

**TÜRK HAVA YOLLARI ANONİM ORTAKLIĐI**

FINANCIAL STATEMENTS

PREPARED IN ACCORDANCE WITH

CAPITAL MARKET BOARD STANDARDS

FOR THE YEAR ENDED 31 DECEMBER 2005

TOGETHER WITH INDEPENDENT AUDITORS' REPORT

To the Board of Directors of  
Türk Hava Yolları Anonim Ortaklığı

1. We have audited the accompanying balance sheet of Türk Hava Yolları Anonim Ortaklığı ("the Company") as at 31 December 2005, and the related statements of income, shareholders' equity and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

2. We conducted our audits in accordance with the standards issued by the Capital Market Boards of Turkey ("CMB"). 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.

3. In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Türk Hava Yolları Anonim Ortaklığı as of 31 December 2005 and the results of its operations and its cash flows for the year then ended in conformity with generally accepted accounting standards issued by the CMB.

4. Additional paragraph for convenience translation into English:

The effects of differences between accounting principles issued by the CMB (see note 2), the accounting principles generally accepted in countries in which the accompanying financial statements are to be distributed and International Financial Reporting Standards ("IFRS") have not been quantified and reflected in the accompanying financial statements. Accordingly, the accompanying financial statements are not intended to present the Company's financial position and results of operations and changes in financial position and cash flows in accordance with accounting principles generally accepted in such countries of users of the financial statements and IFRS.

Can Uluslararası Denetim A.Ş.  
A Member Firm of INPACT International

Abdülkadir SAYICI  
Partner

31 March 2006, İstanbul, Turkey

**TÜRK HAVA YOLLARI ANONİM ORTAKLIĞI**  
**BALANCE SHEETS**  
**AS AT 31 DECEMBER 2005 AND 2004**

*(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)*

<b>ASSETS</b>	<b>Note</b>	<b>Audited</b> <b>31 December 2005</b>	<b>Audited</b> <b>31 December 2004</b>
<b>Current Assets</b>		<b>825.922.684</b>	<b>677.317.067</b>
Cash and Cash Equivalents	4	482.910.555	365.637.483
Marketable Securities (net)	5	-	-
Accounts Receivable (net)	7	191.596.806	158.585.050
Financial Lease Receivables (net)	8	-	-
Due from Related Parties (net)	9	970.701	812.921
Other Receivables (net)	10	6.567.690	2.989.387
Biological Assets (net)	11	-	-
Inventories (net)	12	84.255.279	64.513.843
Receivables from Construction Contracts in Progress (net)	13	-	-
Deferred Tax Assets	14	-	-
Other Current Assets	15	59.621.653	84.778.383
<b>Non-Current Assets</b>		<b>2.688.869.983</b>	<b>2.270.835.407</b>
Accounts Receivable (net)	7	-	-
Financial Lease Receivables (net)	8	-	-
Due from Related Parties (net)	9	-	-
Other Receivables (net)	10	1.901.488	1.921.124
Financial Assets (net)	16	37.406.378	42.636.073
Positive/Negative Goodwill (net)	17	-	-
Investment Property	18	-	-
Tangible Fixed Assets (net)	19	2.631.113.979	2.206.147.116
Intangible Fixed Assets (net)	20	6.154.133	7.463.579
Deferred Tax Assets	14	-	-
Other Non-current Assets	15	12.294.005	12.667.515
<b>Total Assets</b>		<b>3.514.792.667</b>	<b>2.948.152.474</b>

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

**TÜRK HAVA YOLLARI ANONİM ORTAKLIĞI**  
**BALANCE SHEETS**  
**AS AT 31 DECEMBER 2005 AND 2004**

*(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)*

	Note	Audited 31 December 2005	Audited 31 December 2004
<b>LIABILITIES</b>			
<b>Short Term Liabilities</b>			
Bank Borrowings (net)	6	362.903.225	-
Short-term Portion of Long-term Bank Borrowings (net)	6	-	-
Financial Lease Obligations (net)	8	179.092.821	202.712.254
Other Financial Liabilities (net)	10	332.636	281.244
Accounts Payable (net)	7	255.994.916	190.770.953
Due to Related Parties (net)	9	8.022.859	6.508.221
Advances Received	21	52.397.414	34.452.683
Billings on Construction Contracts in Progress (net)	13	-	-
Provisions for Liabilities	23	27.543.644	25.222.977
Deferred Tax Liabilities	14	-	-
Other Liabilities (net)	10	312.615.544	261.924.392
		<b>1.198.903.059</b>	<b>721.872.724</b>
<b>Long Term Liabilities</b>			
Bank Borrowings (net)	6	-	-
Financial Lease Obligations (net)	8	856.730.859	957.728.732
Other Financial Liabilities (net)	10	-	-
Accounts Payable (net)	7	7.124.267	8.556.817
Due to Related Parties (net)	9	-	-
Advances Received	21	-	-
Provisions for Liabilities	23	113.641.242	99.777.377
Deferred Tax Liabilities	14	90.051.647	46.484.742
Other Liabilities (net)	10	-	3.618.326
		<b>1.067.548.015</b>	<b>1.116.165.994</b>
	24	-	-
<b>MINORITY INTERESTS</b>			
		<b>1.248.341.593</b>	<b>1.110.113.756</b>
<b>SHAREHOLDERS' EQUITY</b>			
<b>Share Capital</b>	25	<b>175.000.000</b>	<b>175.000.000</b>
<b>Capital Reserves</b>	26-27-28	<b>1.872.838.374</b>	<b>1.872.838.374</b>
- Share Premium		181.185	181.185
- Share Premium of Cancelled Shares		-	-
- Revaluation Surplus on Tangible Fixed Assets		-	-
- Revaluation Increments on Financial Assets		-	-
- Restatement Effect on Shareholders' Equity		1.872.657.189	1.872.657.189
<b>Profit Reserves</b>	26-27-28	<b>8.223.909</b>	<b>8.223.909</b>
- Legal Reserves		417.011	417.011
- Statutory Reserves		-	-
- Extraordinary Reserves		7.806.889	7.806.889
- Special Funds		9	9
- Associate Shares and Gain on Sale of Investment		-	-
Property to be added to Capital		-	-
- Foreign Currency Translation Differences		-	-
<b>Net Profit for the Year</b>		<b>138.227.837</b>	<b>107.058.441</b>
<b>Accumulated Profits/(Losses)</b>	26-27-28	<b>(945.948.527)</b>	<b>(1.053.006.968)</b>
<b>Total Liabilities and Shareholders' Equity</b>		<b>3.514.792.667</b>	<b>2.948.152.474</b>

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

**TÜRK HAVA YOLLARI ANONİM ORTAKLIĞI**  
**STATEMENTS OF INCOME FOR THE YEARS ENDED**  
**31 DECEMBER 2005 AND 2004**

*(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)*

	Note	Audited 1 January – 31 December 2005	Audited 1 January – 31 December 2004
<b>MAIN OPERATING REVENUES</b>			
Sales Revenues (net)	36	2.953.354.162	2.592.697.139
Cost of Sales (-)	36	(2.435.869.117)	(2.084.379.054)
Service Revenues (net)		-	-
Other Revenues from Main Operations /Interest +Dividend+Rent (net)	36	153.717.446	200.688.807
<b>GROSS OPERATING PROFIT</b>		671.202.491	709.006.892
Operating Expenses (-)	37	(577.630.482)	(566.458.446)
<b>NET OPERATING PROFIT</b>		93.572.009	142.548.446
Income from Other Operations	38	425.430.333	371.382.815
Losses from Other Operations (-)	38	(277.165.588)	(248.497.343)
Financial Expenses (-)	39	(60.042.012)	(42.347.448)
<b>OPERATING PROFIT</b>		181.794.742	223.086.470
Net Monetary Gain /(Loss ) (net)	40	-	(113.210.018)
MINORITY INTEREST	24	-	-
<b>PROFIT BEFORE TAXATION</b>		181.794.742	109.876.452
Taxes	41	(43.566.905)	(2.818.011)
<b>NET PROFIT FOR THE YEAR</b>		<b>138.227.837</b>	<b>107.058.441</b>
<b>EARNINGS PER SHARE (YKr)</b>	42	0,079	0,061

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

**TÜRK HAVA YOLLARI ANONİM ORTAKLIĞI**  
**STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY FOR THE YEARS**  
**ENDED 31 DECEMBER 2005 AND 2004**

*(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)*

	Share Capital	Restatement Effect on Shareholders' Equity	Share Premium	Legal Reserves	Extraordinary Reserves	Special Funds	Net Profit/(Loss) For The Year	Accumulated Losses	Total
Balances at 31 December 2003	175.000.000	1.872.657.189	181.185	417.011	7.806.889	9	243.458.570	(1.296.465.538)	1.003.055.315
Transfer of Previous Year's Profit to Accumulated Losses	-	-	-	-	-	-	(243.458.570)	243.458.570	-
Net Profit for the Year	-	-	-	-	-	-	107.058.441	-	107.058.441
Balances at 31 December 2004	<u>175.000.000</u>	<u>1.872.657.189</u>	<u>181.185</u>	<u>417.011</u>	<u>7.806.889</u>	<u>9</u>	<u>107.058.441</u>	<u>(1.053.006.968)</u>	<u>1.110.113.756</u>
Transfer of Previous Year's Profit to Accumulated Losses	-	-	-	-	-	-	(107.058.441)	107.058.441	-
Net Profit for the Year	-	-	-	-	-	-	138.227.837	-	138.227.837
Balances at 31 December 2005	<u>175.000.000</u>	<u>1.872.657.189</u>	<u>181.185</u>	<u>417.011</u>	<u>7.806.889</u>	<u>9</u>	<u>138.227.837</u>	<u>(945.948.527)</u>	<u>1.248.341.593</u>

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

## **Türk Hava Yolları Anonim Ortaklığı**

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)

### **1 THE COMPANY'S ORGANIZATION AND OPERATIONS**

Türk Hava Yolları A.O. (“the Company” or “THY”) was incorporated in Turkey in 1933. The principal activity of the Company is domestic and international air transportation of passengers and cargo.

As of 31 December 2005, the shareholders and their respective shareholdings in the Company were as follows:

Republic of Turkey Prime Ministry Privatization Administration	75,18 %
Others	<u>24,82 %</u>
Total	<u>100,00 %</u>

The total number of employees working for the Company as of 31 December 2005 is 11.121 (2004: 10.956). The average number of employees working for the Company in the years 2005 and 2004 is 11.151 and 10.341, respectively. Financial assets of the Company are stated at note 16.

The Company is registered in İstanbul, Turkey and its head office address is as follows:  
Türk Hava Yolları Genel Yönetim Binası, Atatürk Havalimanı, 34149 Yeşilköy- İstanbul.

### **2 BASIS OF PRESENTATION OF FINANCIAL STATEMENTS**

#### *Accounting Standards Applied:*

The Company maintains its books of account and prepares its statutory financial statements in accordance with Turkish Uniform Chart of Accounts, Turkish Commercial Code, Turkish Tax Laws and generally accepted accounting principles promulgated by Capital Markets Board and applicable to the companies quoted in Istanbul Stock Exchange.

The Company’s financial statements are prepared in accordance with accounting and reporting principles promulgated by Capital Markets Board. Capital Markets Board issued a comprehensive set of accounting principles in the Comminique Serial XI no:25 “Accounting Principles in the Capital Markets”. In the Comminique, it is stated that alternatively application of accounting standards promulgated by International Accounting Standards Board (IASB) and International Accounting Standards Committee (IASC) is deemed as the application of accounting principles of Capital Markets Board (CMB).

By the decision made on 17 March 2005, Capital Markets Board declared that for companies which operate in Turkey and prepare financial statements in accordance with accounting principles of Capital Markets Board it is not required to apply inflation accounting effective after 1 January 2005. Therefore, IAS 29 “Financial Reporting in Hyperinflationary Economies” issued by IASC was not applied in the financial statements, all other International Financial Reporting Standards pertaining to measurement and all changes made in those standards in 2005 were applied. Financial statements and footnotes are presented in the compulsory formats by an announcement of CMB dated 20 December 2004.

## Türk Hava Yolları Anonim Ortaklığı

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)

### 2 BASIS OF PRESENTATION OF FINANCIAL STATEMENTS (cont'd)

#### *New Turkish Lira:*

A new law, numbered as 5083 on the Monetary Unit of the Republic of Turkey was enacted with the effect from 1 January 2005, which deletes six zeroes from the former currency of Republic of Turkey, The Turkish Lira ("TL"), to form a new currency the New Turkish Lira ("YTL"). Thus, YTL 1 = TL 1.000.000. The New Turkish Lira is divided into 100 New Turkish cents ("YKr"). As per the CMB decision numbered MSD-10/832-43399 dated 1 December 2004, the financial statements to be announced publicly in 2005 should be prepared in YTL including comparatives. Accordingly, the accompanying financial statements are presented in YTL.

#### *Preparation of Financial Statements in Hyperinflationary Periods:*

Depending on the CMB's decision dated on 17 March 2005 which stated that for the companies preparing the financial statements in accordance with CMB Accounting Standards it is not required to apply inflation accounting effective after 1 January 2005, The Company have not applied inflation accounting after 1 January 2005. The balance sheet as of 31 December 2004 and the income statement for the year 2004 which were presented for comparison are stated in the purchasing power of YTL as of 31 December 2004.

International Accounting Standard 29 (IAS 29), "Financial Reporting in Hyperinflationary Economies", requires financial statements prepared in the currency of a hyperinflationary economy to be adjusted by purchasing power of that currency as of balance sheet date and previous period's financial statements to be adjusted for comparison by using the same values. One of the primary reasons requiring application of IAS 29 is three-year cumulative inflation rate approaching to or exceeding 100 %. Adjustment was made by using conversion factors derived from countrywide Wholesale Price Index announced by the State Institute of Statistics. The indices and the conversion factors used to restate the financial statements as at 31 December 2004 and 31 December 2005 are given below:

<u>Dates</u>	<u>Index</u>	<u>Conversion Factor</u>	<u>Three-year cumulative inflation rates %</u>
31 December 2004	8.403,8	1,000	69,7
31 December 2005	8.785,7	1,000	35,6

As at 31 December 2005, the exchange rate announced by Central Bank of Turkey was YTL 1,3418 = US Dollar 1 (2004: YTL 1,3421 = US Dollar 1).

The main procedures for the restatement of previous period's financial statements are given below:

- Previous period's financial statements in the currency of a hyperinflationary economy are expressed at the purchasing power as of 31 December 2004.
- Monetary assets and liabilities are not restated because they are already expressed in terms of the monetary unit at the balance sheet date.
- Non-monetary assets and liabilities and shareholders' equity which was not expressed at the purchasing power as of balance sheet date are restated by using relevant conversion factors.
- All items in the income statement are restated by using relevant (monthly) conversion factors and expressed at the purchasing power as of 31 December 2004.
- The effect of inflation on the Company's net monetary position is reflected as net monetary gain/loss in the previous period's income statement.

### 2 BASIS OF PRESENTATION OF FINANCIAL STATEMENTS (cont'd)



## **Türk Hava Yolları Anonim Ortaklığı**

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)

### **Basis of Consolidation:**

The associate of which participation rate of THY is 50% and not controlled by the Company is valued by equity method.

For purposes of financial statements, the associate's principal activity and direct and indirect participation rate of the Company are given below:

<u>Name of the Company</u>	<u>Principal Activity</u>	<u>Direct Participation</u>	<u>Indirect Participation</u>	<u>Country of Registration</u>
Güneş Ekspres Havacılık A.Ş.	Air Transportation	50%	-	Turkey

In equity method, the associate is presented on the balance sheet at net asset value and the portion of the Company from its operations is added to the income statement.

### *Comparative Information*

Current period financial statements have been prepared as comparative with the prior year financial statements. In order to provide an appropriate presentation of current period's financial statements, the comparative information have been re-classified in terms of any necessity occurrences.

### *Offsetting*

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to set off the recognized amounts and there is an intention to settle on a net basis, or realize the asset and settle the liability simultaneously.

## **3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

The significant accounting policies followed in the preparation of the accompanying financial statements are as follows:

### **3.1 Revenue Recognition and Commission Expenses**

Passenger fares and cargo revenues are recorded as operating revenue when the transportation service is provided. Tickets sold but not yet used are recorded as passenger flight liabilities.

The Company develops estimations using historical statistics and data for unredeemed tickets. Total estimated unredeemed tickets were recognized as operating revenue.

Agency commissions to relating to the passenger revenue are recognized as expense when the transportation service is provided.

### **3.2 Inventory Valuation**

Inventories are valued at the lower of cost, by using the moving weighted average method, or net realizable value.

## Türk Hava Yolları Anonim Ortaklığı

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)

### 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd)

#### 3.3 Tangible Fixed Assets

Tangible fixed assets are measured at net book value calculated as acquisition cost at 31 December 2005 less accumulated depreciation. Tangible fixed assets are depreciated on a periodical basis for all categories.

The useful lives and residual values used for the depreciable assets are as follows:

	<u>Useful Life (Years)</u>	<u>Residual Value</u>
- Land	-	-
- Buildings	25-50	-
- Aircraft	15	30%
- Engines	15	30%
- Components	5-8-10	-
- Repairables	2-3	-
- Simulators	10	-
- Machinery and Equipments	3-5-7-10	-
- Furniture and Fixtures	3-4-5	-
- Motor Vehicles	4-5-7	-
- Other Equipments	5	-

#### 3.4 Intangible Fixed Assets

Intangible fixed assets, include leasehold improvements, rights, information systems and software. Intangible fixed assets are reflected at cost as of 31 December 2005, leasehold improvements are depreciated over their lease periods and other intangible fixed assets are depreciated over their useful life of 5 years, on a periodical basis.

#### 3.5 Impairment on Assets:

In international markets, purchasing and second hand trading of aircraft and similar assets are realized in US Dollar. As a result of inflation rate being higher than devaluation of YTL against US Dollar in recent years, net book values of aircraft, spare engines and simulators adjusted for the effect of inflation have exceeded net book values of these assets based on their US Dollar acquisition costs.

The Company's management considers that the situation explained above causes a fictitious increase in value. Therefore, the Company decreases the adjusted net book value of its aircraft, spare engines and simulators to net book value of these assets based on US Dollar acquisition costs. An examination is then made of whether net book values based on US Dollar acquisition costs may exceed their recoverable amount. Recoverable amount is determined as higher of the present value of cash flows expected from the use of assets and the net selling price of these assets. Net selling price is determined according to International Aircraft Price Guide. In the accompanying financial statements, the difference between adjusted net book values of these assets and net book values based on US Dollar acquisition costs is netted off against monetary gain. The difference between net book values of these assets based on US Dollar acquisition costs and recoverable amount is recognized as impairment loss under operating expenses.

## **Türk Hava Yolları Anonim Ortaklığı**

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)

### **3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd)**

#### **3.6 Borrowing Costs**

Banks loans are recognized initially at cost, less attributable transaction costs. Subsequent to initial recognition, borrowings are stated at amortised costs with any difference between cost and redemption value being recognised in the income statement over the period of the borrowings on an effective interest basis. Finance expenses resulted from bank loans are recorded to income statement in the period in which they are incurred.

#### **3.7 Manufacturers' Credits**

Manufacturers' credits are received against acquisition and/or lease of aircraft and engines. The Company records these credits as a reduction to the cost of the owned or financial leased assets and amortizes them over the related asset's remaining useful life. Manufacturers' credits related to operational leases are recorded as deferred revenue and amortized over the lease term.

#### **3.8 Financial Instruments and Financial Risk Management**

##### **(a) Classification and Accounting**

The Company classifies and accounts for financial instruments as follows:

##### *Securities Held for Trading:*

Securities held for trading are those acquired principally for the purpose of generating profit from short-term fluctuations in their prices. Subsequent to initial recognition, held for trading securities are valued at their fair value if measured reliably. Gains or losses on these securities are recognized in net profit or loss for the period in which they arise.

##### *Investments Held to Maturity:*

Investments held-to-maturity are securities with fixed or determinable payments and fixed maturity that the Company has the positive intent and ability to hold to maturity.

##### *Investments Available for Sale:*

Investments available-for-sale are those investments that the ownership rate is less than or equivalent to 20% and are not held for trading. Subsequent to acquisition, available for sale investments which are traded at stock markets are valued at market rate on balance sheet date. Those whose market value cannot be measured reliably are valued at cost. Gains or losses on available for sale investments are recognized in net profit or loss for the period in which they arise.

##### *Investments At Equity:*

Investment that the ownership rate is 50% and the Company is not in a position to exercise sole control are carried at equity.

##### **(b) Measurement**

Fair value is the amount for which an asset could be exchanged or a liability settled, between knowledgeable willing parties in an arm's-length transaction. Market value is the amount obtainable from the sale or payable on the acquisition, of a financial instrument in an active market, if one exists.

The estimated fair values of financial instruments have been determined by the Company using available market information and appropriate valuation methodologies. However, judgment is necessarily required to interpret market data to develop the estimated fair value. Accordingly, the estimates presented here in may not necessarily be indicative of the amounts the Company could realize in a current market exchange.

## **Türk Hava Yolları Anonim Ortaklığı**

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)

### **3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd)**

#### **3.8 Financial Instruments and Financial Risk Management (cont'd)**

Balances with banks, receivables, contingent liabilities such as letters of guarantee and letters of credit are important financial instruments which would have negative effects on the financial structure of the Company if the other party failed to comply with the terms and conditions of the agreement.

The fair values of certain financial assets carried at cost are considered to be representative of carrying values due to their short-term nature.

The Company's principal financial assets are cash and cash equivalents, accounts and other receivable, due from related parties and available for sale financial assets.

Book values of trade receivables and due from related parties along with the related allowances for uncollectibility are estimated to be their fair value except for discount of these receivables to their present value when they hold significant credit periods.

Güneş Ekspres Havacılık A.Ş. is accounted for using the equity method as the Company exercises a significant influence. Uçak Servisi A.Ş. and France Telecom shares are classified as available for sale investments and changes in their fair value are recognized in net profit or loss.

Financial assets, other than Güneş Ekspres Havacılık A.Ş., Uçak Servisi A.Ş. and France Telecom where the Company is not in a position to exercise significant influence or joint control, are stated at cost as their fair value can not be measured reliably.

Financial liabilities are classified according to the substance of the contractual arrangements entered into. Significant financial liabilities include bank borrowings, financial lease obligations, accounts and other payables, due to related parties. Foreign currency bank loans are translated into New Turkish Lira at the rates of change ruling at the balance sheet date.

Book values of accounts payable and due to related parties are estimated to reach their fair value, except discounting of these liabilities.

Financial expenses are accounted for on an accrual basis and are traced under related financial liability account to the extent that they are not settled in the period in which they arise. Accounts and other payables and due to related parties are recorded at their nominal value, which approximates their fair value.

#### *Credit Risk*

The Company's credit risk is primarily attributable to its trade receivables. The amounts disclosed in the balance sheet are net of allowances for doubtful receivables, estimated by the Company's management based on prior experience and the current economic environment. The Company has no significant concentration of credit risk, with exposure spread over a large number of counter parties and customers.

### **3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd)**

#### **3.8 Financial Instruments and Financial Risk Management (cont'd)**

## Türk Hava Yolları Anonim Ortaklığı

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)

### Price Risk

#### • Currency Risk:

The Company is exposed to exchange rate fluctuations between foreign currencies and New Turkish Lira due to the nature of its business. The major part of the Company's ticket income is in Euro and US Dollar or linked to these currencies and the major part of its expenses is denominated in US Dollar and New Turkish Lira.

#### • Interest Risk:

Some of the interest rates related to leasing transactions are based on LIBOR. Therefore the Company is exposed to interest rate fluctuations on international markets. The Company does not have hedging transactions to limit currency and interest rate risks.

#### • Market Risk:

The Company invests in government bonds acquired under reverse repurchase agreements made for short periods or deposits to banks on a monthly or quarterly basis. Fair values of these investments fluctuate based on market conditions.

#### • Liquidity Risk

In general, tickets are sold in advance and transportation is provided later. Therefore, the Company takes advantage of collecting revenue in advance and incurring transportation cost later. The Company also benefits from the difference between the collection and the payment periods.

### 3.9 Foreign Currency Transactions

Transactions in foreign currencies are translated into New Turkish Lira at the rates of exchange ruling at the transaction dates. Monetary assets and liabilities denominated in foreign currencies are translated at the exchange rate ruling at the balance sheet date. Gains and losses arising on settlement and translation of foreign currency items are included in the statements of income.

The closing and average NTL to US Dollar exchange rates for the periods are as follows:

	<u>Closing Rate</u>	<u>Average Rate</u>
31 December 2004	1,3421	1,4223
31 December 2005	1,3418	1,3405

### 3.10 Earnings Per Share

Earnings per share is calculated by dividing net profit by weighted average number of shares outstanding in the relevant period.

In Turkey, Companies are allowed to increase their capital by distributing free shares to share holders from accumulated profits. In calculation of earnings per share, such free shares are considered as issued shares. Therefore, weighted average number of shares in the calculation of earnings per share is found by applying distribution of free shares retrospectively.

## **Türk Hava Yolları Anonim Ortaklığı**

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)

### **3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd)**

#### **3.11 Events Subsequent To The Balance Sheet Date**

The Company discloses the events subsequent to the balance sheet date in the relevant period.

#### **3.12 Provisions, Contingent Liabilities and Contingent Assets**

Provisions are recognized when there exists a legal liability as a result of the Company's transactions in the past and it is necessary to settle the liability for flow of resources out of the Company and the amount of outflow can be reliably measurable.

Liabilities and assets resulting from past events and existence of which can be approved by occurrence or non-occurrence of one or more events that are not in full control of the entity are not recognized in the financial statements and considered as contingent assets and liabilities.

#### **3.13 Leases**

The Company leases aircraft, engines, simulators, computer equipments and vehicles by financial leases or operational leases. Financial leases are reflected in the Company's balance sheet by recording leased assets and lease liabilities equal to the present value of lease payments. The finance leased assets are depreciated over their useful lives. Operating leases are accounted for as operating expense when incurred.

#### **3.14 Related Parties**

The shareholders, key management personnel and board members of the Company, in each case together with their families and companies controlled by or affiliated with them, are considered and referred to as related parties in the accompanying financial statements. Transactions with related parties for ordinary operations have taken place at prices compliant with market conditions.

#### **3.15 Segmental Reporting**

##### *Business Segments*

The Company operates predominantly in one industry segment, its primary business being the air transportation of passengers and cargo within, to or from Turkey.

##### *Geographical Segments*

Revenue analysis is based on the destinations that the Company serves. All passenger fare and cargo revenue within Turkey is attributed to the revenue from domestic services. Revenue from both scheduled and non-scheduled international flights is attributed to flight destination's geographical area.

#### **3.16 Taxation and Deferred Taxes**

Taxes on income for the period comprise of current tax and deferred tax. The Company accounts for current and deferred taxation on the results for the period.

Provision is made in the financial statements for the Company's estimated liability for Turkish corporation tax on its results for the period. The charge for current tax is based on the results for the period as adjusted for items, which are non-assessable or disallowed.

## **Türk Hava Yolları Anonim Ortaklığı**

Notes to the financial statements as at 31 December 2005

*(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)*

### **3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd)**

#### **3.16 Taxation and Deferred Taxes (cont'd)**

Deferred tax assets and liabilities are recognized using the liability method in respect of material temporary differences arising from different treatment of items for accounting and taxation purposes.

Deferred tax liabilities are recognized for all taxable temporary differences whereas deferred tax assets are only recognized when it is probable that future taxable profit will be available against which the deductible temporary differences can be utilized.

Deferred tax is calculated at the tax rates that are expected to apply to the period when the asset is realized or the liability is settled. Deferred tax is charged or credited in the statement of income.

Prepaid corporation taxes and corporation tax liabilities are offset as they relate to income taxes levied by the same taxation authority. Deferred tax assets and liabilities are also offset.

#### **3.17 Employee Retirement and Termination Indemnities**

Employee retirement and termination indemnities as required by Turkish Labor Law are recognized in the accompanying financial statements as earned. Future retirement payments are discounted to their present value at the balance sheet date at an interest rate determined by the net of an expected inflation rate and an appropriate discount rate. The interest amount included in employee retirement expense is disclosed in the financial result as interest expense.

#### **3.18 Use of Estimates**

The preparation of financial statements in conformity with Accounting Standards promulgated by Capital Markets Board requires management to make estimates and assumptions that affect reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the period. Actual results could differ from those estimations.

#### **3.19 Maintenance and Repair Costs**

Regular maintenance and repair costs for owned and leased assets are charged to operating expense as incurred. Heavy maintenance checks for owned and finance leased aircraft are expensed as incurred and delivery maintenance checks of operational leased aircraft are accrued on a periodical basis.

#### **3.20 Frequent Flyer Program**

The Company provides a frequent flyer program named “Miles and Smiles” in the form of free travel award to its members on accumulated mileage. The estimated cost of providing free travel, using the incremental cost method as adjusted for estimated redemption rates, is recognized as a liability.

The Company also sells mileage credits to participating partners in “Shop and Miles” program. A portion of such revenue is deferred and amortized as transportation is provided.

### **4 CASH AND CASH EQUIVALENTS**

## Türk Hava Yolları Anonim Ortaklığı

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)

Cash and cash equivalents comprised the following:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Cash	195.489	162.030
Cheques received	138.532	116.877
Banks	477.065.690	363.838.243
Other liquid assets	5.510.844	1.520.333
	<u>482.910.555</u>	<u>365.637.483</u>

Foreign currency bank balances are YTL 295.610.051 at 31 December 2005 (2004: YTL 247.555.286).

Time Deposits:

<u>Amount</u>	<u>Currency</u>	<u>Opening Date</u>	<u>Maturity</u>	<u>31 December 2005</u>
170.390.000	YTL	22.07.2005 - 30.12.2005	02.01.2006 - 30.01.2006	170.390.000
31.653.000	Euro	30.12.2005	02.01.2006	50.249.138
149.163.000	US Dollar	27.12.2005 - 30.12.2005	02.01.2006 - 30.01.2006	200.146.913
				<u>420.786.051</u>

<u>Amount</u>	<u>Currency</u>	<u>Opening Date</u>	<u>Maturity</u>	<u>31 December 2004</u>
112.500.000	YTL	25.10.2004 - 31.12.2004	03.01.2005 - 24.01.2005	112.500.000
89.790.000	Euro	31.12.2004	03.01.2005	164.028.372
22.500.000	US Dollar	31.12.2004	03.01.2005	30.197.250
				<u>306.725.622</u>

### 5 MARKETABLE SECURITIES (NET)

None (2004: None).

### 6 BANK BORROWINGS (NET)

Bank Borrowings comprised the following short-term bank credit:

<u>Bank Name</u>	<u>Maturity</u>	<u>Original Amount</u>	<u>Interest Accruals</u>	<u>YTL</u>
T.İş Bankası / Citibank NA London	31.03.2006	270.000.000 US Dollar	459.998 US Dollar	362.903.225

(2004: None).

### 7 ACCOUNTS RECEIVABLE AND PAYABLE (NET)

i) Short-term accounts receivable comprised the following:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Trade receivables	210.448.412	175.591.911
Discount on receivables	(2.334.886)	(341.303)
Provision for doubtful receivables	(16.516.720)	(16.665.558)
	<u>191.596.806</u>	<u>158.585.050</u>



## Türk Hava Yolları Anonim Ortaklığı

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)

### 7 ACCOUNTS RECEIVABLE AND PAYABLE (NET) (cont'd)

ii) Short-term accounts payable comprised the following:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Trade payables	252.278.380	186.439.488
Deposits and guarantees received	3.715.141	4.221.819
Other	1.395	109.646
	<u>255.994.916</u>	<u>190.770.953</u>

iii) Long-term accounts receivable comprised the following:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Deposits and guarantees received	7.124.267	8.556.817

### 8 FINANCIAL LEASE RECEIVABLES AND OBLIGATIONS (NET)

i) Financial Lease Receivables: None (2004: None).

ii) Financial Lease Obligations:

The future lease rental payments under financial leases are as follows:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Not later than one year	221.054.754	237.797.984
Between 1 - 4 years	540.757.739	608.219.202
Over 4 years	458.520.976	451.213.188
	<u>1.220.333.469</u>	<u>1.297.230.374</u>
Less: Future interest expense	<u>(184.509.789)</u>	<u>(136.789.388)</u>
Principal value of future rentals shown in the balance sheets	<u>1.035.823.680</u>	<u>1.160.440.986</u>
Represented by :		
Current liabilities	179.092.821	202.712.254
Long term liabilities	856.730.859	957.728.732
	<u>1.035.823.680</u>	<u>1.160.440.986</u>
Interest range:		
Floating rate obligations	982.205.221	872.924.584
Fixed rate obligations	53.618.459	287.516.402
	<u>1.035.823.680</u>	<u>1.160.440.986</u>

As of 31 December 2005, the US Dollar denominated lease obligations' interest rates for the fixed rate obligations are between 7,12% and 7,70%; and for the floating rate obligations are a margin ranging between LIBOR minus %0,05 and LIBOR plus %3.

The future lease rental payments under operating leases are as follows:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Not later than one year	118.983.335	74.824.262
Between 1 - 4 years	176.568.422	117.723.485
Over 4 years	124.747.806	1.488.724
	<u>420.299.563</u>	<u>194.036.471</u>

### 9 DUE TO AND FROM RELATED PARTIES (NET)

## Türk Hava Yolları Anonim Ortaklığı

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)

i) Due to and from related parties as of 31 December 2005 and 31 December 2004 comprised the following:

Due from related parties comprised the following:

	<b>31 December 2005</b>	<b>31 December 2004</b>
Güneş Ekspres Havacılık A.Ş. (Sun Express)	970.701	812.763
Uçak Servisi A.Ş. (USAŞ)	-	158
	<u>970.701</u>	<u>812.921</u>

Due to related parties comprised the following:

	<b>31 December 2005</b>	<b>31 December 2004</b>
Güneş Ekspres Havacılık A.Ş. (Sun Express)	459.029	211.054
Uçak Servisi A.Ş. (USAŞ)	7.563.830	6.297.167
	<u>8.022.859</u>	<u>6.508.221</u>

ii) Transactions with related parties in the periods ended as of 31 December are as follows:

	<b>31 December 2005</b>	<b>31 December 2004</b>
Services rendered to Sun Express	3.655.346	1.912.675
Services rendered to USAŞ	372.382	256.824
	<u>4.027.728</u>	<u>2.169.499</u>

	<b>31 December 2005</b>	<b>31 December 2004</b>
Services received from Sun Express	866.914	2.603.397
Services received from USAŞ	79.320.622	66.785.003
	<u>80.187.536</u>	<u>69.388.400</u>

Dividends received from Related Parties:

	<b>31 December 2005</b>	<b>31 December 2004</b>
Sun Express	7.080.216	4.237.552
Uçak Servisi A.Ş. (USAŞ)	1.113.723	192.844
Emek İnşaat ve İşletme A.Ş.	69	6.560
France Telecom	157.326	94.106
	<u>8.351.334</u>	<u>4.531.062</u>

## 10 OTHER RECEIVABLES AND LIABILITIES (NET)

i) Other short-term receivables comprised the following:

	<b>31 December 2005</b>	<b>31 December 2004</b>
Due from insurance firms	3.192.141	-
Foreign receivables from technical suppliers	1.557.088	920.791
Receivables relating to RJ aircrafts modifications	560.516	-
Personnel salary advances	375.337	326.363
Due from personnel	278.853	247.834
Receivable from SITA deposit certificates	155.882	150.242
Business advances	95.989	345.966
Bank deposits at banks having transfer difficulties (*)	-	845.502
Other receivables	351.884	152.689
	<u>6.567.690</u>	<u>2.989.387</u>

(\*) As of 31 December 2004, the balance of this account is related to bank balance in Egypt.

## Türk Hava Yolları Anonim Ortaklığı

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)

### 10 OTHER RECEIVABLES AND LIABILITIES (NET) (cont'd)

ii) Other long-term receivables comprised the following:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Due from personnel	1.006.711	1.127.433
Receivable from SITA deposit certificates	804.107	702.736
Other receivables	90.670	90.955
	<u>1.901.488</u>	<u>1.921.124</u>

iii) Other short-term financial liabilities comprised the following:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Debt to banks (*)	332.636	281.244

(\*) Debt to banks consists of overnight interest-free borrowings obtained for settlement of monthly tax and social security premium payments.

iv) Other short-term liabilities comprised the following:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Flight liability resulting from ticket sales	154.979.724	124.731.094
Flight liability resulting from mileage sales	51.770.242	52.071.858
Frequent flyer program liability	30.577.262	6.993.168
Taxes and funds payable	16.204.908	19.340.449
Gross manufacturers' credits	19.690.997	16.956.092
Accumulated amortization on manufacturers' credits(-)	(16.199.785)	(14.564.872)
Social security premiums payable	14.840.062	12.188.329
Accruals for maintenance costs	12.585.613	15.944.575
Expense accruals for insurance premiums	10.468.387	10.074.286
Accruals for sales incentive premiums	6.684.627	7.734.390
Deferred income from USAŞ shares transfer	5.016.608	3.618.326
Debt to personnel	276.417	253.428
State Airport Administration ("DHMI") protocol payable	-	1.822.211
Discount on DHMI protocol payable	-	(36.401)
Other liabilities	1.373.121	790.475
Accruals for other expenses	4.347.361	4.006.984
	<u>312.615.544</u>	<u>261.924.392</u>

v) Other long-term liabilities comprised the following:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Deferred income from USAŞ shares transfer	-	3.618.326
	-	3.618.326

### 11 BIOLOGICAL ASSETS (NET)

None (2004: None).

### 12 INVENTORIES (NET)

	<u>31 December 2005</u>	<u>31 December 2004</u>
Spare parts, flight equipments	69.659.366	54.483.543
Other inventories	14.595.913	10.030.300
	<u>84.255.279</u>	<u>64.513.843</u>

### 13 RECEIVABLES FROM CONSTRUCTION CONTRACTS IN PROGRESS AND BILLINGS ON THE CONTRACTS (NET)

## Türk Hava Yolları Anonim Ortaklığı

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)

None (31 December 2004: None).

### 14 DEFERRED TAX ASSETS AND LIABILITIES

The Company recognizes deferred tax assets and liabilities based upon temporary differences arising from the differences between its financial statements compliant to Capital Markets Board's accounting standards and statutory tax standards. These differences generally result from the recognition of revenue and expenses in different reporting periods considering CMB and tax standards and calculated for the items such as fixed assets, retirement pay, allowance for doubtful receivables. The deferred tax rate is 30%.

Temporary differences: Deferred tax assets / (liabilities)

	<b>31 December 2005</b>	<b>31 December 2004</b>
Allowance for unrecoverable bank accounts	246	276
Provision for doubtful receivables	230.607	416.692
Restatements on inventory	520.391	8.716.457
Appreciation in value of financial assets	(666.579)	(1.483.820)
Other short term assets	-	60.960
Short term lease obligations	36.369.506	47.867.011
Deferred income and expenses	456.107	290.395
Expense accruals	17.283.762	13.125.543
Provision for advance ticket sales	(21.609.699)	(17.973.936)
Deferred income	1.504.979	1.851.799
Adjustments to long term assets	-	(620.529)
Fixed assets	(365.532.429)	(425.380.016)
Long term lease obligations	185.266.465	287.318.620
Retirement pay liability	34.092.373	29.933.213
Manufacturers' credit	1.392.681	717.366
Discount on receivables	772.994	102.072
Discount on payables	(811.742)	(19.996)
Unused investment incentives	20.048.657	3.704.211
Unused tax losses	630.034	4.888.940
Deferred tax liability	<u>(90.051.647)</u>	<u>(46.484.742)</u>

Movement in deferred tax liability is as follows:

	<b>31 December 2005</b>	<b>31 December 2004</b>
Net deferred tax charge related to temporary differences	43.566.905	2.818.011
Monetary gain on deferred tax liabilities	-	(6.043.575)
Net change in deferred tax	<u>43.566.905</u>	<u>(3.225.564)</u>

## Türk Hava Yolları Anonim Ortaklığı

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)

### 15 OTHER CURRENT/NON-CURRENT ASSETS AND SHORT-TERM/LONG-TERM LIABILITIES

i) Other current assets comprised the following:

	<b>31 December 2005</b>	<b>31 December 2004</b>
Prepaid taxes and funds	13.363.884	51.305.913
Prepaid sales commissions	11.149.101	10.414.391
Maintenance service income accruals	10.127.094	6.172.005
Deferred insurance expenses	6.787.420	6.154.237
Prepaid operating lease expenses	5.314.180	3.982.248
Interline passenger income accruals	3.843.430	182.580
Tax to be refunded	2.965.389	2.682.798
Prepaid Eximbank USA guarantee and exposure fee	1.092.408	1.092.408
Prepaid financial expense of bank borrowing	740.124	-
Prepaid rent expenses	574.125	440.142
Prepaid aircraft financing expense	487.846	539.501
VAT deductible	437.170	152.793
Other prepaid expenses	2.739.482	1.659.367
	<u>59.621.653</u>	<u>84.778.383</u>

ii) Other non-current assets comprised the following:

	<b>31 December 2005</b>	<b>31 December 2004</b>
Prepaid Eximbank USA guarantee and exposure fee	5.889.372	7.001.219
Advances given for operating leases	2.637.672	1.241.311
Prepaid aircraft financing expense	2.067.151	2.688.118
Deposits given	1.325.066	1.736.867
Prepaid operating lease expenses	374.744	-
	<u>12.294.005</u>	<u>12.667.515</u>

### 16 FINANCIAL ASSETS (NET)

i) The investment accounted for using the equity method is as follows:

	<b>31 December 2005</b>	<b>31 December 2004</b>
Güneş Ekspres Havacılık A.Ş. (Sun Express)	<u>17.490.282</u>	<u>16.706.000</u>

ii) Financial assets available for sale are as follows:

	<b>31 December 2005</b>	<b>31 December 2004</b>
France Telecom shares	20.214.336	20.214.336
Diminution in value of France Telecom shares	(13.458.870)	(11.192.456)
Uçak Servisi A.Ş. (USAŞ)	8.085.622	8.213.707
Appreciation in value of USAŞ shares	3.367.104	6.880.463
Sita Inc.	1.679.619	1.785.738
Emek İnşaat ve İşletme A.Ş.	26.859	26.859
Other financial assets	1.426	1.426
	<u>19.916.096</u>	<u>25.930.073</u>
	<u>37.406.378</u>	<u>42.636.073</u>

## Türk Hava Yolları Anonim Ortaklığı

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)

### 16 FINANCIAL ASSETS (NET) (cont'd)

Tender for the catering service was won by Uçak Servisi A.Ş. (USAŞ) and service agreement was signed on 1 January 2002. Based on share transfer agreement made between USAŞ's main shareholder Gate Gourmet Holding A.G. (GGH) and the Company, USAŞ will transfer its group B free shares corresponding to 15% of its total share capital to the Company. According to the agreement, ownership of first 10% of shares was transferred on 21 June 2002, 1,25% of shares was transferred on 2 January 2003 and 1,25% of shares was transferred on 2 January 2004, 1,25% of shares was transferred on 3 January 2005 and the transfer will be completed to 15% by transferring 1,25% of shares in the year 2006. Consequently, 1.140 million shares corresponding to 13,75% of USAŞ's share capital, transferred to the Company, were recorded to "financial assets" and "deferred income" accounts at market value of YTL 19.650.109. "Deferred income" amount is amortized to income during 5 years catering service agreement on a straight-line basis. The Company has sold 342 million USAŞ shares in 2003 and 1.026 million shares in 2005 at İstanbul Stock Exchange.

USAŞ gave 1.852.500.000 free shares to the Company based on the decision taken in Non-general Assembly held on 8 December 2004 related to the share capital increase originated from the inflation adjustment difference arising from capital restatement.

Details of the Company's financial assets at 31 December 2005 are as follows:

<u>Name of the Company</u>	<u>Place of Incorporation and Operation</u>	<u>Ownership Rate</u>	<u>Voting Power Rate</u>	<u>Principal Activity</u>
Güneş Ekspres Havacılık A.Ş. (Sun Express)	Turkey	50%	50%	Air transportation
Emek İnşaat ve İşletme A.Ş.	Turkey	0,3%	0,3%	Construction
Sita Inc.	Holland	Less than 0,1%	Less than 0,1%	Information & Telecommunication Services
Uçak Servisi A.Ş. (USAŞ)	Turkey	4,75%	4,75%	Catering
France Telecom	France	Less than 0,1%	Less than 0,1%	Telecommunication

### 17 POSITIVE/NEGATIVE GOODWILL (NET)

None (2004: None).

### 18 INVESTMENT PROPERTY (NET)

None (2004: None).

### 19 TANGIBLE FIXED ASSETS (NET)

	<u>31 December 2005</u>	<u>31 December 2004</u>
Tangible fixed assets (net)	2.051.105.815	1.810.476.604
Advances given for aircraft purchases	570.531.933	395.670.512
Advances given for other tangible fixed assets	9.476.231	-
	<u>2.631.113.979</u>	<u>2.206.147.116</u>

## Türk Hava Yolları Anonim Ortaklığı

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)

### 19 TANGIBLE FIXED ASSETS (NET) (cont'd)

	Land, Land Improvements & Buildings	Technical Equipments, Simulators and Vehicles	Other Equipments, Fixtures and Softwares	Aircraft and Spare Engines	Components and Repairable Spare Parts	Construction in Progress	Total Assets Owned	Leased Aircraft	Other Leased Fixed Assets & Simulator s	Total Leased Assets	Total
<b>Cost</b>											
Opening balance 1 January 2005	164.394.003	293.126.703	216.627.863	1.271.455.508	284.390.748	386.260	2.230.381.085	3.359.221.949	17.796.598	3.377.018.547	5.607.399.632
Transfers from finance leased aircraft	-	-	-	719.930.479	-	-	719.930.479	(719.930.479)	-	(719.930.479)	-
Additions	-	5.089.635	5.083.323	92.789.901	104.757.919	1.667.822	209.388.600	262.118.349	-	262.118.349	471.506.949
Disposals	-	(3.113.184)	(21.182.606)	(57.043.500)	(79.498.014)	(383.627)	(161.220.931)	-	-	-	(161.220.931)
Closing balance 31 December 2005	164.394.003	295.103.154	200.528.580	2.027.132.388	309.650.653	1.670.455	2.998.479.233	2.901.409.819	17.796.598	2.919.206.417	5.917.685.650
<b>Accumulated depreciation</b>											
Opening balance 1 January 2005	45.636.971	252.663.395	196.713.598	778.440.216	139.865.031	-	1.413.319.211	936.557.576	5.265.168	941.822.744	2.355.141.955
Transfers from finance leased aircraft	-	-	-	212.888.307	-	-	212.888.307	(212.888.307)	-	(212.888.307)	-
Depreciation for the period	2.736.555	13.116.453	7.455.455	60.038.540	86.525.225	-	169.872.228	124.189.315	1.381.514	125.570.829	295.443.057
Disposals	-	(3.096.621)	(19.602.881)	(443.671)	(79.498.014)	-	(102.641.187)	-	-	-	(102.641.187)
Closing balance 31 December 2005	48.373.526	262.683.227	184.566.172	1.050.923.392	146.892.242	-	1.693.438.559	847.858.584	6.646.682	854.505.266	2.547.943.825
Accumulated impairment	-	5.710.483	-	533.859.545	-	-	539.570.028	774.651.895	4.414.087	779.065.982	1.318.636.010
<b>31 December 2005 net book value</b>	<b>116.020.477</b>	<b>26.709.444</b>	<b>15.962.408</b>	<b>442.349.451</b>	<b>162.758.411</b>	<b>1.670.455</b>	<b>765.470.646</b>	<b>1.278.899.340</b>	<b>6.735.829</b>	<b>1.285.635.169</b>	<b>2.051.105.815</b>
<b>31 December 2004 net book value</b>	<b>118.757.032</b>	<b>32.529.232</b>	<b>19.914.266</b>	<b>202.929.868</b>	<b>144.525.717</b>	<b>386.260</b>	<b>519.042.375</b>	<b>1.283.505.372</b>	<b>7.928.857</b>	<b>1.291.434.229</b>	<b>1.810.476.604</b>

## Türk Hava Yolları Anonim Ortaklığı

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)

### 20 INTANGIBLE FIXED ASSETS (NET)

	<u>Rights</u>	<u>Leasehold Improvements</u>	<u>Total</u>
<b><u>Cost</u></b>			
Opening balance 1 January 2005	60.098.447	18.829.214	78.927.661
Additions	1.533.298	461.899	1.995.197
Disposals	-	(58.052)	(58.052)
Closing balance 31 December 2005	<u>61.631.745</u>	<u>19.233.061</u>	<u>80.864.806</u>
<b><u>Accumulated depreciation</u></b>			
Opening balance 1 January 2005	53.301.396	18.162.686	71.464.082
Amortization charge for the period	2.793.911	504.228	3.298.139
Disposals	-	(51.548)	(51.548)
Closing balance 31 December 2005	<u>56.095.307</u>	<u>18.615.366</u>	<u>74.710.673</u>
Accumulated impairment	-	-	-
<b>31 December 2005 net book value</b>	<u>5.536.438</u>	<u>617.695</u>	<u>6.154.133</u>
<b>31 December 2004 net book value</b>	<u>6.797.051</u>	<u>666.528</u>	<u>7.463.579</u>

### 21 ADVANCES RECEIVED

i) Short-term advances received comprised the following:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Advances received for mileage credit sales	21.649.478	23.101.559
MCO advances	15.962.740	8.360.092
E-pos ticket advances	9.675.611	348.806
Special rent advances	3.413.900	2.394.541
Advances received for financial leases	1.151.059	-
Other advances received	544.626	247.685
	<u>52.397.414</u>	<u>34.452.683</u>

ii) Long-term advances received: None (2004: None).

### 22 RETIREMENT PLANS

Except for retirement pay liability which is explained under Provisions for Liabilities, there is not any agreement of retirement commitment

### 23 PROVISIONS FOR LIABILITIES

i) Provisions for short-term liabilities comprised the following:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Accrued salaries	17.993.508	15.619.949
Provisions for legal claims	9.202.870	9.245.739
Other provisions	347.266	357.289
	<u>27.543.644</u>	<u>25.222.977</u>

ii) Provisions for long-term liabilities comprised the following:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Provision for Retirement Pay Liability	113.641.242	99.777.377



## Türk Hava Yolları Anonim Ortaklığı

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)

### 23 PROVISIONS FOR LIABILITIES (cont'd)

Provision for Retirement Pay Liability is recognized as explained below:

Under Turkish Labor Law, employees are entitled to receive a lump sum payment when their employment is terminated without due cause or when they retire, completing 25 years of service (20 years for women), or are called up for military service. The amount payable consists of one month's gross salary per year of service. The gross salary is the salary at the date of termination, but subject to a limit of YTL 1.727 as at 31 December 2005 (2004: YTL 1.575). The number of service years required before retirement is rising according to a sliding scale based on new legislation enacted in 1999. The system described here can be named as an unfunded defined benefit system. The total provision recognised in the financial statements represents the estimated present value of the vested benefit obligation.

Amounts recognized in the income statement as provision for retirement pay liability are as follows:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Current service cost	15.156.287	11.702.155
Interest cost	5.594.993	4.883.377
	<u>20.751.280</u>	<u>16.585.532</u>

Movements in the provision for retirement pay liability in the balance sheet are as follows:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Provision at 1 January	99.777.377	89.528.586
Charge for the period	20.751.280	16.585.532
Payments during the period	(6.887.415)	(6.336.741)
Provision at 31 December	<u>113.641.242</u>	<u>99.777.377</u>

The estimated value of the vested benefit obligation is discounted with an approximate rate of 5,61% (2004: 5,45 %) per annum considering the effect of increase in eligible pay and its limit.

### 24 MINORITY INTERESTS

None (2004: None).

### 25 SHARE CAPITAL/RECIPROCAL ASSOCIATE CAPITAL ADJUSTMENT

The ownership of the Company's share capital is as follows:

	<u>Group</u>	<u>%</u>	<u>31 December 2005</u>	<u>%</u>	<u>31 December 2004</u>
Republic of Turkey Prime Ministry Privatization Administration(*)	A, C	75,18(**)	131.565.696	75,17	131.538.948
Others	A	24,82(**)	43.434.304	24,83	43.461.052
Share capital (historic)			175.000.000		175.000.000
Restatement effect			1.739.005.871		1.739.005.871
Restated Share Capital			<u>1.914.005.871</u>		<u>1.914.005.871</u>

## **Türk Hava Yolları Anonim Ortaklığı**

Notes to the financial statements as at 31 December 2005

*(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)*

### **25 SHARE CAPITAL/RECIPROCAL ASSOCIATE CAPITAL ADJUSTMENT (cont'd)**

(\*) 1.644 shares belonging to various private shareholders were not taken into consideration when the Company was included to the privatization program in 1984. Subsequently, these shares were registered on behalf of Privatization Administration according to Articles of Association of the Company, approved by the decision of the Turkish Republic High Planning Board on 30 October 1990.

(\*\*) YTL 26.748 nominal valued shares of the Company subject to the second public offering during 1, 2 and 3 December 2004 were transferred to the accounts of Republic of Turkey Prime Ministry Privatization Administration by İş Yatırım Menkul Değerler A.Ş. The transfer was made due to default of private shareholders who did not transfer the amounts of the shares following the conclusion of last installment.

As at 31 December 2005, the Company's issued and paid-in share capital consists of 174.999.999.999 Class A shares and 1 Class C share, all with a par value of YKr 0.1 each. These shares are issued to the name. The Class C share belongs to the Republic of Turkey Prime Ministry Privatization Administration and has the following privileges:

Articles of Association 7: Positive vote of the Board member representing class C share and approval of the Board of Directors are necessary for transfer of shares issued to the name.

Articles of Association 10: The Board of Directors consists of seven members of which one member has to be nominated by the class C shareholder.

Articles of Association 14: The following decisions of the Board of Directors are subject to the positive vote of the class C Shareholder:

- a) As defined in Article 3.1 of the Articles of Association, taking decisions that will negatively affect the Company's mission
- b) Suggesting change in the Articles of Association at General Assembly
- c) Increasing share capital
- d) Approval of transfer of the shares issued to the name and their registration to the "Share Registry"
- e) Making decisions or taking actions which will put the Company under commitment over 5% of its total assets considering the latest annual financial statements prepared for Capital Market Board per agreement (this statement will expire when the Company's shares held by Turkish State is below 20%)
- f) Making decisions relating to merges and liquidation
- g) Making decisions to cancel flight routes or significantly decrease number of flights except for the ones that cannot recover even its operational expenses subject to the market conditions

Articles of Association Temporary Article 1: Head of the Board of Directors, members of the Board of Directors, auditors and general manager meeting the conditions defined in law numbered 4046, are to be selected from candidates suggested by A group shareholders, by the offer of Republic of Turkey Prime Ministry Privatization Administration and the approval of the Prime Minister or authorized minister, as long as the Company's shares held by Turkish State are not below 50%. The article 315 of Turkish Commercial Code is applicable for the members representing non-public membership.

## Türk Hava Yolları Anonim Ortaklığı

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)

### 26-27-28 CAPITAL RESERVES, PROFIT RESERVES AND ACCUMULATED LOSSES

The Shareholder's Equity items, based on the Communiqué No: 25 of Series XI, "Communiqué on Capital Market Accounting Standards" issued by Capital Market Board on 15 November 2003, are stated below with their nominal amounts and the differences arising from inflation adjustments are recognized in "Shareholders' Equity Inflation Adjustment Differences" account.

	<u>31 December 2005</u>	<u>31 December 2004</u>
Share Capital	175.000.000	175.000.000
Share Premium	181.185	181.185
Legal Reserves	417.011	417.011
Extraordinary Reserves	7.806.889	7.806.889
Special funds	9	9
Shareholders' Equity Inflation Adjustment Differences (*)	1.872.657.189	1.872.657.189
Net Profit for the Year	138.227.837	107.058.441
Accumulated Losses	(945.948.527)	(1.053.006.968)
	<u>1.248.341.593</u>	<u>1.110.113.756</u>
<b>(*) Shareholders' Equity Inflation Adjustment Differences</b>		
Share Capital	1.739.005.871	1.739.005.871
Share Premium	714.307	714.307
Legal Reserves	60.597.395	60.597.395
Extraordinary Reserves	67.026.275	67.026.275
Special funds	5.313.341	5.313.341
	<u>1.872.657.189</u>	<u>1.872.657.189</u>

Accumulated profits in statutory books can be distributed except for the following legal provision related to legal reserves. According to Turkish Commercial Code, legal reserves can be categorized as order I legal reserves and order II legal reserves. Order I legal reserves are apportioned as 5% of statutory net profit to the extent that they reach to 20% of the company's paid-in capital. Order II legal reserves equal to 10% of distributable profit exceeding 5% of paid-in capital. According to Turkish Commercial Code, legal reserves can only be used to set off losses as long as they do not exceed 50% of paid-in capital. Publicly held companies distribute dividends in the following way that Capital Market Board requires.

In accordance with Communiqué No: 25 of Series XI part 15th clause number 399, losses arising from the first time application of inflation accounting and recorded in "accumulated losses" account shall be considered as a deduction in determining the distributable profit with respect to CMB regulations. However, these losses can be reduced by the profit for the year and accumulated profits, and the remaining losses can then be reduced by in an order of extraordinary reserves, legal reserves and shareholders' equity inflation adjustment differences.

## Türk Hava Yolları Anonim Ortaklığı

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)

### 29 FOREIGN CURRENCY POSITION

Foreign currency risk arises from the change of the value of financial instruments due to change in exchange rates. The Company has a foreign currency risk because of the foreign currency denominated debts. As of 31 December 2005, the Company does not have derivative financial instruments to hedge its foreign currency risks. US Dollar, Euro and Sterling are the main currencies that make the foreign currency position of the Company.

The foreign currency position of the Company as of 31 December 2005 and 31 December 2004 in terms of YTL is as follows:

<b>31 December 2005</b>	<b>US Dollar</b>	<b>Euro</b>	<b>Sterling</b>	<b>Other</b>	<b>Total</b>
<b><i>Foreign currency denominated assets</i></b>					
Cash and cash equivalents	209.110.558	63.411.560	1.701.717	27.041.304	301.265.139
Accounts receivable (net)	24.881.620	45.615.416	5.907.491	40.429.558	116.834.085
Due from related parties (net)	469.066	446.745	-	-	915.811
Other receivables (short term) (net)	4.230.783	522.195	75.320	91.366	4.919.664
Inventory-advances	1.117.566	53.958	71.109	18.599	1.261.232
Other current assets	28.138.494	2.946.996	298.931	9.047.045	40.431.466
Other receivables (long term) (net)	1.810.818	-	-	-	1.810.818
Tangibles fixed assets (advances for aircraft)	579.865.473	-	142.691	-	580.008.164
Other non-current assets	11.312.071	463.364	71.791	414.991	12.262.217
	<b>860.936.449</b>	<b>113.460.234</b>	<b>8.269.050</b>	<b>77.042.863</b>	<b>1.059.708.596</b>
<b><i>Foreign currency denominated liabilities</i></b>					
Bank borrowings (net)	362.903.225	-	-	-	362.903.225
Financial lease obligations (short term)	179.092.821	-	-	-	179.092.821
Accounts payable (short term) (net)	68.596.451	56.577.386	3.195.299	28.019.720	156.388.856
Due to related parties (net)	8.022.859	-	-	-	8.022.859
Deposits and advances received	23.008.165	148.138	412	-	23.156.715
Other accrued liabilities (short term)	347.266	-	-	-	347.266
Other liabilities (net)	92.278.977	83.458.279	13.058.372	45.196.135	233.991.763
Financial lease obligations(long term)(net)	856.730.859	-	-	-	856.730.859
Accounts payable (long-term) (net)	428.254	5.270.953	103.467	1.321.592	7.124.266
	<b>1.591.408.877</b>	<b>145.454.756</b>	<b>16.357.550</b>	<b>74.537.447</b>	<b>1.827.758.630</b>
<b><i>Net foreign currency position (*)</i></b>	<b>(730.472.428)</b>	<b>(31.994.522)</b>	<b>(8.088.500)</b>	<b>2.505.416</b>	<b>(768.050.034)</b>

(\*) Whereas, the Company seems to be in an open position based on its monetary assets and liabilities, as explained in Note 3.5, the Company values its aircraft and spare engines according to their US Dollar acquisition costs or US Dollar selling prices. In this respect, the Company's management is of the opinion that the Company's those tangible assets which are carried by their US Dollar values should also be considered in the overall evaluation of the sensitivity of the Company's assets and liabilities against the changes in foreign exchange rates.

## Türk Hava Yolları Anonim Ortaklığı

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)

### 29 FOREIGN CURRENCY POSITION (cont'd)

As of 31 December 2005, the net book value of aircraft and spare engines, which are carried by their US Dollar acquisition costs or US Dollar selling prices is YTL 1.735.882.362 (2004: YTL 1.504.373.218).

31 December 2004	US Dollar	Euro	Sterling	Other	Total
<b>Foreign currency denominated assets</b>					
Cash and cash equivalents	40.353.808	178.302.052	2.317.807	28.309.351	249.283.018
Accounts receivable (net)	35.521.212	32.904.743	5.421.928	38.641.943	112.489.826
Due from related parties (net)	477.642	311.411	-	-	789.053
Other receivables (short term) (net)	739.008	288.734	49.340	909.014	1.986.096
Inventory-Advances	277.197	41.698	47.031	64.103	430.029
Other current assets	27.689.397	2.206.977	461.616	1.917.674	32.275.664
Other receivables (long-term) (net)	1.919.808	-	-	-	1.919.808
Tangible fixed assets (advances for aircraft)	395.670.512	-	-	-	395.670.512
Other non-current assets	1.241.311	-	-	-	1.241.311
	<u>503.889.895</u>	<u>214.055.615</u>	<u>8.297.722</u>	<u>69.842.085</u>	<u>796.085.317</u>
<b>Foreign currency denominated liabilities</b>					
Financial lease obligations (short term)	202.712.254	-	-	-	202.712.254
Accounts payable (short-term) (net)	54.284.440	47.389.637	4.071.525	20.360.591	126.106.193
Due to related parties	215.959	1.268	-	-	217.227
Deposits and advances received	347.345	-	-	-	347.345
Other liabilities (net)	88.429.414	69.226.821	14.621.078	45.579.476	217.856.789
Financial lease obligations (long term)	957.728.732	-	-	-	957.728.732
	<u>1.303.718.144</u>	<u>116.617.726</u>	<u>18.692.603</u>	<u>65.940.067</u>	<u>1.504.968.540</u>
<b>Net foreign currency position(*)</b>	<u>(799.828.249)</u>	<u>97.437.889</u>	<u>(10.394.881)</u>	<u>3.902.018</u>	<u>(708.883.223)</u>

### 30 GOVERNMENT GRANTS

The Company has investment incentive certificates; dated 23 May 2003 covering the period of 22.04.2003 – 22.04.2006 at amount of YTL 2.416.819.000 and dated 9 March 2005 covering the period of 24.01.2005 – 24.01.2007 at amount of YTL 136.969.308. The investment incentive certificates provide benefits for the exemption of Value Added Tax regarding domestic and international purchases of goods and exemption of customs duty for investment goods imported from countries other than European Union members.

In addition, of investment spending by 31 December 2005, YTL 39.886.126 is subject to 100% investment allowance and YTL 26.942.730 is subject to 40% investment allowance.

Investment allowances are deducted from current or future taxable income .

## **Türk Hava Yolları Anonim Ortaklığı**

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)

### **31 PROVISIONS, CONTINGENT ASSETS AND CONTINGENT LIABILITIES**

#### a) Guarantees Given:

Amount of letter of guarantees given is YTL 38.040.225 as of 31 December 2005 (2004: YTL 34.044.958).

#### b) Purchase Commitments:

The Company has signed agreements for delivery of 59 aircraft with delivery dates between years 2005-2008. Total value of these aircraft is approximately US Dollar 4.7 billion according to the list prices before any discounts applicable by aircraft manufacturers. The Company paid a deposit of US Dollar 421 million as of 31 December 2005 related to these aircraft.

#### c) Letters of comfort:

	<b>31 December 2005</b>	<b>31 December 2004</b>
Letters of comfort given to Sun Express	US Dollar 2.900.000	US Dollar 2.900.000
	Euro 2.556.459	Euro 2.556.459

d) The Company's discounted retirement pay provision is YTL 113.641.242. The Company's undiscounted liability for retirement pay would be approximately YTL 184 million as of 31 December 2005, if all employees were dismissed on that date.

### **32 BUSINESS COMBINATIONS**

None (2004: None).

### **33 SEGMENTAL REPORTING**

#### Business Segments

The Company predominantly operates in one industry segment, its primary business is being the air transportation of passengers and cargo within, to or from Turkey.

#### Geographical Segments

The revenue analysis is based on the destinations that the Company serves. All passenger fare and cargo revenue within Turkey is attributed to the revenue from domestic services. Revenue from both scheduled and non-scheduled international flight are attributed to destinations' geographical areas.

## **Türk Hava Yolları Anonim Ortaklığı**

Notes to the financial statements as at 31 December 2005

*(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)*

### **34 EVENTS SUBSEQUENT TO THE BALANCE SHEET DATE**

a) Market price of 202.735 France Telecom securities, which is quoted at Paris Stock Exchange, included in the financial investments available for sale as of 31 December 2005, has decreased from Euro 20,99 at 31 December 2005 to Euro 18,68 at 29 March 2006. Hence, the total market value of these securities decreased by YTL 743.455 compared to balance sheet date.

b) Market price of 1.624,5 million USAŞ securities, which is traded in İstanbul Stock Exchange, and included in the financial investments available for sale as of 29 March 2006, has decreased from YTL 7,05 at 31 December 2005 to YTL 6,85 at 29 March 2006. Hence, the total market value of these securities decreased by YTL 324.900 compared to balance sheet date.

c) The Company has sold 1.026 million of USAŞ shares in January 2006 at İstanbul Stock Exchange. After the transaction, the percentage of the shares owned by the company within the capital of USAŞ is 3 %.

d) According to the decision dated 20.03.2006 and numbered 2006/19 of Privatization High Commission, 25% of A group shares of the Company owned by Turkish Republic Prime Ministry Privatization Administration have been decided to be sold through public offering. It has been also decided to use the right for the selling of additional shares and to complete public offering within the twelve months beginning from the decision date.

e) Retirement pay ceiling has been increased to YTL 1.770,62 as of 1 January 2006.

f) The company has cancelled financial the lease contracts of two A340 aircrafts of which lease contracts would be due by 22 July 2006 and 19 June 2007, by paying the remaining lease payments before the maturity date thus having the ownership of these two aircraft.

### **35 DISCONTINUED OPERATIONS**

None (2004: None).

## Türk Hava Yolları Anonim Ortaklığı

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)

### 36 MAIN OPERATING REVENUES

Main operating revenues comprised the following:

	<b>31 December 2005</b>	<b>31 December 2004</b>
Scheduled flights		
- Passenger	2.686.817.564	2.329.331.104
- Cargo and mail	266.536.598	263.366.035
Non-scheduled flights	30.986.034	46.078.926
Other revenues	122.747.906	154.615.997
<b>Total revenues</b>	<b>3.107.088.102</b>	<b>2.793.392.062</b>
Less: Discounts and sales returns	(16.494)	(6.116)
<b>Net Sales</b>	<b>3.107.071.608</b>	<b>2.793.385.946</b>
Cost of Sales (-)	(2.435.869.117)	(2.084.379.054)
<b>Gross Operating Profit</b>	<b>671.202.491</b>	<b>709.006.892</b>

Geographical details of revenue from the scheduled flights is as follows:

	<b>31 December 2005</b>	<b>31 December 2004</b>
- Europe	1.267.513.611	1.090.666.171
- Middle East	281.514.326	249.712.506
- North Africa	77.769.603	68.970.569
- North America	154.198.652	153.764.088
- Far East	486.167.200	438.635.084
	<u>2.267.163.392</u>	<u>2.001.748.418</u>
Domestic	686.190.770	590.948.721
Total revenue from the scheduled flights	<u>2.953.354.162</u>	<u>2.592.697.139</u>

Cost of Sales consists of the following:

	<b>31 December 2005</b>	<b>31 December 2004</b>
Fuel expenses	729.386.690	517.297.738
Staff expenses	523.619.808	416.433.682
Depreciation expenses	285.638.122	287.273.732
Landing and overflight expenses	245.249.413	240.215.847
Handling expenses	157.321.224	162.863.442
Passenger service and catering expenses	146.643.592	129.469.337
Maintenance expenses	141.000.727	140.439.645
Operating lease expenses	100.924.585	58.840.591
Insurance expenses	51.058.405	65.956.974
Other renting expenses	15.026.757	13.375.133
Aircraft wet-lease expenses	10.223.259	25.922.694
Communication expenses	7.972.597	8.798.621
Service expenses	6.921.026	5.654.263
Other taxes	5.096.775	2.673.125
Lighting, heating, energy and water expenses	3.790.684	4.239.882
Transportation expenses	2.689.662	1.486.718
Cost of other sales	3.305.791	3.437.630
	<u>2.435.869.117</u>	<u>2.084.379.054</u>



**Türk Hava Yolları Anonim Ortaklığı**

Notes to the financial statements as at 31 December 2005

*(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)***37 OPERATING EXPENSES (-)**

Operating expenses comprised the following:

	<b>31 December 2005</b>	<b>31 December 2004</b>
<b>Sales and marketing expenses (-)</b>		
Commission and promotion expenses	212.444.272	207.547.785
Staff expenses	125.487.955	112.546.475
Reservation system expenses	55.300.819	49.226.480
Communication expenses	13.372.145	14.191.223
Other renting expenses	13.226.105	13.126.284
Service expenses	8.197.697	5.611.697
Advertisement expenses	7.654.857	4.523.055
Transportation expenses	5.039.813	3.869.315
Passenger service and catering expenses	4.404.684	3.852.944
Other taxes	4.128.938	2.695.220
Code share expenses	2.059.097	1.870.056
Lighting, heating, energy and water expenses	1.492.957	1.470.491
Maintenance expenses	1.052.548	1.591.666
Software and computer equipment expenses	634.039	676.774
Fuel expenses	525.559	391.662
Insurance expenses	287.514	500.027
Other sales and marketing expenses	13.201.723	12.966.241
	<u>468.510.722</u>	<u>436.657.395</u>
	<b>31 December 2005</b>	<b>31 December 2004</b>
<b>General administrative expenses (-)</b>		
Staff expenses	70.304.250	89.573.691
Depreciation expenses	13.103.074	13.178.104
Other taxes	3.726.375	3.539.217
Maintenance expenses	3.879.646	4.129.903
Software and computer equipment expenses	3.492.256	3.967.982
Communication expenses	2.424.355	2.400.550
Commission and promotion expenses	2.239.262	1.836.426
Service expenses	2.026.024	2.363.496
Lighting, heating, energy and water expenses	1.641.541	790.898
Other renting expenses	1.242.136	848.276
Insurance expenses	384.735	1.213.916
Fuel expenses	221.145	5.805
Other general administrative expenses	4.434.961	5.952.787
	<u>109.119.760</u>	<u>129.801.051</u>
Total operating expenses	<u>577.630.482</u>	<u>566.458.446</u>

## Türk Hava Yolları Anonim Ortaklığı

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)

### 38 INCOME/LOSSES FROM OTHER OPERATIONS

Income from other operations consists of the following:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Foreign exchange gains	209.523.006	250.059.990
Change in provision for diminution in value of fixed assets	123.145.0 65	22.249.212
Interest income	42.289.467	42.256.159
Reversal of unnecessary provision	11.009.988	20.764.780
Discounts received from spare parts suppliers	10.442.021	8.556.212
Dividend income	8.351.334	4.531.062
Cost free materials income	5.019.663	1.511.262
Profit on sale of marketable securities	3.611.850	-
Compensation received	3.473.513	5.642.184
Income from manufacturers' credit	1.774.511	1.695.609
Gain on sale of fixed assets	798.359	605.066
Income from financial investment accounted per equity method	784.282	8.615.374
Discount income	596.515	-
Other income	4.610.759	4.895.905
	<u>425.430.333</u>	<u>371.382.815</u>

Loss from other operations consists of the followings:

Foreign exchange losses	238.201.803	222.638.553
Provision expenses	30.491.374	8.156.108
Interest expenses-third parties	-	4.324.789
Retirement pay interest cost	5.594.993	4.883.377
Rent expense of RJ aircraft to be returned	-	4.507.796
Discount expense	-	783.128
Expenses incurred for passengers with no visas	796.374	1.699.204
Other expenses	2.081.044	1.504.388
	<u>277.165.588</u>	<u>248.497.343</u>

### 39 FINANCIAL EXPENSES

Financial expenses consist of the following:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Finance Lease interest expenses	45.658.088	42.347.448
Interest expenses for bank borrowings	12.163.552	-
Other financial expenses	2.220.372	-
	<u>60.042.012</u>	<u>42.347.448</u>

### 40 NET MONETARY GAIN/LOSS

By the decision issued on 17 March 2005, Capital Markets Board announced that it is not required to apply inflation accounting effective from 1 January 2005 for the companies operating in Turkey and reporting in accordance with the accounting standards of CMB. Due to this announcement, The Company has ended the application of inflation accounting after 1 January 2005. Consequently, for the period ended on 31 December 2005, there is no monetary gain / loss (2004: YTL 113.210.018).

## Türk Hava Yolları Anonim Ortaklığı

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)

### 41 TAX

Corporation tax payable is as follows:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Provision for corporate tax payable	-	-
Prepaid taxes and funds	(13.363.884)	(51.305.913)
	<u>(13.363.884)</u>	<u>(51.305.913)</u>

Tax expense is as follows:

	<u>31 December 2005</u>	<u>31 December 2004</u>
Current period tax expense	-	-
Deferred tax expense	43.566.905	2.818.011
Tax expense	<u>43.566.905</u>	<u>2.818.011</u>

#### *Corporate tax:*

The Company is subject to Turkish corporate taxes. There is provision for the estimated tax liabilities based on the Company's financial results for the period.

Corporate tax is applied on taxable corporate income, which is calculated from the statutory accounting profit by adding back non-deductible expenses, and deducting dividends received from resident companies, other exempt income and investment incentives utilized.

The effective tax rates are as follows:

- In 2004: 33% (the corporate tax rate was increased from 30% to 33% by Law No. 5035 published in the Official Gazette on 2 January 2004)
- In 2005: 30 %

In Turkey, prepaid corporate taxes are calculated and accrued on a quarterly basis. The prepaid corporate tax rate was 33% in 2004. In 2005, the prepaid corporate tax rate is 30% .

Tax losses can be carried forward for offsetting against future taxable income for up to 5 years. However, losses cannot be carried back for offsetting against profits from previous periods.

In Turkey, there is no procedure for a final and definitive agreement on tax assessments. Companies file their tax returns until 15 April following the close of the accounting period to which they relate. The tax authorities may, however, examine such returns and the underlying accounting records and may revise assessments within five years.

#### *Income withholding tax:*

In addition to corporate taxes, companies should also calculate income withholding taxes and funds surcharge on any dividends distributed, except for companies receiving dividends who are resident companies in Turkey and Turkish branches of foreign companies. The rate of income withholding tax is 10% starting from 24 April 2003. Undistributed dividends incorporated in share capital are not subject to income withholding taxes.

## Türk Hava Yolları Anonim Ortaklığı

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)

### 41 TAX (cont'd)

#### *Income withholding tax:(cont'd)*

Income withholding tax which was calculated in 2002 and prior years on various types of income and gains exempt from corporation tax, whether distributed or not, has been removed in general. However, 19.8% withholding tax is still applicable to investment allowances relating to investment incentive certificates obtained prior to 24 April 2003. Such allowances may be used to relieve corporation tax liability until the profits reach the calculated level of exemption. If companies fail to make a profit or incur losses, any allowance outstanding may be carried forward to following years so as to be deducted from taxable income of subsequent profitable years. Carried forward investment incentives to be deducted from corporate tax liability in the following periods are revalued with the applicable WPI.

### 42 EARNINGS PER SHARE

There is no dilutive equity instruments outstanding which would require the calculation of separate diluted earnings per share.

A summary of the weighted average number of shares outstanding and the basic earnings per share calculation are as follows:

	<b>31 December 2005</b>	<b>31 December 2004</b>
Number of shares outstanding on 1 January (in full)	175.000.000.000	175.000.000.000
New shares issued (cash increase) (in full)	-	-
Number of shares outstanding on 31 December (in full)	175.000.000.000	175.000.000.000
Weighted average number of shares outstanding during the period (in full)	175.000.000.000	175.000.000.000
Net profit for the period	138.227.837	107.058.441
Basic earnings per share (YKr)	<b>0,079</b>	<b>0,061</b>

## Türk Hava Yolları Anonim Ortaklığı

Notes to the financial statements as at 31 December 2005

(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)

### 43 STATEMENTS OF CASH FLOWS

	<b>Audited</b> <b>31 December 2005</b>	<b>Audited</b> <b>31 December 2004</b>
<b>Cash flows from operating activities</b>		
Profit before taxation	181.794.742	109.876.452
<b>Adjustments to reconcile profit for the period to net cash provided by operating activities:</b>		
Depreciation	298.741.196	300.451.836
Provision for retirement pay liability	20.751.280	16.585.532
Interest income	(42.289.467)	(42.256.159)
Gain on sales of fixed asset	(798.359)	(605.066)
Monetary gain on deferred taxes liabilities	-	(6.043.575)
Change in provision for diminution in value of fixed assets	(123.145.065)	(22.249.212)
Income from financial investment accounted per equity method	(784.282)	(8.615.374)
Interest expense	57.821.640	46.672.237
Movement in manufacturers' credit	1.099.992	(2.447.513)
Foreign exchange gain on financial leases	2.229.427	30.920.326
Provision for diminution in value of financial assets	5.924.343	(8.506.026)
Amortization of deferred income from USAŞ shares transfer	(2.220.044)	(2.119.206)
Increase/(Decrease) in provision for doubtful receivables	(148.838)	(5.269.940)
<b>Operating profit before working capital change</b>	<b>398.976.565</b>	<b>406.394.312</b>
Increase in accounts receivable	(32.862.918)	(18.823.805)
(Increase)/ decrease in due from related parties (short term)	(157.780)	58.920.756
(Increase)/ decrease in other short and long term receivables	(3.558.667)	18.538.432
Increase in inventories	(19.741.436)	(12.354.531)
Decrease in other current assets	38.520.614	5.537.837
Decrease in other non-current assets	373.510	4.247.502
Increase in other financial liabilities	51.392	281.244
Increase/(decrease) in accounts payable	63.791.413	(6.882.897)
Increase in due to related parties	1.514.638	394.481
Increase/(decrease) in advances received	17.944.731	(24.701.237)
Increase/(decrease) in provision for short term liabilities	2.320.667	(4.971.658)
Increase in other short and long term liabilities	48.192.878	26.472.313
Retirement benefits paid	(6.887.415)	(6.336.741)
Interest paid	(59.179.468)	(48.679.413)
Income taxes paid	(13.363.884)	(73.234.322)
<b>Cash generated from operations</b>	<b>435.934.840</b>	<b>324.802.273</b>
<b>Cash flows from investing activities</b>		
Cash outflow from purchase of financial assets	-	(8.207)
Cash inflow from sale of financial assets	89.634	-
Cash inflow from sale of tangible and intangible fixed assets	59.000.980	6.952.148
Interest received	42.289.467	42.256.159
Acquisition of tangible and intangible fixed assets	(473.118.517)	(118.563.959)
Advances given for aircrafts and other tangible assets	(184.337.652)	(388.118.049)
<b>Net cash used in investing activities</b>	<b>(556.076.088)</b>	<b>(457.481.908)</b>
<b>Cash flows from financing activities</b>		
Principal payment of financial leases	(387.625.942)	(252.814.146)
Change in financial lease obligations	262.137.037	-
Change in bank borrowings	362.903.225	-
<b>Net cash provided by/(used in) financing activities</b>	<b>237.414.320</b>	<b>(252.814.146)</b>
<b>Net increase/(decrease) in cash and cash equivalents</b>	<b>117.273.072</b>	<b>(385.493.781)</b>
<b>Cash and cash equivalents at the beginning of period</b>	<b>365.637.483</b>	<b>751.131.264</b>
<b>Cash and cash equivalents at the end of period</b>	<b>482.910.555</b>	<b>365.637.483</b>

## **Türk Hava Yolları Anonim Ortaklığı**

Notes to the financial statements as at 31 December 2005

*(All amounts expressed in New Turkish Lira (YTL) unless otherwise stated.)*

### **44 OTHER ISSUES AFFECTING FINANCIAL STATEMENTS MATERIALLY OR NECESSARY TO MAKE FINANCIAL STATEMENTS SOUND, INTERPRETABLE AND UNDERSTANDABLE**

None (2004: None).