently on its own behalf. The Federal Agency also administers the health insurance fund for civil servants (*Postbeamtenkrankenkasse*) and the pension fund for non-civil servants (VAP) employed by Deutsche Telekom, Deutsche Postbank, Deutsche Post and others. The Federal Agency has certain additional responsibilities and rights with respect to civil servants employed by Deutsche Telekom, Deutsche Post and Deutsche Postbank. The Federal Agency has the right to provide advice concerning the coordination of the activities of Deutsche Telekom, Deutsche Postbank and Deutsche Post, particularly, with respect to their public image, issues that may arise if the business plans of these entities conflict and, upon request, with respect to certain personnel issues.

Services provided by the Federal Agency pursuant to applicable law are rendered on the basis of service agreements between Deutsche Telekom, Deutsche Postbank or Deutsche Post, on the one hand, and the Federal Agency, on the other. Since German law currently requires that each of Deutsche Telekom, Deutsche Postbank and Deutsche Post enter into a service agreement with the Federal Agency covering the services described above, Deutsche Telekom has not considered entering into arrangements with third parties for the provision of these services. The total costs of the Federal Agency, consisting mainly of personnel costs for its employees, are allocated pursuant to the cost attribution system of the Federal Agency in accordance with actual expenses. Costs of the Federal Agency incurred in connection with providing these services are financed from fees agreed upon with Deutsche Telekom, Deutsche Post and Deutsche Postbank. Deutsche Telekom paid costs of EUR 70 million, EUR 78 million, and EUR 75 million in 2001, 2000, and 1999, respectively.

Federal Republic as Regulator

The Federal Republic's role as regulator is independent and distinct from its role as shareholder. This regulatory function is exercised by the Regulatory Authority.

Federal Republic and Affiliated Entities as Customers

The Federal Republic is Deutsche Telekom's largest customer and purchases services on an arm's-length basis. Deutsche Telekom deals with the various departments and agencies of the Federal Republic of Germany as separate customers, and the provision of services to any one department or agency does not constitute a material part of Deutsche Telekom's revenues. Deutsche Telekom also entered into contracts to provide telecommunications services to entities affiliated with the Federal Republic, principally Deutsche Post, on an arm's-length basis in the ordinary course of business.

Arrangement with Deutsche Post

Deutsche Telekom entered into an agreement with Deutsche Post AG in 2000 that calls for Deutsche Telekom to provide, among other things, information technology and corporate network services to Deutsche Post. In return, Deutsche Post provides distribution and transportation, printing, warehousing and other services. The objective of the arrangement is to allow each company to focus on its core competencies and dispose of peripheral activities. The arrangement resulted in a net transfer of 1,500 Deutsche Telekom employees to Deutsche Post in 2001.

Arrangements with Deutsche Postbank AG

Deutsche Telekom has a credit facility with Deutsche Postbank AG amounting to EUR 200 million in both 2001 and 2000. A second credit facility existed at the end of 2001 for EUR 354 million.

Acquisition of UMTS licenses from Federal Republic

In 2000 Deutsche Telekom acquired UMTS licenses from the Federal Republic at an auction price of EUR 8,540 million.

Federal Republic Guarantees

Under German law, all liabilities of Deutsche Telekom outstanding as of January 2, 1995, the date of Deutsche Telekom's registration in the Commercial Register (*Handelsregister*), became guaranteed by the Federal Republic. This guarantee replaced the Federal Republic's obligations with respect to Deutsche Telekom's liabilities when it was a state-owned special asset. Liabilities incurred after January 2, 1995 are not guaranteed by the Federal Republic. See footnote (29) Liabilities for additional information.

Pension Contributions for Civil Servants

Civil servants (*Beamte*) employed by Deutsche Telekom are entitled to pension benefits provided by the Federal Republic. Under German law, Deutsche Telekom is required to make annual contributions to a special pension fund (*Unterstützungskasse*) established to fund these pension obligations. Deutsche Telekom's contributions amounted to EUR 845 million, EUR 895 million and EUR 1,500 million in 2001, 2000, and 1999, respectively.

Real Estate Investigation

Deutsche Telekom is advancing funds to cover the legal expenses being incurred by current and former board members in connection with the Bonn public prosecutors investigation of certain real estate valuation-related questions. These funds will be required to be repaid to Deutsche Telekom if there is a final determination that these individuals violated the law.

Telecommunication Services

Deutsche Telekom provides telecommunications services to numerous companies, mainly throughout Europe, in the ordinary course of business, including firms in which it holds an ownership interest and firms with which certain members of the Supervisory Board are affiliated.

(f) Recently issued U.S. GAAP accounting standards

In June 2001, the FASB issued Statement of Financial Accounting Standards (SFAS) No. 141, "Business Combinations," and SFAS No. 142, "Goodwill and Other Intangible Assets." SFAS 141 supersedes APB Opinion 16, "Business Combinations," and SFAS No. 38, "Accounting for Pre-acquisition Contingencies of Purchased Enterprises." This statement requires that the purchase method of accounting be used for all business combinations initiated after June 30, 2001, and changes the criteria for recognizing intangible assets apart from goodwill. SFAS 142 supercedes APB Opinion 17, "Intangible Assets," and addresses how purchased intangibles should be accounted for upon acquisition. The statement prescribes the necessary accounting for both identifiable intangibles and goodwill after initial recognition. SFAS 142 requires that goodwill, including net book value associated with equity method investments, and indefinite lived intangible assets no longer be amortized upon adoption of this statement, but instead tested for impairment at least annually. Amortization of definite lived intangibles will continue over the useful life. For U.S. GAAP reporting, the provisions of SFAS 141 apply to all business combinations initiated after June 30, 2001. The provisions of SFAS 142 are required to be applied starting with fiscal years beginning after December 15, 2001, except for the nonamortization provisions for goodwill and indefinite-lived intangible assets acquired after June 30, 2001, which will be subject immediately to provisions of this statement. The Company has adopted the provisions of SFAS 141 for its acquisition of Croatian Telecom (Croatian Telecom). See further discussion in note (20).

As a result of the implementation of SFAS 142, a number of major wireless carriers in the United States have concluded that the U.S. Federal Communications Commission (''FCC'') wireless spectrum licenses should be considered to be intangible assets with indefinite lives under SFAS 142. Classification by Deutsche Telekom of the FCC licenses as indefinite lived would require scheduled amortization of licenses to cease commencing January 1, 2002 and trigger a number of related issues, the treatment of which is currently being evaluated. These issues include the method of testing for impairment and accounting for deferred income taxes related to the change to indefinite lives. Prior to January 1, 2002, these licences were treated as intangibles with definite lives and the reversal of their related deferred tax liabilities was deemed to match the realization of the deferred tax assets and, as such, no valuation allowance for the deferred tax asset was necessary. If it is concluded that the FCC licenses are indefinite, however, subsequent to January 1, 2002, the deferred tax liabilities associated with these licenses would no longer be available to support the realization of the VoiceStream and Powertel deferred tax assets or future deferred tax assets because of the resulting indefinite timing of the reversal of such deferred tax liabilities. Therefore, a reassessment of the useful lives of the licenses would require Deutsche Telekom for U.S. GAAP purposes to record a valuation allowance with a corresponding charge to earnings of EUR 4.3 billion in the first quarter of 2002 relating to all of the VoiceStream and Powertel deferred tax assets. These deferred tax assets were recorded in respect of net operating loss carryforwards assumed upon the acquisition of VoiceStream and Powertel in May 2001.

Deutsche Telekom is currently assessing whether the change in the amortization of the FCC licenses for U.S. GAAP purposes should have any implications on its net income under German GAAP as well and the further impact of the implementation of SFAS 141 and 142 on its results of operations, financial position, and cash flows, except for the non-amortization provision of goodwill which was considered upon the acquisition of Croatian Telecom.

In July 2001, the FASB issued SFAS 143, ''Accounting for Asset Retirement Obligations.'' The objective of this statement is to provide accounting guidance for legal obligations associated with the retirement of long-lived assets. SFAS 143 requires that the fair value of a liability for an asset retirement obligation be recognized in the period in which it is incurred and accreted to its present value each period. The associated asset retirement costs are capitalized as part of the carrying amount of the long-lived asset and subsequently depreciated over the asset's useful life. The statement is effective for financial statements issued for fiscal years beginning after June 15, 2002. Deutsche Telekom is currently determining the impact of the adoption of SFAS 143 on its results of operations, financial position and cash flows.

In October 2001, the FASB issued SFAS 144, ''Accounting for the Impairment or Disposal of Long-Lived Assets.'' This new standard supersedes SFAS 121, ''Accounting for the Impairment of Long-Lived Assets and for the Long-Lived Assets to be Disposed Of'', providing one accounting model for the review of asset impairment. SFAS 144 retains the current requirement to recognize an impairment loss only if the carrying amounts of long-lived assets to be held and used are not recoverable from their expected undiscounted future cash flows and exceeds its fair value. However, goodwill is no longer required to be allocated to these long-lived assets when determining their carrying amounts. SFAS 144 requires that a long-lived asset to be disposed of other than by sale be considered held and used until it is disposed of, requiring the depreciable life to be adjusted as an accounting change. The criteria used to classify long-lived assets to be disposed of by sale have changed from SFAS 121. However, the statement continues to require that the amortization and depreciation of all long-lived assets to be disposed of by sale cease and that these assets be recorded at the lower of their carrying amount or fair value less cost to sell. Statement 144 also supersedes the section of the APB Opinion 30 which prescribes reporting for the effects of a disposal of a segment of a business. Discontinued operations are no longer measured on a net realizable value basis, and future operating losses are no longer recognized before they occur. The statement also broadens the definition of a discontinued operation to include a component of an entity. The provisions of SFAS 144 are effective for financial statements issued for fiscal years beginning after December 15, 2001, and interim periods within those fiscal years. The Company has assessed the impact of adopting this statement to be an asset write-down of approximately EUR 50 million, which will be recorded for U.S. GAAP during the first quarter of 2002.

(g) Subsequent Events

In March 2002, T-Mobile Deutschland entered into lease financing arrangements (the ''Lease Transactions'') whereby certain equipment, mainly GSM infrastructure and software, was leased to several US-based trusts (the ''US Trusts'') and leased back to T-Mobile Deutschland. Concurrent with entering into the Lease Transactions, T-Mobile Deutschland entered into payment undertaking agreements with two counter-parties, whereby the counter-parties agreed to make certain payments to the Trusts on behalf of T-Mobile Deutschland in exchange for an irrevocable payment of EUR 905 million equal to the scheduled rent payable by T-Mobile Deutschland and, if fixed price purchase options in the lease backs are exercised, the exercise prices of these options. For German GAAP purposes, the difference between the cash proceeds from the US Trusts and the amounts paid by T-Mobile Deutschland pursuant to the payment undertaking agreements represents a gain on the transfer of a tax benefit between T-Mobile Deutschland and the US Trusts, which amounted to EUR 60 million, net of transaction costs of EUR 7 million. This gain has been deferred and is being recognized as other operating income over the 16-year lease back term. For U.S. GAAP purposes, T-Mobile Deutschland applies Statement of Financial Accounting Standards No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*, to the Lease transactions, pursuant to which the US Trusts are consolidated into T-Mobile Deutschland. As a result, T-Mobile Deutschland eliminated all transactions between T-Mobile Deutschland and the US Trusts and consolidated the US Trusts' assets, liabilities, and results of operations.

Bonn, March 18, 2002

Deutsche Telekom AG
Board of Management

Dr. Ron Sommer
Dr. Karl-Gerhard Eick
Dr. Max Hirschberger
Kai-Uwe Ricke
Josef Brauner
Jeffrey A. Hedberg
Dr. Heinz Klinkhammer
Gerd Tenzer

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BEN NEDERLAND HOLDING B.V.

CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2001

BEN NEDERLAND HOLDING B.V.

CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2001

CONTENTS

DIRECTORS

R.G.W. Holekamp (appointed July 4, 2001)
S.M. Fries (appointed July 4, 2001)
J.J.A. van Leeuwen (appointed July 4, 2001)
W.A.L. Schrijver (appointed July 4, 2001; resigned October 16, 2001)
P.E. de Weerd († June 18, 2001)
R.D. Whiteside (resigned December 7, 2001)

TO THE SHAREHOLDERS OF
BEN NEDERLAND HOLDING B.V.

REPORT OF INDEPENDENT ACCOUNTANTS

We have examined the accompanying consolidated balance sheets of Ben Nederland Holding B.V., Amsterdam, and its subsidiaries as of December 31, 2001 and 2000 and the related consolidated profit and loss accounts and statements of cash flows, for each of the three years in the period ended December 31, 2001, all expressed in Euros. Our examinations of these statements were made in accordance with auditing standards generally accepted in the United States and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the consolidated financial statements referred to above present fairly the financial position of Ben Nederland Holding B.V., Amsterdam, and its subsidiaries at December 31, 2001 and 2000, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2001, in conformity with accounting principles generally accepted in the Netherlands.

As discussed in Note 2 to the financial statements, the Company changed its method of capitalizing asset construction costs in 2001 and ceased the capitalization of interest costs related to assets under construction in 2000.

Accounting principles generally accepted in the Netherlands vary in certain respects from accounting principles generally accepted in the United States. The application of the latter would have affected the determination of consolidated net loss expressed in Euros for each of the three years in the period ended December 31, 2001 and the determination of consolidated stockholders' equity and consolidated financial position also expressed in Euros at December 31, 2001 and 2000 to the extent summarized in Note 16 to the consolidated financial statements.

PricewaterhouseCoopers N.V.

Amsterdam, The Netherlands
April 24, 2002

BEN NEDERLAND HOLDING B.V.

CONSOLIDATED BALANCE SHEETS
AT DECEMBER 31, 2001 AND 2000
(After proposed appropriation of the result for the years)
(Amounts expressed in thousands of Euros)

	2001	2000
	€'000	€'000
ASSETS		
FIXED ASSETS		
Intangible fixed assets	548,075	549,369
Tangible fixed assets	460,752	335,538
Financial fixed assets	—	23
Total fixed assets	1,008,827	884,930
CURRENT ASSETS		
Short term loans	2,680	6,421
Receivables	83,715	86,142
Inventory	13,064	14,228
Cash and bank balances	26,251	13,166
Total current assets	125,710	119,957
TOTAL ASSETS	1,134,537	1,004,887
SHAREHOLDERS' EQUITY & LIABILITIES		
TOTAL SHAREHOLDERS' EQUITY	608,549	807,415
CURRENT LIABILITIES	525,988	197,472
TOTAL SHAREHOLDERS' EQUITY & LIABILITIES	1,134,537	1,004,887

The accompanying notes form an integral part of these financial statements.

BEN NEDERLAND HOLDING B.V.

CONSOLIDATED PROFIT AND LOSS ACCOUNTS
FOR THE THREE YEARS ENDED DECEMBER 31, 2001
(Amounts expressed in thousands of Euros)

	2001	2000	1999
	€'000	€'000	€'000
Net sales	447,527	244,842	66,655
Cost of sales[1]	(226,546)	(156,633)	(69,757)
Gross profit	220,981	88,209	(3,102)
Operating expenses	(410,039)	(316,390)	(172,585)
Other operating income	482	1,229	470
Operating loss	(188,576)	(226,952)	(175,217)
Net financial expense	(10,290)	(12,427)	(3,716)
Extraordinary income	—	—	16,504
Net loss	(198,866)	(239,379)	(162,429)

(1) Cost of sales excludes depreciation and amortization, which is included in operating expenses.

The accompanying notes form an integral part of these financial statements.

BEN NEDERLAND HOLDING B.V.

CONSOLIDATED CASH FLOW STATEMENTS
FOR THE THREE YEARS ENDED DECEMBER 31, 2001
(Amounts expressed in thousands of Euros)

	2001	2000	1999
	€'000	€'000	€'000
CASH FLOW FROM OPERATING ACTIVITIES			
Result after taxation for the period	(198,866)	(239,379)	(162,429)
Adjustments:			
Depreciation of tangible and intangible fixed assets	75,032	54,785	29,166
Loss on disposal of financial fixed assets	23	—	—
Changes in working capital:			
Decrease/(increase) inventory	1,164	(6,742)	(6,012)
Decrease/(increase) receivables	2,427	(52,982)	(27,495)
Decrease/(increase) short term loans	3,741	557	(3,802)
Decrease/(increase) current liabilities exclusive of shareholder loans	11,947	(46,309)	146,309
	19,279	(105,476)	109,000
Net cash used in operating activities	(104,532)	(290,070)	(24,263)
CASH FLOWS FROM INVESTING ACTIVITIES			
Investment in tangible fixed assets	(163,433)	(128,965)	(192,197)
Disposal of tangible fixed assets	1,382	1,445	1,135
Investment in intangible fixed assets	(36,901)	(432,018)	(21,464)
Investment in financial fixed assets	—	(23)	—
Net cash used in investing activities	(198,952)	(559,561)	(212,526)
CASH FLOWS FROM FINANCING ACTIVITIES			
Paid in capital	—	1,070,714	—
Loans from shareholders	316,569	(214,222)	236,857
Net cash provided by financing activities	316,569	856,492	236,857
NET INCREASE IN CASH	13,085	6,861	68
Cash and cash equivalents beginning of year	13,166	6,305	6,237
Cash and cash equivalents end of year	26,251	13,166	6,305

The accompanying notes form an integral part of these financial statements.

BEN NEDERLAND HOLDING B.V.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE THREE YEARS ENDED DECEMBER 31, 2001**

1. ACTIVITIES

In accordance with Article 2 of its Articles of Association the principal activities of the company are to participate in, to finance, to collaborate with, to conduct the management of companies and enterprises active in the area of telecommunications and to provide advice and all other services.

Furthermore, the company's objective is to exploit, to apply for and to hold all licenses required for establishing a full-scale mobile telecommunications business in the Netherlands and to maintain and operate a mobile telecommunications infrastructure in the Netherlands.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation

The accompanying consolidated financial statements have been prepared in accordance with principles of accounting generally accepted in the Netherlands.

Changes in accounting policies

In 2001, the Company upgraded its accounting system to identify direct costs of Engineering & Operations employees working on assets under construction. These costs were not separately identifiable in prior years. As a result of the accounting system change, the Company began capitalizing these costs beginning January 1, 2001. Total costs capitalized for the year ended December 31, 2001 were EUR 4,595,000. No such costs were capitalized related to prior years.

Up to January 1, 2000 the Company capitalised interest on construction in progress. As of January 1, 2000 all interest is expensed. The balance of € 1,795,000 at December 31, 1999 was charged to income in the year 2000.

Principles of consolidation

Group companies included in the consolidated accounts are those in which the company exercises significant influence. All intercompany balances and transactions are eliminated on consolidation.

Group companies included in the consolidated accounts are as follows:

		Proportion of voting rights held	
	Domicile	**2001**	**2000**
BEN Nederland B.V	The Hague	100%	100%
BEN Klantenservice B.V	The Hague	100%	100%
3 G-Blue B.V	The Hague	—	100%

3 G-Blue B.V. merged into Ben Nederland B.V. in 2001.

Cash flow statement

The cash flow statements are prepared using the indirect method, in accordance with IAS 7.

Foreign currencies

In the profit and loss accounts, all transactions denominated in a currency other than the Euro are translated into Euros at the exchange rate prevailing at the time of the transaction. Assets and liabilities denominated in foreign currencies are translated into Euros at the exchange rates prevailing on the balance sheet dates with differences recorded through the profit and loss account.

Impairment of fixed assets

The carrying amounts of fixed assets are reviewed annually and written down where necessary for impairment.

Intangible fixed assets

Intangible fixed assets are stated at cost less amortisation calculated using the straight-line method over their estimated useful lives.

The DCS-1800 license, acquired in 1998, is carried at cost less amortisation on a straight-line basis from the launch of services to the end of the license period. (15 years).

The UMTS license is carried at cost. This license will be amortised on a straight-line basis, as from the launch of services to the end of the license period. The UMTS license runs through December 31, 2016.

Software licenses and capitalised software development costs are carried at cost less amortisation calculated using the straight-line method evenly over their useful lives of 3 years.

Tangible fixed assets

Tangible fixed assets are stated at cost less accumulated depreciation calculated over their estimated useful lives using the straight-line method.

The estimated useful life for certain network equipment was revised during 2000, and this change was applied prospectively. This had the impact of reducing the annual depreciation charge by approximately € 9 million.

The annual depreciation rates are:

Installation, machinery and equipment	13%-33%
Furniture and fixtures	20%
Leasehold improvements	10%

Financial fixed assets

Participations of less than 20% equity interest are carried at cost. If necessary, provisions are recorded when there are permanent impairments in value. As of 2001, there have been no impairments to date. Income derived from these participations is recognised only when dividends are declared.

Accounts receivable

Subscriber and other debtors are stated at nominal value less a provision for doubtful debts.

Inventory

Inventory, consisting of packaging, handsets, sim-cards and reload vouchers, is carried at cost. Appropriate allowance is made for obsolete and slow-moving goods.

Revenue recognition

Revenues are recorded at the time the service is rendered. Revenues from services rendered are recorded net of discounts and VAT.

Deferred income tax

Deferred income tax is provided, using the liability method, for all temporary differences arising between the tax bases of assets and liabilities and their carrying values for financial reporting purposes. Currently enacted tax rates are used to determine deferred income tax.

Deferred tax assets relating to the carry forwards of unutilised tax losses are recognised to the extent that it is probable that future taxable income will be available against which the unused tax losses can be utilised.

At December 31, 2001, losses available for carry forward (all indefinite) of € 620,988,000 were not recognised in determining the deferred tax asset.

Interest

It is the policy of the Company to expense interest as incurred.

3. FINANCIAL FIXED ASSETS

	2001	2000
	€'000	€'000
Balance at January 1	23	—
Additions/(Disposals)	(23)	23
Balance at December 31	—	23

Ben Nederland B.V. acquired 50 shares (13%) with a nominal value of € 454 in B-Genius, the E-Academy, N.V. on June 5, 2000. The participation has been disposed for NLG 1 in 2001.

4. INTANGIBLE FIXED ASSETS

	€'000
COST	
Balance at January 1, 2001	592,079
Additions	36,901
Disposals	—
Balance at December 31, 2001	628,980
ACCUMULATED AMORTISATION	
Balance at January 1, 2001	(42,710)
Amortisation for the year	(38,195)
Balance at December 31, 2001	(80,905)
Net book value at December 31, 2001	548,075

5. TANGIBLE FIXED ASSETS

	Installations, machinery and equipment	Furniture and fixtures	Leasehold improvements	Assets under construction	Total
	€'000	€'000	€'000	€'000	€'000
AT COST					
Balance at January 1, 2001	169,436	4,729	92,143	110,791	377,099
Additions	57,693	1,823	24,602	85,951	170,069
Disposals	(1,227)	—	(132)	(266)	(1,625)
Transfers from assets under construction	24,757	—	10,545	(41,938)	(6,636)
Balance at December 31, 2001	250,659	6,552	127,158	154,538	538,907
ACCUMULATED DEPRECIATION					
Balance at January 1, 2001	(30,554)	(1,266)	(9,741)	—	(41,561)
Charge for the year	(24,560)	(1,216)	(11,061)	—	(36,837)
Disposals	235	—	8	—	243
Balance at December 31, 2001	(54,879)	(2,482)	(20,794)	—	(78,155)
Net book value at December 31, 2001	195,780	4,070	106,364	154,538	460,752

Assets under construction mainly represent costs incurred in the design and construction of the company's network.

6. RECEIVABLES

	2001	2000
	€'000	€'000
Third party receivables	80,758	79,514
Prepaid expenses	1,034	564
Taxation	1,923	6,064
	83,715	86,142

7. ISSUED SHARE CAPITAL

The total authorised share capital consists of 500,000,000 shares each having a nominal value of € 0,45 (NLG 1), of which 199,999,998 have been issued and fully paid at December 31, 2001 (2000: € 90,756,042).

8. SHARE PREMIUM ACCOUNT

	2001	2000
	€'000	€'000
Balance at January 1	1,138,781	113,445
Share premium paid on shares issued	—	1,025,336
Balance at December 31, 2001	1,138,781	1,138,781

9. ACCUMULATED DEFICIT

	2001	2000
	€'000	€'000
Balance at January 1	(422,122)	(182,743)
Current year net result/(loss)	(198,866)	(239,379)
Balance at December 31	(620,988)	(422,122)

10. CURRENT LIABILITIES

	2001	2000
	€'000	€'000
Loans from shareholders	379,845	63,276
Trade creditors	112,787	119,120
Accruals and other creditors	23,904	12,000
Tax and social security	9,452	3,076
	525,988	197,472

11. OPERATING EXPENSES

	2001	2000
	€'000	€'000
Selling and marketing expenses	150,390	128,310
General and administrative expenses	184,617	133,295
Depreciation and amortisation	75,032	54,785
	410,039	316,390

12. REMUNERATION OF DIRECTORS

The company's directors received remuneration of € 874,105 during the year 2001.

13. EMPLOYEES

Total employee expenses amounted to € 40,940,035 (2000: € 30,166,093) including social security of € 3,711,361 (2000: € 2,645,145) and pension costs of € 3,083,489 (2000: € 1,883,913). Employee expenses are included in General and administrative expenses.

The group had an average of 1,142 employees during 2001 (2000: 691).

14. NET FINANCIAL INCOME/(EXPENSE)

	2001	2000
	€'000	€'000
Interest and similar income	985	890
Interest and similar expense	(11,900)	(12,850)
Foreign exchange gain/(loss)	(158)	(493)
Other financial income/(expenses)	783	26
	(10,290)	(12,427)

Interest expense primarily relates to that payable on shareholder financing.

15. COMMITMENTS

At December 31, 2001, the group had entered into various agreements, principally relating to the network, resulting in commitments of € 393 million.

The company has issued guarantees under article 403 of the Dutch Civil Code to the group companies Ben Nederland B.V. en Ben Klantenservice B.V.

16. RECONCILIATION TO U.S. GAAP

The consolidated financial statements of Ben Nederland Holding B.V. have been prepared in accordance with Dutch GAAP, which differs in certain respects from generally accepted accounting principles in the United States (U.S. GAAP). Application of U.S. GAAP would have affected the balance sheet as of December 31, 2001 and 2000 and the net loss for each of the years in the three-year period ended December 31, 2001 to the extent described below.

(1) Capitalisation of interest on assets under construction and mobile communication licences

a) Under Dutch GAAP capitalisation of interest accumulated from borrowings during the asset construction period is voluntary. Prior to January 1, 2000, the Company capitalised interest accumulated during the construction period and amortized these costs over the assets useful life. As of January 1, 2000 the company elected to cease capitalization of interest costs related to assets under construction. As part of this change in accounting policy the unamortised balance of € 1,795,000 capitalized as of December 31, 1999 was reversed and charged to income in the year 2000.

Under U.S. GAAP, interest accumulated on borrowings during the asset construction period are capitalised and are amortized once the respective assets are placed in operation resulting in an increase in the net loss of € 692,000 in 2001 and a decrease in the net loss in 2000 of € 4,375,000.

b) Under Dutch GAAP, interest costs related to the financing of the mobile communications licences are expensed as incurred. Under US GAAP, the license is considered an inextricable part of the network used to provide the actual services and accordingly interest costs related to the financing of the licenses during the network construction period are capitalized as part of network cost. This results in a decrease in net loss of € 11,653,000, € 7,754,000 and € 379,000 in 2001, 2000 and 1999, respectively.

(2) Technical equipment lease

During 1999, the Company entered into a sales lease back transaction relating to certain technical equipment in use by the Company. Under Dutch GAAP, the net cash received was recognized as other operating revenues. Under US GAAP, the gross cash received of € 65.6 million and payment liabilities of € 61.7 million are recognized on the balance sheet and the net cash gain on the transaction is recognized as other income over the lease term of 16 years.

(3) Vendor penalties

During 1998 and 1999 the Company received penalties from a vendor as the vendor failed to meet certain contractual requirements with respect to the roll out of the network. These payments relate to refunds on amounts paid for network assets purchased. Under Dutch GAAP these amounts were recorded as income. Under U.S. GAAP these payments are recorded as a deduction from the cost of the network assets resulting in a reduction of net income and the carrying value of network assets by € 13.2 million in 1998 and € 4.6 million in 1999. Additionally, depreciation expense related to these assets is reduced by € 2.5 million, € 2.5 million and € 1.2 million for the years ended December 31, 2001, 2000 and 1999, respectively.

The effect of these items is set out in the following tables.

Reconciliation of net loss from Dutch GAAP to U.S. GAAP:
(Amounts in € ’000)

	2001	2000	1999
Net loss as reported in the consolidated financial statements under Dutch GAAP	(198 866)	(239 379)	(162 429)
Interest capitalisation(1)	10 961	12 129	379
Technical equipment lease(2)	250	250	(3 875)
Vendor penalties(3)	2 540	2 540	(3 358)
Net loss in accordance with U.S. GAAP	(185 115)	(224 460)	(169 283)

Reconciliation of shareholders’ equity from Dutch GAAP to U.S. GAAP
(Amounts in € ’000)

	Dec 31, 2001	Dec 31, 2000
Shareholders’ equity in accordance with Dutch GAAP	608 549	807 415
Interest capitalisation(1)	26 181	15 220
Technical equipment lease(2)	(3 375)	(3 625)
Vendor penalties(3)	(9 555)	(12 095)
Shareholders’ equity in accordance with U.S. GAAP	621 800	806 915

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DT-FT ITALIAN HOLDING GmbH, Bonn

CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2000

CONTENTS

REPORT OF INDEPENDENT ACCOUNTANTS

To the Board of Management and Shareholders' of DT-FT Italian Holding GmbH Bonn:

We have audited the accompanying balance sheet of DT-FT Italian Holding GmbH, Bonn as of December 31, 2000, and the related statements of income and of cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of DT-FT Italian Holding GmbH, Bonn as of December 31, 2000, and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in Germany.

Frankfurt am Main, April 30, 2001

PwC Deutsche Revision
Aktiengesellschaft
Wirtschaftsprüfungsgesellschaft

(Kütting)	(ppa.Sahorsch)
Wirtschaftsprüfer	Wirtschaftsprüfer

DT-FT ITALIAN HOLDING GmbH, BONN

STATEMENT OF INCOME

	2000
	€
Other operating income	4,617,026,502
Other operating expenses	(13,439)
Interest and similar income	117,757,061
Results from ordinary business activities	**4,734,770,124**
Income taxes	(45,311,726)
Other taxes	(15,789,937)
Annual net income	**4,673,668,461**
Net operating loss carryforward	(97,345)
Unappropriated net income	**4,673,571,116**

The accompanying notes are an integral part of the consolidated financial statements.

DT-FT ITALIAN HOLDING GmbH, BONN

BALANCE SHEET

	December 31, 2000
	€
Assets	
A. Noncurrent assets	
Financial assets	
1. Subsidiaries & associated companies	—
	—
B. Current assets	
I. Receivables and other assets	
1. Other assets	4,861,701,151
II. Cash in banks	627,156,812
	5,488,857,963
	5,488,857,963
Liabilities	
A. Shareholders' equity	
I. Capital stock	25,564
II. Additional paid-in capital	773,394,283
III. Net operating loss carryforward	(97,345)
IV. Income/loss after taxes	4,673,668,461
	5,446,990,963
B. Accruals	
1. Tax accruals	41,843,414
2. Other accruals	23,519
	41,866,933
C. Liabilities	
1. Trade accounts payable	67
2. Other liabilities	—
	67
	5,488,857,963

The accompanying notes are an integral part of the consolidated financial statements.

DT-FT ITALIAN HOLDING GmbH, BONN

DEVELOPMENT OF NONCURRENT ASSETS

	Acquisition values				Dev. of accumulated write-downs/depreciation				Remaining book Values
	01/01/2000	Additions	Disposals	31/12/2000	01/01/2000	Additions	Disposals	31/12/2000	31/12/2000
	€	€	€	€	€	€	€	€	€
Financial assets									
1. Investments in unconsolidated subsidiaries	443,990,462	328,983,812	772,974,274	0	0	0	0	0	0
	443,990,462	328,983,812	772,974,274	0	0	0	0	0	0

DEVELOPMENT OF ACCRUALS

	01/01/2000	Consumption	Reversal	Addition	31/12/2000
	€	€	€	€	€
Tax accruals					
Corp. income tax & solidarity surcharge	0	0	0	23,117,093	23,117,093
Trade tax	0	0	0	18,726,321	18,726,321
	0	**0**	**0**	**41,843,414**	**41,843,414**
Other accruals					
Outstanding expenses	10,701	0	476	13,294	23,519
Litigation risks	76,694	76,394	300	0	0
	87,395	**76,394**	**776**	**13,294**	**23,519**
	87,395	**76,394**	**776**	**41,856,708**	**41,866,933**

The accompanying notes are an integral part of the consolidated financial statements.

DT-FT ITALIAN HOLDING GmbH, BONN

STATEMENT OF CASH FLOWS

	December 31, 2000
	€
Income after taxes	4,673,668,461
Net interest expense	(117,757,061)
Income tax expense	61,101,664
Book profits from the selling of noncurrent assets	(4,617,025,726)
Other noncash income and expense	—
Cashflow before changes in working capital	**(12,662)**
Increase (–)/decrease in accruals	(63,876)
Increase (–)/decrease in liabilities	(6,038)
	(82,576)
Income tax paid (–)/received	(19,258,250)
Interest paid (–)/received	26,755,910
Net cash provided by operating activities	**7,415,084**
Net investments in noncurrent assets	(328,983,809)
Proceeds from sale of noncurrent assets	619,300,000
Net cash used for investing activities	**290,316,191**
Transfer to additional paid-in capital	
In-payments of the shareholders	328,983,045
Net cash provided by (used for) financing activities	**328,983,045**
Decrease (–) in liquid funds maturing within 3 months	**626,714,320**
Liquid funds maturing within 3 months (beginning of the year)	442,496
Liquid funds maturing within 3 months (end of the reporting period)	627,156,812
Changes in the amounts of liquid funds maturing within 3 months and in Deutsche Telekom's cash pool	**626,714,316**

The accompanying notes are an integral part of the consolidated financial statements.

DT FT ITALIAN HOLDING GmbH, BONN

DECEMBER 31, 2000

I. General information and comments

Basic principles and methods

The corporate purpose is to purchase, own and manage WIND Telecomunicazioni S.p.A. shares.

Accounting and valuation principles

The annual financial statements of DT FT Italian Holding GmbH have been prepared in accordance with the provisions of the German Commercial Code. The classification of the consolidated statement of income is based on the total cost method of accounting.

The money accounts stated under current assets are verified through statements of account.

The translation of the receivables owed in foreign currency is based on the price valid on the day the transaction is performed or on the lower buying rate on the balance sheet date. The translation of the foreign currency liabilities is based on the price valid on the day the transaction is performed or on the higher selling rate on the balance sheet date.

II. Notes on the balance sheet and the statement of income

Financial assets (see table of consolidated noncurrent assets)

DT FT Italian Holding GmbH sold and transferred 43% of its Wind shares to FT Participations Belgium S.A. (FTPB) at a price of EUR 4.73 billion and 0.37% of its Wind shares at a price of EUR 40.7 million, effective from 27 July 2000. FTPB and France Telecom S.A. (FT) provided promissory notes in the amount of the purchase price to DT FT Italien Holding GmbH.

In addition, the DT FT Italian Holding GmbH sold 5.63% of its Wind shares to Enel S.p.A. at a price of EUR 619.3 million.

Other assets

The other assets consist of interest accruals and deferrals deriving from a EUR 1.5 million fixed-term deposit investment with Deutsche Bank, Bonn and EUR 40.7 million and EUR 4.73 billion in promissory notes from the selling of the Wind shares to FTPB. In addition, this item includes EUR 89 million in promissory notes from the note receivable.

Liquid funds

The liquid funds include a EUR 614 million fixed-term deposit investment with Deutsche Bank in Bonn which is based on the selling of the Wind shares to Enel. The credit balance with the banks consists of balances with the Postbank (EUR 21,474) and with Deutsche Bank (EUR 31,189).

Shareholders' equity

The capital stock remains at Euro 25,565.

Capital reserves

According to the 20 April 2000 resolution of the Shareholders' Meeting, the capital stock of WIND Telecomunicazioni S.p.A. was raised from Lit. 889,964,813,000 to Lit. 2,189,964,813,000 through the emission of 1,300,000,000 new ordinary shares at a nominal value of Lira 1,000 each. The value of the payments received from the shareholders was effective from 24 March 2000. 637.00 million shares at a nominal value of EUR 328.00 million go on DT FT Italien Holding GmbH.

Accruals

The accruals include trade income tax (EUR 18.9 million) and the corporate income tax, including the solidarity surcharge (EUR 23 million) as well as accruals for the annual audit (EUR 23,519).

Liabilities

The other liabilities relate to notarial charges.

Statement of income

Other operating income

The other operating income includes EUR 511 in income from the reversal of accruals and EUR 4.6 billion in income from the selling of the Wind shares.

Other operating expenses

The other operating expenses, amounting to EUR 13,294, are costs related to the preparation of the annual financial statements.

Interest income

The interest income (EUR 117.6 million) states the interest of the fixed-term deposit investment with the Deutsche Bank and the credit interest of the bank account (EUR 12.3 million). In addition, interest was due for DTFT's claim in connection with FTBP's note receivable from the selling of the WIND shares (EUR 105.3 million). The interest rate is EURIBOR 3 months roll-over plus 0.25%.

Income taxes

The income taxes state the corporate income tax (EUR 22 million), the trade income tax (EUR 18.9 million), the solidarity surcharge (EUR 1.5 million) and the capital gains tax (EUR 3 million). The interest due for the claim in connection with the note receivable from FTBP's results in a foreign withholding tax amounting to EUR 15.9 million which is creditable against the corporate income tax.

In the year under review, no compensation was paid for Managing Directors.

Statement of Cash Flows

The statement of cash flows has been prepared in conformity with International Accounting Standard (IAS) 7, Cash Flow Statements. Besides IAS 7, German Accounting Standard (DRS) No. 2, Cash Flow, is used.

Significant differences between German and United States generally accepted accounting principles

DT-FT Italian Holding GmbH, Bonn prepares its financial statements in accordance with German GAAP. Significant differences arise from the application of U.S. GAAP as compared to German GAAP. The significant differences are described as follows:

For German GAAP the investment in WIND Telecomunicazioni S.p.A. ("WIND") is accounted for at cost. For U.S. GAAP the investment would be accounted for using the equity method, which requires that the DT-FT's percentage of the losses of WIND are recorded in the income statement. This accounting would reduce the investment balance in WIND, thus increasing the gain on the sale of WIND. In addition, U.S. GAAP would require significant disclosures related to the WIND investment.

1. Management

Wolfgang Kaiser
Corporate legal adviser
Bonn

Philippe McAllister
Corporate legal adviser
Paris

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POLSKA TELEFONIA CYFROWA SP. Z O.O.

CONSOLIDATED FINANCIAL STATEMENTS
TOGETHER WITH REPORT OF
INDEPENDENT PUBLIC ACCOUNTANTS
FOR THE YEARS ENDED
DECEMBER 31, 2001, DECEMBER 31, 2000
AND DECEMBER 31, 1999

POLSKA TELEFONIA CYFROWA SP. Z O.O.

CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2001, 2000 AND 1999

CONTENTS

Report of Independent Public Accountants

To the Supervisory Board of Polska Telefonia Cyfrowa Sp. z o.o.

We have audited the accompanying consolidated balance sheets of Polska Telefonia Cyfrowa Sp. z o.o. (a Polish limited liability company) and its subsidiaries as of December 31, 2001, 2000 and 1999, and the related consolidated statements of operations, consolidated statements of changes in equity and consolidated statements of cash flows for each of the consecutive three years ended December 31, 2001. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Polska Telefonia Cyfrowa Sp. z o.o. and its subsidiaries, as at December 31, 2001, 2000 and 1999, and the results of their operations and their cash flows for each of the consecutive three years ended December 31, 2001 in accordance with Statements of International Accounting Standards (''IAS'') issued by the International Accounting Standards Board (''IASB'').

Accounting practices used by the Company in preparing the accompanying consolidated financial statements conform with IAS but do not conform with accounting principles generally accepted in the United States (''US GAAP''). A description of these differences and a reconciliation of net income and shareholders' equity from accounting principles generally accepted under IAS and US GAAP are set forth in Note 32.

As explained in Note 4.1.b to the consolidated financial statements, the Company has given retrospective effect to the change in its revenue recognition policy relating to multiple-element contracts.

Arthur Andersen Sp. z o.o.

Warsaw, Poland
March 1, 2002

POLSKA TELEFONIA CYFROWA SP. Z O.O. AND SUBSIDIARIES

Consolidated Statements of Operations
for the years ended December 31, 2001, December 31, 2000 and December 31, 1999
(in thousands of PLN)

	Notes	Year ended December 31, 2001	Year ended December 31, 2000 (restated)	Year ended December 31, 1999 (restated)
Net sales	7	4,344,896	3,684,723	2,515,556
Cost of sales	8	(2,727,437)	(2,286,426)	(1,586,346)
Gross margin		**1,617,459**	**1,398,297**	**929,210**
Operating expenses	8	(785,429)	(766,016)	(612,559)
Operating profit		**832,030**	**632,281**	**316,651**
Non-operating items				
Interest and other financial income	9	316,616	227,125	58,042
Interest and other financial expenses	10	(694,546)	(716,665)	(456,305)
Profit/(loss) before taxation		**454,100**	**142,741**	**(81,612)**
Taxation charge	11	(26,879)	(33,354)	(40,891)
Net profit/(loss) for the period		**427,221**	**109,387**	**(122,503)**

The accompanying notes are an integral part of these consolidated financial statements.

POLSKA TELEFONIA CYFROWA SP. Z O.O. AND SUBSIDIARIES

Consolidated Balance Sheets
as at December 31, 2001, December 31, 2000 and December 31, 1999
(in thousands of PLN)

	Notes	As at December 31, 2001	As at December 31, 2000 (restated)	As at December 31, 1999 (restated)
Current assets				
Cash and cash equivalents	28	36,511	29,465	1,095,509
Short-term investments and other financial assets	12	98,278	191,679	198,468
Debtors and prepayments	13	543,422	481,666	464,245
Inventory	14	167,114	209,290	183,980
		845,325	912,100	1,942,202
Long-term assets				
Tangible fixed assets, net	15	3,783,810	3,514,091	2,573,905
Intangible fixed assets, net	16	2,412,810	2,314,171	1,050,775
Financial assets	17	105,985	96,880	301,829
Deferred costs	18	69,523	202,747	248,807
		6,372,128	6,127,889	4,175,316
Total assets		**7,217,453**	**7,039,989**	**6,117,518**
Current liabilities				
Accounts payable	19	290,436	521,983	709,714
Amounts due to State Treasury	19	46,184	44,732	27,790
Interest-bearing liabilities	19	82,272	1,335,526	234,746
Accruals	21	234,763	131,614	152,061
Other liabilities	19	217,525	148,129	52,349
		871,180	2,181,984	1,176,660
Long-term liabilities				
Interest-bearing liabilities	20	5,083,933	3,986,391	4,578,412
Non-interest-bearing liabilities	20	193,822	111,251	163,554
Deferred tax liability, net	11	52,121	60,508	27,322
Provisions for liabilities and charges	21	20,652	12,908	3,764
		5,350,528	4,171,058	4,773,052
Total liabilities		**6,221,708**	**6,353,042**	**5,949,712**
Capital and reserves	22			
Share capital		471,000	471,000	471,000
Additional paid-in capital		409,754	409,754	—
Hedge reserve		(96,955)	—	—
Accumulated profit/(deficit)		211,946	(193,807)	(303,194)
		995,745	**686,947**	**167,806**
Total equity and liabilities		**7,217,453**	**7,039,989**	**6,117,518**

The accompanying notes are an integral part of these consolidated financial statements.

POLSKA TELEFONIA CYFROWA SP. Z O.O. AND SUBSIDIARIES

Consolidated Statements of Cash Flows
for the years ended December 31, 2001, December 31, 2000 and December 31, 1999
(in thousands of PLN)

	Year ended December 31, 2001	Year ended December 31, 2000 (restated)	Year ended December 31, 1999 (restated)
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net profit/(loss) before taxation	**454,100**	**142,741**	**(81,612)**
Adjustments for:			
Depreciation and amortization	850,572	519,705	281,697
Charge to provision and write-offs of doubtful debtors	67,626	146,624	143,890
Charge to provision for inventory	11,151	7,082	4,410
Other provisions long-term	7,744	9,144	3,764
Foreign exchange (gains)/losses, net and changes in financial instruments fair value	(91,609)	(92,207)	143,602
(Gain)/loss on disposal of tangibles and intangibles	(1,582)	8,664	8,146
Interest expense, net	469,539	501,580	247,527
Operating cash flows before working capital changes	**1,767,541**	**1,243,333**	**751,424**
(Increase)/decrease in inventory	31,025	(32,392)	(110,918)
Increase in debtors, prepayments and deferred cost	(129,383)	(104,527)	(342,701)
Increase/(decrease) in trade payables and accruals	(69,851)	(1,869)	173,699
Cash from operations	**1,599,332**	**1,104,545**	**471,504**
Interest paid	(450,820)	(453,183)	(103,220)
Interest received	15,213	38,005	7,277
Income taxes paid	(1,325)	(4,451)	(25,549)
Net cash from operating activities	**1,162,400**	**684,916**	**350,012**
CASH FLOWS USED IN INVESTING ACTIVITIES:			
Purchases of intangible fixed assets	(1,372,058)	(329,064)	(346,019)
Purchases of tangible fixed assets	(1,128,118)	(1,434,875)	(985,298)
Proceeds from/(purchase of) investments, net	199,699	193,959	(511,603)
Proceeds from sale of equipment and intangibles	25,250	14,905	7,309
Net cash used in investing activities	**(2,275,227)**	**(1,555,075)**	**(1,835,611)**
CASH FLOWS (USED IN)/FROM FINANCING ACTIVITIES:			
Net proceeds from Bank Credit Facilities	1,288,594	—	—
Proceeds from/(repayment) of Loan Facility	(836,158)	(248,643)	487,972
Proceeds from Notes issued	704,141	—	1,843,822
Proceeds from shareholder's loan	—	—	296,756
Net change in overdraft facility	(36,342)	36,342	(24,558)
Additional paid-in capital, net	—	16,827	—
Net cash (used in)/from financing activities	**1,120,235**	**(195,474)**	**2,603,992**
Net (decrease)/increase in cash and cash equivalents	**7,408**	**(1,065,633)**	**1,118,393**
Effect of foreign exchange changes on cash and cash equivalents	**(362)**	**(411)**	**(28,579)**
Cash and cash equivalents at beginning of period	**29,465**	**1,095,509**	**5,695**
Cash and cash equivalents at end of period	**36,511**	**29,465**	**1,095,509**

The accompanying notes are an integral part of these consolidated financial statements.

POLSKA TELEFONIA CYFROWA SP. Z O.O. AND SUBSIDIARIES

Consolidated Statements of Changes in Equity
for the years ended December 31, 2001, December 31, 2000 and December 31, 1999
(in thousands of PLN)

	Share Capital	Additional paid-in capital	Hedge reserve	Accumulated profit/(deficit)	Total
Balance as at January 1, 1999 (restated)	**471,000**	**—**	**—**	**(180,691)**	**290,309**
Net loss for the period	—	—	—	(122,503)	(122,503)
Balance as at December 31, 1999 (restated)	**471,000**	**—**	**—**	**(303,194)**	**167,806**
Balance as at January 1, 2000 (restated)	**471,000**	**—**	**—**	**(303,194)**	**167,806**
Additional paid-in capital	—	409,754	—	—	409,754
Net profit for the period	—	—	—	109,387	109,387
Balance as at December 31, 2000 (restated)	**471,000**	**409,754**	**—**	**(193,807)***	**686,947**
Balance as at January 1, 2001	**471,000**	**409,754**	**—**	**(193,807)***	**686,947**
Effect of adopting IAS 39 (see Note 4.1.a)	—	—	—	(21,468)	(21,468)
Adjusted balance as at January 1, 2001	**471,000**	**409,754**	**—**	**(215,275)**	**665,479**
Fair value losses on cash flow hedge, less tax effect	—	—	(96,955)	—	(96,955)
Net profit for the period	—	—	—	427,221	427,221
Balance as at December 31, 2001	**471,000**	**409,754**	**(96,955)**	**211,946**	**995,745**

* The amount of PLN 193,807 representing accumulated deficit as at December 31, 2000 includes PLN 11,736 (decrease of accumulated deficit) of the revenue recognition retrospective adjustment (see Note 4.1.b).

The accompanying notes are an integral part of these consolidated financial statements.

1. Incorporation and Principal Activities

Polska Telefonia Cyfrowa Sp. z o.o. (the ''Company'') is located in Warsaw, Al. Jerozolimskie 181 and was incorporated by the Notarial Deed dated December 20, 1995 and entered on the National Court Register kept by District Court in Warsaw, XIX Economic Department of National Court Register, Entry No. KRS 0000029159.

The principal activities of the Company are providing cellular telephone communication services in accordance with the GSM 900 and 1800 licenses granted by the Minister of Communications and the sale of cellular telephones and accessories compatible with its cellular services. On December 20, 2000 the Minister of Communications granted the Company a license to provide telecommunication services according to the Universal Mobile Telecommunication System (''UMTS'') standard (see Note 4.2.b and 16).

The principal activities of the Company are not seasonal or cyclical.

Authorization of the consolidated financial statements

These consolidated financial statements, which include the financial statements of Polska Telefonia Cyfrowa Sp. z o.o. and its wholly owned subsidiaries, PTC International Finance B.V. and PTC International Finance (Holding) B.V. (consolidated) were authorized for issue by Management Board of Polska Telefonia Cyfrowa Sp. z o.o. on March 1, 2002.

2. Significant events in the year 2001

On February 20, 2001 the Company signed the two loan facility agreements (''Main Bank Facility Agreement'' and ''Supplemental Bank Facility Agreement'' — together ''Bank Credit Facilities'') with the consortium of banks (''Bank Consortium'') organized by Deutsche Bank AG London, Deutsche Bank Polska S.A., Dresdner Bank Luxembourg S.A. and the European Bank of Reconstruction and Development. The Bank Credit Facilities were signed in order to support the GSM business and UMTS development and to refinance the Loan Facility arranged in 1997 with Citibank N.A. (see Note 20b).

On March 30, 2001 the Company signed the senior subordinated bridge facility agreement organized by Deutsche Bank AG London (''Bridge Facility'') to fund approximately one third of the UMTS License installment due on March 30, 2001. The Bridge Facility was repaid in May 2001.

On April 24, 2001 the Registration Court in Warsaw registered the pledge on substantially all of the Company's assets in favour of Deutsche Bank Polska S.A., as the Security Agent of the Bank Consortium.

On May 8, 2001, the Company finalized its third long-term Notes issuance for the amount of EUR 200 million that will mature on May 1, 2008 (see Note 20a). Proceeds from the Notes issuance were used to partially repay the Bank Credit Facilities in the amount of EUR 150 million and the Bridge Facility in the amount of EUR 28 million.

On May 25, 2001, the Bank Consortium that organized the Bank Credit Facilities accepted the UMTS business plan of the Company. This approval removes all restrictions on the Company's utilization of funds available under these facilities for UMTS operational and capital expenditures.

On September 24, 2001 the Supplemental Bank Facility Agreement was amended to increase the available tranches of the facility by EUR 50 million (see Note 20b).

During September 2001, the Company together with both other wireless operators in Poland submitted a request to URT (the Regulator for the Telecommunication Market in Poland) to extend the UMTS service launch deadlines by 12 months till January 1, 2005. As at the date of these financial statements the Company has not received a response from URT.

Also during August 2001, the Company submitted a request to URT to reduce the cost of its GSM 1800 license from EUR 100 million to EUR 50 million. In 1999, the Company committed to pay EUR 100 million for use of the relevant frequencies across the whole country while its competitors, purchased similar rights for a limited area for lower price. In its claim the Company is seeking equal treatment to its competitors. As at today, the Company has not received any decision from URT.

3. Principles of Consolidation

a. Group Entities

The consolidated financial statements include the financial statements of Polska Telefonia Cyfrowa Sp. z o.o. and its wholly owned subsidiaries, PTC International Finance B.V. and PTC International Finance (Holding) B.V. (consolidated).

All intercompany balances and transactions are eliminated in consolidation.

On June 17, 1997, PTC International Finance B.V. was incorporated under the laws of the Netherlands for the purpose of issuing long-term Notes. The Company acquired 40 fully paid shares with a par value of 1,000 Netherlands Guilders each, issued by PTC International Finance B.V. PTC International Finance B.V. has no subsidiaries on its own.

On November 5, 1999 PTC International Finance II S.A. was incorporated under the laws of Luxembourg and on November 16, 1999, PTC International Finance (Holding) B.V. was incorporated under the laws of the Netherlands for the purpose of issuing long-term Notes. The Company acquired 40 fully paid shares with a par value of 1,000 Netherlands Guilders each, issued by PTC International Finance (Holding) B.V.

Additionally, the Company acquired 125 fully-paid shares with a par value of EUR 1,000 each issued by PTC International Finance II S.A. and contributed all of its shares except one, (owned by the Company, but held locally, due to legal requirements) to PTC International Finance (Holding) B.V. in exchange for 1 additional share of PTC International Finance (Holding) B.V. thus, PTC International Finance II S.A. became a fully owned subsidiary of PTC International Finance (Holding) B.V. PTC International Finance II S.A. has no subsidiaries on its own.

b. Reporting Currency

The Company generates and expends cash through its operating activities mostly in Polish zloty (“PLN”). The majority of the Company’s receivables and the large part of its short-term liabilities are PLN denominated. Therefore, the Management has designated the PLN as the reporting (functional) currency of the Company.

The accompanying consolidated financial statements are reported in thousands of PLN.

4. Principal Accounting Policies

The Company maintains its books of account in accordance with accounting principles and practices employed by enterprises in Poland as required by Polish Accounting Standards (“PAS”). The accompanying consolidated financial statements reflect certain adjustments not reflected in the Company’s statutory books to present these statements in accordance with standards issued by the International Accounting Standards Board. These adjustments and their effect on earnings for the years ended December 31, 2001, December 31, 2000 and December 31, 1999 are shown in Note 31 to these consolidated financial statements.

The differences between International Accounting Standards (“IAS”) and generally accepted accounting principles in the United States (“U.S. GAAP”) and their effect on net results for the years ended December 31, 2001, 2000 and 1999 have been presented in Note 32 to these consolidated financial statements.

The IAS rules that were mandatory as at December 31, 2001 were applied to these consolidated financial statements.

At January 1, 2001 the Company adopted IAS 39 — Financial Instruments: Recognition and Measurement (“IAS 39”). The effect of adopting of IAS 39 is summarized in the consolidated statement of changes in shareholders’ equity and further information is disclosed in the Note 4.1.a.

In the first quarter of 2001 the Company applied new revenue recognition policy related to multiple-element contracts. Accordingly, the Company calculated the effect of the revenue recognition policy and restated all interim information previously reported during 2000. The effect of the application is disclosed in the Note 4.1.b.

(in thousands of PLN)

4. Principal Accounting Policies — (Continued)

4.1. Introduction of new standards

a. Adoption of IAS 39

At the beginning of year 2001, the Company applied the identification and valuation criteria required by the standard. Any adjustment of the previous carrying amount was recognized as an adjustment of the balance of retained earnings at the beginning of the year 2001.

The adoption of IAS 39 resulted as at January 1, 2001 in an increase of accumulated deficit of PLN 21,468, which was due to following adjustments:

Options embedded in long-term Notes	(22,174)
Derivatives embedded in finance lease contracts	(11,715)
Derivatives split from rental contracts	6,789
Initial treatment of transaction costs	5,632
	(21,468)

Recognition and measurement

In accordance with IAS 39, all financial assets and financial liabilities are recognized in the balance sheet. All these financial assets and liabilities are initially measured at cost, which is the fair value of the consideration given or received to acquire the financial asset or liability (plus certain hedging gains and losses). All ''regular way'' purchases of financial assets are accounted for at the trade date.

The table below presents the measurement categorization of financial assets and liabilities.

Category	Balance sheet item	Measurement
Financial assets		
Held for trading	Cash and cash equivalent,	Fair value
	Derivatives: forward contracts, Note options	Fair value model using market data
Held to maturity	Short-term investments	Amortized cost
Loans and receivables originated by the Company	Trade and other debtors	Original recorded cost
Hedging derivatives	Cross currency interest rate swaps	Fair value model using market data
Financial liabilities		
Held for trading	Forward contracts	Fair value model using market data
	Index swaps	Fair value model using market data
Non-trading liabilities	License liabilities	Amortized cost
	Construction payables	Original recorded cost
	Trade and other creditors	Original recorded cost
	Long-term Notes	Amortized cost
	Finance lease	Amortized cost
	Bank Credit Facilities	Costs plus accrued interest
	Overdrafts	Costs plus accrued interest
	Accruals	Original recorded cost
Hedging derivatives	Cross currency interest rate swaps	Fair value model using market data

4. Principal Accounting Policies — (Continued)

4.1. Introduction of new standards — (Continued)

a. Adoption of IAS 39 — (Continued)

Derecognition

The Company derecognises a financial asset or a portion of a financial asset if the Company loses control of the contractual rights that comprise the financial asset or a portion of a financial asset.

The Company removes a financial liability (or a part of a financial liability) from its balance sheet when, and only when, it is extinguished — that is when the obligation specified in the contract is discharged, cancelled, or expires.

Notes

The Company is full and unconditional guarantor of the Notes issued by its subsidiaries (see Note 20a). The Notes were recognized at fair value of consideration received with transaction costs and call options recognition included in the initial measurements. They are amortized accordingly to effective interest rates.

Foreign exchange forward contracts ("Forward contracts")

The Company enters into derivative financial instruments such as forward contracts to hedge its foreign exchange transaction exposure (see Note 24). Forward contracts are valued in the balance sheet at their fair value and are presented in current assets or liabilities. The fair value is calculated using a market model.

The Company has not applied hedge accounting for forward contracts in the consolidated financial statements. They are treated as derivative financial instruments held for trading purposes and gains or losses resulting from these transactions are included in the consolidated statement of operations. The forward contracts are used according to the Company's hedging policy and strategy.

The Company had applied IAS 39 principles to forward contracts before January 1, 2001.

Cross currency interest rate swaps ("CC swaps")

The Company uses cross currency interest rate swap transactions to hedge its exposure against foreign currency fluctuations on fixed interest liabilities related to the Notes (see Note 24). These contracts are designated as hedges against exposure to changes in future cash flows arising from the foreign exchange risk on the future coupon payments. The CC swaps are valued in the balance sheet at their fair value based on the quoted market prices. They are presented in long-term financial assets/(liabilities) and short-term assets/(liabilities) depending on maturity of the related coupon.

The Company applied hedge accounting for the CC swaps. As a result changes in the fair value of the derivatives that are highly effective are recognized in shareholders' equity, net of tax effect. Amounts deferred in shareholders' equity are transferred to the statement of operations and classified as financial income or expense in the periods when the hedged coupon payments accrue in the statement of operations.

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

4. Principal Accounting Policies — (Continued)

4.1. Introduction of new standards — (Continued)

a. Adoption of IAS 39 — (Continued)

Embedded derivatives

An embedded derivative causes some or all of the cash flows that otherwise would be required by the contract to be modified by a variable such as an interest rate, security price, commodity price, foreign exchange rate, index of prices or rates and others. The Company separates the embedded derivatives from the host contracts and accounts for them as derivatives if the following conditions are met:

- the economic characteristics together with risks of the embedded derivatives and the host contracts are not clearly and closely related,
- a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative,
- the hybrid instrument is not measured at fair value with changes in fair value reported in the statement of operations.

• *Options embedded in the long- term Notes ("Note options")*

Long-term Notes issued by the Company have embedded derivatives — options of issuer and holders (see Notes 20a and 24). The issuer options are separated from host contracts and accounted for as a derivative under IAS 39.

The valuation of Note options is done with the use of the binominal model. The model is based on the backward induction methodology using the replication rule, stating that a portfolio of base instruments at their present value can replace an option.

The options are presented in the balance sheet in financial assets and gains and losses arising from changes in their fair value are included in the statement of operations for the period.

As at January 1, 2001 the Company recognized the options value at PLN 18,077. The respective adjustment resulted in an increase of the Notes liabilities by PLN 46,874 and an increase of the accumulated deficit by PLN 22,174, net of a tax benefit.

• *Derivatives embedded in finance lease contracts ("Index swaps")*

The Company has bifurcated the derivatives from its finance leasing agreements (see Note 4.2.e and 20c). These derivatives swap payments based on the Consumer Price Index in the USA ("CPI") into interest-based payments. CPI is not related to inflation in the Company's own economic environment. Thus, the embedded derivatives are not clearly and closely related to the host contracts.

The fair value of Index swaps is estimated using a model based on discounting estimated future cash flows at money market interest rates.

The Index swaps are presented in the balance sheet in liabilities (separately short-term and long-term portion) and gains and losses arising from the changes in fair value are recorded in the statement of operations for the period.

As at January 1, 2001 the Company separated the Index swaps from the leasing liabilities and recognized with a negative fair value of PLN 35,962 as derivatives under long-term liabilities. As a result the finance leasing liabilities decreased by PLN 20,748. The respective adjustment of retained earnings resulted in an increase of the accumulated deficit by PLN 11,715, net of a tax benefit.

4. Principal Accounting Policies — (Continued)

4.1. Introduction of new standards — (Continued)

a. Adoption of IAS 39 — (Continued)

- *Derivatives split from rental contracts ("Rental derivatives")*

In accordance with IAS 39 the Company has bifurcated the derivatives embedded in the foreign currency denominated rental contracts. These contracts are firm commitments of the Company and none of the parties to the contracts uses foreign currency in its primary economic environment. Some of these contracts also include indexing of lease payments according to changes in the price indices, which is not related to the Company's own economic environment.

The Company has separated the embedded derivatives and measured them at fair value using models based on discounting estimated future cash flows at money market interest rates.

The rental derivatives are presented in the balance sheet in financial assets/(liabilities), separately short-term and long-term portion, and gains and losses arising from changes in their fair value are included in the statement of operations.

The respective adjustment as at January 1, 2001 resulted in a decrease of the accumulated deficit by PLN 6,789, net of a tax charge.

Transaction costs

In accordance with IAS 39 transaction costs, being incremental costs that are directly attributable to the acquisition or disposal of financial asset or liability are included in the initial measurement of all financial assets and liabilities. Prior to IAS 39 implementation the Company deferred transaction costs and amortized over the period of financing. After adoption of IAS 39 the Company included the transaction costs related to the issuance of the Notes (fixed term to maturity instruments) in the Notes initial measurement.

The related adjustment as at January 1, 2001 resulted in a decrease of the accumulated deficit by PLN 5,632, net of a tax charge.

The transaction costs related to the Loan Facility and Bank Credit Facilities (variable term to maturity instrument) were reclassified from deferred costs into intangible assets (see Note 16 and 18).

b. Revenue recognition — multi-element contracts

In the first quarter of 2001, the Company adopted a new accounting policy regarding multi-element sale transactions and applied it retrospectively. The resulting adjustment to the opening balance of accumulated deficit as at January 1, 2001 resulted in a decrease by PLN 11,736, net of a tax charge and there were no changes to the balances as at January 1, 2000 and 1999. Both, net sales and cost of sales increased by PLN 41,728, PLN 52,303 and decreased by PLN 76,505 in 2001, 2000 and 1999, respectively.

The change in the revenue recognition policy was initiated by Staff Accounting Bulletin No. 101 "Revenue Recognition in Financial Statements" ("SAB 101") that was issued by the Securities and Exchange Commission staff. SAB 101 reflects basic principles of revenue recognition in existing generally accepted accounting principles in the United States. Based on the above bulletin and further interpretations, the Company set criteria for recognition of multiple-element transactions and their presentation in the IAS consolidated financial statements.

The multiple-element transactions with post-paid clients are classified as separable or non-separable contracts whereas the pre-paid services are treated as separable transactions. The initial revenue from a multiple-element arrangement that is non-separable (handset price and activation fee) is deferred over the average expected life of the customer. The direct cost of a product sold in this contract is also deferred in line with the revenue. The initial excess of cost over the revenue is immediately expensed. The revenue from separable multiple-element transactions and costs related to these transactions are recognized in the statement of operations as incurred.

(in thousands of PLN)

4. Principal Accounting Policies — (Continued)

4.1. Introduction of new standards — (Continued)

b. Revenue recognition — multi-element contracts — (Continued)

The accounting treatment of revenues and relevant costs for multi-element arrangements is summarized in the following table:

Multi-element contract (handset, activation and telecommunication service)

	Separable	Non-separable
Accounting treatment	Activation represents up-front non-refundable fee. Handset is sold separately from the rest of the multi-element contract	Handset, activation and service are treated as multi-element contract that is non-separable.
Revenue recognition	Activation and handset revenue is recognized immediately.	*Multiple Element Revenue:* Activation and handset revenue is deferred over average expected life of the customer.
Cost recognition	Cost of the activation card and handset is recognized immediately.	*Multiple Element Cost:* Cost of activation card and cost of handset equal to activation and handset revenue is deferred over average expected life of the customer. The excess of the costs over revenues is immediately expensed.

Total sales price of handsets sold together with prepaid service cards is allocated on a pro-rata basis based on the relative fair value of the elements.

4.2. Other accounting standards

a. Tangible Fixed Assets

Tangible fixed assets are shown at historical cost less accumulated depreciation.

The costs of tangible fixed assets include foreign exchange differences and interests resulting from payments or valuation of liabilities financing the relevant tangible fixed asset acquisition or construction.

Depreciation is calculated using the straight-line method over the estimated useful life of the asset. The following depreciation rates have been applied:

	Annual rate in %	Estimated Useful Lives in years
Leasehold improvements		Lease term
Buildings	2.5%	40
Plant and equipment	6.7 - 30.0%	3.3 - 15
Motor vehicles	12.5 - 30.0%	3.3 - 8
Other	4.0 - 20.0%	5 - 25

(in thousands of PLN)

4. Principal Accounting Policies — (Continued)

4.2. Other accounting standards — (Continued)

b. Intangible Fixed Assets

Licenses

Intangible fixed assets include three licenses (GSM 900, GSM 1800 and UMTS licenses), which the Company acquired from the Polish State. Telecommunication licenses are measured at cost less accumulated depreciation. As the payments are deferred beyond normal credit terms the cost of license is the cash price equivalent. The difference between this amount and total payments is recognized as interest expense over the period of credit unless it is capitalized on the license value during its development period. The cost of the GSM 1800 and UMTS licenses includes also interests and foreign exchange differences resulting from payments or valuation of liabilities related to financing the license acquisitions. The licenses are amortized using the straight-line method over the periods of their validity, i.e. GSM 900 license — over 14.5 years (173 months); GSM 1800 license — over 14.5 years (174 months) and UMTS license will be amortized over 20 years (240 months) from the date of the operational start-up of the underlying services.

For further disclosure see Note 16.

Other intangible fixed assets

Other intangible assets are stated at cost less accumulated amortization. Amortization is calculated using the straight-line method over the estimated useful life of the asset. The following amortization rates have been applied:

	Annual rate in %
Computer software	20.0 - 50.0%
Network software	6.7 - 66.7%
Trademarks	6.7%

The Company implemented in 2001 amortization rates for computer software used in the network equipment in range of 6.7% - 66.7%. The amortization charges for this software are calculated using the straight-line method over the further estimated useful life of the network equipment starting from the date on which new software is brought into use.

c. Debtors

Amounts due from debtors are measured at cost net of provisions for doubtful accounts. The provisions are based on specific amounts due where realization is unlikely and on a general basis, calculated using historic collection experience.

d. Inventories

Inventories are stated at the lower of cost and net realizable value. The cost of inventories is principally assigned by using weighted average cost formulas.

The costs of inventories become unrecoverable if those inventories are damaged, become wholly of partially obsolete or if their selling price declines. The Company writes down the cost of inventories to net realizable value by setting adequate provisions netted with related inventory balance.

4. Principal Accounting Policies — (Continued)

4.2. Other accounting standards — (Continued)

e. Leasing

The Company acquired its head-office premises under finance lease conditions and initially recognized assets and liabilities in the balance sheet at amounts equal to the present value of the minimum lease payments. In calculating the present value of the minimum lease payments the Company's incremental borrowing rate was used. The finance lease liability was initially measured at an amortized cost. After the bifurcation of embedded derivative (Index swaps — see Note 4.1.a) it has two components: main liability measured at amortized costs and the indexing (embedded derivative) measured at fair value. See also ''Tangible fixed assets held under capital lease'' in Note 15, ''Finance leases'' in Note 20c.

f. Special funds

Special funds consist primarily of the social fund. The social fund is an employer's obligation based on a government mandated calculation based on number of employees and the monthly minimum wage in Poland. The amounts calculated under this formula must be used for the benefits of the employees.

g. Advertising expense

The Company charges the cost of advertising to expense as incurred.

h. Vacation pay

Vacation pay is accrued when earned by employees.

i. Taxation

The income tax charge is based on profit for the period and takes into account deferred taxation. Deferred taxation is calculated using the balance sheet liability method. Under the balance sheet liability method the expected tax effects of temporary differences are determined using enacted tax rates and reported either as liabilities for taxes payable or assets representing the amounts of income taxes recoverable in future periods in respect of deductible temporary differences and the carry forward of unused tax losses and credits. Temporary differences are the differences between the carrying amount of an asset or a liability in the balance sheet and its taxable base.

Deferred tax assets are recognized for all deductible temporary differences to the extent that it is probable that taxable profit will be available against which the deductible temporary differences can be utilized.

j. Net sales

Net sales consist of the value of sales (excluding value added tax) of goods and services in the normal course of business but exclude extraordinary disposals of inventory and other assets. Revenue is recognized when services are provided or goods are shipped out. Sales allowances are accounted in the same period when the related portion of revenue is recognized.

k. Transactions in foreign currencies

Transactions denominated in foreign currencies are recorded in the local currency (the Polish zloty — PLN) at actual exchange rates prevailing at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are reported at the rates of exchange prevailing at the end of the period. Any gain or loss arising from a change in exchange rates subsequent to the date of the transaction is recorded in the statement of operations as a foreign exchange gain or loss and included in non-operating items in the statement of operations, unless capitalized — see points: (a) tangible fixed assets and (b) intangible fixed assets (license) and (m) below (borrowing costs).

4. Principal Accounting Policies — (Continued)

4.2. Other accounting standards — (Continued)

l. Use of estimates

Preparation of consolidated financial statements requires Management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

m. Capitalization of borrowing costs

Borrowing costs (including interest, foreign exchange gains and losses and the discount relating to the present value of license payments) that are attributable to the acquisition, construction or production of qualifying assets are capitalized as a part of the cost of those assets. The borrowing costs capitalized are only those incurred during the period of construction or production of qualifying assets.

5. Events after the balance sheet date

Effective January 2002 the Company changed the useful lives for a part of network fixed assets and related depreciation rates from 4% - 12.5% to 10% - 25%, according to the Management Board's Resolution dated January 29, 2002.

6. Financial risk management

The Company's treasury function is responsible for managing financial risk in accordance with the Company's hedging policy. Principle exposures and methods used by the Company to mitigate those exposures are described below:

The hedging policy approved by the Supervisory Board provides principles for overall financial risk management in the Company. This policy sets a framework within which the hedging activity should operate. However, it also allows some discretion in the precise hedging strategy to be adopted, to allow the treasury function to react to market conditions. According to the hedging policy, each year the treasury function prepares a hedging strategy regarding transaction risk, which is later submitted to the Management Board and Supervisory Board.

The ultimate responsibility for agreeing the details of the annual hedging strategy rests with the Management Board and the Supervisory Board based on the recommendations of the Risk Management Committee consisting of the CFO, the Treasurer, the Controller and the Tax Manager. The responsibility for the execution of foreign exchange and interest rate hedge transactions, within the agreed strategy and in conformity with the hedging policy, rests with the treasury function of the Company. On the other hand, the Management Board and the Supervisory Board must approve any actions taken to hedge translation risk.

a. Foreign exchange risk

A significant proportion of the financing liabilities of the Company is denominated in foreign currencies (EUR and USD). The financial risk management is aimed both at minimizing the volatility of cash flows, in PLN terms, arising from fluctuations in the exchange rate of the PLN against other currencies and at minimizing the adverse effect of movements in exchange rates on the earnings and book value of the Company in PLN terms.

The treasury function manages the foreign exchange exposure based on forecasts of cash flows denominated in foreign currencies. These forecasts distinguish between forecasts of cash flows where there is significant certainty as to both the amount and timing of the cash flow (''Committed Exposures'') and those where there is some uncertainty about the amount and/or timing of the cash flow (''Uncommitted Exposures'').

Hedge activities are undertaken on the basis of short to long-term cash flow forecasts provided by treasury function and business units of the Company. The Company normally seeks to cover Committed Exposures in the range of such figures to be agreed by the Management Board and the Supervisory Board on at least an annual

6. Financial risk management — (Continued)

a. Foreign exchange risk — (Continued)

basis, providing hedging can be obtained at acceptable cost. The Company may undertake actions to cover individually identified Uncommitted Exposures providing, they are in compliance with hedging policy and constitute integral part of annually accepted hedging strategies.

The Company does not speculate in foreign currency. Speculation is defined as taking any action to increase an exposure beyond that which exists due to an underlying commercial activity, in the expectation of making a foreign currency gain.

Foreign exchange risk management transactions of the Company may be undertaken using the following instruments:

— forward and non-delivery forward transactions (''NDF contracts/transactions''),

— currency swaps,

— cross-currency interest rate swaps,

— foreign exchange options.

In 2001 the Company started hedging its long-term foreign exchange exposure arising from coupon payments on EUR and USD denominated Notes by concluding cross-currency interest rate swaps (see Note 4.1.a and 24).
In respect of short-term hedging the Company entered into a series of foreign exchange forward and NDF contracts together with foreign exchange options to reduce volatility of current operating and financial cash flows resulting from foreign exchange rate fluctuations (see Note 24).
The Company has not applied hedge accounting to the above risk management activities, except for CC swaps (see Note 4.1.a).

b. Interest rate risk

The Company is exposed to interest rate risk related to short-term and long-term credit facilities. Interest rate risk exposure arises from external financing denominated both in domestic and foreign currencies. The Company's interest bearing liabilities are based on fixed and floating interest rates.

Debt liabilities based on fixed interest rate are as follows (see Note 20a):

— the $10\frac{3}{4}$ Notes with a face value of USD 253,203,000

— the $11\frac{1}{4}$ Notes with a face value of USD 150,000,000

— the $11\frac{1}{4}$ Notes with a face value of EUR 300,000,000

— the $10\frac{7}{8}$ Notes with a face value of EUR 200,000,000

Debt liabilities based on floating interest rates consist of Bank Credit Facilities (see Note 20b). The Company may utilize all facilities by individual drawdowns for the maturity of one, three, six or twelve months. The interest rate related to each drawdown is determined at the drawdown date and fixed for the maturity of the respective drawdown.
The interest rate exposure consists of a risk of increasing short-term interest rates, which would result in higher financing costs. Interest rate exposure also arises from the possibility of decreasing long-term interest rates that would result in relative increase of financing costs versus market yields. The Company is protected against such a scenario by series of prepayment options embedded into all Notes.

The Company's interest rate exposure is managed by:

— varying the maturity periods of investments and borrowings,

— varying the proportions of debt which bears interest on a fixed and a floating basis,

— varying the period of time for which the interest rate is fixed in respect to the Bank Credit Facilities.

(in thousands of PLN)

6. Financial risk management — (Continued)

b. Interest rate risk — (Continued)

In addition to the interest rate management tools described above, the Company may, in line with its hedging policy enter into the following interest rate hedging transactions:

— forward rate agreements (FRAs),

— interest rate swaps,

— interest rate options (caps, floors, collars).

c. Credit risk

Commercial credit risk

The Company operates in one industry segment, providing cellular telephone communication services. Substantially all of the Company's trade debtors are Polish businesses and individuals. Further, the Company has established a network of dealers within Poland to distribute its products. The dealers share many economic characteristics thus receivables from each of these dealers present similar risk to the Company.
Concentrations of credit risk with respect to trade receivables are limited due to the large number of customers comprising the Company's customer base.
The Company maintains provisions for potential credit losses and such losses which in the aggregate, have not exceeded Management's expectations. With the exception of Telekomunikacja Polska S.A. ("TP S.A."), which purchases terminating interconnection services from the Company, no single customer accounts for 10% or more of revenues.
The balance of receivables as at December 31, 2001, representing the total net commercial credit risk exposure as at this date, is presented in Note 13.

Financial credit risk

There is a risk that the counterparties may be unable to meet their obligations related to financial instruments. This credit risk is monitored and measured by the treasury function in the Company. In order to minimize the risk the Company limits its counterparties to a sufficient number of major banks and financial institutions with high financial ratings.

The balance of financial assets, short-term investments and other financial assets as at December 31, 2001, representing the total financial credit exposure, is presented in Notes 12 and 17.

7. Net sales

	Year ended December 31, 2001	Year ended December 31, 2000 (restated)	Year ended December 31, 1999 (restated)
Service revenues and fees	4,123,555	3,460,579	2,374,827
Sales of telephones and accessories	221,341	224,144	140,729
	4,344,896	**3,684,723**	**2,515,556**

The Company operates in one segment (providing cellular telecommunication services and the ancillary sale of cellular telephones and accessories) and in one market (the Republic of Poland). The main sources of the Company's revenue are airtime tariffs, consisting primarily of monthly service fees (from incoming and outgoing calls), and charges for calls that originate or terminate in the Company's network, and calls placed by the Company's subscribers on foreign networks ("roaming calls").

(in thousands of PLN)

8. Costs and expenses

	Year ended December 31, 2001	Year ended December 31, 2000 (restated)	Year ended December 31, 1999 (restated)
Cost of sales:			
Cost of services sold	1,778,687	1,383,893	944,420
Cost of sales of telephones and accessories	948,750	902,533	641,926
	2,727,437	2,286,426	1,586,346
Operating expenses:			
Selling and distribution costs	585,463	576,318	454,807
Administration and other operating costs	199,966	189,698	157,752
	785,429	766,016	612,559
	3,512,866	**3,052,442**	**2,198,905**

The following costs and expenses were included in cost of sales:

	Year ended December 31, 2001	Year ended December 31, 2000 (restated)	Year ended December 31, 1999 (restated)
Merchandise sold	949,805	895,452	637,516
External services	869,995	815,227	635,557
Depreciation and amortization	790,796	476,011	257,071
Staff costs	81,315	71,091	36,717
Other	35,526	28,645	19,485
	2,727,437	**2,286,426**	**1,586,346**

The following costs and expenses were included in selling and distribution costs:

	Year ended December 31, 2001	Year ended December 31, 2000 (restated)	Year ended December 31, 1999 (restated)
External services including all advertising costs	292,367	259,124	193,396
Staff costs	158,700	127,043	88,873
Depreciation and amortization	40,213	22,491	9,563
Other	94,183	167,660	162,975
	585,463	**576,318**	**454,807**

The following costs and expenses were included in administration costs:

	Year ended December 31, 2001	Year ended December 31, 2000 (restated)	Year ended December 31, 1999 (restated)
External services	87,100	80,076	77,623
Staff costs	77,904	70,366	52,036
Depreciation and amortization	19,563	21,203	15,063
Other	15,399	18,053	13,030
	199,966	**189,698**	**157,752**

(in thousands of PLN)

9. Interest and other financial income

	Year ended December 31, 2001	Year ended December 31, 2000 (restated)	Year ended December 31, 1999 (restated)
Foreign exchange gains	207,911	185,195	45,414
Gains on valuation of derivatives	81,944	—	—
Interest income	26,761	41,930	12,628
	316,616	**227,125**	**58,042**

10. Interest and other financial expenses

	Year ended December 31, 2001	Year ended December 31, 2000 (restated)	Year ended December 31, 1999 (restated)
Interest expense	496,300	543,510	260,155
Losses on valuation of derivatives	144,226	67,884	—
Foreign exchange losses	54,020	105,271	196,150
	694,546	**716,665**	**456,305**

11. Taxation

	Year ended December 31, 2001	Year ended December 31, 2000 (restated)	Year ended December 31, 1999 (restated)
Polish current tax benefit/(charge)	—	802	(10,555)
Polish deferred tax charge	(25,460)	(33,186)	(30,088)
Foreign current tax charge	(1,419)	(970)	(248)
Tax charge	**(26,879)**	**(33,354)**	**(40,891)**

Tax loss carry forwards available as at December 31, 2001 amounted to PLN 911,374. The loss can be offset against taxable income if any, during the next five fiscal years after December 31, 2001.

According to the Polish tax regulations, the tax rates in effect in 2001, 2000 and 1999 were 28%, 30% and 34%, respectively. The tax rates set for years 2002, 2003 and 2004 and thereafter are 28%, 24% and 22%, respectively.

(in thousands of PLN)

11. Taxation — (Continued)

The reconciliation between tax charge and the product of accounting profit or loss multiplied by the applicable statutory tax rates is as follows:

	Year ended December 31, 2001	Year ended December 31, 2000 (restated)	Year ended December 31, 1999 (restated)
Profit/(loss) before taxation	454,100	142,741	(81,612)
Tax rate	28%	30%	34%
Tax benefit/(charge) using statutory rate	(127,148)	(42,822)	27,748
Permanent differences	12,309	(19,256)	(5,643)
Change in temporary differences for which realization is not probable	32,653	(712)	(62,053)
Effect of different tax rates and rules in foreign entities	1,881	4,685	559
Change in tax rates	51,803	23,343	14,364
Tax loss carry forward for which realization is not probable	—	—	(12,049)
Refilling of previous years' tax return	—	802	(10,555)
Adjustments to deferred taxes	1,623	606	6,738
Tax charge	**(26,879)**	**(33,354)**	**(40,891)**

	Year ended December 31, 2001	Year ended December 31, 2000 (restated)	Year ended December 31, 1999 (restated)
Deferred tax assets in Poland:			
Tax loss carry forward	227,661	17,688	—
Bad debt provision	82,807	84,365	71,807
Accrued interest	49,864	19,132	26,029
Unrealized foreign exchange loss, net	—	4,474	37,623
Accrued expenses	52,672	14,730	9,457
Financial instruments, net	46,530	12,844	—
Inventory provision	7,398	4,276	2,293
Accrued advertising	7,847	3,812	1,638
Development costs	—	656	1,719
Book versus tax basis of fixed assets	—	—	21,631
	474,779	161,977	172,197
Temporary differences for which realization is not probable ("valuation allowance")	(54,585)	(87,967)	(97,037)
	420,194	74,010	75,160
Deferred tax liabilities in Poland:			
Book versus tax basis of GSM/UMTS licenses	(386,037)	(127,418)	(102,482)
Book versus tax basis of fixed assets	(62,794)	(7,100)	—
Unrealized foreign exchange gain, net	(23,484)	—	—
Net deferred tax liability	**(52,121)**	**(60,508)**	**(27,322)**

The amount of valuation allowance as at December 31, 2001 consists primarily of the bad debt provision for which tax deductibility is yet uncertain and as at December 31, 2000 and December 31, 1999 — of the bad debt provision not recoverable together with unrealized foreign exchange losses.

(in thousands of PLN)

11. Taxation — (Continued)

The increase in tax loss carry forward resulted mainly from payments for telecommunication licenses in 2001 which are tax deductible expenses whereas under accounting rules they represented decrease of liabilities. Under accounting rules the licenses are expensed during their useful life through amortization.

12. Short-term investment and other financial assets

	As at December 31, 2001	As at December 31, 2000	As at December 31, 1999
		(restated)	(restated)
Treasury Bills	91,456	191,679	198,468
Rental derivatives — short-term portion (see Note 17)	6,822	—	—
	98,278	**191,679**	**198,468**

The Treasury Bills represent short-term portion of US Treasury and German Treasury Bills which are part of an escrow fund established to secure payment of interest during the first two and a half years on the 11¼% Notes.

The Treasury Bills are recorded at cost plus accrued interest that approximates their market value. Their fair value as at December 31, 2001 amounted to PLN 92 million comparing to PLN 191 million and PLN 198 million as at December 31, 2000 and December 31, 1999, respectively.

Rental derivatives represent short-term portion of the derivatives separated from rental contracts (see also Notes 4.1.a and 17).

13. Debtors and prepayments

	As at December 31, 2001	As at December 31, 2000	As at December 31, 1999
		(restated)	(restated)
Trade debtors and accrued revenue	671,621	626,054	505,043
Prepaid expenses	24,141	17,660	27,862
Other debtors	19,078	26,188	43,145
Amounts due from State Treasury	11,908	32,390	54,835
Accounts receivable from shareholders	614	1,195	194
	727,362	703,487	631,079
Provision for doubtful debtors	(183,940)	(221,821)	(166,834)
	543,422	**481,666**	**464,245**

14. Inventory

	As at December 31, 2001	As at December 31, 2000	As at December 31, 1999
		(restated)	(restated)
Telephones	117,653	154,015	135,362
Network spare parts and accessories	75,884	70,547	56,808
	193,537	224,562	192,170
Inventory provision	(26,423)	(15,272)	(8,190)
	167,114	**209,290**	**183,980**

(in thousands of PLN)

15. Tangible fixed assets, net

	As at December 31, 2001	As at December 31, 2000 (restated)	As at December 31, 1999 (restated)
Land and buildings	186,473	191,372	195,771
Plant and equipment	2,821,953	2,688,668	1,954,057
Motor vehicles	18,800	12,456	12,061
Other fixed assets	548,470	420,473	208,389
Construction in progress	208,114	201,122	203,627
	3,783,810	**3,514,091**	**2,573,905**

During the year ended December 31, 2001 the Company capitalized PLN 6,817 of foreign exchange gains, PLN 15,116 of interest expense and PLN 187 of hedging expense. For the year ended December 31, 2000 the Company capitalized PLN 3,412 of foreign exchange losses and PLN 3,111 of interest expense and for the year ended December 31, 1999, PLN 10,043 of foreign exchange losses and no interest expense was capitalized.

The restated movement in each year was as follows:

	Land and Buildings	Plant and equipment	Motor vehicles	Other fixed assets	Construction in progress	Total
Cost						
As at January 1, 1999	80,768	951,995	14,915	48,530	702,567	1,798,775
Additions	119,169	—	—	4,164	1,023,527	1,146,860
Transfers	—	1,287,060	9,317	182,419	(1,503,373)	(24,577)
Disposals	—	(1,273)	(794)	(2,923)	(19,094)	(24,084)
As at December 31, 1999	199,937	2,237,782	23,438	232,190	203,627	2,896,974
Depreciation						
As at January 1, 1999	814	107,266	6,661	12,852	—	127,593
Charge	3,352	189,142	5,158	13,678	—	211,330
Transfers	—	(12,190)	—	4	—	(12,186)
Disposals	—	(493)	(442)	(2,733)	—	(3,668)
As at December 31, 1999	4,166	283,725	11,377	23,801	—	323,069
Net book value as at December 31, 1999	**195,771**	**1,954,057**	**12,061**	**208,389**	**203,627**	**2,573,905**
Cost						
As at January 1, 2000	199,937	2,237,782	23,438	232,190	203,627	2,896,974
Additions	125	7,670	—	2,564	1,323,533	1,333,892
Transfers	—	1,060,431	6,140	237,067	(1,303,638)	—
Disposals	—	(12,186)	(851)	(3,020)	(22,400)	(38,457)
As at December 31, 2000	200,062	3,293,697	28,727	468,801	201,122	4,192,409
Depreciation						
As at January 1, 2000	4,166	283,725	11,377	23,801	—	323,069
Charge	4,524	331,671	5,559	26,903	—	368,657
Disposals	—	(10,367)	(665)	(2,376)	—	(13,408)
As at December 31, 2000	8,690	605,029	16,271	48,328	—	678,318
Net book value as at December 31, 2000	**191,372**	**2,688,668**	**12,456**	**420,473**	**201,122**	**3,514,091**

(in thousands of PLN)

15. Tangible fixed assets, net — (Continued)

	Land and Buildings	Plant and equipment	Motor vehicles	Other fixed assets	Construction in progress	Total
Cost						
As at January 1, 2001	200,062	3,293,697	28,727	468,801	201,122	4,192,409
Additions	35	—	—	8,881	912,561	921,477
Transfers	—	709,370	13,698	164,274	(887,342)	—
Disposals	—	(7,450)	(7,204)	(10,930)	(18,227)	(43,811)
As at December 31, 2001	200,097	3,995,617	35,221	631,026	208,114	5,070,075
Depreciation						
As at January 1, 2001	8,690	605,029	16,271	48,328	—	678,318
Charge	4,934	571,670	7,076	44,510	—	628,190
Transfer	—	1,108	5	(1,113)	—	—
Disposals	—	(4,143)	(6,931)	(9,169)	—	(20,243)
As at December 31, 2001	13,624	1,173,664	16,421	82,556	—	1,286,265
Net book value as at December 31, 2001	**186,473**	**2,821,953**	**18,800**	**548,470**	**208,114**	**3,783,810**

In 2001 the Company recognized PLN 119,641 of impairment losses related to scheduled sales of part of network equipment. The impairment losses were calculated on the basis of net selling price, which was the price offered by the potential buyers. The impairment losses were recognized as additional depreciation.

Tangible fixed assets held under capital leases (included in the previous schedule):

	As at December 31, 2001			As at December 31, 2000 (restated)			As at December 31, 1999 (restated)		
	Land	Buildings	Other	Land	Buildings	Other	Land	Buildings	Other
Cost	6,293	193,177	990	6,293	193,177	990	6,293	193,177	990
Accumulated depreciation	—	(13,625)	(240)	—	(8,690)	(140)	—	(4,166)	(41)
Net	6,293	179,552	750	6,293	184,487	850	6,293	189,011	949

16. Intangible fixed assets, net

	As at December 31, 2001	As at December 31, 2000 (restated)	As at December 31, 1999 (restated)
GSM and UMTS licenses	2,143,111	2,166,875	953,226
Computer and network software	240,402	147,150	97,388
Trademark	132	146	161
Transaction costs	29,165	—	—
	2,412,810	**2,314,171**	**1,050,775**

During the year ended December 31, 2001 the Company capitalized to intangible fixed assets PLN 101,873 of foreign exchange gains, PLN 153,808 of interest expense and PLN 1,428 of hedging expenses. For the year ended December 31, 2000 the Company capitalized to intangible fixed assets PLN 764 of foreign exchange losses and PLN 7,255 of interest expense and for the year ended December 31, 1999 the Company capitalized PLN 3,416 of foreign exchange losses and PLN 15,569 of interest expense.

Transaction costs as at December 31, 2001 related to the Bank Credit Facilities (see Note 4.1.a).

The Company has no intangible assets generated internally.

(in thousands of PLN)

16. Intangible fixed assets, net — (Continued)

The restated movement in each year was as follows:

	GSM & UMTS Licenses	Computer and network software	Trade Mark	Transaction costs	Total
Cost					
As at January 1, 1999	700,564	46,691	206	—	747,461
Additions	408,905	82,833	—	—	491,738
As at December 31, 1999	1,109,469	129,524	206	—	1,239,199
Amortization					
As at January 1, 1999	107,498	10,527	32	—	118,057
Charge	48,745	21,609	13	—	70,367
As at December 31, 1999	156,243	32,136	45	—	188,424
Net book value as at December 31, 1999	**953,226**	**97,388**	**161**	**—**	**1,050,775**
Cost					
As at January 1, 2000	1,109,469	129,524	206	—	1,239,199
Additions	1,286,030	129,922	—	—	1,415,952
Disposals	—	(6,149)	—	—	(6,149)
As at December 31, 2000	2,395,499	253,297	206	—	2,649,002
Amortization					
As at January 1, 2000	156,243	32,136	45	—	188,424
Charge	72,381	78,652	15	—	151,048
Disposals	—	(4,641)	—	—	(4,641)
As at December 31, 2000	228,624	106,147	60	—	334,831
Net book value as at December 31, 2000	**2,166,875**	**147,150**	**146**	**—**	**2,314,171**
Cost					
As at January 1, 2001	2,395,499	253,297	206	—	2,649,002
IAS 39 adjustments	—	—	—	16,553	16,553
As at January 1, 2001	2,395,499	253,297	206	16,553	2,665,555
Additions	—	222,168	—	34,254	256,422
Disposals	—	(6,524)	—	(15,670)	(22,194)
Capitalization	53,363	—	—	—	53,363
As at December 31, 2001	2,448,862	468,941	206	35,137	2,953,146
Amortization					
As at January 1, 2001	228,624	106,147	60	—	334,831
IAS 39 adjustments	—	—	—	5,217	5,217
As at January 1, 2001	228,624	106,147	60	5,217	340,048
Charge	77,127	128,816	14	16,425	222,382
Disposals	—	(6,424)	—	(15,670)	(22,094)
As at December 31, 2001	305,751	228,539	74	5,972	540,336
Net book value as at December 31, 2001	**2,143,111**	**240,402**	**132**	**29,165**	**2,412,810**

16. Intangible fixed assets, net — (Continued)

Licenses

The balance of GSM and UMTS licenses consist of GSM 900, GSM 1800, UMTS and Lease line licenses acquired by the Company from the Polish State, represented by the Minister of Communications.

The GSM 900 license was acquired on February 23, 1996 and issued for a term of 15 years and allows the Company to apply for an extension for an agreed period one year prior to its expiration date together with a permit to install and utilize telecommunication equipment and network, and allocation of frequencies in the ETSI/GSM 900 MHz band. The Company was required to pay the Polish government a fee equal to the Zloty equivalent of EUR 218 million, which was fully paid till December 31, 2001.

The GSM 900 license is subject to a number of commercial and technical conditions. While Polish law provides that the license may be revoked or limited in the event that the Company fails to meet any of these conditions. The Company believes that it is currently in compliance in substance with all of the GSM 900 license conditions.

The GSM 1800 license was acquired on August 11, 1999 and was in use from March 1, 2000. The Company was required to pay the Polish government a fee equal to the Zloty equivalent of EUR 100 million, which is payable in four installments. As at December 31, 2001 the outstanding liability balance amounted to PLN 55,747 being the last installment payable in 12 months.

Similar to the GSM 900 license, the GSM 1800 license requires that the Company meets certain coverage and technical criteria, including a requirement that the dropped call rate does not exceed 5% during peak hours and that the Company attains geographical coverage combined with the 900 MHz and 1800 MHz frequencies of 90% by June 2004. The Company has already exceeded this level of coverage.

On September 29, 2000 the Minister of Communications granted the Company a license to lease the telecommunication lines in the Company's network, including a permit to install and utilize telecommunication equipment and network (''the Lease Lines license''). The Lease Line license is valid for 15 years from the date when it was delivered to the Company and has been valued at the nominal value as the license fee was paid in a single installment.

On December 20, 2000 the Minister of Communications granted the Company a license to provide telecommunication services according to the UMTS standard in the 2 GHz band, including a permit to install and utilize telecommunication equipment and network, and allocation of frequencies in the 2 GHz band (''the UMTS license''). The UMTS license is valid for 22 years from the date of acquisition. The Company is required to pay to the Polish government a fee equal to the Zloty equivalent of EUR 650 million, which is payable in 22 installments. For the further disclosure of liability balance see Note 20d.

The UMTS license requires the Company to attain 20% population coverage by the end of 2004 and 40% population coverage by the end of 2007.

Currently the Company is also required to start offering UMTS services not earlier that January 1, 2003 and not later than January 1, 2004. In 2001 along with the other wireless operators in Poland the Company submitted a request to URT to extend the UMTS launch deadlines by 12 months. The Company has not received the answer till the day of the authorization of these consolidated financial statements.

The above-described GSM 900 license, the GSM 1800 license, the UMTS license and the Lease Lines license are not transferable assets.

(in thousands of PLN)

17. Financial assets

	As at December 31, 2001	As at December 31, 2000 (restated)	As at December 31, 1999 (restated)
Note Options (see Note 4.1.a and 24)	82,860	—	—
Rental derivatives long-term portion (see Note 4.1.a and 24)	23,125	—	—
Long-term investments	—	96,880	301,829
	105,985	**96,880**	**301,829**

As at December 31, 2001 financial assets consisted of the Note options that were separated from host contracts and Rental derivatives that were bifurcated from the foreign currency denominated rental contracts — for description of derivatives see Note 4.1.a and 24.

As at December 31, 2000, and December 31, 1999 the financial assets consisted of the long-term portion of the Treasury Bills, which are part of an escrow fund established to secure payments of interests on the Notes issued by PTC International Finance II S.A. in 1999. Those Bills have been partially paid during the year 2001. The outstanding balance as at December 31, 2001 amounted to PLN 91,456 and is included in short-term investments and other financial assets (see Note 12).

18. Deferred costs

	As at December 31, 2001	As at December 31, 2000 (restated)	As at December 31, 1999 (restated)
Multiple-element transaction costs	69,523	111,251	163,554
Notes issuance cost	—	67,522	69,897
Loan Facility issuance cost	—	11,336	12,493
Other	—	12,638	2,863
	69,523	**202,747**	**248,807**

Multiple-element transaction cost represents the deferred costs from non-separable contracts (see Note 4.1.b).

According to the requirements of IAS 39 Notes issuance costs were included in the initial measurement of long-term Notes liabilities and Loan Facility and Bank Credit Facilities issuance costs were reclassified into intangible assets (see Note 4.1.a).

(in thousands of PLN)

19. Current liabilities

	As at December 31, 2001	As at December 31, 2000 (restated)	As at December 31, 1999 (restated)
Accounts payable			
Construction payables	139,817	354,727	455,557
Trade creditors	147,699	165,508	247,956
Accounts payable to shareholders	2,920	1,748	6,201
	290,436	**521,983**	**709,714**
Amounts due to State Treasury	**46,184**	**44,732**	**27,790**
Interest-bearing liabilities			
GSM and UMTS licenses liability current portion (see Note 20d)	55,747	1,184,488	206,666
Finance lease payable — current portion (see Note 20c)	21,802	28,845	28,080
Index swaps-current portion (see Note 4.1.a, 20c and 24)	4,723	—	—
Short-term portion of Loan Facility (see Note 20b)	—	85,851	—
Overdraft facilities	—	36,342	—
	82,272	**1,335,526**	**234,746**
Accruals (see Note 21)	**234,763**	**131,614**	**152,061**
Other liabilities			
Deferred income	123,005	100,209	48,998
Forward contracts (see Note 24)	88,473	45,873	—
Payroll	138	2,047	3,351
CC swaps-current portion (see Note 4.1.a and 24)	5,909	—	—
	217,525	**148,129**	**52,349**
	871,180	**2,181,984**	**1,176,660**

In May 1998, the Company entered into a short-term renewable overdraft agreement with Bank Rozwoju Eksportu S.A. The terms provided for maximum borrowings of PLN 30,000 and interest based on 1 month WIBOR plus 0.5% p.a. (12.61% as at December 31, 2001). As at December 31, 2001 the overdraft facility was not utilized comparing to utilization of PLN 25,950 as at December 31, 2000.

In June 2000, the Company entered into a short-term renewable overdraft agreement with Bank Handlowy w Warszawie S.A. (a member of Citigroup). The terms provided for maximum borrowings of DEM 10,000 thousands and interest based on TOMNEXT WIBOR plus 0.5% p.a. counted for each interest period separately (13.50% as at December 31, 2001). As at December 31, 2001 the overdraft facility was not utilized comparing to utilization of PLN 10,392 (DEM 5,273 thousands) as at December 31, 2000.

(in thousands of PLN)

20. Long-term liabilities

	As at December 31, 2001	As at December 31, 2000 (restated)	As at December 31, 1999 (restated)
Interest-bearing liabilities			
Long-term Notes	3,258,680	2,651,052	2,654,021
Bank Credit Facilities	1,288,594	—	—
GSM and UMTS licenses liability	342,692	389,998	332,491
Loan Facility	—	751,980	1,076,566
Finance leases payable	174,112	193,361	190,259
Index swaps — long-term portion (see Note 4.1.a, 20c and 24)	19,855	—	—
Shareholders Loan	—	—	325,075
	5,083,933	**3,986,391**	**4,578,412**
Non-interest-bearing liabilities			
Multiple-element transaction revenue	69,523	111,251	163,554
CC swaps — long-term portion (see Note 4.1.a and 24)	124,299	—	—
	193,822	**111,251**	**163,554**
Deferred tax liability, net (see Note 11)	**52,121**	**60,508**	**27,322**
Provisions for liabilities and charges (see Note 21)	**20,652**	**12,908**	**3,764**
	5,350,528	**4,171,058**	**4,773,052**

a. Notes

10¾ Senior Subordinated Guaranteed Discount Notes ("10¾ Notes")

On July 1, 1997, PTC International Finance B.V., a wholly owned subsidiary of the Company, issued 10¾ Notes. The 10¾ Notes are unsecured, subordinated obligations of PTC International Finance B.V. and are limited to an aggregate principal amount at maturity of approximately USD 253 million (PLN 1,009 million as at December 31, 2001). The 10¾ Notes were issued at a discount to their principal amount at maturity to generate gross proceeds of approximately USD 150 million (PLN 493 million at historical exchange rate). The 10¾ Notes will mature on July 1, 2007. Cash interest does not accrue on the 10¾ Notes prior to July 1, 2002. The obligations of PTC International Finance B.V. under the 10¾ Notes are fully and unconditionally guaranteed by the Company on a senior subordinated and unsecured basis pursuant to the Company's guarantee. The net proceeds from the 10¾ Notes are loaned to the Company.

(in thousands of PLN)

20. Long-term liabilities — (Continued)

a. Notes — (Continued)

The 10¾ Notes are redeemable at the option of the holders or issuer at the following redemption conditions:

Issuer Option (CALL)	Redemption, American Type
Period 1	July 1, 2002 - July 1, 2007
Redemption Amount	In whole or in part at price in range of 105.375% - 100.00% of nominal value
Plus	Accrued and unpaid interest to the date of redemption
Period 2	July 1, 1997 - July 1, 2000
Redemption Amount	Any amount up to 35% of the outstanding principal amount, from the net proceeds of the issuance of ordinary shares of the Company in a public offering. Redemption price — 110.75% of Accreted Value in range of USD 592.41 - USD 1,000 per Note, depending on the redemption date
Plus	Accrued and unpaid interest to the date of redemption
Option of holders (PUT)	Right to require the issuer to purchase the holder's Notes
Condition	Occurrence of a change of control
Purchase Amount	All or any part at price of 101.00% of Accreted Value in range of USD 592.41 - USD 1,000 per Note, depending on the redemption date
Plus	Accrued and unpaid interest to the purchase date
Change of control events	
Rating Decline	At least two Notches below or withdrawing and,
50% Voting Power	If any person or group becomes the beneficial owner of 50% or more of the total voting power except for Permitted Holders (basically existing shareholders or large and reliable telecommunication company)
Consolidation	Sale of substantially all the assets of the Company

The 10¾ Notes are measured in the balance sheet at an amortized cost. They are traded publicly in the United States and their market value as at December 31, 2001 was 87% of the nominal value (USD 220 million or PLN 878 million) whilst the carrying amount was PLN 953 million.

11¼ Senior Subordinated Guaranteed Discount Notes ("11¼ Notes")

On November 23, 1999, PTC International Finance II S.A., a wholly owned subsidiary of PTC International Finance (Holding) B.V. that is wholly owned by the Company, issued 11¼ Notes. The 11¼ Notes are unsecured, subordinated obligations of PTC International Finance II S.A. and are limited to an aggregate principal amount at maturity of EUR 300 million and USD 150 million (together PLN 1,655 million as at December 31, 2001). The 11¼ Notes were issued at a discount to their principal amount at maturity to generate gross proceeds of approximately EUR 296 million and USD 148 million (together PLN 1,897 million at historical exchange rate). The 11¼ Notes will mature on December 1, 2009. Cash interest accrues on the 11¼ Notes and is payable semi-annually, on each June 1 and December 1, beginning in year 2000. The accrued interest on the 11¼ Notes is presented in the balance sheet within the current liabilities.

Payment of the first five interest coupons were and will be delivered from the funds set on escrow account and invested in the Treasury Bills (see Note 12). The obligations of PTC International Finance II S.A. under the 11¼ Notes are fully and unconditionally guaranteed by the Company on a senior subordinated and unsecured basis pursuant to the Company's guarantee. The net proceeds from the 11¼ Notes are loaned to the Company.

(in thousands of PLN)

20. Long-term liabilities — (Continued)

a. Notes — (Continued)

The 11¼ Notes are redeemable at the option of the holders or issuer at the following redemption conditions:

Issuer Option (CALL)	Redemption, American Type
Period 1	December 1, 2004 - December 1, 2009
Redemption Amount	In whole or in part at price in range of 105.625% - 100.00% of nominal value
Plus	Accrued and unpaid interest to the date of redemption
Period 2	November 23, 1999 - December 1, 2002
Redemption Amount	Any amount up to 35% of the outstanding principal amount, from the net proceeds of the issuance of ordinary shares of the Company in a public offering. Redemption price — 111.25% of nominal value
Plus	Accrued and unpaid interest to the date of redemption
Option of holders (PUT)	Right to require the issuer to purchase the holder's Notes
Condition	Occurrence of a change of control
Purchase Amount	All or any part at price of 101.00% of nominal value
Plus	Accrued and unpaid interest to the purchase date
Change of control events	
Rating Decline	At least two Notches below or withdrawing and,
50% Voting Power	If any person or group becomes the beneficial owner of 50% or more of the total voting power except for Permitted Holders (basically existing shareholders or large and reliable telecommunication company)
Consolidation	Sale of substantially all the assets of the Company

The 11¼ Notes are measured in the balance sheet at an amortized cost. They are traded publicly in the United States and their market value as at December 31, 2001 was 101% of the nominal value for the EUR part (EUR 303 million or PLN 1,067 million) and 102% of the nominal value for the USD part (USD 153 million or PLN 610 million). The carrying amounts as at December 31, 2001 were PLN 1,035 million and PLN 581 million for EUR and USD parts, respectively.

10⅞ Senior Subordinated Guaranteed Notes ("10⅞ Notes")

On May 8, 2001, PTC International Finance II S.A., a wholly owned subsidiary of the Company, issued 10⅞ Notes with the face value of EUR 200 million (PLN 704 million as at December 31, 2001) and maturity date on May 1, 2008. The 10⅞ Notes were issued at par. The interest coupon is paid every January 31 and July 31, commencing July 31, 2001.

The obligations of PTC International Finance II S.A. under the 10⅞ Notes are fully and unconditionally guaranteed by the Company on a senior subordinated and unsecured basis pursuant to the Company's guarantee. The net proceeds from the 10⅞ Notes are loaned to the Company.

(in thousands of PLN)

20. Long-term liabilities — (Continued)

a. Notes — (Continued)

The 10⅞ Notes are redeemable at the option of the holder or issuer at the following redemption conditions:

<u>Issuer Option (CALL)</u>	Redemption, American Type
Period 1	May 1, 2005 – May 1, 2008
Redemption Amount	In whole or in part at price in range of 105.438% – 100.00% of nominal value
Plus	Accrued and unpaid interest to the date of redemption
Period 2	May 8, 2001 – May 1, 2004
Redemption Amount	Any amount up to 35% of the outstanding principal amount, from the net proceeds of the issuance of ordinary shares of the Company in a public offering. Redemption price — 110.875% of nominal value
Plus	Accrued and unpaid interest to the date of redemption
<u>Option of holders (PUT)</u>	Right to require the issuer to purchase the holder's Notes
Condition	Occurrence of a change of control
Purchase Amount	All or any part at price of 101.00% of nominal value
Plus	Accrued and unpaid interest to the purchase date
Change of control events:	
Rating Decline	At least two Notches below or withdrawing and,
50% Voting Power	if any person or group becomes the beneficial owner of 50% or more of the total voting power except for Permitted Holders (basically existing shareholders or large and reliable telecommunication company) and,
Consolidation	sale of substantially all the assets of the Company,
Supervisory Board	certain changes in Supervisory Board.

The 10⅞ Notes are measured in the balance sheet at an amortized cost. They are traded publicly in the United States and their market value as at December 31, 2001 was 100% of the nominal value (EUR 200 million or PLN 704 million). The carrying amount as at December 31, 2001 was PLN 690 million.

b. Bank Credit Facilities

On February 20, 2001 the Company signed the Main Bank Facility Agreement amounting to EUR 550 million and the Supplemental Bank Facility Agreement amounting to EUR 100 million with the consortium of banks organized by Deutsche Bank AG London, Deutsche Bank Polska S.A., Dresdner Bank Luxembourg S.A. and the European Bank of Reconstruction and Development.

As at December 31, 2001 the balance outstanding under the Main Bank Facility Agreement amounted to PLN 873 million, which consisted in full of the domestic tranche (equivalent of EUR 257.5 million at the drawndown foreign exchange rate).

The main terms of the Main Bank Facility Agreement are as follows:

Facilities limits	equivalent of EUR 550 million available under two tranches: foreign exchange tranche amounting to EUR 292.5 million and domestic tranche of EUR 257.5 million available in PLN
Interests	LIBOR, EURIBOR, WIBOR plus negotiated margins
Collateral	pledge on the Company's assets and rights except for future real estates, the escrow fund for Notes and leased assets
Repayment date	quarterly reduction in facility limit starting from September 30, 2004 to February 20, 2006.

(in thousands of PLN)

20. Long-term liabilities — (Continued)

b. Bank Credit Facilities — (Continued)

As at December 31, 2001 the balance outstanding under Supplemental Bank Facility Agreement amounted to PLN 415 million of domestic tranche (equivalent of EUR 108 million at the drawndown foreign exchange rate). The agreement was amended on September 21, 2001 and extended from EUR 100 million to EUR 150 million.

The main terms of the amended Supplemental Bank Facility Agreement are as follows:

Facilities limits	equivalent of EUR 150 million available under two tranches: foreign exchange tranche amounting to EUR 20 million and domestic tranche of EUR 130 million available in PLN
Interests	LIBOR, EURIBOR, WIBOR plus negotiated margins
Collateral	pledge on the Company's assets and rights except for future real estates, the escrow fund for Notes and leased assets
Repayment date	reduction in facility limit starting from September 30, 2005 to March 31, 2007.

The changes in the pledge agreement related to the increase of the Supplemental Bank Facility Agreement were registered on October 26, 2001.
The Loan Facility was paid out from the Bank Credit Facilities newly signed in February 2001.

c. Finance leases

On March 25, 1997 the Company entered into a finance lease agreement relating to its new headquarters building and underlying land. The headquarters lease obligation is denominated in USD and payable in PLN. The term of the lease is 15 years and the Company has a right to acquire the leased asset at the end of the lease not sooner than on April 30, 2013 and not later than by the July 31, 2013 (the value of the purchase option calculated as the rental space multiplied by the price per square meter amounts to USD 11,825).

The minimum lease payments have been discounted at 11.338% (first building leased in second half of 1998) and at 11.174% (second building leased in July 1999), which approximated the Company's borrowing rate for USD as at the date of acquisition of the leased assets.

The timing and values of lease payments are presented below.

The future value payments under finance leases as at December 31, 2001 include full indexing of minimal lease payments (Index swap).

	As at December 31, 2001				
	Future Value	Interest	Discounted with index swaps	Discounted	Index swaps
Due in					
one year	31,208	4,683	26,525	21,802	4,723
two years	32,144	9,757	22,387	18,763	3,624
three years	33,109	14,361	18,748	16,148	2,600
four years	34,102	18,565	15,537	13,897	1,640
five years	35,125	21,798	13,327	12,586	741
after five years	299,760	175,792	123,968	112,718	11,250
	465,448	**244,956**	**220,492**	**195,914**	**24,578**

(in thousands of PLN)

20. Long-term liabilities — (Continued)

c. Finance leases — (Continued)

	As at December 31, 2000		
	Future Value	(restated) Interest	Discounted
Due in			
one year	30,577	1,732	28,845
two years	30,577	4,671	25,906
three years	30,577	7,306	23,271
four years	30,577	9,662	20,915
five years	30,577	11,768	18,809
after five years	276,181	171,721	104,460
	429,066	**206,860**	**222,206**

	As at December 31, 2000		
	Future Value	(restated) Interest	Discounted
Due in			
one year	29,807	1,727	28,080
two years	29,807	4,676	25,131
three years	29,807	7,315	22,492
four years	29,807	9,673	20,134
five years	29,807	11,782	18,025
after five years	300,363	195,886	104,477
	449,398	**231,059**	**218,339**

d. License fee payables

The fees for the Company's GSM 900, GSM 1800 and UMTS licenses are denominated in EUR and payable in installments. These deferred payments have been discounted at 6.78% (the GSM 900 license), at 9.52% (the GSM 1800 license) and at 12.06% for short-term and 12.11% for long-term installments (the UMTS license), which approximated the Company's borrowing rate for EUR as at the date of acquisition of the licenses. As at December 31, 2001 the carrying amount of the GSM 1800 license approximated its fair value and the fair value of the UMTS license amounted to PLN 360 million. As at that date there was no GSM 900 license liability outstanding.

The balances payable on the licenses as at December 31, 2001 were:

Maturity	EUR'000 nominal	EUR'000 discounted	PLN'000 discounted
Due in one year (see Note 19)	16,716	15,829	55,747
Due in year four	15,000	9,783	34,454
Due in year five	15,000	8,726	30,733
Due after year five	360,000	78,794	277,505
	406,716	**113,132**	**398,439**

(in thousands of PLN)

20. Long-term liabilities — (Continued)

d. License fee payables — (Continued)

The restated balances payable as at December 31, 2000 were:

Maturity	EUR'000 nominal	EUR'000 discounted	PLN'000 discounted
Due in one year (see Note 19)	322,816	307,309	1,184,488
Due in year two	16,715	14,498	55,881
Due in year five	15,000	8,715	33,592
Due after year five	375,000	77,969	300,525
	729,531	**408,491**	**1,574,486**

The restated balances payable as at December 31, 1999 were:

Maturity	EUR'000 nominal	EUR'000 discounted	PLN'000 discounted
Due in year one (see Note 19)	51,035	49,573	206,666
Due in year two	72,815	66,587	277,596
Due in year three	16,716	13,168	54,895
	140,566	**129,328**	**539,157**

21. Accruals and Provisions for liabilities and charges

	As at December 31, 2001	As at December 31, 2000 (restated)	As at December 31, 1999 (restated)
Accruals			
Accruals	231,843	129,756	150,841
Social fund	2,920	1,858	1,220
	234,763	**131,614**	**152,061**
Provisions for liabilities and charges			
Provision for loyalty program and potential losses			
Opening balance	12,908	3,764	—
Additions	15,144	18,789	3,764
Disposals, including:			
Usage	(1,048)	(1,242)	—
Cancellation	(6,352)	(8,403)	—
Closing balance	**20,652**	**12,908**	**3,764**

The presentation of the accruals has been changed comparing to the consolidated financial statements for the year 2000. The Company transferred the provision for the loyalty program that has been implemented in October 1999 from short to long-term liabilities.

The balances of accruals included mainly interests, employee bonuses and operating costs not invoiced.

The social fund is an employer's obligation based on a mandated calculation based on the number of employees and the monthly minimum wage in Poland. The amounts calculated under this formula must be used for the benefits of the employees.

(in thousands of PLN)

22. Capital

	As at December 31, 2001	As at December 31, 2000 (restated)	As at December 31, 1999 (restated)
Allotted, called-up and fully paid:			
471,000 ordinary shares of PLN 1,000 each	471,000	471,000	471,000
Additional paid-in capital	409,754	409,754	—
	880,754	**880,754**	**471,000**

According to the Company's Shareholders' Meeting resolution dated November 30, 2000, the shareholders' equity was increased with the additional paid-in capital. The shareholders contributed the capital proportionally to their voting rights. The contributions were transferred from the Shareholder loan and paid in cash in the amount of PLN 16,827.

23. Related party transactions

	As at and for the year ended December 31, 2001	As at and for the year ended December 31, 2000 (restated)	As at and for the year ended December 31, 1999 (restated)
Elektrim S.A.			
Inter-company receivables	93	132	—
Inter-company payables	23	224	925*
Inter-company sales	741	839	560
Inter-company purchases	272	1,990	5,615
Elektrim Telekomunikacja Sp. z o.o. ("ET")			
Inter-company sales	38	—	—
DeTeMobil Deutsche Telekom MobilNet GmbH ("DeTeMobil")			
Inter-company receivables	521	1,063	—
Inter-company payables	2,897	1,524	5,082*
Inter-company sales	24,365	19,670	19,795
Inter-company purchases	22,128	22,246	27,543
MediaOne International B.V. ("MediaOne")			
Inter-company purchases	278	7,834	14,426

* Balances of the inter-company payables as at December 31, 1999 represent net amounts.

Management believes that related party transactions were conducted primarily on market terms.

(in thousands of PLN)

24. Derivative financial instruments

Type of derivative	Forward and option contracts	Note options	CC swaps	Index swaps	Rental derivatives	Total
Balance as at January 1, 2001 asset/(liability)	**(45,873)**	**18,077**	**—**	**(35,962)**	**8,853**	**(54,905)**
Reclassification between leasing liability and index swap	—	—	—	20,890	—	20,890
Initial measurement of new financial instruments	1,076	4,227	—	—	—	5,303
Cash paid/(received)	90,485	—	1,959	(4,910)	(2,272)	85,262
Changes in the fair value reported in the statement of operations	(134,161)	60,556	(7,868)	(4,596)	23,366	(62,703)
Changes in the fair value reported in shareholders' equity (hedge reserve)	—	—	(124,299)	—	—	(124,299)
Balance as at December 31, 2001 asset/(liability)	**(88,473)**	**82,860**	**(130,208)**	**(24,578)**	**29,947**	**(130,452)**

Forward and foreign exchange option contracts

During the year 2001 the Company undertook actions aimed at reducing the foreign currency transaction exposure resulting from operating activities forecasted for 2001 and 2002. Realization of the operating activity hedging program included entering into 130 NDF transactions for the total amount of EUR 297 million.

In order to hedge part of the UMTS license fees payable in 2001 the Company concluded ten NDF transactions for the total amount of EUR 116 million maturing in March and September 2001, and two EUR call PLN put non-delivery options for total amount of EUR 20 million maturing in September 2001.

The Company entered also into five forward transactions for the amount of EUR 22 million to hedge foreign exchange rate for the repayment of Bank Credit Facility EUR tranche in November 2001.

CC swaps

On April 4, 2001 the Company entered into the cross currency interest rate swap transaction which swapped its fixed rate interest coupon payments on EUR 60 million aggregate amount of 11¼ Notes with 15.20% coupon payments on PLN 217,140. The coupons will be swapped during the period commencing on June 3, 2002 and terminating on December 1, 2007.

On May 21, 2001 the Company entered into the cross currency interest rate swap transaction which swapped its fixed rate interest coupon payments on EUR 90 million aggregate amount of 11¼ Notes with 15.26% coupon payments on PLN 314,640. The coupons will be swapped during the period commencing on June 3, 2002 and terminating on December 1, 2007.

On May 23, 2001 the Company entered into the cross currency interest rate swap transaction which swapped its fixed rate interest coupon payments on EUR 100 million aggregate amount of 10⅞ Notes with 13.96% coupon payments on PLN 344,890. The coupons will be swapped during the period commencing on May 8, 2001 and terminating on May 1, 2007.

On June 1, 2001 the Company entered into the cross currency interest rate swap transaction which swapped its fixed rate interest coupon payments on USD 75 million aggregate amount of 11¼ Notes with 14.79% coupon payments on PLN 298,837. The coupons will be swapped during the period commencing on June 3, 2002 and terminating on December 1, 2007.

On June 11, 2001 the Company entered into the cross currency interest rate swap transaction which swapped its fixed rate interest coupon payments on USD 125 million aggregate amount of 10¾ Notes with 13.52% coupon

(in thousands of PLN)

24. Derivative financial instruments — (Continued)

payments on PLN 496,438. The coupons will be swapped during the period commencing on July 1, 2002 and terminating on July 1, 2005.

On December 10, 2001 the Company entered into two cross currency interest rate swap transactions. The Company swapped its fixed rate interest coupon payments on EUR 75 million aggregate amount of $11\frac{1}{4}$ Notes with 13.56% coupon payments on PLN 271,650. The coupons will be swapped during the period commencing on December 1, 2002 and terminating on December 1, 2007. Under the terms of the second transaction the Company swapped its fixed rate interest coupon payments on EUR 50 million aggregate amount of $10\frac{7}{8}$ Notes with 12.69% coupon payments on PLN 181,700. The coupons will be swapped during the period commencing on January 31, 2002 and terminating on May 1, 2007.

As at December 31, 2001 the fair value of the CC swaps described above amounted to a liability of PLN 130,208 of which PLN 124,299 is deferred in equity (as effective cash flow hedge) net of tax effect of PLN 27,344.

As at December 31, 2001 the Company transferred PLN 5,909 relating to fair value of the CC swaps from the equity to the statement of operations to match with hedged interests. The hedge is fully effective.

Index swaps and rental derivatives

As at December 31, 2001 the fair value of rental derivatives amounted to PLN 29,947. The change of fair value in the amount of PLN 21,094 net of tax effect of PLN 4,852 was recognized in the net income (see also Note 4.1.a and 20c).

Index swaps were presented in the Note 20c.

Note options

See Note 4.1.a (recognition and measurement) and Note 20a (conditions).

25. Financial commitments

a. Operating leases (not included in liabilities)

The minimum annual rentals payable on operating leases are as follows:

	As at December 31, 2001	As at December 31, 2000 (restated)	As at December 31, 1999 (restated)
Operating leases maturity			
Due in one year	13,621	9,218	17,475
Due in two years	11,440	13,399	9,010
Due in three years	8,244	10,008	14,201
Due in four years	8,185	7,182	6,253
Due in five years	10,081	6,202	2,345
Due after five years	89,693	95,185	31,896
	141,264	**141,194**	**81,180**

Assets under operating leases include primarily network sites, office space, retail outlets and warehouses.

(in thousands of PLN)

25. Financial commitments — (Continued)

b. Capital equipment commitments (not included in liabilities)

	As at December 31, 2001	As at December 31, 2000 (restated)	As at December 31, 1999 (restated)
Authorized and contracted	393,841	970,532	319,725
Authorized and not contracted	709,780	1,487,877	1,495,522
	1,103,621	**2,458,409**	**1,815,247**

26. Contingent liabilities

As at December 31, 2001 the Company did not have any significant contingent liabilities.

27. Dividend restriction

The Company's statutory financial statements are prepared in accordance with Polish accounting regulations. Dividends may only be distributed from the net profit reported in the Polish annual statutory financial statements. As at the date of signing this report there was not Shareholders' decision regarding net income distribution.

As at the day of authorization of these consolidated financial statements the Company's Shareholders' Meeting has not made a decision of a distribution of profits, yet.

Dividend distribution is restricted mainly by Notes Agreements that require the Company to have Debt to Adjusted Consolidated Net Worth ratio at the level below 2.0:1.0.

(in thousands of PLN)

28. Supplementary cash flow information

Cash and cash equivalents consist of cash on hand, balances deposited with banks and short-term, highly liquid investments.

	As at December 31, 2001	As at December 31, 2000 (restated)	As at December 31, 1999 (restated)
Balances deposited with banks:			
Current accounts	10,416	14,669	29,422
Term deposits with original maturity of less than 90 days	25,609	14,033	654,305
Treasury bills with original maturity of less than 90 days	—	—	410,694
Social fund cash	301	602	468
Cash on hand	185	161	620
	36,511	**29,465**	**1,095,509**

As at December 31, 2001 the Company revalued cash on hand and balances deposited with banks denominated in foreign currencies. The net result of the revaluation was PLN 362 of foreign exchange losses, which were reported under interest and other financial expenses. The social fund cash is restricted for the benefits of the employees as described in Note 4.2.f.

Non-cash transactions

	As at December 31, 2001	As at December 31, 2000 (restated)	As at December 31, 1999 (restated)
UMTS license acquisition	—	1,279,147	—
Transfer of Shareholders' Loan to capital (see Note 22)	—	392,927	—
GSM 1800 license acquisition	—	—	389,923
Assets acquired under finance lease	—	—	119,963

29. Employment

Average headcount in the Company during the presented years was as follows:

	Year ended December 31, 2001	Year ended December 31, 2000 (restated)	Year ended December 31, 1999 (restated)
Average headcount	3,399	2,865	2,170

(in thousands of PLN)

30. Estimation of the fair values

The following table presents the carrying amounts and fair values of the Company's financial instruments outstanding as at December 31, 2001, 2000 and 1999, in million PLN. The carrying amounts in the table are included in the balance sheet under the indicated captions.

	As at December 31, 2001		As at December 31, 2000 (restated)		As at December 31, 1999 (restated)	
	million PLN		million PLN		million PLN	
	Carrying amount	Fair value	Carrying amount	Fair value	Carrying amount	Fair value
Financial Assets						
Cash and cash equivalents	37	37	29	29	1,096	1,096
Short-term investments and other financial assets	98	99	192	191	198	198
Debtors and accrued revenue	507	507	432	432	382	382
Financial assets (long-term)	106	106	97	97	302	299
Financial Liabilities						
Current liabilities and accruals	680	680	2,008	2,008	1,072	1,072
Long-term liabilities	5,055	5,073	3,806	3,526	4,392	4,315

Debtors, current liabilities and accruals

The carrying amounts are a reasonable estimate of the fair values because of the short maturity of such instruments.
The carrying amounts of forward foreign exchange contracts are based on quoted market forward rates as at the year-end balance sheet dates.

Cash and cash equivalents, short-term investments and financial assets (long-term)

The carrying amounts of cash and cash equivalents approximate fair values. The fair value of publicly traded short-term and long-term investments is based on quoted market values.

Long-term liabilities

The fair value of fixed rate long-term debt is estimated using the expected future payments discounted at market interest rates, except for the publicly traded liabilities, which are quoted at market values. The carrying amount of market-based floating rate long-term loans approximates their fair value.

(in thousands of PLN)

31. Supplementary Information to IAS Consolidated Financial Statements

A reconciliation of the Company's consolidated net profit/(loss) under PAS and IAS is summarized as follows:

	Year ended December 31, 2001	Year ended December 31, 2000 (restated)	Year ended December 31, 1999 (restated)
Net profit/(loss) under PAS	263,442	62,795	(138,203)
Foreign translation difference	(2,098)	(636)	(1,582)
IAS adjustment for GSM licenses amortization	6,279	5,992	4,562
IAS adjustment for GSM licenses discount	(11,186)	(26,591)	(22,602)
Unrealized foreign exchange differences	111,227	45,188	29,569
Finance lease	(5,173)	(511)	1,113
IAS assets adjustment	(2,400)	(2,972)	(964)
Development and start-up costs	2,296	3,586	3,586
Notes valuation	6,132	—	—
Valuation of financial instruments	77,056	—	—
Change in revenue recognition policy	50,019	16,300	—
Deferred tax benefit/(charge)	(68,373)	6,236	2,018
Net profit/(loss) under IAS (restated)	**427,221**	**109,387**	**(122,503)**

A reconciliation of the Company's shareholders' equity under PAS and IAS is summarized as follows:

	As at December 31, 2001	As at December 31, 2000 (restated)	As at December 31, 1999 (restated)
Shareholders' equity under PAS	788,192	623,371	151,681
Foreign translation difference	(1,861)	(1,429)	(1,652)
IAS adjustment for GSM licenses amortization	27,892	21,613	15,621
IAS adjustment for GSM licenses discount	(90,961)	(79,775)	(53,184)
Unrealized foreign exchange differences	196,270	85,043	39,855
Finance lease	(17,681)	2,706	3,217
IAS assets adjustment	5,396	7,796	10,768
Development and start-up costs	—	(2,296)	(5,882)
Notes valuation	17,012	—	—
Valuation of financial instruments	53,424	—	—
Change in revenue recognition policy	66,319	16,300	—
Deferred tax asset/(liability)	(48,257)	13,618	7,382
Shareholders' equity under IAS (restated)	**995,745**	**686,947**	**167,806**

The above differences are caused by the following reasons:

- Recognition of the long-term license liabilities at present value for IAS purposes, while they were recorded at undiscounted nominal value under Polish accounting regulations. This accounting results in higher interest expense under IAS, which is partially offset by lower amortization expense and foreign exchange losses.
- Unrealized foreign exchange gains recognized as financial income for IAS purposes but deferred for PAS purposes.
- Recognition of the finance lease liabilities at present value together with bifurcation of the index derivative for IAS purposes, while they were recorded at undiscounted nominal value under Polish accounting regulations. Difference in treatment of assets held under finance lease and other capital assets written off for PAS purposes.

(in thousands of PLN)

31. Supplementary Information to IAS Consolidated Financial Statements — (Continued)

- Development and start-up costs expensed in IAS according to IAS 38 "Intangible Assets".
- The transaction costs related to the Bank Credit Facilities are amortized under IAS based on the credit limits available, whereas they are amortized on a straight-line basis under Polish accounting regulations.
- Recognition of long-term Notes liabilities at present value with transaction costs included in the initial measurement in IAS. Under Polish accounting regulations they were recorded at undiscounted nominal value and are recognized as deferred expenses being amortized on a straight-line basis.
- Derivatives embedded in the Company's Notes, finance lease liabilities, rental and other trade contracts recognized under IAS are not recognized for PAS purpose (see Note 4.1.a).
- Certain costs not relating to multiple-element transactions under IAS are accrued for PAS purpose (see Note 4.1.b).
- Adjustment to deferred tax on temporary differences in preceding adjustments.

32. Differences between IAS and U.S. GAAP

The Company's consolidated financial statements are prepared in accordance with International Accounting Standards, which differ in certain aspects from U.S. GAAP.

The effects of the principal differences between IAS and U.S. GAAP in relation to the Company's consolidated financial statements are presented below, with explanations of certain adjustments that affect total comprehensive net income.

Reconciliation of consolidated net income/(loss):

	Year ended December 31, 2001	Year ended December 31, 2000 (restated)	Year ended December 31, 1999 (restated)
Net income/(loss) under IAS (restated)	427,221	109,387	(122,503)
U.S. GAAP adjustments:			
(a) Removal of foreign exchange differences capitalized for IAS	107,075	4,176	(18,224)
(b) Depreciation and amortization of foreign exchange differences	9,268	9,188	6,392
(c) Development and start-up cost	—	—	(9,468)
(d) Revenue recognition (SAB 101)	1,151	(1,589)	—
(e) SFAS 133/IAS 39 implementation	(28,072)	—	—
(g) Deferred tax on above	(8,367)	445	2,938
Net income/(loss) under U.S. GAAP before cumulative effect on accounting changes	508,276	121,607	(140,865)
Accounting changes adjustments:			
(e) SFAS 133/IAS 39 implementation	(35,158)	—	—
(f) Transaction costs	7,220	—	—
(g) Deferred tax on above	6,470	—	—
Net income/(loss) under U.S. GAAP	**486,808**	**121,607**	**(140,865)**

(in thousands of PLN)

32. Differences between IAS and U.S. GAAP — (Continued)

Reconciliation of consolidated shareholders' equity:

	As at December 31, 2001	As at December 31, 2000 (restated)	As at December 31, 1999 (restated)
Consolidated shareholders' equity under IAS (restated)	995,745	686,947	167,806
U.S. GAAP adjustments:			
(a) Removal of foreign exchange differences capitalized for IAS	8,011	(99,064)	(103,240)
(b) Depreciation and amortization on above	32,233	22,965	13,777
(c) Development and start-up cost	—	—	—
(d) Revenue recognition (SAB 101)	(438)	(1,589)	—
(e) SFAS 133/IAS 39 implementation	(56,869)	—	—
(f) Transaction costs	—	—	—
(g) Deferred tax on above	(1,299)	445	—
Consolidated shareholders' equity under U.S. GAAP before cumulative effect on accounting changes	977,383	609,704	78,343
Accounting changes adjustments:			
(e) SFAS 133/IAS 39 implementation	28,797	—	—
(g) Deferred tax on above	(6,623)	—	—
Consolidated shareholders' equity under U.S. GAAP	**999,557**	**609,704**	**78,343**

a. Removal of foreign exchange differences capitalized for IAS

In accordance with IAS 23 "Borrowing Costs", the Company capitalizes financing costs, including interest and foreign exchange gains or losses, into assets under construction.

For tangible fixed assets under construction, the Company capitalizes interest and foreign exchange gains or losses incurred and directly attributable to the acquisition and construction of the qualifying assets that would have been avoided if the expenditure on the qualifying assets had not been made. The financing costs are capitalized only during the period of construction of the qualifying assets (see Note 15). The Company capitalized financing costs attributable to the acquisition of its GSM 900, GSM 1800 and UMTS licenses, including interest on the related long-term obligation and foreign exchange losses because these licenses are integral parts of the network (see Note 16).

Under Statement of Financial Accounting Standards 52 "Foreign Currency Translation", however, foreign exchange differences relating to financing obligations should be included in the statement of operations of the Company. Consequently, the amounts of foreign exchange differences capitalized in accordance with IAS 23 in the Company's consolidated financial statements are expensed under U.S. GAAP.

b. Depreciation and amortization

The U.S. GAAP adjustments for depreciation and amortization shown above represent the amounts of depreciation and amortization charges relating to capitalized foreign exchanges differences in the Company's IAS consolidated financial statements. Since under U.S. GAAP these foreign exchange differences are not permitted to be capitalized and are instead expensed, the depreciation and amortization of these capitalized differences under IAS has been reversed.

32. Differences between IAS and U.S. GAAP — (Continued)

c. Development and start-up cost

The Company has adopted IAS 38 ''Intangible Assets'' in 1999 giving its effect retrospectively. This has resulted in writing-off of development and start-up cost when they arose in 1996. For U.S. GAAP purposes the Company has written off in 1999 start-up costs following the issuance the SOP 98-5 in the United States.

d. Revenue recognition (SAB 101)

As described in Note 4.1.b the Company applied under IAS certain principles of SAB 101 retrospectively. Under U.S. GAAP a calendar year company is required to adopt the new rules in the fourth quarter of 2000. The Company should calculate the effect of SAB 101 as at January 1, 2000, make the cumulative entry as at that date, and restate all quarterly information previously reported during 2000.

Under U.S. GAAP, the application of SAB 101 results in the different treatment of the separable multiple-element transactions. Revenues and costs related to those transactions are recognized in the income statement as incurred, except for up-front non-refundable fees (activation fees) and direct costs related to these fees. These activation fees and related costs are deferred over the average expected life of the customer. Under IAS up-front non-refundable fees are recognized immediately.

e. SFAS 133

In June 1998, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 133, Accounting for Derivative Instruments and Hedging Activities. In June 1999, the FASB issued Statement No. 137, Accounting for Derivative Instruments and Hedging Activities — Deferral of the Effective Date of FASB Statement No. 133. In June 2000, the FASB issued Statement 138, Accounting for Certain Derivative Instruments and Certain Hedging Activities, an amendment of FASB Statement No. 133.

Statement 133, as amended, establishes accounting and reporting standards requiring that every derivative instrument (including certain derivative instruments embedded in other contracts) be recorded in the balance sheet as either an asset or liability measured at its fair value. The Statement requires that changes in the derivative instrument's fair value be recognized currently in earnings unless specific hedge accounting criteria are met. Special accounting for qualifying hedges allows a derivative instrument's gains and losses to offset related results on the hedged item in the income statement, to the extent effective, and requires that a company must formally document, designate, and assess the effectiveness of transactions that receive hedge accounting.

The Company adopted Statement 133 on January 1, 2001 and applied it to all hybrid instruments.

Long-term Notes issued by the Company have embedded derivatives (CALL options). These options should be separated from host contract and accounted for as a derivative under IAS 39, while they should not be separated under SFAS 133. Therefore, the fair value of the bifurcated options is not recognized for U.S. GAAP purposes.

The transition rules of IAS 39 specifies that any adjustment of the previous carrying amount was recognized as an adjustment of the balance of retained earnings at the beginning of the year 2001. The accounting change principles under U.S. GAAP advise to include the cumulative effect in the net income of the period of the change. However, for qualifying cash flow hedge instruments portion (or the entirety) of the cumulative effect should be classified in the other comprehensive income (hedge reserve), a component of shareholders' equity.

The cumulative adjustment as at January 1, 2001 resulted in an increase of accumulated deficit of PLN 4,926, net of a tax benefit.

32. Differences between IAS and U.S. GAAP — (Continued)

f. Transaction costs

As described in Note 4.1.a, IAS 39 requires transaction costs to be included in the initial measurement of financial assets and liabilities. Under U.S. GAAP these costs should be presented as deferred costs in the amount of PLN 73,642 as at January 1, 2001 and PLN 83,645 as at December 31, 2001.

The cumulative adjustment to the net income as at January 1, 2001 resulted in the increase of PLN 5,632 due to differences in transition rules in implementation of IAS 39 and SFAS 133.

g. Presentation of deferred taxation

Under IAS the Company may, if certain criteria are met, net deferred tax liabilities and assets and present a net balance in the balance sheet. Under U.S. GAAP current and non-current portions, by tax jurisdiction, of the above should be disclosed separately. As at December 31, 2001 the Company recognized PLN 210,978 of net current deferred tax asset (PLN 47,574 as at December 31, 2000 and PLN 21,254 as at December 31, 1999) and PLN 271,021 of net long-term deferred tax liability (PLN 107,637 as at December 31, 2000 and PLN 48,576 as at December 31, 1999).

h. Extraordinary item

In the first quarter of 2001 the Company refinanced the existing Loan Facility by the new Bank Credit Facilities. The intangible asset related to the Loan facility arrangement amounting to PLN 10,122 was written-off, net of a tax benefit of PLN 2,834. According to U.S. GAAP the Company should recognize this costs as an extraordinary item. Under IAS it is presented under amortization expense.

i. Other comprehensive income

The hedge reserve under U.S. GAAP constitutes a part of other comprehensive income, a component of shareholders' equity. The changes in other comprehensive income (hedge reserve) are reflected in accumulated other comprehensive income. A sum of other comprehensive income and net income for the period represents comprehensive income for the period.

j. SFAS 95

According to IAS 7-Cash Flow Statement cash flow from operating activities begins with net income before taxation, whereas Statement of Financial Accounting Standards No. 95, Statement of Cash Flows requires cash flow from operating activities to begin with net income after tax.

k. New accounting standards

The Company plans to implement the Statements No. 141, Business Combinations, No. 142, Goodwill and Other Intangible Assets and No. 144, Accounting for the Impairment of Long Lived Assets from January 1, 2002 and the Statement No. 143, Accounting for Asset Retirement Obligations from January 1, 2003 as the Statement is effective for fiscal years beginning after June 15, 2002.

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OJSC MOBILE TELESYSTEMS

CONSOLIDATED FINANCIAL STATEMENTS
AS OF DECEMBER 31, 2001 and 2000

TOGETHER WITH REPORT OF
INDEPENDENT PUBLIC ACCOUNTANTS

OJSC MOBILE TELESYSTEMS

CONSOLIDATED FINANCIAL STATEMENTS
AS OF DECEMBER 31, 2001 AND 2000

CONTENTS

Report of Independent Public Accountants

To Mobile TeleSystems:

We have audited the accompanying consolidated balance sheets of Mobile TeleSystems, a Russian Open Joint-Stock Company, and its subsidiaries as of December 31, 2000 and 2001, and the related consolidated statements of operations, cash flows and shareholders' equity for each of the three years in the period ended December 31, 2001. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Mobile TeleSystems and its subsidiaries as of December 31, 2000 and 2001, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2001, in conformity with accounting principles generally accepted in the United States.

Arthur Andersen ZAO

Moscow, Russia
April 18, 2002

MOBILE TELESYSTEMS

Consolidated Balance Sheets
at December 31, 2000 and 2001
(Amounts in thousands of U.S. dollars, except share amounts)

	December 31 2000	December 31 2001
CURRENT ASSETS:		
Cash and cash equivalents (Note 7)	$ 75,828	$ 219,629
Short-term investments (Note 8)	170,000	85,304
Trade receivables, net (Note 9)	15,817	24,258
Accounts receivable, related parties (Note 22)	4,937	2,377
Inventory, net (Note 10)	23,551	26,184
Prepaid expenses	11,268	22,712
VAT receivable	17,741	82,216
Deferred tax asset (Note 19)	2,071	12,040
Other current assets	8,771	8,374
Total current assets	329,984	483,094
PROPERTY, PLANT AND EQUIPMENT, net of accumulated depreciation of $87,676 and $168,989, respectively (Note 11)	439,307	841,308
LICENSES, net of accumulated amortization of $43,913 and $79,783, respectively (Notes 6 and 25)	204,996	297,490
OTHER INTANGIBLE ASSETS, net of accumulated amortization of $33,648 and $52,953, respectively (Note 12)	57,586	83,507
GOODWILL, net of accumulated amortization of $14,756 and $20,861, respectively (Note 6)	27,984	22,411
SUBSCRIBER ACQUISITION COSTS, net of accumulated amortization of $74,803 and $nil, respectively (Note 13)	27,553	—
DEBT ISSUANCE COSTS, net of accumulated amortization of $900 and $1,209, respectively (Note 1)	450	3,997
INVESTMENTS IN AND ADVANCES TO AFFILIATES	13,472	740
Total assets	$1,101,332	$1,732,547

The accompanying notes to financial statements are an integral part of these statements.

MOBILE TELESYSTEMS

Consolidated Balance Sheets
at December 31, 2000 and 2001
(Amounts in thousands of U.S. dollars, except share amounts)

	December 31 2000	December 31 2001
CURRENT LIABILITIES:		
Accounts payable, related parties (Note 22)	$ 5,797	$ 6,142
Trade accounts payable	37,860	106,068
Deferred connection fees (Note 14)	14,923	21,419
Subscriber prepayments and deposits	44,610	63,741
Debt, current portion (Note 15)	24,000	18,245
Promissory notes payable, current portion (Note 17)	—	580
Capital lease obligation, current portion (Notes 16 and 22)	—	14,401
Income tax payable	15,082	23,078
Accrued liabilities (Note 18)	38,175	51,626
Other payables	2,316	3,357
Total current liabilities	182,762	308,657
LONG-TERM LIABILITIES:		
Notes payable, net of discount (Note 15)	—	248,976
Debt, net of current portion (Note 15)	23,305	30,150
Capital lease obligation, net of current portion (Notes 16 and 22)	—	7,696
Promissory notes payable, net of current portion (Note 17)	5,468	5,792
Deferred connection fees, net of current portion (Note 14)	16,630	26,269
Deferred taxes (Note 19)	72,083	72,192
Total long-term liabilities	117,486	391,075
Total liabilities	300,248	699,732
COMMITMENTS AND CONTINGENCIES	—	—
MINORITY INTEREST	—	12,999
SHAREHOLDERS' EQUITY:		
Common stock: (2,096,975,792 shares with a par value of 0.1 rubles authorized and 1,993,326,138 shares issued as of September 30, 2001 and December 31, 2000, 345,244,080 of which are in the form of ADS (Note 1))	50,558	50,558
Treasury stock (9,966,631 common shares at cost) (Note 21)	(10,206)	(10,206)
Additional paid-in capital	552,030	555,794
Shareholder receivable	(49,519)	(38,958)
Retained earnings	258,221	462,628
Total shareholders' equity	801,084	1,019,816
Total liabilities and shareholders' equity	$1,101,332	$1,732,547

The accompanying notes to financial statements are an integral part of these statements.

MOBILE TELESYSTEMS

Consolidated Statements of Shareholders' Equity for the Years Ended December 31, 1999, 2000 and 2001 (Amounts in thousands of U.S. dollars, except share amounts)

	Common Stock		Treasury Stock		Additional Paid-in Capital	Shareholder Receivable	Retained Earnings	Total
	Shares	Amount	Shares	Amount				
BALANCES,								
December 31, 1999	1,634,527,440	$49,276	—	—	$182,975	$ (70,331)	$181,804	$ 343,724
Receivable from Sistema:								
Increases for interest	—	—	—	—	6,268	(6,268)	—	—
Payments from Sistema	—	—	—	—	—	27,080	—	27,080
Issuance of common shares, net of direct expenses (Note 1)	345,244,080	1,233	—	—	347,320	—	—	348,553
Purchase of treasury stock under the stock bonus plan and stock option plan (Note 21)	13,554,618	49	(13,554,618)	(13,880)	13,831	—	—	—
Exercise of stock bonus plan (Note 21)			3,587,987	3,674	(3,661)	—	—	13
Non-cash expense associated with issuance of stock bonus to employees	—	—	—	—	5,297	—	—	5,297
Net income	—	—	—	—	—	—	90,048	90,048
Dividends declared	—	—	—	—	—	—	(13,631)	(13,631)
BALANCES,								
December 31, 2000	1,993,326,138	50,558	(9,966,631)	(10,206)	552,030	(49,519)	258,221	801,084
Receivable from Sistema:								
Increases for interest	—	—	—	—	3,764	(3,764)	—	—
Payments from Sistema	—	—	—	—	—	14,325	—	14,325
Net income	—	—	—	—	—	—	207,366	207,366
Dividends declared	—	—	—	—	—	—	(2,959)	(2,959)
BALANCES,								
December 31, 2001	1,993,366,138	$50,558	(9,966,631)	$(10,206)	$555,794	$ (38,958)	$462,628	$1,019,816

The accompanying notes to financial statements are an integral part of these statements.

MOBILE TELESYSTEMS

Consolidated Statements of Operations
for the Years Ended December 31, 1999, 2000 and 2001
(Amounts in thousands of U.S. dollars, except share and per share amounts)

	December 31		
	1999	2000	2001
NET REVENUES:			
Service revenues	$ 314,568	$ 484,469	$ 830,308
Connection fees	12,755	14,885	21,066
Equipment sales	31,004	36,358	41,873
	358,327	535,712	893,247
COST OF SERVICES AND PRODUCTS (including related party amounts of $17,219, $20,040 and $30,537, respectively):			
Interconnection and line rental	38,958	41,915	75,278
Roaming expenses	21,725	41,178	68,387
Cost of equipment	29,932	39,217	39,828
	90,615	122,310	183,493
OPERATING EXPENSES (including related party amounts of $9,670, $5,064 and $8,882, respectively and expenses associated with management stock bonus plan of $nil, $5,297 and $nil, respectively) (Note 21 and 23):	74,612	110,242	134,598
SALES AND MARKETING EXPENSES (including related party amounts of $930, $6,400 and $8,707, respectively):	23,722	76,429	107,729
DEPRECIATION AND AMORTIZATION	53,766	87,684	133,143
Net operating income	115,612	139,047	334,284
CURRENCY EXCHANGE AND TRANSLATION LOSSES	3,238	1,066	1,871
OTHER EXPENSES (INCOME) (including related party amounts of $nil, $952 and $2,978, respectively, (Note 22)):			
Interest income (Note 8)	(801)	(7,626)	(11,829)
Interest expenses, net of amounts capitalized	11,805	11,335	6,944
Impairment of investments and other	(829)	(502)	10,108
Total other expenses, net	10,175	3,207	5,223
Income before provision for income taxes and minority interest	102,199	134,774	327,190
PROVISION FOR INCOME TAXES (Note 19)	18,829	51,154	97,414
MINORITY INTEREST	(2,291)	(6,428)	6,614
NET INCOME before cumulative effect of a change in accounting principle and extraordinary gain	85,661	90,048	223,162
Cumulative effect of a change in accounting principle, net of income taxes of $9,644 (Note 4)	—	—	(17,909)
Extraordinary gain on debt repayment, net of income taxes of $667 (Note 15)	—	—	2,113
NET INCOME	$ 85,661	$ 90,048	$ 207,366
Weighted average number of shares outstanding	1,634,527,440	1,806,968,096	1,983,359,507
Earnings per share (basic and diluted):			
Net income before cumulative effect of a change in accounting principle and extraordinary gain	$ 0.052	$ 0.050	$ 0.113
Cumulative effect of a change in accounting principle	—	—	(0.009)
Extraordinary gain on debt repayment	—	—	0.001
Net income	$ 0.052	$ 0.050	$ 0.105

The accompanying notes to financial statements are an integral part of these statements.

MOBILE TELESYSTEMS

Consolidated Statements of Cash Flows
for the Years Ended December 31, 1999, 2000 and 2001
(Amounts in thousands of U.S. dollars, except share amounts)

	1999	2000	2001
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net income after cumulative effect on prior years (to December 31, 2000) of a change in accounting principle	$ 85,661	$ 90,048	$207,366
Adjustments to reconcile net income to net cash provided by operating activities:			
Minority interest	(2,291)	(6,428)	6,614
Depreciation and amortization	53,766	87,684	133,143
Amortization of deferred connection fees	(12,755)	(14,867)	(20,027)
Deferred subscriber acquisition cost	(23,674)	(49,232)	(30,978)
Amortization of deferred subscriber acquisition costs	12,285	53,604	30,978
Cumulative effect of a change in accounting principle	—	—	17,909
Gain on debt extinguishment	—	—	(2,113)
Provision for obsolete inventory	590	2,114	2,543
Provision for doubtful accounts	8,006	2,403	3,219
Provision for other assets	379	—	—
Loan interest accrued	11,809	11,335	5,845
Loan interest paid	(11,431)	(17,850)	(4,068)
Deferred taxes	(17,594)	(932)	(49,742)
Non-cash expenses associated with stock bonus plan	—	5,297	—
Impairment of investments	—	—	10,000
Changes in operating assets and liabilities:			
Decrease/(Increase) in trade receivables	3,435	6,730	(7,181)
Decrease/(Increase) in accounts receivable, related parties	(5,245)	4,223	(3,091)
Increase in inventory	(8,074)	(8,922)	(4,129)
Increase in prepaid expenses	(267)	(1,680)	(8,552)
Increase in VAT receivable	(2,944)	(6,033)	(59,618)
(Increase)/Decrease in other current assets	2,818	(7,363)	1,613
Increase/(Decrease) in accounts payable, related parties	(11,921)	743	1,049
(Decrease)/Increase in trade accounts payable	29,143	(29,801)	20,470
Increase in subscriber prepayments and deposits and deferred connection fees	7,901	43,382	19,424
Increase/(Decrease) in income tax payable	(7,401)	19,787	49,980
Increase in accrued liabilities and other payables	4,605	6,672	17,547
Net cash provided by operating activities	116,801	190,914	338,201
CASH FLOWS FROM INVESTING ACTIVITIES:			
Purchase of UDN-900, net of cash acquired	(180)	—	—
Purchase of ACC, net of cash acquired	(83)	—	—
Purchase of Telecom XXI, net of cash acquired	—	—	(49,680)
Purchase of Telecom 900, net of cash acquired	—	—	(25,665)
Purchase of ReCom, net of cash acquired	—	—	(199)
Purchase of Novitel, net of cash acquired	—	—	13
Purchase of 20% interest in Rosico	—	(16,085)	—
Purchase of 32.5% interest in MSS	—	—	(327)
Purchase of property, plant and equipment	(109,012)	(194,983)	(396,667)
Purchase of intangible assets	(9,326)	(29,915)	(44,533)
Purchases of short term investments	—	(170,000)	(110,000)
Proceeds from sale of short term investments	—	—	195,602
Other non-current assets realized	2,313	—	—
Decrease/(Increase) in investments in and advances to affiliates	1,104	(12,366)	(10,067)
Net cash used in investing activities	(115,184)	(423,349)	(441,523)
CASH FLOWS FROM FINANCING ACTIVITIES:			
Proceeds from issuance of capital stock, net of direct expenses	—	348,553	—
Proceeds from issuance of notes, net of underwriter discount	—	—	248,135
Notes issuance cost	—	—	(3,856)
Capital lease obligation principal paid	—	—	(7,947)
Dividends paid	(11,224)	(14,425)	(2,959)
Proceeds from short-term debt	18,000	—	13,577
Loan principal paid	(18,333)	(62,665)	(13,683)
Payments from Sistema	—	27,080	14,325
Net cash provided by (used in) financing activities	(11,557)	298,543	247,592
Effect of exchange rate changes on cash and cash equivalents	(944)	(280)	(469)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS:	(10,884)	65,828	143,801
CASH AND CASH EQUIVALENTS, at beginning of year	20,884	10,000	75,828
CASH AND CASH EQUIVALENTS, at end of year	$ 10,000	$ 75,828	$219,629
SUPPLEMENTAL INFORMATION:			
Income taxes paid	$ 59,484	$ 35,052	$129,418

The accompanying notes to financial statements are an integral part of these statements.

Notes to Consolidated Financial Statements
(Amounts in thousands of U.S. dollars, unless otherwise stated)

1. General

Business of the Company

MTS was created in October 1993 to design, construct and operate a cellular telecommunications network in Moscow and the Moscow region. Over the recent years the Company has expanded in 44 other regions of Russia.

MTS was originally registered on October 28, 1993 as a closed joint stock company, and began commercial operations in the middle of 1994.

In November 1993, MTS was granted a 900 MHz or GSM-900 cellular license for operation in Moscow and the Moscow region. The license gave MTS the exclusive right to operate on the GSM-900 standard for 10 years from the commencement of operations. In June 1998, MTS was granted a new license, which gave MTS the right to operate on the GSM standard up to December 2004, however exclusive operating rights were no longer guaranteed.

In 1997, MTS was granted GSM-900 cellular licenses for operations in the Tver region as well as the Kostroma region and the Komi Republic (See Note 25 Operating Licenses).

In 1998, MTS acquired controlling stakes in Rosico (80%) and RTC (100%), both Russian joint stock companies, which hold licenses to operate, respectively, GSM-1800 and GSM-900 cellular networks in Moscow, certain areas in Central and Northern Russia, the Urals and Western Siberia and GSM-900 cellular networks in certain regions in Central Russia. During 2000, MTS purchased the remaining 20% of Rosico stock.

In 1998 MTS acquired 49.9% of ReCom, a Russian joint stock company. In April 2001, MTS acquired an additional 4% of the outstanding common stock of ReCom from a third party increasing its share in ReCom to 53.9%. ReCom holds GSM-900 licenses for operations in Voronezh, Belgorod, Bryansk, Kursk, Lipetsk, and Orel regions of Russia (Note 6 Businesses Acquired).

In 1999, MTS acquired 51% of Udmurt Digital Network (UDN-900), a Russian closed joint stock company, which is licensed to operate a GSM-900 cellular network in the Udmurt region, and 100% of Amur Cellular Communications (ACC), a Russian closed joint stock company, which is licensed to operate a GSM-900 cellular network in the Amursk region.

In March 2000, MTS acquired a 51% interest in Mobilnye Sistemy Svyazi OJSC, or MSS, a Russian open joint-stock company. In 2001, MTS purchased an additional 32.5% of MSS stock for approximately $327, increasing its share in MSS up to 83.5% as of December 31, 2001. MSS has License No. 5544 to operate a GSM-900 network in the Omsk region of Russia.

In May 2001, MTS acquired 100% of the outstanding common stock of Telecom XXI, a Russian closed joint stock company, for $49,742. Telecom XXI holds GSM-900/1800 licenses for operations in St. Petersburg and in the following nine Northwestern regions of Russia: Karelia Republic, Nenetsky autonomous district, Leningrad, Arkhangelsk, Vologda, Kaliningrad, Murmansk, Novgorod and Pskov regions (Note 6 Business Acquired).

In August 2001, MTS acquired 81% of the outstanding common stock of Telecom-900, a Russian closed joint-stock company, for $27,630. Telecom-900 is a company holding controlling interests in three Russian regional companies, namely Uraltel (Ekaterinburg) (53.175%), SCS-900 (Novosibirsk) (51%) and FECS-900 (Khabarovsk) (60%) (''the Telecom 900 Group''), which hold GSM licenses for operation in Altai republic, Ekaterinburg, Sverdlovsk, Novosibirsk and Khabarovsk regions of Russia (see also Notes 6 Business Acquired, 11 Property, Plant and Equipment and 16 Capital lease obligations).

On October 22, 2001 MTS acquired 51% of the outstanding common stock of Novitel, Russian closed joint-stock company, for the total amount of $1,426. Novitel is a dealer of mobile phones and accessories in Moscow.

(Amounts in thousands of U.S. dollars, unless otherwise stated)

Reorganization

In March 2000, closed joint stock company Mobile TeleSystems was merged with RTC, MTS' wholly owned subsidiary, to create the open joint stock company Mobile TeleSystems. This corporate merger has been accounted for at historical cost in a manner similar to that in pooling of interest accounting because the merged companies were entities under common control.

The accompanying financial statements represent those of open joint stock company Mobile TeleSystems and its legal predecessor, closed joint stock company Mobile TeleSystems. Shares, earnings per share and other per share information have been restated in the accompanying financial statements to give retroactive effect to the capital structure of open joint stock company Mobile TeleSystems.

Initial Public Offering

In July 2000, the Company issued additional shares in an initial public offering on the New York Stock Exchange. The Company's shares are traded in the form of American Depositary Shares (ADS). Each ADS represents 20 shares of common stock of the Company. The Company issued a total of 17,262,204 ADS, representing 345,244,080 common shares in the offering. Proceeds from the offering, net of underwriting discount, were $353 million (see also Note 21 Management Stock Bonus and Stock Option Plans).

Issuance of Notes

On December 21, 2001 Mobile TeleSystems Finance S.A. (''MTS Finance''), a 100% beneficially owned subsidiary of MTS registered under the laws of Luxembourg, issued $250 million 10.95% notes at a price of 99.254%. These notes are guaranteed by MTS and mature on December 21, 2004. MTS Finance will make interest payments on the notes semi-annually in arrears on June 21 and December 21 of each year, commencing on June 21, 2002. The notes are listed on the Luxembourg Stock Exchange. Proceeds received from the notes, net of underwriting discount, were $248 million. Related debt issuance costs in the amount of $3,856 were capitalized.

Ownership

As of December 31, 2000 and 2001, MTS' shareholders of record and their respective percentage direct interests were as follows:

Joint Stock Financial Corporation ''Sistema'' (''Sistema'')	34.8%
DeTeMobil GmbH (''DeTeMobil'')	36.2%
Vast, Limited Liability Company (''Vast'')	3.0%
Invest-Svyaz-Holding, Closed Joint Stock Company	8.0%
ADS Holders	18.0%
	100.0%

2. Russian Environment

General

Over the past decade Russia has undergone substantial political, economic and social changes. As an emerging market, Russia does not possess a fully developed business and regulatory infrastructure that would generally exist in a more mature market economy. The current Government is attempting to address these issues; however, it has not yet fully implemented the reforms necessary to create banking, judicial and regulatory systems that usually exist in more developed markets. As a result, and as reflected in the Government's debt default and Ruble devaluation in 1998, operations in Russia involve risks that are not typically associated with those in developed markets. Such risks persist in the current environment with results that include but are not limited to, a currency that is not freely convertible outside of the country, various currency controls, low liquidity levels for debt and equity markets, and continuing inflation.

(Amounts in thousands of U.S. dollars, unless otherwise stated)

Currency Exchange and Control

Foreign currencies, in particular the US Dollar, play a significant role in the underlying economics of many business transactions in Russia. Following the 1998 economic crisis, the Ruble's value fell significantly against the US Dollar, falling from a pre-crisis rate of approximately 6 Rubles to 1 US Dollar, to 27 Rubles to 1 US Dollar by the end of 1999. During 2000 and 2001, the Ruble's value fluctuated between 26.9 and 30.3 to 1 US Dollar. As of April 18, 2002, the exchange rate was 31.15 Rubles to 1 US Dollar.

The Central Bank of Russia has established strict currency control regulations designed to promote the commercial utilization of the Ruble. Such regulations place restrictions on the conversion of Rubles into foreign currencies and establish requirements for conversion of foreign currency sales to Rubles.

MTS's principal currency exchange rate risk arises from the fact that the majority of cash outflows as well as debt and accounts payable balances are either denominated in or tightly linked to the U.S. dollar. As a result, devaluation of the ruble against the U.S. dollar can adversely affect the Company by increasing its costs in ruble terms. In order to manage against this risk, the Company links its tariffs, which are payable in rubles, to the U.S. dollar. The effectiveness of this risk management policy is limited, however, as the Company cannot always increase its tariffs in line with ruble devaluation due to competitive pressures, leading to a loss of revenue in U.S. dollar terms. The devaluation of the ruble also results in losses in the value of ruble-denominated assets, such as ruble deposits. These losses, which are included in currency exchange and translation losses in the accompanying consolidated statements of operations, were approximately $3.2 million in 1999, approximately $1.1 million in 2000 and $1.9 million in 2001. Continued devaluation of the ruble against the U.S. dollar may have a significant negative effect on the Company's financial position and results of its operations.

Inflation

The Russian economy has been characterized by relatively high rates of inflation. The following table summarizes the annual rate of inflation for the past three years:

	Annual Inflation
2001	18.6%
2000	20.2%
1999	36.5%

The Company's principal inflation rate risk arises in connection with probable decrease of sales resulting from decrease of customers' demand, as the Company's services may become expensive and exclusive. As substantially all of the Company' costs are denominated in U.S. dollars or are tightly linked to the U.S. dollar, when the rate of inflation exceeds the rate of devaluation of the ruble against the U.S. dollar, as was the case for years prior to 1998 and in 1999, the Company can experience inflation-driven increases in dollar terms of certain of its costs. These include salaries and rents, which are sensitive to rises in the general price level in Russia. In this situation, due to competitive pressures, the Company may not be able to raise its tariffs sufficiently to preserve operating margins. Accordingly, high rates of inflation relative to the rate of devaluation could increase the Company's costs and decrease the Company's operating margins.

Management is unable to estimate what developments may occur or the resulting effect of any such developments on MTS' financial condition or future results of operations. MTS will continue to be affected, for the foreseeable future, by the country's unstable economy. The financial statements do not include any adjustment that may result from these uncertainties.

Impairment of long-lived assets

As a result of significant devaluation of the ruble described above, MTS has reassessed the recoverability of its investments in long-lived assets, including property, plant and equipment and intangible assets. MTS' accounting policies require an impairment loss to be recognized whenever a review demonstrates that the book value of a long-lived asset is not recoverable in terms of net undiscounted future cash flows.

Management has considered several factors in its analysis, including the following:

- the continued use of each significant segment of its existing network,
- investment needed to build up MTS' network in accordance with current operating plans,
- the development of license areas acquired, in particular in relation to value allocated to licenses of Rosico (See Note 4), and
- management's assessment of the current economic situation.

Based on these factors management has determined that no impairment has occurred in relation to its investment in long-lived assets during the year ended December 31, 2001. However, management believes that it is reasonably possible that its carrying value for Rosico licenses could be significantly affected by the volatility of the Russian economy. Assuming that the Russian economic situation deteriorates over the next few years, the possible impact could be material to MTS' financial position and results of operations.

Taxation

Russia currently has a number of laws related to various taxes imposed by both federal and regional governmental authorities. Applicable taxes include value added tax, corporate income tax (profits tax), a number of turnover-based taxes, and payroll (social) taxes, together with others. Laws related to these taxes have not been in force for significant periods, in contrast to more developed market economies; therefore, the government's implementation of these regulations is often inconsistent or nonexistent. Accordingly, few precedents with regard to tax rulings have been established. Tax declarations, together with other legal compliance areas (as examples, customs and currency control matters), are subject to review and investigation by a number of authorities, who are enabled by law to impose extremely severe fines, penalties and interest charges. These facts create tax risks in Russia substantially more significant than typically found in countries with more developed tax systems.

In recent years, the Russian government has initiated revisions of the Russian tax system. Effective January 1, 1999, the first part of the Tax Code was enacted. Effective January 1, 2001, the second part of the Tax Code was enacted. The new tax system is generally intended to reduce the number of taxes and, thus, the overall tax burden on businesses, and to simplify the tax laws.

Generally, tax declarations remain open and subject to inspection for a period of three years following the tax year. While most of MTS' tax declarations have been inspected without significant penalties, these inspections do not eliminate the possibility of re-inspection. Accordingly, as of December 31, 2001, substantially all of the tax declarations of MTS for the preceding three years are open to further review.

Management believes that it has adequately provided for tax liabilities in the accompanying consolidated financial statements; however, the risk remains that relevant authorities could take differing positions with regard to interpretive issues and the effect could be significant.

3. Summary of Significant Accounting Policies

Accounting Principles

MTS maintains its accounting books and records in Russian rubles based on Russian accounting regulations. The accompanying consolidated financial statements have been prepared in order to present MTS' financial position and its results of operations and cash flows in accordance with accounting principles generally accepted in the United States (U.S. GAAP) and expressed in terms of U.S. dollars.

Basis of Presentation

The accompanying consolidated financial statements include the accounts of MTS and its subsidiaries in which MTS has a direct controlling interest. All significant intercompany balances and transactions have been eliminated.

(Amounts in thousands of U.S. dollars, unless otherwise stated)

As of December 31, 2000 and 2001, MTS has investments in the following legal entities:

	Accounting Method	December 31 2000	December 31 2001
Rosico	Consolidated	100.0%	100.0%
ReCom	Equity/Consolidated	49.9%	53.9%
MTS-Komi Republic (MTS-RK)	Equity	26.0%	26.0%
MTS-Kostroma	Equity	26.0%	26.0%
MTS-Tver (MTS-T)	Equity	26.0%	26.0%
UDN-900	Consolidated	51.0%	51.0%
ACC	Consolidated	100.0%	100.0%
MSS	Consolidated	51.0%	83.5%
MTS-NN	Consolidated	—	65.0%
Telecom XXI	Consolidated	—	100.0%
Telecom-900	Consolidated	—	81.0%
Novitel	Consolidated	—	51%
MTS Finance(1)	Consolidated	—	100%

(1) Represents beneficial ownership.

In 2001, minority interest reflects minority shareholders' interests in ReCom, in Telecom-900, in UDN-900 and in Novitel. During 2001, no loss has been allocated to the minority shareholders of as the balance in the minority interests account has been reduced to nil.

Translation methodology

Translation (remeasurement) of MTS' ruble denominated financial statements into U.S. dollars has been performed in accordance with the provisions of SFAS No. 52 ''Foreign currency translation'', as they relate to hyperinflationary economies. The objective of this remeasurement process is to produce the same results that would have been reported if the U.S. dollar had been the functional currency.

Monetary assets and liabilities have been translated at the period-end exchange rate. Non-monetary assets and liabilities have been translated at historical rates. Capital contributions at the time of Company formation have been translated at the official rate of 1.01 rubles to 1 U.S. dollar as stated in the MTS Foundation Agreement. Capital contributions at later dates have been recorded at the historical translation rate on the date of the investment. Revenues, expenses and cash flows have been translated at historical rates. Translation differences resulting from the use of these rates have been accounted for as currency translation gains and losses in the accompanying consolidated statements of operations.

Management estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and cash equivalents

Cash represents cash on hand and in MTS' bank accounts and short-term investments having original maturities of, or termination clauses for, less than three months.

Short term investments

Short-term investments represent investments in time deposits, which have original maturities in excess of three months but less than twelve months. These investments are being accounted for at cost.

Allowance for doubtful accounts

MTS provides an allowance for doubtful accounts based on management's periodic review of accounts, including the delinquency of account balances.

Prepaid expenses

Prepaid expenses are primarily comprised of advance payments made for inventory and services to vendors.

Inventory

Inventory, accounted for at lower of cost, on a FIFO basis, or market consists of telephones, accessories and spare parts for equipment.

Obsolescence reserves are provided based on specific monthly review of significant inventoried items and expensed as cost of services and products.

Value-added taxes

Value-added taxes related to sales are payable to the tax authorities on an accrual basis based upon invoices issued to the subscriber. VAT incurred for purchases may be reclaimed, subject to certain restrictions, against VAT related to sales.

VAT related to purchase transactions that are not currently reclaimable as of the balance sheet dates are recognized in the balance sheets on a gross basis.

Property, plant and equipment

Property, plant and equipment with a useful life of more than one year is capitalized at historical cost and depreciated on a straight-line basis over their expected useful lives as follows:

Network and base station equipment	5 - 8 years
Leasehold improvements	shorter of 10 years or lease term
Office equipment, computers and software	5 years
Buildings	50 years
Vehicles	4 years

Construction in progress and equipment held for installation are not depreciated until the constructed or installed asset is ready for its intended use.

Maintenance and repair costs are expensed as incurred; while upgrades and improvements are capitalized. MTS capitalizes interest costs with respect to qualifying construction projects.

Other intangible assets

Intangible assets represent various purchased software costs (including the billing system), deferred telephone numbering capacity, and rights to use premises. A significant portion of the rights to use premises were contributed by shareholders to MTS' charter capital. Deferred telephone numbering capacity costs are being amortized over five to ten years and the rights to use premises are being amortized over ten years. Amortization of deferred numbering capacity costs started immediately upon the purchase of numbering capacity. The billing system and other software costs are amortized over four years. Other intangible assets are being amortized over three to four years. All intangible assets are being amortized using the straight-line method.

License costs

License costs are capitalized as a result of (a) purchase price allocated to licenses acquired in business combinations (See Note 6) and (b) licenses granted directly from government organizations which require license payments.

License costs are amortized, subject to periodic review for impairment, on the straight-line method over the term of the license commencing from the date such license area becomes commercially operational.

Goodwill

Goodwill represents the purchase price for businesses acquired in excess of the fair value of net assets identified, primarily related to MTS' acquisition of Rosico. Goodwill is amortized on a straight-line basis over seven years. Amortization expense during each of the years ended December 31, 1999, 2000 and 2001 amounted to $6.1 million.

Leasing arrangements

The Company accounts for leases based on the requirements of Statement of Financial Accounting Standards No. 13, ''Accounting for Leases''. The Telecom 900 Group leases operating facilities, which include switches, base stations and other cellular network equipment as well as the billing system. All these leases were classified as capital leases.

The present value of future minimum lease payments at the inception of the lease is reflected as a liability in the balance sheet. Amounts due within one year are classified as short term liabilities and the remaining balance as long-term liabilities. The interest rate implicit in the leases varies from to 4% to 54%.

Subscriber acquisition costs

Subscriber acquisition costs represent the direct costs paid for each new subscriber enrolled through MTS's independent dealers. Prior to 2001, these costs were capitalized to the extent of any revenues that had been deferred from the acquisition of a subscriber, such as connection fees charged to a subscriber to initiate call service, and amortized as a component of sales and marketing expense on a straight-line basis over the estimated average subscriber life. Effective 2001, MTS changed its accounting policy and now expenses subscriber acquisition costs as incurred. The change was made to facilitate the comparison of MTS's results with other telecommunication companies (See also Note 4 Accounting Changes).

Investments

Beginning in 1998, MTS has acquired interests in several Russian legal entities, engaged in telecommunications activity. Investments in entities where MTS holds 20 to 50% and can exercise significant influence but not control are accounted for under the equity method. All investments are made in companies that are not traded in open markets. Management periodically assesses realizability of the carrying values of the investments and if necessary records impairment losses to write the investment down to fair value.

Debt issuance costs

Debt issuance costs are amortized using the effective interest method over the terms of the related loans.

Impairment of long-lived assets

MTS periodically evaluates the recoverability of the carrying amount of its long-lived assets in accordance with SFAS 121, *Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be disposed of*. Whenever events or changes in circumstances indicate that the carrying amounts of those assets may not be recoverable, MTS will compare undiscounted net cash flows estimated to be generated by those assets to the carrying amount of those assets. When these undiscounted cash flows are less than the carrying amounts of the assets, MTS will record impairment losses to write the asset down to fair value, measured by the discounted estimated net future cash flows expected to generated from the assets. During the years ended December 31, 1999, 2000 and 2001, management believes that no such impairments have occurred.

Subscriber prepayments

In 1998, MTS initiated a program whereby subscribers were required to pay in advance for telecommunications services. All amounts received in advance of service provided are recorded as a subscriber prepayment liability and are not recorded to revenues until the related services have been provided to the subscriber.

Revenue recognition

Revenues are recognized on an accrual basis, i.e. when the goods and services are actually provided regardless of when the resulting monetary or financial flow occurs.

MTS categorizes the revenue sources in the statements of operations as follows:

1. Service revenues: (a) subscription fees, (b) usage charge, (c) value added service fees, (d) roaming fees charged to other operators for guest roamers utilizing MTS' network and (e) prepaid phone cards

2. Connection fees.

3. Equipment sales: (a) sales of handsets as part of contracts and (b) sales of accessories.

Subscription fees

MTS recognizes revenues related to the monthly network fees in the month that the wireless service is provided to the subscriber.

Usage charges and Value added services fees

Call fees consist of fees based on airtime used by the caller, the destination of the call and the service utilized.

Fees are based on usage of airtime or volume of data transmitted for value added services, such as short message services, Internet usage and data services. MTS recognizes revenues related to usage charges and value added services in the period when services were rendered.

Pre-paid phone cards

MTS also sells to subscribers pre-paid phone cards, separately from the handset. These cards allow subscribers to make a predetermined allotment of wireless phone calls and/or take advantage of other services offered by the Company, such as short messages and sending or receiving faxes.

At the time that the pre-paid phone card is purchased, MTS records the receipt of cash as subscriber deposit. The Company recognizes revenues from the phone cards in the period when subscriber uses time under the phone card. Unused time on sold phone cards is not recognized as revenues until the related services have been provided to the subscriber or the prepaid phone card has expired.

Roaming fees

MTS charges roaming per-minutes fees to other wireless operators for guest roamers utilizing MTS' network. Guest roaming fees were $44,048, $43,214 and $52,639 for the years ended December 31, 1999, 2000 and 2001, respectively.

Connection fees

MTS defers initial connection fees from the moment of initial signing of the contract with subscribers over the estimated average subscriber life. The Company estimates that the average expected term of the subscriber relationship is three years and one quarter (see also Note 14 Deferred Connection Fees).

Equipment sales

MTS sells handsets and accessories to customers who are entering into contracts for service and as separate distinct transactions. The Company recognizes revenues from the handsets and accessories upon the delivery to the customer or upon the initial signing of the contract. These contracts do not require the customer to maintain future service with MTS. MTS records estimated returns as a direct reduction of sales at the time the related sales are recorded.

Expense recognition

Expenses incurred by MTS in relation to the provision of wireless communication services relate to interconnection and line rental costs, roaming expenses, costs of handsets and other accessories sold, depreciation and maintenance of the network.

Calls made by subscribers from areas outside of territories are subject to roaming fees charged by the wireless provider in those territories. These roaming charges are recorded as air time revenues on a gross basis, with the related roaming charges being recorded as operating expense, as MTS acts as the principal in the transaction with the subscriber and bears the risk of non-collection from the subscriber.

The costs of the handset, whether sold to subscribers through the distribution channel or as part of the contract, are expensed as cost of equipment at the initial signing of the contract. Any discounts provided on the direct sale of the handset and any fees paid to dealer commissions are recorded as a component of sales and marketing expenses.

Taxation

Deferred tax assets and liabilities are recognized for the expected future tax consequences of existing differences between financial reporting and tax reporting bases of assets and liabilities, and loss or tax credit carry forwards using enacted tax rates expected to be in effect at the time these differences are realized. Valuation allowances are recorded for deferred tax assets for which it is more likely that these assets will not be realized.

Advertising costs

Advertising costs are expensed as incurred. Advertising costs for the years ended December 31, 1999, 2000 and 2001 were $11,437, $22,218 and $42,715, respectively, and are reflected as a component of sales and marketing expenses in the accompanying consolidated statement of operations.

Earnings per share

Earnings per share have been determined using the weighted average number of shares outstanding during the year. Basic and diluted earnings per share are equivalent as all potentially dilutive securities have an exercise price less than the average stock price during the period. There are 1,856,692 stock options outstanding as of December 31, 2001. Earnings and other per share information have been restated to give retroactive effect to the merger of MTS and RTC in 2000 (See Note 1 General).

Fair value of financial instruments

The fair market value of financial instruments, consisting of cash and cash equivalents, current receivables, and accounts payable, which are included in current assets and liabilities, approximates the carrying value of these items due to the short term nature of these amounts. Based on the on borrowing rates currently available to the Company for debt with similar terms and average maturities of the outstanding debt at December 31, 2000 and 2001, the fair value of long term debt was equivalent to fair value. The fair value of variable rate debt and promissory notes is equivalent to their carrying value.

It is not practical to determine the fair value of MTS's receivable from Sistema and advances to affiliates, due to the current instability in the Russian economy and its effect on interest rates appropriate for determining fair value.

Comprehensive income

Comprehensive income is defined as net income plus all other changes in net assets from non-owner sources. For the years ended December 31, 1999, 2000 and 2001, comprehensive income equaled net income.

Comparative information

Certain prior year amounts and disclosures have been reclassified to conform to the 2001 presentation.

Segment reporting

SFAS No. 131 requires that a business enterprise report financial and descriptive information about its reportable operating segments. MTS currently manages its business as one operating segment, and accordingly, does not report segment information. Furthermore, all of MTS' long-lived assets and revenues are derived in Russia.

Recently Adopted Accounting Pronouncements

In June 1998, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (''SFAS'') 133, *Accounting for derivative instruments and hedging activities*. SFAS 133 establishes accounting and reporting standards requiring that every derivative instrument (including certain derivative instruments embedded in other contracts) be recorded on the balance sheet as either an asset or liability measured at its fair value. The statement requires that changes in the derivative's fair value be recognized currently in earnings unless specific accounting criteria are met. If a derivative instrument qualifies for hedge accounting, the gains or losses from the derivative may offset results from the hedged item in the statement of operations or other comprehensive income, depending on the type of hedge. To adopt hedge accounting, a company must formally document, designate and assess the effectiveness of transactions that receive hedge accounting.

In June 2000 Financial Accounting Standards Board issued SFAS 138, *Accounting for Certain Derivative Instruments and Certain Hedging Activities, an amendment of FASB Statement No. 133*. This Statement amends the accounting and reporting standards of Statement 133 for certain derivative instruments and certain hedging activities. SFAS 137 delayed the effective date of SFAS 133 to fiscal years beginning after June 15, 2000.

MTS adopted SFAS 133 effective January 1, 2001. SFAS 133 and SFAS 138 have not had a material effect on MTS' consolidated balance sheet or its results of operations.

New Accounting Pronouncements

In July 2001, the Financial Accounting Standards Board (''FASB'') issued Statement of Financial Accounting Standards (''SFAS'') No. 141, Business Combinations and SFAS No. 142, Goodwill and Other Intangible Assets. SFAS No. 141 requires the use of the purchase method of accounting for all business combinations initiated after June 30, 2001. SFAS No. 141 requires intangible assets to be recognized if they arise from contractual or legal rights or are ''separable'', i.e., it is feasible that they may be sold, transferred, licensed, rented, exchanged or pledged. As a result, it is likely that more intangible assets will be recognized under SFAS No. 141 than its predecessor, APB Opinion No. 16 although in some instances previously recognized intangibles will be subsumed into goodwill.

Under SFAS No. 142, goodwill will no longer be amortized on a straight-line basis over its estimated useful life, but will be tested for impairment on an annual basis and whenever indicators of impairment arise.

Had SFAS No. 142 been applied since January 1, 2000, we would not have recognized expenses related to amortization of goodwill of $6.1 million for the year ended December 31, 2001. The goodwill impairment test, which is based on fair value, is to be performed on a reporting unit level. A reporting unit is defined as a SFAS No. 131 operating segment or one level lower. Goodwill will no longer be allocated to other long-lived assets for impairment testing under SFAS No. 121, Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed of. Additionally, goodwill on equity method investments will no longer be amortized; however, it will continue to be tested for impairment in accordance with Accounting Principles Board Opinion No. 18, The Equity Method of Accounting for Investments in Common Stock. Under SFAS No. 142 intangible assets with indefinite lives will not be amortized. Instead they will be carried at the lower cost or market value and tested for impairment at least annually. All other recognized intangible assets will continue to be amortized over their estimated useful lives.

SFAS No. 142 is effective for fiscal years beginning after December 15, 2001 although goodwill on business combinations consummated after July 1, 2001 will not be amortized. On adoption, the Company may need to record a cumulative effect adjustment to reflect the impairment of previously recognized intangible assets. In addition, goodwill on prior business combinations will cease to be amortized. The Company has not determined the impact that these Statements will have on intangible assets or whether a cumulative effect adjustment will be required upon adoption.

In August 2001, FASB issued SFAS No. 143, ''Accounting for Asset Retirement Obligations''. SFAS No. 143 requires that the fair value of a liability for an asset retirement obligation be recognized in the period in which it is incurred if a reasonable estimate of fair value can be made. The associated asset retirement costs are capitalized as part of the carrying amount of the long-lived asset. An entity shall measure changes in the liability for an asset retirement obligation due to passage of time by applying an interest method of allocation to the amount of the liability at the beginning of the period. The interest rate used to measure that change shall be the credit-adjusted risk-free rate that existed when the liability was initially measured. That amount shall be recognized as an increase in the carrying amount of the liability and as an expense classified as an operating item in the statement of operations. SFAS No. 143 is effective for fiscal years beginning after June 15, 2002. The Company does not anticipate that adoption of SFAS No. 143 will have a material impact on its results of operations or its financial position.

In October 2001, FASB issued SFAS No. 144, ''Accounting for the Impairment or Disposal of Long-Lived Assets''. SFAS No. 144 establishes a single accounting model for long-lived assets to be disposed of by sale consistent with the fundamental provisions of SFAS No. 121 ''Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of''. Whilst it supersedes APB Opinion 30 ''Reporting the Results of operations — Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions'' it retains the presentation of discontinued operations but broadens that presentation to include a component of an entity (rather than a segment of a business). However, discontinued operations are no longer recorded at net realizable value and future operating losses are no longer recognized before they occur. Under SFAS No. 144 there is no longer a requirement to allocate goodwill to long-lived assets to be tested for impairment. It also establishes a probability weighted cash flow estimation approach to deal with situations in which there are a range of cash flows that may be generated by the asset being tested for impairment. SFAS No. 144 also establishes criteria for determining when an asset should be treated as held for sale.

SFAS No. 144 is effective for fiscal years beginning after December 15, 2001 and interim periods within those fiscal years, with early application encouraged. The provisions of the Statement are generally to be applied prospectively. The Company currently has no plans to dispose of any operations and accordingly, does not anticipate that adoption of SFAS No. 144 will have a material impact on its results of operations or its financial position.

4. Accounting Changes

Effective 2001, the Company changed its accounting principle regarding recognition of subscriber acquisition costs (see also Note 13 Deferred Subscriber Acquisition Costs). Subscriber acquisition costs represent the direct costs paid for each new subscriber enrolled through MTS's independent dealers. Prior to the 2001, these costs were capitalized to the extent of any revenues that had been deferred from the acquisition of a subscriber, such as connection fees charged to a subscriber to initiate call service, and amortized as a component of sales and marketing expense on a straight-line basis over the estimated average subscriber life. MTS now expenses subscriber acquisition costs as incurred. This change of accounting principle was made to facilitate the comparison of MTS's results with other telecommunication companies.

As a cumulative effect of this change, the remaining balance of capitalized subscriber acquisition cost as of December 31, 2000 in the amount of $17,909 (net of $9,644 in taxes) was expensed and included in income during the year ended December 31, 2001.

The following pro forma amounts for the years ended December 30, 1999, 2000 and 2001 show the effect of the retroactive application of the new accounting principle for recognition of subscriber acquisition costs.

	December 31		
	1999	2000	2001
	(In thousands of U.S. dollars, except per share amounts)		
Net income	$78,258	$93,108	$225,275
Earnings per share, basic and diluted	$ 0.052	$ 0.050	$ 0.114

5. New Investments

On January 22, 2001 MTS and certain individuals established and registered closed joint stock company Mobile TeleSystems — Nizhny Novgorod (MTS-NN) located in Nizhny Novgorod. MTS's participation in charter capital of MTS-NN is 65%. Charter capital of MTS-NN is 100,000 Rubles (approximately $3.5).

On December 10, 2001, MTS established MTS Finance (see Note 1 General), a société anonyme organized for unlimited duration under the laws of Luxembourg. MTS Finance has authorized share capital of $125 divided into 1,000 shares with a par value of $125 per share, 999 of which MTS owns directly and one of which MTS beneficially owns through De Luxe Holding S.A. All 1,000 shares are fully paid.

In September 2001, MTS won a tender initiated by the Telecommunications Ministry of the Republic of Belarus for a GSM 900/1800 license to operate in Belarus. Under the tender conditions, MTS paid $10 million which has been written off at December 31, 2001 (see Note 25 Impairment of investment in Belarus).

6. Businesses Acquired

Rosico acquisition

In August 1998, MTS acquired from Sistema 80% of the outstanding common stock of Rosico, a Russian closed joint stock company, in exchange for 408,631,860 shares of newly issued common stock of MTS representing 25% of the issued and outstanding shares of MTS. Prior to the acquisition, Sistema held a 90% controlling interest in Rosico. Rosico holds GSM-1800 licenses covering the Moscow area, 18 regions of Central Russia and 11 regions in the Northern, the Urals and Western Siberia Regions of Russia.

During 2000, MTS completed other acquisitions of Rosico stock that are presented in the table below:

Date of acquisition	Seller	Number of shares	Percentage of ownership	Price per share	Total purchase price
August 2000	Bradleys of London LTD, a subsidiary of Sistema	1,232	7.2%	$5.8401	$ 7,195
September 2000	MGTS, a subsidiary of Sistema	392	2.3%	5.8674	2,300
December 2000	Siemens AG	1,710	10.0%	3.5614	6,090
December 2000	DeTeMobil	86	0.5%	5.8140	500
	Total	3,420	20.0%	—	$16,085

(Amounts in thousands of U.S. dollars, unless otherwise stated)

As of December 31, 2001 MTS owned 100% interest of Rosico.

Purchase of Mobilnye Sistemy Svyasi

In March 2000, MTS acquired for approximately $15 a 51% interest in Mobilnye Sistemy Svyazi OJSC, or MSS, a Russian open joint-stock company. In 2001, MTS acquired an additional 32.5% of MSS stock for approximately $327, increasing its ownership percentage to 83.5% as of December 31, 2001. MSS has license No. 5544 to operate a GSM-900 network in the Omsk Region of Russia. At the time of acquisition, MSS had approximately 3,000 subscribers.

ReCom Acquisition

In 1998 MTS acquired 49.9% of ReCom, a Russian joint stock company for $11. In April 2001, MTS acquired an additional 4% of the outstanding common stock of ReCom for $1,000 increasing its share in ReCom up to 53.9%. The ReCom acquisition was accounted for using the purchase method of accounting. The finalized purchase price allocation was as follows:

Current assets	$ 3,805
Non-current assets, net of allocated excess of fair value over cost	7,095
License costs, net of allocated excess of fair value over cost	8,864
Current liabilities	(16,100)
Deferred taxes	(2,127)
Minority interest	(526)
Purchase price allocation	$ 1,011

During 2000 and 2001, MTS acted as the general contractor for the construction of ReCom's network. During these years, MTS delivered to ReCom network equipment, at its amortized historical cost, in the amount of $19,516. In connection with this, on January 31, 2000, ReCom issued 773 bonds to MTS, convertible under certain circumstances into common stock of ReCom. These bonds have maturities varying from 2003 to 2005. In June 2001, MTS redeemed 27 of these bonds and received approximately $500 of cash. If MTS were to exercise conversion options in full, it would become holder of up to 73.6% of the outstanding common stock of ReCom. The amount of convertible bonds and all other intercompany transactions and balances were eliminated in MTS's consolidated financial statements as of December 31, 2001.

Telecom XXI Acquisition

In May 2001, MTS acquired 100% of the outstanding common stock of Telecom XXI, a Russian closed joint stock company, for $49,742. The Telecom XXI acquisition was accounted for using the purchase method of accounting. The finalized purchase price allocation was as follows:

Current assets	$ 849
Non-current assets, net of allocated excess of fair value over cost	167
License costs, net of allocated excess of fair value over cost	76,415
Current liabilities	(944)
Deferred taxes	(26,745)
Purchase price allocation	$ 49,742

Telecom-900 Acquisition

In August 2001, MTS acquired 81% of the outstanding common stock of Telecom-900, a Russian closed joint-stock company, for $27,630 from Sistema. Telecom-900 acquisition was accounted for using the purchase method of accounting. The finalized purchase price allocation was as follows:

Current assets	$ 12,137
Non-current assets, net of allocated excess of fair value over cost	19,833
License costs, net of allocated excess of fair value over cost	43,087
Current liabilities	(23,195)
Non-current liabilities	(8,866)
Deferred taxes	(10,341)
Minority interest	(5,025)
Purchase price allocation	$ 27,630

Novitel Acquisition

On October 22, 2001 MTS acquired 51% of the outstanding common stock of Novitel, Russian closed joint-stock company, for the total amount of $1,426. Novitel acquisition was accounted for using the purchase method of accounting. The purchase price was allocated at the purchase date as follows:

Current assets	$1,312
Non-current assets	558
Other	533
Current liabilities	(57)
Non-current liabilities	(62)
Minority interest	(858)
Purchase price allocation	$1,426

Pro Forma Results of Operations (unaudited)

The following unaudited pro forma financial data for the years ended December 31, 2000 and 2001 give effect to the acquisitions of ReCom, Telecom XXI, Telecom 900 and Novitel as if they had occurred at the beginning of the respective years.

	December 31	
	2000	2001
	(In thousands of U.S. dollars except per share amounts)	
Net revenues	$563,048	$931,704
Net operating income	147,986	348,740
Net income	95,161	213,319
Earnings per share, Basic and Diluted	$ 0.053	$ 0.108

(Amounts in thousands of U.S. dollars, unless otherwise stated)

7. Cash and Cash Equivalents

Cash and cash equivalents as of December 31, 2000 and 2001 were comprised as follows:

	December 31	
	2000	2001
Rubles	$ 9,950	$ 15,282
U.S. dollar deposits	50,607	195,000
U.S. dollars current accounts	14,999	7,578
Other	272	1,769
Total cash and cash equivalents	$75,828	$219,629

8. Short Term Investments

Short-term investments, denominated in US dollars, as of December 31, 2001 were comprised as follows:

	Annual interest rate	Maturity date	December 31 2001
OJSC Moscow Bank of Reconstruction and Development	6.1%	September 30, 2002	$30,000
OJSC Moscow Bank of Reconstruction and Development	6.1%	September 30, 2002	25,000
Sberbank	8.3%	June 28, 2002	10,000
Sberbank	8.3%	June 28, 2002	10,000
Sberbank	8.3%	June 28, 2002	10,000
Other			340
Total Short-term investments			$85,340

Short-term investments, denominated in US dollars, as of December 31, 2000 were comprised as follows:

	Annual interest rate	Maturity date	December 31 2000
OJSC Moscow Bank of Reconstruction and Development	6.0%	August 31, 2001	$ 30,000
OJSC Moscow Bank of Reconstruction and Development	5.8%	March 31, 2001	20,000
Sberbank	9.5%	September 11, 2001	60,000
Sberbank	9.1%	September 11, 2001	60,000
Total Short-term investments			$170,000

Interest income for the years ended December 31, 1999, 2000 and 2001 amounted to $nil, $7,626 and $11,679, respectively. Interest receivable as of December 31, 2000 and 2001 amounted to $2,988 and $388, respectively, and is recorded as other current assets.

9. Trade Receivables

Trade receivables as of December 31, 2000 and 2001 were comprised as follows:

	December 31	
	2000	2001
Accounts receivable, subscribers	$ 9,280	$19,091
Accounts receivable, roaming	8,356	10,345
Allowance for doubtful accounts	(1,819)	(5,178)
Trade receivables, net	$15,817	$24,258

(Amounts in thousands of U.S. dollars, unless otherwise stated)

The following table summarizes the changes in the allowance for doubtful accounts for the years ended December 31, 1999, 2000 and 2001:

	December 31		
	1999	2000	2001
Balance, beginning of year	$ 19,610	$ 5,395	$1,819
Balance of business acquired	—	—	140
Provision for doubtful accounts	8,006	2,403	3,219
Accounts receivable written off	(22,221)	(5,979)	—
Balance, end of year	$ 5,395	$ 1,819	$5,178

10. Inventory

MTS' inventory as of December 31, 2000 and 2001 was comprised as follows:

	December 31	
	2000	2001
Spare parts for base stations	$ 8,469	$10,795
Handsets and accessories	16,363	11,712
Other inventory	1,656	9,157
Provision for obsolescence	(2,937)	(5,480)
Inventory, net	$23,551	$26,184

Obsolescence expense during the year ended December 31, 1999, 2000 and 2001 amounted to $590, $2,114 and $2,543, respectively, and was included in operating expenses in the accompanying statements of operations.

11. Property, Plant and Equipment

The net book value of property, plant and equipment as of December 31, 2000 and 2001 was comprised as follows:

	December 31	
	2000	2001
Network and base station equipment (including leased network and base station equipment of $nil and $32,248, respectively)	$387,664	$601,951
Leasehold improvements	6,720	7,233
Office equipment, computers and software (including leased office equipment, computers and software of $nil and $1,824, respectively)	21,134	42,340
Buildings	12,301	37,412
Vehicles	2,725	4,931
Property, plant and equipment, at cost	430,544	693,867
Accumulated depreciation	(87,676)	(158,994)
Accumulated depreciation on leased property	—	(9,995)
Equipment for installation	61,214	263,483
Construction in progress	35,225	52,947
Property, plant and equipment, net	$439,307	$841,308

All leased property, plant and equipment relate to Telecom 900 Group companies which were acquired by MTS in August 2001 (see Note 1 General), therefore there were no leased property, plant and equipment in 2000.

(Amounts in thousands of U.S. dollars, unless otherwise stated)

Depreciation expenses during the years ended December 31, 1999, 2000 and 2001 amounted to $24.8 million, $39.9 million and $73.7 million, respectively, including depreciation expenses for lease property, plant and equipment in the amount of $nil, $nil and $1,589, respectively.

12. Intangible Assets

Intangible assets at December 31, 2000 and 2001 were comprised as follows:

	December 31	
	2000	2001
Numbering capacity	$ 55,177	$ 66,203
Rights to use premises	20,877	24,380
Software and other	15,180	45,877
	91,234	136,460
Accumulated amortization	(33,648)	(52,953)
Total intangible assets, net	$ 57,586	$ 83,507

As a result of limited availability of local telephone numbering capacity in Moscow and the Moscow region, MTS has been required to enter into agreements for the use of telephone numbering capacity with several telecommunications operators in Moscow. Costs of acquiring numbering capacity are amortized over periods of five to ten years in accordance with the terms of the contract entered into to acquire such capacity. For contracts wherein the terms of use are unlimited, MTS amortizes such costs over ten years.

The principal component of MTS' right to use premises were obtained in the form of contributions to its original capital in 1993. These premises included MTS' administrative offices and facilities utilized for mobile switching centers.

Amortization expense during the years ended December 31, 1999, 2000 and 2001 amounted to $7.1 million, $12.9 million and $17.5 million, respectively.

13. Deferred Subscriber Acquisition Costs

Deferred subscriber acquisition costs for the years ended December 31, 2000 and 2001 were as follows:

	December 31	
	2000	2001
Balance at beginning of year	$ 31,925	$ 27,553
Payments made and deferred during the year	49,232	30,978
Amounts amortized and recognized as expenses during the year	(53,604)	(58,531)
Balance at end of year	$ 27,553	—

Effective 2001, the Company changed its accounting principle regarding recognition of subscriber acquisition costs (see Note 16 Accounting Changes). Subscriber acquisition costs represent the direct costs paid for each new subscriber enrolled through MTS' independent dealers. Prior to 2001, these costs were capitalized to the extent of any revenues that had been deferred from the acquisition of a subscriber, such as connection fees charged to a subscriber to initiate call service, and amortized as a component of sales and marketing expense on a straight-line basis over the estimated average subscriber life. MTS now expenses subscriber acquisition costs as incurred. This change of accounting principle was made to facilitate the comparison of MTS's results with other telecommunication companies.

(Amounts in thousands of U.S. dollars, unless otherwise stated)

14. Deferred Connection Fees

Deferred connection fees for the years ended December 31, 2000 and 2001 were as follows:

	December 31	
	2000	2001
Balance at beginning of year	$ 24,622	$ 31,553
Balance of business acquired	—	1,141
Payments received and deferred during the year	21,798	36,060
Amounts amortized and recognized as revenue during the year	(14,867)	(21,066)
Balance at end of year	$ 31,553	$ 47,688

MTS defers initial connection fees from the moment of initial signing of the contract with subscribers and the estimated average subscriber life (see Note 3 Summary of Significant Accounting Policies).

15. Debt

The Notes

On December 21, 2001, MTS Finance, a 100% beneficially owned subsidiary of MTS registered under the laws of Luxembourg, issued $250 million 10.95% notes at the price of 99.254%. These notes are guaranteed by MTS and mature on December 21, 2004. MTS Finance will make interest payments on the notes semi-annually in arrears on June 21 and December 21 of each year, commencing on June 21, 2002. The notes are listed on the Luxembourg Stock Exchange. Proceeds received from the notes, net of underwriting discount, were $248 million. Related debt issuance costs in the amount of $3,856 were capitalized.

These notes are subject to certain restrictive covenants including, but not limited to, limitations on the incurrence of additional indebtedness, limitations on the Company's ability to enter into sales leaseback transactions, restriction on any merger, consolidation or disposition of assets, restrictions on the sales of any licenses. In addition, these notes provide the holders a right to require MTS Finance to redeem all of the notes outstanding at 101% of the principal amount of the notes plus accrued interest upon any change in control, as defined.

Ericsson Debt Restructuring

In December 1996, Rosico entered into a credit agreement with Ericsson Project Finance AB (''Ericsson'') that provided for a credit facility with an aggregate principal amount of $60,000 and had a maximum term of five years. The loan was repayable in ten equal consecutive quarterly payments of $6,000 commencing in 1999. The amounts advanced under the agreement bear interest of LIBOR plus 4%, the overdue amount bears interest at a rate of an additional 6% per annum.

Concurrent with the Company's acquisition of Rosico, Sistema agreed to fund the full and timely repayment of the Ericsson Loan and to indemnify Rosico and MTS for any costs incurred by either of Rosico or MTS in connection with the repayment of the Ericsson Loan. During 2000, Sistema and MTS agreed on a method that would allow Sistema to fund its obligation in a manner that minimizes the total costs of meeting this obligation (including related tax costs). Under this method, MTS entered into a long-term, ruble-denominated promissory notes with 0% interest and maturities from 2049 to 2052 to repay a portion of the funding from Sistema. The carrying value of these notes is insignificant at December 31, 2001. The Company will record interest expense on these notes over the term such that the full amount of the obligation will be reflected as a liability at the date of repayment. Through December 31, 2001, Sistema has made payments to Rosico under this obligation in the amount of $41,405 of which $28,897 is repayable in the form of long-term, ruble-denominated promissory notes with 0% interest.

At December 31, 2000 and 2001, $42 million and $34.7 million were outstanding, respectively, under the Ericsson Loan at an interest rate then in effect of 10.0% and 6.5%, respectively. Interest payable on the

(Amounts in thousands of U.S. dollars, unless otherwise stated)

Ericsson Loan as of December 31, 2000 and 2001 is $431 and $219, respectively, and is included in accrued liabilities.

On July 24, 2001 MTS, Rosico and Ericsson signed an amendment to the credit agreement rescheduling Rosico principal payments in nineteen consecutive quarterly installments.

The following table presents a schedule by years of principal amount repayments as of December 31, 2001:

	December 31 2001
Payments due in the year ended December 31	
2002	$ 4,500
2003	6,750
2004	8,550
2005	11,700
2006	3,150
	$34,650

Dresdner credit facility

In July 1999, MTS entered into a rollover credit facility with "BNP — Dresdner Bank" ("Dresdner Bank") for the purpose of financing working capital. The credit facility in the amount up to $12 million was granted to MTS with the final repayment date no later than July 2, 2002. The amount advanced under the agreement bears interest of LIBOR plus 2.5% per annum. Default interest is 12% per annum. As of December 31, 2000 and 2001, there were no amounts outstanding on this facility.

Dresdner Bank Credit Facility to Telecom XXI

In November 2001, Telecom XXI entered into a credit facility with Dresdner Bank CJSC to borrow up to $20 million. Amounts borrowed by Telecom XXI under this credit facility are repayable within one to six months from the disbursement date and the credit facility has a final repayment date of November 2003. The borrowings bear interest of LIBOR plus 3.2% per annum. Any overdue amount currently bears interest at a rate of 12% per annum. At December 31, 2001 $3 million was outstanding under this agreement and is included in the current portion of long term debt.

International Moscow Bank Credit Facility to Telecom XXI

In November 2001, Telecom XXI entered into a credit facility with the International Moscow Bank to borrow up to $15 million. Amounts borrowed under the credit facility must be repaid within two months of the first disbursement under the credit facility and will bear interest of LIBOR plus 3.1% per annum. Any overdue amount bears interest at a rate of 7.9% per annum. At December 31, 2001 $10 million was outstanding under this agreement and is included in the current portion of long term debt.

Inkombank Credit Facility to MSS

In August 1997, MSS entered into a credit facility with OJSC "AB Inkombank" ("Inkombank") for the purposes of financing GSM 900 network development. A credit facility in the amount of up to $12 million was granted to MSS with a final repayment date no later than March 31, 2002. The amount advanced under the agreement bears interest of 16% per annum.

During December 2001, MTS negotiated with Inkombank to pay $4,169 immediately to extinguish the outstanding obligation of $6,949. This resulted in an extraordinary gain of $2,113, net of taxes of $667, upon the extinguishment.

(Amounts in thousands of U.S. dollars, unless otherwise stated)

16. Capital lease obligations

The following table presents a schedule by years of future minimum lease payments under capital leases together with the present value of the net minimum lease payments as of December 31, 2001:

	December 31 2001
Payments due in the year ended December 31	
2002	$ 16,017
2003	7,779
2004	2,002
2005	198
Total minimum lease payments (undiscounted)	25,996
Less: Amount representing interest	(3,899)
Present value of net minimum lease payments	22,097
Less current portion of lease payable	(14,401)
Non-current portion of lease payable	$ 7,696

All leased property, plant and equipment relate to Telecom 900 Group companies which were acquired by MTS in August 2001 (see Note 1 General), therefore there were no leases payable as of December 31, 2000.

For a schedule by years of future minimum lease payments under capital leases to Invest-Svyaz-Holding, a related party, together with the present value of the net minimum lease payments as of December 31, 2001 see Note 22 Related Parties.

17. Promissory Notes Payable

Promissory notes primarily represent MSS' outstanding notes payable to Motorola Inc. for delivery and installation of GSM-900 cellular equipment in the Omsk region. Promissory notes in the amount of $5.4 million were issued in April 1999. These promissory notes were due to be repaid on various dates through September 2001. On November 27, 2001, MSS entered into an agreement to restructure this liability. This restructuring established a new repayment schedule. MSS' total payments under this agreement have not changed by greater than 10% due to this restructuring. Promissory notes and the associated interest are to be repaid in regular installments starting from February 2002 up to May 2004. As of December 31, 2001 the amount of these promissory notes payable was $6,766, which represented the principal and accrued interest. The payments on these notes are due as follows:

2002	$ 818
2003	3,162
2004	2,786
Total principal and accrued interest	$6,766

18. Accrued Liabilities

Accrued liabilities at December 31, 2000 and 2001, were comprised as follows:

	December 31	
	2000	2001
VAT	$21,345	$31,213
Taxes other than income	10,816	13,781
Interest	1,909	1,636
Other accruals	4,105	4,996
Total accrued liabilities	$38,175	$51,626

(Amounts in thousands of U.S. dollars, unless otherwise stated)

19. Income Tax

MTS' provision for income taxes is as follows for the respective periods ended:

	December 31		
	1999	2000	2001
Current provision for income taxes	$ 36,423	$52,086	$138,092
Deferred benefit for income taxes	(17,594)	(932)	(39,342)
Total	$ 18,829	$51,154	$ 97,414

MTS' statutory income tax rate in 1998 was 35%. From April 1, 1999, MTS' statutory income tax rate was 30% as a result of changes in Russian legislation. This reduction in the statutory income tax rate resulted in the recognition of a deferred tax benefit of approximately $15 million in 1999. From January 1, 2001, MTS' statutory income tax rate is 35% as a result of changes in Russian legislation. The increase in tax rate to 35% resulted in recognition of a deferred tax liability of approximately $10 million in 2000. In August 2001, a new law regarding taxation of income became effective. Under that law, effective from January 1, 2002, the statutory income tax rate will be 24%. This reduction in the statutory income tax rate resulted in the recognition of a net deferred tax benefit of approximately $22 million in 2001. The statutory income tax rate reconciled to MTS' effective income tax rate is as follows for the respective periods ended:

	December 31		
	1999	2000	2001
Statutory income tax rate for year	30%	30%	35%
Adjustments:			
Effect from realization of benefits previously reserved	(7.7)	—	—
Expenses not deductible for Russian statutory taxation purposes	23.9	17.4	13.6
Tax allowance generated from investment in infrastructure	(16.7)	(18.2)	(8.3)
Effects of increase in income tax rate	—	7.0	—
Effects of decrease in income tax rate	(18.6)	—	(6.6)
Other	7.5	1.8	(3.9)
Effective income tax rate	18.4%	38.0%	29.7%

Unused credits may not be carried forward under Russian tax legislation Accordingly, income tax credits are reflected in MTS' financial statements only to the extent, and in the year in which the credits are utilized.

(Amounts in thousands of U.S. dollars, unless otherwise stated)

Temporary differences between the Russian statutory accounts and these financial statements give rise to the following deferred tax assets and liabilities at December 31, 2000 and 2001:

	December 31	
	2000	**2001**
Assets/(liabilities) arising from tax effect of:		
Deferred tax assets		
Allowance for doubtful accounts	$ 671	$ 1,130
Deferred revenue and expenses	1,401	10,910
Loss carry forward (Rosico and MSS)	12,823	14,709
Other	4,865	11,183
	19,760	37,932
Reserve for deferred tax assets	(17,689)	(25,892)
Total deferred tax assets	$ 2,071	$ 12,040
Deferred tax liabilities		
Licenses acquired (Note 4)	(72,083)	(71,432)
Other	—	(760)
Total deferred tax liabilities	(72,083)	(72,192)
Net deferred tax (liability)	$(70,012)	$(60,152)

As of December 31, 2000 and 2001, Rosico and MSS were entitled to loss carry forwards in the amounts of $36,638 and $61,286, respectively. These loss carry forwards resulted in a deferred tax asset for the years ended December 31, 2000 and 2001 in the amounts of $12,823 and $14,709, respectively. As Russian companies are required to file tax declarations on a standalone basis, MTS is not able to utilize these losses to offset its taxable income. Due to uncertainties with regards to Rosico's and MSS's ability to realize this benefit, a valuation reserve was provided for the entire amount.

20. Shareholders' Equity

In accordance with Russian statutory accounting regulations, earnings available for dividends are limited to profits, denominated in rubles, after certain deductions. At December 31, 2000 and 2001 retained earnings which are distributable under Russian legislation totaled 136 million rubles ($4,845) and 8,490 million rubles ($281,677) respectively.

21. Management Stock Bonus and Stock Option Plans

On April 27, 2000, contingent on the closing of MTS's initial public offering (see Note 1 General), MTS established a stock bonus plan and stock option plan for selected officers, key employees and key advisors.

Under the plans, directors, key employees and key advisors received 3,587,987 of MTS's common shares and will participate in a stock option plan under which they may receive options to purchase up to an additional 9,966,631 of MTS's common shares. At the time of the initial public offering, MTS issued 13,554,618 shares of common stock to its subsidiary Rosico pursuant to these plans at a price of $1.024 per share for the total amount of $13.9 million. These shares have been classified as treasury stock in the accompanying consolidated balance sheets.

(Amounts in thousands of U.S. dollars, unless otherwise stated)

Under the stock bonus plan, during the period from September 12, 2000 through September 22, 2000, 3,587,987 common shares were purchased from Rosico at nominal price of 0.1 rubles per share as follows:

	Number of shares purchased	Percentage of total shares outstanding
Directors	3,049,786	0.153
Key Advisors	538,201	0.027
Total	3,587,987	0.180

All of those listed above were restricted from selling these shares for 180 days from the date of purchase. However, if an employee should leave the company before the end of the two year restricted period, such employee will not retain the rights to the shares purchased and will lose the shares. On the date the shares were granted, MTS recognized aggregate expenses under this plan as compensation and consulting expenses amounting to $4.5 million and $797, respectively, based on the intrinsic value of the shares on the date they were granted (see also Note 22 Related Parties).

Under the stock option plan, MTS's Board members and key employees, upon being granted stock options, will have the right to purchase up to 9,966,631 common shares of MTS. On August 14, 2001, option agreements for 1,026,682 and 830,010 common shares of MTS were granted to MTS's Board members and key employees, respectively. These options provide that on July 15, 2003, MTS's Board members and key employees may purchase MTS's common shares at $1.31 per share, which represents the 100-day average sales price of the shares at August 14, 2001.The stock options for MTS's Board members will terminate if the Board member's role is terminated before the 2002 annual general shareholder's meeting of Mobile TeleSystems. The stock options for MTS's key employees will terminate if the employee should leave MTS before July 15, 2003.

MTS is accounting for the management stock option plan in accordance with APB No. 25 under which expense is generally only recognized for a difference between the exercise price and the fair market value at the date of measurement which is the grant date in the case of a fixed plan. At August 14, 2001 the fair market price of MTS's common shares was $1.17, which is less than the exercise price of $1.31. Accordingly, no compensation expense has been recorded during the year ended December 31, 2001.

In accordance with the Russian legislation, MTS's Board members and key employees may be considered insiders with respect to Mobile TeleSystems and thus may be restricted from selling their shares.

22. Related Parties

Related party balances as of December 31, 2000 and 2001, were comprised of the following:

	December 31	
	2000	2001
Accounts receivable, related parties:		
DeTeMobil receivable for roaming	$1,082	$ 677
ReCom receivable for network equipment	3,187	—
ReCom receivable for telecommunication services	425	—
Receivables from other investee companies	243	1,700
Total accounts receivable, related parties	$4,937	$2,377
Accounts payable, related parties:		
DeTeMobil payable for consulting services	$1,970	$1,970
DeTeMobil other payables	1,308	1,266
Telmos for interconnection	411	207
MTU-Inform payable	2,004	2,593
MGTS for interconnection	103	106
Total accounts payable, related parties	$5,797	$6,142

Moscow Bank of Reconstruction and Development (MBRD)

Starting August 2000, MTS has been keeping certain bank and deposit accounts with MBRD, whose major shareholder is Sistema. As of December 31, 2000, MTS' cash position at MBRD amounted to $51.4 million including $50 million in time deposit and $1.4 million in a current account. As of December 31, 2001 MTS' cash position at MBRD amounted to $112.4 million including $105 million in time deposits and $7.4 million in a current account. The related interest accrued and collected on the deposits for the years ended December 31, 2000 and 2001 amounted to $1 million and $3 million, respectively, and was shown as a component of interest income.

Rosno OJSC

In 1999, 2000 and 2001, MTS arranged medical insurance for its employees and MTS insured its property at the amounts of approximately $193 million, $274 million and $612 million in 1999, 2000 and 2001, respectively, with Rosno Insurance whose major shareholder is Sistema. Insurance premiums paid to Rosno for the years ended December 31, 1999, 2000 and 2001, amounted to $4.7 million, $6.5 million and $8 million, respectively, including premiums paid for medical insurance amounted to $683, $1,583 and $2,542, respectively. Management believes that all of the insurance contracts with Rosno have been entered at market terms.

Maxima Advertising Agency (Maxima)

In 1999, 2000 and 2001, MTS had agreements for advertising services with Maxima. Advertising fees paid to Maxima for the years ended December 31, 1999, 2000 and 2001 were $1.2 million, $6.4 million and $10.1 million, respectively. Maxima is related to MTS trough MTS' directors who are also members of Maxima's board of directors

Telmos

In 1999, 2000 and 2001, MTS had interconnection arrangements with, and received domestic and international long-distance services from, Telmos. Interconnection and line rental fees paid to Telmos for the years ended December 31, 1999, 2000 and 2001 were approximately $3 million, $4.3 million and $4.0 million, respectively. Management believes that these arrangements are at market terms. Telmos is 40% owned by MGTS, which is majority-owned by Sistema and its affiliates.

Moscow City Telephone Network (MGTS)

In 1999, 2000 and 2001 MTS had a line rental agreements with MGTS and rented cable plant from MGTS for installation of optic-fiber cable. MTS also rented buildings for administrative office, sales and marketing offices as well as premises for switching and base station equipment. Amounts paid under these agreements for the years ended December 31, 1999, 2000 and 2001 were approximately $0.5 million, $1 million and $1.5 million, respectively. In December 2000 and 2001, MTS purchased buildings from MGTS and paid $2.9 million and $2.6 million, respectively. Management believes that all these purchases were made at market terms. MGTS related to MTS trough its directors who are members of MGTS' board of directors. In addition Sistema is the majority shareholder of MGTS.

MTU-Inform

In 1999, 2000 and 2001 MTS had interconnection and line rental agreements with MTU-Inform. Amounts paid under these agreements for the years ended December 31, 1999, 2000 and 2001 amounted to approximately $8.4 million, $17.4 million and $29 million, respectively. In 1999, 2000 and 2001 MTS purchased telephone numbering capacity from MTU-Inform. Amounts paid under these agreements for the years ended December 31, 1999, 2000 and 2001 amounted to $3.4 million, $11.7 million and $4.7 million, respectively. Management believes that these agreements are at market terms. MTU-Inform is owned 51% by MGTS, which is majority-owned by Sistema and its affiliates.

(Amounts in thousands of U.S. dollars, unless otherwise stated)

Other

In 2000 consultants from MTS's two major shareholders advised MTS in connection with MTS's initial public offering. In April 2000, contingent on the closing of this stock offering, MTS established a stock bonus plan (see Note 21 Management Stock Bonus and Stock Option Plans). Under this plan, consultants purchased 538,201 common shares of MTS's from Rosico at nominal price 0.1 Rbls per share. In 2000 MTS recognized consulting expenses under this plan in the amount of $797 based on the intrinsic value of the shares on the date of grant.

As discussed in Note 6, MTS acquired 81% of the outstanding stock of Telecom-900, a Russian closed joint stock company, for $27,630 from Sistema.

Invest-Svyaz-Holding

In 2001, Uraltel, FECS-900 and SCS-900 signed agreements with Invest-Svyaz-Holding, a shareholder of MTS, for leasing of network equipment and a billing system. These leases were recorded as capital leases based on the requirements of Statement of Financial Accounting Standards No 13, "Accounting for Leases". The present value of future lease payments is reflected as a liability in the balance sheet. Amounts due within 1 year are classified as short term and the remaining balance as long-term liabilities. The interest rate implicit in these leases varies from 15% to 54%.

The following table represents a schedule by years of future minimum lease payments under capital leases to Invest-Svyaz-Holding together with the present value of the net minimum lease payments as of December 31, 2001:

	December 31 2001
Payments due in the year ended December 31	
2002	$ 4,097
2003	2,829
2004	1,247
Total minimum lease payments (undiscounted)	8,173
Less: Amount representing interest	(1,970)
Present value of net minimum lease payments	6,203
Less current portion of lease payable	(2,794)
Non-current portion of lease payable	$ 3,409

The current portion and long-term portion of the lease payable to Invest-Svyaz-Holding were included in current portion of capital lease obligation and capital lease obligation, net of current portion, respectively.

Principal and interest paid to Invest-Svyaz-Holding for the period from the date of acquisition of Telecom-900 on August 10, 2001 through December 31, 2001 were $503 and $139, respectively.

(Amounts in thousands of U.S. dollars, unless otherwise stated)

23. Operating Expenses

Operating expenses for 1999, 2000 and 2001 were comprised of the following:

	December 31		
	1999	2000	2001
Salaries and social contributions	$17,108	$ 33,753	$ 44,425
Taxes other than income taxes	15,655	26,859	25,312
General and administrative	11,633	20,355	21,569
Rent	4,062	7,241	9,479
Insurance	4,953	4,251	5,258
Repair and maintenance	3,252	3,225	10,578
Provision for doubtful accounts (note 9)	8,006	2,403	3,219
Consulting expenses	1,390	2,621	2,093
Billing and data processing	444	2,285	2,981
Other operating expenses	8,109	7,249	9,684
Total operating expenses	$74,612	$110,242	$134,598

For use of certain base station sites, MTS provides specified amounts of free usage of mobile telephones in lieu of rent payments. Amounts of revenues for such free usage and expenses for base station site rentals are shown at fair value. Base station site expenses incurred under barter arrangements for the years ended December 31, 1999, 2000 and 2001 were approximately $2,427, $3,251 and $2,234, respectively, and are shown as a component of rent expenses.

24. Impairment of the investment in Belarus

In September 2001, MTS won a tender initiated by the Telecommunications Ministry of the Republic of Belarus to form a joint venture which will have a GSM 900/1800 license to operate in Belarus. Under the tender conditions, MTS is obliged:

- to make a one-time payment of $10 million to the government of Belarus;
- to form a joint venture company, in which MTS will own a 49% stake, together with the government of Belarus and a state-owned entity, and into which MTS must make a capital contribution of approximately $2.5 million in cash and
- to pay $6 million in annual installments to the government of Belarus of $1.2 million from 2003 through 2007.

Under the terms of the tender, the joint venture will be required to pay to the government of Belarus for the license a one-time fee of $5 million and an annual fee of $60,000. Once the joint venture receives the license, it will be valid for ten years, after which it may be prolonged for two additional five-year periods as long as the joint venture fulfills the conditions of the license.

In November 2001 MTS made the $10 million payment to the government of Belarus. This amount represented an initial investment in the joint venture as it is required to allow participation in such joint venture. However, we believe there is significant doubt as to whether we will receive all governmental licenses and approvals necessary to begin operations in Belarus. Due to this substantial doubt whether the joint venture will be able to commence operations, the $10 million investment has been expensed. This is reflected in impairment of investments and other expenses in the accompanying consolidated statement of operations.

Based on the tender agreement, whereby the government of Belarus guaranteed the Company that the joint venture would receive a license to operate, the Company does not believe that it is legally obligated to make the additional $6 million of payments to the government of Belarus unless it is granted a license and commences operations. If operations do commence, this obligation will be recorded at that time or when the uncertainty is resolved.

25. Operating Licenses

In connection with providing telecommunication services, MTS and its legal predecessor have been issued various operating licenses by the Ministry of Communications (the ''Ministry'').

MTS' principal operating licenses are presented below.

GSM-900 Licenses

Moscow and Moscow Region — MTS has a GSM-900 cellular license (License No. 14665) for operation in Moscow and the Moscow region. This license expires in December 2004.

Tver Region — MTS has a GSM-900 cellular license (License No. 14662) for operations in the Tver region. This license expires in April 2007.

Kostroma Region — MTS has a GSM-900 cellular license (License No. 14664) to operate in the Kostroma region. This license expires in August 2007.

Komi Republic — MTS has a GSM-900 cellular license (License No. 14663) for operations in the Komi Republic. This license expires in August 2007.

MTS has GSM-900 licenses (Licenses Nos. 14452 through 14457) covering six regions bordering the Moscow region. These licenses expire in October 2006.

In connection with the ReCom acquisition, MTS gained access to GSM-900 licenses covering the Voronezh, Belgorod, Bryansk, Kursk, Lipetsk (Licenses No. 10020 through 10024), and Orel (License No. 10015) regions. These licenses expire in May 2008.

In connection with the UDN-900 and ACC acquisition, MTS gained access to the GSM-900 licenses covering the Udmurt Republic (License No. 5964) and the Amur region (License No. 5608), respectively. These licenses expire in February 2007 and January 2007, respectively.

In connection with the MSS acquisition on March 2000, MTS gained access to GSM-900 license (License No. 5544) covering the Omsk region of Russia. This license expires in December 2006.

Altai Republic — In connection with the acquisition of Telecom 900 MTS gained access to GSM-900 cellular license (License No. 18808) for operations in the Altai Republic. The License allows SCS-900 to operate from July 2001 to July 2011 provided that commencement of cellular services occurs no later than July 2002. In addition, these license requires that the network numbering capacity to achieve 800, 2,900 and 6,000 numbers as of December 2002, 2005 and 2010, respectively.

Sverdlovsk Region — In connection with the acquisition of Telecom 900 MTS gained access to GSM-900 cellular license (License No. 4817) for operations in the Sverdlovsk region. This license requires that the network numbering capacity to achieve 300,000 numbers as of December 31, 2006 and expires in March 2006.

Khabarovsk Region — In connection with the acquisition of Telecom 900 MTS gained access to GSM-900 cellular license (License No. 5607) for operations in the Khabarovsk region. This license requires that the network numbering capacity achieve 4,000 and 11,000 numbers as of December 2001 and 2007, respectively, and expires in January 2007.

GSM-1800 Licenses

In connection with the Rosico acquisition, MTS gained access to three GSM-1800 licenses covering Moscow and the Moscow region, 18 regions in Central Russia and 11 regions in Northern, Urals and the Western Siberia Regions of Russia. These licenses expire in 2008.

Moscow and the Moscow Region — In April 1998, Rosico was granted a GSM-1800 cellular license (License No. 10006) for operation in Moscow and the Moscow region. This license requires that the installed network numbering capacity to achieve 100,000 numbers as of December 31, 2001 and expires in April 2008.

Central, Central Black Earth and Volga Regions — In April 1998, Rosico was granted a GSM-1800 cellular license (License No. 10007) for operation in the following 17 regions of the Central, Central Black Earth and Volga regions of Russia: Bryansk, Vladimir, Ivanovo, Tver, Kaluga, Kostroma, Orel, Ryazan, Smolensk, Tula, Yaroslavl, Belgorod, Voronezh, Kursk, Lipetsk, Tambov and Kirov. In addition, in October 2000, amendments to this license were approved by the Ministry that allowed Rosico to operate on the GSM-900/1800 standards in the Nizhniy Novgorod region. This license requires that the network numbering capacity to achieve 20,000 numbers as of December 31, 2001 and expires in April 2008. Services under the license commenced in March 2000. Management believes that the risk that the aforementioned delay would cause the license to be revoked is remote.

Northern, Urals and Western Siberia Regions — In April 1998, Rosico was granted a GSM-1800 cellular license (License No. 10011) for operation in a total of the following 6 regions of the Urals region of Russia: Udmurt Republic; Kurgan, Orenburg, Perm, Komi-Permyatsk Autonomous district and the Sverdlovsk region; Komi Republic in the Northern Region of Russia; and three regions of Western Siberia: the Tyumen Region, and the Khanty-Mansiysk and Yamalo-Nenetsk autonomous districts. In addition, in October 2000 amendments to this license were approved by the Ministry that allowed Rosico to operate on the GSM-900/1800 standards in the Kirov, Perm and Chelyabinsk Regions. This license requires that the network numbering capacity to achieve 16,000 numbers as of December 31, 2001 and expires in April 2008. Cellular services under this license had not commenced in October 1999. Other services under the license commenced only in February 2000. Management believes that the risk that the aforementioned delay would cause the license to be revoked is remote.

North-Western Region of Russia — In connection with the acquisition of Telecom XXI MTS gained access to the GSM-900/1800 cellular license (License No. 10004) for operations in St. Petersburg and the following nine North-Western regions of Russia: the Karelia Republic, the Nenetsky autonomous district, and the Leningrad, Arkhangelsk, Vologda, Kaliningrad, Murmansk, Novgorod and Pskov regions. This license requires the network numbering capacity to achieve 45,000 numbers as of December 31, 2001 and expires in April 2008.

Novosibirsk Region — In connection with the acquisition of Telecom 900 MTS gained access to a GSM-900 cellular license (License No. 5965) for operation in the Novosibirsk region. In addition, in October 2000, amendments to this license were approved by the Ministry that allows SCS-900 to operate on the GSM-1800 standards in the Novosibirsk region. The license requires that the network numbering capacity to achieve 10,000 numbers and 25,000 numbers as of December 31, 2002 and 2007, respectively, and expires in February 2007.

When MTS commenced its operations in 1994, licenses generally contained certain provisions for unspecified fees to be paid for utilization of the frequency. Most of MTS' current licenses now provide for payments to be made to finance telecommunication infrastructure improvements, which in the aggregate could total approximately $103,080. However, no decisions regulating the terms and conditions of such payments have been formulated. Accordingly, no payments have been made to date pursuant to any of the current licenses, which could require such payments. Further, management believes that MTS will not required to make any such payments. If such payments would be required in the future, management believes that it would be limited to purchasing certain equipment for its own use in the related license area.

In relation to these uncertainties, no amounts have been recorded in the accompanying financial statements.

Other Telecommunication Licenses

MTS has a License No. 14668 for fixed local and intercity telephone communication operations in Moscow, the Moscow region, the Tver and Kostroma regions and the Komi Republic. This license requires the number of subscribers be greater than 30,000 as of December 31, 2004 and expires in August 2004. MTS also has a License No. 15282 for fixed local and intercity telephone communication operations in the Vladimir, Kaluga, Pskov, Ryazan, Smolensk and Tula regions. This license expires in July 3, 2005. It requires the numbering capacity of network to achieve 14,700 numbers at the end of the third year of operation and specifies that the operations should commence no later than January 3, 2002.

MTS has a channel rent license (License No. 14666) in Moscow and the Moscow region, the Kostroma and Tver regions and the Komi Republic, and a channel rent license (License No. 14680) in the Vladimir, Kaluga, Pskov, Ryazan, Smolensk and Tula regions. These licenses expire in November 2003 and April 2004, respectively. MTS has a license for channel rent (License No. 16245) in the Ivanovo, Kirov, Nizhniy Novgorod, Yaroslavl regions, and a channel rent license (License No. 17774) in the Amur, Kurgan, Orenburg, Perm, Sverdlovsk, Tambov, Tyumen, Chelyabinsk regions, the Udmurt Republic, and the Komi-Permyatskiy, Khanty-Mansiysk and Yamalo-Nenetsk autonomous districts. These licenses expire in October 2005 and April 2006, respectively.

MTS has a license for data transmission services (License No. 14667) in Moscow and the Moscow region, the Kostroma and Tver regions and the Komi Republic. This license expires in December 2004.

MTS also has a license for data transmission services (License No. 15403) in the Vladimir, Kaluga, Pskov, Ryazan, Smolensk and Tula regions. This license expires in July 2005.

On February 15, 2001 MTS was granted a new license for data transmission services (License No. 17333) in the Komi Republic and the Udmurt Republic, in the following 3 autonomous districts: Komi-Permyatsky, Khanty-Mansiysk and Yamalo-Nenetsk, and in the following 28 regions: Amur, Belgorod, Briansk, Vladimir, Voronezh, Ivanovo, Kaluga, Kirov, Kostroma, Kurgan, Kursk, Lipetsk, Moscow, Nizhny Novgorod, Omsk, Orenburg, Orel, Perm, Pskov, Ryazan, Sverdlovsk, Smolensk, Tambov, Tver, Tula, Tyumen, Chelyabinsk and Yaroslavl, and Moscow. This license requires the numbering capacity of network to achieve 100 and 1,000 numbers as of December 31, 2002 and at the end of the license period, respectively, and specifies that the operations should be commenced no later than February 15, 2002. This license expires in February 2006.

On January 25, 2001 MTS was granted a new license for video conference services (License No. 17169) in the Komi Republic and the Udmurt Republic, in the following 3 autonomous districts: Komi-Permyatsky, Khanty-Mansiysk and Yamalo-Nenetsk; and in the following 28 regions: Amur, Belgorod, Briansk, Vladimir, Voronezh, Ivanovo, Kaluga, Kirov, Kostroma, Kurgan, Kursk, Lipetsk, Moscow, Nizhny Novgorod, Omsk, Orenburg, Orel, Perm, Pskov, Ryazan, Sverdlovsk, Smolensk, Tambov, Tver, Tula, Tyumen, Chelyabinsk and Yaroslavl, and Moscow city. This license requires the numbering capacity of network to achieve 2 and 24 numbers as of December 31, 2002 and at the end of the license period, respectively, and specifies that the operations should be commenced no later than January 25, 2002. This license expires in January 2006.

On May 18, 2001 MTS was granted a new license for audio conference services (License No. 18228) in the Komi republic and the Udmurt republic, in the following 3 autonomous districts: Komi-Permyatsky, Khanty-Mansiysk and Yamalo-Nenetsk; and in 28 regions as follows: Amur, Belgorod, Briansk, Vladimir, Voronezh, Ivanovo, Kaluga, Kirov, Kostroma, Kurgan, Kursk, Lipetsk, Moscow, Nizhny Novgorod, Omsk, Orenburg, Orel, Perm, Pskov, Ryazan, Sverdlovsk, Smolensk, Tambov, Tver, Tula, Tyumen, Chelyabinsk and Yaroslavl, and Moscow city. This license requires that the numbering capacity of network to achieve 3 and 10 numbers as of December 31, 2002 and at the end of the license period, respectively, and specifies that the operations should be commenced no later than May 18, 2002. This license expires in May 2006.

On October 4, 2001 MTS was granted a new license for fixed local and long distance communication operations (License No. 19615) in the Amur, Ivanovo, Kirov, Nizhny Novgorod, Omsk. Perm, Sverdlovsk and Yaroslavl regions and the Udmurt republic. This license requires that the numbering capacity of the network to achieve 900 numbers as of December 31, 2004 and specifies that the operations should be commenced no later than October 4, 2002. This license expires in October 2011.

On October 4, 2001 MTS was granted a new license for data transmission services (License No. 19596) in the Karelia republic, the Nenetsk autonomous region, St. Petersburg and the following 6 north-western regions: Arkhangelsk, Vologda, Kaliningrad, Leningrad, Murmansk, Novgorod. This license requires that the numbering capacity of network to achieve 10 and 100 numbers as of December 31, 2002 and at the end of the license period, respectively, and specifies that operations should be commenced no later than October 4, 2002. This license expires in October 2006.

(Amounts in thousands of U.S. dollars, unless otherwise stated)

In connection with ReCom acquisition, MTS gained access to ReCom licenses for data transmission services and channels rent (License No. 14113 and No. 14024, respectively) in the Voronezh, Belgorod, Bryansk, Kursk, Lipetsk and Orel regions. The licenses expire in December 2004.

In connection with the acquisition of MSS MTS gained access to the MSS license for fixed local telephone communication using wireless connection operations (License No. 8957) in the Omsk region. This license requires that the network numbering capacity to achieve 14,000 and 20,000 numbers at the end of the third year of operation and as of December 31, 2002, respectively, and expires in December 2007

In connection with the acquisition of Telecom 900 MTS gained access to license for channel rent (License No. 9476) in the Sverdlovsk region. This license requires the network numbering capacity to achieve 1,176 and 1,680 numbers at the end of the third year of operation and at the end of the license period, respectively, and expires in March 2003.

In connection with the acquisition of Telecom 900 MTS gained access to a license for channel rent (License No. 11843) in the Novosibirsk region. This license requires that the network numbering capacity achieve 9,240 and 13,200 numbers at the end of the third year of operation and at the end of the license period, respectively, and expires in April 2004.

In connection with the acquisition of Telecom 900 MTS gained access to a license for data transmission services (License No. 15486) in the Sverdlovsk region. This license requires that the numbering capacity achieve 1,500 and 2,500 numbers as of December 31, 2001 and at the end of the license period, respectively, and expires in July 2005.

In connection with the acquisition of Telecom 900 MTS gained access to a license for data transmission services (License No. 17810) in the Novosibirsk region. This license requires that the numbering capacity achieve 50,000 and 150,000 numbers as of December 31, 2002 and at the end of the license period, respectively, and expires in April 2006.

In connection with the acquisition of MSS gained access to a license for data transmission services (License No. 17152) in the Omsk region. This license permits operations from January 2001 to January 2006 provided that commencement of cellular services occurs no later than January 2002. The license requires that network numbering capacity to achieve 350 and 500 numbers at the end of the third year of operation and at the end of the license period, respectively.

In connection with the acquisition of MSS MTS gained access to for channel rent license (License No. 17030) in the Omsk region. The license requires that the network numbering capacity to achieve 350 and 500 numbers at the end of the third year of operation and at the end of the license period, respectively, and expires in April 2006.

In connection with the acquisition of Telecom 900 MTS gained access to for channel rent license (License No. 17765) in the Khabarovsk region. The license requires the commencement of operations no later than April 2002 and expires in April 2006.

Recorded values of licenses acquired

	December 31 2001
Moscow license area (Rosico)	$227,025
North-Western region (Telecom XXI)	76,415
Five regions of Asian Russia (Telecom-900)	43,087
Seven regions of European Russia (RTC)	19,503
Six regions of European Russia (ReCom)	8,864
Other	2,379
Licenses, at gross book value	$377,273
Accumulated amortization	(79,783)
Total licenses, net	$297,490

26. Commitments and Contingencies

Commitments

As of December 31, 2001, MTS committed to further purchase of network property, plant and equipment in the amount of approximately $189 million.

In 2002 MTS agreed to purchase its previously rented office building from MGTS, a related party, for the amount of approximately $2.6 million.

Negative Net Equity of Rosico

In accordance with Russian legislation, joint stock companies must maintain a level of equity (net assets) that is greater than the charter capital. In the event that a company's equity (net assets), as determined under Russian accounting legislation, falls below certain minimum levels, specifically below zero, such company can be forced to liquidation.

During 2000 and 2001, Rosico reported significant losses in its financial statements compiled in accordance with Russian accounting legislation. As a result, at December 31, 2000 and 2001, Rosico reported a deficit in equity (negative net equity) in its financial statements compiled in accordance with Russian accounting legislation.

27. Subsequent Events

Issue of Eurobonds

On March 19, 2002 MTS Finance issued $50 million 10.95% notes at a price of 101.616%. These notes are guaranteed by MTS and mature on December 21, 2004. MTS Finance will make interest payments on the notes semi-annually in arrears on June 21 and December 21 of each year, commencing on June 21, 2002. The notes are listed on the Luxembourg Stock Exchange. Proceeds received from the notes, including the offering premium, were $50.8 million.

Acquisition of ZAO Kuban GSM

On March 29, 2002 MTS completed acquisition of a controlling share (51%) in Krasnodar-based CJSC Kuban GSM for $71.4 million. Kuban GSM has about 500,000 subscribers and operates in thirteen major cities throughout the Russian Federation, including Sochi, Krasnodar and Novorossisk. The remaining 49% of shares in Kuban GSM are owned by OOO "KubTelecom". Under the terms of the acquisition agreement, MTS has the right to buy and OOO "KubTelecom" has the right to sell all remaining shares of Kuban GSM held by OOO "KubTelecom" at market price anytime until February 15, 2006. Also MTS will subscribe for an additional 3,600 ordinary shares of Kuban GSM through a closed subscription approved by an Extraordinary General Meeting of shareholders of Kuban GSM on February 15, 2002, at a price of $14,000 per share. If MTS were to subscribe for these additional 3,600 shares, its stake in Kuban GSM would increase to approximately 63%. Management believes that this transaction will be completed in first half of 2002. This acquisition will be accounted for by the purchase method in the first quarter of 2002.

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VIRGIN MOBILE TELECOMS LIMITED

US GAAP

CONSOLIDATED FINANCIAL STATEMENTS
For the years ended 31 December 2001 and 2000 and for the period from incorporation (29 January 1999) to 31 December 1999

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REPORT OF INDEPENDENT AUDITORS

To the Shareholders of Virgin Mobile Telecoms Limited:

We have audited the accompanying consolidated balance sheets of Virgin Mobile Telecoms Limited (a UK company) and subsidiary as of 31 December 2001 and 2000 and the related consolidated statements of operations, shareholders' equity and cash flows for the years ended 31 December 2001 and 2000 and for the period from its incorporation (29 January 1999) to 31 December 1999. These financial statements are the responsibility of Virgin Mobile Telecoms Limited's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Virgin Mobile Telecoms Limited and subsidiary as of 31 December 2001 and 2000, and the results of their operations and their cash flows for the year ended 31 December 2001 and 2000 and for the period from 29 January 1999 to 31 December 1999 in conformity with accounting principles generally accepted in the United States.

Arthur Andersen

6 June 2002

VIRGIN MOBILE TELECOMS LIMITED

CONSOLIDATED BALANCE SHEETS
31 December 2001 and 2000

	31 December 2001	31 December 2000
	£'000	£'000
Assets		
Current assets:		
Cash and cash equivalents	9,714	1,965
Accounts receivable, net of allowance for doubtful debts of £438,000 (2000 — £481,000)	17,189	7,575
Due from other related companies	13,271	3,215
VAT receivable	516	5,059
Prepayments	2,773	1,955
Inventories	4,927	8,457
	48,390	28,226
Non-current assets:		
Deferred financing costs	1,528	1,936
Property and equipment, net of accumulated depreciation of £21,229,000 (2000 — £9,043,000)	17,307	22,215
SIM cost deferral	6,425	3,569
	25,260	27,720
	73,650	55,946
Liabilities		
Current Liabilities:		
Accounts payable	21,664	12,527
Accrued liabilities	8,667	12,741
Deferred revenue	27,556	14,558
Interest rate swaps and forward foreign exchange contracts	1,292	7
Capital lease	255	—
Due to other related companies	2,874	28,329
Other accounts payable	2,089	547
	64,397	68,709
Deferred revenue	6,972	5,114
Capital lease	233	—
Bank loan	100,000	25,000
Due to other related companies	64,314	58,659
	235,916	157,482
Cumulative redeemable preference shares, £0.01 par value, 300 (2000 — 300)	37,160	33,563
Shareholders' equity		
'D' ordinary shares, £0.01 par value, 10,000 (2000 — 10,000)	—	—
Non-voting preference 'B' shares, £0.01 par value, 475,000 (2000 — 475,000)	5	5
'E' shares, £0.02 par value, 13,500 (2000 — 13,500)	—	—
Preference voting 'A' shares, £0.02 par value, 485,000 (2000 — nil)	10	—
Zero dividend voting 'C' shares, £0.01 par value, 475,000 (2000 — nil)	4	—
Accumulated deficit	(199,445)	(135,104)
	(199,426)	(135,099)
Shareholders' equity and cumulative redeemable preference shares	(162,266)	(101,536)
	73,650	55,946

The accompanying notes are an integral part of these consolidated financial statements.

VIRGIN MOBILE TELECOMS LIMITED

CONSOLIDATED STATEMENTS OF OPERATIONS
31 December 2001, 2000 and 1999

	Year ended 31 December 2001	Year ended 31 December 2000	Period from incorporation to 31 December 1999 (11 month period)
	£'000	£'000	£'000
Revenues			
Equipment revenue, net of discounts	25,782	20,013	8,175
Service revenue	137,940	47,929	719
	163,722	67,942	8,894
Expenses			
Network and equipment cost	(118,192)	(78,198)	(13,806)
General and administrative expense	(82,442)	(82,210)	(20,033)
Depreciation and amortization	(12,186)	(8,043)	(1,681)
Operating loss	(49,098)	(100,509)	(26,626)
Interest expense	(11,789)	(5,005)	—
Interest income	483	516	47
Loss before income taxes	(60,404)	(104,998)	(26,579)
Provision for income taxes	—	—	—
Net loss before cumulative effect of adoption of SFAS No. 133	(60,404)	(104,998)	(26,579)
Cumulative effect of adoption of SFAS No. 133	(340)	—	—
Net loss	(60,744)	(104,998)	(26,579)
Financing cost of cumulative redeemable preference shares	(3,597)	(2,921)	(606)
Net loss attributable to equity shareholders	(64,341)	(107,919)	(27,185)

The accompanying notes are an integral part of these consolidated financial statements.

VIRGIN MOBILE TELECOMS LIMITED

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
31 December 2001, 2000 and 1999

	Share capital	Accumulated Deficit	Total Shareholders' Funds/ (Deficit)
	£'000	£'000	£'000
At incorporation	—	—	—
Shares issued	5	—	5
Net loss attributable to equity shareholders	—	(27,185)	(27,185)
Balance, 31 December 1999	5	(27,185)	(27,180)
Net loss attributable to equity shareholders	—	(107,919)	(107,919)
Balance, 31 December 2000	5	(135,104)	(135,099)
Increase of share capital	14	—	14
Net loss attributable to equity shareholders	—	(64,341)	(64,341)
Balance, 31 December 2001	19	(199,445)	(199,426)

There was no other comprehensive income other than the results for the periods.

The accompanying notes are an integral part of these consolidated financial statements.

VIRGIN MOBILE TELECOMS LIMITED

CONSOLIDATED STATEMENTS OF CASH FLOWS
31 December 2001, 2000 and 1999

	Year ended 31 December 2001	Year ended 31 December 2000	Period from incorporation to 31 December 1999 (11 month period)
	£'000	£'000	£'000
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net loss	(60,744)	(104,998)	(26,579)
Adjustments to reconcile net loss to net cash provided by operating activities:			
Cumulative effective of adoption of SFAS No. 133	340	—	—
Amortization of financing costs	408	102	—
Depreciation and amortization	12,186	8,043	1,681
Add/(deduct) net changes in operating assets and liabilities:			
Accounts receivable	(9,614)	(6,049)	(1,526)
Due from other related companies	(10,056)	1,686	(4,901)
Other accounts receivable	883	(3,679)	(6,357)
Inventories	3,530	2,370	(10,827)
Accounts payable and accrued liabilities	7,594	5,767	16,962
Deferred revenue	14,856	15,885	3,787
Due to other related companies	(19,800)	14,472	18,016
Other accounts payable	2,480	328	219
Net cash used by operating activities	(57,937)	(66,073)	(9,525)
Cash flows from investing activities			
Net cash received in acquisition of subsidiary	—	—	3,429
Cash paid for property and equipment	(9,172)	(15,605)	(13,764)
Net cash used in investing activities	(9,172)	(15,605)	(10,335)
Cash flows from financing activities			
Financing costs incurred	—	(2,038)	—
Proceeds from issuance of share capital	14	—	5
Proceeds from issuance of cumulative redeemable preference shares	—	—	30,036
Proceeds from unsecured loans from other related companies	—	49,500	1,000
Proceeds from loans secured on share capital and net assets of the group	75,000	25,000	—
Repayment of capital lease	(156)	—	—
Net cash provided by financing activities	74,858	72,462	31,041
Net increase/(decrease) in cash and cash equivalents	7,749	(9,216)	11,181
Cash and cash equivalents, beginning of year	1,965	11,181	—
Cash and cash equivalents, end of year	9,714	1,965	11,181

The accompanying notes are an integral part of these consolidated financial statements.

VIRGIN MOBILE TELECOMS LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
31 December 2001, 2000 and 1999

1 Background and organization

The company was incorporated on 29 January 1999 in the United Kingdom. The principal activities of the group comprise the sale of mobile phone handsets and the provision of mobile telecommunication services.

Virgin Mobile Telecoms Limited has a 100% holding in Bluebottle Call Limited. The only activity of this company is the leasing of property on behalf of Virgin Mobile Telecoms Limited. Together these two companies form the group.

2 Significant accounting policies

These financial statements have been prepared in accordance with accounting principles generally accepted in the United States and are expressed in British Pounds Sterling. The significant accounting policies are summarized as follows:

a) Basis of preparation

As at 31 December 2001 the group had a total shareholder deficit of £199,426,000 (2000 — £135,099,000). The group is currently being financed by a syndicated bank loan (see note 4) and by its shareholders, T-Mobile and the Virgin Group (see note 8). The group has drawn down £100,000,000 under the £115,000,000 syndicated bank loan. The continued availability of this funding is based on achieving a number of financial and operating covenants (see note 4). While there can be no certainty about the group's future operating performance, based on the group's current approved plan for 2002 and forecasts for subsequent periods, the directors expect that the group will be cash neutral in the twelve months ending 31 December 2002 and that the group will comply with the syndicated bank loan covenants. Therefore, the directors have prepared these accounts on a going concern basis.

b) Basis of consolidation

The financial statements consolidate the financial statements of the Company and its subsidiary company after eliminating all intercompany transactions and balances.

c) Use of estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, as well as the reported amounts of revenue and expenses during the reporting period. Actual amounts and results could differ from those estimates.

d) Foreign currencies

The consolidated financial statements are prepared in British Pounds Sterling. The functional currency is local currency in which the Company and its subsidiary are located (UK). Transactions in foreign currencies are translated at the exchange rate in effect at the date of each transaction. Differences in exchange rates during the period between the date a transaction denominated in a foreign currency is consummated and the date on which it is either settled or translated are recognized in the statement of operations.

The foreign currency exchange gain or loss recognized in the statement of income was a loss of £93,000 (2000 — £4,000, 1999 — £nil).

e) Cash and cash equivalents

For purposes of the statement of consolidated cash flows, the Company considers all highly liquid debt instruments purchased with an original maturity of three months or less to be cash. No such instruments were held during the period.

f) *Accounts receivable — trade*

Accounts receivable — trade are stated at nominal value less a provision for doubtful accounts. The provision is based on the risk of non-collectability then known. Amounts written off amounted to £206,000 (2000 — £97,000, 1999 — £nil) and the provision decreased by £43,000 (increased by £481,000 in 2000).

g) *Revenue recognition*

Equipment

Handsets

Handsets revenue is recognized based on the amounts received, net of rebates and commissions paid to the channels, at the date of sale. Commissions payable to channels are accrued when the channel has fulfilled the conditions to which the commission relates. This revenue is considered a separate earnings process to airtime and SIM card sales and hence is recognized upon delivery to the distributor.

SIM cards

SIM cards are sold to channels or directly to subscribers. The sale of a SIM card represents an ongoing commitment to provide service to a subscriber over the average subscriber's life. Revenue is therefore deferred and recognized over the average subscriber life commencing at the date of sale.

Service

Revenue earned directly from customers is recognized based on usage of the network in the period when services are rendered. No revenue is recognized on initial free airtime. Revenue is earned from third parties for the provision of services, including the network, to Virgin Mobile customers. This revenue is recognized in the period when services are rendered.

h) *Direct costs related to revenue*

Handset costs

Handset costs are recognized based on the amounts paid, net of rebates received from the suppliers, at the date of sale.

SIM cards

Costs are deferred and recognized over the average subscriber life commencing at the date of sale. Deferred costs are included within non-current assets.

Network charges

Network costs including the cost of providing initial free airtime are recognized on usage of the network.

i) *Advertising costs*

Advertising costs are expensed as incurred. Such costs are included in sales and general and administrative expenses in the accompanying consolidated statements of operations and for the year ended 31 December 2001 were £17,172,000 (2000 — £17,844,000, 1999 — £1,626,000).

j) *Financing costs*

Debt issuance costs relating to the Company's bank loans are deferred and amortized to interest expense using the effective interest method over the term of the bank loan.

k) *Property and equipment*

Property and equipment are stated at cost, net of accumulated depreciation. Maintenance repairs and minor renewals are charged to expense as incurred. Major renewals and improvements are capitalized and depreciated over their estimated useful lives. When assets are retired or otherwise disposed of, the cost is removed from the asset account and the corresponding accumulated depreciation is removed from the related reserve account. Any gain or loss resulting from such retirement or disposal is included in current income.

The recoverability of fixed assets is assessed whenever events or circumstances indicate a potential impairment. This assessment involves comparing the carrying value of the assets with management's best estimate of the future undiscounted cash flows to be generated by using the asset. Where this calculation indicates an impairment the asset is written down to its fair value, which is estimated based upon management's best estimate of future discounted cash flows.

Depreciation is provided on a straight-line basis over the estimated useful lives of the property and equipment as follows:

Leasehold improvements	3 years
Fixtures and fittings	3 years
Office equipment	3 years
Computer systems	2-3 years

Assets under development are not depreciated until development has been completed and the fixed asset is fully operational.

l) Inventories

Inventories which comprise handsets held for resale are stated at the lower of standard cost and market value. Market value is based on estimated selling price, less further direct selling costs. Provision is made for obsolete, slow-moving or defective items where appropriate.

m) Income taxes

Income taxes are accounted for under the liability method in accordance with FAS 109, "Accounting for Income Taxes." Deferred tax assets and liabilities are determined based on differences between the financial reporting and tax basis of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse. Deferred tax assets are reduced by a valuation allowance to the extent that it is more likely than not that a portion of the assets will not be realized.

n) Derivative financial instruments

The Company uses derivative financial instruments for the purpose of reducing its exposure to adverse fluctuations in interest rates, currencies and other market risks. The counterparties to these instruments are major financial institutions with high credit quality. The Company is exposed to credit loss in the event of non-performance by these counterparties.

On 1 January 2001, the Company adopted FAS 133, which establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts and used for hedging activities. All derivatives, whether designated for hedging relationships or not, are required to be recorded on the balance sheet at fair value. If the derivative is designated as a fair value hedge, all changes in the fair value of the derivative and changes in the fair value of the hedged item attributable to the hedged risk are recognized in earnings. If the derivative is designated as a cash flow hedge, the effective portions of the changes in the fair value of the derivative are recorded in other comprehensive income and are recognized in the statement of operations when the hedged item affects earnings. The ineffective portions of both fair value and cash flow hedges are immediately recognized in earnings.

The Company's interest rate swap has never been designated as an accounting hedge, consequently upon the adoption of SFAs No 133, this swap was recorded in the balance sheet at fair value at the transition date (1 January 2001). The resulting adjustment of £340,000 was recorded as the cumulative effect of adoption of SFAs No 133.

After adoption of FAS 133, the interest rate swaps are accounted for at fair value, marking to market (fair value) any differences between periods through the statement of operations at the end of each reporting period. Swaps contracts are recorded at fair value and any differences between periods are recorded through the statement of operations at the end of each reporting period. The charge in the period is taken as a general and administrative expense.

n) Deferred revenue

Deferred revenue represents:

- Deferred SIM card revenue. This revenue is recognized over the average subscriber life.
- The balance of services due to pre-pay customers. This revenue is recognized upon usage.
- The cash payments received as an incentive to sign rental agreements. This revenue is recognized over the term of the rental agreements.

o) Leases

Assets obtained under capital leases are capitalised in the balance sheet and depreciated over their estimated useful lives or the leases' term, whichever is shorter. The interest element of these obligations is charged to the profit and loss account over the relevant period. The capital element of the future payment is treated as a liability.

Rentals under operating leases are charged on a straight-line basis over the lease term, even if the payments are not made on such a basis. Benefits received and receivable as an incentive to sign an operating lease are similarly spread on a straight-line basis over the lease term, except where the period to the review date on which the rent is first expected to be adjusted to the prevailing market rate is shorter than the full lease term, in which case the shorter period is used.

p) Recent accounting pronouncements

In June 2001, the Financial Accounting Standards Board issued FAS 143 "Accounting for Asset Retirement Obligations". FAS 143 requires the fair value of a liability for asset retirement obligations to be recognised in the period in which it is incurred if a reasonable estimate of the fair value can be made. The associated asset retirement costs are capitalized as part of the carrying amount of the related long-lived asset.

FAS 143 is effective for financial statements issued for fiscal years beginning after June 15, 2002. The Company believes that the adoption of FAS 143 will have no impact on the company's financial statements.

In August 2001, the Financial Accounting Standards Board issued FAS 144 "Accounting for the Impairment of Disposal of Long-Lived Assets to be Disposed Of". While it supersedes APB Opinion 30 "Reporting the Results of operations — Reporting the Effects of the Disposal of a Segment of a business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions" it retains the presentation of discontinued operations but broadens that presentation to include a component of an entity (rather than a segment of a business). However, discontinued operations are no longer recorded at the net realisable value and future operating losses are no longer recognised before they occur. Under FAS 144, there is no longer a requirement to allocate goodwill to long-lived assets to be tested for impairment. It also establishes a probability weighted cash flow estimation approach to deal with situations in which there is a range of cash flows that may be generated by the asset being tested for impairment. FAS 144 also establishes criteria for determining when an asset should be treated as held for sale.

FAS 144 is effective for fiscal years beginning after December 15 2001 and interim periods within those fiscal years, with early application encouraged. The provisions of the Statement are generally to be applied prospectively. The Company currently has no plans to dispose of any operations and, accordingly, does not anticipate that adoption of FAS 144 will have any impact on its results of operations or its financial position.

In April 2002, the FASB issued SFAS 145 "Rescission of FASB Statements No. 4, 44 and 64, Amendment of FASB Statement No. 13 and Technical Corrections." The principal change is that gains or losses from extinguishment of debt which are classified as extraordinary items by SFAS 4 will no longer be classified as such. The provisions of SFAS 145 are effective for fiscal years beginning after 15 May 2002 although early application of the Statement related to the rescission of SFAS 4 is encouraged. The Company plans to adopt SFAS 145 for its fiscal year ending 31 December 2003. When adopted, prior extraordinary items related to the extinguishment of debt will need to be reclassified.

3 Property and equipment

Property and equipment consist of the following:

	Leasehold improvements	Fixtures and fittings	Office equipment	Computer systems	Total
	£'000	£'000	£'000	£'000	£'000
Cost					
At 1 January 2001	7,718	642	271	22,627	31,258
Additions	74	20	2	7,182	7,278
At 31 December 2001	7,792	662	273	29,809	38,536
Depreciation					
At 1 January 2001	1,591	263	78	7,111	9,043
Charge for the period	2,517	213	101	9,355	12,186
At 31 December 2001	4,108	476	179	16,466	21,229
Net book value					
At 31 December 2001	3,684	186	94	13,343	17,307
At 31 December 2000	6,127	379	193	15,516	22,215

Property and equipment include computer equipment of £644,375 (2000 — £nil) and net book value of £536,537 (2000 — £nil) in respect of assets held under a capital lease.

4 Long term debt

The Group's long-term debt comprises the following:

	2001	2000
	£'000	£'000
Capital lease	233	—
Bank loan	100,000	25,000
Due to other related companies	64,314	58,659
	164,547	83,659

As at 31 December 2001, contractual maturities of the Group's indebtedness were as follows:

	Capital lease	Bank loan	Due to other related companies
	£'000	£'000	£'000
Year ended 31 December			
2002	255	—	—
2003	233	23,000	—
2004	—	46,000	—
2005	—	31,000	—
2005 or later	—	—	64,314
Total	488	100,000	64,314

The bank loan is in the form of a syndicated loan facility. The loan facility is secured on the share capital and assets of the group. The interest rate on the floating rate element of the facility loan is linked to the LIBOR. The undrawn committed borrowings under this facility at 31 December 2001 was £15,000,000 (2000 — £55,000,000). The continued availability of this facility is based on achieving a number of financial and operating covenants, the principal covenants being subscriber numbers and revenue and earnings to debt ratios.

The interest rate on floating shareholder loans for which there is no fixed repayment date is at 4% above the three-month LIBOR rate. These loans and associated interest do not become repayable until the bank has been repaid.

5 Shareholders' equity

	2001	2000
	£	£
Authorised		
10,000 'D' ordinary shares of £0.01 each	100	100
475,000 non-voting preference 'B' shares of £0.01 each	4,750	4,750
30,000 'E' shares of £0.02 each	600	600
485,000 preference voting 'A' shares of £0.02 each	9,700	9,700
475,000 zero dividend voting 'C' shares of £0.01 each	4,750	4,750
	19,900	19,900

	2001	2000	
	Called-up and fully paid	Called-up and fully-paid	Called-up
	£	£	£
Allotted			
10,000 'D' ordinary shares of £0.01 each	100	100	100
475,000 non-voting preference 'B' shares of £0.01 each	4,750	4,750	4,750
13,500 'E' shares of £0.02 each	270	270	270
485,000 preference voting 'A' shares of £0.02 each	9,700	—	9,700
475,000 zero dividend voting 'C' shares of £0.01 each	4,750	2	4,750
	19,570	5,122	19,570

'D' Ordinary shares (" 'D' shares")

'D' shares are entitled to receive a preferred dividend being a portion of the first £100 million to be distributed after payment of cumulative redeemable preference share dividends and any arrears of that dividend. Holders of 'D' shares together with 'B' shareholders are entitled to receive 50% of this preferred dividend. 'D' shareholders are also eligible to receive ordinary dividends. Holders of 'D' shares receive 1 vote per share. On a winding-up, 'D' shareholders together with 'B' shareholders are eligible to receive, after payment to the cumulative redeemable preference shareholders, a 50% share in the first £100 million to be distributed together with an equal share of any remaining surplus assets.

Non-voting preference 'B' shares (" 'B' shares")

'B' shares are entitled to receive a preferred dividend being a portion of the first £100 million to be distributed after payment of cumulative redeemable preference share dividends and any arrears of that dividend. Holders of 'B' shares together with 'D' shareholders are entitled to receive 50% of this preferred dividend. 'B' shareholders are also eligible to receive ordinary dividends. Holders of 'B' shares have no voting rights. On a winding-up, 'B' shareholders together with 'D' shareholders are entitled to receive, after payment to the cumulative redeemable preference shareholders, a 50% share in the first £100 million to be distributed together with an equal share of any remaining surplus assets.

'E' shares

'E' shares are only entitled to receive ordinary dividends (after cumulative redeemable preference share dividends and preferred dividends to 'A', 'B' and 'D' shareholders) at the earlier of 5 years after the date of issue of the shares and the date of realisation (being flotation, sale or a winding-up). After 5 years or realisation, 'E' shareholders are entitled to 1 vote per share. On a winding-up, they are entitled to receive a share in the surplus assets after payment to the cumulative redeemable preference shareholders and the 'A', 'B' and 'D' shareholders.

Preference voting 'A' shares (" 'A' shares")

'A' shares are entitled to receive a preferred dividend of 50% of the first £100 million to be distributed after payment of cumulative redeemable preference share dividends and any arrears of that dividend. 'A' shareholders are also eligible to receive ordinary dividends and receive 1 vote per share. Holders of 'A' shares have the right on a winding-up to receive, after payment to the cumulative redeemable preference shareholders, a 50% share in the first £100 million to be distributed together with an equal share of any remaining surplus assets.

Zero dividend voting 'C' shares (" 'C' shares")

'C' shareholders are not entitled to receive any dividend income but have 1 vote per share. On a winding-up, they are entitled to receive a share in the surplus assets after payment to the cumulative redeemable preference shareholders and the 'A', 'B' and 'D' shareholders.

6 Cumulative redeemable preference shares

Cumulative redeemable preference shares carry an entitlement to dividend at the rate 9% per annum on the issue price (being £30,036,000 paid in 1999) and may be redeemed at £100,122 per share at any time at the option of the company. Holders of the cumulative redeemable preference shares have no voting rights. On a winding-up, the holders are entitled to receive, in priority to any other classes of shares, the sum of £100,122 per share together with any arrears of dividend because the holders of the cumulative redeemable preference shares are the shareholders in, and have joint control of, the Company redemption is not under the control of the Company and according to EITF topic D-98, cumulative redeemable preference shares have not been classified as share capital. The following table presents a reconciliation of the carrying amount of the cumulative redeemable preference shares as of 31 December 2001, 2000 and 1999:

	31 December 2001	31 December 2000	31 December 1999
	£'000	£'000	£'000
Balance, beginning of the year/period	33,563	30,642	—
Share capital	—	—	—
Share premium	—	—	30,036
Financing cost — cumulative dividend	3,597	2,921	606
Balance, end of the year	37,160	33,563	30,642

7 Financial instruments

The company believes the amounts presented for financial instruments in the accompanying financial statements, consisting of cash equivalents, accounts receivables, accounts payables, are reasonable estimates of their fair value.

The following table presents the carrying amounts and fair values at the Company's other financial instruments as of 31 December 2001 and 2000:

	2001			2000		
	Principal Amount	Carrying Amount	Fair Value	Principal Amount	Carrying Amount	Fair Value
	£'000	£'000	£'000	£'000	£'000	£'000
Long-term debt	100,233	100,233	105,191	25,000	25,000	26,797
Interest rate swap	75,000	(1,256)	(1,256)	20,000	(7)	(347)
Forward contract	6,250	(36)	(36)	—	—	—

There were no financial instruments used in the year ended 31 December 1999.

The company has entered into interest rate swaps to hedge against adverse movements in LIBOR in relation to its syndicated loan facility. The company's policy is to keep between 50 per cent and 75 per cent of the syndicated loan borrowing at fixed rates of interest. At the year-end, 75 per cent of the syndicated loan was at fixed rates after taking account of interest rate swaps.

About one-third of the handset purchases made by the company are from suppliers in continental Europe. These purchases are invoiced in Euros. The company's policy is to eliminate some currency exposure on payments at the time of purchase through forward currency contracts. All other purchases are denominated in sterling.

The fair value of the interest rate swaps and foreign exchange contracts have been determined by reference to prices available from the markets on which the instrument involved is traded.

The fair value of the long term loan has been calculated by discounting cash flows at prevailing interest rates.

The fair values of shareholder loans have not been presented. As they are not publicly traded, it would be impractical to make an estimate with sufficient reliability.

The fair values of the cumulative redeemable preferences shares have not been presented. As they are not publicly traded and can be redeemed at any time at the option of the company, it would be impractical to make an estimate with sufficient reliability.

8 Taxes

The provision for income taxes is comprised of the following:

	31 December 2001	31 December 2000	31 December 1999
	£'000	£'000	£'000
Current tax payable	—	—	—
Deferred tax asset due to property, plant and equipment	6,189	2,374	279
Deferred tax asset for carried forward losses	52,311	36,999	7,297
Cumulative valuation allowance	(58,500)	(39,373)	(7,576)
	—	—	—

The reconciliation of the tax expense with the product of accounting multiplied by the applicable tax rate is as follows:

	Year ended 31 December 2001	Year ended 31 December 2000	11 month period ended 31 December 1999
	£'000	£'000	£'000
Loss before income taxes	(60,404)	(104,998)	(26,579)
Effective tax (rate — 30%)	18,121	31,499	7,974
Tax effect of accelerated capital allowances	(3,815)	(2,095)	(279)
Tax effect of permanent differences (disallowable expenses)	1,006	298	(398)
Tax credit for the period	15,312	29,702	7,297
Valuation allowance for the period	(15,312)	(29,702)	(7,297)
Tax expense for the period	—	—	—

Total carried forward tax losses at 31 December 2001 were in the region of £174,000,000 (2000 — £123,000,000, 1999 — £24,000,000). These losses result in significant deferred tax assets, however management believes that recognition of these assets is not appropriate given the current position of the company.

9 Related party transactions

T-Mobile (formerly known as One 2 One), through One 2 One Personal Communications Limited, and The Virgin Group, through Bluebottle Investments S.A. and Bluebottle UK Limited, are joint venture partners in Virgin Mobile. The following transactions occurred with these partners in the year.

T-Mobile

The company was partially financed by a loan facility provided by T-Mobile on which interest at variable rates accrues. The principal amount of £32,156,945 (2000 — £29,329,643) was outstanding as at 31 December 2001. Interest has been rolled up to the principal quarterly. Total interest for the year payable to T-Mobile is £2,827,303 (2000 — £2,627,874). There are no fixed repayment dates, however this loan and associated interest does not become repayable until the bank syndicated loan (see note 4) has been repaid.

Some handsets, service packs and other accessories are purchased by T-Mobile on behalf of the company. The total cost to the company in respect of such purchases amounted to £18,116,136 (2000 — £55,366,696) and of this £880,190 remained unpaid as at 31 December 2001 (2000 — £28,088,902).

T-Mobile pay a marketing support contribution to the company and the company pays charges to T-Mobile both as a result of Virgin Mobile's customers' use of the network. The total income from marketing support contributions to the company, net of payments to T-Mobile for use of its network, amounted to £10,851,585 (2000 — £2,307,600) of which a net amount of £2,552,222 (2000 — £1,146,643) remained outstanding as at 31 December 2001.

T-Mobile distribute airtime vouchers to certain retailers on behalf of the company. The total amount invoiced during the period in respect of these vouchers, net of management and distribution fees, amounted to £26,769,848 (2000 — £13,512,352). £2,041,684 (2000 — £4,400,690) of this total remained outstanding from T-Mobile as at 31 December 2001.

T-Mobile incurred additional expenses, particularly third party recharges and staff time, which were recharged on to the company and the company incurred similar expenses which were recharged to T-Mobile. The net amount recharged by T-Mobile was £463,179 (2000 — £1,828,440). As at 31 December, a net amount of £114,200 was owing from T-Mobile to the company (2000 — £230,000 was owing from the company to T-Mobile).

T-Mobile provides three directors of the company and receives a £45,000 (2000 — £45,000) annual consultancy fee for these executive services. An amount of £18,750 (2000 — £64,000) remained outstanding at the end of December 2001.

Virgin Group

The company was partially financed by a loan facility provided by Bluebottle UK Limited, a member of the Virgin Group, on which interest at variable rates accrues. The principal amount of £32,156,945 (2000 — £29,329,643) was outstanding as at 31 December 2001. Interest has been rolled up to the principal quarterly. Total interest for the year payable to companies within the Virgin Group was £2,827,303 (2000 — £2,079,643). There are no fixed repayment dates, however this loan and associated interest does not become repayable until the bank syndicated loan (see note 4) has been repaid.

During the period, handset, airtime vouchers and other stock items were sold through retailers who are members of the Virgin Group. These sales amounted to £36,639,689 (2000 — £33,909,281) of which £9,443,202 (2000 — £3,197,681) remained outstanding as at 31 December 2001.

Members of the Virgin Group performed additional services including printing, brand licensing and promotion, which were recharged on to the company. These amounted to £8,300,147 (2000 — £8,364,958) of which £2,532,076 (2000 — £580,230) remained unpaid as at 31 December 2001.

Virgin Management Limited provides three directors of the company and receives a £45,000 (2000 — £45,000) annual consultancy fee for these executive services. An amount of £7,500 (2000 — £64,000) remained outstanding at the end of December 2001.

The group uses some other sundry services provided by members of the Virgin Group. These are transacted on an arm's length basis under normal commercial terms.

10 Financial Commitments

Annual commitments under non-cancellable operating leases are as follows:

	Land and Buildings 2001	Land and Buildings 2000
	£'000	£'000
2002	1,092	1,092
2003	1,092	1,092
2004	1,092	1,092
2005	1,092	1,092
2006 or later	8,713	9,816
	13,081	14,184

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COMDIRECT BANK AKTIENGESELLSCHAFT

CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

For the years ended 31 December 2001 and 2000

COMDIRECT BANK AKTIENGESELLSCHAFT

CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
AS OF DECEMBER 31, 2001 AND 2000

CONTENTS

CONSOLIDATED INCOME STATEMENTS OF COMDIRECT BANK GROUP ACCORDING TO IAS (UNAUDITED)

	Notes	1.1.-31.12.2001 (€ thousand) (unaudited)	1.1.-31.12.2000 (€ thousand) (unaudited)
INCOME STATEMENT			
Interest income		138,621	121,046
Interest expenses		64,538	63,329
Net interest income before provisions	(23)	74,083	57,717
Provision for possible loan losses	(24)	(2,074)	(1,966)
Net interest income after provisions		72,009	55,751
Commission income		96,957	192,656
Commission expenses		3,939	1,793
Net commission income	(25)	93,018	190,863
Trading profit	(26)	(29)	(133)
Result from financial investments		344	0
Administrative expenses	(27)	224,317	220,951
Other operating result	(28)	6,659	35
Profit from ordinary activities		(52,316)	25,565
Extraordinary result and restructuring expenses	(29)	(98,264)	0
Pre-tax profit		(150,580)	25,565
Taxes on income	(30)	10,077	23,371
After-tax profit		(160,657)	2,194
Profit/loss attributable to minority interests		0	484
Net profit/loss for the year		(160,657)	2,678
Transfer from reserves		160,657	0
Consolidated profit/loss		0	2,678

EARNINGS PER SHARE

		1.1.-31.12.2001	1.1.-31.12.2000
BASIC EARNINGS PER SHARE			
Net income/loss for the year	(€ thousand)	(160,657)	2,678
Average number of ordinary shares	unit	140,500,000	104,959,016
Basic earnings per share	€	(1.14)	0.03

		1.1.-31.12.2001	1.1.-31.12.2000
DILUTED EARNINGS PER SHARE			
Net income/loss for the year	(€ thousand)	(160,657)	2,678
Adjustment to the number of ordinary shares issued due to outstanding option rights	unit	97,278	32,660
Weighted average shares outstanding (diluted)	unit	140,597,278	104,991,677
Diluted earnings per share	€	(1.14)	0.03

CONSOLIDATED BALANCE SHEETS OF COMDIRECT BANK GROUP ACCORDING TO IAS (UNAUDITED)

ASSETS	Notes	as of 31.12.2001 (€ thousand) (unaudited)	as of 31.12.2000 (€ thousand) (unaudited)
Cash reserve	(31)	72,005	515
Claims on banks	(32)	1,684,112	1,006,477
Claims on customers	(33)	263,728	575,524
Provisions for possible loan losses	(34)	(4,936)	(3,180)
Trading assets	(35)	2,164	883
Financial investments	(36)	861,212	1,153,239
Intangible assets	(37)	22,076	40,950
Fixed assets	(38)	45,816	76,335
Tax assets		9,634	8,679
Other assets	(40)	18,200	15,683
Total assets		**2,974,011**	**2,875,105**

LIABILITIES AND EQUITY	Notes	as of 31.12.2001 (€ thousand) (unaudited)	as of 31.12.2000 (€ thousand) (unaudited)
Liabilities to banks	(41)	0	3,678
Liabilities to customers	(42)	2,289,327	2,044,554
Provisions	(43)	51,351	5,728
Tax liabilities	(44)	10,444	10,794
Other liabilities		28,162	40,967
Subordinated capital	(45)	16,617	29,399
Minority interests		0	287
Equity		578,110	739,698
Subscribed capital		140,500	140,500
Capital reserve		394,327	595,834
Retained earnings			
Legal reserve		0	686
Other revenue reserves		42,200	0
Revaluation reserve		1,083	0
Consolidated profit/loss		0	2,678
Total liabilities and equity		**2,974,011**	**2,875,105**

STATEMENT OF CHANGES IN EQUITY (UNAUDITED)

	Subscribed capital	Capital reserve	Retained earnings	Revaluation reserve	Consolidated profit/loss	Total 2001	Total 2000
				(€ thousand)			
Equity as of 1.1 (unaudited)	**140,500**	**595,834**	**686**	**0**	**2,678**	**739,698**	**62,817**
Reversal of the correction per 31.12.2000	—	3,875	0	—	(3,875)	0	0
Booking of valuation differences due to swap transactions pursuant to IAS 39	—	—	(2,646)	—	0	(2,646)	0
Formation of a revaluation reserve pursuant to IAS 39	—	—	0	1,083	0	1,083	0
Capital increases	—	—	0	—	0	0	695,500
Appropriation of consolidated loss	—	—	0	—	0	0	6,183
Consolidated profit/consolidated loss	—	—	0	—	(160,657)	(160,657)	2,678
Changes in differences arising from currency translation	—	—	632	—	0	632	0
Costs of IPO	—	—	0	—	0	0	(19,803)
Transfer from reserves/allocation to reserves	—	(205,382)	43,528	—	161,854	0	(7,677)
Equity as of 31.12 (unaudited)	**140,500**	**394,327**	**42,200**	**1,083**	**0**	**578,110**	**739,698**

CONSOLIDATED CASH FLOW STATEMENTS (UNAUDITED)

	1 January - 31 December	
	2001	2000
	(in € thousand) (unaudited)	
Net profit/net loss	**(160,657)**	**2,678**
Non-cash positions in net income and adjustments to reconcile net income to net cash provided by operating activities		
Write-downs, depreciations, adjustments and write-ups to fixed assets and changes in provisions	32,830	19,936
Loss/profit from the sale of financial investments and fixed assets	114	0
Other adjustments (net)	(16,798)	(20,384)
Subtotal	**(144,511)**	**2,230**
Change in assets and liabilities from operating activities after correction for non-cash components		
Claims		
— on banks	(683,544)	211,425
— on customers	311,497	(255,385)
Securities	284,171	(447,738)
Other assets from operating activities	55	(20,803)
Liabilities		
— to banks	(3,678)	(18,363)
— to customers	244,773	(107,639)
Other liabilities from operating activities	3,197	(5,248)
Interest and dividends received	143,612	111,601
Interest paid	(64,538)	(61,609)
Income tax paid	0	(4,104)
Cash flow from operating activities	**91,034**	**(595,633)**
Change from investing activities (net)	**(7,394)**	**(103,373)**
Proceeds from capital increases	0	655.885
Change from subordinated capital and other (net)	(12,782)	0
Net cash provided by financing activities	**(12,782)**	**655,885**
Cash and cash equivalents at the end of the previous period	**515**	**43,636**
Cash flow from operating activities	91,034	(595,633)
Cash flow from investing activities	(7,394)	(103,373)
Net cash provided by financing activities	(12,782)	655,885
Effects of changes in exchange rates	632	0
Cash and cash equivalents at the end of the period	**72,005**	**515**

NOTES FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2001 (UNAUDITED)

Accounting principles

The consolidated financial statements of comdirect bank as of 31 December, 2001 were prepared in accordance with the International Accounting Standards (IAS) approved and published by the International Accounting Standards Committee (IAS) and with their interpretation by the Standing Interpretations Committee (SIC).

A summary of all the regulations that have been applied can be found on pages 55 and 56.[1]

As a subsidiary of Commerzbank AG, Frankfurt am Main, we are exempted in accordance with Art. 291, German Commercial Code (HGB), from the duty to present sub-group financial statements. As we have not presented the main differences between financial statements prepared in accordance with IAS and those prepared in accordance with the German Commercial Code, these consolidated financial statements do not conform to the 4th and 7th EC directives and do not, therefore, exempt us from presenting consolidated financial statements in accordance with Art. 292a, HGB. The consolidated financial statements have been prepared in order to satisfy the admission requirements of the Neuer Markt.

The consolidated financial statements also reflect the standards approved by German Accounting Standards Board (GASB) and published by the German Federal Ministry of Justice pursuant to Art. 342, (2), HGB.

The comdirect sub-group is included in the consolidated financial statements of our parent company. The consolidated financial statements of Commerzbank as of 31 December, 2000 were deposited with the lower regional court (Amtsgericht) of Frankfurt am Main under the commercial register no. 32000 and published in the Federal Gazette, no. 111, page 660977 of 20 June, 2001.

We report on both the implementation of the German legislation for control and transparency in the corporate sector (KonTraG) and on the risks posed by future development, pursuant to Art. 315, (1), HGB in the risk report.

In addition to the income statement and the balance sheet, the consolidated financial statements also include the statement of changes in equity, a cash flow statement and the notes. Segment reporting appears as part of the notes, on page 77.[2]

Unless otherwise indicated,all the amounts are shown in thousands of euros.

Accounting and measurement methods

(1) Basic principles

The consolidated financial statements of comdirect are based on the going concern principle.

For our subsidiaries in France (comdirect S.A., Paris/France) and Italy (comdirect bank S.p.A., Milan/Italy), no selling agreement had been signed or the liquidation of the company in question had not been completed by the day on which the balance sheet and income statement were prepared. In view of the decisions taken by the majority shareholder, we have not applied the going concern principle to these subsidiaries.

The principle of profit or loss for the period is applied in our consolidated financial statements. Income and expenses are recognised on a pro-rata basis; they are shown for the period to which they may be assigned in economic terms.

As a matter of principle, accounting is at net book value, with the exception of financial instruments as defined by IAS 39, which are shown at their fair value. These financial instruments appear under the items Trading assets and Financial investments.

All the companies included in the consolidation prepared their financial statements as of 31 December 2001.

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(1) For the purposes of this filing, please refer to page A-136.
(2) For the purposes of this filing, please refer to page A-153.

(2) IAS, SIC and GASB rules applied

Within the comdirect Group and within the Commerzbank Group, to which it belongs, only those IASs and SICs are applied for accounting and measurement purposes which had been approved and published by 31 December, 2001.

The interpretation of the standard with regard to Consolidation — Special purpose entities — (SIC-12) was not applied, as no holdings existed on the balance-sheet date.

The follow list provides a summary of the International Accounting Standards (IASs) applied in comdirect's 2001 consolidated financial statements.

IAS 1	Presentation of financial statements
IAS 7	Cash flow statements
IAS 8	Net profit or loss for the period, fundamental errors and changes in accounting policies
IAS 10	Events after the balance-sheet date
IAS 12	Income taxes
IAS 14	Segment reporting
IAS 16	Property, plant and equipment
IAS 17	Leases
IAS 18	Revenue
IAS 19	Employee benefits
IAS 21	The effects of changes in foreign-exchange rates
IAS 22	Business combinations
IAS 24	Related party disclosures
IAS 26	Accounting and reporting by retirement benefit plans
IAS 27	Consolidated financial statements and accounting for investments in subsidiaries
IAS 30	Disclosures in the financial statements of banks and similar financial institutions
IAS 32	Financial instruments: disclosure and presentation
IAS 33	Earnings per share
IAS 35	Discontinuing operations
IAS 36	Impairment of assets
IAS 37	Provisions, contingent liabilities and contingent assets
IAS 38	Intangible assets
IAS 39	Financial instruments: recognition and measurement

In addition, we provide a list below of the SIC interpretations relevant for us, which we have taken into consideration in our 2001 consolidated financial statements.

		relates to:
SIC-6	Costs of modifying existing software	Framework
SIC-7	Introduction of the euro	IAS 21
SIC-15	Operating leases — incentives	IAS 17
SIC-17	Equity costs of an equity transaction	IAS 32
SIC-18	Consistency — alternative methods	IAS 1

(3) Consolidated companies

Apart from the parent company, the consolidated companies consist of three subsidiaries, so that altogether four companies were included in our consolidated financial statements. comdirect bank AG holds over 50% of the capital of each subsidiary directly. A detailed presentation of holdings appears on page 80.[3]

(3) For the purposes of this filing, please refer to page A-156.

(4) Principles of consolidation

The consolidation of the capital accounts is based on the book-value method,whereby the historical cost of the shares held by the parent company in each individual subsidiary and the share of each subsidiary's capital held by the parent company are set off against the proportion of the subsidiary's equity that was acquired.

On principle, any residual positive differences in amount are shown as goodwill under intangible assets in the balance sheet and depreciated to reflect their probable economic lives over a period of 15 years, using the straight-line method.

Ordinary amortisation of goodwill are included in other operating results and the extraordinary amortisation of goodwill are included in extraordinary result and restructuring expenses. We draw attention to the remarks on Intangible assets on page 69.(4)

Intra-group expenses and income, as well as claims and liabilities, are eliminated as part of the consolidation.

Minority shares in equity and profit or less are shown separately as minority interests and as profit/loss attributable to minority interests.

As part of our efforts to sell comdirect S.A., Paris/France,we purchased the shares held by outside shareholders as of January 2002, raising our interest in the company to 100%.

(5) Changes in accounting and disclosure methods

IAS 39 was applied at Group level for the first time for the 2001 financial year. As this standard may not be applied retrospectively all by itself, the year-ago figures have not been adjusted.

The quarterly reports published by comdirect in 2001 already incorporated aspects of IAS 39.

IAS 39 regulates how financial instruments are treated in the balance sheet, and especially their recognition and measurement.

All financial instruments, including all financial derivatives, are shown using the "trade date accounting" method.

Throughout the Group, all financial instruments are assigned exclusively either to the "available for sale" or "trading" categories.

The "available for sale" category includes all the bonds, other fixed-income securities and also equities and other variable-yield securities not held for trading purposes.

Securities from the trading portfolio and unsecured derivative financial instruments are assigned to the trading category.

As part of the first-time application of IAS 39, we have adjusted the opening balance sheet to recognise the valuation differences for derivative financial instruments due to the book value approach and the current values to be attributed, and to show these within equity under retained earnings, taking deferred taxes into account.

Taking deferred taxes into account, we have recognised valuation differences arising from other financial instruments under equity in the item revaluation reserve. As of end-2001, the revaluation reserve amounted to € 1,083 thousand.

As of 31 December, 2001, we measured all the financial instruments in the "available for sale" and "trading" categories at market prices in active markets.

The profits generated by the disposal or maturing of financial instruments assigned to the "available for sale" category amounted to altogether € 350 thousand as of 31 December, 2001. The corresponding losses came to € 6 thousand.

The interest income generated by the financial instruments assigned to the "available for sale" category amounted to € 61,732 thousand at end-2001.

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(4) For the purposes of this filing, please refer to page A-147.

(6) Currency translation

The items from the income statement and also the assets and liabilities from the balance sheet which are denominated in foreign currencies are translated at the spot rates of the balance-sheet date.

Holdings in affiliated companies that are denominated in foreign currencies appear at historical cost.

comdirect nets translation gains and losses from the consolidation of the capital accounts against retained earnings.

The annual financial statements prepared by our subsidiaries in foreign currencies are translated at the spot rates of the balance-sheet date. Any income and expenses resulting from translation appear in the income statement.

The most important translation rates for the comdirect Group can be found in the table below:

Unit/1 €	31.12.2001 (unaudited)	31.12.2000 (unaudited)
GBP	0.6085	0.6241
FRA	6.55957	6.55957
ITL	1,936.27	1,936.27

(7) Claims

All claims on banks and customers are shown at amortised cost without valuation allowances.

Valuation allowances to claims appear under provisions for possible loan losses.

On the balance-sheet date, we had no acquired claims, i.e. sections of a credit originated by another lender, in our portfolio.

(8) Provisions for possible loan losses

Valuation allowances, in the form of individual and lump-sum valuation allowances, are formed exclusively for claims on customers.

Throughout the Group, the relevant individual valuation allowances are formed on the scale of the potential default to cover credit-standing risks related to claims on customers.

We cover latent credit risks by means of lump-sum valuation allowances. Past loan losses serve as a yardstick for the scale on which such lump-sum valuation allowances have to be formed.

Unrecoverable accounts are written down immediately. Amounts received on such claims appear in the income statement. Claims are deemed unrecoverable if income from them is unlikely to be received in the foreseeable future or if they have been waived either wholly or in part.

(9) Trading assets

Securities acquired as part of the small trading portfolio and derivative financial instruments (swaps) appear under Assets held for dealing purposes.

On the balance-sheet date, only interest-rate swaps measured at fair value were included under this item.

Realised gains and losses from the purchase and sale of securities from the small trading portfolio are shown in the income statement under Trading profit.

Gains or losses registered upon remeasurement of the derivative financial instruments are also included in the Trading profit.

The Trading profit also reflects all the interest and dividend income arising from the trading portfolio.

(10) Financial investments

Under Financial investments, we show all the securities which we have assigned to the "available for sale" category.

On the balance-sheet date, bonds and other fixed-income securities as well as investment fund units were assigned to the ''available for sale'' category.

All the securities of this category were measured at their fair value.

Gains or losses on remeasurement are recognised with an income-neutral effect in the form of a revaluation reserve as part of equity.

All the interest income generated by securities of the ''available for sale'' category is shown under Interest received.

(11) Intangible assets

Under Intangible assets, we include software produced in-house and Goodwill. Purchased software is shown under Fixed assets.

More details can be found under Changes in book value of fixed assets and investments (page 70,[5] note 39).

Software produced in-house is recognised if all the provisions of IAS 38 are met. Recognition is made at producer cost, reflecting only the costs that can be assigned directly to the specific project.

In principle software produced in-house is amortised against earnings over a period of five years.

The goodwill created by the acquisition of comdirect S.A. was examined on the balance-sheet date with regard to its future utility.

We have found that under existing conditions no future utility can be expected. As a result, we made an extraordinary write-down of € 25,924 thousand in the year under review.

The extraordinary write-down is shown in the income statement under Extraordinary result and restructuring expenses.

(12) Fixed assets

Only office furniture and equipment and purchased software are included here.

All the fixed assets are capitalised at cost and depreciated using the straight-line method to reflect their probable useful economic lives.

In determining the useful life of an asset, its likely physical wear and tear, its technical obsolescence and also legal restrictions are taken into consideration. All fixed assets are de-preciated over a period of two to ten years.

Gains and losses arising from the sale of fixed assets are shown in the income statement under Other operating result.

We made extraordinary depreciation on fixed assets in the year under review when the amount that could probably be achieved through future use had fallen below their book value.

(13) Other assets

Other assets mainly consist of other assets on Commerzbank AG and deferred items.

(14) Liabilities

Liabilities are shown at the respective amounts to be repaid.

(15) Other liabilities

Other liabilities consist primarily of trade liabilities, liabilities to Commerzbank AG not arising from banking activities, tax liabilities not related to earnings and accruals.

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(5) For the purposes of this filing, please refer to page A-148.

(16) Provisions for pensions and similar commitments

The pension commitments that are shown exist solely towards members of the Board of Managing Directors of comdirect bank AG. These are based on the length of service, the pensionable salary and the currently valid scales for employer subsidies.

In accordance with IAS 19, the projected-unit-credit method was used to calculate pension commitments.

Commitments are calculated on the basis of actuarial surveys. The calculation also takes into account the rates of increase for salaries and pensions that can be expected in the future.

If actuarial commitments prove to be higher or lower, these are recognised under Personnel costs.

(17) Other provisions

Other provisions were formed for liabilities of uncertain amount towards third parties.

In addition, we have formed provisions for contingent losses for existing adverse agreements, in which the expense required in order to fulfil the agreement is greater than the income generated by the agreement.

We formed the major provisions for contingent losses on account of restructuring measures, i.e. due to the sale or closure of our subsidiaries in France and Italy.

(18) Taxes on income

Tax expenses are shown under Taxes on income. A breakdown of this item into current and deferred taxes on income can be found in these notes on page 66[(6)], note 30.

Deferred taxes were formed in accordance with IAS 12. Temporary differences are the result of the discrepancy between assigned values in accordance with IAS and the respective tax rate that was applied. These temporary differences are measured using the specific income-tax rates which apply in the country where the company in question has its seat and which can be expected to apply for the period in which they are realised. Deferred taxes on as yet unused losses carried forward are only shown for comdirect bank AG. Deferred taxes on losses carried forward formed in previous years have been released.

Deferred tax assets and liabilities are netted against one another in Germany, as they exist towards the same tax authority.

Claims on tax authorities are shown under Tax assets in the balance sheet.

Other taxes not related to income appear under Other operating result in the income statement.

When the profit-and-loss-transfer agreement was terminated on 31 December, 1999, it was assumed — with the agreement of the tax authorities — that, for accounting purposes, the integrated inter-company relationship between comdirect bank AG and Commerzbank AG had ceased to exist. In a final judgement, however, it was decided that this relationship continued to exist as regards turnover and trade tax for the 2000 and 2001 assessment periods. As a result of the amendments to Germany's legislation on the further development of corporate taxation, the fiscal unity in terms of trade tax ended on 31 December, 2001; and was maintained only with regard to turnover tax as from 2002.

(19) Conditional and authorised capital

Through the resolution adopted on 10 April, 2000, and its entry into the commercial register on 19 April, 2000, authorised capital of € 60,000 thousand was created. The authorisation for the capital increase expires on 31 March, 2005.

In addition, since the resolution adopted on the same date and entered into the commercial register on 31 May, 2000, conditional capital of € 3,600 thousand was created in order to issue subscription rights as part of the bank's stock option scheme.

(6) For the purposes of this filing, please refer to pages A-144 to A-145.

(20) Transfer from reserves

In connection with decisions relating to our subsidiaries in Italy and France in the 2001 financial year, we have transferred a net € 160,657 thousand from reserves in order to cover the accumulated losses.

(21) Earnings per share

Earnings per share calculated in accordance with IAS 33 are based on the net profit/loss for the year. We show both the undiluted and the diluted earnings per share below the income statement.

In working out the undiluted result, we have set off the net profit/loss for the year against the average number of shares in the financial year.

The diluting effects result from a stock option scheme launched in July 2000 with a maximum of 3,600,000 subscription rights, 875,000 option rights of which had been issued in two tranches per 31 December, 2001.

In calculating the diluting effects, we set off the two sub-sets of rights under the stock option scheme with their conditions against well-founded estimated values for them and took account of the residual amount.

The nominal value per share is 1 euro.

(22) Relations with affiliated companies

comdirect uses services provided by Commerzbank AG through a general agreement concluded in December 1999 (and effective as from 1 January, 1999) and also services agreed separately on this basis.

The general agreement has a fixed term of five years and ends on 31 December, 2003. It is automatically extended for a further period of three years, unless one of the parties to the agreement gives notice at least 18 months before the agreement expires.

On the basis of the general agreement, the following services were agreed upon and were used during the 2001 financial year:

- Trading services
- Processing services
- Payments and cash dispenser service
- IT services
- Other services

In February 2000, comdirect concluded another general agreement with Commerzbank, in which Commerzbank undertook to provide internal auditing services on the basis of a plan to be agreed separately. The agreement was concluded for an indefinite period and may be terminated giving six months' notice before the end of the calendar year, but not before 31 December, 2002.

comdirect is party to an agreement of Commerzbank with Commerzbank Capital Markets, enabling comdirect to trade on US stock exchanges.

On 22 March, 2000, comdirect concluded an agreement with Commerzbank concerning support for comdirect after its IPO. Among other things, the agreement relates to support for PR activities, compliance with stock-exchange and other obligations resulting from admission to the stock exchange and advice on the holding of the first public annual general meeting of shareholders in 2001.

Commerzbank received compensation in line with market rates for the goods and services it provides for comdirect.

When forming or purchasing subsidiaries, comdirect pledged directly or indirectly to ensure that they comply with the specific equity capital requirements of the country in question.

In this connection, comdirect allocated equity of € 39,978 thousand to comdirect S.A., Paris/France, in the 2001 financial year.

Over the same period, comdirect bank S.p.A, Milan/Italy, was allocated € 20,800 thousand.

comdirect ltd, London/United Kingdom, received equity of € 12,356 thousand in the 2001 financial year.

(23) Net interest income

	2001	2000
	(€ thousand) (unaudited)	
Interest and dividends from shares and other non-fixed interest securities held in the "available for sale" portfolio	18,589	4,876
Interest income from fixed-income securities held in the "available for sale" portfolio and from government-inscribed debt	43,143	35,485
Other interest income including discount surplus	76,889	80,685
Interest on participation rights and subordinate liabilities	(1,050)	(1,491)
Other interest expenses	(63,488)	(61,838)
Total	**74,083**	**57,717**

(24) Provision for possible loan losses

The provisions of the comdirect Group breaks down as follows:

	2001	2000
	(€ thousand) (unaudited)	
Allocations to provisions	(4,215)	(2,151)
Write-back of provisions	2,356	211
Direct write-downs	(222)	(37)
Income received on written-down claims	7	11
Total	**(2,074)**	**(1,966)**

(25) Net commission income

	2001	2000
	(€ thousand) (unaudited)	
Securities transactions	89,316	189,172
Payment transactions	3,335	1,408
Other commissions	367	283
Total	**93,018**	**190,863**

(26) Trading profit

All the financial instruments assigned to the Assets held for dealing purposes are measured at fair value. The results arising from trading activities are included along with interest and dividend income, attributable to instruments shown under Assets held for dealing purposes, in the Trading profit.

	2001	2000
	(€ thousand) (unaudited)	
Result of securities trading	**(332)**	**(133)**
Result from trading in bonds and notes	9	0
Result from trading in shares and other non-fixed interest securities	(341)	(133)
Other trading result	**(726)**	**0**
Result from trading in interest-rate risks	(726)	0
Valuation result	**1,029**	**0**
Interest-rate derivatives	1,029	0
Total	**(29)**	**(133)**

(27) Administrative expenses

Personnel expenses

	2001	2000
	(€ thousand) (unaudited)	
Wages and salaries	(42,484)	(36,170)
Compulsory social-security contributions	(8,398)	(6,739)
Expenses for pensions and other employee benefits	(550)	(604)
Total	**(51,432)**	**(43,513)**

Breakdown of expenses for pensions and other employee benefits

	2001	2000
	(€ thousand) (unaudited)	
Costs of company pension scheme	(535)	(594)
Contributions to Versicherungsverein des Bankengewerbes a.G. (BVV)	(15)	(10)
Total	**(550)**	**(604)**

General operating expenses

	2001	2000
	(€ thousand) (unaudited)	
Costs of advertising, PR and representation	(55,356)	(59,148)
Communication expenses	(16,552)	(19,929)
Consulting expenses	(12,510)	(22,105)
External services	(28,992)	(38,675)
Other general operating expenses	(30,769)	(19,305)
Total	**(144,179)**	**(159,162)**

The expenses for operating lease contracts are considered as rental expenses and included in the other general operating expenses.

Depreciation of office furniture and equipment and intangible assets

	2001	2000
	(€ thousand) (unaudited)	
Office furniture and equipment	(23,986)	(15,677)
Intangible assets	(4,720)	(2,599)
Total	**(28,706)**	**(18,276)**

(28) Other operating result

The Other operating result primarily comprises income from tax consolidations, income from recoverable input taxes and income from the writing-back of provisions. Other details on taxes and tax consolidation can be found in these notes on page 60 ff.[7]

	2001	2000
	(€ thousand) (unaudited)	
Other operating expenses	**(6,146)**	**(5,768)**
Payments to settle customers' complaints/provisions for process risks in direct brokerage business	(2,305)	(3,288)
Depreciation of goodwill	(2,043)	(1,761)
Sundry expense items	(1,798)	(719)
Other operating income	**12,805**	**5,803**
Income from recoverable input taxes	2,630	3,810
Income from the writing-back of provisions and accruals	1,465	487
Income from tax consolidation	4,153	0
Sundry income items	4,557	1,506
Total	**6,659**	**35**

(29) Extraordinary result and restructuring costs

Due to restructuring decisions relating to our subsidiaries, the comdirect bank Group's extraordinary result and restructuring costs comprises the following expenses and income:

	2001	2000
	(€ thousand) (unaudited)	
Extraordinary expenses	**(98,340)**	**0**
extraordinary depreciation of goodwill	(25,924)	0
extraordinary depreciation on investments	(10,500)	0
extraordinary depreciation on intangible and fixed assets	(21,196)	0
Restructuring costs (especially personnel costs and expenses arising from current contracts)	(21,575)	0
Costs of disposal/liquidation	(17,398)	0
Sundry expenses	(1,747)	0
Extraordinary income	**76**	**0**
Proceeds from disposal	76	0
Total	**(98,264)**	**0**

All the effects on net profit of the closure of comdirect S.p.A. and the disposal of comdirect S.A. are included in this item.

(30) Taxes on income

	2001	2000
	(€ thousand) (unaudited)	
Current taxes on income	(906)	32,048
Deferred taxes	10,983	(8,677)
Total	**10,077**	**23,371**

(7) For the purposes of this filing, please refer to page A-140.

Transitional presentation of income taxes

	2001
	(€ thousand) (unaudited)
Profit from ordinary activities	**(150,580)**
multiplied by the German income tax rate of 36.93%	
= calculated income-tax expenses in part financial year	(55,609)
– effects of different domestic tax rates on current income taxes and deferred taxes	623
– effects of different income-tax rates in the various countries where group companies based	2,109
+ amortisation of goodwill	10,311
+ effects of taxes on income in previous years	2,149
+ effects due to extraordinary results	75,392
+ effects on deferred taxes on losses carried forward	8,816
– effect of consolidation measures	27,586
– other causes	664
Total	**10,077**

(31) Cash reserve

Cash reserve breaks down as follows:

	31.12.2001	31.12.2000
	(€ thousand) (unaudited)	
Cash on hand	232	131
Balances with central banks	71,773	384
Total	**72,005**	**515**

The minimum reserve requirement to be met at the end of December 2001 totalled € 44,756 thousand (2000: € 40,690 thousand).

(32) Claims on banks

	Total		Due on demand		Other claims	
	31.12.2001	31.12.2000	31.12.2001	31.12.2000	31.12.2001	31.12.2000
			(€ thousand) (unaudited)			
German banks	1,600,166	959,357	1,098,541	291,935	501,625	667,422
Foreign banks	83,946	47,120	46,446	47,120	37,500	0
Total	**1,684,112**	**1,006,477**	**1,144,987**	**339,055**	**539,125**	**667,422**

Claims on banks include foreign-currency amounts equal to € 39,310 thousand (2000: € 15,535).

Claims on banks primarily consist of overnight money and fixed deposits (€ 1,634,874 thousand/2000: € 964,015 thousand, incl. "occurred interest").

(33) Claims on customers

Claims on customers consist of:

	Total		Due on demand		Other claims	
	31.12.2001	31.12.2000	31.12.2001	31.12.2000	31.12.2001	31.12.2000
			(€ thousand) (unaudited)			
Claims on domestic customers	**261,293**	**571,294**	**261,293**	**561,265**	**0**	**10,029**
Public-sector entities	0	10,029	0	0	0	10,029
Private customers	261,293	561,265	261,293	561,265	0	0
Claims on foreign customers	**2,435**	**4,230**	**2,435**	**4,230**	**0**	**0**
Private customers	2,435	4,230	2,435	4,230	0	0
Total	**263,728**	**575,524**	**263,728**	**565,495**	**0**	**10,029**

All claims on private customers are deemed to be due on demand. Claims on customers include € 250,603 thousand (2000: € 548,127 thousand) from loans to finance purchases of securities. These claims are loans secured by securities. In view of the concentration of loans, we point out that the original loan business is carried out with private customers only. Claims on customers include foreign-currency amounts equal to € 75 thousand (2000: € 15 thousand).

(34) Provision for possible loan losses

	Credit default risks		General provisions		Total	
	31.12.2001	31.12.2000	31.12.2001	31.12.2000	31.12.2001	31.12.2000
			(€ thousand) (unaudited)			
Balance 1 January	(3,149)	(1,254)	(31)	(31)	(3,180)	(1,285)
Allocations	(4,215)	(2,151)	0	0	(4,215)	(2,151)
Deductions	2,459	256	0	0	2,459	256
of which utilised	103	45	0	0	103	45
of which written back	2,356	211	0	0	2,356	211
Exange-rate changes	0	0	0	0	0	0
Provision for possible loan losses as of 31 December	**(4,905)**	**(3,149)**	**(31)**	**(31)**	**(4,936)**	**(3,180)**

The adjusted value of non-interest bearing non-productive claims amounts to € 4,943 thousand (2000: € 3,268 thousand).

The comdirect Group made a direct write-down of € 222 thousand (2000: € 37 thousand) and recorded receipts on written-down claims in an amount of € 7 thousand (2000: € 11 thousand).

The total balance of risk provisions for credit default risks breaks down as:

	31.12.2001	31.12.2000
	(€ thousand) (unaudited)	
German borrowers	(4,831)	(3,137)
Foreign borrowers	(74)	(12)
Total	**(4,905)**	**(3,149)**

(35) Trading assets

Under this item, financial instruments acquired as part of the small trading portfolio are shown at fair value. In addition,derivative financial instruments assigned to trading with positive fair values and interest for the respective period appear here.

	31.12.2001	31.12.2000
	(€ thousand) (unaudited)	
Shares and other non-fixed interest	**1,226**	**883**
Shares	0	883
German securities	0	636
Foreign securities	0	247
Other non-fixed interest securities	1,226	0
Positive market value attributable to derivate financial instruments	**938**	**0**
Interest-rate derivatives	938	0
Total	**2,164**	**883**

There were no restrictions on the disposal of any of the trading assets as of the balance sheet date.

(36) Financial investments

All the financial instruments shown under Financial investments are assigned to the "available for sale" category and are measured at fair value.

	31.12.2001	31.12.2000
	(€ thousand) (unaudited)	
Bonds and other fixed-income securities of the "available for sale" portfolio	840,719	910,943
Bonds and notes	840,719	910,943
issued public-sector borrowers	0	0
issued by other borrowers	840,719	910,943
Investments	0	10,500
Shares and other non-fixed interest securities of the "available for sale" portfolio	20,493	231,796
Holdings in subsidiaries	0	0
Total	**861,212**	**1,153,239**

There were no restrictions on the disposal of any of the financial assets as of the balance-sheet date.

Through a resolution of 31 December, 2001 the Wiesbaden lower regional court opened bankruptcy proceedings against the assets of Censio AG. We no longer expect a repayment of capital. For this reason, comdirect bank AG entirely wrote its investment in 2001. The impact of this write-off on the bank's net profit and loss is shown under the position Extraordinary result and restructuring costs.

On the balance-sheet date, no write-downs were made due to permanent impairment on financial instruments measured at fair value.

(37) Intangible assets

	31.12.2001	31.12.2000
	(€ thousand) (unaudited)	
Goodwill	0	27,052
Other intangible assets	22,076	13,898
Total	**22,076**	**40,950**

Changes in fixed assets are shown in schedule of assets (page 70(8), note 39).

(38) Fixed assets

	31.12.2001	31.12.2000
	(€ thousand) (unaudited)	
Office and furniture equipment	**45,816**	**76,335**

Changes in fixed assets are shown in schedule of assets (page 70(8), note 39).

(39) Schedule of assets

	Fixed assets		Intangible assets		
	Software	Other	Other	Goodwill	Investments
			(€ thousand) (unaudited)		
Book value as of 1 January 2001	**10,705**	**65,630**	**13,898**	**27,052**	**10,500**
Costs of acquisition/manufacture as of 1 January 2001	17,919	89,213	20,841	28,813	10,500
Additions 2001	5,344	10,041	12,898	915	0
Disposals 2001	(2,065)	(910)	0	0	0
Costs of acquisition/manufacture as of 31 December 2001	21,198	98,344	33,739	29,728	10,500
Cumulative write-downs as of 1 January 2001	7,214	23,583	6,943	1,761	0
Additions 2001	9,173	36,067	4,720	27,967	10,500
Disposals 2001	(826)	(1,485)	0	0	0
Cumulative write-downs as of 31 December 2001	15,561	58,165	11,663	29,728	10,500
Book value as of 31 December 2001	**5,637**	**40,179**	**22,076**	**0**	**0**

Additions to write-downs in 2001 relate to extraordinary write-downs of € 57.620 thousand. These are spread between the items goodwill, investments,fixed assets and intangible assets.

(40) Other assets

	31.12.2001	31.12.2000
	(€ thousand) (unaudited)	
Deferred items	5,693	1,211
Sundry assets	12,507	14,472
Total	**18,200**	**15,683**

Sundry assets comprise the following items:

	31.12.2001	31.12.2000
	(€ thousand) (unaudited)	
Claims on affiliated companies	8,494	9,446
Other	4,013	5,026
Total	**12,507**	**14,472**

(8) For the purposes of this filing, please refer to page A-148.

(41) Liabilities to banks

	Total		Due on demand		Other liabilities	
	31.12.2001	31.12.2000	31.12.2001	31.12.2000	31.12.2001	31.12.2000
	(€ thousand) (unaudited)					
German banks	0	1,918	0	0	0	1,918
Foreign banks	0	1,760	0	0	0	1,760
Total	0	3,678	0	0	0	3,678

(42) Liabilities to customers

	Total		Due on demand		Other liabilities	
	31.12.2001	31.12.2000	31.12.2001	31.12.2000	31.12.2001	31.12.2000
	(€ thousand) (unaudited)					
Liabilities to domestic private customers	2,196,023	2,011,316	2,150,113	1,999,863	45,910	11,453
Liabilities to foreign private customers	93,304	33,238	92,433	32,979	871	259
Total	**2,289,327**	**2,044,554**	**2,242,546**	**2,032,842**	**46,781**	**11,712**

Foreign-currency amounts equal to € 28,846 thousand (2000: € 2,550 thousand).

Through the deposit insurance scheme of the Association of German Banks, Cologne, each customer of comdirect bank AG is insured for deposits of up to € 233 millions.

In addition,comdirect bank AG is a member of Entschädigungseinrichtung deutscher Banken GmbH.

(43) Provisions

	31.12.2001	31.12.2000
	(€ thousand) (unaudited)	
Provisions for pensions and similar commitments	1,775	1,337
Other provisions	49,576	4,391
Total	**51,351**	**5,728**

The changes in provisions for pensions were as follows:

	as of 1.1.2001	Utilised/ change	Depreciation	Allocation	as of 31.12.2001
	(€ thousand) (unaudited)				
Pension expectancies of active employees	1,337	0	0	438	1,775

The allocations to pension provisions in 2001 break down as follows:

Service cost	312 € (thousand)
Interest cost	95 € (thousand)
Cost arising from changes in actuarial assumptions	2 € (thousand)

In the 2001 financial year, comdirect bank AG took over pension provisions of € 29 thousand due to staff recruitment.

Actuarial gains and losses are amortised over three years (2001:2 € thousand).

Parameters	31.12.2001 (unaudited)	31.12.2000 (unaudited)	31.12.1999 (unaudited)
Calculatory interest rate	5.75%	6.50%	5.75%
Changes in salaries	3.00%	3.50%	3.00%
Changes in pensions	1.50%	2.00%	2.00%

Changes in other provisions:

	as of 1.1.2001	Utilised	Depreciation	Allocation	as of 31.12.2001
			(€ thousand) (unaudited)		
Provisions for staff	2,277	1,757	324	2,033	2,229
Provisions for anniversary bonuses	87	33	45	32	41
Provisions for non-income-related taxes	145	0	0	877	1,022
Provisions for contingent losses	0	0	0	44,234	44,234
Other provisions	1,882	851	815	1,834	2,050
Total	**4,391**	**2,641**	**1,184**	**49,010**	**49,576**

Provisions for staff mainly relate to provisions for bonuses. The provisions for staff will probably be used in the 2002 financial year.

Changes in provisions for contingent losses break down as follows:

	as of 1.1.2001	Utilised	Depreciation	Allocation	as of 31.12.2001
			(€ thousand) (unaudited)		
Provisions for contingent losses	**0**	**0**	**0**	**44,234**	**44,234**
Restructuring	0	0	0	39,890	39,890
Other	0	0	0	4,344	4,344

The scale of the contingent losses for restructuring was measured on the basis of the information expected expenses that were available when the financial statements were prepared.

(44) Tax liabilities

Tax liabilities are comprised as follows:

	31.12.2001	31.12.2000
	(€ thousand) (unaudited)	
Current tax liabilities	**5,683**	**7,287**
Provisions for income taxes	5,683	7,287
Deferred tax liabilities	**4,761**	**3,507**
Total	**10,444**	**10,794**

The provision for taxes on income includes tax liabilities for which no final formal assessment note has been received. Deferred taxes are attributable to temporary differences between the values assigned to assets and liabilities in the balance sheet according to IAS and the balance sheets prepared by Group companies in accordance with local tax provisions.

Deferred tax liabilities were created in connection with the following balance sheets accounts:

	31.12.2001	31.12.2000
	(€ thousand) (unaudited)	
Provision for possible loan losses	23	23
Trading assets	347	0
Financial investments	2,300	(1,559)
Intangible assets	7,575	5,237
Fixed assets	(68)	0
Provisions	(2,226)	(194)
Equity	(3,190)	0
Total	**4,761**	**3,507**

The domestic income tax rate used to compute deferred taxes is composed of the applicable tax rates effective in Germany for corporate income tax (25.0%), plus the solidarity surcharge (5.5%) and the trade tax (14.3%) taken together. This yields a domestic income tax rate of 36.93%.

(45) Subordinated capital

	31.12.2001	31.12.2000
	(€ thousand) (unaudited)	
Subordinated liabilities	6,391	6,391
Profit-sharing certificates outstanding	10,226	23,008
Total	**16,617**	**29,399**

The subordinated capital (€ 16,617 thousand) meets the requirements of supplementary capital as defined by Art. 10, paragraph 5(a) of the German Banking Act. The claims of creditors to repayment of these liabilities are subordinate to those of other creditors.

Terms of subordinated liabilities:

Start of maturity (unaudited)	Amount € thousand	Interest rate per 31.12.2001	Maturity date
1996	6,391	3.549%	2006

The interest rate on subordinated liabilities is fixed for three years from the beginning of the period, after which the interest rate is adjusted annually.

During the financial year, comdirect incurred interest expenses on subordinated liabilities of € 317 thousand (2000: € 270 thousand).

Interest is paid only insofar as such payments do not lead to an accounting loss. The claims of the holders of the profit-sharing certificates are subordinated to the claims of other creditors.

Terms of the profit-sharing certificates:

Start of maturity (unaudited)	Amount € thousand	Interest rate per 31.12.2001	Maturity date
1998	10,226	6.000%	2006

During the financial year comdirect incurred interest expenses on profit-sharing certificates of € 733 thousand (2000: € 1,221 thousand). This includes also interest expenses for profit-sharing certificates of € 12,782 thousand, which was repaid in 2001. As a net loss for the year is shown, the interest payment for the current profit-sharing right will not be made in the 2002 financial year.

(46) Maturities, by remaining lifetime

	Remaining lifetimes as of 31.12.2001					
	Total	Due on demand and unlimited in time	Up to three months	Three months to one year	One to five years	More than five years
			(€ thousand) (unaudited)			
Claims on banks	1,684,112	1,144,987	339,125	50,000	150,000	0
Claims on customers	263,728	263,728	0	0	0	0
Bonds and notes held in the available for sale portfolio	840,719	20,873	51,362	163,860	501,083	103,541
Total	**2,788,559**	**1,429,588**	**390,487**	**213,860**	**651,083**	**103,541**
Liabilities to banks	0	0	0	0	0	0
Liabilities to customers	2,289,327	2,242,546	20,052	24,844	1,885	0
Subordinated capital	16,617	0	0	0	16,617	0
Total	**2,305,944**	**2,242,546**	**20,052**	**24,844**	**18,502**	**0**

	Remaining lifetimes as of 31.12.2000					
	Total	Due on demand and unlimited in time	Up to three months	Three months to one year	One to five years	More than five years
			(€ thousand) (unaudited)			
Claims on banks	1,006,477	339,049	414,620	102,559	150,249	0
Claims on customers	575,524	565,495	10,029	0	0	0
Bonds and notes — held as financial investments	910,943	0	99,423	269,574	459,608	82,338
Total	**2,492,944**	**904,544**	**524,072**	**372,133**	**609,857**	**82,338**
Liabilities to banks	3,678	3,678	0	0	0	0
Liabilities to customers	2,044,554	2,032,842	5,019	4,729	1,964	0
Subordinated capital	29,399	12,782	0	0	0	16,617
Total	**2,077,631**	**2,049,302**	**5,019**	**4,729**	**1,964**	**16,617**

(47) Claims on/liabilities to affiliated companies

	31.12.2001	31.12.2000
	(€ thousand) (unaudited)	
Claims on banks	754,471	501,358
Liabilities to banks	0	3,678
Subordinated capital	16,617	29,399
Total	**771,088**	**534,435**

(48) Interest-rate risks

	Fixed-interest assets		Fixed-interest liabilities		Fixed-interest gap	Interest differential
	€ million	interest in %	€ million	interest in %	€ million	% points
	(unaudited)		(unaudited)		(unaudited)	
Up to one year	2,704	4.00	2,524	1.88	(180)	2.12
One to five years	258	4.42	765	4.08	507	(0.34)
More than five years	20	5.25	17	5.60	(3)	(0.35)

(49) Number of employees at the end of the reporting period

	31.12.2001 (unaudited)	31.12.2000
Group	1,291	1,536
in Germany	1,117	1,387
abroad	174	149
At comdirect bank AG	**1,117**	**1,387**
of which:		
in the call centre	517	854
in the back office	317	303
in other areas	283	230

(50) Segment reporting

Segment reporting by geografical markets:

	comdirect Germany	comdirect Europe, excluding Germany	Group management/ others/ consolidation	comdirect bank group total
	(€ thousand) (unaudited)			
Net interest income before provisions	72,610	1,473	0	74,083
Provision for possible loan losses	(2,074)	0	0	(2,074)
Net interest income after provisions	70,536	1,473	0	72,009
Net commission income	91,719	1,299	0	93,018
Trading profit	(29)	0	0	(29)
Result from the securities portfolio (available for sale)	344	0	0	344
Administrative expenses	159,767	64,550	0	224,317
Other operating result	9,241	(786)	(1,796)	6,659
Profit from ordinary activities	**12,044**	**(62,564)**	**(1,796)**	**(52,316)**
Extraordinary result and restructurings costs	(215,311)	(28,204)	145,251	(98,264)
Pre-tax profit	**(203,267)**	**(90,768)**	**143,455**	**(150,580)**
Taxes on income	1,261	8,816	0	10,077
After-tax profit	**(204,528)**	**(99,584)**	**143,455**	**(160,657)**
Profit/loss attributable to minority interests	0	0	0	0
Net income/Net loss	**(204,528)**	**(99,584)**	**143,455**	**(160,657)**
Acquisition costs of segment assets	**16,425**	**12,773**		**29,198**
Depreciation of segment assets	**20,248**	**8,458**		**28,706**
Cost/Income ratio	**0.9206**	**32.5025**		**1.2912**
Segment earnings	**241,633**	**6,474**	**247**	**248,354**
Segment expenses	**229,933**	**69,038**	**2,043**	**301,014**
Segment assets	**1,932,769**	**92,304**	**(8,000)**	**2,017,073**
Segment debts	**2,252,532**	**44,795**	**(8,000)**	**2,289,327**

Allocation to the segments is based on the domicile of the subsidiaries or the consolidated company.

(51) Other liabilities

Rental and leasing agreements concluded by comdirect will lead to expenses of € 7,074 thousand during the 2002 financial year, € 9,216 thousand for each of the years 2003 to 2006, and € 6,170 thousand as of the year 2007.

A job guarantee has been given to the city of Kiel.

(52) Letter of comfort

comdirect bank AG provides no general letter of comfort for the subsidiaries included in the consolidated financial statements.

(53) The company's boards

Supervisory board

Klaus-Peter Müller
(since of 10 May, 2001)
Frankfurt am Main
Chairman of the Supervisory Board
Chairman of the Board of Managing Directors of Commerzbank AG,
Frankfurt am Main

Dr. Norbert Käsbeck
(until 10 May, 2001 Chairman of the Supervisory Board)
Frankfurt am Main
Member of the Board of Managing Directors of Commerzbank AG,
Frankfurt am Main

Klaus Müller-Gebel
Frankfurt am Main
Deputy Chairman of the Supervisory Board
Member of the Board of Managing Directors of Commerzbank AG,
Frankfurt am Main

Dr. Franz-Georg Brune
(since 10 May, 2001)
Frankfurt am Main
Co-manager of Frankfurt am Main main branch of Commerzbank AG,
Frankfurt am Main

Dr. Ferdinand Vogel
(until 10 May, 2001)
Frankfurt am Main
Head of IT Development service department
Director of Commerzbank AG,
Frankfurt am Main

Burkhard Graßmann
Weiterstadt
Member of the Board of Managing Directors of
T-Online International AG, Weiterstadt

Angelika Kierstein
Quickborn
Chairman of Staff Council of comdirect bank Aktiengesellschaft
Commercial employee

Maria Xiromeriti
Quickborn
Deputy Chairman of Staff Council of comdirect bank
Aktiengesellschaft
Commercial employee

Vorstand

Bernt Weber
Christian Jessen
Hans-Joachim Nitschke
Dr. Andre Carls

(54) Shares of comdirect bank AG

Number of shares held by the boards:

	31.12.2001 (unaudited)	31.12.2000
Members of the Board of Managing Directors	**700**	**700**
Dr. Andre Carls	0	0
Christian Jessen	200	200
Hans-Joachim Nitschke	0	0
Bernt Weber	500	500
Members of the Supervisory Board	**150**	**250**
Klaus-Peter Müller	0	0
Klaus Müller-Gebel	0	0
Dr. Franz-Georg Brune	0	0
Burkhard Graßmann	0	0
Angelika Kierstein	100	200
Maria Xiromeriti	50	50

The number of options held to subscribe to comdirect bank AG shares breaks down as follows:

	31.12.2001 (unaudited)	31.12.2000
Members of the Board of Managing Directors	**90,000**	**36,000**
Dr. Andre Carls	13,500	0
Christian Jessen	25,500	12,000
Hans-Joachim Nitschke	25,500	12,000
Bernt Weber	25,500	12,000
Members of the Supervisory Board	**0**	**0**
Klaus-Peter Müller	0	0
Klaus Müller-Gebel	0	0
Dr. Franz-Georg Brune	0	0
Burkhard Graßmann	0	0
Angelika Kierstein	0	0
Maria Xiromeriti	0	0

(55) Remuneration and loans to board members

The following remuneration was paid to members of the Board of Managing Directors and members of the Supervisory Board:

	31.12.2001	31.12.2000
	(€ thousand) (unaudited)	
Board of Managing Directors	1,290	783
Supervisory Boards	87	99

Neither advance payments nor loans were extended.comdirect did not take on any contingent liabilities.

Holdings

Affiliated companies included in the consolidation:

Name	Domicile	Share of capital held in %	Equity in thousand	
comdirect ltd	London/United Kingdom	100.0	GBP	10,485
comdirect nominee ltd	London/United Kingdom	100.0	GBP	(1,00)
comdirect S.A.	Paris/France	99.3	EUR	13,064
comdirect bank S.p.A	Milan/Italy	100.0	EUR	6,374

Quickborn, 25 February 2002
The Board of Managing Directors

Bernt Weber Christian Jessen Hans-Joachim Nitschke Dr. Andre Carls

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