

**PROKOM SOFTWARE SA
CONSOLIDATED FINANCIAL STATEMENTS
31 DECEMBER 1998**

Report of Independent Accountants

To the Board of Directors and Shareholders of Prokom Software S.A.

We have audited the accompanying consolidated balance sheets of Prokom Software S.A. (the Company) as at 31 December 1998 and 1997 and the related consolidated statements of operations, of changes in shareholders' equity and of cash flows for the years ended 31 December 1998 and 1997 prepared in accordance with International Accounting Standards and on the basis set out in Note 2 to the financial statements, expressed in Polish Złoty (PLN). These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements audited by us present fairly, in all material respects, the financial position of the Company as at 31 December 1998 and 1997 and the results of its operations, changes in shareholders' equity and cash flows for the years ended 31 December 1998 and 1997 in accordance with International Accounting Standards.

Warsaw, Poland
10 May 1999

Prokom Software S.A.
Consolidated Balance Sheets
(Expressed in Polish Złoty (PLN) all amounts in thousands)

	<u>Note</u>	<u>31 December 1998</u>	<u>31 December 1997</u>
ASSETS			
CURRENT ASSETS			
Cash at bank and in hand		27,274	25,854
Cash in Escrow	4	-	192,487
Short term securities	5	87,832	862
Related parties	23	59,384	1,629
Accounts receivable			
Trade		91,257	73,924
Other		7,604	3,109
Inventories	6	25,116	12,286
Prepaid expenses	7	<u>18,264</u>	<u>3,204</u>
TOTAL CURRENT ASSETS		316,731	313,355
LONG TERM DEBTORS	8	15,213	1,171
RELATED PARTIES	23	21,761	5,591
DEFERRED TAX	9	9,071	5,204
INVESTMENTS, AT COST	10	6,521	1,775
INTEREST IN ASSOCIATED UNDERTAKING	11	7,476	6,413
GOODWILL ON CONSOLIDATION	12	763	1,144
INTANGIBLE FIXED ASSETS, NET	13	2,052	6,705
TANGIBLE FIXED ASSETS, NET	14	<u>30,322</u>	<u>21,823</u>
TOTAL ASSETS		<u><u>409,910</u></u>	<u><u>363,181</u></u>
LIABILITIES			
CURRENT LIABILITIES			
Short term borrowings	16	946	1,800
Accounts payable and accruals			
Trade		63,135	37,349
Related parties	23	-	5,479
Government	17	10,786	27,695
Employees		181	4,166
Unpaid dividends		-	11,412
Accruals and other		5,534	4,289
Deferred income	18	<u>10,690</u>	<u>13,025</u>
TOTAL CURRENT LIABILITIES		91,272	105,215
MINORITY INTEREST		2,399	2,240
SHAREHOLDERS' EQUITY	15		
Share capital		12,994	12,994
Share premium		188,847	189,330
Retained earnings		114,398	53,402
TOTAL SHAREHOLDERS' EQUITY		<u>316,239</u>	<u>255,726</u>
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY		<u><u>409,910</u></u>	<u><u>363,181</u></u>

The accompanying notes are an integral part of these financial statements

Prokom Software S.A.
Consolidated Statements of Operations
(Expressed in Polish Złoty (PLN) all amounts in thousands)

	Note	Year ended 31 December <u>1998</u>	Year ended 31 December <u>1997</u>
REVENUES		374,414	273,583
COST OF SALES	19	<u>(229,538)</u>	<u>(184,459)</u>
GROSS MARGIN		144,876	89,124
SELING COSTS	19	(13,744)	(11,129)
GENERAL AND ADMINISTRATIVE COSTS	19	(53,066)	(29,436)
OTHER OPERATING INCOME/(EXPENSES), NET	20	(5,180)	372
INTEREST IN ASSOCIATED UNDERTAKING	11	<u>(860)</u>	<u>(1,282)</u>
OPERATING PROFIT		72,026	47,649
FINANCIAL INCOME/ (EXPENSE), NET	21	31,217	4,210
PROFIT BEFORE INCOME TAXES		103,243	51,859
CORPORATE INCOME TAXES	22	(37,032)	(19,999)
MINORITY INTEREST		<u>(770)</u>	<u>(428)</u>
NET PROFIT		<u>65,441</u>	<u>31,432</u>
EARNINGS PER SHARE (in PLN)	26	<u>5.15</u>	<u>3.11</u>

The accompanying notes are an integral part of these financial statements

Prokom Software S.A.
Consolidated Statements of Changes in Shareholders' Equity
(Expressed in Polish Złoty (PLN) all amounts in thousands)

	Number of shares	Share capital	Share premium	Retained earnings	Total shareholders' equity
Balance as at 1 January 1997	301	480	-	33,439	33,919
Net profit for the year		-	-	31,432	31,432
Dividend paid		-	-	(22,000)	(22,000)
Increase in share capital	12,699,699	12,514	199,800	-	212,314
Share issue costs, net of deferred tax effect		-	(10,470)	-	(10,470)
Funding injection by Prokom Investments SA into IT business	-			10,531	10,531
Balance as at 31 December 1997	<u>12,700,000</u>	<u>12,994</u>	<u>189,330</u>	<u>53,402</u>	<u>255,726</u>
Net profit for the year	-	-	-	65,441	65,441
Dividend paid	-	-	-	(4,445)	(4,445)
Share issue costs, net of deferred tax effect	-	-	(483)	-	(483)
Balance as at 31 December 1998	<u><u>12,700,000</u></u>	<u><u>12,994</u></u>	<u><u>188,847</u></u>	<u><u>114,398</u></u>	<u><u>316,239</u></u>

The accompanying notes are an integral part of these financial statements

Prokom Software S.A.
Consolidated Statements of Cash Flows
(Expressed in Polish Złoty (PLN) all amounts in thousands)

	Year ended 31 December 1998	Year ended 31 December 1997
Net cash flow from operating activities:		
Net profit before taxation	103,243	51,859
Adjustments to reconcile net profit to net cash generated by operating activities		
Depreciation and amortization	15,960	12,068
Loss in associated undertaking	860	1,282
Changes in working capital	(49,977)	(12,975)
Gain on sale of land (see Note 20)	(1,960)	-
Interest expense	380	1,512
Investment income	(31,597)	(5,722)
Other	-	(241)
Net cash generated by operating activities	36,909	47,783
Interest paid	(380)	(1,512)
Tax paid	(49,129)	(8,188)
Cash flow from investing activities:		
Purchase of short term securities, net of sales	(71,013)	(862)
Purchase of tangible fixed assets	(32,904)	(12,438)
Purchase of intangible fixed assets	(1,853)	(999)
Purchase of investments	(4,696)	(1,610)
Capital contributions to associated undertaking	(2,181)	(6,293)
Purchase of subsidiaries (see Note 24)	-	(13,348)
Purchase of additional shares in subsidiaries (see Note 24)	-	(1,211)
Contribution to real estate projects with related party (see Note 23)	(14,530)	-
Loans given	(6,748)	-
Bank interest received	13,341	3,424
Other	-	(1,171)
Net cash used in investing activities	(120,584)	(34,508)
Cash flow from financing activities:		
Decrease in short term borrowings	(854)	(2,134)
Dividends paid	(15,857)	(22,703)
Proceeds from issue of shares	-	212,314
Share issue costs paid	(3,657)	(12,734)
Receipts/(payments) on related party loans	(1,260)	24,217
Payments for short term securities from related parties	(57,571)	-
Receipts from sales of short term securities issued by related parties	20,898	-
Interest received from loans to related party	418	-
Funding injection by Prokom Investments SA into IT business	-	10,531
Net cash (used in)/ provided by financing activities	(57,883)	209,491
Net change in cash and cash equivalents	(191,067)	213,066
Cash and cash equivalents at the beginning of the period	218,341	5,275
Cash and cash equivalents at the end of the period	27,274	218,341
Changes in working capital and long term operating items:		
Trade receivables	(17,197)	(34,178)
Other receivables	(379)	(1,186)
Inventories	(12,830)	116
Prepaid expenses	(15,060)	4,655
Long term debtors	(13,749)	1,401
Trade creditors	28,728	3,964
Due to related parties	(5,479)	5,479
Due to government	(9,145)	13,471
Due to employees	(3,985)	3,992
Accruals and other payables	1,252	732
Deferred income	(2,133)	(11,421)
Total	(49,977)	(12,975)

The accompanying notes are an integral part of these financial statements

Prokom Software S.A.
Notes to consolidated financial statements
(Expressed in Polish Złoty (PLN) all amounts in thousands)

1. The Company

Prokom Software S.A. ("the Company") (formerly Prokom International Sp. z o.o.) based in Warsaw, Al. Jerozolimskie 65/79, was formed in 1991 under the laws of Poland.

In December 1997 the Company offered 2,700,000 shares in a public offering. The transaction was successfully completed in 1998 and since 10 February 1998 the Company's shares have been listed on the Warsaw Stock Exchange. In December 1997 the Company also signed an agreement with the Bank of New York on the basis of which Global Depository Receipts were issued which are currently listed in London and traded under Rule 144(a) in the United States of America.

The Company's principal activity in 1998 and in 1997 was the provision of information technology services comprising design, installation and implementation of comprehensive information technology solutions to large companies in Poland. The Company also trades in computer software and hardware.

Details of subsidiaries and associates are provided in Notes 2 and 10

2. Basis of preparation of the financial statements

Basis of Accounting

The Company maintains its accounting records and prepares statutory financial statements in accordance with Polish accounting and tax regulations. These financial statements have been prepared based upon the Company's accounting records in order to present the financial position, results of operations and cash flows in accordance with International Accounting Standards (IAS).

Currency of Presentation

The accompanying financial statements are presented in Polish Złoty (PLN), which is the functional currency of the Company.

Principles of Consolidation

The consolidated financial statements include the following subsidiaries:

Entity's name	Business activity	Percentage Owned 31 December 1998	Percentage owned 31 December 1997
Koma SA (Koma)	Software trading, IT services	75.0%	75.0%
Combidata Poland Sp. z o.o. (Combidata)	Information technology training	83.3%	67.5%
Zeto Sp. z o.o.(Zeto)	Information technology services	100.0%	100.0%
Powszechna Agencja Informacyjna "Pagi" SA (Pagi)	Telecommunications services	42.4%	42.4%

Koma and Combidata were purchased by the Company in May 1997 from Prokom Investments S.A. and have been accounted for on a uniting of interests basis.

Pagi has been accounted for as an associate using the equity method.

All the above companies are incorporated and operate principally in Poland.

Subsidiaries and associates, which were not included in the consolidation due to the immateriality of balances involved, are listed in Note 10 of the financial statements.

Goodwill arising on acquisition is capitalized and amortized over 5 years on a straight-line basis.

Where the purchase price of a subsidiary is less than the attributable fair value of the underlying assets acquired, the excess is recorded as deferred income and amortized over 5 years on a straight line basis.

Prokom Software S.A.
Notes to consolidated financial statements
(Expressed in Polish Złoty (PLN) all amounts in thousands)

3. Summary of significant accounting policies

Use of Estimates

The preparation of financial statements in conformity with IAS necessarily requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and reported expenses during the reported period. Actual results could differ from these estimates.

Cash and Cash Equivalents

The Company considers all debt instruments purchased with a maturity of three months or less to be cash equivalents.

Short Term Securities

Government and commercial bonds are carried at market value. Investments in companies listed on the Warsaw Stock Exchange are valued at the lower of cost and market value. Market value is calculated by reference to quoted selling prices at the close of business on the balance sheet date. Changes in carrying amount are charged or credited to the income statement. On disposal of an investment, the difference between the net disposal proceeds and the carrying amount is charged or credited to the income statement.

Investments at cost

Shares in other entities and long term securities are valued on the basis of their purchase price less provision for any permanent diminution in value.

Transfers of entities under common control

Such transfers are accounted for using the purchase method of accounting when both of the following criteria are met:

- (i) the change in the ownership interest is substantive; and
- (ii) the value of the transaction is supported by independent evidence, for example market valuation or similar transactions.

If these criteria are not met, such transactions are accounted for as unitings of interests.

Inventories

Inventories are valued on a FIFO basis at the lower of purchase price and net realisable value. The Company has recorded a provision for obsolete and slow moving inventory.

Tangible and Intangible Fixed Assets

Fixed assets are stated at cost plus related inflation up to 31 December 1996, and additions are at cost thereafter, less accumulated depreciation.

Depreciation expense is recorded utilising the straight-line method over the estimated useful life of the assets. These rates are summarised as follows:

Type	Depreciation rate	Term
Patents, licenses and similar rights	25%	4 years
Vehicles	20 - 40%	2.5 to 5 years
Computers	30 - 60%	1.5 to 3 years
Leasehold improvements	10%	10 years
Buildings and structures	10%	10 years
Office equipment	10 - 50%	2 to 10 years

Land is not depreciated.

Foreign currency transactions

Foreign currency transactions are valued according to the average exchange rate announced by the central bank at the transaction date. Debtors and creditors are valued according to the central bank average exchange rate as at the balance sheet date for a given currency.

Gains and losses arising on foreign currency transactions are included in other operating income or expense, respectively.

Prokom Software S.A.
Notes to consolidated financial statements
(Expressed in Polish Złoty (PLN) all amounts in thousands)

Corporate income tax provision

Deferred income tax is provided, using the liability method, for all temporary differences arising between the tax basis of assets and liabilities and their carrying values for financial reporting purposes. Currently enacted tax rates are used to determine deferred income tax.

Revenues

Revenues (and the related profit) from information technology services are recognized based on completion of a given stage of the relevant contract. This is normally evidenced by formal customer acceptance procedures. Sales of hardware are recognized on delivery to the customer. Revenues from software licenses are recognized ratably over the duration of the systems contract to which they relate.

Royalties

Royalties payable in respect of revenues from third party software products are accounted for in the same period as the related revenues.

Borrowing costs

All borrowing costs are expensed in the period to which they relate.

Research and development

Research and development expenditure is expensed as incurred.

Comparatives

Comparative figures have been adjusted to conform with changes in presentation in the current year. In particular, the comparatives have been adjusted or extended to take into account the requirements of the IAS 12 (Revised) - Income Taxes. The Company implemented IAS 1 (Revised) - Presentation of Financial Statements in 1997.

4. Cash in Escrow

Cash received by the Company from the public offering in December 1997 was paid into an Escrow account pursuant to the terms of the offering, and released to the Company on 16 January 1998.

5. Short term securities

	<u>31 December 1998</u>	<u>31 December 1997</u>
Government bonds	56,285	-
Equity securities	31,547	862
	<u>87,832</u>	<u>862</u>

Government bonds include 26-week and 52-week bonds issued by the Polish government. Equity securities include investments in companies listed on the Warsaw Stock Exchange. The market value of equity securities was PLN 31,795 at 31 December 1998.

Equity securities include 1,596 shares of Prokom Software SA at cost of PLN 186 purchased by Koma. In 1998 Koma realized a gain of PLN 270 on sales of the Company's shares.

Government bonds of PLN 560 were pledged as security given for the proper conduct of contracts by the Company.

6. Inventories

	<u>31 December 1998</u>	<u>31 December 1997</u>
Raw materials and components used in systems installations	10,385	6,817
Computer equipment for resale	2,041	5,469
Costs incurred relating to work not yet invoiced	12,690	-
	<u>25,116</u>	<u>12,286</u>

7. Prepayments

Prepayments principally include software license fees prepaid.

Prokom Software S.A.
Notes to consolidated financial statements
(Expressed in Polish Złoty (PLN) all amounts in thousands)

8. Long term debtors

	<u>31 December 1998</u>	<u>31 December 1997</u>
Long term trade receivable	12,117	-
Loans to employees	1,058	1,171
Deposits and other	2,038	-
	<u>15,213</u>	<u>1,171</u>

The long-term trade receivable principally includes amounts for sale of third party software licenses to be paid in 2000. Loans to employees are repayable on 1 January 2000 and bear interest of 5% per annum.

9. Deferred tax

1 January 1997	-
Deferred tax on share issue costs	<u>5,204</u>
31 December 1997	<u>5,204</u>
Deferred tax on share issue costs	233
Deferred tax – income statement charge	<u>3,634</u>
31 December 1998	<u>9,071</u>

Deferred tax on share issue costs was calculated on costs incurred in the public offering of PLN 16,389, which were charged against share premium account.

Deferred taxation arises in respect of the following:

	<u>31 December 1998</u>	<u>31 December 1997</u>
Share issue costs	4,222	5,204
Prepaid expenses	(748)	(1,056)
Intangible fixed assets	-	(1,946)
Tangible fixed assets	(161)	(406)
Deferred income	3,454	4,410
Accounts payable and accruals	2,819	1,131
Unrealized gain on revaluation of short term securities, net	(373)	-
Interest accrued not yet received	(192)	(827)
Other, net	50	(1,306)
	<u>9,071</u>	<u>5,204</u>

10. Investments at cost

The following table provides a summary of investments at cost.

Company	Percentage Ownership	Number of votes	31 December 1998	31 December 1997
Grupa Inwestycyjna Pro SA	58%	58%	89	89
International Data System	15%	15%	51	51
Prokom Sp. z o.o.	67%	67%	174	124
Optix Polska Sp. z o.o.	60%	67%	313	313
Postdata S.A.	49%	49%	798	798
Multitrade Sp. z o.o.	99%	99%	240	240
Elterix SA	10%	10%	2,893	-
NKA Investments Sp.z o.o.	15%	15%	1,803	-
Other			160	160
Total			<u>6,521</u>	<u>1,775</u>

Other includes shares in Koma Nord Sp. z o.o., Technimex SA (net of a provision for permanent diminution in value of PLN 102) and Gliwicki Bank Handlowy SA owned by Koma.

Prokom Software S.A.
Notes to consolidated financial statements
(Expressed in Polish Złoty (PLN) all amounts in thousands)

The above companies, all of which are incorporated and operate principally in Poland, were not included in the consolidated financial statements due to the immateriality of amounts involved.

In 1998 the Company acquired interests in Elterix SA and NKA Investments Sp. z o.o., in both of which Ryszard Krauze holds a financial interest.

The Company's investments operate in the IT and telecommunication services sector, except for the following:

Gliwicki Bank Handlowy SA – banking
 NKA Investments Sp. z o.o. - real estate development
 Grupa Inwestycyjna Pro SA – business and financial consulting

	<u>31 December 1998</u>	<u>31 December 1997</u>
11. Interest in associated undertaking		
The Company's interest in Pagi is as follows:		
Share of net assets at acquisition	578	578
Goodwill	952	952
Amortization of goodwill	(380)	(190)
Share in post acquisition loss	(2,142)	(1,282)
Capital contributions	8,468	6,293
Other	-	62
Total	7,476	6,413

12. Goodwill on consolidation

Goodwill relates to the acquisition of Koma. Total net amortization charged in 1998 is PLN 381 (PLN 522 in 1997).

13. Intangible fixed assets

Intangible fixed assets includes patents, licenses and similar rights.

Changes in intangible assets:

	<u>1 January 1997</u>	<u>Additions</u>	<u>31 December 1997</u>	<u>Additions</u>	<u>31 December 1998</u>
Gross value	23,565	999	24,564	1,864	26,428
Amortization	(11,719)	(6,140)	(17,859)	(6,517)	(24,376)
Total	11,846	(5,141)	6,705	(4,653)	2,052

14. Tangible fixed assets

31.12.1998

31.12.1997

Tangible fixed assets by category:

Land	2,335	2,335
Buildings	4,185	4,354
Long term lease and leasehold improvements	8,149	5,514
Vehicles	3,630	3,473
Computers and office equipment	12,023	4,507
Payments on account	-	1,640
Total	30,322	21,823

Prokom Software S.A.
Notes to consolidated financial statements
(Expressed in Polish Złoty (PLN) all amounts in thousands)

Changes in tangible fixed assets

	<u>Land</u>	<u>Buildings</u>	<u>Long term lease and leasehold improvements</u>	<u>Vehicles</u>	<u>Computers and office equipment</u>	<u>Payment on account</u>	<u>Total</u>
1 January 1997	51	2,752	2,638	6,974	9,035	1,580	23,030
Additions	2,284	1,864	1,778	1,854	3,018	1,640	12,438
Transfer	-	-	1,580	-	-	(1,580)	-
31 December 1997	2,335	4,616	5,996	8,828	12,053	1,640	35,468
Additions	13,304	152	3,079	1,933	14,049	-	32,517
Disposals	(13,304)	-	-	-	-	-	(13,304)
Reclassification	-	-	-	-	-	(1,640)	(1,640)
31 December 1998	2,335	4,768	9,075	10,761	26,102	-	53,041

Accumulated depreciation

1 January 1997	-	2	172	3,759	4,294	-	8,227
Charge for the year	-	260	310	1,596	3,252	-	5,418
31 December 1997	-	262	482	5,355	7,546	-	13,645
Change for the year	-	321	444	1,776	6,533	-	9,074
31 December 1998	-	583	926	7,131	14,079	-	22,719

15. Share capital (amounts not in thousands)

	<u>Number of shares and paid for</u>	
	<u>31 December 1998</u>	<u>31 December 1997</u>
Series A preferred shares	185,416	185,416
Series B shares	9,814,584	9,814,584
Series C shares	2,700,000	2,700,000
	<u>12,700,000</u>	<u>12,700,000</u>

Each series A preferred share carries five voting rights. The other shares carry one vote per share.

Nominal value of shares

All shares at 31 December 1998 are issued at nominal value of PLN 1.

Shareholders rights

With the exception of the special voting rights attaching to the series A preferred shares, all classes of shares rank equally for dividend and on a return of capital from 1 January 1998.

Dividend

In 1998 the Company declared and paid a dividend out of retained earnings as at 31 December 1997 of PLN 4,445,000.

The Company's management has proposed to pay a dividend in 1999 of PLN 12,429,000 out of the Company's profits for 1998.

Prokom Software S.A.
Notes to consolidated financial statements
(Expressed in Polish Złoty (PLN) all amounts in thousands)

Significant shareholders as at 31 December 1998

The following shareholders had more than 5% of shares:

	<u>shares A</u>	<u>shares B</u>	<u>Total</u>	<u>% of ownership</u>	<u>% of voting rights</u>
Prokom Investments SA	73,920	3,741,201	3,815,121	30.04%	30.58%
Ryszard Krauze	46,200	2,176,662	2,222,862	17.50%	17.91%
Nihonswi AG	64,680	1,254,172	1,318,852	10.38%	11.73%

31 December 1998

31 December 1997

16. Short term borrowings

At 31 December 1998 the balance comprises loans taken by Combidata secured on certain tangible fixed assets.

31 December 1998

31 December 1997

17. Government payables

Corporate income tax	3,810	12,256
Value added tax	1,877	8,179
Other	5,099	7,260
	<u>10,786</u>	<u>27,695</u>

Other includes mainly payables for customs duties, personal income taxes withheld on payroll and social security.

31 December 1998

31 December 1997

18. Deferred income

Deferred income on software licenses	10,199	12,251
Other deferred income	491	774
	<u>10,690</u>	<u>13,025</u>

Other deferred income includes the difference between the purchase price of Combidata and Zeto in 1996 and purchase of additional shares in Combidata in 1997 and 1998 and the attributable fair value of the underlying assets acquired. The excess is amortized over 5 years on a straight-line basis. Total amount of amortization of the balance in 1998 was PLN 202 (PLN 202 in 1997).

Year ended
31 December
1998

Year ended
31 December
1997

19. Operating expenses

Cost of hardware supplied and materials used in installations	125,201	122,249
External services	66,339	34,168
Payroll	51,054	35,449
Social security	22,688	15,522
Depreciation and amortization of goodwill	15,960	12,068
Other	15,106	5,568
Total	<u>296,348</u>	<u>225,024</u>
Cost of sales	229,538	184,459
Selling costs	13,744	11,129
General and administrative costs	53,066	29,436
Total	<u>296,348</u>	<u>225,024</u>

The average number of employees in 1998 in the Company was 1,433 (814 in 1997).

Operating expenses in 1998 include PLN 12,300 for research and development.

Prokom Software S.A.
Notes to consolidated financial statements
(Expressed in Polish Złoty (PLN) all amounts in thousands)

	<u>Year ended 31 December 1998</u>	<u>Year ended 31 December 1997</u>
20. Other operating income/(expenses), net		
Foreign exchange losses, net	(247)	(1,819)
Gain on sale of land (see Note 23)	1,960	-
Donations	(7,268)	-
Other provisions, net	846	2,010
Other, net	(471)	181
Total	<u>(5,180)</u>	<u>372</u>

Donations comprise amounts given by the Company for religious, health protection, sport, educational and charitable purposes.

	<u>Year ended 31 December 1998</u>	<u>Year ended 31 December 1997</u>
21. Financial income /(expense), net		
Interest from bank deposits	11,016	5,722
Realized gains on sales of equity investments	6,984	-
Dividend received from equity investments	277	-
Write-down of equity securities to market value	(7,191)	-
Realized gains on sales of government bonds	11,494	-
Increase in market value of government bonds	5,374	-
Financial income from related parties (see Note 23)	4,597	-
Interest on loans from non-related parties	576	-
Bank charges, fees and commissions	(1,276)	-
Bank interest payable	(380)	(1,512)
Other, net	(254)	-
Total	<u>31,217</u>	<u>4,210</u>

	<u>Year ended 31 December 1998</u>	<u>Year ended 31 December 1997</u>
22. Corporate income tax		
Current tax	40,666	19,999
Deferred tax	(3,634)	-
	<u>37,032</u>	<u>19,999</u>

On the basis of the Act of 23 December 1988 on economic activity with foreign capital participation the Company was exempted from corporate income tax from 30 March 1994 to 29 March 1997. The corporate income tax charge for 1997 therefore covers the period from 30 March 1997 to 31 December 1997.

Reconciliation of tax expense:

The Company's corporate income tax charge differs from the amount that would arise using the statutory tax rate as follows:

Profit before tax	<u>103,243</u>	<u>51,859</u>
Expected income tax expense	37,167	19,706
Increase/(decrease) resulting from:		
Benefit of tax holiday	-	(5,056)
IT business acquired from Prokom Investments accounted for as uniting of interest	-	4,371
Tax losses in subsidiaries not utilized	373	559
Tax on other, net	(508)	419
	<u>37,032</u>	<u>19,999</u>

The corporate tax rate in Poland for 1998 was 36% (38% in 1997).

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There is no procedure for final agreement of tax assessments. The tax authorities may examine the accounting records for up to five years after the end of the year to which they relate. Consequently, the Company may be subject to additional tax liabilities in the event of such an audit. However, the Management Board is not aware of any significant unaccrued potential tax liability that might arise in these circumstances.

The Company has not had a deferred tax liability throughout the periods covered by these financial statements.

23. Related party transactions

	<u>31.12.1998</u>	<u>31.12.1997</u>
Related party receivables		
Amounts due from Prokom Investments SA	73,575	5,591
Amounts due from Nihonsvi AG	4,288	-
Other related party balances	3,282	1,629
	81,145	7,220
less long term	(21,761)	(5,591)
	<u>59,384</u>	<u>1,629</u>

Prokom Investments SA is one of the shareholders of the Company in which Mr Ryszard Krauze, the chairman of the management board and a major shareholder of the Company, has a dominant interest.

Nihonsvi AG is one of the shareholders of the Company and it also has a financial interest in Prokom Investments SA.

	<u>31.12.1998</u>	<u>31.12.1997</u>
Amounts due from Prokom Investments SA:		
Long term loans (i)	5,591	5,591
Trade receivable	326	-
Other short term receivables (ii)	15,024	-
Funding for joint real estate projects (iii)	16,170	-
Prokom Investments SA commercial papers (iv)	24,072	-
Bills of exchange drawn on Prokom Investments SA (v)	12,392	-
	73,575	5,591
less long term (i), (iii)	(21,761)	(5,591)
	<u>51,814</u>	<u>-</u>

- (i) Non-interest bearing loans with no fixed repayment date which are regarded as long-term in nature.
- (ii) In February 1998 the Company purchased land in Warsaw for PLN 13,064. In June 1998 this land was sold to Prokom Investments SA for PLN 15,024. The gain on sale of PLN 1,960 is recorded as other operating income (see Note 20). According to the agreement with Prokom Investments SA the receivable for this transaction should have been settled by 31 December 1998. In January 1999 the Company postponed repayment until 31 December 1999 and since 1 January 1999 this amount bears interest of 16% annually.
- (iii) The Company has advanced PLN 16,170 to Prokom Investments SA, of which PLN 14,530 was paid in cash in 1998, to provide funding for real estate projects by that company. The amount does not bear interest and has no fixed repayment date; it is therefore regarded as long term in nature. The return to the Company on this advance will be based on the performance of the underlying real estate project in proportion to the amounts contributed by each party.
- (iv) In 1998 the Company purchased commercial papers issued by Prokom Investments SA for the total consideration of PLN 37,076, of which PLN 14,557 was sold in 1998. The total gain recognised on sale of the commercial papers in 1998 was PLN 984. The other commercial papers will be redeemed at 29 June 1999. Income earned on the commercial papers held at 31 December 1998 was PLN 1,553.
- (v) In 1998 the Company purchased 5 bills of exchange from Prokom Investments SA for PLN 11,326. The bills of exchange are payable at the Company's call and bear interest of 18%. Interest accrued not received in 1998 was PLN 1,066.

In 1998 the Company purchased two bills of exchange from Nihonsvi AG for PLN 3,000 and 3,300 which bear an interest of 19.39% and 18% respectively. The bills of exchange are payable at the Company's call. In October 1998 Nihonsvi AG repaid PLN 2,242. Interest receivable in 1998 on the bills of exchange was PLN 345, of which PLN 230 was accrued at 31 December 1998.

Other related party balances include:

Loans to NKA Investments Sp. z o.o. (vi)	926	-
Loan to Kompap SA (vii)	442	-
Receivables and loans to non-consolidated subsidiaries	1,914	1,629
	<u>3,282</u>	<u>1,629</u>

- (vi) In November and December 1998 the Company made loans to NKA Investments Sp. z o.o., a company in which Ryszard Krauze holds a majority of shares (see Note 10). The loans bear interest at 18% and are to be repaid on demand. Interest recorded on the loan in 1998 was PLN 8.

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(vii) In February 1998 the Company made a loan to Kompap SA, a company in which Prokom Investments SA holds a financial interest, for the amount of PLN 350. The loan bears interest at 31% and is to be repaid on demand. Interest recorded on the loan in 1998 was PLN 92. The loan was repaid in January 1999.

Financial income from related parties (see Note 21)

	Year ended 31 December 1998	Year ended 31 December 1997
Prokom Investments SA	3,603	-
Nihonsvi AG	345	-
KPNS Sp. z o.o.	418	-
Baltway SA	131	-
NKA Investments Sp. z o.o.	8	-
Kompap SA	92	-
	<u>4,597</u>	<u>-</u>

KPNS Sp. z o.o. is a company in which Mr Ryszard Krauze has a dominant interest. In 1998 the Company purchased commercial papers issued by KPNS Sp. z o.o. which were subsequently sold. Baltway SA is a subsidiary of Prokom Investments SA. The Company purchased commercial papers issued by Baltway SA during the year, which were sold before 31 December 1998.

Related party payables

Amounts payable to related parties at 31 December 1997 consisted of amounts due to Prokom Investments SA in respect of the transfer in 1997 of that company's information technology business to the Company.

Services purchased from related parties in 1998

	Year ended 31 December 1998	Year ended 31 December 1997
Prokom Investments SA	6,851	-
Baltway SA	643	-
	<u>7,494</u>	<u>-</u>

The services purchased from Prokom Investments SA comprise:

Rental costs of aircraft	3,604	-
Rental of cars	1,294	-
Marketing costs	1,568	-
Accounting services	20	-
Other	365	-
	<u>6,851</u>	<u>-</u>

Services purchased from Baltway SA comprise mainly office rent.

In July 1998 the Company signed an agreement to rent an aircraft from Prokom Investments SA until November 2000. In addition Prokom Investments SA re-invoices the insurance costs to the Company. The total amount outstanding under this rental agreement at 31 December 1998 was PLN 13,570.

In October 1998 the Company signed an agreement to rent cars for business purposes from Prokom Investments SA until September 2000. The total amount outstanding under this rental agreement at 31 December 1998 was PLN 1,537.

In June 1998 the Company signed an agreement with Baltway SA, to lease office space from 1 July 1998 for 5 years. Total rent in 1998 was PLN 643. In addition, the total cost of leasehold improvements incurred by the Company in the offices was PLN 1,876. The total amount outstanding under this rental agreement at 31 December 1998 was PLN 13,419.

Future lease commitments

The future minimum lease payments under non-cancellable operating leases (with related parties) are as follows:

	Year ended 31 December 1998	Year ended 31 December 1997
Amounts falling due:		
In less than 1 year	11,490	-
After 1 year and not later than 5 years	17,036	-
	<u>28,526</u>	<u>-</u>

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Guarantees given

In addition the Company gave guarantees to BIG Bank Gdański SA for the maximum amount of PLN 11,500 and USD 900,000 as surety for the letter of credit issued by the bank to Petrolinvest Sp. z o.o., in which Prokom Investments SA has a financial interest.

24. Purchase of business

In May 1997, the Company purchased Koma S.A. and Combidata Poland Sp. z o.o. from Prokom Investments S.A. These purchases were accounted for as unitings of interests. The book values of assets and liabilities acquired were as follows:

Cash	1,712
Net current assets	5,115
Investments at cost	127
Tangible assets	479
Minority interest	(3,611)
Total	3,822
Excess of acquisition cost over net assets acquired	11,238
Total purchase price	15,060
Less cash acquired	(1,712)
Cash flow on acquisition, net of cash acquired	13,348

Total excess of acquisition cost over net assets acquired was treated as follows:

Goodwill on consolidation	2,608
Deferred income	(647)
Reduction of shareholders' equity	9,277
	11,238

In October 1997 the Company acquired the information technology business previously undertaken by Prokom Investments SA. This acquisition was accounted for as a uniting of interests and the amounts below reflect the values of the assets and liabilities as at 1 January 1996 (the deemed merger date). The book values of assets and liabilities acquired as at 1 January 1996, expressed in terms of the purchasing power of the Polish Złoty at 31 December 1996, were as follows:

Net current assets	(12,135)
Long term assets	21,737
Investments	51
Tangible fixed assets	5,723
Intangible fixed assets	17,638
Long term liabilities	(19,874)
	13,140
less consideration payable	(7,000)
	6,140

The difference between the purchase price and the value of the net assets acquired was treated as an adjustment to shareholders' equity in 1996. Movements in the value of the net assets acquired between 1 January 1996 and the date of acquisition in October 1997 were treated as funding movements with Prokom Investments SA and adjusted against shareholders' equity.

In addition in 1997 the Company increased its interest in Koma to 75% of that company's share capital (51% as at 31 December 1996) and in Combidata to 67.5% (51% as at 31 December 1996) for total consideration of PLN 1,211.

25. Financial instruments

Credit risk

Financial assets, which potentially subject the Company and its affiliates to concentration of credit risk, consist principally of cash and cash equivalents, balances with related parties and trade receivables. The Company's cash deposits are with the major Polish banks.

Trade receivables, which are presented net of the allowance for doubtful receivables, generally include significant amounts from a small number of customers, reflecting the nature of the Company's business that is focused on a small number of large contracts for major Polish corporations.

At 31 December 1998 four customers accounted for 73% of the total amount of trade receivables; at 31 December 1997, three customers accounted for 83 % of the total.

Foreign currency risk

The Company's revenues and costs are predominantly denominated in Polish zloty; the exception to this is equipment purchased in foreign currency for ultimate resale to customers. For such revenues the Polish zloty sale price is, as far as possible, linked to the underlying foreign currency purchase and invoiced in Polish zloty based on a foreign currency value converted at the exchange rate prevailing at date of sale. In view of the costs involved management do not believe it is cost effective to use financial instruments to hedge or otherwise seek to reduce foreign currency risk.

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Fair values

At 31 December 1998 and 31 December 1997 the carrying amounts of cash and cash equivalents, accounts receivable, accounts payable and accrued expenses, short-term borrowings and long-term investments approximated their fair values.

26. Earnings per share (not in thousands)

Earnings per share have been calculated based on net profit for each year divided by the weighted average number of shares in issues.

The weighted average number of shares was 12,700,000 (1997: 10,095,372).

There is no actual or potential dilutive impact on earnings per share at 31 December 1998.

27. Management Board and Supervisory Board Remuneration

The total remuneration, including salary and bonuses, paid or accrued by the Company to the members of the Management and Supervisory Boards in the period 1 January 1998 to 31 December 1998 was PLN 2,843 (1997: PLN 428)

28. Subsequent events

In January 1999 the Company purchased a bill of exchange from Elterix SA (see Note 10) for PLN 1,200 which bears interest of 16.45% and is repayable on 25 January 2000.

29. Guarantees given

In addition to guarantees given described in Note 23, as at 31 December 1998 the Company gave the following guarantees:

- a) Zakład Ubezpieczeń Społecznych – total amount of guarantee is PLN 9,259 for proper conduct of the contract, guarantee is valid until 28 February 2002 (deemed date of the completion of the contract).
- b) Other guarantees totaling PLN 992.

30. Future lease commitments

The future minimum lease payments under non-cancellable operating leases (other than those disclosed in Note 23) are as follows:

	Year ended 31 December 1998	Year ended 31 December 1997
Amounts falling due:		
In less than 1 year	5,485	-
After 1 year and not later than 5 years	5,748	-
	<hr/> 11,233	<hr/> -