

TELECOMMUNICATIONS CO OF CHILE  
Form 6-K  
June 05, 2006

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**SECURITIES AND EXCHANGE COMMISSION**  
**Washington, D.C. 20549**

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**FORM 6-K**

**REPORT OF FOREIGN ISSUER**  
**PURSUANT TO RULE 13a-16 OR 15d-16 OF THE**  
**SECURITIES EXCHANGE ACT OF 1934**

**THROUGH JUNE 05, 2006**

**(Commission File Number: 001-10579)**

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**COMPAÑÍA DE TELECOMUNICACIONES DE CHILE S.A.**  
*(Exact name of Registrant as specified in its Charter)*

**TELECOMMUNICATIONS COMPANY OF CHILE**  
*(Translation of Registrant's name into English)*

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**Avenida Providencia No. 111, Piso 22**  
**Providencia, Santiago, Chile**  
*(Address of principal executive offices)*

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Indicate by check mark whether the registrant files or will file  
annual reports under cover Form 20-F or Form 40-F.

Form 20-F  Form 40-F

Indicate by check mark if the registrant is submitting the Form 6-K  
in paper as permitted by Regulation S-T Rule 101(b)(1): Yes  No

Indicate by check mark if the registrant is submitting the Form 6-K  
in paper as permitted by Regulation S-T Rule 101(b)(7): Yes  No

Indicate by check mark whether by furnishing the information contained in this Form,  
the registrant is also thereby furnishing the information to the Commission pursuant to  
Rule 12g3-2(b) under the Securities Exchange Act of 1934.

Yes  No

If "Yes" is marked, indicated below the file number assigned to the  
registrant in connection with Rule 12g3-2(b):  N/A

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***COMPAÑIA DE TELECOMUNICACIONES DE CHILE S.A. AND SUBSIDIARIES***

***REPORT ON THE CONSOLIDATED FINANCIAL STATEMENTS***

for the three-month periods ended

March 31, 2006 and 2005

*(CONSOLIDATED)*

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**COMPAÑIA DE TELECOMUNICACIONES DE CHILE S.A. AND SUBSIDIARIES**

(Translation of financial statements originally issued in Spanish See Note 2)

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ThCh\$: Thousands of Chilean pesos.

UF : The Unidad de Fomento, or UF, is an inflation-indexed peso-denominated monetary unit in Chile. The daily UF rate is fixed in advance based on the change in the Chilean Consumer Price Index of the previous month.

ThUS\$: Thousands of US dollars.

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## COMPAÑIA DE TELECOMUNICACIONES DE CHILE S.A. AND SUBSIDIARIES

**CONSOLIDATED BALANCE SHEETS**  
**MARCH 31, 2006 AND 2005**

(Restated for general price-level changes and expressed in thousands of constant Chilean pesos as of March 31, 2006)

| A S S E T S                 | Notes | 2006               | 2005               | L I A B I L I T I E S  | Notes  | 2006               | 2005               |
|-----------------------------|-------|--------------------|--------------------|--|--------|--------------------|--------------------|
|                             |       | ThCh\$             | ThCh\$             |  |        | ThCh\$             | ThCh\$             |
| <b>CURRENT ASSETS</b>       |       |                    |                    | <b>CURRENT LIABILITIES</b>                                   |        |                    |                    |
| Cash                        |       | 7.313.876          | 5.144.148          | Short-term obligations with banks and financial institutions |        |                    |                    |
| Time deposits               | (34)  | 27.754.792         | 77.968.249         | Short-term portion of long-term debt                         | (15)   | -                  | 9.876.927          |
| Marketable securities, net  | (4)   | 15.876.763         | 32.871.072         | Commercial paper   | (15)   | 2.007.414          | 17.441.515         |
| Accounts receivable, net    | (5)   | 141.484.751        | 158.632.137        | Current maturities of bonds payable                          | (17 a) | 46.405.565         | 48.637.193         |
| Notes receivable, net       | (5)   | 3.570.343          | 3.329.090          | Current maturities of other long-term obligations            | (17 b) | 28.173.553         | 99.580.381         |
| Other receivables           | (5)   | 12.794.027         | 25.863.220         | Dividends payable  |        | 12.307             | 32.746             |
| Due from related companies  | (6 a) | 16.528.590         | 16.826.597         | Trade accounts payable                                       |        | 1.735.431          | 2.280.058          |
| Inventories, net            |       | 3.448.979          | 4.297.517          | Notes payable  | (35)   | 83.714.282         | 86.267.625         |
| Recoverable taxes           |       | 3.735.403          | -                  | Other payables   |        | 264.681            | -                  |
| Prepaid expenses            |       | 2.988.823          | 4.649.038          | Due to related companies                                     | (36)   | 7.123.137          | 27.831.944         |
| Deferred taxes              | (7 b) | 12.334.810         | 15.416.039         | Accruals   |        | 27.821.965         | 24.770.890         |
| Other current assets        | (8)   | 58.207.800         | 72.984.245         | Withholdings   | (6 b)  | 4.373.063          | 2.767.195          |
|                             |       |                    |                    | Income tax   | (18)   | 14.053.502         | 11.551.157         |
|                             |       |                    |                    | Unearned income  |        | -                  | 30.587.397         |
|                             |       |                    |                    | Other current liabilities                                    |        | 8.344.859          | 8.359.915          |
|                             |       |                    |                    |  |        | 2.379.412          | 1.536.742          |
| <b>TOTAL CURRENT ASSETS</b> |       | <b>306.038.957</b> | <b>417.981.352</b> | <b>TOTAL CURRENT LIABILITIES</b>                             |        | <b>226.409.171</b> | <b>371.521.685</b> |

|   |             |                      |                      |  |               |                    |                    |
|---|-------------|----------------------|----------------------|--|---------------|--------------------|--------------------|
| <b>PROPERTY,<br/>PLANT AND<br/>EQUIPMENT</b>                    | <b>(10)</b> |                      |                      | <b>LONG-TERM<br/>LIABILITIES</b>   |               |                    |                    |
| <b>Land</b>   |             | 27.152.139           | 27.207.038           | <b>Long-term debt with<br/>banks and<br/>Other current<br/>liabilities</b> |               | 2.379.412          | 1.536.742          |
| <b>Buildings and<br/>improvements</b>                           |             | 197.290.304          | 196.073.603          | <b>Bonds payable</b>   | <b>(17 b)</b> | 65.904.044         | 43.692.767         |
| <b>Machinery and<br/>equipment</b>                              |             | 3.241.169.114        | 3.224.401.612        | <b>Other accounts<br/>payable</b>  |               | 22.546.423         | 5.179              |
| <b>Other property,<br/>plant and<br/>equipment</b>              |             | 269.320.422          | 257.738.238          | <b>Accruals</b>  | <b>(18)</b>   | 34.649.896         | 34.704.302         |
| <b>Technical<br/>revaluation</b>                                |             | 9.714.954            | 9.746.443            | <b>Deferred taxes</b>  | <b>(7 b)</b>  | 57.061.195         | 59.047.816         |
| <b>Less:<br/>Accumulated<br/>depreciation</b>                   |             | 2.479.890.587        | 2.326.654.819        | <b>Other liabilities</b>   |               | 4.294.817          | 8.075.208          |
| <b>TOTAL<br/>PROPERTY,<br/>PLANT AND<br/>EQUIPMENT,<br/>NET</b> |             | <b>1.264.756.346</b> | <b>1.388.512.115</b> | <b>TOTAL<br/>LONG-TERM<br/>LIABILITIES</b>                                 |               | <b>511.236.546</b> | <b>514.228.838</b> |
|   |             |                      |                      | <b>MINORITY<br/>INTEREST</b>   | <b>(20)</b>   | <b>1.557.809</b>   | <b>1.666.155</b>   |
| <b>OTHER<br/>NON-CURRENT<br/>ASSETS</b>                         |             |                      |                      | <b>SHAREHOLDERS'<br/>EQUITY</b>  | <b>(21)</b>   |                    |                    |
| <b>Investments in<br/>related<br/>companies</b>                 | <b>(11)</b> | 7.956.777            | 8.528.568            | <b>Paid-in capital</b>   |               | 912.692.729        | 917.292.990        |
| <b>Investments in<br/>other companies</b>                       |             | 4.093                | 4.081                | <b>Price-level restatement<br/>of paid-in capital</b>                      |               | (2.738.078)        | (7.338.344)        |
| <b>Goodwill</b>   | <b>(12)</b> | 17.285.055           | 19.585.489           | <b>Other reserves</b>  |               | (1.586.554)        | (1.030.372)        |
| <b>Other receivables</b>  | <b>(5)</b>  | 13.436.775           | 22.707.059           | <b>Retained earnings</b>   |               | 15.323.743         | 117.096.410        |
| <b>Intangibles</b>  | <b>(13)</b> | 48.731.730           | 47.257.616           | <b>Retained earnings</b>   |               | 25.107.770         | 372.290.453        |
| <b>Less:<br/>Accumulated</b>                                    | <b>(13)</b> | 12.975.999           | 7.897.539            | <b>Net income</b>  |               | 734.109            | 8.507.311          |

|  |             |                      |                      |   |                      |                     |
|--|-------------|----------------------|----------------------|---|----------------------|---------------------|
| <b>amortization<br/>Others<br/>non-current asset</b> | <b>(14)</b> | 17.661.632           | 16.758.621           | <b>Less: Interim<br/>dividend</b>                             | 10.518.136           | 263.701.354         |
| <b>TOTAL OTHER<br/>ASSETS</b>                        |             | <b>92.100.063</b>    | <b>106.943.895</b>   | <b>TOTAL<br/>SHAREHOLDERS'<br/>EQUITY</b>                     | <b>923.691.840</b>   | <b>1.026.020.68</b> |
| <b>TOTAL ASSETS</b>                                  |             | <b>1.662.895.366</b> | <b>1.913.437.362</b> | <b>TOTAL<br/>LIABILITIES AND<br/>SHAREHOLDERS'<br/>EQUITY</b> | <b>1.662.895.366</b> | <b>1.913.437.36</b> |

The accompanying notes 1 to 36 are an integral part of these consolidated financial statements

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## COMPAÑIA DE TELECOMUNICACIONES DE CHILE S.A. AND SUBSIDIARIES

**CONSOLIDATED STATEMENTS OF INCOME  
FOR THE PERIOD ENDED MARCH 31, 2006 AND 2005**

(Restated for general price-level changes and expressed in thousands of constant Chilean pesos as of March 31, 2006)

|   | <b>2006</b>             | <b>2005</b>            |
|---|-------------------------|------------------------|
| <b>OPERATING INCOME:</b>                                    | <b>ThCh\$</b>           | <b>ThCh\$</b>          |
| <b>Operating revenues</b>                                   | 140.803.991             | 142.255.472            |
| <b>Less: Operating costs</b>                                | 89.715.889              | 86.740.419             |
| <b>Gross profit</b>   | <b>51.088.102</b>       | <b>55.515.053</b>      |
| <b>Less: Administrative and selling expenses</b>            | 31.638.204              | 32.907.211             |
| <br><b>OPERATING INCOME</b>                                 | <br><b>19.449.898</b>   | <br><b>22.607.842</b>  |
| <br><b>NON-OPERATING RESULTS:</b>                           |                         |                        |
| <b>Interest income</b>                                      | 673.170                 | 3.479.111              |
| <b>Equity in earnings of equity-method investees</b>        | (11) 459.400            | 408.640                |
| <b>Other non-operating income</b>                           | (22 a) 498.885          | 602.234                |
| <b>Equity in losses of equity-method investees</b>          | (11) 37.003             | 7.663                  |
| <b>Less: Amortization of goodwill</b>                       | (12) 1.113.204          | 389.296                |
| <b>Less: Interest expense and other</b>                     | 4.942.589               | 8.976.972              |
| <b>Less: Other non-operating expenses</b>                   | (22 b) 10.125.274       | 1.495.549              |
| <b>Price-level restatement, net</b>                         | (23) (652.049)          | (5.591.650)            |
| <b>Foreign exchange gain, net</b>                           | (24) 226.786            | 2.471.244              |
| <br><b>NON-OPERATING (LOSS) INCOME, NET</b>                 | <br><b>(15.011.878)</b> | <br><b>(9.499.901)</b> |
| <br><b>INCOME BEFORE INCOME TAXES AND MINORITY INTEREST</b> | <br><b>4.438.020</b>    | <br><b>13.107.941</b>  |
| <b>Income taxes</b>   | (7 c) (3.768.519)       | (4.619.354)            |
| <br><b>INCOME BEFORE MINORITY INTEREST</b>                  | <br><b>669.501</b>      | <br><b>8.488.587</b>   |
| <b>Minority interest</b>                                    | (20) 64.608             | 18.724                 |
| <br><b>NET INCOME FOR THE YEAR</b>                          | <br><b>734.109</b>      | <br><b>8.507.311</b>   |

The accompanying notes 1 to 36 are an integral part of these consolidated financial statements

## COMPAÑIA DE TELECOMUNICACIONES DE CHILE S.A. AND SUBSIDIARIES

**CONSOLIDATED STATEMENTS OF CASH FLOWS  
FOR THE PERIOD ENDED MARCH 31, 2006 AND 2005**

(Restated for general price-level changes and expressed in thousands of constant Chilean pesos as of March 31, 2006)

|   | <b>2006</b>        | <b>2005</b>        |
|---|--------------------|--------------------|
|   | <b>ThCh\$</b>      | <b>ThCh\$</b>      |
| <b>NET CASH<br/>FROM OPERATING ACTIVITIES</b>                             | <b>48.206.938</b>  | <b>74.903.462</b>  |
| <b>Net income for the year</b>  | <b>734.109</b>     | <b>8.507.311</b>   |
| <b>Sales of assets:</b>   | <b>38.788</b>      | <b>(1.235)</b>     |
| Utility on sales of property, plant and equipment                         | -                  | (1.235)            |
| Loss on sales of investments  | 38.788             | -                  |
| <b>Debits ( credits ) to income that do not represent<br/>cash flows:</b> | <b>60.747.896</b>  | <b>61.883.312</b>  |
| Depreciation in operating income for the period                           | 49.787.946         | 51.047.083         |
| Amortization of intangibles   | 1.165.897          | 853.890            |
| Provisions and write offs   | 8.123.726          | 6.227.868          |
| Equity participation in income of equity method investees (less)          | (459.400)          | (408.640)          |
| Equity participation in losses of equity method investees                 | 37.003             | 7.663              |
| Amortization of goodwill  | 1.113.204          | 389.296            |
| Price-level restatement   | 652.049            | 5.591.650          |
| Foreign currency translation  | (226.786)          | (2.471.244)        |
| Other credits to income that do not represent<br>cash flows (less)        | (55.662)           | (6.979)            |
| Other debits to income that do not represent<br>cash flows                | 609.919            | 652.725            |
| <b>Changes in operating assets<br/>(Increase) decrease:</b>               | <b>(9.085.935)</b> | <b>5.690.812</b>   |
| Trade accounts receivable   | (11.257.144)       | (7.401.294)        |
| Inventories   | (1.196.049)        | 1.684.178          |
| Other assets  | 3.367.258          | 11.407.928         |
| <b>Changes in operating liabilities<br/>Increase (decrease):</b>          | <b>(4.163.312)</b> | <b>(1.158.014)</b> |
| Accounts payable related to   |                    |                    |



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|  |                 |                 |
|--|-----------------|-----------------|
| operating activities                                       | (2.930.897)     | 6.522.454       |
| Interest payable   | 222.908         | (2.786.528)     |
| Income taxes payable (net)                                 | 83.650          | 445.031         |
| Other accounts payable related to non-operating activities | (1.121.914)     | (827.463)       |
| V.A.T. and other similar taxes payable                     | (417.059)       | (4.511.508)     |
| <b>Minority interest</b>                                   | <b>(64.608)</b> | <b>(18.724)</b> |

The accompanying notes 1 to 36 are an integral part of these consolidated financial statements

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**COMPAÑIA DE TELECOMUNICACIONES DE CHILE S.A. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF CASH FLOWS  
FOR THE PERIOD ENDED MARCH 31, 2006 AND 2005**

(Restated for general price-level changes and expressed in thousands of constant Chilean pesos as of March 31, 2006)

|   | <b>2006</b>         | <b>2005</b>         |
|---|---------------------|---------------------|
|   | <b>ThCh\$</b>       | <b>ThCh\$</b>       |
| <b>NET CASH USED IN<br/>FINANCING ACTIVITIES</b>        | <b>(38.462.627)</b> | <b>(69.788.588)</b> |
| Obligations with the public                             | 64.812.589          | 12.108.021          |
| Loans repaid (less)                                     | -                   | (10.236.275)        |
| Repayment of obligations with the public (less)         | (103.275.216)       | (71.660.334)        |
| <b>NET CASH USED IN<br/>INVESTING ACTIVITIES</b>        | <b>(18.927.737)</b> | <b>(25.928.621)</b> |
| Sales of property, plant and equipment                  | 60.357              | 154.451             |
| Acquisition of property, plant and equipment (less)     | (18.988.094)        | (14.011.101)        |
| Investments in financial instruments (less)             | -                   | (4.308.159)         |
| Other investing activities (less)                       | -                   | (7.763.812)         |
| <b>NET CASH FLOWS FOR THE PERIOD</b>                    | <b>(9.183.426)</b>  | <b>(20.813.747)</b> |
| <b>EFFECT OF INFLATION ON CASH AND CASH EQUIVALENTS</b> | <b>281.076</b>      | <b>1.357.885</b>    |
| <b>NET INCREASE OF CASH AND CASH EQUIVALENTS</b>        | <b>(8.902.350)</b>  | <b>(19.455.862)</b> |
| <b>CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD</b> | <b>94.975.775</b>   | <b>162.310.735</b>  |
| <b>CASH AND CASH EQUIVALENTS AT END OF PERIOD</b>       | <b>86.073.425</b>   | <b>142.854.873</b>  |

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The accompanying notes 1 to 36 are an integral part of these consolidated financial statements

## COMPAÑÍA DE TELECOMUNICACIONES DE CHILE S.A. AND SUBSIDIARIES

(Translation of financial statements originally issued in Spanish See Note 2)  
Notes to the Consolidated Financial Statements

**1. Composition of Consolidated Group and Registration with the Securities Registry:**

a) The Company is a publicly-held corporation that is registered in the Securities Registry under No. 009 and is therefore subject to supervision by the Chilean Superintendency of Securities and Insurance ( SVS ).

b) Subsidiary companies registered with the Securities Registry:

| Subsidiaries                           | TAXPAYER<br>No. | Registration<br>Number | Participation<br>(direct & indirect) |           |
|--|-----------------|------------------------|--------------------------------------|-----------|
|  |                 |                        | 2006<br>%                            | 2005<br>% |
| Telefónica Mundo S.A.                  | 96,551,670-0    | 456                    | 99.16                                | 99.16     |
| Globus 120 S.A.                        | 96,887,420-9    | 694                    | 99.99                                | 99.99     |
| Telefónica Asistencia y Seguridad S.A. | 96,971,150-8    | 863                    | 99.99                                | 99.99     |

**2. Summary of Significant Accounting Policies:****(a) Accounting period:**

The interim consolidated financial statements correspond to the three-month periods ended March 31, 2006 and 2005.

**(b) Basis of preparation:**

These interim consolidated financial statements (hereinafter the financial statements ) have been prepared in accordance with Generally Accepted Accounting Principles in Chile ( Chilean GAAP ) and standards set forth by the Chilean Superintendency of Securities and Insurance ( SVS ). In the event of any discrepancies in these regulations, SVS regulations supersede Chilean GAAP. Certain accounting practices applied by the Company that conform to Chilean GAAP may not conform to generally accepted accounting principles in the United States ( US GAAP ) or International Financial Reporting Standards ( IFRS ). For the convenience of the reader, these financial statements have been translated from Spanish to English.

The Company s financial statements as of June 30 and December 31 of each year are prepared in order to be reviewed and audited respectively, in accordance with current legal regulations. With respect to the quarterly financial statements as of March and September, the Company voluntarily submits these to an interim financial information review performed in accordance with the regulations established for this type of review, described in generally accepted auditing standard No. 45 Section No. 722, issued by the Chilean Association of Accountants.

**(c) Basis of presentation:**

The interim consolidated financial statements for 2005 and their notes have been adjusted for comparison purposes by 4.1% in order to allow comparison with the 2006 interim financial statements. For comparison purposes, certain

reclassifications have been made to the 2005 financial statements.

**(d) Basis of consolidation:**

These consolidated financial statements include the assets, liabilities, income and cash flows of the Parent Company and subsidiaries. Significant intercompany transactions have been eliminated, and the participation of minority investors has been recognized under Minority Interest (See Note 20).

**2. Summary of Significant Accounting Policies**, continued:**(d) Basis of consolidation**, continued:**Companies included in consolidation:**

As of March 31, 2006, the consolidated group (The Company) is composed of Compañía de Telecomunicaciones de Chile S.A. and the following subsidiaries:

| TAXPAYER<br>No. | Company Name  | Economic Participation Percentage |                  |       | 2005<br>Total |
|-----------------|---|-----------------------------------|------------------|-------|---------------|
|                 |   | Direct                            | 2006<br>Indirect | Total |               |
| 96,551,670-0    | Telefónica Mundo S.A.<br>Telefonica Gestión de Servicios  | 99.16                             | -                | 99.16 | 99.16         |
| 96,961,230-5    | Compartidos Chile S.A.                                    | 99.99                             | -                | 99.99 | 99.99         |
| 74,944,200-K    | Fundación Telefónica Chile                                | 50.00                             | -                | 50.00 | 50.00         |
| 96,887,420-9    | Globus 120 S.A.   | 99.99                             | -                | 99.99 | 99.99         |
| 96,971,150-8    | Telefónica Asistencia y Seguridad S.A.                    | 99.99                             | -                | 99.99 | 99.99         |
| 90,430,000-4    | Telefónica Empresas CTC Chile S.A.                        | 99.99                             | -                | 99.99 | 99.99         |
| 78,703,410-1    | Tecnonáutica S.A. (1)                                     | 99.99                             | -                | 99.99 | 99.99         |
| 96,834,320-3    | Telefónica Internet Empresas S.A. (2)                     | 99.99                             | -                | 99.99 | 99.99         |
| 96,811,570-7    | Administradora de Telepeajes de Chile<br>S.A.             | -                                 | 79.99            | 79.99 | 79.99         |
| 96,545,500-0    | CTC Equipos y Servicios de<br>Telecomunicaciones S.A. (3) | -                                 | -                | -     | 99.99         |

1) On January 26, 2006, Telefónica Internet S.A. sold 449,081 shares to Telefónica CTC Chile for ThCh\$1,624,273 corresponding to its participation in that company. On that same date, CTC Equipos y Servicios S.A. sold 1 share to Telefónica CTC Chile S.A. for ThCh\$4 corresponding to its participation in that company.

2) On January 27, 2006, Telefónica Empresas CTC Chile sold 215,099 shares to Telefónica CTC Chile for ThCh \$1,468,683 corresponding to its participation in that company.  
On January 26, CTC Equipos y Servicios S.A. sold 16 shares to Telefónica CTC Chile for ThCh \$132 corresponding to its participation in that company.

3) On March 1, 2006, Telefónica CTC Chile absorbed subsidiary CTC Equipos y Servicios de Telecomunicaciones S.A. after purchasing 1 share of that company from third parties for ThCh\$11 on February 28, 2006.

**2. Summary of Significant Accounting Policies**, continued:**(e) Price-level restatement:**

The interim consolidated financial statements have been adjusted by applying price-level restatement standards, in accordance with Chilean GAAP, in order to reflect the changes in the purchasing power of the currency during both periods. The accumulated variation in the CPI as of March 31, 2006 and 2005, for initial balances, is -0.3% and -0.8%, respectively.

**(f) Basis of conversion:**

Assets and liabilities in US\$ (United States dollars), Euros, Brazilian Reales and UF (Unidad de Fomento) have been converted to pesos at the exchange rates as of each period end:

| YEAR | US\$   | EURO   | BRAZILIAN<br>REAL | UF        |
|------|--------|--------|-------------------|-----------|
| 2006 | 526.18 | 637.56 | 243.26            | 17,915.66 |
| 2005 | 585.93 | 759.57 | 219.82            | 17,198.78 |

Foreign currency translation differences resulting from the application of this Standard are credited or debited to income for the period.

**(g) Time deposits:**

Time deposits are carried at cost plus adjustments, where applicable, and accrued interest up to period end.

**(h) Marketable securities:**

Fixed income securities are recorded at their price-level restated acquisition value, plus interest accrued as of each period end using the real rate of interest determined as of the date of purchase, or their market value, whichever is less.

**(i) Inventories:**

Equipment held for sale is carried at price-level restated acquisition or development cost or at market value, whichever is less.

Inventories estimated to be used during the next twelve months are classified as current assets and their cost is price-level restated. The obsolescence provision has been determined on the basis of a survey of materials with slow turnover.

**2. Summary of Significant Accounting Policies**, continued:

**(j) Allowance for doubtful accounts:**

Different percentages are applied when calculating the allowance for doubtful accounts, taking into consideration the aging of such accounts. The allowance for debts exceeding 120 days, or 180 days in the case of large customers (corporations), is for 100% of the amount receivable.

**(k) Property, plant and equipment:**

Property, plant and equipment are carried at their price-level restated acquisition and/or construction cost.

Property, plant and equipment acquired up to December 31, 1979 are carried at their appraisal value, as stipulated in Article 140 of D.F.L. No. 4, and those acquired subsequently are carried at their acquisition value, except for those assets which are carried at the appraisal value recorded as of September 30, 1986, as authorized in SVS Circular No. 550. All these values have been price-level restated.

**(l) Depreciation of property, plant and equipment:**

Depreciation has been calculated and recorded on a straight-line basis over the estimated useful lives of the assets. The average annual financial depreciation rate of the Company is approximately 7.82% .

**(m) Leased assets:**

Rented Assets with a purchase option and whose contracts meet the characteristics of a financial lease are recorded in a similar fashion to the acquisition of property, plant and equipment, by recognizing the full obligation and interest on an accrual basis. These assets are not legally owned by the Company; therefore until it exercises the purchase option they cannot be freely disposed of.

**(n) Intangibles:**

**i) Rights to underwater cable:**

Corresponds to the rights acquired by the Company for the use of an underwater cable to transmit voice and data. This right is amortized over the term of the respective contracts, with a maximum of 25 years.

**ii) Software licenses:**

Software licenses are valued at their price-level restated acquisition cost. Amortization is calculated using the straight-line method over their estimated useful life, which does not exceed 4 years.

**(ñ) Investments in related companies:**

These investments are accounted for under the equity method, which recognizes the investor's share of income on an accrual basis. For investments abroad, the valuation methodology applied is that defined in Technical Bulletin No. 64. These investments are controlled in dollars, since they are in countries deemed to be unstable and their activities are not an extension of the operations of the Parent Company.

**2. Summary of Significant Accounting Policies**, continued:

**(o) Goodwill:**

Corresponds to the valuation differences that are created when adjusting the cost of the investments, adopting the equity method or making a new purchase. Goodwill and negative goodwill amortization periods have been determined considering aspects such as the nature and characteristics of the business and the estimated period of return of the investment. Goodwill arising on the acquisition of investments abroad is controlled in United States dollars (same currency in which the investment is controlled) as per Technical Bulletin No. 64 of the Chilean Accountants Association. (See Note 12).

Goodwill impairment has been assessed as required in SVS Circular No.1,697 and Technical Bulletin No. 72 issued by the Chilean Association of Accountants.

**(p) Transactions with repurchase agreements:**

Purchases of securities under agreement to resell are recorded as fixed rate securities and are classified under Other Current Assets (see note 8).

**(q) Obligations with the public:**

- Bonds payable are presented in liabilities at the par value of the issued bonds (see note 17b). The difference between the par and placement value, determined on the basis of the designated interest rate for the transaction, is deferred and amortized using the straight-line method over the term of the respective bond (see notes 8 and 14).
- Commercial paper is presented in liabilities at its placement value, plus accrued interest (see note 17a).

Costs directly related to the placement of these obligations are deferred and amortized using the straight-line method over the term of the respective liability.

**(r) Income tax and deferred income taxes:**

Income tax is recorded on the basis of taxable net income. Deferred taxes on all temporary differences, usable tax loss carry forwards, and other events that create differences between the tax and accounting values are recognized in accordance with, Technical Bulletins No. 60 and its modifications issued by the Chilean Accountants Association and as established by SVS Circular No.1,466 dated January 27, 2000.

**(s) Staff severance indemnities:**

For employees who qualify for this benefit, the Company's staff severance indemnities obligation is provided for by applying the present value of the obligation using an annual discount rate of 6%, considering estimates such as the future service period of the employee, mortality rate of employees and salary increases determined on the basis of actuarial calculations (see Note 19).

Costs for past services of the employees produced by changes in the actuarial bases, are deferred and amortized over average periods of employees' future service periods.

**(t) Revenue recognition:**

The Company's revenues are recognized on an accrual basis in accordance with Chilean GAAP. Since billing dates are different from the accounting close date, as of the date of preparation of these financial statements provisions have



been established for services provided and not billed, which are determined on the basis of contracts, traffic, prices and current conditions for the period. These amounts are recorded under Trade Accounts Receivable.

**2. Summary of Significant Accounting Policies**, continued:

**(u) Foreign currency forwards:**

The Company has entered into future foreign currency contracts, which represent a hedge against the variation in the exchange rate of its obligations in foreign currency.

These instruments are valued in accordance with Technical Bulletin No. 57 of the Chilean Accountants Association.

The rights and obligations acquired are detailed in Note 27, reflecting in the balance sheet only the net right or obligation at period end, classified according to the maturity of each contract under Other Current Assets or Other Payables, as applicable. The contract's implicit premium is deferred and amortized using the straight-line method over the term of the contract.

**(v) Interest rate coverage:**

Interest on loans for which associated interest rate swaps have been entered into is recorded recognizing the effect of those contracts on the interest rate established in such loans. The rights and obligations acquired therein are shown under Other Creditors or under Other Current Assets, as applicable (See Note 27).

**(w) Computer software:**

The cost of software purchased is deferred and amortized using the straight-line method over a maximum period of four years and classified under Other property, plant and equipment.

**(x) Research and development expenses:**

Research and development expenses are charged to income in the period in which they are incurred. Those expenses have not been significant in recent years.

**(y) Accumulated adjustment for conversion differences:**

The Company recognizes in this equity reserve account the difference from exchange rate fluctuations and the Consumer Price Index (C.P.I.) from restating its investments abroad. These investments are controlled in United States dollars. The balance in this account is credited (or charged) to income in the same period in which the net income or loss on the total or partial disposal of these investments is recognized.

**(z) Statement of cash flows:**

For the purposes of preparing the Statement of Cash Flows according to Technical Bulletin No. 50 of the Chilean Accountants Association and SVS Circular No.1,312, the Company defines cash equivalents as securities under agreements to resell and time deposits maturing in less than 90 days.

Cash flows related to the Company's line of business and all cash flows not defined as from investing or financing activities are included under Cash Flows from Operating Activities.

**2. Summary of Significant Accounting Policies, continued:**

**(aa) Correspondents:**

The Company currently has agreements with foreign correspondents, which set the conditions that regulate international traffic. The correspondents are charged or paid, according to net traffic receivable/payable and the rates set in each agreement.

This receivable/payable is recorded on an accrual basis; the costs and income for the period are recognized on an accrual basis, and the net balances receivable and payable of each correspondent are recorded under Trade Accounts Receivable or Accounts Payable, as applicable.

**3. Accounting Changes:**

**a) Accounting changes**

During the periods covered in these interim consolidated financial statements, the accounting principles have been consistently applied.

**b) Change in estimate**

**i) Change in the estimations of staff severance indemnities**

**Changes in actuarial hypotheses**

As established in Technical Bulletin No. 8 issued by the Chilean Association of Accountants and in light of the new contractual conditions derived from the organizational restructuring undergone by the Company, a series of studies were undertaken to modify the calculation base for the staff severance indemnities provision. Initially, in December 2004, this meant recognizing deferred assets of ThCh\$4,872,939 (historical). After these studies were concluded during 2005, the Company decided to also include other actuarial estimates in the calculation methodology used for this provision. The additional variables modified were: personnel turnover index, mortality rate and future salary increases. As a result of these modifications, the Company recorded deferred assets of ThCh\$3,648,704 in the year 2005. Both effects will be amortized over the future service period of the employees with this benefit (see portion to be amortized in the short-term in Note 8 (3) and in the long-term in Note 14 (2)).

**Change in the discount rate**

During the first quarter of 2006 an evaluation was performed of the market interest rate used to calculate the current value of staff severance indemnities. After completing this analysis the Company decided to reduce the discount rate from 7% to 6%. As a result of these modifications, the Company recorded deferred tax assets of ThCh\$ 2,797,402 in 2006 which will be amortized over the future years of service of the employees that qualify for this benefit.

**4. Marketable Securities:**

The balance of marketable securities is as follows:

| DESCRIPTION                       | 2006<br>ThCh\$    | 2005<br>ThCh\$    |
|-----------------------------------|-------------------|-------------------|
| Shares                            | -                 | 442,929           |
| Publicly offered promissory notes | 15,876,763        | 32,428,143        |
| <b>Total</b>                      | <b>15,876,763</b> | <b>32,871,072</b> |

**Publicly offered promissory notes (Fixed Income)**

| Instrument | Date             |          | Par               | Book Value        |           | Market Value      | Provision        |
|------------|------------------|----------|-------------------|-------------------|-----------|-------------------|------------------|
|            | Purchase         | Maturity | Value<br>ThCh\$   | Amount<br>ThCh\$  | Rate<br>% | ThCh\$            | ThCh\$           |
| BCD0500907 | Dec-04           | Sep-07   | 2,630,900         | 2,636,312         | 5%        | 2,636,312         | (43,641)         |
| BCD0500907 | Ago-05           | Sep-07   | 1,841,630         | 1,845,419         | 5%        | 1,845,419         | (14,494)         |
| BCD0500907 | Sep-05           | Sep-07   | 2,104,720         | 2,109,050         | 5%        | 2,109,050         | (28,263)         |
| BCD0500907 | Sep-05           | Sep-07   | 2,630,900         | 2,636,312         | 5%        | 2,636,312         | (34,981)         |
| BCD0500907 | Sep-05           | Sep-07   | 2,630,900         | 2,636,312         | 5%        | 2,636,312         | (33,324)         |
| BCD0500907 | Sep-05           | Sep-07   | 526,180           | 527,263           | 5%        | 527,263           | (6,673)          |
| BCD0500907 | Sep-05           | Sep-07   | 526,180           | 527,263           | 5%        | 527,263           | (6,370)          |
| BCD0500907 | Sep-05           | Sep-07   | 1,052,360         | 1,054,525         | 5%        | 1,054,525         | (12,603)         |
|            | <b>Sub-Total</b> |          | <b>13,943,770</b> | <b>13,972,456</b> |           | <b>13,972,456</b> | <b>(180,349)</b> |
| BCU500909  | Nov-05           | Sep-09   | 1,791,566         | 1,904,307         | 5%        | 1,932,684         | -                |
|            | <b>Sub-Total</b> |          | <b>1,791,566</b>  | <b>1,904,307</b>  |           | <b>1,932,684</b>  | -                |
|            | <b>Total</b>     |          | <b>15,735,336</b> | <b>15,876,763</b> |           | <b>15,905,140</b> | <b>(180,349)</b> |

**5. Current and long-term receivables:**

The detail of current and long-term receivables is as follows:

| Description                              | Current            |                    |                      |                   |                    |                    | Total Current |  |
|--|--------------------|--------------------|----------------------|-------------------|--------------------|--------------------|---------------|--|
|  | Up to 90 days      |                    | Over 90 up to 1 year |                   | Subtotal           | 2006               | %             |  |
|  | 2006               | 2005               | 2006                 | 2005              | 2006               |                    |               |  |
| ThCh\$                                   | ThCh\$             | ThCh\$             | ThCh\$               | ThCh\$            | ThCh\$             | ThCh\$             |               |  |
| <b>Trade accounts receivable</b>         | <b>188,685,057</b> | <b>242,447,362</b> | <b>14,953,038</b>    | <b>4,737,133</b>  | <b>203,638,095</b> | <b>141,484,751</b> | <b>100.0</b>  |  |
| Fixed telephony service                  | 160,960,079        | 168,793,596        | 1,115,650            | 1,779,547         | 162,075,729        | 108,758,074        | 76.87         |  |
| Long distance                            | 10,071,688         | 48,200,946         | 11,799,880           |                   | 21,871,568         | 15,874,836         | 11.22         |  |
| Communications companies                 | 16,261,122         | 21,329,008         | 1,688,267            | 2,789,283         | 17,949,389         | 16,480,499         | 11.65         |  |
| Other                                    | 1,392,168          | 4,123,812          | 349,241              | 168,303           | 1,741,409          | 371,342            | 0.26          |  |
| Allowance for doubtful accounts          | (56,104,730)       | (87,521,874)       | (6,048,614)          | (1,030,484)       | (62,153,344)       | -                  | -             |  |
| <b>Notes receivable</b>                  | <b>8,075,933</b>   | <b>11,796,235</b>  | <b>162,841</b>       | <b>265,049</b>    | <b>8,238,774</b>   | <b>3,570,343</b>   |               |  |
| Allowance for doubtful notes             | (4,668,431)        | (8,732,194)        | -                    | -                 | (4,668,431)        | -                  | -             |  |
| <b>Miscellaneous accounts receivable</b> | <b>10,200,812</b>  | <b>6,934,177</b>   | <b>2,593,215</b>     | <b>18,929,043</b> | <b>12,794,027</b>  | <b>12,794,027</b>  |               |  |
| Allowance for doubtful accounts          | -                  | -                  | -                    | -                 | -                  | -                  | -             |  |

Long-term receivables

**6. Balances and transactions with related entities:****a) Receivables from related parties are as follows:**

| Taxpayer No. | Company  | Short-term        |                   | Long-term      |                |
|--------------|--|-------------------|-------------------|----------------|----------------|
|              |  | 2006<br>ThCh\$    | 2005<br>ThCh\$    | 2006<br>ThCh\$ | 2005<br>ThCh\$ |
| 96,990,810-7 | Telefónica Móviles Chile Distribución S.A.         | 49,744            | -                 | -              | -              |
| Foreign      | Telefónica España                                  | 218,610           | 41,649            | -              | -              |
| 93,541,000-2 | Impresora y Comercial Publicguías S.A.             | 3,335,215         | 4,687,400         | -              | -              |
| Foreign      | Emergia USA  | -                 | 45,817            | -              | -              |
| 96,834,230-4 | Terra Networks Chile S.A.                          | 1,285,464         | 1,204,879         | -              | -              |
| 96,895,220-K | Atento Chile S.A.                                  | 529,693           | 353,324           | -              | -              |
| 96,910,730-9 | TIWS Chile S.A.                                    | 176,160           | 133,722           | -              | -              |
| Foreign      | Telefónica LD Puerto Rico                          | -                 | 3,339             | -              | -              |
| Foreign      | Telefonica Data EEUU                               | 39,532            | 52,169            | -              | -              |
| Foreign      | Telefónica Data España                             | 409,752           | 174,535           | -              | -              |
| Foreign      | Telefónica Argentina                               | 1,313,093         | 837,495           | -              | -              |
| Foreign      | Telefónica Gestión de Servicios Compartidos España | 11,202            | -                 | -              | -              |
| 96,786,140-5 | Telefónica Móvil de Chile S.A.                     | 6,304,010         | 7,453,325         | -              | -              |
| Foreign      | Telefónica Procesos Tec. de Información            | 1,338,177         | 1,453,262         | -              | -              |
| 59,083,900-0 | Telefónica Ingeniería de Seguridad S.A.            | 4,159             | 2,444             | -              | -              |
| Foreign      | TIWS América S.A.                                  | 512,061           | 257,803           | -              | -              |
| 96,672,160-K | Telefónica Móviles Chile S.A.                      | 874,979           | -                 | -              | -              |
| Foreign      | Telefónica Perú                                    | 1,934             | -                 | -              | -              |
| 96,942,730-3 | Telefónica Mobile Solutions Chile S.A.             | 124,805           | 125,434           | -              | -              |
|              | <b>Total</b>                                       | <b>16,528,590</b> | <b>16,826,597</b> | <b>-</b>       | <b>-</b>       |

There have been charges and credits recorded to current accounts with these companies for invoicing of sale of materials, equipment and services.

**b) Payables to related parties are as follows:**

| Taxpayer No. | Company                                | Short-term     |                | Long-term      |                |
|--------------|--|----------------|----------------|----------------|----------------|
|              |  | 2006<br>ThCh\$ | 2005<br>ThCh\$ | 2006<br>ThCh\$ | 2005<br>ThCh\$ |
| Foreign      | Telefónica España                      | -              | 36,025         | -              | -              |
| 96,527,390-5 | Telefónica Internacional Chile S.A.    | 419,226        | 139,680        | -              | -              |
| 93,541,000-2 | Impresora y Comercial Publicguías S.A. | 855,870        | 1,437,337      | -              | -              |
| Foreign      | Telefónica Perú                        | -              | 54,665         | -              | -              |

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|              |   |                   |                   |   |   |
|--------------|---|-------------------|-------------------|---|---|
| 96,834,230-4 | Terra Networks Chile S.A.               | 4,793,546         | 4,255,423         | - | - |
| 96,895,220-K | Atento Chile S.A.                       | 1,273,075         | 3,316,264         | - | - |
| 96,910,730-9 | TIWS Chile S.A.                         | 1,149,484         | 108,807           | - | - |
| 59,083,900-0 | Telefónica Ingenieria de Seguridad S.A. | 2,181             | -                 | - | - |
| Foreign      | Telefónica Guatemala                    | 67,760            | 5,866             | - | - |
| Foreign      | Telefónica El Salvador                  | 17,425            | 162,527           | - | - |
| 96,786,140-5 | Telefónica Móvil de Chile S.A.          | 14,090,992        | 12,331,437        | - | - |
| Foreign      | Telefónica Argentina                    | -                 | 586,326           | - | - |
| Foreign      | TIWS América S.A.                       | 721,741           | 1,352,369         | - | - |
| Foreign      | Telefónica LD Puerto Rico               | 13,820            | -                 | - | - |
| Foreign      | Telefónica Sao Paulo                    | 29,534            | -                 | - | - |
| 96,672,160-K | Telefónica Móviles Chile S.A.           | 3,816,367         | -                 | - | - |
| Foreign      | Telefonica Investigacion y Desarrollo   | 511,567           | 980,358           | - | - |
| 96,942,730-3 | Telefónica Mobile Solutions Chile S.A.  | -                 | 3,806             | - | - |
| Foreign      | Atento Servicios Técnicos Y Consultoría | 59,377            | -                 | - | - |
|              | <b>Total</b>                            | <b>27,821,965</b> | <b>24,770,890</b> | - | - |

As per Article No. 89 of the Corporations Law, all these transactions are carried out under conditions similar to those that normally prevail in the market.

**6. Balances and transactions with related companies**, continued:**c) Transactions:**

| Company                                       | Tax No.      | Nature of Relationship | Description of transaction | 2005<br>ThCh\$            |                           | 2004<br>ThCh\$            |                           |
|---|--------------|------------------------|----------------------------|---------------------------|---------------------------|---------------------------|---------------------------|
|   |              |                        |                            | Amount                    | Effect on income          | Amount                    | Effect on income          |
| Telefónica España                             | Foreign      | Parent Co.             | Sales<br>Purchases         | 113.797<br>(76.959)       | 113.797<br>(76.959)       | 165.719<br>(49.587)       | 165.719<br>(49.587)       |
| Telefonica Data EEUU                          | Foreign      | Associate              | Sales                      | 10.803                    | 10.803                    | -                         | -                         |
| Telefónica Internacional Chile S.A.           | 96,527,390-5 | Parent Co.             | Purchases                  | (139.787)                 | (139.787)                 | (139.706)                 | (139.706)                 |
| Impresora y Comercial Publiguías S.A.         | 93,541,000-2 | Associate              | Sales<br>Purchases         | 915.901<br>(1.491.875)    | 915.901<br>(1.491.875)    | 1.036.345<br>(927.079)    | 1.036.345<br>(927.079)    |
| Terra Networks Chile S.A.                     | 96,834,230-4 | Associate              | Sales<br>Purchases         | 1.397.240<br>(168.689)    | 1.397.240<br>(168.689)    | 1.361.442<br>(139.429)    | 1.361.442<br>(139.429)    |
| Atento Chile S.A.                             | 96,895,220-K | Associate              | Sales<br>Purchases         | 207.223<br>(3.904.742)    | 207.223<br>(3.904.742)    | 455.463<br>(3.794.965)    | 455.463<br>(3.794.965)    |
| Telefónica Argentina                          | Foreign      | Associate              | Sales<br>Purchases         | 502.779<br>(262.821)      | 502.779<br>(262.821)      | 171.843<br>(141.353)      | 171.843<br>(141.353)      |
| Telefonica WholeSale International Services   | Foreign      | Associate              | Sales<br>Purchases         | -<br>-                    | -<br>-                    | 50.160<br>(685.544)       | 50.160<br>(685.544)       |
| Telefónica Sao Paulo                          | Foreign      | Associate              | Sales<br>Purchases         | 51.474<br>(54.232)        | 51.474<br>(54.232)        | 25.714<br>(29.904)        | 25.714<br>(29.904)        |
| Telefónica Guatemala                          | Foreign      | Associate              | Sales<br>Purchases         | 1.912<br>(17.929)         | 1.912<br>(17.929)         | 1.304<br>(3.395)          | 1.304<br>(3.395)          |
| Telefónica Perú                               | Foreign      | Associate              | Sales<br>Purchases         | 161.708<br>(224.223)      | 161.708<br>(224.223)      | 89.349<br>(98.152)        | 89.349<br>(98.152)        |
| Telefónica LD Puerto Rico                     | Foreign      | Associate              | Sales<br>Purchases         | 1.569<br>(4.557)          | 1.569<br>(4.557)          | 2.264<br>(1.906)          | 2.264<br>(1.906)          |
| Telefónica El Salvador                        | Foreign      | Associate              | Sales<br>Purchases         | 1.279<br>(10.272)         | 1.279<br>(10.272)         | 757<br>(3.749)            | 757<br>(3.749)            |
| Telefónica Móvil de Chile S.A.                | 96,786,140-5 | Associate              | Sales<br>Purchases         | 3.046.300<br>(10.833.228) | 3.046.300<br>(10.833.228) | 3.657.818<br>(12.667.378) | 3.657.818<br>(12.667.378) |
| Telefónica Móviles Chile Larga Distancia S.A. | 96,672,160-K | Associate              | Sales<br>Purchases         | -<br>-                    | -<br>-                    | 410.673<br>(3.315.817)    | 410.673<br>(3.315.817)    |



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|   |              |           |                    |                        |                        |                      |                      |
|---|--------------|-----------|--------------------|------------------------|------------------------|----------------------|----------------------|
| Telefónica Móviles Chile Inversiones S.A.           | 87,845,500-2 | Associate | Sales<br>Purchases | 249.207<br>(2.409.774) | 249.207<br>(2.409.774) | -<br>-               | -<br>-               |
| Telefonica WholeSale International Services Uruguay | Foreign      | Associate | Purchases          | (274.137)              | (274.137)              | -                    | -                    |
| TIWS Chile S.A.                                     | 96,910,730-9 | Associate | Sales<br>Purchases | 249.133<br>(1.124.106) | 249.133<br>(1.124.106) | 288.126<br>(432.097) | 288.126<br>(432.097) |

The conditions of the agreement related to intercompany transactions between the Company and its equity-method investees and its mercantile current account are short and long-term, respectively, in the case of Telefónica Internacional Chile S.A., It is denominated in US dollars, accruing interest at a variable rate adjusted to market rates (US\$ + Market Spread)

In the case of Sales and Services Rendered, these mature in the short-term (less than a year) and the maturity terms for each case vary based on the related transaction,

**7. Current and deferred income taxes:****a) General information:**

As of March 31, 2006 and 2005, the Parent Company has established a first category income tax provision, as it has taxable net income of ThCh\$27,209,135 and ThCh\$25,507,788, respectively.

In addition, as of March 31, 2006 and 2005, a provision for first category income tax in subsidiaries was recorded in the amounts of ThCh\$8,396,847 and ThCh\$6,881,371, respectively.

The companies in the group with positive Retained Taxable Earnings and their associated credits are as follows:

| <b>Subsidiaries</b>  | <b>Retained<br/>Taxable<br/>Earnings<br/>w/15% credit<br/>ThCh\$</b> | <b>Retained<br/>Taxable<br/>Earnings<br/>w/16% credit<br/>ThCh\$</b> | <b>Retained<br/>Taxable<br/>Earnings<br/>w/16.5% credit<br/>ThCh\$</b> | <b>Retained<br/>Taxable<br/>Earnings<br/>w/17% credit<br/>ThCh\$</b> | <b>Retained<br/>Taxable<br/>Earnings<br/>w/o credit<br/>ThCh\$</b> | <b>Amount<br/>of<br/>credit<br/>ThCh\$</b> |
|--|--|--|--|--|--|--|
| Telefónica Gestión<br>Servicios Compartidos<br>de Chile S.A. | -  | -  | -  | 455,346  | 93,394   | 93,264                                     |
| Telefónica Mundo<br>S.A.                                     | -  | 66,169   | 4,418,074  | 33,216,402   | 3,574,555  | 7,688,984                                  |
| Globus 120 S.A.  | 2,179,207  | 825,635  | 591,061  | 2,265,630  | 359,555  | 1,122,670                                  |
| Tecnonáutica S.A.  | -  | -  | -  | 26,883   | 33,755   | 5,506                                      |
| Telefónica Empresas<br>CTC Chile S.A.                        | -  | -  | 1,685,904  | 26,747,844   | 2,456,845  | 5,811,609                                  |
| Compañía de<br>Telecomunicaciones de<br>Chile S.A.           | -  | -  | -  | 20,379,836   | 12,485,570   | 4,174,183                                  |
| <b>Total</b>   | <b>2,179,207</b>   | <b>891,804</b>   | <b>6,695,039</b>   | <b>83,091,941</b>  | <b>19,003,674</b>  | <b>18,896,216</b>                          |

**7. Current taxes , and deferred income continued: b) Deferred taxes:**

As of March 31, 2006 and 2005 the accumulated balances of temporary differences that originated net deferred tax liabilities in the amount of ThCh\$44,726,385 and ThCh\$43,631,777, are as follows:

| Description  | 2006                 |                     |                          |                     |                      |           |
|--|----------------------|---------------------|--------------------------|---------------------|----------------------|-----------|
|  | Deferred tax assets  |                     | Deferred tax liabilities |                     | Deferred tax a       |           |
|  | Short-term<br>ThCh\$ | Long-term<br>ThCh\$ | Short-term<br>ThCh\$     | Long-term<br>ThCh\$ | Short-term<br>ThCh\$ | Lo<br>T   |
| Allowance for doubtful accounts                        | 10,500,214           | -                   | -                        | -                   | 14,598,602           |           |
| Vacation provision                                     | 399,520              | -                   | -                        | -                   | 335,335              |           |
| Tax benefits for tax losses                            | 103,556              | 1,041,551           | -                        | -                   | -                    | 1,        |
| Staff severance indemnities                            | -                    | 17,017              | -                        | 5,186,043           | -                    |           |
| Leased assets and liabilities                          | -                    | 57,939              | -                        | 77,666              | -                    |           |
| Property, plant and equipment                          | -                    | 4,166,389           | -                        | 161,041,385         | 9,056                | 4,        |
| Termination provision                                  | 121,973              | -                   | -                        | -                   | -                    |           |
| Difference in amount of capitalized staff severance    | -                    | 485,546             | -                        | -                   | -                    |           |
| Software   | -                    | -                   | -                        | 1,705,989           | -                    |           |
| Deferred charge on sale of assets                      | -                    | -                   | -                        | 839,607             | -                    |           |
| Collective negotiation bonus                           | -                    | -                   | -                        | 143,064             | -                    |           |
| Other  | 1,268,129            | 271,417             | 58,582                   | 4,066,661           | 479,234              |           |
| <b>Sub-Total</b>                                       | <b>12,393,392</b>    | <b>6,039,859</b>    | <b>58,582</b>            | <b>173,060,415</b>  | <b>15,422,227</b>    | <b>6,</b> |
| Complementary accounts net of accumulated amortization | -                    | (3,540,741)         | -                        | (113,500,102)       | -                    | (3,       |
| <b>Sub-Total</b>                                       | <b>12,393,392</b>    | <b>2,499,118</b>    | <b>58,582</b>            | <b>59,560,313</b>   | <b>15,422,227</b>    | <b>2,</b> |
| Tax reclassification                                   | (58,582)             | (2,499,118)         | (58,582)                 | (2,499,118)         | (6,188)              | (2,       |
| <b>Total</b>   | <b>12,334,810</b>    | <b>-</b>            | <b>-</b>                 | <b>57,061,195</b>   | <b>15,416,039</b>    |           |

**7. Current and deferred income taxes**, continued:**c) Income tax breakdown:**

The current tax expense shown in the following table is based on taxable income:

| <b>Description</b>   | <b>2006<br/>ThCh\$</b> | <b>2005<br/>ThCh\$</b> |
|--|------------------------|------------------------|
| Common tax expense before tax credit (income tax 17%)                                  | 6,053,017              | 5,506,157              |
| Current tax expense (article 21 single tax at 35%)                                     | 7,619                  | 6,406                  |
| <b>Income tax subtotal</b>   | <b>6,060,636</b>       | <b>5,512,563</b>       |
| - Current period deferred taxes  | (5,664,818)            | (4,269,678)            |
| - Tax benefits from tax loss carry forwards  | -                      | (15,788)               |
| - Effect of amortization of complementary accounts for deferred assets and liabilities | 3,372,701              | 3,392,257              |
| <b>Deferred tax subtotal</b>   | <b>(2,292,117)</b>     | <b>(893,209)</b>       |
| <b>Total expense tax</b>   | <b>3,768,519</b>       | <b>4,619,354</b>       |

**8. Other Current Assets:**

The detail of other current assets is as follows:

| Description  | 2006<br>ThCh\$    | 2005<br>ThCh\$    |
|--|-------------------|-------------------|
| Fixed income securities purchased with resale agreement (note 9)       | 51,004,757        | 59,742,476        |
| Deferred union contract bonus (1)                                      | 790,346           | 2,316,770         |
| Deferred exchange insurance premiums                                   | 38,618            | 768,676           |
| Telephone directories for connection program                           | 1,728,065         | 3,332,307         |
| Deferred higher bond discount rate (note 25)                           | 234,462           | 59,037            |
| Deferred disbursements for placement of bonds (note 25)                | 282,832           | 423,521           |
| Commercial paper issuance costs (note 25)                              | -                 | 176,703           |
| Deferred disbursements for foreign financing proceeds (2)              | 852,966           | 567,168           |
| Exchange difference insurance receivable (net of partial liquidations) | 1,102,964         | 3,159,401         |
| Deferred staff severance indemnities charges (3)                       | 1,216,284         | 715,237           |
| Dispensable property   | 117,748           | 117,137           |
| Others   | 838,758           | 1,605,812         |
| <b>Total</b>   | <b>58,207,800</b> | <b>72,984,245</b> |

(1) Between November and December 2003, the Company negotiated a 32-month and 36-month union contract with a number of its employees, granting them, among other benefits, a signing bonus. That bonus was paid in November and December 2003. The total benefit of ThCh\$3,425,245 (historical) was deferred using the straight-line method over the term of the union agreement.

The long-term portion is shown under Other (Other long Term assets) (Note 14).

- (2) This amount corresponds to the cost (net of amortization) of the mandatory reserve paid to the Central Bank of Chile and disbursements incurred for foreign loans obtained by the Company to finance its investment plan.
- (3) Corresponds to the short-term portion to be amortized due to changes in the actuarial hypotheses and in the discount rate, as described in Note 3, and for the concept of loans to employees as indicated in Note 14 (3).

**9. Information regarding purchase commitment and sales commitment transactions (agreements):**

| Code | Dates          |                | Counterparty                         | Original<br>currency | Subscription<br>value ThCh\$ | Rate  | Final<br>Value<br>ThCh\$ | Instrument<br>Identification | Book<br>Value<br>ThCh\$ |
|------|----------------|----------------|--------------------------------------|----------------------|------------------------------|-------|--------------------------|------------------------------|-------------------------|
|      | Inception      | End            |                                      |                      |                              |       |                          |                              |                         |
| CRV  | Mar<br>28,2006 | Apr<br>04,2006 | BANCO DEL<br>ESTADO DE<br>CHILE      | \$                   | 106.345                      | 0,36% | 106.434                  | BCP-0800708                  | 106.383                 |
| CRV  | Mar<br>28,2006 | Apr<br>04,2006 | BANCO DEL<br>ESTADO DE<br>CHILE      | \$                   | 1.553.497                    | 0,36% | 1.554.802                | BCP-0800614                  | 1.554.056               |
| CRV  | Mar<br>29,2006 | Apr<br>05,2006 | BANCO DE<br>CREDITO E<br>INVERSIONES | \$                   | 2.000.000                    | 0,39% | 2.001.820                | BCP-0800407                  | 2.000.520               |
| CRV  | Mar<br>27,2006 | Apr<br>06,2006 | BANCO DE<br>CREDITO E<br>INVERSIONES | \$                   | 1.300.000                    | 0,39% | 1.301.690                | BCP-800708                   | 1.300.676               |
| CRV  | Mar<br>30,2006 | Apr<br>06,2006 | BANCO DEL<br>ESTADO DE<br>CHILE      | \$                   | 2.080.318                    | 0,36% | 2.082.065                | BCP0800907                   | 2.080.568               |
| CRV  | Mar<br>30,2006 | Apr<br>06,2006 | CITIBANK                             | \$                   | 972.295                      | 0,38% | 973.157                  | BCP-0800709                  | 972.418                 |
| CRV  | Mar<br>30,2006 | Apr<br>06,2006 | CITIBANK                             | \$                   | 25.969                       | 0,38% | 25.992                   | BCP-0800907                  | 25.972                  |
| CRV  | Mar<br>31,2006 | Apr<br>10,2006 | BBVA                                 | \$                   | 1.000.000                    | 0,32% | 1.001.067                | PCBC09506                    | 1.000.000               |
| CRV  | Mar<br>28,2006 | Apr<br>12,2006 | BANCO DE<br>CREDITO E<br>INVERSIONES | \$                   | 3.000.000                    | 0,39% | 3.005.850                | BCP-800708                   | 3.001.170               |
| CRV  | Mar<br>28,2006 | Apr<br>12,2006 | BANCO DE<br>CREDITO E<br>INVERSIONES | \$                   | 200.000                      | 0,39% | 200.390                  | BCP-800708                   | 200.078                 |
| CRV  | Mar<br>30,2006 | Apr<br>12,2006 | HSBC BANK                            | \$                   | 1.064.348                    | 0,36% | 1.066.008                | BCP-0800708                  | 1.064.476               |
| CRV  | Mar<br>30,2006 | Apr<br>12,2006 | HSBC BANK                            | \$                   | 4.435.652                    | 0,36% | 4.442.572                | BCP-0800614                  | 4.436.184               |
| CRV  | Mar<br>31,2006 | Apr<br>19,2006 | BANCO DEL<br>ESTADO DE<br>CHILE      | \$                   | 8.764.220                    | 0,37% | 8.784.757                | BCP-0800708                  | 8.764.220               |
| CRV  | Mar<br>31,2006 | Apr<br>19,2006 | BANCO DEL<br>ESTADO DE<br>CHILE      | \$                   | 720.972                      | 0,37% | 722.661                  | BCP-0800709                  | 720.972                 |
| CRV  | Mar<br>31,2006 | Apr<br>19,2006 | BANCO<br>SANTADER<br>SANTIAGO        | \$                   | 4.953.590                    | 0,38% | 4.965.512                | PDBC200606                   | 4.953.590               |
| CRV  | Mar<br>31,2006 | Apr<br>19,2006 | BANCO<br>SANTADER<br>SANTIAGO        | \$                   | 346.410                      | 0,38% | 347.244                  | BCD0500108                   | 346.410                 |
| CRV  |                |                |                                      | \$                   | 3.500.000                    | 0,40% | 3.512.133                | BCP-0800708                  | 3.500.000               |

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|     |                |                |                                      |    |           |       |           |             |           |
|-----|----------------|----------------|--------------------------------------|----|-----------|-------|-----------|-------------|-----------|
|     | Mar<br>31,2006 | Apr<br>26,2006 | BANCO DE<br>CREDITO E<br>INVERSIONES |    |           |       |           |             |           |
| CRV | Mar<br>31,2006 | Apr<br>26,2006 | HSBC BANK                            | \$ | 737.991   | 0,36% | 740.294   | BCP0800614  | 737.991   |
| CRV | Mar<br>31,2006 | Apr<br>26,2006 | HSBC BANK                            | \$ | 962.009   | 0,36% | 965.010   | BCP0800907  | 962.009   |
| CRV | Mar<br>28,2006 | Apr<br>04,2006 | BANCO DEL<br>ESTADO DE<br>CHILE      | UF | 40.157    | 0,36% | 40.191    | CERO-010212 | 40.171    |
| CRV | Mar<br>29,2006 | Apr<br>05,2006 | BANCO DEL<br>ESTADO DE<br>CHILE      | UF | 1.005.473 | 0,36% | 1.006.318 | PRC-5D0999  | 1.005.714 |
| CRV | Mar<br>29,2006 | Apr<br>05,2006 | BANCO DEL<br>ESTADO DE<br>CHILE      | UF | 453.395   | 0,36% | 453.776   | PRC-15D0597 | 453.504   |
| CRV | Mar<br>29,2006 | Apr<br>05,2006 | BANCO DEL<br>ESTADO DE<br>CHILE      | UF | 41.133    | 0,36% | 41.168    | CERO-011213 | 41.143    |
| CRV | Mar<br>29,2006 | Apr<br>05,2006 | DEUTSCHE<br>BANK                     | UF | 698.596   | 0,38% | 699.215   | PRC-5D0201  | 698.773   |
| CRV | Mar<br>29,2006 | Apr<br>05,2006 | DEUTSCHE<br>BANK                     | UF | 395.291   | 0,38% | 395.641   | PRC-1D1197  | 395.391   |
| CRV | Mar<br>29,2006 | Apr<br>05,2006 | DEUTSCHE<br>BANK                     | UF | 6.114     | 0,38% | 6.119     | PRC-1B0598  | 6.116     |
| CRV | Mar<br>30,2006 | Apr<br>06,2006 | BANCO DEL<br>ESTADO DE<br>CHILE      | UF | 6.695     | 0,36% | 6.701     | CERO-016613 | 6.696     |
| CRV | Mar<br>30,2006 | Apr<br>06,2006 | BANCO DEL<br>ESTADO DE<br>CHILE      | UF | 212.986   | 0,36% | 213.165   | PRC-7D0502  | 213.012   |
| CRV | Mar<br>30,2006 | Apr<br>06,2006 | CITIBANK                             | UF | 1.735     | 0,38% | 1.737     | CERO-010506 | 1.735     |
| CRV | Mar<br>31,2006 | Apr<br>07,2006 | BANCO BICE                           | UF | 12.303    | 0,36% | 12.313    | CERO-010108 | 12.303    |
| CRV | Mar<br>31,2006 | Apr<br>07,2006 | BANCO BICE                           | UF | 26.238    | 0,36% | 26.260    | CERO-010208 | 26.238    |
| CRV | Mar<br>31,2006 | Apr<br>07,2006 | BANCO BICE                           | UF | 77.280    | 0,36% | 77.345    | CERO-010308 | 77.280    |
| CRV | Mar<br>31,2006 | Apr<br>07,2006 | BANCO BICE                           | UF | 196.410   | 0,36% | 196.575   | CERO-010606 | 196.410   |
| CRV | Mar<br>31,2006 | Apr<br>07,2006 | BANCO BICE                           | UF | 26.740    | 0,36% | 26.762    | CERO-010706 | 26.740    |
| CRV | Mar<br>31,2006 | Apr<br>07,2006 | BANCO BICE                           | UF | 151.413   | 0,36% | 151.540   | CERO-010706 | 151.413   |
| CRV | Mar<br>31,2006 | Apr<br>07,2006 | BANCO BICE                           | UF | 445.332   | 0,36% | 445.706   | CERO-010706 | 445.332   |
| CRV | Mar<br>31,2006 | Apr<br>07,2006 | BANCO BICE                           | UF | 344.526   | 0,36% | 344.815   | CERO-011107 | 344.526   |
| CRV | Mar<br>31,2006 | Apr<br>07,2006 | BANCO BICE                           | UF | 2.566     | 0,36% | 2.568     | PRC-1A0197  | 2.566     |

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|     |                |                |                                 |    |           |       |           |             |           |
|-----|----------------|----------------|---------------------------------|----|-----------|-------|-----------|-------------|-----------|
| CRV | Mar<br>31,2006 | Apr<br>07,2006 | BANCO BICE                      | UF | 151.366   | 0,36% | 151.493   | PRC-0D0597  | 151.366   |
| CRV | Mar<br>31,2006 | Apr<br>07,2006 | BANCO BICE                      | UF | 61.175    | 0,36% | 61.226    | PRC-01D0898 | 61.175    |
| CRV | Mar<br>31,2006 | Apr<br>07,2006 | BANCO BICE                      | UF | 285.600   | 0,36% | 285.840   | PRC-4D0800  | 285.600   |
| CRV | Mar<br>31,2006 | Apr<br>07,2006 | BANCO BICE                      | UF | 98.790    | 0,36% | 98.873    | PRC-4D0801  | 98.790    |
| CRV | Mar<br>31,2006 | Apr<br>07,2006 | BANCO BICE                      | UF | 109.004   | 0,36% | 109.096   | PRC-5D0896  | 109.004   |
| CRV | Mar<br>31,2006 | Apr<br>07,2006 | BANCO BICE                      | UF | 54.324    | 0,36% | 54.370    | PRC-5D0996  | 54.324    |
| CRV | Mar<br>31,2006 | Apr<br>07,2006 | BANCO BICE                      | UF | 1.132.905 | 0,36% | 1.133.857 | PRC-6D0294  | 1.132.905 |
| CRV | Mar<br>31,2006 | Apr<br>07,2006 | BANCO BICE                      | UF | 324.027   | 0,36% | 324.299   | PRC-6D0394  | 324.027   |
| CRV | Mar<br>31,2006 | Apr<br>10,2006 | DEUTSCHE<br>BANK                | UF | 246.920   | 0,36% | 247.216   | PRC-1D0896  | 246.920   |
| CRV | Mar<br>31,2006 | Apr<br>10,2006 | DEUTSCHE<br>BANK                | UF | 1.875.045 | 0,36% | 1.877.295 | PRC-4D0402  | 1.875.045 |
| CRV | Mar<br>31,2006 | Apr<br>10,2006 | DEUTSCHE<br>BANK                | UF | 336.350   | 0,36% | 336.754   | PRC-7B0993  | 336.350   |
| CRV | Mar<br>31,2006 | Apr<br>10,2006 | DEUTSCHE<br>BANK                | UF | 212.563   | 0,36% | 212.818   | PRC-4D0900  | 212.563   |
| CRV | Mar<br>31,2006 | Apr<br>10,2006 | DEUTSCHE<br>BANK                | UF | 560.447   | 0,36% | 561.120   | PRC-7D0993  | 560.447   |
| CRV | Mar<br>31,2006 | Apr<br>10,2006 | DEUTSCHE<br>BANK                | UF | 255.038   | 0,36% | 255.344   | PRC-4D1100  | 255.038   |
| CRV | Mar<br>31,2006 | Apr<br>10,2006 | DEUTSCHE<br>BANK                | UF | 222.872   | 0,36% | 223.139   | PRC-4D1201  | 222.872   |
| CRV | Mar<br>31,2006 | Apr<br>10,2006 | DEUTSCHE<br>BANK                | UF | 472.725   | 0,36% | 473.292   | PRC-1D0200  | 472.725   |
| CRV | Mar<br>31,2006 | Apr<br>10,2006 | DEUTSCHE<br>BANK                | UF | 294.774   | 0,36% | 295.128   | PRC-4D0601  | 294.774   |
| CRV | Mar<br>31,2006 | Apr<br>10,2006 | DEUTSCHE<br>BANK                | UF | 423.268   | 0,36% | 423.776   | PRC-4D0101  | 423.268   |
| CRV | Mar<br>31,2006 | Apr<br>19,2006 | BANCO DEL<br>ESTADO DE<br>CHILE | UF | 13.946    | 0,37% | 13.979    | CERO-010109 | 13.946    |
| CRV | Mar<br>31,2006 | Apr<br>19,2006 | BANCO DEL<br>ESTADO DE<br>CHILE | UF | 862       | 0,37% | 864       | CERO-011107 | 862       |
| CRV | Mar<br>31,2006 | Apr<br>19,2006 | CITIBANK                        | UF | 14.799    | 0,38% | 14.835    | PRC-1B1097  | 14.799    |
| CRV | Mar<br>31,2006 | Apr<br>19,2006 | CITIBANK                        | UF | 14.864    | 0,38% | 14.900    | PRC-1B1097  | 14.864    |
| CRV | Mar<br>31,2006 | Apr<br>19,2006 | CITIBANK                        | UF | 130.921   | 0,38% | 131.236   | PRC-4D0899  | 130.921   |
| CRV | Mar<br>31,2006 | Apr<br>19,2006 | CITIBANK                        | UF | 355.448   | 0,38% | 356.303   | PRC-4D0800  | 355.448   |
| CRV |                |                | CITIBANK                        | UF | 426.186   | 0,38% | 427.212   | PRC-4D1000  | 426.186   |



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|              | Mar<br>31,2006 | Apr<br>19,2006 |          |    |                   |       |                   |            |                   |
|--------------|----------------|----------------|----------|----|-------------------|-------|-------------------|------------|-------------------|
| CRV          | Mar<br>31,2006 | Apr<br>19,2006 | CITIBANK | UF | 216.997           | 0,38% | 217.519           | PRC-5C0796 | 216.997           |
| CRV          | Mar<br>31,2006 | Apr<br>19,2006 | CITIBANK | UF | 233.734           | 0,38% | 234.297           | PRC-5D1294 | 233.734           |
| CRV          | Mar<br>31,2006 | Apr<br>19,2006 | CITIBANK | UF | 544.681           | 0,38% | 545.992           | PRC-5D0596 | 544.681           |
| CRV          | Mar<br>31,2006 | Apr<br>19,2006 | CITIBANK | UF | 62.370            | 0,38% | 62.520            | PRC-450798 | 62.370            |
| <b>Total</b> |                |                |          |    | <b>51.000.000</b> |       | <b>51.091.966</b> |            | <b>51.004.757</b> |

**10. Property, plant and equipment:**

The detail of property, plant and equipment is as follows:

| Description   | 2006                                  |   | 2005                                  |   |
|---|---------------------------------------|---|---------------------------------------|---|
|   | Accumulated<br>depreciation<br>ThCh\$ | Gross prop.,<br>plant<br>and<br>equipment<br>ThCh\$ | Accumulated<br>depreciation<br>ThCh\$ | Gross prop.,<br>plant<br>and<br>equipment<br>ThCh\$ |
| <b>Land</b>   | -                                     | <b>27,152,139</b>                                   | -                                     | <b>27,207,038</b>                                   |
| <b>Building and improvements</b>                            | <b>86,260,802</b>                     | <b>197,290,304</b>                                  | <b>82,666,970</b>                     | <b>196,073,603</b>                                  |
| <b>Machinery and equipment</b>                              | <b>2,226,959,891</b>                  | <b>3,241,169,114</b>                                | <b>2,085,602,340</b>                  | <b>3,224,401,612</b>                                |
| Central office telephone equipment                          | 1,047,328,353                         | 1,271,801,541                                       | 988,438,797                           | 1,263,552,045                                       |
| External plant  | 825,211,563                           | 1,495,855,968                                       | 769,203,576                           | 1,490,433,976                                       |
| Subscribers equipment                                       | 318,140,674                           | 436,384,202   | 291,919,011                           | 432,765,568   |
| General equipment   | 36,279,301                            | 37,127,403  | 36,040,956                            | 37,650,023  |
| <b>Other Property, Plant and Equipment</b>                  | <b>155,772,204</b>                    | <b>269,320,422</b>                                  | <b>147,425,599</b>                    | <b>257,738,238</b>                                  |
| Office furniture and equipment                              | 82,606,213                            | 105,896,501   | 79,020,672                            | 106,086,721   |
| Projects, work in progress and their materials<br>(2)       | -                                     | 71,928,517  | -                                     | 64,683,867  |
| Leased assets (1)   | 57,079                                | 491,202   | 52,901                                | 503,675   |
| Property, plant and equipment temporarily out<br>of service | 5,712,803                             | 6,521,310   | 12,502,618                            | 15,210,844  |
| Software  | 66,457,072                            | 83,336,836  | 55,002,585                            | 70,227,241  |
| Other   | 939,037                               | 1,146,056   | 846,823                               | 1,025,890   |
| <b>Technical revaluation Circular 550</b>                   | <b>10,897,690</b>                     | <b>9,714,954</b>                                    | <b>10,959,910</b>                     | <b>9,746,443</b>                                    |
| <b>Total</b>  | <b>2,479,890,587</b>                  | <b>3,744,646,933</b>                                | <b>2,326,654,819</b>                  | <b>3,715,166,934</b>                                |

(1) Leased assets consider a gross value of ThCh \$491,202 for the concept of buildings for 2006 and 2005 with accumulated depreciation of ThCh\$57,079 and ThCh\$48,924 for 2006 and 2005 respectively.

(2) Up to December 31, 2002, works in progress included capitalization of the related borrowing costs, as per Technical Bulletin No. 31 of the Chilean Association of Accountants, and therefore, the gross property, plant and equipment balance includes interest in the amount of ThCh\$192,834,509. Accumulated depreciation for this interest amounts to ThCh\$126,952,451 and ThCh\$114,465,719 for 2006 and 2005, respectively. The depreciation charge of the period amounted to ThCh\$3,108,572 in 2006 and ThCh\$3,131,660 in 2005.

A depreciation charge for the period amounting to ThCh\$47,498,409 and ThCh\$47,660,142 for 2006 and 2005, respectively, was recorded as operating cost, and a depreciation charge of ThCh\$1,950,188 for 2006 and ThCh\$2,544,118 for 2005 as administrative and selling cost. Depreciation of property, plant and equipment that is temporarily out of service is made up mainly of telephone equipment under repair and incurred depreciation amounting to ThCh\$339,349 and ThCh\$842,823 in 2006 and 2005, which is classified under Other Non-operating

Expenses (note 22b).

The detail by item of the technical revaluation is as follows:

| Description               | Net<br>Balance     | Accumulated<br>Depreciation | Gross property,<br>plant and<br>equipment<br>2006 | Gross property,<br>plant and<br>equipment<br>2005 |
|---------------------------|--------------------|-----------------------------|---|---|
|                           | ThCh\$             | ThCh\$                      | ThCh\$  | ThCh\$  |
| Land                      | (505,034)          | -                           | (505,034)   | (505,034)   |
| Building and improvements | (844,281)          | (4,001,676)                 | (4,845,957)                                       | (4,846,216)                                       |
| Machinery and equipment   | 166,579            | 14,899,366                  | 15,065,945  | 15,097,693  |
| <b>Total</b>              | <b>(1,182,736)</b> | <b>10,897,690</b>           | <b>9,714,954</b>                                  | <b>9,746,443</b>                                  |

Depreciation of the technical reappraisal surplus for the period of ThCh\$(14,434) and ThCh\$(4,974) for 2006 and 2005, respectively.

Gross property, plant and equipment includes assets that have been totally depreciated in the amount of ThCh\$1,124,057,629 in 2006 and ThCh\$949,782,394 in 2005, which include ThCh\$12,930,673 and ThCh\$12,123,622, respectively, from the reappraisals mentioned in Circular No. 550.

**11. Investments in Related Companies:**

The detail of investments in related companies is as follows:

| Taxp. No.    | Company                                    | Currency          |                        | Number of shares | Percentage participation |       | Equity of the companies |             | Net income (loss) of the companies |           |
|--------------|--|-------------------|------------------------|------------------|--------------------------|-------|-------------------------|-------------|------------------------------------|-----------|
|              |  | Country of origin | controlling investment |                  | 2006                     | 2005  | 2006                    | 2005        | 2006                               | 2005      |
|              |  |                   |                        |                  | %                        | %     | ThCh\$                  | ThCh\$      | ThCh\$                             | ThCh\$    |
| Foreign      | TBS Celular Participación S.A. (1) (3) (4) | Brazil            | Dollar                 | 48.950.000       | 2,61                     | 2,61  | 149.306.146             | 168.934.493 | (1.417.723)                        | 176.650   |
| 96,895,220-K | Atento Chile S.A. (4)                      | Chile             | Pesos                  | 3.049.998        | 28,84                    | 28,84 | 14.077.278              | 14.283.560  | 1.592.925                          | 1.400.933 |
| 96,922,950-1 | Empresa de Tarjetas Inteligentes S.A. (2)  | Chile             | Pesos                  | -                | -                        | 20,00 | -                       | (106.066)   | -                                  | (38.318)  |

**Total**

- (1) The Company records its investment in TBS Celular using the equity method since it exercises significant influence through the business group to which it belongs, as established in paragraph N° 4 of Circular N° 1,179 issued by the Superintendency of Securities and Insurance and ratified in Title II of Circular N° 1,697. Although Telefónica CTC Chile only has a 2.61% direct participation in TBS Celular, its Parent Company, Telefónica España directly and indirectly has a percentage exceeding 20% ownership of the capital stock of that company.
- (2) The Extraordinary Shareholders Meeting agreed to the dissolution of Empresa de Tarjetas Inteligentes S.A. During September 2005 the Chilean Internal Revenue Service authorized the closing of this company.
- (3) As of the date of these financial statements there are no liabilities for hedge instruments assigned to foreign investments. The Company has the intention of reinvesting net income from foreign investments on a permanent basis, therefore there is no net income that is potentially remittable.
- (4) The proportional equity value as of May 31, 2005 and 2006 was recognized on the basis of financial statements that were not subject to a limited review.

**12. Goodwill:**

The detail of goodwill is as follows:

| Taxpayer<br>No. | Company                              | Year | 2006   |                                  | 2005   |                                  |
|-----------------|--------------------------------------|------|--|----------------------------------|--|----------------------------------|
|                 |                                      |      | Amount<br>amortized<br>in the period<br>ThCh\$ | Balance of<br>Goodwill<br>ThCh\$ | Amount<br>amortized<br>in the period<br>ThCh\$ | Balance of<br>Goodwill<br>ThCh\$ |
|                 | TBS Celular Participación<br>S.A.    | 2001 | 45,852   | 2,432,721                        | 45,852   | 2,618,679                        |
| 96,887,420-9    | Globus 120 S.A.                      | 1998 | 282,891  | 14,406,633                       | 282,891  | 15,553,911                       |
| 78,703,410-1    | Tecnonáutica S.A. (1)                | 1999 | 761,341  | -                                | 37,433   | 873,435                          |
| 96,834,320-3    | Telefónica Internet Empresas<br>S.A. | 1999 | 23,120   | 445,701                          | 23,120   | 539,464                          |
|                 | <b>Total</b>                         |      | <b>1,113,204</b>                               | <b>17,285,055</b>                | <b>389,296</b>                                 | <b>19,585,489</b>                |

Goodwill amortization periods have been determined taking into account aspects such as the nature and characteristics of the business and estimated period of return of investment.

- (1) As indicated in Note 2d) No. 1 as a product of the sale made on January 26, 2006, the Board of Directors of Telefónica Internet Empresas S.A. agreed to sell the shares of Tecnonáutica S.A. to Telefónica CTC Chile S.A. This sale was made at book value, not considering goodwill in the price, which required the extraordinary recognition of, the total balance of goodwill as of that date.

**13. Intangibles:**

The detail of Intangibles is as follows:

| Description                                | 2006<br>ThCh\$    | 2005<br>ThCh\$    |
|--|-------------------|-------------------|
| Underwater cable rights (gross)            | 36,940,539        | 35,783,150        |
| Accumulated amortization, previous period  | (7,354,073)       | (5,121,997)       |
| Amortization for the period                | (436,027)         | (461,556)         |
| Licenses (Software) (gross)                | 11,791,191        | 11,474,466        |
| Accumulated amortization, previous periods | (4,456,029)       | (1,921,652)       |
| Amortization for the period                | (729,870)         | (392,334)         |
| <b>Total Net Intangibles</b>               | <b>35,755,731</b> | <b>39,360,077</b> |

**14. Other non-current assets:**

The detail of Other is as follows:

| Description  | 2006<br>ThCh\$    | 2005<br>ThCh\$    |
|--|-------------------|-------------------|
| Deferred disbursement for obtaining external financing (see note 8(2)) (1) | 1,129,527         | 1,173,386         |
| Deferred union contract bonus (see note 8(1))                              | 51,210            | 656,016           |
| Bond issue expenses (see note 25)  | 759,602           | 376,714           |
| Bond discount (see note 25)  | 1,262,956         | 221,345           |
| Securities deposits  | 137,194           | 137,349           |
| Deferred charge due to change in actuarial estimations (2)                 | 9,687,922         | 8,395,693         |
| Deferred staff severance indemnities (3)                                   | 4,555,864         | 5,592,073         |
| Deferred foreign exchange insurance premiums to be amortized               | -                 | 37,871            |
| Others   | 77,357            | 168,174           |
| <b>Total</b>   | <b>17,661,632</b> | <b>16,758,621</b> |

- (1) This amount corresponds to the cost (net of amortizations) of the mandatory reserve paid to the Chilean Central Bank and disbursements incurred for foreign loans obtained by the Company, to finance its investment plan.
- (2) In light of the new contractual conditions derived from the organizational evolution experienced by the Company, there have been a series of studies that, beginning in 2004, allowed, the modification of the variable for future years of service of employees within the basis for calculating staff severance indemnities. After concluding these studies, in 2005 other estimations were incorporated such as mortality of employees and futures salary increases and includes the rate change mentioned in Note 3 b i) for 2006, all determined on the basis of actuarial calculations, as established in Technical Bulletin No. 8 of the Chilean Association of Accountants.

The difference at the beginning of the year as a result of changes in the actuarial estimates constitutes actuarial gains or losses, which are deferred and amortized during the years of average future permanence remaining for the employees that will receive the benefit (see Note 2s).

- (2) In conformity with the union agreements between the Company and its employees, loans were granted to employees, the amounts and conditions of which were based, among other aspects, on the accrued balances of staff severance indemnities when they were granted.

The staff severance indemnities provision has been recorded in part at its current value, deferring and amortizing this effect over the years of average remaining service life of employees that subscribe to the benefit. The loan is presented under Other Long-term Receivables.

**15. Short -term obligations with banks and financial institutions:**

The breakdown of short-term obligations with banks and financial institutions is as follows:

| Taxp. No.    | Bank or financial institution               | US\$             |                   | U.F.           |                | Ch\$   |                  | TOTAL            |                   |
|--------------|---|------------------|-------------------|----------------|----------------|--------|------------------|------------------|-------------------|
|              |   | 2006             | 2005              | 2006           | 2005           | 2006   | 2005             | 2006             | 2005              |
|              | <b>Short-term</b>                           | ThCh\$           | ThCh\$            | ThCh\$         | ThCh\$         | ThCh\$ | ThCh\$           | ThCh\$           | ThCh\$            |
| 97,030,000-7 | BANCO ESTADO                                | -                | -                 | -              | -              | -      | 9.876.927        | -                | 9.876.927         |
|              | Total                                       | -                | -                 | -              | -              | -      | <b>9.876.927</b> | -                | <b>9.876.927</b>  |
|              | Outstanding principal                       | -                | -                 | -              | -              | -      | <b>9.650.935</b> | -                | <b>9.650.935</b>  |
|              | Average annual interest rate                | -                | -                 | -              | -              | -      | 3,00%            | -                | 3,00%             |
|              | <b>Current maturities of long-term debt</b> |                  |                   |                |                |        |                  |                  |                   |
| 97,015,000-5 | BANCO SANTANDER SANTIAGO (4)                | -                | -                 | 689.552        | 460.488        | -      | -                | 689.552          | 460.488           |
| Foreign      | CALYON NEW YORK BRANCH Y                    |                  |                   |                |                |        |                  |                  |                   |
| 97,008,000-7 | OTROS                                       | 140.227          | 116.932           | -              | -              | -      | -                | 140.227          | 116.932           |
| Foreign      | CITIBANK (2)                                | 555.778          | -                 | -              | -              | -      | -                | 555.778          | -                 |
| Foreign      | BBVA BANCOMER Y                             |                  |                   |                |                |        |                  |                  |                   |
| Foreign      | OTROS (3)                                   | 621.857          | 1.524.903         | -              | -              | -      | -                | 621.857          | 1.524.903         |
| Foreign      | BANCO BILBAO VIZCAYA ARGENTARIA             | -                | 15.339.192        | -              | -              | -      | -                | -                | 15.339.192        |
|              | Total                                       | <b>1.317.862</b> | <b>16.981.027</b> | <b>689.552</b> | <b>460.488</b> | -      | -                | <b>2.007.414</b> | <b>17.441.515</b> |
|              | Outstanding principal                       | -                | <b>15.252.077</b> | -              | -              | -      | -                | -                | <b>15.252.077</b> |



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|                              |       |       |       |       |   |   |       |       |
|------------------------------|-------|-------|-------|-------|---|---|-------|-------|
| Average annual interest rate | 5,17% | 3,04% | 2,32% | 1,55% | - | - | 4,69% | 3,00% |
|------------------------------|-------|-------|-------|-------|---|---|-------|-------|

|  |         |              |         |          |
|--|---------|--------------|---------|----------|
| Percentage of obligations in foreign currency: | 65,65 % | for 2006 and | 62,16 % | for 2005 |
| Percentage of obligations in local currency:   | 34,35 % | for 2006 and | 37,84 % | for 2005 |

**16. Long-term obligations with banks and financial institutions :**

Long-term obligations with banks and financial institutions:

| Taxp. No.    | Bank or<br>Financial<br>Institution             | Currency                  | Years to maturity for long-term portion |                   |                    |                   | Long-term                           | Average                      | Long-t                           |
|--------------|---|---------------------------|---|-------------------|--------------------|-------------------|-------------------------------------|------------------------------|----------------------------------|
|              |   | or<br>Indexation<br>Index | 1 to 2                                  | 2 to 3            | 3 to 5             | 5 a 10            | portion<br>as of<br>Mar 31,<br>2005 | annual<br>interest<br>rate % | portio<br>as of<br>Mar 3<br>2005 |
|              |   |                           | ThCh\$                                  | ThCh\$            | ThCh\$             | ThCh\$            | ThCh\$                              |                              | ThCh\$                           |
|              | <b>LOANS IN<br/>DOLLARS</b>                     |                           |   |                   |                    |                   |                                     |                              |                                  |
| Foreign      | CALYON<br>NEW YORK<br>BRANCH Y<br>OTROS (1)     | US\$                      | -                                       | -                 | 105.236.000        | -                 | 105.236.000                         | Libor +<br>0,40%             | 122.016                          |
| Foreign      | BBVA<br>BANCOMER<br>Y OTROS (3)                 | US\$                      | -                                       | -                 | -                  | 78.927.000        | 78.927.000                          | Libor +<br>0,375%            | 183.024                          |
| 97,008,000-7 | BANCO<br>CITIBANK (2)                           | US\$                      | -                                       | 78.927.000        | -                  | -                 | 78.927.000                          | Libor +<br>0,35%             |                                  |
|              | <b>SUBTOTAL</b>                                 |                           | <b>-</b>                                | <b>78.927.000</b> | <b>105.236.000</b> | <b>78.927.000</b> | <b>263.090.000</b>                  | <b>5,17%</b>                 | <b>305.041</b>                   |
|              | <b>LOANS IN<br/>UNIDADES<br/>DE<br/>FOMENTO</b> |                           |   |                   |                    |                   |                                     |                              |                                  |
| 97,015,000-5 | BANCO<br>SANTANDER<br>SANTIAGO<br>(4)           | UF                        | -                                       | -                 | 63.690.171         | -                 | 63.690.171                          | Tab 360<br>+ 0.45%           | 63.662                           |
|              | <b>TOTAL</b>                                    |                           | <b>-</b>                                | <b>78.927.000</b> | <b>168.926.171</b> | <b>78.927.000</b> | <b>326.780.171</b>                  | <b>4,69%</b>                 | <b>368.703</b>                   |
|              | Percentage of<br>obligations in<br>foreign      | 80,51%                    | en                                      | 82,73%            | en                 | 2005              |                                     |                              |                                  |
|              |   |                           | 2006 y                                  |                   |                    |                   |                                     |                              |                                  |

currency:

Percentage of obligations in local currency: 19,49% en 2006 y 17,27% en 2005

(1) In December 2004, the Company renegotiated this loan, extending its due date from January and August 2005 to December 2009, in addition to changing the agent bank, that it was the BilbaoViscaya Argentaria Bank.

(2) In May 2005, the Company renegotiated this loan, extending its due date from April 2006 and April 2007 to December 2008, in addition to changing the agent bank, that it was the ABN Amro Bank.

(3) In November 2005, the Company renegotiated this loan, extending its due date from April 2006, April 2007 and April 2008 to June 2011, in addition to changing the agent bank, that is was the ABN Amro Bank.

(4) In April 2005, the Company renegotiated this loan, extending its maturity date from April 2008 to April 2010 and reduce the interest rate to TAB 360 + 0.45%

**17. Obligations with the Public:****a) Commercial paper:**

On January 27, 2003 and May 12, 2004 Telefónica CTC Chile registered a commercial paper line in the securities registry, the inspection numbers of which are 5 and 15, respectively. The maximum amount of the line is ThCh\$35,000,000, and placements charged to this line may not exceed that amount. The term of this line will be 10 years from the date of registration with the Superintendency of Securities and Insurance. The interest rate will be defined upon each issuance of these commercial papers.

On May 12, 2004, there was a placement in two series (C and D) for ThCh\$35,000,000 of the same type of financial instrument. The placement agent was Inversiones Boston Corredores de Bolsa.

On January 18, 2005, a Series E placement of the same type of instrument was made in the amount of ThCh\$12,000,000. The placement agent was Scotiabank Sudamericano Corredores de Bolsa.

On October 25, 2005, a Series G and H placement of the same type of instrument was made in the amount of ThCh\$35,000,000. The placement agent was Scotiabank Sudamericano Corredores de Bolsa.

On March 21, 2006, a Series I placement of the same type of instrument was made in the amount of ThCh\$12,000,000. The placement agent was Inversiones Boston C.B..

The details of these transactions are described below:

| Registration or identification number of the instrument | Series | Current                      | Bond readjustment   | Interest rate % | Final Maturity | Accounting value  |                   | Placement in Chile or abroad |
|---|--------|------------------------------|---------------------|-----------------|----------------|-------------------|-------------------|------------------------------|
|   |        | nominal amount placed ThCh\$ | unit ThCh\$         |                 |                | 2006 ThCh\$       | 2005 ThCh\$       |                              |
| Short-term commercial paper                             |        |                              |                     |                 |                |                   |                   |                              |
| 005   | C      | 17,500,000                   | Ch\$ non-adjustable | 0.2257          | Apr 5, 2005    | -                 | 18,214,709        | Chile                        |
| 005   | D      | 17,500,000                   | Ch\$ non-adjustable | 0.2286          | May 5, 2005    | -                 | 18,174,062        | Chile                        |
| 005   | E      | 12,000,000                   | Ch\$ non-adjustable | 0.3100          | Oct 13, 2005   | -                 | 12,248,422        | Chile                        |
| 005   | G      | 17,500,000                   | Ch\$ non-adjustable | 0.5100          | Apr 20, 2006   | 17,443,666        | -                 | Chile                        |
| 005   | H      | 17,500,000                   | Ch\$ non-adjustable | 0.5100          | Apr 27, 2006   | 17,422,728        | -                 | Chile                        |
| 015   | I      | 12,000,000                   | Ch\$ non-adjustable | 0.4800          | Dec 06, 2006   | 11,539,171        | -                 | Chile                        |
|   |        |                              |                     | <b>Total</b>    |                | <b>46,405,565</b> | <b>48,637,193</b> |                              |



**17. Obligations with the Public , continued :****b) Bonds**

The detail of obligations with the public for bond issues, classified as short and long-term is as follows:

| Registration<br>number or<br>identification<br>of the<br>instrument | Series                  | Nominal<br>Amount<br>of issue | Readjustment<br>unit<br>for bond | Nominal<br>annual<br>interest<br>rate<br><br>% | Final<br>maturity | Frequency           |               | Par value         |                   |
|---|-------------------------|-------------------------------|----------------------------------|--|-------------------|---------------------|---------------|-------------------|-------------------|
|   |                         |                               |                                  |  |                   | Interest<br>payment | Amortizations | 2006<br>ThCh\$    | 2006<br>ThCh\$    |
| <b>Short-term portion of long-term bonds</b>                        |                         |                               |                                  |  |                   |                     |               |                   |                   |
| 143,27,06,91  | <b>F</b>                | 71.429                        | U.F.                             | 6,000  | Apr, 2016         | Semi-annual         | Semi-annual   | 1.647.842         | 1.647.842         |
| 281,20,12,01  | <b>L (1)</b>            | -                             | U.F.                             | 3,750  | Oct, 2012         | Semi-annual         | Maturity      | 10.993            | 10.993            |
| Issued in New York  | <b>Yankee Bonds</b>     | 49.603.000                    | US\$                             | 7,625  | Jul, 2006         | Semi-annual         | Maturity      | 26.514.718        | 26.514.718        |
| Issued in New York  | <b>Yankee Bonds</b>     | -                             | US\$                             | 8,375  | Jan, 2006         | Semi-annual         | Maturity      | -                 | 97.400.000        |
| Total   |                         |                               |                                  |  |                   |                     |               | <b>28.173.553</b> | <b>99.500.000</b> |
| <b>Long-term bonds</b>  |                         |                               |                                  |  |                   |                     |               |                   |                   |
| 143,27,06,91  | <b>F</b>                | 678.572                       | U.F.                             | 6,000  | Apr, 2016         | Semi-annual         | Semi-annual   | 12.157.064        | 13.400.000        |
| 281,20,12,01  | <b>L (1)</b>            | 3.000.000                     | U.F.                             | 3,750  | Oct, 2012         | Semi-annual         | Maturity      | 53.746.980        | 53.746.980        |
| Issued in New York  | <b>Yankee Bonds (b)</b> | -                             | US\$                             | 7,625  | Jul, 2006         | Semi-annual         | Maturity      | -                 | 30.200.000        |
| Total   |                         |                               |                                  |  |                   |                     |               | <b>65.904.044</b> | <b>43.600.000</b> |

**17. Obligations with the Public**, continued:

**b) Bonds**, continued:

1) On March 29, 2006, the Company placed bonds in the local market for a nominal amount of UF3,000,000 (equivalent to US\$102.1 million) of a series denominated L, which is composed of 6,000 bonds with a value of UF 500 each. These bonds mature in one installment on October 25, 2012 at an annual interest rate of UF + 3.75% . Interest is paid biannually. There is a redemption option as of October 25, 2007.

**18. Provisions and Write-offs:**

The detail of provisions and write-offs shown in liabilities is as follows:

|                             | <b>2006</b>       | <b>2005</b>       |
|-----------------------------|-------------------|-------------------|
|                             | <b>ThCh\$</b>     | <b>ThCh\$</b>     |
| <b>Current</b>              |                   |                   |
| Staff severance indemnities | 288,453           | 276,953           |
| Vacation                    | 2,350,118         | 1,691,911         |
| Other employee benefits (1) | 3,111,087         | 3,109,068         |
| Employee benefit advances   | (1,376,595)       | (2,310,737)       |
| <b>Sub-Total</b>            | <b>4,373,063</b>  | <b>2,767,195</b>  |
| <b>Long-term</b>            |                   |                   |
| Staff severance indemnities | 34,649,896        | 34,704,302        |
| <b>Total</b>                | <b>39,022,959</b> | <b>37,471,497</b> |

(1) Includes provisions for the Independence Day bonus, Christmas bonus, bonus guaranteed under the current union contract, and miscellaneous.

During the period, there were bad debt write-offs of ThCh\$2,072,567 and ThCh\$38,111 for 2006 and 2005, respectively, which were charged against the respective allowance for doubtful accounts.

**19. Staff severance indemnities:**

The detail of the charge to income for staff severance indemnities is as follows:

|   | <b>2006</b>      | <b>2005</b>    |
|---|------------------|----------------|
|   | <b>ThCh\$</b>    | <b>ThCh\$</b>  |
| Operating costs and administrative and selling expenses | 792,747          | 724,920        |
| Other non-operating expenses                            | 8,810,502        | -              |
| <b>Total</b>  | <b>9,603,249</b> | <b>724,920</b> |
| Payments and other changes in the period (1)            | (1,667,756)      | 3,578,675      |

(1) Includes the effect for the period of the increase in the provision due to the change in the discount rate from 7% to 6% made in 2006 in the amount of ThCh \$ 2,797,402 ( see Note 3bi) and a total application of ThCh \$ (4,465,158).

**20. Minority interest:**

Minority interest recognizes the portion of equity and revenues of subsidiaries owned by third parties. The detail of 2006 and 2005, respectively, is as follows:



| Subsidiaries   | Percentage<br>Minority<br>Interest |           | Participation<br>in equity |                  | Participation<br>in net income (loss) |                |               |
|--|------------------------------------|-----------|----------------------------|------------------|---------------------------------------|----------------|---------------|
|  | 2006<br>%                          | 2005<br>% | 2006<br>ThCh\$             | 2005<br>ThCh\$   | 2006<br>ThCh\$                        | 2005<br>ThCh\$ |               |
| Administradora de Sistemas de Telepeajes de Chile S.A. | 20.00                              | 20.00     | 234,237                    | 245,495          | 11,608                                | 6,918          |               |
| Telefónica Mundo S.A.                                  | 0.84                               | 0.84      | 1,132,802                  | 1,229,755        | (25,356)                              | (38,257)       |               |
| Fundación Telefónica                                   | 50.00                              | 50.00     | 190,757                    | 190,874          | 78,356                                | 50,065         |               |
| Telefónica Gestión Servicios Compartidos de Chile S.A. | 0.0010                             | -         | 13                         | -                | -                                     | -              |               |
| CTC Equipos y Servicios de Telecomunicaciones S.A.     | -                                  | 0.0001    | -                          | 31               | -                                     | (2)            |               |
|  |                                    |           | <b>Total</b>               | <b>1,557,809</b> | <b>1,666,155</b>                      | <b>64,608</b>  | <b>18,724</b> |

**21. Shareholders' Equity**

During the periods ended March 31, 2006 and 2005, respectively, changes in shareholders' equity accounts are as follows:

|   | <b>Paid-in<br/>capital<br/>ThCh\$</b> | <b>Reserve<br/>equity<br/>indexation<br/>ThCh\$</b> | <b>Other<br/>reserves<br/>ThCh\$</b> | <b>Retained<br/>earnings<br/>ThCh\$</b> | <b>Net income<br/>ThCh\$</b> | <b>Interim<br/>dividend<br/>ThCh\$</b> | <b>Total<br/>shareholders'<br/>equity<br/>ThCh\$</b> |
|---|---------------------------------------|---|--------------------------------------|---|------------------------------|--|--|
| <b>2006</b>   |                                       |   |                                      |   |                              |  |  |
| Balances as of December 31, 2005                    | 912.692.729                           | -   | (1.751.241)                          | -                                       | 25.183.320                   | (10.549.786)                           | 925.575.022  |
| Transfer of 2005 net income to retained earnings    | -                                     | -   | -                                    | 25.183.320                              | (25.183.320)                 | -                                      | -  |
| Adjustment of foreign investment conversion reserve | -                                     | -   | 159.433                              | -                                       | -                            | -                                      | 159.433  |
| Price-level restatement                             | -                                     | (2.738.078)   | 5.254                                | (75.550)                                | -                            | 31.650                                 | (2.776.724)  |
| Net income  | -                                     | -   | -                                    | -                                       | 734.109                      | -                                      | 734.109  |
| Balances as of March 31, 2006                       | <b>912.692.729</b>                    | <b>(2.738.078)</b>                                  | <b>(1.586.554)</b>                   | <b>25.107.770</b>                       | <b>734.109</b>               | <b>(10.518.136)</b>                    | <b>923.691.840</b>                                   |

**2005**

|  |             |   |             |             |               |               |             |
|--|-------------|---|-------------|-------------|---------------|---------------|-------------|
| Balances as of December 31, 2004             | 880.977.537 | - | (1.237.651) | 48.806.351  | 311.628.674   | (255.303.899) | 984.871.012 |
| Transfer of 2004 income to retained earnings | -           | - | -           | 311.628.674 | (311.628.674) | -             | -           |
| Adjustment of foreign investment conversion  | -           | - | 238.170     | -           | -             | -             | 238.170     |

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|  |                    |                    |                    |                    |                  |                      |                      |
|--|--------------------|--------------------|--------------------|--------------------|------------------|----------------------|----------------------|
| reserve                                |                    |                    |                    |                    |                  |                      |                      |
| Price-level restatement                | -                  | (7.047.820)        | 9.901              | (2.883.480)        | -                | 2.042.431            | (7.878.968)          |
| Net income                             | -                  | -                  | -                  | -                  | 8.170.508        | -                    | 8.170.508            |
| Balances as of March 31, 2005          | <b>880.977.537</b> | <b>(7.047.820)</b> | <b>(989.580)</b>   | <b>357.551.545</b> | <b>8.170.508</b> | <b>(253.261.468)</b> | <b>985.400.722</b>   |
| Restated balances as of March 31, 2006 | <b>917.292.990</b> | <b>(7.338.344)</b> | <b>(1.030.372)</b> | <b>372.290.453</b> | <b>8.507.311</b> | <b>(263.701.354)</b> | <b>1.026.020.684</b> |

**21. Shareholders Equity**, continued:**(a) Paid-in capital:**

As of March 31, 2006 the Company's paid-in capital is as follows:

**Number of shares:**

| Series | No. of<br>subscribed<br>shares | No. of paid<br>shares | No. of shares<br>with<br>voting rights |
|--------|--------------------------------|-----------------------|--|
| A      | 873,995,447                    | 873,995,447           | 873,995,447                            |
| B      | 83,161,638                     | 83,161,638            | 83,161,638                             |

**Paid-in capital:**

| Series | Subscribed<br>Capital<br>ThCh\$ | Paid-in<br>Capital<br>ThCh\$ |
|--------|---------------------------------|------------------------------|
| A      | 833,394,333                     | 833,394,333                  |
| B      | 79,298,396                      | 79,298,396                   |

**(b) Shareholder distribution:**

As indicated in SVS Circular No.792, the distribution of shareholders by percentage shareholding in the Company as of March 31, 2006 is as follows:

| Type of shareholder                     | Percentage of Total<br>holdings<br>% | Number of<br>shareholders |
|---|--------------------------------------|---------------------------|
| 10% holding or more                     | 56.17                                | 2                         |
| Less than 10% holding:                  | 43.06                                | 1,718                     |
| Investment equal to or exceeding UF 200 |                                      |                           |
| Investment under UF 200                 | 0.77                                 | 11,247                    |
| <b>Total</b>                            | <b>100.00</b>                        | <b>12,967</b>             |
| Company controller                      | 44.90                                | 1                         |

**21. Shareholders Equity**, continued:

**(c) Dividends:**

**i) Dividend policy:**

In accordance with Law No.18,046, unless otherwise decided at the Shareholders Meeting by unanimous vote of the shares issued, when there is net income, at least 30% must be distributed in dividends.

Considering the cash situation, levels of projected investment and the solid financial indicators for 2005 and future years, on April 14, 2005, the Ordinary Shareholders Meeting modified the dividend distribution policy reported at the Ordinary Shareholders Meeting of April 2004, and agreed to distribute 100% of net income generated during the respective year, by means of an interim dividend in November of each year and a final dividend in May of the following year.

**ii) Dividend distributed in the period:**

On April 14, 2005, the Extraordinary Shareholders Meeting approved the payment of a final dividend (No. 168) of Ch\$ 58.84591 per share with a charge to net income for 2004 of ThCh\$56,324,775. Likewise, it approved payment of a provisional dividend (No.169) of Ch\$ 50.99095 pesos per share, with a charge to retained earnings as of December 2004 of ThCh\$48,806,351. Both dividends were paid on May 30, 2005.

On October 27, 2005, the Board approved payment of an interim dividend (No. 170) of Ch\$11.00 per share, with a charge to 2005 net income, of ThCh\$10,528,728.

**21. Shareholders Equity**, continued:**(d) Other reserves:**

Other Reserves include the net effect of the adjustment for conversion differences as established in Technical Bulletin No. 64 of the Chilean Association of Accountants, the detail of which is as follows:

|         |                                | <b>Amount</b>       |                    |                 |                      |
|---------|--------------------------------|---------------------|--------------------|-----------------|----------------------|
|         | <b>Company</b>                 | <b>December 31,</b> | <b>Price-level</b> | <b>Net</b>      | <b>Balance as of</b> |
|         |                                | <b>2005</b>         | <b>restatement</b> | <b>Movement</b> | <b>March 31,</b>     |
|         |                                | <b>ThCh\$</b>       | <b>ThCh\$</b>      | <b>ThCh\$</b>   | <b>2006</b>          |
|         |                                |                     |                    |                 | <b>ThCh\$</b>        |
| Foreign | TBS Celular Participación S.A. | (1,751,241)         | 5,254              | 159,433         | (1,586,554)          |
|         | <b>Total</b>                   | <b>(1,751,241)</b>  | <b>5,254</b>       | <b>159,433</b>  | <b>(1,586,554)</b>   |

**22. Other Non-Operating Income and Expenses:****(a) Other non-operating income:**

The detail of other non-operating income is as follows:

| <b>Other Income</b>                       | <b>2006<br/>ThCh\$</b> | <b>2005<br/>ThCh\$</b> |
|---|------------------------|------------------------|
| Fines levied on suppliers and indemnities | 17,254                 | 71,532                 |
| Proceeds from sale of used equipment      | 355,974                | 443,302                |
| Real estate rental                        | 69,995                 | 80,421                 |
| Other                                     | 55,662                 | 6,979                  |
| <b>Total</b>                              | <b>498,885</b>         | <b>602,234</b>         |

**(b) Other non-operating expenses:**

The detail of other non-operating expenses is as follows:

| <b>Other Expenses</b>   | <b>2006<br/>ThCh\$</b> | <b>2005<br/>ThCh\$</b> |
|---|------------------------|------------------------|
| Lawsuit indemnities and other provisions  | 366,950                | -                      |
| Depreciation and retirement of out-of-service property, plant and equipment (1) | 339,349                | 842,823                |
| Removal of property, plant and equipment that is out of service                 | 301,328                | 375,585                |
| Lower market value provision  | 13,938                 | 268,266                |
| Restructuring costs   | 8,810,502              | -                      |
| Other   | 293,207                | 8,875                  |
| <b>Total</b>  | <b>10,125,274</b>      | <b>1,495,549</b>       |

(1) As of March 2006 this caption is composed mainly of depreciation of telephone equipment maintained in stock for replacements.

(2) Corresponds mainly to payments made to employees on the basis of the Early Retirement Plan.

**23. Price-level restatement:**

The detail of price-level restatement is as follows:

| <b>Assets (Charges) Credits</b>                          | <b>Indexation</b> | <b>2006<br/>ThCh\$</b> | <b>2005<br/>ThCh\$</b> |
|--|-------------------|------------------------|------------------------|
| Inventory  | C.P.I.            | (2,982)                | (44,127)               |
| Prepaid expenses   | C.P.I.            | (22)                   | (1,448)                |
| Prepaid expenses   | U.F.              | 2,241                  | -                      |
| Other current assets                                     | C.P.I.            | (711)                  | (6,734)                |
| Other current assets                                     | U.F.              | 16,640                 | 153,722                |
| Short and long-term deferred taxes                       | C.P.I.            | (341,019)              | (1,023,396)            |
| Property, plant and equipment                            | C.P.I.            | (3,914,515)            | (11,404,152)           |
| Investments in related companies                         | C.P.I.            | (16,257)               | (69,109)               |
| Goodwill   | C.P.I.            | (53,070)               | (161,086)              |
| Long-term receivables                                    | U.F.              | 43,540                 | 821,598                |
| Long-term receivables                                    | C.P.I.            | 28                     | -                      |
| Other long-term assets                                   | C.P.I.            | (117,271)              | (503,240)              |
| Other long-term assets                                   | U.F.              | (461)                  | 3,848                  |
| Expense accounts   | C.P.I.            | (36,479)               | (202,146)              |
| <b>Total Charges</b>                                     |                   | <b>(4,420,338)</b>     | <b>(12,436,270)</b>    |
|  |                   |                        |                        |
| <b>Liabilities Shareholders Equity (Charges) Credits</b> | <b>Indexation</b> | <b>2006<br/>ThCh\$</b> | <b>2005<br/>ThCh\$</b> |
| Short-term obligations                                   | U.F.              | (153,964)              | (2,058,341)            |
| Long-term obligations                                    | C.P.I.            | 1,569                  | 4,242                  |
| Long-term obligations                                    | U.F.              | 1,085,050              | 364,110                |
| Shareholders equity                                      | C.P.I.            | 2,776,724              | 8,203,753              |
| Revenue accounts   | C.P.I.            | 58,910                 | 330,856                |
| <b>Total Credits</b>                                     |                   | <b>3,768,289</b>       | <b>6,844,620</b>       |
|  |                   |                        |                        |
| <b>Price-level restatement, net</b>                      |                   | <b>(652,049)</b>       | <b>(5,591,650)</b>     |



**24. Foreign currency translation:**

The detail of the gain on foreign currency translation is as follows:

| <b>Assets (Charges) Credits</b>          | <b>Currency</b> | <b>2006<br/>ThCh\$</b> | <b>2005<br/>ThCh\$</b> |
|--|-----------------|------------------------|------------------------|
| Current assets                           | US\$            | 2,261,249              | 10,695,875             |
| Current assets                           | EURO            | (1,938)                | (1,104)                |
|  | BRAZILIAN       |                        |                        |
| Current assets                           | REAL            | 119,777                | -                      |
| Long-term receivables                    | US\$            | 523,700                | 6,297,288              |
| Other long-term assets                   | US\$            | -                      | 23,431                 |
| <b>Total Credits</b>                     |                 | <b>2,902,788</b>       | <b>17,015,490</b>      |
|  |                 |                        |                        |
| <b>Liabilities (Charges) Credits</b>     | <b>Currency</b> | <b>2006<br/>ThCh\$</b> | <b>2005<br/>ThCh\$</b> |
| Short-term obligations                   | US\$            | (799,427)              | 6,044,986              |
| Short-term obligations                   | EURO            | (209)                  | 571                    |
|  | BRAZILIAN       |                        |                        |
| Short-term obligations                   | REAL            | 28,134                 | -                      |
| Long-term obligations                    | US\$            | (1,904,500)            | (20,589,803)           |
| <b>Total Charges</b>                     |                 | <b>(2,676,002)</b>     | <b>(14,544,246)</b>    |
|  |                 |                        |                        |
| <b>Foreign currency translation, net</b> |                 | <b>226,786</b>         | <b>2,471,244</b>       |

**25. Issuance and placement of shares and debt expense:**

The detail of this item is as follows:

|                                   | Short-term     |                | Long-term        |                |
|-----------------------------------|----------------|----------------|------------------|----------------|
|                                   | 2006<br>ThCh\$ | 2005<br>ThCh\$ | 2006<br>ThCh\$   | 2005<br>ThCh\$ |
| Bond issuance expenses            | 282,832        | 423,521        | 759,602          | 376,714        |
| Discount on debt                  | 234,462        | 59,037         | 1,262,956        | 221,345        |
| Commercial paper issuance expense | -              | 176,703        | -                | -              |
| <b>Total</b>                      | <b>517,294</b> | <b>659,261</b> | <b>2,022,558</b> | <b>598,059</b> |

These items are classified under Other Current Assets and Other Long-term Assets, as applicable and are amortized over the term of the respective obligations, as described in Note 17 Obligations with the Public .

**26. Cash flows:**

Financing and investing activities that do not generate cash flows during the period, but which commit future cash flows are as follows:

**a) Financing activities:** Financing activities that commit future cash flows are as follows:

|   |                       |
|---|-----------------------|
| Obligations with banks and financial institutions | - see Notes 15 and 16 |
| Obligations with the public                       | - see Notes 17        |

**b) Investing activities:** Investing activities that commit future cash flows are as follows:

|     | Maturity | ThCh\$     |
|-----|----------|------------|
| BCD | 2007     | 13,972,456 |
| BCU | 2009     | 1,904,307  |

**c) Cash and cash equivalents:**

|                      | 2006<br>ThCh\$    | 2005<br>ThCh\$     |
|----------------------|-------------------|--------------------|
| Cash                 | 7,313,876         | 5,144,148          |
| Time deposits        | 27,754,792        | 77,968,249         |
| Other current assets | 51,004,757        | 59,742,476         |
| <b>Total</b>         | <b>86,073,425</b> | <b>142,854,873</b> |



**27. Derivative Contracts:**

The breakdown of derivative contracts is as follows:

| TYPE OF DERIVATIVE | TYPE OF CONTRACT | CONTRACT VALUE | DESCRIPTION OF CONTRACT |                     |                        |                                 | VALUE OF HEDGED ITEM |             |
|--------------------|------------------|----------------|-------------------------|---------------------|------------------------|---------------------------------|----------------------|-------------|
|                    |                  |                | MATURITY OR EXPIR.      | SPECIFIC ITEM       | PURCHASE SALE POSITION | HEDGED ITEM OR TRANSACTION NAME | AMOUNT               | ThCh\$      |
| FR                 | CI               | 19.000.000     | III Quarter 2006        | Exchange rate       | C                      | Oblig.in US\$                   | 19.000.000           | 9.997.420   |
| FR                 | CCPE             | 20.000.000     | III Quarter 2006        | Exchange rate       | C                      | Oblig.in US\$                   | 20.000.000           | 10.523.600  |
| FR                 | CCPE             | 150.000.000    | III Quarter 2008        | Cross Currency Swap | C                      | Oblig.in US\$                   | 150.000.000          | 78.927.000  |
| FR                 | CCPE             | 200.000.000    | II Quarter 2009         | Cross Currency Swap | C                      | Oblig.in US\$                   | 200.000.000          | 105.236.000 |
| FR                 | CCPE             | 150.000.000    | II Quarter 2011         | Cross Currency Swap | C                      | Oblig.in US\$                   | 150.000.000          | 78.927.000  |
| FR                 | CI               | 20.000.000     | II Quarter 2006         | Exchange rate       | V                      | Oblig.in US\$                   | 20.000.000           | 10.653.150  |
| FR                 | CI               | 5.000.000      | III Quarter 2006        | Exchange rate       | V                      | Oblig.in US\$                   | 5.000.000            | 2.680.700   |
| FR                 | CCPE             | 2.000.000      | II Quarter 2006         | Exchange rate       | C                      | Oblig.in US\$                   | 2.000.000            | 1.052.360   |
| FR                 | CCPE             | 6.000.000      | III Quarter 2006        | Exchange rate       | C                      | Oblig.in US\$                   | 6.000.000            | 3.157.080   |

|    |    |           |                     |                  |   |                  |           |         |
|----|----|-----------|---------------------|------------------|---|------------------|-----------|---------|
| FR | CI | 2.416.478 | II Quarter<br>2006  | Exchange<br>rate | C | Oblig.in<br>US\$ | 2.416.478 | 587.832 |
| FR | CI | 2.416.478 | III Quarter<br>2006 | Exchange<br>rate | C | Oblig.in<br>US\$ | 2.416.478 | 587.832 |
| FR | CI | 2.522.787 | IV Quarter<br>2006  | Exchange<br>rate | C | Oblig.in<br>US\$ | 2.522.787 | 613.692 |
| FR | CI | 391.416   | I Quarter<br>2007   | Exchange<br>rate | C | Oblig.in<br>US\$ | 391.416   | 95.216  |

Deferred income for exchange forward contracts  
 Deferred costs for exchange insurance  
 Exchange forward contracts expensed during the year ( net )

**Total**

**Types of derivatives:**

**Type of Contract:**

FR: Forward  
 S : Swap

CCPE: Hedge contract for existing transactions  
 CCTE: Hedge contract for anticipated transactions  
 CI: Investment hedge contract

## **28. Contingencies and commitments:**

### **a) Lawsuits:**

#### **(i) Claims presented by VTR Telefónica S.A.:**

On September 30, 2000, VTR Telefónica S.A. filed an ordinary suit for the collection of access charges in the amount of ThCh\$2,500,000, based on the differences that would arise from the lowering of access charge rates, due to Rate Decree No.187 of Telefónica CTC Chile. The initial sentence accepted VTR's claim and the compensation alleged by Telefónica CTC Chile. The Company filed a motion to vacate and appeal, which is currently underway.

#### **(ii) Labor lawsuits:**

In the course of normal operations, labor lawsuits have been filed against the Company.

To date, among others, there are labor proceedings involving former employees, who claim wrongful dismissal. These employees did not sign termination releases or receive staff severance indemnities. On various occasions, the Supreme Court has reviewed the sentences handed down on the matter, accepting the argument of the Company and ratifying the validity of the terminations.

There are, in addition, other lawsuits involving former employees, whose staff severance indemnities have been paid and their termination releases signed, who in spite of having chosen voluntary retirement plans or having been terminated due to company needs, intend to have the terminations voided. Of these lawsuits, to date, two have received a sentence favorable to the Company, rejecting the annulments.

Certain unions have filed complaints before the Santiago Labor Courts, requesting damage payments for various concepts.

In the opinion of Management and internal legal counsel, the risk that the Company will be required to pay indemnities in the amount claimed in the previously mentioned lawsuits, in addition to other civil and labor suits in which the Company is the defendant, is remote. Management considers it unlikely that the Company's income and equity will be significantly affected by these loss contingencies.

#### **(iii) Other contingencies; Lawsuit against the Government:**

On October 31, 2001, Telefónica CTC Chile filed an administrative motion before the Ministry of Transport and Telecommunications and the Ministry of Economy, requesting correction of the errors and illegalities in Rate Decree No. 187 of 1999. On January 29, 2002, the Ministries issued a joint response rejecting the administrative recourse, after having carefully evaluated, only the viability and timeliness of the petition made, considering the set of circumstances that concur in the problem stated and the prudence that must orient public actions, to add that such rejection has had no other motivation than to protect the general interest and progress of the telecommunications services.

Upon extinguishing the administrative instances to correct the errors and illegalities involved in the tariff setting process of 1999, in March 2002, Telefónica CTC Chile filed a lawsuit for damages against the State of Chile for the sum of Ch\$ 181,038,411,056, plus readjustments and interest, which covers past and future damages until May 2004.

The judicial process is currently at the stage of issuing a sentence.

**28. Contingencies and restrictions, continued:**

**(iv) Manquehue Net:**

On June 24, 2003, Telefónica CTC Chile filed a forced compliance of contracts complaint with damage indemnity before the mixed arbitration court of Mr. Victor Vial del Río against Manquehue Net, in the amount of Ch\$ 3,647,689,175, in addition to costs incurred during the proceeding. Likewise, and on the same date, Manquehue Net filed a compliance with discounts complaint (in the amount of UF 107,000), in addition to an obligation to perform complaint (signing of a 700 services contract). After completion of the evidence period, on June 5, 2004 the arbiter called the parties together to pronounce a sentence.

On April 11, 2005, the Court notified the first instance sentence accepting the claim made by Telefónica CTC Chile and ordering Manquehue to pay approximately Ch\$ 452 million, and at the same time accepted Manquehue's claim and ordered Telefónica CTC Chile to pay 47,600 UF.

Telefónica CTC Chile filed an appeal for dismissal on the grounds of errors in the form in both cases; which are currently pending before the Court of Appeals of Santiago.

**b) Financial restrictions:**

In order to carry out its investment plans, the Company obtained financing in the local and foreign market (notes 15, 16 and 17), which established, among others restrictions, the maximum debt that the Company may have and interest coverage requirements.

The maximum debt ratio for these contracts is between 1.50 and 1.60, whereas the interest coverage ratio cannot be less than 4.00.

Non-compliance with these clauses implies that all the obligations included in these financing contracts will be considered as due.

As of March 31, 2006 the Company complies with all the financial restrictions.

**29. Third party guarantees:**

The Company has not received any guarantees from third parties.

**30. Local and Foreign Currency:**

A summary of the assets in local and foreign currency is as follows:

| Description  | Currency                | 2006                 | 2005                 |
|--|-------------------------|----------------------|----------------------|
|  |                         | ThCh\$               | ThCh\$               |
| <b>Total current assets:</b>                               |                         | <b>306.014.540</b>   | <b>417.981.350</b>   |
| Cash   | Non-indexed Ch\$        | 7.098.950            | 5.043.173            |
|  | Dollars                 | 179.564              | 45.435               |
|  | Euros                   | 35.362               | 55.540               |
| Time deposits  | Indexed Ch\$            | 24.606.589           | 287.488              |
|  | Non-indexed Ch\$        | -                    | 77.564.846           |
|  | Dollars                 | 3.148.203            | 115.915              |
| Marketable securities                                      | Indexed Ch\$            | 1.904.307            | -                    |
|  | Dollars                 | 13.972.456           | 32.871.072           |
| Notes and accounts receivable (1)                          | Non-indexed Ch\$        | 153.828.244          | 149.435.779          |
|  | Dollars                 | 3.996.460            | 38.388.668           |
| Due from related companies                                 | Non-indexed Ch\$        | 15.012.146           | 14.221.117           |
|  | Dollars                 | 1.516.444            | 2.605.479            |
| Other current assets (2)                                   | Indexed Ch\$            | 20.600.826           | 21.113.519           |
|  | Non-indexed Ch\$        | 58.840.126           | 44.469.706           |
|  | Dollars                 | 1.104.215            | 31.763.613           |
|  | Brazilian Real          | 170.648              | -                    |
| <b>Total property, plant and equipment :</b>               |                         | <b>1.264.756.346</b> | <b>1.388.512.115</b> |
| Property, plant and equipment and accumulated depreciation | Indexed Ch\$            | 1.264.756.346        | 1.388.512.115        |
| <b>Total other long-term assets</b>                        |                         | <b>92.124.480</b>    | <b>106.943.895</b>   |
| Investment in related companies                            | Indexed Ch\$            | 7.981.194            | 8.528.568            |
| Investment in other companies                              | Indexed Ch\$            | 4.093                | 4.081                |
| Goodwill   | Indexed Ch\$            | 17.285.055           | 19.585.489           |
| Other long-term assets (3)                                 | Indexed Ch\$            | 52.652.834           | 68.601.800           |
|  | Non-indexed Ch\$        | 14.198.365           | 4.643.226            |
|  | Dollars                 | 2.939                | 5.580.731            |
| <b>Total assets</b>  |                         | <b>1.662.895.366</b> | <b>1.913.437.360</b> |
| <b>Subtotal by currency</b>                                | <b>Indexed Ch\$</b>     | <b>1.389.791.244</b> | <b>1.506.633.060</b> |
|  | <b>Non-indexed Ch\$</b> | <b>248.977.831</b>   | <b>295.377.847</b>   |
|  | <b>Dollars</b>          | <b>23.920.281</b>    | <b>111.370.913</b>   |
|  | <b>Euros</b>            | <b>35.362</b>        | <b>55.540</b>        |
|  | <b>Brazilian Real</b>   | <b>170.648</b>       | <b>-</b>             |

(1)



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Includes the following balance sheet accounts: Trade Accounts Receivable, Notes Receivable and Miscellaneous Accounts Receivable.

- (2) Includes the following balance sheet accounts: Inventories, Recoverable Taxes, Prepaid Expenses, Deferred Taxes and Other Current Assets.
- (3) Includes the following balance sheet accounts: Long-term Debtors, Intangibles, Accumulated amortization and Others.

**30. Local and foreign currency**, continued

A summary of the current liabilities in local and foreign currency is as follows:

| Description   | Currency         | Up to 90 days    |                                    |                  |                                    | 90 days up to 1 year |                                    |                  |                                    |
|---|------------------|------------------|------------------------------------|------------------|------------------------------------|----------------------|------------------------------------|------------------|------------------------------------|
|   |                  | 2006             |                                    | 2005             |                                    | 2006                 |                                    | 2005             |                                    |
|   |                  | Amount<br>ThCh\$ | Average<br>annual<br>interest<br>% | Amount<br>ThCh\$ | Average<br>annual<br>interest<br>% | Amount<br>ThCh\$     | Average<br>annual<br>interest<br>% | Amount<br>ThCh\$ | Average<br>annual<br>interest<br>% |
| Short-term obligations with banks and financial institutions            | Non-indexed Ch\$ | -                | -                                  | 9.876.927        | 3,00                               | -                    | -                                  | -                | -                                  |
| Short-term portion of obligations with banks and financial institutions | Indexed Ch\$     | 689.552          | -                                  | -                | -                                  | -                    | -                                  | -                | -                                  |
|   | Dollars          | 1.317.862        | -                                  | 17.441.515       | 3,00                               | -                    | -                                  | -                | -                                  |
| Obligations with the public (Commercial paper)                          | Non-indexed Ch\$ | 34.866.394       | 6,12                               | 36.388.770       | 2,73                               | 11.539.171           | 5,76                               | 12.248.423       | 3,72                               |
| Obligations with the public (Bonds payable)                             | Indexed Ch\$     | -                | -                                  | -                | -                                  | 1.658.835            | 6,00                               | 1.682.160        | 5,80                               |
|   | Dollars          | 26.514.718       | 8,40                               | -                | -                                  | -                    | -                                  | 97.898.221       | 8,38                               |
| Long-term obligations maturing within a year                            | Indexed Ch\$     | 3.076            | 8,10                               | 8.187            | 9,06                               | 9.231                | 8,10                               | 24.559           | 9,06                               |
| Due to related parties  | Indexed Ch\$     | -                | -                                  | -                | -                                  | -                    | -                                  | 139.680          | -                                  |
|   | Non-indexed Ch\$ | 27.274.200       | -                                  | 23.732.659       | -                                  | 419.226              | -                                  | -                | -                                  |
|   | Dollars          | 128.539          | -                                  | 898.550          | -                                  | -                    | -                                  | -                | -                                  |

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|                    |                    |                    |   |                    |   |                   |   |                    |
|--------------------|--------------------|--------------------|---|--------------------|---|-------------------|---|--------------------|
| Other              |                    |                    |   |                    |   |                   |   |                    |
| current (4)        | Indexed Ch\$       | -                  | - | -                  | - | 472.055           | - | -                  |
|                    | Non-indexed        |                    |   |                    |   |                   |   |                    |
| liabilities        | Ch\$               | 113.266.696        | - | 161.729.416        | - | 5.676.013         | - | 1.184.380          |
|                    | Dollars            | 2.161.872          | - | 8.268.238          | - | 357.841           | - | -                  |
|                    | Brazilian          |                    |   |                    |   |                   |   |                    |
|                    | Real               | 4.346              | - | -                  | - | 49.544            | - | -                  |
| <b>Total</b>       |                    |                    |   |                    |   |                   |   |                    |
| <b>Current</b>     |                    |                    |   |                    |   |                   |   |                    |
| <b>Liabilities</b> |                    | <b>206.227.255</b> |   | <b>258.344.262</b> |   | <b>20.181.916</b> |   | <b>113.177.423</b> |
| <b>Subtotal by</b> | <b>Indexed</b>     |                    |   |                    |   |                   |   |                    |
| <b>currency</b>    | <b>Ch\$</b>        | <b>692.628</b>     |   | <b>8.187</b>       |   | <b>2.140.121</b>  |   | <b>1.846.399</b>   |
|                    | <b>Non-indexed</b> |                    |   |                    |   |                   |   |                    |
|                    | <b>Ch\$</b>        | <b>175.407.290</b> |   | <b>231.727.772</b> |   | <b>17.634.410</b> |   | <b>13.432.803</b>  |
|                    | <b>Dollars</b>     | <b>30.122.991</b>  |   | <b>26.608.303</b>  |   | <b>357.841</b>    |   | <b>97.898.221</b>  |
|                    | <b>Brazilian</b>   |                    |   |                    |   |                   |   |                    |
|                    | <b>Real</b>        | <b>4.346</b>       |   | <b>-</b>           |   | <b>49.544</b>     |   | <b>-</b>           |

(4) Includes the following balance sheet accounts: Dividends payable, Trade accounts payable, Notes payable, Miscellaneous accounts payable, Accruals, Withholdings, Income taxes, Unearned Income and Other current liabilities.

**30. Local and foreign currency, continued**

A summary of the long-term liabilities in local and foreign currency for 2006 is as follows:

|   |                             | 1 to 3 years<br>2006 |                               | 3 to 5 years<br>2006 |                               | 5 to 10 years<br>2006 |                               |           |  |
|---|-----------------------------|----------------------|-------------------------------|----------------------|-------------------------------|-----------------------|-------------------------------|-----------|--|
|   |                             | Amount<br>ThCh\$     | Average<br>annual<br>interest | Amount<br>ThCh\$     | Average<br>annual<br>interest | Amount<br>ThCh\$      | Average<br>annual<br>interest |           |  |
|   |                             |                      | rate<br>%                     |                      | rate<br>%                     |                       | rate<br>%                     |           |  |
| <b>LONG-TERM LIABILITIES</b>                        |                             |                      |                               |                      |                               |                       |                               |           |  |
| Obligation with banks and<br>financial institutions | Indexed Ch\$                | -                    | -                             | -                    | -                             | 63.690.171            | 2,32                          | -         |  |
|   | Dollars                     | 78.927.000           | 4,69                          | 105.236.000          | 5,07                          | 78.927.000            | 3,75                          | -         |  |
| Bonds payable                                       | Indexed Ch\$                | -                    | -                             | -                    | -                             | -                     | -                             | 12        |  |
| Other long-term liabilities (5)                     | Indexed Ch\$                | 31.469.881           | -                             | 23.546.014           | -                             | 22.995.698            | -                             | 33        |  |
|   | Non-indexed<br>Ch\$         | 999.702              | -                             | 423.531              | -                             | 1.061.256             | -                             | 4         |  |
| <b>Total Long-term Liabilities</b>                  |                             | <b>111.396.583</b>   |                               | <b>129.205.545</b>   |                               | <b>220.421.105</b>    |                               | <b>50</b> |  |
| <b>Subtotal by currency</b>                         | <b>Indexed<br/>Ch\$</b>     | <b>31.469.881</b>    |                               | <b>23.546.014</b>    |                               | <b>140.432.849</b>    |                               | <b>45</b> |  |
|   | <b>Non-indexed<br/>Ch\$</b> | <b>999.702</b>       |                               | <b>423.531</b>       |                               | <b>1.061.256</b>      |                               | <b>4</b>  |  |
|   | <b>Dollars</b>              | <b>78.927.000</b>    |                               | <b>105.236.000</b>   |                               | <b>78.927.000</b>     |                               | <b>-</b>  |  |

A summary of the long-term liabilities in local and foreign currency for 2005 is as follows:

|                               |              | 1 to 3 years<br>2005 |                               | 3 to 5 years<br>2005 |                               | 5 to 10 years<br>2005 |                               | over 10 years<br>2005 |                               |
|-------------------------------|--------------|----------------------|-------------------------------|----------------------|-------------------------------|-----------------------|-------------------------------|-----------------------|-------------------------------|
|                               |              | Amount<br>ThCh\$     | Average<br>annual<br>interest | Amount<br>ThCh\$     | Average<br>annual<br>interest | Amount<br>ThCh\$      | Average<br>annual<br>interest | Amount<br>ThCh\$      | Average<br>annual<br>interest |
|                               |              |                      | rate<br>%                     |                      | rate<br>%                     |                       | rate<br>%                     |                       | rate<br>%                     |
| <b>LONG-TERM LIABILITIES</b>  |              |                      |                               |                      |                               |                       |                               |                       |                               |
| Obligations with<br>banks and | Indexed Ch\$ | -                    | -                             | 63.662.031           | 1,55                          | -                     | -                             | -                     |                               |

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|                                    |                         |                    |      |                    |      |                   |      |                   |      |
|------------------------------------|-------------------------|--------------------|------|--------------------|------|-------------------|------|-------------------|------|
|                                    | Dollars                 | 146.419.936        | 3,64 | 158.621.599        | 3,52 | -                 | -    | -                 |      |
| Bonds payable                      | Indexed Ch\$            | 2.686.163          | 6,00 | 2.686.163          | 6,00 | 6.715.407         | 6,00 | 1.343.084         | 6,00 |
|                                    | Dollars                 | 30.261.951         | 7,63 | -                  | -    | -                 | -    | -                 | -    |
| Other long-term liabilities (5)    | Indexed Ch\$            | 15.072.920         | -    | 8.046.378          | -    | 20.119.177        | -    | 20.460.991        |      |
|                                    | Non-indexed Ch\$        | 944.996            | -    | 362.676            | -    | 906.693           | -    | 35.918.673        |      |
| <b>Total Long-term Liabilities</b> |                         | <b>195.385.966</b> |      | <b>233.378.847</b> |      | <b>27.741.277</b> |      | <b>57.722.748</b> |      |
| <b>Subtotal by currency</b>        | <b>Indexed Ch\$</b>     | <b>17.759.083</b>  |      | <b>74.394.572</b>  |      | <b>26.834.584</b> |      | <b>21.804.075</b> |      |
|                                    | <b>Non-indexed Ch\$</b> | <b>944.996</b>     |      | <b>362.676</b>     |      | <b>906.693</b>    |      | <b>35.918.673</b> |      |
|                                    | <b>Dollars</b>          | <b>176.681.887</b> |      | <b>158.621.599</b> |      | <b>-</b>          |      | <b>-</b>          |      |

(5) Includes the following balance sheet accounts: Due to related companies, Miscellaneous accounts payable, Accruals, Deferred long-term taxes, Other long-term liabilities.

**31. Sanctions:**

Neither the Company, nor its Directors and Managers have been sanctioned by the Superintendency of Securities and Insurance or any other administrative authority during 2006 and 2005.

**32. Subsequent events:**

On April 20, 2006, the Extraordinary Shareholders Meeting of Telefónica CTC Chile agreed to the following:

- a) Modify the Company's bylaws in order to decrease capital by Ch\$ 40,200,513,570.
- b) Add the synthetic name TELEFONICA CHILE, modifying the first article of the bylaws.

The Extraordinary Shareholders Meeting of subsidiary Telefónica Mundo S.A. held on April 19, 2006, agreed to the following:

- a) Approve the merger by incorporation of Globus 120 S.A. in Telefónica Mundo S.A. with the latter acquiring the assets and liabilities of the former as of May 1, 2006.
- b) Increase the share capital of Telefónica Mundo S.A. by Ch\$3,250,440,994, through issuance of 1,398,602 cash shares.
- c) Approve the Company's name change to TELEFONICA LARGA DISTANCIA S.A. modify the synthetic names and reform bylaws.

On April 21, 2006, the Supreme Court issued a verdict in favor of Telefónica Chile in the lawsuit filed by a group of unions requesting compliance with the goal incentives contemplated in the collective agreements in effect in 1998. This verdict constitutes the final and definite pronouncement with respect to this process and has an evident incidence on all the rest of the procedures in course relating to this clause of the collective contracts.

On April 27, 2006, the Board of Directors accepted the resignation of the Company's Director and President, Mr. Bruno Philippi Irrarrazabal, and designated Mr. Emilio Gilolmo López to replace him. Likewise the Board accepted the resignation of deputy Directors Messrs. Juan Carlos Ros Brugueras and Guillermo Ansaldo Lutz, designating Messrs. Manuel Alavarez-Tronge and Manoel Amorin, respectively, as replacements.

In the period from April 1 to 27, 2006, there have been no other significant subsequent events that affect these financial statements.

**33. Environment:**

In the opinion of Management and the Company's in-house legal counsel and because the nature of the Company's operations do not directly or indirectly affect the environment, as of the closing date of these interim financial statements, no resources have been set aside nor have any payments been made for non-compliance with municipal ordinances or to other supervising organizations.

**34. Time deposits:**

The detail of time deposits is as follows:

| Placement       | Institution                    | Currency | Principal | Rate | Maturity        | Principal         | Accrued            | Total             |
|-----------------|--------------------------------|----------|-----------|------|-----------------|-------------------|--------------------|-------------------|
|                 |                                |          | ThCh\$    | %    |                 | ThCh\$            | interest<br>ThCh\$ |                   |
| Mar 21,<br>2006 | Banco de Chile                 | ThCh\$   | 6,500,000 | 5.04 | Apr 26,<br>2006 | 6,500,000         | 9,100              | 6,509,100         |
| Mar 21,<br>2006 | Banco Santander<br>Santiago    | ThCh\$   | 1,700,000 | 5.16 | Apr 26,<br>2006 | 1,700,000         | 2,437              | 1,702,437         |
| Mar 31,<br>2006 | Banco Santander<br>Santiago    | ThCh\$   | 1,928     | -    | Apr 30,<br>2006 | 1,928             | -                  | 1,928             |
| Mar 30,<br>2006 | BBVA                           | ThCh\$   | 6,500,000 | 4.80 | May 02,<br>2006 | 6,500,000         | 867                | 6,500,867         |
| Mar 31,<br>2006 | Banco de Chile                 | ThCh\$   | 1,600,000 | 4.92 | May 02,<br>2006 | 1,600,000         | -                  | 1,600,000         |
| Mar 30,<br>2006 | Banco Santander<br>Santiago    | ThCh\$   | 8,000,000 | 5.40 | May 12,<br>2006 | 8,000,000         | 1,200              | 8,001,200         |
| Dec 06,<br>2005 | Banco Crédito e<br>Inversiones | UF       | 16        | 3.00 | Jun 06,<br>2006 | 290,484           | 573                | 291,057           |
| Mar 31,<br>2006 | ABN Amro Bank                  | USD      | 1,480     | 4.80 | Apr 03,<br>2006 | 780,996           | -                  | 780,996           |
| Mar 03,<br>2006 | Banco Crédito e<br>Inversiones | USD      | 145       | 4.30 | Apr 03,<br>2006 | 76,296            | 255                | 76,551            |
| Mar 06,<br>2006 | Banco Crédito e<br>Inversiones | USD      | 147       | 4.30 | Apr 06,<br>2006 | 77,296            | 231                | 77,527            |
| Mar 23,<br>2006 | Deutsche Bank                  | USD      | 4,200     | 4.70 | Apr 20,<br>2006 | 2,209,956         | 3,173              | 2,213,129         |
| <b>Total</b>    |                                |          |           | -    | -               | <b>27,736,956</b> | <b>17,836</b>      | <b>27,754,792</b> |

**35. Accounts payable:**

The detail of the accounts payable balance is as follows:

|                                       | 2006<br>ThCh\$    | 2005<br>ThCh\$    |
|---------------------------------------|-------------------|-------------------|
| <b>Suppliers</b>                      |                   |                   |
| Chilean                               | 63,189,488        | 61,524,608        |
| Foreign                               | 3,271,390         | 2,587,760         |
| <b>Carrier service</b>                | 7,224,030         | 6,226,552         |
| <b>Provision for work in progress</b> | 10,029,374        | 15,928,705        |
| <b>Total</b>                          | <b>83,714,282</b> | <b>86,267,625</b> |





**36. Other accounts payable:**

The detail of other accounts payable is as follows:

|  | <b>2006</b>      | <b>2005</b>       |
|--|------------------|-------------------|
|  | <b>ThCh\$</b>    | <b>ThCh\$</b>     |
| Exchange insurance contract payables         | 1,113,336        | 22,122,952        |
| Billing on behalf of third parties           | 3,141,464        | 2,402,776         |
| Accrued supports                             | 1,336,131        | 1,420,824         |
| Other accounts payable by received materials | 1,038,908        | 1,193,552         |
| Others                                       | 493,298          | 691,840           |
| <b>Total</b>                                 | <b>7,123,137</b> | <b>27,831,944</b> |

**Juan Cuevas Villegas**  
General Accountant

**José Molés Valenzuela**  
General Manager

***MANAGEMENT'S DISCUSSION AND ANALYSIS OF THE  
CONSOLIDATED FINANCIAL STATEMENTS***

*For the three-month periods ended March 31, 2006 and 2005*

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## Management's Discussion and Analysis of the Consolidated Financial Statements

**COMPAÑÍA DE TELECOMUNICACIONES DE CHILE S.A. AND SUBSIDIARIES****TABLE OF CONTENTS**

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## 1. HIGHLIGHTS

### Consolidated Income and Figures for the Corporation's Business Areas

As of March 31, 2006, Telefónica CTC Chile recorded consolidated net income of Ch\$734 million, whereas in the same period in 2005 it shows net income of Ch\$ 8,507 million.

For comparison purposes, as detailed in the following table, the operating margin reaches 13.8% and 15.9% for the periods ended in March 2006 and 2005, respectively.

The operating income of Telefónica CTC Chile presents a surplus of Ch\$19.45 billion, 14.0% less than the Ch\$22.608 billion reached in the period ended March 31, 2005.

|                         | 2005           | 2006           | % Variation   |
|-------------------------|----------------|----------------|---------------|
| Revenues                | <b>142,255</b> | <b>140,804</b> | <b>-1.0%</b>  |
| Salaries                | -18,025        | -16,482        | -8.6%         |
| Goods and services      | -51,025        | -54,693        | 7.2%          |
| <b>Total Cost</b>       | <b>-69,050</b> | <b>-71,175</b> | <b>3.1%</b>   |
| <b>EBITDA</b>           | <b>73,205</b>  | <b>69,629</b>  | <b>-4.9%</b>  |
| Depreciation            | -50,597        | -50,179        | -0.8%         |
| <b>Operating Income</b> | <b>22,608</b>  | <b>19,450</b>  | <b>-14.0%</b> |
| Operating Margin        | <b>15.9%</b>   | <b>13.8%</b>   |               |

Non-operating income for the period ended as of March 31, 2006 shows a deficit of Ch\$15.012 billion, which compares negatively to the deficit obtained in the same period the previous year in the amount of Ch\$ 9.501 billion, derived mainly from a decrease in financial income together with an increase in other non-operating expenses. Both effects were partly offset by the decrease in financial expenses associated to a lower level of debt and better financing conditions, and a positive price-level restatement effect.

With respect to operating business figures, as of March 31, 2006, Telefónica CTC Chile had a total of 2,418,073 fixed telephone lines, which represents a decrease of 0.8% in relation to March 31, 2005. The Company's ADSL business grew 60.9% in relation to the same period the previous year, with 356,986 customers in service. Long distance traffic through the network of Telefónica CTC Chile, for which access charges are charged, decreased by 19.0% in domestic long distance (DLD) and 24.7% in international long distance (ILD). Total traffic reached 338.4 million minutes and 141.9 million minutes, respectively, as of March 31, 2006.

As of March 31, 2006, the Company had a staff of 3,544, which is a decrease of 7.5% from the staff of 3,833 as of March 31, 2005.

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**Decrease in Financial Debt**

Telefónica CTC Chile has continued to improve its debt level through amortization and prepayment of loans, renegotiation of interest rates and terms of current loans as well as through the global drop in interest rates. As of March 31, 2006, the financial debt reached Ch\$467.263 billion, reflecting a 20.0% decrease in relation to the financial debt of Ch\$585.517 billion recorded as of March 31, 2005. The decrease in the indebtedness levels together with the improved financing conditions and the drop in the value of the dollar translated into a downturn of 44.9% in financial expenses as of March 31, 2006.

**Dividends Policy**

The Ordinary Shareholders Meeting held on April 14, 2005 approved the distribution of both the final and interim dividends and also informed the Dividends Policy for 2005 and future years, which will be a distribution of dividends with a 100% charge to income for each year, by means of an interim dividend in November of each year and a final dividend which will be proposed at the Ordinary Shareholders Meeting.

Likewise, on October 27, 2005, the Board of Directors approved payment of an interim dividend (No.170) of Ch\$11.00 per share, with a charge to 2005 income, equivalent to ThCh\$10,528,728 (historical).

**Permit for Limited Satellite and Cable Television Service**

Through Exempt Resolution No. 1605 of December 23, 2005, the Undersecretary of Telecommunications ( Subtel ) granted Telefónica Multimedia Chile S.A. (formerly Tecnonáutica S.A.) a satellite television limited service permit to operate throughout the national territory for a renewable 10-year term.

In addition, through Resolution No. 81 of February 21, 2006, the Undersecretary of Telecommunications granted Telefónica Multimedia Chile S.A. a cable television limited service permit to provide the service through the broadband network of Telefónica CTC, throughout the national territory for an unlimited term except for the Metropolitan Region, which is covered in the permit granted in 1994.

Subtel dictated the technical standard that establishes that the cable television service can be provided using any technology through physical media, which regulates the operation of the ADSL broadband network to provide television services.

**Wireless Local Public Telephone Concessions on 3,400 - 3,600 MHz Frequency Band**

By means of Resolutions No. 64 and No. 65 of January 20, 2006, the Ministry of Transport and Telecommunications assigned to Telefónica CTC Chile the regional concessions to provide wireless local telephone services in Regions XI and XII, respectively, since it was the only bidder. The resolutions were published in the Official Gazette and in newspapers distributed in both regions on February 7, 2006. The decrees granting those concessions are pending.

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**Modifications of the Regulatory Framework. Extension of the Length of Public Telephone Services Subscriber Number**

By means of Resolution No. 1120, of September 28, 2005, published in the Official Gazette on October 4, 2005, Subtel set a period of 10 months to extend the local telephone numbers in the Primary Zones of Valparaiso and Concepción by one digit. The extension for Santiago and the rest of the zones was deferred.

Furthermore, by means of Decree No. 400, of October 4, 2005, issued by the Ministry of Transport and Telecommunications, the Fundamental Telephone Numbering Technical Plan was modified in order to define the virtual mobile network area code with the number 09, and by means of Exempt Resolution No. 27 of 2006, August 19, 2006 was established as the date in which the new virtual mobile area code will begin operating.

Telefónica CTC Chile is performing the network and systems modifications needed to enable what is established in the regulations on telephone numbers.

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**2. VOLUME STATISTICS, PROPERTY, PLANT AND EQUIPMENT AND STATEMENTS OF INCOME****TABLE No. 1**  
**VOLUME STATISTICS**

| DESCRIPTION   | MARCH     | MARCH     | VARIATION |        |
|---|-----------|-----------|-----------|--------|
|   | 2005      | 2006      | MCh\$     | %      |
| Lines in Service at (end of period)                     | 2,437,542 | 2,418,073 | -19,469   | -0.8%  |
| Total Average Lines in Service                          | 2,432,777 | 2,430,980 | -1,797    | -0.1%  |
| Inter-primary DLD Minute <sup>(2)</sup> (thousands)     | 417,958   | 338,379   | -79,579   | -19.0% |
| Total ILD Minutes <sup>(3)</sup> (thousands)            | 188,546   | 141,889   | -46,657   | -24.7% |
| ILD Minute Outgoing (incl.                              |           |           |           |        |
| Internet)   | 83,084    | 38,811    | -44,273   | -53.3% |
| ILD Minutes Incoming                                    | 105,462   | 103,078   | -2,384    | -2.3%  |
| Line Connections  | 88,778    | 97,695    | 8,917     | 10.0%  |
| ADSL Connections in Service                             | 221,880   | 356,986   | 135,106   | 60.9%  |
| Permanent Personnel Telefónica CTC Chile <sup>(4)</sup> | 2,873     | 2,724     | -149      | -5.2%  |
| Permanent Personnel Subsidiaries <sup>(4)</sup>         | 960       | 820       | -140      | -14.6% |
| Total Corporate Personnel <sup>(4)</sup>                | 3,833     | 3,544     | -289      | -7.5%  |

1. Does not include calls from public phones owned by the Company.
2. DLD: Domestic Long Distance. Corresponds to all outgoing traffic of primary areas attended by Telefónica CTC Chile, including the traffic of *188 Telefónica Mundo and Globus 120*, for which access fees are charged.
3. ILD: International Long Distance. Corresponds to all outgoing and incoming international calls of primary areas attended by Telefónica CTC Chile, including the traffic of *188 Telefónica Mundo and Globus 120*, for which access fees are charged.
4. Does not include staff with contracts for determined term.

**TABLE No. 2**  
**CONSOLIDATED NET PROPERTY, PLANT AND EQUIPMENT**  
*(Figures in millions of pesos as of March 31, 2006)*

| DESCRIPTION                                   | MARCH            | MARCH            | VARIATION      |              |
|---|------------------|------------------|----------------|--------------|
|   | 2005             | 2006             | MCh\$          | %            |
| Land, Infrastructure, Machinery and Equipment | 3,650,483        | 3,672,718        | 22,235         | 0.6%         |
| Projects and Works in Progress                | 64,684           | 71,929           | 7,245          | 11.2%        |
| Accumulated Depreciation                      | (2,326,655)      | (2,479,891)      | (153,236)      | 6.6%         |
| <b>NET PROPERTY, PLANT &amp; EQUIPMENT</b>    | <b>1,264,756</b> | <b>1,388,512</b> | <b>123,756</b> | <b>-8.9%</b> |

**TABLE N° 3**  
**CONSOLIDATED STATEMENTS OF INCOME FOR THE THREE-MONTH PERIODS ENDED MARCH**  
**31, 2006 AND 2005**

(Figures in millions of pesos as of 03.31.06)

| DESCRIPTION                                    | Jan -          | Jan -          | Jan -          | VARIATION      |              |
|--|----------------|----------------|----------------|----------------|--------------|
|  | Mar            | Dec            | Mar            | (2006/2005)    |              |
|  | 2005           | 2005           | 2006           | MCh\$          | %            |
| <b>OPERATING REVENUES</b>                      |                |                |                |                |              |
| <b>FIXED TELECOMMUNICATIONS</b>                | <b>107.083</b> | <b>440.154</b> | <b>108.030</b> | <b>947</b>     | <b>0,9%</b>  |
| <b>Basic Telephony</b>                         | <b>73.380</b>  | <b>293.403</b> | <b>67.569</b>  | <b>(5.811)</b> | <b>-7,9%</b> |
| Fixed Monthly                                  | 32.775         | 123.168        | 24.201         | (8.574)        | -26,2%       |
| Variable charge                                | 24.668         | 96.617         | 19.568         | (5.100)        | -20,7%       |
| Connections and Other Installations            | 675            | 3.271          | 434            | (241)          | -35,7%       |
| Flexible Plans (Minutes)                       | 8.612          | 45.590         | 17.565         | 8.953          | 104,0%       |
| Value Added Services                           | 5.257          | 19.417         | 4.345          | (912)          | -17,3%       |
| Other Basic Telephony Services                 | 1.393          | 5.340          | 1.456          | 63             | 4,5%         |
| <b>BROADBAND</b>                               | <b>8.147</b>   | <b>42.771</b>  | <b>13.784</b>  | <b>5.637</b>   | <b>69,2%</b> |
| ADSL   | 6.533          | 31.823         | 10.848         | 4.315          | 66,0%        |
| Internet Connection for Companies              | 1.614          | 10.948         | 2.936          | 1.322          | 81,9%        |
| <b>Access Charges and Interconnections (1)</b> | <b>10.170</b>  | <b>43.873</b>  | <b>12.183</b>  | <b>2.013</b>   | <b>19,8%</b> |
| Domestic Long Distance                         | 2.740          | 10.313         | 2.222          | (518)          | -18,9%       |
| International Long Distance                    | 654            | 2.364          | 413            | (241)          | -36,9%       |
| Access Charges Mobile - Fixed                  | 2.941          | 14.187         | 4.375          | 1.434          | 48,8%        |
| Other Interconnection Services                 | 3.835          | 17.009         | 5.173          | 1.338          | 34,9%        |
| <b>Other Local Telephone Services</b>          | <b>15.386</b>  | <b>60.107</b>  | <b>14.494</b>  | <b>(892)</b>   | <b>-5,8%</b> |
| Advertising in Telephone Directories           | 1.044          | 5.353          | 902            | (142)          | -13,6%       |
| ISP (Switchboard and Dedicated)                | 666            | 2.522          | 551            | (115)          | -17,3%       |
| Teleemergencia (Security Services)             | 1.913          | 8.057          | 2.234          | 321            | 16,8%        |
| Public Phones                                  | 2.675          | 9.790          | 2.530          | (145)          | -5,4%        |
| Interior Installation and Equipment Rental     | 7.783          | 30.595         | 7.697          | (86)           | -1,1%        |
| Equipment Marketing                            | 1.305          | 3.790          | 580            | (725)          | -55,6%       |
| <b>LONG DISTANCE</b>                           | <b>15.511</b>  | <b>57.798</b>  | <b>14.026</b>  | <b>(1.485)</b> | <b>-9,6%</b> |
| Long Distance                                  | 6.098          | 23.198         | 5.556          | (542)          | -8,9%        |
| International Service                          | 5.615          | 19.406         | 5.137          | (478)          | -8,5%        |
| Network capacity and circuit rentals           | 3.798          | 15.194         | 3.333          | (465)          | -12,2%       |
| <b>CORPORATE COMMUNICATIONS</b>                | <b>18.963</b>  | <b>77.978</b>  | <b>18.054</b>  | <b>(909)</b>   | <b>-4,8%</b> |
| Terminal Equipment                             | 2.378          | 13.338         | 2.284          | (94)           | -4,0%        |
| Complementary Services                         | 3.432          | 14.622         | 3.379          | (53)           | -1,5%        |
| Data Services                                  | 8.224          | 28.034         | 6.127          | (2.097)        | -25,5%       |
| Dedicated links and others                     | 4.929          | 21.984         | 6.264          | 1.335          | 27,1%        |



|   |                  |                  |                  |                |               |
|---|------------------|------------------|------------------|----------------|---------------|
| <b>OTHER BUSINESSES (2)</b>                     | <b>698</b>       | <b>3.038</b>     | <b>694</b>       | <b>(4)</b>     | <b>-0,6%</b>  |
| <b>TOTAL OPERATING REVENUES</b>                 | <b>142.255</b>   | <b>578.968</b>   | <b>140.804</b>   | <b>(1.451)</b> | <b>-1,0%</b>  |
| <b>OPERATING COSTS</b>                          | <b>(86.740)</b>  | <b>(371.935)</b> | <b>(89.716)</b>  | <b>(2.976)</b> | <b>3,4%</b>   |
| Salaries  | (9.065)          | (42.587)         | (8.871)          | 194            | -2,1%         |
| Depreciation                                    | (48.052)         | (189.121)        | (48.228)         | (176)          | 0,4%          |
| Other Operating Costs                           | (29.623)         | (140.227)        | (32.617)         | (2.994)        | 10,1%         |
| <b>ADMINISTRATIVE AND SELLING COSTS</b>         | <b>(32.907)</b>  | <b>(120.198)</b> | <b>(31.638)</b>  | <b>1.269</b>   | <b>-3,9%</b>  |
| <b>TOTAL OPERATING COSTS</b>                    | <b>(119.647)</b> | <b>(492.133)</b> | <b>(121.354)</b> | <b>(1.707)</b> | <b>1,4%</b>   |
| <b>OPERATING INCOME</b>                         | <b>22.608</b>    | <b>86.835</b>    | <b>19.450</b>    | <b>(3.158)</b> | <b>-14,0%</b> |
| Interest Income                                 | 3.479            | 7.961            | 673              | (2.806)        | -80,7%        |
| Other Non-operating Income                      | 602              | 3.097            | 499              | (103)          | -17,1%        |
| Income from Investment in Related Companies (3) | 401              | 1.675            | 422              | 21             | 5,2%          |
| Interest Expenses                               | (8.977)          | (29.412)         | (4.943)          | 4.034          | -44,9%        |
| Amortization of Goodwill                        | (389)            | (1.579)          | (1.113)          | (724)          | 186,1%        |
| Other Non-operating Expenses                    | (1.496)          | (13.038)         | (10.125)         | (8.629)        | s.c.          |
| Price-level restatement                         | (3.121)          | 2.891            | (425)            | 2.696          | -86,4%        |
| <b>NON-OPERATING INCOME</b>                     | <b>(9.501)</b>   | <b>(28.405)</b>  | <b>(15.012)</b>  | <b>(5.511)</b> | <b>58,0%</b>  |
| <b>INCOME BEFORE INCOME TAX</b>                 | <b>13.107</b>    | <b>58.430</b>    | <b>4.438</b>     | <b>(8.669)</b> | <b>-66,1%</b> |
| Income taxes                                    | (4.619)          | (33.292)         | (3.769)          | 850            | -18,4%        |
| Minority Interest                               | 19               | (30)             | 65               | 46             | 242,1%        |
| <b>NET INCOME (4)</b>                           | <b>8.507</b>     | <b>25.108</b>    | <b>734</b>       | <b>(7.773)</b> | <b>-91,4%</b> |

- (1) Due to accounting consolidation does not include access charges of 188 Mundo Telefónica and Globus.
- (2) Includes revenues from T-gestiona, Telepeajes and Tecnonáutica
- (3) For the purposes of a comparative analysis, participation in income from investments in related companies is shown net (net income/losses).
- (4) For comparison purposes certain reclassifications have been made to the 2005 statements of income.

### 3. ANALYSIS OF INCOME FOR THE PERIOD

#### 3.1 OPERATING INCOME

As of March 31, 2006, operating income amounted to Ch\$19.450 billion, which represents a 14.0% decrease with respect to the previous year.

##### Operating Income

Operating income for the period amounted to Ch\$140,804 million, or a decrease of 1.0% in relation to the income for the period from January to March 2005 of Ch\$142.255 billion.

This variation mainly resulted from a decrease in long distance income and in income from corporate communications, partly offset by an increase in fixed telephone services.

**Revenues from Local Telephone Services:** Revenues from local telephone services increased by 0.9%, as a result of a combination of factors. There was a 7.9% drop in **basic telephone services** with respect to the previous year, derived from a 20.7% decrease in the level of **variable charge**, which shows the effect of lower income derived from the application of the new rate decree, the downturn in traffic per line and the migration of customers to flexible plans recorded since 2005. **Fixed monthly charges**, corresponding to the fixed monthly charge for connection to the network, decreased 26.2%, which is mainly explained by the incorporation of new customers to flexible plans. This effect was offset by the effect of higher income due to the application of the new rate decree. Consequently, the incorporation of customers to **flexible plans** positively contributed to the Ch\$8.953 billion increase in income. Income from **connections and other installations** fell 35.7% with respect to the previous year, whereas **value added services** decreased by 17.3%, and **other basic telephone services income** increased by 4.5% .

**Broadband** services increased 69.2% in the period from January to March 2006, to Ch\$13.784 billion, whereas in the same period the previous year income from these services amounted to Ch\$8.147 billion.

**Access charges and interconnections** increased by 19.8%, mainly due to the 34.9% increase in **other interconnection services**, with particularly noteworthy increases in media rental services, carrier information and connection services, and unbundling services, together with a 48.8% increase in **mobile and fixed access charges**. On the other hand there was a 36.9% drop in income from **international long distance** access charges and 18.9% in **domestic long distance**.

**Other fixed telephone services** decreased by 5.8%, equivalent to Ch\$892 million, primarily as a result of the Ch\$725 million drop in income from commercialization of equipment.

**Long Distance:** Revenues from these services decreased by 9.6% in comparison to 2005, due to a decrease of 8.9% and 8.5% in DLD and ILD, respectively, which was influenced by a decrease in average outgoing long distance, a 6.6% drop in DLD and a 9.9% increase in outgoing ILD traffic. The above is increased by the drop in income from media and circuit rental.

**Corporate Communications:** Revenue from corporate communications shows a 4.8% decrease in respect to the previous year, due to a drop in all lines of business: 25.5% in data

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services together with a 4.0% decrease in income from sale of terminal equipment and a 1.5% decrease in income from complementary services. This was partly offset by a 27.1% increase in income from circuits and others.

***Other Businesses:*** This revenue shows a 0.6% decrease mainly due to decrease in income from the subsidiary Telepeajes (teletoll services).

### **Operating Costs**

Operating costs for the period reached Ch\$121.354 billion, increasing by 1.4% in relation to 2005, when they reached Ch\$119.647 billion. This is explained mainly by an increase in the line of goods and services and depreciation, which effect was partly offset by a tendency to reduce expenses, primarily in remunerations, due to the efforts put into efficient use of resources applied by the Company in the last few years.

### **3.2 NON-OPERATING INCOME**

***Non-operating income*** obtained in the period ended March 31, 2006 shows a loss of Ch\$15.012 billion, whereas in the previous year non-operating income reached Ch\$9.501 billion. The change in non-operating income is broken down as follows:

***Financial income*** shows a decrease of 80.7%, mainly because in 2005, the greater volume of funds available from the sale of the subsidiary Móviles was temporarily allocated to financial investments.

***Other non-operating income*** amounted to Ch\$499 million, which is lower than the Ch\$602 million reached in 2005. This is mainly due to lower income obtained on the sale of recovered material.

***Financial expenses*** decreased by 44.9% in 2006, as a product of lower interest bearing debt, renegotiation of the rates of current loans, the drop in market interest rate and the effect of the drop in the exchange rate.

***Amortization of goodwill*** shows a Ch\$724 million increase in relation to 2005, mainly due to the full amortization of goodwill of Tecnonaútica, due to the restructuring of the Telefonica CTC Chile group.

***Other non-operating expenses*** reached Ch\$10,125 million, a Ch\$8,629 million increase in respect to 2005. This is mainly derived from the cost of the restructuring carried out in 2006.

***Price-level restatement*** in 2006 shows a loss of Ch\$425 million, mainly due to the variations in the CPI, UF and exchange rate. It should be noted that a 100% hedge has been maintained for exchange rate fluctuation and a 79% hedge for interest rate. The Company's exchange rate (peso-dollar) hedge policy was, in large part, able to neutralize the effect of the exchange rate variation in 2005 and 2006.

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### 3.3 NET RESULT FOR THE PERIOD

The Company recorded net income of Ch\$734 million for the 2006 period, whereas in the 2005 period, net income was Ch\$8.507 billion. The lower income obtained in the 2006 period in comparison to 2005 is derived from a 14.0% operating surplus and the increase in the non-operating deficit equivalent to Ch\$5,511 million; these effects are offset by the lower income tax liability.

### 4. RESULTS BY BUSINESS AREA

**Local Telephone Business:** Net loss of Ch\$4.855 billion as of March 31, 2006, comparatively lower than the surplus of Ch\$806 million recorded in 2005, due to lower non-operating income, and the higher operating deficit, mainly due to recording the cost of the restructuring carried out in the first quarter of 2006.

**Corporate Communications Business:** This business contributed net income of Ch\$2.625 billion, an 11.6% decrease in relation to 2005, when net income was Ch\$2.968 billion. The difference is the result of lower operating income due to the cost of restructuring carried out in the first quarter of 2006.

**Long Distance Business:** As of March 31, 2006, the Company presented net income of Ch\$3.195 billion, lower than that reached in 2005 which amounted to Ch\$4,550 million. This variation is produced mainly by a 16.1% drop in operating income and operating deficit of Ch\$178 million, which compares negatively to the non-operating surplus obtained in the first quarter of 2005 in the amount of Ch\$325 million.

**Other Businesses:** The businesses as a whole generated a net loss of Ch\$232 million and operating income of Ch\$37 million in the period ended March 31, 2006, whereas during the same period the previous year, they recorded net income of Ch\$183 million, with an operating surplus of Ch\$103 million. These businesses mainly include Telepeajes (teletoll services), Tecnonáutica and T-gestiona.

The following table shows the contribution of each business area to corporate results:

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**REVENUES AND COSTS BY BUSINESS**  
**AS OF MARCH 31, 2005 AND 2006**  
**(Figures in millions of pesos as of 03.31.06)**

|   | Fixed Telecommunications |                  |                  | Corporate Communications |                 |                 | Long Distance   |                 |
|---|--------------------------|------------------|------------------|--------------------------|-----------------|-----------------|-----------------|-----------------|
|   | Jan-Mar                  | Jan-Dec          | Jan-Mar          | Jan-Mar                  | Jan-Dec         | Jan-Mar         | Jan-Mar         | Jan-Dec         |
|   | 2005                     | 2005             | 2006             | 2005                     | 2005            | 2006            | 2005            | 2005            |
| <b>Operating Revenues</b>                 | <b>122.365</b>           | <b>499.694</b>   | <b>119.535</b>   | <b>21.636</b>            | <b>87.718</b>   | <b>20.882</b>   | <b>20.388</b>   | <b>78.853</b>   |
| Revenues                                  | 107.084                  | 440.152          | 108.030          | 18.962                   | 77.979          | 18.054          | 15.512          | 57.798          |
| Intercompany Transfers                    | 15.281                   | 59.542           | 11.505           | 2.674                    | 9.739           | 2.828           | 4.876           | 21.055          |
| <b>Operating Expenses</b>                 | <b>(108.924)</b>         | <b>(437.702)</b> | <b>(108.844)</b> | <b>(18.312)</b>          | <b>(73.256)</b> | <b>(17.149)</b> | <b>(15.378)</b> | <b>(72.941)</b> |
| Payroll                                   | (13.736)                 | (59.499)         | (12.325)         | (2.499)                  | (10.543)        | (2.350)         | (502)           | (2.612)         |
| Depreciation                              | (45.216)                 | (175.638)        | (44.693)         | (2.560)                  | (9.663)         | (2.728)         | (2.779)         | (10.592)        |
| Goods and Services                        | (35.469)                 | (143.975)        | (39.915)         | (4.590)                  | (19.515)        | (4.526)         | (8.807)         | (44.623)        |
| Intercompany Transfers                    | (14.503)                 | (58.590)         | (11.911)         | (8.663)                  | (33.535)        | (7.545)         | (3.290)         | (15.114)        |
| <b>Operating Income</b>                   | <b>13.441</b>            | <b>61.992</b>    | <b>10.691</b>    | <b>3.324</b>             | <b>14.462</b>   | <b>3.733</b>    | <b>5.010</b>    | <b>5.912</b>    |
| <b>Non-operating Income and Expenses</b>  |                          |                  |                  |                          |                 |                 |                 |                 |
| Financial Expenses                        | (8.980)                  | (29.396)         | (4.930)          | 13                       | (7)             | (13)            | (4)             | (4)             |
| Other Income and Expenses                 | (973)                    | 4.113            | (9.189)          | 46                       | (1.226)         | (331)           | 369             | (1.735)         |
| Intercompany Transfers                    | 640                      | 1.599            | 566              | 107                      | 851             | 140             | (40)            | 1.111           |
| <b>Non-operating Income</b>               | <b>(9.313)</b>           | <b>(23.684)</b>  | <b>(13.553)</b>  | <b>166</b>               | <b>(382)</b>    | <b>(204)</b>    | <b>325</b>      | <b>(628)</b>    |
| <b>EBITDA (*) and extraordinary items</b> | <b>58.324</b>            | <b>243.342</b>   | <b>46.761</b>    | <b>6.037</b>             | <b>23.750</b>   | <b>6.270</b>    | <b>8.118</b>    | <b>15.880</b>   |
| <b>Taxes and Others</b>                   | <b>(3.322)</b>           | <b>(26.377)</b>  | <b>(1.993)</b>   | <b>(522)</b>             | <b>(3.334)</b>  | <b>(904)</b>    | <b>(785)</b>    | <b>(3.678)</b>  |
| <b>Income After Taxes</b>                 | <b>806</b>               | <b>11.931</b>    | <b>(4.855)</b>   | <b>2.968</b>             | <b>10.746</b>   | <b>2.625</b>    | <b>4.550</b>    | <b>1.606</b>    |

(\*) EBITDA : Earnings before taxes, interest, depreciation, amortization and extraordinary items.

**GRAPH OF NET INCOME (LOSS) BY BUSINESS**  
**AS OF MARCH 31, 2005 AND 2006**  
**(Figures in millions of pesos as of 03.31.06)**

**5. STATEMENT OF CASH FLOWS**

**TABLE No. 4**  
**CONSOLIDATED CASH FLOWS**  
*(Figures in millions of pesos as of March 31, 2006)*

| DESCRIPTION  | JAN-MAR | JAN-MAR | VARIATION |        |
|--|---------|---------|-----------|--------|
|  | 2005    | 2006    | MCh\$     | %      |
| Net cash from operating activities                   | 74,903  | 48,207  | -26,696   | -35.6% |
| Net cash from financing activities                   | -69,789 | -38,463 | 31,326    | -44.9% |
| Net cash from investing activities                   | -25,929 | -18,928 | 7,001     | -27.0% |
| Effect of inflation on cash and cash equivalents     | 1,358   | 281     | -1,077    | -79.3% |
| Net change in cash and cash equivalents for the year | -19,457 | -8,903  | 10,554    | -54.2% |

The negative variation of Ch\$8.903 billion in cash flows for the 2006 period compared to the negative variation of Ch\$19,457 million in 2005 is because in 2006 cash flows from financing activities increased, and also less cash flows were allocated to short-term investments. Both effects are offset by the lower cash flows obtained from operating activities.



## 6. FINANCIAL INDICATORS

*TABLE No. 5*  
*CONSOLIDATED FINANCIAL INDICATORS*

| DESCRIPTION  | JAN-MAR<br>2005 | JAN-DEC<br>2005 | JAN-MAR<br>2006 |
|--|-----------------|-----------------|-----------------|
| <b><i>LIQUIDITY RATIO</i></b>  |                 |                 |                 |
| <b><u>Current Ratio</u></b>  |                 |                 |                 |
| (Current Assets / Current Liabilities)                                 | 1.13            | 0.97            | 1.36            |
| <b><u>Acid Ratio</u></b>   |                 |                 |                 |
| (Most liquid assets / Current Liabilities)                             | 0.31            | 0.33            | 0.23            |
| <b><i>DEBT RATIOS</i></b>  |                 |                 |                 |
| <b><u>Debt Ratio</u></b>   |                 |                 |                 |
| (Total Liabilities / Shareholders' Equity)                             | 0.86            | 0.84            | 0.80            |
| <b><u>Long-term Debt Ratio</u></b>                                     |                 |                 |                 |
| (Long-term Liabilities / Total Liabilities)                            | 0.58            | 0.58            | 0.56            |
| <b><u>Financial Expenses Coverage</u></b>                              |                 |                 |                 |
| (Income Before Taxes and Interest / Interest Expenses)                 | 2.07            | 2.72            | 2.66            |
| <b><i>RETURN AND EARNINGS PER SHARE RATIO</i></b>                      |                 |                 |                 |
| <b><u>Operating Margin</u></b>   |                 |                 |                 |
| (Operating Income / Operating Revenues)                                | 15.9%           | 15.0%           | 13.8%           |
| <b><u>Operational Income Return</u></b>                                |                 |                 |                 |
| (Operating Income / Net Property, Plant and Equipment <sup>(1)</sup> ) | 1.6%            | 6.2%            | 1.5%            |
| <b><u>Earnings per Share</u></b>                                       |                 |                 |                 |
| (Net Income / Average number of paid shares each year)                 | Ch\$8.50        | Ch\$26.31       | Ch\$0.8         |
| <b><u>Return on Equity</u></b>   |                 |                 |                 |
| (Income / Average shareholders' equity)                                | 0.83%           | 2.60%           | 0.08%           |
| <b><u>Profitability of Assets</u></b>                                  |                 |                 |                 |
| (Income/Average assets)  | 0.44%           | 1.38%           | 0.04%           |
| <b><u>Operating Assets</u></b>   |                 |                 |                 |
| (Net income / Average operating assets <sup>(2)</sup> )                | 0.60%           | 1.85%           | 0.06%           |



**Return on Dividends**

|   |       |       |       |
|---|-------|-------|-------|
| (Paid dividends / Market Price per Share) | 37.1% | 10.8% | 10.3% |
|---|-------|-------|-------|

***ACTIVITY INDICATORS***

|  |     |           |     |           |     |           |
|--|-----|-----------|-----|-----------|-----|-----------|
| <b><u>Total Assets</u></b>   | M\$ | 1,913,438 | M\$ | 1,703,674 | M\$ | 1,665,296 |
| <b><u>Sale of Assets</u></b>   | M\$ | 156       | M\$ | 1,314     | M\$ | 340       |
| <b><u>Investments in other companies and property, plant and equipment</u></b> | M\$ | 10,579    | M\$ | 76,173    | M\$ | 16,995    |

**Inventory Turnover**

|                                     |      |      |      |
|-------------------------------------|------|------|------|
| (Cost of Sales / Average Inventory) | 1.90 | 2.78 | 3.45 |
|-------------------------------------|------|------|------|

**Days in Inventory**

|  |        |        |        |
|--|--------|--------|--------|
| (Average Inventory / Cost of sales times 360 days) | 189.19 | 129.57 | 104.48 |
|--|--------|--------|--------|

(1) **Figures at the beginning of the year, restated.**

(2) **Property, plant and equipment are considered operating assets**

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From the previous table we emphasize the following:

The common liquidity index shows an increase due to a 26.8% drop in current assets, whereas current liabilities decreased by 39.1%, due to a decrease in the financial debt in comparison to December of the previous year.

The decrease in the debt ratio is explained by a 16.7% drop in the level of demand liabilities whereas shareholders equity decreased by 10%, mainly due to distribution of retained earnings through the payment of dividends.

#### **7. EXPLANATION OF THE MAIN DIFFERENCES BETWEEN MARKET OR ECONOMIC VALUE AND THE BOOK VALUE OF THE COMPANY S ASSETS**

Due to market inaccuracies regarding the capital assets of the sector, there is no economic or market value that can be compared to the respective accounting values. However, there are certain buildings with a book value equal or close to zero. These buildings have a market value, but compared to the book value it is not significant with respect to the Company s assets in the aggregate.

In relation to other assets, such as marketable securities (shares and promissory notes) with a referential market value, the corresponding provisions have been established when the market value is less than the book value.

#### **8. REGULATORY ASPECTS Fixed Telephony Tariff Decree**

On May 4, 2004, the Ministries of Transport and Telecommunications and of Economy, Development and Reconstruction dictated Rate Decree No. 169, which they submitted together with the supporting report to the Chilean General Comptroller for the recording process.

On February 8, 2005, the Chilean General Comptroller recorded Tariff Decree No. 169.

Tariff Decree No. 169 was published in the Official Gazette on February 11, 2005. Telefónica CTC Chile enabled the application of the new rates to its customers in its systems and began the rebilling process as of May 6, 2004.

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**Tariff Flexibility**

By means of Resolution No. 709 of October 13, 2003, the Resolution Commission decided to: Accept the request on fs 476 of Compañía de Telecomunicaciones de Chile S.A., only inasmuch as it is necessary to clarify Resolution No. 686, of May 20, 2003, recorded on fs. 440, in the sense that the resolution implies that the market conditions are not present to authorize tariff freedom, and therefore a maximum rate must be set. Lower tariffs or plans may be offered, but the conditions of these, which protect and provide due guarantees to the user from those in dominant positions in the market, must be regulated by the respective authority.

The Official Gazette of February 26, 2004, published Decree No. 742, of December 24, 2003, issued by the Ministry of Transport and Telecommunications, which establishes the regulations that govern, without restrictions as to levels or structure, the conditions under which various plans and joint offers can be offered by the dominant operators of the local telephone service.

The rate flexibility allows Telefónica CTC Chile to offer its customers various commercial plans, other than the plan regulated by the authority, as per the conditions defined by the Company itself.

Telefónica CTC Chile began commercializing the different plans for local telephone public service, so that the interested public can opt for an alternative that is different to the rate structure defined by the regulator.

**Mobile Telephone Tariff Decree**

On January 20, 2004, the Ministries of Transport and Telecommunications and of Economy, Development and Reconstruction, by means of a decree, set the levels, structure and indexation mechanisms of the services subject to tariff setting.

On April 12, 2004, the Chilean General Comptroller recorded the decrees that set the tariffs for access charges for mobile telephony companies. The tariff decrees were published in the Official Gazette of April 14, 2004.

**Modifications of the Regulatory Framework****Extension of the length of the public telephone services subscriber number.**

By means of Resolution No. 1120, of September 28, 2005, published in the Official Gazette on October 4, 2005, Subtel set a period of 10 months to extend the local telephone numbers in the Primary Zones of Valparaiso and Concepción by one digit. The extension for Santiago and the rest of the zones was deferred.

Furthermore, by means of Decree No. 400, of October 4, 2005, issued by the Ministry of Transport and Telecommunications, the Fundamental Telephone Numbering Technical Plan was modified in order to define the virtual mobile network area code as the number 09 and Exempt Resolution No. 27 establishes August 19, 2006 as the date on which the new code of the virtual mobile area will begin operating.

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Telefónica CTC Chile is performing the network and system modifications required to enable the requirements of the telephone numbers regulation.

**New format of Single Telephone Bill.**

Decree No. 510 issued by the Ministry of Transport and Telecommunications establishes the minimum content and other elements of the Single Telephone Bill and a period of 120 days is set to apply the provisions established in the mentioned decree.

On January 12, 2005, Telefónica CTC Chile requested from Subtel approval of the contents and design of the new Single Telephone bill in conformity with Decree No. 510.

Outside of the specified comment period, Subtel made observations to the proposal made by Telefónica CTC Chile, ordering them to be rectified before issuance to the public, in addition to issuing an Official Circular with instructions for applying the Regulation.

Telefónica CTC Chile filed a complaint before the Chilean General Comptroller against Subtel pertaining to the legality of infringing on the standard that establishes that after 30 days the proposal made by the concessionary will be understood to be fully approved, which did in fact occur and that is not recognized in the pronouncement.

On August 30, 2005, Subtel responded to the Chilean General Comptroller in respect to the legality complaint filed by Telefónica CTC against the acts of Subtel which made observations on the new model of the Single Telephone Bill outside of the specified comment period.

In its report, Subtel recognizes that it made observations outside of the specified comment period and formulates its defense on the basis that Telefónica CTC Chile's model of telephone bill does not in accordance with the legal ordinance.

On October 6, 2005, Telefónica CTC Chile presented a writ before the Chilean General Comptroller answering the arguments made by Subtel in its report.

As support for the legal thesis stated in the complaint, Telefónica CTC Chile attached a Legal Report to the Chilean General Comptroller from the Administrative Law Professor, which confirms the relevance of the complaint that was filed.

By means of verdict No. 09695, of February 28, 2006, the Chilean General Comptroller declared that the single telephone bill model presented by Telefónica CTC Chile must be understood to be fully approved, and furthermore it indicated that what was stated by Subtel in their official circular No. 09, of 2005, which determines the sense and scope of the standards of Decree No. 510 of 2004 is not applicable to Telefónica CTC Chile.

**Technical Standard that classifies complementary services into categories.**

By means of Exempt Resolution No. 1319, of October 6, 2004, Subtel established the categories of complementary services and attributed the numeration to the respective categories of complementary services that users can access through the public telephone network.

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Telefónica CTC Chile made the adjustments to its network to enable, among other aspects, numbering of the complementary Internet narrowband access service, the deadline for which is April 8, 2006.

### **Public consultation of regulation projects.**

In July and August 2004, Subtel began making public inquiries to the relevant parties of the telecommunications sector with respect to proposals for regulations regarding Network Unbundling and IP Telephony.

The Network Unbundling proposal, which was subjected to a new public inquiry in December 2004, defines the services, their operating conditions and adds new services that modify the conditions already defined in the tariff decree, defining new obligations that make unbundling more troublesome (obligation to invest, new rights of subscribers, discrimination of obligations according to the technology used, etc.). Furthermore, the obligation to resell is established for mobile companies and the resale conditions are regulated for wholesalers of alternative tariff plans offered by Telefónica CTC Chile. The Company participated in those public inquiries making its observations and formulating its legal objections among which it emphasized that a large part of those proposals are matters of law and not mere regulations, at the same time that other aspects of the regulatory proposal cannot even be addressed in a law since they affect rights guaranteed by the Chilean Constitution.

Regarding the IP Telephony proposal, it defines a special type of broadband telephony, which is provided using the existing broadband infrastructure, with fewer regulatory requirements than traditional telephony (for example, the multicarrier system for DLD is not applicable), which discriminates against traditional operators who could not provide the service under these same conditions. The Company, as well as other operators, made their observations and legal objections to this proposal since they consider it, among other aspects, discriminatory and an attack on the development of the industry since it discourages investment in new infrastructure and in broadband.

As of March 31, 2006, Subtel has not made a pronouncement on either case regarding the observations and legal objections made by the Company and by other companies in the sector, nor has it sent to the Chilean General Comptroller the final texts of such regulations for recording.

### **Lawsuit against the State of Chile**

On October 31, 2001, Telefónica CTC Chile, seeking to correct errors in Tariff Decree No. 187 of 1999, filed a motion for reconsideration with the Ministries requesting corrections to the 1999 Tariff Decree No. 187. On January 29, 2002, the Ministries issued a joint rejection of this request, explaining that having carefully evaluated, only the feasibility and timeliness of the petition made, considering the set of circumstances of the problem and the prudence that must orient public actions, and that the rejection has had no other motivation than to protect the general interest and progress of the telecommunications services.

Having exhausted all administrative remedies aimed at correcting the illegal actions taken in the tariff-setting process of May 1999, in March 2002, Telefónica CTC Chile filed a lawsuit for damages against the Government in the amount of Ch\$181,038,411,056 plus readjustments and

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interest, covering past and future damages incurred up to May 2004.

Expert reports were presented on various aspects of the case supporting the position held by Telefónica CTC Chile. On March 29, 2005, the court dictated a resolution summoning the parties to the first instance sentencing, which involves an end to the discussion and evidence stage. A sentence should be declared in the near future.

**Voissnet Makes an Accusation Before the National Economic Attorney General's Office (Fiscalía Nacional Económica) and Files Suit Before the Antitrust Commission, both against Telefónica CTC Chile**

On January 20, 2005, Telefónica CTC Chile responded to the accusation made by Voissnet filed before the National Economic Attorney General's Office for alleged events which in its opinion attempted to violate free competition, development and growth of Internet technology, fundamentally of broadband telephony, and access to broadband, since they establish the prohibition of carrying voice using the Internet broadband access provided by Telefónica CTC Chile.

On March 14, 2005 Telefónica CTC Chile responded to the complaint filed by Voissnet before the Antitrust Commission (Tribunal de Defensa de la Libre Competencia), hereafter TDLC, which is founded on the same facts that Voissnet indicated in the accusation filed before the National Economic Attorney General's Office. Voissnet's intention is for the TDLC to force Telefónica CTC to allow third parties to provide IP Telephony through the Internet using the ADSL owned by Telefónica.

Telefónica CTC Chile rejected each and every part of the accusations made by the accuser, providing market, legal and regulatory information regarding development of the broadband market in Chile, stating that it has made considerable investments to develop broadband in Chile and has facilitated the participation of all ISP through an open model, and that it is not opposed to IP telephony, but rather to the anti-competitive practices that companies are attempting to use, taking advantage of investments made by others.

Telefónica CTC Chile in turn filed a countersuit against Voissnet, in order for the Court to correct, prohibit and suppress the serious attempts to limit free competition incurred by that company, by providing telephone services to its subscribers without having the concession required by Law, or complying with the legal, regulatory and technical regulations applicable to telephony that are fulfilled by the public telephone service concessionaries, applying market skimming practices of customers of telephone concessionaries with a greater amount of traffic and which have the broadband service, and taking advantage of the existing infrastructure owned by the mentioned companies, without their authorization, and without any retribution or payment whatsoever for the use of the public telephone network and equipment used to provide broadband Internet access.

Subtel submitted the report requested by the TDLC in relation to the complaint presented by Voissnet, without making reference to the countersuit presented by Telefónica CTC Chile, questioning the contractual restrictions imposed by Telefónica CTC Chile.

On April 8, 2005, Voissnet answered the counterplea filed by Telefónica CTC Chile, requesting that it be rejected in all its parts. By means of resolution dated June 1, 2005, the TDLC deemed that there were no substantial, relevant and controversial facts, therefore the case was not to be

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received for evidence, but a date would be set to hear the case.

Telefónica CTC Chile appealed the resolution of the TDLC since it considers that there are substantial, relevant and controversial facts that both parties must prove within the evidence stage, and which are determinant for due resolution of this process and it requested that the Court dismiss it and replace it receiving the case for the evidence stage.

On June 22, 2005, the TDLC dismissed the appeal made by Telefónica CTC Chile, ratifying that in this case only legal and not factual aspects must be clarified.

On August 16, 2005, Telefónica CTC Chile was notified of the requirement filed against it by the Fiscalía Nacional Económica (FNE), based on the same conducts alleged by Voissnet against Telefónica CTC Chile in its complaint of December 2004. In its requirement, the FNE mainly requests the following from the TDLC: That it declare that Telefónica CTC has infringed on free trade, through the creation of artificial entry barriers for new competitors in the local fixed telephony market, ordering it to abstain from persisting in any act or conduct the purpose of which is to prevent granting of IP Telephony; that the Megavía DSL Contracts for Broadband Access to Internet signed by CTC with the ISP be modified, in order to immediately terminate the application of the clauses that prohibit granting of IP voice service; that Telefónica CTC Chile be fined 350 annual tax units ( unidades tributarias anuales ), or whatever fine the TDLC determines, and payment of the costs of this case; and that a request be made to the President of the Chile so that, through the applicable ministries, a study should be performed of the modifications needed to the legal and regulatory precepts of the current regulatory framework of the telecommunications market.

On September 2, 2005, Telefónica CTC Chile answered the complaint of the FNE.

The TDLC ordered both processes to be accumulated, which means that the Voissnet lawsuit is suspended until the new lawsuit arrives at the same stage. Therefore, the allegations cited August 11, 2005 were suspended.

On October 4, 2005, the TDLC accepted the petition of Telefónica CTC Chile to receive the case for evidence, setting the points of evidence. On October 11, 2005, accepting the request of the Company and the FNE for reinstatement, the Court modified the originally defined points of evidence.

On December 15, 2005, Telmex Servicios Empresariales S.A. became a party to the process as a third party interested in the results of the lawsuit, stating to the TDLC that in accordance with current legislation, the broadband voice services provided by Voissnet are a public telecommunications service, and therefore there is no reason whatsoever that in their provision they are exempt from the regime applicable to all local telephone operators.

On December 20, 2005, the TDLC began hearing evidence from witnesses, with Voissnet providing evidence first followed by the National Economic Attorney General's Office and finally Telefónica CTC Chile. Likewise, on December 27, 2005, the parties filed their technical economic reports.

During January, March and April 2006, the TDLC will hear the declarations of the three parties involved in the lawsuit.

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**Setting Rates for Post Supports**

Telefónica CTC Chile together with other telecommunications companies presented objections before the Panel of Experts of the Electricity Law, regarding rates for services corresponding to support on posts, proposing an annual rate for each post support of approximately 0.02 UF.

Similarly, the distribution companies also presented before the Panel of Experts their objections regarding the post support rates proposed by the National Energy Commission, proposing an annual rate of between 0.4 UF and 0.5 UF for each support.

On July 7, 2005 Telefonica CTC Chile and the rest of the telecommunications companies that submitted objections to the Panel of Experts, presented their observations of the objections formulated by the electric companies.

The Court of Appeals rejected the protection petition filed by Chilectra S.A., against the judgment of the Panel of Experts, which made a pronouncement on the objections submitted by the Distributors and the telecommunications companies against the Technical Report of the CNE. The Judgment of the Panel of Experts opted for the values proposed by the CNE, including the service of post supports.

Chilectra S.A. also filed with the Chilean General Comptroller appealing the legality of the tariff process. The same was done by ASEP and Chilquinta, filing separate appeals before the Chilean General Comptroller. The Chilean General Comptroller has not issued its report.

Last September 16, the Ministry of Economy submitted to the Chilean General Comptroller for recording, the Tariff Decree that sets the new rates for associated services.

On December 6, 2005, the Chilean General Comptroller returned the decree to the Ministry of Economy, without recording since it deemed that it lacks legality since tariffs must be established during the tariff setting process completed in November 2004, for a 4-year term.

On December 14, 2005, the Ministry of Economy and the National Energy Commission filed a motion to abandon the proceedings before the Chilean General Comptroller, which is pending a pronouncement from the controlling entity.

Telefónica CTC Chile filed a motion for protection against the decision of the Comptroller before the Santiago Court of Appeals, which was accepted for processing by the court. Telecommunications companies VTR, CNT and Entel became a party to the motion for protection.

On March 14, 2006 the hearing began.

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**Public Tender to Grant Wireless Local Public Telephone Concessions on the 3,400 – 3,600 MHz Frequency Band**

On September 15, 2005 the projects were delivered to the companies participating in the public tender called by Subtel to grant wireless local public telephone concessions on the 3,400 – 3,600 MHz band.

The companies participating in that tender were Telefónica CTC Chile, Telmex Servicios Empresariales, MIC Chile S.A. (owned by Telmex Chile) and VTR.

On December 13, 2005, Subtel informed that VTR and Telmex were awarded the concessions to offer wireless local telephone throughout the country, through the preferential rights of both companies.

The resolution that awards Telmex the national wireless local public telephone service concession was published in the Official Gazette on December 16, 2005 and the resolutions awarding VTR the regional concessions excluding Regions XI and XII, of the public tender, were published on December 21, 2005.

Telefónica CTC Chile appealed the awarding of the concessions in conformity with the procedure established in the General Telecommunications Law. On March 14, 2006, Telefónica CTC Chile filed an appeal against the resolution of the Minister of Transportation and Telecommunications before the Court of Appeals, which rejected the complaint.

Furthermore, on December 27, 2005, Telefónica CTC Chile filed a public law motion to vacate in respect to the preferential rights of VTR. On February 1, 2006 Telefónica CTC Chile filed an illegality complaint before the Chilean General Comptroller due to what was stated in the Public Tender documents to grant Wireless Local Public Telephone Concessions in the 3,400 – 3,600 MHz band.

Regarding the projects corresponding to Regions XI and XII, the Ministry of Transportation and Telecommunications communicated that by means of Resolutions No. 64 and No. 65, both of January 20, 2006, it assigned the regional concessions to provide wireless local telephone services in Regions XI and XII to Telefónica CTC Chile, since it was the only bidder. The resolutions were published in the Official Gazette and in newspapers distributed in both regions on February 7, 2006. The decrees that grant the mentioned concessions are pending.

**Permit for Limited Cable Television Service**

Through Exempt Resolution No. 1605 of December 23, 2005, Subtel granted Telefonica Multimedia Chile S.A. (formerly Tecnonáutica S.A.), a satellite television limited service permit to operate throughout the national territory.

In addition, through Resolution No. 81 of February 21, 2006, Subtel granted Telefónica Multimedia Chile S.A. a cable television limited service permit to provide the service through the broadband network of Telefónica CTC, throughout the national territory for an unlimited term except for the Metropolitan Region, which is covered in the permit granted in 1994

Subtel dictated the technical standard that establishes that the cable television service can be

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provided using any technology through physical media, which regulates the operation of the ADSL broadband network to provide television services.

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## 9. ANALYSIS OF MARKETS, COMPETITION AND RELATIVE PARTICIPATION

### **Relevant Industry Information**

During the first quarter of 2006, the Telecommunications industry maintained its characteristic dynamism, with emphasis on the evolution of the mergers and acquisition processes of operators and the continuity of the constant changes in consumer choices for telecommunications services, particularly within broadband services.

It is estimated that lines in service as of March 2006 reached approximately 3.5 million, reflecting a 2.0% increase in respect to as of March 2005, derived mainly from prepaid telephone services which represent approximately 17% of total lines. Voice services show drops of 4.3% in local, 9.5% in DLD and 4.4% in ILD accumulated in respect to the previous year.

It is estimated that as of March 2006 the mobile telephone market reached a total of 11.5 million subscribers, which represents an accumulated growth of 17% in respect to March 2005.

The Internet market shows a migration from narrowband to broadband, with a 52% decrease in the narrowband market with a total estimated 2,502 million annual minutes and a 48% increase in the broadband market, which as of March 2006, slightly exceeds 800 thousand accesses, 56% with ADSL technology.

### **Relevant Information Regarding Competitive Environment.**

#### ***After being acquired by Almendral, Entel sells its participation in Americatel Corporation.***

On January 24, 2005, Almendral S.A communicated to the Superintendency of Securities and Insurance the completion of its negotiations with Telecom Italia, for the acquisition of its participation in Entel Chile.

On March 29, 2005, Almendral S.A. and its subsidiary Inversiones Altel Limitada, purchased from Telecom Italia International N.V., 5.86% and 48.9%, respectively, of the shares of Entel S.A. The price paid for 54.76% of the shares was US\$ 934 million, with a value of US\$ 7.21 per share.

On March 31, 2006, Entel signed a contract denominated Stock Purchase Agreement ( SPA ), in which they agreed to sell to Platinum Equity, LLC ( Platinum ) all the shares which, through Entel International B.V.I. Corporation, it has in Americatel Corporation. The shares of Americatel that Entel has agreed to sell represent 80% of the capital of Americatel.

#### ***GTD acquires Manquehue Net S.A.***

On June 17, 2005, the Board of Directors of Manquehue Net S.A. received the offer made by GTD Grupo Teleductos S.A. to the shareholders of Manquehue Net S.A.

On September 30, 2005, Manquehue Net S.A notified the Superintendency of Securities and Insurance that GTD Grupo Teleductos S.A through its subsidiaries GTD Teleductos S.A and GTD Telesat S.A. purchased all the shares of Manquehue Net S.A., thereby acquiring control of the company.

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***América Móvil acquires Smartcom.***

On August 3, 2005 América Móvil announced the acquisition of 100% of the ownership of the Endesa Spain Group in Smartcom. The Company value involved in the operation was US\$ 472 million. América Móvil is associated with Telmex Corp. S.A.

***Liberty Media takes control of United Global Com, Parent Company of VTR and merges its operations in Chile.***

On January 5, 2004 Liberty Media, owner of 50% of Metrópolis Intercom in association with the Claro Group, announced the takeover of the management of United Global Com, owner of 100% of VTR Chile. After the operation, Liberty requested that the Antitrust Commission analyze the possibility of merging VTR and Metrópolis Intercom. Both companies concentrate over 90% of the Pay TV market and are relevant competitors for Telefónica CTC Chile in the broadband market providing cable modem. Likewise, VTR is the second operator of local telephone services in the country.

On June 9, 2004 the National Economic Attorney General's Office issued its report to the Antitrust Commission recommending the authorization of the merger subject to compliance with a series of restrictions.

On October 25, 2004, the Antitrust Commission resolved to approve the merger of VTR and Metrópolis Intercom, subject to compliance with a series of corporate conditions, in respect to distribution of contents, prices, quality of service and opening of cable network broadband to other ISP. These conditions are applied to ensure development of effective competition in the pay TV market in the short-term.

On March 10, 2005 the Supreme Court of Chile authorized the merger of VTR and Metrópolis, however it considered that the transaction could hinder development of effective competition in the pay television market in the short-term, therefore it made the transactions subject to fulfillment of eight conditions, thus ratifying the decision of the Antitrust Commission in respect to merger restrictions.

On July 1, 2005 VTR began unifying its program offer for VTR and former Metrópolis customers.

***Telefónica Móvil acquires the assets of Bellsouth in Latin America and the mobile subsidiary of Telefónica CTC Chile.***

On March 8, 2004, Telefónica Móviles S.A. announced the agreement to purchase the assets of Bellsouth Corporation in Latin America. This agreement includes the mobile business of Bellsouth in Chile which operates with a 25 Mhz spectrum on the 800 Mhz band with TDMA and 10 Mhz on the 1900 Mhz band with CDMA.

On May 18, 2004, the Board of Telefónica CTC Chile unanimously accepted the association offer made by Telefónica Móviles S.A., for the acquisition of 100% of the mobile subsidiary of Telefónica CTC Chile, subject to the approval of the Shareholders Meeting.

On July 15, 2004, the shareholders' meeting to decide on the sale of the mobile subsidiary of Telefónica CTC was held. At this meeting a counteroffer was made by the shareholders which

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meant that Telefónica Móviles S.A had to pay for the taxes derived from the operation.

On July 23, 2004, the contract was signed for the sale of all the shares of the subsidiary, with which Telefónica CTC no longer participates in the mobile business.

***Telefónica Móvil consults the Court of Free Competition on the purchase of Bellsouth.***

Telefónica Móvil S.A., a subsidiary of Telefónica S.A., presented to the Court of Free Competition an inquiry regarding the contract denominated Stock Purchase Agreement dated March 5, 2004, signed with Bellsouth Corporation, by which it acquires all the telephony assets of the latter in Central and South America, among which is its indirect full ownership of Bellsouth Chile S.A., current mobile telephony operator in the Chilean market.

On January 4, 2005 the Antitrust Commission resolved to approve the consultation of Telefónica Móvil S.A., subsidiary of Telefónica S.A., setting a series of conditions for the merger. One of these conditions directly affects Telefónica CTC Chile, establishing that, any joint offer of services for fixed and mobile telephone services commercialized by the merged company and which, considers fixed telephone services provided by Telefónica CTC Chile, will be understood to be a joint offer made by the latter, which therefore must be governed by Decree No. 742 issued by the Undersecretary of Telecommunications of Chile, published on February 26, 2004.

On April 5, 2005 Telefónica Móvil S.A, subsidiary of Telefónica S.A. launched Movistar in Chile, grouping under this brand the mobile subsidiary purchased from Telefónica CTC Chile in July 2004 and the operations of Bellsouth acquired with the approval of the Antitrust Commission in January 2005.

**Analysis of relative participation**

***Local Telephone Service.***

This market contemplates providing local telephone services inside the primary areas, interconnection with other telecommunications companies and other unregulated local services. Entrance to this market is regulated by concessions awarded by Subtel.

Currently 10 companies with 13 brands participate in this market, including three exclusively rural operators. The penetration rate as of a March 2006 was 20.8 lines per 100 residents. Telefónica CTC Chile has approximately 71% of the fixed telephone lines as of March 2006.

***Long Distance.***

This market contemplates communications services between primary areas (DLD) and international communications (ILD), also known as intermediate services.

On March 9, 1994 Law No. 19,302 came into effect. It establishes the application of a multicarrier system for domestic and international long distance. This law allows local telephone operators to participate in the long distance market through an independent subsidiary subject to a series of requirements.

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In this market there are currently 15 companies operating with 18 carrier codes. Traffic in the DLD market, through fixed telephone lines recorded a 9.5% drop in the first quarter in respect to the first quarter of 2005. In the same period a decrease of 4.4% is estimated in the ILD market. Telefónica CTC Chile, through its subsidiaries Telefónica Mundo 188 and Globus 120, reached an estimated market share of 46.7% in domestic long distance and 35.7% in outgoing international long distance in the first quarter of 2006.

#### ***Corporate Communications.***

This business area contemplates providing circuit and data services (Datared, E1, ATM, Frame Relay), IP network solutions, Hosting, ASP and advanced telecommunications solutions for companies with Internet service providers (ISPs). It also includes commercialization of advanced equipment (multiple lines and PABx, among others).

In this business Telefónica CTC Chile competes with 8 companies in the private services arena and in the hosting business with at least 10 companies, reaching a market share in income of approximately 43% accumulated as of December 2005, including sale of advanced equipment to companies.

#### ***Mobile Communications.***

Mobile communications includes the provision of mobile communication services (cellular telephone, trunking and wireless data transmission). There are currently three mobile telephone operators, one smaller operator of mobile satellite communications and one operator that offers digital trunking and is authorized to interconnect to the public mobile network.

Telefónica CTC Chile stopped offering mobile services in July 2004. It currently maintains the relationship with this sector through incoming and outgoing fixed telephone service traffic. Fixed mobile traffic has grown by 4% during the period from January to March 2006 in comparison to the same period the previous year. Mobile-fixed traffic increased by 1% in the same period.

#### ***Pay TV.***

In the pay television market there is one dominant operator due to the merger of VTR and Metrópolis Intercom who altogether have over 90% of the pay TV market with 758 thousand connections as of December 2005, two satellite TV operators and close to 20 cable TV operators in specific areas, which altogether do not exceed 10% of the market.

#### ***Internet Access.***

In this market there are currently approximately 35 ISPs operating effectively, with three of these concentrating 82% of traffic. IP traffic (switchboard) accumulated from January to March 2006 in the network of Telefónica CTC Chile reached the order of 483 million minutes, a 48% drop in respect to the same period in 2005, mainly due to migration of users to broadband.

Telefónica CTC Chile continues with an intensive deployment of Internet access through ADSL broadband, directly to the customer and through a wholesale model in the ISP industry. As of March 2006, Telefónica CTC Chile's broadband connections in service reached 356,986 a growth of 48% compared to March 2005, achieving an estimated broadband market share of 43% as of December 2005, considering speeds equal to or exceeding 128 kbps.

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***Other Businesses.***

Comprises the Public Telephone market, in which Telefónica CTC Chile participates through its subsidiary CTC Equipos. There are seven nationwide companies of which CTC Equipos, as of March 2006 has approximately 26% of the market share considering it owns 10,040 public telephones. Additionally, Telefónica CTC Chile has another 11,842 community telephones installed.

On November 20, 2001 a new subsidiary was formed to commercialize and install alarm systems and video cameras for residential and corporate customers, providing monitoring and surveillance services and any other service relating to the above. As of December 2005 it is estimated that Telefónica CTC Chile has a market share of 31% in this service.

**10. ANALYSIS OF MARKET RISK****Financial Risk Coverage**

With the attractive foreign interest rates in certain periods, the Company has obtained financing abroad, denominated mainly in dollars and in certain cases at a floating interest rate. For this reason the Company faces two types of financial risks, the risk of exchange rate fluctuations and the risk of interest rate fluctuations.

***Financial risk due to foreign currency fluctuations.***

The Company has exchange rate coverage instruments, the purpose of which is to reduce the negative impact of the dollar fluctuations on its results. The percentage of interest bearing debt exposure is defined and continuously reviewed, basically considering the volatility of the exchange rate, its trend, and the cost and availability of hedging instruments for different terms.

The main hedging instruments used are Cross Currency Swaps, and dollar/UF and dollar/peso exchange insurance.

As of March 31, 2006, the interest bearing debt in original currency expressed in dollars was US\$ 888 million, including US\$ 550 million in financial liabilities in dollars, US\$ 250 million of debt expressed in unidades de fomento and US\$ 88 million of debt in Chilean pesos. In this manner USCh\$ 550 million corresponds to debt directly exposed to the variations of the dollar.

Simultaneously, the Company had Cross Currency Swaps, dollar/UF, dollar/peso exchange insurance and assets in dollars that resulted, as of the end of the first quarter 2006 in close to 0% exposure to foreign exchange.

***Financial risk due to floating interest rate fluctuations.***

The policy for hedging interest rates seeks to reduce the negative impact on financial expenses due to interest rate increases.

As of March 31, 2006, the Company had debt at variable interest rates Libor and TAB, mainly for bank loans.

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To protect the Company from increases in the floating interest rates, derivative financial instruments have been used, particularly *Cross Currency Swaps (which protect the Libor rate)*, to limit the future fluctuation of interest rates. As of March 31, 2006 this has allowed the Company to end with an exposure of 14% of the total interest bearing debt in original currency.



**SIGNATURE**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Date: June 05, 2006

**COMPAÑÍA DE TELECOMUNICACIONES DE CHILE S.A.**

By:           /s/ Julio Covarrubias F.

Name: Julio Covarrubias F.

Title: Chief Financial Officer