Magyar Telekom Telecommunications
Public Limited Company

Consolidated Annual Report

FOR THE YEAR ENDED DECEMBER 31, 2011

Magyar Telekom Telecommunications
Public Limited Company

Consolidated Financial Statements

FOR THE YEAR ENDED DECEMBER 31, 2011

Prepared in accordance with
International Financial Reporting Standards (IFRS)

MAGYAR TELEKOM

INDEX TO THE CONSOLIDATED FINANCIAL STATEMENTS

INDEPENDENT AUDITOR'S REPORT

To the Shareholders of Magyar Telekom Nyrt.

Report on the consolidated financial statements

We have audited the accompanying consolidated financial statements of Magyar Telekom Nyrt. ("the Company") which comprise the consolidated statement of financial position as of 31 December 2011 (in which the total of statement of financial position is HUF 1,098,028 million, the total comprehensive income for the year is HUF 25,974 million), the consolidated statement of comprehensive income and consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and the notes to the consolidated financial statements including a summary of the significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with International Financial Reporting Standards as adopted by the EU and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with Hungarian Standards on Auditing and with applicable laws and regulations in force in Hungary. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

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

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

Opinion

During our work we have audited the components and disclosures along with the underlying accounting records and supporting documentation in the consolidated financial statements of Magyar Telekom Nyrt. in accordance with Hungarian Standards on Auditing and, on the basis of our audit work, we have gained sufficient and appropriate evidence that the consolidated financial statements have been prepared in accordance with International Financial Reporting Standards as adopted by the EU. In our opinion, the accompanying consolidated financial statements give a true and fair view of the financial position of Magyar Telekom Nyrt. as of 31 December 2011, and of the results of its operation for the year then ended in accordance with International Financial Reporting Standards as adopted by the EU.

Other reporting requirements regarding the business report

We have examined the accompanying consolidated business report of Magyar Telekom Nyrt.("the Company") for the financial year of 2011.

Management is responsible for the preparation of the consolidated business report which is consistent with the consolidated financial statements prepared in accordance with International Financial Reporting Standards as adopted by the EU. Our responsibility is to assess whether or not the accounting information disclosed in the consolidated business report is consistent with that contained in the consolidated financial statements. Our work in respect of the consolidated business report was limited to checking it within the aforementioned scope and did not include a review of any information other than that drawn from the audited accounting records of the Company. In our opinion the 2011 consolidated business report is consistent with the disclosures in the consolidated financial statements as of 31 December 2011.

Budapest, March 5, 2012

Manfred Krawietz
Partner
PricewaterhouseCoopers Auditing Ltd.
1077 Budapest, Wesselényi u. 16.
License Number: 001464

Hegedűsné Szűcs Márta
Statutory auditor
Licence number: 006838
1077 Budapest, Wesselényi u. 16.

Note:

Our report has been prepared in Hungarian and in English. In all matters of interpretation of information, views or opinions, the English version of our report takes precedence over the Hungarian version.

MAGYAR TELEKOM

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

	Note	At December 31, 2010	At December 31, 2011
		(in HUF millions)	
ASSETS			
Current assets			
Cash and cash equivalents	6	15,841	14,451
Trade and other receivables	7	114,625	124,663
Other current financial assets	8.1	56,560	65,286
Current income tax receivable	9.1	1,804	927
Inventories	10	9,592	9,904
Non current assets held for sale	11	2,152	5,165
Total current assets		200,574	220,396
Non current assets			
Property, plant and equipment	12	549,752	536,224
Intangible assets	13	332,993	308,313
Investments in associates and joint ventures	14	77	-
Deferred tax assets	9.4	913	750
Other non current financial assets	8.2	24,033	31,590
Other non current assets	15	664	755
Total non current assets		908,432	877,632
Total assets		1,109,006	1,098,028
LIABILITIES			
Current liabilities			
Financial liabilities to related parties	16	72,208	49,865
Other financial liabilities	17	46,647	70,155
Trade payables	18	88,613	101,119
Current income tax payable	9.1	661	1,335
Provisions	19	7,722	3,703
Other current liabilities	20	30,966	29,213
Total current liabilities		246,817	255,390
Non current liabilities			
Financial liabilities to related parties	16	234,164	230,166
Other financial liabilities	17	8,828	17,928
Deferred tax liabilities	9.4	10,924	26,270
Provisions	19	12,298	11,236
Other non current liabilities	21	1,263	947
Total non current liabilities		267,477	286,547
Total liabilities		514,294	541,937
EQUITY			
Equity of the owners of the parent			
Common stock		104,275	104,275
Additional paid in capital		27,379	27,379
Treasury stock		(307)	(307)
Retained earnings		385,283	325,709
Accumulated other comprehensive income		14,882	30,959
Total Equity of the owners of the parent		531,512	488,015
Non-controlling interests		63,200	68,076
Total equity		594,712	556,091
Total liabilities and equity		1,109,006	1,098,028

These consolidated financial statements were authorized for issue by the Board of Directors on February 23, 2012 and signed on their behalf by:

Christopher Mattheisen
Chairman and Chief Executive Officer

Thilo Kusch
Chief Financial Officer

The accompanying notes form an integral part of these consolidated financial statements.

MAGYAR TELEKOM

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

	Note	2010	2011
		For the year ended December 31,	
		(in HUF millions, except	per share amounts)
Revenue	22	609,579	597,617
Expenses directly related to revenues	23	(157,427)	(161,047)
Employee related expenses	24	(93,884)	(91,823)
Depreciation and amortization		(100,872)	(132,915)
Other operating expenses	25	(148,750)	(155,057)
Operating expenses		(500,933)	(540,842)
Other operating income	26	3,448	6,392
Operating profit		112,094	63,167
Interest income	27	4,938	3,633
Interest expense	28	(23,784)	(23,184)
Other finance expense - net	29	(9,267)	(12,911)
Net financial result		(28,113)	(32,462)
Share of associates' and joint ventures' profits / (losses)	14	(27)	12
Profit before income tax		83,954	30,717
Income tax expense	9.2	(6,583)	(27,538)
Profit for the year		77,371	3,179
Exchange differences on translating foreign operations		6,617	22,816
Revaluation of available-for-sale financial assets – before tax		20	(21)
Revaluation of available-for-sale financial assets – tax effect		-	-
Other comprehensive income for the year, net of tax		6,637	22,795
Total comprehensive income for the year		84,008	25,974
Profit attributable to:			
Owners of the parent		64,378	(7,457)
Non-controlling interests		12,993	10,636
		77,371	3,179
Total comprehensive income attributable to:			
Owners of the parent		69,505	8,620
Non-controlling interests		14,503	17,354
		84,008	25,974
Earnings per share (EPS) information:			
Profit attributable to the owners of the Company		64,378	(7,457)
Weighted average number of common stock outstanding (thousands) used for basic and diluted EPS		1,041,290	1,042,352
Basic and diluted earnings per share (HUF)		61.83	(7.15)

The accompanying notes form an integral part of these consolidated financial statements.

MAGYAR TELEKOM

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Note	2010	2011
		For the year ended December 31, (in HUF millions)	
Cashflows from operating activities			
Profit for the year		77,371	3,179
Depreciation and amortization		100,872	132,915
Income tax expense		6,583	27,538
Net financial result		28,113	32,462
Share of associates' and joint ventures' (profits) / losses		27	(12)
Change in assets carried as working capital		(8,364)	(9,068)
Change in provisions		(4,194)	(5,702)
Change in liabilities carried as working capital		(3,009)	23,277
Income tax paid		(11,419)	(10,999)
Dividend received		95	24
Interest and other financial charges paid		(27,426)	(24,153)
Interest received		4,919	3,650
Other cashflows from operations		1,102	(4,330)
Net cash generated from operating activities		164,670	168,781
Cashflows from investing activities			
Purchase of property plant and equipment (PPE) and intangible assets	30	(87,300)	(80,074)
Purchase of subsidiaries and business units	31	(1,534)	(2,675)
Cash acquired through business combinations		6	468
Proceeds from / (Payments for) other financial assets – net		34,327	(997)
Proceeds from disposal of subsidiaries and associates	26	780	-
Proceeds from disposal of PPE and intangible assets		873	5,526
Net cash used in investing activities		(52,848)	(77,752)
Cashflows from financing activities			
Dividends paid to shareholders and Non-controlling interest		(91,819)	(64,626)
Proceeds from loans and other borrowings		190,797	159,812
Repayment of loans and other borrowings		(229,545)	(188,414)
Change in Non-Controlling interests		(22)	-
Net cash used in financing activities		(130,589)	(93,228)
Exchange gains on cash and cash equivalents		338	809
Change in cash and cash equivalents		(18,429)	(1,390)
Cash and cash equivalents, beginning of year		34,270	15,841
Cash and cash equivalents, end of year	6	15,841	14,451

The accompanying notes form an integral part of these consolidated financial statements.

MAGYAR TELEKOM

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

	pieces	In HUF millions									
	Shares of common stock (a)	Common stock (a)	Additional paid in capital (b)	Treasury stock (c)	Retained earnings (d)	Cumulative translation adjustment (e)	Revaluation reserve for AFS financial assets – net of tax (f)	Reserve for equity settled share based transactions (g)	Equity of the owners of the parent	Non-controlling interests (h)	Total Equity
Balance at December 31, 2009	1,042,742,543	104,275	27,379	(1,179)	398,250	9,768	(62)	49	538,480	66,940	605,420
Dividend (i)					(77,053)				(77,053)	–	(77,053)
Dividend declared to Non-controlling interests (j)									–	(18,243)	(18,243)
Share based compensation program (k)				872	(292)				580	–	580
Total comprehensive income for the year					64,378	5,165	11	(49)	69,505	14,503	84,008
Balance at December 31, 2010	1,042,742,543	104,275	27,379	(307)	385,283	14,933	(51)	-	531,512	63,200	594,712
Dividend (i)					(52,117)				(52,117)	–	(52,117)
Dividend declared to Non-controlling interests (j)									-	(12,478)	(12,478)
Total comprehensive income for the year					(7,457)	16,089	(12)		8,620	17,354	25,974
Balance at December 31, 2011	1,042,742,543	104,275	27,379	(307)	325,709	31,022	(63)	-	488,015	68,076	556,091
Of which treasury stock	(390,862)										
Shares of common stock outstanding at December 31, 2011	1,042,351,681										

The accompanying notes form an integral part of these consolidated financial statements.

NOTES TO THE CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

(a) The total amount of issued shares of common stock of 1,042,742,543 (each with a nominal value of HUF 100) is fully paid as at December 31, 2011. The number of authorized ordinary shares on December 31, 2011 is 1,042,742,543.

(b) Additional paid in capital represents the amount above the nominal value of the shares that was received by the Company during capital increases.

(c) Treasury stock represents the cost of the Company's own shares repurchased.

(d) Retained earnings include the accumulated and undistributed profit of the Group. The distributable reserves of the Company under Hungarian law at December 31, 2011 amounted to approximately HUF 232,569 million (HUF 253,793 million at December 31, 2010).

(e) Cumulative translation adjustment represents the foreign exchange differences arising on the consolidation of foreign subsidiaries.

(f) Revaluation reserve for available-for-sale (AFS) financial assets includes the unrealized gains and losses net of tax on available-for-sale financial assets.

(g) Reserve for equity settled share based transactions includes the compensation expenses accrued in this reserve related to share settled compensation programs. The December 31, 2009 balance of this reserve of HUF 49 million represented the amount reserved for the 103,530 options granted in 2000 to Magyar Telekom's ex-CEO. Since these options lapsed unexercised in 2010, the balance of the reserve was released to Profit for the year in 2010 (Note 24.2).

(h) Non-controlling interests represent the Non-controlling shareholders' share of the net assets of subsidiaries, in which the Group has less than 100% ownership.

(i) In 2011 Magyar Telekom Plc. declared HUF 50 dividend per share (HUF 74 in 2010).

(j) The amount of dividends declared to Non-controlling interests includes predominantly the dividends declared to the Non-controlling owners of Makedonski Telekom (MKT) and Crnogorski Telekom (CT), the Group's subsidiaries.

(k) In 2010 Magyar Telekom launched a share allocation program under which Magyar Telekom shares were awarded to the Company's selected employees. In total, 1,112,679 treasury shares were granted to employees for free in December 2010. (Note 24.3). The fair value of the treasury shares at the grant date was HUF 580 million, which was recognized as employee expense in 2010. The loss on the re-issuance of the treasury shares (measured as the difference between the original cost of re-acquisition and the grant date stock exchange price of the treasury shares) was recognized in Retained earnings in an amount of HUF 292 million.

Together with the approval of these financial statements for issue, the Board of the Company proposes a HUF 50 per share dividend distribution (in total HUF 52,117 million) to be approved by the Annual General Meeting of the Company in April 2012.

The accompanying notes form an integral part of these consolidated financial statements.

1 GENERAL INFORMATION

1.1 About the Company

Magyar Telekom Telecommunications Public Limited Company (the "Company" or “Magyar Telekom Plc.”) with its subsidiaries form Magyar Telekom Group (“Magyar Telekom” or “the Group”). Magyar Telekom is the principal of telecommunications services in Hungary, Macedonia and Montenegro and alternative service provider in Bulgaria and Romania. These services are subject to various telecommunications regulations depending on the countries of operations (Note 1.3).

The Company was incorporated in Hungary on December 31, 1991 and commenced business on January 1, 1992. The Company’s registered address is Krisztina körút 55, 1013 Budapest, Hungary.

Magyar Telekom Plc. is listed on the Budapest stock exchange and its shares are traded on the Budapest Stock Exchange. Magyar Telekom’s American Depository Shares (ADSs) each representing five ordinary shares were also traded on the New York Stock Exchange until November 12, 2010, when the ADSs were delisted.

The immediate controlling shareholder of the Company is MagyarCom GmbH owning 59.21% of the issued shares, while the ultimate controlling parent of Magyar Telekom is Deutsche Telekom AG (DT or DTAG).

The consolidated financial statements are prepared and presented in millions of Hungarian Forints (HUF), unless stated otherwise.

These consolidated financial statements of the Company were approved for issue by the Company’s Board of Directors (the Board), however, the Annual General Meeting (AGM) of the owners, authorized to accept these financials, has the right to require amendments before acceptance. As the controlling shareholders are represented in the Board of the Company that approved these financial statements for issuance, the probability of any potential change required by the AGM is extremely remote, and has never happened in the past.

1.2 Investigation into certain consultancy contracts

As previously disclosed, the Company’s Audit Committee conducted an internal investigation regarding certain contracts relating to the activities of the Company and/or its affiliates in Montenegro and Macedonia that totaled more than EUR 31 million. In particular, the internal investigation examined whether the Company and/or its Montenegrin and Macedonian affiliates had made payments prohibited by U.S. laws or regulations, including the U.S. Foreign Corrupt Practices Act (the “FCPA”). The Company has previously disclosed the results of the internal investigation. The Company’s Audit Committee informed the U.S. Department of Justice (the “DOJ”) and the U.S. Securities and Exchange Commission (the “SEC”) of the internal investigation. The DOJ and the SEC commenced investigations into the activities that were the subject of the internal investigation. For further information regarding the internal investigation, see the Company’s annual report for the year ended December 31, 2010.

In 2011, the Company entered into final settlements with the DOJ and the SEC to resolve the DOJ’s and the SEC’s investigations relating to the Company. The settlements concluded the DOJ’s and the SEC’s investigations.

The Company has entered into a two-year deferred prosecution agreement (the “DPA”) with the DOJ, under which the Company was charged with a violation of the anti-bribery provisions of the FCPA and two violations of the books and records provisions of the FCPA. In accordance with the DPA, on December 29, 2011, the DOJ filed a criminal information (the “Information”) setting out these charges in the U.S. District Court for the Eastern District of Virginia. The Company has agreed to admit to the DOJ’s allegations and to acknowledge responsibility for the acts as charged in the Information. The Company has agreed to pay a criminal penalty of USD 59.6 million to cooperate with the DOJ in future investigations, to refrain from any violations of U.S. federal criminal law, to continue to operate a compliance program and to report to the DOJ annually regarding the compliance program during the term of the DPA. The DOJ will seek to dismiss the charges upon conclusion of the two-year term, unless the Company violates the terms of the DPA.

On December 29, 2011, the SEC filed in the U.S. District Court for the Southern District of New York a Complaint (the "Complaint") and a proposed Final Judgment against the Company (the "Final Judgment"). Without admitting or denying the allegations in the Complaint, the Company consented to the filing of the Complaint and entry of the Final Judgment to resolve the SEC's investigation. The Complaint alleged civil violations of the FCPA's anti-bribery, books and records and internal control provisions. The Final Judgment, which was approved by the U.S. District Court for the Southern District of New York on January 3, 2012, permanently enjoined the Company from violating these provisions and required the Company to pay USD 25.2 million for disgorgement of profits and USD 6.0 million of prejudgment interest thereon.

The final settlements recognize the DOJ's and the SEC's consideration of the Company's self-reporting, thorough internal investigation, remediation and cooperation with the DOJ's and the SEC's investigations. The Company has undertaken several remedial measures to address the issues identified during the course of these investigations. These measures include steps designed to revise and enhance the Company's internal controls, as well as the establishment of the Corporate Compliance Program. The Corporate Compliance Program promotes awareness of the Company's compliance policies and procedures through training, the operation of a whistleblower hotline, and monitoring of, and communications with, employees and subsidiaries of the Company. The Company remains fully committed to responsible corporate behavior.

The aggregate amount of USD 90.8 million (HUF 21,857 million) payable by the Company in settlement of the DOJ's and SEC's investigations was fully provided for before the end of 2011. Of this amount HUF 16,191 million was recognized as Other operating expense, HUF 1,119 million was recognized as Interest expense and HUF 4,547 million was recognized as foreign exchange loss included in Other finance expense –net. The amounts provided for as at December 31, 2011 were reclassified to Other current financial liabilities.

On January 6, 2012 the Company paid a criminal penalty of USD 59.6 million (HUF 14,712 million) pursuant to the settlement with the DOJ and on January 23, 2012 the Company paid USD 25.2 million for disgorgement of profits and USD 6.0 million of prejudgment interest (HUF 7,366 million in total) pursuant to the settlement with the SEC, totaling USD 90.8 million (HUF 22,078 million) paid with respect to the settlements with the DOJ and the SEC.

In addition to the DOJ's and the SEC's investigations, the Ministry of Interior of the Republic of Macedonia, the Montenegrin Supreme State Prosecutor and the Hungarian Central Investigating Chief Prosecutor's Office commenced investigations into certain of the activities that were the subject of the internal investigation. These governmental investigations are continuing, and the Company and its relevant subsidiaries continue to cooperate with these investigations.

1.3 Public service concession and license arrangements

Magyar Telekom's primary activities are the fixed line and mobile operations in Hungary, Macedonia and Montenegro. These services are in most cases regulated by these countries' laws or other legislations. These services in most cases require the acquisition of a license or concession, which usually requires a one-off fee, which is capitalized and amortized over the original duration of license or concession, and also requires annual payments, which are recognized as Other operating expenses (included in Fees and levies) in the year the payment obligation refers to.

The most important features of the regulations of these services are described below.

1.3.1 Hungarian Fixed line

Magyar Telekom Plc. is the market leading fixed line telecom service provider in Hungary. The Implementation of the EU New Regulatory Framework (NRF) Review package had been completed by the amendment of the Act C of 2003 on Electronic Communications (hereinafter: Communications Act). Amendments of the Communications Act came into effect on August 3, 2011. The National Media and Infocommunications Authority of Hungary (NMIAH) is the supreme supervisory body and is responsible for secondary legislation making and the preparation of relevant decrees. In Q4 2011, as the result of secondary legislation making process, the NMIAH published some important decrees, such as Decree on subscriber contracts issues, Decree on Service Quality issues and Decree on Numbering related issues.

Universal services are basic communications services (including access to communication services at a fixed location, public payphones, directory and directory enquiry services) that should be available to all customers at an affordable price. Magyar Telekom Plc. was a Universal Service Provider from 2002 to 2008, for which a universal service contract was valid until December 31, 2008. The necessary modifications of the telecommunications law and the concerning governmental and ministerial decrees entered into force in the first half of 2010. The new legislation provides favorable conditions - in line with market changes – than the earlier regime. Magyar Telekom's universal service contract was signed on July 29, 2011, with a retrospective effect from January 1, 2011. The universal service contract expired on December 31, 2011, however consultations are ongoing with the Ministry about renewal of the contract. Even though there is no universal service contract in place, the Company continues to comply with the provisions of the expired contract.

In the electronic communications field Magyar Telekom was designated as an SMP operator (a service provider with significant market power) on the regulated markets. The current 7 relevant markets include retail and wholesale telephony and broadband services stipulated by the EU (according to the second recommendation on the relevant markets).

Magyar Telekom Plc's retail tariffs are regulated in two ways: 1) there is a price cap regulation based on SMP resolutions on retail residential and business fixed voice markets which limits price increases of monthly fees and 2) price squeeze is prohibited on the markets where Magyar Telekom is designated as SMP as well (i.e. retail prices should be set in accordance with wholesale tariffs providing an acceptable level of retail margins).

Magyar Telekom is Hungary's leading fixed line broadband service provider in the wholesale market and one of the leading ones in the retail market. In 2011, the NMIAH designated the Company again as an SMP operator on the wholesale broadband access market. In accordance with the effective resolution, all retail fix products shall be 'reproducible' by competitors based on the wholesale service. Consequently, the full retail portfolio shall have a wholesale equivalent compliant to the pricing regulations (retail minus methodology) set forth by the NMIAH. The Company has a non-discrimination obligation, which means that the same terms and conditions shall be granted in terms of wholesale services to competitors under identical circumstances.

According to the Act on Electronic Communications, designated SMP operators are obliged to prepare reference unbundling offers for access to (physical) passive network infrastructure (RUO) and to provide these services when there is a request for them by other telecommunications service providers. The reference offer of each SMP operator must be approved by the NMIAH. The price setting of these services has to be cost based and calculated by a Top-Down Long Run Incremental Costs (TD-LRIC).

SMPs are also obliged to prepare reference offers for interconnection (RIO), containing applicable fees, and to provide these services in accordance with the reference offer when there is a request for them by other telecommunications service providers. The reference offers of the SMPs must be approved by the NMIAH, and prices have to be based on LRIC. Fees in the currently effective reference offers are applicable from April 1, 2009. It is expected that the new RIO will be approved by NMIAH in Q1, 2012. However, due to the relevant SMP resolution Magyar Telekom has to apply its new fee retrospectively from December 22, 2011.

According to the Act on Electronic Communications, designated SMP operators are obliged to enable carrier selection to their subscribers. Consequently, voice telephony customers have the right to select different service providers for each call directions by dialing a pre-selected number or by using a call-by-call pre-fixed number. The requirements for carrier selection are set out in the RIO based interconnection agreements between the affected service providers.

Fixed line telecommunications service providers are obliged under the law to provide number portability on their networks starting January 1, 2004. This means that service providers must enable subscribers to change service provider without changing their fixed telephone numbers within the same geographical area.

1.3.2 Macedonian Fixed line

The Group is also present in the Macedonian fixed line telecommunications market through its subsidiary, Makedonski Telekom AD Skopje (MKT). MKT is the largest fixed line service provider in Macedonia. The Macedonian telecommunications sector is regulated by the Electronic Communications Law (ECL), enacted in March 2005. In October 2011 changes of ECL are proposed, with main focus on imposition of mandatory obligation for calling line identification presentation (CLIP) and location for emergency call, harmonizing operators' annual fees which are paid to Agency for Electronic Communications (Agency). Tender for Universal Service (US) providers designation-prequalification phase was held in February 2011. On June 29, 2011 MKT and R3 info media DOO Skopje were designated US providers. MKT is designated for US provider for fixed telephone services, public payphones and equivalent access for disabled end users. R3 info media DOO Skopje is US provider for unique subscriber directory and directory enquiry. Operators are obliged to start providing the universal services on January 1, 2012 for the following 5 years.

Based on the Agency analysis for the relevant markets 1-6 related to fixed voice retail services and the program of the Agency for Electronic Communications (Agency) for 2011, the Agency announced public meeting on October 26, 2011 for start of the process for development and implementation of the methodology for retail price regulation. These activities are expected to result in price decrease of some retail services (business monthly fee, fixed-to mobile, international outgoing calls). By the end of 2011 MKT submitted all data requested by the Agency for development of price squeeze model and methodology for retail price regulation. More intensive retail regulation is expected as of May 2012.

On the public meeting dated October 14, 2011 the Agency presented detailed plan for Bottom UP LRIC model development by consultants which is expected to result in changes of Bitstream Access (BSA) pricing models and will modify service description. The Agency announced that prices will be set on a level of an efficient operator and initial LRIC bottom up results are expected in Q1 2012. On December 29, 2011, the Agency published inception report for development of a Bottom-Up LRIC Model for Bit stream Services. By the end of January 2012 MKT submitted to the Agency all data requested in details for development of a Bottom-Up LRIC Model for Bit stream Services.

MKT has a cost based price obligation for the Regulated wholesale services, using Long Run Incremental Costs methodology (LRIC). During December 2010, the Agency published results from its own developed LRIC Bottom–up costing model. The results from the costing model are implemented as of April 1, 2011 which resulted in the reduction of the monthly fee for Unbundled Local Loop (ULL) and interconnection rates (for origination, termination and transit), as well as in the reduction of the monthly fees for interconnection links and collocation.

As of November 1, 2011 MKT stopped offering PSTN and ISDN services for its customers as well as for its Wholesale Partners and all the newly committed services are be based on IP (Internet Protocol) technology. In line with the PSTN migration of MKT's network, the Agency approved proposed modifications of MKT's Wholesale Line Rental Reference Offer (WLR) and Bitsream Access Service and Bitstream service resale offer (BSA) applicable as of January 1, 2012. In parallel MKT is trying to harmonize the process of PSTN migration with Wholesale operators.

Initial FTTx regulation was introduced in Q2 2011 with the imposed obligation for Reference Access Offer for ducts and dark fiber imposed on MKT by the Agency. The approved reference offer was published on December 5, 2011. It is fully in line with the introduced Rulebook for specific network access and elements and is applicable from 2012.

1.3.3 Montenegrin Fixed line

The Group's Montenegrin subsidiary, Crnogorski Telekom (CT) is registered to provide fixed line telecommunications services in Montenegro as well as to provide domestic voice and data services as well as VOIP, leased line, IPTV, value added services, etc. The telecommunications sector in Montenegro is regulated by the Law on Electronic Communications (the Law) that came into force in August 2008. The Law is based on the 2002 regulatory framework of the EU. All regulations that are contrary to the Law became automatically invalid and new ones have been issued or will have to be issued.

As a result of the market analysis, completed in November 2010, CT was designated as an SMP operator at all seven markets. Local loop unbundling, bit stream access, wholesale leased line and carrier pre-selection were introduced on the Montenegrin market in February 2011, when CT published updated RIOs and ROs. Carrier selection was already implemented by CT in 2008. Number portability was introduced by the end of October 2011. RIO rates have been determined by the Resolution of the Agency for Electronic Communications and Postal Services (NRA) based on international benchmarks.

At the end of May 2011, the NRA adopted Cost Accounting methodology which will be applied by CT. Accounting Separation and Cost Accounting will be introduced before May 2012.

During Q2 2011 the NRA adopted decision on five new relevant markets that were evaluated through the three criteria test. According to the NRA's decision, CT was designated as SMP on 3 markets: 1. Retail market for local and long-distance calls, for business and residential, provided on fixed location 2. Retail market for international calls, for business and residential, provided on fixed location 3. Wholesale market of trunk segments of leased lines. Standard EU remedies (also prescribed in the Montenegrin Law) are imposed to CT.

In December 2010 Montenegro obtained EU candidate status. In accordance with the previously signed Stabilization and Association Agreement with the EU, the harmonization of the telecommunications regulations with the regulatory framework of the EU should be completed within three years of the ratification of the Agreement that is by the end of 2013.

1.3.4 Hungarian Mobile

The Company is also the market leader in the Hungarian mobile market through the brand T-Mobile.

The initial duration of the concession regarding the GSM 900 public mobile radio telephone service was a period of 15 years starting from the execution of the concession agreement (November 4, 1993 to November 4, 2008). On October 7, 1999 an amended concession contract was signed between the Ministry of Transport, Communications and Water Management and the Company extending the Company's rights and obligations to also provide service in the 1800 MHz band in Hungary until October 7, 2014. The duration of the concession regarding the DCS 1800 public mobile radio telephone service is 15 years starting from the execution of the new concession agreement (October 7, 1999 to October 7, 2014). As stipulated in the concession contracts, the Minister is entitled to extend the concession period for both services upon their expiration for another 7.5 years without the invitation of a tender. On November 8, 2007, the Company signed the renewed Concession Contract along with the Cooperation Agreement with the Minister that is effective from November 2008. The new Concession Contract prolonged the duration of the 900 MHz frequency usage right until May 4, 2016.

On December 7, 2004, the Company obtained the exclusive right of use of certain frequency blocks for the deployment and operation of an IMT2000/UMTS mobile telecommunications system (3G system). The duration of the frequency usage right is 15 years (until December 7, 2019) with an option to extend it for another 7.5 years. On August 26, 2005 the Company started to provide 3G service and has been operating it in compliance with the license conditions.

The Company is subject to number portability regulation since 2004, applicable only in case of other mobile operators. In 2005 and 2006 the Company was designated as having significant market power in the mobile wholesale call termination market, and it is currently subject to regulatory obligations regarding the termination charge of calls into its network. In December 2008 the Company was designated as an SMP for the third time in a row and in its resolution reinforced the symmetric mobile termination fees applicable from January 1, 2009, and set out further reduction of tariffs until December 2010 based on a new 'glide path'. At the end of August 2011, NMHH made its three new market analysis decisions, which affect the SMP operators next half-year commitments. On the mobile voice market the three mobile operators have to cut their wholesale prices by 40% in three steps.

Since June 30, 2007, an EU regulation has been regulating international roaming tariffs for wholesale and retail customers on the basis of a price cap system. The Regulation prescribed a glide-path that mandates further annual reductions of wholesale and retail prices in the forthcoming years. As of July 2009 the EU introduced regulated tariffs for SMS and data roaming similarly to the regulation of voice roaming.

The Company won a tender for a spectrum usage right license for a 26 GHz block on April 30, 2009.

The Company filed an auction bid in December 2011 with the Hungarian National Media and Infocommunications Authority for unused spectrum in the 900 MHz frequency band, relating to the provision of radio communications services. The spectrum can be utilized in a technology-neutral manner, allowing for the installation and operation of GSM, UMTS, LTE and/or WiMAX mobile networks. On January 31, 2012, the Company received from the Authority the first instance, non-final decision closing the auction. Pursuant to the first instance decision, the Company won the right of use of two duplex frequency blocks of 1 MHz each (one EGSM-band duplex frequency block of 1 MHz plus one PGSM-band duplex frequency block of 1 MHz) for a period of 15 years. See also Note 33.5.

1.3.5 Macedonian Mobile

T-Mobile Macedonia (T-Mobile MK), Magyar Telekom's subsidiary, is the leading mobile service provider in Macedonia. With the changes of the Electronic Communications Law ("ECL") published on August 4, 2008, the existing Concession Contract of T-Mobile MK ceased to be valid as of August 5, 2008. On September 5, 2008 the Agency for Electronic Communications, ex officio, issued a notification to T-Mobile MK for those public electronic communication networks and/or services which have been allocated thereto under the Concession Contracts. The license for radiofrequencies used by T-Mobile MK with a bandwidth of 25 MHz in the GSM 900 band, was also issued in a form regulated in the ECL with a validity period until September 5, 2018, which can be renewed up to an additional 20 years in accordance with the ECL.

After the analysis of the market 16 "Call termination services in public mobile communication networks" the Agency on November 26, 2007 brought a decision by which T-Mobile MK was designated with SMP status on Market 16. T-Mobile MK published a RIO with regulated termination rate effective from August 1, 2008.

Based on the second round analysis on Market 16 published by the Agency on May 14, 2010, on July 30, 2010 T-Mobile MK received a Decision for changing the RIO by which the mobile termination rate (MTR) has been defined with a glide path decrease in a four years' time frame (until 2013). At the same time the Agency regulated the MTR's for the competitors as well with a respective 4 year glide path but introducing asymmetry between all three mobile operators which will lead to equal termination rates in September 2013. In August 2010 T-Mobile MK initiated a procedure before the Administrative Court to dispute the decision of the Agency arguing against the lowering of the MTR as well as against unjustified asymmetry. The administrative procedure has not started yet.

On July 7, 2010 the Agency concluded market analysis on Market 15 (Service for access and call initiation in the public mobile communication networks) and on July 28, 2010 brought a decision by which T-Mobile MK was designated with SMP status on Market 15. As a result of the SMP designation, T-Mobile MK was obliged to prepare and publish Referent Access Offer ("RAO"). T-Mobile MK submitted the offer to the Agency on August 28, 2010 and it was approved on November 29, 2010. On August 30, 2010 T-Mobile MK initiated a procedure before the Administrative Court challenging this decision of the Agency for designating T-Mobile MK as SMP on Market 15. The administrative procedure has not started yet.

On September 2, 2008 a decision for granting three 3G licenses was published. T-Mobile MK started commercial operations of the 3G services on June 11, 2009. The validity of the license is 10 years i.e. December 17, 2018, with a possibility for extension for 20 years in accordance with the ECL.

Four bylaws, for General terms, RIO provisions, LRIC calculation for mobile operators and for specific network elements, were enacted in 2011, after the completion of the public debates. Since the beginning of 2011, a number of other bylaws and acts in the secondary legislation were put on public debate and enacted, among which are a bylaw on accounting separation and a decision for relevant electronic communication markets where the market for SMS termination was included as a new relevant market in addition to the existing 13 relevant markets.

In January 2011 the Agency officially published the draft market analysis for SMS termination. In March 2011 the Agency published the final market analysis for SMS termination, and in May 2011 all 3 mobile operators were designated with SMP status on the SMS termination market. In June 2011 all 3 mobile operators submitted draft RIOs with the SMS termination service included, and in July 2011 the RIOs were approved by the Agency.

In October 2011, a public call for submission of requests for acquiring a radiofrequency license for mobile services in 790 – 862 MHz was published by the Agency, for which T-Mobile MK applied. No results were published so far.

The Electronic Communications Law was amended in January 2012. The changes are: obligation for sending location data for the subscribers when dialing the emergency numbers, obligations for free of charge SMS for promotion of cultural heritage of Republic of Macedonia upon a written request from the relevant state institutions, Agency discretion for Accounting separation obligations imposition. The Agency will create electronic register for the telecommunication terminal equipment for mobile communication services by July 1, 2012 and it shall control and measure the quality parameters of the public communications services which should be in line with the recommendations and standards of the EU.

1.3.6 Montenegrin Mobile

Crnogorski Telekom, the Group's Montenegrin subsidiary is also providing mobile services under the T-Mobile brand (T-Mobile CG). CT is registered as one of three GSM/UMTS providers in Montenegro. T-Mobile CG, as the second mobile operator, was launched in 2000. The third mobile operator entered the market in 2007. T-Mobile CG started 3G operations in 2007.

As a result of the market analysis of the NRA T-Mobile CG is designated as an SMP in the market of termination of voice calls in its own network. Interconnect rates have been determined by the Regulator based on benchmarks. New updated RIO was published in February 2011. Number portability was introduced also in the mobile sector. In the new cycle of relevant market analysis completed at the end of 2011 CT is designated as SMP at one mobile market: Wholesale market on access and origination of calls in public mobile telephone networks. Among other standard EU remedies imposed to CT, the NRA also obliged CT to provide carrier selection on this market.

The NRA launched a tender for the 4th Mobile license in Montenegro at the end of 2011. Existing operators were also allowed to bid for certain radio frequency ranges. There was no interest from new operators but Telenor participated and won the tender. Telenor is obliged by the NRA Decision to offer the transfer of right of 1/3 of granted frequency resources to each of the other two competitors. Only CT expressed its interest for offered range. The NRA is supposed to issue the approval for transferring the resources to the interested operator in February 2012.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

2.1 Basis of preparation

The consolidated financial statements of Magyar Telekom have been prepared in accordance with International Financial Reporting Standards (IFRS) as endorsed by the European Union (EU). All standards and interpretations issued by the International Accounting Standards Board (IASB) effective at the time of preparing the consolidated financial statements and applicable to Magyar Telekom have been endorsed by the EU. Therefore the consolidated financial statements currently also comply with IFRS as issued by the IASB and also comply with the Hungarian Accounting Law on consolidated financial statements, which refers to the IFRS as endorsed by the EU.

The consolidated financial statements are presented in millions of HUF.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Group's accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements, are disclosed in Note 4.

2.1.1 Standards, amendments and interpretations effective and adopted by the Group in 2011

- IAS 24 (revised). In November 2009, the IASB issued a revised version of IAS 24 Related Party Disclosures. Until now, if a government controlled, or significantly influenced, an entity, the entity was required to disclose information about all transactions with other entities controlled, or significantly influenced by the same government. The revised standard still requires disclosures that are important to users of financial statements but eliminates requirements to disclose information that is costly to gather and of less value to users. It achieves this balance by requiring disclosure about these transactions only if they are individually or collectively significant. Furthermore the IASB has simplified the definition of related party and removed inconsistencies. The Group adopted the revised standard as of January 1, 2011. The revised standard did not have a significant impact on the disclosures in the Group's financial statements.

2.1.2 Standards, amendments and interpretations effective in 2011 but not relevant for the Group

- IAS 32 (amended) - The IASB published an amendment to IAS 32 Financial Instruments: Presentation in October 2009. The amendment clarifies the classification of rights issues as equity or liabilities for rights issues that are denominated in a currency other than the functional currency of the issuer. These rights issues are recorded as derivative liabilities before the amendment. The amendment requires that such right issues offered pro rata to all of an entity's existing shareholders are classified as equity. The classification is independent of the currency in which the exercise price is denominated. The amendment did not have any impact on the Group's financial statements as Magyar Telekom has no such instruments.

- IFRS 1 The IASB amended IFRS 1 in January 2010 and in December 2010. As the Group has been reporting according to IFRS for many years, neither the original standard, nor any revision to that is relevant for the Group.

- IFRIC 14 (amended) IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction. In November 2009, the IASB issued an amendment to IFRIC 14, which corrects an unintended consequence of IFRIC 14. Without the amendments, in some circumstances entities are not permitted to recognize some voluntary prepayments for minimum funding contributions as an asset. The amendment permits such an entity to treat the benefit of such an early payment as an asset. The amended interpretation is not applicable to Magyar Telekom as the Group has no funded defined post-retirement benefit schemes.

- IFRIC 19 Extinguishing Financial Liabilities with Equity Instruments. This interpretation issued in November 2009 clarifies the requirements of IFRSs when an entity renegotiates the terms of a financial liability with its creditor and the creditor agrees to accept the entity's shares or other equity instruments to settle the financial liability fully or partially. The interpretation did not have any impact on Magyar Telekom's financial statements as the Group does not extinguish any of its financial liabilities with equity instruments.

2.1.3 Standards, amendments and interpretations that are not yet effective and have not been early adopted by the Group

- IAS 1 (amended) - The IASB published amendments to IAS 1 Presentation of Financial Statements in June 2011. The amendments to IAS 1 retain the 'one or two statement' approach at the option of the entity and only revise the way other comprehensive income is presented: requiring separate subtotals for those elements which may be reclassified to the profit or loss section of the income statement (recycled) and those elements that will not. The application of the amendment is required for annual periods beginning on or after July 1, 2012. The European Union has not yet endorsed the amendments of the standard.

- IAS 19 (amended) - The IASB published amendments to IAS 19 - Employee Benefits in June 2011. The amendments focus on the following key areas:
  - Recognition (only defined benefit plans) - elimination of the "corridor approach"
  - Presentation (only defined benefit plans) - gains and losses that arises from remeasurements should be presented (only) in other comprehensive income (elimination of the remaining options)
  - Disclosures - enhancing of disclosure requirements, e.g.
    - the characteristics of a company's defined benefit plans,
    - amounts recognized in the financial statements,
    - risks arising from defined benefit plans and
    - participation in multi-employer plans
  - Improved / clarified guidance relating to several areas of the standard, e.g.
    - classification of benefits,
    - recognition of termination benefits and
    - interest rate relating to the expected return on the plan assets

  The application of the amendment is required for annual periods beginning on or after January 1, 2013. We do not expect that the adoption of the amended standard would result in significant changes in the financial statements of the Group. The European Union has not yet endorsed the amendments of the standard.

- IAS 32 (amended) - The IASB published amendments to IAS 32 Financial Instruments: Presentation in December 2011. The amendments to IAS 32 clarify the IASB's requirements for offsetting financial instruments. The amendments address inconsistencies in current practice when applying the offsetting criteria in IAS 32. The pronouncement clarifies:
  - the meaning of "currently has a legally enforceable right of set off the recognized amounts"; and
  - that some gross settlement systems may be considered equivalent to net settlement.

  The application of the amendment is required for annual periods beginning on or after January 1, 2014. A reporting entity must apply the amended standard retrospectively. We do not expect that the adoption of the amended standard would result in significant changes in the financial statements of the Group. The European Union has not yet endorsed the amendment of the standard.

- IFRS 7 (amended) - The IASB published an amendment to IFRS 7 Amendments to IFRS 7 Financial Instruments: Disclosures in October 2010. The amendment requires quantitative and qualitative disclosures regarding transfers of financial assets that do not result in entire derecognition, or that result in continuing involvement. This is intended to allow users of financial statements to improve their understanding of such transactions (for example, securitizations), including understanding the possible effects of any risks that may remain with the entity that transferred the assets. The amendments also require additional disclosures if a disproportionate amount of such transactions are undertaken around the end of a reporting period. The application of the amendment is required for annual periods beginning on or after July 1, 2011. An earlier application is permitted. We do not expect that the adoption of the amended standard would result in significant changes in the financial statements disclosures of the Group. The European Union has not yet endorsed the amended standard.

The IASB published amendments to IFRS 7 Amendments to IFRS 7 Financial Instruments: Disclosures in December 2011. The IASB and the Financial Accounting Standards Board (FASB) issued common disclosure requirements that are intended to help to better assess the effect or potential effect of offsetting arrangements on a company's financial position. The common disclosure requirements also improve transparency in the reporting of how companies mitigate credit risk, including disclosure of collateral pledged or received. The application of the amendment is required for annual periods beginning on or after January 1, 2013. A reporting entity must apply the amended standard retrospectively. We do not expect that the adoption of the amended standard would result in significant changes in the financial statements disclosures of the Group. The European Union has not yet endorsed the amended standard.

- IFRS 9 Financial Instruments. The standard forms the first part of a three-phase project to replace IAS 39 (Financial Instruments: Recognition and Measurement) with a new standard, to be known as IFRS 9 Financial Instruments. IFRS 9 prescribes the classification and measurement of financial assets and liabilities. The remaining phases of this project, dealing with the impairment of financial instruments and hedge accounting, as well as a further project regarding derecognition, are in progress.

Financial assets - At initial recognition, IFRS 9 requires financial assets to be measured at fair value. After initial recognition, financial assets continue to be measured in accordance with their classification under IFRS 9. Where a financial asset is classified and measured at amortized cost, it is required to be tested for impairment in accordance with the impairment requirements in IAS 39. IFRS 9 defines the below rules for classification.

- IFRS 9 requires that financial assets are classified as subsequently measured at either amortized cost or fair value. There are two conditions needed to be satisfied to classify financial assets at amortized cost: (1) The objective of an entity's business model for managing financial assets has to be to hold assets in order to collect contractual cash flows; and (2) The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding. Where either of these conditions is not satisfied, financial assets are classified at fair value.

- Fair Value Option: IFRS 9 permits an entity to designate an instrument, that would otherwise have been classified in the amortized cost category, to be at fair value through profit or loss if that designation eliminates or significantly reduces a measurement or recognition inconsistency ('accounting mismatch').

- Equity instruments: The default category for equity instruments is at fair value through profit or loss. However, the standard states that an entity can make an irrevocable election at initial recognition to present all fair value changes for equity investments not held for trading in other comprehensive income. These fair value gains or losses are not reported as part of a reporting entity's profit or loss, even when a gain or loss is realized. Only dividends received from these investments are reported in profit or loss.

- Embedded derivatives: The requirements in IAS 39 for embedded derivatives have been changed by no longer requiring that embedded derivatives be separated from financial asset host contracts.

- Reclassification: IFRS 9 requires reclassification between fair value and amortized cost when, and only when there is a change in the entity's business model. The 'tainting rules' in IAS 39 have been eliminated.

Financial liabilities - IFRS 9 "Financial Instruments" sets the requirements on the accounting for financial liabilities and replaces the respective rules in IAS 39 "Financial Instruments: Recognition and Measurement". The new pronouncement

- Carries forward the IAS 39 rules for the recognition and derecognition unchanged.
- Carries forward most of the requirements in IAS 39 for classification and measurement.
- Eliminates the exception from fair value measurement for derivative liabilities that are linked to and must be settled by delivery of an unquoted equity instrument.
- Changes the requirements related to the fair value option for financial liabilities to address own credit risk.

The IASB issued amendments to IFRS 9 in December 2011 and deferred the mandatory effective date of IFRS 9 from January 1, 2013 to January 1, 2015. The deferral will make it possible for all phases of the IFRS 9 project to have the same mandatory effective date. The amendments also provide relief from the requirement to restate comparative financial statements for the effect of applying IFRS 9. This relief was originally only available to companies that chose to apply IFRS 9 prior to 2012. Instead, additional transition disclosures will be required to help investors understand the effect that the initial application of IFRS 9 has on the classification and measurement of financial instruments. The adoption of the new standard will likely result in changes in the financial statements of the Group, the exact extent of which we are currently analyzing. The European Union has not yet endorsed either the standard or its amendment.

- IFRS 10, IFRS 11, IFRS 12, IAS 27 (amended) and IAS28 (amended) - The IASB published IFRS 10 Consolidated Financial Statements, IFRS 11 Joint Arrangements, IFRS 12 Disclosures of Interests in Other Entities and amendments to IAS 27 Separate Financial Statements and IAS 28 Investments in Associates and Joint Ventures in May 2011.

  IFRS 10 replaces the consolidation guidance in IAS 27 Consolidated and Separate Financial Statements and SIC-12 Consolidation — Special Purpose Entities by introducing a single consolidation model for all entities based on control, irrespective of the nature of the investee (i.e., whether an entity is controlled through voting rights of investors or through other contractual arrangements as is common in special purpose entities). Under IFRS 10, control is based on whether an investor has
  - power over the investee;
  - exposure, or rights, to variable returns from its involvement with the investee; and
  - the ability to use its power over the investee to affect the amount of the returns.

  IFRS 11 introduces new accounting requirements for joint arrangements, replacing IAS 31Interests in Joint Ventures. The option to apply the proportional consolidation method when accounting for jointly controlled entities is removed. Additionally, IFRS 11 eliminates jointly controlled assets to now only differentiate between joint operations and joint ventures. A joint operation is a joint arrangement whereby the parties that have joint control have rights to the assets and obligations for the liabilities. A joint venture is a joint arrangement, whereby the parties that have joint control have rights to the net assets.

  IFRS 12 will require enhanced disclosures about both consolidated entities and unconsolidated entities in which an entity has involvement. The objective of IFRS 12 is to require information so that financial statement users may evaluate the basis of control, any restrictions on consolidated assets and liabilities, risk exposures arising from involvements with unconsolidated structured entities and non-controlling interest holders' involvement in the activities of consolidated entities.

  The requirements relating to separate financial statements are unchanged and are included in the amended IAS 27 Separate Financial Statements. The other portions of IAS 27 are replaced by IFRS 10.

  IAS 28 Investments in Associates and Joint Ventures is amended for conforming changes based on the issuance of IFRS 10, IFRS 11 and IFRS 12.

An entity shall apply this package of five new and revised standards for annual periods beginning on or after January 1, 2013. We do not expect that their adoption would result in significant changes in the financial statements of the Group, the exact extent of which we are currently analyzing. The European Union has not yet endorsed the new standards and the amendments.

- IFRS 13 The IASB published IFRS 13 Fair Value Measurement in May 2011in order to replace the guidance on fair value measurement in existing IFRS accounting literature with a single standard. The IFRS is the result of joint efforts by the IASB and FASB to develop a converged fair value framework. IFRS 13 defines fair value, provides guidance on how to determine fair value and requires disclosures about fair value measurements. However, IFRS 13 does not change the requirements regarding which items should be measured or disclosed at fair value. IFRS 13 seeks to increase consistency and comparability in fair value measurements and related disclosures through a 'fair value hierarchy'. The hierarchy categorizes the inputs used in valuation techniques into three levels. The hierarchy gives the highest priority to (unadjusted) quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. If the inputs used to measure fair value are categorized into different levels of the fair value hierarchy, the fair value measurement is categorized in its entirety in the level of the lowest level input that is significant to the entire measurement (based on the application of judgment). The new standard should be applied for annual periods beginning on or after January 1, 2013. Earlier application is permitted. We do not expect that the adoption of the new standard would result in significant changes in the financial statements of the Group, the exact extent of which we are currently analyzing. The European Union has not yet endorsed the new standard.

2.1.4 Standards, amendments and interpretations that are not yet effective and not relevant for the Group's operations

- IAS 12 (amended). In December 2010, the IASB issued the pronouncement "Deferred Tax: Recovery of Underlying Assets - Amendments to IAS 12". The new pronouncement "Deferred Tax: Recovery of Underlying Assets - Amendments to IAS 12" sets presumptions for the recovery (e.g. use or sale) of certain assets. This is relevant in cases where the type of recovery has different tax consequences. The pronouncement sets the rebuttable presumption that the carrying amount of investment property that is measured using the fair value model in IAS 40 will be recovered through sale. Moreover, the carrying amount of a non-depreciable asset measured using the revaluation model in IAS 16 is always deemed to be recovered through sale. The amendment supersedes SIC 21 and shall be applied for annual periods beginning on or after 1 January 2012. Earlier application is permitted. As Magyar Telekom does not have investment properties or non-depreciable asset measured using the revaluation model in IAS 16, the amended standard will not have any impact on the Group's financial statements. The European Union has not yet endorsed the amended standard.

- IFRIC 20 In October 2011, the IASB published IFRIC 20 Stripping Costs in the Production Phase of a Surface Mine. The interpretation shall be applied for annual periods beginning on or after 1 January 2013. Earlier application is permitted. As Magyar Telekom does not have mining activity, the interpretation will not have any impact on the Group's financial statements. The European Union has not yet endorsed the interpretation.

2.2 Consolidation

2.2.1 Subsidiaries

Subsidiaries in which the Group has an interest of more than one half of the voting rights or otherwise has power to govern the financial and operating policies as to obtain benefit from its activities, are consolidated.

The existence and effect of potential voting rights that are presently exercisable or presently convertible are also considered when assessing whether the Group controls another entity.

Subsidiaries are consolidated from the date on which control is transferred to the Group, and are no longer consolidated from the date control ceases. The acquisition method of accounting is used to account for business combinations. The cost of an acquisition is measured as the fair value of the assets given up, shares issued or liabilities undertaken at the date of acquisition whereby costs directly attributable to the acquisition are expensed for transactions closed after January 1, 2010. The excess of the cost of acquisition over the fair value of the net assets and contingent liabilities of the subsidiary acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognized directly in the Profit for the year (Other operating income).

If applicable, the Group recognizes at the acquisition date a liability for any contingent purchase consideration. If the amount of contingent consideration accounted for as a liability changes as a result of a post-acquisition event (such as meeting an earnings target), it is recognized in accordance with other applicable IFRSs, as appropriate rather than as an adjustment of goodwill for acquisitions concluded after January 1, 2010. For acquisitions concluded before, the difference between the contingent consideration recognized at the acquisition date and the actual contingent consideration paid is recognized as an adjustment to goodwill.

As for the measurement of non-controlling interest, from January 1, 2010, the Group may recognize 100% of the goodwill of the acquired entity, not only the Group's portion of the goodwill. This is elected on a transaction-by-transaction basis. Before that date, the Group could only recognize its own share of the goodwill. The Group attributes their share of losses to the non-controlling interests even if this results in the non-controlling interests having a deficit balance since January 1, 2010. Before that date, the balance of the Non controlling interests could not be a negative amount and thus these losses would be allocated to the Group.

In a step acquisition, the fair values of the acquired entity's assets and liabilities, including goodwill, are measured on the date when control is obtained. Accordingly, goodwill is measured as the difference at the acquisition date between the fair value of any investment the business held before the acquisition, the consideration transferred and the fair value of the net asset acquired and non-controlling interest is recorded at fair value when the Group elects the fair value option.

In case of acquisitions where the transaction takes place between companies under common control (i.e. with other Deutsche Telekom group companies), the transaction is recorded at the carrying amounts as recorded in the selling owner's accounts, and any gains, losses or differences between the carrying amount and the sale-purchase price are recognized in Retained earnings.

A partial disposal of an investment in a subsidiary while control is retained is accounted for as an equity transaction with owners, therefore gain or loss is not recognized in profit or loss for disposals concluded since January 1, 2010. Before that date, the gain or loss was recognized as a current year income.

A partial disposal of an investment in a subsidiary that results in loss of control triggers re-measurement of the residual interest to fair value. Any difference between fair value and carrying amount is a gain or loss on the disposal, recognized in profit or loss since January 1, 2010. Before that date, no such re-measurement took place.

Inter-company transactions, balances and unrealized gains on transactions between the Magyar Telekom Group companies are eliminated. Accounting policies of subsidiaries have been adjusted to ensure consistency with the policies adopted by the Group.

At December 31, 2011 and 2010 the principal operating subsidiaries of the Group were as follows:

Subsidiaries	Group interest in capital as at December 31, 2010	2011	Activity
Incorporated in Hungary:			
Dataplex Kft., Budapest	100.00%	100.00%	IT hardware co-location service provider
Origo Zrt., Budapest	100.00%	100.00%	Internet and TV content provider
KFKI Zrt., Budapest	100.00%	100.00%	System integration and IT services
IQSYS Zrt., Budapest	100.00%	100.00%	System integration and IT services
Pro-M Zrt., Budapest	100.00%	100.00%	Professional Mobile Radio (PMR) network operator
ISH Kft., Budapest	100.00%	100.00%	Integrated healthcare IT services
Daten-Kontor Kft., Budapest	-	100.00%	Software development
Telekom New Media Zrt., Budapest	100.00%	100.00%	Interactive service provider of telecommunications applications
Incorporated in Macedonia:			
Makedonski Telekomunikacii A. D., Skopje (MKT)	56.67%	56.67%	Fixed line telecom service provider
T-Mobile Macedonia A. D., Skopje (T-Mobile MK)	56.67%	56.67%	Cellular telecom service provider
Stonebridge A. D., Skopje	100.00%	100.00%	Holding company
Incorporated in Montenegro:			
Crnogorski Telekom a. d., Podgorica (CT)	76.53%	76.53%	Telecom service provider
Incorporated in Romania:			
Combridge S.R.L., Bucharest	100.00%	100.00%	Wholesale telecommunications service provider
Incorporated in Bulgaria:			
Novatel EOOD, Sofia	100.00%	100.00%	Wholesale telecommunications service provider
Incorporated in the Ukraine:			
Novatel Ukraine LLC., Kiev	100.00%	100.00%	Alternative telecommunications and internet service provider

The Group's interest in the capital of the above subsidiaries equals the voting rights therein.

2.2.2 Associates and joint ventures

Associates are all entities over which the Group has significant influence but not control, generally reflecting a voting right between 20% and 50%. Joint ventures are entities in which the Group has a voting right of 50% with and equivalent external partner holding the other 50% of the voting rights. Investments in associates and joint ventures are accounted for using the equity method of accounting and are initially recognized at cost. The Group's investment in associates and joint ventures includes goodwill arising on acquisitions, and net of any accumulated impairment loss.

The Group's share of its associates' and joint ventures' post-acquisition profits or losses is recognized in the Profit for the year (Share of associates' and joint ventures' profits). The cumulative post-acquisition movements are adjusted against the carrying amount of the investment. When the Group's share of losses in an associate or joint venture equals or exceeds its interest in the company, the Group does not recognize further losses, unless it has incurred legal or constructive obligations or made payments on behalf of the associate or joint venture.

Unrealized gains on transactions between the Group and its associates and joint ventures are eliminated to the extent of the Group's interest in the company. Accounting policies of associates and joint ventures have been adjusted where necessary to ensure consistency with the policies adopted by the Group.

At December 31, 2011 the Group had no associates or joint ventures, while at the end of 2010 the Group had one insignificant operational associate and one joint venture in liquidation, which was completed in 2011.

2.3 Foreign currency translation

2.3.1 Functional and presentation currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ('the functional currency').

The consolidated financial statements are presented in millions of HUF, as the Group's presentation currency is the Hungarian Forint.

2.3.2 Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognized in the Profit for the year (Other finance expense - net).

2.3.3 Group companies

The income and financial position of all of the Group's entities (none of which has the currency of a hyperinflationary economy) that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- For the initial consolidation of foreign subsidiaries acquired, their assets and liabilities at the acquisition date are incorporated into the consolidated financial statements after translating the balances into HUF using the exchange rate prevailing at the date of acquisition. The fair value adjustments resulting from the purchase price allocation and goodwill are accounted for in HUF for acquisitions before March 31, 2004, after which date these adjustments arising on consolidation are accounted for in the functional currency of the subsidiary.

- Assets and liabilities for each Statement of financial position presented are translated at the closing rate at the date of that Statement of financial position.

- Statements of comprehensive income are translated at cumulated average exchange rates.

- All resulting exchange differences are recognized directly in the consolidated equity (Cumulative translation adjustment). When a foreign operation is fully or partially disposed of so that control is given up, exchange differences that were recorded in equity are recognized in the Profit for the year as part of the gain or loss on sale.

2.4 Financial instruments

A financial instrument is any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity.

Financial assets of the Group include cash and cash equivalents, equity instruments of another entity (available-for-sale) and contractual rights to receive cash (trade and other receivables) or another financial asset from another entity or to exchange financial assets or financial liabilities with another entity under conditions that are potentially favorable to the entity (derivatives).

Financial liabilities of the Group include liabilities that originate from contractual obligations to deliver cash or another financial asset to another entity (non-derivatives); or to exchange financial assets or financial liabilities with another entity under conditions that are potentially unfavorable to the entity (derivatives).

Financial liabilities, in particular, include liabilities to banks and related parties, finance lease payables, trade payables and derivative financial liabilities.

Finance lease receivables and liabilities meet the criteria of a financial instrument, but these are recognized and measured according to IAS 17 – Leases. See Note 2.17.

The fair value of traded financial instruments is determined by reference to their market prices at the end of the reporting period. This typically applies to available-for-sale (AFS) financial instruments.

The fair value of financial instruments that are not traded in an active market (e.g. derivative financial instruments) is determined by using discounted cash flow valuation technique. The fair value of forward foreign exchange contracts is determined using quoted spot exchange rates and appropriate interest rates at the end of the reporting period.

The fair value of other financial instruments is also determined by using discounted cash flow valuation technique. The expected quarterly cash inflows or outflows are discounted by market based interest rates interpolated from the official Budapest and EUR Interest Rate Swap.

The fair value of long term fixed-rate financial liabilities (Financial liabilities to related parties, Bank loans and Nonconvertible bonds and debentures) is also determined by using discounted cash flow valuation technique. The cash flows of the liabilities are discounted by interest rates, which are reasonable to the Group for similar financial instruments. The carrying amount of floating-rate financial liabilities or those expiring within one year approximate the fair values at the end of the reporting period.

Assumptions applied in the fair value calculations are subject to uncertainties. Changes in the assumptions applied in the calculations would have an impact on the carrying amounts, the fair values and/or the cash flows originating from the financial instruments. Sensitivity analyses related to the Group's financial instruments are provided in Note 3.

2.4.1 Financial assets

The Group classifies its financial assets in the following categories:

- at fair value through profit or loss
- loans and receivables
- available-for-sale (AFS)
- held-to-maturity

The classification depends on the purpose for which the financial asset was acquired. Management determines the classification of financial assets at their initial recognition.

Standard purchases and sales of financial assets are recognized on the trade-date, the date on which the Group commits to purchase or sell the asset. Investments are initially recognized at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets carried at fair value through profit or loss are initially recognized at fair value, and transaction costs are expensed in the Profit for the year.

The Group assesses at each financial statement date whether there is objective evidence that a financial asset is impaired. There is objective evidence of impairment if as a result of loss events that occurred after the initial recognition of the asset have an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

Impairment losses of financial assets are recognized in the Profit for the year against allowance accounts to reduce the carrying amount until the derecognition of the financial asset, when the net carrying amount (including any allowance for impairment) is derecognized from the Statement of financial position. Any gains or losses on derecognition are calculated and recognized as the difference between the proceeds from disposal and the (net) carrying amount derecognized.

Financial assets are derecognized when the rights to receive cash flows from the investments have expired or have been transferred and the Group has transferred substantially all risks and rewards of ownership.

2.4.1.1 Financial assets at fair value through profit or loss

The "financial assets at fair value through profit or loss" measurement category includes the following financial assets:

- Financial assets that are designated as "at fair value through profit or loss" using the fair value option as per IAS 39
- Financial assets incurred for the purpose of selling immediately or in the near term and thus classified as "held for trading"
- Derivative financial assets are classified as "held for trading"

Assets in this category are normally classified as current assets (Other financial current assets). Derivatives aimed to hedge the cash flow risk of non current financial instruments are classified as non current assets (Other financial non current assets).

No reclassification between categories has been made in the past and no reclassifications are expected in the future.

Assets in this category are initially recognized and subsequently carried at fair value. Gains or losses arising from changes in the fair value and impairment losses or their reversals are recognized in the Profit for the year (Other finance expense - net) in the period in which they arise. The Group only classifies derivative financial instruments in this category.

Derivatives are initially recognized at fair value on the date a derivative contract is entered into and their fair values are re-measured at subsequent financial statement dates. Magyar Telekom does not apply hedge accounting for its financial instruments, therefore all gains and losses are recognized in the Profit for the year (Other finance expense - net).

2.4.1.2 Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Receivables are included in current assets, except those with maturities over 12 months after the financial statement date. These are classified as Other non-current financial assets.

The following items are assigned to the "loans and receivables" measurement category.

- cash and cash equivalents,
- trade receivables,
- other receivables,
- employee loans,
- loans granted to related parties and third parties.

Loans and receivables are initially recognized at fair value and subsequently carried at amortized cost using the effective interest method, less any impairment.

The carrying amount of loans and receivables, which would otherwise be past due, whose terms have been renegotiated is not impaired if the collectability of the renegotiated cash flows are considered ensured.

(a) Cash and cash equivalents

Cash and cash equivalents include cash on hand and in banks, and all highly liquid deposits and securities with original maturities of three months or less, and exclude all overdrafts.

Should an impairment on cash and cash equivalents occur, it would be recognized in the Profit for the year (Other finance expense - net).

(b) Trade and other receivables

Trade and other receivables are recognized initially at fair value and subsequently measured at amortized cost using the effective interest method, less provision for impairment.

A provision for impairment of trade and other receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the underlying arrangement. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganization, and default or delinquency in payments as well as historical collections are considered indicators that the trade receivable is impaired.

If there is objective evidence that an impairment loss on loans and receivables carried at amortized cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate (i.e. the effective interest rate computed at initial recognition). The carrying amount of the asset is reduced through the use of an allowance account, and the amount of the loss is recognized in the Profit for the year (Other operating expenses – Bad debt expense).

The Group first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and collectively for financial assets that are not individually significant. If no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, Magyar Telekom includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is recognized are not included in a collective assessment of impairment.

The Group's benchmark policy for collective assessment of impairment is based on the aging of the receivables due to the large number of relatively similar type of customers.

Individual valuation is carried out for customers under litigation; bankruptcy proceedings and for the total receivables of customers with overdue receivables. Itemized valuation is also performed in special circumstances, if there is an overdue receivable from any designated customer with different credit risk attributes.

When a trade or an other receivable is established to be uncollectible, it is written off with a parallel release of cumulated impairment against Other operating expenses in the Profit for the year (Bad debt expense). Subsequent recoveries of amounts previously written off are credited against the same line of the Statement of comprehensive income.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized (such as an improvement in the debtor's credit rating), the previously recognized impairment loss shall be reversed by adjusting the allowance account. The reversal shall not result in a carrying amount of the financial asset that exceeds what the amortized cost would have been had the impairment not been recognized at the date the impairment is reversed. The amount of the reversal shall be recognized in the Profit for the year as a reduction to Other operating expenses (Bad debt expense).

Amounts due to, and receivable from, other network operators are shown net where a right of set-off exists and the amounts are settled on a net basis (such as interconnection receivables and payables).

(c) Employee loans

Employee loans are recognized initially at fair value and subsequently measured at amortized cost using the effective interest method, less any impairment loss.

The difference between the nominal value of the loan granted and the initial fair value of the employee loan is recognized as prepaid employee benefits. Interest income on the loan granted calculated by using the effective interest method is recognized as Interest income, while the prepaid employee benefits are amortized to Employee related expenses evenly over the term of the loan.

Impairment losses on Employee loans are recognized in the Profit for the year (Employee related expenses).

(d) Loans granted to related parties and third parties

Loans granted to related parties and third parties include short term loans and deposits made with DTAG or other trading partners.

Impairment losses on Loans granted to related parties and third parties are accounted for in the Profit for the year (Other finance expense - net).

2.4.1.3 Available-for-sale (AFS) financial assets

AFS financial assets are non-derivative financial assets that are either designated in this category or not classified in any of the other categories. They are included in Other non current financial assets unless management intends to dispose of the investment within 12 months of the financial statement date. In this latter case they are included in current assets (Other financial assets).

The “available-for-sale financial assets” measurement category includes:

- listed equity instruments that are neither consolidated nor included using the equity method in the consolidated financial statements
- unlisted equity instruments that are neither consolidated nor included using the equity method in the consolidated financial statements
- debt instruments

AFS financial assets are initially recognized and also subsequently carried at fair value. The unrealized changes in the fair value of available-for-sale financial assets are recognized in equity (Revaluation reserve for AFS financial assets).

Interest on available-for-sale debt securities calculated using the effective interest method is recognized in the Profit for the year (Interest income). Dividends on available-for-sale equity instruments are recognized in the Profit for the year (Other finance expense - net) when the Group’s right to receive payments is established.

The Group assesses at each financial statement date whether there is objective evidence that a financial asset is impaired. There is objective evidence of impairment if as a result of loss events that occurred after the initial recognition of the asset have an impact on the estimated future cash flows of the financial asset that can be reliably estimated. If any such evidence exists for AFS financial assets, the cumulative unrealized gain (if any) is reclassified from Other comprehensive income to Profit for the year, and any remaining difference is also recognized in the Profit for the year (Other finance expense - net). Impairment losses recognized on equity instruments are not reversed through the Profit for the year, while impairment losses recognized on debt instruments are reversed through the Profit for the year.

When AFS financial assets are sold or redeemed, therefore derecognized, the fair value adjustments accumulated in equity are reclassified from Other comprehensive income to Profit for the year (Other finance expense - net).

2.4.1.4 Held-to-maturity investments

This category includes non-derivative financial assets with fixed or determinable payments and fixed maturity that the Group has the positive intention and ability to hold to maturity. The Group does not classify any of its financial instruments in this category.

2.4.2 Financial liabilities

There are two measurement categories for financial liabilities used by the Group:

- Financial liabilities carried at amortized cost
- Financial liabilities at fair value through profit or loss

No reclassification between categories has been made in the past and no reclassifications are expected in the future. Both types of financial liabilities are initially recognized at fair value, while subsequent measurements are different (see below). We remove a financial liability (or a part of a financial liability) from the Statement of financial position when, and only when, it is extinguished – i.e. when the obligation specified in the contract is discharged, cancelled or expired.

2.4.2.1 Financial liabilities carried at amortized cost

The measurement category for “financial liabilities measured at amortized cost” includes all financial liabilities not classified as “at fair value through profit or loss”.

(a) Loans and other borrowings

Borrowings are recognized initially at fair value less transaction costs, and subsequently measured at amortized costs using the effective interest rate method. The effective interest is recognized in the Profit for the year (Interest expense) over the period of the borrowings.

(b) Trade and other payables

Trade and other payables (including accruals) are recognized initially at fair value and subsequently measured at amortized cost using the effective interest method. The carrying values of trade and other payables approximate their fair values due to their short maturity.

2.4.2.2 Financial liabilities at fair value through profit or loss

Since the Group currently has no intention of measuring non-derivative financial liabilities at fair value, generally only derivative financial instruments are assigned to this category.

The Group does not designate any derivatives as hedging instruments, therefore, all derivatives are classified as “held for trading”.

Derivatives are initially recognized at fair value on the date a derivative contract is entered into and their fair values are re-measured at subsequent financial statement dates. Magyar Telekom does not apply hedge accounting for its financial instruments, therefore all gains and losses are recognized in the Profit for the year (Other finance expense - net).

The Group considers only those contracts as a separable host contract and an embedded derivative which are denominated neither in the functional currency of either of the contracting parties nor in a currency that is commonly used in contracts to purchase or sell non-financial items in the economic environment in which the transaction takes place (e.g. a relatively stable and liquid currency that is commonly used in local business transactions or external trade). The Group has identified EUR and USD (except Montenegro) as currencies commonly used in the Group’s operating area.

2.5 Inventories

Inventories are stated at the lower of cost or net realizable value using the historical cost method of accounting, and are valued on a weighted average basis. The cost of inventories comprises all costs of purchase, cost of construction and other costs incurred in bringing the inventories to their present location and condition. Net realizable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

Phone sets are often sold for less than cost in connection with promotions to obtain new subscribers with minimum commitment periods (Note 4.6). Such loss on the sale of equipment is only recorded when the sale occurs if the normal resale value is higher than the cost of the phone set. If the normal resale value is lower than costs, the difference is recognized as impairment immediately.

Impairment losses on Inventories are recognized in Other operating expenses (Materials, maintenance and service fees).

2.6 Non current assets held for sale

An asset is classified as held for sale if it is no longer needed for the future operations of the Group, and has been identified for sale, which is highly probable and expected to take place within 12 months. These assets are accounted for at the lower of carrying value or fair value less cost to sell. Depreciation is discontinued from the date of designation to the held for sale status. When an asset is designated for sale, and the fair value is determined to be lower than the carrying amount, the difference is recognized in the Profit for the year (Depreciation and amortization) as an impairment loss.

2.7 Property, plant and equipment (PPE)

Property, plant and equipment are stated at historical cost less accumulated depreciation and impairment losses.

The cost of an item of PPE comprises its purchase price, including import duties and non-refundable purchase taxes, after deducting trade discounts and rebates, any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management. The initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located is also included in the costs if the obligation incurred can be recognized as a provision according to IAS 37 – Provisions, Contingent Liabilities and Contingent Assets.

Government grants relating to the purchase of PPE are deducted from the original cost of the items and are recognized in the Profit for the year through the reduced amount of depreciation of the related assets over their useful lives. Investment tax credits relating to qualifying investment projects (Note 9.5) are also recognized in this manner.

Cost in the case of telecommunications equipment comprises of all expenditures including the cabling within customers' premises and borrowing costs of related loans.

Subsequent expenditure on an asset that meets the recognition criteria to be recognized as an asset or an addition to an asset is capitalized, while maintenance and repairs are charged to expense when incurred.

When assets are scrapped, the cost and accumulated depreciation are removed from the accounts and the loss is recognized in the Profit for the year (Depreciation and amortization).

When assets are sold, the cost and accumulated depreciation are removed from the accounts and any related gain or loss is recognized in the Profit for the year (Other operating income).

Depreciation is calculated on a straight-line basis from the time the assets are deployed and charged over their economic useful lives. On an annual basis, Magyar Telekom reviews the useful lives and residual values for consistency with current development plans and advances in technology. For further details on the groups of assets impacted by the most recent useful life revisions refer to Note 12. The annual revisions are conducted in the second quarter of the year and the resulting changes are applied from the third quarter of the year. In addition to the regular revisions, any investment decisions made throughout the year may also result in a change of useful life of a group of assets in any period of the year.

2.8 Intangible assets

Intangible assets are stated at historical cost less accumulated amortization and impairment losses.

Acquired computer software licenses are capitalized on the basis of the costs incurred to acquire and bring to use. These costs are amortized over the estimated useful life of the software. Costs associated with developing or maintaining computer software programs are generally recognized as an expense as incurred. Costs directly associated with the production of identifiable and unique software products controlled by the Group, and that will probably generate economic benefits exceeding costs beyond one year, are recognized as intangible assets. Direct costs include the software development employee related costs and an appropriate portion of relevant overhead. Computer software development costs recognized as assets are amortized over their estimated useful lives. As these assets represent an immaterial portion of all software, these are not disclosed separately.

Costs associated with the acquisition of long term frequency licenses are capitalized including any related borrowing costs. The useful lives of concessions and licenses are determined based on the underlying agreements and are amortized on a straight line basis over the period from availability of the frequency for commercial use until the end of the initial concession or license term. No renewal periods are considered in the determination of useful life.

Amortization is calculated on a straight-line basis from the time the assets are deployed and charged over their economic useful lives. On an annual basis, Magyar Telekom reviews the useful lives for consistency with current development and replacement plans and advances in technology. For further details on the groups of assets impacted by the most recent useful life revisions refer to Note 13. The annual revisions are conducted in the second quarter of the year and the resulting changes are applied from the third quarter of the year. In addition to the regular revisions, any investment decisions made throughout the year may also result in a change of useful life of a group of assets in any period of the year.

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net assets and contingent liabilities of the acquired subsidiary or business at the date of acquisition. Goodwill is carried at cost less accumulated impairment losses. Impairment testing is carried out on an annual basis for all goodwill in the last quarter of the year based on the carrying values as at September 30 of the year. Impairment losses on goodwill are not reversed. Gains and losses on the disposal of an entity or business include the carrying amount of goodwill relating to the entity or business sold.

In determining whether an asset that incorporates both intangible and tangible elements should be treated under IAS 16 - Property, Plant and Equipment or as an intangible asset under IAS 38 – Intangible Assets, management uses judgment to assess which element is more significant and recognizes the assets accordingly.

2.9 Impairment of PPE and intangible assets

Assets that are subject to amortization or depreciation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of the assets' fair value less costs to sell and its value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units - CGUs).

The fair values of the individual tangible and intangible assets of the Group in most cases cannot be determined as individual assets do not generate cash flows. Instead, the Group determines CGUs to which the individual assets are allocated and the fair values can only be determined at CGU level, primarily by using discounted cash flow analyses.

See also Note 4.3. Corporate assets which have the distinctive characteristics of not generating cash inflows independently of other assets or groups of assets are allocated to CGUs when conducting impairment tests.

Goodwill is tested for impairment annually or more frequently if circumstances indicate that impairment may have occurred. When conducting the impairment tests, Magyar Telekom allocated goodwill to its cash generating units or groups of cash generating units, which, in 2010 in the vast majority of the cases, were determined at the operating segment level. In 2011, the goodwill was allocated and tested at operating segment level. See also Note 4.2. Operating segments may include one clearly identifiable company or a group of companies, or components of one company and other companies as well.

For the subsidiaries included in the operating segments the Group establishes the subsidiaries' recoverable amounts by determining their fair value less cost to sell by using valuation techniques. These include the use of recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analyses and option pricing models, making maximum use of market inputs and relying as little as possible on entity-specific inputs. The fair values determined as described above are used as a basis when establishing the need for an impairment of any goodwill allocated to the CGUs or the operating segments. See also Note 4.2. If the calculated fair value less cost to sell is lower than the carrying amount of the operating segment, goodwill is impaired.

The impairment losses of PPE and intangible assets are accounted for in the Depreciation and amortization line of the Statement of comprehensive income.

2.10 Provisions and contingent liabilities

Provisions are recognized when Magyar Telekom has a present legal or constructive obligation as a result of past events and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made.

Provisions are measured and recorded as the best estimate of the economic outflow required to settle the present obligation at the financial statement date. The estimate can be calculated as the weighted average of estimated potential outcomes or can also be the single most likely outcome. Expenses for provisions are recognized in the statement of comprehensive income line where the actual expense is expected to be incurred. When a provision is released unused, it is released to the same statement of comprehensive income line where it was originally provided for. Provisions made for liabilities expected to be incurred in foreign currency are recognized in the functional currency at the spot FX rate, and any change in the provision in the functional currency as a result of a subsequent change in the FX rate is recognized in Other finance expense – net.

Provisions for obligations expected to fall due after 12 months are generally recognized at their present value and are accreted (against Interest expense) until utilization or reversal.

No provision is recognized for contingent liabilities. A contingent liability is a possible obligation that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity; or a present obligation that arises from past events but is not recognized because it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation or the amount of the obligation cannot be measured with sufficient reliability.

2.11 Treasury stock

When the Company or its subsidiaries purchase the Company's equity shares, the consideration transferred including any attributable incremental external costs are deducted from the Equity of the owners of the parent as Treasury stock until they are re-sold or cancelled. When such shares are subsequently sold, the treasury share balance decreases by the original cost of the shares, thereby increasing equity, while any gains or losses are also recognized in equity (Retained earnings). Treasury stock transactions are recorded on the transaction date.

2.12 Revenues

Revenues for all services and equipment sales (Note 22) are shown net of VAT, discounts and excluding sales within the Group. Revenue is recognized when the amount of the revenue can be reliably measured, and when it is probable that future economic benefits will flow to the Group and all other specific recognition criteria of IAS 18 or IAS 11 on the sale of goods and rendering of services are met for the provision of each of the Group's services and sale of goods.

Customers of the Group are granted loyalty awards (credit points) based on their usage of the Group's services including timely payment of their invoices. Loyalty awards can be accumulated and redeemed to obtain future benefits (e.g. call credits, handset discounts, etc.) from the operators of the Group. When customers earn their credit points, the fair value of the credit points earned are deducted from the revenue invoiced to the customer, and recognized as Other liabilities (deferred revenue). On redemption (or expiry) of the points, the deferred revenue is released to revenue as the customer collected (or waived) the undelivered element of the deemed bundle.

Revenues from operating leases are recognized on a straight line basis over the period the services are provided. Operating lease revenues are primarily included in the System integration and IT revenues.

2.12.1 Fixed line and mobile telecommunications revenues

Revenue is primarily derived from services provided to Magyar Telekom's customer subscribers and other third parties using Magyar Telekom's telecommunications network, and equipment sales.

Customer subscriber arrangements typically include an equipment sale, subscription fee and charge for the actual voice, internet, data or multimedia services used. The Group considers the various elements of these arrangements to be separate earnings processes and classifies the revenue for each of the deliverables into the categories as disclosed in Note 22 using the residual method for each of the elements. These units are identified and separated, since they have value on a standalone basis and are sold not only in a bundle, but separately as well. Therefore the Group recognizes revenues for all of these elements using the residual method which is the amount of consideration allocated to the delivered elements of the arrangements equals the total consideration less the fair value of the undelivered elements.

The Group provides customers with narrow and broadband access to its fixed, mobile and TV distribution networks. Service revenues are recognized when the services are provided in accordance with contractual terms and conditions. Airtime revenue is recognized based upon minutes of use and contracted fees less credits and adjustments for discounts, while subscription and flat rate revenues are recognized in the period they relate to.

Revenues and expenses associated with the sale of telecommunications equipment and accessories are recognized when the products are delivered, provided that there are no unfulfilled obligations that affect the customer's final acceptance of the arrangement.

Advertising revenues are recognized in the period that the advertisements are exhibited.

Revenues from premium rate services (Voice and non-voice) are recognized on a gross basis when the delivery of the service over Magyar Telekom's network is the responsibility of the Group, the Group establishes the prices of these services and bears substantial risks of these services, otherwise these revenues are presented on a net basis.

Customers may also purchase prepaid mobile, public phone and internet credits ("cards") which allow those customers to use Magyar Telekom's telecommunications network for a selected amount of time. Customers must pay for such services at the date when the card is purchased. Revenues from the sale of cards are recognized when used by the customers or when the credits expire with unused traffic.

Third parties using Magyar Telekom's telecommunications network include roaming customers of other service providers and other telecommunications providers which terminate or transit calls on Magyar Telekom's network. These wholesale (incoming) traffic revenues included in Voice and Non-voice (Data and Internet) revenues are recognized in the period of related usage. A proportion of the revenue received is often paid to other operators (interconnect) for the use of their networks, where applicable. The revenues and costs of these transit calls are stated gross in the Financial statements as the Group is the principal supplier of these services using its own network freely defining the pricing of the services, and recognized in the period of related usage.

2.12.2 System integration and IT revenues

Contracts for network services, which consist of the installation and operation of communication networks for customers, have an average duration of 2-3 years. Revenues for voice and data services are recognized under such contracts when used by the customer.

Revenue from outsourcing contracts reflects the extent of actual services delivered in the period in accordance with the terms of the contract. The contracts are analyzed based on the requirements of IFRIC 4 - Determining whether an Arrangement contains a Lease, and if they include embedded lease elements, the revenues attributable to these are recognized according to IAS 17 - Leases as described in Note 2.17.

Revenue from system integration contracts requiring the delivery of customized products and/or services is generally covered by one of the following types of contracts: fixed-price or time and material-based. For fixed-price contracts, revenue is generally recognized based on percentage of completion taking into account the proportion that contract costs incurred for work performed to date bear to the estimated total contract costs. In the case of contracts billed on the basis of time and material, revenue is recognized as the services are rendered.

Revenue from maintenance services (generally fixed fee per month) is recognized over the contractual period or as the services are provided. Revenue from repairs, which are not part of the maintenance contract, billed on the basis of time and material used is recognized as the services are provided.

Revenue from hardware and software sales or sales-type leases is recognized when the risk of ownership is substantially transferred to the customer, provided there are no unfulfilled obligations that affect the customer's final acceptance of the arrangement. Any costs of these obligations are recognized when the corresponding revenue is recognized.

Revenues from construction contracts are accounted for using the percentage-of-completion method. The stage of completion is determined on the basis of the costs incurred to date as a proportion of the estimated total costs. Receivables from construction contracts are classified in the Statement of financial position as Trade receivables. If the total actual and estimated expenses exceed revenues for a particular contract, the loss is recognized immediately (in Expenses directly related to revenues) against a provision.

2.13 Employee benefits

2.13.1 Short term employee benefits

Short term employee benefits are recognized as a current expense in the period when employees render their services. These include wages, social security contributions, bonuses, paid holidays, discounted telephone bills, meal and holiday contributions and other fringe benefits and the tax charges thereon.

Payments to defined contribution pension and other welfare plans are recognized as an expense in the period in which they are earned by the employees.

2.13.2 Share based compensation

Magyar Telekom recognizes the costs of services received from its employees in a share based payment transaction when services are received. Magyar Telekom recognizes a corresponding increase in its equity reserves (Reserve for equity settled share based transactions) if the services are received in an equity-settled share based payment transaction. When the share based compensation program is completed, i.e. the shares are transferred to the employees' ownership or the share options have forfeited, the respective reserve is transferred to Retained earnings. If the services are received in a cash-settled share based payment transaction, the Group recognizes the expense against a liability, re-measured at each financial statement date.

Fair values are determined using option pricing models (such as Black-Scholes and Monte Carlo simulation) and other relevant techniques. As Magyar Telekom Plc. is listed and actively traded on the Budapest Stock Exchange, the share price and its history is readily available as a basis for fair value calculations.

Bonuses tied to the long term performance of the Magyar Telekom share are recognized in the Profit for the year at their time-proportioned fair value (Note 24.1) against an accumulating balance in Provisions.

2.13.3 Termination benefits

Termination benefits are payable whenever an employee's employment is terminated before the nominal retirement date or whenever an employee accepts voluntary redundancy in exchange for these benefits. The Group recognizes termination benefits when it is demonstrably committed to either terminate the employment of current employees according to a detailed formal plan without the possibility of withdrawal or to provide termination benefits as a result of an offer made to encourage voluntary redundancy.

2.13.4 Post-employment defined benefits

Magyar Telekom does not have significant post-employment defined benefit schemes.

2.14 Research and Marketing expenses

Research as well as marketing costs are expensed as incurred. Research costs are not material, while marketing expenses are disclosed in Note 25.

2.15 Borrowing costs

Borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset form part of the cost of that asset. Other borrowing costs are recognized as an expense. Borrowing costs include interest and other costs that the Group incurs in connection with the borrowing of funds. The borrowing costs eligible for capitalization are capitalized applying the weighted average of the borrowing costs applicable to the general borrowings of the Group that are outstanding during the period. A qualifying asset is an asset that necessarily takes a substantial period of time, in general over 12 months, to get ready for its intended use.

2.16 Income taxes

2.16.1 Corporate income taxes

Corporate income taxes are payable to the central tax authorities of the countries in which the Group's consolidated entities operate. The basis of the tax is the taxable entities' accounting profit adjusted for non-deductible and non-taxable items. The nominal tax rates and the determination of the tax bases vary among the countries in which the Group operates.

2.16.2 Other income taxes

Other income taxes include certain local and central taxes levied in Hungary on the companies' net margins, determined at a substantially higher level than the corporate tax base, but applying a significantly lower tax rate.

2.16.3 Deferred taxes

Deferred tax is recognized applying the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the Consolidated financial statements. However, deferred tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit. Deferred tax is determined using income tax rates that have been enacted or substantially enacted by the financial statement date and are expected to apply when the related deferred tax asset is realized or the deferred tax liability is settled.

Deferred tax assets are recognized to the extent that it is probable that future taxable profit (or reversing deferred tax liabilities) will be available against which the temporary differences can be utilized.

Deferred tax is also provided on taxable temporary differences arising on investments in subsidiaries and associates and joint ventures, except where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the temporary difference will not reverse in the foreseeable future.

2.17 Leases

2.17.1 Operating lease –Group as lessor

Assets leased to customers under operating leases are included in Property, plant and equipment in the Statement of financial position. They are depreciated over their expected useful lives on a basis consistent with similar assets. Rental income is recognized as revenue on a straight-line basis over the lease term.

2.17.2 Finance lease – Group as lessor

Leases of assets where Magyar Telekom transfers substantially all the benefits and risks of ownership are recognized and disclosed as revenue against a finance lease receivable. The revenue equals the estimated present value of the future minimum lease payments receivable and any unguaranteed residual value (net investment in the lease). The cost of the asset sold in a finance lease transaction is recognized at the inception of the lease. Each lease receipt is then allocated between the receivable and interest income so as to achieve a constant rate of return on the finance receivable balance outstanding. The interest element of the lease receipt is recognized in Interest income.

2.17.3 Operating lease –Group as lessee

Costs in respect of operating leases are charged to the Profit for the year (Operating expenses) on a straight-line basis over the lease term.

2.17.4 Finance lease – Group as lessee

Leases of property, plant and equipment where Magyar Telekom assumes substantially all the benefits and risks of ownership are classified as finance leases. Finance leases are capitalized at the fair value of the asset or if lower, at the estimated present value of the future minimum lease payments against a finance lease payable. Each lease payment is allocated between the finance liability and interest expense so as to achieve a constant rate of interest on the outstanding finance balance payable. The finance lease obligations, net of finance charges, are included in the Statement of financial position (Other financial liabilities). The interest element of the lease payments is charged to the Profit for the year (Interest expense) over the lease period. Property, plant and equipment acquired under finance lease contracts are depreciated over the shorter of the lease term or the useful life of the asset.

2.17.5 Sale and leaseback transactions

Sale and leaseback transactions involve the sale of an asset by Magyar Telekom and the leasing of the same asset or part of it back to Magyar Telekom. When sale and leaseback transactions qualify as finance leases any gain on the sale is deferred and recognized in the Profit for the year over the lease term through lower depreciation expense. If the leaseback qualifies as an operating lease, any gains or losses on the sale are recognized in the Profit for the year (Other operating income) at the time of the sale as the sales price reflects the fair value of the asset, while the lease payments are recognized in the Profit for the year (Operating expenses) on a straight line basis over the period of the lease.

2.18 Earnings per share

Basic earnings per share is calculated by dividing profit attributable to the owners of the Company for the period by the weighted average number of common stocks outstanding. Diluted earnings per share is calculated considering the weighted average number of diluting share options (if any) in addition to the number of common stocks outstanding.

2.19 Dividends

Dividends payable to the Company's shareholders and to Non-controlling shareholders of the Group's subsidiaries are recorded as a liability and debited against equity (Retained earnings or Non-controlling interests) in the Group's financial statements in the period in which the dividends are approved by the shareholders.

2.20 Segments

In the Financial statements, the Group's segments are reported in a manner consistent with the internal reporting provided to the chief operating decision makers, the members of the Management Committee (MC) of Magyar Telekom Plc. The MC is responsible for allocating resources to, and assessing the performance of, the operating segments on a monthly basis. The accounting policies and measurement principles of the operating segments are very similar to those applied for the Group described in the previous sub-notes of the Summary of significant accounting policies. The differences primarily originate from the fact that the operating segments' annual results are determined and closed at an earlier stage, around January 10-12 each year, than these Financial statements. Any items discovered and requiring adjustment between the closing date of the segment results and the approval date of the Financial statements are reflected in the next year's segment results.

The operating segments' revenues include revenues from external customers as well as the internal revenues generated from other segments for telecommunications and, to a lesser extent, from inter-segment support services. In order to concentrate on real performance achieved on third party transactions, the number of inter-segment cross-charges applied within the organizations of Magyar Telekom Plc. operating in different segments is fairly limited. These cross-charges are not meant to allocate all the actual costs to the operating segment which are in fact incurred for the operation of the particular segment. Consequently, regardless of the costs incurred for the operation of another segment, the supporting organizations of the operating segments do not charge revenues for the services delivered within Magyar Telekom Plc., the largest legal entity of the Group.

The operating segments' results are monitored by the MC down to EBITDA (Earnings before interest, tax, depreciation and amortization) level, which is defined by the Group as Operating profit without Depreciation and amortization expense.

The MC does not monitor the assets and liabilities at the segment level.

Another important KPI monitored at segment level is capital expenditure (Capex), which is determined as the gross additions to PPE and Intangible assets, excluding those due to business combinations.

2.21 Comparative information

In order to maintain consistency with the current year presentation in the Financial statements and the Notes thereto, certain items may have been reclassified for comparative purposes. Material changes in disclosures, if any, are described in detail in the relevant Notes. In 2011 there were no material reclassifications.

3 FINANCIAL RISK MANAGEMENT

3.1 Financial risk factors

Magyar Telekom is primarily exposed to credit risks related to its financial assets. In addition, the Group is also exposed to risks from movements in exchange rates, interest rates that affect the fair value and/or the cash flows arising from financial assets and liabilities.

Financial risk management aims to limit these risks through ongoing operational and finance activities. Selected derivative and non-derivative hedging instruments are also used for this purpose, depending on the risk assessment. Magyar Telekom only hedges the risks that affect the Group's cash flows, no hedges are concluded to hedge fair values. Derivatives are exclusively used as hedging instruments, i.e., not for trading or other speculative purposes. To reduce the counterparty risk, hedging transactions are generally only concluded with Deutsche Telekom or leading Hungarian financial institutions. Nevertheless, hedge accounting is not applied to such transactions, considering that not all the criteria in IAS 39 are met.

The detailed descriptions of risks, the management thereof as well as sensitivity analyses are provided below. These sensitivity analyses calculate with reasonably possible changes in the relevant risk variables and their impact on profit before tax. The impacts disclosed below are subject to an average effective income tax rate of approximately 25% (2010: approximately 10%) in the Group, i.e. the impact on Profit for the year would be approximately 75% of the pre tax amount in a year that is free from significant one-off non-deductible pre-tax impacts and significant changes in the tax legislation. The potential impacts disclosed (less tax) would be the same on the Group's Equity.

There were no major changes in these risks compared to the previous reporting period.

3.1.1 Market risk

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises three types of risk: currency risk, interest rate risk and other price risk.

The fundamentals of Magyar Telekom's financing strategy are established each year by the Board of Directors. The Group's policy is to borrow centrally using a balanced combination of medium term and short term loans, and fixed and floating interest rates on those loans. The Board of Directors has approved two debt protection ratio limits, and monitors their fulfillment annually. At the end of 2010 and 2011 Magyar Telekom fulfilled both criteria; Total Debt to EBITDA ratio of 1.88 in 2011 (2010: 1.70), the allowed maximum of which would be 2.5 and EBITDA to Interest Expense ratio of 6.04 in 2011, (2010: 7.58), the allowed minimum of which would be 3.0. The Group's Treasury department is responsible for implementing the finance policy and for ongoing risk management. The details of foreign exchange, liquidity and counterparty risk management guidelines are determined and monitored by the Group Treasurer continuously.

Magyar Telekom is exposed to interest and foreign exchange (FX) rate risk associated with its interest bearing assets and liabilities and anticipated transactions. As the vast majority of the revenues and expenses of the Hungarian entities arise in HUF, the functional currency of Magyar Telekom is HUF. Consequently, Magyar Telekom's objective is to minimize the level of its financial risk in HUF terms.

For the presentation of market risks, we also provided sensitivity analyses that show the effects of hypothetical changes of relevant risk variables on Profit before tax. These hypothetical changes were modeled to present a reasonably possible change in the relevant risk variables. The periodic effects are determined by relating the hypothetical changes in the risk variables to the balance of financial instruments at the end of the latest reporting period (2011) and the preceding reporting period (2010). The balances at the end of the reporting period are usually representative for the year as a whole, therefore the impacts are calculated using the year end balances as though the balances had been constant throughout the reporting period. The methods and assumptions used in the sensitivity calculations did not change significantly. As a result of the still rather volatile international capital and securities markets, higher fluctuations of the FX and interest rates are also possible.

3.1.1.1 Foreign currency risk

Foreign currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in FX rates. Currency risks primarily arise on financial instruments being denominated in a currency that is not the functional currency of the given operating segment of the Group. Differences resulting from the translation of the foreign subsidiaries financial statements into the Group's presentation currency are not taken into consideration. Relevant risk variables are generally all non-functional currencies in which Magyar Telekom has financial instruments.

Due to the free-float of the HUF introduced in 2008, the Group is exposed to FX risk in case of FX denominated financial instruments of the Hungarian entities to a higher degree than before. In order to mitigate this risk, Magyar Telekom minimized its foreign currency borrowings in the past years, or covered them with derivative instruments to substantially reduce FX risk.

(a) FX risks arising on loans from DTIF and related swaps with DT AG

From 2002 to 2009 all new related party loans taken from DT were denominated in HUF. In agreement with Deutsche Telekom, the new related party loans taken to finance general corporate needs from the financing vehicle of Deutsche Telekom, Deutsche Telekom International Finance B.V. (DTIF) from June 2009 are denominated in EUR, while, at the same time, cross-currency interest rate swaps are concluded with Deutsche Telekom AG to fix the actual cash flows of Magyar Telekom in HUF for the whole nominal amount and interest payments of these loans. Even though the Group does not apply hedge accounting, the change in the HUF/EUR exchange rate has limited (net) impact on Profit before tax related to the hedged loans and the swaps together. A 20% weaker HUF would cause an FX loss of approximately HUF 20 billion on the EUR denominated loans, while the swap agreements would have a compensating impact of a gain of approximately HUF 22 billion. A 20% stronger HUF would cause an FX gain of approximately HUF 20 billion on the EUR denominated loans, while the swap agreements would have a compensating impact of a loss of approximately HUF 22 billion.

(b) FX risks arising on third party loans and related swaps

Magyar Telekom also has third party loans denominated in EUR, for the majority of which we also concluded cross-currency interest rate swap agreements with one of the substantial Hungarian banks to eliminate FX risk in connection with these loans and hedge the whole foreign currency denominated cash flows of these loans. Even though the Group does not apply hedge accounting, the change in the HUF/EUR exchange rate has no significant (net) impact on Profit before tax related to the hedged loans and the swaps together.

(c) Other FX exposure

The remaining FX exposure of Magyar Telekom is mostly related to (i) holding foreign currency cash balances in its subsidiaries in the Southern and Eastern Europe region, and (ii) operating activities through revenues from, and payments to, international telecommunications carriers as well as capital expenditure contracted with vendors in foreign currency. In line with currency hedging policy, the Company holds sufficient amounts of foreign currencies on its bank accounts, the amounts of which are determined considering the balance of FX denominated trade and leases payables and trade receivables in order to hedge the currency risk arising in connection with those assets and liabilities. The Group's foreign currency denominated assets (primarily held by the Group's foreign subsidiaries), however, exceed the Group's foreign currency denominated liabilities (other than the above described loans), therefore changes of the functional currencies' exchange rates would have significant impact on the profit of the Group. Compared to the spot FX rates as of December 31, 2011, a 20% weaker functional currency HUF against the EUR and a 35% weaker functional currency HUF against the USD would have caused an unrealized loss of less than HUF 2.4 billion on this net balance (2010: HUF 0.1 billion loss). The same amount of gain would have been caused by a 20% and 35% stronger functional currency HUF against the EUR and USD, respectively. Compared to the spot FX rates as of December 31, 2011, a 15% weaker functional currency MKD against the EUR and USD would have caused HUF 3.5 billion unrealized gain on this net balance (2010: HUF 3.9 billion gain). The same amount of loss would have been caused by a 15% stronger functional currency MKD against the EUR and USD.

In order to reduce the above exposure, Magyar Telekom occasionally enters into derivative contracts. The fair value of the open short term forward positions was HUF 3.5 billion (asset) as of December 31, 2011 (2010: HUF -666 million (liability)). These positions were opened to hedge the FX risks of future FX payments exceeding FX income. Compared to the spot FX rates as of December 31, 2011, a 20% weaker functional currency HUF against the EUR and a 35% weaker functional currency HUF against the USD would have caused HUF 18.4 billion unrealized gain on this net balance while a 20% and 35% stronger HUF against the EUR and USD, respectively would have caused HUF 11.3 billion unrealized loss.

As a result of the volatile international capital and securities markets, even a more than 20% fluctuation of the functional currency HUF against EUR and a more than 35% fluctuation of the functional currency HUF against USD and a more than 15% fluctuation of the functional currency MKD against the EUR and USD is possible as extraordinary market conditions may cause extreme volatility on FX markets.

3.1.1.2 Interest rate risk

Magyar Telekom is also exposed to interest rate fluctuations. This is due to the fact that changing interest rates affect the fair value of the fixed rate instruments and also affect the cash flows through the floating rate instruments.

Changes in the market interest rates of non-derivative financial instruments with fixed interest rates only affect income if these are measured at their fair value. On the other hand, all financial instruments with fixed interest rates (which are carried at amortized cost) are not subject to cash flow interest rate risk.

Changes in the market interest rate of interest rate derivatives (interest rate swaps, cross-currency swaps) that are not part of a hedging relationship as set out in IAS 39 affect financial income or expense (net gain/ loss from re-measurement of the financial assets to fair value).

Changes in market interest rates affect the interest income or expense of non-derivative floating-interest financial instruments for which no cash flow hedges are in place.

(a) Financial assets

Excess cash of the Group's Hungarian operations is primarily used to repay loans, however, significant amount of cash of the Group's Macedonian and Montenegrin subsidiaries are held in local banks. These amounts are deposited primarily on fixed interest rate terms in order to minimize exposure to market changes that would potentially adversely change the cash flows from these instruments.

The Group had no significant HUF denominated bank deposits at the end of 2011 and 2010.

The Group's MKD denominated bank deposits amounted to HUF 19.3 billion at the end of 2011 (2010: HUF 15.7 billion). A 1 percentage point higher interest rate throughout 2011 (assuming the year-end 2011 balance throughout 2011) would have resulted in HUF 0.2 billion higher interest income in 2011 (2010: HUF 0.2 billion). The interest income would be lower by the same amount in case of 1 percentage point lower interest rate.

The Group's EUR denominated bank deposits amounted to HUF 40.5 billion at the end of 2011 (2010: HUF 38.0 billion). A 1 percentage point higher interest rate throughout 2011 (assuming the year-end 2011 balance throughout 2011) would have resulted in HUF 0.4 billion higher interest income in 2011 (2010: HUF 0.4 billion). The interest income would be lower by the same amount in case of 1 percentage point lower interest rate.

As a result of the volatile international capital and securities markets, a higher fluctuation of the interest rates is also possible, the exposure to which is mitigated by the balanced portfolio of fixed and floating interest rate deposits (see above). Sensitivities have been disclosed for a movement of 1 percentage point for EUR, but extraordinary market conditions may cause extreme volatility on money markets, which can result in even higher percentage point change in interest rates.

(b) Financial liabilities

Financial liabilities exposed to interest rate risk are primarily the related party (DTIF) and third party loans and the related swap agreements in place. These loans are almost exclusively taken by the Company as the financing of the Group is managed centrally. The analysis below describes the Group's net exposure to the net interest rate risks related to the loans and the related swap agreements.

As the vast majority of debt portfolio is denominated in HUF, or swap agreements are in place so that the loans payable are exposed to changes in HUF interest rates, the Group is mostly exposed to the HUF interest rate fluctuations for its financial liabilities. To control this interest rate risk, a combination of fixed and floating rate debt is used. Fixed interest-bearing debts (including loans swapped to fixed interest and excluding loans swapped to floating interest) made up 58% of the Group's total debt as of December 31, 2011 (2010: 63%).

In addition, some of the Group's loan agreements with Deutsche Telekom include a fixed interest rate that in fact may change in case of downgrading the credit rating of Deutsche Telekom by specific international rating agencies below the level of credit rating BBB+. Such rating downgrades from the current grade would have caused additional annual interest payments of approximately HUF 0.2 billion (assuming the year-end 2011 balance and rating throughout 2011) on top of the pre-fixed amount of interest (2010: HUF 0.2 billion). On the other hand, such rating upgrades would have caused no change in interest expense for 2011 as loans affected by DT credit rating upgrade matured in 2011 (2010: HUF 0.2 billion lower interest expense in case of rating upgrades above the level of the credit rating A assuming the year-end 2010 balance and rating throughout 2010).

Floating interest-bearing debts (including loans swapped to floating interest and excluding loans swapped to fixed interest) made up 42% of the Group's total debt as of December 31, 2011 (2010: 37%). A 2 percentage point higher interest rate throughout 2011 (assuming the year-end 2011 balance throughout 2011) would have resulted in HUF 2.9 billion higher interest expense in 2011, while the same decrease of interest rates would cause the same decrease in interest payments (2010: HUF 2.7 billion).

The fair value of the swap agreements contracted with DT are also exposed to changes in the HUF and EUR interest rates. Assuming an unchanged HUF interest but an increase of 1% in the EUR interest rates, the fair value of the swap agreements would also change causing a loss of HUF 3.7 billion, while a 1% decrease in the EUR rates would result in an income of HUF 3.8 billion. Similarly, assuming an unchanged EUR interest but an increase of 2% in the HUF interest rates, the fair value of the swap agreements would also change resulting in an income of HUF 4.4 billion, while a 2% decrease in the HUF rates would cause a loss of HUF 4.6 billion.

3.1.1.3 Other price risk

As of the end of the reporting periods, Magyar Telekom did not hold any material investments, which could be affected by risk variables such as stock exchange prices or other indices, therefore, the Group's exposure to such price changes is very limited. See also Note 8.2.

3.1.2 Credit risk

Credit risk is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation.

The maximum exposure to credit risk as at the financial statement dates are represented by the carrying amounts of the financial assets in the Statement of financial position. Guarantee agreements reducing the maximum exposure to credit risk as at the end of the reporting period are described later in this section.

The following table represents Magyar Telekom's maximum exposure to credit risk as at December 31, 2010 and 2011.

In HUF millions	At December 31, 2010	At December 31, 2011
Cash and cash equivalents	15,841	14,451
Bank deposits with original maturities over 3 months	47,798	54,926
Trade receivables	106,732	113,350
Finance lease receivables	20,385	16,783
Employee loans	4,704	5,392
Derivative financial instruments	1,305	14,325
Trade receivables over one year	1,524	1,696
Loans to third parties	947	1,164
Financial assets available for sale	296	278
RDC receivables	715	620
Other current	2,400	1,422
Other non-current	519	270
	203,166	224,677

The vast majority of credit risks may arise in respect of Cash and cash equivalents, Bank deposits with original maturities over 3 months and Trade receivables, and to a lesser extent, of Finance lease receivables. Cash and cash equivalents, Bank deposits with original maturities over 3 months and Trade receivables have short term maturities, which represent the vast majority of the Group's financial assets.

According to the Group's risk management policy Magyar Telekom Group companies deposit the excess cash only in banks rated at least BBB+ (or equivalent), or make efforts to get guarantees for the deposits from banks rated at least BBB+. Moreover, Magyar Telekom prefers to deposit in banks which grants loans for Magyar Telekom to make possible the compensation of debts and loans in case of the default of the bank.

In case of Cash and cash equivalents and Bank deposits with maturities over 3 months held in Hungary concentrations of credit risk are limited as Magyar Telekom places its cash in Hungary with substantial credit institutions. Further, excess HUF cash is also used for repayment of the HUF denominated loans and borrowings, or is deposited at partner banks which grant loans for Magyar Telekom, therefore, the credit risk related to cash held in HUF is very limited.

Cash and cash equivalents and Bank deposits with maturities over 3 months held in Macedonia are primarily denominated in MKD and EUR, while the Cash and cash equivalents and Bank deposits with maturities over 3 months held in Montenegro are primarily denominated in EUR. Cash and cash equivalents and Bank deposits with maturities over 3 months deposited in these countries run higher counterparty risk, due to the small amount of internationally substantial financial institutions in those countries. The bank deposits in Montenegro of HUF 14.1 billion as at December 31, 2011 (2010: HUF 10.1 billion) and those in Macedonia of HUF 45.7 billion as at December 31, 2011 (2010: HUF 43.7 billion) are fully covered with bank guarantees issued by international financial institutions rated at BBB or above, or Magyar Telekom has the right to net the deposits with loans taken from the guarantor, in case of default of the bank. Credit risk related to bank deposits is further limited by the diversification of the deposits among several independent credit institutions determinant on the local market.

Finance lease receivables, in most cases, are legally embedded in service contracts also requiring to provide assets related to the services, which are legally in the Group's ownership. Should the customers fail to pay their bills, we are entitled to discontinue the services and take the assets back to the Group's locations. As these assets are rarely customer specific, we can utilize these assets in other ways as well, therefore, the credit risk related to finance leases is in fact rather limited.

Concentrations of credit risk relating to trade receivables are limited due to the large number of customers comprising the Group's customer base and their dispersion across many different geographic areas and industries.

No financial assets other than trade and other receivables had to be impaired in the reported years, as they are neither past due nor are there any signs of impairment.

The following table contains the carrying amount of trade receivables broken down by country of operation.

In HUF millions	At December 31, 2010	At December 31, 2011
Hungary	88,099	92,902
Macedonia	12,852	13,998
Montenegro	4,792	5,205
Other	989	1,245
	106,732	113,350

The amounts in the table above are shown net of provisions for impairment losses of HUF 34.6 billion as at December 31, 2011 (2010: HUF 34.5 billion). The annual bad debt expense of the Group in 2011 was 1.0% (2010: 1.6%) of the consolidated revenues. Adverse changes in customer payment behavior in the future, however, may result in higher impairment losses. Each additional 1 percentage point of uncollectible revenue would result in additional impairment charges of HUF 6.0 billion in 2011 (2010: HUF 6.1 billion).

Hungary

There are varying credit checking practices applied across the members of the Group. The majority of customers are located in Hungary. For these customers the Company follows the practice described below.

Credit checking at the time of the service request is carried out automatically by the credit checking application of the Sales Department. A variety of checks including checking the bankruptcy list, the internal database of risky installation locations, the collection history of the past 6 months, the outstanding debt and the joint database of debtors of the Hungarian mobile operators are performed depending on the service to be used. The Fraud Detecting System monitors extreme usage and fraudulent behavior of customers for mobile, fixed-line and Internet services. In case of business customers, account managers check if the customer has outstanding debts.

Dunning procedures are run automatically by the billing systems and include various reminder tools like SMS, telephone calls, reminder letters, restricted service, termination letters and disconnections. Over a minimum overdue amount we apply varying and customized reminder procedures with specific deadlines to the different customer groups. After the termination of the contract and depending on the expected success of the process, we combine the different collection steps of involving external partners, selling the outstanding debt or initiating legal proceedings. All parts of the process are regulated by internal directives.

Macedonia

The process of managing the credit risk from operating activities includes preventive measures such as credibility checking and prevention barring, corrective measures during legal relationship (reminding and disconnection activities), collaboration with collection agencies and collection after legal relationship as litigation process, court proceedings and involvement of the executive unit. The overdue payments are monitored through a debt escalation procedure based on customer type, credit class and amount of debt. The credit risk is controlled through credibility checking – which determines that the customer is not indebted and the customers credit worthiness and through preventive barring – which determines the credit limit based on the usual level of the customer's consumption. There is no concentration of risk in Macedonia either with any single customer or group of customers with similar characteristics. The procedures in Macedonia ensure on a permanent basis that sales are made to customers with an appropriate credit history and that an acceptable level of credit exposure is not exceeded.

Montenegro

In Montenegro, receivables management and credit risk control were focus points of the efficiency program in the finance area in 2010 and 2011. In 2010, through organizational change, Customer Finance department has been formed, with the goal of reducing bad debt expenses, when most of the processes have been changed: reminder processes were changed and harmonized to different residential customer segments; strong focus has been given to earlier collection of business revenues; the credit checking processes for new and existing customers have been redesigned. Further improvement in collection processes was continued in 2011. All of these activities resulted in sharp decline of bad debt expenses. Still, as the economic situation in Montenegro has not improved and liquidity of the economy is very low, the collection process is closely monitored and activities are tuned in accordance with it.

3.1.3 Liquidity risk

Liquidity risk is the risk that an entity may encounter difficulty in meeting obligations associated with financial liabilities.

Prudent liquidity risk management implies maintaining sufficient Cash and cash equivalents and Bank deposits as well as available funding through adequate amount of committed credit lines. The Group Treasury's management aims at maintaining flexibility in funding by keeping committed credit lines available. The undrawn credit lines amounted to HUF 51.4 billion as at December 31, 2011 (2010: HUF 54.6 billion), and the Company also had uncommitted credit lines from several Hungarian Banks as at December 31, 2011 and 2010. In addition to the above, Deutsche Telekom confirmed its readiness to finance Magyar Telekom Group's budgeted financing needs until the end of June 2013.

The following two tables summarize the maturity structure of Magyar Telekom's financial liabilities including the interest payable on those liabilities as of December 31, 2011 and 2010. As the majority of the financial liabilities are paid from the cash generated from the ongoing operations, the maturity analysis of the financial assets as at the end of the reporting periods (in comparison with the financial liabilities) would not be useful, therefore, is not included in the tables below.

December 31, 2011 (in HUF millions)	Total	within 1 year	1 to 5 years	after 5 years
Trade payables	101,119	101,119	-	-
Dividend payable	392	392	-	-
Financial liabilities to related parties	334,153	64,835	243,751	25,567
Bank loans	65,250	48,759	16,491	-
Finance lease liabilities	8,877	1,537	4,484	2,856
Nonconvertible bonds and debentures	190	70	120	-
Other financial liabilities	23,491	22,995	492	4
Total other financial liabilities	97,808	73,361	21,587	2,860
Total cash flows	533,472	239,707	265,338	28,427
Open swap positions' cash flows				
Gross cash inflow in EUR million	383	23	281	79
Gross cash inflow in HUF million (at spot rate)	119,286	7,290	87,527	24,469
Gross cash outflow in HUF million	(119,033)	(10,244)	(87,429)	(21,360)
Net cash inflow / (outflow) in HUF million	253	(2,954)	98	3,109
Open forward positions' cash flows				
Gross cash inflow in EUR million	100	100	-	-
Gross cash inflow in USD million	103	103	-	-
Total gross cash inflow in HUF million (at spot rate)	55,831	55,831	-	-
Gross cash outflow in HUF million	(52,803)	(52,803)	-	-
Net cash inflow in HUF million	3,028	3,028	-	-

December 31, 2010 (in HUF millions)	Total	within 1 year	1 to 5 years	after 5 years
Trade payables	88,613	88,613	-	-
Dividend payable	319	319	-	-
Financial liabilities to related parties	363,184	87,788	245,188	30,208
Bank loans	52,813	46,348	6,465	-
Finance lease liabilities	4,462	1,080	2,664	718
Nonconvertible bonds and debentures	191	70	121	-
Other financial liabilities	1,243	1,119	123	1
Total other financial liabilities	58,709	48,617	9,373	719
Total cash flows	510,825	225,337	254,561	30,927
Open swap positions' cash flows				
Gross cash inflow in EUR million	312	25	287	-
Gross cash inflow in HUF million (at spot rate)	87,089	6,861	80,228	-
Gross cash outflow in HUF million	(100,849)	(10,037)	(90,812)	-
Net cash outflow in HUF million	(13,760)	(3,176)	(10,584)	-
Open forward positions' cash flows				
Gross cash inflow in EUR million	123	123	-	-
Gross cash inflow in USD million	5	5	-	-
Total gross cash inflow in HUF million (at spot rate)	35,253	35,253	-	-
Gross cash outflow in HUF million	(36,395)	(36,395)	-	-
Net cash outflow in HUF million	(1,142)	(1,142)	-	-

The average maturity of Magyar Telekom's debt portfolio was 2.6 years as at December 31, 2011 (2010: 2.5 years), both of which are in line with the predefined liquidity management limit range of keeping the average maturity of the debt portfolio between 2 and 3 years.

The floating interest payments arising from the financial instruments were calculated using the last interest rates fixed before December 31, 2011 and 2010.

3.2 Capital risk management

The Group's objectives when managing capital are to safeguard the Group's ability to continue as a going concern in order to provide returns for shareholders and benefits for other stakeholders and to maintain an optimal capital structure to reduce the cost of capital.

The Company's management proposes to the owners (through the Board) of the Company to approve dividend payments or adopt other changes in the Company's equity capital in order to optimize the capital structure of the Group. This can be achieved primarily by adjusting the amount of dividends paid to shareholders, or alternatively, by returning capital to shareholders by capital reductions, selling or buying own shares. Consistent with others in the industry, the Group monitors capital on the basis of the gearing ratio.

This ratio is calculated as Net debt divided by Equity (including Non-controlling interest) and Net debt. Net debt is calculated as follows:

- Current and non current financial liabilities to related parties – Note 16
- plus Other current and non current financial liabilities – Note 17
- less Cash and cash equivalents – Note 6
- less Other current financial assets – Note 8.1.

During 2010 and 2011, the Group's strategy as approved by the Board was to maintain a gearing ratio within 30% to 40%. The gearing ratio at December 31, 2011 was 34.1% (2010: 32.7%).

In addition to the above, according to the Hungarian Companies Act, Magyar Telekom Plc. has to ensure that the Company's Equity does not fall below its Common stock, i.e. the total of the reserves should not be negative. The Company is in compliance with this regulation, and no such statutory regulation exists for consolidated equity.

The equity capital, which the Group manages, amounted to HUF 556 billion on December 31, 2011 (2010: HUF 595 billion).

4 CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS

Estimates and judgments are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, rarely equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities are outlined below.

4.1 Useful lives of assets

The determination of the useful lives of assets is based on historical experience with similar assets as well as any anticipated technological development and changes in broad economic or industry factors. The appropriateness of the estimated useful lives is reviewed annually, or whenever there is an indication of significant changes in the underlying assumptions. We believe that this is a critical accounting estimate since it involves assumptions about technological development in an innovative industry and heavily dependent on the investment plans of the Group. Further, due to the significant weight of depreciable assets in our total assets, the impact of any changes in these assumptions can be material to our financial position, and results of operations. As an example, if Magyar Telekom was to shorten the average useful life of its assets by 10%, this would result in additional annual depreciation and amortization expense of approximately HUF 10 billion (2010: HUF 10 billion). See Notes 12 and 13 for the changes made to useful lives in 2011.

The Group constantly introduces a number of new services or platforms including, but not limited to, the UMTS and 4G based broadband services in the mobile communications and the fiber-to-the-home rollout in the fixed line operations. In case of the introduction of such new services, the Group conducts a revision of useful lives of the already existing platforms, but in the vast majority of the cases these new services or assets are designed to co-exist with the existing platforms, resulting in no change-over to the new technology. Consequently, the useful lives of the existing platforms usually do not require shortening.

4.2 Estimated impairment of goodwill

Goodwill is not amortized, but tested for impairment annually or more frequently. The recoverable amounts of the operating segments (or CGUs) are calculated based on fair value less cost to sell determined by the discounted projected cash flows of the operating segments over the next ten years with a terminal value. This is highly judgmental, which carries the inherent risk of arriving at materially different recoverable amounts if estimates used in the calculations would prove to be inappropriate. The Group has an implemented policy to make the impairment test based on a 10-year cash flow projection on reasonable and supportable assumptions that present the management's best estimate on market participants' assumptions and expectations. We use 10 year cash flow projections as the payback period of our investments in the telecommunications operations often exceeds 5 years.

In order to determine the recoverable amounts of the operating segments, the Group calculates the operating segments' fair values less cost to sell. In the calculations, Magyar Telekom uses a range of weighted average cost of capital (WACC) and estimated perpetual growth rate (PGR) depending on the country of operations and the characteristics of the markets the Group's segments operate in. The WACCs are determined based on CAPM (capital asset pricing model) using the average betas of the peer group, 10 year zero coupon yields and a debt ratio in line with the usual indebtedness of listed peer telecommunications companies, while the PGRs used are in line with the long-term average growth rate for the particular segment.

Costs of certain central functions that are not cross charged are also considered in the fair value calculations, when conducting the goodwill impairment tests. The costs of these central functions are allocated to the operating segments based on the segments' revenue share of the Group's total revenue.

Goodwill is allocated to the following operating segments of the Group: Hungary, T-Systems, Macedonia and Montenegro.

As a result of the impairment testing carried out in 2011, using the above described valuation techniques, we identified and recognized an impairment loss on the goodwill of the Macedonia segment. The main reason for the impairment is that the revenue plans of the Macedonia segment prepared in 2011 had to be reduced by 7-19% compared to the plans prepared a year before due to the unfavorable economic environment and fiercer than expected mobile competition resulting in significant pricing pressure and increasing level of handset subsidies. Even though management will try to compensate the loss in cash inflows with stricter control on cash outflows, this foreseen decrease in revenues will not be possible to be fully compensated by the planned reduction of operating expenses and the planned reduction of capital expenditures. In addition to the decrease in expected cash flows, the increase of the applied WACC from 10.96% to 12.11% also resulted in additional reduction of the enterprise value of the Macedonia segment. Further, due to the above described reasons, the PGR used in the 2010 calculations had to be decreased from 1.7% to 0.5% in the 2011 calculations.

Due to the above described changes in the economic circumstances an impairment loss of HUF 31,390 million was recognized for the Macedonia segment based on the fair value less cost to sell (FVLCS) calculations. Magyar Telekom's management believes that preparing the value in use (VIU) calculation is unnecessary, since it would result in a lower enterprise value than the FVLCS. The VIU method is assuming a model without future investments, meaning that additional capex and related revenues and gains to be recognized in the future cannot be considered in the calculations. Assuring the revenues on long term in a telecom business very much depends on future investments. In Magyar Telekom on average only approximately 20% of the capex spent in a year is related to maintenance. Others are new investments, also related to providing new connections to the network. It is obvious, that without this the revenue generation would start to sharply decline on a long term. Consequently, we have not prepared the value in use calculations for the Macedonia or any other segments.

In 2011 no goodwill allocated to the other segments had to be impaired and no goodwill in 2010 had to be impaired.

The tables below show the WACCs and PGRs used in the fair value calculations of the Group's operating segments (and the MBU CGU in 2010) for the goodwill impairment test conducted in 2011 and 2010. The tables below also include sensitivity analyses that show how much impairment (or additional impairment in case of Macedonia) would have been recognized as at December 31, 2011 or 2010 for the goodwill allocated to the operating segments (or the MBU CGU in 2010) if we changed the sensitive parameters in the calculations.

In case of the WACCs we disclose what impact a 2 percentage point increase of the WACC would have on the goodwill. In case of the PGRs we disclose what impact a 5 percentage point decrease of the PGR would have on the goodwill. In case of the cash flow projections we disclose what impact a 10% or a 20% lower than projected cash flow stream would have on the goodwill.

2011	**Hungary**	**T-Systems**	**Macedonia (after impairment)**	**Montenegro**
WACC				
Used in the calculation	12.99%	13.27%	12.11%	10.54%
If changed to	14.99%	15.27%	14.11%	12.54%
Potential impairment (HUF million)	33,969	-	9,170	-
PGR				
Used in the calculation	1.0%	1.5%	0.5%	0.0%
If changed to	-4.0%	-3.5%	-4.5%	-5.0%
Potential impairment (HUF million)	15,771	-	7,240	-
Cash flows				
If changed by	-10%	-10%	-10%	-10%
Potential impairment (HUF million)	8,595	-	6,777	-
If changed by	-20%	-20%	-20%	-20%
Potential impairment (HUF million)	74,621	-	13,576	-

There were certain changes in the operating segment structure of the Group from January 2011, whereby the Group's new operating segment Hungary includes the former Consumer Services Business Unit (CBU), the small and medium size business (SMB) customers of the Business Services Business Unit (BBU) and the former Headquarters and Technology Units. The T-Systems segment includes the former BBU, without the SMB customers. The Macedonia and Montenegro segments have not changed. The table below shows the impairment sensitivity analysis using the same potential change in the parameters as for the 2011 impairment calculations, however in the old segment structure. There was no need for an impairment due to the re-segmentation of the Group as at December 31, 2010, and as it can be seen from the table below, there was no risk of material impairment even when changing the parameters used in the 2010 calculations to reasonably possible levels.

2010	**CBU**	**BBU**	**MBU**	**Macedonia**	**Montenegro**
WACC					
Used in the calculation	12.36%	12.28%	12.56%	10.96%	10.68%
If changed to	14.36%	14.28%	14.56%	12.96%	12.68%
Potential impairment (HUF million)	-	-	-	-	-
PGR					
Used in the calculation	1.5%	2.0%	2.0%	1.7%	1.2%
If changed to	-3.5%	-3.0%	-3.0%	-3.3%	-3.8%
Potential impairment (HUF million)	-	-	-	-	-
Cash flows					
If changed by	-10%	-10%	-10%	-10%	-10%
Potential impairment (HUF million)	-	-	-	-	-
If changed by	-20%	-20%	-20%	-20%	-20%
Potential impairment (HUF million)	-	-	-	1,841	-

4.3 Estimated impairment of property, plant and equipment, and intangibles

We assess the impairment of identifiable property, plant, equipment and intangibles whenever there is a reason to believe that the carrying value may materially exceed the recoverable amount and where impairment of value is anticipated. The calculations of recoverable amounts are primarily determined by value in use calculations, which use a broad range of estimates and factors affecting those. Among others, we typically consider future revenues and expenses, technological obsolescence, discontinuance of services and other changes in circumstances that may indicate impairment. If impairment is identified using the value in use calculations, we also determine the fair value less cost to sell (if determinable), to calculate the exact amount of impairment to be charged. As this exercise is highly judgmental, the amount of a potential impairment may be significantly different from that of the result of these calculations.

4.4 Estimated impairment of trade and other receivables

We calculate impairment for doubtful accounts receivable based on estimated losses resulting from the inability of our customers to make required payments. For the largest customers and other telecommunications service providers, impairment is calculated on an individual basis, while for other customers it is estimated on a portfolio basis, for which we base our estimate on the aging of our accounts receivable balance and our historical write-off experience, customer credit-worthiness and recent and expected changes in our customer payment terms. These factors are reviewed periodically, and changes are made to the calculations when necessary. In addition, we consider also the nature of the business (residential, business, fixed line, mobile, internet, cable TV, etc.) and the environment in which the Group's entities operate in the various markets. The estimates also involve assumptions about future customer behavior and the resulting future cash collections. If the financial condition of our customers were to deteriorate, actual write-offs of currently existing receivables may be higher than expected and may exceed the level of the impairment losses recognized so far. See also Note 3.1.2.

4.5 Provisions

Provisions in general are highly judgmental, especially in case of legal disputes. The Group assesses the probability of an adverse event as a result of a past event and if the probability of an outflow of economic benefits is evaluated to be more than fifty percent, the Group fully provides for the total amount of the estimated liability (see also Note 2.10). The assessment of the probability is highly judgmental, as – for example – in Hungary there are very few cases where the appealed NMIAH decisions have been finally concluded by the Supreme Court. Further, in Macedonia, there is also a lack of sufficient history for Competition Office or Agency decisions appealed against at the Administrative Court. In order to determine the probabilities of an adverse outcome, the Group uses internal and external legal counsel.

4.6 Subscriber acquisition and retention costs

Subscriber acquisition and retention costs primarily include the loss on the equipment sales (revenues and costs disclosed separately) and fees paid to subcontractors that act as agents to acquire new customers or retain the existing subscribers. The Group's agents also spend a portion of their agent fees for marketing the Group's products, while a certain part of the Group's marketing costs could also be considered as part of the subscriber acquisition and retention costs. The up-front fees collected from customers for activation or connection are marginal compared to the incremental acquisition and retention costs. These revenues and costs are recognized when the customer is connected to the Group's fixed or mobile networks. No such costs or revenues are capitalized or deferred. These acquisition and retention costs (losses) are recognized immediately as they are not accurately separable from other marketing costs. Among these, net losses on equipment sales of the Group amounted to HUF 14.7 billion in 2011 (2010: HUF 13.9 billion), while agent fees amounted to HUF 10.1 billion in 2011 (2010: HUF 9.2 billion). The Group's marketing costs amounted to HUF 12.9 billion in 2011 (2010: HUF 13.4 billion).

5 BUSINESS COMBINATIONS

5.1 Acquisitions in 2011

5.1.1 Daten-Kontor

Magyar Telekom signed a share purchase agreement to acquire 100% of Daten-Kontor Kft. on July 20, 2010. The closing of the transaction was subject to the approval of the Competition Office. The maximum purchase price of HUF 1.4 billion is dependent on the 2011 and 2012 financial performance and was adjusted with the value of the net debt at the closing of the transaction on February 28, 2011, when the Group obtained control over Daten-Kontor. Daten-Kontor develops, installs and operates IT applications in Hungary. In 2010 the revenue of Daten-Kontor Kft. was HUF 2.7 billion and its EBITDA was HUF 340 million. Daten-Kontor has been a consolidated subsidiary of the Group since February 28, 2011, included in the T-Systems operating segment.

The carrying values and the fair values of assets and liabilities acquired as well as the considerations transferred are disclosed in the table below.

In HUF millions	Fair values	Carrying values
Initial purchase price	900	
Additional estimated contingent purchase price	498	
Consideration transferred	1,398	
Net assets acquired	1,332	
Goodwill	66	
Net assets acquired:		
Cash and cash equivalents	455	455
Trade and other receivables	701	701
Income tax payable	(2)	(2)
Inventories	5	5
Property, plant and equipment	93	93
Intangible assets	619	79
Trade and other payables	(312)	(312)
Provision	(173)	(173)
Net deferred tax liability	(54)	-
	1,332	846

The initial purchase price in a total amount of HUF 900 million and HUF 173 million of the estimated additional purchase price were paid in cash in 2011 while the remaining amount is expected to be payable in 2012 and 2013.

The goodwill arising on this acquisition (fully allocated to the T-Systems segment) mostly represent the assembled workforce that cannot be recognized as a separable asset.

In Hungarian GAAP, there is also no goodwill amortization, but in case of impairment, the total amount of goodwill (HUF 429 million) recognized is tax deductible according to the corporate tax law prevailing in 2011.

5.1.2 Globe

In May 2011, Magyar Telekom signed a sale purchase agreement to acquire the ownership rights of the Globe Banking Software (Globe) in a value of HUF 1 billion, and entered into a 7-year IT outsourcing service contract with the clients applying Globe. Globe is a software system applied as central administration system of finance institutions in Hungary. Globe was used by 14 Hungary-based finance institutions and their branches as central administration system of financial service activity at the date of acquisition. As the scope of activities acquired includes inputs, processes and immediate outputs as defined by IFRS 3, the transaction qualifies as an acquisition of a business.

Globe is a market-leader system in its customer segment and the revenue generated from the services provided to the Savings banks amounts to approximately HUF 320 million per annum. The Globe software system and the related revenues and expenses have been consolidated from June 2011, included in the T-Systems operating segment of the Group.

The fair values of assets acquired as well as the consideration transferred are disclosed in the table below.

In HUF millions	Fair values
Software	300
Customers	563
Goodwill	137
Assets acquired / Total consideration transferred	1,000

The purchase price of HUF 1,000 million was paid in cash in 2011.

The customer value recognized as an intangible asset represents the customer base and services rendered to them existing on the acquisition date, while goodwill (fully allocated to the T-Systems segment) represents the value of, and the future expected revenues from, customers to be acquired from the acquisition date and the planned extension of services.

In Hungarian GAAP no goodwill was recognized.

5.1.3 Budakalász

Magyar Telekom acquired the remaining 75% of Budakalász Kábel TV Kft. on November 30, 2011. Budakalász is a cable TV service provider in Hungary, which had approximately 1.7 thousand subscribers at the acquisition date. The purchase price was HUF 239 million. Budakalász has been a consolidated subsidiary of the Group since that day included in the Hungary operating segment. Budakalász was an associate of Magyar Telekom before the acquisition, the disposal of which resulted in a net profit of HUF 58 million.

The carrying values and the estimated fair values of assets and liabilities acquired as well as the considerations transferred are disclosed in the table below.

In HUF millions	Fair values	Carrying values
Purchase price of the remaining 75%	239	
Fair value of the 25% ownership	80	
Consideration transferred	319	
Net assets acquired	199	
Goodwill	120	
Net assets acquired:		
Cash and cash equivalents	13	13
Trade and other receivables	7	7
Income tax receivable	7	7
Inventories	1	1
Property, plant and equipment	72	72
Intangible assets	112	1
Trade and other payables	(2)	(2)
Net deferred tax liability	(11)	-
	199	99

The purchase price of HUF 239 million was paid in cash in 2011.

The customer value recognized as an intangible asset represents the customer base and services rendered to them existing on the acquisition date, while goodwill (fully allocated to the Hungary segment) represents the value of, and the future expected revenues from, customers to be acquired from the acquisition date and the planned extension of services.

In Hungarian GAAP, there is also no goodwill amortization, but in case of impairment, the total amount of goodwill (HUF 185 million) recognized is tax deductible according to the corporate tax law prevailing in 2011.

5.2 Acquisitions in 2010

5.2.1 Modultechnika

Magyar Telekom signed a share purchase agreement to acquire 100% of Modultechnika Kft. in July 2010. The purchase price paid in cash in 2010 was HUF 1,421 million. A maximum additional HUF 143 million is payable in the period until 2015, depending on potential third party and certain authority claims. The fair value of this amount was recognized as a liability. Modultechnika is a cable TV service provider in Hungary with approximately 13,000 customers and annual revenues of HUF 500 million. The transaction was closed on July 22, 2010, since when Modultechnika has been a consolidated subsidiary of the Group, included in the Hungary operating segment.

The purchase price allocation was not completed by the issuance of the 2010 financial statements, but was completed later in 2011. The table below includes the provisional and the final fair values of assets and liabilities acquired at the time acquisition.

In HUF millions	Provisional fair values	Final fair values
Purchase price of ownership acquired	1,421	1,421
Additional estimated purchase price	143	143
Consideration transferred	1,564	1,564
Net assets acquired	861	897
Goodwill	703	667
Net assets acquired:		
Cash and cash equivalents	6	6
Trade receivables	26	26
Inventories	9	9
Other receivables	6	6
Income tax receivable	2	2
Property, plant and equipment	197	272
Intangible assets	799	764
Trade and other payables	(102)	(102)
Net deferred tax liability	(82)	(86)
	861	897

The initial purchase price was paid in cash in 2010, while the additional purchase price is expected to be paid in the period until 2015, of which HUF 41 million was paid in 2011.

The customer contract value recognized as an intangible asset only represents the customers and services rendered to them existing on the acquisition date, while the majority of the goodwill represents the value of, and the future expected revenues from, customers to be acquired from the acquisition date and the planned extension of services.

In Hungarian GAAP, there is also no goodwill amortization, but in case of impairment, the total amount of goodwill (HUF 1,477 million) recognized is tax deductible according to the corporate tax law prevailing in 2010.

5.3 Pro forma information on business combinations

The following pro forma information shows the most important financial data of the Group, including the subsidiaries and businesses acquired as if they had been consolidated from the beginning of 2011, and also how much the business combinations contributed to the reported figures since the acquisition date in the year of acquisition.

In HUF millions	2010	2011
Revenues		
Reported	609,579	597,617
Pro forma – if consolidated from beginning of year	609,825	598,030
Current year contribution since date of business combination in the year of acquisition	192	2,818
Profit for the year		
Reported	77,371	779
Pro forma – if consolidated from beginning of year	77,363	861
Current year contribution since date of business combination in the year of acquisition	(42)	319

6 Cash and cash equivalents

Cash and cash equivalents include cash on hand and in banks, and all highly liquid deposits and securities with original maturities of three months or less, and exclude all overdrafts. These financial assets are exposed to credit risks, for which see more details in Note 3.1.2. No impairment had to be recognized for any of these balances in the reported years.

In HUF millions	At December 31,	
	2010	2011
Cash on hand	157	196
Cash in bank (demand deposits)	9,490	9,145
Bank deposits with original maturities less than 3 months	6,194	5,110
	15,841	14,451

Cash and cash equivalents by country of location	At December 31,	
In HUF millions	2010	2011
Hungary	7,945	7,625
Macedonia	6,598	5,691
Montenegro	893	651
Other countries	405	484
	15,841	14,451

7 Trade and other receivables

7.1 Trade and other receivables – carrying amounts

In HUF millions		At December 31, 2010	2011
Trade receivables from third parties		99,741	105,017
Trade receivables from Deutsche Telekom Group companies		6,991	8,333
Trade receivables from associates and joint ventures		-	-
Total trade receivables	(a)	106,732	113,350
Prepayments and advance payments		4,748	8,275
Other taxes receivable		2,056	2,650
Other		1,089	388
Total other receivables		7,893	11,313
		114,625	124,663

(a) Age profile of Trade receivables

The following tables show the age profile of the Group's trade receivables by country of operation by days outstanding (past due). The carrying amounts of past due receivables are shown net of impairment losses charged as of the financial statement dates.

In HUF millions	Carrying amount as of Dec 31, 2011	of which not past due	of which past due by: less than 30 days	30 – 60 days	61 – 90 days	91 – 180 days	181 – 360 days	over 360 days
Hungary	92,902	77,627	9,234	1,714	587	1,071	1,029	1,640
Macedonia	13,998	9,700	2,192	724	288	458	220	416
Montenegro	5,205	3,316	811	284	127	296	69	302
Other countries	1,245	1,027	42	35	13	17	22	89
Total	113,350	91,670	12,279	2,757	1,015	1,842	1,340	2,447

In HUF millions	Carrying amount as of Dec 31, 2010	of which not past due	of which past due by: less than 30 days	30 – 60 days	61 – 90 days	91 – 180 days	181 – 360 days	over 360 days
Hungary	88,099	69,033	9,529	3,091	1,284	2,612	1,167	1,383
Macedonia	12,852	8,823	2,017	872	380	357	244	159
Montenegro	4,792	2,967	905	320	127	205	201	67
Other countries	989	613	95	54	40	26	101	60
Total	106,732	81,436	12,546	4,337	1,831	3,200	1,713	1,669

The vast majority of trade receivables is impaired on a portfolio basis. The vast majority of past due trade receivables are partly or fully impaired depending on the period of delay of payments. Only insignificant amounts of past due trade receivables are not impaired based on past experience of payment behavior of certain business and governmental customers. As these amounts are not significant, these are not disclosed separately.

Non past due receivables are not assessed collectively for impairment, but in case of bankruptcy of the customer non past due receivables may have to be partly or fully impaired, the amount of which is not significant, therefore, not disclosed separately. The non past due trade receivables represent approximately 1.8 months of revenue (2010: 1.6 months of revenue). As disclosed in Note 3.1.2, the annual bad debt expense of the Group is approximately 1.0 percent of the annual consolidated revenue, therefore, we can estimate that approximately this percentage of the non past due portion of trade receivables will not be collected, i.e. will have to be impaired in future periods, but are not impaired at the end of the reporting period.

The Group has no collaterals related to its trade receivables.

7.2 Impairment losses of trade and other receivables

The table below shows the impairment loss and changes therein for 2010 and 2011.

In HUF millions	At December 31, 2010	At December 31, 2011
Impairment loss, beginning of period	29,665	34,486
Charged to expense - net (included in Other operating expenses)	9,991	6,255
Translation difference	326	1,433
Utilized	(5,496)	(7,606)
Impairment loss, end of period	34,486	34,568

The carrying amount of financial assets that would otherwise be past due or impaired whose terms have been renegotiated is not material therefore no separate disclosure is provided on those.

The amount of receivables that are individually determined to be impaired is not material, therefore, these are not disclosed separately.

The table below includes the impairment losses and the changes therein in 2010 and 2011 for the countries of operation of the Group.

In HUF millions	At December 31, 2009	Charged to expense	Translation difference	Utilized	At December 31, 2010
Hungary	16,329	8,733	-	(3,776)	21,286
Macedonia	9,315	663	205	(1,614)	8,569
Montenegro	3,966	518	119	(29)	4,574
Other countries	55	77	2	(77)	57
Group	29,665	9,991	326	(5,496)	34,486

In HUF millions	At December 31, 2010	Charged to expense	Translation difference	Utilized	At December 31, 2011
Hungary	21,286	5,829	-	(6,246)	20,869
Macedonia	8,569	1	942	(530)	8,982
Montenegro	4,574	411	484	(830)	4,639
Other countries	57	14	7	-	78
Group	34,486	6,255	1,433	(7,606)	34,568

8 Other financial assets

Other financial assets include receivables due within 12 months from the financial statement date (current) and due after 12 months from the financial statement date (non current). These financial assets are exposed to credit risks, for which see more details in Note 3.1.2. The impairment loss accounted for other current and non current financial assets is not material therefore its reversal is also insignificant.

8.1 Other current financial assets

In HUF millions		At December 31, 2010	2011
Bank deposits with original maturities over 3 months	(a)	47,798	54,926
Finance lease receivable	(b)	4,298	4,267
Loans and receivables from employees	(c)	542	727
RDC receivable	(d)	199	222
Derivative financial instruments contracted with related parties	(e)	1,004	193
Derivative financial instruments contracted with third parties	(f)	301	3,500
Other		2,418	1,451
		56,560	65,286

(a) The table below shows the Bank deposits with original maturities over 3 months by country of location.

In HUF millions	At December 31, 2010	2011
Macedonia	37,686	40,785
Montenegro	10,091	14,121
Hungary	21	20
	47,798	54,926

8.2 Other non current financial assets

In HUF millions		At December 31, 2010	2011
Finance lease receivable	(b)	16,087	12,516
Loans and receivables from employees	(c)	4,219	4,714
RDC receivable	(d)	516	398
Trade receivables over one year	(g)	1,524	1,696
Derivative financial instruments contracted with related parties	(e)	-	10,291
Derivative financial instruments contracted with third parties	(f)	-	341
Financial assets available for sale	(h)	296	278
Other		1,391	1,356
		24,033	31,590

(b) See Note 33.3 for more information on Finance lease receivable.

(c) Loans and receivables from employees primarily represent the housing loans provided to the employees of the Group. There are no past due employee receivables, and the loans are pledged with mortgage.

(d) RDC receivable represents Crnogorski Telekom's receivable from the Government of Montenegro originating from the Share Transfer Agreement on the sale of ownership in the Radio Difuzni Centar (RDC) entered into in 2004.

(e) Derivative financial instruments contracted with related parties include the fair value of open currency forwards and cross-currency interest rate swaps (see more details in Note 3.1.1.1).

(f) Derivative financial instruments contracted with third parties include the fair value of open currency forwards and cross-currency interest rate swaps (see more details in Note 3.1.1.1).

(g) Trade receivables over one year includes receivables from customers paying over 1-2 years in installments for telecommunications equipment sold, as well as installment payments on software and hardware implementation services.

(h) Financial assets available for sale include insignificant investments in equity securities.

9 Income tax

9.1 Current income tax receivable and payable

Current income tax receivable and payable in the Statement of financial position represent the amount of corporate and other income taxes receivable from, and payable to, the tax authorities of the countries in which the Group operates.

9.2 Income tax expense

The table below shows the tax expenses charged in the Profit for the year.

In HUF millions	For the year ended December 31, 2010	2011
Corporate income tax	5,158	4,336
Other income taxes	8,237	7,853
Deferred income taxes	(6,812)	15,349
Total income tax expense	6,583	27,538

9.3 Tax rate reconciliation

The reconciliation between the reported income tax expense and the theoretical amount arising by applying the statutory income tax rates is as follows:

In HUF millions		For the year ended December 31, 2010	2011
IFRS profit before income tax		83,954	30,717
Tax at 19%		(15,951)	(5,836)
Impact of different tax rates	(a)	6,074	4,901
Tax on items not subject to income tax	(b)	1,254	973
Tax on non deductible items	(c)	(745)	(4,035)
Other income taxes	(d)	(8,237)	(7,853)
Impact of tax deductibility of other income taxes	(e)	1,565	1,492
Withholding tax on dividends	(f)	(2,370)	(3,011)
(De)/recognized deferred tax on tax losses	(g)	-	(527)
Broadband tax credit accretion	(h)	1,473	1,365
Changes in the Macedonian tax regime	(i)	(4,172)	-
Change in the Hungarian corporate tax rate	(j)	14,526	(15,007)
Income tax expense		(6,583)	(27,538)
Effective tax rate		7.8%	89.7%

(a) Impact of different tax rates

The corporate tax rate in Hungary was 19% in 2011 and in 2010. In 2010, an amendment was made to the corporate tax law, introducing a lower rate of corporate tax (10%) as of July 1, 2010 for the first HUF 500 million tax base (on an annual basis) of the legal entities, above which the regular rate of 19% applies. The impact of the lower tax rate applicable to the Hungarian legal entities of the Group is included in this line of the reconciliation.

This line of the reconciliation also includes the tax impacts of the different tax rates of the foreign countries where the Group is also present through its subsidiaries. The tax rate in Macedonia is 0% for undistributed profits. The corporate tax rate is 9% in Montenegro, 16% in Romania, and 10% in Bulgaria in the reported years. The corporate tax rate was 25% until March 31, 2011 in the Ukraine, when it was decreased to 23%. This line of the reconciliation includes the tax impacts of the above differences compared to the 19% theoretical tax rate applied to the profit before tax.

(b) Tax on items not subject to income tax

Items not subject to income tax consist primarily of donation for non-profit organizations and R&D cost deductible from corporate income tax base. This line of the reconciliation includes the positive tax impact of the above items.

(c) Tax on non deductible items

This line of the reconciliation shows the negative tax impact of the non deductible expenses, including primarily the premature receivable write-downs, certain impairment losses and entertainment expenses as well as non deductible penalties. Non deductible penalties in 2011 included the amount of the criminal penalty payable to the DOJ, which was qualified as a non deductible expense in 2011 in an amount of HUF 14,345 million, the negative tax impact of which at 19% is HUF 2,726 million in this line of the reconciliation in 2011.

(d) Other income taxes

Other income taxes include certain local and central taxes levied in Hungary on the companies' net margins, determined at a substantially higher level than the corporate tax base, but with substantially lower tax rates. As the first line of the reconciliation calculates theoretical tax expense calculated using the corporate tax rate, the Hungarian local business tax, energy supplier tax and the innovation fee impose additional income tax expenses for the Hungarian entities of the Group, included in this line of the reconciliation.

(e) Deductibility of other income taxes from the corporate tax base

The above described Hungarian other income taxes are deductible expenses for corporate tax purposes, the positive impact of which is included in this line of the reconciliation.

(f) Withholding tax

Macedonia and Montenegro levy a 5% withholding tax on dividend distribution to Hungary. In addition, according to the Macedonian tax law changes in 2010, Macedonian companies have to pay "corporate income tax" on their annual profits if they distribute those profits as dividends to foreign companies (or Macedonian individuals) at 10%. We assess that the Macedonian corporate tax in 2010 and 2011 is in fact a withholding tax that is levied at the dividend distributions from Macedonia to Hungary, which imposes additional tax expenses for the Group related to the 2010 and 2011 profits of the Macedonian subsidiaries.

The reconciliation includes the amount of withholding tax accruing on the current year's profits to be distributed from the foreign subsidiaries to the Company. Dividends received by the Hungarian parent companies (from Macedonia and Montenegro as well) are eliminated on consolidation, therefore, the Group's profit before tax excludes these dividends. As these dividends are not subject to corporate tax in Hungary, the reconciliation includes the withholding tax burden on such dividends as a separate line.

(g) (De)/recognized deferred tax on tax losses

Deferred tax asset is recognized on tax losses only to the extent that the realization of the related tax benefit is probable. Deferred tax assets on tax losses that will probably not be recovered are un-recognized in the period of the loss or de-recognized in subsequent periods. On the other hand, when the recoverability of the previously un/derecognized tax losses becomes probable, these deferred tax assets are recognized.

(h) Broadband investment tax credit accretion

Broadband investment tax credit accretion shows the increase of the net present value of the investment tax credit deriving from the utilization of the tax credits in year(s) subsequent to the year of recognition.

(i) Changes in the Macedonian tax regime

The change in the Macedonian tax law in 2010 resulted in the transformation of the Macedonian corporate tax (10%) to an additional withholding tax. In 2010, we recognized an additional deferred tax liability on the accumulated undistributed profits of our Macedonian subsidiaries expected to be distributed as dividends to Hungary. In the 2010 number of the reconciliation we included the impact of the change of the corporate tax to withholding tax. As the undistributed corporate tax rate in 2009 was 0%, no deferred tax was recognized for the accumulated profit of 2009, while the change in 2010 resulted in a withholding tax to be recognized at 10% (+5%) for 2009. See also subnotes (a) and (f) of this Note.

(j) Change in the Hungarian tax rate

In 2010, an amendment was made to the Hungarian corporate tax law, introducing a lower rate of corporate tax (10%) as of July 1, 2010 for the first HUF 500 million tax base of the legal entities (HUF 250 million in 2010), above which the regular rate of 19% applies. A further amendment was made to the Hungarian tax law in 2010, which stated that the corporate tax rate from January 1, 2013 will be 10%. Deferred tax balances were recalculated accordingly, the impact of which is included in this line of the reconciliation for 2010.

In 2011, the amendment made to the corporate tax law to lower the corporate tax rate from January 1, 2013 uniformly to 10% has been eliminated. As a result after January 1 2013 the 19% of corporate tax rate has to be applied to the part of the tax base which exceeds HUF 500 million. Deferred tax balances were recalculated accordingly in 2011.

9.4 Deferred taxes

Magyar Telekom's deferred tax balances are as follows:

In HUF millions	Balance at Dec. 31, 2009	Effect on profit	Other movements	Balance at Dec. 31, 2010	Effect on profit	Other movements	Balance at Dec. 31, 2011
Deferred tax assets and (liabilities)							
Investment tax credits	16,786	(751)	(3)	16,032	(526)	-	15,506
Net operating loss carry-forward	1,789	(794)	-	995	(39)	-	956
Investments in subsidiaries	(1,326)	392	-	(934)	5,968	-	5,034
Withholding tax	(3,099)	(3,206)	-	(6,305)	(1,919)	-	(8,224)
Other financial assets	348	(30)	-	318	(3,009)	-	(2,691)
Impairment of receivables and inventory	2,063	780	-	2,843	484	-	3,327
Property, plant and equipment and intangible assets	(27,694)	8,137	(116)	(19,673)	(8,772)	(160)	(28,605)
Goodwill	(9,852)	3,626	-	(6,226)	(6,992)	-	(13,218)
Trade and other payables	120	(62)	-	58	9	-	67
Loans and other borrowings	357	(236)	-	121	192	-	313
Deferred revenue	(130)	(220)	-	(350)	26	-	(324)
Provisions for liabilities and charges	3,934	(824)	-	3,110	(771)	-	2,339
Total net deferred tax asset / (liability)	(16,704)	6,812	(119)	(10,011)	(15,349)	(160)	(25,520)
Of which deferred tax liability after netting	(18,594)			(10,924)			(26,270)
Of which deferred tax asset after netting	1,890			913			750

In HUF millions	Other movements 2010	Other movements 2011
Items included in other movements		
Investment tax credit recognized / (derecognized) against cost of PPE	(3)	-
Currency translation adjustment arising on consolidation	(68)	(95)
Arising on business combinations	(48)	(65)
	(119)	(160)

The Group consists of a number of legal entities, most of which have deferred tax assets and liabilities. The assets and liabilities are netted by legal entity so that one legal entity has either a deferred tax asset or a liability and the consolidated Statement of financial position includes these items accordingly.

The Group's net deferred tax liability balance is HUF 25,520 million which includes a high amount of individual deferred tax asset and liability items (see in the above table). Of these items, approximately HUF 2,701 million net deferred tax asset is expected to reverse in 2012 (deferred tax asset of HUF 5,723 million and deferred tax liability of HUF 3,022 million). The above items exclude deferred tax items expected to arise in 2012.

The Group's net deferred tax liability balance was HUF 10,011 million at December 31, 2010 which included a high amount of individual deferred tax asset and liability items (see in the above table). Of these items, approximately HUF 5,984 million net deferred tax asset was expected to reverse in 2011 (deferred tax asset of HUF 6,360 million and deferred tax liability of HUF 376 million). The above items excluded deferred tax items expected to arise in 2011.

Deferred tax arising on investment tax credits are recognized against the cost of the related investment.

Temporary differences associated with investments in subsidiaries for which deferred tax liabilities or assets have not been recognized amounted to a net liability of HUF 5,376 million at December 31, 2011 (2010: net liability of HUF 10,484 million).

If the Group's Macedonian and Montenegrin subsidiaries distribute their distributable reserves in the form of a dividend, the amounts paid to Hungary are subject to withholding tax. We recognize a deferred tax liability for the total amount of reserves distributable to the Company, considering our share of ownership.

Deferred tax assets are recognized for tax loss carry forwards only to the extent that realization of the related tax benefit is probable. There is no tax loss expiring in 2012 for which a deferred tax asset has been recognized. As of December 31, 2011, the balance of recognized tax losses is HUF 10,434 million of which HUF 117 million is subject to statutory limitations (2010: HUF 9,944 million of which no tax loss was subject to statutory limitations). The Group recognized deferred tax asset on tax losses for HUF 5,167 million as at December 31, 2011, while in 2010 deferred tax asset was recognized for the total amount of tax losses.

9.5 Investment tax credits

In order to increase broadband internet penetration in Hungary, companies investing over HUF 100 million in a year in broadband assets (e.g. DSL lines, UMTS assets) from 2003 can apply for a corporate tax reduction. The potential reduction of the corporate tax charge was defined as a percentage of the companies' capital investment in broadband assets. As these investment tax credits are of a government grant nature, Magyar Telekom recognized the deferred tax asset against the cost of the related investment. If the tax credits are not utilized in the year when earned, the amount of tax credits carried forward can be utilized at a higher amount as outstanding amounts can be accreted. This accretion is recognized as an increase in the investment tax credit against a reduction in the deferred tax expense.

The following table shows the details of the tax credits in HUF millions:

Earned in year	Amount of qualifying broadband investment	Amount of tax credit earned	Accretion recognized in tax expense to date	Tax credit utilized	Tax credit carried forward at December 31, 2011
2003	6,194	2,592	1,132	(3,724)	-
2004	6,876	2,985	1,878	(4,863)	-
2005	13,925	5,598	2,254	(2,836)	5,016
2006	14,993	4,372	2,015	(473)	5,914
2007	11,078	2,958	1,120	(87)	3,991
2008	2,204	459	126	-	585
Total	55,270	18,964	8,525	(11,983)	15,506

Expires in year	2015	5,016
	2016	5,914
	2017	3,991
	2018	585
		15,506

In order to utilize the tax credits and certain tax deductibility opportunities earned by the Group's entities, they have to comply with strict requirements as set out in the relevant tax regulations. The most important requirement is that the relevant assets have to be operated for at least 5 years. Management believes that the Group has complied and will be able to comply with the requirements to recognize these as deferred tax assets.

9.6 Tax reviews

The tax authorities may at any time inspect the books and records within five years from the end of the year when tax declarations were submitted and may impose additional tax assessments with penalties and penalty interest. Management is not aware of any circumstances which may give rise to a potential material liability in this respect.

9.7 Dividends paid by Magyar Telekom Plc.

The dividends paid and payable by Magyar Telekom Plc. to its owners may be subject to withholding or income taxes of the owners, which do not have an impact on the amount of the dividend declared or on the Company's tax expense as these taxes – if any – are levied on the owners.

10 Inventories

In HUF millions	At December 31, 2010	At December 31, 2011
Inventory for resale	6,901	7,574
Other inventory and advances	2,880	2,657
Subtotal	9,781	10,231
Less allowances for obsolete inventory	(189)	(327)
	9,592	9,904

The impairment loss accounted for inventories is not material therefore any reversal is also insignificant.

The Group has no inventory pledged as security as at December 31, 2011 or December 31, 2010.

11 Non current assets held for sale

Non current assets held for sale include primarily land and buildings identified for sale or exchange, allocated mainly to the Macedonia and Hungary segments, which is expected within 12 months, as a result of the continuing improvement of utilization of properties and headcount reductions.

12 Property, plant and equipment

In HUF millions	Land and related rights	Buildings	Telecom. equipment	Other equipment	Total
At January 1, 2010					
Cost	7,333	135,732	1,171,086	102,550	1,416,701
Accumulated depreciation	(1,766)	(36,102)	(745,471)	(79,827)	(863,166)
Carrying amount	5,567	99,630	425,615	22,723	553,535
Of which held for sale					(2,790)
					550,745
Carrying amount - January 1, 2010	5,567	99,630	425,615	22,723	553,535
Exchange differences	35	445	1,727	184	2,391
Additions due to business combinations	-	11	188	9	208
Additions due to and revisions of asset retirement obligations	-	616	(4)	-	612
Investments	1	2,117	62,674	7,697	72,489
Disposals	(21)	(77)	(168)	(246)	(512)
Decrease due to sale of subsidiary	-	-	(487)	(59)	(546)
Depreciation charge	(115)	(4,080)	(64,344)	(7,734)	(76,273)
Reclassifications	643	(643)	-	-	-
Carrying amount - December 31, 2010	6,110	98,019	425,201	22,574	551,904
At December 31, 2010					
Cost	7,979	137,403	1,204,746	102,834	1,452,962
Accumulated depreciation	(1,869)	(39,384)	(779,545)	(80,260)	(901,058)
Carrying amount	6,110	98,019	425,201	22,574	551,904
Of which held for sale					(2,152)
					549,752
Carrying amount - January 1, 2011	6,110	98,019	425,201	22,574	551,904
Exchange differences	142	2,123	7,493	1,192	10,950
Additions due to business combinations	-	-	221	36	257
Additions due to and revisions of asset retirement obligations	-	234	44	-	278
Investments	4	2,904	53,521	6,180	62,609
Disposals	(101)	(1,961)	(160)	(245)	(2,467)
Depreciation charge	(114)	(3,787)	(69,681)	(7,079)	(80,661)
Reclassifications	118	(118)	(1,481)	-	(1,481)
Carrying amount - December 31, 2011	6,159	97,414	415,158	22,658	541,389
At December 31, 2011					
Cost	8,140	139,553	1,236,234	101,473	1,485,400
Accumulated depreciation	(1,981)	(42,139)	(821,076)	(78,815)	(944,011)
Carrying amount	6,159	97,414	415,158	22,658	541,389
Of which held for sale					(5,165)
					536,224

The closing balance of Property, plant and equipment (PPE) includes assets in the course of construction in an amount of HUF 44,252 million as at December 31, 2011 (2010: HUF 42,670 million). In the table above the assets in course of construction are shown in the categories where the asset is expected to be placed into service.

Additions due to business combinations include the fair value of the assets acquired by Magyar Telekom through business combinations in the reported years. Differences between the preliminary and the final purchase price allocation are also included in this line.

Additions due to and revisions of asset retirement obligations represent the amounts recognized as part of the carrying amounts of the constructed assets against a provision for asset retirement obligation in the reported year (see also Note 19.5).

Investments represent the regular investing activity in PPE assets. These additions are shown net of the investment tax credit related to broadband investments. For more details, see Note 9.4.

No impairment was identified in 2011 and 2010.

The reclassifications between asset categories or their impact on depreciation expense was not material.

Included in buildings are assets sold and leased back under finance lease conditions. At December 31, 2011 the gross book value of the leased back assets is HUF 2,595 million (2010: HUF 1,706 million) and the net book value is HUF 1,590 million (2010: HUF 668 million).

Included mainly in buildings and telecom equipment are assets leased under finance lease conditions (other than sale and lease back). At December 31, 2011 the gross book value of the finance leased assets is HUF 1,360 million (2010: HUF 1,642) and the net book value is HUF 590 million (2010: HUF 780 million).

Included in telecommunications equipment at December 31, 2011 are assets leased under operating lease contracts to customers with a gross book value of HUF 943 million (2010: HUF 1,120 million) and net book value of HUF 35 million (2010: HUF 78 million). The future minimum lease payments receivable under these contracts are disclosed in Note 33.4.

HUF 2,180 million of PPE has restricted titles as at December 31, 2011 (2010: HUF 1,448 million), which are included in our assets as finance leases. The Group has no PPE pledged as security as at December 31, 2011 or December 31, 2010.

The reviews of the useful lives (and residual values) of property, plant and equipment during 2011 affected the lives of a large number of assets including primarily radio equipment, cable TV network, and antennas. In case of radio equipment, the revision resulted in a faster depreciation in 2011 and 2012 as a result of a group wide modernization of the radio access network to enable 4G services. The rest of the revisions on the other hand primarily resulted in the extension of the useful lives of the assets as a result of later expected replacement of the affected assets than originally estimated. The revision results in the following change in the original trend of depreciation in the current and future years .

In HUF millions	**2011**	**2012**	**2013**	**2014**	**After 2014**
(Decrease) / increase in depreciation expense	1,219	(7)	1,460	(392)	(2,435)

The useful lives assigned to different types of property, plant and equipment are as follows:

	Years
Buildings	5 - 50
Duct, cable and other outside plant	3 - 38
Other telecommunications equipment	2 - 25
Other equipment	2 - 12

13 Intangible assets

In HUF millions	Goodwill	Software	Concessions and licenses	Other	Total
At January 1, 2010					
Cost	247,109	164,668	52,134	25,906	489,817
Accumulated amortization	-	(118,058)	(18,289)	(16,407)	(152,754)
Accumulated goodwill impairment	(969)	-	-	-	(969)
Carrying amount	246,140	46,610	33,845	9,499	336,094
Carrying amount - January 1, 2010	246,140	46,610	33,845	9,499	336,094
Exchange differences	200	214	154	107	675
Additions due to business combinations	1,227	-	-	763	1,990
Investments	-	18,760	117	396	19,273
Disposals	-	(23)	-	(10)	(33)
Decrease due to sale of subsidiary	(74)	-	(333)	-	(407)
Amortization charge	-	(18,064)	(4,301)	(2,234)	(24,599)
Reclassifications	-	-	(838)	838	-
Carrying amount - December 31, 2010	247,493	47,497	28,644	9,359	332,993
At December 31, 2010					
Cost	247,493	182,250	50,357	27,520	507,620
Accumulated amortization	-	(134,753)	(21,713)	(18,161)	(174,627)
Accumulated goodwill impairment	-	-	-	-	-
Carrying amount	247,493	47,497	28,644	9,359	332,993
Of which held for sale					-
					332,993
Carrying amount - January 1, 2011	247,493	47,497	28,644	9,359	332,993
Exchange differences	833	1,068	605	369	2,875
Additions due to business combinations	323	462	-	1,251	2,036
Investments	-	20,908	139	140	21,187
Disposals	-	-	-	(5)	(5)
Impairment	(31,390)	-	-	-	(31,390)
Amortization charge	-	(13,748)	(4,403)	(2,713)	(20,864)
Reclassifications	-	1,481	-	-	1,481
Carrying amount - December 31, 2011	217,259	57,668	24,985	8,401	308,313
At December 31, 2011					
Cost	248,649	206,520	51,469	20,292	526,930
Accumulated amortization	-	(148,852)	(26,484)	(11,891)	(187,227)
Accumulated goodwill impairment	(31,390)	-	-	-	(31,390)
Carrying amount	217,259	57,668	24,985	8,401	308,313
Of which held for sale					-
					308,313

Additions due to business combinations include the fair value of assets acquired by Magyar Telekom through business combinations in the reported years and the goodwill arising on these business combinations. Differences between the preliminary and the final purchase price allocation are also included in this line.

Investments represent the regular investing activity in intangible assets.

The amortization expense as well as the impairment losses of intangible assets including also goodwill is accounted for in the depreciation and amortization line of the Statement of comprehensive income.

Other than goodwill, the Group has no intangible assets with indefinite useful life. Intangible assets other than goodwill are amortized over their respective economic useful lives, as indicated below.

	Years
Software	2 - 8
Concessions and licenses	3 - 25
Other intangible assets	3 - 10

The reviews of the useful lives of intangible assets during 2011 affected the lives of a large number of assets including primarily acquired and internally developed software and server user rights. The revisions primarily resulted in the extension of the useful lives as a result of later expected replacement of the affected assets than originally estimated. The revision results in the following change in the original trend of depreciation in the current and future years .

In HUF millions	2011	2012	2013	2014	After 2014
(Decrease) / increase in depreciation expense	(2,618)	(216)	1,014	619	1,201

The most significant intangible assets of the Group are the goodwill arising on business combinations. For the goodwill impairment tests, the total amount of goodwill was allocated to the operating segments of the Group as follows.

In HUF millions	As at December 31,	
	2010	2011
Hungary	162,589	162,661
T-Systems	27,749	27,952
Macedonia	51,379	20,199
Montenegro	5,776	6,447
Total goodwill	247,493	217,259

The Group regularly carries out an impairment test on goodwill in the last quarter of the financial years. During the annual impairment test conducted in the last quarter of 2010 no goodwill impairment was established for any goodwill of the Group. As a result of the impairment testing carried out in 2011 we identified and recognized an impairment loss of HUF 31,390 million on the goodwill of the Macedonia segment. No goodwill allocated to the other segments had to be impaired in 2011. For more details, see Note 4.2.

Besides goodwill, the most significant individual intangible assets are the concessions and licenses, which are listed in the table below.

In HUF millions	As at December 31,	
	2010	2011
Hungarian GSM license	10,747	8,466
Hungarian UMTS license	10,699	9,508
Macedonian UMTS license	2,342	2,289
Other	4,856	4,722
Total concessions and licenses	28,644	24,985

The Group has no intangible assets with restricted title or pledged as security as at December 31, 2011 or December 31, 2010.

14 Investments in associates and joint ventures

In HUF millions	For the year ended December 31, 2010	2011
Opening balance	186	77
Dividends	(81)	(9)
Share of associates' and joint ventures' profits / (losses)	(27)	12
Budakalász fully acquired in 2011	-	(22)
Liquidation of Netrekész	(1)	-
Liquidation of Hunsat.	-	(58)
Closing balance	77	0

Hunsat discontinued its commercial operations in 2010 and was liquidated in 2011. Netrekész was liquidated in 2010.

The remaining 75% shares of Budakalász were acquired in November 2011 (see also Note 5.1.3), as a result of which the Group has no associates or joint ventures as of December 31, 2011.

15 Other non current assets

Other non current assets mainly include long-term prepaid employee benefits.

16 Financial liabilities to related parties

Financial liabilities to related parties include HUF and EUR denominated loans taken from DT Group. In addition, for the whole nominal amount and interest payment of loans denominated in EUR granted by DTIF we have cross-currency interest rate swap agreements in place so that Magyar Telekom's exposure in fact remains in HUF. The loans and the related swap agreements are accounted for and disclosed on a gross basis. These loans were primarily taken for significant acquisitions and dividend payments. Some of these loans, when expiring, are also refinanced by DTIF, depending on the actual cash position of the Group.

The tables below show the details of the financial liabilities towards Deutsche Telekom Group members as at December 31, 2011 and 2010.

December 31, 2011	Carrying amount in HUF millions	Currency	Interest rate (%)	Fixed / floating	Repayable
	9,594	HUF	6.53	floating	Jan 2012
	40,271	HUF	7.75	floating	May 2012
Due within 1 year	49,865				
Derivatives	-				
Total current	49,865				
	9,594	HUF	6.54	floating	Jan 2013
	25,326	HUF	7.25	fixed	Oct 2013
	24,298	EUR	3.76	fixed	Jun 2014
	51,553	EUR	4.46	fixed	Jan 2015
	53,038	HUF	8.30	fixed	May 2015
	28,487	HUF	6.23	fixed	Dec 2016
	14,059	HUF	6.30	fixed	Dec 2016
	7,842	EUR	3.71	fixed	May 2017
	15,969	EUR	4.08	fixed	Nov 2018
Total non current	230,166				

December 31, 2010	Carrying amount in HUF millions	Currency	Interest rate (%)	Fixed / floating	Repayable
	9,579	HUF	5.72	floating	Jan 2011
	25,323	HUF	6.02	floating	Apr 2011
	35,324	HUF	7.21	fixed	Jul 2011
Due within 1 year	70,226				
Derivatives	1,982				
Total current	72,208				
	9,579	HUF	5.72	floating	Jan 2012
	40,225	HUF	6.39	floating	May 2012
	9,579	HUF	5.72	floating	Jan 2013
	25,327	HUF	7.26	fixed	Oct 2013
	21,896	EUR	3.76	fixed	Jun 2014
	46,046	EUR	4.46	fixed	Jan 2015
	53,034	HUF	8.30	fixed	May 2015
	28,478	HUF	6.23	fixed	Dec 2016
Total non current	234,164				

The table below shows the carrying amounts and fair values of the related party loans.

	At December 31,			
In HUF millions	2010		2011	
	Book value	Fair value	Book value	Fair value
HUF denominated loans				
At fixed rate	142,163	143,880	120,910	118,758
At floating rate	94,285	94,285	59,459	59,459
	236,448	238,165	180,369	178,217
EUR denominated loans				
At fixed rate	67,942	72,928	99,662	108,254
At floating rate	-	-	-	-
	67,942	72,928	99,662	108,254
Swaps	1,982	1,982	-	-
Total related party financial liabilities	306,372	313,075	280,031	286,471

The weighted average interest rate on related party loans was 6.23% in 2011 (6.30% in 2010). The fixed interest rate loans are exposed to fair value risk as it can be seen in the table above. Any decrease of market interest rates will result in an increase of the fair value of the fixed interest rate liabilities.

Derivatives contracted with related parties include cross-currency interest rate swaps and FX forwards concluded with DT AG to change the Group's exposure to HUF in case of the EUR denominated loans and to cover FX needs of expected future foreign currency outflows.

There were no defaults and breaches in connection with the financial liabilities to related parties.

17 Other financial liabilities

		At December 31,	
In HUF millions		2010	2011
Bank loans	(a)	43,924	46,082
Finance lease payable (Note 33.1)		605	580
Accrued interest		60	428
Third party derivatives	(b)	869	-
Payable to the SEC and the DOJ	(c)	-	21,857
Other		1,189	1,208
Total other financial liabilities – current		46,647	70,155
Bank loans	(a)	6,199	14,579
Finance lease payable (Note 33.1)		2,254	2,733
Other		375	616
Total other financial liabilities – non current		8,828	17,928

(a) Bank loans

In HUF millions	As at December 31, 2010	2011
Due within 1 year	43,924	46,082
Due in 1-2 years	2,788	3,576
Due in 2-3 years	3,411	11,003
Due after 3 years	-	-
Total bank loans	50,123	60,661

Loans totaling HUF 37,970 million at December 31, 2011 are revolving loans (2010: HUF 15,761 million) which can be prepaid at any time and may be drawn down in one to six month rolling periods.

The weighted average interest rate on bank loans was 6.98% in 2011 (5.74% in 2010).

The following table compares the carrying values and the fair values of the Group's bank loans.

In HUF millions	At December 31, 2010		2011	
	Book value	Fair value	Book value	Fair value
HUF denominated bank loans				
At fixed rate	11,850	12,150	-	-
At floating rate	27,135	27,135	53,286	53,286
	38,985	39,285	53,286	53,286
EUR denominated bank loans				
At fixed rate	8,128	8,198	4,667	4,699
At floating rate	3,010	3,010	2,708	2,708
	11,138	11,208	7,375	7,407
Total bank loans	50,123	50,493	60,661	60,693

Floating interest rate loans are subject to interests calculated based on mostly BUBOR (Budapest Inter-Bank Offered Rate) and EURIBOR (Euro Inter-Bank Offered Rate) plus a margin interest formula.

The majority of the Group's third party loans and borrowings are subject to floating interest rates, which are exposed to cash flow risks. If interest rates are rising, it results in higher cash outflows through interest payments.

There were no defaults and breaches in connection with other financial liabilities.

(b) Third party derivatives

Third party derivatives included FX forward and cross currency interest rate swaps.

(c) Payable to the SEC and the DOJ

During 2011 the Company made provisions related to the expected penalty to be paid to the DOJ and the disgorgement of profits and the related prejudgment interest expected to be paid to the SEC (see also Note 19) . As the agreements signed in December 2011 were approved by the relevant courts in early January 2012, the amounts provided for were reclassified as Other current financial liabilities. These amounts were paid to the DOJ and the SEC on January 6, 2012 and January 23, 2012 respectively. See Note 1.2 for more details.

(d) Credit facilities

At December 31, 2011, Magyar Telekom had un-drawn committed credit facilities of HUF 51,444 million (2010: HUF 54,603 million). These credit facilities, should they be drawn down, are subject to an interest rate of EURIBOR, BUBOR and commercial floating bank prime rates plus a margin depending on the currency and institution providing the facilities.

18 Trade payables

In HUF millions	At December 31, 2010	At December 31, 2011
Payable to DT Group companies	7,103	7,972
Payable to associates and joint ventures	7	-
Other trade payables	81,503	93,147
	88,613	101,119

19 Provisions

In HUF millions	Severance	MTIP	Employee-related Subtotal	DOJ/ SEC	Other legal cases	ARO	Other	Total
January 1, 2010	8,747	356	9,103	-	5,650	5,010	2,650	22,413
Amounts reversed	(1,005)	-	(1,005)	-	(1,574)	(8)	(347)	(2,934)
Additions	3,892	127	4,019	-	2,196	620	703	7,538
Accretion	-	-	-	-	477	174	53	704
Exchange rate difference	3	1	4	-	103	-	5	112
Amounts utilized	(5,427)	(5)	(5,432)	-	(551)	(110)	(1,314)	(7,407)
Reclassified to liabilities	-	(406)	(406)	-	-	-	-	(406)
December 31, 2010	6,210	73	6,283	-	6,301	5,686	1,750	20,020
Of which current	4,982	-	4,982	-	2,136	136	468	7,722
Of which non current	1,228	73	1,301	-	4,165	5,550	1,282	12,298
January 1, 2011	6,210	73	6,283	-	6,301	5,686	1,750	20,020
Amounts reversed	(577)	-	(577)	-	(1,153)	-	(574)	(2,304)
Acquired through business combinations	-	-	-	-	-	-	173	173
Additions	4,269	661	4,930	16,191	485	278	1,605	23,489
Accretion / interest	-	-	-	1,119	303	151	5	1,578
Exchange rate difference	12	-	12	4,547	287	-	63	4,909
Amounts utilized	(7,332)	-	(7,332)	-	(1,440)	(26)	(1,735)	(10,533)
Reclassified to liabilities	-	(536)	(536)	(21,857)	-	-	-	(22,393)
December 31, 2011	2,582	198	2,780	-	4,783	6,089	1,287	14,939
Of which current	1,563	-	1,563	-	1,492	56	592	3,703
Of which non current	1,019	198	1,217	-	3,291	6,033	695	11,236

Magyar Telekom does not expect any reimbursement with regards to the provisions recognized, therefore, no related assets have been recognized in the financial statements.

19.1 Severance

The majority of the provision for severance as at December 31, 2011 relates to the stand-by-pool and the employee terminations in 2012 in relation to the further efficiency improvement in Magyar Telekom Plc. The stand-by-pool of employees include people whose legal status is an employee, however, these people do not provide services to the Company any more, but the Company provides a reduced amount of compensation and pays social security expenses for them for maximum 4 years. This is a way of severance that is not paid in one lump sum but in maximum 48 installments following the discontinuation of services. The majority of the provision for severance as at December 31, 2010 related to the stand-by-pool and the employee terminations in 2011 in relation to the further efficiency improvement in Magyar Telekom Plc.

588 employees were dismissed in 2011 (2010: 552) at Group level, related to which severance payments were made. The balance of provision as at December 31, 2011 relates to 347 employees and former employees in the stand-by-pool (2010: 669).

The total payments made in relation to employee termination in 2011 amounted to HUF 9,627 million (2010: HUF 8,505 million).

19.2 MTIP

For more details on the Mid-term Incentive Plan see Note 24.1.

19.3 DOJ/SEC

During 2011 the Company made provisions related to the expected penalty to be paid to the DOJ and the disgorgement of profits and the related prejudgment interest expected to be paid to the SEC. When the expected payments became probable and estimable, the Company recognized the provisions in USD as the payments were expected to be agreed in USD terms. From the initial recognition of the provisions, the provided amounts were exposed to FX fluctuation, which is reflected in the exchange rate difference line of the table. As the agreements signed in December were approved by the relevant courts in early January 2012, the amounts provided for were reclassified as Other current financial liabilities as at December 31, 2011. See Note 1.2 for more details.

19.4 Other legal cases

Provisions for other legal cases mainly include amounts expected to be paid to regulatory and competition authorities as well as to ex-employees and trading partners as a result of legal disputes. There are numerous legal cases for which provisions were recognized, none of which are individually material, therefore not disclosed.

19.5 Asset retirement obligations (ARO)

Asset retirement obligations primarily exist in case of the telecommunications structures constructed on third parties' properties. The Group carries out a revision of the necessary provisions every year. The revisions did not result in material changes in 2011 or 2010.

19.6 Other provisions

Other provisions include guarantee obligations, onerous contracts and further other individually small items.

20 Other current liabilities

In HUF millions	At December 31, 2010	2011
Deferred revenue and advances received	11,273	10,739
Other taxes and social security	10,833	9,069
Salaries and wages	6,458	6,884
Dividend payable to Non-controlling interests	319	392
Other liabilities	2,083	2,129
	30,966	29,213

21 Other non current liabilities

Other non current liabilities primarily include deferred revenues related to long term projects and customer loyalty programs.

22 Revenue

In HUF millions	For the year ended December 31, 2010	2011
Fixed line revenues		
Voice retail	106,623	91,798
Voice wholesale	21,317	21,790
Internet	53,755	52,560
Data	27,710	27,050
TV	28,549	31,787
Equipment	4,091	3,852
Other fixed line revenues	7,588	11,715
Total Fixed line revenue	249,633	240,552
Mobile revenues		
Voice retail	185,967	177,226
Voice wholesale	36,815	31,728
Voice visitor	4,217	3,590
Non voice	57,789	62,146
Equipment	22,691	25,999
Other mobile revenues	7,694	7,829
Total Mobile revenue	315,173	308,518
System integration and IT revenue	44,773	48,547
Total revenue	609,579	597,617

None of the Group's customers represent a significant source of revenue. Revenues from transactions with a single external customer (or group of entities that - knowingly to us – are under common control of a third party or government) do not exceed 10 per cent of the Group's revenues.

23 Expenses directly related to revenues

In HUF millions	For the year ended December 31, 2010	2011
Voice, data and internet related payments	65,247	60,598
Material cost of equipment sold	41,037	44,595
Payments to agents and other subcontractors	51,143	55,854
	157,427	161,047

24 Employee related expenses

In HUF millions	For the year ended December 31, 2010	2011
Short term benefits	93,992	92,203
Share based payments - MTIP (Note 24.1)	127	661
Share based payments - ex-CEO (Note 24.2)	(49)	-
Share based payments - Share bonus to employees (Note 24.3)	580	-
Termination benefits (Note 19.1)	5,965	5,987
Total before capitalization	100,615	98,851
Expenses capitalized	(6,731)	(7,028)
	93,884	91,823
Total costs expensed in relation to defined contribution plans (including social security)	20,361	19,978
Average number of employees (full time equivalent)	10,351	10,127
Closing number of employees (full time equivalent)	10,258	10,111

24.1 Mid-term incentive plan (MTIP)

In 2004 Magyar Telekom launched a Mid Term Incentive Plan (MTIP) for its top and senior management, whereby the targets to be achieved are based on the performance of the Magyar Telekom share. The MTIP is a cash settled long term incentive instrument which was planned to cover five years, with a new package being launched in each year, and with each tranche lasting for three years. In 2009, 2010 and 2011, Magyar Telekom decided to prolong the original program by one additional year respectively, with the same concept. At the beginning of the plan each participant has an offered bonus. This bonus will be paid out at the end of the plan, depending on the achievement of the two fixed targets, an absolute Magyar Telekom share specific and a relative Index target. Depending on the achievement of the targets, 0%, 50% or 100% of the bonus is paid if neither, one or both of the targets are met, respectively.

The relative performance target is linked to the Total Return of the Magyar Telekom share compared to the performance of the Dow Jones Euro STOXX Total Return Index during the vesting period, each at the last 20 trading days. Measurement is the un-weighted average Magyar Telekom share price plus dividend payments. The absolute performance target is achieved when the Magyar Telekom share price, adjusted for dividends paid during the tenure, is more than 35 percent higher at the end of the lock–up period than at the beginning of the plan. The basis of the calculation is the un-weighted average closing price of the Magyar Telekom share at the Budapest Stock Exchange during the last 20 trading days before the beginning and the end of the plan.

The share price calculated according to the above are included in the table below. When determining the Group's liability, these target figures are weighted with the fair value factors of achieving these targets. The fair value factors are calculated using the Monte Carlo technique. The target figures are multiplied by the relevant fair value factors and these amounts are then accrued for the given tranche period. This technique aims to determine the fair values of the share options granted and present it in accordance with the accruals concept.

Tranche	Vesting period	MT Share price at the beginning of the vesting period (HUF)	Fulfillment
2008	January 1, 2008 – December 31, 2010	912	Only relative target met
2009	January 1, 2009 – December 31, 2011	561	Only relative target met
2010	January 1, 2010 – December 31, 2012	725	-
2011	January 1, 2011 – December 31, 2013	524	-

The provision for the payments in relation to the MTIP program and the movements thereof are disclosed in Note 19.

24.2 The former CEO's share option plan

The former CEO of Magyar Telekom was granted share options in the past, out of which the options granted in 2000 remained unexercised until 2010, when they lapsed. The lapse of these share options resulted in the release of the total balance of the Reserve for equity settled share based transactions.

24.3 Shares allocated to employees

The Board of Directors of Magyar Telekom approved a share allocation program under which Magyar Telekom shares were awarded to the Company's best performing employees in December 2010. In total, 1,112,679 treasury shares were granted to employees for free. The amount recognized as an expense includes the grant date fair value of the shares. The program awarded the participants based on their past performance without any further service commitments made by either the employees or the employer. Consequently, the total cost of the share based compensation program was recognized in 2010.

24.4 Matching Share Plan of Magyar Telekom

In December 2011 the Board of Directors approved the implementation of the revolving Matching Share Plan of Magyar Telekom. The program is implemented for the CEO of Magyar Telekom starting in 2012. In order to ensure the long-term incentive effect and orientation toward the sustained development of the Company, an amount of minimum 10% of the gross annual variable bonus is to be invested in shares of Magyar Telekom. The investment must be made from the net payout. The CEO has the option of voluntary increase to a maximum of 33.3% of his bonus. These shares are to be held for a period of at least 4 years (lock-up period). After the lock-up period of 4 years has passed, one additional share („matching share") will be granted for every share acquired as part of the aforementioned personal investment. The program is planned to be revolving in 5 consecutive years starting in 2012. As the vesting period of the program starts with the first purchase of shares by the CEO in 2012, no expenses have been recognized for the program in 2011.

25 Other operating expenses

In HUF millions		For the year ended December 31, 2010	2011
Materials, maintenance and service fees		63,373	61,602
Hungarian telecommunications and other crisis taxes	(a)	26,970	25,350
DOJ criminal penalty and SEC disgorgement of profits	(b)	-	16,191
Marketing		13,437	12,895
Rental and operating lease		12,981	13,794
Fees and levies		12,276	12,298
Bad debt expense		9,991	6,255
Consulting, audit and other expert fees	(c)	7,825	5,406
Other expenses		1,897	1,266
		148,750	155,057

(a) Hungarian telecommunications and other crisis taxes

On October 18, 2010 the Hungarian Parliament passed an act imposing special "crisis" taxes on telecommunications services, retail sales and energy sales as of January 1, 2010. These taxes were enacted for a defined period of 2010-2012.

Although Magyar Telekom is also engaged in energy and retail sales, the tax burden on those are either not applicable to the Group (energy) or not material (retail). The vast majority of the amount included in the table above relates to the revenues earned from electronic telecommunications services provided by the Hungarian members of the Group in the years presented. The tax is defined as a certain percentage of the revenue generated from the services defined as electronic telecommunications. The tax is progressive, i.e. the more revenue is generated a higher tax rate is applicable. Due to the high amount of revenues generated by the Group, the vast majority of the Group's Hungarian revenues are in the highest tax band subject to a tax rate of 6.5%.

The classification of these taxes requires judgment. Management believes that these taxes are not taxes on consumption of services by end customers but rather taxes on entities operating in selected industries. These taxes were levied retrospectively in 2010, the taxes are calculated on the combined revenues of groups using graduated tax rates and the calculation ignores whether the revenues are collected from end customers or not. Therefore management believes that there are strong indicators that these taxes are not sales taxes collected on behalf of the government, but rather taxes on the operations of the companies, and consequently these taxes are classified as operating expense in the consolidated financial statements.

(b) DOJ criminal penalty and SEC disgorgement of profits

During 2011 the Company made provisions related to the expected penalty to be paid to the DOJ and the disgorgement of profits expected to be paid to the SEC. The amount in the table above includes these items recognized as operating expenses during the year. See Note 1.2 for more details.

(c) Audit costs included in Consulting, audit and other expert fees

Consulting, audit and other expert fees among others include expenses incurred in relation to the audit of the standalone and consolidated financial statements of the Company by PricewaterhouseCoopers (PwC) as follows.

In HUF millions	For the year ended December 31, 2010	2011
Audit of the financial statements	527	375
Other audit related fees	40	84
Other non audit related fees	4	25
Total expenses payable to PwC	571	484

Audit of the financial statements in the above table are the aggregate fees of PwC in connection with the audit of our annual financial statements, reviews of quarterly reports and services performed in relation to legal obligations and submissions required by regulatory provisions.

Other audit-related fees in the above table are the aggregate fees of PwC for services which are normally performed by the external auditor in connection with the auditing of the annual financial statements, e.g. advice on issues of accounting and reporting, which were not classified as audit services, and support with the interpretation of new accounting and reporting standards. Audit-related fees in 2011 included HUF 21 million (2010: HUF 40 million) incurred relating to the investigations (Note 1.2).

Other non audit related fees in the above table are fees of PwC primarily related to services like participation by Magyar Telekom employees in conferences and training sessions organized by PwC.

26 Other operating income

In HUF millions	For the year ended December 31, 2010	2011
Gain on the sale of PPE, Intangible assets and assets held for sale	327	1,940
Income received for the relocation and reconstruction of our own network	1,233	1,166
Penalty interest collected	853	964
Government grants received/receivable for the compensation of expenses	-	811
Other operating income	1,035	1,511
	3,448	6,392

27 Interest income

In HUF millions	For the year ended December 31, 2010	2011
Finance lease interest income	1,334	1,150
Other interest income	3,604	2,483
	4,938	3,633

28 Interest expense

In HUF millions	For the year ended December 31, 2010	2011
Interest expense to DT	18,397	17,492
Other interest expense	4,660	3,476
Finance lease interest expense	529	922
Accretion / interest on provisions	704	1,578
less: borrowing costs capitalized	(506)	(284)
	23,784	23,184

Accretion / interest on provisions include HUF 1,119 million of prejudgment interest related to the disgorgement of profits as approved in the Final judgment filed by the SEC against the Company. For more details see Note 1.2.

Interest expense is shown net of interest capitalized using an average borrowing rate of 5.78% in 2011 (2010: 6.02%). When calculating the borrowing costs capitalized, other financial expenses (included in Note 29) are also considered, however, for disclosure purposes, we included the borrowing costs capitalized in the table above.

29 Other finance expense – net

In HUF millions	For the year ended December 31, 2010	2011
Fee expense	4,236	4,174
Net foreign exchange losses / (gains)	2,855	21,095
Losses / (gains) on the subsequent measurement of financial instruments at fair value through profit and loss (derivatives) contracted with related parties	(1,410)	(11,303)
Losses / (gains) on the subsequent measurement of financial instruments at fair value through profit and loss (derivatives) contracted with third parties	998	(4,359)
Losses / (gains) on the derecognition of financial instruments at fair value through profit and loss contracted with related parties	1,996	2,581
Losses / (gains) on the derecognition of financial instruments at fair value through profit and loss contracted with third parties	592	723
Losses / (gains) on the derecognition of AFS financial instruments (Reclassifications from Other comprehensive income)	-	-
	9,267	12,911

Net foreign exchange losses include HUF 4,547 million foreign exchange loss incurred on the provisions recognized for the amounts paid to the DOJ and the SEC. For more details see Note 1.2.

30 Purchase of property, plant and equipment and intangible assets

In HUF millions	For the year ended December 31, 2010	2011
Investments in property, plant and equipment (Note 12)	72,489	62,609
Investments in intangible assets (Note 13)	19,273	21,187
Total investments in PPE and intangible assets	91,762	83,796
Recognition / (Derecognition) of investment tax credit (Note 9.4)	(3)	-
Change in payables relating to capital expenditures	(4,459)	(3,722)
Cash payments for purchases of PPE and intangible assets	87,300	80,074

The Group had no significant non cash transactions in any of the reported years.

31 Purchase of subsidiaries and business units

In HUF millions	For the year ended December 31, 2010	2011
Daten-Kontor (Note 5.1.1)	-	1,073
Globe (Note 5.1.2)	-	1,000
Budakalász (Note 5.1.3)	-	239
Cable TV networks	39	212
ISH	74	110
Modultechnika (Note 5.2)	1,421	41
Cash payments for purchases of subsidiaries and business units	1,534	2,675

Cash payments related to the purchase of subsidiaries and business units also include amounts paid as additional contingent purchase prices disbursed in years following the year of the business combination.

32 Reportable segments and information about geographical areas

32.1 Reportable segments

Magyar Telekom introduced a new reporting structure from the beginning of 2011. The Group's new operating segments are Hungary (which includes the former CBU, the SMB customers of BBU and the Headquarters and Technology Units) and T-Systems (which includes the former BBU, without the SMB customers). The Macedonia and Montenegro segments have not changed.

The Hungary segment operates in Hungary providing mobile, fixed line telecommunications and TV distribution services (including marketing, sales and customer relations activities) to residential and small businesses telecommunications customers with several million customers mainly under the T-Mobile and T-Home brands. The Hungary segment is also responsible for the wholesale mobile and fixed line services in Hungary, and performs strategic and cross-divisional management and support functions including Procurement, Treasury, Real estate, Accounting, Tax, Legal, Internal Audit and similar shared services and other central functions of the Group's management. This segment is also responsible for the Group's points of presence in Bulgaria, Romania and Ukraine providing wholesale services to local companies and operators. In addition, the Hungary segment is responsible for the operations and development of the mobile, fixed line and cable TV network as well as IT management in Hungary.

T-Systems operates in Hungary providing mobile and fixed line telecommunications, infocommunications and system integration services (including marketing, sales and customer relations activities) mainly under the T-Systems and T-Mobile brands to key business partners (large corporate customers and public sector).

The Group also has full-scale mobile and fixed line telecommunications operations in Macedonia and Montenegro, which represent two additional operating segments of the Group.

32.1.1 Information regularly provided to the MC

The following tables present the segment information by reportable segment regularly provided to the Management Committee of the Group, reconciled to the corresponding Group numbers. The information regularly provided to the MC includes several measures of profit which are considered for the purposes of assessing performance and allocating resources, including EBITDA adjusted for the impact of certain items considered as "special influence". These items vary year-over-year in nature and magnitude. Management believes that EBITDA is the segment measure that is most consistent with the measurement principles used in measuring the corresponding amounts in these financial statements.

Revenues	**For the year ended December 31,**	
In HUF millions	**2010**	**2011**
Total Hungary revenues	432,054	422,794
Less: Hungary revenues from other segments	(38,873)	(35,506)
Hungary revenues from external customers	393,181	387,288
Total T-Systems revenues	117,869	122,237
Less: T-Systems revenues from other segments	(11,780)	(15,783)
T-Systems revenues from external customers	106,089	106,454
Total Macedonia revenues	77,598	71,359
Less: Macedonia revenues from other segments	(134)	(130)
Macedonia revenues from external customers	77,464	71,229
Total Montenegro revenues	32,874	32,697
Less: Montenegro revenues from other segments	(44)	(42)
Montenegro revenues from external customers	32,830	32,655
Total consolidated revenue of the segments	609,564	597,626
Measurement differences to Group revenue	15	(9)
Total revenue of the Group	**609,579**	**597,617**

Segment results (EBITDA)	**For the year ended December 31,**	
In HUF millions	**2010**	**2011**
Hungary	144,909	128,223
T-Systems	14,756	18,444
Macedonia	40,248	37,914
Montenegro	11,370	11,453
Total EBITDA of the segments	211,283	196,034
Measurement differences to Group EBITDA	1,683	48
Total EBITDA of the Group	**212,966**	**196,082**
Depreciation and amortization of the Group	(100,872)	(132,915)
Total Operating profit of the Group	112,094	63,167
Net financial result	(28,113)	(32,462)
Share of associates’ and joint ventures’ profits / (losses)	(27)	12
Total Profit before income tax of the Group	83,954	30,717
Income tax expense	(6,583)	(27,538)
Total Profit for the year of the Group	77,371	3,179

Capital expenditure (Capex) on PPE and Intangible assets In HUF millions	As at December 31, 2010	 2011
Hungary	68,395	65,559
T-Systems	3,559	4,289
Macedonia	15,208	9,961
Montenegro	4,639	4,135
Total capital expenditure of the segments	91,801	83,944
Measurement differences to capital expenditure of the Group	(39)	(148)
Total investments of the Group in PPE and Intangible assets	**91,762**	**83,796**

Total investments of the Group in PPE and Intangible assets correspond to the "Investments" lines disclosed in Notes 12, 13 and 30.

32.2 Information about geographical areas

The table below shows the revenues generated from external customers in the countries where the Group operates, using the same measurement principles as for the corresponding Group numbers.

Revenues In HUF millions	For the year ended December 31, 2010	 2011
Hungary	495,385	489,691
Macedonia	77,464	71,229
Montenegro	32,830	32,655
Romania	2,958	3,274
Bulgaria	922	768
Ukraine	20	-
Total revenue of the Group	609,579	597,617

None of the Group's external customers represent a significant source of revenue.

The table below shows the Non current assets of the Group located in the countries of operations (including goodwill allocated to operating segments operating in these countries) and the reconciliation to the total Non current assets of the Group, using the same measurement principles as for the corresponding Group numbers.

Non current assets In HUF millions	As at December 31, 2010	 2011
Hungary	703,783	696,693
Macedonia	132,510	99,870
Montenegro	41,734	43,301
Bulgaria	3,165	3,361
Romania	2,281	2,059
Ukraine	13	8
Total excluding Other non current financial assets and Deferred tax assets	883,486	845,292
Other non current financial assets (Note 8.2)	24,033	31,590
Deferred tax assets (Note 9.4)	913	750
Total Non current assets of the Group	908,432	877,632

33 Leases and other commitments

33.1 Finance lease –Group as lessee

Finance leases in 2010 and 2011 mainly relate to the sale and lease back of spaces in buildings accommodating telephone exchanges. In most cases the contracts are denominated in EUR, the term of the leases is 5-10 years, and the contracts include renewal options but no purchase options.

Future lease payments under finance leases related to sale and lease back transactions at December 31, 2010 and 2011 are as follows:

In HUF millions	At December 31, 2010			At December 31, 2011		
	Present value	Interest component	Minimum lease payment	Present value	Interest component	Minimum lease payment
Within 1 year	277	344	621	354	858	1,212
1-5 years	1,064	812	1,876	1,518	2,512	4,030
After 5 years	276	62	338	596	1,916	2,512
Total	1,617	1,218	2,835	2,468	5,286	7,754

Finance leases other than sale and lease back in 2010 and 2011 mainly relate to vehicles and IT equipment. In most cases the contract term of the leases is 3-5 years with renewal and purchase options.

Future lease payments under finance leases other than sale and lease back transactions at December 31, 2010 and 2011 are as follows:

In HUF millions	At December 31, 2010			At December 31, 2011		
	Present value	Interest component	Minimum lease payment	Present value	Interest component	Minimum lease payment
Within 1 year	328	131	459	226	99	325
1-5 years	593	195	788	331	123	454
After 5 years	321	59	380	288	56	344
Total	1,242	385	1,627	845	278	1,123

The Group has no contingent rents related to its finance leases. The Group does not sub-lease any of the assets leased in a finance lease contract.

33.2 Operating lease –Group as lessee

Operating lease commitments are mainly in respect of the rental of mobile cell sites, and to a lesser extent, related to buildings, network and other telecommunications facilities.

In HUF millions	At December 31, 2010	2011
Within 1 year	7,711	8,017
1-5 years	20,987	19,746
After 5 years	14,171	13,057
Total	42,869	40,820

The lease commitments represent a high amount of individually immaterial lease agreements, the terms of which vary on a wide range, spanning from 3 to 20 years with renewal options in most cases, but no purchase options.

33.3 Finance lease –Group as lessor

Finance leases primarily include the private mobile Tetra network constructed for the exclusive use of the Hungarian State, and to a lesser extent equipment provided to business customers as part of our outsourcing contracts where the Group is the service provider.

Future lease receivables under finance leases at December 31, 2010 and 2011 are as follows:

In HUF millions	At December 31, 2010			At December 31, 2011		
	Present value	Interest component	Minimum lease receipt	Present value	Interest component	Minimum lease receipt
Within 1 year	4,298	1,403	5,701	4,267	1,140	5,407
1-5 years	15,809	3,102	18,911	12,147	1,715	13,862
After 5 years	278	74	352	369	98	467
Total	20,385	4,579	24,964	16,783	2,953	19,736

The interest component represents the unearned finance income. The present value due within one year is included in Other current financial assets, while the present value after one year is included in Other non current financial assets. The finance income accruing to the Group over the lease term is recognized in the Profit for the year (Interest income).

The unguaranteed residual values accruing to the benefit of the Group are insignificant.

33.4 Operating lease – Group as lessor

The following table includes the future minimum lease payments receivable by the Group for the operating leases of towers and PBX (private business exchange) equipment where Magyar Telekom is the lessor.

In HUF millions	At December 31, 2010	At December 31, 2011
Within 1 year	1,165	1,340
1-5 years	2,755	1,901
After 5 years	1,072	949
Total	4,992	4,190

33.5 Purchase commitments for tangible and intangible assets

The table below summarizes Magyar Telekom's contractual purchase commitments for tangible and intangible assets with the majority falling due within one year.

In HUF millions	At December 31, 2010	At December 31, 2011
Property, plant and equipment	5,951	4,150
Intangible assets	3,000	9,825
Total	8,951	13,975

In addition to the above commitments, the Company filed an auction bid in December 2011 with the Hungarian

National Media and Infocommunications Authority for unused spectrum in the 900 MHz frequency band, relating to the provision of radio communications services. The spectrum can be utilized in a technology-neutral manner, allowing for the installation and operation of GSM, UMTS, LTE and/or WiMAX mobile networks.

On January 31, 2012, the Company received from the Authority the first instance, non-final decision closing the auction. Pursuant to the first instance decision, the Company won the right of use of two duplex frequency blocks of 1 MHz each (one EGSM-band duplex frequency block of 1 MHz plus one PGSM-band duplex frequency block of 1 MHz) for a period of 15 years. Pursuant to the first instance decision, Magyar Telekom is required to pay an auction price of 10.9 billion HUF + VAT for these frequency blocks.

34 Related party transactions

No provision was recognized for doubtful debts related to the amount of outstanding balances; and no expense was incurred during the periods presented in respect of doubtful debts due from related parties.

34.1 Deutsche Telekom Group and the Federal Republic of Germany

34.1.1 Deutsche Telekom Group

Deutsche Telekom AG (DTAG) is the ultimate controlling owner of Magyar Telekom Plc. holding 59.21% of the issued shares. Deutsche Telekom (DT) Group has a number of fixed line, mobile and IT service provider subsidiaries worldwide, with whom Magyar Telekom Group has regular transactions.

The Company is directly owned by MagyarCom GmbH, which is a holding subsidiary of DTAG. Magyar Telekom pays dividends annually to its owners including MagyarCom GmbH.

Deutsche Telekom International Finance (DTIF) is the treasury center of DT Group, which typically provides loan financing across the DT Group including Magyar Telekom.

The table below summarizes the above related party transactions with DT group.

In HUF millions	2010	2011
Revenues from telecom services provided to DT Group companies	22,395	25,594
Costs of services provided by DT Group companies	(16,497)	(15,751)
Interest expense to DTIF	(18,397)	(17,492)
Dividend paid to MagyarCom GmbH	(45,690)	(30,872)
Accounts receivable from DT Group companies	6,991	8,333
Accounts payable to DT Group companies	(7,103)	(7,972)
Loans payable to DT Group companies	(304,390)	(280,031)
Fair value of swap agreements with DTAG - asset	1,004	10,484
Fair value of swap agreements with DTAG - liability	(1,982)	-

Deutsche Telekom has pledged its support for Magyar Telekom’s financing needs through to June 30, 2013.

34.1.2 The Federal Republic of Germany

The Federal Republic of Germany is both a direct and an indirect shareholder and holds approximately 32 percent of the share capital of DTAG. Due to the average attendance at the shareholders’ meeting, the Federal Republic of

Germany represents a solid majority at the shareholders' meeting of DTAG, although it only has a minority shareholding, making DTAG a dependant company of the Federal Republic. Therefore, the Federal Republic and the companies controlled by the Federal Republic or companies over which the Federal Republic can exercise a significant influence are classified as related parties of DTAG, and consequently of Magyar Telekom as well.

DTAG and Magyar Telekom did not execute as part of its normal business activities any transactions that were individually material in the 2011 financial year with companies controlled by the Federal Republic or companies over which the Federal Republic can exercise a significant influence.

34.2 Associates and joint ventures

The Group has no significant associates or joint ventures and the transactions with them are also insignificant.

34.3 Board and supervisory board members

In HUF millions	For the year ended December 31, 2010	2011
Remuneration of the members of the Board of Directors	13	14
Remuneration of the members of the Supervisory Board	48	56
Loans granted to the members of the Board of Directors	-	-
Loans granted to the members of the Supervisory Board	3	2

34.4 Key management

Key management has been identified as the members of the Group's Management Committee, which is the chief operating decision making body of Magyar Telekom.

The table below shows in total the compensation expenses (including social security and other payroll related taxes) incurred by the Group in relation to the key management.

In HUF millions	For the year ended December 31, 2010	2011
Salaries and other short-term employee benefits	1,335	1,521
Contractual termination expense	497	-
Share based compensation (Note 24.1)	45	216
	1,877	1,737

The Group does not provide loans to its key management.

In 2001, DT's shareholders approved the introduction of the 2001 Stock Option Plan, resulting in the granting of stock options in 2001 and 2002. 50 percent of the options granted to each beneficiary may only be exercised following the end of a vesting period of two years. The remaining 50 percent of the options granted to each beneficiary may be exercised after the end of a vesting period of three years. All options are vested as of December 31, 2011. The exercise price of the 2001 option is EUR 30.00, the term of the options ran until August 12, 2011. The exercise price of the 2002 option is EUR 12.36, the term of the options runs until July 14, 2012. At the time they were granted, the options of the 2001 and 2002 tranches had no intrinsic value, but a fair value of EUR 4.87 and EUR 3.79 respectively. The Company's Chief Financial Officer (CFO), who was a senior manager of DT at the time of the stock option, is a participant of the 2002 tranche, having 6,510 share options. Magyar Telekom does not have any potential obligation deriving from the CFO's share options, and no expenses or liabilities have been recognized in the presented years as these options are not in the scope of IFRS 2 and IFRIC 11 according to the transitional rules.

35 Additional disclosures on financial instruments

35.1 Financial assets and liabilities

The tables below include the carrying amounts and fair values of the Group's financial assets and liabilities as at December 31, 2011 and 2010.

The Group classifies fair value measurements using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. The fair value hierarchy has the following levels:

(a) quoted prices (unadjusted) in active markets for identical assets or liabilities (Level 1);
(b) inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly (Level 2); and
(c) inputs for the asset or liability that are not based on observable market data (Level 3).

The level in the fair value hierarchy within which the fair value measurement is categorized in its entirety is determined on the basis of the lowest level input that is significant to the fair value measurement in its entirety. The significance of an input is assessed against the fair value measurement in its entirety.

There was no transfer between Level 1 and Level 2 financial instruments. Loans and receivables and most of the financial liabilities are measured at amortized cost, but fair value information is also provided for these. The fair values of these assets and liabilities were determined using level 3 type information. There are no assets or liabilities carried at fair value where the fair value was determined using level 3 type information.

35.1.1 Financial assets – Carrying amounts and fair values

December 31, 2011 In HUF millions	Carrying amount Loans and receivables	Held-to-maturity	Available-for-sale (Level 1)	Held for trading (Level 2)	Total	Fair value
Cash and cash equivalents	14,451	-	-	-	14,451	14,451
Bank deposits with original maturities over 3 months	54,926	-	-	-	54,926	54,926
Trade receivables	113,350	-	-	-	113,350	113,350
Trade receivables over one year	1,696	-	-	-	1,696	1,554
Employee loans	5,392	-	-	-	5,392	3,815
Derivative financial instruments contracted with related parties	-	-	-	10,484	10,484	10,484
Derivative financial instruments contracted with third parties	-	-	-	3,841	3,841	3,841
Loans to third parties	1,164	-	-	-	1,164	892
RDC receivables	620	-	-	-	620	566
Financial assets AFS	-	-	278	-	278	278
Other current	1,422	-	-	-	1,422	1,422
Other non current	270	-	-	-	270	270
Total	193,291	-	278	14,325	207,894	205,849

December 31, 2010 In HUF millions	Carrying amount Loans and receivables	Held-to-maturity	Available-for-sale (Level 1)	Held for trading (Level 2)	Total	Fair value
Cash and cash equivalents	15,841	-	-	-	15,841	15,841
Bank deposits with original maturities over 3 months	47,798	-	-	-	47,798	47,798
Trade receivables	106,732	-	-	-	106,732	106,732
Trade receivables over one year	1,524	-	-	-	1,524	1,609
Employee loans	4,704	-	-	-	4,704	4,849
Derivative financial instruments contracted with related parties	-	-	-	1,004	1,004	1,004
Derivative financial instruments contracted with third parties	-	-	-	301	301	301
Loans to third parties	947	-	-	-	947	947
RDC receivables	715	-	-	-	715	689
Financial assets AFS	-	-	296	-	296	296
Other current	2,400	-	-	-	2,400	2,400
Other non current	519	-	-	-	519	519
Total	181,180	-	296	1,305	182,781	182,985

Loans and receivables are measured at amortized cost, while available-for-sale and held-for-trading assets are measured at fair value.

Cash and cash equivalents, trade receivables, loans to Deutsche Telekom Group companies and other current financial assets mainly have short times to maturity. For this reason, their carrying amounts at the end of the reporting period approximate their fair values.

Financial assets available for sale include insignificant investment in equity instruments, all measured at fair value.

Finance lease receivables meet the criteria of a financial instrument, but these are recognized and measured according to IAS 17 – Leases, therefore not included in the tables above, but in Note 33.3.

35.1.2 Financial liabilities – Carrying amounts and fair values

December 31, 2011

In HUF millions	**Carrying amount** Measured at amortized cost	**Carrying amount** Held for trading (Level 2)	**Total**	**Fair value**
Financial liabilities to related parties	280,031	-	280,031	286,471
Bank loans	61,089	-	61,089	61,120
Trade payables	101,119	-	101,119	101,119
Dividend payable	392	-	392	392
Nonconvertible bonds and debentures	190	-	190	172
Derivative financial instruments contracted with third parties	-	-	-	-
Other current	22,955	-	22,955	22,955
Other	496	-	496	496
Total	466,272	-	466,272	472,725

December 31, 2010

In HUF millions	**Carrying amount** Measured at amortized cost	**Carrying amount** Held for trading (Level 2)	**Total**	**Fair value**
Financial liabilities to related parties	304,390	1,982	306,372	313,075
Bank loans	50,183	-	50,183	50,553
Trade payables	88,613	-	88,613	88,613
Dividend payable	319	-	319	319
Nonconvertible bonds and debentures	191	-	191	168
Derivative financial instruments contracted with third parties	-	869	869	869
Other current	1,024	-	1,024	1,024
Other	210	-	210	210
Total	444,930	2,851	447,781	454,831

Derivatives are measured at fair value, while all other financial liabilities are measured at amortized cost.

Additional fair value information on the financial liabilities is provided in Notes 16 and 17.

Trade payables, dividend payable and other current financial liabilities generally have short times to maturity, therefore the carrying values approximate the fair values.

Finance lease liabilities meet the criteria of a financial instrument, but these are recognized and measured according to IAS 17 – Leases, therefore not included in the tables above, but in Note 33.1.

35.2 Items of income, expense, gains and losses arising on financial instruments

The tables below include income, expense, gains and losses arising on financial instruments in 2011 and 2010.

2011 In HUF millions	From interest	From subsequent measurement			From derecog-nition	From fee expense	Total net gain / (loss)
		At fair value	Currency translation	Impairment loss			
Available-for-sale financial assets (Level 1)	-	(21)	-	-	-	-	(21)
Financial instruments held for trading (Level 2)	-	15,683	-	-	(3,304)	-	12,379
Loans and receivables	2,473	-	1,378	(6,299)	-	(3,989)	(6,437)
Held-to-maturity investments	-	-	-	-	-	-	-
Financial liabilities measured at amortized cost	(20,493)	-	(22,235)	-	-	(141)	(42,869)
Net gain/(loss) of financial instruments under the scope of IAS 39	(18,020)	15,662	(20,857)	(6,299)	(3,304)	(4,130)	(36,948)

2010 In HUF millions	From interest	From subsequent measurement			From derecog-nition	From fee expense	Total net gain / (loss)
		At fair value	Currency translation	Impairment loss			
Available-for-sale financial assets (Level 1)	-	20	-	-	-	-	20
Financial instruments held for trading (Level 2)	-	412	-	-	(2,588)	-	(2,176)
Loans and receivables	3,597	-	749	(9,991)	-	(4,076)	(9,721)
Held-to-maturity investments	-	-	-	-	-	-	-
Financial liabilities measured at amortized cost	(21,772)	-	(3,364)	-	-	(160)	(25,296)
Net gain/(loss) of financial instruments under the scope of IAS 39	(18,175)	432	(2,615)	(9,991)	(2,588)	(4,236)	(37,173)

Impairment losses on Loans and receivables includes all expenses incurred or expected to be incurred in relation to the default of our customers. Before writing off or factoring, we impair the receivables to their recoverable amounts through the use of an impairment provision account, as a result of which the actual write-off or factoring of these receivables results in no derecognition gains or losses.

35.3 Other disclosures about financial instruments

Magyar Telekom Plc. is also exposed to risks that arise from the possible drawdown of guarantees in a nominal amount of HUF 17.7 billion as at December 31, 2011 (2010: HUF 14.1 billion). These guarantees were issued by Hungarian banks on behalf of Magyar Telekom as collateral to secure the fulfillment of the Group's certain contractual obligations. The Group has been delivering on its contractual obligations and expects to continue doing so in the future, therefore no drawdown of the guarantees has happened in 2011, and is not expected to happen in the future.

There were no financial assets or liabilities, which were reclassified into another financial instrument category.

No financial assets were transferred in such a way that part or all of the financial assets did not qualify for de-recognition.

The Group does not have compound financial instruments with multiple embedded derivatives.

36 Contingent assets and liabilities

36.1 Contingent assets

A contingent asset is a possible asset that arises from past events and whose existence will be confirmed only by the occurrence of uncertain future events not within the control of the Group. These assets are not recognized in the statement of financial position. The Group has no such contingencies where the inflow of economic benefits would be probable and material.

36.2 Contingent liabilities

The most significant contingent liabilities of the Group are described below. No provisions have been recognized for these cases as management estimates that it is unlikely that these claims originating from past events would result in any material economic outflows from the Group, or the amount of the obligation cannot be measured with sufficient reliability.

36.2.1 Macedonia

36.2.1.1 Compensation for termination of a service contract by T-Mobile MK

In January 2002, T-Mobile MK signed an agreement with a subcontractor, including a 3-month trial period, for the collection of T-Mobile MK's overdue receivables. After the expiration of the 3-month trial period, T-Mobile MK terminated this contract in April 2002 due to breaches of the contractual obligations by the subcontractor. The subcontractor initiated a lawsuit in April 2003 requesting damage compensation for foregone profit and compensation for services already rendered. Management estimates it unlikely that the subcontractor would win the court case against T-Mobile MK. The potential loss from the claim is approximately HUF 5.0 billion. The first instance decision in 2010 was in favor of T-Mobile MK, but the plaintiff submitted an appeal, therefore the timing of the final resolution is uncertain.

36.2.1.2 MKT's dispute on fixed-to-mobile termination fees

In 2005, MKT changed the retail prices for the traffic from fixed to mobile network. According to the interconnection agreements with the mobile operators the change in retail prices automatically decreased the interconnection fees for termination in the mobile networks. In February 2006, one of the Macedonian mobile operators, ONE, submitted to the Agency a request for dispute resolution with reference to the termination prices. The Agency rejected the requests of ONE as "ungrounded". This decision of the Agency was appealed by ONE by filing a lawsuit at the Administrative Court of Macedonia. The potential loss from the claim is approximately HUF 0.5 billion, but the management estimates it unlikely that this would result in any material cash outflows. The final decision will be made by the Administrative Court of Macedonia, the timing of which is uncertain.

36.2.2 Montenegro

36.2.2.1 Employee salary disputes in Montenegro

In July 2010, the Trade Union of Crnogorski Telekom submitted a claim to increase the salaries by 15.3% for the period between September 2009 and September 2010, based on the clause on minimum wage calculation in the Collective Bargaining Agreement (CBA). Management believes that the Trade Union is not entitled to submit such claim and also disagrees to the calculation methodology. There has not been any hearing yet in this case. The potential exposure is HUF 1.8 billion.

36.2.3 Hungary

36.2.3.1 Guarantees

Magyar Telekom Plc. is exposed to risks that arise from the possible drawdown of guarantees for which see more details in Note 35.3.

37 Event after the reporting period

37.1 Deregistration

The Company delisted its ADSs from the New York Stock Exchange effective November 12, 2010. On November 14, 2011 Magyar Telekom filed with the U.S. Securities and Exchange Commission (the "SEC") a Form 15F to terminate registration of its shares and American Depositary Shares ("ADSs") in the US. The deregistration became effective on February 12, 2012, 90 days after the filing of the Form 15F. The Company will maintain its American Depositary Receipt program on a Level I basis. The Company will maintain its primary listing on the Budapest Stock Exchange and will continue to make English translations of its annual reports, financial statements and investor releases.

Management Report of Magyar Telekom for 2011

Introduction

This Business Report covers the analysis of our results as well as all additional information necessary to evaluate our operations, including, among others, our outlook with the accompanying risk factors, the introduction of our management, our HR and risk management policies, and our R+D activities. The Company's activities are described in the Notes General Information section (section 1).

1. The company's share capital, voting rights and transfer of shares

As of December 31, 2011, the share capital of Magyar Telekom Plc. (the "Company" or "Magyar Telekom") was HUF 104,274,254,300, consisting of 1,042,742,543 Series "A" ordinary shares. All Series "A" ordinary shares have a nominal value of HUF 100. Rights and obligations related to Series "A" ordinary shares are described in detail in the Articles of Association Section 4. Information concerning our ownership structure as of December 31, 2011 is described in the following table:

Shareholder	Number of shares	Percentage of share capital
MagyarCom	617,436,759	59.21
Publicly traded	424,914,922	40.75
Treasury stock	390,862	0.04
	1,042,742,543	100.00

1.1. Voting Rights and Voting

Each ordinary share entitles the holder to one vote. Only shareholders or nominees registered in the shareholders' register at least two working days prior to the date of the General Meeting may participate at the General Meeting with voting right. The General Meeting shall adopt its resolutions by a simple majority vote except for resolutions on issues listed in the Articles of Associations, which shall require at least a three-quarters majority of the votes cast. There is no limitation on the rights of non-resident or foreign shareholders to hold or exercise voting rights on the ordinary shares. There is no limitation of voting rights for ordinary shares in the Articles of Association. The Company has no shares assigned with special management rights.

1.2. Transfer of Shares

(a) The acquisition and transfer of the dematerialized share shall only be effected through crediting or debiting the securities account. The owner of the security – unless the contrary is proved – shall be the person on whose account the security is registered. The transfer of registered or Interim Share Certificates shall be effective with respect to the Company when the name of the new owner of the shares has been entered in the Shareholders' Register.

(b) If any request regarding the registration at the registrar is justified by the appropriate documents, the Company shall make a prompt entry into the Shareholders' Register. If the Company establishes that the transfer occurred in violation of the Articles, it shall not register such transfer of shares. The Company shall promptly notify the new owner of its reasoned decision and the new owner shall have the right to request, within thirty (30) days of the rendering of such decision, the competent court to review the decision.

(c) Those shareholders who wish so, shall not be registered in the Shareholders' Register in addition to those who obtained the shares in violation of laws or these Articles regarding the transfer of shares.

(d) The registrar, except in case set forth in Section 2.4. (b) and (c) of the Articles of Association, shall not refuse prompt registry and shall promptly delete such shareholder who wishes so.

(e) If the ownership of the shareholder ceased to exist with the transfer of shares the custodian shall notify the registrar on this fact within two working days upon such event. The registrar, based on the notification, shall promptly incorporate such changes in the Shareholders' Register.

The transfer of any Series "A" ordinary shares is not bound to any restriction or attainment of agreement.

2. Corporate governance report

Magyar Telekom Plc. is a public limited company listed on the Budapest Stock Exchange. In 2004, the Budapest Stock Exchange issued its Corporate Governance Recommendations (the "Recommendations") containing suggestions related to the corporate governance practice of companies listed on the Budapest Stock Exchange, taking account of the most commonly used international principles, of experiences gathered in Hungary, and of the characteristics of the Hungarian market as well as the Companies Act. The Recommendations were updated in 2007 and 2008.

In line with the current regulations, the Board of Directors and the Supervisory Board of Magyar Telekom Plc. approved the Corporate Governance Report of the Company prepared based on the Corporate Governance Recommendations and submitted it to the Annual General Meeting. The report – along with other corporate governance related documents - is posted on the Corporate Governance section of our website:

http://www.telekom.hu/investor_relations/corporate_governance/corporate_governance_documents

The Corporate Governance Declaration on Compliance with the Corporate Governance Recommendations, and in case of specific recommendations the possible deviations and their explanations are included in the report. Points 1, 2, 3, 4 and 5 of the above report include the description and operation of the Board of Directors, the Supervisory Board, the relevant committees and executive management. Point 6 of the report includes a description of our internal controls and risk management procedures, while point 8 of the report describes our disclosure policies and insider trading guidelines.

The General Meeting of the shareholders has the sole right to approve and amend the Articles of Association (section 6.2. (a)) unless otherwise provided by law.

The detailed rules on the competencies and operation of the Board of Directors are detailed in 7.4. of our Articles of Association and in the Rules of Procedure of the Board of Directors, which are also posted on the Corporate Governance section of our website. The rules of competence regarding the capital increase and purchase of treasury shares are detailed in Sections 6.2 (b) and (s) as well as 7.4.1 (l) and (m) of our Articles of Association.

2.1. Board of Directors

Under Hungarian laws, the Board of Directors is responsible for all matters relating to the Company's management and course of business not otherwise reserved for the General Meeting or for other corporate bodies by the Articles of Association or by the Hungarian laws. The Board of Directors is required to report annually to the shareholders at the General Meeting and quarterly to the Supervisory Board on our business administration, state of assets, financial situation and business policy.

Pursuant to our Articles of Association, the Board of Directors consists of a minimum of six and a maximum of eleven members elected by the General Meeting of the shareholders for a term of three years. On December 31, 2011, there were nine members of the Board of Directors.

Meetings of the Board of Directors are held at least four times a year. Meetings of the Board of Directors require the presence of six members for a quorum. Each member has one vote. The Board of Directors passes resolutions by a simple majority vote.

On December 31, 2011, members of the Board of Directors, their principal occupations and the years of their original election were as follows:

Name	Born	Principal Occupation	Member since
Christopher Mattheisen................	1961	Chairman and Chief Executive Officer of Magyar Telekom Plc.	2006
Dr. Ferri Abolhassan	1964	Director Production and Member of the Board of Management, T-Systems Int. GmbH, Deutsche Telekom AG	2010
Dr. István Földesi	1949	International business consultant	2003
Dietmar Frings	1959	Vice President Human Resources Compensation and Benefits and Labor Law, Deutsche Telekom AG	2010
Dr. Mihály Gálik	1946	Professor of the Media, Marketing Communication and Telecommunications Department at the Faculty of Business Administration of the Corvinus University of Budapest	2006
Thilo Kusch	1965	Chief Financial Officer of Magyar Telekom Plc.	2006
Dr. Klaus Nitschke........................	1961	Senior Vice President, Head of the Pay TV activities in Deutsche Telekom AG's European footprint	2010
Frank Odzuck	1959	Chief Executive Officer of Zwack Unicum Plc.	2006
Dr. Ralph Rentschler....................	1960	Finance Europe, Financial Director Europe, Deutsche Telekom AG	2003

2.2. Management Committee

Pursuant to the Rules of Procedures of the Board of Directors, the Board of Directors established a Management Committee in 2000. The Management Committee carries out its activities based on its Rules of Procedures approved by the Board of Directors, which is available on the Company's website.

Members of the Management Committee are elected for an indefinite period.

On December 31, 2011, the Management Committee consisted of nine chief officers of Magyar Telekom. The members and the years of their original election were as follows:

Name	Born	Current position	Member since
Christopher Mattheisen	1961	Chairman and Chief Executive Officer	2006
Attila Keszég	1966	Chief Sales and Services Officer	2010
István Király	1965	Chief Marketing Officer	2010
Thilo Kusch	1965	Chief Financial Officer	2006
István Maradi......................................	1964	Chief Technology and IT Officer	2007
Balázs Máthé......................................	1968	Chief Legal and Corporate Affairs Officer	2010
Róbert Pataki	1971	Chief Strategy and Corporate Development Officer	2009
Róbert Budafoki	1966	Chief Operating Officer, Business Services Business Unit	2010
Éva Somorjai	1966	Chief Human Resources Officer	2007

2.3. Supervisory Board

The Supervisory Board carries out its activities based on Section 8 of the Articles of Association and its Rules of Procedures approved by the General Meeting of the shareholders. The Supervisory Board has to examine every important report on business policy and every submission made on matters falling into the exclusive competence of the General Meeting. The General Meeting may pass resolution on the annual report prepared in accordance with the Act on Accounting and the use of the profit after income tax only upon receipt of the written report of the Supervisory Board, whereas the proposal of the Board of Directors on the payment of dividends and the Company's corporate governance report can only be submitted to the General Meeting with the prior approval of the Supervisory Board.

Pursuant to the Articles of Association, the Supervisory Board consists of a minimum of three and a maximum of fifteen members elected by the General Meeting for a term of three years. The Workers' Council nominates one third of the Supervisory Board members. Meetings of the Supervisory Board have a quorum if two-thirds of the elected members are present.

On December 31, 2011, the members of the Supervisory Board, their principal occupation and the years of their original election were as follows:

Name	Born	Principal Occupation	Member since
Dr. László Pap..............................	1943	Budapest University of Technology, Professor	1997
Dr. János Bitó	1936	Chairman of the Thesis and Final Examination Board at Pázmány Péter Catholic University, Information Technology Faculty	2010
Attila Bujdosó................................	1967	President of the Telecommunications Trade Union	2010
Dr. János Illéssy	1962	Managing Director, Lebona Kft.	2006
Dr. Sándor Kerekes......................	1948	Director of Institute of Environmental Sciences Corvinus University Budapest	2006
Konrad Kreuzer	1948	Chairman of the Board of Directors of E.ON Hungary Zrt.	2006
Tamás Lichnovszky......................	1962	Chairman of the Central Workers' Council	2010
Martin Meffert................................	1960	Country manager for Hungary, Head office of T-Home, Deutsche Telekom AG	2009
Dr. Károly Salamon	1954	Chairman - Chief Executive Officer of MKB General Insurance Zrt. and MKB Life Insurance Zrt.	2010
Zsoltné Varga................................	1969	Quality Manager, Magyar Telekom Plc.	2008
György Varju	1946	Central Workers' Council expert	2005
Dr. Konrad Wetzker..........	1950	Chairman, Corvinus School of Management	2011

The members' mandate lasts until May 31, 2013.

2.4. Audit Committee

The Audit Committee executes its duties pursuant to the Articles of Association Point 8.7, and its own Rules of Procedures. The members of the Audit Committee have been elected from the independent members of the Supervisory Board.

On December 31, 2011, the members of the Audit Committee, their principal occupation and the years of their original election were as follows:

Name	Born	Principal Occupation	Member since
Dr. János Illéssy	1962	Managing Director, Lebona Kft.	2006
Dr. János Bitó	1936	Chairman of the Thesis and Final Examination Board at Pázmány Péter Catholic University, Information Technology Faculty	2010
Dr. Sándor Kerekes......................	1948	Director of Institute of Environmental Sciences Corvinus University Budapest	2006
Dr. László Pap...............................	1943	Budapest University of Technology, Professor	1997
Dr. Károly Salamon	1954	Chairman - Chief Executive Officer of MKB General Insurance Zrt. and MKB Life Insurance Zrt.	2010

2.5. Remuneration Committee

The Remuneration Committee makes proposals to the Board of Directors with respect to appointment and dismissal, as well as remuneration of chief officers, including establishment and assessment of bonus targets. The Remuneration Committee meets at least three times a year.

The Remuneration Committee consists of three members. The members are elected by the Board of Directors from its members.

On December 31, 2011, the members of the Remuneration Committee, their principal occupation and the years of their original election were as follows:

Name	Principal Occupation	Member since
Dr. Ralph Rentschler..........	Finance Europe, Financial Director Europe, Deutsche Telekom AG	2003
Dietmar Frings	Vice President Human Resources Compensation and Benefits and Labor Law, Deutsche Telekom AG	2011
Frank Odzuck	Chief Executive Officer of Zwack Unicum Plc.	2006

3. Human policy

In line with Magyar Telekom's corporate strategy we renewed our HR principles and strategic priorities. In 2011 we prepared for a total paradigm change in terms of all HR related activities. A new Human strategy was elaborated that generates a complete structural change influencing the Company, the employees and the HR team.

1. Human strategy from the Company's aspect

- Efficient company – continuous and proportionate decrease of Total Workforce Management (TWM) cost
- Competitive company – competitive edge based on human capital through training development and career management
- Energized company – international, diverse and healthy organization that experiences success

2. Human strategy from the employees' aspect

People development will be carried through enhancing employee experience that is a major element of our strategy. The stages of Telekom employment cycle were identified in 2011 and we matched appropriate HR tools with each stage in order to develop all of our employees:

- Employer brand building – we create a livable and likeable workplace, which is satisfactory for our employees and attractive on the labor market. We are going to be among the "Top 3 Best Employer" and be among the "Top 5 Most Desired Employer" in Hungary.
- Selection – we create a diverse workplace with maintaining the healthy level of internal succession rate and encouraging atypical staffing. We also plan to increase the ratio of women in management to 30%.
- Agreements – we establish transparent, flexible and reliable frameworks of conditions. We maintain a balanced partnership with employee representative bodies and identical contracts will be concluded with people in identical employment pools.
- Orientation – we make our new colleagues real members of the team by sharing our knowledge, culture and experience with them. Our Orientation program will be renewed in order to have an informative and efficient event for the new employees. We introduce a buddy program to make assimilation into the corporate culture easier.
- Remuneration – We introduce a transparent, simpler and consistent job grading model, which reflects primarily the respective values of jobs, and provides for market comparison, as a basis for a competitive remuneration policy.
- Training development, organizational development – our qualified employees provide us a competitive edge. Following the international best practice we spend two percent of personnel expenditure on training and development. Ten percent of all training will be provided from internal resources.
- Work – life balance – Our energized employees make us successful. We are going to introduce and run a complex stress management that helps preserving mental and physical condition of our employees.
- Fair dismissal – when we dismiss an employee, we do it in a fair manner. We make it clear for employees that retaining one's marketability is one's own responsibility.

Our company's practice is adapted to Hungarian legislative norms. The principles of justice and equal opportunities are set out in the basic standards articulated in our Code of Ethics published in 1997, which complies with the S-OX (Sarbanes-Oxley) act. Alternative forms of employment like telework, part-time work, flex-work, employment of disabled persons provide possibilities for the practical implementation of equal opportunities.

3.1. Headcount

We had 10,111 employees as of December 31, 2011. The following table provides information concerning the number of full-time employees, including full-time equivalents, of Magyar Telekom Plc. and its consolidated subsidiaries:

	At December 31,		
	2009	2010	2011
Magyar Telekom Plc.	6,459	6,076	6,097
Magyar Telekom Plc. and its consolidated subsidiaries	10,828	10,258	10,111

The following table provides information on the breakdown of Magyar Telekom's employees by segment:

	At December 31,		
	2009	2010	2011
Hungary	6,152	6,084	6,124
T-Systems	1,709	1,662	1,594
Macedonia	1,754	1,698	1,668
Montenegro	876	814	725
All other	337	0	0
Total	10,828	10,258	10,111

3.2. Total Workforce Management

From 2009, Magyar Telekom introduced a Total Workforce Management ("TWM") system. This scheme focuses on the total labor cost and not solely on headcount number and employee-related expenses. As a result, it enables us to increase the flexibility and efficiency with which all human resource-related expenses are managed, including contracted or temporary employees as well as outsourcing and entrepreneurial contracts.

3.3. Workforce Reduction and Redeployment

Centralization, technological improvements and attrition have allowed us to reduce the size of our workforce. While overall personnel levels are falling (disregarding the technical effects of acquisitions and Total Workforce Management), the number of highly skilled employees is increasing. We plan to further reduce the number of our employees.

In order to simplify and streamline its organization, Magyar Telekom has already implemented several integration steps. The merger with T-Mobile Hungary in March 2006, the integration of Emitel and the access business area of T-Online into the parent company from October 2007 and the integration of T-Kábel from October 2009 enabled the management to eliminate overlaps and simplify the processes and the operational structure of the Group. The decision on the change in the organizational model was a further step to ensure a more customer-focused approach and a lean management structure. With the aim to further improve efficiency and reduce headcount, management started negotiations with the trade unions and reached an agreement in October 2011.

According to the terms of the agreement, the Company plans to make 250 employees redundant in 2012. The majority have left the Company by the end of 2011. This figure does not include – among others – the employment termination of executives and employees retiring. In addition, to achieve further efficiency improvements, the organization will be simplified and the number of directors will be cut by 24%. Total severance expenses related to the headcount reduction will be approximately HUF 2.6 bn and the majority of these were accounted for in the fourth quarter of 2011. Furthermore due to change of the structure of the remuneration system HUF 1.0 bn was accounted.

The agreement with the trade unions also states there will be no general increase in the base salary for employees in 2012. However, to meet the Government's expectation to compensate employees with below average wages for adverse tax law changes, benefits in kind will be increased for effected employees. These additional employee benefits will be cut at managerial positions.

These efficiency improvement measures are necessary steps to mitigate the negative trends in the telecommunications industry being faced by Magyar Telekom. Increasing competition in all segments and a tougher regulatory (roaming regulation and reducing termination fees) and macroeconomic environment will put pressure on our performance in coming years.

3.4. Employee Representation and Labor Relations

Magyar Telekom Plc. has entered into a collective bargaining agreement with the Hungarian telecommunications trade unions (Távközlési Szakszervezet, "TÁVSZAK" and Magyar Távközlési Ágazati Szakszevezet, "MATÁSZ"). The agreement, which can be terminated by either party with three months' notice, applies to all Magyar Telekom Plc. employees except the CEO, regardless of their union membership status. Wage terms in the agreement must be renegotiated annually. Under the agreement, employees are generally entitled to prior notice before termination. Furthermore, employees are entitled to a specific amount of severance pay, which depends on the tenure of the employee. Employees are also entitled to welfare benefits as discussed below.

In addition to the collective bargaining agreement, employees of our Hungarian operations are generally covered by the Hungarian Labor Code, Law XXII of 1992, as amended, which imposes various restrictions on the involuntary termination of employment. The Hungarian Labor Code protects employee interests through two different labor organizations: the Trade Union and the Workers' Council.

The Trade Union, as the official representative of employee interests in negotiations relating to the terms of employment, has the right to be informed of all corporate measures that may significantly affect the interests of employees and to commence legal action against us for employment-related conduct that infringes an employment rule. In addition, the Workers' Council directly represents employee interests in dealings with management and decides jointly with management on matters involving employee welfare funds and institutions. The Workers' Council must be informed semi-annually on issues affecting our economic performance and changes in wages, employment conditions and working hours. The Workers' Council must also be consulted on corporate measures affecting employees.

Under the Act IV of 2006 on Business Associations (the "Companies Act"), employee representatives on the Supervisory Board are nominated by the Workers' Council in cooperation with the Trade Union. The composition of the Supervisory Board is approved by the AGM. At least one third of the members of the Supervisory Board must be employee representatives. On December 31, 2011, three members of the Supervisory Board were employee representatives. These members were Tamás Lichnovszky, Zsoltné Varga and György Varju.

We believe that our relations with our employees are good. We have not experienced any labor strikes or disruptions since our formation.

3.5. Pensions and Benefit Programs

Magyar Telekom's welfare and social benefits constitute an exceedingly wide-ranging pool. A part of them is granted to every employee, while others are available on certain conditions or are of an insurance nature, the basis of which is the employees' collective contribution. The way social benefits and discretionary benefits are granted is set out in the Collective Agreement and related regulations.

We provide employees with discounted telephone services, subsidized meals, interest-free loans to purchase real estate (such loans are not offered or extended to the Company's executive officers and directors), discount holiday facilities and other fringe benefits. In addition to our statutory contributions to governmental health, retirement and unemployment schemes, we contribute to the employees' voluntary pension fund and supplementary benefits fund, which provide private pension and health insurance benefits supplementing government pension and health benefits. We do not, however, guarantee payment by the benefits fund to its members. At the end of 2011, approximately 79% of all employees participated in the pension plan, 53% in the self-help plans and 80% in the health fund.

4. Compensation of Directors, Officers and Employees

At December 31, 2011, the aggregate compensation of the members of the Board of Directors in their capacity as Board members was HUF 14.0 million.

At December 31, 2011, the aggregate compensation of the members of the Supervisory Board in their capacity as Supervisory Board members was HUF 55.5 million.

At December 31, 2011, the aggregate compensation of the members of the Management Committee ("MC") was HUF 1,064 million.

Currently two of the MC members have an employment contract for a fixed duration. Pursuant to Hungarian legislation, if an employment contract is terminated before the end of its term, the average compensation received by the employee prior to such termination is payable for the remaining period up to 12 months. In case an employment contract for an undetermined duration is terminated, the notice period is normally six months, and severance is between 10 and 16 months.

In addition to the above, the affected persons are bound by the non-compete clause, under which the employee is barred from entering into employment with any Hungarian or international competitor of Magyar Telekom and is required to refrain from providing direct or indirect services or activities of any kind to such companies for a definite period (not longer than one year) upon termination of his/her employment. Furthermore, such employee is barred from any action aimed to recruit employees of Magyar Telekom for any other company. This limitation entails certain compensation which is proportional with the above obligation. If the employee is in breach of the agreement, he/she will reimburse the net amount of compensation to the employer. In addition, the employee will be liable for a payment of compensation to the employer.

The MC members from foreign countries may be entitled to housing subsidies.

In line with the Company's remuneration guidelines, the Company provides contribution-based personal pension scheme and personal insurance scheme on behalf of the MC members. In addition, the MC members are entitled to the use of company cars.

For information about our Mid-term Incentive Plan ("MTIP"), see Note 24.1 to the consolidated financial statements. For information about the Matching Share Plan, see Note 24.4 to the consolidated financial statements. For further information about the compensation of key management and Deutsche Telekom's Stock Option Plan, see Note 34.4 to the consolidated financial statements.

5. Research and development

In 2011 Magyar Telekom continued to strengthen the alignment of its innovation processes with the corporate strategy under the governance of the Innovation and Corporate Development Directorate. The cross-functional R&D Committee devised the R&D priorities based on the Group Strategy. The R&D Committee assesses and approves the research topics proposed by the business units according to this priority set.

The R&D Committee convenes regularly in order to discuss and decide on the approval of individual R&D proposals, initiated and executed within a project framework by the respective business units. During 2011, the Committee reviewed more than 100 proposals, out of which 55 have been approved, accounting for a total investment of HUF 512 million (including HUF 470 million reflected as operating expenses and HUF 42 million reflected as employee-related expenses).

The Company leverages the synergy effect of external and internal knowledge base by collaborating to well known innovation centers both within Hungary and abroad. Our main partners are the well known Hungarian Universities (Budapest University of Technology and Economics, Corvinus University of Budapest, University of Szeged) and the Hungarian Academy of Sciences.

Magyar Telekom has also participated in several international R&D projects, for example:

- the NAPA-WINE project, which started in 2008 and finished in 2011, supported by the European Union (FP7: Seventh Framework Program) together with established universities (e.g., Politecnico di Torino, Budapest University of Technology and Economics) and other significant telecommunications companies (e.g. France Telecom, Telekom Polska).
- The Optical Access Seamless Evolution which started in 2010 and will end in 2012 as a collaboration between major telecommunication operators, technology providers and universities from Europe supported also by the European Union (FP7: Seventh Framework Program).

6. Real estate, sites of operation

We have one of the largest real estate holdings in Hungary and we are also a major real estate owner in Macedonia and Montenegro. We use substantially all of these properties for telecommunications installations, offices, warehouses, garages and shops. Our equipment and machinery primarily consist of switches, communication towers and other telecommunications equipment.

- The registered office of the Company:
  1013 Budapest, Krisztina krt. 55.

- Sites of the Company:
  1117 Budapest, Gábor Dénes u. 2.
  1107 Budapest, Bihari u.6.
  1117 Budapest, Magyar tudósok krt.9.
  1073 Budapest, Dob u. 76-78.
  1051 Budapest, Petőfi Sándor u. 17-19.
  1117 Budapest, Kaposvár u. 5-7
  1117 Budapest, Budafoki u. 103-107
  1107 Budapest, Száva u. 3-5.
  1077 Budapest, Kéthly Anna tér 1.
  1117 Budapest, Szerémi út 4.

- Branch Offices of the Company:
  4026 Debrecen, Bethlen u. 1.
  3525 Miskolc, Régiposta u. 9.
  9400 Sopron, Széchenyi tér 7-10.
  7601 Pécs, Rákóczi út 19.
  8174 Balatonkenese, Parti sétány 51.
  6722 Szeged, Tisza Lajos krt. 41.
  5600 Békéscsaba, Andrássy u. 44.
  6723 Szeged, Etelka sor 1.
  6721 Szeged, Csongrádi sgt. 12.

The number of sites used by Magyar Telekom Plc. is approximately 2,500, out of which approximately 22% are owned by the Company, 40% jointly owned and 38% leased. These figures include the sites used for telecommunications towers and antennas, but do not include the number of base stations. We have 3,522 base stations, of which five percent is owned by Magyar Telekom Plc. and 95% is leased from other telecommunications operators or other third parties.

The total area of properties used by Magyar Telekom Plc. as of December 31, 2011 was 576,154 m^2. The majority of sites used in our operations are smaller than 100 m^2. The largest site is our headquarters building located at Krisztina krt. 55 in Budapest, with floor space of over 30,000 m^2. In order to increase the utilization of real estates and increase efficiency, we sell or rent our surplus properties.

7. Environment protection, sustainability

7.1. Sustainability strategy

7.1.1 Sustainability strategy 2008-2010

The Company's 3-year sustainability strategy was closed last year. The key strategic objective of 2008-2010 was: 'While maintaining its position, Magyar Telekom's leading sustainability role should become clear and visible for employees and customers'. This was implemented alongside the following key challenges:

- Corporate governance and risk management: Magyar Telekom strives to maintain transparent and accountable operations, while ensuring compliance, anti-corruption and efficient risk management. Its goals include, for example, the development of our compliance system, as well as the improvement of environmental and social performance of our suppliers.
- Customer relations: The Company aims to increase awareness among its customers about its efforts made in order to promote sustainable development. The relevant set of objectives include, among others, popularizing electronic product and service order placement solutions, an increasing quality of service provision to customers, as well as familiarizing customers with the Group's sustainability initiatives.

- Strengthening the communication means available to society: It is important for Magyar Telekom that in addition to following technological development trends, the benefits offered by ICT solutions would be available for everyone. The Group's objectives include the continuance and development of its programs aimed at eliminating the digital divide, the provision of ICT services of special relevance in the context of sustainability, as well as the communication of the sustainability impacts of our products and strengthening our customers' sense of responsibility.
- Decreasing the environmental footprint: Telecommunication products and services - while enabling raw material and energy savings - also burden the environment. The Company's aim is to further decrease this burden. The key task is fighting climate change: the Company has set the target of decreasing its CO2 emission by 10% by 2011. Magyar Telekom also wishes to help customers to decrease their emissions, while it supports them in adapting to the climate change.
- Human resources management: "Committed, professionals ready to take the initiative are the key success factor to Magyar Telekom Group's business effectiveness." (Magyar Telekom's HR Vision). In this spirit, the Company strives to further develop its human capital, attract and retain talent, as well as ensure equal opportunities and promote the establishment of work-life balance.
- Maintaining trust and credibility: In order to maintain social trust, every company must conduct its business transparently and upon consideration of all stakeholders' expectations. In light of this concept, Magyar Telekom's goal, among others, is to further strengthen the protection of children from adult content, as well as to join and to start major sustainability initiatives.

We determined 34 tasks as part of the strategy, which we further broke down to sub-tasks. Overall, the tasks were implemented with 94% success rate.

We measure our sustainability position by the Dow Jones Sustainability Index (DJSI) and by various prizes, while the visibility of our leading role is measured by residential and employee surveys. These help establish the following:

- In the professional evaluation, on the basis of the DJSI (in 2010, 72 points) we earned a position in the top third league worldwide and also topped this position with several awards. Besides, in the CSR 24/7 rating we took the first place in 2009 both in Hungary and in Central Europe. In 2010 we maintained our first place in Hungary, but OMV from Austria was better than us in the region. It is also a warning sign that, although we do not know their points, another Hungarian company has also made it to the DJSI.
- Awards in 2011: Green HR Award, CSR 24/7 Rating 1st place, "Business World for the Environment" (HBLF) 2nd place, Employee Volunteering Award, CEERIUS sustainability index membership
- The awards we won during the term of the strategy are available on the following website: http://www.telekom.hu/society_and_environment/prizes_ratings
- In the residential survey 6-7% of the respondents name Magyar Telekom and its offered brands as leading sustainability company and products, but 90% of the respondents cannot specifically name any company. In the employee survey 18% name the Company as leading player, but 60% cannot name any company at all. In view of this, we do not consider this part of the main objective implemented.

7.1.2 Trends influencing the new sustainability strategy, adopted in 2011

- Professional evaluation of the previous strategic period
- The European Union's 'Europe 2020' strategy
- The EU's 3x20 climate package that lasts until 2020
- EU recommendation for the ICT sector: 20% CO2 reduction by 2015
- Corporate trends, e.g. Climate Groups' 30 percent initiative
- Deutsche Telekom sustainability requirements
- Responsible investments and increase of their value
- Changing customer requirements

7.1.3 Sustainability strategy 2011-2015

Our new Sustainability Strategy, encompassing five years (2011- 2015), has been harmonized with the strategies of other corporate divisions. The main objective of the strategy is to make sustainability part of Magyar Telekom's identity, thus providing a competitive edge to the Company in the long run.

We wish to achieve this objective on the basis of our performance demonstrated so far, the responsible investment ratings and the principles followed during the last three years, with a more intensive communication of our commitment to our stakeholders, new and ambitious goals, adopting best practices, as well as forceful and targeted communication.

The strategy will be implemented through the tasks of 22 topics, along the following key priorities:

- Brand management: our goal is to raise awareness to the concept of sustainability and to enhance the sustainability perception of Magyar Telekom
- Innovation management: our goal is to increase innovations aimed at society and environment
- Climate strategy: our goal is to reduce the CO2 emission of the group by 20% by 2015 (base year: 2004)
- Supplier standards: our goal is to develop a regulated sustainable supplier chain process
- Effects of telecommunication services: our goal is to increase the ratio of sustainable products and services, and to keep our customers informed

Magyar Telekom Group as the leading info-communication service provider of the region - in harmony with its Mission - is committed to the idea of sustainable development and within it to the environmental issues. The Company, realizing its role and potential in the information society, contributes to the decrease of negative environmental impacts in Hungary by performing our activities in a regulated and controlled way, fulfilling the EU requirements and complying with the international standards. The Magyar Telekom Group's environmental commitment and taken responsibilities are published in the Magyar Telekom Group Environmental Policy (http://www.telekom.hu/static/sw/download/Magyar_Telekom_environmental_policy.pdf), which contains obligations for the group-members individually and for the Group all together.

7.2. Climate protection

- In 2011 Magyar Telekom purchased 34 GWh renewable energy from E.ON, as part of its total energy consumption. In the new 5-year strategy, the goal in order to achieve the defined KPI is 46 GWh of green energy.
- In 2011, two 100% electric cars were purchased; they have been in operation since January 2012 in Magyar Telekom's fleet. One of the vehicles supports the mechanics of the Technical Services Directorate in their work, while the other one is available to the employees of Telekom, as a so-called key car. One of the important benefits of electronic cars is that no hazardous substances are emitted during their operation (0 g/km emission), and their fuel consumption is also low (electric energy equal to 1 – 1.5 liters of gas for 100 kilometers).
- Besides a five percent reduction of fuel consumption, the Sustainability Strategy for the 2011-2015 period defines two basic objectives: by the end of 2015, the average CO2 emission of the vehicles must not exceed 157.7 g/km, and the ratio of hybrid and electronic cars among all vehicles of personal use should be increased to 20 %. In order to promote the achievement of the above objectives, Magyar Telekom issued a regulation and subsidizes the procurement of hybrid benefit cars by a special allocated budget and has elaborated a system of incentives (bonus-malus) aimed at encouraging people to opt for low-CO2 cars.
- In order to achieve its climate protection objectives, Magyar Telekom has launched a research and development project on its base station located in Iszkahegy, based on the utilization of wind and solar energy. During the project a wind-wheel with vertical axis will be mounted on the tower (planned implementation by the end of March 2012), and a solar cell following the sun was installed on the roof of the container near the tower. An additional goal is to continuously monitor the green power generation results and to analyze the possibility of expansion.

7.3. Voluntary programs

In 2011, the European Year of Volunteering we increased the social sensitivity of our employees by organizing voluntary programs. Similarly to previous years, the Jövő/Menő program offered voluntary work opportunities for those interested. The objective of the program is to ensure sustainable development for the handicapped small regions (the first location is the Mezőcsát small region). The objective of the Digital Bridge in Small Settlements program is to introduce and disseminate the achievements and opportunities of information and communications technology in regions where digital divide is present. Furthermore, as of 2011 we have encouraged the spreading of corporate volunteering by organizing charity team buildings. During the year 389 of our colleagues did 480 working days (3840 working hours) of voluntary work, within the frame of which we granted to the society 19.9 million HUF of theoretical voluntary contribution.

7.4. Initiatives concerning stakeholders

- The stakeholders of the Magyar Telekom Group include all those groups, which have an influence on, or hold an interest in the implementation of the objectives of the Company. The Company earlier identified its stakeholders through review of its management systems and making benchmark studies, and keeps continuous contact with them to ensure that their interests are taken into consideration in the course of its operations. Our most important stakeholders are regulators, investors, customers, employees, communities, NGOs, suppliers and partners, as well as the future generations.
- In 2011 we organized the Sustainability Roundtable Discussion for the twelfth time, the objective of which is to have an open dialogue for the sake of understanding the demands towards Magyar Telekom Group, discussing the arising problems, and to provide a suitable background for thinking together and co-operating in building a sustainable future.
- In 2008 our Company founded the DELFIN award, which in Hungarian stands for Award for a Committed, Sustainable, Innovative Generation. With the DELFIN award Magyar Telekom wants to promote the idea of a sustainable development and recognize efforts made towards this goal. The award is given to suppliers offering outstanding performance in the field of sustainability, in four categories: Support of equal opportunity and promotion of non-discrimination inside and outside the Company; Innovation realized in the interest of sustainability; Sustainability education and awareness raising; Investment and development related to climate protection. The award is given on the basis of applications judged by a board of professionals. The fourth award ceremony was held on June 24, 2011, in the Sustainability Roundtable.
- The objective of Magyar Telekom's Digital Bridge in Small Settlements program is to introduce the achievements and opportunities of information and communications technology in regions where digital divide is present and may deepen to a ravine over time. In 2011 we arranged 8 Digital Bridge events, including 2 Digital Bridge Fests (event including a talent seeking contest), and the program was also arranged this year in the Valley of Arts, Kapolcs. Until the end of 2011 we organized a total of 159 events. The events in 2011 were visited by about 1000 spectators, and their orientation on the worldwide web was helped by 300 Magyar Telekom employees in total.
- The Egalnet program was launched in 2006. This is an initiative offering support to organizations dealing with handicapped groups to create their own websites in a simple and cost-free way. In addition, the program provides the opportunity for the organizations to maintain relations among each other and to share their experiences, which may significantly improve the efficiency of their operation. Until the end of 2011 73 organizations have joined to the program.
- The Company further developed its vendor prequalification system, which now ensures registered suppliers to complete the sustainability-focused questionnaire, and also its evaluation. The results ensure the identification of risks and the possibility of joint improvement with the suppliers. In order to develop a sustainable supplier chain, Magyar Telekom continues to treat the regular evaluation of its top suppliers as priority with the help of the detailed supplier self-evaluation questionnaire developed by Global e-Sustainability Initiative ("GeSI"), which, in addition to environmental queries, also contains questions concerning compliance with human rights, occupational health, security and business ethics requirements. So far 38 supplier evaluations have been completed. We ensure compliance with the statutory and corporate expectations by including sustainability clauses in the supplier contracts.
- Since 2008 Magyar Telekom has joined to the world's largest voluntary environmental campaign, the Earth Hour. In 2011, within the frame of the 'hello holnap!' (meaning 'hello tomorrow') movement, Magyar Telekom joined to the international movement with an event of its own. In the evening, the company's large flashers, the lights in its T-Pont shops and office buildings went off for an hour and, during the day certain environmentally friendly products were available at a 50% discount. From 7 p.m. various programs and concerts were offered to the audience in Budapest, in the Millenáris Park to increase their awareness of sustainability and climate protection.
- At the initiative of Magyar Telekom, a Sustainability Media Club has been set up in the framework of the 'hello holnap!' movement, with the participation of leading Hungarian printed, electronic and online media groups. The purpose of the Club is to help familiarize with the concept of sustainability, its practical implications and everyday examples by an increasingly broader audience in Hungary. In every quarter of the year civil organizations ("NGO"s) may apply for support of their own sustainability projects in the topic of definition, importance and goals of sustainable development. Winning applications are selected by the members of the Media Club within the frame of a personal meeting, whereas the implementation is financed by Magyar Telekom. In 2011 the Media Club also established a Sustainability Press Prize to recognize journalists, editors and broadcasters who have contributed most to communicating the topic in the given period of time. The one million HUF prize granted by Magyar Telekom is handed over once a year. The first winner was announced in September 2011 on the 4th Sustainability Day.

- On September 24th 2011, the 4th Sustainability Day was organized with the participation of more than 1700 young people, who got closer to understanding the concept of sustainability. Professional talks were built on the three pillars of sustainability – society, economy and environmental protection – to which volunteering was added as a reference to the European Year of Volunteering 2011. In the discussions about poverty, the participants evaluated the possibilities of integration and recovery. In relation to the topic of water – in addition to the Danube Strategy – the participants – including the ombudsman of future generations, as well as other renowned specialists - discussed the impact of the climate change on the water reserves. The role of the 'hello holnap!' Press Prize was also brought up in the section discussion about press communication, where the participants brought the attention to various advertising tricks and pseudo-Hungarian products. Besides the professional discussions, visitors had the chance to test drive alternative vehicles, to taste fair trade coffee and tea, to watch creative objects made of waste and even to participate in a flashmob. During the intermissions of section talks, participants of the festival conference had the chance to have a look on works made for the 4th Sustainability day.

7.5. Annual Sustainability Report

One of Magyar Telekom Group's commitments is that it annually publishes a report about its sustainability performance. Reports are prepared in accordance with the GRI G3 principles of Global Reporting Initiative (GRI) published in 2006, thus meeting the expectation that the reports comply with the principles of transparency and international comparability. Each year since 2007 Magyar Telekom achieved the highest compliance in accordance with the international principles, so its Sustainability report for the year 2010 continued to apply the principles on A+ level for the fourth time already. In 2011 independent assurance report with the GRI criteria was completed and certified by PricewaterhouseCoopers in accordance with ISAE 3000 international standard. Further details on the sustainability performance of the company can be found in the annual reports available on the site: http://www.telekom.hu/society_and_environment/sustainability_reports.

8. Economic environment

The telecommunications industry is undergoing a major change globally. Worldwide trends are driving towards an integrated telecommunications, information, media and entertainment market. These trends together with local specifics create new set-up in our eco-system both in terms of infrastructure, servicing and new types of business models.

Market delivers moderate growth with strong restructuring between segments that puts pressure on margin levels. We expect that the traditional telecommunications market will no longer deliver sizeable revenue growth in Hungary. The fixed voice market as a major revenue and profit source is declining; mobile is no longer able to compensate this decline. However, we expect that new core segments, especially mobile broadband, broadcasting and IT services will deliver sizable revenue growth in the coming years. The fixed market is characterized by 3Play bundles, with TV being a core element of service offerings, while the mobile market is driven by fierce competition in broadband and content services. An increasing technology platform-based competition can be observed in the domestic market, where our competitors are extensively deploying next-generation countrywide fixed and mobile networks. The battle for customer contact has pushed prices down. We expect continued consolidation in the fixed arena, especially in the cable market. In mobile, new entrants are expected as virtual network operators (MVNOs), but also, based on the first instance decision of the National Media and Infocommunications Authority in the spectrum auction process, a new infrastructure player, the consortium of Magyar Posta, MFB and Magyar Villamos Művek, is also very likely to enter the market.

Latest macroeconomic forecasts lag significantly behind previous assumptions, especially in terms of consumer consumption and public spending. Market development is challenged by significant uncertainties in macroeconomic outlook putting further pressure on market players.

The introduction of the tax reform resulted in a rather unfavorable investment climate. The weakness of domestic demand entails negative changes in the economic structure and a decline in services. Decrease in corporate tax rate has not yet generated an increase in either consumption or investments. The new flat personal income tax rate system increased savings at higher income categories. The crisis taxes are impacting telecom operators' financial stability and investment intensity having a negative effect on overall telecom market growth. GDP is expected to reach the pre-crisis level only after 2014.

9. The Company's targets and strategy

9.1. Outlook

We have observed several long-term trends in the telecommunications industry which are changing the structure of the Hungarian telecommunications market. These long-term trends include changes in technology (i.e., IP-based broadband products and solutions, emerging wireless broadband technologies), customer requirements (i.e., increase in mobile usability of content services and terminal devices, 4Play solutions and the growing need for customized content) and competition and regulation (i.e., low entry barriers, new business models, convergence in the telecommunications and media broadcast industry).

To adapt to these changes in the market, we have redefined the focus areas of our corporate strategies to better exploit our position as an integrated telecommunications operator with a full range of services, as well as to ensure our long-term competitiveness. Our strategies are designed to enable us to exploit and develop our extended customer base, significantly improve efficiency and capture growth opportunities.

Magyar Telekom's current plans and outlook are based on our best knowledge and expected circumstances. Nevertheless, we cannot predict the behavior of our competitors. Therefore, a stronger than assumed impact of alternative operators, new market entrants and new solutions in any country where we are present could result in a negative impact on our business performance.

Each of our business segments is affected by its unique business environment, and we are subject to circumstances and events that are unforeseen or beyond our control. The European economy has slowed down and shows signs of recession risk in 2012. Major uncertainties surrounding the future of the euro, the debt crisis escalated for several euro-zone members. The Hungarian economy impacted heavily by the second wave of the financial crisis. GDP projections for 2012 were reduced significantly, analyst and government forecasts indicate GDP growth about half percent in 2012. The unemployment rate remains very high, above ten percent, and the volatility of the Hungarian currency is expected to continue. The government experienced difficulties to finance the Hungarian budget deficit from the financial markets at the end of 2011. As a result, negotiations were reopened with international financial institutions, such as the International Monetary Fund ("IMF") and the European Central Bank ("ECB") to receive precautionary loan facilities.

In order to balance the government budget, the government implemented several measures to decrease the deficit to 2,5 percent of GDP in 2012. The most significant of these was the 2 ppt VAT increase, from 25% to 27%. The special telecommunications tax, which came into effect in 2010, expected to have a negative impact of more than HUF 24 billion on our EBITDA in 2012. Our T-Systems segment was also affected by heavy spending cuts by the government, our largest business customer. Despite these measures and a negative business environment, we expect that our core business units will be able to continue to generate strong cash flows from the operations, although the special telecommunications tax will impact our dividend policy.

We have identified several risk factors which may affect our business in the future including changes in the regulatory environment, in competition, and in foreign exchange rates. See the detailed description of these and other risk factors in Section 10.2 Risk factors.

9.2. Revenue and EBITDA targets

In 2011 our revenues and underlying EBITDA decreased more moderately than our previous estimates of a 3-5 percent and 4-6 percent, respectively. The revenue decline was 2.0 percent and underlying EBITDA was down by 1.3 percent, primarily due to our strong focus on cost efficiency. We also over performed our capex plans of a 5 percent decrease and reached a saving of 8.7 percent. Our free cash flow (defined as operating cash flow and investing cash flow adjusted for proceeds from / payments for other financial assets) was HUF 92.0 billion and improved by HUF 14.5 billion in 2011 compared to the previous year.

For this year, however, expectations for a deteriorating economic environment, recession and declines in disposable income are strengthening. In addition, while our initiatives for finding new revenue sources are showing results and we expect to stabilise revenues, these new revenues have lower profitability and will dilute our profit margins. Therefore, while we foresee revenues to only decline by up to 2%, underlying EBITDA is expected to deteriorate by 4-6% in 2012. CAPEX spending is expected to remain on the same level as in 2011 to support our internal efficiency projects and the ongoing network modernization.

9.3. Strategy

As a result of our focused strategic efforts, Magyar Telekom has maintained leading positions in its Hungarian fixed line, mobile, Internet and ICT businesses in 2011. We successfully improved customer retention and delivered strong volume figures. Also, we gradually extended our network and offering capabilities proactively leveraging various partnering models as well. We continue our transformation to become the most highly regarded service company in an extended market of telecommunications and related industries.

Even with foreseen macroeconomic and market challenges we believe our corporate strategy –FIX, TRANSFORM, INNOVATE– will deliver turnaround in financials and continued stable cash generation in the long run. Our strategy enables us to exploit and develop our extended customer base, significantly improve efficiency and capture growth opportunities. The strategic objective in the short/mid-term is to fix critical factors within the core business (simplified and focused lean operation, lower cost structure, end-to-end responsibilities) and to further strengthen our positions in core connectivity segments (voice, broadband, interactive TV), while conscious revenue restructuring efforts secure sustainable revenue mix. Innovation clearly supports monetization of our customer contacts and new services. Growth in our new core segments, such as mobile broadband, broadcasting and IT services, is expected to gradually compensate for lower revenues from traditional telecommunications, while non-core areas, such as energy, e-health, finance and insurance services, support customer retention and new revenue streams.

10. The Company's risks and related uncertainties

10.1. Risk management policies

It is our policy that all disclosures made by us to our security holders and the investment community be accurate and complete, and fairly present our financial condition and results of operations in all material respects. Such disclosures should be made on a timely basis as required by applicable laws, rules and regulations, including by-laws of the Budapest Stock Exchange and rules adopted by the U.S. Securities and Exchange Commission ("SEC"). To achieve these objectives, we formed the Disclosure Committee and developed and have continuously enhanced our risk management policies.

Our risk management includes identification, assessment and evaluation of risks, development of necessary action plans, and monitoring of performance and results. For risk management to be effective, we must ensure that management make business decisions with full understanding of all relevant risks.

In 1999, we established a formal risk management system. This system was integrated into the risk management system of Deutsche Telekom in 2002.

All risks related to material internal and external operations, financial and legal compliance and certain other risks are evaluated and managed by a well-defined internal mechanism. A risk management handbook and internal regulation on risk management were published. A risk management course was developed for employees responsible for risk management in all organizational areas. Risk items affecting our operations are reviewed quarterly throughout the Group. All of our subsidiaries, business units, divisions and entities are obliged to identify and report their operational risks on a quarterly basis. After evaluation of these risks, results are reported to our management, to the Board of Directors, to the Audit Committee, to the Disclosure Committee and to Deutsche Telekom.

As part of the integration into DT's risk management process, we enhanced our risk management procedures with a new element. For the sake of prompt disclosure of all risk items influencing investors' decisions, we complemented our quarterly risk reporting system with a continuous reporting procedure which requires all of our departments and subsidiaries to report on a real-time basis any new material fact, information or risk that comes to their knowledge. Information thus submitted is monitored and evaluated by the risk management area and CFO is notified when a new material risk or information is identified.

An internal regulation has been issued to define responsibilities of each employee in risk monitoring and management. In addition, an e-learning course was introduced to train our employees on requirements of the Sarbanes-Oxley Act, our enhanced reporting and corporate governance obligations and the enhanced risk reporting procedures. Completion of this course has been made compulsory for all of our employees.

We established the Disclosure Committee on July 31, 2003. The Disclosure Committee acts both in plenary meetings and through its members acting individually. It supports CEO and CFO in fulfilling their responsibility to oversee processes designed to ensure accuracy and timeliness of our disclosures.

10.2. Risk factors

Our financial condition or results of operations, or the trading prices of our securities, could be materially adversely affected by any of these risks. The risks described below are not the only risks we face. Additional risks not currently known to us or risks that we currently regard as immaterial also could have a material adverse effect on our financial condition or results of operations or the trading prices of our securities.

- Our operations (both in Hungary and abroad) are subject to substantial government regulation, which can result in adverse consequences for our business and results of operations;
- We are subject to more intense competition due to the liberalization of the telecommunications sector;
- We may be unable to adapt to technological changes in the telecommunications market;
- The future of our current operational model is subject to currently unforeseeable changes in the future business environment;
- Developments in the technology and telecommunications sectors have resulted and may result in impairments in the carrying value of certain of our assets;
- We depend on a limited number of suppliers for equipment and maintenance services;
- Our business may be adversely affected by actual or perceived health risks associated with mobile communications technologies;
- System failures could result in reduced user traffic and revenue and could harm our reputation;
- Loss of key personnel could weaken our business;
- Our share price may be volatile, and your ability to sell our shares may be adversely affected due to the relatively illiquid market for our shares and ADSs;
- Fluctuations in the currency exchange rate could have an adverse effect on our results of operations;
- We are continuously involved in disputes and litigation with regulators, competitors and other parties. The ultimate outcome of such legal proceedings is generally uncertain. The results of those procedures may have a material adverse effect on our results of operations and financial condition;
- The value of our investments, results of operations and financial condition could be adversely affected by economic developments in Hungary and other countries;
- We are subject to unpredictable changes in Hungarian tax regulations.

10.3. Financial risk management

Magyar Telekom is primarily exposed to credit risks related to its financial assets. In addition, the Group is also exposed to risks from movements in exchange rates, interest rates that affect the fair value and/or the cash flows arising from financial assets and liabilities.

Financial risk management aims to limit these risks through ongoing operational and finance activities. Selected derivative and non-derivative hedging instruments are used for this purpose, depending on the risk assessment. Magyar Telekom only hedges the risks that affect the Group's cash flow, no hedges are concluded to hedge fair values. Derivatives are exclusively used as hedging instruments, i.e., not for trading or other speculative purposes. To reduce the counterparty risk, hedging transactions are generally only concluded with Deutsche Telekom or leading Hungarian financial institutions.

The detailed descriptions of risks, and their mitigation are provided below.

10.3.1 Market risk

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises three types of risk: currency risk, interest rate risk and other price risk.

The fundamentals of Magyar Telekom's financing strategy are established each year by the Board of Directors. The Group's policy is to borrow centrally using a balanced combination of medium term and short term loans, and fixed and floating interest rates on those loans. The Board of Directors has approved two debt protection ratio limits, and monitors their fulfillment annually. At the end of 2010 and 2011 Magyar Telekom fulfilled both criteria. The Group's Treasury department is responsible for implementing the finance policy and for ongoing risk management. The details of foreign exchange, liquidity and counterparty risk management guidelines are determined and monitored by the Group Treasurer continuously.

Magyar Telekom is exposed to interest and foreign exchange rate ("FX") risk associated with its interest bearing assets and liabilities and anticipated transactions. As the vast majority of the revenues and expenses of the Hungarian entities arise in HUF, the functional currency of Magyar Telekom is HUF. Consequently, Magyar Telekom's objective is to minimize the level of its financial risk in HUF terms.

(a) Foreign currency risk

Due to the free-float of the HUF introduced in 2008, the Group is exposed to FX risk in case of FX denominated financial instruments of the Hungarian entities to a higher degree than before. In order to mitigate this risk, Magyar Telekom minimized its foreign currency borrowings in the past years, or covered it with derivative instruments to completely eliminate FX risk.

The FX exposure of Magyar Telekom is mostly related to

(i) FX risks arising on loans from DTIF and related swaps with DT AG;
(ii) FX risks arising on third party loans and related swaps;
(iii) holding foreign currency cash balances in its subsidiaries in the Southern and Eastern Europe region; operating activities through revenues from, and payments to, international telecommunications carriers as well as capital expenditure contracted with vendors in foreign currency.

In line with currency hedging policy, the Company holds sufficient amounts of foreign currencies on its bank accounts, the amounts of which are determined considering the balance of FX denominated trade and leases payables and trade receivables in order to hedge the currency risk arising in connection with those assets and liabilities. The Group's foreign currency denominated assets (primarily held by the Group's foreign subsidiaries), however, exceed the Group's foreign currency denominated liabilities (other than the above described loans), therefore changes of the functional currencies' exchange rates would have significant impact on the profit of the Group.

In order to reduce the above exposure, Magyar Telekom occasionally enters into derivative contracts.

(b) Interest rate risk

Magyar Telekom is also exposed to interest rate fluctuations. This is due to the fact that changing interest rates affect the fair value of the fixed rate instruments and also affect the cash flows through the floating rate instruments.

Changes in the market interest rates of non-derivative financial instruments with fixed interest rates only affect income if these are measured at their fair value. On the other hand, all financial instruments with fixed interest rates (which are carried at amortized cost) are not subject to cash flow interest rate risk.

(c) Other price risk

As of December 31, 2011, Magyar Telekom did not hold any material investments, which could be affected by risk variables such as stock exchange prices or other indices.

10.3.2 Credit risk

Credit risk is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation. The vast majority of credit risks may arise in respect of Cash and cash equivalents, Bank deposits with original maturities over 3 months and Trade receivables.

According to the Group's risk management policy Magyar Telekom Group companies deposit the excess cash only in banks rated at least BBB+ (or equivalent), or make efforts to get guarantees for the deposits from banks rated at least BBB+. Moreover, Magyar Telekom prefers to deposit in banks which grants loans for Magyar Telekom to make possible the compensation of debts and loans in case of the default of the bank.

Concentrations of credit risk relating to trade receivables are limited due to the large number of customers comprising the Group's customer base and their dispersion across many different geographic areas and industries.

10.3.3 Liquidity risk

Liquidity risk is the risk that an entity may encounter difficulty in meeting obligations associated with financial liabilities.

Prudent liquidity risk management implies maintaining sufficient Cash and cash equivalents and Bank deposits as well as available funding through adequate amount of committed credit lines. The Group Treasury's management aims at maintaining flexibility in funding by keeping committed credit lines available. In addition to the above, DT confirmed its readiness to finance Magyar Telekom Group's budgeted financing needs until the end of June 2013.

10.3.4 Capital risk management

The Group's objectives when managing capital are to safeguard the Group's ability to continue as a going concern in order to provide returns for shareholders and benefits for other stakeholders and to maintain an optimal capital structure to reduce the cost of capital.

The Company's management proposes to the owners (through the Board) of the Company to approve dividend payments or adopt other changes in the Company's equity capital in order to optimize the capital structure of the Group. This can be achieved primarily by adjusting the amount of dividends paid to shareholders, or alternatively, by returning capital to shareholders by capital reductions, selling or buying own shares. Consistent with others in the industry, the Group monitors capital on the basis of the gearing ratio. This ratio is calculated as Net debt divided by Equity (including Non-controlling interest) and Net debt.

In addition to the above, according to the Hungarian Companies Act, Magyar Telekom Plc. has to ensure that the Company's Equity does not fall below its Common stock, i.e., the total of the reserves should not be negative. Magyar Telekom Plc. is in compliance with this regulation, and no such statutory regulation exists for consolidated equity.

11. Analysis of financial results for 2011

11.1. Revenues

Total revenues amounted to HUF 597.6 bn in 2011 as compared to HUF 609.6 bn in 2010, representing a 2.0% decline year on year. The drivers of this decrease are the following:

Fixed line voice-retail revenues decreased by 13.9% and amounted to HUF 91.8 bn in 2011 compared to HUF 106.6 bn in 2010, mainly driven by lower PSTN subscription fee revenues and lower outgoing traffic revenues.

Subscription fee revenues decreased from HUF 64.4 bn in 2010 to HUF 55.3 bn in 2011 due to lower number of our fixed line subscribers mainly in Hungary.

Outgoing traffic revenues decreased mainly in Hungary as a result of the continuous decline in the number of revenue producing fixed lines and decreased ARPA (due to flat rate packages, such as Hoppá) while PSTN traffic slightly increased as higher traffic in F2M relation (thanks to Hoppá package) compensated the decrease in minutes in other relations.

Magyar Telekom Plc. offered several price discounts to customers choosing different flat-rate and optional tariff packages. Our Hoppá tariff package was very successful in 2011, generating more than 406,000 subscribers by the end of December 2011. The vast majority of customers choosing this package signed a 2-year loyalty contract, therefore this offer proved to be a very useful tool to decrease fixed line customer churn in Hungary. Our integrated fixed and mobile offer, the Paletta tariff package, was subscribed by almost 43,000 customers at December 31, 2011.

Outgoing traffic revenues decreased also at Makedonski Telekom and at Crnogorski Telekom primarily due to lower usage.

Value added and other service revenues showed a 50.6% increase and amounted to HUF 5.1 bn in 2011 compared to HUF 3.4 bn in 2010, mainly due to revenues from the reconnection of customers previously suspended due to non-payment. At Magyar Telekom Plc., the greater part of the provision made for KAP loyalty points was reversed due to unused points in 2011, which also contributed to the increase.

Fixed line voice-wholesale revenues increased by 2.2% reaching HUF 21.8 bn in 2011 compared to HUF 21.3 bn in 2010 mainly due to the increase in international incoming traffic revenues.

Domestic incoming fixed line traffic revenues decreased from HUF 8.1 bn in 2010 compared to HUF 7.9 bn in 2011. The drop in revenue from other domestic fixed line operators is due to lower call origination and termination revenues at Magyar Telekom Plc. as a result of decreased traffic in Hungary. These decreases were partly offset by higher revenue from other domestic fixed line operators at Makedonski Telekom resulting from higher termination fees of international traffic in its network due to deregulation. At Magyar Telekom Plc., the increase in revenues from mobile operators was mainly due to higher mobile-to-international traffic volume, partly compensated by reduced termination fees.

International incoming fixed line traffic revenues increased by 5.2% in 2011 and amounted to HUF 13.9 bn compared to HUF 13.2 bn in 2010. Higher international incoming traffic revenue at Makedonski Telekom was driven by higher international termination fees effective from May 2010 which was slightly offset by lower settlement rate and decreased traffic. Incoming international voice traffic revenue increased also at Magyar Telekom Plc., primarily due to higher volume of incoming international minutes, partly compensated by lower average fees applied. These increases were somewhat offset by the decrease in international incoming traffic revenues at Crnogorski Telekom caused by lower volume of international incoming and transit traffic.

Internet revenues of the fixed line operations decreased to HUF 52.6 bn in 2011 compared to HUF 53.8 bn in 2010. In Hungary, the number of DSL connections slightly decreased from 623,723 at December 31, 2010 to 621,491 at December 31, 2011 as the lower number of wholesale connections was largely offset by the increase in the number of retail DSL subscribers. Cablenet customer base and the number of fiber connections increased but the broadband volume increase could not compensate the effect of lower average revenue per user ("ARPU") resulting from lower prices forced by strong competition. The migration towards T-Home double- and triple-play packages also put downward pressure on blended ARPU level. Magyar Telekom Plc. accounted for an estimated 64% retail DSL market share and an approximately 22% cable broadband market share at November 30, 2011. Decreased Internet revenues in Hungary were somewhat compensated by the higher revenues at Crnogorski Telekom due to increased number of DSL connections.

TV revenues amounted to HUF 31.8 bn in 2011 as compared to HUF 28.5 bn in 2010. The increase is mainly attributable to higher IPTV revenues driven by enlarging IPTV subscriber base both in Hungary and at our foreign subsidiaries in 2011. The fast growth of IPTV customer base was helped by our development of high speed Internet access (mainly ED3) and it shows the increasing popularity of interactive television. The growth in satellite TV revenues was due to the higher number of satellite TV customers which reached 281,312 at December 31, 2011 and, on the other hand, due to the increased satellite TV ARPU year over year. These increases were partly offset by lower Cable TV revenues driven by lower subscriber base and decreased ARPU in Hungary.

Revenues from fixed line equipment decreased by 5.8% in 2011 compared to 2010 resulting from decreased equipment revenues at Novatel EOOD as there were no IRU (long-term right of use) sales in 2011. The decrease at Makedonski Telekom was due to lower sales volume of computers, TV sets, ADSL modems and telephone sets. These decreases were partly mitigated by higher equipment sales revenues at Magyar Telekom Plc. due the higher sale of Tablet PCs and TV sets in 2011. Higher equipment sales revenue at Crnogorski Telekom as a result of introducing TV sets' sale from October 2011 also mitigated these decreases.

Other fixed line revenues increased by 54.4% in 2011 compared to 2010. Other revenues include construction, maintenance, rental, energy trade and miscellaneous revenues. The increase in Hungary was mainly due to the significant revenues generated from the retail energy trade business in 2011, partly compensated by lower revenues from telephone book publishing.

Mobile revenues amounted to HUF 308.5 bn for the year ended December 31, 2011 compared to HUF 315.2 bn in 2010 (2.1% decrease). The decrease in mobile revenues resulted mainly from lower voice revenues at the mobile operations of Magyar Telekom (T-Mobile Hungary, "TMH") and at our foreign subsidiaries. These decreases were offset by higher broadband and equipment revenues at TMH.

Within mobile telecommunications services, voice revenues represent the largest portion of revenues. It amounted to HUF 212.5 bn in 2011. At TMH, lower retail tariffs forced by strong competition and the lower customer base together with declined average usage per customer per month ("MOU") resulted in lower voice-retail traffic revenues in prepaid segment. Lower voice-retail revenues at T-Mobile Macedonia ("T-Mobile MK") were mainly resulting from lower customer number and lower average price per minute. The decrease in voice-wholesale revenues in Hungary reflects decreased termination fees (16% decrease from December 1, 2010), slightly offset by higher customer base and higher incoming MOU. At T-Mobile Crna Gora ("T-Mobile CG"), lower voice-wholesale revenues were due to lower interconnection tariffs towards domestic operators and also due to lower volume of incoming minutes in the postpaid segment. Visitor revenues declined at TMH due to regulated tariff reduction and lower usage.

TMH's blended MOU increased from 168 minutes in 2010 to 172 minutes in 2011. TMH's monthly ARPU decreased only by 2.1% from HUF 3,732 in 2010 to HUF 3,655 in 2011, as the effect of lower average tariffs were largely offset by higher usage and the increased proportion of postpaid customers.

Mobile penetration reached 117.3% in Hungary and TMH accounted for 45.0% market share in the highly competitive mobile market at December 31, 2011 based on the total number of SIM cards. TMH's customer base increased by 1.1% year over year. The proportion of postpaid customers increased to 50.8% at December 31, 2011 from 48.2% a year earlier.

Higher non-voice revenues were primarily due to TMH's higher mobile Internet revenues. This increase was partially offset by lower messaging revenues. Non-voice revenues represented 22.8% of total ARPU in 2011. By December 31, 2011 TMH had 1,048,514 mobile broadband customers and accounted for a 48.7% market share based on total number of subscriptions in the mobile broadband market.

Mobile equipment and activation revenues increased by 14.6% in 2011 compared to last year mainly at TMH. Higher retention revenues resulted from higher average handset prices reflecting increased sales ratio of higher priced smartphones and lower prepaid handset subsidy. The increase at our foreign subsidiaries was primarily attributable to higher number of handsets sold.

Other mobile revenues remained broadly stable year over year.

System Integration ("SI") and IT revenues increased by 8.4% from HUF 44.8 bn in 2010 to HUF 48.5 bn in 2011. Increased infrastructure revenues at Magyar Telekom Plc. driven mainly by significantly higher project revenues in 2011. The inclusion of Daten-Kontor revenues in 2011 and the higher application revenue at IQSYS due to revenues from sale of Digital table in 2011 also contributed to the increase. These increases were mitigated by considerably less government projects at KFKI in 2011 and declined outsourcing revenues at Dataplex mainly due to lower revenues from the invoicing of energy cost in 2011.

11.2. Operating Expenses

Voice-, data- and Internet-related payments decreased to HUF 60.6 bn in 2011 compared to HUF 65.2 bn in 2010, predominantly resulting from lower voice-related payments to domestic mobile operators in Hungary driven by lower mobile termination fees applied from December 2010 and also by declined traffic. Drop in payments to mobile operators at Makedonski Telekom were mainly due to lower traffic volumes. At Crnogorski Telekom, the decrease is mainly due to lower traffic volumes and decreased tariffs from April 2011.

Other direct costs include HUF 0.9 bn content-related payments, HUF 10.9 bn TV-related payments, HUF 11.0 bn agent commissions and HUF 8.1 bn other revenue-related payments in 2011. Increased other direct costs at Magyar Telekom Plc. ("MT Plc.") are mainly due to energy costs appearing in line with the launch of retail energy trade in 2010. Higher TV-related payments at MT Plc. and at Makedonski Telekom, due to higher TV subscriber base, also contributed to the increase. These increases were partly offset by lower agent commissions year over year. The decline in agent commissions at T-Mobile MK is due to decreased sale through dealers and at MT Plc. due to drop in agent activity and lower commission fees per transaction.

Employee-related expenses in 2011 amounted to HUF 91.8 bn compared to HUF 93.9 bn in 2010 (a decrease of 2.2%). Decrease was mainly attributable to the 1.4% lower employee figure on MT Group-level year over year (from 10,258 on December 31, 2010 to 10,111 on December 31, 2011) and decreased income tax on fringe benefits due to modified legislation in Hungary. The inclusion of the employees of Daten-Kontor after its consolidation in 3Q 2011 partially offset these decreases. Higher bonus payments and higher provision made for the future lay-offs at MT Plc. also mitigated these decreases.

Depreciation and amortization increased by 31.8% in 2011 compared to 2010. The significant increase is resulting from the HUF 31.4 bn goodwill impairment booked in the Group for the Macedonian segment. This increase was slightly offset by decreased amortization at MT Plc., mainly due to the amortization effect of the change in estimated useful life of certain assets and higher amount of assets fully written off.

Other operating expenses increased by 4.2% to HUF 155.1 bn in 2011 from HUF 148.8 bn in 2010. The majority of the increase in other operating expenses is due to the HUF 16.2 bn provision booked in 2011 in connection with the investigation. Higher rental fees at MT Plc. were predominantly due to the rental fee of set top boxes from June 2010. These increases were partly offset by decreased consultancy fee due to lower expenses recognized relating to the CRM and Finance Streamlining projects and also due to lower investigation-related costs in 2011 at MT Plc. Decreased marketing expenses at MT Plc. are resulted from rescheduled marketing spending. Decreased bad debt expenses at MT Plc. are mainly the result of the substantial efforts made for debt collecting in 2011. Materials and maintenance decreased at MT Plc., predominantly resulting from lower IT support costs (renegotiated hardware and software support contracts).

On October 18, 2010 the Hungarian Parliament approved an act imposing a special tax ("crisis tax") on a number of sectors including telecommunications sector. Special tax for the full year of 2010 (amounting to HUF 27.0 bn) was recognized in December 2010 among other operating expenses, while it is booked on a monthly basis in 2011 amounting to HUF 25.4 bn in 2011.

Other operating income increased from HUF 3.4 bn in 2010 to HUF 6.4 bn in 2011 mainly due to the gains from disposal of real estates at Magyar Telekom Plc. A government grant received for the Norwegian project at Mindentudás Egyeteme in 2011 also contributed to the increase. Higher other operating income at Makedonski Telekom was mainly due to release of provision for legal cases and also due to increased gain from sale of fixed assets in 2011.

11.3. Operating Profit

Operating margin for the year ended December 31, 2011 was 10.6% while operating margin for 2010 was 18.4%. The decrease was mainly due to the 2.0% revenue decline, the HUF 31.4 bn goodwill impairment and the HUF 16.2 bn provision made in relation to the investigation in 2011.

11.4. Net financial results

Net financial expenses increased by 15.5%, from HUF 28.1 bn in 2010 to HUF 32.5 bn in 2011. The increase in net financial expenses is primarily resulting from higher net foreign exchange loss realized in 2011, as the weakening of HUF against EUR was more intensive in 2011. In 2011, MT Plc. booked HUF 1.1 bn as interest and HUF 4.5 bn forex loss on the provision for litigation in connection with the investigation. Lower interest received on loans given and on bank deposits mainly at our foreign subsidiaries in line with lower average amount of loans also had a negative effect on net financial results. Lower net forex gain at Makedonski Telekom and Stonebridge due to the less favorable movement of EUR/MKD also contributed to the increase in 2011. These impacts were partly offset by higher gain on derivative transactions due to change in interest and exchange rates at MT Plc. Lower interest paid on loans received is due to lower average interest rate and lower average amount of loans at MT Plc., which also positively affected net financial expenses.

11.5. Income tax

Income tax expense increased significantly despite of the lower profit before tax of the Group year over year. The main indicator is the elimination of the enacted reduction of the Hungarian corporate tax rate from 19% to 10% effective from 2013, which results a large one-off deferred tax expense. The non deductibility of the DOJ penalty from the corporate income tax base also increased the tax expense in 2011.

12. Subsequent events between the end of the year and the release of the report

12.1. Hungarian mobile spectrum auction

The Company filed an auction bid in December 2011 with the Hungarian National Media and Infocommunications Authority for unused spectrum in the 900 MHz frequency band, relating to the provision of radio communications services. The spectrum can be utilized in a technology-neutral manner, allowing for the installation and operation of GSM, UMTS, LTE and/or WiMAX mobile networks. On January 31, 2012, the Company received from the Authority the first instance, non-final decision closing the auction. Pursuant to the first instance decision, the Company won the right of use of two duplex frequency blocks of 1 MHz each (one EGSM-band duplex frequency block of 1 MHz plus one PGSM-band duplex frequency block of 1 MHz) for a period of 15 years.

12.2. Deregistration

The Company delisted its ADSs from the New York Stock Exchange effective November 12, 2010. On November 14, 2011 Magyar Telekom filed with the U.S. Securities and Exchange Commission (the "SEC") a Form 15F to terminate registration of its shares and American Depositary Shares ("ADSs") in the US. The deregistration became effective on February 12, 2012, 90 days after the filing of the Form 15F. The Company will maintain its American Depositary Receipt program on a Level I basis. The Company will maintain its primary listing on the Budapest Stock Exchange and will continue to make English translations of its annual reports, financial statements and investor releases.

Budapest, February 23, 2012.

Christopher Mattheisen
Chairman and Chief Executive Officer

Thilo Kusch
Chief Financial Officer

Declaration

We the undersigned declare that

- the attached condensed set of financial statements which have been prepared in accordance with the applicable set of accounting standards and to the best of our knowledge, gives a true and fair view of the assets, liabilities, financial position and profit or loss of Magyar Telekom Plc. and the undertakings included in the consolidation as a whole, and
- the management report gives a fair view of the position, development and performance of Magyar Telekom Plc. and the undertakings included in the consolidation as a whole, together with a description of the principal risks and uncertainties of its business.

Budapest, April 16, 2012

Christopher Mattheisen
Chairman and Chief Executive Officer

Thilo Kusch
Chief Financial Officer