



A French corporation (*société anonyme*) with share capital of €10,130,830.84
Registered office: 8 Rue de la Ville l'Evêque – 75008 Paris

Paris Trade and Companies Register No. 342 376 332

2004 ANNUAL REPORT



Pursuant to articles 211-1 to 211-42 of the Regulations of the *Autorité des Marchés Financiers* (AMF), this document was registered by the AMF on May 24, 2005 as No. R.05-072. It may not be used in support of a financial transaction unless it is accompanied by a *note d'opération* approved by the AMF.

This annual report has been prepared by the issuer and its signatories are liable for it. This registration, following an examination of the relevance and consistency of information provided regarding the Company's position, does not imply an authentication of the accounting and financial items presented herein.

Copies of this document are available free of charge from Iliad, 8 Rue de la Ville l'Evêque, 75008 Paris, France, and on the internet through the AMF website (<http://www.amf-france.org>).

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CHAPTER 1

CERTIFICATION BY THE INDIVIDUAL RESPONSIBLE FOR THE REGISTRATION DOCUMENT AND THE INDIVIDUALS RESPONSIBLE FOR AUDITING THE FINANCIAL STATEMENTS

In this annual report, the term “Iliad” or “Company” refers to Iliad, and the term “Group” refers to the group of companies comprising the Company and all its subsidiaries.

1.1 CERTIFICATION BY THE INDIVIDUAL RESPONSIBLE FOR THE REGISTRATION DOCUMENT

1.1.1 Individual responsible for the registration document

Mr. Michaël Boukobza, General Manager.

1.1.2 Certification by the individual responsible for the registration document

“To my knowledge, the information contained in this registration document is accurate; it includes all information necessary for investors to evaluate the assets, business activity, financial position, results, and prospects of Iliad and its subsidiaries, and contains no omission that could render the information provided misleading.”

Michaël Boukobza, General Manager

1.2 CERTIFICATION BY THE STATUTORY AUDITORS

1.2.1 Principal statutory auditors

PricewaterhouseCoopers Audit
Represented by Xavier Cauchois
Tour AIG
34 Place des Corolles
92908 Paris La Défense 2

Boissière Expertise Audit
Represented by Tita A. Zeitoun
57 Rue Boissière
75016 Paris

Initially appointed at the October 19, 2000 shareholders meeting; the appointment expires at the close of the shareholders meeting to be called to approve the financial statements for the fiscal year ending December 31, 2005.

Initially appointed at the December 30, 1997 shareholders meeting; the appointment expires at the close of the shareholders meeting to be called to approve the financial statements for the fiscal year ending December 31, 2008.

1.2.2 Alternate statutory auditors

Pierre Coll
32 Rue Guersant
75017 Paris

FIDUCO
Represented by Jean-Luc Cohen
2-4 Rue Adolphe Mille
75019 Paris

Initially appointed at the May 28, 2004 shareholders meeting; the appointment expires at the close of the shareholders meeting to be called to approve the financial statements for the fiscal year ending December 31, 2005.

Initially appointed at the December 30, 1997 shareholders meeting; the appointment expires at the close of the shareholders meeting to be called to approve the financial statements for the fiscal year ending December 31, 2008.

1.2.3 Translation of the statutory auditors' certification of the registration document

In our capacity as statutory auditors of Iliad S.A. and as required by article 211-5-2 , Book II of the Regulations of the *Autorité des Marchés Financiers*, we have examined, in accordance with professional standards applicable in France, the information concerning the financial position and the historical accounts included in this annual report.

This annual report is the responsibility of Mr. Cyril Poidatz, General Manager of Iliad. Our responsibility is to express an opinion on the fairness of the information concerning the financial position and the accounts contained in this document.

Our procedures, which were performed in accordance with professional standards applicable in France, consisted of assessing the fairness of the information concerning the financial position and the accounts and verifying that this information is consistent with the audited financial statements. Our procedures also consisted of reading the other information contained in the annual report in order to identify any material inconsistencies with the information concerning the financial position and the accounts and reporting any materially incorrect information that came to our attention, based on our overall knowledge of the Company as acquired during our audit. This annual report does not contain any specific forward-looking information determined according to a structured process.

We audited the financial statements of the Company and the Group for the years ended December 31, 2002, 2003 and 2004, as approved respectively by the management board and by the board of directors. Our audits were performed in accordance with professional standards applicable in France. Our reports on these financial statements were unqualified without any observation.

Based on the procedures described above and taking into account the observation made in one of our previous reports as indicated above, we have nothing to report with respect to the fairness of the information concerning the financial position and the historical financial statements contained in this annual report.

Paris, May 24, 2005

The Statutory Auditors

PricewaterhouseCoopers Audit

Xavier Cauchois

Boissière Expertise Audit

Tita A. Zeïtoun

This annual report includes:

- the reports on the consolidated financial statements and on the financial statements for fiscal year 2004 including in pages 92 and 130 explanations for our estimations in accordance with the provisions of Article L. 225-235 of the French Commercial Code.
- the statutory auditors' report (page 160) drawn up in application of the last paragraph of Article L. 225-235 of the French Commercial Code, on the report of the chairman of the board of directors

describing the procedures for internal control relative to the elaboration and treatment accounting and financial information.

1.3 INFORMATION POLICY

1.3.1 Individual responsible for information

Mr. Olivier Rosenfeld
Chief Financial Officer
Iliad
8 Rue de la Ville l'Evêque
75008 Paris
Telephone: +33 1 73 50 20 00

1.3.2 Projected timetable for communication of financial information

All financial information provided by Iliad (press releases, presentations, annual reports) is available on its website at the following address: *http://www.iliad.fr*

The projected timetable for communication of Iliad's financial information for the year 2005 is as follows:

- Annual shareholders meeting: May 27, 2005;
- Revenue for the first half of 2005: on or before August 15, 2005;
- Earnings for the first half of 2005: on or before September 30, 2005;
- Revenue for third quarter 2005: on or before November 15, 2005;
- Revenue for fiscal year 2005: on or before February 14, 2006;
- Publication of interim financial statements for fiscal year 2005: on or before April 30, 2006;
- Revenue for first quarter 2006: on or before May 15, 2006;
- Annual shareholders meeting: May 2006.

CHAPTER 2

INFORMATION REGARDING THE TRANSACTION

In the event of transaction involving a public offering, the information contained in this chapter will be presented in a *note d'opération* submitted for approval by the *Autorité des marchés financiers*.

CHAPTER 3

GENERAL INFORMATION CONCERNING THE COMPANY AND ITS CAPITAL

3.1 GENERAL INFORMATION CONCERNING THE ISSUER

3.1.1 Corporate name and registered office

Corporate name: Iliad

Registered office: 8 Rue de la Ville l'Evêque, 75008 Paris.

3.1.2 Legal form

Iliad is a French corporation (*société anonyme*) with a board of directors and is governed by the French Commercial Code and Decree No. 67-236 of March 23, 1967 concerning commercial companies.

3.1.3 Incorporation, registration, and term

The Company is registered in the Paris Trade and Companies Register (RCS Paris) as SIREN No. 342 376 332.

The Company's French industrial classification code (*Nomenclature d'Activités Française*) is 22.1 E, Publication of Reviews and Periodicals.

The Company was incorporated on August 31, 1987, for a fixed term of ninety-nine years from the date of the Company's registration with the RCS Paris, expiring on October 15, 2086 unless the Company is dissolved or its term extended.

3.1.4 Corporate purpose (Article 2 of the bylaws)

The Company's purpose is to directly or indirectly conduct the following activities in France or any other country:

- to study, implement, maintain, operate, manage or market all systems, equipment, networks or services in the fields of telecommunications, Internet, data processing, telematics and communications, including installation and operation of electronic communications networks;
- to publish and disseminate all services, programs and information, in particular, to publish and provide telephone and telematics services to the public and disseminate audiovisual communications services by any technical means, in particular, through the press, radio, audio-visual media, video or remote transmission, on magnetic or other media;
- to acquire by any means and manage investments in the capital of any French or foreign companies, regardless of their form and purpose, by purchase, subscription or otherwise;
- to acquire, by any means, bonds, founders' shares or other securities issued by such companies;
- to provide any services relating to commercial, financial, accounting and administrative activities;
- to directly or indirectly invest, through contributions from partnerships or otherwise, in any companies having one or more activities directly or indirectly related to the Company's corporate purpose;
- to invest in any business or company with one or more activities which may be directly or indirectly related to the Company's corporate purpose or to any similar or associated purpose, in particular by creating new companies, contributions, mergers, joint ventures, partnerships or consortia;
- and more generally, to conduct any industrial, commercial, financial, real estate, real and personal property or securities transaction which directly or indirectly relate to the Company's corporate purpose or any similar or associated purpose.

3.1.5 Consultation of legal documents

The Company's bylaws, minutes and other corporate documents required to be made available to shareholders pursuant to applicable regulations may be consulted at the Company's registered office.

3.1.6 Fiscal year

The Company's fiscal year begins on January 1st and ends on December 31st of each calendar year.

3.1.7 Distribution of income (Article 31 of the bylaws)

The Company's income statement reports the Company's profit or loss for the fiscal year after deduction of depreciation, amortization and provisions.

Five percent of fiscal year profit, less any prior losses, is allocated to the legal reserve. This deduction is no longer required when that reserve equals one-tenth of the Company's share capital, and is resumed whenever the legal reserve falls below one-tenth of the Company's share capital for any reason.

Distributable income represents fiscal year revenue, less prior losses and amounts allocated to reserves pursuant to applicable law or the Company's bylaws, plus deferred revenue. From this amount, the shareholders meeting may deduct any amount deemed appropriate to allocate to optional reserves or carry forward.

The shareholders meeting may also decide to distribute funds drawn from available reserves, expressly indicating the reserve items from which the funds are drawn. However, dividends are deducted first from distributable fiscal year income.

Except in the case of the capital reduction, no distribution may be made to shareholders when shareholders' equity is or would become following the distribution less than the amount of capital and reserves that may not be distributed under applicable laws or the Company's bylaws.

The revaluation surplus may not be distributed; all or part of it may be incorporated into the capital account.

Any loss is recorded in a special account to be carried forward and offset against net income in future years until the balance is eliminated.

3.1.8 Payment of dividends (Article 32 of the bylaws)

The method of paying dividends is determined by vote of the shareholders meeting or, when necessary, by the board of directors.

However, cash dividends must be paid no later than nine months following the close of the fiscal year unless an extension is authorized by court of law.

The shareholders meeting may, under the conditions determined by law, offer each shareholder the option of receiving all or part of dividend payments or advances on dividends in the form of new shares of the Company.

3.1.9 Corporate management

At its December 12, 2003 meeting, the Company's board of directors decided to separate the functions of chairman of the board and general manager.

The general manager is vested with all powers relating to the Company's day-to-day management and represents the Company to third parties. The chairman of the board is responsible for ensuring that the corporate bodies function properly. The board of directors is responsible for establishing the Company's strategic direction and ensuring that the Company operates efficiently; it is also responsible for overseeing the Company's management. For a description of the corporate bodies' operations, see section 6.1.1.

3.1.10 Shareholder meetings

The collective decisions of the Company's shareholders are made in the shareholders meetings, which are classified as regular or special according to the types of decisions they are called to make.

The shareholders meetings duly convened and constituted represent all the Company's shareholders. Their decisions are binding on all shareholders, including those absent, dissenting or disqualified.

3.1.10.1 Convocation and meetings (Article 4 of the bylaws)

Shareholders meetings are called by the board of directors or, when necessary, by the statutory auditors or any person authorized by law.

They are held at the Company's registered office or any other location indicated in the notice of meeting.

They may be held by videoconference or any other telecommunications technology, including the Internet, which permits identification of the shareholders under the terms and conditions prescribed by applicable laws and regulations.

3.1.10.2 Agenda (Article 25 of the bylaws)

The agenda for the shareholders meeting is determined by the party calling the meeting.

However, one or more shareholders or the works council may request the inclusion of proposed resolutions on the agenda under the terms and conditions prescribed by applicable laws and regulations.

The shareholders meeting may not consider matters not included on the agenda. However, it may remove or replace one or more directors at any time.

The agenda for a shareholders meeting may not be amended on a second notice of meeting.

3.1.10.3 Access to and representation at shareholders meetings (Article 26 of the bylaws)

Any shareholder may participate in shareholders meetings in person or by proxy, regardless of the number of shares owned, subjected to proof of the shareholder's identification and ownership of the shares in the form of:

- registration of the shares in the shareholder's name; or
- certification by an authorized account custodian verifying that shares held electronically are unavailable for trading until the date of the shareholders meeting.

The documentation must be provided at least five days prior to the meeting. However, the board of directors may shorten or eliminate this time requirement provided that such change applies to all shareholders.

Shareholders of the Company residing outside French territory may be registered and represented at the shareholders meeting by any intermediary registered on their behalf and holding a valid power of attorney to manage their shares, provided that the intermediary has previously registered with the Company or the account custodian as an intermediary holding shares on behalf of a third party.

Any shareholders who will not attend the meeting in person may choose one of the following three options:

- be represented by another shareholder or his or her spouse;
- vote by mail using a form which may be obtained by following instructions provided in the notice of meeting; or
- send a proxy to the Company without indicating a representative; the chairman of the meeting will vote in favor of resolutions presented or approved by the board of directors and against all other proposed resolutions. In order to vote otherwise, the shareholder must appoint a representative who agrees to vote as instructed by the shareholder.

3.1.10.4 Meeting officers (Bureau) (Article 27 of the bylaws)

The shareholders meetings are chaired by the chairman of the board or, in his absence, by a director appointed by the board for this purpose. Where the meeting is called by the statutory auditors or a court-appointed representative, the meeting is chaired by the party calling the meeting. Otherwise, the meeting elects the chair.

The role of election inspector (*scrutateur*) is filled by the two shareholders present who hold the largest number of votes, either in their own right or as proxies, and agree to serve in this capacity.

Those two meeting officers appoint a secretary, who need not be a shareholder.

The meeting officers are responsible for verifying, certifying and signing the attendance register, oversee deliberations, resolving matters that arise during the meeting, monitoring and ensuring the propriety of the voting process, and overseeing preparation of the minutes.

3.1.10.5 Quorum and voting in shareholders meetings (Article 28 of the bylaws)

Subject to the double voting rights described in section 3.1.11 below, each shareholder shall have a number of votes equal to the number of shares owned or represented in the regular and special shareholders meetings.

The quorum is calculated based on the total number of shares constituting the corporate capital other than those classified as non-voting shares pursuant to applicable law or provisions of the bylaws.

A regular shareholders meeting cannot validly deliberate upon first notice of meeting unless the shareholders present, represented or voting by mail represent at least one-fourth of the voting shares. No quorum is required on the second notice of meeting. The shareholders meeting adopts decisions by a majority of the votes of shareholders present, represented or voting by mail.

A special shareholders meeting cannot validly deliberate unless the shareholders present, represented or voting by mail represent at least one-third on the first notice of meeting, or one-fourth on the second notice of meeting, of the voting shares. In the absence of a quorum on the second notice of meeting, the second shareholders meeting may be postponed to a date two months later than the initial scheduled date. The special shareholders meeting adopts decisions by a majority of two-thirds of the shareholders present, represented or voting by mail. In the event of a capital increase through capitalization of reserves, earnings or premiums, the quorum and majority rules for regular shareholders meetings will apply.

Shareholders who participate in a meeting by videoconference or other telecommunications technology that allows shareholders to be identified and complies to the terms and conditions prescribed by applicable regulatory provisions are deemed present for the purpose of calculating the quorum and majority.

3.1.11 Double voting rights (Article 28 of the bylaws)

The special shareholders meeting of December 12, 2003 voted to institute double the voting rights of other shares in respect of the proportion of capital represented for all fully paid shares shown to have been registered to the same shareholder for at least three years on or after the date the Company's securities were admitted to trading on a regulated exchange.

In the event of a capital increase through capitalization of reserves, earnings or premiums, or by exchange of shares in connection with a stock split or consolidation, double voting rights will be granted to new shares issued in respect of registered shares, provided they are held as registered shares from the time of their issuance and the shares in respect of which they are issued have double voting rights.

Any shares that are transferred or converted to bearer shares shall forfeit the double voting rights attributed pursuant to Article 28-1 of the bylaws.

However, the transfer by right of succession, liquidation, spousal community property or inter vivos gift to a spouse or parent does not result in forfeiture of double voting rights or suspend the holding period provided by the bylaws.

Moreover, a merger or spin-off of the Company does not affect the double voting rights, which may be exercised in the new company if provided by the bylaws.

The special shareholders meeting may not eliminate double voting rights without the approval of a special meeting of the shareholders holding those rights.

3.1.12 Form of shares and identification of shareholders (Article 9 of the bylaws)

Except as provided by law, fully paid shares shall be registered or bearer shares, at the option of the shareholder. They are required to be registered until this time they are fully paid.

The Company is entitled to request at any time, under the terms and conditions provided by applicable legal and regulatory provisions, that the securities clearing organization provide it with a list of the name, address, nationality, date of birth, or year of incorporation for a corporation, of parties holding securities conferring present or future voting rights in the shareholders meetings, as well as the number of shares held by each party and any restrictions on those shares.

With respect to the list provided and those listed parties whom the Company believes may be holding shares on behalf of third parties, the Company is also entitled to ask the securities clearing organization or the parties themselves, under the same terms and conditions, whether they are holding shares on behalf of third parties, and if so, to provide the Company with information identifying those third parties. If the identity of the owner or owners is not disclosed, the vote or proxy exercised by the registered intermediary will not be recognized.

3.1.13 Ownership threshold (Article 12 of the bylaws)

Any natural person or legal entity, acting alone or jointly with others, that directly or indirectly owns or controls a number of shares representing 1% or more of the Company's capital or voting rights must report to the Company, within five trading days of the transaction that caused the shareholder(s) to reach or exceed this threshold, the date of the transaction, the total number of shares and voting rights held, the number of instruments held that confer entitlement to future shares, and the attached voting rights. The report must be sent by registered mail with return receipt requested, or by equivalent means for shareholders residing outside France

This report must be renewed under the same terms and conditions whenever the portion of capital or voting rights held increases or decreases by a whole multiple of 1% of the capital and voting rights.

In the event of failure to comply with the foregoing, those shares in excess of the threshold which should have been reported will be stripped of voting rights in all shareholders meetings held during the two years after the date the noncompliance is cured, at the request of one or more shareholders holding at least 1% of the Company's capital and voting rights, as evidenced in the minutes of the shareholders meeting.

3.2 GENERAL INFORMATION CONCERNING THE COMPANY'S SHARE CAPITAL

3.2.1 Amount of share capital (Article 6 of the bylaws)

On the date of filing this registration document, the Company's share capital totaled €10,130,830.84 represented by 54,151,550 fully subscribed and paid shares of the same class.

3.2.2 Modification of share capital or voting rights attached to shares

As there are no specific governing provisions of the Company's bylaws, any modification of the share capital or voting rights attached is subject to the provisions of applicable laws and regulations.

3.2.3 Acquisition of treasury shares

The twenty-ninth resolution of the December 12, 2003 shareholders meeting authorized the board of directors, with authority to delegate under the terms provided by law, to acquire up to 10% of the Company's shares. This authorization was granted for a term of eighteen months and remains in effect until June 11, 2005.

Pursuant to this authorization, the Company's board of directors voted at its February 12, 2004 meeting to implement a stock repurchase program. The Company prepared a *note d'information* in connection with this program, which was approved by the AMF on March 16, 2004 under No. 04-163, and launched the program on March 18, 2004.

The maximum purchase price under the stock repurchase program is €43 per share, and the minimum price is €11 per share.

The objectives of the stock repurchase program, in decreasing order of priority, are as follows:

- a) to stabilize the Company's share price by systematically trading against the market;
- b) to purchase or sell the Company's shares according to market conditions;
- c) to implement any stock option plan pursuant to the provisions of Articles L.225-177 *et seq.* of the French Commercial Code;
- d) to invest in existing shares or securities conferring present or future entitlement to the Company's shares under the terms and conditions provided by law, in particular, pursuant to Articles L.443-1 *et seq.* of the French Labor Code or in connection with employee profit-sharing plans;
- e) to deliver shares (in payment, exchange or otherwise) in connection with acquisitions by the Company;
- f) to deliver shares in connection with the exercise of rights attached to securities redeemable, convertible, exchangeable or otherwise exercisable for shares of the Company; and
- g) to implement an asset and financial management policy that involves holding, selling or transferring such shares in general, including the option to cancel any or all of such shares.

The Company executed the following transactions in connection with the stock repurchase program:

	Purchases	Sales
Number of shares	610,684	603,097
Average transaction price.	23.5858	23.58
Totals (in euros)	14,403,517	14,221,008

As a result of the above purchases and sales, the Company's portfolio of treasury shares on March 31, 2005 was as follows:

Percentage directly or indirectly held by the Company	0.01%
Number of shares cancelled in the preceding 24 months	0
Number of securities held in portfolio	7,587
Book value of portfolio	220,440.21 euros
Market value of portfolio	217,746.90 euros

The stock repurchase program was used for the sole purpose of stabilizing the Company's stock price by executing purchases and sales against the market.

The board of directors will recommend that the meeting of the Company's shareholders to be held on May 27, 2005 grant the board of directors a new authorization to implement a stock repurchase program in accordance with the AMF General Regulations, in particular, European Commission Regulation No. 2273/2003 of December 22, 2003 concerning the implementation of European Directive 2003/6/EC of January 28, 2003.

3.2.4 Capital stock authorized but unissued

The special shareholders meeting of December 12, 2003 delegated authority to the board of directors to increase the Company's capital as follows:

Authority delegated to the board of directors by the special shareholders meeting	Nominal amount authorized	Nominal amount used (in euros)	Term of delegation	Expiration date
To issue securities entitling the holder to shares of the Company while preserving shareholders' preferential subscription rights.	400,000	0	26 months	2/11/2006
To issue securities entitling the holder to shares of the Company and eliminate shareholders' preferential subscription rights.	400,000	122,374.68 ⁽¹⁾	26 months	2/11/2006
To issue securities entitling the holder to shares of the Company and transfer preferential subscription rights to categories of individuals.	200,000	0	24 months	12/11/2005
To increase capital through capitalization of reserves, earnings or premiums.	75,000,000	8,877,625.32	60 months	12/11/2008

(1) Result of capital increases at the time of Iliad's IPO.

The board of directors will recommend that the shareholders meeting to be held on May 27, 2005 terminate the above-referenced delegations of authority and authorize the board to carry out capital increases subject to certain limitations.

3.2.5 Potential share issues

3.2.5.1 Founders' warrants (*Bons de souscription de parts de créateur d'entreprise*)

The June 28, 2001 special meeting of the Company's shareholders issued founders' warrants as follows:

- 240,000 founders' warrants ("**Founders' A Warrants**") subject to Article 163a (G) of the French Tax Code entitling the holder to subscribe new shares. All of the Founders' A Warrants exercisable through June 27, 2006, entitling the holder to subscribe 104,010 shares at €2.97 per share, were exercised as of March 15, 2005.
- 192,000 founders' warrants ("**Founders' B Warrants**") subject to Article 163a (G) of the French Tax Code. On June 3, 2004, Olivier Rosenfeld irrevocably waived the exercise of his 192,000 Founders' B Warrants exercisable for 83,200 shares of Iliad.
- 197,440 founders' warrants ("**Founders' C Warrants**") subject to Article 163a (G) of the French Tax Code. On June 3, 2004, Olivier Rosenfeld irrevocably waived the exercise of his 197,440 Founders' C Warrants exercisable for 85,560 shares of Iliad.

The special shareholders meeting of August 12, 2002 issued 238,124 founders' warrants ("**Founders' 2002 Warrants**") subject to the provisions of Article 163a (G) of the French Tax Code entitling the holders to subscribe new shares. On June 3 and 4, 2004, Olivier Rosenfeld, Michaël Boukobza and Cyril Poidatz each irrevocably waived the exercise of their 59,531 Founders' 2002 Warrants exercisable, respectively, for 595,310 shares of Iliad. All of the remaining 59,531 Founders' 2002 Warrants exercisable through August 11, 2007 and entitling the holder to subscribe 595,310 shares at €2.97 per share, were exercised on March 15, 2005.

As a result of the above-referenced cancellations and exercises, there are no outstanding founders' warrants issued by the Company at this date.

The minutes of the April 8, 2005 meeting of Company's board of directors reported the increases in the Company's share capital pursuant to the exercise of the Founders' A Warrants and Founders 2002 Warrants.

3.2.5.2 *Stock purchase and subscription options*

The special meeting of the Company's shareholders held on December 12, 2003, pursuant to Articles L.225-177 *et seq.* of the French Commercial Code, authorized the board of directors to grant employees and managers of the Company or affiliated companies within the meaning of Article L.225-180 of the French Commercial Code, on one or more occasions, options to subscribe or purchase the Company's shares.

The total number of shares subject to the options granted under this authorization and options previously granted may not exceed 3% of the Company's share capital at the date the options are granted. This authorization was granted for a term of thirty-eight months from the date of the shareholders meeting, or February 11, 2007.

The exercise price of the options granted pursuant to this authorization may not be less than 80% of the average price for the 20 trading days preceding grant of the options; no option may be granted less than 20 trading days after shares have been stripped of dividend rights or preferential subscription rights in connection with a capital increase. In addition, the option exercise price may not be less than 80% of the average purchase price of shares held by the Company pursuant to Article L.225-208 of the French Commercial Code or a stock repurchase program in effect, if applicable.

In connection with the above-referenced authorization by the shareholders meeting, the board of directors met on January 20 and 29, 2004 and voted to implement a stock option and stock subscription plan and issue the 485,769 subscription options to 22 employees of the Group, each option entitling the holder to subscribe one new share at €16.30 per share.

Twenty-one of the Group's employees held 444,132 options to subscribe 444,132 shares of the Company as of April 1, 2005.

The following table summarizes the Company's outstanding stock subscription options as of April 1, 2005.

Date of shareholders meeting	12/12/2003
Date of board of directors meeting	1/20/2004
Total number of options granted by the board of directors	485,769
– <i>Number of options granted to directors</i>	0
Total number of recipients	21
– <i>Number of directors</i>	0
Exercise price per share (in euros)	16.30
Option exercise date	1/20/2008
Option expiration date	1/19/2014
Number of options exercised	0
Number of options expired	41,637
Total number of options exercisable	0
Total number of potential new shares to be issued	444,132
Maximum dilutive effect of outstanding options	0.82 %

3.2.5.3 Information concerning potential dilution of the Company's capital resulting from transactions during the prior three fiscal years involving potential issues of new shares (addition of new shareholders or transactions affecting existing shareholders)

Other than the stock subscription options identified in section 3.2.5.2 above (the "Dilutive Instruments"), there are no instruments directly or indirectly conferring present or future rights to the Company's shares or voting rights.

Type of Dilutive Instrument	Date Granted	Exercise Price (euros)	Expiration Date	Number of potential shares to be issued	Dilutive Effect (%)
Subscription options	1/20/2004	16.30	1/19/2014	444,132	0.82
Total				444,132	0.82

(1) Unless the beneficiary leaves the Company.

3.2.6 Instruments not representing capital

At the date of this registration document, there are no instruments issued by the Company that do not represent share capital.

3.2.7 Change in capital stock during the previous five years

Date of special shareholders' meeting	Transaction	Number of shares issued or cancelled	Nominal amount of capital increase or reduction (in euros)	Share premium (in euros)	Total share premiums (in euros)	Total par value of capital stock (in euros)	Total shares outstanding	Par value of shares (in euros)
12/30/2000	Capital increase through contributions in kind	868,493	1,351,449.87	25,350.32	25,350.32	10,470,950.08	6,868,493	1.52
	Capital increase through capitalization of reserves	—	518,638.72	—	25,350.32	10,989,588.80	6,868,493	1.60
6/28/2001	Conversion of capital to euros	—	—	—	25,350.32	10,989,588.80	6,868,493	1.60
	Multiplication by number of shares and decrease in par value of shares	103,027,395	—	—	25,350.32	10,989,588.80	109,895,888	0.10
3/13/2002	Capital reduction and increase in par value of shares	103,027,395	9,989,588.80	9,989,588.80	10,962,034.12	1,000,000	6,868,493	0.15
	Capital reduction	2,106,070	306,627.67	9,528,719.35	1,433,314.77	693,372.33	4,762,423	0.15
5/15/2002	Capital increase through capitalization of premiums	—	306,627.67	306,627.67	1,126,687.10	1,000,000	4,762,423	0.21
12/12/2003	Multiplication by number of shares and decrease in par value of shares	42,861,807	—	—	1,126,687.10	1,000,000	47,624,230	0.02
1/29/2004	Capital increase through cash contributions	5,000,000	104,988.57	78,034,413.23	79,161,200.33	1,104,988.57	52,624,230	0.02
2/03/2004	Capital increase through exercise of subscription warrants	828,000	17,386.11	13,479,841.89	92,641,042.22	1,122,374.68	53,452,230	0.02
2/19/2004	Capital increase through capitalization of reserves	—	8,877,625.32	-8,877,625.32	83,763,416.90	10,000,000	53,452,230	0.19
4/8/2005	Capital increase through exercise of founders' warrants	699,320	130,830.84	2,958,176.56	86,721,953.46	10,130,830.84	54,151,550	0.19

3.3 SHAREHOLDING STRUCTURE

3.3.1 Shareholding structure as of April 1, 2005

On April 1, 2005, the Company's capital and voting rights were distributed as follows:

Shareholder	Shares and voting rights	Percentage of capital and voting rights
Xavier Niel ⁽¹⁾	36,633,910	67.65%
Antoine Levavasseur ⁽²⁾	1,052,590	1.94%
Rani Assaf ⁽²⁾	952,590	1.76%
Olivier Rosenfeld ⁽¹⁾	729,500	1.35%
Cyril Poidatz ⁽¹⁾	719,199	1.33%
Michaël Boukobza ⁽¹⁾	744,199	1.37%
Franck Brunel ⁽²⁾	729,525	1.35%
Alain Weill ⁽³⁾	84,697	0.16%
<i>Subtotal, management members</i>	<i>41,646,210</i>	<i>76.91%</i>
Employees (other than management members)	61,000	0.11%
Iliad SA.	7,587	0.01%
Public	12,436,753	22.97%
Total	54,151,550	100.00%

(1) Shareholder, manager and director of the Company.

(2) Shareholder and manager of the Company.

(3) Shareholder and director of the Company.

On March 23, 2005, Iliad announced that following a private placement of 2,135,980 shares held by Xavier Niel, an employee of the Group, and the Goldman Sachs fund with institutional investors, outstanding shares increased from 19.6% to 23.3%, or close to 4%.

To the Company's knowledge, there are no shareholders other than those listed above who directly or indirectly hold more than 1% of the Company's capital and voting rights.

3.3.2 Changes in the Company's shareholding structure during the prior three fiscal years

The Company's capital and voting rights were held as follows at the close of the three previous fiscal years (as percentages of the total):

Shareholders	12/31/2002	12/31/2003	12/31/2004
Xavier Niel ⁽¹⁾	77.93%	77.95%	69.45%
Antoine Levavasseur ⁽²⁾	2.42%	2.42%	1.97%
Rani Assa ⁽²⁾	2.42%	2.42%	1.78%
Olivier Rosenfeld ⁽¹⁾	2.00%	2.00%	1.36%
Cyril Poidatz ⁽¹⁾	2.00%	2.00%	1.35%
Michaël Boukobza ⁽¹⁾	2.00%	2.00%	1.39%
Franck Brunel ⁽²⁾	2.00%	2.00%	1.37%
Alain Weill ⁽¹⁾	0.20%	0.20%	0.16%
<i>Subtotal, management members</i>	<i>90.97%</i>	<i>90.99%</i>	<i>78.83%</i>
Goldman Sachs fund	6.90%	6.90%	1.75%
Axa fund	—	0.65%	—
Employees (other than management members)	2.13%	1.46%	0.11%
Iliad SA	0.00%	0.00%	0.00%
Public	0.00%	0.00%	19.31%
Total	100.00%	100.00%	100.00%

(1) Shareholder and director of the Company.

(2) Shareholder and manager of the Company.

The changes in the Company's capital and voting rights during fiscal year 2004 is largely the result of operations in connection with listing the Company's shares for trading on the Euronext Premier Marché (now Eurolist) in January 2004. Since the transaction, only the Goldman Sachs funds has reported a decrease in holdings involving the bylaws' reporting threshold during the second half of 2004. To the Company's knowledge, the Goldman Sachs fund no longer held any shares of the Company's at the date this registration document was filed.

3.3.3 Shareholding commitments, shareholder agreements and joint actions

3.3.3.1 Shareholding commitments

Xavier Niel gave a commitment to JP Morgan Cazenove Limited to retain all his shares until September 22, 2005.

3.3.3.2 Shareholder agreements

None.

3.3.3.3 Joint actions

To the Company's knowledge, there are no shareholders acting jointly other than the Company's managers and shareholders (Xavier Niel, Rani Assaf, Franck Brunel, Antoine Levavasseur, Michaël Boukobza, Cyril Poidatz, Olivier Rosenfeld and Alain Weill), who act jointly in their capacity as managers of the Company.

3.3.4 Pledged shares

3.3.4.1 Pledge of registered shares managed by the transfer agent

None.

3.4.2 2004 Historical Data

	Price per share (in euros)		Total trades (in thousands of euros)	Volume traded (number of shares)
	High	Low		
2004				
January	22.70	16.30	109,433	5,238,255
February	21.84	19.14	48,770	2,355,824
March	21.80	17.10	24,464	1,346,681
April	21.17	17.31	24,406	1,255,051
May	21.45	18.00	22,606	1,171,250
June	20.18	17.15	19,252	1,036,619
July	19.64	18.00	28,250	1,576,478
August	19.30	16.30	10,478	591,021
September	19.50	17.35	37,048	2,005,670
October	22.73	18.87	32,657	1,571,494
November	22.80	20.00	49,108	2,220,367
December	28.29	22.16	30,587	1,253,891
2005				
January	29.44	25.85	39,874	1,433,923
February	32.48	25.22	87,205	3,043,620
March	29.50	27.03	52,808	1,867,213

3.4.3 Transfer Agent

Shareholder services (record keeping and dividend disbursement) are provided for Iliad by Société Générale (SBAN/BCT/CLE, 32 Rue du Champ de Tir, BP 81236, 44312, Nantes Cedex 3).

3.5 DIVIDENDS

During the previous five fiscal years, the Company distributed dividends for fiscal years 2001, 2002 and 2003.

The annual shareholders meeting of June 25, 2002 distributed dividends of €4,000,435 (or €0.84 per share), representing approximately 45.34% of net earnings for fiscal year 2001.

The shareholders meeting of May 6, 2003 distributed dividends of €4,286,181 (or €0.9 per share), representing approximately 16.45% of net earnings for 2002.

The shareholders meeting of May 28, 2004 distributed dividends of €5,345,223 (or €0.1 per share), representing approximately 92.35% of net earnings for 2003.

The board of directors meeting of December 6, 2004 approved the payment of €4,008,917 in dividends (or €0.075 per share), representing approximately 41.45% of net earnings for the first three quarters of fiscal year 2004.

The board of directors determines the dividend payment policy based on a review of the Company's earnings and financial position and other factors. The board will recommend payment of a dividend of €0.04 per share in addition to the advance on dividends paid on December 6, 2004 to the May 27, 2005 shareholders meeting.

Dividends remaining unclaimed 5 years after the payment date expire and are remitted to the French State.

3.6 LIQUIDITY AGREEMENT

Iliad executed a liquidity agreement with Oddo & Cie Entreprise d'Investissement and Oddo Pinatton Corporate on February 16, 2004. The agreement complies with the French Association of Investment Firms' code of professional conduct and will provide liquidity of transactions and protect against volatility of the Company's share price. The agreement was renewed on January 1, 2005 for a term of twelve months.

The following transactions were executed in connection with the liquidity agreement in 2004:

	Number of shares	Purchases Unweighted average price (in euros)	Total (in euros)	Number of shares	Sales Unweighted average price (in euros)	Total (in euros)
March	8,670	18.04	156,401	7,815	18.05	146,065
April	33,283	19.88	661,714	33,159	19.83	657,643
May	34,343	19.90	683,425	32,910	19.93	655,992
June	46,716	18.77	877,064	46,938	18.80	882,642,
July	19,791	18.33	372,586	17,953	18.89	339,115
August	17,330	17.69	306,496	15,759	17.63	277,776
September	49,726	18.43	916,210	48,960	18.50	905,859
October	52,370	20.48	1,072,387	54,042	20.42	1,103,667
November	61,335	22.05	1,352,650	63,046	22.03	1,388,896
December	32,294	24.56	793,051	32,707	24.45	799,631
Total	355,858	19.81	7,191,984	353,289	19.85	7,157,286

CHAPTER 4

DESCRIPTION OF ILIAD'S BUSINESS

All technical terms used in this chapter are defined in a glossary which can be found at the end of this document on page 182.

4.1 OVERVIEW OF THE COMPANY AND THE GROUP

A leading Internet service provider and telecommunications operator in France

Formed in 1991, the Group has leveraged its telecommunications networking expertise to establish itself as the second largest Internet service provider in France¹. It is also one of the best performing operators in the fixed telephony market in France.

The Group is now one of the major players in the Internet and telecommunications sector in France due to its highly attractive services as viewed by the consumer market. The Group is currently:

- the second largest ADSL broadband Internet service provider with a 17.4%² share of the residential market. As of December 31, 2004, Free had 1,064,000 ADSL broadband subscribers³;
- a leading player leader in the unbundling of the local loop in France, having unbundled almost 36% of the total number of unbundled access lines (i.e. 566,000 lines out of a total of 1,590,707 unbundled lines as of January 1, 2005⁴). This leading position in the unbundling arena has enabled the Group to provide technically sophisticated services (such as high connection speeds and “triple play” services) that are both attractively priced and profitable for the Group; and
- a successful fixed telephony operator through its subsidiaries One.Tel and Kertel. The Group is therefore able to make the most of its network infrastructure, which can be used to transport both data and switched voice traffic.

Over the last few years, the Group has seized opportunities for external growth in order to enhance and optimize the use of its network. Its existing data traffic business (Free) has now been complemented with a voice business generated by the fixed telephony operator One.Tel, which was acquired by the Group in December 2001, and with prepaid phone cards marketed by Kertel, acquired in March 2003. These two acquisitions have contributed to the Group's growth and profitability since 2002 and have enabled it to spread network costs over a more diversified business, which now covers both Internet traffic and switched voice traffic.

The Group's business is based on one of the leading alternative telecommunications networks in France and includes a range of services focused on the residential sector. Today the Group's business falls into three main segments: Internet, Telephony and Other Services.

The *Internet* segment is undergoing a period of significant growth driven by the expansion in infrastructure, lower hardware costs (for computers, modems, etc.) and lower charges for Internet access services, as well as by the increase in the number of public projects and, more particularly, by the expansion in the availability of broadband technologies such as ADSL. The Group's Internet business is centered on (i) the provision of Internet access by the company Free, based on both dial-up access (which includes two services, one a pay-as-you-go service and the other a fixed-rate package offering 50 hours of access per month) and broadband Internet access via ADSL and (ii) the provision of shared website hosting and the registration of domain names by the company Online.

Following the success, first, of its “Pay-as-you-go” and “50-hour plan” services and subsequently of its unlimited broadband access service which costs €29.99 per month, Free is now the second largest Internet service provider in the French residential broadband market with 17.4%⁵ of all ADSL subscribers as of December 31, 2004. For its part, Online hosts approximately 77,000 websites, making it a major provider of shared hosting solutions for business websites.

¹ Source: Iliad/France Télécom

² Source: Iliad/France Télécom.

³ Source: Iliad.

⁴ Source: ART and Iliad.

⁵ Source: Iliad/France Telecom

The Group's *Telephony segment* is centered on the activities of the fixed telephony operator One.Tel and those of the prepaid phone card provider Kertel, as well as on the call termination business developed by Kedra.

With approximately 335,000 customers as of December 31, 2004, One.Tel is a relatively small fixed telecommunications operator, but it is profitable and has adopted an aggressive pricing policy likely to result in an increase in its market share. Following the acquisition of this company in December 2001, the Group concentrated on repositioning One.Tel's service offering, adopting a policy of carrier preselection, simplifying the range of services offered and establishing an attractive pricing policy (a price of 0.01 euros per minute for all local and national calls). Since its takeover by Iliad, a system of payment by direct debit has been strongly encouraged in order to guarantee the payment of bills by its customers, and as of December 31, 2004 more than 84% of One.Tel's customers used this method of payment, compared with 73% as of December 31, 2003. With the benefit of being able to use the Group's network and boosted by a positive marketing strategy, One.Tel is now in a position to win a large number of new customers without compromising its profitability.

Kertel, which is the second largest provider of prepaid phone cards in France, was acquired by the Group in 2003 and benefits from both the quality and reach of a first-rate distribution network (particularly through its exclusive agreement with the French post office, La Poste, for the top up of mobile phone cards) and very attractive tariffs achieved as a result of economies of scale made possible by its use of the Group's network. Finally, Kedra offers high-quality call termination services in particular to the Group's fixed telephony business.

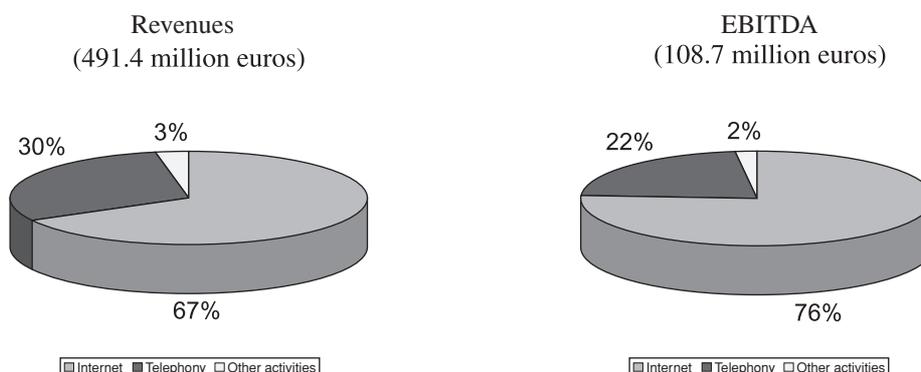
The *Other Services* segment includes in particular the reverse look-up directory ANNU, which is accessed mainly via Minitel and also by telephone, as well as web content services provided by the Group subsidiaries Assunet S.A., a web-based insurance broker, and Société S.A., which operates a website providing information about companies.

The following table shows the changes in the Group's consolidated net revenues, gross operating income and EBITDA¹ over the last three financial periods:

(in millions of euros)	December 31, 2002	December 31, 2003	December 31, 2004
Consolidated net revenues	160.3	293.1	491.4
EBITDA	43.2	53.6	108.7
Operating income	35.1	35.0	53.1

¹ EBITDA (earnings before interest, tax, depreciation and amortization) equates to the operating income, plus depreciation allowances and operating allowances on tangible and intangible fixed assets

Breakdown of revenue and EBITDA by line of business as of December 31, 2004



Local loop unbundling: a key strategy for the profitable growth of the Group

The unbundling of the local loop is a technical operation which allows operators to control the access to their subscribers and thereby free themselves to a great extent from their dependence on France Télécom's network. Local loop unbundling (LLU) is vital for the Group's ADSL services, as this enables it to take full advantage of the density and quality of its network in order to provide end-to-end management of the infrastructures connecting it to its customers.

LLU allows the Group to offer its customers attractive prices (currently €29.99 per month for the ADSL broadband Internet access package, with a download rate of 20 Mbits per second) and a competitive range of services, providing higher transmission speeds (see the comparative speeds listed on www.grenouille.com) combined, for customers who have a Freebox modem, with telephony and audiovisual services.

LLU is a key element for the profitability of the Group due to the high margins that can be generated. At present, most of the recurrent charges paid to France Télécom relate to the rental of equipment used for connecting the subscriber's modem to the corresponding DSLAM belonging to the Group.

By placing LLU at the heart of its strategy and adopting an aggressive and profitable pricing policy, Free succeeded in winning one in five new ADSL broadband customers during 2004, in an extremely competitive market. As of December 31, 2004, the company had 1,064,000 ADSL customers, 566,000 of whom are on unbundled lines¹.

Growth in Free's broadband customer base between 2002(*) and 2003

	31/12/2002	30/06/2003	31/12/2003	30/06/2004	31/12/2004
Broadband customers	99,100	275,630	485,000	768,000	1,064,000
Number using unbundled lines	3,300	45,850	163,000	355,000	566,000
<i>Percentage using unbundled lines</i>	3.3%	16.6%	33.6%	46.2%	53.2%
Share of residential ADSL access market in France	7.2%	13.3%	15.0%	16.8%	17.4%

(*) Free's ADSL broadband Internet access service was launched in October 2002.

¹ Source: Iliad.

Key dates and development of the Group's organizational structure

The key dates in the development of the Group are as follows:

- 1996 – Launch of the reverse look-up directory 3617 ANNU.
- 1999 – Creation of the Internet service provider Free.
 - The Group was granted category L. 33-1 and L. 34-telecommunications licenses, authorizing it to roll out a telecommunications network and to provide telecommunications services to the public.
- 2000 – Start of the roll-out of the Group's telecommunications network and interconnection with France Télécom's network.
 - Sale of the Group's Minitel business (excluding ANNU).
- 2001 – Completion in April 2001 of the interconnection between the Free Telecom network and the France Télécom network at regional level and in the Paris urban area.
 - Launch of the Freebox (modem and DSLAM) research and development project.
 - Acquisition of the French subsidiary of the Australian telecommunications operator One.Tel in December 2001.
- 2002 – Restructuring of One.Tel and migration of its traffic to the Group's network.
 - Launch of Free's broadband service.
 - Start of local loop unbundling operations in Paris.
- 2003 – Roll-out of LLU to the majority of residents in France.
 - In March 2003, the Group became the second largest ADSL broadband Internet service provider in France.¹
 - Acquisition of the prepaid phone card specialist Kertel
 - Launch of the ADSL fixed telephony service using the Freebox modem in August 2003 (under Option 1).
 - Launch of an ADSL-based audiovisual content service offering in December 2003.
- 2004 – Iliad's initial public offering. Listing on the Euronext Paris Premier Marché on January 30, 2004.
 - Launch in March 2004 of voice over ADSL services under Option 5 using the Freebox modem.
 - Launch of a fully unbundled service offering in June 2004
 - Launch of the ADSL 2+ service offering in October 2004
 - Broadcast of Canal+ TV offers via the Freebox in November 2004.

¹ Source: IDATE, *Le marché mondial de l'Internet, 2003 edition*.

4.2 COMPETITIVE ADVANTAGES

The Group benefits from a number of competitive advantages which should enable it to sustain its profitable growth and maintain its position as the second largest Internet service provider in France, in addition to reinforcing its position as a fixed telecommunications operator. The Group believes it is well-placed to take full advantage of the growth potential in the Internet and telecommunications sectors because it has the following competitive advantages:

An established Internet services provider, Free, with a well-known brand

As a result of the success of its consumer market services, Free has managed to establish itself as a major player in the Internet access market in France since 1999. Free's successive launching of its dial-up "Pay-as-you-go" and "50-hour plan" offerings and its €29.99 per month broadband service have established the credibility and recognition of the brand. The Group benefits from a brand associated with the concepts of freedom, cutting-edge technology and value-for-money.

Technically sophisticated and attractively priced service offerings

The Group's network enables it to design sustainable service offerings that are at once easy to understand (the charge for the One.Tel service is a straightforward 1 eurocent per minute, see paragraph 4.5.2.1 below), technically sophisticated and attractively priced. The three Internet access offerings, consisting of two dial-up services (the "Pay-as-you-go" service and the "50-hour plan", which is charged at a fixed rate of €14.94 per month) and the broadband access service at €29.99 per month, are among the most competitively priced on the market in their respective segments while providing a high level of quality. This positioning is a central factor in the Group's strategy and aims to create the right environment for lasting and profitable growth of its business.

A high-performance national network supporting both Internet service provider and fixed telephony operations for the consumer market

In order to be able to offer high-performance and innovative services to its customers and to guarantee the profitability of its business operations, the Group decided, in 1999, to establish its own telecommunications network, which would allow it to control the technical aspects and pricing of its services for the routing of both data (Internet) and voice (telephony). Since early in the second half of 2001, the Group has been rolling out and operating its own optical fiber network. The skills and experience acquired by the Group's network teams now mean that it is able to use its own resources to operate and maintain a nationwide network and guarantee its Internet customers a level of quality and connection speeds which are each recognized as among the best on the market. The specific technical features of the network and its high level of density are key factors in the success and profitability of the Group's service offerings in both Internet access and telephony. The size, design and scalable architecture of the Group's network make it currently capable of serving, without significant additional investments, all potential customers simultaneously using the Group's telephony, broadband and audiovisual services in areas where unbundling of the local loop has taken place.

A leading player in local loop unbundling

The Group considers that the unbundling of the local loop is at the heart of its ability to offer original, sustainable and profitable broadband Internet access services. Currently the Group has the largest number of unbundled lines (566,000 out of a total of 1,590,707 unbundled lines) of any of the alternative operators in France, according to figures provided by the French regulator, the *Autorité de Régulation des Télécommunications* ("ART") as of January 1, 2005. This has been achieved by the installation of approximately 1,342 Freebox DSLAMs in 410 co-location facilities located in France Télécom exchanges. The Group intends to capitalize on its experience in unbundling the local loop to expand the areas in which it can offer differentiated services to its customers.

Targeted research and development focusing on the consumer market

The Group's investment in research and development of hardware and software products has enabled it to position itself as a frontrunner in the implementation of innovative solutions on the consumer market. The success of this policy is based largely on the Group management's commitment to providing high-quality

technical equipment and retaining flexibility in its choice of hardware, resulting in the design of hardware specifically suited to the Group's service offerings and using cutting-edge technologies such as design of the Freebox modem/DSLAM unit, and in the development of innovative software solutions (such as billing software, Cisco SS7 interconnect software, etc.). By relying largely on its internal resources in this way, the Group has, from the start, been able to optimize its capital expenditures.

Understanding of key regulatory issues

The Group has demonstrated its understanding of regulatory issues by establishing a constructive dialogue with the ART, particularly in the context of the local loop and interconnect working groups set up by the ART. The Group has also shown its ability to take full advantage of the appeal procedures offered by the ART in order to defend its interests. The Group believes that it has a good overall understanding of the current legislative and regulatory environment, as well as of the proposals under discussion which could have an impact on its activities as an Internet service provider and telecommunications operator.

A proven ability to generate profits in periods of high revenue growth

The Group has posted net profits each year since 2001, despite its significant investments in interconnection and LLU operations and the significant level of competition in its markets. The Group has demonstrated its capacity to finance internally the majority of its capital expenditures and new business start-up costs, while continuing to distribute dividends. With its high-performance network and large customer base, the Group believes it will be able to continue to pursue its strategy of profitable growth.

The ability to build on its experience

As the different parts of the Group's network complement and are integrated with one another, the Group is able to put its experience in certain areas of its business to work in the development of other services. The Group's expertise in fixed telephony acquired in the course of restructuring and running One.Tel enabled Free to launch the first available fixed telephony over ADSL services for the consumer market beginning in August 2003, without changing the prices of its broadband Internet access offering.

An experienced management team with complementary skills

Over the last few years, the management team has succeeded in positioning the Group as the second largest Internet service provider in France, while sustaining the profitability of the Group and pursuing a strategy of internally financed growth. This success is due largely to the experience and complementary skills of the management team in the following areas: knowledge of the Internet and telecommunications sector, understanding of key regulatory issues, consumer marketing know-how, strong technological expertise, sound financial management and commitment to a graduated investment policy. These skills have transformed a Group that originally specialized purely in electronic data transmission services into a leading player in the Internet market in France, even in today's highly competitive environment. They have also enabled the Group to acquire and integrate, on very favorable terms, new and complementary businesses (One.Tel in 2001 and Kertel in 2003).

4.3 STRATEGY

Leveraging its competitive strengths described in paragraph 4.2 above, the Group's strategy is based on the following four principles:

Continuing to provide the most competitive Internet access offerings in France

In order to continue the growth of its market share, the Group plans to pursue its policy of winning new ADSL broadband customers by combining a competitive pricing policy with a focus on the quality of its services (such as by offering ever-increasing bandwidth and innovative ADSL-based telephony and audiovisual content) and its technical and customer support services. The Group's aim is to implement this policy of winning new customers in a fast-growing market in a manner that further enhances the Group's profitability.

Increasing the number of subscribers on unbundled lines (Option 1)

The Group intends to increase the number of customers on unbundled lines in two complementary ways. First, the Group plans to increase its market share in areas which have already been unbundled by continuing to offer its Freebox services directly to new subscribers (Option 1). It also plans to encourage the migration of the maximum possible number of Option 5 subscribers (subscribers on lines that have not yet been unbundled) to Option 1 (subscribers on unbundled lines) by expanding the density of its network. The expansion of the network will not only be subject to technical constraints but will also depend on the prioritization of areas to be unbundled. This targeted expansion of the network will be carried out as a priority in areas that already have a large number of subscribers, so that a return on investment can be achieved quickly. Given the significant difference in profitability between subscribers using unbundled lines and subscribers not using such lines, the objective of this expansion of LLU (either with the aim of migrating existing subscribers or winning new subscribers) is to substantially increase the Group's profit margins.

Promoting the brand and increasing the market share of the Group's fixed telephony business

Following the restructuring of One.Tel, the Group's fixed telephony business is now profitable, but remains underused because of One.Tel's relative lack of brand recognition. As a result, the Group aims to take the necessary measures to promote the One.Tel brand, particularly by carrying out targeted publicity campaigns emphasizing the competitiveness and simplicity of One.Tel's offering.

Considering acquisition opportunities which could contribute to Group growth

Although it continues to focus on internal growth as the core of its strategy, the Group will pursue a policy of external expansion if targeted opportunities arise in areas that strongly complement its existing business or would result in improved use of the Group's network.

4.4 A NETWORK SERVICING THE GROUP'S INTERNET AND TELEPHONY OPERATIONS

In order to access the Internet, data must be routed between the user's computer and the Internet. Such Internet access is traditionally provided by Internet service providers using interconnect services, i.e. by connecting to the incumbent operator's network or to that of other licensed operators.

After Free was established, the Group believed it was critical to have control over as many network elements used for connecting its subscribers to the Internet as possible. This decision meant that Free could operate its own network infrastructure and quickly resulted in an influx of recurrent revenues from its "Pay-as-you-go" services and increased its profitability (largely as a result of the reduction in its spend on interconnect charges).

The Group began its network roll-out strategy in December 1999 when it obtained licenses awarded under Articles L. 33-1 and L. 34-1 of the French Post and Telecommunications Code (which in July 2004 was renamed the Post and Electronic Communications Code), authorizing Free Telecom (known at that time as Linx) to build and operate a telecommunications network and to provide telecommunications services to the public. Rather than build its own optical fiber infrastructure, Free's strategy was to obtain and operate optical fibers already installed by other operators, particularly by concluding with these operators long-term IRU (Indefeasible Right of Use) agreements granting Free an irrevocable right to use the dark optical fibers, in order to optimize its capital expenditures and guarantee a rapid interconnection with the incumbent operator's network.

The Group's network has been developed in three main phases:

- August 2000 – April 2001: interconnection with the digital main switching units and all digital local exchanges in the Paris urban area for the collection of data traffic;
- April 2001 – August 2002: interconnection at a number of digital local exchanges outside Paris and upgrading for routing of voice traffic;
- Since September 2002: unbundling of the local loop and expansion of the national network.

These three development phases, described in more detail in section 4.4.2 below, demonstrate the Group's constant efforts to achieve an appropriate balance between network density and return on investment.

Connection points between the Group's network and the France Télécom network as of 12/31/2004		
Type of France Télécom site	No. of connection points	Total No. of France Télécom sites
Digital main switching units	18	18
Digital local exchanges	225	540
France Télécom LLU sites	410	N/A

Main equipment used by Free's optical fiber network as of 31/12/2004	
Type of equipment installed	Quantity
Freebox DSLAM	1,342
Lucent ADM	236
Cirpack switches	23
Nokia switches	2
Cisco modem servers	38
Cisco switch routers	50
Huawei DWDM equipment	101

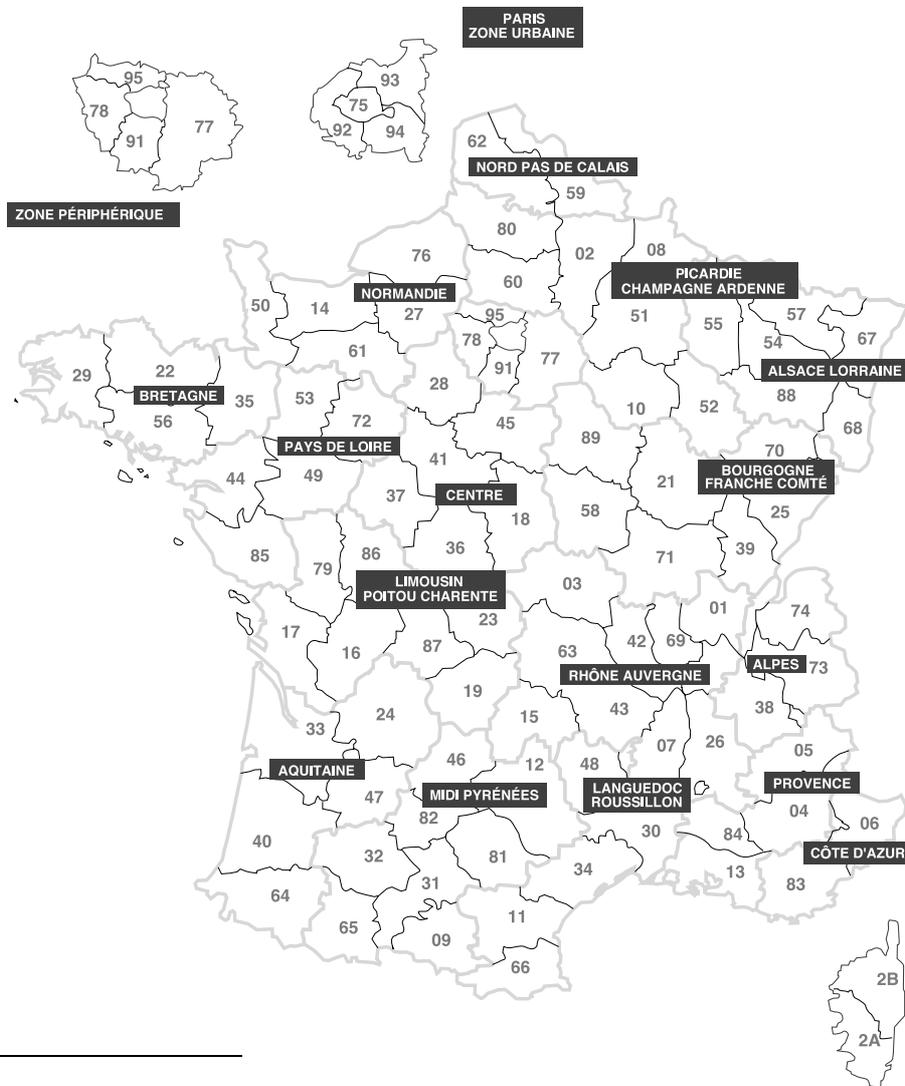
4.4.1 General principles of interconnection and local loop unbundling in France

Interconnection and local loop unbundling allow operators to access and use part of the incumbent operator's network in return for payment to the incumbent operator of access and usage charges. Interconnection to the incumbent operator's network allows the alternative operator to deliver its customers' telephony traffic, while local loop unbundling offers it complete control over the line connecting the customer to the Main Distribution Frame (MDF).

4.4.1.1 Interconnection

Interconnection means the linking together of several telecommunications networks in order to allow uninterrupted routing of communications between them.

France Télécom network showing the 18 trunk exchange areas



Source: Iliad

In order to interconnect to the incumbent operator's network in a given trunk exchange area, the alternative operator must install a physical connection from a Point of Presence (POP) to a France Télécom switch located in one of the eighteen France Télécom digital main switching units.

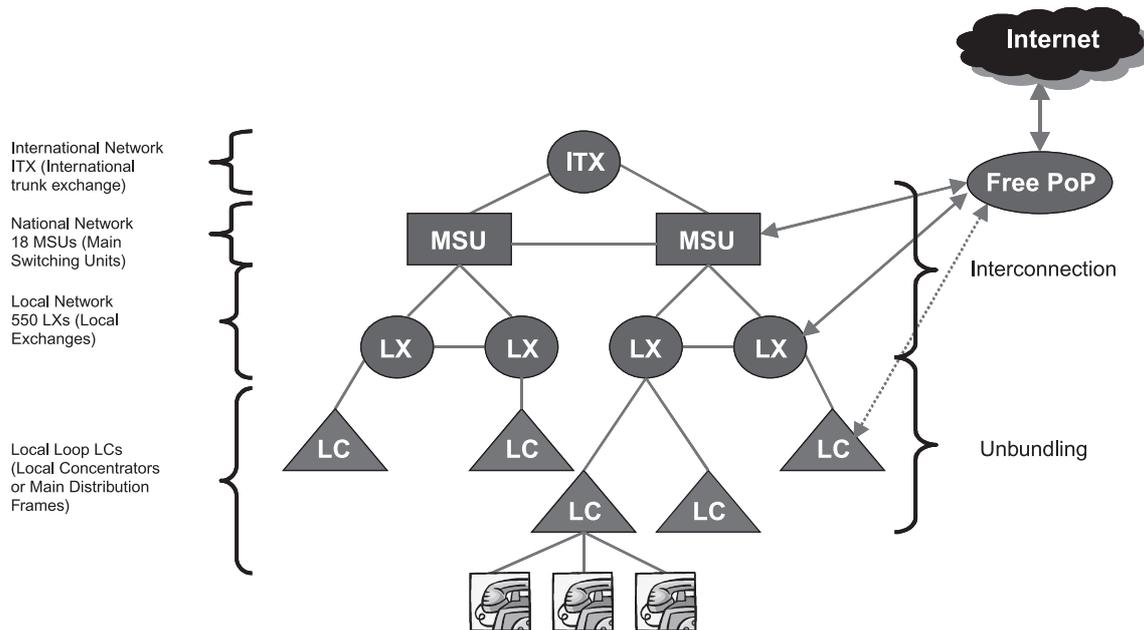
The alternative operator may also connect to the lowest hierarchical level of switches installed on the network, i.e. the digital local exchange, which is the switch closest to the customer.

In turn, each user is connected to a digital local exchange by means of a local concentrator.

Under an interconnect agreement, the incumbent operator charges the alternative operator on the basis of the transmission capacity placed at its disposal, measured in digital primary blocks (E1, a unit of measure corresponding to a bit rate of approximately 2 Mbits per second).

The OLO (Other Licensed Operator) can choose the level at which it wishes to make the interconnection, i.e. at the main switching unit or the local exchange, and the number of E1 blocks it wishes to reserve at each level. The higher the level in the France Télécom network at which traffic delivery takes place, the higher the interconnect charges and the charges for transport and collection of data billed by the incumbent operator to the alternative operator.

Schematic diagram of France Télécom's switched network



4.4.1.2 Unbundling of the local loop

The local loop is that part of the network located between the telephone socket on the subscriber's premises and the main distribution frame (or local concentrator) to which the subscriber's line is connected.

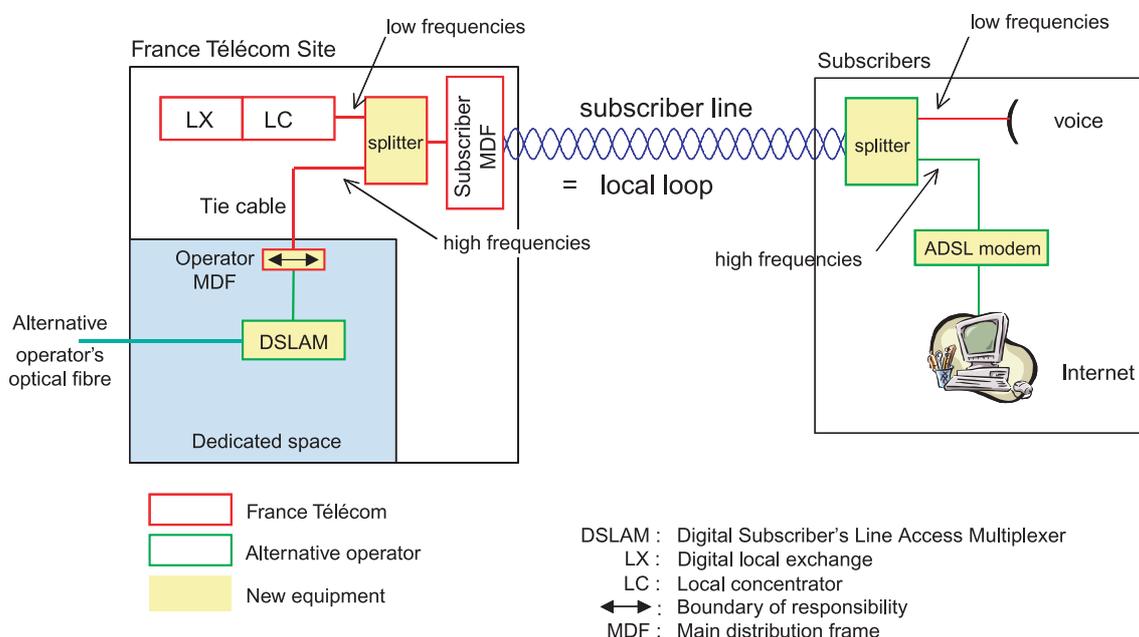
The incumbent operator must, upon request, provide any Other Licensed Operator (OLO) with direct access to the local loop. This access, which is referred to as unbundling, allows these OLOs to control access to their customers by operating their own equipment.

In an unbundled system, the copper pair (the part of the subscriber's line which connects the subscriber to the closest digital local exchange) is not connected directly to the equipment managed by France Télécom, but rather to an ADSL line concentrator (also called a DSLAM) installed in co-location facilities or dedicated rooms provided for this purpose in the France Télécom exchanges and managed by the operator chosen by the subscriber. A special modem is installed on the subscriber's premises to allow the subscriber to receive data transmissions at a speed of up to 20 Mbit/s.

In the case of partial unbundling, the alternative operator uses only the "high" frequencies of the copper pair needed for transporting data, while the "low" frequencies are still used by France Télécom to provide the ordinary telephone service. In this case, the user still pays the telephone line rental to France Télécom.

The following diagram shows the technical architecture used for this type of access.

Schematic diagram of partial unbundling



Source: Iliad

In practice, an alternative operator needs to use an optical fiber network which terminates in France Télécom's premises and install its own DSLAM equipment in co-location facilities or in dedicated spaces.

Local loop unbundling completely frees an operator from dependence on France Télécom's network. The recurring charges payable to France Télécom relate primarily to the rental of the copper pair, the splitter and the copper tie cable linking the subscriber's modem to the operator's DSLAM.¹

For purposes of clarification, the following sections contain the abbreviations MSU (for the digital main switching unit) and LX (for the digital local exchange) in relation to interconnection and the term "France Télécom site" in relation to local loop unbundling.

4.4.2 Phases of development of the Group's network

4.4.2.1 Phase 1: August 2000 – April 2001: Interconnection at the digital main switching units (MSU) and all digital local exchanges (LX) in the Paris urban area for the collection of data traffic

Initially, the Group's main objective was to interconnect its network to that of France Télécom in order to require a minimum level of national coverage. This required the Group to be connected as a minimum to the 18 France Télécom MSUs covering all regions of mainland France. The Group's network at that time consisted of a network of modem servers operated by Free and capable of meeting the needs of dial-up Internet subscribers.

Between August 2000, the date of the first interconnection in Lille to the MSU for the northern region, and June 2001, the date of the last interconnection in Poitiers to the MSU for the central region, Free's teams ordered E1 transmission capacity on France Télécom's network which it interconnected directly to the Group's network using optical fibers leased from a provider which had already installed the fiber network.

¹ See sections 5.2.1.2 and 5.2.1.3 for a detailed description of the fixed and variable LLU charges.

Free's innovative interconnection concept was to establish a direct connection between France Télécom's switches and the Group's Cisco modem servers. Therefore, instead of installing conventional switches between the France Télécom switches and its modem servers, Free helped to develop an application on the Cisco modem servers which supported the France Télécom network protocol.

This type of architecture, designed for data traffic, resulted in (i) a significant reduction in the level of capital expenditure required by reducing the quantity of equipment necessary for operation of the network, and particularly by avoiding the need for a central switch, (ii) greater control over the quality of service, and (iii) bandwidth savings over the national network as data is converted to IP mode at the level of the regional Point of Presence (POP).

By April 2001, the Group was interconnected to the 18 regional MSUs and to the 119 LXs in the Paris urban area, thereby covering all of mainland France, mainly through the leasing of optical fibers at the MSU level and of bandwidth capacity for the national transport of data.

4.4.2.2 Phase 2: April 2001 – August 2002: Interconnection at a number of digital local exchanges outside Paris and upgrading for voice traffic routing

The second phase of development focused on increasing the density of the Group's network by interconnecting it to a greater number of LXs in order to reduce the level of interconnect charges payable to France Télécom.

Through the conclusion of IRU agreements with several operators, including in particular the company Louis Dreyfus Communications ("LDCom"), Free was able, beginning in April 2001, to begin taking delivery of dark optical fiber pairs contained in cables laid by LDCom in fifteen regional towns and cities and of several dark optical fiber pairs in cables laid in the sewers of Paris.

This second development phase was a fundamental stage in the development of the Group's network as it exists today. The principal benefit of these optical fibers is that they provide Free with a high level of density at the urban level and enable it to interconnect at a lower hierarchical level in the France Télécom network, i.e. at the LX level rather than the regional MSU level. This closer proximity to its subscribers has considerably reduced the recurring interconnection charges paid by Free to France Télécom. During this phase, Free's teams worked on the highly complex task of taking delivery of each pair of dark optical fibers in France Télécom's digital local exchanges and installing optical equipment (Add/Drop Multiplexers (ADM)) to enable these fibers to carry data (lit fibers).

The Group also decided during this period to enable its network to transport voice as well as data. In addition therefore to the central switch located in the main POP in Courbevoie, Free's teams installed switches in each regional POP. This provided Free with a network capable of transporting both voice and data, a development which coincided with the acquisition of One.Tel. The use of the Cirpack softswitch technical solution helped keep any additional necessary capital expenditure to a minimum compared with the potential profits the Group could obtain from providing a conventional telephone service.

By August 2002, after completion of these operations, Free had regional-level interconnection at the 18 MSUs and local-level interconnection at 208 LXs, covering all of mainland France. This optical fiber network, largely operated under IRU agreements with a ten-year term in the case of metropolitan loops (expiring between 2011 and 2013) and a twenty-five year term in the case of the northern Paris loop (expiring in 2025), can be used to transport both data and voice, permitting the migration of One.Tel traffic (during 2002) and Kertel traffic (since June 2003) to the Group's network and the launch of an ADSL voice service (since August 2003). In order to guarantee the security and independence of the traffic flows, voice and data traffic are processed by different equipment.

4.4.2.3 Since September 2002: Unbundling of the local loop and expansion of the national network

The unbundling of the local loop is the latest major development in the Group's network, allowing the Group to have direct access to its customers. From early in the second half of 2002, Free has been able to design and launch a broadband Internet access offer using an optical fiber network which was already connected to 162 France Télécom sites. End-to-end management of the network allows for a broadband offering along the entire chain linking the subscriber to the World Wide Web.

Although, as of December 31, 2004, Free maintained its interconnections at all 18 MSUs in mainland France and at 225 LXs (including those located within the Paris city limits), it also enjoyed autonomy on a national level as a result of the fifteen-year IRU agreement for the provision of an optical fiber pair which it operates for its own account.

As of April 1, 2005, the Group's network comprises more than 17,000 km of optical fiber, compared with 16,000 km as of December 31, 2004, and 7,135 km as of December 31, 2003. The substantial majority of the network is held pursuant to IRU agreements, Free's preferred method. In June, 2004, Free signed an agreement with Neuf Telecom extending until December 31, 2030 the validity of most of the IRUs it had already concluded. The few sections of the network that are not covered by such agreements are either leased or owned, often in conjunction with joint construction projects undertaken with private operators or local authorities.

In 2004, the Group continued to pursue its policy of developing relationships with local authorities (Garonne Networks, Réseau Pégase in Montpellier, the Reims municipal authority, the agglomeration of Greater Nancy, CA2M in Metz, Réseau Lumière in Besançon, Irisé-Réseau Sipperec, e-tera, the Rennes municipal authority, the Saint-Etienne municipal authority, Manche Numérique, Eiffage Connectic 78, Telcité and Toulouse), with highway concession companies (SAPRR, ASF, Escota) and other network operators (neuf telecom, CompleTel, Electricité de Strasbourg, TDF, Vilais and Est Vidécommunications, etc.), as well as conducting similar negotiations with other local authorities which have decided to develop their own networks.

4.4.3 Other network elements

Network security

The Group's network is built on a secure architecture, using stable, proven technical and software solutions which have been scaled to absorb significant growth in the number of customers and to accommodate the foreseeable increase in value-added services generated by broadband. The network is monitored 24 hours a day, seven days a week by a dedicated and multi-skilled team.

The network is mainly arranged in a loop configuration, allowing data to be transmitted from either side of the loop. If the network fiber on one side of the loop is interrupted, traffic will continue to be routed from the other side. Moreover, the data and equipment (Nokia switch and data back-up equipment) are duplicated at two different sites, allowing the network to remain functional even if one site suffers a technical fault. Finally, a preventive and corrective maintenance contract is provided as part of each IRU agreement pursuant to which the operator owning the fibers undertakes to remedy any problems which may arise in a timely manner.

Firewalls are installed to protect the network architecture against attacks. The server platform is connected to the switched and ADSL access networks via the Group's IP transport network.

The Group has developed its server platform to run mainly on "open" software such as Linux in order to provide a range of services including web services, search engines, communication services, games, personal pages, news and email. The Group manages its databases, customers, sales, billing and customer accounts using software developed in-house based on Linux architecture.

Peering

One year after the launch of its network, Free set up the FREEIX system for the free exchange of traffic between Internet service providers (access and hosting) at multiple points called "peering points". These peering points use Cisco and Extreme Network infrastructure and allow exchanges between close to forty Internet service providers, providing a high level of Internet connectivity in France. Free is also connected to the SFINX peering point (1 Gigabyte) and operates several multi-Gigabyte private peering connections.

The Group has decided to reinforce its peering capabilities in Europe by being present on several new exchange points. In particular, the Group has purchased fiber IRUs connecting Paris to London, Amsterdam, Brussels and Frankfurt.

International transit

As of December 31, 2004 for international transit, Free uses the services of three transit service providers offering bandwidth capacity of more than 10 Gigabits per second: Opentransit (France Télécom International), Telia (Telia-Sonera Group) and Sprint.

Server platform

All Free's servers run on a Linux operating system, which is a well-established system used by many Internet-based companies.

Free's Linux-based infrastructure consists mainly of Dell 1U PC servers installed at its various POPs. Free uses Network Appliance file servers for data storage.

4.5 DESCRIPTION OF THE COMPANY'S MAIN BUSINESS ACTIVITIES

4.5.1 Internet access

4.5.1.1 Free

Free is the second largest broadband Internet access provider in France and one of the few such providers to have become profitable through the provision of ISP services. Free first posted a profit in April 2001, only 24 months after the start-up of its business.

Today, Free has three different Internet access offerings, characterized by their simplicity, attractive pricing and recognized technical quality and which provide tools allowing subscribers to take full advantage of the Internet's many features, including portals, search engines, email, personal website construction tools and account management tools. These three offerings consist of the "Pay-as-you-go" service, the "50-hour plan" and Free's broadband offering.

Free initially based its growth strategy on the provision of non-subscription access to the Internet ("Pay-as-you-go" access) offering a limited range of content. Its marketing strategy was based on minimizing advertising expenditure and emphasized the simplicity and low cost of the offering. This strategy was successful, with Free now claiming nearly three million user-created email addresses.

After completing the roll-out of its telecommunications network and interconnecting with the France Télécom network in April 2001, Free was in a position to control the cost structure of an offering based on Internet connection time. Free therefore launched an attractive and profitable dial-up package, charging a fixed rate of €14.94 for 50 hours of Internet usage per month.

With 143,500 "50-hour plan" subscribers as of December 31, 2004 (compared with 215,000 as of December 31, 2003), Free has capitalized on the different nuances of its brand name, transforming it from a name implying that the offering is free of charge into a name associated with high-quality paid services and the freedom offered to users of these services.

This new brand image was enhanced with the launch in October 2002 of Free's ADSL broadband offering for €29.99 per month. Through the use of its network and by building on its experience in dial-up offerings, Free has developed a high-quality broadband access offering which is attractively priced and, where possible, which makes the most of the opportunities afforded by the unbundling of the local loop.

Free's offerings are pertinent to all Internet user segments and have different maturity profiles, with some subscribers migrating from one offering to another (such as from the "Pay-as-you-go" service to the "50-hour plan" and from the "50-hour plan" to the Free broadband offering). The flat growth of the "50-hour plan" offering and the slight decline in the "Pay-as-you-go" offering are more than offset by strong growth in the broadband offering.

The following tables give details of all the Internet access services marketed by Free.

Details of Internet access services provided by Free as of April 1, 2005

“Pay-as-you-go”	“50-hour plan”
	€14.94 per month, including VAT
<ul style="list-style-type: none"> • No subscription/no commitment access via PSTN or Numéris (cost of telephone call billed by France Télécom) • An unlimited number of email addresses • 1 Gb of space for hosting the customer’s personal website • Specific tools enabling customers to manage and customize their websites 	<ul style="list-style-type: none"> • 50 hours Internet usage per month with no minimum contract period • An unlimited number of email addresses • The least expensive charge per additional minute on the market (local Internet call rate) • 1 Gb of space for hosting the customer’s personal website • Specific tools enabling customers to manage and customize their websites

Free's Broadband Service Offering																											
€29.99 per month, including VAT																											
Option 1 (Unbundled line)*	Option 5*																										
<ul style="list-style-type: none"> Unlimited usage for a fixed price – up to 20 Mbits per second download rate and 1 Mbit per second upload Freebox modem provided to subscribers free of charge No minimum contract period Termination charge: €96 maximum including VAT (reduced by €3 for each month of duration of the subscription) Unlimited use of bandwidth Unlimited number of email addresses 1 Gb of space for hosting the customer's personal website Specific tools enabling customers to create and manage their websites Ability for customers to be entirely independent of France Télécom's subscription in the case of full unbundling In the case of migration from partial unbundling to full unbundling: migration charge of €90 including VAT (reduced by €3 for each month of duration of the subscription to Free's broadband service) Access to telephony services and audiovisual content offerings for customers with a Freebox modem: <table border="1" data-bbox="225 947 761 1413"> <thead> <tr> <th colspan="2">Charges for calls made using the Freebox modem</th> </tr> <tr> <th>Type of call</th> <th>Charge</th> </tr> </thead> <tbody> <tr> <td>Local and national</td> <td>Free</td> </tr> <tr> <td>International</td> <td>From €0.03 per minute (billed per second)</td> </tr> <tr> <td rowspan="2">Mobile</td> <td>To Orange and SFR Peak: €0.16/minute Off-peak: €0.05/minute Connection charge: €0.21 per call</td> </tr> <tr> <td>To Bouygues Peak: €0.28/minute Off-peak: €0.13/minute Connection charge: €0.29 per call</td> </tr> <tr> <td>To Freebox subscribers</td> <td>Free</td> </tr> </tbody> </table>	Charges for calls made using the Freebox modem		Type of call	Charge	Local and national	Free	International	From €0.03 per minute (billed per second)	Mobile	To Orange and SFR Peak: €0.16/minute Off-peak: €0.05/minute Connection charge: €0.21 per call	To Bouygues Peak: €0.28/minute Off-peak: €0.13/minute Connection charge: €0.29 per call	To Freebox subscribers	Free	<ul style="list-style-type: none"> Unlimited usage for a fixed price – up to 10 Mbits per second download rate and 320 kbits per second upload Freebox modem provided to subscribers free of charge No minimum contract period Termination charge: €96 maximum including VAT (reduced by €3 for each month of duration of the subscription) Unlimited use of bandwidth Unlimited number of email addresses 1 Gb of space for hosting the customer's personal website Specific tools enabling customers to create and manage their websites Access to telephony services for customers with a Freebox modem <table border="1" data-bbox="857 947 1393 1413"> <thead> <tr> <th colspan="2">Charges for calls made using the Freebox modem</th> </tr> <tr> <th>Type of call</th> <th>Charge</th> </tr> </thead> <tbody> <tr> <td>Local and national</td> <td>Free</td> </tr> <tr> <td>International</td> <td>From €0.03 per minute (billed per second)</td> </tr> <tr> <td rowspan="2">Mobile</td> <td>To Orange and SFR Peak: €0.16/minute Off-peak: €0.05/minute Connection charge: €0.21 per call</td> </tr> <tr> <td>To Bouygues Peak: €0.28/minute Off-peak: €0.13/minute Connection charge: €0.29 per call</td> </tr> <tr> <td>To Freebox subscribers</td> <td>Free</td> </tr> </tbody> </table>	Charges for calls made using the Freebox modem		Type of call	Charge	Local and national	Free	International	From €0.03 per minute (billed per second)	Mobile	To Orange and SFR Peak: €0.16/minute Off-peak: €0.05/minute Connection charge: €0.21 per call	To Bouygues Peak: €0.28/minute Off-peak: €0.13/minute Connection charge: €0.29 per call	To Freebox subscribers	Free
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To Freebox subscribers	Free																										
<table border="1" data-bbox="220 1507 750 1664"> <thead> <tr> <th colspan="2">Audiovisual content offerings</th> </tr> </thead> <tbody> <tr> <td>Unscrambled general interest or public service channels</td> <td>Free</td> </tr> <tr> <td>Pay channels and packages</td> <td>From €0.25 per month</td> </tr> </tbody> </table>	Audiovisual content offerings		Unscrambled general interest or public service channels	Free	Pay channels and packages	From €0.25 per month																					
Audiovisual content offerings																											
Unscrambled general interest or public service channels	Free																										
Pay channels and packages	From €0.25 per month																										

* subject to the eligibility of the line for ADSL

Dial-up Internet access offering

The "Pay-as-you-go" offering

In April 1999, Free entered the Internet service provider (ISP) market with a simple, no-subscription service. This commercial strategy was at first based solely on providing "Pay-as-you-go" access and enabled Free to win a large share of the dial-up market with relatively small advertising outlay as compared to its competitors.

With this type of offering, the customer pays France Télécom for the telephone call while using the Internet at the local Internet call rate. France Télécom then repays approximately 98% of the average revenues generated to Free. The economic model for this type of service is therefore based entirely on repayments by France Télécom.

With nearly 133 million minutes of connection time generated by “Pay-as-you-go” customers per month in 2004, this dial-up service remains a profitable business for the Group, despite a slight decrease in revenues (see paragraph 5.2.2).

The “50-hour plan”

Following the appearance of fixed-rate packages on the Internet access market and once Free was able to control the cost of providing telecom minutes following the completion of the first phase of the roll-out of the Group's network, Free decided in April 2001 to launch its own fixed-rate service whose main selling points were its reasonable price (€14.94 per month) and the significant number of usage hours offered (50 hours). The “50-hour plan” was therefore designed to complement and serve as an alternative to the “Pay-as-you-go” offering for users wishing to access the Internet for long periods of time at the lowest possible price. This fixed-rate package is still one of the most attractively priced on the dial-up market, but is suffering from competition from the unlimited broadband offerings, particularly in the case of subscribers whose Internet usage approaches or exceeds 50 hours per month.

Broadband Internet access offering

Free's broadband service is based on two modes of access referred to by the ART as “Option 5” (subscribers on lines that have not been unbundled) and “Option 1” (subscribers on unbundled lines).

- *Option 5.* Under Option 5, the ADSL subscriber's traffic is delivered directly to the Internet service provider's main server center through regional server centers by France Télécom. In this case, the Internet service provider is dependent on France Télécom for access and for the collection of all the traffic. Since March 18, 2004, a Freebox has been provided by Free to each new subscriber, free of charge.
- *Option 1.* Under Option 1, or local loop unbundling, a Freebox DSLAM is installed in France Télécom sites and a Freebox modem is installed on the subscriber's premises. With this configuration, the Group leases the copper pair for transporting Internet traffic from France Télécom. The “high” frequencies are entirely at the alternative operator's disposal for routing data, voice and audiovisual content. ADSL traffic can thereby be managed from end to end by the Group. In the case of partial unbundling, France Télécom's role is restricted to leasing the equipment between the Freebox modem installed on the subscriber's premises and the Freebox DSLAM, plus the initial wiring installation. In the case of full unbundling, the subscriber no longer has any link to France Télécom.

A further increase in bandwidth was implemented in the autumn of 2004, with the launch of version 4 of the Freebox modem and of the upgraded DSLAM, both of which now use ADSL 2+ technology (see the paragraph entitled “ADSL 2+ services” below).

This increase in bandwidth was provided to customers without any increase in the price of their subscription, and therefore has not had any impact on the Iliad Group's profit margin.

Free's profit margin from its €29.99 per month broadband offering varies significantly according to whether the customer is an Option 1 (unbundled) customer or an Option 5 (not unbundled) customer (for further information, see paragraph 5.2.1.2 below). Therefore, Free's objective, while still continuing to increase its market share with both its Option 1 and Option 5 offerings, is to offer Option 1 directly to new subscribers in unbundled local loop areas and also to migrate existing Option 5 subscribers to the Option 1 configuration.

Freebox

The Group has chosen to develop its own broadband Internet upload and download equipment in-house in order to win as many new customers as possible in a competitive and fast-growing market by providing differentiated service offerings. As a result of the technological resources of the development team at Freebox S.A. and a very

selective purchasing policy, the Group has been able to optimize the cost of designing a DSLAM and a modem capable of meeting the high bandwidth requirements necessary to offer high value-added services. The use of both a Freebox DSLAM and a Freebox modem enables Free to provide its customers with a first rate technical service offering capable of transmitting bandwidth-intensive voice, data and audiovisual content simultaneously and over long distances ("Triple Play" service offering).

The Freebox DSLAM. The DSLAM developed by Freebox S.A. is configured to optimize the existing Free network and guarantees each subscriber a theoretical download rate of up to 25 Mbits per second (with the latest version) from the local concentrator. Each Freebox DSLAM, installed in racks which can hold up to four DSLAMs, can be connected to 384 lines and is designed to leverage the Free network which uses only IP protocol, unlike conventional transmission networks which use ATM/SDH protocol. The latest version of the DSLAM can be connected to 1,000 lines. The Freebox DSLAM has a Giga Ethernet output and was designed to accommodate the high bandwidth requirements of the new audiovisual services launched in December 2003.

The Freebox modem. The Freebox modem is a multi-function ADSL modem developed to enable customers to receive services that can be offered via broadband Internet access. In addition to traditional access using a personal computer connected via a USB or Ethernet socket, the Freebox modem has one telephone socket for voice-over-DSL services and a Peritel TV socket and is capable of decoding audiovisual content compressed in MPEG-2 format.

The Freebox modem and the Freebox DSLAM include components acquired from third party suppliers and assembled by companies which are not part of the Group. However, the software used has mainly been developed in-house by the Group using open software such as Linux.

The use of both the Freebox modem and the Freebox DSLAM allows Free to provide its customers with the best in ADSL and ADSL 2+ technology as well as a very high theoretical bandwidth (up to 25 Mbits per second) while reducing the loss of bandwidth over distance. Free has been using this high bandwidth capacity since December 2003 to offer high value-added services such as audiovisual services over ADSL (MPEG-2 format) and voice services, as well as, since October 2004, high-speed Internet access (up to 20 Mbits per second).

In conclusion, Free's unbundled service offering enables the company to have complete control over the network from end to end and thereby over the transmission of traffic and the quality of its services, with:

- a presence on the subscriber's premises in the form of a Freebox modem;
- a presence in the France Télécom sites in the form of the Freebox DSLAM;
- optical fibers between the France Télécom sites and Free's regional POP; and
- optical fibers between Free's regional POP and the Free server center.

The ADSL 2+ service offered to subscribers with a Freebox V4 modem

On October 20, 2004, Free announced the launch of the first ADSL 2+ service in France, using the Freebox V4 modem and offering transmission rates of up to 20 Mbits per second, provided that the line is technically capable of supporting this. The implementation of ADSL 2+ requires the installation of the upgraded version of the DSLAM.

Telephone service offered to subscribers with a Freebox modem

Since August 25, 2003, Free has been offering a voice-over-ADSL (VoDSL) service to all its subscribers with a Freebox modem, enabling them to make and receive calls over a fixed-line telephone connected directly to their Freebox modem. In order to receive this service, the Freebox subscriber applies for a new telephone number on Free's website. Free is the first operator in France to provide this type of offering. Based on a policy of per-second billing and a very attractive per-minute tariff, Free's telephony service is very attractive not only for local and national calls, which are free, but also for international calls and calls to mobile phones (see the tables on pages 36 and 50 hereof for details of the telephone service provided through the Freebox modem). The availability of this service to Freebox subscribers is a result of both the upgrading of the Group's network since

2002 to allow it to carry voice traffic and also the development of a billing system following the takeover of One.Tel, as well as the company's skill in designing the Freebox DSLAMs and modems.

Since March 18, 2004, as shown in the table entitled "Details of Internet access services provided by Free" above, each new subscriber (Option 1 or Option 5) has been provided with a Freebox modem free of charge and benefits from the ADSL telephony offering which includes free local and national calls to fixed telephones in mainland France.

Since August 24, 2004, Free has offered its subscribers with a Sagem modem the opportunity to replace their Sagem modem with a Freebox V4 modem, for a small charge, in order to be able to benefit from the ADSL telephony service, and, since November 2004, it has also offered to replace subscribers' old generation Freebox modems with a Freebox V4, so that they can benefit from ADSL 2+ technology.

Audiovisual content offered to subscribers with a Freebox modem

At the end of November 2003, Free launched an audiovisual content service available from the end of December 2003 free of charge to all subscribers with a Freebox modem in an unbundled local loop area. This offering allows subscribers to receive free-to-air general interest or public service channels, as well as pay channels and packages from €0.25 per month by linking the Peritel socket of the Freebox modem to their television.

These programs are transmitted in MPEG-2 format at a rate of 3.5 Mbits per second. The use of Multicast technology prevents an overload of the network, as the capacity used is the same regardless of how many subscribers are watching the same channel simultaneously.

Pursuant to the terms and conditions of the non-exclusive distribution agreements between the Group and the audiovisual content providers, Free takes responsibility, without charge, for encrypting and transmitting the audiovisual channels and packages. The Group invoices subscribers directly for pay channels and packages and remits the bulk of the invoiced fees to the content providers (with the exception of channels in the Canal+ Group).

During 2004, Free continued to expand its range of audiovisual content and services, and on September 17, 2004, announced the signature of a distribution agreement with the Turner Group for the channels CNN and Boomerang, and then, on November 24, 2004, another with the Canal+ Group relating to its premier channel Canal+ and its digital offshoots, as well as the Canal SatDSL bouquet of channels.

4.5.1.2 Online

Online was created in 1999 and now manages more than 77,000 Internet domains (compared with 55,000 at the end of 2003), making it the second largest provider of shared web hosting services in France. Its core customer base consists of small office/home office (SOHO) customers, and small and medium-sized businesses which wish to benefit from a cost-effective solution for hosting their websites.

Following its merger in December 2003 with its subsidiary BookMyName, a company accredited by the Internet Corporation for Assigned Names and Numbers (ICANN) for the registration of Internet domain names, Online is now also a domain name registrar.

In practice, Online's service offering consists of hosting its customers' domain name in its Domain Name Systems (DNS) and providing the associated disk space, as well as managing the hosted space. The customer pays a rental charge based on the type of hosting service chosen and may choose its own website address. Online's hosting and registration offerings are presented below:

Online's web hosting and domain name registration services as of April 1, 2004 (extracts)

Hosting	Disk space	Charge (excl. VAT) per year (in euros)	Options
<i>Service offerings</i>			
XS	100 kb	0.00(*)	Upgrade only
M	100 Mb	29.90	All
L	250 Mb	59.90	All
XL	500 Mb	119.90	All
XXL	1,024 Mb	239.90	All
<i>Options</i>			
10 additional email accounts	Per account/year	20.00	
Secure payment.		100.00	

(*) This offering is subject to conditions and is only available for ".com", ".net" or ".org" domains. On purchase of a domain name, XS hosting is free. For domains transferred to the XS service, the charge is €5 excluding VAT per year.

Domain name registration (examples)		Charge excl. VAT (in euros)	
Domain	Duration	Purchase cost	Renewal
.com	1 year	6.95	9.90
.fr(*)	1 year	19.00	19.00

(*) Certain ".fr" domain names are subject to special terms and conditions of purchase.

Once the customer has been allocated web space by Online, the customer is responsible for creating its website content using the website construction and management software provided by Online. The customer is therefore completely free to choose its website content, provided such content complies with all current national and international laws and regulations, particularly those concerning intellectual property and copyright, and does not contain any material which may be considered derogatory, defamatory, offensive or subversive of public order or which could result in an invasion of privacy.

As part of its hosting services, Online also provides its customers with email addresses, email aliases and email forwarding services, the number of which will vary according to the subscription package chosen by the customer.

4.5.1.3 Centrapel: a technical support and customer service platform used by all Group companies

Free, One.Tel and Kertel offer their customers technical support and customer service through a helpdesk platform installed in the Group's offices in Paris and run by a Group subsidiary, Centrapel S.A. The Group is currently in the process of expanding and training its technical support and customer service teams. Centrapel seeks to recruit operators who have completed two years of post-baccalauréat level studies or who have experience working in technical support for an ISP, and is also investing in providing training for its operators. All new employees are therefore given one month's training in support techniques before starting work answering customer calls. As of December 31, 2004, Centrapel employed 617 people compared to 343 as of January 1, 2004. This support service operates from 8 a.m. to 10.30 p.m. Monday to Friday and from 9 a.m. to 8 p.m. on weekends and public holidays. A dedicated helpline for fully unbundled customers was brought into service at the beginning of 2005.

Centrapel's support team includes approximately fifty employees based in Paris and elsewhere in France responsible solely for dealing with problems related to local loop unbundling (relations with France Télécom, migration of lines, etc.).

Centrapel also provides Free's customers with an online support service available through Free's website. This service provides answers to user FAQs and allows Free's customers to email specific questions to the support service.

With a view to reducing customer churn and contributing to the Group's customer loyalty policy, Centrapel uses high-quality software tools developed in-house by the Group's IT team. These tools are used for monitoring customer relationships, handling faults and maintaining a log of problems encountered by Free's customers. This customer loyalty policy is part of the Group's strategy to improve customer service resources and to provide advice to customers who may wish to upgrade to other services provided by the Group.

4.5.2 Telephony segment

The Group's telephony business is centered around the fixed telephony operator One.Tel acquired by the Group in 2001 and the call termination business operated by Kedra, and was expanded during 2003 with the acquisition of the prepaid phone card provider Kertel. In a market dominated by large players, the Group has managed to develop a sustainable and profitable business largely due to the economies of scale offered by the use of its own network.

4.5.2.1 One.Tel

The fixed telephony operator One.Tel France SAS ("One.Tel") was established in 1998, but was placed in administration in June 2001 largely as a result of the financial difficulties encountered by its Australian parent company. One.Tel was acquired by the Group in December 2001 as part of its business continuity plan and the One.Tel trademark was licensed to the Group for ten years by the British company Centrica Telecommunications Ltd., the successor in interest to One.Tel (UK).

The restructuring plan carried out after the takeover involved the migration of One.Tel's voice traffic to the Group's network during the first half of 2002, improving the business's gross margin, and the changeover from One.Tel's old billing system to the existing billing and customer tracking system developed by the Group's engineers.

Since its takeover by the Group, One.Tel has implemented a procedure for optimizing the cost of winning customers and managing its customer base by recommending that all new customers provide bank details before any new connection to the service, thus allowing for payment by direct debit. This measure, together with the in-house development of an efficient billing system and heavy promotion of the use of carrier preselection, automatically ensuring that customers' calls use the Group's network, contributes to a high bill collection rate and increases customer loyalty.

On a commercial level, as in the case of the Group's Internet access offerings, One.Tel launched a very competitive and simple offering in September 2002 at just one eurocent per minute for local and national calls (see detailed pricing in the table below). For international calls, One.Tel benefits from its past experience as part of a multinational group in its negotiations with the leading international telecommunications operators. One.Tel is interconnected with several international operators and with two trading platforms for buying and selling international call minutes, which enables it to offer both competitive rates and a high level of quality for all its call destinations.

As a result of a more aggressive and better targeted marketing strategy, the number of billed customers has increased from 215,000 as of December 31, 2003 to 335,000 as of December 31, 2004, i.e. an increase of almost 56%. One.Tel's fixed telephony offering is both simple and attractively priced. The following table compares the One.Tel offering with that of its main competitors, and should be read together with the table shown in paragraph 4.6.3.

**One.Tel tariff offering for carrier preselection calls as of April 1, 2005 (extracts)
(in euros including VAT per minute)**

Type of call	Connection charge or minimum charge per call		Charge per minute	
	<i>Peak</i>	<i>Off-peak</i>	<i>Peak</i>	<i>Off-peak</i>
<i>Calls to fixed lines</i>				
National call		0.11		0.01 ⁽¹⁾
Local call	0.10	0.09		0.01 ⁽¹⁾
<i>Calls to GSM mobiles</i>				
To Orange and SFR	60 seconds billed 0.30 ⁽²⁾	50 seconds billed 0.23 ⁽²⁾	0.22	0.08
To Bouygues, Spot and Nomad		50 seconds billed 0.29 ⁽²⁾	0.32	0.16
<i>International calls</i>		0.11		From 0.06

(1) Billed per second from the first second; rate for calls from a preselected One.Tel phone towards a fixed phone in mainland France, with payment by direct debit.

(2) Billed per second after the minimum charge.

Since the first half of 2003, in addition to One.Tel's service offering, the Group has provided a telephony service to small and medium enterprises under the name Iliad Telecom.

4.5.2.2 Kertel

The acquisition in 2003 of the prepaid phone card provider Kertel from the Pinault-Printemps-Redoute Group was another facet of the Group's strategy for optimizing its network, particularly on the basis of the synergies developed with One.Tel and Kedra. These synergies have allowed the Group to benefit from shared experience and know-how in such matters as billing and rate negotiations, especially for international rates.

Kertel is a leading provider of prepaid phone cards in France. Its strategy of focusing on this single sector of activity has borne fruit and Kertel sold more than 7.5 million cards in 2004, compared with 4.9 million in 2003.

Kertel sells its products nationwide through the largest distribution network in the market, and the brand is well known in France. Kertel cards are sold in more than 40,000 outlets such as post offices (on the basis of the distribution agreement signed between the company and the French post office, La Poste), tobacco stores (under the terms of a distribution agreement with the French tobacco company Altadis and the Société Pipière Française) and the Relay newsstand chain, as well as a large number of local shops (gasoline stations, grocery stores, etc.) and large chain stores (Carrefour, Casino, Monoprix, Fnac, etc.).

On a commercial level, the difference in call charges between prepaid phone cards sold by Kertel and the France Télécom smart card was as high as 80% for certain call destinations as of December 31, 2004.

Group management believes that by further increasing its distribution network, Kertel will be in a position to further enhance its competitive position in the prepaid phone card market.

4.5.2.3 Kedra

Since 2002 Kedra has been offering a low-cost fixed telephony call termination service. The philosophy behind this service is similar to the "call-back" system which, since the early 1990s and particularly in the United States, has resulted in a significant drop in the cost of international calls. The service, aimed at fixed telephony carriers in general and at the Group's subsidiaries providing telephony services in particular, transfers at a minimal cost calls destined for certain operators which charge high prices. When a subscriber calls one of these operators, the call is forwarded to the Kedra platform which connects it directly to the telephone operator called, but at a lower cost than would normally be charged, thus allowing the customer to benefit from the decreased mark-up.

Kedra charges the Group companies offering telephony services for its services. It also sells minutes to other alternative operators. Kedra's profits are therefore largely based on margins earned on contracts with operators outside the Group.

4.5.3 “Other Services” segment

The “Other Services” segment mainly consists of the Minitel-based reverse look-up directory service, which historically has been one of the most profitable of the Group’s services. Before it sold almost all Minitel services in its portfolio in 1998, Minitel services provided by the Group were the main source of its internally-financed growth. This segment also includes the Group’s subsidiaries Assunet and the company Société S.A. which offer web content services to their customers.

4.5.3.1 ANNU

The Minitel-based reverse look-up directory, ANNU, was launched by Iliad in 1996. This service, which is widely known in the consumer market, allows users to find a name and address associated with a telephone or fax number, either via Minitel, telephone, Internet or SMS text messaging.

Based on an easy-to-use electronic data transmission solution, the ANNU service uses the directory database established and maintained by France Télécom in return for the payment of an annual charge to the incumbent operator. In 2002, France Télécom invoiced €3.35 million in respect of this charge. In 2003, following decisions issued by the French competition authority, the *Conseil de la Concurrence*, and the ART, Iliad obtained a significant reduction in this charge, which was fixed at €180,000 per year. Iliad has also demanded the reimbursement of the charge invoiced for fiscal year 2002 and previous years.

ANNU uses the standard pricing model for Minitel services (payment of €0.84 per minute of usage) or Audiotel services (payment of the equivalent of a local call charge from a fixed-line telephone).

In spite of efforts to promote new ways of using the reverse look-up directory (text messaging, mobile telephony or Internet), the Group considers that the decline in the use of Minitel in France is irreversible and, in the medium term, is likely to result in a significant loss in revenue from this business.

Furthermore, the Group’s reverse look-up directory is faced with strong competition from France Télécom, which has launched its own reverse look-up directory service (3617 QuiDone). The combined effect on Iliad’s earnings of this increase in competition and the decline in the use of Minitel in France has been significant, resulting in a decrease in revenues from ANNU of approximately 30% for 2004 compared to 2003.

Despite the fall in revenue from Minitel services and competition from the incumbent operator, the Group plans to continue this profitable activity as long as possible, as it requires little in the way of human resources or capital expenditure, although the Group will take into account in its forecasting the foreseeable reduction in earnings from its reverse look-up directory service.

4.5.3.2 E-commerce business

Iliad operates two web content sites, Assunet.com and Société.com, which account for only a very minor proportion of the Group’s revenues. These two companies were restructured in 2001. Société.com currently has positive operating results, and Assunet.com is approaching positive operating results.

Assunet.com

Assunet is a web-based insurance broker which provides an online quotation search engine service allowing its customers to obtain quotes online from fifteen major insurance companies. The customer enters his or her request on the Assunet site, free of charge, and Assunet immediately responds with the three most attractive quotes based on the coverage and deductible levels in accordance with the customer’s profile and requirements.

Société.com

Société.com provides information about companies, such as entries, amendments and removals from the French Trade Register.¹ The Société.com website also provides access to a number of documents which can be ordered and paid for in a number of different ways.

¹ Source: INPI.

4.6 THE GROUP'S MARKETS AND COMPETITIVE POSITIONING

4.6.1 Internet access

DETERMINING FACTORS IN THE GROWTH OF INTERNET USAGE IN WESTERN EUROPE

In Western Europe, following a period of very strong growth in the level of Internet usage, particularly as a result of so-called "free" services followed by the introduction of fixed-rate inclusive packages, the prospects for further growth now partly depend on the roll-out of broadband technologies. The market should continue to grow during 2005, largely due to:

the level of penetration of home computer use. The use of home computers is a key element in the development and expansion of the Internet access market. Western Europe is still not at the same level as the United States, which is a far more mature market, although the disparity is decreasing. There are still considerable disparities within Western Europe itself;

the use of new technologies offering both broadband Internet access (such as ADSL and cable) and the widespread distribution of new types of content (such as TV, video on demand, network gaming, etc.);

a significant drop in the cost of Internet access, bringing it within the reach of the general public;

the growth and general improvement of local language content and e-commerce;

increased liberalization and competition in the telecommunications sector;

the commitment on the part of the authorities towards promoting ever-wider usage of the Internet.

The broadband market: an excellent basis for growth

With 6.1 million ADSL lines as of January 1, 2005¹, France is one of the frontrunners among European countries in terms of both the number of ADSL lines and market penetration. Approximately one household in four now has a broadband Internet connection. In 2004, the growth of the French market approached 100% for the third year running. As of January 1, 2005, France ranked second in Europe, behind Germany, in terms of the number of unbundled lines.

Countries with a high rate of Internet penetration continue to attract new users, but from now on the main driver for growth in this market will be the migration of subscribers to broadband connection technologies.

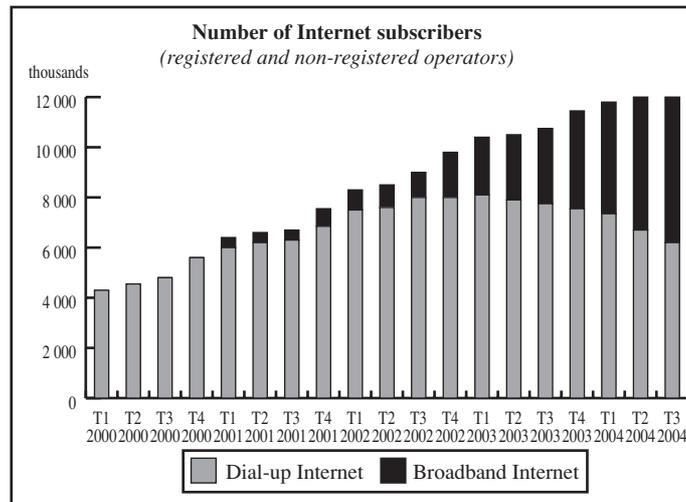
Choice of broadband technology

The predominance of one broadband connection technology over another varies from country to country. In Western Europe, ADSL appears to have become the technology of choice, accounting for 80% of the broadband access market. In France, ADSL has established itself as the primary technology used for broadband access, accounting for more than 92% of all broadband connections².

¹ Source: ART

² Source: ART

Number of Broadband/Dial-up Internet Subscribers in France
(Q1 2000-Q3 2004)



Source : ART

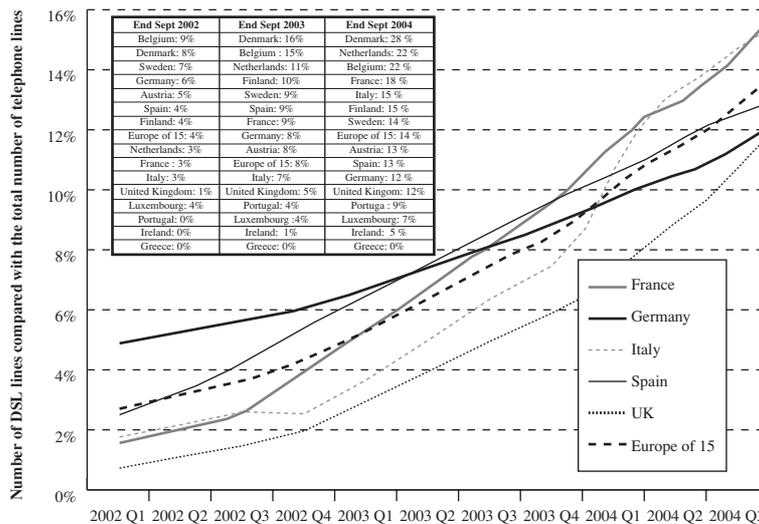
Broadband penetration rate in Europe – still enormous potential in France

The number of DSL and cable modem connections in Europe doubled during 2004. The northern European countries are generally ahead of other European countries in terms of penetration of broadband technologies, particularly due to the early deregulation of the telecommunications sector, as was the case in Sweden (deregulated in 1993), as well as a high level of commitment on the part of the public authorities.

According to the ART, in the second half of 2004 broadband continued to develop rapidly in most European countries, among which the French market appears to be flourishing, with the largest growth in Europe over the last six months.

Broadband penetration rate

(expressed as the proportion of the number of DSL lines to the total number of telephone lines)



(source ECTA et extrapolation linéaire pour les trimestres manquants)

Source : ART

Table inside graph:

End Sept 2002	End Sept 2003	End Sept 2004
Belgium: 9%	Denmark: 16%	Denmark: 28%
Denmark: 8%	Belgium: 15%	Netherlands: 22%
Sweden: 7%	Netherlands: 11%	Belgium: 22%
Germany: 6%	Finland: 10%	France: 16%
Austria: 5%	Sweden: 9%	Italy: 15%
Spain: 4%	Spain: 9%	Finland: 15%
Finland: 4%	France: 9%	Sweden: 14%
Europe of 15: 4%	Germany: 8%	Europe of 15: 14%
Netherlands: 3%	Austria: 8%	Austria: 13%
France: 3%	Europe of 15: 8%	Spain: 13%
Italy: 3%	Italy: 7%	Germany: 12%
United Kingdom: 1%	United Kingdom: 5%	United Kingdom: 12%
Luxembourg: 4%	Portugal: 4%	Portugal: 9%
Portugal: 0%	Luxembourg: 4%	Luxembourg: 7%
Ireland: 0%	Ireland: 1%	Ireland: 5%
Greece: 0%	Greece: 0%	Greece: 1%

A thriving broadband market in France

According to the ART, as of September 30, 2004, France had a household broadband penetration rate of 16%, for the first time above the European average (14%). As of January 1, 2005, France Télécom had delivered 893 sites to unbundling operators, which represents a population coverage of more than 50%. Only 6 local districts remain without a single unbundled site. All the overseas dependencies have at least one unbundled site. There is likely to be accelerated growth in France in terms of the number of households with broadband access, which means that prospects are healthy for the Group in light of its positioning in this sector of the market.

Players on the Internet access market in France

In France, as in the rest of Europe, after a period in which there was a proliferation of access providers in the market, the Internet service provider market has matured. Incumbent operators have made up for initial lost ground and have reestablished their positioning in their domestic markets. At the same time, a wave of consolidation and concentration has reduced the overall number of players in the market.

The Group's main competitors in the French access market are:

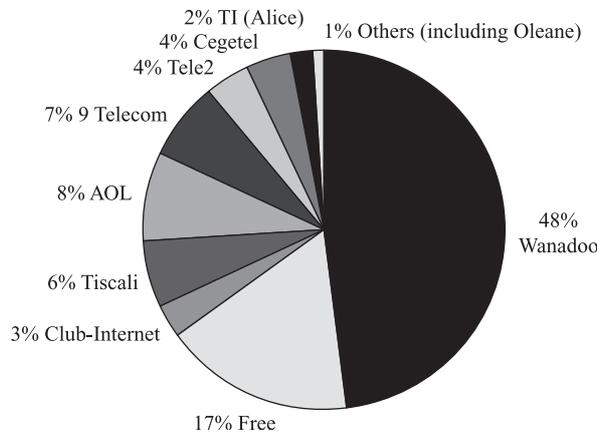
international Internet service providers, some of which are partnered with telecommunications operators, such as Wanadoo, AOL, TOnline.net (Club-Internet), Tiscali, Telecom Italia and neuf telecom;

companies operating cable networks (Noos);

independent local access providers; and

companies offering Internet access as a means of winning customers for their services, such as banks and mass-marketing companies.

**Market share of leading ISPs
in the ADSL sector (December 31, 2004)**



Source: France Telecom, Iliad and other ISPs

The launch of so-called “free” Internet in France was the driving force behind the growth of the residential market, and Free rapidly positioned itself as a leading player in this sector. With the introduction of fixed-rate inclusive packages at the end of 1999, this type of service became increasingly popular and established itself as the core of the dial-up Internet sector. Today, the “pay-as-you-go” or “free” services are showing a slight decline while subscription offerings are relatively stable.

Since mid-2002, most of the Group’s main competitors have decided to focus on providing ADSL-based broadband offerings. The proliferation of different service offerings accompanied by increased segmentation and strong competitive pressure stimulated growth in the Internet market during 2003 and 2004.

Since the end of 2002, local loop unbundling has provided a major opportunity for growth for the Group, particularly with regard to profitability and the development of service offerings (such as fixed telephony and audiovisual services).

In addition to pursuing market growth for broadband access in order to increase broadband use in the home as a means of winning new customers, Internet service providers also aim to migrate as many subscribers as possible from dial-up services to broadband in order to benefit from higher average revenue per user.

4.6.2 Website hosting and sale of Internet domain names

Online’s business covers both the web hosting market and, since the merger between Online and its subsidiary BookMyName, the sale of domain names.

The web hosting market is highly competitive, as demonstrated by the very large number of web hosting and service providers in the market (approximately 200). According to the OECD, Online.net ranks with sites such as ovh.com, lerelaisinternet.com, amen.fr and transpac.fr as one of the best known Internet hosting sites. The fragmentation of competition in this sector has resulted in a wide range of pricing according to the size of the site to be hosted, the services provided (telephone support, dedicated server, forums, multiple simultaneous connections, etc.) and the expected number of visitors to the site.

The more specialized business of domain name sales is also subject to intense competition, and includes a number of specialist players such as gandi.net, joker.com and nsi.com, as well as most Internet service providers which offer web hosting services, such as Wanadoo or Tiscali.

4.6.3 Telephony operators

Competition in the fixed telephony market is characterized by the overwhelming dominance of the incumbent operator and by the considerable number of emerging operators.

Telephony

Since January 1, 2002, all subscribers have been able to choose which operator to use for local calls, as had already been the case since January 1, 1998 for long distance and international calls and since November 1, 2000 for calls from fixed-line phones to mobiles. The operator can be selected on a call-by-call basis or else by automatic carrier preselection which allows subscribers to specify that all calls be automatically routed through the operator of their choice. As of September 30, 2004 (Source: ART), 5,200,747 customers had opted for carrier preselection and 2,629,584 for call-by-call selection.

In order to improve its position vis-à-vis its principal competitors (France Télécom, Cegetel, Tele 2, neuf telecom, Omnicom), One.Tel is continuing to encourage its customers to opt for carrier preselection and is firmly positioned as having one of the most attractive pricing structures of any alternative operator in the market.

In 2003, in view of the fact that it was undergoing restructuring, One.Tel did not undertake any major television advertising campaigns, unlike its competitors. However, in light of potential profits going forward, the Group believes that investing in this type of advertising is an important means of promoting the brand and increasing market share.

The following table shows a comparison between the Group's fixed telephony offering and those of its main competitors in France.

The Group's fixed telephony offering compared with its main competitors
(prices in euros, including VAT, per minute as of April 1, 2005, excluding promotions)

Calls made	from the Freebox modem	from a France Télécom line routed by:				
		One.Tel	France Télécom	TELE 2	Cegetel	Neuf Telecom
Local	Free, unlimited	0.01	0.028	0.008	0.013	0.009
Connection charge:						
Peak	None	0.10/call	0.078/call	0.119/call	0.118/call	0.12/call
Connection charge:						
Off-peak	None	0.09/call	0.078/call	0.119/call	0.118/call	0.12/call
National	Free, unlimited	0.01	0.078	0.034	0.013	0.03
Connection charge	None	0.11/call	0.105/call	0.119/call	0.118/call	0.12/call
International						
E.g: United Kingdom	0.03	0.059	0.22	0.06	0.06	0.05
Connection charge	None	0.11/call	0.12/call	0.119/call	0.118/call	0.12/call
Mobiles Orange/SFR						
Peak	0.16	0.22	0.152	0.148	0.17	0.19
Minimum charge	0.21/call	60 sec: 0.30	0.179/call	0.21/call	0.20/call	0.22/call
Off-peak	0.05	0.08	0.079	0.032	0.03	0.03
Minimum charge	0.21/call	50 sec: 0.23	0.179/call	0.21/call	0.20/call	0.22/call
Mobiles Bouygues Telecom						
Peak	0.28	0.32	0.199	0.199	0.17	0.25
Minimum charge	0.29/call	50 sec: 0.29	0.179/call	0.21/call	0.20/call	0.29/call
Off-peak	0.13	0.16	0.099	0.099	0.03	0.07
Minimum charge	0.29/call	50 sec: 0.29	0.179/call	0.21/call	0.20/call	0.29/call
Freebox	Free	Cost of a local call	Cost of a local call	Cost of a local call	Cost of a local call	Cost of a local call

Source: Operators' websites

Prepaid phone cards

France Télécom launched the first prepaid phone smart card (the “*Télécarte*”) in 1987. Prior to 1998, 100 million cards were sold each year. After the initial liberalization of the French market, a number of new prepaid phone card providers entered this market as from 1997-1998 with a PIN-based calling card product line and rapidly gained market share through aggressive pricing and wide distribution networks. During 2000, in response to this competition, France Télécom launched its own line of calling card products (known as the “*Ticket Téléphone*”) as an addition to its *Télécarte* product.

The prepaid phone card market covers two main products:

smart cards: a chip inserted on the front of the card records the remaining credit. This type of card is mainly sold by France Télécom under the *Télécarte* brand and may only be used in phone booths equipped with a special decoder. Today, the market for this product is in sharp decline due to the increasing popularity of PIN-based calling cards;

calling cards: these cards have a unique PIN on the back which corresponds to a prepaid account in the operator's central system. This type of card, sold by Kertel, may be used from any type of touchtone phone, regardless of whether it is a residential, mobile or public phone.

To use PIN calling cards, customers dial a toll free number (3003 or 3031 for Kertel). After entering a 12-digit code, customers can call anywhere in the world.

Kertel has chosen to focus on the PIN calling card market, offering consumers a choice among a complete range of cards:

standard cards for general fixed telephony usage (the main competitors in this segment are France Télécom, Intercall and GTS Omnicom);

geographical or “ethnic” cards aimed at specific regions or communities abroad (the main competitors in this segment are Telecom Center and Leader Communication);

promotional cards provided by advertisers as part of their publicity strategy (such as product launches, promotions and customer loyalty campaigns) which serve as an ideal and widely accessible publicity tool for current or prospective customers.

Kertel's service offering is part of a relatively mature market.

Kertel's main competitor is the incumbent operator. A large number of other phone card providers have entered the prepaid card market, but they do not have as wide a distribution network or as attractive a pricing structure as the France Télécom group.

The Group believes that in view of France Télécom's position in the smart phone card market, where the cost of the *Télécarte* service covers both the cost of manufacturing the smart card and the cost of its phone booths, there is no incentive for the incumbent operator to align its prices with those of its competitors.

4.7 BREAKDOWN OF REVENUES BY LINE OF BUSINESS OVER THE LAST THREE FISCAL YEARS

See paragraph 5.2.2 hereof.

4.8 PRINCIPAL ESTABLISHMENTS

The main premises used for the Group's business are occupied under long-term lease agreements with third parties.

The Group has a long-term lease for a building occupying an area of 5,800 square meters located at 8 rue de la Ville l'Evêque, in the 8th *arrondissement* of Paris, which houses all the Group companies. It also leases premises in the 16th *arrondissement* of Paris which houses technical equipment and is used by one of the Group company's

staff, as well as premises situated at Bezons under a lease entered into on December 11, 2003 (6,900 square meters) and an equipment room in Courbevoie, Hauts-de-Seine, to house its national network hub (1,140 square meters).

4.9 ILIAD'S POTENTIAL DEPENDENCE ON CERTAIN FACTORS

4.9.1 Dependence on patents and software licenses

The Group uses software licenses owned by third parties, particularly software relating to the distribution of audiovisual content. However, the Group also develops its own software and in fact has always given priority to the development of equipment and software (particularly based on so-called "open" software such as Linux) by its research and development teams. For its ANNU service, the Group holds a license to use France Télécom's subscriber database, but believes that there is very little risk of this license not being renewed. Among the trademarks used by the Group's companies, only the One.Tel trademark is covered by a license for use in France, granted in 2001 by the British company Centrica Telecommunications Ltd. for a ten-year term in consideration for an annual fee based on revenues but capped at €250,000. However, Centrica granted the Group exemption from the fee until August 31, 2004.

4.9.2 Dependence on supply, industrial, commercial or financial agreements

Network operated by the Group

Through its subsidiary Free, the Group has concluded agreements granting it Indefeasible Rights of Use ("IRU") relating to the dark optical fibers it uses. Under these long-term agreements, the Group has acquired the indefeasible right to use these fibers for a given period, without having to obtain any right-of-way easements. Most of these agreements were signed with the neuf telecom group and with local authorities. In June 2004, Free concluded an agreement with neuf telecom to extend the term of most of these IRUs until December 31, 2030. The Group considers the risk of non-renewal of these agreements to be very low, in view of the over-capacity of dark fibers already laid by neuf telecom and local authorities.

However, if any of the agreements were not to be renewed, requiring the Group to find alternative solutions, the Group considers that the existence of many alternative operators already offering dark fibers provides satisfactory assurance that a replacement solution could be found before the expiration of the IRU agreements, particularly at the local level where many sections of dark fiber have been laid in recent years.

Furthermore, the Group believes that the IRU agreements reduce the risk of Group liability for damage caused by the fibers of its network. The Group does acknowledge, however, that certain sections of the network which are laid on publicly owned land may be subject to certain restrictions related to the use and occupancy of public property. Finally, in accordance with the provisions of the IRU agreements signed with neuf telecom, neuf telecom and the Group are committed to jointly financing the construction of a new fiber route in the event of physical problems (such as a power failure caused by natural hazards, civil engineering works, etc.) affecting a section of neuf telecom's optical fiber network that is covered by the IRU agreements.

Freebox modem and Freebox DSLAM

The Group uses the services of two equipment assembly companies located in France to assemble the Freebox modem and the Freebox DSLAM with generic electronic components purchased from third party manufacturers. The choice of the components, the construction of equipment and the development of the software used by the Group for its business do not depend on components protected by intellectual property rights such that the Group's growth would be adversely affected were it to be deprived of access to such components. The Group considers the components used in its equipment to be highly standardized and therefore easily interchangeable. In the event of breakdown at the factories responsible for assembling the Freebox modems and DSLAMs, the Group also considers that it could use the services of other equipment assemblers. However, any such substitution of components or assemblers could be on less favorable financial terms and result in additional costs for the Group.

To minimize any risk of suspension or slowdown in the installation of its Freebox DSLAMs or delivery of its Freebox modems to customers, the Group aims to maintain constant stock levels sufficient to meet the Group's estimated needs for two months.

4.9.3 Dependence on new operating processes

Apart from the technical processes involved in local loop unbundling and the DSL technology itself, which is highly advanced, the Group does not consider itself to be dependent on new technical processes necessary for carrying out its business.

4.9.4 Main customers and suppliers of the Group

As the Group's service offerings are mainly targeted at the consumer market, almost all its revenue is achieved through sales to private individuals. Consequently, no single customer of the Group (other than France Télécom in the context of the "pay-as-you-go" access offering described in paragraph 4.5.1.1 and the ANNU business described in paragraph 4.5.3.1 above) represents a significant percentage of its revenues.

As far as the Group's suppliers are concerned, the main contracts entered into by the Company relate to the Group's network and can be subdivided into two categories: contracts for the use of dark optical fibers, allowing the Group to operate its network, and contracts granting the Group access to the subscriber through interconnect and unbundling agreements entered into primarily with France Télécom.

IRU agreements involve the granting by local authorities or private suppliers such as neuf telecom and Completel of the right to use the optical fibers which make up the Group's network. Pursuant to these long-term contracts, a single up-front payment is made when the fiber is made available. A description of these contracts is provided in paragraph 4.4.2.3 hereof. The risk to the Group of the non-renewal of these contracts is described in paragraph 4.9.2 hereof.

Interconnection and unbundling agreements provide the Group with access to its subscribers, either by means of the France Télécom network in the case of interconnection agreements or directly in the case of unbundling arrangements. As described more fully in paragraphs 4.4.1.1 and 4.4.1.2, the interconnection and unbundling agreements, respectively, allow the Group (i) to interconnect its own network with the France Télécom network by means of a physical connection to one of the incumbent operator's switches and (ii) to take advantage of direct access to a segment of the network between the subscriber's telephone socket and the main distribution frame to which the subscriber is connected in order to achieve the closest possible proximity to the subscriber. In the case of interconnection agreements, the incumbent operator charges fees based on the transmission capacity made available to the operator. In the case of unbundling, the amounts charged by France Télécom are essentially limited to the rental of the copper pair, the splitter and the copper tie cable that connect the subscriber's modem to the operator's DSLAM. France Télécom is required to offer both interconnection and unbundling to all alternative operators.

The Group is also party to less strategically important supply agreements, primarily with the assemblers of the Freebox modems and DSLAMs and with advertising agencies.

The amounts charged by the incumbent operator under interconnection and unbundling agreements as well as amounts invoiced by the Group to France Télécom in connection with the "pay-as-you-go" access offering and the reverse look-up directory service are subject to review by the ART.

4.10 CHANGES IN THE AVERAGE NUMBER OF EMPLOYEES OVER THE LAST THREE FINANCIAL YEARS

4.10.1 Breakdown by line of business

As of April 1, 2005, the Group had a workforce of 929 employees, all with open-ended employment contracts. This number will continue to rise as a result of the Group's policy of increasing its technical support and customer service teams working for its subsidiary Centrapel. The Group anticipates that the number of employees working for this subsidiary will rise due to the expected increase in the number of subscribers, particularly those using its telephony services, but also because of the Group's aim to improve the support service offered to the Group's customers.

The Group also offers callout support to its subscribers. In the case of problems with their connection, Free's technicians will visit the subscriber to establish the cause of the problem (faulty user equipment, faulty jumpers,

DSLAM failure, etc.) and rectify it. The subscriber must pay for this service unless his/her personal equipment is not involved.

Agreements relating to the reduction of working hours to 35 hours per week have been entered into within the Group companies in compliance with applicable legislation.

The table below presents the recent changes in the Group's workforce, broken down between management and non-management employees.

	as of 12/31/2002	as of 12/31/2003	as of 12/31/2004	as of 04/01/2005
Management	73	114	95	100
Non-management	188	391	657	829
Total	261	505	752	929

4.10.2 Breakdown of the Group's employees by line of business as of December 31, 2004

Business	Number of employees		
	Management	Non-management	Total
Iliad (holding company)	25	6	31
Internet (Free, Online, Freebox)	41	9	50
Centrapel	3	614	617
Telephony (Kertel, One.Tel, Kedra, Endeis Telecom)	21	25	46
Other Services	5	3	8
Total	95	657	752

4.10.3 Assessment of employee relations

The Company is not obliged to draw up an annual report on its employee relations as provided for by Articles L.432-1 to L.432-10 of the Labor Code.

Iliad considers that relations with its employees are good. Almost all the Group's employees work in the building housing all the Group companies, located in the 8th *arrondissement* of Paris.

4.11 CAPITAL EXPENDITURE POLICY

Figures relating to the Group's capital expenditures for the last three full fiscal years and for the fiscal year 2004 are provided in paragraph 5.2.2 hereof.

4.11.1 Company research and development policy

The Group's research and development policy was initially structured around two main objectives: offering differentiated services to subscribers using dedicated equipment and reducing costs relating to the construction and operation of its network.

It was with these two objectives in mind that Freebox S.A. developed the Freebox modems and the Freebox DSLAMs installed by Free. The Group intends to continue to develop in-house the architecture of the equipment used both in the operation of its network and in the provision of services to its customers, as well as the software applications based on "open" systems such as Linux used by all Group companies.

The team responsible for the Group's research and development is based at Freebox S.A. and is composed of 13 employees. In 2004, the Group devoted €1.9 million to research work mainly relating to the Group's Internet and Telephony businesses.

The aim of the Group's research and development policy is to ensure the development of network architectures and software solutions adapted for specific offerings and needs, and to ensure that the development of the corresponding equipment can easily be assembled by third party manufacturers on optimal financial terms. In 2004, the R&D team finalized the new versions of the Freebox modem (Freebox V4) and DSLAM which will allow subscribers to receive ADSL 2+ services, and is continuing to work on other technologies still in the experimental stage, while maintaining a technology watch on developments in ADSL and ADSL 2+, as well as other technologies (such as WiFi networks or the development of fiber-to-home technology).

4.11.2 Principal capital expenditure and acquisition of interests during the last three fiscal years

Details of the capital expenditure devoted to expanding the Group's national network (network equipment, IRU agreements, etc.) can be found in paragraph 5.2.1.3 hereof.

The Group took control of One.Tel in 2001 and of Kertel in 2003.

4.11.3 Principal capital expenditure in progress

The Group is currently concentrating its capital expenditure on local loop unbundling and is installing its Freebox DSLAMs in dedicated or shared co-location facilities provided by France Télécom. The Group is also investing in an increase in its network density (increasing the number of connections to France Télécom sites) by constructing additional sections of optical fibers jointly with private operators or local authorities or by concluding IRU agreements with such operators or local authorities. In June 2004, Free concluded a contract extension with neuf telecom for 60 million euros. Approximately 25 million euros remain committed for this contract as of December 31, 2004 (see note 28 of the notes to the consolidated financial statements). In addition to the capital expenditure corresponding to the Freebox modems, the Group is investing in the production of Freebox modems and Freebox DSLAMs by the Group's independent assemblers in order to be able to meet the growth in demand for broadband Internet access.

Description and method of financing

The table below shows the amount of principal capital expenditures undertaken during the years ended December 31, 2002, 2003 and 2004:

(in thousands of euros)	2002	2003	2004
Intangible assets	8,770	37,911	102,689
Tangible assets.	16,823	62,171	112,166
Long-term investments	319	1,022	3,386
Total	25,912	101,104	218,241

The Group's tangible fixed assets mainly consist of the transmission equipment necessary for operating its network, plus the modems and DSLAMs used for Free's broadband Internet access service offering. The intangible assets relate mainly to the rights to use optical fiber held by the Group under the terms of IRU agreements, and the charges payable to France Télécom for wiring connections. A detailed breakdown of the Group's capital expenditures and the method of financing them can be found in paragraph 5.2.1.3.

4.11.4 Principal future capital expenditure

The Group anticipates devoting substantially all of its future capital expenditures to (i) producing both the current and future versions of the Freebox modem and distributing these modems to its subscribers and (ii) increasing its network density by installing additional Freebox DSLAMs in France Télécom sites and operating new sections of optical fiber. The Group also intends to continue to develop its access to the unbundled local loop by financing the construction of shared co-location facilities in France Télécom sites. This development will accelerate the migration of broadband subscribers to Option 1 (unbundled) which, as explained in paragraph 5.2.1.2 below, will result in a substantial reduction in the cost of providing broadband Internet access. In addition, the Group will

continue to invest as necessary in securing and extending its network by increasing the number of optical fiber loops (thereby reducing risk of loss of service in the event of a failure in any one section of the network) and will carry out certain civil engineering works, either independently or in conjunction with other parties, to extend its network (thereby increasing network density).

With respect to the unbundling of the local loop, the Group is using the information it has available regarding the geographical breakdown of its broadband subscribers to give priority to unbundling the local loops at those France Télécom sites serving the greatest number of subscribers and to secure a rapid and satisfactory return on its investment.

4.12 RISK FACTORS

Investors should be aware of the risks described below before making any investment decision. If one or more of these risks were to materialize, the Group's business activities, financial situation, results of operations and growth could be adversely affected.

4.12.1 Risks relating to Iliad's business and strategy

Difficulty in predicting future growth and profitability

The Group's revenues depend for the most part on the number of subscribers to its Internet access service, which is closely linked, directly or indirectly, to the increase in the number of Internet users in France and particularly in the number of broadband users. The level of future revenues generated by subscribers is therefore difficult to predict. If the increase in the number of Internet users in France were to slow, the Group's business, results of operations and financial situation could be seriously affected and the Group could be unable to meet all or some of its objectives.

Difficulty in upgrading the capacity of the platform for online access to the Group's services in line with the growth in Internet traffic

Until now the Group has been able to upgrade the capacity of its technical platform for online access in line with the growth in Internet traffic. Given the generally accepted forecasts for the growth of Internet traffic in France, however, the objectives that the Group has set for itself in terms of both increasing the number of users of its services (particularly for broadband Internet access) and expanding its network, the Group will require the resources necessary to provide a corresponding increase in the capacity of its access infrastructures. There can be no assurance that the Group will be able to obtain such resources.

Dependence on managers and key employees

The Group's success is highly dependent on maintaining its relationship with Xavier Niel, an Iliad director and the Group's majority shareholder, and with other managers and key employees. The Group has a culture which fosters teamwork and motivation, and has arranged for its main employees to acquire an ownership stake in Iliad's share capital, which significantly contributes to employee loyalty. However, there can be no assurance that these key employees will remain with the Group in the strong growth environment that is expected to continue.

In order to sustain its business, the Group is taking particular care to ensure that the engineers and technicians working on its platform and network and designing and developing the Freebox modem and the Freebox DSLAM are skilled in a number of different areas. The Group's future success will depend in particular on its ability to attract, train, retain and motivate highly qualified employees and managers. However, since competition to attract employees with such qualifications is intense, there can be no assurance that the Group will be able to do so.

The loss of one or more key employees or a manager or the Group's inability to attract other qualified employees could have a material adverse effect on the Group's revenues, results of operations and financial situation.

Dependence on the principal shareholder

Xavier Niel holds a substantial percentage of shares of the Company's share capital and is Senior Vice President and Vice Chairman of the Board. He is thus in the position of having a decisive influence over most of the

Group's corporate decisions and in particular those requiring shareholder approval (such as the appointment and removal of directors, distribution of dividends, amendments to the bylaws and decisions concerning important Group transactions, including issuances of new shares of capital stock).

Rapid changes in pricing and technical aspects of Internet access offerings

The Internet access services market is characterized by rapidly changing pricing structures (such as usage-based charges, unlimited use packages and free access) and technical access methods (such as dial-up access, ADSL, etc.). The Group's access services are currently available on or through almost all the above pricing terms and technical methods. The development of new pricing structures and access methods based on different economic models, unforeseen changes in the relative importance of the various existing access service offerings or growth in use of existing replacement technologies (such as cable, satellite, and fiber to home) could undermine the economic assumptions on which the Group's development plan is based, which could have an adverse effect on the Group's business, results of operations and financial situation and on the Group's ability to meet its objectives.

Need to improve the technical features and functionality of the services offered by the Group

The Internet market is characterized by rapid changes in technology and in the types of services and features offered to customers. To remain competitive, the Group will continually have to improve the speed with which it responds to technological or other changes and the functionalities and features of its products and services, and will have to develop new products and services that are attractive to its customers. The Group may not succeed in making these improvements or developments in a timely manner, which would have an adverse effect on the Group's business, financial situation, and results of operations and on the Group's ability to meet its objectives.

Availability of equipment for the development of the broadband Internet access offering

The Group believes that the components used in its Freebox modems and DSLAMs are standardized and substitutable and that its component stock management policy allows it to anticipate growth in demand for broadband Internet access. Nevertheless, a shortage in the availability of these components or a significant increase in their price could hinder the Group's ability to provide new customers, in a timely manner, with the Freebox modem required to access value-added broadband services, which could have an adverse effect on the Group's growth.

Effect of acquisitions or investments

As part of its external growth strategy, which may take the form of acquisitions, partnerships or alliances, the Group may make acquisitions or investments in any one of its business segments. Part of these acquisitions or investments could be paid for by the issuance of Iliad shares, which would result in dilution of the Group's existing shareholders. Such acquisitions and investments, whether paid for in cash or shares, could have an adverse effect on the market price of Iliad's shares.

Subsequent sale of shares by significant shareholders

The company's principal shareholders today are Xavier Niel and the managers. If any of these shareholders were to sell a large number of shares, Iliad's share price could be affected, depending on the market condition at the time of the sale, the number of shares sold and the reasons for and the terms of the sale, as well as the public's perception of such sales.

4.12.2 Risks relating to the Internet and telecommunications sectors

Consequences of changes in the pricing set out in France Télécom's Reference Interconnect Offer and Reference Unbundling Offer approved by the Autorité de Régulation des Télécommunications (ART)

The Group's profitability depends in part on the pricing and technical conditions established by France Télécom in its Reference Interconnect Offer (revised each year) and in its Reference Unbundling Offer (revised from time to time). Any significant increase in the prices or change in the technical conditions set forth in the Reference

Interconnect Offer or the Reference Unbundling Offer, as approved by the ART, could have a material adverse effect on the Group's business, financial situation and results of operations and on the Group's ability to meet its objectives.

Competition

The Internet, telephony and broadband television markets are extremely competitive.

Internet

In the Internet sector, competition for customers for access services is intense and is likely to increase significantly in the future. The Group anticipates that competition in its market will increase due to (i) the continued growth of Internet use in France, (ii) the increase in the number of strategic alliances among the Group's competitors, (iii) the introduction by some of the Group's competitors of pricing policies intended to counter Free's aggressive offerings and (iv) the presence in the market of certain multinational companies with greater economic resources than those of the Group.

Telephony

The fixed telephony sector in France is a mature market and therefore not likely to undergo rapid expansion, and is heavily dominated by the incumbent operator. Although the Group believes it possesses a number of competitive advantages in this market, including in particular the use of its own network, it cannot guarantee that it will manage to develop its fixed telephony business as planned in a sector where the players are principally multinational companies whose financial resources exceed those of the Group and whose capacity for investment, particularly in advertising, presents a considerable advantage.

Television

In the broadband television sector, competition increased substantially during 2004, and is likely to continue to grow. Although the Group considers that it has a competitive edge in this market, particularly as a result of the use of its Freebox modem, which protects the transmission of audiovisual content, it cannot guarantee that it will be able to develop its audiovisual business as planned. Any such development will depend on the audiovisual content being broadcast and on being able to expand unbundling into new areas.

Other Services

The ANNU service is based essentially on a license to use France Télécom's directory database. Iliad can make no assurances that France Télécom will not grant this license to third parties or that its revenues from the Minitel market, which are already in decline, will not fall more rapidly than anticipated.

Security and confidentiality of information on the Internet

The need to secure communications and transactions on the Internet has been a major obstacle in the development of the Internet in general. Internet use may decrease if the level of protection of communications and transactions achieved proves to be inadequate or diminishes. The Group has taken and is continuing to take significant measures to guarantee the reliability of its security system and to limit problems that may be caused by security failures or a breach of the security system. Unauthorized persons might attempt to penetrate the Group's network security system. If they manage to do so, these persons might appropriate privileged information about the users of the Group's services or cause the service to be suspended. Some leading sites and suppliers of Internet services have suffered from "denial of service" attacks, in which very large numbers of requests for information are sent to the site with the aim of overloading its servers, or have been the victims of Internet viruses. Although the Group is taking the steps necessary to protect itself against such attacks, there can be no assurance that further attacks would not result in the incurrence of damages, even if only in terms of image. Consequently, the Group might be required to increase its expenditures and its efforts to protect itself against these risks or to alleviate their effects, which could have a significant impact on its business, financial situation and results of operations and on its ability to meet its targets.

4.12.3 Market risks

Foreign exchange risks

The only operations carried out by the Group which could entail a foreign exchange risk are those which involve the purchase of certain components of the Freebox modems and DSLAMs, which are billed and paid for in dollars. There is no coverage in place at this date. The Group believes that the foreign exchange risks linked to these operations are not likely to have a significant impact on its results.

Liquidity risk

The Group has historically financed its growth principally with internal resources, with limited recourse to borrowing from time to time to finance specific projects. As of March 31, 2005, the Group's net cash position stood at €24.5 million compared with €23 million as of December 31, 2004. The Group is not subject to any liquidity risk as a result of prepayment clauses in loans entered into by Group companies or as a result of the breach of any financial covenants (such as ratios, objectives, etc.).

There are agreements in place, in particular, on three confirmed lines of credit for a maximum of 70 million euros. Iliad is in compliance with the great majority of these agreements (which take the form of financial ratios) as of December 31, 2004 and March 31, 2005.

	Financial ratios required	Impact of non- compliance with financial ratios	Ratios as of December 31, 2004
Line of credit No. 1 (borrower: Free)	Gearing ratio < 1* Leverage ratio < 2.5**	Balance immediately payable	Gearing ratio: 0.08 Leverage ratio: 0.07
Line of credit No. 2 (borrower: Free)	Gearing ratio: <1 Leverage ratio: <2**	Balance immediately payable	Gearing ratio: 0.08 Leverage ratio: 0.07
Line of credit No. 3 (Borrower: Iliad)	Gearing ratio <1* Leverage ratio <2**	Balance immediately payable	Gearing ratio: -0.0066 Leverage ratio: -0.0104

* Net debt/shareholders' equity

** Net debt /EBITDA

The following is a breakdown of Group's debt as of December 31, 2004:

Nature of loan	Fixed or variable rate	Total amount (EUR millions)	Maturity	Coverage in place
Mortgage	Euribor	2.3	2013	None
Loan agreement	Fixed	3.0	2005	None
Loan agreement	Euribor	1.7	2005	None
Loan agreement	Euribor	4.0	2006	None
Loan agreement	Euribor	4.0	2006	None
Credit agreement 1	Euribor	20.0	2008	None
Credit agreement 2	Euribor	20.0	2008	None
Credit agreement 3	Euribor	30.0	2008	None
Loan agreement	Euribor	3.0	2008	None

Interest rate risk

The Group is not exposed to any significant interest rate risk. During the fiscal year 2004, the Group companies opened several confirmed lines of credit for a maximum amount of €70 million, which are available for use up to November 2008 in order to finance the roll-out of the network. As of December 31, 2004, the Group had drawn €10 million of the 70 million available. The Group's loans and leasing are described in Chapter 5 hereof, and in respect of which the outstanding balance amounted to €24.6 million as of December 31, 2004, compared with €20.9 million as of December 31, 2003. The Group's cash is placed in variable rate investments. As of December 31, 2004, the Group had not entered into any hedging arrangements to cover interest rate risk. In addition, the

Group has no significant investment assets (such as bonds, treasury bills, other negotiable debt instruments, loans and advances) and no off balance sheet commitments which might expose the Group to interest rate risk (such as securities subject to put rights, term interest rate contracts, etc.).

The table below shows the Group's net interest rate exposure (as of December 31, 2004) as well as an analysis of the sensitivity of the Group to interest rate fluctuations:

(in thousands of euros)	Less than 1 year	From 1 to 5 years	More than 5 years
Investment liabilities	16,683	4,610	635
Investment assets	0	0	1,378
Net exposure prior to hedging	16,683	4,610	-743
Off balance sheet commitments	0	0	0
Net exposure after hedging	16,683	4,610	-743
Net interest rate exposure renewable in less than one year (in thousands of euros)			16,683
Interest rate fluctuation			1%
Average remaining time prior to maturity (in months)			12
Sensitivity (in thousands of euros)			167

Share risk

None.

4.12.4 Legal risks

Risks relating to the Group's relations with the incumbent operator

Despite the legal and regulatory framework requiring the incumbent operator, France Télécom, to permit the development of local loop unbundling and to grant the Group access to its installations, the Group may be confronted by situations where there is a conflict of interest with France Télécom as the dominant competitor and principal supplier. France Télécom could exercise a significant influence over the Group's operations and strategy and restrict its capacity for growth.

Risks relating to liability for content

French law on the liability of access or hosting providers and portal operators, such as Free and Online, for the content of websites accessible through their services changed during 2004 with the promulgation of the law on confidence in the digital economy on June 21, 2004. The Group has placed on the Free portal home page forms which can be used to report unlawful content, and has established a procedure for reporting any violation of human dignity, so that web users can report any illegal content and Free can respond promptly to any complaints. However, in the past a number of suits have been filed, in France and other countries, against access or hosting providers because of the content of the information transmitted or made available online (in particular for press-related violations, invasion of privacy and trademark infringement). Free and Online may be subject to similar suits and could incur significant costs in order to defend themselves against such claims. Analysis of the proceedings and the preparation of an appropriate defense could prove to be costly even if Free and Online were eventually held not liable. Finally, the existence of any such proceedings could have an adverse effect on the Group's reputation.

Intellectual property rights

The Group can provide no assurance that measures taken in France and abroad to protect its intellectual property rights, particularly its trademarks, logos and domain names, will be effective or that third parties will not infringe or appropriate its intellectual property rights. Furthermore, given the worldwide reach of the Internet, the Group's trademarks, and particularly Iliad, Free, ANNU and Kertel and other forms of intellectual property, could be distributed in countries offering less intellectual property protection than European countries or the United States

of America. Given the importance to the Group of the recognition of its trademarks, any infringement or appropriation of this kind could materially adversely affect the Group's business, results of operations, financial situation and its ability to meet its objectives.

Furthermore, certain of the Group's trademarks (particularly Free and Online) co-exist with other identical trademarks registered by third parties for similar telecommunications services.

This situation is likely to require the Group in the long term to co-exist on its market with trademarks similar to its own. There is a risk that this co-existence could result in a dilution of these trademarks on the market which could adversely effect the Group's business, results of operations and financial situation and its ability to meet its objectives.

Lastly, given the hi-tech nature of the Group's business, the Group can provide no assurance that it is not infringing the intellectual property rights of third parties. This is an inherent risk for all operators in the telecommunications, audiovisual and Internet sectors and is typically resolved through licensing agreements with the holders of the relevant intellectual property rights.

Risk relating to the use of "open" system software

The Group is developing its own software programs on the basis of so-called "open" software, and in particular Linux. Open software consists of programs made available to users either free of charge or for a small fee. Based on the concepts of sharing and free use of source code, such software is distributed under a specific type of license (such as the GNU General Public License) generally allowing the user to modify and re-use the software without having to obtain prior permission from the rights holder. Furthermore, any software development which uses open software must, in turn, be freely accessible to and re-usable by third parties under the same conditions as the integrated open software.

The use of open software allows the user to benefit from the expertise of a community of developers at a lower cost than that charged for other commercially available software. However, open software does not come with a contractual warranty. Furthermore, the chain of ownership of the copyright to open software is uncertain. Consequently, the Group may be subject to liability in the event of the failure of an open system software program or an infringement action by a third party claiming to be the holder of intellectual property rights in such a program.

Confidentiality constraints

The Group does not consider that it has any specific confidentiality constraints.

Links with or dependence on other companies

In order to achieve transmission capacity and quality levels required to respond to the increase in the number of customers and to meet their requirements, the Group relies partly on the use of passive telecommunications infrastructures belonging to neuf telecom and other operators such as Completel or on networks deployed by certain local authorities.

Assets required for business operations not owned by Iliad

Other than networks to which Iliad is interconnected and certain interconnection equipment and the dark fibers used by its network under long-term IRU agreements, the Group considers that it is the owner of all the assets required for carrying out its business operations.

Special tax provisions

Iliad is not subject to any special tax provisions.

Exceptional events and disputes

In the normal course of its business, the Group is involved in a certain number of legal proceedings. Provisions have been recorded for these disputes in accordance with generally accepted accounting principles in France. The Group considers that the provisions established to cover known or outstanding risks, disputes or proceedings are of a sufficient amount to ensure that the consolidated financial position of the Group would not be affected to any significant degree by an unfavorable outcome. To the Company's knowledge, there does not exist any litigation, arbitration or exceptional event which has had or is likely to have a significant impact on the financial situation, results of operations, activity and assets of the Company or the Group.

The Group, like other companies in this sector, is frequently served with writs as part of proceedings instigated by subscribers in relation to a dispute about the provision of services. Generally speaking, the financial risk posed by each of these types of proceedings is relatively small. However, any proliferation of such proceedings could constitute a risk for the Group. In such cases, the Group tries to negotiate an amicable settlement, which helps to reduce considerably the final total cost of these proceedings. The Group believes that the number of these proceedings is not significant compared to the number of subscribers.

4.12.5 Regulatory situation

The Group's business activities are subject to the specific legislation and regulations of both the European Union and France governing the electronic communications sector (including telecommunications and Internet access) and the information society.

4.12.5.1 Regulation of electronic communications networks and services

The EC regulatory framework for electronic communications

1990 – 2003: strengthening of the regulatory framework to allow the opening up of the markets

Between 1990 and 1997, the EU legislator enacted a series of Directives providing for the abolition, as from January 1, 1998, of the national monopolies on the telecommunications market. The EC telecommunications framework also included harmonization measures concerning the rules governing licenses and authorizations, interconnection and access to the network, and the universal voice telephony service. These measures were due to have been transposed into national law by January 1, 1998. The EC regulatory framework was transposed into French law, in particular by Law No. 96-659 of July 27, 1996, and Order No. 2001-670 of July 25, 2001, amending the French Post and Telecommunications Code.

Since July 2003: simplification of the regulatory framework to underpin the opening up of the markets

The European Commission, considering that the first phase of the opening up of the market had been achieved, proposed that the EU legislator should relax the specific regulations and standardize the rules applicable to all electronic communications networks, taking into account the heralded convergence of telecommunications, audiovisual and information technologies. The new regulatory framework also allows for a distinction to be made between the regulations applicable to different markets, in order to allow for the eventual transition towards full competition in each individual market, based on competition law.

On July 25, 2003, the existing European regulatory framework was replaced by a new regulatory framework (the "2002 Telecoms Package") and this was due to have been transposed into the national legal order of the member states by that date.

The 2002 Telecoms Package subjects all types of transmission networks and related services to the same regime. The scope of the regulation is therefore no longer limited to just telecommunications but covers the whole of the electronic communications sector (mobile, cable, satellite, telecommunications and broadcasting of radio or audiovisual programs). It does not, on the other hand, apply to the content of the services provided on electronic communications networks using electronic communications services, such as the broadcasting of content (in particular radio or television programs), financial services and certain services specific to the information society (see the paragraph entitled "Regulation of the content of electronic communications" below) which are subject to other regulations.

In particular the 2002 Telecoms Package includes the following texts:

- Directive 2002/21/EC of March 7, 2002, on a common regulatory framework for electronic communications networks and services (“Framework Directive”), which establishes a harmonized regulatory framework for electronic communications networks and services. The Framework Directive defines the role of the national regulatory authorities (“NRAs”) in respect of the management of radio frequencies, numbering, rights of way, co-location and sharing of resources, accounting separation, interoperability and the resolution of disputes between operators. It also introduces a new concept concerning the designation of undertakings with significant market power on the relevant markets and establishes criteria and procedures aimed at ensuring a coherent assessment of the dominant undertakings throughout the European Union. In this regard, the Framework Directive is supplemented by (i) the Commission Recommendation of February 11, 2003 (C(2003)497) on the identification of the relevant product and service markets susceptible to *ex ante* regulation in relation to operators having significant market power on the relevant market, and (ii) the Commission Guidelines of July 11, 2002 (2002/C165/03), the purpose of which is to assist the NRAs with the market analysis process and the identification of operators with significant market power on the relevant markets. The Framework Directive provides that Member States must impose obligations on undertakings with significant market power proportional to the distortion of competition on the market in question.
- Directive 2002/19/EC of March 7, 2002, on access to, and interconnection of, electronic communications networks and associated facilities (“Access Directive”). This directive harmonizes the rights and obligations of operators and service providers requesting interconnection or access to electronic communications services or networks. The Access Directive establishes objectives for the NRAs concerning access and interconnection, and determines procedures for ensuring that the obligations imposed by the NRAs are reassessed and possibly withdrawn once the desired targets are actually met.
- Directive 2002/22/EC of March 7, 2002, on universal service and users’ rights relating to electronic communications networks and services (“Universal Service Directive”). The aim of the Universal Service Directive is first to ensure the availability throughout the EC of good quality publicly available services through effective competition and choice, and second to deal with circumstances where the needs of end users are not satisfactorily met by the market. The Directive defines a minimum set of services of a specified quality to be available to all end users at an affordable price, taking into account specific national conditions and without distorting competition. The Universal Service Directive also determines obligations in terms of the supply of a certain number of mandatory services, such as the retail provision of leased lines or carrier selection (either by carrier preselection or selection on a call-by-call basis).
- Directive 2002/20/EC of March 7, 2002, on the authorization of electronic communications networks and services (“Authorization Directive”). This Directive harmonizes and simplifies the rules and conditions for authorization to supply electronic communications networks and services. It does away with the individual license regime in favor of a general authorization regime (i.e. based on a notification procedure). Only the allocation of scarce resources (i.e. radio frequencies and numbers) may be subject to individual licenses.
- Directive 2002/77/EC of September 16, 2002, on competition in the markets for electronic communications networks and services. It replaces Directive 90/388/EEC, as last amended, and its aim is to extend the scope of the liberalization process to cover all electronic communications. The Directive takes into account the convergence phenomenon and groups under one single definition all the services and networks used for the conveyance of signals, thereby reaffirming the principle of the freedom to offer communications services and networks.
- Regulation (EC) 2887/2000 of December 18, 2000, on unbundled access to the local loop. This Regulation, which is directly applicable in all the Member States, provides that all operators with significant market power must offer unbundled access to their local loop and associated facilities, under transparent, fair and non-discriminatory conditions.

The progress of the implementation of the regulatory package in the member states is monitored in an annual report by the European Commission, available at the following address:

http://europa.eu.int/information_society/topics/ecommm/all_about/implementation_enforcement/index_en.htm

Responsibility for the control and actual implementation of the European regulatory framework lies with the national regulatory authorities, and in France this is the responsibility of the *Autorité de Régulation des Télécommunications* (“ART”), which was created in January 1997.

In France, the transposition of the 2002 Telecoms Package has taken place essentially in the form of Law 2004-669 of July 9, 2004, together with its series of implementing decrees, most of which had still not been enacted by January 31, 2005.

Market analysis

The analysis of the markets is the cornerstone of the new regulatory framework, because it will be the basis for adapting the new regulations specifically to suit each individual market. It will be an ongoing process, subject to periodic review, with a view eventually to bringing the regulations into line with competition law. The aim is also to limit *ex ante* regulation to markets where the level of competition is low (which today is the case in the majority of the wholesale markets), and to apply *ex post* regulation to markets where the level of competition is high (currently the case in most retail markets).

Pursuant to the Framework Directive and Articles L.37-1 to L.38-3 of the Post and Electronic Communications Code, the ART is required, under the supervision of the European Commission and on the recommendation of the French competition authority, the *Conseil de la Concurrence*, (i) to define the relevant markets applicable in France, (ii) to analyze these markets and to identify operators or undertakings as having significant market power (SMP) in these markets and (iii) to decide whether or not to impose on these undertakings regulatory obligations (or “measures”) commensurate with the competition problems which have been identified and which will ensure a certain level of competition in the relevant market in question.

In 2004, the ART began a public consultation process in the 18 relevant markets likely to be subject to specific regulation, including 6 retail markets and 12 wholesale markets. Descriptions of each market and the status of the market analysis process can be found on the ART’s website at the following address: <http://www.art-telecom.fr/dossiers/marches/index-d.htm>.

As a result of the delayed transposition of the 2002 Telecoms Package (including in particular Decree 2004-1301 of November 23, 2004), by February 28, 2005, the ART had only completed its analysis of the following markets:

- Market 16, i.e. termination of voice calls (fixed and mobile) on individual mobile networks in mainland France and in the overseas dependencies. The ART notified the SMP operators (SFR, Bouygues Télécom and Orange France in mainland France, and SFR and Orange Caraïbes in the overseas dependencies) of their obligations which basically involve the orientation of tariffs towards the cost of providing call termination services and the publication of a reference offer.
- With respect to markets 11 (access to the local loop) and 12 (broadband access at a regional point of presence), the ART has completed its analysis and obtained the opinion of the *Conseil de la Concurrence* (Opinion 05-A-03 dated January 31, 2005) and is preparing a draft decision on the obligations applicable to France Télécom for submission to the European Commission.
- With respect to the fixed telephony wholesale and retail markets, the ART has completed its analysis and obtained the opinion of the *Conseil de la Concurrence* (Opinion 05-A-05 dated February 16, 2005).
- With respect to market 15 (call origination in mobile networks), the ART is currently analyzing the responses to its public consultation.

The regulatory measures which can be imposed by the ART on operators designated as having significant market power in a relevant market are specified in Articles L.38 (wholesale markets) and L.38-1 (retail markets) of the Post and Electronic Communications Code. These measures include in particular the obligation to publish detailed technical and pricing specifications relating to interconnection and access, the obligation to provide

interconnection or access under non-discriminatory conditions, the obligation not to charge excessive or predatory prices on the market in question and to charge prices which are oriented towards the corresponding costs, the obligation to provide retail services under non-discriminatory conditions, the obligation not to unreasonably bundle these services, the obligation to comply with the price cap mechanism set by the ART over a number of years and the obligation to obtain the ART's approval of its prices prior to applying them, etc.

The business activities of each of the operators operating in the various markets will be affected as the ART's decisions based on its analysis of the markets take effect. In particular, those operators designated as having significant market power in a relevant market could experience a reduction in the profitability of their business activities in the market in question. Our Company does not, however, consider that the ART's decisions should have any significant effect on the markets in which it is active.

Operation of a public telecommunications network/Provision of a public telephone service

Until July 25, 2003, the installation and operation of a public telecommunications network (provided for in Article L.33-1 of the former Post and Telecommunications Code) and the provision of a public telephone service (provided for in Article L.34-1 of the same code) required an individual administrative authorization, valid for fifteen years, issued by the Minister for Telecommunications after examination by the ART.

Following the enactment of Law 2004-669 and the amendment of Article L.33-1 of the Post and Electronic Communications Code, a simple notification to the ART is henceforth all that is required (except for the allocation of frequencies or numbering resources which still require a prior individual license). Law 2004-669 also specifies that existing authorizations are deemed to be a notification within the meaning of the 2002 Telecoms Package, in accordance with the principles laid down in Article 17 of the Authorization Directive.

The Minister for Telecommunications has issued the following authorizations to Group companies: an L.33-1/L.34-1 license granted to Free (Ministerial Order of December 14, 2000, amending the Order of November 9, 1999), an L.34-1 license granted to One.Tel (Order of September 1, 2002, amending the Order of November 21, 2000) and an L.34-1 license granted to Kertel (Order of March 14, 2002).

The holder of an L.33-1 license (and, since July 25, 2003, of an L.33-1 notification of an electronic communications network) may obtain rights of way in consideration for the payment of a fee, in order to establish its network infrastructure on public highway land or other public property and to benefit, under certain conditions, from easements on private property. The Group benefits from these rights and has developed its network infrastructure mainly on public property.

All licensed operators must pay the annual license fees, including in particular the fees for management and control of the licenses and for the numbers or frequencies allocated to the operator.

Internet service provider business

Since the enactment of Law 2004-669, Internet service providers need to submit prior notification to the ART in order to carry out their activities.

Internet service providers, like other electronic communications operators, are obliged to contribute to the funding of universal service (*cf.* below).

Prepaid cards

The sale of prepaid phone cards (such as those sold by Kertel) and, more generally, the purchase (and/or resale) of telecom minutes is free and does not as such require a license or notification.

Interconnection

The provision of regulations governing the access and interconnection of each licensed operator to the networks of the incumbent operator and of other licensed operators is essential for opening up the market. Such regulations lower the barrier to entry represented by the high cost to a new entrant of having to build its own network. The

ART has therefore focused on interconnection pricing and technical conditions, and has succeeded in developing a specific and functional framework.

The access and interconnection regulations applicable in the EU and in France set out specific principles for the pricing of interconnection services and the allocation of the cost of universal service obligations, impose specific accounting obligations in order to avoid the artificial support of one activity by another by unfair cross-subsidization, define the principles of access to essential facilities (ducts, conduits, sites and buildings) and the principles for the allocation of telephone numbers, define the role of the national regulatory authorities, and introduce a common process for settling disputes. Operators that the national regulatory authorities have designated as having "significant market power on a relevant market" must offer interconnection to other operators on a reasonable and non-discriminatory basis.

Up to July 25, 2003, four relevant markets had been defined in France: (i) the fixed public telephony market, (ii) the leased lines market, (iii) the mobile public telephony market and (iv) the national interconnection market. In 2005, following the ART's analysis of the relevant markets, there will be eighteen markets instead of these four existing markets (*cf.* above).

Under the former regulatory framework, prior to publication of the ART's decisions relating to its analysis of the markets, only those operators of public networks designated as having significant market power on the fixed telephony and leased lines markets were required to publish a document detailing their interconnection pricing and technical conditions ("Reference Interconnect Offer"), which was subject to prior approval by the ART. A list of these operators was drawn up each year by the ART, after consulting the French competition authority. In addition to their obligation to meet interconnection requirements, these operators were (and are still) required to meet justified requests for special access. These operators had (and still have) to comply, under objective, transparent and non-discriminatory conditions, with requests for interconnection submitted by any licensed operator. Consequently, France Télécom had (and still has) to provide interconnection services to its competitors, including Free and One.Tel, under the same conditions as offered to other licensed operators (including its subsidiaries). Requests for interconnection must not be refused if they are reasonable, considering the needs of the requesting party and the operators' ability to meet such needs. The requests for interconnection will be the subject of an agreement between the parties, a copy of which is sent to the ART, and which must comply with legal and regulatory requirements, including in particular Decree No. 97-1881. The ART has the power, after consulting the *Conseil de la Concurrence*, to require changes to be made to an interconnection agreement, in order to ensure that both competition and the interoperability of the telecommunications services are maintained. Finally, in the case of any dispute relating to interconnection, either party may refer it for arbitration by the ART, whose decision is binding on the operators, although they do have a non-suspensive right of appeal.

On February 15, 2000, Free signed an interconnection agreement reflecting in operational terms the principles set out in France Télécom's Reference Interconnect Offer. Amendments were added to this agreement to take account not only of the implementation of services introduced in successive editions of the Reference Interconnect Offer but also of the interconnection services supplied by Free to France Télécom (call termination on Free's local loop, collection of calls made from Free's local loop to France Télécom's special numbers).

Every year, after approval from the ART, France Télécom publishes a Reference Interconnect Offer, which sets out the main interconnection prices, a list of the interconnection access points, the terms for connection by third party network operators to these access points, the support services provided by France Télécom, the conditions applying to carrier selection (selection on a call-by-call basis or preselection), and the interconnection of other operators' leased lines, as well as the provision of partial leased lines and in-span interconnect links.

The ART has issued several decisions relating to the successive versions of France Télécom's Reference Interconnect Offer, and has in particular imposed a gradual reduction in prices based on the principle of cost orientation (see in particular Decision No. 02-1027 of November 5, 2002, in which the ART introduced long-run average incremental costs as a reference for France Télécom's interconnection prices, instead of the relevant projected average accounting costs, the method previously used). On November 23, 2004, in Decision No. 2004-1000, the ART ruled that the whole of France Télécom's 2004 Reference Interconnect Offer should remain in effect until all the decisions relating to the market analysis have been adopted.

As far as the Group's business is concerned, the ART issued a decision on July 24, 2003 (Decision No. 03-905) on the request made by the Company on March 28, 2003, for the ART to settle a dispute with France Télécom concerning the terms of the interconnection used for routing telephone calls to the "universal and personal numbers" of its "Freebox" subscribers (08 7B PQ MC DU numbers). The ART decided that, after a transitional phase ending no later than July 1, 2004, the parties should implement a direct interconnection arrangement for the routing of calls to the Freebox subscribers' numbers assigned to the Company. However, the ART felt that the unusual circumstances of the dispute between France Telecom and Free merited the immediate, temporary application of the technical and pricing conditions of the indirect interconnection offer currently provided by France Telecom to route calls to the special services of third-party operators at a tariff equal to that applied to calls to France Telecom's "Azur" numbers, thus allowing the Company to launch its ADSL telephony service via the Freebox modem. In its notice No. 04-31 of January 8, 2004, the ART validated the financial terms proposed by France Télécom for direct interconnection, allowing the routing of calls to the "Freebox" telephone numbers, which specifically means that France Télécom must apply to such calls an average price per minute lower than the average price per minute charged for a national call. This mechanism has subsequently been extended to apply to the routing of calls to 08 7B PQ MC DU numbers belonging to Wanadoo (Decision No. 04-597), Cegetel and AzurTel (Decision No. 04-1096) and Tiscali (Decision No. 05-0058).

Dial-up Internet access

The regulations relating to dial-up access to the Internet are based on the interconnection regulations.

In France, France Télécom's Reference Interconnect Offer has been progressively amended to reflect numerous opinions and decisions issued by the ART, particularly those concerning the settlement of disputes between France Télécom and new entrants on the market, in order to allow Internet service providers to benefit from operational and pricing conditions enabling them to carry out their business. France Télécom supplies interconnected operators with call collection services at cost-oriented prices, combined with third-party billing of traffic generated by customers, charged at a rate of 4% of the turnover billed (these rates were changed in July 2004).

France Télécom's interconnection offer was improved during the second half of 2001 by the addition of new pricing conditions for the routing of switched traffic, with the introduction of a flat-rate Internet access connection (FRIACO) offer, where the price is based on the network capacity bought by the operator, unlike the traditional offer which is based on duration of the connection.

Broadband Internet access and local loop unbundling

The provision of broadband Internet access is based either (i) on physical access to France Télécom's copper local loop allowing the new entrant operator to operate its own access equipment with the aim of offering its own services, as distinct from France Télécom's services, or (ii) on access to France Télécom's DSLAMs, combined with collection of subscribers' data traffic and delivery of this traffic to one or more of the service provider's points of presence. In the first case, the service provided by France Télécom is known as "local loop unbundling" while in the second case, the service offers "bit stream access", more commonly called "Option 5" or "Option 3" in France.

The Group uses both these options to provide its customers with broadband Internet access (see paragraph 4.5.1.1 above).

Local loop unbundling

EC Regulation No. 2887/2000 of December 18, 2000 on unbundled access to the local loop requires operators designated as having significant market power on the access segment (in practice this means France Télécom in France) to publish a reference offer for unbundled access, including shared access, to their local loops and related facilities (prior information about the technical characteristics of the copper links, the addresses of the main MDFs, the co-location conditions, etc.). As this is a Regulation, it is to be applied directly in all the Member States and therefore does not require any transposition at national level. In France, however, Decree No. 2000-881, dated September 12, 2000, ("the local loop decree") requires dominant operators (i.e. in practice France Télécom) to meet reasonable requests for access to their copper local loop infrastructure as from January 1, 2001.

However, it was not until the first half of 2002 that France Télécom's reference offer, amended as requested by the ART, first permitted the effective start of unbundling in France. In fact, the ART had to make repeated requests for changes to France Télécom's reference offer for unbundled access to its local loop, including in particular on April 16, 2002, resulting in the publication of a new reference offer on June 14, 2002. This new reference offer included the changes required by the ART, particularly those relating to the co-location of third party operator equipment next to France Télécom's equipment, as well as the prices for leasing of unbundled lines by network operators.

Access to the local loop can take one of the following two forms:

- either the incumbent operator provides access to the metallic part of its network, between the main MDF and the termination point located in the subscriber's premises (full unbundled access to the local loop);
- or the incumbent operator provides access to the high frequency spectrum on this same part of its network and itself continues to provide a traditional public telephone service using the low frequencies (shared access to the local loop).

The terms of access to the local loop are determined by a private law agreement that must be submitted to the ART at its request.

On December 6, 2002, Free signed an agreement for access to France Télécom's local loop reflecting in operational terms the principles set out in the public reference offer.

In accordance with the EC Regulation and with the local loop decree, the prices of unbundled access to the local loops must be cost-oriented. In particular, the network elements are valued at their long-run average incremental cost. For the valuation of shared access to the local loop, the ART decided that the shared access to the local loop should be valued in terms of the specific costs incurred (Decision No. 02-323 of April 16, 2002).

In June 2002, France Télécom appealed to the French supreme administrative court, the *Conseil d'Etat*, asking it to overturn the ART's Decision No. 02-323 of April 16, 2002, which amended France Télécom's reference offer. In particular, France Télécom was challenging the method used by the ART to set the price for full access to the local loop. In her conclusions dated February 18, 2005, *Conseil d'Etat's* advocate general, the *Commissaire du Gouvernement*, ruled that the ART (i) did have the power to make changes to France Télécom's reference offer, (ii) could change the methods used to establish the prices for full access to the local loop, and (iii) could specify a method weighting the average cost of two pools of lines based on the likelihood that operators would request total access to these pools. On the other hand, the *Commissaire* considered that the ART had not met its duty of transparency as required under the terms of Decree No. 2000-881. The *Conseil d'Etat* issued a ruling on February 25, 2005, setting aside, on the grounds of procedural irregularity, the *Autorité de Régulation des Télécommunications'* Decision No. 02-323 dated April 16, 2002, in which the regulator ordered France Télécom to change its unbundling tariffs in order to achieve greater orientation towards costs. This ruling was not retroactive and will take effect two months after the date of notification. The ART will therefore need to issue a new decision changing France Télécom's reference offer which complies with procedural requirements.

As far as full unbundling is concerned, France Télécom's pricing and operational conditions were such that it could not be properly put into effect until the summer of 2004. The ART's intervention in January 2005 resulted in a reduction in the charges for access to the service billed by France Télécom to operators wishing to avail themselves of full unbundling.

The ART began its analysis of the relevant markets relating to broadband Internet access (markets 11 and 12) during the course of 2004.

Approval process

Access to France Télécom's DSLAMs and the associated collection of ADSL traffic are organized under the terms of a set of contracts ("IP/ADSL" and "IP/ADSL Collection"), and price changes are now subject to an approval process following an arbitration decision issued in 1999 by the Minister for Telecommunications (cf. ART Decision No. 99-582 in response to the France Télécom pricing decision No. 99077 E in relation to the new Netissimo and Turbo IP services).

Decree No. 2005-75 of January 31, 2005 transferred the power to approve the pricing of the universal service from the Minister to the ART.

Furthermore, in the context of its analysis of markets 11 and 12, the ART noted in its consultation document that it was considering imposing on France Télécom the obligation to publish a reference offer relating to broadband access delivered at a regional point of presence. This reference offer will include the technical principles set forth in the IPADSL and ADSL Connect ATM contracts.

On completion of the market analysis process, therefore, the pricing of the IP/ADSL offering will no longer be subject to ministerial approval, but will be subject to the terms of a reference offer which can be amended by the ART.

Free will also be able to refer to the ART any dispute or disagreement arising in connection with the technical or pricing principles of the IP/ADSL offering.

Numbering and carrier preselection

Since January 17, 2000, subscribers have been able to opt for the automatic preselection of their long distance operators, allowing them to access the latter's network without having to dial the operator's one or four figure prefix. The carrier preselection facility has also been available for calls to mobiles since November 2000 and for local calls since the beginning of 2002, at the option of the carrier. Since January 1, 1998, any subscriber who changes operator for fixed telephone services, but does not change geographical location, has been able to keep his/her number. Number portability has been available for shared-cost services since the second half of 2001 and for shared-revenue services since December 17, 2002. The technical conditions for carrier preselection and number portability are set out in France Télécom's Reference Interconnect Offer and are set forth in the interconnection agreements concluded between France Télécom and third party operators.

Directories and provision of subscriber lists

The Group's services mainly affected by the provisions described below are the Minitel version (3617 ANNU) and telephone version of its reverse look-up directory service, ANNU.

The company entered into an agreement with France Telecom to provide directory information to France Telecom for its published directories and/or information service. The contract provides that France Telecom may terminate the contract in the event of a modification affecting the structure or control of Iliad's capital or Iliad's ownership or management.

However, Order No. 2001-670 of July 25, 2001, adapting the Intellectual Property Code and the Post and Telecommunications Code to EC law, transposed several European directives into French law, including the Directive on the protection of personal data in the telecommunications sector (Directive 97/66/EC) and the Directive of February 26, 1998 on the application of open network provision (ONP) to voice telephony (98/10/EC). The aforementioned Order No. 2001-670 of July 25, 2001 provides that operators are required to supply their subscriber lists when so requested, under non-discriminatory conditions and at a price reflecting the actual cost of the service provided, with the aim of publishing a universal directory or providing a directory enquiries service, even if geographically restricted.

The means of obtaining access to these lists are governed by the provisions of a legal and regulatory framework requiring non-discriminatory access and a fee reflecting costs, as well as the protection of personal rights. These provisions have been set forth in an implementing decree (Decree No. 2003-752 of August 1, 2003) which determines the conditions for provision of the lists and will make it possible to establish truly universal directories and directory enquiries services, including mobile subscribers. In accordance with the 1998 directive mentioned above, these lists must be provided at a price reflecting actual cost.

As far as the Group's business is concerned, the ART issued a decision on September 23, 2003 (Decision No. 03-1038) following a request submitted by the Company asking the ART to rule on a dispute with France Télécom concerning the technical and pricing conditions of access to the incumbent operator's subscriber list in order to provide a universal directory service. The ART considered that the structure of France Télécom's pricing offer did not respect the principles of cost-orientation and non-discrimination and was likely to restrict the

development of competition. The ART directed France Télécom to propose to the Company, within a period of 60 days, an offer respecting the principles of cost-orientation and non-discrimination. On October 23, 2003, France Télécom filed an appeal before the Paris Court of Appeal, asking it to set aside the September 23, 2003 decision. The Paris Court of Appeal issued a ruling on April 6, 2004, setting aside and quashing Decision No. 03-1038.

The issue of access to France Télécom subscriber lists also gave rise to a ruling by the French competition authority, the *Conseil de la Concurrence*, on September 12, 2003 (Decision No. 03-D-43). On the basis of general competition law, and following a complaint by Sonera France and Scoot France, the competition authority considered that France Télécom had failed to comply with the injunctions made against it by the Paris Court of Appeal in its ruling of June 29, 1999, concerning the operator's failure to comply with the principles of non-discrimination and cost-oriented pricing of its file management function, and fined France Télécom 40 million euros for this practice.

On December 16, 2004, the ART published technical and financial guidelines for the transfer of subscriber lists. These guidelines set forth the principles for the provision by telecommunications operators to publishers of directories of lists of all their subscribers, regardless of whether the numbers in question are fixed or mobile telephone numbers, 0870 numbers, or Audiotel numbers, etc.

Contribution to universal service funding

The universal service comprises (i) the provision of a good quality telephone service at an affordable price, (ii) a directory enquiries service and directories in printed and electronic forms, and (iii) access to public payphones located on public property. Each of these three components must include special facilities for disabled users, so that they can be assured of access to the preceding three services under conditions equivalent to those enjoyed by other users.

Following the enactment of Law No. 2003-1365 of December 31, 2003, France Télécom is no longer designated by law as the operator responsible for provision of the universal service, and in future the operator or operators required to guarantee the provision of universal service will be designated on the basis of calls for tender. Three calls for tender, relating to each of the three components of the universal service, were published in the Official Gazette of November 25, 2004.

The aforementioned law modifies the means used for calculating the contribution of electronic communications operators (including Internet service providers) to the funding of universal service obligations. The cost of the universal service will henceforth be shared between operators pro rata to their turnover derived from telecommunications services (and no longer pro rata to their volume of traffic), "*excluding revenues from interconnection and access services subject to the agreements defined in paragraph I of Article L.34-8 and other services provided or billed on behalf of third party operators*". These new means of funding the universal service apply as from the financial year 2002. The publication of implementing Decree No. 04-1222 of November 17, 2004, relating to public service obligations and the funding of the universal electronic communications service provided a regulatory framework for evaluating the contribution due for the financial period ended 2002. The ART was therefore able to issue its Decision No. 04-1027 on November 25, 2004, adopting a notice of declaration of the turnover to be taken into account for calculating the contribution to universal service funding for the year 2002. In its Decision No. 04-1068 of December 21, 2004, the ART estimated the net cost of universal service obligations to be €124,989,000 for the year 2002, after taking account of intangible benefits.

Finally, Decree No. 2005-75 of January 31, 2005, governing price controls for the electronic communications universal service, supplements the provisions of Article R.20-30-11 of the Post and Electronic Communications Code. It defines the cases in which the prices for the universal service proposed by an operator responsible for providing one of the components thereof may be subject either to a price cap over a number of years, or to prior approval or rejection by the ART.

Government initiatives relating to information society networks

The growth of the Internet is particularly dependent on the roll-out of infrastructures capable of sustaining an increase in bandwidth-hungry services, and in fact such infrastructures are already in place or are in the process of

being developed, i.e. optical fiber networks, cable, satellite, wireless networks (including standard 802.11) and UMTS networks.

In November 2002, the French government launched its RE/SO 2007 initiative (for a digital REpublic in the information SOciety) with a view to making up the ground lost by France in the information society sector. This initiative is banking on an increase in access to broadband, the objectives being, on the one hand, to reach a target of ten million broadband Internet subscribers in France within the next five years and, on the other hand, to enable every local district in France to have access to broadband Internet by 2007. The plan is, first of all, to work on the supply side, by creating a favorable environment for the development of the infrastructures, content and services, whilst developing a climate of confidence intended to ensure the effective protection of users and especially to promote the development of e-commerce.

Law No. 2004-575 of June 21, 2004 (“on confidence in the digital economy”) is intended to adapt French law to meet the demands of the growth of the digital economy and to increase confidence in the use of new technologies. This law, which supplements the transposition into national law of the electronic commerce directive, sets out the provisions governing the liability of access and hosting providers and also deals with the domain name addressing system and encryption. The law also amends the current provisions of the General Local Authorities Code in order to facilitate the roll-out of telecommunications infrastructures by local authorities (new Article L.1425-1).

Broadcasting of audiovisual services via ADSL

The 2002 Telecoms Package provides that the transmission and broadcast of radio and television services (whatever the means of transmission of the signals) falls within its scope and must consequently be subject to the control of the national regulatory authorities.

Law No. 2004-669 extends the competence of the French broadcasting watchdog, the *Conseil Supérieur de l’Audiovisuel* (“CSA”) to cover all radio and television services, whatever their method of transmission and broadcast. It also makes the regime governing the broadcast of radio and television services more flexible by making the distribution of such services on a network not using frequencies allocated by the CSA (including, therefore, distribution via ADSL) subject solely to prior declaration to the CSA. The obligation to make this declaration to the CSA will not take effect until an implementing decree has been published, which had still not taken place as of February 10, 2005.

In its capacity as a broadcaster of audiovisual services via ADSL, Free is subject to the regulatory “must-carry” provisions, i.e. the obligation upon a provider of services via cable, satellite or ADSL to carry certain audiovisual services on its network. There are two sides to the legal obligations involved in the must-carry provisions, i.e. (i) the obligation for the service provider – i.e. a cable operator or satellite operator – to carry certain channels, and (ii) the obligation for the must-carry channels to agree to being carried by the operator or service provider.

With respect to the broadcast of audiovisual services via ADSL, the new must-carry obligations are now governed by Articles 34-2 and 34-4 of Law No. 86-1067 of September 30, 1986, as follows:

- Article 34-2 provides, in respect of all types of network (cable, satellite, ADSL), for the free retransmission of public service channels broadcast over microwave, the Chaîne Parlementaire, TV5 and RFO services specifically aimed at the general public in mainland France (i.e. the program RFO-Sat). The same rules apply (except for satellite) to local cable channels;
- Article 34-4 provides, in respect of free-to-air analog or digital channels broadcast via microwave, for must-carry rights on all means of transmission (cable, satellite, ADSL) under fair, reasonable and non-discriminatory conditions. In this connection, it is only the channels themselves that can demand that their programs are carried by the distribution networks and not vice versa.

On November 28, 2003, following the refusal by TF1 and Métropole Télévision (M6) to agree to Free’s request that their content should be broadcast on Free’s ADSL network, the Company and Free submitted a complaint to the *Conseil de la Concurrence*, citing an abuse by France Télécom, TF1, TPS and possibly Métropole Télévision (M6) of their dominant position in respect of the broadcasting of private television content. The Company presented this complaint to the *Conseil de la Concurrence* on December 10, 2003.

On April 15, 2004, the *Conseil de la Concurrence* gave its decision on the request by the companies Iliad and Free for the application of interim measures in respect of the companies TF1, Métropole Télévision (M6), TPS and France Télécom. The *Conseil de la Concurrence* has not, as yet, granted Iliad and Free these interim measures, thus depriving them of the content broadcast by two major players in the field of audiovisual content in France. The Company is still awaiting the competition authority's ruling on the merits of the complaint.

When it was first listed on the stock exchange, the Company declared that a rejection by the *Conseil de la Concurrence* of the Group's request would not have any effect on its future prospects. As the market for the broadcast of audiovisual services via ADSL has grown considerably in recent months with the appearance of competing services offered by other telecommunications operators, the Group now feels that it is not in a position to assess the financial impact and consequences of not being able to broadcast the television channels TF1 and M6 as part of Free's bouquet of channels.

Furthermore, discussions are currently under way on the regime to be applied to video-on-demand services, as well as to radio and television services with partially interactive content.

4.12.5.2 Regulation of the content of electronic communications

Content of online services and liability of players on the Internet market

The provisions currently governing the content of online services make a distinction between private correspondence, whose secrecy is protected, and public communications using electronic means, whose freedom is guaranteed. Whilst this legal framework is based on the fundamental principle of freedom of communication, which is guaranteed under the Constitution, the Law of July 29, 1881, on the freedom of the press and the Law No. 86-1067 of September 30, 1986, as amended, on freedom of expression, its aim is also to respect great principles of French law, such as the protection of privacy, the protection of minors, the prevention of unlawful content, the protection of personal reputation and rights and respect for human dignity.

Directive 2000/31/EC of June 8, 2000, on certain legal aspects of information society services, particularly e-commerce, in the internal market ("Directive on electronic commerce") sets out the responsibilities and obligations of access and hosting providers. This directive was due to have been transposed into domestic law by January 17, 2002, at the latest. Under French law, the question of the liability of intermediary ISPs (access and hosting providers) was until 2004 dealt with by Chapter VI, Section II of the Law of September 30, 1986, as amended by Law No. 2000-719 of August 1, 2000. These provisions were repealed by Law No. 2004-575 of June 21, 2004, on confidence in the digital economy.

The main provisions of Law No. 2004-575 of June 21, 2004, with respect to the liability of access and hosting providers, are as follows:

- Providers of online communication services are obliged directly or indirectly to identify themselves. Pursuant to Article 6.III of Law No. 2004-575, therefore, individuals providing an online communication service on a non-professional basis are obliged to indicate on their website their name and address or the name and address of their hosting provider if they wish to remain anonymous. Legal entities and private individuals offering professional services on a website must, for their part, give their full details on their website, as well as the name of the publications director or co-director and the name and address of their hosting provider. Hosting providers and access providers must supply the providers of online services with the technical means to meet their identification obligations.
- Access providers and hosting providers are required to keep data that could identify persons having participated in the creation of the content of the services which they provide, in order to be able to pass such data to the judicial authorities. This provision is to be included in an implementing decree which will define the data to be kept and the duration and the means of keeping such data. This decree could in particular have an impact on the costs borne by the technical service providers for the storage and processing of data.
- Pursuant to Article 6 of Law No. 2004-575, hosting providers cannot be held civilly liable on the grounds of the activities or information stored at the request of a recipient of these services if they were not aware of their unlawful nature or of any facts or circumstances making this unlawful nature obvious,

or if, as soon as they do become aware of it, they act promptly to withdraw the data or to prevent access to it. Furthermore, these same hosting providers cannot be held criminally liable if they are unaware of the unlawful activity or information or if, as soon as they do become aware of it, they act promptly to withdraw the information or to prevent access to it. These rules concerning liability do not apply if the recipient of the service is acting under the authority or control of the hosting provider.

- Pursuant to Article L.32-3-3 of the Post and Electronic Communications Code, access providers cannot be held either civilly or criminally liable for the content of the services to which they provide access, except in circumstances where either they have originated the request for the transmission at issue, or they select the recipient of the transmission, or they select or modify the content being transmitted.

Furthermore, Article L.34-1 of the Post and Electronic Communications Code states that electronic communications operators and Internet service providers are obliged to keep the technical connection data necessary for criminal investigations. They may also keep the technical data required for the recovery of their bills. Apart from these two specific cases, the operators concerned must delete or render anonymous all data concerning a communication once it is completed.

The Group makes access to Free's no-subscription services conditional upon the provision by customers of a physical address to which their connection settings can be sent by post. Free is therefore in a position to respond to any requests for information from the judicial authorities. As the flat-rate and broadband services are linked to the physical access, Free is also able to respond to requests from the authorities concerning the subscribers of these services.

Processing of personal data and protection of individuals

The framework Directive 95/46/EC of October 24, 1995, on the protection of individuals with regard to the processing of personal data and on the free movement of such data, specifies the elements necessary for effective protection of the rights and freedom of individuals. The purpose of this directive is, amongst others, to harmonize European legislation governing the processing of personal data, to facilitate the movement of such data (provided that the country of destination of the information in question offers a satisfactory level of protection) and to ensure the protection of the rights and freedom of individuals. This framework directive was completed by the sector-specific Directive 97/66/EC of December 15, 1997, concerning the processing of personal data and the protection of privacy in the telecommunications sector. This directive has been repealed and replaced by Directive 2002/58/EC of July 12, 2002.

Law No. 2004-801 of August 6, 2004, on the protection of individuals with respect to the processing of personal data, amending Law No. 78-17 of January 6, 1978, relating to information technology, computer files and civil liberties, transposes the Framework Directive of October 24, 1995, and certain provisions of the Directive of July 12, 2002, into French law.

Law No. 2004-575 of June 21, 2004, on confidence in the digital economy and Law No. 2004-669 of July 9, 2004, on electronic communications and audiovisual communication services, have also transposed certain provisions of the Directive of July 12, 2002, into French law.

The main provisions of Law No. 2004-801 of August 6, 2004, are as follows:

- Article 7 of Law No. 2004-801 establishes the principle that no personal data may be processed without the consent of the person concerned. This article does, however, set forth a limited number of circumstances in which such processing may be lawful, even without the consent of the person concerned. This applies in particular if it is necessary in the legitimate interests of the data processor or the recipient "provided that it does not disregard the interests or infringe the fundamental rights and freedoms of the person concerned". Such exceptions do not, however, apply to the processing of "sensitive data", for which Article 8 of Law No. 2004-801 requires the express consent of the person concerned.
- The data processor's obligation to provide information covers all situations in which personal data is being processed, even if this data has not been collected directly from the person concerned (file transfers). In the latter case, Article 32-III of Law No. 2004-801 states that the data processor must

provide this information as soon as the data is recorded or, at the latest, when the data is first divulged to a third party. This information is not necessary, however, if the sole purpose of the processing is to permit or facilitate communication by electronic means.

In addition to the obligation to inform people of the mandatory or optional nature of their responses, of the consequences of any failure to respond, of the recipients of the data and of their right to access and correct their personal data, Article 32 of Law No. 2004-801 imposes on data processors the obligation to inform the person from whom the personal data is collected of the identity of the data processor, the purpose for which the data is processed, and of their right to object to the information being transferred to a third party, as well as, where necessary, of any proposed transfers of data to a country which is not a member state of the European Community.

This obligation is immediately applicable and concerns all types of processing. Companies have until August 6, 2007, to comply with the new requirements in respect of processing which was implemented before Law No. 2004-801 entered into force.

The obligation to provide information also applies to cookies. Article 32-II of Law No. 2004-801 states that “anyone using a communications network must be clearly and fully informed about the purpose of any action taken to access, by electronic means, information stored in their connection terminal or to enter, by similar means, any information in its terminal equipment [and] about the means he or she may take to refuse this”.

- Law No. 2004-801 is also characterized by the very considerable increase in the means which can be used to ensure compliance. The powers of oversight, investigation, injunction and sanction available to the French national commission for information technology and freedom, the *Commission Nationale de l'Informatique et des Libertés* (CNIL) have been substantially increased. Furthermore, any failure to comply with the provisions of Law No. 2004-801 is now subject to harsher criminal sanctions. Breaches of the law and the penalties to be applied are provided for in Articles 226-16 to 226-24 of the Criminal Code. Such breaches may be subject to a fine of up to 300,000 euros and 5 years in prison.

As far as spam is concerned, Article 22 of Law No. 2004-575 of June 21, 2004, on confidence in the digital economy, prohibits, as from December 22, 2004, “direct marketing by means of automatic calling systems, fax or email, using the contact details of a private individual who has not given prior consent to receiving such material by these means”. Any unsolicited commercial communications sent by email to private individuals will henceforth require prior permission from the person to whom they are sent.

With respect to location data, Articles L.34-1, L.34-2, L.34-3, L.34-4 and L.34-5 of the Post and Electronic Communications Code, as amended by Law No. 2004-669 of July 9, 2004, state that such data may only be processed if it has been made anonymous, or with the consent of the users or subscribers concerned. Location data may only be processed for the sole purpose of providing a specific value added service and only for the duration of the provision thereof. The users concerned must be informed in advance of the type of location data which will be processed, of the purpose and duration of the processing and whether the data will be transmitted to a third party. It must, in particular, be possible for users to withdraw their consent on a temporary basis, using a simple means and free of charge, apart from the actual cost of transmitting their withdrawal of consent.

And finally, **in the case of directories**, Article L.34 of the Post and Electronic Communications Code states that subscribers must be given the opportunity to decide if their personal data is to be included in a public directory and, if so, which data may be included. No charge is to be made for being excluded from a public subscriber directory, or for checking, correcting or removing personal data from the directory in question (Article R.10 of the Post and Electronic Communications Code).

In the course of its business, the Group records and processes statistical data, including in particular data concerning the number of visits to its websites. Technical means identifying customers' main areas of interest and online behavior are also used in order to optimize the Group's services. In order to offer its services, the Group collects and processes personal data. The majority of the databases it has established for this purpose have been declared to the CNIL.

Legal protection of databases

The principal innovation presented in the directive adopted on March 11, 1996 (Directive 96/9/EC) is the creation of a *sui generis* right which aims to ensure the protection of the investment made in obtaining, verifying or presenting the contents of a database for the limited duration of the right, it being specified that this investment may take the form of financial and/or human resources. This directive was transposed into French law by Law No. 98-536 of July 1, 1998, providing for this *sui generis* right, independently of the protection offered by copyright, in order to protect the producers of databases.

Article L. 341-1 of the Intellectual Property Code provides that the producer of a database, understood to be the person taking the initiative and bearing the risk of the investments relating to the preparation of the database in question, benefits from a protection of the content of the database “when its compilation, verification or presentation involves a substantial financial, material or human investment”. This protection is independent and applies without prejudice to the protection resulting from copyright or any other right relating to the database in question or one of its component parts, pursuant in particular to Article L. 112-3 of the Intellectual Property Code.

The producer of the database therefore has the right to prohibit any substantial extraction of the content of its database and any reuse of this content. Article L. 342-2 of the Intellectual Property Code also states that “the producer can also prohibit the repeated and systematic extraction or reuse of parts of the content of the database that are not qualitatively or quantitatively substantial when these operations manifestly exceed the normal conditions of use of the database”.

Intellectual property law and online broadcasting

The purpose of Directive 2001/29/EC of May 22, 2001, on “the harmonization of certain aspects of copyright and related rights in the information society” is to adapt intellectual property law to the specifics of digital broadcasting. A draft bill presented to the Council of Ministers on November 12, 2003, for the transposition of this directive into French law, will be examined by Parliament during 2005. The transposition of this directive was supposed to have been completed by December 2002, and in July 2003 the European Commission instigated proceedings against France for its failure to transpose this directive.

This directive introduces a mandatory exception for reproduction as part of a technological process, but does not achieve its primary objective of harmonization, as Member States are able to choose whether or not to adopt other optional exceptions, such as the exception for reproduction for private use, accompanied by fair compensation.

Domain names

Domain names are assigned to the digital addresses of the servers connected to the Internet and constitute Internet addresses. They are used for easier identification of Internet sites and make it easier to remember the addresses of these sites. Domain names are logically, therefore, major marketing advantages for companies carrying out all or part of their business on the Internet. The Group has registered a certain number of domain names in France.

Top level domain names can be generic (known as generic top level domain names, or “gTLDs”), such as “.com” for commercial companies, “.net” for companies providing Internet-related services, “.org” for public interest bodies or “.edu” for teaching establishments, or they can correspond to a specific geographical area (known as country code top level domain names, or “ccTLDs”), such as “.fr” for France, “.de” for Germany or “.es” for Spain. Second level domain names correspond to subcategories, for example “.asso.fr” for associations. The domain names in the “.com”, “.net” and “.org” domains are registered by a certain number of organizations accredited by the Internet Corporation for Assigned Names and Numbers (“ICANN”), an international not-for-profit organization. Various registrars are responsible for managing extensions, such as Verisign in the case of the “.com” and “.net” extensions. The registration of geographical domain names is supervised in each country by a designated national authority, which keeps a central register and accredits private companies as registrars. In general, domain names are allocated on a “first-come, first-served” basis and most registrars, in the case of both generic or geographical domain names, consider that it is up to the person registering them to ensure that no prior right would be infringed by the registration of the domain name concerned.

Each national authority is, to a certain extent, able to define its own policy for the allocation of domain names, which means that the requirements for registering geographical domain names can differ from those relating to the registration of generic domain names and can also vary from one country to another. Some registrars may, for instance, prove to be stricter than others with respect to infringements of the intellectual or other property rights held by third parties resulting from the registration of a particular domain name.

In France, the *Association Française pour le Nommage Internet en Coopération* ("AFNIC") is responsible for registering domain names for the ".fr" extension. A certain number of subdomains have been created in the ".fr" extension and several Internet service providers, including Online, a subsidiary of Iliad, have been accredited by the AFNIC to handle requests for the registration of domain names.

The rules for allocating domain names are set out in the AFNIC's naming charter. This charter is constantly changing and the rules for allocation are changed on a regular basis. The allocation rules currently in force, since January 3, 2005, are as follows:

- the allocation of a domain name in each subdomain of the ".fr" domain is governed by specific rules;
- since May 11, 2004, it is no longer necessary to prove the right to a name to register a domain name directly in the ".fr" domain. Persons identifiable in the online databases of court registries or of the INPI or the INSEE (companies, trademark owners, local authorities, professional associations) can register the domain names of their choice, provided they comply with the syntax rules and do not try to register a name which is included in the list of prohibited terms;
- those registering domain names must ensure that their registration request is not in breach of prior rights held by third parties, particularly intellectual property rights or the right to one's name, or of competition rules, and it should be noted that the AFNIC does not carry out any checks of this kind;
- the registration of domain names in the ".tm.fr" subdomain is only available to applicants who can produce a trademark registration certificate;
- the ".nom.fr" subdomain is only available to individuals of French nationality or residing on French territory who wish to use their surname as a domain name; and
- domain names can be freely registered in the ".com.fr" subdomain without the need to produce supporting documentation, provided that these domain names have not already been registered in another subdomain.

Even though the French courts have now accepted that the use of a term on an Internet site or as a domain name can infringe trademark rights, the outcome of any potential disputes in this area remains uncertain. This uncertainty is due in particular to the fact that the scope of trademark rights is limited, either geographically or by the type of products and services covered by the trademark registration, while the use of a term on the Internet can result in a risk of confusion or encourage unfair competition way beyond these limits.

4.12.6 Industrial and environmental risks

The sector in which Iliad operates is not a major source of harm to the natural environment, does not require any significant samples to be taken of the natural environment surrounding Iliad's activities and does not have any significant impact on the quality of the environment.

4.13 INSURANCE AND COVERAGE OF RISKS

The Group's strategy is to obtain insurance from an outside source to cover the risks which can be insured at reasonable cost. Its current insurance policies cover the Group companies' property, operating losses and third party liability, under normal terms.

The cost of Iliad's insurance cover for all the companies of the Group as of December 31, 2004, stood at approximately €0.7 million for all the insurance premiums paid by the Group companies. In order to obtain the best possible coverage for all the Group's companies, Iliad uses the services of its Internet insurance brokerage company, Assunet, which negotiates the insurance policies on its behalf. The Group's main policy covers third

party liability in case of fire as required by France Télécom in respect of its occupancy of the co-location facilities, for an insured sum of €76.2 million. Three specific insurance policies each with a maximum insured sum of €7.6 million for bodily injury and €1.5 million for material damage have also been effected to cover the use of the Paris municipal highways for the roll-out of Free's metropolitan network in the capital and to cover the use of deactivated optical fiber pairs belonging to Electricité de Strasbourg, as well as those installed on public property owned by the city of Reims. The Group has arranged a general policy to cover property damage, with an insured sum of €7.62 million. Finally, the Group also, in March 2005, arranged third party liability cover for the managers and corporate officers of the company, in order to cover any type of complaint which might be made against the managers of the group, with an insured sum of €15 million per claim.

Iliad considers that this insurance cover takes into account the nature of the risks incurred by the companies of the Group and matches the scope of other insurance cover currently available on the market for groups of a similar size and with similar business activities.

CHAPTER 5

ASSETS – FINANCIAL POSITION – RESULTS

5.1 KEY CONSOLIDATED FINANCIAL DATA

(in € thousands)	Year ended December 31,		
	2004	2003	2002
STATEMENT OF INCOME			
Revenues	491,446	293,051	160,263
Other operating revenue	3,900	1,837	379
Total operating revenues	495,346	294,888	160,642
Operating expenses	442,256	259,921	125,545
Operating income	53,090	34,967	35,097
Net interest income/(expense)	2,735	(940)	(2,447)
Operating income after interest	55,825	34,027	32,650
Exceptional items	5,168	116	(2,747)
Amortization of goodwill	254	313	95
Income before tax	60,739	33,830	29,808
Corporate income tax	19,907	(45)	5,980
Net income	40,832	33,875	23,828
Diluted earnings per share	0.75	0.67	0.47
Earnings before interest, tax, depreciation and amortization (EBITDA)	108,672	53,643	43,249
BALANCE SHEET:			
Fixed assets	278,204	124,344	39,871
Operating assets	117,789	85,202	61,755
Cash and marketable securities	30,548	11,357	15,756
Total assets	426,541	220,903	117,382
Shareholders' equity	178,285	55,227	25,638
Provisions for contingencies and charges	1,492	6,745	5,470
Borrowings	29,354	20,877	15,023
Operating liabilities	217,410	138,054	71,251
Total liabilities and shareholders' equity	426,541	220,903	117,382
CASH FLOWS:			
Net cash provided by operating activities	139,131	91,410	48,976
Net cash used by investing activities	(210,700)	(97,300)	(25,097)
Net cash provided by financing activities	84,054	1,843	(11,991)
Change in cash and cash equivalents	12,485	(4,047)	11,888
Net cash and cash equivalents at year-end	23,158	10,673	14,720

5.2 MANAGEMENT REPORT

5.2.1. Overview

The Group's operations are made up of three business segments:

- The Internet segment, which includes Internet service provider operations (under Free and related brands) and hosting services (the brands Online and BookMyName);

- The Telephony segment, which includes fixed-line telephony (One.Tel and Iliad Telecom), prepaid phone cards (Kertel) and resale of minutes to operators (Kedra);
- Other Services, which include directory services (mainly the ANNU reverse look-up directory accessible by Minitel, telephone, Internet and SMS text messaging) and e-commerce operations (Société.com and Assunet.com).

These business segments may change in the future, based on the development of Group operations and according to operating criteria.

The Group's scope of operations remained unchanged in 2004. There were no notable changes in percentages of control and interest.

Group Management particularly draws the reader's attention to the points of this Management Report presented in the table below, although this list is by no means exhaustive. The Management invites the reader to read this Management Report in its entirety and make his or her own assessment of which points are of particular importance.

Paragraph	Description
5.2.1.1.1. . .	Application of the 5.5% VAT rate for revenues concerning audio-visual content
5.2.1.2. . . .	Change in rates for Option 5 ADSL
5.2.1.3. . . .	Change in depreciation/amortization periods for LDCOM IRUs and Freebox DSLAMs
5.2.2.1.1. . .	Change in provision for the contribution to the Universal Service Fund
5.2.3.	Issuance of shares related to the Iliad Group IPO Change in working capital
5.2.4.	Iliad ownership structure at December 31, 2004

5.2.1.1. Breakdown of revenues

Internet revenues

- **“Pay-as-you-go” access.** For this no-subscription dial-up offer, the customer pays the price of the phone call invoiced by France Telecom. Customers dial the Free access number (08 60 92 20 00) from any fixed line in France, and the call is charged by France Telecom at the local Internet rate. Revenues from the “Pay-as-you-go” offer are therefore directly related to the time customers spend online and to the fee passed on to Free by France Telecom. Free invoices France Telecom on a monthly basis and is paid 45 days after receipt of the invoice. The customer pays France Telecom a connection charge of €0.10 (including tax) and a flat rate of €0.02 per minute (including tax), excluding special offers, 24 hours per day, seven days per week. The fee passed on by France Telecom to Free as the operator of an interconnected network amounts to €0.0231 before tax per minute of use (rate at December 31, 2004). The amount per minute is calculated by France Telecom and approved by the French Telecommunications Regulatory Authority (ART).
- **The “50-hour” plan.** Under the “50-hour plan” launched in April 2001, the customer is entitled to 50 hours of dial-up Internet access per month for a flat fee of €14.94 (including tax). The customer connects to the Internet by dialing a toll-free number (08 68 92 20 00). The subscription fee is paid directly to Free by direct debit at the beginning of each month. Any additional dial-up time and charges for incomplete months are invoiced by Free at the local Internet rate. They are debited to the customer at the beginning of the following month but are recognized in revenue for the current month.
- **Unlimited ADSL broadband offer.** Since October 2002, Free has been offering its customers unlimited broadband access for €29.99 per month (including tax), including use of an ADSL modem and without installation fees. This unique offer allows customers to access the Internet at a speed of at least 2 MB per second and up to 20 MB (observed) in areas where the local loop is unbundled (which depends on whether a subscriber's line is eligible). Free invoices customers by direct debit for their €29.99 monthly subscription. Customers who cancel their subscription are invoiced and charged a termination fee that decreases by €3 for every month of their subscription period, from a maximum of €96 (including tax).

Free lodged an official request with the French Tax Legislation Department asking for detailed information on the VAT rates applicable to subscriptions for television services using the Freebox modem, as well as on breakdowns of revenues by different tax rates. Following this request, based on data provided by Group Management, the French Budget and Budgetary Reform Minister estimated that the portion of television services in the Freebox subscription – the only portion that is eligible for the reduced VAT rate – amounted to 56%. This reduced rate applies for four years as from January 1, 2004. Iliad is required to inform the Ministry of any changes resulting from technological developments or operating procedures, subsequent to which the proportion of revenues taxed at the reduced VAT rate may have to be amended.

- **Telephony via ADSL.** Since August 2003 (unbundled areas) and March 2004 (bundled areas), a telephony service has been offered as part of subscriptions to high speed broadband access using the Freebox modem. Telephone calls made through the Freebox to another Freebox subscriber or to any standard France Telecom line in mainland France (excluding short numbers and special numbers) are completely free. Revenues generated by calls to French mobile phones and to international numbers, as well as revenues generated by incoming calls to Freebox subscribers, are included within the revenues of the Internet segment.
- **Television via ADSL.** Since December 2003, subscribers to very high-speed broadband Internet access via the Freebox, in unbundled areas, have been offered a television service with more than 140 channels, including 53 pay-per-view channels, as of December 2004. Revenues generated by the pay-per-view channels are included within the revenues of the Internet segment. These revenues are subject to 5.5% VAT. Since November 2004, the Canal+ Group channels are also available via Freebox. These offers are billed directly by the Canal+ Group, which pays a commission to Free.
- **Modem offering and migration to the fully unbundled service.** Since June 2004, Free Haut Débit subscribers can request migration from partially to fully unbundled access. Customers are invoiced a fee for this migration that decreases in line with the duration of their subscription period, from a maximum of €90 (including tax). In addition, since September 2004, subscribers who have Sagem modems can receive a Freebox modem in return for a €60 administrative fee for people who have held a subscription for less than one year and €30 for those who have been subscribers for between 12 and 24 months.
- **Hosting services.** Revenues from the hosting of websites are invoiced at a flat annual rate by domain name or by site.
- **Marketing of domain names and selling of advertising space** on Free’s portal.
- **Other Internet-based revenues** corresponding mainly to the sale of switched time to the Telephony segment.

Telephony revenues

Telephony segment revenues are mainly attributable to One.Tel and Kertel and break down as follows:

- **One.Tel’s** offer is a no-subscription carrier preselection offer. By signing up with One.Tel, the customer authorizes the company to make a preselection request to France Telecom so that all calls made from the designated fixed line are transferred to One.Tel (excluding special numbers). This enables the customer to benefit from One.Tel’s rates on all local, national and international calls, as well as on calls to mobile phones, including the €0.01 per minute offer for all local and national calls. At the end of each month, the total cost of calls is calculated for each customer and invoiced for payment within two weeks. Since Iliad took over One.Tel, customers have been strongly encouraged to pay by direct debit in order to reduce the risk of non-payment. As of December 31, 2004, over 84% of customers had signed up for this payment method, compared with 73% at December 31, 2003.
- **Kertel’s** revenues are generated by the use of telephone services. They are recognized as the phone cards are used, but also include what is known as “breakage”, i.e. the unused amount remaining on cards when they reach their expiration date.

Revenues from Other Services

Revenues from the “Other Services” segment mainly come from ANNU, the reverse look-up directory accessible by Minitel, telephone, Internet and SMS text messaging. Minitel access to this service is billed directly by France Telecom on the user’s telephone bill, and part of the fee is passed on by France Telecom to the company running the service. For ANNU, the fee passed on by France Telecom amounts to €36.15 per hour. Fee payments are received on a bi-monthly basis.

Société.com’s e-commerce revenues come from online sales of documents or subscriptions and, to a lesser extent, from advertising. Assunet, an online insurance broker, derives its revenues from commissions on sales of insurance policies to private individuals and to Group companies.

5.2.1.2 Interconnect costs for Option 5 ADSL service (subscribers not on an unbundled line) and Option 1 ADSL (subscribers on an unbundled line)

The Group had three clear financial goals for the roll-out of its network, in addition to the goal of maximizing service quality:

- Increase revenues from “pay-as-you-go” access fees, leveraging Free’s status as an operator;
- Minimize interconnect costs for Free’s “pay-as-you-go” and “50-hour plan” offers and for One.Tel and Kertel telephony services;
- Guarantee high margins for the broadband offer, on the one hand by enrolling new subscribers directly under Option 1, and on the other by migrating Option 5 subscribers (not unbundled) to Option 1 (unbundled) by ensuring that the Group’s network has points of presence at a large number of France Telecom exchanges.

Interconnect operating costs

Direct interconnect costs represent the amounts charged by France Telecom to Free as an operator, as follows:

- Fixed costs corresponding to the rental cost of primary digital blocks and main switching units in the France Telecom network;
- Variable costs calculated based on actual connection time in minutes.

Fixed and variable costs are different depending on whether traffic goes through the digital local exchange or the digital main switching unit. The cost per minute is the same for Free’s “pay-as-you-go” and “50-hour plan” offers, as both involve only a single call collection charge. For local and national calls through One.Tel and Kertel, however, the cost per minute is doubled because there is a call termination charge in addition to the collection charge.

Operating costs of broadband offers

Free’s ADSL offer involves two types of services:

- Option 5 (subscribers not on an unbundled line), representing a France Telecom wholesale offer marketed by Free.
- Option 1 (subscribers on an unbundled line), corresponding to an offer carried entirely by the Free network. Since June 2004, Free Haut Débit subscribers can choose between a partially or fully unbundled service. In the case of the partially unbundled service, users subscribe to the Free Haut Débit broadband offering but continue to pay the telephone line rental to France Telecom and can still make and receive telephone calls through the incumbent operator. Where subscribers opt for the fully unbundled service, they have no commercial link with France Telecom and do not therefore pay a telephone line rental charge. In this case, all telephone calls transit through the broadband connection.

Under Option 1, direct costs per subscriber and per month, as mentioned in the basic unbundling offer, are as follows at December 31, 2004:

Operating costs of Option 1 (partial unbundling)

– Rental of the copper pair and the ADSL splitter:	€2.90
– Copper tie cable:	€1.32

Operating costs of Option 1 (full unbundling)

– Rental of the copper pair:	€10.50
– Copper tie cable:	€1.32

Under Option 5, for a subscription that is sold at the same price, costs per subscriber and per month are as follows:

Operating costs of Option 5

– IP-ADSL CO > 20,000 subscribers (512 Kbps):	€13.00
– IP-ADSL CO < 20,000 subscribers (512 Kbps):	€15.50
– IP-ADSL CO > 20,000 subscribers (1,024 Kbps):	€13.00
– IP-ADSL CO < 20,000 subscribers (1,024 Kbps):	€18.00
– IP-ADSL CO > 20,000 subscribers (2,048 Kbps):	€13.00
– IP-ADSL CO < 20,000 subscribers (2,048 Kbps):	€20.00

The costs of the IP-ADSL collection service vary depending on the bit rate used by Option 5 subscribers. These costs have been changed following the decision of the ART on February 8, 2005.

Option 1 gross margin and EBITDA margin are significantly higher than Option 5 margins. Free's objective is therefore to maximize the proportion of its subscribers registered under Option 1 by encouraging its Option 5 subscribers to migrate to Option 1 or, when technically feasible, by directly making an Option 1 offer available to new customers living in an area where the local loop has been unbundled.

5.2.1.3 Capital expenditures and depreciation/amortization expense

The Group has rolled out a telecommunications network in metropolitan France. Most of the underlying optical fiber for this network was obtained under IRU (Indefeasible Right of Use) contracts with an initial term ranging from 10 to 25 years, that involve a single up-front payment when the fiber is made available. These IRU contracts are recognized as intangible assets and are amortized over the life of the contract. In the first half of 2004, the Iliad Group signed a memorandum of understanding with Neuf Telecom, under which Iliad has the option of extending all IRU agreements between Free and Neuf Telecom, up to December 31, 2030. The amortization period relating to these agreements has been altered accordingly, as Group Management considers that the option will be exercised.

Just as operating costs differ significantly between Option 1 and Option 5, so do levels of capital expenditure on tangible and intangible assets.

In addition to capital expenditures on optical fiber during the network roll-out phase, under Option 1 the Group is required to make available a Freebox modem and a Freebox DSLAM and to pay fees to France Telecom for access to unbundling services. The cost of these three items came to about €200 per customer in 2004. The cost of access to France Telecom's unbundling services is amortized over three years from the date of customer installation. The cost of the Freebox modem is depreciated over the same period, while the Freebox DSLAM, like all other network equipment, was depreciated over six years until June 30, 2004. The Group's R&D team has designed an amended version of the Freebox DSLAM that includes ADSL 2+ technology. The Group is now installing these DSLAMs in France Telecom sites. To provide a consistent quality of service to all of its subscribers, the Group has decided to gradually replace older-version Freebox DSLAMs over a period of 18 months, from July 2004 to December 31, 2005.

As a result of these decisions:

- The final date of use of the older version Freebox DSLAMs has been set at December 31, 2005 and their depreciation period has been altered accordingly;
- The depreciation period for the amended version DSLAMs has been set at 3 years.

Under Option 5, total capital expenditure is lower, amounting to approximately €125 per customer. The cost of access to France Telecom unbundling services is amortized over three years, the same period used for the depreciation of the ADSL modem or Freebox modem provided to the customer.

5.2.1.4 Earnings before interest, tax, depreciation and amortization (EBITDA)

EBITDA (earnings before interest, tax, depreciation and amortization) is one of the key performance indicators used throughout this Management Report.

5.2.2 Comparison of results for the years ended December 31, 2004 and December 31, 2003

The following comments are based on the consolidated financial statements for the years ended December 31, 2004 and December 31, 2003.

The following section reviews revenues, EBITDA and operating income for the Group as a whole and by business segment.

Consolidated revenues and operating expenses disclosed in the financial statements do not match the sum of the segment revenues and expenses in the section below, due to adjustments for inter-segment transactions. The bulk of these inter-segment transactions corresponds to the resale to the Telephony segment of telecommunications services provided over the network operated by Free, for a total amount of €43.4 million in 2003 and €89.7 million in 2004.

Kertel was consolidated as from April 1, 2003. The impact on Group results of consolidating Kertel for the first quarter of 2003 would not have been material.

For ease of reference, in this Management Report operating expenses are presented for the first time net of capitalized production costs (Other operating revenues). These costs correspond to the production cost of the Freebox modems and DSLAMs that are manufactured within the Group and recorded under tangible assets inventories. This new presentation is deemed to better reflect the economic reality of the Group's business. Other operating revenue now only includes reversals of provisions, as well as expense transfers and miscellaneous revenues.

(in € thousands)	Year ended December 31, 2004	Year ended December 31, 2003	% change
Net revenues	491,446	293,051	67.7
Other operating revenue	3,900	1,837	112.3
Purchases used in production and other operating expenses	355,215	220,056	61.4
Payroll costs	22,064	14,421	53.0
Taxes other than on income	3,822	1,623	135.5
Additions to provisions	5,573	5,145	8.3
EBITDA	108,672	53,643	102.6
Depreciation and amortization	55,582	18,676	197.6
Operating income	53,090	34,967	51.8
Net interest income/(expense)	2,735	(940)	NM
Operating income after interest	55,825	34,027	64.1
Exceptional items	5,168	116	NM
Goodwill amortization	254	313	(18.8)
Income before tax	60,739	33,830	79.5
Corporate income tax	19,907	(45)	NM
Net income	40,832	33,875	20.5

Revenues

Revenues for 2004 rose nearly 68% compared to fiscal 2003. Growth was driven by: (i) increased revenues from Internet access, particularly ADSL broadband access, (ii) higher revenues in the Telephony segment thanks to significantly stronger marketing for the One.Tel brand, (iii) the new sales momentum enjoyed by Kertel's teams since their integration into a telecommunications group, as well as the consolidation of Kertel's revenues over a full year.

Operating expenses

Operating expenses, excluding depreciation and amortization expense, increased 60% in 2004, to €386.7 million. Against a backdrop of rapid revenue growth, the Group has crossed the inflection point beyond which the increase in revenues outpaces that in net operating expenses.

Operating income

Operating income rose significantly, to €53.1 million in 2004, up from €35.0 million one year ago. This growth reflected the combined impact of greater profitability in the Internet segment, thanks to the ever-increasing proportion of broadband subscribers on unbundled lines, and improved operating income in the Telephony segment. It was, however, partly offset by lower margins in the ANNU directory business.

In addition, capital expenditure on equipment for broadband customers fueled a threefold rise in depreciation and amortization expense between 2003 and 2004, to €55.6 million. This represents over 11% of revenues, compared with just over 6% in 2003.

Earnings before interest, tax, depreciation and amortization (EBITDA)

Group EBITDA totaled €108.7 million in 2004, rising 102.6% compared to 2003. This jump was mainly the result of signing up new ADSL subscribers directly under Option 1, in addition to migrating existing Option 5 subscribers to Option 1. The Group EBITDA margin also improved from 18.3% in 2003 to 22.1% in 2004.

Net interest income

Net interest income totaled €2.7 million in 2004. This total includes interest income from cash investments relating to proceeds from the IPO, as well as exchange-rate gains on purchases of Freebox components and reversals of provisions for investments, offset by interest expense on borrowings and on lease financing obtained by Free.

Exceptional items

Exceptional items mainly include revenues from asset disposals, in the form of sales of shared France Telecom collocation rooms, and of Free's invoicing, in accordance with the general terms of sale, of Sagem and Freebox modems not returned by customers following the canceling of their subscription.

The Group recorded the following as exceptional income in 2004: (i) a gain of €1.6 million from the sale of an office building; (ii) a gain of €2.6 million on the waiver by Siris of a One.Tel receivable as part of the memorandum of understanding signed in December 2004; and (iii) two reversals of provisions for contingencies and charges in One.Tel's accounts, amounting to €2.0 million. The Group recorded an exceptional expense of some €730,000, corresponding to the withdrawal of the Kertel billing platform.

Income before tax

Income before tax rose 79.5% compared to 2003, reaching €60.7 million.

Net income

Net income amounted to €40.8 million in 2004, up from €33.9 million in 2003. The income tax charge for 2004 was €19.9 million, versus no tax charge for 2003.

5.2.2.1 Analysis of results for the Internet segment

The Internet segment includes the following operations:

- Internet Service Provider (ISP) operations, both through the switched telephone network and via ADSL, marketed under the Free, Free haut débit, Free Telecom and Freebox brands;
- Hosting and domain-name creation services, marketed under the Online and BookMyName brands.

Free is the Group subsidiary responsible for operating the Group's telecommunications network.

(in € thousands)	Year ended December 31, 2004	Year ended December 31, 2003	% change
Net revenues	394,052	215,042	83.2
Other operating revenue	2,778	1,139	143.9
Purchases used in production and other operating expenses	291,573	173,485	68.1
Payroll costs	16,773	9,170	82.9
Taxes other than on income	2,731	1,027	165.9
Additions to provisions	3,268	3,333	(2.0)
EBITDA	82,485	29,166	182.9
Depreciation and amortization	54,226	17,423	211.2
Operating income	28,259	11,743	140.6

Revenues

The table below shows the breakdown by category of consolidated revenues for the Internet segment for the years ended December 31, 2004 and December 31, 2003, as well as the percentage change between these two years.

(in € thousands)	Year ended December 31, 2004	Year ended December 31, 2003	% change
ISP revenues (<i>Pay-as-you-go, 50-hour plan, ADSL</i>)	322,179	177,118	81.9
Hosting and advertising revenues	6,294	4,743	32.7
Inter-segment and other revenues	65,579	33,181	97.6
Total revenues	394,052	215,042	83.2

Internet segment revenues for fiscal 2004 grew by €179.0 million or 83% compared to fiscal 2003, mainly due to the success of Free's ADSL broadband offer.

ISP revenues

	At December 31, 2002	At December 31, 2003	At June 30, 2004	At December 31, 2004
ADSL subscribers	99,100	485,000	768,000	1,064,000
Of which customers on unbundled lines	3,300	163,000	355,000	566,000
Percentage of unbundled line customers	3.3%	33.6%	46.2%	53.2%
Share of residential market¹	7.2%	15.0%	16.8%	17.4%

ISP revenues (Free, Free Telecom and Free haut débit), through both the switched telephone network and ADSL, totaled €322.2 million for the year ended December 31, 2004.

Revenue growth in the ISP business resulted from the following factors:

- **Continuing success of the broadband offer.** At December 31, 2004, broadband customers numbered nearly 1,064,000, against 485,000 at December 31, 2003. This 119.4% increase was achieved despite a

reduction in market share in the fourth quarter of the year, primarily caused by an advertising campaign launched by France Telecom which was subsequently held by the French courts to be parasitic advertising;

- **Use of the new paying services available through the Freebox (telephony and television).** In 2004, revenues related to these services totaled nearly €13.5 million;
- **Decline in the “pay-as-you-go” and “50-hour plan” dial-up offers.** Call minutes generated by the pay-as-you-go offer declined almost 24% to around 1.6 billion minutes in 2004 from some 2.1 billion in 2003. As regards the 50-hour plan, the number of subscribers declined from 211,000 in January 2004 to 143,500 by the end of the year.

Hosting and advertising revenues

The marketing of domain names in France, value-added hosting services and the sale of advertising space (including the sale of sponsored links as part of a partnership with Google) on Free’s portal generated hosting and advertising revenues of €6.3 million in 2004. The €1.6 million increase compared with 2003 was driven by a 21% rise in hosting revenues and an increase of nearly 40% in advertising revenues on the back of sustained volume growth in online advertising in France during the year.

Inter-segment and other revenues

Inter-segment and other revenues correspond primarily to the resale to the Telephony segment of call minutes on Free’s directly-operated network. Growth in these revenues in 2004 mainly reflected higher revenues in the Telephony segment.

Purchases used in production and other operating expenses

Purchases used in production and other operating expenses were 68% higher in 2004 than in 2003. Operating expenses for the Internet segment are rising at a slower pace than revenues, as a result of the unbundling strategy adopted by the Group. The key factors causing operating expenses to fall as a proportion of revenues are as follows:

- The rising proportion of Option 1 ADSL subscribers among total broadband customers, reaching 53.2% at December 31, 2004, up from 33.6% at January 1, 2004.
- The overall decline in costs of Option 5 subscriptions (see paragraph 1.2.1.2), offset by the opportunity offered to subscribers of increasing their available bandwidth from 512 Kbps to 1,024 Kbps and subsequently 2,048 Kbps, thereby raising Free’s costs of IP connection and transit.

In addition, Free’s decision to use France Telecom POP and Interlan optical fiber connections had a negative impact on operating expenses in 2004, because some of these connections, which are being billed to Free as rental expenses, were not used during the year.

Payroll costs

The rise in payroll costs in the Internet segment was a direct result of the recruitments carried out at Centrapel to handle the surge in demand for the ADSL broadband offer. Centrapel’s payroll costs rose to €12.9 million from €5.7 million in 2003, reflecting an increase in the company’s average number of employees (including part-time employees) from 239 in 2003 to 517 in 2004.

Additions to provisions

Additions to provisions amounted to €3.3 million in 2004, and primarily corresponded to provisions for doubtful customer accounts. In percentage of revenue terms, this figure was on a par with 2003, when total additions to provisions came to €3.3 million, including €1.7 million set aside for contributions to the French Universal Service Fund.

As stated in the management report for the year ended December 31, 2003, calculations of contributions to the Universal Service Fund have undergone a number of changes in recent years, for all telecommunications operators, including Free. The situation was clarified in 2004, following a Decree dated November 17, 2004, published in the *Journal Officiel* on November 19, 2004, which set out the definitive calculation rules. This Decree approved the use of a percentage of revenues as the basis for calculating contributions to the Fund and also confirmed the powers of the French Telecommunications Regulatory Authority (ART) in relation to determining the costs of the Universal Service. By way of a decision dated December 19, 2004, published in the *Journal Officiel* on December 21, 2004, the ART set the final amount of the Universal Service Fund at €124.9 million for 2002 and the contribution rate at 0.42% of telecommunications revenues. For 2003 and subsequent years, Iliad's Management has adjusted the Group's liability for Universal Service contributions using 0.43% of telecommunications revenues as the calculation base. This led to a €2.6 million reversal from the related provision in 2004, which represented the majority of the amount recorded under other operating revenue for the Internet segment during the year. The amount payable for the Universal Service contributions in 2004 represented an operating expense of €1.1 million.

EBITDA and operating income

Internet segment EBITDA for 2004 was up almost 183% on the prior-year figure. Excluding inter-segment transactions, the EBITDA margin for the Internet segment rose to 24.9% from 16.0% in 2003. This performance was the result of the greater number of France Telecom sites connected with optical fiber or rented lines, which made it possible to increase the number of subscribers having access to broadband connections through the unbundling of the local loop (Option 1).

In 2004, the number of connected France Telecom sites rose from over 160 to nearly 410. The number of unbundled lines leapt to 566,000 at December 31, 2004, from 163,000 at December 31, 2003. This high number of Option 1 subscribers demonstrates the validity of the Group's strategy of encouraging migration from Option 5 to Option 1, as well as Management forecasts of EBITDA trends.

Operating income for the year ended December 31, 2004 came to €28.3 million, representing a €16.5 million increase compared to 2003.

5.2.2.2 Analysis of results for the Telephony segment

The Telephony segment includes the following operations:

- Fixed-line telephony and prepaid phone card operations under the One.Tel and Kertel brands;
- Telephony services provided to operators by Kedra.

(in € thousands)	Year ended December 31, 2004	Year ended December 31, 2003	% change
Net revenues	162,976	96,366	69.1
Other operating revenue	979	664	47.4
Purchases used in production and other operating expenses	134,304	73,823	81.9
Payroll costs	2,737	3,033	(9.8)
Taxes other than on income	819	347	136.0
Additions to provisions	2,286	1,810	26.3
EBITDA	23,808	18,017	32.1
Depreciation and amortization	1,069	957	11.7
Operating income	22,739	17,060	33.3

Revenues

The table below shows the breakdown by category of consolidated revenues for the Telephony segment for the years ended December 31, 2004 and December 31, 2003, as well as the percentage change between the two years.

(in € thousands)	Year ended December 31, 2004	Year ended December 31, 2003	% change
Fixed telephony and prepaid phone card revenues . . .	123,492	75,269	64.1
Revenues from services to operators and inter-segment sales	39,484	21,097	87.1
Total revenues	162,976	96,366	69.1

Revenues for the Telephony segment for fiscal 2004 rose by nearly €66.6 million, or 69.1%, compared to fiscal 2003.

Fixed telephony and prepaid phone card revenues

Revenues from fixed telephony and prepaid phone cards, generated primarily by One.Tel and Kertel, amounted to €123.5 million for the year ended December 31, 2004.

Revenue growth stemmed primarily from the combination of the following three factors:

- **Growth in the number of One.Tel customers in 2004.** As stated at the time of the Group's IPO, raising the number of One.Tel subscribers was one of the priorities for Management. As a result of more extensive and precisely targeted marketing expenditure, the number of invoiced customers rose to 335,000 in December 2004, up almost 56% from the 215,000 at December 31, 2003;
- **A slight contraction (9%) in average revenue per user (ARPU);**
- **Contribution from Kertel.** Further to the Group's acquisition of Kertel in March 2003, the company's new sales organization and pricing structure has boosted sales of prepaid phone cards, with 7.5 million sold in 2004, compared to 4.9 million the previous year.

Revenues from services to operators and inter-segment sales

The increase in revenues from services to operators and inter-segment sales was mainly attributable to a greater volume of transactions with the Internet segment, and with Free in particular, which centralizes all purchases of minutes by the Group.

Purchases used in production and other operating expenses

Purchases used in production and other operating expenses rose 81.9% in 2004 compared to the prior year, while revenues increased 69.1%.

This outpacing of growth in revenues by operating expenses was mainly due to rising interconnect costs related to greater traffic from One.Tel customers and users of Kertel cards, as well as the significant increase in marketing expenses for One.Tel, as had been announced at the time of Iliad's IPO.

Payroll costs

The reduction in payroll costs in the Telephony segment reflects the economies of scale that can be achieved in alternative fixed-line telephony operations.

EBITDA and operating income

The Telephony segment's EBITDA came to €23.8 million in 2004, €5.8 million up on the 2003 figure. At the time of the IPO, Iliad's Management had undertaken to maintain the EBITDA of the Telephony segment or achieve a slight increase, despite the forecast rise in the marketing budget. The EBITDA margin, excluding inter-segment sales, came to 16.2%.

2004 operating income for the Telephony segment climbed to €22.7 million.

5.2.2.3 Analysis of results for the Other Services segment

The Other Services segment includes:

- Reverse look-up directory services, one of Iliad's historic businesses, marketed under the names 3617 ANNU and Annu.com, accessible via Minitel, telephone, Internet and SMS text messaging;
- E-commerce operations, including Assunet.com, an online insurance broker, and Société.com, an online provider of financial information.

(in € thousands)	Year ended December 31, 2004	Year ended December 31, 2003	% change
Net revenues	24,152	25,026	(3.5)
Other operating revenue	142	35	NM
Purchases used in production and other operating expenses	19,071	16,132	18.2
Payroll costs	2,533	2,218	15.1
Taxes other than on income	272	249	9.2
Additions to provisions	19	2	NM
EBITDA	2,379	6,460	(63.2)
Depreciation and amortization	287	296	(3.0)
Operating income	2,092	6,164	(66.1)

Revenues

Overall revenues from Other Services contracted by 3.5% in 2004.

Directory services revenues contracted by almost 30% in 2004, reflecting the slow but sure fall-off in use of the Minitel in France since 1998. Even though directory services have generally held up better than leisure or other non-work-related Minitel services, the Group has markedly felt the impact of this decline since the end of 2001, which could not be offset by growth in e-commerce revenues.

Purchases used in production and other operating expenses

The increase in purchases used in production mainly reflected higher headquarters costs and marketing expenditure re-invoiced to other Group entities, in particular One.Tel.

EBITDA and operating income

Despite decreasing revenues, the Group's reverse look-up directory services remain profitable, contributing to the Other Services segment's EBITDA of €2.4 million and operating income of nearly €2.1 million for fiscal 2004.

5.2.3 Liquidity and capital resources

(in € thousands)	Year ended December 31,		
	2004	2003	2002
CASH FLOWS:			
Cash flows provided by operating activities	139,131	91,410	48,976
Cash flows used by investing activities	(210,700)	(97,300)	(25,097)
Cash flows provided by financing activities	84,054	1,843	(11,991)
Change in cash and cash equivalents	12,485	(4,047)	11,888
Net cash and cash equivalents at year-end	23,158	10,673	14,720

The Group's sources of financing include operating cash flows on a recurrent basis. In addition, cash proceeds from the issue of shares at the time of Iliad's IPO of January 30, 2004, with the greenshoe clause, allowed Iliad to raise approximately €91.6 million net of IPO costs.

As regards Group operating cash flow, the contribution to working capital amounted to nearly €39 million (or 7.9% of revenues) in 2004, as opposed to €41.2 million (14% of revenues) for 2003. Although Group revenues rose by more than 68%, working capital generation fell to 77 days of sales in 2004 versus 81 in 2003, as a direct result of the Group's strategic decision to provide a Freebox modem to every new subscriber.

In the consolidated financial statements, amounts due to fixed asset suppliers are not accounted for separately from amounts due to suppliers of goods and services. The average payment period for Iliad Group suppliers improved slightly in 2004, corresponding to 90 days.

Another factor to be noted in relation to cashflows is that DSLAMs had to be manufactured in 2004 to respond to the extension of unbundled areas, with the number of installed units rising from 575 at December 31, 2003 to nearly 1,342, including 419 ADSL 2+ DSLAMs. Further, the Group is constantly in a credit position with the tax authorities in terms of VAT, as on average, VAT credits are only repaid every four and a half months. The related VAT receivables amounted to some €13.5 million at December 31, 2004.

Aside from Freebox modems and DSLAMs, network optical fiber makes up the bulk of acquisitions of fixed assets, which broke down as follows in 2004:

- Acquisitions of intangible assets (including IRU contracts, France Telecom collocation rooms and access fees to the France Telecom service): €102.6 million;
- Acquisitions of tangible assets (including Freebox modems and DSLAMs, transmission equipment, etc.): €112.2 million.

On June 11, 2004, Iliad paid out a dividend of €0.10 per share (excluding the *avoir fiscal* tax credit), representing a total payout of €5.3 million.

On December 19, 2004, Iliad paid out an interim dividend of €0.075 per share (excluding the *avoir fiscal* tax credit), representing a total payout of €4.0 million.

In the second half of 2004, Iliad purchased the Free shares issued on the exercise of founders' share subscription warrants (BSPCE) by Free employees, for a net amount of €1.6 million. These share purchases were in line with the Group's decision to retain full control of its subsidiary, Free, in 2004.

5.2.4 Ownership structure at December 31, 2004

At December 31, 2004, Iliad's capital stock was composed of 53,452,230 ordinary shares, breaking down as follows:

- Executive Management: 42,051,013 shares, or 78.6% of capital stock
- Goldman Sachs Fund: 936,670 shares or 1.8% of capital stock
- Public: 10,464,547 shares or 19.6% of capital stock

At December 31, 2004, outstanding options exercisable for Iliad shares broke down as follows: founders' share subscription warrants (BSPCE) exercisable at any time for a total of 699,320 shares and Iliad share subscription options exercisable as from February 2008 for a total of 444,132 shares.

5.2.5 Off-balance sheet commitments

The table below analyzes the Group's commitments under non-cancelable leases at December 31, 2004 by type of asset and by maturity. See also the information provided in the notes to the consolidated financial statements.

(in € thousands)	Within	1 to 2	2 to 3	3 to 4	4 to 5	Beyond	TOTAL
Type of leased asset	1 year	years	years	years	years	5 years	
Real estate	4,387	4,302	4,076	4,072	2,307	1,755	20,899
Vehicles.	182	132	23	—	—	—	337
Equipment	681	542	72	—	—	—	1,295
Other	414	313	199	160	129	859	2,074
TOTAL.	5,664	5,289	4,370	4,232	2,436	2,614	24,605

5.2.6 Group indebtedness

- (i) As far as Iliad is aware, the Group is not subject to any liquidity risk as a result of prepayment clauses entered into by Group companies or as a result of non-compliance with financial covenants (ratios, targets, etc.).
- (ii) Outstanding borrowings and obligations under finance leases totaled €21.8 million at December 31, 2004.

At December 31, 2004, the Group had confirmed credit lines of €70 million, available until November 2008, €10 million of which had been drawn down.

5.3 ADDITIONAL INFORMATION

5.3.1 Subsequent events

No material events have occurred since the balance sheet date.

5.3.2 IFRS Transition

A working group has been set up to review the impact of IFRS transition on the Group's accounts. The working group continues its analysis to this date. The Group will respect the AMF recommendation and publish 2004 consolidated accounts concomitantly with 1st half 2005 publication. Based on the analysis conducted thus far, the main issues have been identified as follows:

Presentation of consolidated accounts

Under IFRS, the income statement will not feature exceptional or non-operating items. The balance sheet will be represented on the basis of assets and liabilities maturity.

R&D Expenses (IAS 38)

IAS 38 will probably increase the amount of R&D costs to be immobilized. In the past, the Group was limiting the immobilization of R&D costs only to costs related to the development of new technologies.

Goodwill amortization (IFRS 3)

As of today, the Group amortizes over 10 years maximum the positive goodwill booked in its intangible assets. The amortization will be replaced by an annual valuation of the underlying assets. Based on the actual goodwills, the Group does not believe that the valuation analysis should lead to any loss of value.

IRU (IAS 17)

The Group believes that the current accounting treatment of the IRUs (as an asset) should not be affected by the application of IAS 17. However, the Group is in the process of examining carefully IFRIC 4, released on December 2, 2004, and to gauge its potential impact.

5.4 FINANCIAL STATEMENTS

5.4.1 Consolidated financial statements

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STATUTORY AUDITORS' REPORT ON THE CONSOLIDATED FINANCIAL STATEMENTS

(Year ended December 31, 2004)

PricewaterhouseCoopers Audit

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This is a free translation into English of the statutory auditors' report issued in the French language and is provided solely for the convenience of English speaking readers. The statutory auditors' report includes information specifically required by French law in all audit reports, whether qualified or not, and this is presented below the opinion on the consolidated financial statements. This information includes an explanatory paragraph discussing the auditors' assessments of certain significant accounting and auditing matters. These assessments were considered for the purpose of issuing an audit opinion on the consolidated financial statements taken as a whole and not to provide separate assurance on individual account captions or on information taken outside of the consolidated financial statements.

This report should be read in conjunction with, and construed in accordance with, French law and professional auditing standards applicable in France.

To the shareholders of Iliad S.A.:

In compliance with the assignment entrusted to us by the annual general shareholders' meeting, we have audited the accompanying consolidated financial statements of Iliad S.A. and its subsidiaries for the year ended December 31, 2004.

The consolidated financial statements have been approved by the board of directors. Our responsibility is to express an opinion on these financial statements based on our audit.

I — Opinion on the consolidated financial statements

We conducted our audit in accordance with professional standards applicable in France. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements give a true and fair view of the financial position of Iliad S.A. and its subsidiaries and their assets and liabilities at December 31, 2004, and of the results of operations for the year then ended, in accordance with the accounting rules and principles applicable in France.

II — Justification of our assessments

In accordance with the requirements of article L.225-235 of the Commercial Code relating to the justification of our assessments, we bring to your attention the following matters:

As stated in the accounting principles described in the notes to the financial statements under "Use of estimates", the company's management makes use, in preparing the financial statements, of estimates and assumptions that

affect the amounts provided in these financial statements and their notes. Actual amounts may differ from these estimates.

As part of our evaluation of the material estimates used in the closing of the accounts, our work consisted in reviewing the approaches followed by the management, in accordance with the accounting principles described in note 1.3 to the financial statements, and to confirm that the assumptions used and the valuations resulting therefrom were reasonable.

The assessments were made in the context of our audit of the consolidated financial statements, taken as a whole, and therefore contributed to the formation of the unqualified opinion expressed in the first part of this report.

III — Specific verification

In accordance with professional standards applicable in France, we have also verified the information given in the group management report. We have no matters to report regarding its fair presentation and conformity with the consolidated financial statements.

Paris, April 24, 2005

The Statutory Auditors

PricewaterhouseCoopers Audit

Xavier Cauchois

Boissière Expertise Audit

Tita A. Zeitoun

CONSOLIDATED BALANCE SHEETS

ASSETS	Note	2004	2003	2002
		(in € thousands)		
Fixed assets				
Goodwill	13	4,206	3,869	0
Intangible assets	14	127,383	45,528	14,413
Property, plant and equipment	15	141,241	73,317	24,782
Long-term investments	16	5,374	1,630	676
Total fixed assets		278,204	124,344	39,871
Current assets				
Inventories and work in progress	17	10,086	4,134	5,411
Trade accounts and notes receivable	18	53,693	38,017	30,282
Other receivables and accruals	19	54,010	43,051	26,062
Own shares		63	0	0
Marketable securities	20	2,112	2,571	2,788
Cash and cash equivalents		28,373	8,786	12,968
Total current assets		148,337	96,559	77,511
Total assets		426,541	220,903	117,382

CONSOLIDATED BALANCE SHEETS

LIABILITIES AND SHAREHOLDERS' EQUITY	Note	2004	2003	2002
		(in € thousands)		
Shareholders' equity				
Capital stock	21	10,000	1,000	1,000
Additional paid-in capital.		83,763	1,126	1,126
Retained earnings/(deficit)		43,691	19,226	(315)
Consolidated net income		40,831	33,875	23,827
Cumulative translation adjustment.		0	0	0
Shareholders' equity		178,285	55,227	25,638
Minority interests		0	0	0
Provisions for contingencies and charges . .	23	1,492	6,745	5,470
Liabilities				
Borrowings	24	29,354	20,877	15,023
Trade accounts and notes payable	25	173,409	106,700	51,153
Other payables and accruals	25	44,001	31,354	20,098
Total provisions and liabilities		248,256	165,676	91,744
Total liabilities and shareholders' equity . .		426,541	220,903	117,382

CONSOLIDATED STATEMENTS OF INCOME

		2004	2003	2002
	Note	(in € thousands)		
Revenues	4	491,446	293,051	160,263
Capitalized production costs		83,893	27,729	4,459
Other operating revenue		3,900	1,837	3,79
Purchases used in production.		428,021	243,779	103,066
Payroll costs		22,064	14,421	10,595
Other operating expenses		11,087	4,006	4,012
Taxes other than on income		3,822	1,623	1,738
Additions to provisions	7	5,573	5,145	2,441
EBITDA (earnings before interest, tax, depreciation and amortization)		108,672	53,643	43,249
Depreciation and amortization	7	55,582	18,676	8,152
Operating income		53,090	34,967	35,097
Net interest income/(expense)	8	2,735	(940)	(2,447)
Operating income after interest		55,825	34,027	32,650
Exceptional items	9	5,168	116	(2,747)
Corporate income tax	10	19,907	(45)	5,980
Net income of fully consolidated companies.		41,086	34,188	23,923
Income from companies accounted for by the equity method		0	0	0
Goodwill amortization	13	254	313	95
Net income before minority interests		40,832	33,875	23,828
Minority interests		1	0	1
NET INCOME		40,831	33,875	23,827
Basic earnings per share (in €).	11	0.76	0.71*	0.50
Diluted earnings per share (in €)	11	0.75	0.67	0.47

- Following the ten-for-one share split at end-2003.

CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

(in € thousands)	Capital stock	Additional paid-in capital	Retained earnings/ (deficit)	Net income for the year	Other			Total	Total shareholders' equity
					Cumulative translation adjustment	Revaluation reserve	Treasury stock		
Shareholders' equity at January 1, 2003	1,000	1,126	(315)	23,827	0	/	/	0	25,638
Movements in 2003									
- Issuance of shares									
- Appropriation of 2002 net income			23,827	(23,827)					0
- Dividends paid			(4,286)						(4,286)
- Net income for the year				33,875					33,875
- Translation adjustments									
Shareholders' equity at December 31, 2003	1,000	1,126	19,226	33,875	0	/	/	0	55,227
Movements in 2004									
- Issuance of shares	9,000	82,637							91,637
- Appropriation of 2003 net income			33,875	(33,875)					0
- Dividends paid			(9,354)						(9,354)
- Net income for the year				40,831					40,831
- Impact of recording post-employment benefits			(56)						(56)
Shareholders' equity at December 31, 2004	10,000	83,763	43,691	40,831	0	/	/	0	178,285

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in € thousands)	Note	Year ended December 31		
		2004	2003	2002 ⁽²⁾
CASH FLOWS FROM OPERATING ACTIVITIES				
Net income before minority interests		40,831	33,875	23,828
Adjustments to reconcile net income to net cash provided by operations:				
– Depreciation, amortization and provisions ⁽¹⁾	7	51,286	20,344	11,411
– Changes in deferred taxes	10	8,440	(3,939)	4,115
– Gains on disposals of fixed assets, net of tax		(422)	(37)	(430)
Income from companies accounted for by the equity method		0	0	0
Cash flow of fully consolidated companies		100,135	50,243	38,924
Dividends received from companies accounted for by the equity method		0	0	0
Changes in working capital	12	38,996	41,167	10,052
Net cash provided by operations		139,131	91,410	48,976
CASH FLOWS FROM INVESTING ACTIVITIES				
Acquisitions of fixed assets	14/15/16	(214,992)	(101,104)	(25,912)
Disposals of fixed assets, net of tax		6,032	1,186	738
Effect of changes in Group structure		(1,740)	(2,618)	77
Net cash used by investing activities		(210,700)	(97,300)	(25,097)
CASH FLOWS FROM FINANCING ACTIVITIES				
Iliad SA capital reduction		0	0	(9,835)
Dividends paid to parent company shareholders		(9,354)	(4,286)	(4,000)
Dividends paid to minority shareholders of consolidated companies		0	(1)	0
Issuance of shares		91,637	0	0
New borrowings	24	17,886	14,707	6,309
Repayments of borrowings	24	(16,115)	(8,577)	(4,465)
Net cash provided/(used) by financing activities		84,054	1,843	(11,991)
Change in cash and cash equivalents		12,485	(4,047)	11,888
Cash and cash equivalents at beginning of year	12	10,673	14,720	2,832
Cash and cash equivalents at year-end	12	23,158	10,673	14,720

(1) Excluding provisions against current assets.

(2) The cash flow statement for the year ended December 31, 2002 has been prepared based on pro forma data at January 1, 2002 including One.Tel at that date.

SEGMENT INFORMATION

2004	Internet	Telephony	Other	Eliminations	Consolidated
Revenues					
Revenues from outside Group	330,767	147,304	13,375		491,446
Inter-segment revenues	63,285	15,672	10,777	(89,734)	0
Total revenues	394,052	162,976	24,152	(89,734)	491,446
Earnings					
EBITDA	82,485	23,808	2,379	0	108,672
Operating income	28,259	22,739	2,092	0	53,090
Other information					
Fixed assets	271,221	4,252	2,731		278,204
Depreciation and amortization of operating assets	54,226	1,069	287		55,582
Number of employees at year-end. . . .	667	47	38		752

2003	Internet	Telephony	Other	Eliminations	Consolidated
Revenues					
Revenues from outside Group	182,333	92,988	17,730		293,051
Inter-segment revenues	32,709	3,378	7,296	(43,383)	0
Total revenues	215,042	96,366	25,026	(43,383)	293,051
Earnings					
EBITDA	29,165	18,019	6,459	0	53,643
Operating income	11,743	17,061	6,163	0	34,967
Other information					
Fixed assets	115,467	6,557	2,320		124,344
Depreciation and amortization of operating assets	17,423	958	296		18,677
Number of employees at year-end. . . .	402	58	45		505

2002	Internet	Telephony	Other	Eliminations	Consolidated
Revenues					
Revenues from outside Group	93,347	44,426	22,490		160,263
Inter-segment revenues	8,309	120	3,528	(11,957)	0
Total revenues	101,656	44,546	26,018	(11,957)	160,263
Earnings					
EBITDA	21,626	12,828	8,795	0	43,249
Operating income	14,564	12,104	8,429	0	35,097
Other information					
Fixed assets	37,410	1,123	1,338		39,871
Depreciation and amortization of operating assets	7,062	724	366		8,152
Number of employees at year-end. . . .	178	53	30		261

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1: ACCOUNTING PRINCIPLES

1.1 – Accounting standards

The consolidated financial statements have been prepared in compliance with applicable French generally accepted accounting principles, including *Comité de Réglementation Comptable* standard CRC 99-02.

The presentation and valuation rules applied to the consolidated financial statements are unchanged from last year, except for the impact of recording post-employment benefits.

Standard CRC 02-10 of December 12, 2002 concerning depreciation, amortization and impairment of assets is applicable as from January 1, 2005 and may be implemented early. The Iliad Group did not opt for early application of this standard for its consolidated financial statements for the year ended December 31, 2004.

Recommendation 03-R of April 1, 2003 issued by the French National Accounting Board (*Conseil National de la Comptabilité*) concerning the recognition and measurement of post-employment benefit obligations has been applicable since January 1, 2004. The impact of this recommendation was taken into account when preparing the consolidated financial statements for the year ended December 31, 2004.

Under the French Financial Security Act of August 2, 2003 (*Loi sur la Sécurité Financière*), since January 1, 2004, entities over which a group exercises control have to be consolidated, irrespective of whether the group holds shares in that entity. The Iliad Group does not currently exercise control over any entities in which it does not have legal ownership.

The opinion issued by the Urgent Issues Task Force of the *Conseil National de la Comptabilité* on February 2, 2005 concerning the reform of long-term capital gains taxation in France, applicable since December 31, 2004, will have a non-material €54,000 impact on shareholders' equity. This impact will be recognized in the 2005 financial statements.

1.2 – Basis of consolidation

Consolidation methods

All material companies that are exclusively controlled by the Iliad Group are fully consolidated.

Material companies in which the Iliad Group exercises joint control are proportionally consolidated.

Material companies in which the Iliad Group exercises significant influence over the management and financial strategy are accounted for by the equity method.

Material intercompany transactions and balances are eliminated on consolidation.

Goodwill

Goodwill represents the difference between the cost of shares in consolidated companies and the Group's equity in the fair value of the underlying net assets at the date of acquisition. Fair value adjustments may be made up to the end of the year following the accounting period in which the acquisition takes place. Minority interests are also valued using the fair value method.

Positive goodwill is recorded under the "Goodwill" caption on the assets side of the balance sheet.

Negative goodwill is recorded under "Provisions for contingencies and charges" on the liabilities side.

Goodwill is generally amortized on a straight-line basis over ten years, except when a different period is considered justified based on the assumptions used and objectives set at the time of acquisition, or based on the circumstances of the transaction.

The carrying amount of goodwill is tested annually for impairment, or whenever there is any indication that it may be impaired. Such an indication may arise further to significant unfavorable changes of a lasting nature that may have an impact either on the economic environment or the assumptions made and objectives set at the time of acquisition.

The Iliad Group analyzes and measures the recoverable amount of goodwill at the level of each consolidated company.

Recoverable amount is defined as the higher of fair value, based on market valuations, and value in use.

Foreign currency translation

All consolidated companies have the euro as their operating currency.

Fiscal year-end

All Group companies have a December 31 fiscal year-end.

The income statements of companies acquired during the year are included in the consolidated income statement from the date of their acquisition. The income statements of companies that have been disposed of or liquidated during the year are included in consolidation up to the date of disposal or liquidation.

Information on changes in Group scope are provided in Note 2.

1.3 – Main accounting policies

The main accounting policies applied by the Group are as follows:

Recognition of revenues

a) Main Group revenues

Revenues are recognized as follows in the consolidated financial statements:

- Revenues from usage of connection time are recognized in the period in which the usage took place;
- Revenues from subscriptions and fixed-rate packages are recognized over the period covered by the subscriptions or packages;
- Revenues from the sale of advertising banners are spread over the period during which the banners are displayed;
- Finally, for prepaid telephone cards, invoices are issued at the time of shipping or activating the card, but revenues are recognized only as the card is used (and the corresponding traffic costs are recorded under operating expenses) or at their expiry date. At the balance sheet date, the unused portion of the invoiced amount is recorded under “Deferred income.”

b) Other operating revenue

Other operating revenue is essentially made up of the following:

- Capitalized production costs for modems, Freebox DSLAMs and other specific equipment,
- Reversals of operating provisions.

Research and development expenses

Research and development costs are expensed in the period in which they were incurred, except those relating to the development of new equipment, which are capitalized in the consolidated balance sheet when the costs can be separated out as relating to definite projects which have strong chances of achieving technical success and producing future economic gains.

Earnings before interest, tax, depreciation and amortization (EBITDA)

This indicator corresponds to operating income plus depreciation and amortization of tangible and intangible operating assets.

Foreign currency transactions

Income and expenses in foreign currencies are converted at the exchange rate on the date of the transaction.

Balance sheet items are converted at the period-end rate.

Unrealized exchange gains and losses are taken to the income statement for the period concerned.

Difference between operating and exceptional items

Exceptional income and expenses include both exceptional items relating to ordinary activities and extraordinary items.

Exceptional items relating to ordinary activities correspond to items that are unusual in terms of their size or impact or which arise from events that occur rarely.

Earnings per share

Basic earnings per share are obtained by dividing net income by the weighted average number of shares outstanding during the period.

Diluted earnings per share are calculated by assuming conversion into ordinary shares of all dilutive instruments outstanding at the balance sheet date.

Intangible assets other than goodwill

- Organization expenses are expensed as incurred.
- Capitalized development costs are amortized over a two-year period.
- Registered codes, names, client files and trademarks are amortized over one to ten years depending on the estimated period of use.
- Software is amortized on a straight-line basis over one to three years.
- Amounts paid as consideration for obtaining indefeasible rights of use (IRU) on dark optical fibers are amortized over the term of use of these fibers, which can be 11, 15, 25 or 27 years.
- Access fees for co-location facilities used to conduct unbundling operations are amortized over a 10-year period.
- Other access fees for services, particularly those required for the development of broadband Internet operations, are amortized over three years.

Property, plant and equipment

Property, plant and equipment are recorded on the balance sheet at the acquisition cost, including transaction expenses, or at production cost.

Depreciation is calculated by the straight-line or reducing balance method, as follows:

– Buildings	20 to 30 years	Straight-line
– Technical equipment	3 to 14 years	Straight-line or reducing balance
– General equipment	10 years	Straight-line
– Computer equipment	3 to 5 years	Straight-line or reducing balance
– Office furniture and equipment	2 to 10 years	Straight-line or reducing balance

Finance leases

Material assets acquired under finance leases are capitalized in the consolidated financial statements.

Leases are considered to be finance leases when they have the effect of transferring to the lessee substantially all the benefits and risks inherent in ownership of the asset.

In such cases:

- The assets acquired are recorded in the balance sheet at their value at the inception of the lease or at fair value for leases in progress when a subsidiary is consolidated for the first time. They are depreciated over their probable useful lives.
- The related obligation is recorded under short- and long-term debt, based on the lease terms.
- Lease payments are allocated between the repayment of the obligation and interest expense.

Gains and losses on lease-back operations are recognized over the term of the lease.

Long-term investments

Shares held in companies which do not fulfill the Group’s consolidation criteria are recorded in the balance sheet at the lower of cost and fair value to the Group.

Cost does not include transaction expenses. Fair value to the Group is determined based on the net assets of the company concerned and its projected future earnings.

Inventories

Inventories are valued by the FIFO (first-in first-out) method.

Where appropriate, inventories are written down to probable realizable value. In this case, the amount of the provision includes the estimated costs remaining to be incurred up to the date of sale.

Accounts and notes receivable

Accounts receivable are recorded on the balance sheet at nominal value. A provision is recorded for doubtful accounts based on the estimated risk of non-recovery.

The likelihood of payment is estimated based on an individual or statistical assessment of the risk of default on the receivable concerned.

Deferred taxes

Deferred taxes are computed by the liability method on:

- all timing differences between the recognition of income and expenses for financial reporting and tax purposes, except for goodwill and valuation differences related to unamortized intangible assets that cannot be disposed of without selling the acquired company,
- tax loss carryforwards when their utilization is considered probable,
- consolidation adjustments and eliminations which have an impact on the tax base for future periods.

Net deferred tax balances are calculated based on each company's tax situation or on the overall results of companies belonging to the tax group.

Net deferred tax assets are recognized only if the company or tax group to which they relate has a reasonable likelihood of being able to utilize them in future years.

Deferred tax assets and liabilities are only discounted if the impact of such discounting is deemed to be material.

Marketable securities

Marketable securities are recorded on the balance sheet at the lower of cost and market value, excluding transaction expenses.

- Shares in mutual funds are estimated at fair value at the balance sheet date, and unrealized gains are recorded in the income statement.
- Listed securities are valued based on the average stock market price for the last month of the year.

Own shares

Own shares are recorded:

- either on the assets side of the consolidated balance sheet under "Marketable securities", when they are being held specifically to stabilize the share price or for allocation to employees;
- or as a deduction from shareholders' equity in all other cases. If they are deducted from equity, provisions for impairment, together with any disposal gains or losses on own shares recorded in the parent company accounts, are eliminated on consolidation.

Provisions for contingencies and charges

When the Group's obligations to third parties known at the balance sheet date are certain or likely to cause an outflow of resources, without at least equivalent consideration, a provision is recorded when the amount can be estimated with sufficient reliability.

This caption also includes:

- deferred tax liabilities,
- provisions for investments accounted for by the equity method, which correspond to the deficits of non-material companies that were deconsolidated in 2000 and are to be wound up.

Post-employment benefit obligations

Actuarial valuations of post-employment benefit obligations are made using the projected unit credit method, with employee rights recorded on an accruals basis.

For each active participant, the benefit likely to be paid is estimated based on the rules defined in the applicable collective-bargaining agreement and/or company-level agreement, using personal data projected to the standard age for payment of the benefit. The Group's total obligations toward each participant (total actuarial value of future benefits) are then calculated by multiplying the estimated benefit by an actuarial factor, which takes into account the following:

- Assumptions concerning the employee's probability of either leaving the Group or dying before the age of payment of the benefit,
- The discounted value of the benefit at the valuation date.

These total benefits are then allocated over each of the past and future years for which the participant accrued rights under the program. The company's actuarial liability corresponds to the portion of its obligation relating to accrued service at the balance sheet date.

The individual results of the valuation are then aggregated to obtain Group-level results.

The following economic assumptions were used to measure the Group's post-employment benefit obligation at December 31 2003 and 2004:

- Discount rate: 5%
- Inflation rate: 2%
- Salary growth rate: 3%

Deferred income

Based on the revenue recognition methods described above, deferred income includes the following:

- the portion of advertising revenues invoiced during the year that corresponds to display periods subsequent to the balance sheet date,
- the unused portion of revenues from prepaid telephone cards.

Stock option plans

Stock options granted to certain Group employees are recorded at the exercise date of the options.

Use of estimates

The preparation of the financial statements in accordance with accounting principles generally accepted in France involves the use of estimates and assumptions which may have an impact on the reported amounts in the financial statements and accompanying notes. Actual amounts may differ from these estimates.

NOTE 2: SCOPE OF CONSOLIDATION

List of consolidated companies and consolidation methods

The scope of consolidation and consolidation methods used are described in note 30 for the year ended December 31, 2004 and in note 31 for the year ended December 31, 2003.

2.1 Changes in scope of consolidation in 2004

A table presenting changes in the scope of consolidation in 2004 is provided in note 32.

The only changes during the year relate to additional interests acquired in Free and Société, which were already fully consolidated in prior years.

2.2 Changes in scope of consolidation in 2003

A table presenting changes in the scope of consolidation in 2003 is provided in note 33.

Newly consolidated companies

- *KERTEL*

In March 2003, Iliad acquired Kertel, a company specializing in the sale and top-up of prepaid telephone cards.

This business line opened up a new avenue of growth for the Iliad Group.

Key data concerning this transaction, as stated in the 2003 consolidated financial statements, are provided in the table below.

(in € thousands)	KERTEL
Cost of shares (1)	800
% acquired (2)	100%
Net worth (3)	(3,018)
Adjusted net worth (4)	(3,382)
Group interest in adjusted net worth (5) = (2) x (4)	(3,382)
Goodwill (6) = (1) – (5)	4,182

Note: the share purchase price has been finalized.

Changes in accounting estimates in 2004 (within the 12-month time period allowed for fair value adjustments) caused the Group to revise Kertel's adjusted net worth, and consequently to adjust the related goodwill amount.

The impact of these changes in accounting estimates is shown in note 13.

– *IH*

Although this company had been an Iliad subsidiary since its creation, it was not consolidated as it was dormant.

However, at the end of 2003 it acquired various fixed assets which it began managing. Consequently, it was included in the scope of consolidation. Its non-material results of operations prior to consolidation were recorded as an exceptional expense in 2003, in the amount of €14,000.

Internal restructuring

BookMyName and Online merged in 2003.

Prior to the merger, the two companies had been fully consolidated by the Iliad Group.

The transaction did not impact the 2003 consolidated financial statements or their comparability with prior years.

2.3 Non-consolidated subsidiaries

Non-material companies

Since 2001, three virtually dormant subsidiaries scheduled to be wound up have not been consolidated. Shares in these companies are carried in the consolidated balance sheet at an amount corresponding to the Group's equity in their net assets at December 31, 2000, their last date of consolidation, as follows:

– either on the assets side under “Investments accounted for by the equity method” (companies with a positive net worth):

31/12/2004	31/12/2003	31/12/2002
57 KEuros	52 KEuros	40 KEuros

– or on the liabilities side under “Provisions for investments accounted for by the equity method” (companies with a negative net worth):

31/12/2004	31/12/2003	31/12/2002
381 KEuros	467 KEuros	966 KEuros

The changes between 2002 and 2003 were mostly due to the Group's acquisition of all the assets of another company which was not consolidated by Iliad.

The prior period losses of these subsidiaries were mostly attributable to tax disputes which had been provided for in full. As these disputes are gradually resolved, the value of the shares carried under the equity method is adjusted as needed and steps are taken to liquidate these subsidiaries.

NOTE 3: YEAR-ON-YEAR COMPARISONS

Changes in accounting principles and methods

There have been no changes in the consolidation principles and methods applied.

However, the Group's first-time application of Recommendation 03-R issued by the French National Accounting Board (*Conseil National de la Compabilité*) on April 1, 2003 concerning the recognition and measurement of post-employment benefit obligations, applicable since January 1, 2004, impacted opening shareholders' equity in the amount of €56,000.

Effect of changes in scope of consolidation on comparability of 2003 financial statements

The consolidation of IH in 2003 did not have a material impact on the comparability of the financial statements. The acquisition of Kertel led to its consolidation as from April 1, 2003.

The table below provides a comparison of the consolidated financial statements for the year ended December 31, 2004 with proforma accounts for 2003 which include a full year of operations for Kertel.

Statement of income (in € thousands)	Comparable data				
	Published 2003 consolidated financial statements	Kertel's impact on 2003 consolidated net income 3 months	Proforma 2003 consolidated data	Published 2004 consolidated financial statements	Change on a constant Group structure basis
Revenues	293,051	6,213	299,264	491,446	192,182
Capitalized production costs	27,729	0	27,729	83,893	56,164
Other operating revenue	1,837	22	1,859	3,900	2,041
Purchases used in production.	243,779	5,421	249,200	428,021	178,821
Payroll costs	14,421	776	15,197	22,064	6,867
Other operating expenses	4,006	26	4,032	11,087	7,055
Taxes other than on income	1,623	81	1,704	3,822	2,118
Additions to provisions	5,145	42	5,187	5,573	386
EBITDA	53,643	(111)	53,532	108,672	55,140
Depreciation and amortization	18,676	615	19,291	55,582	36,291
Operating income	34,967	(726)	34,241	53,090	18,849
Net interest income/(expense)	(940)	15	(925)	2,735	3,660
Operating income after interest	34,027	(711)	33,316	55,825	22,509
Exceptional items	116	363	479	5,168	4,689
Corporate income tax	(45)	0	(45)	19,907	19,952
Net income of fully consolidated companies	34,188	(348)	33,840	41,086	7,246
Income from companies accounted for by the equity method	0	0	0	0	0
Goodwill amortization	313	105	418	254	(164)
Net income before minority interests	33,875	(453)	33,422	40,832	7,410
Minority interests	0		0	1	1
Net income	33,875	(453)	33,422	40,831	7,409

The following table summarizes the impact on the balance sheet at December 31, 2003 of the consolidation of Kertel.

(in € thousands)	2002	+ / —	Consolidation of Kertel 2003	Other changes in Group structure in 2003	Other	2003
FIXED ASSETS						
Goodwill	0	-313	4,182			3,869
Intangible assets	14,413	30,425	690			45,528
Property, plant and equipment . . .	24,782	48,100	435			73,317
Long-term investments	676	881	73			1,630
Current assets						
Inventories and other receivables .	61,755	18,325	5,122			85,202
Marketable securities	2,788	-217	0			2,571
Cash and cash equivalents	12,968	-6,787	2,605			8,786
Total assets	117,382	90,414	13,107	—	—	220,903
Shareholders' equity						
Capital stock	1,000	—	—			1,000
Additional paid-in capital.	1,126	—	—			1,126
Retained earnings/(deficit)	(315)	19,541	0			19,226
Net income for the year	23,827	10,048	0			33,875
Other	0	—	—			0
Minority interests	0	0	0	—	—	0
Provisions for contingencies and charges	5,470	893	382			6,745
Borrowings	15,023	5,777	77			20,877
Trade accounts and notes payable .	51,153	50,651	4,896			106,700
Other payables and accruals	20,098	3,504	7,752			31,354
Total liabilities and shareholders' equity	117,382	90,414	13,107	—	—	220,903

NOTE 4: REVENUES

Information concerning revenues is provided in the “Segment information” table in the first part of the consolidated financial statements.

As almost all of the Group’s operations are in France, presenting data by region would not be significant.

NOTE 5: HUMAN RESOURCES DATA

Number of employees

	At Dec. 31, 2004	At Dec. 31, 2003	At Dec. 31, 2002
– Management	95	114	73
– Other	657	391	188
Total	752	505	261

The increase in the number of employees is primarily due to recruitments for Iliad’s call center.

Headcount by segment is presented in the “Segment information” table.

Post-employment benefits

The Group's post-employment benefit obligations, calculated in accordance with the accounting principles described in note 1 that have been applicable since January 1, were included for the first time in the consolidated financial statements in 2004. The impact on opening shareholders' equity was €56,000.

A provision of €38,000 was also recorded in 2004 income statement to reflect the estimated value of the Group's post-employment benefit obligations.

NOTE 6: RESEARCH AND DEVELOPMENT

Research and development costs include the cost of developing new products, tailoring existing products to the Internet, research and development of databases for new applications and marketing developments for new products.

Research and development expenditure			
	2004	2003	2002
	1,867	1,636	2,452

The majority of the costs of creating Freebox modems and other specific equipment was incurred in 2002 and prior years.

NOTE 7: ADDITIONS TO DEPRECIATION, AMORTIZATION AND PROVISIONS

The following table shows the breakdown between the various components of depreciation, amortization and provisions:

(in € thousands)	2004	2003	2002
Additions			
– Depreciation and amortization expense	55,423	18,676	8,152
– Provisions for impairment in value of fixed assets	159	0	0
– Provisions for contingencies and charges	147	2,030	3
– Provisions for impairment in value of current assets	5,426	3,115	2,438
Total	61,155	23,821	10,593
REVERSALS OF OPERATING PROVISIONS			
– Provisions for impairment in value of fixed assets	0	0	98
– Provisions for contingencies and charges	2,715	839	94
– Provisions for impairment in value of current assets	867	928	101
Total	3,582	1,767	293

NOTE 8: NET INTEREST INCOME/(EXPENSE)

The main components of net interest income and expense are presented in the table below:

(in € thousands)	2004	2003	2002
– Interest expense, net of interest income	(1,394)	(1,582)	(1,729)
– Exchange gains	2,465	469	88
– Net gains on the sale of marketable securities.	942	131	109
– Provisions for new contingencies	0	(8)	(915)
– Reversal of surplus provisions	722	50	0
Total	2,735	(940)	(2,447)

Interest expense is mostly made up of interest on borrowings and finance leases.

Exchange gains in 2004 mainly relate to changes in the value of the US dollar.

Additions to provisions recorded in 2002 and reversals of surplus provisions in 2004 primarily concern other investment securities (see note 16).

NOTE 9: EXCEPTIONAL ITEMS

The main components of exceptional items are presented in the table below:

(in € thousands)	2004	2003	2002
– Gains on fixed asset disposals	1,817	68	539
– Restructuring costs	(144)	(243)	378
– Actual expenses previously provided for, net of provision reversals	0	(46)	9
– Provisions for new contingencies and exceptional write-downs	(1,907)	(1,824)	(7,091)
– Adjustment of One.Tel's bankruptcy debts	2,601	0	196
– Reversal of surplus provisions	1,481	713	3,302
– Other exceptional income and expense, net	1,320	1,448	(80)
Total	5,168	116	(2,747)

Comments on 2004 data:

Gains on fixed asset disposals mainly include:

- the impact of billing modems not returned by customers;
- the capital gain generated on the sale of an office building.

Additions to provisions relate to the write-downs of fixed assets in the amount of €1,598,000, and contingencies and charges in the amount of €309,000.

In 2004, a dispute was settled favorably for the Group in relation to an aged debt concerning the liabilities of One Tel incurred prior to its bankruptcy filing, and for which a debt repayment plan is in progress.

Reversals of surplus provisions mostly concern a claim that was settled during the year.

Comments on 2003 data

Exceptional items for 2003 corresponded to the cost of adjustments in provisions for contributions to the Universal Service Fund (see note 23) and the impact of settlements obtained in the Group's favor related to disputes with suppliers.

Comments on 2002 data

In 2002, certain fixed assets were retired resulting in exceptional charges to provisions for impairment in value. In addition, following the transfer of all Group employees to a single site, rents due under non-cancelable leases on existing premises were recorded as exceptional costs.

The reversal of unused provisions was mostly due to the settlement of a dispute in the Group's favor.

NOTE 10: CORPORATE INCOME TAX

Analysis of the corporate income tax charge

The corporate income tax charge breaks down as follows:

(in € thousands)	2004	2003	2002
– Current tax charge	11,742	3,894	1,861
– Deferred tax charge/benefit	8,165	(3,939)	4,119
Total tax charge	19,907	(45)	5,980

Tax rates

(in € thousands)	2004		2003		2002	
	in € thousands	%	in € thousands	%	in € thousands	%
Consolidated income before tax	60,739		33,830		29,808	
Theoretical tax rate for the parent company		35.43		35.43		35.43
Theoretical tax charge	21,520	35.43	11,985	35.43	10,560	35.43
Effective tax and tax rate	19,907	32.77	(45)	(0.13)	5,980	20.06

Comments on 2004 data

Under the French Finance Act for 2005, passed on December 30, 2004, the surtax introduced by the French government will be reduced by half effective as from fiscal year 2005.

As a consequence the tax rate used for calculating deferred taxes was reduced to 34.93% from the 35.43% rate applied previously.

The €275,000 expense arising as a result of this rate change was recorded under exceptional items.

Comments on 2003 data

In 2003, the utilization of tax losses carried forward from prior periods and the recognition of additional deferred tax assets for tax loss carryforwards previously wholly or partially unrecognized had a material impact on the

Group's effective tax rate. These mainly related to the tax losses of One.Tel due to the company's turnaround as well as to new tax legislation introduced making all tax losses evergreen.

Tax group

The Iliad Group has set up a tax group, which in 2004 included all consolidated companies except Assunet, Endeis Telecom and IH.

Tax proof

The table below reconciles:

- on the one hand, the Group's theoretical tax charge calculated by applying the income tax rate in effect for the year to consolidated income before tax,
- on the other hand, the actual tax charge recorded in the consolidated statement of income.

(in € thousands)	2004		2003		2002	
	in € thousands	%	in € thousands	%	in € thousands	%
Consolidated income before tax	60,739		33,830		29,808	
Theoretical tax rate for the parent company		35.43		35.43		35.43
Theoretical tax charge	21,520	35.43	11,985	35.43	10,560	35.43
– Impact of changes in Group structure on consolidated results	0	0	1	0	(1,533)	(5.21)
– Net impact of permanent differences	(234)	(0.39)	26	0.08	(2)	(0.01)
– Net impact of the recognition of deferred taxes for tax loss carryforwards	0	0	(10,368)	(30.65)	(3,296)	(11.06)
– Impact of loss-making companies outside the tax group	(838)	(1.38)	120	0.35	263	0.88
– Impact of unrecognized tax assets	(55)	(0.09)	(1,708)	(5.05)	(11)	(0.04)
– Impact of tax credits	(255)	(0.42)	(102)	(0.30)	(142)	(0.48)
– Impact of changes in tax rates	(155)	(0.19)	0	0	(4)	(0.01)
– Net impact of the 3.3% surtax	(18)	(0.03)	(26)	(0.08)	(48)	(0.16)
– Other	(98)	(0.16)	27	0.09	213	0.71
Effective tax and tax rate	19,907	32.77	(45)	(0.13)	5,980	20.06

No specific comments are required in relation to 2004 data.

The net impact of the recognition of deferred taxes for tax loss carryforwards in 2003 mainly related to the tax losses of One.Tel. As this company confirmed its turnaround and thanks to new tax legislation making all tax losses evergreen, the Group was able to recognize all deferred tax assets from tax loss carryforwards.

Deferred taxes

The only movements in deferred tax assets for the year ended December 31, 2004, correspond to the utilization of tax losses carried forward from prior periods, or the recognition of additional deferred tax assets for tax loss carryforwards previously wholly or partially unrecognized. These additional deferred tax assets have been recorded because their future recovery is now probable based on the projected future earnings of the companies concerned.

Movements in deferred taxes in 2004 can be analyzed as follows:

Type of differences	Value of DT assets/ (liabilities) at Jan. 1, 2004	+ Credits	– (Charges)	Changes in Group structure	Currency translation	Other ⁽¹⁾	Value of DT assets/ (liabilities) at Dec. 31, 2004
Recognition of deferred tax assets arising from tax loss carryforwards	11,777	—	9,167	—	—	904	3,514
Consolidation entries	(756)	2,429	759	—	—	83	997
Timing differences	1,525	561	1,229	—	—	(88)	769
Other	—	—	—	—	—	—	—
Total	12,546	2,990	(11,155)	—	—	899	5,280

DT assets at Jan. 1, 2004	13,053	DT assets at Dec. 31, 2004	5,280
DT liabilities at Jan. 1, 2004	507	DT liabilities at Dec. 31, 2004	0
NET DT ASSETS at Jan. 1, 2004	12,546	NET DT ASSETS at Dec. 31, 2004	5,280

(1) Other movements include:

the recognition of deferred taxes relating to:

- Kertel’s tax loss carryforwards (see note 13) €1,148,000
- post-employment benefit obligations (see note 3) €26,000 and the impact of changes in tax rates (see above) €(275,000)

Movements in deferred taxes in 2003 can be analyzed as follows:

Type of differences	Value of DT assets/ (liabilities) at Jan. 1, 2003	+ Credits	– (Charges)	Changes in Group structure	Currency translation	Other	Value of DT assets/ (liabilities) at Dec. 31, 2003
Recognition of deferred tax assets arising from tax loss carryforwards	8,973	11,570	(8,766)	—	—	—	11,777
Consolidation entries	(1,078)	1,974	(1,652)	—	—	—	(756)
Timing differences	712	933	(120)	—	—	—	1,525
Other	—	—	—	—	—	—	—
Total	8,607	14,477	(10,538)	—	—	—	12,546

DT assets at Jan. 1, 2003	9,073	DT assets at Dec. 31, 2003	13,053
DT liabilities at Jan. 1, 2003	466	DT liabilities at Dec. 31, 2003	507
NET DT ASSETS at Jan. 1, 2003	8,607	NET DT ASSETS at Dec. 31, 2003	12,546

Movements in deferred taxes in 2002 can be analyzed as follows:

Type of differences	Value of DT assets/ (liabilities) at Jan. 1, 2002	+ Credits	– (Charges)	Changes in Group structure	Currency translation	Other	Value of DT assets/ (liabilities) at Dec. 31, 2002
Recognition of deferred tax assets arising from ordinary and evergreen tax loss carryforwards	8,700	2,498	(7,026)	4,801	—	—	8,973
Consolidation entries	(1,139)	1,891	(1,827)	—	—	(3)	(1,078)
Timing differences	360	392	(47)	—	—	7	712
Other	—	—	—	—	—	—	—
Total	7,921	4,781	(8,900)	4,801	—	4	8,607

DT assets at Jan. 1, 2002	8,876	DT assets at Dec. 31, 2002	9,073
DT liabilities at Jan. 1, 2002	955	DT liabilities at Dec. 31, 2002	466
NET DT ASSETS at Jan. 1, 2002	7,921	NET DT ASSETS at Dec. 31, 2002	8,607

Unrecognized deferred tax assets

Unrecognized deferred tax assets concern:

- tax loss carryforwards of companies outside the Iliad tax group, which have been in a loss-making position for several years and are not expected to return to profit in the near future;
- tax loss carryforwards that are not expected to be utilized based on the projected future earnings of the companies concerned at the balance sheet date, or when the companies concerned have been historically loss-making and their turnaround is in progress.

Unrecognized deferred taxes break down into the following broad categories:

(in € thousands)	Dec. 31, 2004	Dec. 31, 2003
– timing differences	—	18
– tax loss carryforwards	180	2,128
Total	180	2,146

The decrease in 2004 primarily reflects the recognition of deferred taxes on Kertel's tax loss carryforwards (see note 13).

NOTE 11: NUMBER OF SHARES USED TO CALCULATE BASIC AND DILUTED EARNINGS PER SHARE

Basic earnings per share

Number of shares used	2004	2003	2002
– Number of shares at the end of the year	53,452,230	47,624,230	4,762,423
– Weighted average number of shares	52,653,874	6,993,586	25,576,556
– Number of shares used	53,452,230	47,624,230	47,624,230

Diluted earnings per share

Number of shares used	2004	2003	2002
– Weighted average number of shares outstanding (see above)	52,653,874	6,993,586	25,576,556
– Number of share equivalents:			
• Founders' share subscription warrants (BSPCEs)	699,320	2,654,010	265,401
• Stock options	446,794		
Maximum weighted average number of shares after dilution	53,799,988	9,647,596	25,841,957
– Number of shares used (see above).	53,452,230	47,624,230	47,624,230
– Number of share equivalents at Dec. 31, 2004:			
• Founders' share subscription warrants (BSPCEs)	699,320	2,654,010	2,654,010
• Stock options	444,132		
Maximum number of shares assuming full dilution	54,595,682	50,278,240	50,278,240

For 2002 and 2003, it was deemed more relevant to use the number of shares following the ten-for-one share split voted by the General Shareholders' Meeting of December 12, 2003. Similarly, for 2004, it was deemed more relevant to use the number of shares following Iliad's IPO.

NOTE 12: STATEMENTS OF CASH FLOWS

Changes in working capital

Changes in working capital can be analyzed as follows for 2004, 2003 and 2002:

2004	Balance at Jan. 1, 2004	Net debits	Net credits	Changes in Group structure	Other	Balance at Dec. 31, 2004
– Net inventories	4,134	5,952				10,086
– Trade accounts and notes receivable, net of customer prepayments	38,017	15,676				53,693
– Other net receivables	29,998	18,732				48,730
– Supplier payables	106,700		66,709			173,409
– Other liabilities	31,354		12,647			44,001
Total	(65,905)	40,360	79,356			(104,901)
Change in working capital in 2004.			38,996			

2003	Balance at Jan. 1, 2003	Net debits	Net credits	Consolidation of Kertel	Other	Balance at Dec. 31, 2003
– Net inventories	5,411		1,710	433		4,134
– Trade accounts and notes receivable, net of customer prepayments	30,282	4,980		2,736	19	38,017
– Other net receivables	16,990	9,607		1,953	1,448	29,998
– Supplier payables	51,153		50,650	4,896	1	106,700
– Other liabilities	20,098		3,394	7,752	110	31,354
Total	(18,568)	14,587	55,754	(7,526)	1,356	(65,905)
Change in working capital in 2003			41,167			

2002	Balance at Jan. 1, 2002	Net debits	Net credits	Consolidation of One.Tel & BOOKMYNAME	Other	Balance at Dec. 31, 2002
– Net inventories	14	5,397				5,411
– Trade accounts and notes receivable, net of customer prepayments	21,889	1,316		7,084	(7)	30,282
– Other net receivables	12,736		960	5,356	(142)	16,990
– Supplier payables	25,697		13,128	12,418	(90)	51,153
– Other liabilities	13,437		2,677	4,198	(214)	20,098
Total	(4,493)	6,713	16,765	(4,176)	155	(18,568)
Change in working capital in 2002			10,052			

Acquisitions of fixed assets

Acquisitions of fixed assets can be analyzed as follows:

	Note	2004	2003	2002 ⁽¹⁾
– Intangible assets	14	102,689	37,911	13,124
– Property, plant and equipment	15	112,166	62,171	12,469
– Long-term investments including seller’s credit with no cash impact	16	3,386 (3,249)	1,022	319
Total		214,992	101,104	25,912

(1) NB: The cash flow statement for the year ended December 31, 2002 has been prepared based on pro forma data at January 1, 2002 including One.Tel at that date.

Cash flows

	Note	Cash and cash equivalents at Dec. 31, 2004	Cash and cash equivalents at Dec. 31, 2003	Cash and cash equivalents at Dec. 31, 2002
Cash		28,373	8,786	12,968
Marketable securities	20	2,175	2,571	2,788
Short-term borrowings	24	(7,390)	(684)	(1,036)
Total		23,158	10,673	14,720

NOTE 13: GOODWILL

Goodwill breaks down as follows:

(in € thousands)	At December 31, 2004			At Dec. 31, 2003	At Dec. 31, 2002
	At cost	Amortization	Net	Net	Net
Free	4,312	2,609	1,703	0	0
Kertel	3,034	531	2,503	3,869	0
Other	95	95	0	0	0
Total	7,441	3,235	4,206	3,869	0

The main movements can be analyzed as follows:

(in € thousands)	2004	2003	2002
Net amount at Jan. 1	3,869	0	0
Increase following acquisitions:			
– BOOKMYNAME			95
– Kertel	(1,148)	4,182	—
– Free (acquisitions of additional interests)	1,740		
Amortization	(255)	(313)	(95)
NET AMOUNT AT DEC. 31.	4,206	3,869	0

Changes in 2004

– Kertel

Due to the turnaround of Kertel’s business, all deferred taxes relating to the company’s tax loss carryforwards can now be recognized. The amount of deferred taxes thus recognized amounted to €1,148,000.

This change of accounting estimate was made during the 12-month period allowed under French law for value adjustments. As the initial amount of goodwill recorded was positive, the change led to a €1,148,000 reduction in goodwill from €4,182,000 to €3,034,000. This goodwill is being amortized over 10 years.

Further to the adjustment to the amount of goodwill relating to Kertel, amortization for the year represented €218,000.

Based on a comparison of Kertel’s 2004 results and the residual goodwill value, the Group considers that the recoverable amount of the Kertel goodwill is not lower than its carrying amount.

– Free

In 2004, Free, a wholly-owned Iliad subsidiary, issued shares further to the exercise of founders’ share subscription warrants granted in prior years to certain employees. As Iliad wished to retain exclusive ownership of Free, the Company purchased these newly issued shares from the beneficiaries of the warrants exercised. Total goodwill of €1,740,000 was recorded in the consolidated balance sheets in relation to these share purchases. This goodwill is being amortized over ten years, with the charge for 2004 amounting to €37,000.

Based on Free’s results, no impairment charge had to be recorded in relation to this goodwill.

– Société

In 2004, the Group bought out minority interests in Société representing 4.8% of the company’s capital. Goodwill arising on this acquisition was not material (€100,000) and was expensed during the year.

Situation at December 31, 2003

Goodwill recorded on the acquisition of Kertel was calculated based on the fair value of the company’s assets and liabilities at March 31, 2003.

Some non-material adjustments were made in connection with Kertel’s financial position at March 31, 2003. Organization expense of €164,000 was amortized in full and a €200,000 restructuring provision was set up and fully used during 2003.

Following these adjustments, goodwill recorded on the Kertel acquisition amounted to €4,182,000. It is being amortized over a period of 10 years.

Situation at December 31, 2002

The acquisition of One.Tel resulted in the recognition of goodwill in a non-material amount of €1,000, which was expensed in 2002.

NOTE 14. OTHER INTANGIBLE ASSETS

Other intangible assets break down as follows:

(in € thousands)	At December 31, 2004			At Dec. 31,	At Dec. 31,
	At cost	Amortization	Net	2003 Net	2004 Net
– Indefeasible Rights of Use	72,704	3,068	69,636	23,247	12,189
– Access fees for services	70,905	13,798	57,107	20,094	0
– Other	2,456	1,816	640	2,187	2,224
Total	146,065	18,682	127,383	45,528	14,413

Changes in net intangible assets can be analyzed as follows:

(in € thousands)	2004	2003	2002
Net amount at Jan. 1	45,528	14,413	2,703
Acquisitions	102,689	37,911	13,124
Disposals	0	(863)	(99)
Effect of changes in Group structure	0	690	(197)
Amortization	(20,834)	(6,623)	(1,118)
Net amount at Dec. 31.	127,383	45,528	14,413

The Iliad Group has invested heavily to build up a telephone network covering most of France and the country's main towns and cities. For this purpose, it has entered into long-term IRU contracts for dark optical fibers and made the necessary investments to light the optical fibers.

In 2004, the Iliad Group entered into new agreements in order to increase the capillarity of its optical fiber network and to ensure long-term access to the infrastructure. The agreements related to:

- adding to the Group's network in order to obtain access to France Telecom's new dispatchers,
- obtaining an option to extend the term of the IRU agreements entered into with the Neuf Telecom Group up to December 31, 2030.

The amortization period of the IRU agreements have therefore been adjusted, leading to an approximate €1,000,000 decrease in the amortization charge for 2004.

NOTE 15: PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment can be analyzed as follows:

(in € thousands)	At December 31, 2004			At Dec. 31,	At Dec. 31,
	At cost	Depreciation	Net	2003 Net	2002 Net
– Land and buildings	962	268	694	2,829	2,930
– Network equipment (1)	162,739	42,122	120,617	60,160	17,934
– Other	25,128	5,198	19,930	10,328	3,918
Total	188,829	47,588	141,241	73,317	24,782

(1) of which finance leases 9,449 5,253 4,196 3,876 3,450

In 2004, the Group sold an office building and granted the purchaser a seller's credit (see note 16).

Changes in net property, plant and equipment can be analyzed as follows:

(in € thousands)	2004	2003	2002
Net amount at Jan. 1	73,317	24,782	21,974
Acquisitions	112,166	62,171	12,469
Disposals	(8,541)	(186)	(300)
Effect of changes in Group structure	0	435	1,574
Depreciation	(35,701)	(12,562)	(10,935)
Reclassification	—	(1,323)	—
Net amount at Dec. 31.	141,241	73,317	24,782

The Group's R&D team has designed a new version of the Freebox DSLAM that includes innovative technological features. Iliad has been installing these new Freebox DSLAMs at France Telecom sites since July 1, 2004 and in order to provide consistent service quality to all of its subscribers, the Group has decided to gradually replace older-version Freebox DSLAMs over a period of 18 months, up to December 31, 2005.

As a result, accelerated depreciation is being applied to the older-version DSLAMs for an 18 month period from July 1, 2004. The depreciation period for the new-version Freebox DSLAMs has been set at 3 years.

NOTE 16: LONG-TERM INVESTMENTS

Long-term investments break down as follows:

(in € thousands)	At December 31, 2004			At Dec. 31,	At Dec. 31,
	At cost	Provisions	Net	2003	2002
				Net	Net
– Investments accounted for by the equity method	57	—	57	52	40
– Investment-related receivables.	—	—	—	195	284
– Loans	3,248	—	3,248	—	—
– Other investment securities	1,769	1,078	691	15	52
– Guarantee deposits	1,378	—	1,378	1,368	300
Total	6,452	1,078	5,374	1,630	676

The portion of receivables due in more than one year amounted to €4,331,000 at December 31, 2004, €1,368,000 at December 31, 2003 and €300,000 at December 31, 2002.

The Group granted a nine-year interest-bearing seller's credit to the purchaser of an office building in 2004.

Changes in net long-term investments can be analyzed as follows:

(in € thousands)	2004	2003	2002
Net amount at Jan. 1	1,630	676	1,534
Acquisitions	3,386	1,022	75
Disposals	(316)	(141)	(229)
Effect of changes in Group structure	0	73	172
Additions to provisions	0	0	(876)
Reversals of provisions	674	0	0
Net amount at Dec. 31.	5,374	1,630	676

NOTE 17: INVENTORIES

Inventories break down as follows:

(in € thousands)	2004	2003	2002
Raw materials	6,798	3,350	3,407
Work in progress	2,548	38	962
Finished products	1,128	825	2,427
	<hr/>	<hr/>	<hr/>
Inventories at cost	10,474	4,213	6,796
Provisions.	(388)	(79)	(1,385)
	<hr/>	<hr/>	<hr/>
Net inventories	10,086	4,134	5,411

Raw materials inventories primarily comprise electronic components intended for the production of Freebox modems and other specific equipment.

Work in progress primarily includes Freebox modems.

Finished products comprise:

- For 2003 and 2004: Kertel prepaid telephone cards.
- For 2002: Freebox modems and other specific equipment.

NOTE 18: TRADE ACCOUNTS AND NOTES RECEIVABLE

Trade accounts and notes receivable are due in less than one year.

The breakdown between value at cost and provisions for impairment in value is as follows:

(in € thousands)	2004	2003	2002
Trade accounts and notes receivable, at cost	61,358	41,352	31,447
Provisions for impairment in value	7,665	3,335	1,165
	<hr/>	<hr/>	<hr/>
Trade accounts and notes receivable, net	53,693	38,017	30,282

NOTE 19: OTHER RECEIVABLES AND ACCRUALS

Other receivables and accruals break down as follows:

(in € thousands)	2004	2003	2002
Advances and prepayments.	3,357	1,819	2,558
Deferred tax assets	5,280	13,053	9,073
Tax receivables (VAT)	34,216	21,329	9,739
Tax receivables (corporate income tax).	3	23	346
Other receivables	3,470	2,650	2,344
Prepaid expenses.	8,904	5,427	4,133
	<hr/>	<hr/>	<hr/>
Total	55,230	44,301	28,193
	<hr/>	<hr/>	<hr/>
Provisions.	1,220	1,250	2,131
	<hr/>	<hr/>	<hr/>
Net total	54,010	43,051	26,062

This item only concerns receivables due in less than one year.

The detail of deferred taxes is shown in note 10.

NOTE 20: MARKETABLE SECURITIES

Marketable securities break down as follows:

(in € thousands)	At Dec. 31, 2004		At Dec. 31, 2003		At Dec. 31, 2002	
	Carrying value	Market value	Carrying value	Market value	Carrying value	Market value
Listed securities, at cost	681		1,068		1,066	
Provisions for impairment in value of listed securities	(681)		(934)		(980)	
Net value	0	0	134	134	86	86
Money-market mutual funds, at cost . .	2,112		2,437		2,702	
Provisions for impairment in value of money-market mutual funds	—		—		—	
Net value	2,112	2,112	2,437	2,437	2,702	2,702
Own shares held	63					
Provisions for impairment in value of own shares held	—					
Net value	63	72				
Total, net	2,175	2,184	2,571	2,571	2,788	2,788

Further to the authorization granted by the General Shareholders' Meeting of December 12, 2003, the Board of Directors set up a share buyback program in 2004. The information memorandum describing the program was approved by the *Autorité des Marchés Financiers* (French securities regulator) on March 16, 2004 under number 04-163.

For all of the Iliad shares purchased or sold during the year, the transactions were carried out under a liquidity agreement representing a maximum of €300,000. In relation to this agreement, at December 31, 2004, the Iliad Group held €260,000 in liquid assets and €63,000 in shares (2,569 shares with a fair value of €72,000).

NOTE 21: CAPITAL STOCK

At December 31, 2003, the Company's capital stock amounted to €1 million, made up of 47,624,230 shares following the ten-for-one share split approved by the General Shareholders' Meeting of December 12, 2003.

On January 30, 2004, the shares of the Iliad Group were listed on the *Premier Marché* of Euronext Paris. The shares offered in this flotation were 5,828,000 new shares issued by Iliad and 1,400,000 shares sold by Goldman Sachs mutual funds. The price of these shares, which were made available as part of a guaranteed private placement to institutional investors and an IPO in France, was set on January 29, 2004, at €16.30 per share, for a total placement of some €118 million. The total capital increase amounted to €94,997,000 and the IPO costs came to €3,360,000 (net of tax).

Between December 31, 2003 and December 31, 2004 the Company's capital stock was increased from €1,000,000 to €10,000,000.

At December 31, 2004, Iliad's ownership structure was as follows:

Shareholder	Number of shares	%
Executive Management	42,051,013	78.6
Goldman Sachs	936,670	1.8
Public	10,464,547	19.6
Total	53,452,230	100.0%

NOTE 22: STOCK OPTION AND SIMILAR PLANS

The following table summarizes the main features of the various stock option and similar plans approved in prior years and outstanding at the year-end.

At December 31, 2003

Date of Shareholders' Meeting	Date of plan launch	Number of options exercisable ⁽¹⁾	Number of beneficiaries	Exercise price	Number of options exercised in 2003	Options outstanding at Dec. 31, 2003
June 28, 2001	June 28, 2001	187,210	2	2.97		187,210
June 28, 2001	June 28, 2001	85,560	1	13.87		85,560
August 12, 2002	August 12, 2002	2,381,240	4	4.67		2,381,240
Total						2,654,010

(1) Taking into account transactions involving the Company's share capital since the issuance or granting of the dilutive instruments and following the share split approved by the General Shareholders' Meeting held on December 12, 2003.

At December 31, 2004

Date of Shareholders' Meeting	Date of plan launch	Number of options exercisable	Number of beneficiaries	Exercise price	Number of options exercised in 2004	Options outstanding at Dec. 31, 2004
June 28, 2001	June 28, 2001	104,010	1	2.97		104,010
August 12, 2002	August 12, 2002	595,310	1	4.67		595,310
December 12, 2003	January 20, 2004	444,132	21	16.30		444,132
Total						1,143,452

Three members of the Iliad Group's Executive Management team have unilaterally waived their entitlement to the options granted to them. Prior to being forfeited, these options had a maximum potential dilutive effect of 3.66%.

NOTE 23: PROVISIONS FOR CONTINGENCIES AND CHARGES

Provisions break down as follows:

(in € thousands)	Note	2004	2003	2002
Provisions for contingencies and charges		1,111	5,771	4,038
Provisions for deferred taxes	10	0	507	466
Provisions for investments accounted for by the equity method	2	381	467	966
Total		1,492	6,745	5,470

Movements in provisions for contingencies and charges were as follows in 2004:

(in € thousands)	At Dec. 31, 2003	Increase in 2004	Decreases in 2004 (utilizations)	Decreases in 2004 (surplus provisions)	Impact of recording post- employment benefits	At Dec. 31, 2004
Provisions for claims and litigation and general contingencies	1,657	416	22	1,263	—	788
Provisions for restructuring costs . . .	1,208	—	814	200	—	194
Provision for contributions to the Universal Service Fund	2,550	—	1,217	1,333	—	0
Other	356	40	332	19	84	129
Total	5,771	456	2,385	2,815	84	1,111

Movements in provisions for contingencies and charges were as follows in 2003:

(in € thousands)	At Dec. 31, 2002	Increase in 2003	Decreases in 2003 (utilizations)	Decreases in 2003 (surplus provisions)	Changes in Group structure in 2003	At Dec. 31, 2003
Provisions for claims and litigation and general contingencies	2,129	340	234	713	135	1,657
Provisions for restructuring costs . . .	1,108	100	247	—	247	1,208
Provision for contributions to the Universal Service Fund	780	2,550	780	—	—	2,550
Other	21	377	42	—	—	356
Total	4,038	3,367	1,303	713	382	5,771

Movements in provisions for contingencies and charges were as follows in 2002:

(in € thousands)	At Dec. 31, 2001	Increase in 2002	Decreases in 2002 (utilizations)	Decreases in 2002 (surplus provisions)	Changes in Group structure in 2002	At Dec. 31, 2002
Provisions for claims and litigation and general contingencies	1,019	2,026	737	2,882	2,703	2,129
Provisions for restructuring costs . . .	205	1,108	621	—	416	1,108
Provision for contributions to the Universal Service Fund	780	—	—	—	—	780
Provisions for preselection costs . . .	—	—	—	420	420	0
Other	135	1	31	—	(84)	21
Total	2,139	3,135	1,389	3,302	3,455	4,038

The impact (net of charges incurred) of movements in provisions on operating income, net interest expense and exceptional items was as follows:

(in € thousands)	2004	2003	2002
Operating income	1,187	(2,030)	(3,135)
Net interest expense	0	0	0
Exceptional items	1,172	(624)	3,302
Total	2,359	(2,654)	167

– **Provisions for claims and litigation and general contingencies**

These provisions are intended to cover the various risks incurred by Group companies.

– **Provisions for restructuring costs**

These provisions concern the impact of the decision taken by the Group in early 2003 to rationalize its facilities by bringing all employees together on one site. As some of the leases on the Group's other facilities have three-year non-cancelable periods and cannot be terminated immediately, a provision to cover the cost of these leases up to their termination was set up at the end of 2002 and adjusted in 2003 and 2004.

– **Provision for contributions to the Universal Service Fund**

In 2004 a reversal was recorded in relation to the provision for contributions to the Universal Service Fund further to the latest decisions and communications issued by the French Telecommunications Regulatory Authority (ART). The reversal reflects the reclassification of these contributions under accrued expenses, as well as a reduction in the rates of the contributions.

– **Provisions for deferred taxes**

This item primarily corresponds to the impact of consolidation adjustments and timing differences for the profitable companies in the Group (see note 10).

NOTE 24: BORROWINGS

Borrowings can be analyzed as follows:

(in € thousands)	2004	2003	2002
Bank borrowings	3,397	7,054	3,971
Borrowings related to finance leases	1,848	2,479	4,151
Other	0	0	0
	<hr/>	<hr/>	<hr/>
Long-term borrowings	5,245	9,533	8,122
	<hr/>	<hr/>	<hr/>
Bank borrowings	13,695	7,078	1,757
Borrowings related to finance leases	2,938	3,424	4,108
Other	7,514	842	1,036
	<hr/>	<hr/>	<hr/>
Short-term borrowings	24,109	11,344	6,901
	<hr/>	<hr/>	<hr/>
Total	29,354	20,877	15,023
	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>

Other borrowings primarily represent short-term bank facilities used to cover temporary cash shortfalls.

All Group borrowings are in euros.

The table below summarizes movements in borrowings in 2004, 2003 and 2002:

(in € thousands)	2004	2003	2002
Borrowings at Jan. 1	20,877	15,023	12,410
New borrowings	17,886	14,707	6,309
Repayments of borrowings	(16,115)	(8,577)	(4,465)
Impact of changes in Group structure	—	77	3,100
Other	6,706	(353)	(2,331)
	<hr/>	<hr/>	<hr/>
Total borrowings at Dec. 31	29,354	20,877	15,023
	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>

Breakdown of borrowings

Net borrowings at the year-end can be analyzed as follows:

(in € thousands)	2004	2003	2002
Fixed-rate borrowings	12,402	9,206	11,054
Variable-rate borrowings	16,952	11,671	3,969
Total borrowings	29,354	20,877	15,023

NOTE 25: OPERATING LIABILITIES

Operating liabilities break down as follows:

(in € thousands)	2004	2003	2002
Trade accounts and notes payable	173,409	106,700	51,153
Other liabilities	44,001	31,354	20,098
– Advances and prepayments	35	0	2,761
– Accrued taxes and payroll costs	27,540	20,803	12,284
– Other liabilities	6,605	2,105	4,335
– Deferred income	9,821	8,446	718
Total	217,410	138,054	71,251
of which due in less than one year	212,278	132,028	64,473
of which due in one to five years	4,476	3,987	3,478
of which due in more than five years	656	2,039	3,300

Amounts payable in more than one year include the liabilities of One.Tel prior to its filing for bankruptcy, for which a debt repayment plan is in progress.

NOTE 26: NON-CANCELABLE LEASE COMMITMENTS

The table below analyzes the Group's commitments under non-cancelable leases at December 31, 2004 by type of asset and by maturity.

Type of leased asset (in € thousands)	Within 1 year	In 1 to 2 years	In 2 to 3 years	In 3 to 4 years	In 4 to 5 years	Beyond 5 years	TOTAL
Real estate	4,387	4,302	4,076	4,072	2,307	1,755	20,899
Vehicles	182	132	23	—	—	—	337
Equipment	681	542	72	—	—	—	1,295
Other	414	313	199	160	129	859	2,074
Total	5,664	5,289	4,370	4,232	2,436	2,614	24,605

NOTE 27: EXPOSURE TO EXCHANGE-RATE AND INTEREST-RATE RISKS

Exchange-rate risk

(in € thousands)	2004			Total 2004
	US \$	£ sterling	Other currencies	
Monetary assets	217	0	0	217
Monetary liabilities	(19,699)	(54)	0	(19,753)
Gross exposure	(19,482)	(54)	0	(19,536)

Monetary liabilities correspond to routine operating liabilities.

Interest-rate risk

The Group is not subject to any liquidity risk as a result of prepayment clauses relating to loans contracted by Group companies nor as a result of non-compliance with financial covenants (ratios, targets, etc.).

NOTE 28: OTHER OFF BALANCE SHEET COMMITMENTS AND CONTINGENT RISKS

Guarantees given

The following table itemizes the guarantees given by Iliad to third parties:

Beneficiary of the guarantee	Amount of guarantee (in € thousands)	Purpose of guarantee
SITA (Suez Environnement)	1,700	Guarantee relating to premises at Rue de la Ville l'Evêque Commitment to minimum purchase volumes (minutes and terminations) between July 1, 2004 and December 31, 2006
Neuf Telecom	4,620	corresponding to revenues of €4,620,000.
Neuf Telecom	(*)	Investments relating to network extension

(*) In 2004, the Iliad Group entered into new agreements in order to increase the capillarity of its optical fiber network and to ensure long-term access to the infrastructure. The agreements related to:

- adding to the Group's network in order to obtain access to France Telecom's new dispatchers, thus significantly extending the accessible area for Freebox products via the unbundling of the local loop;
- obtaining an option to extend the term of the majority of the IRU agreements entered into with the Neuf Telecom Group up to December 31, 2030.

These agreements represent a total investment of €60 million, including fiber, equipment and the extension option, for 2004 and 2005. Over half of this amount has already been recorded in the financial statements for the year ended December 31, 2004.

Commitments received

At December 31, 2004, the Group had confirmed credit lines of up to €70 million, available until November 2008, €10 million of which had been drawn down.

Collateralized debts

None of the property belonging to the Iliad Group has been used as collateral for any debt.

Accrued discounted trade notes

The Iliad Group does not make use of this type of financing.

Dependence of the Iliad Group on patents and licenses

The Iliad Group holds a license to use the One.Tel brand in France, granted in 2001 by Centrica Telecommunications Ltd for a 10-year period in return for an annual fee based on revenues but capped at €250,000. However, Centrica waived the annual fee until August 31, 2004.

Claims and litigation

Group companies are involved in a certain number of disputes arising in the normal course of business. When the Group and its counsels estimate that charges are likely to result, provisions for contingencies and charges are recorded.

The Group considers that the provisions set up to cover such contingencies, litigation or disputes known of or in progress at December 31, 2004 are sufficient to ensure that there would be no material impact on the Group's consolidated financial position in the event of unfavorable outcomes.

NOTE 29: SUBSEQUENT EVENTS

No material events have occurred since the balance sheet date.

NOTE 30: LIST OF CONSOLIDATED COMPANIES AT DECEMBER 31, 2004

	Registration number	Head office	Percentage voting rights at Dec. 31, 2004	Percentage voting rights at Dec. 31, 2003	Percentage ownership at Dec. 31, 2004	Percentage ownership at Dec. 31, 2003	Consolidation method in 2004
ILIAD	342 376 332	Paris	100.00%	100.00%	100.00%	100.00%	Full
ASSUNET	421 259 797	Paris	89.88%	89.88%	89.88%	89.88%	Full
ENDEIS TELECOM	428 969 141	Paris	50.00%	50.00%	50.00%	50.00%	Proportional
FREE	421 938 861	Paris	100.00%	100.00%	100.00%	100.00%	Full
SOCIETE	428 116 065	Paris	99.99%	95.20%	99.99%	95.20%	Full
CENTRAPEL	434 130 860	Paris	99.98%	99.98%	99.98%	99.98%	Full
FREEBOX	433 910 616	Paris	95.00%	95.00%	95.00%	95.00%	Full
KEDRA	439 597 857	Paris	99.98%	99.98%	99.98%	99.98%	Full
ONE TEL	419 392 931	Paris	100.00%	100.00%	100.00%	100.00%	Full
ON LINE	433 115 904	Paris	100.00%	100.00%	100.00%	100.00%	Full
KERTEL	422 135 459	Paris	100.00%	100.00%	100.00%	100.00%	Full
IH	441 532 173	Paris	99.98%	99.98%	99.98%	99.98%	Full

NOTE 31: LIST OF CONSOLIDATED COMPANIES AT DECEMBER 31, 2003

	Registration number	Head office	Percentage voting rights at Dec. 31, 2003	Percentage voting rights at Dec. 31, 2002	Percentage ownership at Dec. 31, 2003	Percentage ownership at Dec. 31, 2002	Consolidation method in 2003
ILIAD	342 376 332	Paris	100.00%	100.00%	100.00%	100.00%	Full
ASSUNET	421 259 797	Paris	89.88%	89.84%	89.88%	89.84%	Full
ENDEIS TELECOM	428 969 141	Paris	50.00%	50.00%	50.00%	50.00%	Proportional
FREE	421 938 861	Paris	100.00%	100.00%	100.00%	100.00%	Full
SOCIETE	428 116 065	Paris	95.20%	95.20%	95.20%	95.20%	Full
CENTRAPEL	434 130 860	Paris	99.98%	99.98%	99.98%	99.98%	Full
FREEBOX	433 910 616	Paris	95.00%	99.98%	95.00%	99.98%	Full
KEDRA	439 597 857	Paris	99.98%	99.98%	99.98%	99.98%	Full
ONE TEL	419 392 931	Paris	100.00%	100.00%	100.00%	100.00%	Full
ON LINE	433 115 904	Paris	100.00%	100.00%	100.00%	99.98%	Full
KERTEL	422 135 459	Paris	100.00%	—	100.00%	—	Full
IH	441 532 173	Paris	99.98%	—	99.98%	—	Full

NOTE 32: CHANGES IN SCOPE OF CONSOLIDATION IN 2004

	Percentage voting rights at Dec. 31, 2003	Consolidation method at Dec. 31, 2003	Acquisition date	Percentage voting rights at Dec. 31, 2004	Consolidation method at Dec. 31, 2004
ILIAD	100%	Full	Parent company	100.00%	Full
ASSUNET.	89.88%	Full	12/29/1998	89.88%	Full
ENDEIS TELECOM (formerly TELECOM)	50.00%	Proportional	12/31/1999	50.00%	Proportional
FREE	100.00%	Full	02/01/1999	100.00%	Full
SOCIETE	95.20%	Full	01/01/1999	99.99%	Full
CENTRAPEL	99.98%	Full	12/01/2000	99.98%	Full
FREEBOX	95.00%	Full	12/01/2000	95.00%	Full
KEDRA	99.98%	Full	10/01/2001	99.98%	Full
ONE TEL	100.00%	Full	01/01/2002	100.00%	Full
ON LINE	100.00%	Full	07/01/2002	100.00%	Full
KERTEL	100.00%	Full	03/15/2003	100.00%	Full
IH	99.98%	Full	01/01/2003	99.98%	Full

NOTE 33: CHANGES IN SCOPE OF CONSOLIDATION IN 2003

	Percentage voting rights at Dec. 31, 2002	Consolidation method at Dec. 31, 2002	Acquisition date	Percentage voting rights at Dec. 31, 2003	Consolidation method at Dec. 31, 2003
ILIAD	100%	Full	Parent company	100.00%	Full
ASSUNET.	89.84%	Full	12/29/1998	89.88%	Full
ENDEIS TELECOM (formerly TELECOM)	50.00%	Proportional	12/31/1999	50.00%	Proportional
FREE	100.00%	Full	02/01/1999	100.00%	Full
SOCIETE	95.20%	Full	01/01/1999	95.20%	Full
CENTRAPEL	99.98%	Full	12/01/2000	99.98%	Full
FREEBOX	99.98%	Full	12/01/2000	95.00%	Full
ON LINE	99.98%	Full	05/10/2001	Merged	Not consolidated.
KEDRA	99.98%	Full	10/01/2001	99.98%	Full
ONE TEL	100.00%	Full	01/01/2002	100.00%	Full
ON LINE (formerly BOOKMYNAME)	100.00%	Full	07/01/2002	100.00%	Full
KERTEL	—	Not consolidated	03/15/2003	100.00%	Full
IH	—	Not consolidated	01/01/2003	99.98%	Full

5.4.2 Summary financial statements of the Company

The full financial statements of Iliad S.A. as well as the accompanying notes are available on request from the Company. The attached Statutory Auditors' reports refer to the full financial statements of the Company.

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STATUTORY AUDITORS' REPORT ON THE FINANCIAL STATEMENTS OF THE COMPANY

(Year ended December 31, 2004)

PricewaterhouseCoopers Audit

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92908 Paris La Défense 2
France

Boissière Expertise Audit

Represented by Tita A. Zeïtoun
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Iliad S.A.

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75008 PARIS

This is a free translation into English of the statutory auditors' report issued in the French language and is provided solely for the convenience of English speaking readers. The statutory auditors' report includes information specifically required by French law in all audit reports, whether qualified or not, and this is presented below the opinion on the financial statements. This information includes an explanatory paragraph discussing the auditors' assessments of certain significant accounting and auditing matters. These assessments were considered for the purpose of issuing an audit opinion on the financial statements taken as a whole and not to provide separate assurance on individual account captions or on information taken outside of the financial statements.

This report should be read in conjunction with, and construed in accordance with, French law and professional auditing standards applicable in France.

To the shareholders of Iliad S.A.:

In compliance with the assignment entrusted to us by the general shareholders' meetings, we hereby report to you, for the year ended December 31, 2004, on:

- the audit of the accompanying financial statements of Iliad S.A.,
- the justification of our assessments
- the specific verifications and information required by law.

The financial statements have been approved by the board of directors. Our responsibility is to express an opinion on these financial statements based on our audit.

I – Opinion on the financial statements

We conducted our audit in accordance with the professional standards applicable in France. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements give a true and fair view of the Company's financial position and its assets and liabilities as of December 31, 2004 and of the results of its operations for the year then ended, in accordance with French accounting principles and regulations.

II – Justification of our assessments

In accordance with the requirements of article L.225-235 of the Commercial Code relating to the justification of our assessments, we bring to your attention the following matter:

Note 1.4.2 to the financial statements explains the accounting rules and methods applicable to valuing investments and receivables related to investments. As part of our assessment of the accounting rules and principles applied by your company, we verified the appropriateness of these accounting methods and of the calculation of provisions for impairment in value.

The assessments were made in the context of our audit of the financial statements, taken as a whole, and therefore contributed to the formation of the unqualified opinion expressed in the first part of this report.

III – Specific verifications and information

We have also performed the specific verifications required by law in accordance with the professional standards applicable in France.

We have no comments as to the fair presentation and the conformity with the financial statements of the information given in the management report and in the documents addressed to the shareholders with respect to the financial position and the financial statements.

In accordance with legal requirements, we have confirmed that the information concerning acquisitions of investments and controlling interests has been provided to you in the management report.

Paris, April 24, 2005

The Statutory Auditors

PricewaterhouseCoopers Audit
Xavier Cauchois

Boissière Expertise Audit
Tita A. Zeïtoun

BALANCE SHEET

ASSETS (in € thousands)	At cost	Depr., amort.	Net at Dec. 31, 2004	Net at Dec. 31, 2003
INTANGIBLE ASSETS				
Concessions, patents and trademarks . . .	179	105	74	93
PROPERTY, PLANT AND EQUIPMENT				
Land.	119	0	119	119
Buildings	356	203	153	170
Fixtures and fittings	789	442	347	415
Technical equipment	7	5	2	3
Computer equipment	400	237	163	154
Furniture	126	28	98	110
LONG-TERM INVESTMENTS				
Investments in subsidiaries and affiliates	36,580	3,364	33,216	28,109
Loans and advances to subsidiaries and affiliates	139,263	101	139,162	34,260
Other long-term investments	1,014	0	1,014	971
TOTAL FIXED ASSETS	178,833	4,485	174,348	64,404
Trade accounts and notes receivable . . .	5,773	193	5,580	25,215
Due from suppliers	0	0	0	4,385
Employee-related receivables	0	0	0	6
Sales taxes receivable	495	0	495	2,749
Other receivables	1,435	1,220	215	241
Marketable securities	2,309	680	1,629	1,837
Cash and cash equivalents	23,863		23,863	6,374
Prepaid expenses.	990		990	957
TOTAL CURRENT ASSETS	34,865	2,093	32,772	41,764
ACCRUALS				
Conversion losses	1		1	6
TOTAL ASSETS	213,699	6,578	207,121	106,174

BALANCE SHEET

LIABILITIES AND SHAREHOLDERS' EQUITY (in € thousands)	At Dec. 31, 2004	At Dec. 31, 2003
Capital stock	10,000	1,000
Additional paid-in capital.	83,763	1,126
Legal reserve	100	100
Untaxed reserves.	2,654	2,654
Retained earnings	23,338	26,904
Net income for the year	12,959	5,788
Shareholders' Equity	132,814	37,572
Provisions for contingencies	1	6
Total Provisions	1	6
Bank borrowings.	10,000	0
Bank overdrafts	3,612	2,267
Other	393	293
Current accounts with subsidiaries.	47,019	28,935
Trade accounts and notes payable	3,331	8,515
Employee-related payables	119	97
Accrued payroll and other employee-related taxes	191	146
Accrued corporate income tax	6,246	2,537
Accrued sales taxes	1,386	4,438
Other accrued taxes	440	573
Other liabilities	1,569	20,795
Total Liabilities.	74,306	68,596
Total Liabilities and Shareholders' Equity	207,121	106,174

STATEMENT OF INCOME

(in € thousands)	2004	2003
Total Revenues	23,817	23,828
Reversals of depreciation, amortization and provisions, expense transfers . .	626	307
Other revenue	1	3
Total operating revenues	24,444	24,138
Rebilled purchases	7,916	5,792
Other purchases and external charges	10,941	9,423
Taxes other than on income	235	220
Wages and salaries	1,590	1,302
Payroll taxes	662	536
Depreciation and amortization of fixed assets	279	276
Additions to provisions for current assets	72	56
Additions to provisions for contingencies and charges	0	0
Other expenses	307	314
Total operating expenses	22,002	17,919
Operating income	2,442	6,219
Interest and other financial income	10,869	2,686
Reversals of provisions	6,459	116
Net gains on disposals of marketable securities	776	7
Total financial income	18,104	2,809
Interest and other financial expense	4,323	838
Additions to provisions	1,500	217
Net losses on disposals of marketable securities	206	
Total financial expense	6,029	1,055
Net financial income	12,075	1,753
Operating income before exceptional items and tax	14,517	7,972

STATEMENT OF INCOME (cont'd)

(in € thousands)	2004	2003
Exceptional income from revenue transactions.	248	109
Exceptional income from capital transactions	0	48
Reversals of provisions	28	1,415
TOTAL EXCEPTIONAL INCOME	276	1,572
Exceptional expense on revenue transactions	19	670
Exceptional expense on capital transactions		431
Exceptional depreciation, amortization and provisions		139
TOTAL EXCEPTIONAL EXPENSE.	19	1,240
NET EXCEPTIONAL INCOME	257	333
Corporate income tax	1,815	2,518
TOTAL INCOME	42,824	44,122
TOTAL EXPENSE.	29,865	31,789
NET INCOME	12,959	12,333

STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

(in € thousands)	Capital stock	Additional paid-in capital	Retained earnings	Net income for the year	Total share- holders' equity
Shareholders' equity at December 31, 2002 . .	1,000	1,126	7,886	26,058	36,070
Movements in 2003					
– Issuance of shares					
– Appropriation of 2002 net income			21,772	(21,772)	0
– Dividends paid.				(4,286)	(4,286)
– Net income for the year				5,788	5,788
Shareholders' equity at December 31, 2003 . .	1,000	1,126	29,658	5,788	37,572
Movements in 2004					
– Issuance of shares	9,000	82,637			91,637
– Appropriation of 2003 net income			5,788	(5,788)	0
– Dividends paid.			(9,354)		(9,354)
– Net income for the year				12,959	12,959
Shareholders' equity at December 31, 2004 . .	10,000	83,763	26,092	12,959	132,814

LIST OF SUBSIDIARIES AND AFFILIATES

	Capital stock (in € thousands)	Retained earnings/ (deficit) (in € thousands)	% ownership interest	Last published net income (in € thousands)	Value of shares, at cost (in € thousands)	Net value of shares (in € thousands)	Loans and advances granted (in € thousands)	Guarantees given by (in €/\$ thousands)	Last published revenues (in € thousands)	Dividends received (in € thousands)
ASSUNET SA	38	(2,882)	89.88	2,366	34	0	101	—	389	0
CENTRAPEL SA	38	(770)	99.98	172	38	38	4,970	—	14,940	0
FREE BOX SA	38	(782)	95.00	1,841	36	36	31,288	1,200/\$3,000	79,823	0
FREE SAS	3,028	44,085	100.00	18,547	29,432	29,432	94,883	68,852	389,295	0
IH SA	39	(22)	99.98	68	39	39	1,355	—	663	0
KEDRA SA	39	977	99.98	1,473	39	39	6,666	—	38,513	975
KERTEL	45	(3,050)	100.00	3,009	800	800	—	—	52,983	0
ON LINE SA	85	946	100.00	1,052	85	85	—	—	2,485	0
ONE TEL SAS	2,511	11,444	100.00	21,074	0	0	—	235	67,911	6,113
SASAM SARL	1	51	96.66	(1)	195	0	—	—	0	0
SNDM SARL	2	(392)	100.00	10	297	0	—	—	5	0
SOCIETE SA	76	(329)	99.99	356	3,538	2,000	—	—	1,516	0
ENDEIS TELECOM SA (formerly TELECOM)	38	(273)	50.00	804	19	19	—	—	4,626	0
TOUTCOM SARL	8	(80)	99.94	80	275	0	—	—	0	0

**STATUTORY AUDITORS' SPECIAL REPORT ON AGREEMENTS SUBJECT TO THE
PRIOR APPROVAL OF THE SUPERVISORY BOARD**

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This is a free translation into English of the statutory auditors' report issued in the French language and is provided solely for the convenience of English speaking readers.

This report should be read in conjunction with, and construed in accordance with, French law and professional auditing standards applicable in France.

To the shareholders of Iliad S.A.,

In our capacity as Statutory Auditors of Iliad S.A., we present below our report on agreements subject to the prior approval of the supervisory board or board of directors (*conventions réglementées*).

I – Agreements entered into during the fiscal year

Under the provisions of Section L. 225-88 of the French Commercial Code, we have been informed of those agreements approved in advance by the board of directors.

Our responsibility does not include identifying any undisclosed agreements. We are required to report to shareholders, based on the information provided, about the main terms and conditions of agreements that have been disclosed to us, without commenting on their relevance or substance. Under the provisions of Article 117 of the March 23, 1967 decree, it is the responsibility of the shareholders to determine whether the agreements are appropriate and should be approved.

We conducted our review in accordance with the professional standards applicable in France. Those standards require that we carry out the necessary procedures to verify the consistency of the information disclosed to us with the primary source documents.

1. Agreement entered into with ASSUNET

Members of the board of directors concerned:

Mr. Cyril Poidatz

Your board of directors of June 4, 2004 authorized an abandonment of credit of 2,464,979 euros authorized by your company to his Assunet subsidiary company.

2. Agreement entered into with Xavier Niel – member of the board of directors

Members of the board of directors concerned:

Mr. Cyril Poidatz

On July 1st and September 1st, 2004, your board of directors authorized a convention of current account advance between your company and Mr Xavier Niel. The balance of the current account advance of Mr Xavier Niel raised, at December 31, 2004, 3,472,341 euros. This current account advance is not the subject of any remuneration.

3. *Agreement entered into with TOUTCOM*

Members of the board of directors concerned:

Mr. Cyril Poidatz

Your board of directors of December 13, 2004 authorized an abandonment of credit of 82,624 euros authorized by your company to his Toutcom subsidiary company.

4. *Agreement entered into with SOCIETE.COM*

Members of the board of directors concerned:

Messrs. Cyril Poidatz
Olivier Rosenfeld

Your board of directors of December 13, 2004 authorized your Company to be subscribed to the new issue of capital of 3,400,000 euros to which proceeded the Société.com company. The subscription for this new issue of capital was released by compensation of current account.

Agreements entered into in prior years which remained in force during the year

In application of the decree of March 23, 1967, we were advised of the following agreements entered into in prior years which remained in force during the last fiscal year.

Agreement entered into with Kedra S.A.

On December 12, 2001, the supervisory board authorized the Company to enter into a cash pooling agreement with Kedra.

At December 31, 2004, the balance of Kedra's current account advance amounted to €6,666,154. Interest of €150,329 was invoiced by the Company to Kedra on this account during the year.

Agreement entered into with Endeis S.A. (ex Telecom SA)

On December 12, 2001, the supervisory board authorized the Company to enter into a cash pooling agreement with Télécom.

The balance of the current account advance of the Endeis company was balanced at December 31, 2004 and the interests invoices by your company to Endeis, 2004, amounted to €1,206.

Agreement entered into with Freebox S.A.

On December 12, 2001, the supervisory board authorized the Company to enter into a cash pooling agreement with Freebox.

At December 31, 2004, the balance of Freebox's current account advance amounted to €31,287,848 . Interest of €1,080,542 was invoiced by the Company to Freebox on this account during the year.

Agreement entered into with Centrapel S.A.

On December 12, 2001, the supervisory board authorized the Company to enter into a cash pooling agreement with Centrapel.

At December 31, 2004, the balance of Centrapel's current account advance amounted to €4,970,251 Interest of €158,209 was invoiced by the Company to Centrapel on this account during the year.

Agreement entered into with Société S.A.

On July 12, 2000, the board of directors authorized the Company to enter into a cash pooling agreement with Société.

At December 31, 2004, the Company had a current account advance of €123,992 from Société. Interest invoiced by the Company to Société on this account during the year amounted to €66,268.

Agreement entered into with Assunet S.A.

On July 12, 2000, the board of directors authorized the Company to enter into a cash pooling agreement with Assunet.

At December 31, 2004, the balance of Assunet's current account advance amounted to €101,809. Interest of €39,862 was invoiced by the Company to Assunet on this account during the year.

Agreement entered into with Kertel S.A.

On December 17, 2003, the supervisory board authorized the Company to enter into a cash pooling agreement with Kertel.

At December 31, 2004, the Company had a current account advance of €4,707,838 from Kertel. Interest invoiced by Kertel to the Company on this account during the year amounted to €169,004.

Agreement entered into with Toutcom

The cash pooling agreement entered into with Toutcom remained in force during the year.

The balance of the current account advance of Toutcom was balanced at December 31, 2004 and the interests invoices by your company to Toutcom, 2004, amounted to €926.

Agreement entered into with Free S.A.S.

The cash pooling agreement entered into with Free remained in force during the year.

At December 31, 2004, the balance of Free's current account advance amounted to €94,883,241. Interest of €2,130,743 was invoiced by the Company to Free on this account during the year.

The Company has undertaken to provide Free S.A.S. with a maximum of 120 million FF, representing 18.3 million Euros, in financing over five years in order to enable Free S.A.S. to incur the capital expenditure required under its license application filed with the *Autorité de Régulation des Télécommunications*.

The contract signed by the Company and Free concerning promotion for the French directory service www.annu.com, published by the Company, remained in force during the year. As consideration for the right granted by Free S.A.S. to the Company to manage an offer of a multiple-criteria telephone directory search on the www.free.fr and www.home.free.fr portals, Free invoiced €700,000 for 2004.

Agreement entered into with One.Tel S.A.S.

On December 12, 2002, the supervisory board authorized the Company to enter into a cash pooling agreement with One.Tel.

At December 31, 2004, the Company had a current account advance of €36,942,123 from One.Tel. Interest invoiced by One.Tel to the Company on this account during the year amounted to €1,292,898.

Agreement entered into with Online S.A.

On December 12, 2002, the supervisory board authorized the Company to enter into a cash pooling agreement with Online.

At December 31, 2004, the balance of Online's current account advance amounted to €1,285,456. Interest of €42,014 was invoiced by the Company to Online on this account during the year.

Agreement entered into with IH S.A.

On December 12, 2002, the supervisory board authorized the Company to enter into a cash pooling agreement with IH.

At December 31, 2004, the balance of IH's current account advance amounted to €1,354,756. Interest of €49,354 was invoiced by the Company to IH on this account during the year.

Agreement entered into with Free S.A.S., Assunet S.A., Télécom S.A., Freebox S.A., Online S.A.S., Kedra S.A., One.Tel S.A.S. and Société S.A.

The Company has entered into an automatic cash pooling agreement with Fortis Banque France and Free, Assunet, Télécom, Freebox, Online, Kedra and One.Tel. Pursuant to this agreement, the bank nets out the various credit and debit balances of the subsidiaries' accounts and enters this balance to the Company's account. As consideration for this service, the bank charges a monthly fee of €38 before tax to each company. The agreement is unlimited in duration and may be cancelled by any of the parties by giving 30 days' prior notice.

This agreement was not implemented during the year.

Paris, April 19, 2005

The Statutory Auditors

Boissière Expertise Audit
Tita A. Zeïtoun

PricewaterhouseCoopers Audit
Xavier Cauchois

5.5 FEES PAID BY THE GROUP TO THE STATUTORY AUDITORS AND MEMBERS OF THEIR NETWORKS

(in € thousands)	PricewaterhouseCoopers Audit				Boissière Expertise Audit			
	Amount		%		Amount		%	
	2004	2003	2004	2003	2004	2003	2004	2003
Audit								
– Statutory audit and contractual audits . . .	125.5	90	100%	100%	121	98	100%	100%
– Other engagements	—	—	—	—	—	—	—	—
Sub-total	<u>125.5</u>	<u>90</u>	<u>100%</u>	<u>100%</u>	<u>121</u>	<u>98</u>	<u>100%</u>	<u>100%</u>
Other services	—	—	—	—	—	—	—	—
– Legal and tax advisory services	—	—	—	—	—	—	—	—
– IT	—	—	—	—	—	—	—	—
– Internal audit	—	—	—	—	—	—	—	—
– Other (specific review for Iliad’s initial public offering)	176.7	—	—	—	135	—	—	—
Sub-total	<u>176.7</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>135</u>	<u>—</u>	<u>—</u>	<u>—</u>
Total	<u>302.2</u>	<u>90</u>	<u>100%</u>	<u>100%</u>	<u>256</u>	<u>98</u>	<u>100%</u>	<u>100%</u>

CHAPTER 6

CORPORATE GOVERNANCE

6.1 COMPOSITION AND OPERATION OF MANAGEMENT AND OVERSIGHT BODIES

6.1.1 Operation of management bodies

6.1.1.1 Board of directors

6.1.1.1.1 Composition – Appointment (Articles 13-15 of the bylaws)

Subject to the exceptions provided by law, the board of directors is composed of a minimum of three and a maximum of eighteen members appointed by the annual shareholders meeting.

Each director must own at least 100 shares of the Company. If a director does not own the required number of shares on the date of his appointment, or his shareholding decreases below that threshold during his term, he will be deemed to have resigned if the situation is not remedied within three months.

If there are vacancies on the board due to the death or resignation of one or more directors, the board may replace those directors whose positions were vacated during their term between two annual shareholders meetings.

However, if the number of directors in office falls below the legal minimum, the board of directors, or the statutory auditors if necessary, must call a regular shareholders meeting immediately to appoint the required number of directors.

The provisional appointments by the board of directors are subject to ratification by the following annual shareholders meeting.

If the provisional appointments are not ratified by the shareholders meeting, the deliberations and actions taken by or with the support of the provisionally appointed directors remain valid nonetheless.

A director appointed to replace another director will remain in office only until the expiration of his predecessor's term.

6.1.1.1.2 Directors' terms (Article 16 of the bylaws)

The directors' terms are six years.

A director's duties cease at the end of the annual shareholders meeting called to approve the financial statements for the year prior to and held during the year in which the director's term expires.

Outgoing directors may be reelected without restriction.

6.1.1.1.3 Organization, meetings and deliberations of the board of directors (Article 17 of the bylaws)

Chairman

The board of directors elects a chairman from among its members who are not corporate members, and determines the chairman's compensation.

The chairman is appointed for a term not to exceed his term as director, and may be reelected. The board of directors may remove the chairman at any time.

In the event of temporary absence or death of the chairman, the board of directors may delegate the chairman's functions to another director. In case of temporary absence, the delegation is granted for a limited time and is renewable. In case of the chairman's death, the delegation remains in effect until the new chairman is elected.

The chairman represents the board of directors. He organizes and oversees its work, reports to the shareholders meeting and executes its decisions. He ensures that the Company's management bodies operate effectively and that the directors are able to perform their duties.

Board meetings

The board of directors meets as often as the company's interests require, on notice from the chairman. In addition, if the board has not met for over two months, directors representing at least one-third of the board's members may call a meeting and indicate the agenda to be addressed.

If the company is managed by a general manager, he may also request that the chairman convene a board meeting to consider a specific agenda.

Requests made pursuant to the preceding two paragraphs are binding on the chairman.

A notice of meeting may be given by any written means (letter, telecopy, telex or electronic transmission). The notice of meeting must be issued at least two days in advance except in an emergency, in which case it must be issued no later than the day prior to the meeting, by any means. In any event, a meeting may be called verbally without notice if all the board members consent.

An attendance register is maintained at board meetings and signed by the directors.

Quorum and majority

The board of directors' deliberations are not valid unless at least one-half of its members are present. Decisions are adopted by the majority of members present or represented. In the event of a tie, the chairman casts the deciding vote.

Directors who participate in the meeting by means of videoconference or any other telecommunications technology, subject to the limitations and conditions prescribed by applicable laws, are considered present for the purpose of calculating the quorum and majority.

Representation

Any director may authorize another director, by any written means, to represent him at a board meeting. No director may have more than one proxy for a given meeting.

These provisions are applicable to the permanent representative of a corporate director.

Obligation of confidentiality

The directors, and any person invited to attend board meetings, are bound by an obligation of confidentiality in regard to confidential information identified as such by the chairman of the board.

Minutes of meetings

The board of directors' deliberations are recorded in minutes, which are numbered and signed and maintained in a special register at the Company's main office, as provided by applicable regulations.

The meeting minutes indicate the names of directors present, excused and absent. They reflect the presence or absence of persons invited to attend the meeting pursuant to legal requirements, and the presence of any other person attending all or part of the meeting. The minutes bear the signature of the chairman of the meeting and at least one director. If the chairman is absent from the meeting, the minutes are signed by at least two directors.

Copies or excerpts from the minutes are certified in accordance with applicable regulations.

6.1.1.1.4 Powers of the board of directors (Article 18 of the bylaws)

Introduction

The board of directors determines the company's strategic direction and oversees its implementation.

Subject to the powers expressly reserved to the shareholders meetings and within the limitations of the corporate purpose, the board of directors considers any issue concerning the Company's operations and decides matters affecting the Company through its deliberations.

In relationships with third parties, the Company is bound by the actions of the board of directors, even those beyond the scope of the corporate purpose, unless it is shown that the third party knew, or in light of the circumstances could not have been unaware, that such act exceeded the scope of the corporate purpose, on the understanding that the mere publication of the bylaws does not suffice to constitute such proof.

The board of directors shall conduct inspections and audits as it deems appropriate.

Each director must receive the information necessary to discharge his duties and may obtain any documents he considers useful from the Company's management.

The board of directors may delegate any powers to the chairman, with or without authority to delegate, and to any officer of its choosing, whether or not a shareholder, within the limitations provided by law.

6.1.1.1.5 Board of directors' internal rules of operation and code of conduct

The operations of the company's board of directors is governed by the internal rules adopted at the board meeting of December 12, 2003 and amended at the meeting of March 9, 2005.

The board of directors' internal rules include, inter alia, an annex containing a code of conduct which defines the directors' duties and obligations.

Composition of the board of directors

The board of directors must be composed of directors chosen for their expertise and experience in the company's activities as well as their integrity. It may include independent directors as defined below.

Independent directors

The board of directors is required to verify that candidates for the office of director fulfill the requirements for independence set forth in its internal rules. It reports the conclusions of its review to the shareholders at the shareholders meeting called to appoint the company's directors or ratify the board of directors' appointments through co-optation.

Each year, the board of directors must also verify the individual status of each director in regard to the criteria for independent directors and report its conclusions in its annual report.

In order to be considered independent, a director:

- cannot currently or during the five preceding years have been an employee of the Company, held a management position within the Company, or been an employee or director of the parent company or a company it consolidates;
- cannot be a corporate officer (within the meaning of COB recommendation 2002-01) of a company for which the Company directly or indirectly serves as a director, or in which an employee designated as such, a current officer of the company, or an individual who has held a position as officer within five years, holds a position as director;
- cannot be a customer, supplier, investment banker or a banker providing significant financing to the Company or Group, or for which the Company or Group represents a significant portion of his business;

- cannot have close families ties to a corporate officer;
- cannot have been an auditor of the Company during the five preceding years;
- cannot have been a director of the Company during the twelve preceding years;
- cannot represent a significant shareholder of the Company, considering:
 - (i) a shareholder who owns over 10% of the Company’s capital or voting rights is considered significant; and
 - (ii) below this threshold, the board of directors will systematically inquire into the director’s independence in view of the composition of the Company’s capital and the potential for conflicts of interest.

In regard to these criteria, the February 9, 2005 board of directors meeting ascertained that the board includes three independent directors: Mr. Alain Weill, AXA Investment Managers Private Equity Europe, and Mr. Jean-Louis Missika.

Meetings of the board of directors

The board of directors met on 21 occasions in 2004 upon notice from the chairman or another person authorized for that purpose. In addition, if the board of directors has not met for more than two months, directors representing at least one-third of the board’s members may call a meeting and indicate the agenda to be addressed.

The general manager may also request that the chairman call a board meeting to consider a specific agenda.

The board of directors’ rules establish the terms applicable to participation in meetings by videoconference.

Evaluation of the board of directors

The Company has not instituted formal measures to evaluate the board of directors’ performance. In the interest of good governance, the board of directors intends to include discussion of its operations as a regular agenda item.

Committees of the board of directors

The board of directors may be assisted in performing its duties by technical committees.

Subject to the composition rules described below, the board of directors is authorized to establish an audit committee and a compensation committee.

The audit committee is composed of a minimum of three (3) and maximum of five (5) members appointed by the board of directors and selected from among the directors. A majority of audit committee members must be selected from among the independent directors as defined above.

The compensation committee is composed of a minimum of three (3) and maximum of five (5) members appointed by the board of directors and selected from among the directors. A majority of audit committee members must be selected from among the independent directors as defined above. The board of directors may compensate members of technical committees for the work performed in the context of those committees.

The board of directors may establish technical committees whenever it deems necessary.

Responsibilities of the audit committee

The audit committee is responsible for:

- reviewing individual and consolidated financial statements prior to their submission to the board of directors;

- ensuring the relevance and consistency of accounting methods used in preparing financial statements;
- verifying internal procedures for collecting and auditing information used in their preparation;
- providing all appropriate reports and recommendations on the above, both on a periodic basis when accounts are closed and as warranted by events;
- overseeing the process of selecting the statutory auditors or renewing their appointments, providing an opinion on the fees requested and submitting the results of their selection to the board of directors; and
- reviewing in detail the fees paid by the Company and the group to the statutory auditors and verifying that the portion of fees paid to each auditing firm relative to its revenue is not likely to impair the auditors' independence.

Responsibilities of the compensation committee

The compensation is responsible for:

- making recommendations to the board of directors on the compensation and benefits to be provided to corporate officers;
- to this end, establishing and conducting an annual review of the rules governing the variable portion of corporate officers compensation, ensuring that it is consistent with their performance assessments and the company's medium-term strategy;
- defining general policies for allocating stock options, with or without discounts;
- reviewing stock option or subscription plans for the Company's or Group's corporate officers or employees; and
- providing recommendations on compensation and incentive systems for managers of the Company.

Code of conduct applicable to trading in the Company's securities

The board of directors' internal rules implement Articles 222-14 and 222-15 of the General Regulations of the AMF concerning the directors' obligation to report transactions involving the Company's securities to the Company on an individual basis, and the Company's responsibility to inform the public of those trades through the press within five trading days from receipt of such report.

The board of directors' code of conduct prohibits directors from trading in the securities of companies as to which they possess non-public information by reason of their positions.

If the Company's securities are traded on a regulated exchange, the directors are barred from buying or selling the Company's shares during the thirty calendar days preceding announcement of the Company's quarterly, half year or annual earnings.

6.1.1.2 Executive management (Article 19 of the bylaws)

6.1.1.2.1 Organization

French law provides that the Company's management may be placed under the responsibility of either the chairman of the board of directors or another individual appointed by the board who holds the title of general manager.

The board of directors decides which mode of management structure to adopt for the Company.

The board's decision concerning the choice of management structures is made by an absolute majority of the directors present or represented.

The option chosen by the board of directors must remain in effect for at least one year.

6.1.1.2.2 General Manager

Appointment – Removal

When the board of directors opts to separate the duties of chairman of the board and general manager, it appoints the general manager and determines his term of office, compensation and any limitations on authority.

The general manager may be removed at any time by the board of directors. If the general manager is not the chairman of the board, he may be entitled to damages if it is determined that he was removed without cause.

The general manager is subject to the provisions of L.225-94-1 of the French Commercial Code concerning concurrent appointments as general manager, director, member of the management board, sole general manager or member of the supervisory board of corporations (sociétés anonymes) domiciled in French territory.

If the chairman of the board of directors is also responsible for managing the Company, the provisions concerning the general manager apply to the chairman of the board.

Powers

The general manager is invested with full power to act on behalf of the Company in all circumstances. Those powers are subject to the limitations of the corporate purpose and the powers expressly reserved to the shareholders meetings and the board of directors.

The general manager represents the Company vis-à-vis third parties. The Company is bound by the actions of the general manager, even if they exceed the scope of the corporate purpose, unless it is shown that the third party knew, or in light of the circumstances could not have been unaware, that such act exceeded the scope of the corporate purpose, on the understanding that the mere publication of the bylaws does not suffice to constitute such proof.

6.1.1.2.3 Senior Vice Presidents

On the recommendation of the General Manager, the board of directors may appoint one or more individuals holding the title of Senior Vice President to assist the General Manager.

The maximum number of Senior Vice Presidents is five.

The board of directors, with the General Manager's consent, determines the scope and duration of authority granted to Senior Vice Presidents.

Senior Vice Presidents have the same powers as the General Manager vis-à-vis third parties.

The board of directors determines the Senior Vice Presidents' compensation.

Senior Vice Presidents may be removed by the board of directors at any time on the recommendation of the General Manager.

In the event of the General Manager's absence or departure, the Senior Vice Presidents retain their positions and powers until a new general manager is appointed, unless otherwise decided by the board of directors.

6.1.1.3 Meetings of the board of directors

The Company's board of directors met 21 times in 2004, compared to 14 times in 2003, with an average of 78% of its members in attendance.

6.1.2 Composition of the board of directors

Director	Position	Initial Appointment	Date Term Expires	Other offices held in French companies not part of the Group
Cyril Poidatz	Chairman of the board of directors ⁽¹⁾	12/12/2003	2009 ⁽²⁾	
Michaël Boukobza	Director and General Manager ⁽¹⁾	12/12/2003	2009 ⁽²⁾	
Xavier Niel	Director and Senior Vice President ⁽¹⁾	12/12/2003	2009 ⁽²⁾	
Olivier Rosenfeld	Director and Senior Vice President	12/12/2003	2009 ⁽²⁾	
Alain Weill	Director	12/12/2003	2009 ⁽²⁾	Chairman of the management board, NextRadio Chairman of the board, BFM Acting Chairman, RMC general manager of NRJ.
François Jerphagnon ⁽³⁾	Director	22/01/2004	2009 ⁽²⁾	Deputy chairman of the supervisory board, Financière Daum Member of the supervisory board, CFC Daum, Member of the supervisory board, Omnium's Member of the supervisory board, ASD Equity Permanent representative of AXA Investment Managers Private Equity Europe to the Riber supervisory board Permanent representative of AXA Investment Managers Private Equity Europe to the Moteurs Baudoin supervisory board
Shahriar Tadjbakhsh ⁽⁴⁾	Director	12/12/2003	2009 ⁽²⁾	
Jean-Louis Missika	Director	6/28/2004	2010 ⁽⁵⁾	Chairman and general manager of JLM Conseil

(1) Since July 1, 2004, following Mr. Niel indictment.

(2) Following the shareholders meeting called to approve the financial statements for the fiscal year ending December 31, 2008.

(3) Permanent representative of AXA Investment Managers Private Equity Europe.

(4) Permanent representative of Goldman Sachs Paris Inc. and Cie.

(5) Following the shareholders meeting called to approve the financial statements for the fiscal year ending December 31, 2009.

Messrs. Alain Weill and Jean-Louis Missika and AXA Investment Managers Private Equity Europe and Goldman Sachs Paris Inc. are the only independent directors on the Company's board of directors.

The criteria used by the Company to characterize the directors' independence are those set forth in the Rapport Bouton of September 23, 2002. According to those criteria, Messrs. Weill and Missika and AXA Investment Managers Private Equity Europe and Goldman Sachs Paris Inc. have no relationship of any kind with the Company, the Group or their management which may compromise their independent judgment.

6.1.3 General Manager and Senior Vice Presidents

Name	Position	Appointed	Term expires	Other positions held in French companies outside the Group
Michaël Boukobza	General Manager	07/01/2004	2009 ⁽¹⁾	
Xavier Niel	Senior Vice President	07/01/2004	2009 ⁽¹⁾	
Olivier Rosenfeld	Senior Vice President	12/12/2003	2009 ⁽¹⁾	
Rani Assaf	Senior Vice President	12/12/2003	2009 ⁽¹⁾	
Franck Brunel	Senior Vice President	12/12/2003	2009 ⁽¹⁾	
Antoine Levavasseur	Senior Vice President	12/12/2003	2009 ⁽¹⁾	

(1) Following the shareholders meeting called to approve the financial statements for the fiscal year ending December 31, 2008.

6.1.4 Biographies of the directors and officers

Cyril Poidatz, Chairman of the Board of Directors. Before joining the Group, Mr. Poidatz worked for 10 years at Cap Gemini. For several years he served as Director of Finance for Cap Gemini Italia, heading the restructuring of Cap Gemini's Italian divisions. Mr. Poidatz began his career as an auditor with Coopers & Lybrand. He joined the Group in 1998.

Michaël Boukobza, General Manager. Mr. Boukobza holds a Master's degree in Management from the Université de Paris IX Dauphine and graduated from the École Supérieure de Commerce in Paris. He began his career in the mergers & acquisitions departments of Rothschild in Paris and Morgan Stanley in London. He went on to work with i-Bazar in fundraising and mergers & acquisitions. Mr. Boukobza joined the Group in January 2000.

Xavier Niel, Senior Vice President. Mr. Niel is the Group's founder and majority shareholder. He has been active in the data communications, Internet and telecommunications industry since the late 1980s. In 1993, prior to devoting himself full-time to the Group's development, he founded France's first ISP, Worldnet, which was sold to Kaptech (LDCOM Group) in December 2000. Mr. Niel is the architect behind the Group's major strategic developments, from the launch of the ANNU service to its Internet access offer based on the economic model of France Telecom's repayment scheme to the launch of the Freebox project.

Olivier Rosenfeld, Chief Financial Officer. A graduate of the École de Commerce Solvay, Mr. Rosenfeld began his career with Merrill Lynch's investment banking division, where he worked on privatization projects before joining the Goldman Sachs team handling primary issues in New York and Hong Kong. Mr. Rosenfeld joined the Group in January 2001.

Rani Assaf, Technical Director. Mr. Assaf is in charge of the Group's IP and telecom network and the rollout of its DSL contract. Since 1999, he has been involved in implementing the group's IP network infrastructures as well as its interconnection with the incumbent operator on a Cisco SS7 platform. He is also one of the founders of the Freebox project. Mr. Assaf joined the Group in 1999.

Franck Brunel, Director of Regulatory Affairs. Mr. Brunel is in charge of the Group's regulatory affairs and is responsible for relations with the telecommunications authorities. Since 1999, he has been involved in preparing the Group's applications for L-33.1 and L-34.1 licenses and has participated in all the multilateral and bilateral relations between ART, the incumbent operator and Iliad. Mr. Brunel holds a doctoral degree (*Docteur ès Sciences*). He joined the Group in 1999.

Antoine Levavasseur, Technical Director. Mr. Levavasseur holds an engineering degree from the French engineering school EFREI. He joined Iliad in 1999 as manager of Free's system platform and servers. Since 1999, he has been involved in developing subscriber management information system and operating and developing the e-mail platforms, Web servers and applications used by subscribers.

Alain Weill, director. Mr. Weill holds a degree in economics and is a graduate of the Institut Supérieur des Affaires. Between 1985 and 1989, he was Network Director for NRJ S.A., then general manager of Quarare (Sodexo Group). In 1990, he joined the management team of Compagnie Luxembourgeoise de Télédiffusion (CLT), then became Chairman and General manager of the network, a subsidiary of CLT and the Spanish group

SER. In 1992, he was appointed to the senior management of the NRJ Group, followed by NRJ Régies in 1995, where he has served as Deputy Chairman of the Management Board since 1997. He has served as Chairman of Next Radio S.A. since November 8, 2000, and has been Chairman of the French association of radio advertising sales groups, SIRRP (*Syndicat indépendant des régies de radios privées*) since 1998.

Shahriar Tadjbakhsh, director representing the Goldman Sachs fund. Mr. Tadjbakhsh holds a Bachelor of Arts degree from Northwestern University and a doctorate in law from Harvard Law School. He began his career as an associate at Cleary, Gottlieb, Steen & Hamilton, where he worked from 1987 to 1996. Currently he is Senior Vice President of the investment banking division of Goldman Sachs International.

François Jerphagnon, director representing AXA Investment Managers Private Equity Europe. Mr. Jerphagnon began his career at the Caisse des Dépôts et Consignations before joining MACIF in 1995 where he managed asset allocation and equity portfolios. He then joined Axa Investments Managers Private Equity in 2001, where he is currently a Senior Investment Manager. Mr. Jerphagnon has a Masters in Finance from Université Paris Dauphine and is also a graduate of the French business school ENSAE (*École Nationale de la Statistique et de l'Administration Économique*). Mr. Jerphagnon is a member of the French Institute of Actuaries.

Jean-Louis Missika, director, holds a doctoral degree (*Doctorat d'État*) in Management (Paris IX Dauphine) and degrees from the Institut d'Études Politiques in Paris and the Institut d'Études Supérieures de Sciences Économiques (Paris I Panthéon-Sorbonne) and a degree in philosophy (Paris I Panthéon-Sorbonne). He began his career as adviser to the Chairman and general manager of Antenne 2, the French public broadcaster, from 1979 to 1984. He is currently Chairman and general manager of JLM Conseil, a consulting firm specializing in media strategies, new media and communications strategies that he founded in 1998.

6.2 MANAGEMENT MEMBERS' SHAREHOLDING AND COMPENSATION

6.2.1 Management members' shareholding in the Company and companies of the Group

Holdings as of April 1, 2005	Number of shares	Percentage of capital and voting rights
Iliad		
Xavier Niel	36,633,910	67.65%
Antoine Levavasseur	1,052,590	1.94%
Rani Assaf	952,590	1.76%
Cyril Poidatz.	719,199	1.33%
Olivier Rosenfeld	729,500	1.35%
Michaël Boukobza	744,199	1.37%
Franck Brunel	729,525	1.35%
<i>Total management members</i>	<i>41,561,513</i>	<i>76.75%</i>

Messrs. Poidatz, Boukobza, Rosenfeld, Assaf and Brunel each hold one share of Kertel; the total holdings of the Company's managers represent approximately 0.16% of the capital and voting rights of Kertel.

Messrs. Niel, Poidatz, Boukobza and Rosenfeld each hold one share of Kedra; the total holdings of the Company's managers represent approximately 0.01% of the capital and voting rights of Kedra.

Messrs. Niel, Poidatz, Boukobza and Levavasseur each hold one share of Freebox. Mr. Assaf also holds an additional 500 shares of Freebox. Accordingly, the total holdings of the Company's managers represent approximately 2.02% of the capital and voting rights of Freebox.

Mr. Poidatz holds one share of Online; the total holdings of the Company's managers represents approximately 0.01% of the capital and voting rights of Online.

Mr. Poidatz holds one share of One.Tel; the total holdings of the Company's managers in One.Tel is not significant.

Mr. Niel holds one share of Société; the total holdings of the Company's managers in Société is not significant.

Messrs. Niel, Poidatz and Boukobza each hold one share of Centrapel; the total holdings of the Company's managers represent approximately 0.01% of the capital and voting rights of Centrapel.

Messrs. Niel, Cyril, Boukobza, Rosenfeld, Assaf and Brunel each hold one share of IH; the total holdings of the Company's managers represent approximately 0.02% of the capital and voting rights of IH.

Messrs. Niel and Boukobza each hold one share of Assunet; the total holdings of the Company's managers represent approximately 0.02 of the capital and voting rights of Assunet.

6.2.2 Compensation and benefits in kind paid to management members during 2004

6.2.2.1 Attendance fees

The shareholders meeting adopted no resolution concerning allocation of attendance fees to members of the board of directors during the fiscal year ending December 31, 2004.

6.2.2.2 Individual compensation of corporate officers during fiscal year 2004

Name	Position	Compensation received (in euros)		Benefits in kind (in euros)	Total (in euros)
		Fixed portion	Variable portion		
Cyril Poidatz	Chairman of the Board of Directors	112,860	—	—	112,860
Michaël Boukobza	Director General Manager	80,460	—	—	80,460
Olivier Rosenfeld	Director Senior Vice President	107,354	—	—	107,354
Xavier Niel	Director Senior Vice President	79,122	—	46,878	126,000
Rani Assaf	Senior Vice President	77,825	—	—	77,825
Franck Brunel	Senior Vice President	55,927	—	—	55,927
Antoine Levavasseur	Senior Vice President	63,547	—	—	63,547
Alain Weill	Director	—	—	—	—
Goldman Sachs Paris Inc et Cie	Director	—	—	—	—
Axa Investment Managers Private Equity Europe	Director	—	—	—	—
Jean-Louis Missika	Director	—	—	—	—

There is no retirement plan established specifically for the Company's managers.

There is no severance payment plan for the Group's corporate officers or members of the management.

6.2.3 Change in total compensation paid to members of the management during the previous three fiscal years

Name	Position	Total compensation (in euros)		
		Fiscal year 2002	Fiscal year 2003	Fiscal year 2004
Cyril Poidatz	Chairman of the Board of Directors	136,763	147,167	112,860
Michaël Boukobza	Director General Manager	51,222	92,705	80,460
Olivier Rosenfeld	Director Senior Vice President	118,469	116,469	107,354
Xavier Niel	Director Senior Vice President	146,731	84,000	126,000
Rani Assaf	Senior Vice President	107,738	71,651	77,825
Franck Brunel	Senior Vice President	52,335	45,735	55,927
Antoine Levavasseur	Senior Vice President	64,029	64,065	63,547
Alain Weill	Director	—	—	—
Goldman Sachs Paris Inc et Cie	Director	—	—	—
Axa Investment Managers Private Equity Europe	Director	—	—	—
Jean-Louis Missika	Director	—	—	—

Goldman Sachs Paris Inc. & Cie, Axa Investment Managers Private Equity Europe and Jean-Louis Missika were appointed directors of the Company in December 2003, January 2004 and May 2004, respectively.

6.2.4 Options to subscribe shares and founders' shares subscription warrants (BSPCE) allocated to corporate officers and exercised as of April 1, 2005

By letters of June 2 and June 3, 2004 Messrs. Poidatz, Boukobza and Rosenfeld individually and irrevocably waived the exercise of all founders' shares subscription warrants allocated to them. As of June 3, 2004, no director of the Company held founders' warrants issued by the Company.

No director of the Company holds options to subscribe the Company's shares.

6.2.5 Information on transactions executed with members of the corporate management and oversight bodies or the Company's principal shareholders

6.2.5.1 Regulated agreements

Intra-group current account as of December 31, 2004

Iliad executed cash management agreements with certain subsidiaries having officers in common with Iliad.

The table below presents the intra-group current account balance for each of those subsidiaries as of December 31, 2004:

Lender company	Borrower company	Balance of current account as of December 31, 2004 (in thousands of euros)
Iliad SA.	Assunet SA	101
Iliad SA.	Free SAS	94,883
Iliad SA.	Online SAS	1,286
Iliad SA.	Centrapel SA	4,970
Iliad SA.	Freebox SA	31,288
Iliad SA.	IH SA	1,355
Société SA	Iliad SA	124
One.Tel SAS	Iliad SA	36,942
Kedra SA	Iliad SA	6,666
Kertel SA	Iliad SA	4,708

6.2.5.2 Regulated agreements for the fiscal year ending December 31, 2004

Refer to the report of the statutory auditors on regulated agreements at section 5.3.4 of this document.

6.2.5.3 Regulated agreements for the current fiscal year

At its February 9, 2005 meeting, the board of directors approved an advance to the Company's current account from Mr. Niel and the transfer of Freebox shares between Mr. Assaf, Senior Vice President, and the Company.

6.2.6 Loans and guarantees granted or provided to members of management or oversight bodies

As of this date, no loan or guarantee has been granted or issued to any of the members of the management or oversight bodies.

6.3 EMPLOYEE PROFIT-SHARING

Not applicable.

6.4 SUBSCRIPTION OPTIONS AND FOUNDERS' WARRANTS GRANTED TO OR EXERCISED OR HELD BY THE TOP TEN EMPLOYEES OF THE GROUP NOT MEMBERS OF THE MANAGEMENT

6.4.1 Subscription options and founders' warrants granted during the fiscal year ending December 31, 2004

On January 20, 2004, the Company's board of directors granted 485,769 subscription options to 22 employees of the Group, each option exercisable for one new share at €16.30 per share. As of April 1, 2005, 21 employees of the Group held 444,132 shares exercisable for 444,132 shares of the Company.

The following table provides the key features of the subscription options granted to the ten non-executive employees of the Group receiving the greatest number of options:

	Number of options	Exercise Period	Potential new shares to be issued	Exercise price (in euros)
Total for the 10 non-executive employees of the Group receiving the greatest number of options	291,461	1/20/2008 to 1/20/2014	291,461	16.30

(1) Unless the employee leaves the Company.

No founders shares were granted by the Company during the fiscal year ending December 31, 2004.

6.4.2 Subscription options and founders' warrants exercised during the fiscal year ending December 31, 2004

No subscription options were exercised during the fiscal year ending December 31, 2004.

240,000 2001 Founders' Warrants exercisable for 104,010 new shares at €2.97 per share were exercised on March 15, 2005.

59,531 2002 Founders' Warrants exercisable for 595,310 new shares at €4.67 per share were exercised on March 15, 2005.

As of April 1, 2005, there were no founders' warrants issued by the Company in circulation.

6.4.3 Subscription Options held as of April 1, 2005

	Exercise price (in euros)	Exercise Period	Potential new shares to be issued	Potential dilution
Total for the 10 employees not members of the management of the Group receiving the greatest number of options	16.30	1/20/2008 au 1/20/2014	291,461	0.54 %

(1) Unless the employee leaves the Company.

6.5 FOUNDERS' WARRANTS ISSUED BY FREE

Free, a 100%-owned subsidiary of the Company, issued founders' warrants (the "Free Founders' Warrants") to 14 of its employees. The Company made a offer to holders of Free Founders' Warrants to buy the Free shares issued upon exercise of their Free Warrants, or a maximum of 1,623,000 shares representing 2% of Free's capital and voting rights, every six months beginning June 30, 2004. All of the holders of Free Founders' Warrants have accepted the Company's offer to buy their Free shares.

Thirteen holders of Free Founders' Warrants exercised 715,200 Free Founders' Warrants in 2004, subscribing 715,200 new Free shares as a result.

The total acquisition price of those 715,200 Free shares issued in 2004 totaled €1.6 million. The Company's acquisition of the 715,200 Free shares occurred as follows:

- ownership of the 715,200 Free shares was transferred to the Company during the second half of 2004;
- the Company paid the purchase price of the 715,200 Free shares to the holders of Free Founders' Warrants in the days following the transfer of ownership.

As of April 1, 2005, 907,800 Free Founders' Warrants held by 12 employees of Free remained in circulation.

6.6 INTERNAL CONTROL PROCEDURES

6.6.1 Report of the Chairman of the Board of Directors on the conditions of preparing and organizing the Board's work and the internal control procedures implemented by the Company

6.6.1.1 Corporate governance

The Company is managed by a General Manager, who manages the Company with the Senior Vice Presidents. The board of directors, at its December 12, 2003 meeting, voted to separate the functions of chairman of the board and general manager. The board of directors imposed no specific limitations on the powers of the general manager.

- As of December 31, 2004, the Board of Directors was composed of eight members:
- Mr. Cyril Poidatz, Chairman of the board of directors;
- Mr. Michaël Boukobza, director and General Manager;
- Mr. Xavier Niel, director and Senior Vice President;
- Mr. Olivier Rosenfeld, director and Senior Vice President;
- Goldman Sachs Paris Inc. & Cie, represented by Mr. Shahriar Tadjbakhsh, director;
- Mr. Alain Weill, director;
- AXA Investment Managers Private Equity Europe, represented by Mr. François Jerphagnon, director; and
- Mr. Jean-Louis Missika, director.

According to the criteria provided in the board of directors rules adopted December 12, 2003 and amended February 9, 2005, Messrs. Weill and Missika, AXA Investment Managers Private Equity and Goldman Sachs Paris Inc. & Cie were the four directors the board considered independent as of December 31, 2004.

The majority of the directors were elected at the shareholders meeting of December 12, 2003 for a term expiring at the close of the shareholders meeting to be called to approve the financial statements for the fiscal year ending December 31, 2009.

Mr. Missika was elected at the shareholders meeting of June 28, 2004 for a term expiring at the close of the shareholders meeting to be called to approve the financial statements for the fiscal year ending December 31, 2009.

The board of directors provides an opinion on all decisions concerning the Company's strategic, economic, financial and technological objectives and oversees their implementation by management.

Meetings and activities of the board

During the fiscal year ended, the Company's board of directors met 21 times with an average attendance rate of 78%.

The increased number of meetings held in 2004 demonstrates the board's intention to expand its responsibilities and oversight role.

Reporting to directors

In order to ensure that the board members are prepared to consider the matters to be addressed at each meeting, they receive a dossier in advance containing the information required to prepare for the items on the agenda.

Meetings

The board of directors meetings are held at the Company's main office: 8 Rue de la Ville l'Evêque, 75008 Paris.

In addition to the directors, the statutory auditors are invited to attend on a regular basis and were present at board meetings where the interim and annual financial statements were reviewed or approved.

Minutes of meetings

Minutes of the board of directors meetings are prepared by the secretary of the board at the close of each meeting. A draft of the minutes is provided to all directors for their comments, and the draft is then submitted to the Chairman for approval by the directors at the following meeting.

Management operations

Since June 2004, the Company's management has been organized around a management committee headed by the chairman of the board of directors. The management committee is the Group's decision-making center. It monitors the weekly activity reports, shares responsibility for the Group's strategy and operations, debates and collectively makes key management decisions and, finally, defines the Group's annual outlook and objectives. It meets twice a week, with the chairman of the board, the General Manager, the Senior Vice Presidents and the head of the Group's Research and Development department in attendance. The Chairman and chief executive officer of Centrapel and the manager of the Group's collections department also attend on a regular basis. Matters addressed during these meetings also serve as the basis for presentations by management to the board of directors meetings.

6.6.1.2 Internal control procedures

6.6.1.2.1 Presentation and organization of the Group

All of the Group's divisions and employees have been located in the same building, at 8 Rue de la Ville l'Evêque, 75008 Paris, since June 2003. This arrangement serves to simplify the transmission of information and enhance the monitoring and consistency of internal control procedures.

In addition, each of the Group's operational departments (finance and accounting, legal, human resources, technical, marketing) is centralized and serves all the entities comprising the Group. This organization ensures genuine coherence among the Group's leadership and management and simplifies control.

The Group's activities continue to expand significantly during 2004 (consolidated revenue increased from €293 million to €491 million).

6.6.1.2.2 Objectives of internal control

Internal control is a process implemented by management in order to provide reasonable assurance as to the achievements of objectives in the following categories:

- efficiency and effectiveness of operations,
- reliability of financial information, and
- compliance with laws and regulations in force.

An internal control system, regardless of its merits, can only provide reasonable assurance, not an absolute guarantee, that the Company's objectives will be achieved.

The Iliad Group's internal control mechanisms are based on two sources of guidance:

- first and foremost, the internal regulations prescribed the rules to be observed by employees of every company in the Group; and
- a set of operational procedures is maintained and updated by the finance department.

The group does not have an internal audit department per se, but the finance department, assisted by accounting and management control teams and the other departments described above are central to the Group's internal control mechanisms.

The accounting and financial information of all the Group's companies is audited by each company a monthly basis.

6.6.1.2.3 Internal control procedures for managing key risks

The Group has implemented internal control mechanisms to manage risks associated with its strategy, growth and decision-making process.

Risks associated with the Group and its strategy

In order to preserve its ability to remain technically innovative, the Group established a research and development team in 2000. This team works directly under the Group's management.

Similarly, in order to prepare the Group for rapid growth and anticipate recruiting needs, particularly among the Centrapel teams, a reporting procedure was implemented at Centrapel in order to measure calls received, completed and answered and wait times. The reports are provided to management on a regular basis.

Technical information is also provided to management on a regular basis regarding the status of the Group's platform and network and requirements in terms of recruiting (number and discipline) and financing for expansion of its technical infrastructure.

Risks associated with the Internet and telecommunications sectors

The risks associated with the Group's business sectors are covered primarily by a dedicated internal team that monitors regulations governing the Internet and telecommunications sectors and their economic and legal impact on our business.

This team works under the supervision of the Senior Vice President for regulatory affairs.

Legal risks associated with Internet access

In order to limit legal risks faced by Internet access and Web hosting providers, Free's subscriber registration process prohibits anonymous users on its network. The registration procedure ensures that no user may connect online until he or she receives a confirmation message providing a login and password to connect to Free for the first time.

This procedure, which allows us to validate the name and address of each new subscriber, was implemented with the launch of Free, and ensures that no anonymous users are present on the network. Free is therefore able to respond to and cooperate in any requests for the identity of indiscreet users in the event of legal proceedings.

Security

The Group has implemented procedures to guarantee the security and physical integrity of its network.

Control procedures applicable to financial reporting

The Company is required to provide information to its shareholders and the financial markets in general regarding its financial position.

All financial communications are prepared by the finance department. Every financial communication, including press releases, management reports and financial statements, is reviewed by management for all entities of the group, and in particular by the chairman of the board of directors, the General Manager, the Senior Vice Presidents and the legal department, and are submitted to the directors on a regular basis for approval.

In order to limit risks associated with erroneous or contradictory communications, our internal control procedures provide that the Group's press attaché compiles all communications (strategic, marketing, financial, technical) issued by the Group. Management provides the information that may be released directly to the Group's press attaché, and the procedures in place require that the press attaché attend all interviews, regardless of the format or individual interviewed, in order to ensure consistency of the information provided

6.6.1.3 Financial information

Multiple procedures have been implemented to ensure control of the Group's financial management and proper reporting of the Group's accounting information.

6.6.1.3.1 Budgetary process

Each year, the finance department, assisted by the management control team, develops an economic forecast for the Group. This economic model is prepared on the basis of the Group's strategic choices and is validated by management.

The assumptions used in this budgetary process are updated on a quarterly basis.

The budget and quarterly reviews are then used to interpolate monthly estimates, which serve as the basis for the Group's monthly reporting procedures.

This budgetary process is replicated in each of the Group's subsidiaries.

6.6.1.3.2 Monthly reporting process

A monthly reporting is prepared by the Group's finance divisions. A management controller was recruited during fiscal year 2004 to monitor the Group's purchases and investments, particularly with respect to Freebox modem components. The management controller's reports are forwarded to the finance department and included in the monthly report, which tracks key figures on activity and results. The monthly report is an essential component of the control and financial information mechanism. It is management's preferred tool for monitoring, control and direction.

The board of directors reviews the latest available indicators when it meets.

6.6.1.3.3 Quarterly closing process

The Group's finance department closes the accounts of each of the Group's companies every quarter.

It should be noted that the Group's organization, which provides for a single finance department for all of the Group's companies and the use of common accounting procedures, ensures consistency of accounting principles, methods and processes.

In addition, the Group's finance department retains an outside auditor to review the corporate accounts of the Group's companies at least once per quarter.

A quarterly consolidation is prepared and submitted to the board of directors.

6.6.1.3.4 Preparation for conversion to IFRS standards

The Group's finance department has undertaken a diagnostic process in connection with the transition to IFRS standards. This process is still in progress at this time. Management agrees to comply with the AMF's recommendation and report comparative 2004 IFRS information on or before the date it reports 2005 half year results.

The following internal control procedures concerning significant operational functions are in effect in the Group:

Sales: revenue figures for each company of the Group are audited by the finance department, assisted by operational teams who test communications and subscriber flows, pricing and invoicing as well as receipts and collections.

Investment: monitoring of investments and asset management for the telecommunications network is implemented through expenditure commitment and validation procedures based on predefined authorization limits and budget allocations.

Purchasing: purchase commitments are monitored under a procedure providing for authorization limits and separation of tasks: monitoring of operational costs for Internet and fixed telephone.

Cash position: control of cash resources is provided through bank reconciliations, secured means of payment and delegation of signature authority for off-balance-sheet commitments.

Personnel: employee payroll is controlled by procedures incorporating the principle of separation of hierarchical controls.

6.6.2 Report of the Statutory Auditors pursuant to Article L.225-235 of the French Commercial Code on the report by the Chairman of the Board of Directors of Iliad SA on internal control procedures relating to the preparation and processing of financial and accounting information

To the shareholders of Iliad SA
8 Rue de La Ville L'Evêque
75008 Paris

In our capacity as statutory auditors of Iliad SA, and pursuant to the provisions of the last paragraph of Article L.225-235 of the French Commercial Code, we present our report on the report prepared by the Chairman of your company in accordance with Article L.225-37 of the French Commercial Code for the fiscal year ending December 31, 2004.

In his report, the Chairman is required to provide an account, *inter alia*, of the terms and conditions of preparing and organizing the Board of Directors' work and the internal control procedures in place in the company. It is our responsibility to report to you our observations on the information provided in the Chairman's report concerning the internal control procedures applicable to the preparation and processing of financial and accounting information.

We have performed our work in accordance with professional guidelines applicable in France, which require that we conduct procedures to assess the fairness of the information provided in the Chairman's report about the internal control procedures applicable to the preparation and processing of financial and accounting information. These procedures include:

- gaining an understanding of the internal control objectives, organization and procedures applicable to the preparation and processing of financial and accounting information as described in the Chairman's report;
- reviewing the work underlying the information presented in the report.

Based on our work, we have no matters to report with respect to the information on the company's internal control procedures applicable to the preparation and processing of financial and accounting information contained in the report of the Chairman of the Board of Directors prepared in accordance with Article L.225-37 of the French Commercial Code.

Paris, April 19, 2005

The Statutory Auditors

PricewaterhouseCoopers Audit

Xavier Cauchois

Boissière Expertise Audit

Tita A. Zeïtoun

CHAPTER 7

RECENT DEVELOPMENTS AND OUTLOOK

7.1 RECENT DEVELOPMENTS

(in € thousands)	Revenues as of March 31, 2005		
	First quarter 2004	First quarter 2005	Change
Consolidated revenues (1)	104,496	163,199	56%
Consolidated Internet revenues	66,291	122,499	85%
Consolidated telephony revenues	34,444	37,794	10%
Other services (consolidated)	3,760	2,826	(25%)

(1) Total inter-segment: 20,500,000 euros (Q1 2004)

On March 23, 2005, Iliad announced that, following the private placement with institutional investors of 2,135,980 shares held by Xavier Niel, an employee of the Group and the Goldman Sachs Funds, the float had increased from 19.6% to 23.3%, *i.e.* by almost 4%.

As of March 31, 2005, the number of Free's ADSL subscribers stood at 1,214,000 compared with 1,064,000 subscribers as of December 31, 2004. Accordingly, Free gained 150,000 additional subscribers during first quarter 2005. Free captured 18.4% of new ADSL subscribers during the first quarter 2005.

Over 1 million subscribers had a Freebox installed as of March 31, 2005. The value-added services available on the Freebox generated sales of 11.7 million euros during first quarter 2005, compared with 13.5 million euros for all of 2004. As of March 31, 2005 Free had 96,000 pay-channel subscribers and 850,000 users of Freebox telephone service.

7.2 OUTLOOK

The Management of the Group plans to concentrate its efforts on the unbundling of the local loop and the rollout of its network, the objective being to connect 250 new sites rapidly and to bring the total number of sites to 1,000 by the end of 2006.

Iliad intends to remain the first alternative residential broadband provider in France and to continue its strategy of pursuing profitable growth.

The Management of the Group is also actively working in the pursuit of the following objectives:

- to achieve 1.5 million broadband customers by the end of 2005,
- to reach a proportion of 70% of unbundled subscribers during 2005,
- to complete migration of 100% of DSLAMs to ADSL2+ before the end of 2005.

GLOSSARY OF TECHNICAL TERMS

The glossary below is provided as a supplement and as an aid to understanding this document. Some of the definitions below therefore give only a summary of the technical processes described, without providing details as to the functioning of such processes.

Add/Drop Multiplexer (ADM): equipment on a telecommunications network used for inserting or extracting packets of data.

ADM (Add/Drop Multiplexer): see Add/Drop Multiplexer.

ADSL (Asymmetrical Digital Subscriber Line): ADSL is an xDSL technology used for high-speed transmission of data, particularly when using a subscriber's conventional telephone line consisting of a pair of copper wires. By using two modems, one installed on the subscriber's premises and the other in a DSLAM located in the main distribution frame, ADSL technology is able to increase network bandwidth considerably and obtain transmission speeds up to 160 times faster than with a conventional analog modem. The principle behind ADSL is that part of the bandwidth is reserved for transporting voice traffic (low frequencies) while another part is used for transporting data (high frequencies) either in the direction of the network backbone (upload) or in the direction of the subscriber (download). The technology is asymmetrical in the sense that the upload bit rate (data sent by the user) is lower than the download rate (data received by the user). For the correct restoration of voice traffic (using the low frequency spectrum), splitters located at each end of the line eliminate those parts of the signal which are not needed.

The bandwidth of the line is divided as follows:

0 – 5 kHz.	analog telephone line,
30 kHz – 130 kHz.	narrowband channel in the direction of the network (upload)
30 kHz – 1.1 MHz	broadband channel in the direction of the subscriber (download)

FDM (Frequency Division Multiplexing) is used to separate the various data traffic flows. An echo cancellation system is used for spectrum recovery on the upload and download channels.

AFNIC (*Association française pour le nommage Internet en coopération* – www.afnic.fr): the AFNIC is a non-profit organization whose principal function is to establish and implement a naming system for the .fr (France) and .re (the island of Reunion) domains. It has drawn up naming charters which sets out its rules for registering domain names in these areas. Members of the AFNIC include service providers who have been accredited as registrars of domain names in the French domain name areas.

ART (*Autorité de régulation des télécommunications* – www.art-telecom.fr): the ART is an independent administrative authority. It was established on January 5, 1997 and, together with the Minister for Telecommunications, has overall responsibility for regulating the telecommunications sector in France.

ATM (Asynchronous Transfer Mode): this network technology is used for the simultaneous transmission of data, voice and video. It is based on the transmission of signals in short, fixed-length packets. The transmission of these packets is said to be asynchronous because they are transported over different routes and do not necessarily arrive at their destination in the same chronological order as they were sent.

Backbone: network consisting of a number of very high bandwidth links to which other, smaller networks are connected (including metropolitan networks).

Bandwidth: the transmission capacity of a transmission line. It determines the quantity of information (in bits per second) which can be transmitted simultaneously.

Bit: contraction of "binary digit". It is the smallest unit of information processed by a computer. In a binary system, one bit takes the value 0 or 1. Information recorded in digital form is coded in the form of bits. One character (letter or figure) is generally coded as 8 bits (1 byte).

Bit rate: amount of information passing through a communication channel over a given period of time. The bit rate is measured in bits per second or in multiples thereof (kbits per second = kilobits per second, Mbits per second = megabits per second, Gbits per second = gigabits per second, Tbits per second = terabits per second). The upload bit rate corresponds to the transmission of data from the subscriber to the network and the download bit rate corresponds to information transmitted from the network to the subscriber.

Broadband: The concept of broadband is a relative concept, depending on the status of transmission technology at any given time. At present broadband is generally accepted as corresponding to a bit rate of at least 512 kbits per second. See also “bit rate”.

Byte: a set of eight bits. Bytes and their multiples (kilobyte (kB), megabyte (MB), gigabyte (GB), Terabyte (TB), etc.) are used to measure the size of electronic files. When such measurements are given in multiples of bytes, it is generally accepted that a kilobyte is equal to 210, or 1,024, bytes (and not 1,000 bytes), and that a megabyte is equal to 220 bytes (and not 1,000,000 bytes).

Call termination: This operation consists of the routing of calls to subscribers on a particular network. In principle, call termination requires either that the call be made from the network on which the called party is a subscriber or from a network interconnected with such network.

CNIL (*Commission nationale de l’informatique et des libertés* – www.cnil.fr): The CNIL (National Commission for Information Technology and Freedom) is an independent administrative authority established by Law No. 78-17 of January 6, 1978, known as the “information technology and freedom” (*informatique et libertés*) law. Its principal role is the protection of privacy and of personal or public freedom, and it is responsible for ensuring compliance with the information technology and freedom law.

Co-location facilities or space: a room located in France Télécom sites containing equipment belonging to third party operators used for local loop unbundling. The room is built by France Télécom which then reinvoices the cost of construction to the operators located in the room. The third party operators then rent whatever space they need (one or more racks each occupying a floor area of 600 mm x 600 mm) for their unbundling activities.

Cookie: information recorded by a server in a text file located on the client’s computer and which can be read by this same server (and by this server alone) at a later time.

Copper pair: type of cable used for the transmission of electrical signals, consisting of one or more pairs of metal conductors. The two wires forming the pair are braided in order to minimize potential interference between two conductors. By extension, the copper pair also refers to the local loop link between a subscriber and the local concentrator. See also “local loop”.

CSA (*Conseil supérieur de l’audiovisuel* – www.csa.fr): The CSA is an independent administrative authority established by the Law of January 17, 1989. Its principal role is to guarantee the freedom of audiovisual communications in France in accordance with the provisions of the Law of September 30, 1986, as amended.

Dark optical fiber: raw optical fiber without the equipment which allows it to be used.

Dedicated facilities or space: a room in a France Télécom site containing equipment belonging to a third party operator used for unbundling. Third party operators rent the space (one or more racks each occupying a floor area of 600 mm x 600 mm) necessary for their unbundling activities. See also “co-location facilities”.

Dial-up (also called narrowband): historically this corresponds to the bit rate of a conventional telephone line using the voice frequency spectrum. By way of example, an Internet connection using a conventional telephone line is established at a maximum download rate of 56 kbits per second. See also “bit rate”.

Digital: coding in binary form (0 or 1) of information to be processed by a computer.

Digital local exchange (LX): switch on the France Télécom telephone network to which subscribers are connected by means of local concentrators. The France Télécom network is organized in a hierarchical fashion, with the digital local exchange being the lowest level in the hierarchy of exchanges installed on the network.

Digital main switching unit (MSU): France Télécom’s interconnect point, occupying the highest level in the hierarchy of switches in a trunk exchange area. See also “trunk exchange area”.

DNS (Domain Name System): the DNS is a database which registers Internet resources (computer, router, etc.) in the form of a domain name and allocates them a unique IP address. The Internet protocol converts the domain name to the corresponding IP address. Without the DNS, users would have to remember websites or email addresses in the form of the domain’s IP address. See also “domain name”.

Domain name: a domain name is the unique identifier of an IP address. The DNS (see “DNS – Domain Name System”) matches the domain name to the IP address. A domain name consists of a string of characters (from “a” to “z” or “0” to “9”, plus “-”) corresponding to the name of a trademark, association, company individual, etc., plus a suffix known as the TLD (see “TLD – Top Level Domain”), such as .fr, .de, .net, .com, etc.

Domain name registration: domain name registration consists of hosting domain names on a computer with an IP address on behalf of the domain name owners, who are in turn entered in the register relating to their TLD. See also “TLD”.

DSL (Digital Subscriber Line): See xDSL.

DSLAM (Digital Subscriber Line Access Multiplexer): equipment installed in the telephone exchange closest to the subscriber which is part of the equipment used to transform a conventional telephone line into an xDSL line. DSLAMs connect several xDSL lines and are connected to the modem on the subscriber’s premises via the local loop.

DWDM (Dense Wavelength Division Multiplexing): technology permitting the transmission of a large number of frequencies on the same fiber strand, thereby significantly increasing the bandwidth capacity of the optical fiber.

Eligibility: A telephone line is said to be “eligible” for ADSL when the technical characteristics of the line in terms of signal loss are such that xDSL type technologies can be used. The length and diameter of the copper pairs (local loop) are the main parameters determining eligibility. As the technology stands at present, the subscriber’s socket must not be more than 4 km from the DSLAM in order for a 512 kbits per second Internet connection to be possible.

Firewall: hardware or software device which controls access to all the computers on a network from a single point of entry. The main function of the firewall is to filter the information packets transmitted between the protected network and outside networks. In addition, a firewall can be used to perform advanced security functions such as virus detection, IP address masking on the protected network or the establishment of encryption tunnels associated with an authentication process.

Full unbundling: Full unbundling consists of allowing a third party operator to control the entire local loop (both low and high frequencies).

IEEE 802.11a and 802.11b standards: radio-telecommunications standards established by the IEEE (Institute of Electrical and Electronic Engineers) describing the characteristics of wireless networks using the 5 GHz and 2.4 GHz frequency bands, respectively. (See also “RLAN – Radio Local Area Network” and “WLAN – Wireless Local Area Network”).

Interconnection: the term interconnection refers to the reciprocal services provided by two operators of networks open to the public, permitting all of their users to communicate freely with one another, no matter the type of network or services they use. The term also refers to the provision to a public telephone service provider of access to a public network operator’s network. The objective of interconnection is to allow a given operator’s subscribers to make telephone calls to the subscribers of all other interconnected operators. Interconnection between the incumbent operator (France Télécom) and third party operators is governed by the provisions of the French Post and Telecommunications Code and is regulated by the ART.

Internet Service Provider (ISP): organization or company providing its customers with access to the Internet.

IP address: the IP address allows a router using TCP/IP protocol to identify the unique network interface of a machine connected to the Internet. In order to be accessible or to send information over the Internet, a machine must have a public IP address, *i.e.* an address that is known on the Internet. ICANN has overall responsibility for managing IP addressing on a worldwide basis, but delegates responsibility for certain areas to regional and local organizations. An IP address is a sequence of 32 binary digits (see also “bit”) grouped into four bytes in the form A.B.C.D where A, B, C and D are numbers between 0 and 255 (this structure corresponds to version 4 of the IP protocol, or IPv4). The problem of limited addressing resources highlighted by the growth of the Internet has led

to the development of a new version of the IP protocol (IPv6), based on 128 binary elements, which will gradually be brought into use.

IP (Internet Protocol): telecommunications protocol used on the networks supporting the Internet which divides the information to be transmitted into packets, addresses the various packets, transports them independently of one another and, finally, recreates the initial message once the packets reach their destination. This protocol uses a technique known as packet switching. On the Internet, it is associated with a data transmission control protocol (TCP), hence the term TCP/IP protocol.

IRU (Indefeasible Right of Use): special type of agreement, peculiar to the telecommunications sector, for the provision of optical fibers (or transmission capacity) over a long period.

L. 33-1 license: this license, referring to former Article L. 33-1 of the French Post and Telecommunications Code, is the authorization held by an operator of a telecommunications network open to the public.

L. 34-1 license: this license, referring to former Article L. 34-1 of the French Post and Telecommunications Code, is the authorization held by an undertaking providing a public telephone service.

Linux: Linux is a multi-task and multi-user UNIX (Uniplexed Information and Computer Service) operating system. It is a so-called “open” software system, *i.e.*, it is freely available in source code form and modifiable under the terms of a GNU General Public License.

Local concentrator: active telecommunications equipment connected to both the digital local exchange and the copper pairs constituting the local loop. This is the primary active equipment in the France Télécom network. The function of the local concentrator is to group several subscriber lines into one cable.

Local loop: physical circuit of the telephone network which connects the termination point of the network on the subscriber’s premises (*i.e.*, the subscriber’s telephone socket) and the local loop operator’s main distribution frame (*i.e.* generally France Télécom’s local telephone exchange) which contains a digital switch. The local loop is composed of a pair of braided copper wires.

Main distribution frame (MDF): device which establishes a temporary connection between a copper pair (local loop) and any active equipment on the operator’s network. It is a vital point of flexibility in the operation of a telecommunications network.

Modem (modulator-demodulator): device transforming analog signals into digital signals and vice versa. This equipment is necessary for connecting to the Internet (where the data exchanged are digital data).

MPEG-2: video signal compression standard, used mainly for DVDs.

Multicast: routing system minimizing the number of data flows from a server to various customers by multiplying the data flows only when they are as close as possible to the destination terminals (the subscribers’ copper pairs).

Multiplexing: technique permitting several communication flows to pass through the same channel/transmission bearer. Multiplexing can work in different ways: frequency multiplexing uses different frequencies for the various communications, while time division multiplexing allocates a period of time (known as a slot) to each communication.

Narrowband: see “dial-up”

Optical fiber: transmission medium which routes digital data in the form of modulated pulses of light. It consists of an extremely thin glass cylinder (the core strand) surrounded by a concentric layer of glass (the sheath). The potential bandwidth that can be passed through an optical fiber in conjunction with the corresponding active equipment is enormous.

Partial unbundling: partial unbundling involves providing an operator with access to the France Télécom local loop and allowing the operator to use the high (non-voice) frequencies of the frequency spectrum on the copper pair. France Télécom continues to use the local loop in order to provide conventional telephone service to the

public (using the low frequencies of the local loop). Customers continue to pay the telephone line rental to France Télécom.

Peering: type of interconnection agreement between two IP backbone networks (called peer networks) for the exchange of Internet traffic destined for their respective networks free of charge. These reciprocal exchanges take place at exchange nodes called peering points.

Ping: Ping is an acronym for Packet Internet Groper, and is a component of the Internet connection protocol which verifies the connections established on the Internet between one or more remote hosts and measures the time the data packets require to be transmitted to one computer connected to the Internet and back again. The lower the ping value (*i.e.*, the nearer to zero) the better the network connection.

POP (Point of Presence): operator's physical site from which the operator can use an interconnection link to connect to the interconnect point of another operator (whether another POP or, in the case of France Télécom, a digital main switching unit or a digital local exchange). The POP is located on the operator's network backbone. See also "digital main switching point".

Portability: possibility for a subscriber to keep his or her telephone number when changing operators and/or geographical location.

Preselection: carrier selection mechanism allowing a subscriber automatically to route all eligible calls (local, national, international, and calls to mobile phones) so that they are carried by the operator of the subscriber's choice, without having to dial a special prefix.

Primary digital block (E1): basic unit of measurement of the capacity of interconnection links to the France Télécom network (telephone traffic and dial-up Internet traffic). It corresponds to a grouping of several communications on the same physical support structure (31 simultaneous communications, *i.e.* a capacity of 2 Mbits per second).

PSTN (Public switched telephone network): conventional telephone network which uses switching (a non-permanent link established by line seizure and then dialing). Each call established on the PSTN ties up network resources.

Reference Interconnect Offer: document describing the technical and pricing terms of France Télécom's interconnect offer (or the interconnect offer of any other operator designated as having significant market power pursuant to Article L. 36-7 of the French Post and Telecommunications Code). It allows third party operators to know what interconnection services are available and sets out the prices and the technical terms of these services.

Reverse look-up directory: service allowing users to retrieve the name and address of the owner of a telephone line on the basis of a search of the telephone number.

RLAN (Radio Local Area Network): wireless network. RLANs generally conform to IEEE 802.11 standards.

SDH (Synchronous Digital Hierarchy): multiplexing technique providing for the secure transmission of different types of information. This technique is used for the transmission of data on conventional telephone networks.

SMS (Short Message Services): short alphanumerical text messages.

Source code: list of instructions in a computer program in a language capable of being understood by human beings.

Spamming: the bulk mailing of unsolicited electronic messages. These types of messages are generally sent to email lists obtained illegally (for example, through the use of a search engine on public websites or through the sale of email address files without the permission of the owners of such addresses).

Switch: equipment which routes calls to their destinations by establishing a temporary link between two circuits on a telecommunications network (or occasionally by routing information organized into packets). Switches are

organized in a hierarchical fashion, *i.e.*, the higher the position they occupy in the hierarchy, the more subscribers they serve.

TLD (Top Level Domain): the top level domain name classification, corresponding to a geographical area or a sector of activity, such as .com, .org or .fr.

Triple Play: a technical service capable of managing bandwidth-intensive voice, data and audiovisual content simultaneously and over long distances.

Trunk exchange (TX): telephone network switch linking together the digital local exchanges. The France Télécom network is organized in a hierarchical fashion, with the trunk exchange being the highest level in the hierarchy of national exchanges. Through the digital local exchanges, the trunk exchange serves all subscribers in a given geographical area called a trunk exchange area. See also “trunk exchange area”.

Trunk exchange area: the geographical area covered by a trunk exchange. France Télécom’s switched network in mainland France is divided into 18 trunk exchange areas, defined by France Télécom in its Reference Interconnect Offer and generally corresponding to the administrative regional divisions of France. See also “Trunk exchange (TX)”.

Unbundling: operation involving the separation of a range of telecommunications services into several distinct units. Unbundling of the local loop (or unbundled access to France Télécom’s local network) consists of separating the access services provided over the local loop, mainly by separating the high frequencies from the low frequencies of the access network which constitutes the local loop, allowing new operators to use the local network of the incumbent operator in order to provide services directly to their subscribers.

Universal service: the main element of the public telecommunications service as defined by law, with the purpose of providing high quality telephone service to the general public at an affordable price.

Urban area: in the architecture of the France Télécom network, Ile-de-France is divided into two trunk exchange areas. The urban area corresponds to the former département of Seine (Paris, Hauts-de-Seine, Seine-Saint-Denis, Val de Marne) and the peripheral area covers the Seine-et-Marne, Essonne, Yvelines and Val d’Oise départements.

VoDSL (Voice over DSL): transmission of voice traffic (in packets) using ADSL technology, *i.e.*, using the high frequencies of the local loop, as compared to conventional telephony which uses the low frequencies of the local loop.

WLAN (Wireless Local Area Network): a network using radio telecommunications (wireless network). RLANs (see “RLAN – Radio Local Area Network”) are a specific type of WLAN.

xDSL (x Digital Subscriber Line): the family of technologies used to transmit digital data over the copper pair (local loop) at high speeds (such as ADSL, VDSL, etc.) See also ASDL.

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