

WESTERN ASSET INTERMEDIATE MUNI FUND INC.

Form N-Q

April 25, 2017

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM N-Q**

**QUARTERLY SCHEDULE OF PORTFOLIO HOLDINGS OF REGISTERED**

**MANAGEMENT INVESTMENT COMPANY**

Investment Company Act file number **811-6506**

**Western Asset Intermediate Muni Fund Inc.**

(Exact name of registrant as specified in charter)

**620 Eighth Avenue, 49<sup>th</sup> Floor, New York, NY 10018**

(Address of principal executive offices) (Zip code)

**Robert I. Frenkel, Esq.**

**Legg Mason & Co., LLC**

**100 First Stamford Place**

**Stamford, CT 06902**

(Name and address of agent for service)

Registrant's telephone number, including area code: (888)777-0102

Date of fiscal year end: **November 30**

Date of reporting period: **February 28, 2017**

**ITEM 1. SCHEDULE OF INVESTMENTS.**

**WESTERN ASSET INTERMEDIATE MUNI FUND INC.**

FORM N-Q

FEBRUARY 28, 2017

## WESTERN ASSET INTERMEDIATE MUNI FUND INC.

## Schedule of investments (unaudited)

February 28, 2017

SECURITY	RATE	MATURITY DATE	FACE AMOUNT	VALUE
<b>MUNICIPAL BONDS - 133.1%</b>				
<b>Alabama - 1.2%</b>				
Jefferson County, AL, Sewer Revenue, Subordinated Lien Warrants	5.000%	10/1/21	\$ 1,500,000	\$ 1,618,065
<b>Arizona - 4.2%</b>				
Navajo Nation, AZ, Revenue	5.000%	12/1/25	250,000	269,045 <sup>(a)</sup>
Phoenix, AZ, Civic Improvement Corp., Wastewater System Revenue, Junior Lien	5.000%	7/1/27	1,000,000	1,170,790
Pinal County, AZ, Electric District No. 3 Revenue	4.000%	7/1/23	1,000,000	1,073,900
Pinal County, AZ, Electric District No. 3 Revenue	5.000%	7/1/24	1,760,000	2,027,537 <sup>(b)</sup>
Pinal County, AZ, Electric District No. 3 Revenue	5.000%	7/1/25	1,280,000	1,474,573 <sup>(b)</sup>
<i>Total Arizona</i>				<i>6,015,845</i>
<b>California - 19.9%</b>				
Alameda, CA, Corridor Transportation Authority Revenue, Second Subordinated Lien	5.000%	10/1/34	500,000	558,415
Anaheim, CA, Public Financing Authority Lease Revenue	5.000%	5/1/26	2,000,000	2,354,600
Bay Area Toll Authority, CA, Toll Bridge Revenue, San Francisco Bay Area	1.740%	4/1/24	2,000,000	2,021,100 <sup>(c)(d)</sup>
California State PCFA, Water Furnishing Revenue	5.000%	7/1/27	2,000,000	2,140,560 <sup>(a)(e)</sup>
California State, GO	1.246%	12/1/17	1,500,000	1,502,055 <sup>(c)(d)</sup>
California State, GO, Bid Group C	5.000%	8/1/33	1,000,000	1,154,040
California Statewide CDA Revenue, Lodi Memorial Hospital, CMI	5.000%	12/1/22	2,000,000	2,063,120 <sup>(b)</sup>
California Statewide CDA, Student Housing Revenue, Provident Group-Pomona Properties LLC	5.600%	1/15/36	560,000	593,790
Long Beach, CA, Bond Finance Authority Lease Revenue	5.000%	8/1/31	1,855,000	2,103,366
Los Angeles County, CA, Public Works Financing Authority, Lease Revenue:				
Multiple Capital Project II	5.000%	8/1/21	1,000,000	1,150,220
Multiple Capital Project II	5.000%	8/1/22	1,000,000	1,170,460
M-S-R Energy Authority, CA, Gas Revenue	6.125%	11/1/29	3,000,000	3,740,340
Modesto, CA, Irrigation District Electric Revenue	5.000%	7/1/24	4,130,000	4,681,479
Modesto, CA, Irrigation District Electric Revenue	5.000%	7/1/25	2,000,000	2,262,600
River Islands, CA, Public Financing Authority Special Tax, Community Facilities District No. 2003-1	5.250%	9/1/34	430,000	446,994
Riverside County, CA, Transportation Commission Sales Tax Revenue, Limited Tax	5.250%	6/1/26	300,000	357,345
<i>Total California</i>				<i>28,300,484</i>
<b>Colorado - 5.2%</b>				
Base Village Metropolitan District #2 Co., GO	5.500%	12/1/36	500,000	504,660
E-470 Public Highway Authority Revenue, CO	5.250%	9/1/25	2,000,000	2,148,240
Public Authority for Colorado Energy, Natural Gas Purchase Revenue	6.125%	11/15/23	3,940,000	4,692,619
<i>Total Colorado</i>				<i>7,345,519</i>
<b>Connecticut - 0.8%</b>				
Connecticut State HEFA Revenue, Bristol Hospital, AGC	5.500%	7/1/21	1,125,000	1,128,533

**See Notes to Schedule of Investments.**

## WESTERN ASSET INTERMEDIATE MUNI FUND INC.

Schedule of investments (unaudited) (cont d)

February 28, 2017

MATURITY DATE	FACE AMOUNT	VALUE
6/15/35	\$ 150,000	\$ 153,500 <sup>(a)</sup>
6/1/30	125,000	121,541 <sup>(a)</sup>
10/1/27	545,000	616,319
10/1/30	1,500,000	1,718,460
10/1/31	4,000,000	4,362,880 <sup>(e)</sup>
10/1/32	1,000,000	1,088,060 <sup>(e)</sup>
7/1/26	1,500,000	1,734,405
2/1/24	2,000,000	2,152,240 <sup>(b)</sup>
8/1/36	250,000	266,207
		12,213,612

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11/1/23	2,000,000	2,254,020 <sup>(b)</sup>
4/1/20	1,000,000	1,014,270 <sup>(c)(d)</sup>
11/15/29	2,000,000	2,162,920
7/1/29	1,000,000	1,104,480
4/1/28	500,000	560,200
		7,095,890
1/1/30	1,000,000	1,006,870
12/1/29	850,000	962,268
1/1/31	1,750,000	1,923,267 <sup>(e)</sup>
1/1/36	500,000	573,555
1/1/37	400,000	457,768
4/1/29	1,670,000	1,780,955





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

## Notes to the Consolidated Financial Statements, continued

**6. Balances and transactions with related entities:****a) Receivable from:**

Taxpayer No.	Company	Short-term		Long-term	
		2005 ThCh\$	2004 ThCh\$	2005 ThCh\$	2004 ThCh\$
96,990,810-7	Telefónica Móviles Chile Distribución S.A.	155,009	113,194	-	-
Foreign	Telefónica España	675,028	489,680	-	-
93,541,000-2	Impresora y Comercial Publiguías S.A.	4,582,754	5,295,210	-	-
Foreign	Telefónica Sao Paulo	-	144,769	-	-
Foreign	Emergia USA	-	45,324	-	-
96,834,230-4	Terra Networks Chile S.A.	1,392,125	725,200	-	-
96,895,220-k	Atento Chile S.A.	362,625	337,761	-	-
96,910,730-9	Emergia Chile S.A.	99,097	93,799	-	-
Foreign	Telefónica LD Puerto Rico	-	14,663	-	-
Foreign	Telefonica Data EEUU	20,599	51,610	-	-
Foreign	Telefónica Data España	260,492	495,621	-	-
Foreign	Telefónica Argentina	1,475,226	1,849,993	-	-
Foreign	Telefónica Gestión de Servicios Compartidos España	11,202	-	-	-
96,786,140-5	Telefónica Móviles de Chile S.A.	6,997,836	5,460,879	-	-
Foreign	Telefónica Procesos Tec. de Información	1,338,177	10,280,773	-	-
59,083,900-0	Telefónica Ingeniería de Seguridad S.A.	5,914	9,218	-	-
Foreign	Telefonica WholeSale International Services	349,290	195,166	-	-
Foreign	Telefónica Guatemala	-	6,022	-	-
Foreign	Telefónica El Salvador	-	76,780	-	-
79,919,680-8	Administradora de Créditos Comerciales	1,309,766	-	-	-
Foreign	Telefónica Perú	-	432,521	-	-
	<b>Total</b>	<b>19,035,140</b>	<b>26,118,183</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) Payable to:**

**Short-term**                      **Long-term**

<b>Taxpayer No.</b>	<b>Company</b>	<b>2005 ThCh\$</b>	<b>2004 ThCh\$</b>	<b>2005 ThCh\$</b>	<b>2004 ThCh\$</b>
Foreign	Telefónica España	-	429,397	-	-
96,527,390-5	Telefónica Internacional Chile S.A.	138,197	138,115	-	-
93,541,000-2	Impresora y Comercial Publicguías S.A.	791,132	2,017,051	-	-
Foreign	Telefónica Perú	52,653	503,051	-	-
96,834,230-4	Terra Networks Chile S.A.	4,424,790	4,020,000	-	-
96,895,220-k	Atento Chile S.A	4,681,997	1,976,876	-	-
96,910,730-9	Emergia Chile S.A.	338,830	171,292	-	-
Foreign	Telefónica International Wholesale Services América S.A.	-	2,179,338	-	-
Foreign	Telefónica Guatemala	73,852	14,359	-	-
Foreign	Telefónica El Salvador	52,996	195,756	-	-
96,786,140-5	Telefónica Móviles de Chile S.A.	14,136,845	11,467,166	-	-
Foreign	Telefónica Argentina	-	1,309,323	-	-
Foreign	Telefónica Procesos Tec. de Información	-	7,288,750	-	-
Foreign	Telefonica WholeSale International Services	591,227	908,066	-	-
Foreign	Telefónica LD Puerto Rico	7,193	10,989	-	-
82,049,000-2	Coasin Chile S.A.	-	4,920	-	-
Foreign	Telefónica Sao Paulo	3,372	155,434	-	-
87,845,500-2	Telefónica Móviles Chile S.A.	4,468,310	-	-	-
Foreign	Telefonica Investigacion y Desarrollo	941,546	-	-	-
	<b>Total</b>	<b>30,702,940</b>	<b>32,789,883</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.

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS, continued  
(Translation of financial statements originally issued in Spanish)**6. Balances and transactions with related companies, continued:****c) Transactions:**

Company	Tax No.	Nature of Relationship	Description of transaction	2005		2004	
				Amount	Effect on income	Amount	Effect on income
Telefónica España	Foreign	Parent Co.	Sales Purchases	713,551 (166,994)	713,551 (166,994)	371,432 (233,074)	371,432 (233,074)
Telefónica Internacional Chile S.A.	96,527,390-5	Parent Co.	Purchases Financial Expenses	(420,013) -	(420,013) -	(416,672) (265,898)	(416,672) (265,898)
Impresora y Comercial Publiguías S.A.	93,541,000-2	Associate	Sales Purchases	4,340,296 (2,408,967)	4,340,296 (2,408,967)	4,859,634 (5,688,282)	4,859,634 (5,688,282)
Terra Networks Chile S.A.	96,834,230-4	Associate	Sales Purchases	3,888,811 (689,453)	3,888,811 (689,453)	4,118,938 (1,266,494)	4,118,938 (1,266,494)
Atento Chile S.A.	96,895,220-k	Associate	Sales Purchases	1,371,251 (12,143,976)	1,371,251 (12,143,976)	735,210 (10,685,967)	735,210 (10,685,967)
Emergia Chile S.A.	96,910,730-9	Associate	Sales Purchases	747,720 -	747,720 -	840,413 (54,483)	840,413 (54,483)
Telefónica Argentina	Foreign	Associate	Sales Purchases	765,680 (614,588)	765,680 (614,588)	989,021 (663,233)	989,021 (663,233)

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Telefónica Mobile Solutions Chile S.A.	96,942,730-3	Associate	Sales	58,741	58,741	-	-
Telefonica WholeSale International Services	Foreign	Associate	Sales	-	-	1,751,298	1,751,298
Telefónica Sao Paulo	Foreign	Associate	Sales Purchases	116,831 (139,894)	116,831 (139,894)	144,768 (144,806)	144,768 (144,806)
Telefónica Guatemala	Foreign	Associate	Sales Purchases	- -	- -	6,021 (12,091)	6,021 (12,091)
Telefónica Perú	Foreign	Associate	Sales Purchases	357,489 (406,363)	357,489 (406,363)	427,599 (503,051)	427,599 (503,051)
Telefónica LD Puerto Rico	Foreign	Associate	Sales Purchases	8,265 (11,631)	8,265 (11,631)	11,773 (10,989)	11,773 (10,989)
Telefónica El Salvador	Foreign	Associate	Sales Purchases	3,562 (19,949)	3,562 (19,949)	3,728 (33,577)	3,728 (33,577)
Telefónica Móvil de Chile S.A.	96,786,140-5	Associate	Sales Purchases	9,687,957 (34,419,248)	9,687,957 (34,419,248)	3,088,321 (9,796,243)	3,088,321 (9,796,243)
Telefonica Data USA	Foreign	Associate	Sales Financial Income	4,276 1,077,283	4,276 1,077,283	- -	- -
Bellsouth Chile S.A.	96,672,160-k	Associate	Sales Purchases	1,170,926 (9,302,781)	1,170,926 (9,302,781)	- -	- -
Telefonica WholeSale International Services España	Foreign	Associate	Sales Purchases	213,291 (1,828,496)	213,291 (1,828,496)	- -	- -

Telefónica Móviles Chile Inversiones S.A.	96,672,150-2	Associate	Sales	480,757	480,757	-	-
			Purchases	(27,993)	(27,993)	-	-
Atento Guatemala	Foreign	Associate	Sales	6,168	6,168	-	-
			Purchases	(23,335)	(23,335)	-	-
Telefonica WholeSale International Services Uruguay	Foreign	Associate	Purchases	(808,342)	(808,342)	-	-
Telefónica Ingeniería de Seguridad S.A.	59,083,900-0	Associate	Sales	7,481	7,481	-	-

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,

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

## Notes to the Consolidated Financial Statements, continued

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

As of September 30, 2005 and 2004, the Parent Company has established a first category income tax provision, as it has taxable net income of ThCh\$ 68,259,794 and ThCh\$ 90,525,497, respectively.

In addition, as of September 30, 2005 and 2004, a provision for first category income tax in subsidiaries was recorded in the amounts of ThCh\$ 34,635,527 and ThCh\$ 47,074,661, respectively.

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

Subsidiaries	Retained Taxable Earnings w/15% credit ThCh\$	Retained Taxable Earnings w/16% credit ThCh\$	Retained Taxable Earnings w/16.5% credit ThCh\$	Retained Taxable Earnings w/17% credit ThCh\$	Retained Taxable Earnings w/o credit ThCh\$	Amount of credit ThCh\$
CTC Equipos y Servicios de Telecomunicaciones S.A.	-	-	9,274,824	24,024,005	1,928,422	6,753,320
Telefónica Mundo S.A.	-	-	4,362,258	32,920,380	3,548,441	7,617,168
Globus 120 S.A.	2,153,965	816,072	584,214	1,679,903	240,897	995,079
Telefónica Empresas CTC Chile S.A.	942,463	7,492,938	5,002,010	20,699,199	1,445,535	6,821,553
Compañía de Telecomunicaciones de Chile S.A.	-	-	-	56,655,630	11,604,165	11,604,149
<b>Total</b>	<b>3,096,428</b>	<b>8,309,010</b>	<b>19,223,306</b>	<b>135,979,117</b>	<b>18,767,460</b>	<b>33,791,269</b>

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

## Notes to the Consolidated Financial Statements, continued

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

As of September 30, 2005 and 2004 the accumulated balances of temporary differences that originated net deferred tax (liabilities) assets in the amount of ThCh \$ 45,569,106 and ThCh\$ 43,702,266, are as follows:

Description	2005				2004			
	Deferred tax assets		Deferred tax liabilities		Deferred tax assets		Deferred tax liabilities	
	Short-term ThCh\$	Long-term ThCh\$	Short-term ThCh\$	Long-term ThCh\$	Short-term ThCh\$	Long-term ThCh\$	Short-term ThCh\$	Long-term ThCh\$
<b>Temporary differences</b>								
Allowance for doubtful accounts	9,368,647	-	-	-	15,410,203	-	-	-
Vacation provision	2,056,812	-	-	-	500,793	-	-	-
Tax benefits for tax losses	23,471	1,320,925	-	-	-	1,575,015	-	-
Staff severance indemnities	-	-	-	6,102,358	-	-	-	6,261,388
Leased assets and liabilities	-	60,201	-	121,057	-	64,677	-	96,422
Property, plant and equipment	8,819	3,997,160	-	165,455,928	-	3,974,608	-	182,198,853
Difference in amount of capitalized staff severance	-	572,660	-	-	-	781,170	-	-
Software	-	-	-	2,753,316	-	-	-	4,100,000
Deferred charge on sale of assets	-	-	-	1,281,207	-	-	-	1,588,611
Collective negotiation bonus	-	-	-	41,470	-	-	-	72,800
Other	1,061,066	283,777	9,914	4,276,851	149,600	88,844	13,504	1,404,700
<b>Sub-Total</b>	<b>12,518,815</b>	<b>6,234,723</b>	<b>9,914</b>	<b>180,032,187</b>	<b>16,060,596</b>	<b>6,484,314</b>	<b>13,504</b>	<b>195,722,833</b>

Complementary accounts net of accumulated amortization	-	(3,704,403)	-	(119,423,860)	-	(4,097,774)	-	(133,586,93
<b>Sub-Total</b>	<b>12,518,815</b>	<b>2,530,320</b>	<b>9,914</b>	<b>60,608,327</b>	<b>16,060,596</b>	<b>2,386,540</b>	<b>13,504</b>	<b>62,135,89</b>
Tax reclassification	(9,914)	(2,530,320)	(9,914)	(2,530,320)	(13,504)	(2,386,540)	(13,504)	(2,386,54
<b>Total</b>	<b>12,508,901</b>	<b>-</b>	<b>-</b>	<b>58,078,007</b>	<b>16,047,092</b>	<b>-</b>	<b>-</b>	<b>59,749,35</b>



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

Notes to the Consolidated Financial Statements, continued

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

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

Description	2005 ThCh\$	2004 ThCh\$
Current tax expense before tax benefits (income tax 17%)	17,924,638	24,713,123
Current tax expense (article 21 single tax at 35%)	43,522	29,474
Current tax expense (first category tax in the nature of a single income tax)	335,298	32,015,941
Tax expense adjustment (previous period)	86,962	217,959
	<b>Income tax</b>	
<b>subtotal</b>	<b>18,390,420</b>	<b>56,976,497</b>
- Current period's deferred taxes	(3,335,624)	(5,916,039)
- Tax benefits from tax loss carry forwards	(432,432)	(1,321,096)
- Effect of amortization of deferred assets and liabilities complementary accounts	10,089,157	11,834,802
	<b>Deferred tax</b>	
<b>subtotal</b>	<b>6,321,101</b>	<b>4,597,667</b>
	<b>Total</b>	
<b>expense tax</b>	<b>24,711,521</b>	<b>61,574,164</b>



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

Notes to the Consolidated Financial Statements, continued

**8. Other Current Assets:**

The detail of other current assets is as follows:

Description	2005 ThCh\$	2004 ThCh\$
Fixed income securities purchased with resale agreement	13,503,496	200,788,529
Deferred union contract bonus (a)	1,779,298	2,299,888
Deferred exchange insurance premiums	195,550	581,484
Telephone directories for connection program	4,087,800	2,727,821
Deferred higher bond discount rate (note 25)	54,671	2,133,290
Deferred disbursements for placement of bonds (note 25)	404,918	1,376,089
Commercial paper issuance costs (note 25)	217,833	305,864
Deferred disbursements for foreign financing proceeds (b)	596,954	717,703
Exchange difference insurance receivable (net of partial liquidations)	4,359,219	5,984,271
Deferred staff severance indemnities charges (c)	1,018,801	-
Others	840,010	541,382
<b>Total</b>	<b>27,058,550</b>	<b>217,456,321</b>

- (a) During June 2002, the Company signed a 2-year collective agreement with employees (3 years for employees of Telefónica Móvil) granting them, among other benefits, a special signing bonus. That bonus was paid between June and July 2002. The total benefit amounts to ThCh\$ 2,494,544 (historical) and is being deferred using the straight-line method over the term of the respective union contracts.

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 Long-term (Note 14).

- (b) 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.
- (c) Corresponds to the short-term portion to be amortized due to changes in the actuarial hypothesis, as described in Note 3, and for the concept of loans to employees as indicated in Note 14.

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

Notes to the Consolidated Financial Statements, continued  
(Translation of financial statements originally issued in Spanish)

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

Code	Dates		Counterparty	Original currency	Subscription value	Rate	Final Value	Instrument Identification	Book Value
	Inception	End							
CRV	Sep 26, 2005	Oct 05, 2005	Banco de Créditos e Inversiones (BCI )	\$	2,800,000	0.33%	2,802,772	BCP800708	2,801,232
CRV	Sep 29, 2005	Oct 07, 2005	HSBC Bank	\$	966,294	0.44%	967,428	BCP0800708	966,436
CRV	Sep 30, 2005	Oct 07, 2005	HSBC Bank	\$	2,171,588	0.35%	2,173,362	BCP800708	2,171,588
CRV	Sep 27, 2005	Oct 11, 2005	Banco de Créditos e Inversiones (BCI )	\$	2,071,507	0.33%	2,074,697	BCP800907	2,072,190
CRV	Sep 27, 2005	Oct 11, 2005	Banco de Créditos e Inversiones (BCI )	\$	628,493	0.33%	629,461	BCP800907	628,701
CRV	Sep 28, 2005	Oct 11, 2005	Banco de Chile	\$	64,713	0.33%	64,805	PDBC051125	64,727
CRV	Sep 27, 2005	Oct 04, 2005	Banco del Estado de Chile	UF	572,896	0.32%	573,324	PRC7B0393	573,080
CRV	Sep 27, 2005	Oct 04, 2005	Banco del Estado de Chile	UF	197,527	0.32%	197,674	PRC1D0797	197,590
CRV	Sep 27, 2005	Oct 04, 2005	Banco del Estado de Chile	UF	13,393	0.32%	13,403	PRC1D0296	13,397
CRV	Sep 27, 2005	Oct 04, 2005	Banco del Estado de Chile	UF	11,576	0.32%	11,585	PRC5C0894	11,580
CRV	Sep 27, 2005	Oct 04, 2005	Banco del Estado de Chile	UF	4,608	0.32%	4,611	PRC5B0994	4,609
CRV	Sep 28, 2005	Oct 04, 2005	Banco del Estado de	UF	1,017,242	0.32%	1,017,893	BCU0500907	1,017,459

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CRV	Sep 28, 2005	2005	Chile Banco del Estado de Chile	UF	436,291	0.32%	436,570	CERO010408	436,384
CRV	Sep 28, 2005	2005	Chile Banco del Estado de Chile	UF	44,184	0.32%	44,212	CERO010412	44,193
CRV	Sep 28, 2005	2005	Chile Banco del Estado de Chile	UF	372	0.32%	372	CERO010808	372
CRV	Sep 28, 2005	2005	Chile Banco del Estado de Chile	UF	1,912	0.32%	1,913	CERO011108	1,912
CRV	Sep 29, 2005	2005	HSBC Bank	UF	33,706	0.44%	33,746	CERO010808	33,711
CRV	Sep 30, 2005	2005	HSBC Bank	UF	28,412	0.35%	28,435	CERO010111	28,412
CRV	Sep 27, 2005	2005	Banco Santander Santiago	USD	1,000,000	0.32%	1,001,493	BCD0500108	1,000,320
CRV	Sep 28, 2005	2005	Banco de Chile	USD	275,306	0.33%	275,699	PRD04C0102	275,366
CRV	Sep 28, 2005	2005	Banco de Chile	USD	552,372	0.33%	553,162	PRD04C1201	552,494
CRV	Sep 28, 2005	2005	Banco de Chile	USD	552,372	0.33%	553,162	PRD04D1201	552,494
CRV	Sep 28, 2005	2005	Banco de Chile	USD	55,236	0.33%	55,317	PRD04B1201	55,249
<b>Totals</b>					<b>13,500,000</b>		<b>13,515,096</b>		<b>13,503,496</b>

CRV= Purchases under agreements to resell.

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

Notes to the Consolidated Financial Statements, continued

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

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

Description	2005		2004	
	Accumulated	Gross prop.,	Accumulated	Gross prop.,
	depreciation ThCh\$	plant and equipment ThCh\$	depreciation ThCh\$	plant and equipment ThCh\$
<b>Land</b>	-	<b>26,973,405</b>	-	<b>26,970,977</b>
<b>Building and improvements</b>	<b>83,814,027</b>	<b>194,740,631</b>	<b>80,095,636</b>	<b>194,141,180</b>
<b>Machinery and equipment</b>	<b>2,126,746,806</b>	<b>3,199,969,517</b>	<b>1,989,467,798</b>	<b>3,179,341,948</b>
Central office telephone equipment	1,007,210,583	1,255,753,514	944,013,225	1,240,887,353
External plant	787,331,577	1,481,999,101	735,283,397	1,473,983,351
Subscribers equipment	296,531,594	425,370,400	275,072,230	427,375,886
General equipment	35,673,052	36,846,502	35,098,946	37,095,358
<b>Other Property, Plant and Equipment</b>	<b>151,230,799</b>	<b>247,625,760</b>	<b>142,318,902</b>	<b>259,043,773</b>
Office furniture and equipment	79,121,608	106,504,937	77,085,965	107,984,480
Projects, work in progress and their materials (2)	-	46,922,894	-	55,701,840
Leased assets (1)	57,563	499,339	3,994,709	5,336,760
Property, plant and equipment temporarily out of service	10,386,329	11,666,292	12,814,328	20,193,215
Software	60,781,730	80,909,090	47,604,806	68,784,900
Other	883,569	1,123,208	819,094	1,042,578
<b>Technical revaluation Circular 550</b>	<b>10,830,808</b>	<b>9,637,400</b>	<b>10,884,136</b>	<b>9,668,570</b>
<b>Total</b>	<b>2,372,622,440</b>	<b>3,678,946,713</b>	<b>2,222,766,472</b>	<b>3,669,166,448</b>

(1) As of September 2005, this item includes mainly the ThCh\$ 486,973 gross value of buildings with accumulated depreciation of ThCh\$ 52,545.

(2) Up to December 31, 2002, works in progress included capitalization of financing cost of loans related to its financing, as per Technical Bulletin No. 31 of the Chilean Association of Accountants, thus, the gross property, plant and equipment balance includes interest in the amount of ThCh\$ 188,274,458. Accumulated depreciation for this interest amounts to ThCh\$ 119,681,520 and ThCh\$ 106,217,449 for 2005 and 2004, respectively.

A depreciation charge for the period amounting to ThCh\$ 140,712,326 and ThCh\$ 178,214,103 for 2005 and 2004, respectively, was recorded as operating cost, and a depreciation charge of ThCh\$ 5,098,125 for 2005 and ThCh\$ 3,062,952 for 2004 as administration 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\$ 2,132,251 and ThCh\$ 3,012,783 in 2005 and 2004, which is classified under Other Non-operating Expenses .

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

Description	Net	Accumulated	Gross	Gross
	Balance	Depreciation	property, plant and equipment 2005	property, plant and equipment 2004
	ThCh\$	ThCh\$	ThCh\$	ThCh\$
Land	(500,685)	-	(500,685)	(500,685)
Building and improvements	(876,796)	(3,927,701)	(4,804,497)	(4,804,497)
Machinery and equipment	184,073	14,758,509	14,942,582	14,973,752
<b>Total</b>	<b>(1,193,408)</b>	<b>10,830,808</b>	<b>9,637,400</b>	<b>9,668,570</b>

Depreciation of the technical reappraisal surplus for the period of ThCh\$(15,853) and ThCh\$40,621 for 2005 and 2004, respectively.

Gross property, plant and equipment includes assets that have been totally depreciated in the amount of ThCh\$ 1,038,539,973 in 2005 and ThCh\$ 868,634,900 in 2004, which include ThCh\$ 12,094,179 and ThCh\$ 12,516,111, respectively, from the reappraisals mentioned in Circular N°550.

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

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS, continued

(Translation of financial statements originally issued in Spanish)

**11. Investments in Related Companies:**

The detail of investments in related companies is as follows:

Taxp. No.	Company	Country of origin	Currency controlling the investment	Number of shares	Percentage participation		Equity of the companies		Net income of the companies	
					2005	2004	2005	2004	2005	2004
					%	%	ThCh\$	ThCh\$	ThCh\$	ThCh\$
Foreign	TBS Celular participación S.A. (2)	Brazil	Dollar	48,950,000	2.61	2.61	148,792,584	172,594,539	2,408,174	5
96,895,220-K	Atento Chile S.A.	Chile	Pesos	3,049,998	28.84	28.84	14,688,431	11,798,298	3,766,640	1,25
96,922,950-1	Empresa de Tarjetas Inteligentes S.A. (3)	Chile	Pesos	298,815	20.00	20.00	12,091	409,844	(162,550)	(3)
93,541,000-2	Impresora y Comercial Publiciguías S.A. (1)	Chile	Pesos	-	-	9.00	-	-	-	-

**Totals**

- (1) On April 26, 2004, Compañía de Telecomunicaciones de Chile S.A. sold its 9% holding in Impresora y Comercial Publiciguías S.A., to Telefónica Publicidad e Información S.A.. The selling price was US\$ 14,760,000, equivalent to Ch\$ 9,256 million, with a gain after taxes of Ch\$ 5,073 million.
- (2) 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 No. 4 of Circular 1179 issued by the Superintendency of Securities and Insurance and ratified in Title II of Circular 1697. 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.
- (3) 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.

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.

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

Notes to the Consolidated Financial Statements, continued

**12. Goodwill:**

The detail of goodwill is as follows:

Taxpayer No.	Company	Year	2005		2004	
			Amount amortized in the period ended September 30 ThCh\$	Balance of Goodwill ThCh\$	Amount amortized in the period ended September 30 ThCh\$	Balance of Goodwill ThCh\$
Foreign	TBS Celular participación S.A.	2001	137,888	2,503,704	138,419	2,688,068
96,887,420-9	Globus 120 S.A.	1998	850,714	14,849,751	854,000	15,987,211
78,703,410-1	Tecnonáutica S.A.	1999	112,569	790,457	113,047	941,096
96,786,140-5	Telefónica Móvil de Chile S.A. (a)	1997	-	-	142,998,189	-
96,834,320-3	Telefónica Internet Empresas S.A.	1999	69,527	488,215	69,813	581,184
96,811,570-7	Telepeajes S.A.	2001	-	-	30,669	10,184
	<b>Total</b>		<b>1,170,698</b>	<b>18,632,127</b>	<b>144,204,137</b>	<b>20,207,743</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.

- (a) As indicated in Note 2d) No. 1 with the sale of this subsidiary on July 23, 2004, the Company performed extraordinary amortization of the remaining goodwill on that investment as of September 30, 2004 of ThCh\$ 137,491,070.

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

Notes to the Consolidated Financial Statements, continued

**13. Intangibles:**

The detail of Intangibles is as follows:

Description	2005 ThCh\$	2004 ThCh\$
Underwater cable rights (gross)	35,574,207	32,321,322
Accumulated amortization, previous period	(5,085,543)	(3,438,984)
Amortization for the period	(1,284,110)	(1,266,321)
Licenses (Software) (gross)	11,373,999	3,462,741
Accumulated amortization, previous period	(1,905,109)	(963,752)
Amortization for the period	(1,801,683)	(697,828)
<b>Total Net Intangibles</b>	<b>36,871,761</b>	<b>29,417,178</b>

**14. Other (from Other Assets):**

The detail of Other is as follows:

Description	2005 ThCh\$	2004 ThCh\$
Deferred disbursement for obtaining external financing (see note 8b) (a)	1,092,363	951,264
Deferred union contract bonus (see note 8a)	86,964	1,783,529
Bond issue expenses (see note 25)	27,914	722,983
Bond discount (see note 25)	186,176	253,846
Deferred forward contract premiums	-	54,918
Securities deposits	136,062	151,563
Deferred charge due to change in actuarial estimations (b)	7,421,354	-
Deferred staff severance indemnities (c)	4,778,287	-
Others	33,678	157,612
<b>Total</b>	<b>13,762,798</b>	<b>4,075,715</b>

(a) 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.

(b) In light of the new contractual conditions derived from the organizational evolution experienced by the Company, there have been a series of studies that allowed, beginning in 2004, the modification of the variable

for future permanence 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 salary increases, 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).

- (c) 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.

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

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS, continued

(Translation of financial statements originally issued in Spanish)

**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	
		2005	2004	2005	2004	2005	2004	2005	2004
	<b>Short-term</b>	ThCh\$	ThCh\$	ThCh\$	ThCh\$	ThCh\$	ThCh\$	ThCh\$	ThCh\$
97,030,000-7	BANCO ESTADO	-	-	-	-	-	9,627,051	-	9,627,051
97,015,000-5	BANCO SANTANDER SANTIAGO	-	-	-	-	-	10,287,135	-	10,287,135
	Total	-	-	-	-	-	<b>19,914,186</b>	-	<b>19,914,186</b>
	Outstanding principal	-	-	-	-	-	<b>19,673,438</b>	-	<b>19,673,438</b>
	Average annual interest rate	-	-	-	-	-	2.98%	-	2.98%
	<b>Current maturities of long-term debt</b>								
97,015,000-5	BANCO SANTANDER SANTIAGO	-	-	576,584	458,038	-	-	576,584	458,038
	CALYON NEW YORK BRANCH Y								
Foreign	OTROS	101,606	-	-	-	-	-	101,606	-
97,008,000-7	CITIBANK	470,106	-	-	-	-	-	470,106	-
Foreign	ABN AMRO BANK	16,713,211	1,287,036	-	-	-	-	16,713,211	1,287,036

	BANCO								
	BILBAO								
	VIZCAYA								
Foreign	ARGENTARIA	-	141,825,762	-	-	-	-	-	141,825,762
	Total	<b>17,284,923</b>	<b>143,112,798</b>	<b>576,584</b>	<b>458,038</b>	-	-	<b>17,861,507</b>	<b>143,571,313</b>
	Outstanding principal	<b>15,876,000</b>	<b>141,116,608</b>	-	-	-	-	<b>15,876,000</b>	<b>141,116,608</b>
	Average annual interest rate	4.67%	2.38%	1.95%	1.55%	-	-	4.58%	2.38%
	Percentage of obligations in foreign currency:	96.77 %	for 2005	and	87.54 %	for 2004			
	Percentage of obligations in local currency:	3.23 %	for 2005	and	12.46 %	for 2004			

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

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS, continued

(Translation of financial statements originally issued in Spanish)

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

Long-term obligations with banks and financial institutions:

Taxp. No.	Bank or Financial Institution	Currency	Years to maturity for long-term portion			Long-term	Average	Long-term
		or Indexation	1 to 2	2 to 3	3 to 5	portion as of Sep 30, 2005	annual interest rate %	portion as of Sep. 30, 2004
	Index		ThCh\$	ThCh\$	ThCh\$	ThCh\$		ThCh\$
	<b>LOANS IN DOLLARS</b>							
	CALYON NEW YORK BRANCH Y OTROS (1)	US\$	-	-	105,840,000	105,840,000	Libor + 0,40%	-
97,008,000-7	CITIBANK ABN AMRO	US\$	-	-	79,380,000	79,380,000	Libor + 0,35%	-
Foreign	BANK (2)	US\$	31,752,000	31,752,000	-	63,504,000	Libor + 1,125%	188,155,478
	<b>SUBTOTAL</b>		<b>31,752,000</b>	<b>31,752,000</b>	<b>185,220,000</b>	<b>248,724,000</b>	<b>4.34%</b>	<b>188,155,478</b>
	<b>LOANS IN UNIDADES DE FOMENTO</b>							
	BANCO SANTANDER SANTIAGO (3)	UF	-	-	62,985,926	62,985,926	Tab 360 + 0,426%	62,948,419

<b>TOTAL</b>	<b>31,752,000</b>	<b>31,752,000</b>	<b>248,205,926</b>	<b>311,709,926</b>	<b>3.86%</b>	<b>251,103,897</b>
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Percentage of obligations in foreign currency:	79.79%	for	2005	and	74.93 %	for 2004
Percentage of obligations in local currency:	20.21%	for	2005	and	25.07 %	for 2004

- (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.
- (2) In April 2003, the Company renegotiated this loan, extending its maturity date from December 2003 to April 2008, in addition to changing the agent bank which was Citibank N.A..
- (3) 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 + 0.426%



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

Notes to the Consolidated Financial Statements, continued

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

On January 27, 2003, Telefónica CTC Chile registered a commercial paper line in the securities registry, the inspection number of which is 5. 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 Santander Investment S.A.

On January 18, 2005, Series E of the same type and instrument were placed in the amount of ThCh\$ 12,000,000. The placement agent was Inversiones Boston Corredores de Bolsa.

On April 27, 2005 a Series F placement of the same type of instrument was made in the amount of ThCh\$ 23,000,000. The placement agent was Scotiabank Sudamericano Corredores de Bolsa.

The details of these transactions are described below:

Registration or identification  number of the instrument	Series	Current nominal  amount placed ThCh\$	Bond readjustment unit  ThCh\$	Interest  rate %	Final  Maturity	Accounting value		Placement  in Chile or abroad
						2005 ThCh\$	2004 ThCh\$	
Short-term commercial paper								
005	C	17,500,000	Ch\$ non-adjustable	0.2257	Apr 5, 2005	-	17,793,995	Chile
005	D	17,500,000	Ch\$ non-adjustable	0.2286	May 5, 2005	-	17,751,377	Chile
005	E	12,000,000	Ch\$ non-adjustable	0.3100	Oct 13, 2005	11,984,314	-	Chile
015	F	23,000,000	Ch\$ non-adjustable	0.4100	Mar 28, 2006	22,463,646	-	Chile

**Total**                    **34,447,960**   **35,545,372**

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

NOTES TO THE FINANCIAL STATEMENTS, continued  
(Translation of financial statements originally issued in Spanish)

**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 number		Nominal Amount	Readjustment unit	Nominal annual interest rate	Final maturity	Frequency Interest payment	Amortizations	Par value 2005 ThCh\$		
or identification of the instrument	Series	of issue	for bond	%						
<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	1,649,274	13
203.23.04.98	<b>K (a)</b>	-		U.F.	6.750	Feb.2020	Semi-annual	Semi-annual	-	70
Issued in New York	<b>Yankee Bonds (b)</b>	49,603,000		US\$	7.625	Jul.2006	Semi-annual	Maturity	26,678,018	2
Issued in New York	<b>Yankee Bonds (c)</b>	156,440,000		US\$	8.375	Jan.2006	Semi-annual	Maturity	84,540,682	1
								<b>Total</b>	<b>112,867,974</b>	<b>7</b>
<b>Long-term bonds</b>										
143.27.06.91	<b>F</b>	714,286		U.F.	6.000	Apr.2016	Semi-annual	Semi-annual	12,655,408	13
203.23.04.98	<b>K (a)</b>	-		U.F.	6.750	Feb.2020	Semi-annual	Semi-annual	-	70
Issued in New York	<b>Yankee Bonds (b)</b>	-		US\$	7.625	Jul.2006	Semi-annual	Maturity	-	117
Issued in New York	<b>Yankee Bonds (c)</b>	-		US\$	8.375	Jan.2006	Semi-annual	Maturity	-	125

Total **12,655,408** 32

COMPAÑÍA DE TELECOMUNICACIONES DE CHILE S.A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements, continued

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

**b) Bonds**, continued:

a) During December 2004, and as stated in the sixth clause, letter K of the Bond Issuance Agreement, Telefónica CTC Chile decided to exercise the advanced redemption option of all the Bonds of this series. The amount of the redemption of this issuance is U.F. 3,992,424 plus interest accrued as of February 15, 2005, the effective date of the redemption. This has meant recognizing in income the balances pending amortization for "Bond issue expenses" and "Bond discount", reducing the term to the advanced redemption date. As of September 30, 2005 the extraordinary effects from these amortizations on total income amount to ThCh\$ 539,000 (included in Financial Expenses).

b) Starting May 2003 and until December of that same year, Telefónica CTC Chile, partially repurchased US\$ 12.3 million of its placement denominated in the same currency. This repurchase was carried out at an average of 111.05% of par value, which meant a payment of US\$ 13.68 million, plus accrued interest as of that date on the nominal amount of the repurchase. During November and December 2004, Telefónica CTC Chile made a tender offer for the dollar issuances, and as a result, the Company repurchased US\$ 138,082,000 during those two months. This operation was carried out paying an average price of 107.0 % of the par value. The partial repurchase of this series resulted in the Company recognizing extraordinary proportional amortization of the balances corresponding to "Bond issue expenses" and "Bond discount", as well as on payment of the repurchase. The net of these three effects of ThCh\$ 6,631,649 (historic) was charged to the financial expenses for the period.

c) During November and December 2004, Telefónica CTC Chile made a tender offer to repurchase dollars issuances. and as a result the Company repurchased US\$ 43,560,000. This operation was carried out at a price of 105.356% of par value. The partial repurchase of this series meant recognizing extraordinary amortizations proportional to the balances corresponding to "Bond issue expenses", "Bond discount", as well as on payment of the repurchase. The net of these three effects of ThCh\$ 1,461,539 (historic) was charged to financial expenses for the period.

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

Notes to the Consolidated Financial Statements, continued

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

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

	<b>2005</b>	<b>2004</b>
	<b>ThCh\$</b>	<b>ThCh\$</b>
<b>Current</b>		
Staff severance indemnities	367,466	107,748
Vacation	3,867,318	2,950,757
Other employee benefits (a)	7,373,795	6,655,243
Employee benefit advances	(2,704,378)	(3,035,231)
	<b>Sub-Totals</b>	<b>6,678,517</b>
	<b>8,904,201</b>	<b>6,678,517</b>
<b>Long-term</b>		
Staff severance indemnities	34,821,893	19,629,734
	<b>Total</b>	<b>26,308,251</b>
	<b>43,726,094</b>	<b>26,308,251</b>

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

During 2005, there was bad debt write-offs of ThCh\$ 32,283,372, 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>2005</b>	<b>2004</b>
	<b>ThCh\$</b>	<b>ThCh\$</b>
Operating costs and administrative and selling expenses	3,363,424	3,468,017
Other non-operating expenses	-	3,284,663
	<b>Total</b>	<b>6,752,680</b>
	<b>3,363,424</b>	<b>6,752,680</b>
Payments and other changes in the period (a)	2,203,643	(7,116,925)

(a) Includes the effect of the ThCh\$ 3,648,704 increase in the provision due to a change in actuarial estimations of employees made in 2005 (see Note 3) and payments of ThCh\$1,445,061.

**20. Minority interest:**

Minority interest recognizes the portion of equity and revenues of subsidiaries owned by third parties. The detail of 2005 and 2004, respectively, is as follows:

Subsidiaries	Percentage Minority Interest		Participation in equity		Participation in net income (loss)	
	2005 %	2004 %	2005 ThCh\$	2004 ThCh\$	2005 ThCh\$	2004 ThCh\$
Administradora de Sistemas de Telepeajes de Chile S.A.	20.00	20,00	230,760	128,613	(19,470)	31,353
Telefónica Mundo S.A.	0.84	0,84	1,099,511	1,214,425	1,493	116,322
Fundación Telefónica	50.00	50,00	189,565	222,299	(49,299)	37,151
CTC Equipos y Servicios de Telecomunicaciones S.A.	0.0001	-	37	38	4	5
<b>Total</b>			<b>1,519,873</b>	<b>1,565,375</b>	<b>(67,272)</b>	<b>184,831</b>

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

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS, continued

(Translation of financial statements originally issued in Spanish)

**21. Shareholders' Equity**

During the periods ended September 30, 2005 and 2004, respectively, changes in shareholders' equity accounts are as follows:

	<b>Paid-in capital</b>	<b>Reserve equity indexation</b>	<b>Other reserves</b>	<b>Retained earnings</b>	<b>Net income</b>	<b>Interim dividend</b>	<b>Total shareholders' equity</b>
	<b>ThCh\$</b>	<b>ThCh\$</b>	<b>ThCh\$</b>	<b>ThCh\$</b>	<b>ThCh\$</b>	<b>ThCh\$</b>	<b>ThCh\$</b>
<b>2005</b>							
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 net income to retained earnings	-	-	-	311,628,674	(311,628,674)	-	-
Adjustment of foreign investment conversion reserve	-	-	(300,175)	-	-	-	(300,175)
Absorption of interim dividend	-	-	-	(255,303,899)	-	255,303,899	-
Final Dividend 2004	-	-	-	(56,324,775)	-	-	(56,324,775)
Interim Dividend	-	-	-	(48,806,351)	-	-	(48,806,351)
Price-level restatement	-	21,143,461	(29,704)	-	-	-	21,113,757
Net income	-	-	-	-	21,727,781	-	21,727,781
Balances as of September 30, 2005	<b>880,977,537</b>	<b>21,143,461</b>	<b>(1,567,530)</b>	<b>-</b>	<b>21,727,781</b>	<b>-</b>	<b>922,281,249</b>

**2004**



Balances as of December 31, 2003	859,490,281	-	(791,199)	421,404,583	10,133,882	-	1,290,237,547
Transfer of 2003 income to retained earnings	-	-	-	10,133,882	(10,133,882)	-	-
Adjustment of foreign investment conversion reserve	-	-	(29,889)	-	-	-	(29,889)
Final Dividend 2003	-	-	-	(3,062,903)	-	-	(3,062,903)
Final eventual dividend	-	-	-	(383,441,784)	-	-	(383,441,784)
Interim dividend 2004	-	-	-	-	-	(252,244,349)	(252,244,349)
Price-level restatement	-	16,330,315	(16,121)	5,789,769	-	(783,245)	21,320,718
Net income	-	-	-	-	324,372,126	-	324,372,126
Balances as of September 30, 2004	<b>859,490,281</b>	<b>16,330,315</b>	<b>(837,209)</b>	<b>50,823,547</b>	<b>324,372,126</b>	<b>(253,027,594)</b>	<b>997,151,466</b>
Restated balances as of September 30, 2005	<b>885,300,293</b>	<b>16,820,705</b>	<b>(862,350)</b>	<b>52,349,750</b>	<b>334,112,839</b>	<b>(260,625,871)</b>	<b>1,027,095,366</b>

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

Notes to the Consolidated Financial Statements, continued

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

As of September 30, 2005 the Company's paid-in capital is as follows:

**Number of shares:**

Series	No. of subscribed shares	No. of paid shares	No. of shares with 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 Capital ThCh\$	Paid-in Capital ThCh\$
A	804,434,684	804,434,684
B	76,542,853	76,542,853

**(b) Shareholder stratification:**

As indicated in Circular No. 792 of the Chilean Superintendency of Securities and Insurance, the stratification of shareholders by percentage shareholding in the Company as of September 30, 2005 is as follows:

Type of shareholder	Percentage of Total holdings %	Number of shareholders
10% holding or more	56.60	2
Less than 10% holding:		
Investment equal to or exceeding UF 200	42.61	1,771
Investment under UF 200	0.79	11,410
<b>Total</b>	<b>100.00</b>	<b>13,183</b>

Company controller

44.90

1

35

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COMPAÑÍA DE TELECOMUNICACIONES DE CHILE S.A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements, continued

**21. Shareholders Equity**, continued:

**(c) Dividends:**

**i) Dividend policy:**

Considering the cash situation, levels of projected investment and the solid financial indicators for 2005 and following 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 year:**

On April 15, 2004, the Annual General Shareholders Meeting approved a final dividend of (No. 164) Ch\$ 3,20 per share equivalent to ThCh \$ 3,062,903, with a charge to net income for 2003. The dividend was paid on May 7, 2004.

Additionally, during July 2004 the following dividend distribution was agreed:

- On June 14, 2004, the Board of Directors of the Company agreed to pay shareholders an interim dividend, charged to 2004 net income.

- In turn, the Extraordinary Shareholders Meeting of July 15, 2004, approved the sale of subsidiary Telefónica Móvil de Chile S.A., and distribution of a final dividend charged to retained earnings as of December 31, 2003.

Both dividends, in the amount of US\$ 800 million, were subject to materialization of the sale of all the shares of Telefónica Móvil de Chile S.A., which would occur if Telefónica Móviles S.A, accepted the proposal of the Extraordinary Shareholders Meeting, which implied that it would assume responsibility for the taxes arising at of the sale operation, which amounted to US\$ 51 million.

On July 23, 2004, the contract for the sale of the shares of the former subsidiary Telefónica Móvil de Chile S.A. was signed. Therefore, on August 31, 2004, the Company paid the approved dividends relating to the sale of its subsidiary. The dividends are analyzed in the following manner:

- Dividend No. 165, with a charge to retained earnings of ThCh\$ 383,441,784.
- Dividend No. 166, in the nature of an interim dividend of ThCh\$ 127,813,928, with a charge to 2004 net income.

In the context of the modification of the dividend policy approved in September 2004, the Board agreed to distribute interim dividend (No. 167) with a charge to 2004 net income of Ch\$130 per share, which amounts to ThCh\$ 124,430,423 and was paid on November 4, 2004.

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 equivalent to 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 equivalent to ThCh\$ 48,806,351. Both dividends were paid on May 30, 2005.



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

Notes to the Consolidated Financial Statements, continued

**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:

Company	Amount		Net Movement ThCh\$	Balance as of September 30, 2005 ThCh\$
	December 31, 2004 ThCh\$	Price-level restatement ThCh\$		
Foreign TBS Celular Participación S.A. (1)	(1,237,651)	(29,704)	(300,175)	(1,567,530)
<b>Total</b>	<b>(1,237,651)</b>	<b>(29,704)</b>	<b>(300,175)</b>	<b>(1,567,530)</b>

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

Notes to the Consolidated Financial Statements, continued

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

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

<b>Other Income</b>	<b>2005 ThCh\$</b>	<b>2004 ThCh\$</b>
Fines levied on suppliers and indemnities	-	131,579
Proceeds from sale of used equipment	985,870	703,646
Sales of promotional material	-	104,111
Real estate rental	253,790	131,144
Proceeds from sale of Publiguías	-	6,657,769
Proceeds from sale of Telefónica Móvil de Chile S.A.	-	476,026,180
Gain on sale Intelsat	625,816	-
Accruals for lower market value of New Skies Satellites	-	229,092
Others	332,986	1,869,298
<b>Total</b>	<b>2,198,462</b>	<b>485,852,819</b>

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

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

<b>Other Expenses</b>	<b>2005 ThCh\$</b>	<b>2004 ThCh\$</b>
Lawsuit indemnities and other provisions	1,051,118	1,175,633
Depreciation and retirement of out-of-service property, plant and equipment (1)	2,132,251	3,012,783
Withdrawal of out-of-service property, plant and equipment	1,066,465	-
Unrecovered VAT tax credit	971,456	-
Lower market value provision	87,708	-
Restructuring costs	-	3,284,663
Other	706,908	548,578
<b>Total</b>	<b>6,015,906</b>	<b>8,021,657</b>

(1) As of September 2005 this item is mainly composed of depreciation of telephone equipment maintained in stock for replacement of lines in service. In 2004, it includes depreciation of the La Serena Cable TV network (assets temporarily out of service) not transferred in the sale of subsidiary Multimedia to Cordillera Comunicaciones.



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

Notes to the Consolidated Financial Statements, continued

**23. Price-level restatement:**

The detail of price-level restatement is as follows:

<b>Assets (Charges) Credits</b>	<b>Indexation</b>	<b>2005 ThCh\$</b>	<b>2004 ThCh\$</b>
Inventory	I.P.C.	62,404	119,876
Prepaid expenses	I.P.C.	4,587	3,414
Prepaid expenses	U.F.	(9,473)	(31,031)
Other current assets	I.P.C.	(27,510)	339,705
Other current assets	U.F.	(142,594)	(4,019,722)
Short and long-term deferred taxes	I.P.C.	2,948,639	2,605,539
Property, plant and equipment	I.P.C.	33,304,206	31,718,307
Investments in related companies	I.P.C.	175,311	101,770
Goodwill	I.P.C.	464,129	1,534,180
Long-term receivables	U.F.	(1,890,226)	(194,586)
Long-term receivables	I.P.C.	196,094	184,248
Other long-term assets	I.P.C.	999,053	636,132
Other long-term assets	U.F.	7,314	33,794
Expense accounts	I.P.C.	6,229,069	5,913,110
<b>Total (Charges) Credits</b>		<b>42,321,003</b>	<b>38,944,736</b>
<b>Liabilities Shareholders Equity (Charges) Credits</b>	<b>Indexation</b>	<b>2005 ThCh\$</b>	<b>2004 ThCh\$</b>
Short-term obligations	I.P.C.	-	(9,547)
Short-term obligations	U.F.	(7,107,727)	(4,021,422)
Long-term obligations	I.P.C.	(12,222)	(215,817)
Long-term obligations	U.F.	(4,858,736)	(2,407,165)
Shareholders equity	I.P.C.	(21,113,757)	(21,960,969)
Revenue accounts	I.P.C.	(10,176,773)	(12,674,149)
<b>Total Credits (Charges)</b>		<b>(43,269,215)</b>	<b>(41,289,069)</b>
<b>(Loss) Gain from price-level restatement, net</b>		<b>(948,212)</b>	<b>(2,344,333)</b>



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

Notes to the Consolidated Financial Statements, continued

**24. Foreign currency translation:**

The detail of foreign exchange gain (loss) is as follows:

Assets (Charges) Credits	Currency	2005 ThCh\$	2004 ThCh\$
Inventories	US\$	(511,687)	-
Current assets	US\$	5,886,732	25,306,023
Current assets	EURO	(7,748)	3,877,178
	BRAZILIAN		
Current assets	REAL	(25,998)	-
Long-term receivables	US\$	5,884,400	5,363,258
Other long-term assets	US\$	6,258	109,758
Other long-term assets	EURO	-	73
<b>Total Credits</b>		<b>11,231,957</b>	<b>34,656,290</b>
Liabilities (Charges) Credits	Currency	2005 ThCh\$	2004 ThCh\$
Short-term obligations	US\$	(960,137)	377,053
Short-term obligations	EURO	222	(3,778,231)
	BRAZILIAN		
Short-term obligations	REAL	17,181	-
Long-term obligations	US\$	(8,910,854)	(17,386,123)
<b>Total Charges</b>		<b>(9,853,588)</b>	<b>(20,787,301)</b>
<b>Foreign currency translation, net</b>		<b>1,378,369</b>	<b>13,868,989</b>

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

## Notes to the Consolidated Financial Statements, continued

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

The detail of this item is as follows:

	Short-term		Long-term	
	2005 ThCh\$	2004 ThCh\$	2005 ThCh\$	2004 ThCh\$
Bond issuance expenses	404,918	1,376,089	27,914	722,983
Discount on debt	54,671	2,133,290	186,176	253,846
Commercial paper issuance expense	217,833	305,864	-	-
<b>Total</b>	<b>677,422</b>	<b>3,815,243</b>	<b>214,090</b>	<b>976,829</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 No. 15 and 16
Obligations with the public	- see Notes No. 17

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

	Maturity	ThCh\$
PRD	2005	4,356,598
Zero	2005	18,200,305
BCD	2005	4,610,186
BCD	2007	14,193,741

**c) Cash and cash equivalents:**

<b>2005</b>	<b>2004</b>
-------------	-------------

	<b>ThCh\$</b>	<b>ThCh\$</b>
Cash	8,664,013	6,755,966
Time deposits	3,094,847	167,180,438
Mutual funds	-	447,288
Marketable securities (less than 90 days to maturity)	542,375	-
Other current assets	13,503,496	200,788,529
<b>Total</b>	<b>25,804,731</b>	<b>375,172,221</b>

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

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS, continued

(Translation of financial statements originally issued in Spanish)

**27. Derivative Contracts:**

The breakdown of derivative contracts is as follows:

TYPE OF DERIVATIVE CONTRACT	TYPE OF CONTRACT	DESCRIPTION OF CONTRACT	CONTRACT VALUE	MATURITY OR EXPIR.	SPECIFIC ITEM	PURCHASE SALE POSITION	HEDGED ITEM OR TRANSACTION		HEDGED ITEM ThCh\$	ASSET NAME
							NAME	AMOUNT		
FR	CI		60,000,000	IV Quarter 2005	Exchange rate	C	Oblig.in US\$	60,000,000	31,752,000	asset liabilitie
FR	CI		19,000,000	III Quarter 2006	Exchange rate	C	Oblig.in US\$	19,000,000	10,054,800	asset liabilitie
FR	CCPE		164,700,000	IV Quarter 2005	Exchange rate	C	Oblig.in US\$	164,700,000	87,159,240	asset liabilitie
FR	CCPE		24,300,000	I Quarter 2006	Exchange rate	C	Oblig.in US\$	24,300,000	12,859,560	asset liabilitie
FR	CCPE		20,000,000	III Quarter 2006	Exchange rate	C	Oblig.in US\$	20,000,000	10,584,000	asset liabilitie
FR	CCPE		150,000,000	III Quarter 2008	Exchange rate	C	Oblig.in US\$	150,000,000	79,380,000	asset liabilitie
FR	CCPE		200,000,000	II Quarter 2009	Exchange rate	C	Oblig.in US\$	200,000,000	105,840,000	asset liabilitie
FR	CI		16,500,000	IV Quarter 2005	Exchange rate	C	Oblig.in US\$	16,500,000	8,731,800	asset liabilitie
FR	CCPE		100,000,000	IV Quarter 2005	Exchange rate	C	Oblig.in US\$	100,000,000	52,920,000	asset liabilitie

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FR	CCPE	6,000,000	III Quarter 2006	Exchange rate	C	Oblig.in US\$	6,000,000	3,175,200	asset liabilitie
FR	CI	67,696,741	IV Quarter 2005	Exchange rate	V	Oblig.in US\$	67,696,741	38,063,413	asset liabilitie
FR	CI	1,421,965	IV Quarter 2005	Exchange rate	V	Oblig.in US\$	1,421,965	25,193,742	asset liabilitie
FR	CI	1,061,127	IV Quarter 2005	Exchange rate	V	Oblig.in US\$	1,061,127	263,298	asset liabilitie
FR	CI	353,709	IV Quarter 2005	Exchange rate	V	Oblig.in US\$	353,709	87,766	asset liabilitie
S	CCPE	150,000,000	III Quarter 2008	Interest rate	C	Oblig.in US\$	150,000,000	-	asset
S	CCPE	200,000,000	II Quarter 2009	Interest rate	C	Oblig.in US\$	200,000,000	-	asset

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

**Total**

**Types of derivatives:**

FR: Forward  
 S : Swap

**Type of Contract:**

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

COMPAÑÍA DE TELECOMUNICACIONES DE CHILE S.A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements, continued

**28. Contingencies and restrictions:**

**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 originate from the lowering of access charges rate 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. As a consequence, no provision has been established in relation to the indemnities claimed. Consequently provisions have been established in relation to the indemnities claimed.

**(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, determination which they arrived at 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.

COMPAÑÍA DE TELECOMUNICACIONES DE CHILE S.A. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements, continued

**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, the Court notified the first instance sentence accepting the claim made by Telefónica CTC Chile condemning Manquehue to pay approximately Ch\$ 452 million, and at the same time accepted Manquehue's claim condemning 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: maximum debt that the Company may have, interest and cash flows coverage.

The maximum debt ratio for these contracts is 1.50, whereas the interest coverage ratio cannot be less than 4.00 and lastly the cash flow ratio must be equal to or greater than 0.166.

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

As of September 30, 2005 the Company complies with all the financial restrictions.

**29. Third party guarantees:**

The Company has not received any guarantees from third parties.

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS, continued  
(Translation of financial statements originally issued in Spanish)

**30. Local and Foreign Currency:**

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

Description	Currency	2005 ThCh\$	2004 ThCh\$
<b>Total current assets:</b>		<b>292,252,949</b>	<b>676,208,391</b>
Cash	Non-indexed Ch\$	5,357,432	5,991,277
	Dollars	3,258,537	714,426
	Euros	48,044	50,263
	Indexed		
Time deposits	Ch\$	284,767	147,549,550
	Non-indexed Ch\$	2,810,080	-
	Dollars	-	19,630,888
	Indexed		
Marketable securities	Ch\$	-	447,288
	Dollars	41,360,830	24,631,153
	Indexed		
Notes and accounts receivable (a)	Ch\$	-	15,742,342
	Non-indexed Ch\$	161,058,094	174,211,477
	Dollars	6,667,404	14,833,091
Due from related companies	Non-indexed Ch\$	16,683,134	12,998,473
	Dollars	2,352,006	13,119,710
	Indexed		
Other current assets (b)	Ch\$	17,330,985	31,253,086
	Non-indexed Ch\$	32,176,594	208,022,998
	Dollars	2,821,263	7,012,369
	Brazilian Real	43,779	-
<b>Total property, plant and equipment :</b>		<b>1,306,324,273</b>	<b>1,446,399,976</b>
Property, plant and equipment and accumulated depreciation	Indexed Ch\$	1,306,324,273	1,446,399,976
<b>Total other long-term assets</b>		<b>92,022,709</b>	<b>80,920,583</b>
	Indexed		
Investment in related companies	Ch\$	8,119,632	7,989,314
	Indexed		
Investment in other companies	Ch\$	4,045	4,045
	Indexed		
Goodwill	Ch\$	18,632,127	20,207,743

	Indexed		
Other long-term assets (c)	Ch\$	62,402,414	42,879,629
	Non-indexed Ch\$	2,864,491	9,121,786
	Dollars	-	718,066
<b>Total assets</b>		<b>1,690,599,931</b>	<b>2,203,528,950</b>
	<b>Indexed</b>		
	<b>Ch\$</b>	<b>1,413,098,243</b>	<b>1,712,472,973</b>
	<b>Non-indexed Ch\$</b>	<b>220,949,825</b>	<b>410,346,011</b>
	<b>Dollars</b>	<b>56,460,040</b>	<b>80,659,703</b>
	<b>Euros</b>	<b>48,044</b>	<b>50,263</b>
	<b>Brazilian Real</b>	<b>43,779</b>	<b>-</b>

- (a) Includes the following balance sheet accounts: Trade Accounts Receivable, Notes Receivable and Miscellaneous Accounts Receivable.
- (b) Includes the following balance sheet accounts: Inventories, Recoverable Taxes, Prepaid Expenses, Deferred Taxes and Other Current Assets.
- (c) Includes the following balance sheet accounts: Long-term Debtors, Intangibles, Accumulated amortization and Others.

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS, continued  
(Translation of financial statements originally issued in Spanish)

**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			
		2005		2004		2005		2004	
		Amount ThCh\$	Average annual interest %	Amount ThCh\$	Average annual interest %	Amount ThCh\$	Average annual interest %	Amount ThCh\$	Average annual interest %
Short-term obligations with banks									
and financial institutions	Indexed Ch\$	-	-	-	-	-	-	-	-
	Non-indexed Ch\$	-	-	-	-	-	19,914,186	2.98	
	Dollars	-	-	-	-	-	-	-	-
Short-term portion of obligations with banks and financial institution	Indexed Ch\$	576,584	-	458,038	1.55	-	-	-	-
	Dollars	1,408,923	4.46	143,040,847	1.74	15,876,000	4.69	71,951	2.21
Obligations with the public (Commercial paper)	Non-indexed Ch\$	11,984,314	3.72	-	-	22,463,646	4.92	35,545,372	2.27
Obligations with the public (Bonds payable)	Indexed Ch\$	1,649,274	6.00	1,050,762	6.75	-	-	1,882,690	6.59

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	Dollars	-	-	-	-	111,218,700	8.38	4,379,199	-
Long-term obligations maturing									
within a year	Indexed Ch\$	5,364	9.06	8,236	9.01	16,091	9.06	24,703	9.01
Due to related parties	Indexed Ch\$	-	-	-	-	138,196	-	-	-
	Non-indexed Ch\$	29,825,899	-	20,272,670	-	-	-	7,288,750	-
	Dollars	738,845	-	5,057,171	-	-	-	171,292	-
Other current liabilities (d)	Indexed Ch\$	-	-	-	-	157,761	-	-	-
	Non-indexed Ch\$	122,173,001	-	241,383,251	-	5,374,984	-	30,029,198	-
	Dollars	3,550,882	-	1,305,710	-	-	-	-	-
<b>TOTAL CURRENT LIABILITIES</b>		<b>171,913,086</b>		<b>412,576,685</b>		<b>155,245,378</b>		<b>99,307,341</b>	
<b>Subtotal by currency</b>	<b>Indexed Ch\$</b>	<b>2,231,222</b>		<b>1,517,036</b>		<b>312,048</b>		<b>1,907,393</b>	
	<b>Non-indexed Ch\$</b>	<b>163,983,214</b>		<b>261,655,921</b>		<b>27,838,630</b>		<b>92,777,506</b>	
	<b>Dollars</b>	<b>5,698,650</b>		<b>149,403,728</b>		<b>127,094,700</b>		<b>4,622,442</b>	

(d) 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.

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

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS, continued

(Translation of financial statements originally issued in Spanish)

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

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

		1 to 3 years		3 to 5 years		5 to 10 years		over 10 years	
		2005		2005		2005		2005	
		Amount	Average annual interest rate	Amount	Average annual interest rate	Amount	Average annual interest rate	Amount	Average annual interest rate
		ThCh\$	%	ThCh\$	%	ThCh\$	%	ThCh\$	%
<b><u>LONG-TERM LIABILITIES</u></b>									
Obligation with banks and financial institutions	Indexed Ch\$	-	-	62,985,926	1.95	-	-	-	-
	Dollars	63,504,000	4.69	185,220,000	4.22	-	-	-	-
Bonds payable	Indexed Ch\$	2,531,080	6.00	2,531,080	6.00	7,593,248	6.00	-	-
Other long-term liabilities (e)	Indexed Ch\$	12,196,138	-	7,852,174	-	19,638,914	-	19,270,478	-
	Non-indexed Ch\$	9,812,717	-	477,823	-	9,276,115	-	36,750,652	-
<b>TOTAL LONG-TERM LIABILITIES</b>		<b>88,043,935</b>		<b>259,067,003</b>		<b>36,508,277</b>		<b>56,021,130</b>	
<b>Subtotal by currency</b>	<b>Indexed Ch\$</b>	<b>14,727,218</b>		<b>73,369,180</b>		<b>27,232,162</b>		<b>19,270,478</b>	
	<b>Non-indexed Ch\$</b>	<b>9,812,717</b>		<b>477,823</b>		<b>9,276,115</b>		<b>36,750,652</b>	
	<b>Dollars</b>	<b>63,504,000</b>		<b>185,220,000</b>		<b>-</b>		<b>-</b>	

1 to 3 years

3 to 5 years

5 to 10 years

over 10 years

2004

2004

2004

2004

		Average annual interest		Average annual interest		Average annual interest		Average annual interest	
		Amount	rate	Amount	rate	Amount	rate	Amount	rate
		ThCh\$	%	ThCh\$	%	ThCh\$	%	M\$	%
<b><u>LONG-TERM LIABILITIES</u></b>									
Obligations with banks and financial institutions	Indexed Ch\$	-	-	62,948,419	-	-	-	-	-
	Dollars	150,524,382	-	37,631,096	-	-	-	-	-
Bonds payable	Indexed Ch\$	4,541,734	-	7,090,470	-	25,821,219	-	46,482,400	-
	Dollars	243,150,189	-	-	-	-	-	-	-
Other long-term liabilities (e)	Indexed Ch\$	12,157,860	-	8,284,263	-	20,647,880	-	19,822,689	-
	Non-indexed Ch\$	815,396	-	428,078	-	1,070,196	-	21,567,912	-
<b>TOTAL LONG-TERM LIABILITIES</b>		<b>411,189,561</b>		<b>116,382,326</b>		<b>47,539,295</b>		<b>87,873,001</b>	
<b>Subtotal by currency</b>	<b>Indexed Ch\$</b>	<b>16,699,594</b>		<b>78,323,152</b>		<b>46,469,099</b>		<b>66,305,089</b>	
	<b>Non-indexed Ch\$</b>	<b>815,396</b>		<b>428,078</b>		<b>1,070,196</b>		<b>21,567,912</b>	
	<b>Dollars</b>	<b>393,674,571</b>		<b>37,631,096</b>		<b>-</b>		<b>-</b>	

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



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

## Notes to the Consolidated Financial Statements, continued

**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 2005 and 2004.

**32. Subsequent events:****a) Placement of Commercial Marketable Instruments:**

On October 25, 2005, the Company placed the third issuance of its line of Marketable Instruments. This issuance consists of two series (G and H) both for ThCh \$ 17,500,000, the first maturing on April 20, 2006 and the second on April 27, of the same year; at a placement rate of 0.51% monthly for both series. On this opportunity the placement agent was Scotia Sudamericano Corredores de Bolsa.

In the period from October 1 to 27, 2005, there have been no other significant subsequent events that affect these financial statements.

**33. Environment:**

In the opinion of Management and their 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 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 ThCh \$	Rate %	Maturity	Principal ThCh \$	Accrued interest	Total
Ago 31, 2005	Banco Santander Santiago	ChTh\$	2,800,000	4.32	Oct 03, 2005	2,800,000	10,080	2,810,080
Sep 30, 2005	Banco Santander Santiago	ChTh\$	1,928	0.00	Oct 01, 2005	1,928	-	1,928
Sep 30, 2005	Bci	UF	282,839	0.00	Dec 06, 2005	282,839	-	282,839
	<b>Total</b>		<b>3,084,767</b>			<b>3,084,767</b>	<b>10,080</b>	<b>3,094,847</b>



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

Notes to the Consolidated Financial Statements, continued

**35. Accounts payable:**

The detail of the accounts payable balance is as follows:

	<b>2005</b>	<b>2004</b>
	<b>ThCh\$</b>	<b>ThCh\$</b>
<b>Suppliers</b>		
Chilean	54,000,956	45,620,993
Foreign	4,805,259	2,649,090
<b>Carrier service</b>	6,456,008	6,659,863
<b>Provision for work in progress</b>	5,338,393	8,199,174
<b>Total</b>	<b>70,600,616</b>	<b>63,129,120</b>

**36. Other accounts payable:**

The detail of other accounts payable is as follows

	<b>2005</b>	<b>2004</b>
	<b>ThCh\$</b>	<b>ThCh\$</b>
Exchange insurance contract payables	25,350,549	16,391,301
Billing on behalf of third parties	2,597,283	2,398,698
Accrued supports	1,220,610	723,592
Others	1,437,391	1,479,538
<b>Total</b>	<b>30,605,833</b>	<b>20,993,129</b>

**Alejandro Espinoza Querol**  
General Accountant

**José Molés Valenzuela**  
General Manager

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

*For the nine-month periods ended September 30, 2005 and 2004*

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Análisis razonado consolidado

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

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Análisis razonado consolidado

## 1. HIGHLIGHTS

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

As of September 30, 2005, Telefónica CTC Chile recorded consolidated net income of Ch\$21,728 million, whereas in the same period in 2004 it shows net income of Ch\$ 334,113 million. 2004 income includes the effects derived from the sale of subsidiary Telefónica Móvil de Chile S.A. in July 2004, which produced net income of approximately Ch\$ 316,250 million.

The operating income of Telefónica CTC Chile in the first nine months of 2005 presents a surplus of Ch\$ 66,144 million, 17.0 % less than the Ch\$79.694 million reached in the period ended as of September 30, 2004.

Comparison of operating income for 2004 - 2005 includes the effects of the deconsolidation of subsidiary Telefónica Móvil de Chile S.A. as of July 2004.

For comparative purposes, after purging the effects of Telefónica Móvil in 2004, as detailed below, the operating margin reaches 15.3% and 18.8% for the period from January to September 2005 and 2004, respectively. Operating income decreased by 20.8% due to a 2.7% decrease in income and a 3.5% increase in operating costs.

#### **Operating Income for the period excluding T. Móvil**

	<u>2004</u>	<u>2005</u>	<u>% Variation</u>
Revenues	<b>443,343</b>	<b>431,212</b>	<b>-2.7%</b>
Salaries	-58,762	-59,085	<b>0.5%</b>
Goods and services	-153,051	-160,173	<b>4.7%</b>
Total Cost	<b>-211,813</b>	<b>-219,258</b>	<b>3.5%</b>
<b>EBITDA</b>	<b>231,530</b>	<b>211,954</b>	<b>-8.5%</b>
Depreciation	-148,019	-145,810	<b>-1.5%</b>
<b>Operating Income</b>	<b>83,511</b>	<b>66,144</b>	<b>-20.8%</b>
Operating Margin	18.8%	15.3%	<b>-18.57%</b>

It should be noted that as of May 6, 2004, operating income includes the effects of the rate decree which is in force until May 2009.

Non operating income for the period ended as of September 30, 2005, shows a deficit of Ch\$19,772 million, which compares negatively to the surplus obtained in the same period the previous year in the amount of Ch\$ 316,178 million, derived mainly from income obtained on the sale of Telefónica Móvil de Chile S.A. Without considering this effect, the variations are favorable and are basically due to a decrease in financial expenses associated to a lower level of debt and better financing conditions, partly offset by the decrease in non-operating income and price-level restatement.

#### Análisis razonado consolidado

In respect to operating business figures, as of September 30, 2005, Telefónica CTC Chile's fixed telephone lines reached 2,475,007, presenting an increase of 3.2% in relation to September 30, 2004. ADSL customers in service reached 268,344, with a growth of 48.7% in relation to the previous year. Long distance traffic decreased by 25.9% in domestic long distance (DLD) and 60.2% in outgoing international long distance (ILD), reaching 1,219.7 million minutes and 216.0 million minutes, respectively. ATM link services decreased by 34.6%, whereas dedicated IP links grew by 20.7%.

As of September 30, 2005, the Company's staff reached 3,914, which implies a 1.0% increase in comparison to September 2004, where the staff was 3,874.

#### **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 and also through the global drop in interest rates. As of September 30, 2005, the financial debt reached Ch\$484,993 million, reflecting a 37.5% decrease in relation to the financial debt of Ch\$776,216 million recorded as of September 30, 2004. The decrease in the indebtedness levels together with the improved financing conditions and drop in the value of the dollar translated into a downturn of 38.4% in financial expenses as of September 30, 2005.

#### **Tariff Setting Process for Telefónica CTC (Local Telephony)**

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

On June 2, Telefónica CTC Chile made two presentations to the Chilean General Comptroller within the process of recording Tariff Decree No. 169. The first presentation denounces manifest mathematical errors in Decree 169, requesting that the controlling organization order these to be corrected. The second presentation includes the legal objections relating to conceptual aspects that have an impact on the definition and scope of the services included in the decree. In both presentations the Company expressly reserves the right to take jurisdictional actions.

Entel, Chilesat and Telmex filed a complaint with the Chilean General Comptroller against tariff Decree No. 169, objecting to scaling of access charges and the criteria for cost assignment of the different tariff.

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### Análisis razonado consolidado

On September 16, 2004, the Ministries of Transport and Telecommunications, Economy, Development and Reconstruction issued their report to the Chilean General Comptroller relating to the complaints filed by Telefónica CTC Chile, Chilesat, Entel and Telmex. In this respect, the Ministries informed that due to their review of the tariff model a large part of the mathematical errors denounced by Telefónica CTC Chile were corrected, notwithstanding that other errors apparently contained in the mentioned tariff decree were also corrected.

In turn, the Ministries defended the scaling of access charges of D.S. 169, stating that such criteria has been taken in conformity with the resolutions of antitrust organizations and those prescribed by the Economic Technical Bases established for this tariff setting process.

Regarding the conceptual aspects claimed by Telefónica CTC Chile impacting the definition and scope of services included in the decree, the ministries rejected them as they rejected the objections of Entel, Chilesat and Telmex.

Last October 4, Telefónica CTC Chile once again appealed to the Chilean General Comptroller, in order for them to correct new mathematical errors incurred by the Ministries precisely at the time that they corrected the errors informed by Telefónica CTC Chile. Likewise they insisted on certain conceptual aspects.

Subtel once again submitted Decree No.169 to the Chilean General Comptroller on December 30, 2004, after modifying certain network unbundling tariffs, in the item Adjustment of Civil Works ( Adecuación de Obras Civiles ). Likewise, Subtel once again modified among other tariffs, those of the Adjustment of Civil Works item, resubmitting Decree 169 to the Chilean General Comptroller on January 14, 2005.

Furthermore, in January 2005. Entel and Telmex submitted new presentations to the Chilean General Comptroller, where Entel complains about the tariffs set by the Ministries in respect to Adjustment of Civil Works and Telmex attaches information sustaining that access charge rates must be at direct cost.

On February 8, 2005, the Chilean General Comptroller recorded Tariff Decree No. 169. The report of the Chilean General Comptroller does not accept the complaints regarding conceptual aspects presented by Telefónica CTC Chile and does not make a pronouncement regarding the new mathematical errors denounced in October 2004. The complaints filed by Telmex, Chilesat and Entel were rejected by the Chilean General Comptroller.

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.

### **Tariff Flexibility**

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 public service.

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### Análisis razonado consolidado

The tariff flexibility allows Telefónica CTC Chile to offer its customers various commercial plans, adhering to the general framework for the application of the flexibility that must be defined by the authority, without requiring authorization for each plan.

Telefónica CTC Chile began commercializing different local telephone service plans, in order for the interested public to be able to opt for an alternative that is different to the rates defined by the regulator.

### **Dividends Policy**

On September 21, 2004, the Board of Compañía de Telecomunicaciones de Chile S.A. agreed to modify the policy for distribution of dividends with a 30% to 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. In this context, the Board agreed to distribute an interim dividend charged against 2004 net income, for the total sum of Ch\$124,430 million in November 2004 (equivalent to US\$ 200 million).

In January 2005, the Board agreed to propose payment of a final dividend of Ch\$58.84591 per share with a charge to net income for the year to the Extraordinary Shareholders Meeting, thus complying with the aforementioned dividend policy. Likewise they agreed to propose payment of an eventual dividend of Ch\$50.99095 pesos per share, with a charge to retained earnings as of December 2004 at the next Ordinary Shareholders Meeting.

The Ordinary Shareholders Meeting held on April 14, 2005 approved the distribution of both the final and eventual dividend; in addition to revealing the Dividends Policy for 2005 and future years, as mentioned in the first paragraph of this section.

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Análisis razonado consolidado

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

DESCRIPTION	SEPTEMBER	SEPTEMBER	VARIATION	
	2004	2005	Q	%
Lines in Service at (end of period)	2,398,137	2,475,007	76,870	3.2%
Total Average Lines in Service	2,405,316	2,448,883	43,567	1.8%
Local calls (millions) <sup>(1)</sup>	3,434	3,309	(125)	-3.6%
Inter-primary DLD Minute <sup>(2)</sup> (thousands)	1,646,855	1,219,692	(427,163)	-25.9%
Total ILD Minutes <sup>(3)</sup> (thousands)	847,913	539,340	(308,573)	-36.4%
ILD Minute Outgoing (incl. Internet)	542,750	215,981	(326,769)	-60.2%
ILD Minutes Incoming	305,164	323,359	18,195	6.0%
Line Connections	242,034	274,934	32,900	13.6%
ADSL Connections in Service	180,487	268,344	87,857	48.7%
Permanent Personnel Telefónica CTC Chile (4)	2,914	2,944	30	1.0%
Permanent Personnel Subsidiaries <sup>(4)(5)</sup>	960	970	10	1.0%
Total Corporate Personnel <sup>(4)</sup>	3,874	3,914	40	1.0%

- Does not include calls from public phones owned by the Company.
- 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.
- 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.
- Does not include staff with contracts for determined term.
- In 2004 includes Móviles.

**TABLE N° 2**  
**CONSOLIDATED NET PROPERTY, PLANT AND EQUIPMENT**  
*(Figures in millions of pesos as of September 30, 2005)*

DESCRIPTION	SEPTEMBER	SEPTEMBER	VARIATION	
	2004	2005	MCh\$	%
	3,613,465	3,632,024	18,559	0.5%

Land, Infrastructure, Machinery and Equipment				
Projects and Works in Progress	55,701	46,923	(8,778)	-15.8%
Accumulated Depreciation	(2,222,766)	(2,372,622)	(149,856)	6.7%
<b>NET PROPERTY, PLANT &amp; EQUIPMENT</b>	<b>1,446,400</b>	<b>1,306,325</b>	<b>(140,075)</b>	<b>-9.7%</b>

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

**TABLE N° 3**  
**CONSOLIDATED STATEMENTS OF INCOME FOR THE PERIOD**  
**ENDED AS OF SEPTEMBER 30, 2005 AND 2004**  
(Figures in millions of pesos as of 09.30.05)

DESCRIPTION	Jan - Sep 2004	Jan - Dec 2004	Jan - Sep 2005	VARIATION (2005/2004)	
				MCh\$	%
<b>OPERATING REVENUES</b>					
<b>FIXED TELECOMUNICATIONS</b>	<b>325,647</b>	<b>432,356</b>	<b>329,460</b>	<b>3,813</b>	<b>1.2%</b>
<b>Basic Telephony</b>	<b>232,195</b>	<b>307,048</b>	<b>222,019</b>	<b>(10,176)</b>	<b>-4.4%</b>
Fixed Monthly	114,800	150,328	95,785	(19,015)	-16.6%
Variable charge	93,613	121,031	74,119	(19,494)	-20.8%
Connections and Other Installations	2,881	3,990	2,313	(568)	-19.7%
Flexible Plans (Minutes)	2,473	8,901	30,557	28,084	S.C.
Value Added Services	13,298	17,497	14,919	1,621	12.2%
Others Basic Telephony Services	5,130	5,301	4,326	(804)	-15.7%
<b>BROADBAND</b>	<b>18,096</b>	<b>25,766</b>	<b>30,175</b>	<b>12,079</b>	<b>66.7%</b>
ADSL	13,306	19,401	22,360	9,054	68.0%
Internet Connection for Companies	4,790	6,365	7,815	3,025	63.2%
<b>Access Charges and Interconnections (1)</b>	<b>23,576</b>	<b>32,344</b>	<b>31,926</b>	<b>8,350</b>	<b>35.4%</b>
Domestic Long Distance	7,782	10,364	7,911	129	1.7%
International Long Distance	2,143	2,874	1,929	(214)	-10.0%
Access Charges Mobile - Fixed	5,816	7,930	10,214	4,398	75.6%
Other Interconnection Services	7,835	11,176	11,872	4,037	51.5%
<b>Other Local Telephone Services</b>	<b>51,780</b>	<b>67,198</b>	<b>45,340</b>	<b>(6,440)</b>	<b>-12.4%</b>
Advertising in Telephone Directories	4,860	6,023	4,340	(520)	-10.7%
ISP (Switchboard and Dedicated)	2,242	3,193	1,928	(314)	-14.0%
Telemercencia (Security Services)	4,998	6,841	5,850	852	17.0%
Public Phones	8,399	11,098	7,565	(834)	-9.9%
Interior Installation and Equipment					
Rental	24,390	32,026	22,704	(1,686)	-6.9%
Equipment Marketing	6,891	8,017	2,953	(3,938)	-57.1%
<b>LONG DISTANCE</b>	<b>47,289</b>	<b>63,067</b>	<b>43,506</b>	<b>(3,783)</b>	<b>-8.0%</b>
Long Distance	19,476	25,215	17,744	(1,732)	-8.9%
International Service	18,546	24,501	14,550	(3,996)	-21.5%
Network capacity and circuit rentals	9,267	13,351	11,212	1,945	21.0%
<b>CORPORATE COMMUNICATIONS</b>	<b>61,246</b>	<b>84,896</b>	<b>56,113</b>	<b>(5,133)</b>	<b>-8.4%</b>
Terminal Equipment	10,643	13,901	9,449	(1,194)	-11.2%
Complementary Services	12,643	17,105	10,814	(1,829)	-14.5%
Data Services	23,873	31,898	21,157	(2,716)	-11.4%

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Dedicated links and others	14,087	21,992	14,693	606	4.3%
<b>MOBILE COMMUNICATIONS</b>	<b>135,372</b>	<b>135,372</b>	<b>0</b>	<b>(135,372)</b>	<b>S.C.</b>
Mobile Communications (outgoing traffic)	95,783	95,783	0	(95,783)	S.C.
CPP Interconnection (2)	39,589	39,589	0	(39,589)	S.C.
<b>OTHER BUSINESSES (3)</b>	<b>3,206</b>	<b>4,054</b>	<b>2,133</b>	<b>(1,073)</b>	<b>-33.5%</b>
<b>TOTAL OPERATING REVENUES</b>	<b>572,760</b>	<b>719,745</b>	<b>431,212</b>	<b>(141,548)</b>	<b>-24.7%</b>
<b>OPERATING COSTS</b>	<b>(367,968)</b>	<b>(455,116)</b>	<b>(272,715)</b>	<b>95,253</b>	<b>-25.9%</b>
Salaries	(39,749)	(49,199)	(31,399)	8,350	-21.0%
Depreciation	(178,214)	(224,958)	(140,712)	37,502	-21.0%
Other Operating Costs	(150,005)	(180,959)	(100,604)	49,401	-32.9%
<b>ADMINISTRATIVE AND SELLING COSTS</b>	<b>(125,098)</b>	<b>(163,114)</b>	<b>(92,353)</b>	<b>32,745</b>	<b>-26.2%</b>
<b>TOTAL OPERATING COSTS</b>	<b>(493,066)</b>	<b>(618,230)</b>	<b>(365,068)</b>	<b>127,998</b>	<b>-26.0%</b>
<b>OPERATING INCOME</b>	<b>79,694</b>	<b>101,515</b>	<b>66,144</b>	<b>(13,550)</b>	<b>-17.0%</b>
Interest Income	7,351	9,509	6,227	(1,124)	-15.3%
Other Non-operating Income	485,853	486,901	2,198	(483,655)	-99.5%
Income from Investment in Related Companies (4)	276	555	1,117	841	304.7%
Interest Expenses	(36,601)	(55,351)	(22,558)	14,043	-38.4%
Amortization of Goodwill	(144,204)	(143,772)	(1,171)	143,033	-99.2%
Other Non-operating Expenses	(8,022)	(25,262)	(6,016)	2,006	-25.0%
Price-level Restatement	11,525	9,198	431	(11,094)	-96.3%
<b>NON-OPERATING INCOME</b>	<b>316,178</b>	<b>281,778</b>	<b>(19,772)</b>	<b>(335,950)</b>	<b>C.S.</b>
<b>INCOME BEFORE INCOME TAX</b>	<b>395,872</b>	<b>383,293</b>	<b>46,372</b>	<b>(349,500)</b>	<b>-88.3%</b>
Income taxes	(61,574)	(63,892)	(24,711)	36,863	-59.9%
Minority Interest	(185)	(290)	67	252	-136.2%
<b>NET INCOME (5)</b>	<b>334,113</b>	<b>319,111</b>	<b>21,728</b>	<b>(312,385)</b>	<b>-93.5%</b>

(1) Due to accounting consolidation does not include access charges of 188 Mundo Telefónica and Globus.

(2) Corresponds to income recorded in Telefónica Móvil.

- (3) Includes revenues from Tgestiona, Telepeajes and Tecnonautica
  - (4) For the purposes of a comparative analysis, participation in income from investments in related companies is shown net (net income/losses).
  - (5) For comparative purposes certain reclassifications have been made for 2004 statements of income.
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Análisis razonado consolidado

### 3. ANALYSIS OF INCOME FOR THE PERIOD

#### 3.1 OPERATING INCOME

As of September 30, 2005, operating income reached Ch\$ 66,144 million, which represents a 17.0% decrease in respect to the period from January to September of the previous year. This decrease shows, an extraordinary change associated to of lower income and higher costs associated to the correspondent business, among other effects

#### Operating Income

Operating income for the period amounted to Ch\$431,212 million, a decrease of 24.7% in relation to the income obtained in the period from January to September 2004 of Ch\$572,760 million.

This variation was mainly originated by the deconsolidation of subsidiary Telefónica Móvil de Chile S.A. in July 2004, together with a decrease in long distance income and in income from corporate communications, partly offset by an increase in income from fixed telephone services.

***Revenues from Local Telephone Services:*** This income shows a 1.2% increase, due to the effects of a 4.4% drop in **basic telephone services** in respect to the pervious year, derived from the 20.8% 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 in the first nine months of 2005. **Fixed monthly charge**, corresponding to the fixed monthly charge for connection to the network, decreased by 16.6% mainly explained by the incorporation of customers to flexible plans, offset by the effect of higher income due to the application of the new rate decree. Consequent with the above, the incorporation of customers to **flexible plans** positively contributed to the Ch\$28,084 million increase in income. Income from **connections and other install ations** dropped 19.7% in respect to the first nine months of the previous year, whereas **value added services** grew by 12.2% partly due to an increase in advanced corporate services. **Other basic telephony services income** dropped by 15.7% .

**Broadband** services increased by 66.7% in the period from January to September 2005, reaching Ch\$30,175 in 2005 whereas in the same period the previous year income from these services amounted to Ch \$18,096 million.

**Access charges and interconnections** increased by 35.4%, mainly due to the 51.5% increase in **other interconnection services**, highlighted by media rental services, carrier information, connection services and unbundling services, together with a 75.6% increase in **mobile and fixed access charges**. It should be noted, that these increases are influenced by the recognition in 2005 of income from services generated with Telefónica Móvil. There was a 10.0% drop in income from international long distance access charges, effect which was partly offset by a 1.7% increase in income from domestic access charges.

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Análisis razonado consolidado

**Other fixed telephone services** decreased by 10.8%, equivalent to Ch\$5,606 million explained fundamentally by the Ch\$3,938 million drop in income from commercialization of equipment and Ch\$1,686 million in income from interior installations and equipment rental.

**Long Distance:** Revenues from these services decreased by 8.0% in comparison to 2004, due to a decrease of 8.9% and 21.5% in income from DLD and ILD, respectively, situation that was influenced by a decrease in average outgoing long distance prices, a 25.9% drop in DLD traffic and a 60.2% drop in outgoing ILD traffic, added to the extraordinary effect of lower income due to the new valuation of correspondents. The above is partly offset by the incorporation of income from media and circuit rental to Telefónica Móviles de Chile, as of July 2004.

**Corporate Communications:** This business revenue shows an 8.4% decrease in respect to the previous year, mainly due to a 14.5% drop in income from complementary services, together with an 11.2% decrease in income from sale of terminal equipment and an 11.4% drop in data services. This was partly offset by a 4.3% increase in income from circuits and others.

**Mobile Communications:** No income for this concept has been recorded in 2005 since this business was deconsolidated due to the sale of Telefónica Móvil de Chile S.A. in July 2004. In the same period in 2004 this income amounted to Ch\$135,372 million.

**Other Businesses:** This revenue shows a 33.5% decrease mainly due to a decrease in income from the Subsidiary Telepeajes (teletoll services).

### **Operating Costs**

Operating costs for the period reached Ch\$ 365,068 million, decreasing by 26.0% in relation to the first nine months of 2004, period in which they reached Ch\$493,066 million. Notwithstanding, after separating the effect of Móviles, consolidated operating income reached Ch\$ 359,832 increasing by 1.4% in relation to 2004.

The above is mainly explained by the extraordinary adjustment made for the concept of correspondents, effect that is compensated by a tendency to drop and/or maintain expense levels, mainly in goods and services and depreciation 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 as of September 30, 2005 shows a deficit of Ch\$ 19,772 million, whereas in the same period of 2004 non-operating income reached Ch\$316,178 million. The change in non-operating income is broken down as follows:

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Análisis razonado consolidado

**Financial income** shows a decrease of 15.3%, mainly because a greater volume of available funds in 2004 from the sale of subsidiary Móviles were transitorily destined to financial investments.

**Other non-operating income** amounted to Ch\$2,198 million, figure which is lower than the Ch\$485,853 million reached in 2004. This is mainly due to net income generated by the sale of Telefónica Móviles de Chile and the sale of the participation of Publiguías recorded in 2004.

**Financial expenses** decreased by 38.4% in 2005, mainly associated to 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\$143,033 million decrease in relation to 2004, mainly due to amortization of goodwill of subsidiary Telefónica Móvil de Chile, sold during 2004.

**Other non-operating expenses** decreased by 25.0%, derived mainly from restructuring costs recognized in the first nine months of 2004; which were offset by higher expenses associated to lawsuits and write offs of inactive property, plant and equipment.

**Price-level restatement** in the first nine months of 2005 shows a net gain of Ch\$432 million, mainly due to the variations experienced in the CPI and the la unidad de fomento. It should be noted that a 100% hedge has been maintained for exchange rate fluctuation and a 71% hedge for interest rate. The Company's exchange rate (peso-dollar) hedge policy in great measure was able to neutralize the effect of the exchange rate variation in 2004 and 2005.

### 3.3 NET RESULT FOR THE YEAR

Net result in the first nine months of 2005 reached net income of Ch\$ 21,728 million, whereas from January to September 2004 net income was Ch\$334,113 million. The lower income obtained in the 2005 period in comparison to 2004, is derived from a 17.0% decrease in operating income and the decrease in non-operating deficit to Ch\$ 335,950 million. Both effects are offset by the lower level of income tax, which in 2004 was influenced by the tax paid on the sale of subsidiary Telefónica Móvil.

### 4. RESULTS BY BUSINESS AREA

**Local Telephone Business:** Recorded net income of Ch\$12,990 million as of September 2005, which was lower than the surplus of Ch\$315,581 million recorded in the first nine months of 2004, due to lower non-operating income and lower taxes derived mainly from the sale of subsidiary Móvil in 2004, offset by the better operating behavior of 2005 in relation to 2004.

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Análisis razonado consolidado

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**Corporate Communications Business:** This business contributed net income of Ch\$7,409 million in the period, a 38.8% decrease in relation to the first nine months of 2004, which presents net income of Ch\$12,103 million, due mainly to 33.5% lower operating income.

**Long Distance Business:** As of September 30, 2005 presented net income of Ch\$689 million, lower than that reached in the first nine months of 2004 which amounted to Ch\$14,273 million. This variation is produced mainly by a 76.0% drop in operating income greatly due to the extraordinary adjustment performed due to changes experienced in international businesses.

**Mobile Business:** Only 2004 income is presented (loss of Ch\$8,216 million) due to the deconsolidation of Telefónica Móviles de Chile S.A. in July 2004.

**Other Businesses:** The businesses as a whole generated net income of Ch\$644 million and operating income of Ch\$604 million in the nine-month period ended as of September 30, 2005, whereas during the same period the previous year they recorded net income of Ch\$371 million with operating income of Ch\$515 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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## Management's Discussion and Analysis of the Consolidated Financial Statement

**REVENUES AND COSTS BY BUSINESS  
AS OF SEPTEMBER 30, 2005 AND 2004  
(Figures in millions of pesos as of 09.30.05)**

	Fixed Telecommunications		Corporate Communications		Long Distance			Mobile Telephony			
	Jan-Sep 2004	Jan-Dec 2004	Jan-Sep 2005	Jan-Sep 2004	Jan-Dec 2004	Jan-Sep 2005	Jan-Sep 2004	Jan-Dec 2004	Jan-Sep 2005	Jan-Sep 2004	Jan-Dec 2004
<b>Operating Revenues</b>	<b>377,310</b>	<b>501,564</b>	<b>374,259</b>	<b>75,500</b>	<b>103,922</b>	<b>63,823</b>	<b>66,840</b>	<b>90,150</b>	<b>59,084</b>	<b>140,095</b>	<b>140,095</b>
Revenues	325,647	432,356	329,460	61,246	84,896	56,113	47,289	63,067	43,506	135,372	135,372
Intercompany Transfers	51,663	69,208	44,799	14,254	19,026	7,710	19,551	27,083	15,578	4,723	4,723
<b>Operating Expenses</b>	<b>(330,708)</b>	<b>(441,692)</b>	<b>(325,900)</b>	<b>(60,106)</b>	<b>(83,131)</b>	<b>(53,588)</b>	<b>(48,853)</b>	<b>(70,615)</b>	<b>(54,768)</b>	<b>(143,911)</b>	<b>(143,688)</b>
Payroll	(45,707)	(60,091)	(44,748)	(6,872)	(9,336)	(7,824)	(2,053)	(3,037)	(1,913)	(8,789)	(8,789)
Depreciation	(130,908)	(173,149)	(130,545)	(9,024)	(11,815)	(7,264)	(7,957)	(12,305)	(7,868)	(36,962)	(36,740)
Goods and Services	(99,433)	(135,725)	(106,602)	(13,212)	(21,087)	(13,122)	(27,747)	(38,403)	(32,689)	(92,178)	(92,178)
Intercompany Transfers	(54,660)	(72,727)	(44,005)	(30,998)	(40,893)	(25,378)	(11,096)	(16,870)	(12,298)	(5,982)	(5,982)
<b>Operating Income</b>	<b>46,602</b>	<b>59,872</b>	<b>48,359</b>	<b>15,394</b>	<b>20,791</b>	<b>10,235</b>	<b>17,987</b>	<b>19,535</b>	<b>4,316</b>	<b>(3,816)</b>	<b>(3,593)</b>
<b>Non-operating Income and Expenses</b>											
Financial Expenses	(36,081)	(54,827)	(22,550)	(37)	(41)	2	(1)	(1)	(4)	(480)	(480)
Other Income and Expenses	352,889	342,348	4,667	(106)	(357)	(1,008)	240	(4,393)	(796)	(162)	(340)
Intercompany Transfers	8,346	9,042	1,767	116	196	538	(306)	(622)	260	(5,138)	(5,138)
<b>Non-operating Income</b>	<b>325,154</b>	<b>296,563</b>	<b>(16,116)</b>	<b>(27)</b>	<b>(202)</b>	<b>(468)</b>	<b>(67)</b>	<b>(5,016)</b>	<b>(540)</b>	<b>(5,780)</b>	<b>(5,968)</b>
<b>R.A.I.I.D.A.I.E (*)</b>	<b>538,745</b>	<b>584,411</b>	<b>185,338</b>	<b>24,428</b>	<b>32,445</b>	<b>17,029</b>	<b>25,878</b>	<b>26,825</b>	<b>11,648</b>	<b>27,846</b>	<b>27,660</b>

**Taxes and  
Other**

(56,175)	(57,082)	(19,253)	(3,264)	(4,407)	(2,358)	(3,647)	(3,942)	(3,087)	1,380	1,370
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**Income After  
Taxes**

<b>315,581</b>	<b>299,353</b>	<b>12,990</b>	<b>12,103</b>	<b>16,182</b>	<b>7,409</b>	<b>14,273</b>	<b>10,577</b>	<b>689</b>	<b>(8,216)</b>	<b>(8,180)</b>
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(\*) R.A.I.I.D.A.I.E. : Income before taxes, interest, depreciation, amortization and extraordinary item

**GRAPH OF NET INCOME (LOSS) BY BUSINESS  
AS OF SEPTEMBER 30, 2005 AND 2004  
(Figures in millions of pesos as of 09.30.05)**

Análisis razonado consolidado

**5. STATEMENT OF CASH FLOWS**

**TABLE No. 4**  
**CONSOLIDATED CASH FLOWS**  
*(Figures in millions of pesos as of September 30, 2005)*

DESCRIPTION	JAN-SEP 2004	JAN-SEP 2005	VARIATION MCh\$ %	
Net cash from operating activities	171,030	155,482	15,548	9.1%
Net cash from financing activities	-634,423	-213,443	-420,980	66.4%
Net cash from investing activities	808,262	-75,918	884,180	c.s.
Effect of inflation on cash and cash equivalents	-4,681	-1,229	-3,452	73.7%
Net change in cash and cash equivalents for the period	340,188	-135,108	475,296	c.s.

The negative variation of Ch\$ 135,108 million in cash flows for 2005 compared to the positive variation of Ch\$ 340,188 million in 2004, is mainly due to resources obtained from the sale of subsidiary Telefónica Móvil in 2004, presented as cash flows from investment activities. Due to this, during January-June 2004, cash flows were destined to amortization and prepayment, in order to decrease the financial debt of Telefónica, and to pay dividends, effects that are presented under financing activities. During 2005 the policy of decreasing the financial debt and distribution of dividends has continued, partly explaining the negative net variation in cash and cash equivalents.

Análisis razonado consolidado

**6. FINANCIAL INDICATORS**

**TABLE No. 5**  
**CONSOLIDATED FINANCIAL INDICATORS**

DESCRIPTION	JAN-SEP 2004	JAN-DEC 2004	JAN-SEP 2005
<b>LIQUIDITY RATIO</b>			
<b><u>Current Ratio</u></b> (Current Assets / Current Liabilities)	1.32	1.21	0.89
<b><u>Acid Ratio</u></b> (Most liquid assets / Current Liabilities)	0.39	0.25	0.16
<b>DEBT RATIOS</b>			
<b><u>Debt Ratio</u></b> (Total Liabilities / Shareholders' Equity)	1.14	0.92	0.83
<b><u>Long-term Debt Ratio</u></b> (Long-term Liabilities / Total Liabilities)	0.56	0.62	0.57
<b><u>Financial Expenses Coverage</u></b> (Income Before Taxes and Interest / Interest Expenses)	11.62	7.75	2.78
<b>RETURN AND NET INCOME PER SHARE RATIO</b>			
<b><u>Operating Margin</u></b> (Operating Income / Operating Revenues)	13.9%	0.14%	15.3%
<b><u>Operational Income Return</u></b> (Operating Income / Net Property, Plant and Equipment <sup>(1)</sup> )	4.1%	5.3%	4.7%
<b><u>Net Income per Share</u></b> (Net Income / Average number of paid shares each year)	\$338.9	\$323	\$22.7
<b><u>Return on Equity</u></b> (Income / Average shareholders' equity)	28.06%	27.0%	2.25%
<b><u>Profitability of Assets</u></b> (Income/Average assets)	13.86%	14.0%	1.20%
<b><u>Operating Assets Yield</u></b> (Net income / Average operating assets (2))	19.85%	19.13%	1.60%

**Return on Dividends**

(Paid dividends / Market Price per Share)	29.1%	42.4%	7.1%
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***ACTIVITY INDICATORS***

<b><u>Total Assets</u></b>	MM\$	2,202,987	MM\$	1,940,092	MM\$	1,691,182
<b><u>Sale of Assets</u></b>	MM\$	213,510	MM\$	212,954	MM\$	784
<b><u>Investments in other companies and property, plant and equipment</u></b>	MM\$	64,593	MM\$	86,289	MM\$	46,703
<b><u>Inventory Turnover</u></b>						
(Cost of Sales / Average Inventory)		6.10		3.48		2.38
<b><u>Days in Inventory</u></b>						
(Average Inventory / Cost of sales times 360 days)		59.0		103.5		151.2

Figures at the beginning of the period,

- (1) restated.
- (2) Property, plant and equipment are considered operating assets

## Análisis razonado consolidado

The table below shows, a decrease in the liquidity ratio due to a 41.1% decrease in current assets, whereas current liabilities decreased by 25.9%, due to a decrease in the financial debt in comparison to September of the previous year. Both issues were influenced by the effects of the deconsolidation of Móvil. This liquidity ratio lower than one, (i.e. current assets lower than current liabilities) is basically explained by the reclassification of short-term Yankee bonds, since both series of bonds will be paid during 2006. The Company contemplates covering these obligations with cash flows generated by its operations.

The decrease in the debt ratio is explained by a 36.4% drop in the level of demand liabilities whereas shareholders equity decreased by 31.2%, 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 zero or close to zero, which have a market value, which compared to the book value is not significant in 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 set up, when the market value is less than the book value.

### **8 REGULATORY ASPECTS**

#### **Fixed Telephony Tariff Decree**

Decree No. 187 is in effect as of May 5, 1999. It establishes maximum tariffs for Telefónica CTC Chile for local telephone services and interconnection services for a period of 5 years, which expired on May 5, 2004.

The main services subject to regulation of tariffs are: Telephone Line Service (formerly fixed charge), Local Measured Service, Local Tranche, Access Charges, Communications Service from Public Telephones and Network Unbundling Services.

In relation to the procedure to be followed for setting tariffs for services subject to tariff regulation, on January 13 of this year, Telefónica CTC Chile requested that the Antitrust Commission decree freedom of tariffs in specific geographic areas, that they define telephone services which will be subject to tariff regulation in areas where the market conditions are not sufficient to guarantee a freedom of tariffs regime and that they determine that Telefónica CTC Chile has the right to offer alternative tariff plans without prior authorization.

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## Análisis razonado consolidado

Together with the tariff setting process of Telefónica CTC Chile, Subtel began the rate setting process for public services provided by Entelphone in Easter Island and the tariffs for interconnection services (access charges) provided by Entelphone, CMET, Telesat and Manquehue Net.

On April 30, 2003, Telefónica CTC Chile presented to Subtel its Technical Economic Bases for the Tariff Setting Study for the services provided by Telefónica CTC Chile to other public telephone concessionaries, to intermediate services concessionaries which provide long distance telephone services, and to suppliers of complementary services.

On May 20, 2003, the Antitrust Commission dictated Resolution No. 686 which defines the services subject to rate setting by the Ministries of Economy and Transport and Telecommunications, which are similar to those established for the 1999 - 2004 period. The mentioned Resolution No. 686 rejects the petition for freedom of rates for the specific primary zones requested by Telefónica CTC Chile, and in relation to the request for rate flexibility, informed favorably by the Regulator, the Antitrust Commission did not make a specific pronouncement in spite of the fact that most of its members were in favor of making a pronouncement, whereas the rest of the members considered that such matters did not correspond to that Commission. By request from Telefónica CTC Chile the Antitrust Commission clarified Antitrust No. 686, dictating to this effect Resolution No. 709, which provided that notwithstanding the rate setting by the administrative authority, the dominant companies could offer lower rates or different plans under the conditions defined by the respective authority.

On May 30, 2003, Subtel submitted to Telefónica CTC Chile the Preliminary Technical Economic Bases. Telefónica CTC Chile formulated 84 controversies to the Preliminary Technical Economic Bases of Subtel and requested the formation of an Experts Commission as established in the law and in the Regulations that govern the procedure, advertising and participation of the rate setting process.

The Experts Commission was officially formed on June 17, composed of experts designated by Telefónica CTC Chile and Subtel, and issued its report on July 17, 2003, making a unanimous pronouncement on all the controversies, with the exception of only one of these which was by majority.

On July 25, 2003, Subtel dictated Exempt Resolution No. 827 of 2003 which sets the Final Technical Economic Bases that will govern the rate study to set the levels, structure and indexation mechanisms of the services provided by Telefónica CTC Chile that are subject to rate setting.

Entelphone, CMET, Manquehue Net and Telesat did not formulate controversies to the Preliminary TEB. Consequent with the above, Subtel dictated the Final Technical Economic Bases for the respective companies.

On November 6, 2003 Telefónica CTC Chile, presented the Rate Study that sets the levels, structure and indexation mechanisms of the services subject to rate setting.

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## Análisis razonado consolidado

On March 5, 2004, the Ministries of Transport and Telecommunications and Economy, Development and Reconstruction submitted the Report on Objections and Counterproposals to the Rate Study. Telefónica CTC Chile requested the formation of the Experts Commission, which was officially formed on March 12, 2004. The Experts Commission issued its report on April 2, 2004, making a pronouncement on the inquiries made by Telefónica CTC Chile.

On April 4, 2004, Telefónica CTC Chile submitted to the Ministries the Report on Modifications and Insistence of the Rate Study, incorporating the recommendations of the Experts Commission and insisting on those matters that were not the object of inquiries.

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 June 2, 2004, Telefónica CTC Chile presented to the Chilean General Comptroller two presentations within the recording process of Rate Decree No. 169. The first denounces manifest mathematical errors included in Decree 169, requesting that the controlling organization correct them. The second presentation formulates legal objections relating to conceptual aspects that have an impact on the definition and scope of the services included in the decree. In both presentations the Company expressly reserves the right to take jurisdictional actions.

Entel, Chilesat and Telmex filed a complaint with the Chilean General Comptroller against Rate Decree No. 169, objecting to scaling of access charges and the criteria for cost assignation of the different rates.

On September 16, 2004, the Ministries of Transport and Telecommunications, Economy, Development and Reconstruction issued their report to the Chilean General Comptroller relating to the complaints filed by Telefónica CTC Chile, Chilesat, Entel and Telmex. In this respect, the Ministries informed that due to their review of the tariff model a large part of the mathematical errors denounced by Telefónica CTC Chile were corrected, notwithstanding that other errors apparently contained in the mentioned tariff decree were also corrected.

In turn, the Ministries defended the scaling of access charges of Tariff Decree N°169, stating that such criteria has been taken in conformity with the resolutions of antitrust organizations and those prescribed by the Economic Technical Bases established for this tariff setting process.

Regarding the conceptual aspects claimed by Telefónica CTC Chile impacting the definition and scope of services included in the decree, the ministries reject them as they reject the objections of Entel, Chilesat and Telmex.

On October 4, 2004, Telefónica CTC Chile once again appealed to the Chilean General Comptroller, in order for them to correct new mathematical errors incurred by the Ministries precisely at the time that they corrected the errors informed by Telefónica CTC Chile. Likewise they insisted on certain conceptual aspects.

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## Análisis razonado consolidado

Subtel once again submitted Decree No.169 to the Chilean General Comptroller on December 30, 2004, after modifying certain network unbundling tariffs, in the item Adjustment of Civil Works ( Adecuación de Obras Civiles ). Likewise, Subtel once again modified among other tariffs, those of the Adjustment of Civil Works item, resubmitting Decree 169 to the Chilean General Comptroller on January 14, 2005.

Furthermore, in January 2005. Entel and Telmex submitted new presentations to the Chilean General Comptroller, where Entel complains about the tariffs set by the Ministries in respect to Adjustment of Civil Works and Telmex attaches information sustaining that access charge rates must be at direct cost.

On February 8, 2005, the Chilean General Comptroller recorded Tariff Decree No. 169. The report of the Chilean General Comptroller does not accept the complaints regarding conceptual aspects presented by Telefónica CTC Chile and does not make a pronouncement regarding the new mathematical errors denounced in October 2004. The complaints filed by Telmex, Chilesat and Entel were rejected by the Chilean General Comptroller.

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.

### **Tariff Flexibility**

By means of Resolution No. 709 of October 13, 2003, the Antitrust Commission decided to: Accept the request on fs 476 of Compañía de Telecomunicaciones de Chile S.A., only in respect to that 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, 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 public 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 for these purposes by the respective authority.

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.

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Análisis razonado consolidado

### **Mobile Telephone Tariff Decree**

Decree No. 7 is in effect as of February 12, 1999. It establishes maximum rates for Telefónica Móvil for interconnection services, including Mobile Access Charges, for a period of five years, which expired on February 12, 2004.

On July 25, 2003, Telefónica Móvil presented the Rate Study to set the tariffs for services subject to tariff setting.

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. That decree was submitted for recording by the Chilean General Comptroller, together with the supporting report.

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 by one digit the local telephone numbers in the Primary Zones of Valparaiso and Concepción. The extension for Santiago and the rest of the zones was deferred.

#### **Attention of customer complaints by telephone and free communications for emergency services**

Decree No. 590 issued by the Ministry of Transport and Telecommunication establishes free communications destined to emergency service levels 131, 132 and 133 and communications destined to emergency services are exempt from disconnection of service; it establishes the obligation of the telephone companies to attend to complaints over the telephone and defines a new special number for telephone complaints (105). Telefónica CTC Chile had already incorporated such free of charge communications as of May 6, 2004, in accordance with tariff decree No. 169 and in turn, telephone complaints have been operating since the end of 2000 through the special 107 number. In relation to the enabling of communication with emergency services from a line which has been disconnected, Telefónica CTC Chile enabled telephone lines that depend on switchboards that currently have the capacity and functions necessary to maintain availability of access to emergency services even in case of service disconnection due to breach by the subscriber.

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Análisis razonado consolidado

### **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 of 2005 is set to apply the provisions established in the mentioned decree.

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

Outside of the deadline Subtel made observations to the proposal made by Telefónica CTC Chile, ordering them to be overcome 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, situation that did in fact occur and that is not recognized in the pronouncement.

On August 30, 2005, Subtel answered to the Chilean General Comptroller in respect to the legality complaint filed by Telefónica CTC against the acts of Subtel which extemporaneously made observations to the new model of the Single Telephone Bill.

In its report, Subtel recognizes acting outside the deadlines, and formulates its defense on the basis that Telefónica CTC Chile's model of telephone bill does not adjust to the legal ordinance.

On October 6, 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 will attach a Legal Report to the Chilean General Comptroller from the Administrative Law professor, which confirms the relevance of the complaint that was filed.

With this information the Chilean General Comptroller must decide whether it accepts or rejects the complaint filed, which should occur before year-end.

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

By means of Exempt Resolution No. 1319, of October 6, 2004, the Undersecretary of Telecommunications 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.

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

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

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## Análisis razonado consolidado

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 our Constitution.

Regarding the IP Telephony proposal, it defines a special type of broadband telephony, that 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 attempt against development of the industry since it discourages investment in new infrastructure and in broadband.

As of September 30, 2005, 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 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 resolution that involves an end to the discussion and evidence stage sentence should be dictated in the following months.

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Análisis razonado consolidado

**Voissnet makes an accusation before the National Economic Attorney General's Office( Fiscalía Nacional Económica ) and files lawsuit before the Antitrust Commission, both against Telefónica CTC Chile**

On January 20, 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 against 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 counterplea against Voissnet, in order for the Court to correct, prohibit and suppress the serious attempts against 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 counterplea presented by Telefónica CTC Chile, questioning the contractual restrictions imposed by Telefónica CTC Chile.

Last April 8, 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 received for evidence, but a date was 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.

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## Análisis razonado consolidado

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 elucidated.

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 unidades tributarias anuales, o whatever fine the TDLC in justice 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 for last August 11 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.

### **Setting Rates for Post Supports**

Telefónica CTC Chile together with other telecommunications companies presented discrepancies 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.

Likewise, the distribution companies also presented before the Panel of Experts their discrepancies 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 together with the rest of the telecommunications companies that formulated discrepancies to the Panel of Experts, presented their observations of the discrepancies formulated by the electric companies.

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## Análisis razonado consolidado

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 discrepancies formulated 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 Chilquita, filing separate appeals before the Chilean General Comptroller. The Chilean General Comptroller has not issued its report.

On September 16, 2005, the Ministry of Economy submitted to the Chilean General Comptroller for recording, the Tariff Decree that sets the new rates for associated services, which is in the process of legal and economic review by the Chilean General Comptroller.

**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.

Subtel must review the information presented by the companies to qualify the points obtained by the applicant companies. According to the tender documents, it will be resolved in function of the points granted to the projects, which privilege geographic coverage and speed of implementing the project. In case of a tie between two or more companies, it will be resolved in favor of the company that has a preferential right recognized in the Tender; in case of a tie between companies with preferential rights, it will be resolved through a tender on the basis of the greatest amount of money offered by the bidder. Telefónica CTC Chile does not have preferential rights in the Tender; these are given to Telmex Servicios Empresariales, MIC Chile and Chile Wireless (owned by VTR).

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Análisis razonado consolidado

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

### **Relevant aspects of the industry**

During the third quarter of 2005, the Telecommunications industry maintained the dynamism that characterizes it, with emphasis on the evolution of the mergers and acquisition processes of operators and continuity of the constant changes in consumer choices for telecommunications services.

It is estimated that lines in service as of September 2005 reached approximately 3.4 million, reflecting a 5.9% increase in respect to the same period last year, derived mainly from prepaid telephone services. Voice services show variations of approximately 10% in local, -12.9% in DLD and 5.5% in ILD in respect to the previous year.

It is estimated that as of September 2005, the mobile telephone market reached a total of 10.8 million subscribers, which represents an accumulated growth in the order of 22% in respect to as of September 2004.

The Internet market shows a migration from narrowband to broadband, with a 48% decrease in the narrowband market with a total estimated 3,389 million minutes and a 39% increase in the broadband market, which as of September 2005, reaches 640 thousand accesses, 55% with ADSL technology.

### **Relevant aspects in the competitive areas**

#### ***GTD made an offer to purchase 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, through a purchase contract, GTD Grupo Teleductos S.A. through its subsidiaries GTD Teleductos S.A, GTD Telesat S.A. and GTD Internet S.A. purchased all the shares of Manquehue Net S.A. thus acquiring control of the company.

Furthermore, and by separate contract on the same date, GTD Teleductos S.A. acquired at their par value, loans against Manquehue for a total value of UF 318,321 including principal and interest.

#### ***América Móvil acquires Smartcom***

On August 3, 2005 América Móvil announced the acquisition of 100% ownership of Smartcom by the Endesa España Group, the value of the company involved in the operation was US\$ 472 million.

#### ***Telecom Italia sells its participation in ENTEL S.A.***

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

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## Análisis razonado consolidado

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.

***Liberty Media takes control of United Global Com, Parent Company of VTR and requests the merger of 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 of a series of corporate conditions, of 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.

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## Análisis razonado consolidado

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 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., 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 the Undersecretary of Telecommunications of the Ministry of Transport and Telecommunications (SUBTEL).

Currently 12 companies with 13 brands participate in this market, including four rural operators. The penetration rate as of September 2005 was in the order of 21.1 lines per 100 inhabitants. Telefónica CTC Chile has approximately 72% of fixed telephone lines as of September 2005.

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Análisis razonado consolidado

### ***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.

In this market there are currently 15 companies operating with 18 carrier codes. Traffic in the DLD market, through fixed telephone lines recorded a 13.2% drop in the third quarter of 2005 in respect to the third quarter of 2004. In the same period a decrease of 5.1% is estimated in 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 32.9% in outgoing international long distance in the third quarter of 2005. When considering market share accumulated from January to September of this year, Telefónica CTC Chile obtains 46.4% of the Domestic Long Distance market and 32.3% of the International Long Distance market.

### ***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). Likewise 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 44% accumulated as of the third quarter of 2004, including sale of advanced equipment to companies.

### ***Mobile Communications***

Contemplates providing 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 who 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 decreased by 8% in the period from January to September 2005 in respect to the same period the previous year, the upward tendency continues mainly due to the increase in mobile subscribers. Mobile-fixed traffic increased by +8% in the same period.

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Análisis razonado consolidado

### ***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 746,800 subscribers as of June 2005, two satellite TV operators and close to 20 cable TV operators in specific areas, which altogether do not exceed 4% of the market.

### ***Internet Access***

In this market there are currently approximately 35 ISPs operating effectively, with three of these concentrating 83% of traffic. IP traffic (switchboard) accumulated from January to September 2005 in the network of Telefónica CTC Chile reached the order of 2,575 million minutes, a 31% drop in respect to the same period in 2004, 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 September 2005, Telefónica CTC Chile's broadband connections in service reached 268,344 a growth of 49% compared to as of September 2004, achieving an estimated broadband market share of 42% as of September 2005, considering speeds equal to or exceeding 128 kbps.

### ***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 September 2005 has approximately 24% of the market share considering its own 9,945 public telephones. Additionally, Telefónica CTC Chile has another 14,494 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 September 2005 it is estimated that Telefónica CTC Chile has a market share of 31% in this service

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Análisis razonado consolidado

## 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 is dollar/UF and dollar/peso exchange insurance.

As of September 30, 2005, the interest bearing debt in original currency expressed in dollars was US\$ 916 million, including US\$706 million in financial liabilities in dollars, US\$145 million in debt expressed in unidades de fomento and US\$65 million of debt in Chilean pesos. In this manner US\$706 million correspond to debt exposed directly to the variations of the dollar.

Simultaneously, the Company had dollar/UF, dollar/peso exchange insurance and assets in dollars that resulted, as of closing of the third quarter of 2005, 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 September 30, 2005, the Company had debt at variable interest rates Libor and TAB mainly for syndicated loans.

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 September 30, 2005 this has allowed the Company to end with an exposure of 29% of the total interest bearing debt in original currency.

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**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: December 29, 2005

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

By:           /s/ Julio Covarrubias F.

Name: Julio Covarrubias F.

Title: Chief Financial Officer

**FORWARD-LOOKING STATEMENTS**

This press release may contain forward-looking statements. These statements are statements that are not historical facts, and are based on management's current view and estimates of future economic circumstances, industry conditions, company performance and financial results. The words "anticipates", "believes", "estimates", "expects", "plans" and similar expressions, as they relate to the company, are intended to identify forward-looking statements. Statements regarding the declaration or payment of dividends, the implementation of principal operating and financing strategies and capital expenditure plans, the direction of future operations and the factors or trends affecting financial condition, liquidity or results of operations are examples of forward-looking statements. Such statements reflect the current views of management and are subject to a number of risks and uncertainties. There is no guarantee that the expected events, trends or results will actually occur. The statements are based on many assumptions and factors, including general economic and market conditions, industry conditions, and operating factors. Any changes in such assumptions or factors could cause actual results to differ materially from current expectations.

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