eurofly

# REPORT ON OPERATIONS AND FINANCIAL STATEMENTS FOR FISCAL YEAR 2005

Eurofly S.p.A. - Registered Office in Milan (MI) - Via Ettore Bugatti, 15 - Share Capital 13,355,302 Euro
R.E.A. Milano no. 1336505 - Company Register Milan 05763070017
VAT No. 03184630964 - Fiscal Code 05763070017

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## BOARD OF DIRECTORS
(appointed by the Shareholders' Meeting of 15 September 2003)

| | | |
|---|---|---|
| President | Giuseppe | **BONOMI** |
| Managing Director | Augusto | **ANGIOLETTI** |
| Directors | Ruggeromassimo | **JANNUZZELLI** |
| | Eugenio<br>(appointed on 12 September 2005) | **LAPENNA** |
| | Laura<br>(appointed on 12 September 2005) | **SANVITO** |
| | Arnaldo<br>(resigned on 12 September 2005) | **GRIMALDI** |
| | Giovanni<br>(resigned on 01 July 2005) | **ROSSI** |

## BOARD OF STATUTORY AUDITORS
(appointed by the Shareholders' Meeting of 15 September 2003)

| | | |
|---|---|---|
| President | Guido | **MONGELLI** |
| Statutory Auditors | Maurizio | **DATTILO** |
| | Michele | **SARACINO** |
| Alternate Auditors | Giovanni<br>(appointed on 29 July 2004) | **INTRIGLIOLO** |
| | Dario<br>(appointed on 29 July 2004) | **FANGARESI** |

## INDEPENDENT AUDITING FIRM **DELOITTE & TOUCHE S.p.A.**
(appointed by the Shareholders' Meeting of 12 September 2005 for the three years period 2005 - 2007)

# MANAGEMENT REPORT ON OPERATIONS

**Dear Shareholders,**

The following Report, prepared on the basis of the criteria provided by art. 2428 of the Italian Civil Code, refers to the financial statements as of 31 December 2005, which closed with a loss of 3,123 thousand Euro after amortization and depreciation, and provision for risks and charges in the amount of 6,081 thousand Euro, and which shows extraordinary net proceeds of 711 thousand Euro and capital gains from disinvestments of assets amounting to 1,581 thousand Euro.

As better analyzed below, fiscal year 2005 – subject to the negative effects of extraordinary natural events and acts of terrorism – represented a turning point for the Company's activity, which completed the listing process for the Stock Exchange on 21 December 2005.

We are presenting the principal economic and financial data below together with asset indicators for fiscal year 2005, compared with that of the previous fiscal year:

| *Unless otherwise specified, Euro/000* | 2005 | 2004 | Variation | Variation % |
|---|---|---|---|---|
| **Significant information** | | | | |
| Total flight hours | 42,060 | 38,202 | 3,858 | 10.1 |
| Passengers transported | 1,603,240 | 1,474,341 | 128,899 | 8.7 |
| Available fleet rented and in wet lease (machine months) | 136 | 133 | 3 | 2.2 |
| Productivity Long Range fleet (in flight hours) | 5,441 | 5,462 | (21) | (0.4) |
| Productivity Mid Range fleet (in flight hours) | 3,192 | 2,855 | 337 | 11.8 |
| **Summary Statement of profits and losses** | | | | |
| Revenue from sales and services, net of *code share income* (1) | 271,475 | 232,113 | 39,362 | 17.0 |
| Total revenue net of *code share income* (1) | 277,461 | 234,391 | 43,070 | 18.4 |
| EBITDAR (2) | 30,823 | 24,261 | 6,562 | 27.0 |
| Percentage on total revenue | 11.4% | 10.5% | | |
| EBITDA (3) | 1.392 | 8.100 | (6,709) | (82.8) |
| Percentage on total revenue | 0.5% | 3.5% | | |
| EBIT (4) | (4,689) | 4,263 | (8,952) | (210.0) |
| Percentage on total revenue | (1,7%) | 1.8% | | |
| Results of the year | (3,123) | 6,835 | (9,958) | (145.7) |
| **Summary Balance Sheet** | | | | |
| Total Fixed Assets | 64,407 | 60,899 | 3,508 | 5.8 |
| Total Current Assets | 95,762 | 62,110 | 33,652 | 54.2 |
| Non current assets to be divested | – | 4,302 | (4,302) | (100.0) |
| Total assets | 160,169 | 127,311 | 32,858 | 25.8 |
| Net equity | 45,427 | 16,224 | 29,203 | 180.0 |
| Total non current liabilities | 11,819 | 7,688 | 4,131 | 53.7 |
| Total current liabilities | 102,923 | 103,398 | (475) | (0.5) |
| Total net equity and liabilities | 160,169 | 127,311 | 32,858 | 25.8 |
| **Other financial data** | | | | |
| Additions to fixed assets | 39,207 | 48,614 | (9,407) | (19.4) |
| Net financial position (5) | 23,387 | 4,891 | 18,496 | 378.2 |
| Net available liquidity (short term net financial indebtedness) | 13,251 | (801) | 14,052 | – |
| Net Equity | 45,427 | 16,224 | 29,203 | 180.0 |

(1) The revenue for 2004 is indicated net of code share revenue which, in the reclassified income statement, is included among other revenues, net of the relative costs.

(2) EBITDAR: *Earnings Before Interest, Taxes, Depreciation, Amortization and aircraft Rentals* (i.e. EBIT gross of operative rental costs for aircraft – exclusive of wet leases – and depreciation and provisions to risk and charges).

(3) EBITDA: *EBITDA: Earnings Before Interest, Taxes, Depreciation, Amortization.*

(4) EBIT: *Earnings Before Interest and Taxes.*

(5) With respect to net liquidity (net short term financial indebtedness), the net financial position includes financial fixed assets and the non current portion of bank loans.

Reference is made to the paragraphs "Analysis of results" and "Financial operations" for a detailed review of the trend of the scope of the above, however we feel it is important to immediately emphasize the operations on Capital and Net Equity that took place during the fiscal year.

In particular, we note that the Shareholders' Meeting of 11 May 2005, at the time of the approval of the financial statements for the fiscal year ended 31 December 2004, had approved appropriating the profit for the year of 6,835 thousand Euro by allocating 342 thousand Euro to the legal reserve, 5,000 thousand Euro to dividends to be distributed within June 2005 and the remainder, amounting to 1,493 thousand Euro, to a special available reserve of net equity. An Extraordinary Shareholders' Meeting was held on 26 May 2005, which approved attributing the Board of Directors, in accordance with article 2443 of the Italian Civil Code, with the right to increase the share capital on one or more occasions, on a gratuitous basis, within 31 July 2005 for a maximum nominal amount of 500 thousand Euro by means of the issue of a maximum number of 500,000 ordinary shares, enjoying regular rights, to be awarded to the Company's employees in accordance with article 2349 of the Italian Civil Code and article 29 of the By-laws, designating a portion of the available reserve to a specific reserve for a corresponding amount.

In conformity with the resolution approved by the Extraordinary Shareholders' Meeting of 26 May 2005, the Board of Directors resolved on 1 July 2005 to increase the share capital from 6,666,922.00 Euro to 7,065,302.00 Euro, and thus to 398,380.00 Euro by means of the use, for a corresponding amount, of the special reserve that the ordinary Shareholders' Meeting of 11 May 2005 had created. The operation was performed by means of the issue of 398,380 new shares having a nominal value of 1.00 (one) Euro each, and enjoying regular rights relative to fiscal year 2005. Said shares were awarded to a limited number of the Company's employees, in accordance with article 2349 of the Civil Code and article 29 of the By-laws.

On 12 September 2005, the Shareholders' Meeting voted to present a request for Eurofly S.p.A.'s ordinary shares to be listed on the Telematic Stock Market (Mercato Telematico Azionario), organized and managed by Borsa Italiana S.p.A.. Further, at the same time it approved an increase of the share capital in exchange for consideration, in a divisible form, for a maximum of 7,000 thousand Euro by means of the issue, including in more than one tranche, of a maximum of 7,000,000 new ordinary shares having a nominal value of 1.00 (one) Euro each and with the regular enjoyment of rights, with the exclusion of an option right in accordance with art. 2441, paragraph V, Italian Civil Code, to be reserved as support to the offer aimed at listing the Company's shares on the Telematic Stock Market organized and managed by Borsa Italiana S.p.A.

The listing took place by means of a Global Offer of 6,300,000 shares, of which 5,900,000 newly issued shares and 400,000 shares offered for sale by the shareholder Spinnaker Luxembourg S.A., globally destined as follows:

- a minimum of 1,600,000 shares to a Public Offer aimed at an indistinct public in Italy;
- a maximum of 4,100,000 shares to an institutional placement exclusively aimed at institutional investors;
- a maximum of 600,000 shares to a private placement aimed at parties discretionally identified by the Company, together with the Joint Global Coordinators Centrobanca and Banca Profilo, who benefited from a discount of 10% of the offer price in exchange for a temporary undertaking not to transfer the shares for a period of 12 months.

The listing process was positively completed on 21 December 2005, and the Company's shares were listed on the Telematic Stock Market organized and managed by Borsa Italiana S.p.A..

As requests for 10,758,718 shares were received in the context of the Global Offer, the Joint Global Coordinators exercised the Overallotment Option for a further 900,000 shares, made available on loan by Spinnaker Luxembourg S.A., thus awarding a total of 7,200,000 shares divided as follows:

- 1,597,050 shares in the context of the public offer
- 5,051,561 shares in the context of the institutional placement
- 551,389 shares in the context of the private placement

5,900,000 shares were subscribed to. The placement price was 6.40 Euro per share.

On 26 January 2006, at the end of the stabilization period, the Coordinators of the Global Offer exercised the option right to subscribe to 390,000 shares at the offer price (Greenshoe). The share capital was therefore increased by an additional 390,000 shares at the price of 6.40 Euro each. Subsequent to such increase, as of the date of approval of the financial statements, the share capital was equal to 13,355,302.00 Euro, sub-divided into 13,355,302 shares having a nominal value of 1.00 Euro each.

## 1. THE REFERENCE BACKGROUND

### 1.1 Macroeconomic framework

The macroeconomic framework of reference for 2005 was characterized by a growth of the PIL that was not particularly high but which was continuous, and which interrupted the negative cycle present at the end of 2004 and the first months of 2005.

The pressure of inflation continued to be moderate, notwithstanding the strong increase of energy costs. In particular, the year 2005 was characterized by a strong increase in the costs of crude oil, which touched its historic maximum during the month of September (Brent at 67.5 $ a barrel). The growth of the price of crude oil is represented in the following table.

| Crude Oil | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 05/04 % |
|---|---|---|---|---|---|---|---|
| WTI - USA | 30.38 | 25.98 | 26.18 | 31.08 | 41.51 | 56.64 | 36.4 |
| Brent - Europe | 28.66 | 24.46 | 24.99 | 28.85 | 38.26 | 54.57 | 42.6 |

*Source*: Energy Information Administration - US government 2005.

The Euro/Dollar exchange rate had an opposite trend in 2005 with respect to the previous year.

In fact, while in 2004 the exchange rate grew from 1.2613 in January to 1.3408 in December, in 2005 the Euro weakened, decreasing from 1.3119 in January to 1.1856 in December.

The interest rates confirmed their growth trend in 2005, both in the United States as well as in Europe.

In addition to such macroeconomic phenomenon, there were particular natural and terrorist events that decisively darkened the geo-political scene and, in particular, some geographic areas that are significant destinations with regard to the Company's network. More specifically, the first part of 2005 was influenced by the tragedy of the Tsunami (26 December 2004), which heavily impacted the area of the Indian Ocean, hitting significant destinations for Eurofly such as Sri Lanka and the Maldives. Numerous hurricanes (hurricane Wilma, Catherine …) hit the Caribbean areas during the summer period (the first in July, the last at the end of October), causing heavy damages to the Mexican and Dominican tourist infrastructures. The terrorist attack at Sharm El Sheikh on 22 July 2005 should also be mentioned, which resulted in the death of 88 people in the famous tourist spot of the Sinai and strongly conditioned Italian tourist flow towards Egypt during the following months. It should be noted that, with regard to the Red Sea, Eurofly holds the position as leader in the Italian market.

The Company's activity was significantly penalized by the above indicated events, which affected productivity and margins, precisely during peak periods of transportation activity.

### 1.2 Background of the sector

The worldwide air transportation market registered a growth year in volumes in 2005, but with economic results that were still negative.

IATA (International Air Transport Association – which represents 265 airline companies throughout the world, which perform approximately 94% of total scheduled flights), indicated in its annual report on the sector's trend that the industry registered an overall loss even in 2005, amounting to approximately 6 billion USD, even if lower with respect to previous years and concentrated on US airline companies.

According to IATA, what occurred was prevalently due to an increase in costs, especially tied to jet fuel, which was only counterbalanced in part by an increase in invoiced sales. Said increase of invoiced sales was prevalently obtained due to the growth of transported passengers (+7.6% with respect to 2004), whereas the reduction of average yield remains, i.e. the average revenue per passenger (Source: IATA report 2005).

Turning to the Italian framework of reference, 2005 was a year of traffic growth in Italy, as demonstrated by the following table relating to airport traffic data (Source: Assaeroporti).

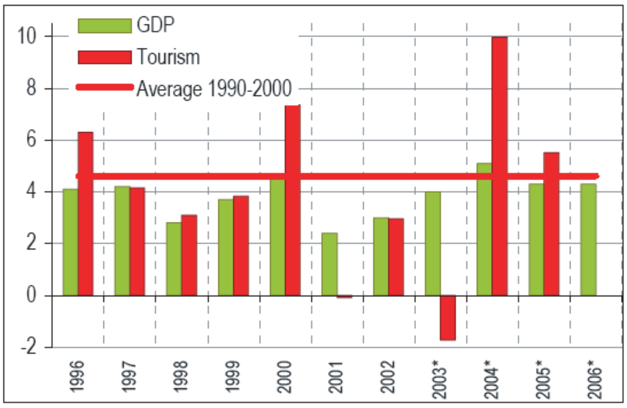
| Passengers | |
|---|---|
| National | 48,440,901 |
| *Delta % vs 2004* | *(0.4%)* |
| International | 64,095,668 |
| *Delta % vs 2004* | *10.6%* |
| Transit | 1,040,115 |
| *Delta % vs 2004* | *(5.7%)* |
| **Total Commercial** | **113,576,684** |
| *Delta % vs 2004* | *5.5%* |

The growth largely involved the international market, with very interesting percentages that were greater than the global average, rather than domestic, which demonstrated a slight decline. The reason for such increase can without doubt be attributed to the stimulus of the Italian market generated by the offer of direct flights, particularly advantageous tariffs, and secondary airports (prevalently Low Cost).

Turning instead to an analysis of demand relative to the leisure and tourist sector, the annual report of the World Tourism Organization (UNWTO) demonstrates that the number of worldwide arrivals tied to tourism grew on an annual basis of 5.5%, arriving at more than 800 million arrivals per year.

International Tourist Arrivals and Economic Growth (GDP)

World % change over previous year




Source: IMF, World Tourism Organization (WTO) ©

Growth was therefore greater than the average of the last 10 years, even if the analysis by worldwide geographic region demonstrates that it took place prevalently towards countries in the Far East, Latin American and Africa, while Europe stopped overall at 4.3%.

Turning instead to the market analysis of the Tour Operators, the ASTOI observatory (Associazione Italiana Tour Operator) indicated that Italy had undergone a reduction of approximately 2% in 2005, both with regard to transported passengers as well as for the sector's invoiced sales. ASTOI states that organized tourism suffered an exceptional sequence of negative facts and external events in 2005, which inevitably influenced the trend. The tragedy of the Tsunami that hit the area of the Indian Ocean during the first part of the year, the terrible terrorist attacks at Sharm El Sheikh in the month of July and the hurricanes that devastated the Caribbean during the course of the autumn undoubtedly represented a terrible mix of negative external factors that was reflected on the demand for air transportation to these destinations.

Anticipating what will be commented on in greater detail below, such difficult framework for Tour Operators had, among other effects, that of negatively influencing Eurofly's net working capital, because of the reduction of activity and slow down of collection times.

Turning to an analysis of Eurofly's direct competitors, the Italian market registered a net decrease of activity starting from November 2004 of the Volare Group which, with its 30 aircraft, was one of the principal competitors. The group was subjected to extraordinary administration (Marzano Law) and currently operates with a reduced number of aircraft (1 Long Range aircraft and 5 Mid Range aircraft). Such reduction in the offer was offset by an increase in the capacity of other carriers present in the market and by an increase in the number of competitors. With regard to the capacity offered, both Blue

Panorama as well as Neos increased the number of aircraft in their fleets (B757 and B767). A new Long Range carrier was born, Air Italy, which initiated new connections in the mid and Long Range leisure market by means of 2 B757 during the summer period, and with further B767 aircraft during the winter period. Two new Mid Range carriers must be added to this, one with a greater focus on the Low cost sector (My Way) and the other more evidently charter (Italy Airlines).

## 1.3 Legal and regulatory framework

The principal acts of a legislative nature during the course of 2005 having an impact on air carriers can be summarized as follows:

### • Law no. 248/2005 on "Systems requisites"

By means of Law 248/2005 of 2 December 2005, the legislator converted into law Decree no. 203 of 30 September 2005 (published in the Official Gazette no. 243 of 18 October 2005). Such law includes a series of measures (the so-called "systems requisites") having the objective of providing incentives for the increased competitiveness of national air transportation. Among the principal measures having the most immediate impact for carriers we note:

1. the abolition of the increase, equal to 50%, for nocturnal flights, of charges for landing, take-off, stopovers or shelter at national airports;
2. the elimination of the so-called "royalties", i.e. surcharges applied by airport managers and service providers to the carriers, that are unrelated to the actual costs sustained for the service provided. A typical example are the royalties applied to supplies of jet fuel;
3. the reduction of airport charges (passengers, landing, take-off and stopovers) for a value equal to the diminution of the concessions paid by the airports;
4. the reduction of terminal and route taxes, in view of to the objective of recovery of productivity and development, as well as the level of services offered and the amount of costs sustained;
5. recognition of the responsibilities that the carrier has in matters of security, with the consequent attribution to it of a share of the relative cost.

The Ministry of Transportation and ENAC have provided interpretative indications of the above law. Some national airport companies have filed petitions to obtain its annulment – upon its suspension as injunctive relief. In such context, Eurofly – as beneficiary of the application of said law - was recently served with an appeal filed by the company "Aeroporti di Roma" in front of the TAR (Regional Administrative Court) of Lazio against ENAC and the Ministry of Transportation.

### • Regulation on time limits for flight times and service

By means of the Regulation of 23 March 2005, ENAC established new limits for flight times and service, as well as rest requirements for the flight crew, in order to increase safety conditions for flight activity.

Such Regulation provides for a more restrictive discipline than the prior one with regard to the work schedules of the flight crew and new rules with regard to the make-up of the crews. Said regulation should have been completely implemented by the companies within 26 March 2006, except for two provisions relative to the "reinforced crew", which should have become effective starting from 1° July 2005.

The application of the new regulation has an impact on the size of the flight crew in that it requires, differently to the prior regime, the reinforcement of the crew in the event certain limits of daily flight hours are exceeded and, in view of the evaluation of "operational fatigue", flight assistants and pilots are considered as equivalents.

Eurofly – together with other national air carriers – deeming said Regulation to be censurable, both with regard to some aspects of merit as well as for the particular brevity of the time in which it must be implemented, filed a petition in front of the TAR of Lazio to obtain its annulment, upon its prior suspension.

The TAR of Lazio, by means of order no. 3422 of 23 June 2005, allowed the request for precautionary measures in order to re-examine the term within which its requirements had to be complied with. Subsequent to said order, ENAC's Board of Directors voted on 14 July 2005 to extend such term, setting it for the following 30 October. By means of an act served on 7 October 2005, Eurofly (and the other petitioning companies) appealed, repeating the request for injunctive relief, including with regard to such resolution. At the hearing of 20 October 2005, the request for suspension was denied and the hearing on the merits was adjourned to a hearing set for 26 January 2006.

Reference is made to chapter 13 of the present Report for developments during fiscal year 2006.

- **Revision of the Navigation Code**

By means of Legislative Decree no. 69 of 9 May 2005, the revision of the aeronautical part of the current navigation code was approved.

The principal effects on air transportation carriers can be summarized as follows:

1. Extra-community scheduled air transportation services: the airline carriers can be designated, by means of an authorization from ENAC, to perform such services on the basis of criteria established in advance and made public by means of transparent and non-discriminatory procedures. It was therefore deemed opportune to substitute the current regime of concessions with an authorization regime, in consideration of the evolution of Community law;
2. Intra-community airline services for consideration, both scheduled flights as well as charter: in conformity with the regulation set forth in EEC Reg. no. 2407/92, the principle has been established within the legal system that the authorization to perform air transportation services for passengers, mail or goods rests with air carriers holding an aircraft operator certificate (COA) and must have a license to perform such activity issued by a Member State. In this sense ENAC was specified as being the competent authority to issue the COA and the license;
3. Recognition of passenger rights due to the carrier's impediment: in the case of denial to board, cancellation or delay in take-off, or interruption of the trip, even if due to force majeure, it has been established that the passenger shall in any event have the right to the services provided by Community law, EC Reg. 261/04;
4. License for air transportation: the renewed navigation code implements the principle that the performance of air transportation activity is subordinate to the issuance of the relative license required by the provisions of EC Reg. no. 2407/92;
5. Obligation of insurance against damages: the law that required the mandatory insurance of passengers has been substituted with insurance, also mandatory, of the carrier's liability required by Community law. Because Community law does not contain a detailed regulation of such insurance, it was deemed opportune to attribute the damaged passenger, on the basis of the general principles of the Italian Civil Code, with the right of direct action against the insurer.

- **Outstanding law on Privacy**

As provided by point 19 of the technical regulations – annex B to Legislative Decree no. 196 of 30 June 2003, which regulates the Code in matters of the protection of personal data – the Company has adopted suitable security measures and preparation of the programmatic document that must be completed within the terms set by law is in course.

## 2. MANAGEMENT TREND AND OPERATING ACTIVITIES

### 2.1 Commercial activity

During the course of the year 2005, Eurofly consolidated the strategies outlined during the previous year, at the same time initiating new activities with the objective of the enhancement of unit revenue and the profitability of the aircraft.

**Leisure Activities**

In the context of leisure activity, with regard to Mid Range Eurofly consolidated the strategy initiated during the course of the year 2004 related to the creation of an operative base in Egypt. Starting from October 2004, in fact, some of the Company's aircraft were based in Egypt in order to further promote traffic from Italy towards this country, directly connecting numerous airports of the Italian provinces (for ex. Pisa, Ancona, Bari, Naples etc.) with the well-known tourist destination of Sharm El Sheikh.

The movement to Sharm of capacity equivalent to three aircraft in fact rendered such flights convenient, which previously had been made only with expensive positioning from one of Eurofly's Italian bases.

During the first six months of the year, the Company increased the number of passengers transported to Egypt by 50%, whereas on an annual basis, due to the attack at the end of July, passengers only grew by 3%.

During the course of the summer of 2005, with regard to Long Range Eurofly also initiated scheduled "point to point" flights between the most important regional towns and New York. Such flights, made during the period June - September, were launched with the following objectives:

- promote innovative initiatives in tourist markets with a decreased presence of Tour Operators, directly overseeing new markets, both Italian and foreign, and developing components of "incoming" traffic (tourism to Italy) to flank the traditional "outgoing" flows (tourism from Italy abroad);
- stimulate demand with direct "point to point" flights in intercontinental markets, copying in part the experience of the low cost companies on Mid Range flights.

The summer test of New York led to positive results both in terms of passengers as well as in operative terms. Eurofly transported approximately 37,000 passengers, with an overall load factor (coefficient of occupation of the aircraft) in excess of 70% and a percentage of sales from the US market amounting to 60% of the total. The Company's operative performance was satisfying, considering that it is a market that is typically served by traditional airline companies.

Further, for both Mid as well as Long Range, the space dedicated to multi-channels was increased, with sales of Eurofly's capacity on various channels, both from Tour Operators as well as travel agencies, as well as directly to the final user by means of the call center and web site. This kind of sale, which in 2004 involved a minimum part of Eurofly's capacity, grew until reaching approximately 7% of its total invoiced sales.

**Scheduled flights in code-sharing**

During the course of 2005, Eurofly made flights in code-sharing from Linate to domestic and international destinations with primary airline companies such as Air One and British Airways. In 2004, and until the end of the IATA 2004-2005 winter season, this activity was performed exclusively with Alitalia. A more attentive management allowed a net improvement of the margin produced by this activity, which passed from 240 thousand Euro in 2004 to 507 thousand Euro in 2005.

**ACMI (1) activity for third party operators**

During the course of 2005, Eurofly began collaborating with the carrier My Way to which it leased two aircraft of its Mid Range fleet using the ACMI formula, during the low season of 2005 (from mid

(1) A.C.M.I is the acronym of Aircraft, Crew, Maintenance and Insurance, it refers to a form of lease of the aircraft from or to third parties, whose rent includes the costs of the aircraft, crew, maintenance and insurance.

September throughout December). Such lease allowed concentrating Eurofly's traditional activity, in part reduced due to the terrorist attack at Sharm, on a minor number of aircraft increasing, consequently, their productivity. The activity, initiated in 2005 as a tactic, could be repeated in the future given the results produced.

## Statistical data and unit revenues

| | 2005 | 2004 | Variation | Variation % |
|---|---|---|---|---|
| Total flight hours | 42,060 | 38,202 | 3,858 | 10.10 |
| Mid Range | 27,996 | 26,258 | 1,738 | 6.62 |
| Long Range | 14,064 | 11,944 | 2,120 | 17.75 |
| Passengers transported | 1,603,240 | 1,474,341 | 128,899 | 8.74 |
| Eurofly | 1,496,293 | 1,451,107 | 45,186 | 3.11 |
| Other carriers | 106,947 | 23,234 | 83,713 | 360.30 |
| Mid Range | 1,199,611 | 1,122,641 | 76,970 | 6.86 |
| Long Range | 403,629 | 351,700 | 51,929 | 14.77 |

The year 2005 showed an increase of flight hours and transported passengers, and 2005 showed an increase of flight hours amounting to 10%, more concentrated on Long Range (approximately 18%) and less on Mid Range (approximately 7%).

With regard to the events of an external nature that affected the destinations where Eurofly operates with greater frequency (Egypt and the Maldives), the increase of the flight hours and the relative increase of passengers demonstrates a net capacity of reaction to negative external events.

It is also noted how Eurofly's growth was in any event greater than the percentage of growth of the traffic indicated by IATA at a world level (+7.6%), and aligned to the growth of international passengers originating in Italy, as shown from the data of Asseroporti (+10.6%).

| **Fleet Productivity**<br>*Amounts expressed in flight hours* | **2005** | **2004** | **Variation** | **Variation %** |
|---|---|---|---|---|
| Mid Range | 3,192 | 2,855 | 337 | 11.80 |
| Long Range | 5,441 | 5,462 | (21) | (0.38) |

The analysis of the productivity per aircraft (that refers only to aircraft that are a stable part of Eurofly's fleet, thus excluding aircraft in "wet lease" ), an important indicator of the efficiency in the use of an airline carrier's capacity, demonstrates how Eurofly has maintained the optimum results already achieved over the course of 2004 in Long Range, notwithstanding the increase of the capacity offered over the course of the year 2005 and the negative events cited various times. In Mid Range the increase of productivity was more decisive (+12%), and was tied to a greater use of the aircraft on the routes to and from Egypt during the first part of the year, to an improved commercial sales and distribution activity to users other than Tour Operators, and to a use of capacity in low season by means of agreements with third party operators (active wet lease).

| **Revenue per flight hour**<br>*Amounts expressed in Euro* | **2005** | **2004** | **Variation** | **Variation %** |
|---|---|---|---|---|
| Mid Range | 5,439 | 5,152 | 287 | 5.57 |
| Long Range | 8,255 | 7,882 | 373 | 4.73 |
| **Total** | **6,417** | **6,014** | **403** | **6.70** |

The unit revenue is determined only on the basis of the proceeds directly deriving from the flight activity. Because the active ACMI activity is characterized by revenue per flight hour that is less than that of charter activity, the unit proceeds in the table do not consider the revenue and the flight hours deriving from such activity.

The data demonstrates an improvement of Eurofly's commercial capacity with respect to the previous year. The average increase of approximately 7% of the entire fleet, with respect to industry data that shows a tendency of decreasing unit revenue, should be considered a positive fact, especially considering the difficult situation faced during the course of the year (increase of competition, extraordinary events, etc).

(2) Wet Lease: this refers to the lease from third parties of an aircraft having a crew (ACMI formula).

The increase of unit revenue also contributed to reducing the weight of the external increase of some costs, in particular the costs of jet fuel, even if not in a sufficient manner to recuperate them entirely.

## 2.2 The fleet

During the course of 2005 the entire Eurofly fleet was repainted in order to adopt the new livery, with grey stripes on the fuselage and the red logo "e" on the tail, chosen by Eurofly with the technical support of the Airbus design offices, anticipating the deadline of April 2006 within which it would have been necessary to eliminate the previous livery of the Alitalia Group, at the end of the transition period subsequent to Alitalia's sale to Eurofly. This was done for the purpose of giving a further signal of autonomy and to differentiate the image at the time of the launch of the operations regarding New York, with which the new grey and red uniforms for the cabin crew were introduced.

During the course of 2005, further aircraft was acquired as follows:

### *Mid Range (A320)*

During the month of February 2005, with the entrance in the fleet of the eighth aircraft, I-EEZK MSN 1125, the Mid Range A320 fleet was consolidated. An operative rental having a duration of 4 years and 10 months was stipulated with GECAS. The motors (CFM56-5B4) and the configuration of the passenger cabin (180 seats in economy class) are standard for the Company for the Mid Range fleet.

### *Long Range (A330)*

During the month of May 2005, Airbus delivered the third A330-200 aircraft, I-EEZJ MSN 665. An operative rental having a 7 year duration was stipulated with ILFC, owner of the other two A330 already present in the fleet. The motors that were chosen are the standard ones of the Company for such fleet: Pratt&Whitney PW4168A. The technical specifications of the aircraft are those of the "enhanced" version, which became standard starting from 2005 in Airbus's production line, which incorporates some technological and aesthetic developments. The configuration of the passenger cabin has 26 seats in business and 260 in economy (of which 4 are dedicated to "crew rest"). Such choice was oriented by the current request for first class seats on the Company's most frequented destinations, in particular the Maldives.

It should be noted that this new configuration was also subsequently incorporated on two other aircraft already in the fleet, by means of extraordinary maintenance performed during the period September-December 2005 at EADS Sogerma in Bordeaux, together with the "4C" maintenance operations (five year inspection) and the repainting of the liveries.

### *All business (A319-CJ/LR)*

During the month of May 2005, AIRBUS delivered an A319 CJ/LR aircraft (Corporate Jet/Long Range), registered as F-ONAS MSN 2440, with CFM56-5B7 motors and a configuration of only 48 seats in first/business, with Recaro 6510 seats and IFE (in-flight entertainment) Panasonic eFX of the last generation. In order to finance the purchase of this aircraft the Company took out a finance leasing having a duration of ten years with LOCAT S.p.A..

In order to guarantee its temporary use while waiting for the launch of the "All Business" Milan - New York route, forecast for the month of May 2006 (see chapter 13 of the present Report), the aircraft was offered in operative rental for a period of seven months, subsequently extended to ten months through 5 April 2006, to the Saudi company NAS (National Air Services), specialized in VIP transport.

The A319-CJ/LR model derives from the A319 standard model and shares all of the characteristics with the Airbus A320 family. Initially designed by Airbus to satisfy the needs of Long Range transportation for private parties and executive aerotaxi companies, it offers a very spacious passenger cabin and above all the technology and reliability of the Airbus airliner. It is currently the object of interest also by airline companies due to the possibility of offering new exclusive Long Range services. The principal differences of the A319 CJ/LR with respect to a standard A319 are the greater maximum weight at takeoff, which allows more jet fuel to be stored and thus autonomy for Long Range, removable supplemental tanks for greater refueling capacity and controllable load as well as motors with more thrust.

### *Purchase of capacity in wet lease*

During the course of the year the Company purchased capacity in wet lease in order to handle peaks of demand. In particular, this occurred during the first part of the year on Long Range, by means of the wet lease of an A330 aircraft, to anticipate the fleet's composition of three aircraft and satisfy available market demand.

During the Mid Range high season, two MD 80 aircraft were acquired in wet lease for a total of seven months.

The following table summarizes the make-up of the fleet in 2005.

| Registration mark | Type | Entry in fleet | Jan 2005 | Feb 2005 | Mar 2005 | Apr 2005 | May 2005 | Jun 2005 | Jul 2005 | Aug 2005 | Sep 2005 | Oct 2005 | Nov 2005 | Dec 2005 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| I-EEZB | A330 | Agu-02 | | | | | | | | | | | | |
| I-EEZA | A330 | Sep-02 | | | | | | | | | | | | |
| I-EEZJ | A330 | May-05 | | | | | | | | | | | | |
| I-EEZC | A320 | Oct-02 | | | | | | | | | | | | |
| I-EEZD | A320 | Feb-03 | | | | | | | | | | | | |
| I-EEZE | A320 | Mar-03 | | | | | | | | | | | | |
| I-EEZF | A320 | Apr-03 | | | | | | | | | | | | |
| I-EEZG | A320 | May-03 | | | | | | | | | | | | |
| I-EEZH | A320 | Dec-04 | | | | | | | | | | | | |
| I-EEZI | A320 | Dec-04 | | | | | | | | | | | | |
| I-EEZK | A320 | Feb-05 | | | | | | | | | | | | |
| I-DAVD | MD-82 | May-04 | | | | | | | | | | | | |
| I-DAVC | MD-82 | Jun-04 | | | | | | | | | | | | |

The following table indicates the capacity acquired in wet lease.

| Registration mark | Type | Entry in fleet | Jan 2005 | Feb 2005 | Mar 2005 | Apr 2005 | May 2005 | Jun 2005 | Jul 2005 | Aug 2005 | Sep 2005 | Oct 2005 | Nov 2005 | Dec 2005 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Mid Range | MD-82 | | | | | | | | | | | | | |
| Mid Range | MD-82 | | | | | | | | | | | | | |
| Long Range | A330-300 | | | | | | | | | | | | | |

### *Future acquisitions (A330, A350)*

During the course of the second six months of 2005 agreements were executed with leasing companies and with Airbus in order to consolidate the development of the Long Range fleet over the mid and long term period. In particular:

- AIRBUS A330

In August 2005 two operative rentals were signed with the companies CIT and ILFC, for two new A330-200 aircraft, with specifications and passenger configurations identical to the aircraft already delivered in May 2005. The delivery of said aircraft is forecast respectively for the end of the year 2006 and in March 2007, with leases having durations of eight and seven years.

- AIRBUS A350

In December 2005 a contract was stipulated with Airbus for the purchase of three A350-800 aircraft, with delivery dates forecast in 2013 and 2014, as well as three other option rights for the purchase of three aircraft to be delivered starting from 2015.

The costs of the three purchased aircraft will be financed in part using the proceeds of the listing operation and in part by means of the use of operative rentals or finance leasing. In 2005 a down payment of approximately 5.7 million USD was paid. With regard, instead, to the rights to purchase three additional A350-800, which were obtained without any financial undertaking by Eurofly, the economic conditions are identical to those of the three aircraft already purchased. The rights can be transformed into options within 2006 by means of the payment of 500 thousand USD per aircraft, whereas the confirmation of the orders can take place within 2011.

Eurofly is the “launching customer” of the A350 in Italy and is therefore the first company to acquire this type of aircraft in Italy. Said situation allowed Eurofly to benefit from particularly advantageous purchase conditions, both due to the significant reduction of the list price, as well as for some accessory contributions agreed upon by Airbus to sustain the development of the Long Range fleet.

The A350-800 is the new model of the Airbus family, officially launched in October 2005. With regard to dimensions it is totally similar to the A330-200 operated by Eurofly on Long Range, but it benefits from all of the most technologically advanced innovations experimented on the new A380, both at an avionics level, as well as with regard to new materials used. The great advantages of the A350 are its capacity to transport more of a load, at a greater distance, with year operational charges that are lower by approximately 20% with respect to the current models. Further, it has start up costs in the fleet that are very reduced for a carrier already operating with the Airbus family, given the similar level of operation. The A350 maintains, in fact, the concept of “mixed fleet flying” due to which the pilots, opportunely trained, can be used indifferently on Mid or Long Range, guaranteeing greater flexibility and productivity.

## 2.3 Invitation to tender for the purchase of the business unit “Gruppo Volare”

With regard to the procedure for the sale of the business unit of the Volare Group, whose terms and conditions are regulated by an invitation to tender authorized by the Ministry of Productive Activities on 12 October 2005, on 18 November 2005, Eurofly, together with Meridiana S.p.A., formulated its manifestation of interest in purchasing Volare’s business unit. Eurofly and Meridiana had complementary interests in the operation. Eurofly was interested in the Long Range activities, whereas Meridiana in Short and Mid Range. In particular, the purchase of traffic rights on some routes served by the Volare Group would have allowed Eurofly to complete its offer on destinations currently not served (Mauritius and the Seychelles) or served only marginally (Cuba).

On 28 December 2005, the parties presented a binding purchase offer. See chapter 13 of the present Report for developments in fiscal year 2006.

## 3. ANALYSIS OF RESULTS

| **Reclassified Income Statement** *Amounts Euro/000* | **2005** | **% on revenues** | **2004** | **on % revenues** | **Variation** | **Variation %** |
|---|---|---|---|---|---|---|
| Revenue from sales and services | 271,475 | 100.0 | 232,113 | 100.0 | 39,362 | 17.0 |
| Other revenue | 5,986 | 2.2 | 2,278 | 1.0 | 3,708 | 162.8 |
| **Total revenue** | **277,461** | **102.2** | **234,391** | **101.0** | **43,070** | **18.4** |
| Direct commercial costs | 2,674 | 1.0 | 1,090 | 0.5 | 1,584 | 145.4 |
| **Revenue net of direct commercial costs** | **274,786** | **101.2** | **233,300** | **100.5** | **41,485** | **17.8** |
| Jet Fuel | 72,788 | 26.8 | 51,814 | 22.3 | 20,974 | 40.5 |
| Costs for personnel | 39,143 | 14.4 | 35,195 | 15.2 | 3,948 | 11.2 |
| Maintenance materials and services | 33,253 | 12.2 | 34,592 | 14.9 | (1,339) | (3.9) |
| Other operating costs and wet lease | 84,449 | 31.1 | 75,009 | 32.3 | 9,440 | 12.6 |
| Other commercial and corporate costs | 14,330 | 5.3 | 12,429 | 5.4 | 1,901 | 15.3 |
| **Subtotal costs** | **243,963** | **89,9** | **209,040** | **90.1** | **34,923** | **16.7** |
| **EBITDAR** | **30,823** | **11.4** | **24,261** | **10.5** | **6,562** | **27.0** |
| Rentals | 29,431 | 10.8 | 16,160 | 7.0 | 13,271 | 82.1 |
| **EBITDA** | **1,392** | **0.5** | **8,100** | **3.5** | **(6,709)** | **(82.8)** |
| Depreciation and amortization | 2,821 | 1.0 | 2,368 | 1.0 | 453 | 19.1 |
| Other provisions | 2,000 | 0.7 | 164 | 0.1 | 1,836 | 1,119.5 |
| Provisions for risk and charges | 1,259 | 0.5 | 1,305 | 0.6 | (46) | (3.5) |
| **Subtotal costs** | **6,081** | **2.2** | **3,837** | **1.7** | **2,244** | **(58.5)** |
| **EBIT** | **(4,689)** | **(1.7)** | **4,263** | **1.8** | **(8,952)** | **(210.0)** |
| Financial Revenues/(Charges) | 775 | 0.3 | 371 | 0.2 | 404 | 109.0 |
| Results of divestments of assets | 1,581 | 0.6 | 1,034 | 0.4 | 547 | 52.9 |
| Extraordinary income/(Charges) | 711 | 0.3 | 2,235 | 1.0 | (1,524) | (68.2) |
| **Profits before taxes** | **(1,622)** | **(0.6)** | **7,904** | **3.4** | **(9,525)** | **(120.5)** |
| Tax charges | 1,501 | 0.6 | 1,069 | 0.5 | 432 | 40.5 |
| **Results of the year** | **(3,123)** | **(1.2)** | **6,835** | **2.9** | **(9,958)** | **(145.7)** |

## Revenues

In 2005 the growth of revenues from sales and services continued, with an increase of 17.0% (+39,362 thousand).

The growth interested both areas of business of the Company (Mid and Long Range), as seen from the following table:

| **Revenues from sales and services** *Amounts €/000* | **2005** | **2004** | **Variation** | **Variation %** |
|---|---|---|---|---|
| Mid Range | 149,204 | 135,060 | 14,144 | 10.47 |
| Long Range | 122,271 | 97,053 | 25,218 | 25.88 |
| **Total** | **271,475** | **232,113** | **39,362** | **16.96** |

The increase of revenue was determined both by the growth of flight hours as well as by the increase of average revenue per flight hour. The trend of the flight hours, productivity and revenue per flight hour were commented on in the previous paragraphs of the Report.

In particular, with regard to Mid Range the growth of flight hours derives from the increase of the fleet's productivity, as its availability was inferior with respect to the prior year.

With regard to Long Range, the increase of flight hours is primarily related to an increase of the availability of the total fleet, in that productivity remained substantially in line with the previous year, notwithstanding the "Tsunami" effect at the beginning of the year and "Cancun" in autumn, which certainly impacted Long Range activity.

In said context the cancellation should be noted, during the fiscal year, of a conspicuous part of the contractual activity with the Tour Operator Teorema. Said cancellations definitely had an impact on the year's results.

The increase of other revenue, amounting to 3,708 thousand Euro, was primarily due to revenue for the lease of the A319 CJ aircraft to the Saudi company NAS.

The significant increase of direct commercial costs is primarily related to the increase of scheduled activities and the development of alternative sales channels.

Revenue net of direct commercial costs grew by 41,485 thousand Euro (+17.8%), with a performance that was definitely significant.

## Costs

- **Jet fuel**

The results of the period were strongly conditioned by the trend of the cost of jet fuel, which was influenced by the quotations of raw materials, the Euro/Dollar exchange rate and the mix of the airports where the aircraft are refueled.

The cost of jet fuel in absolute values increased with respect to the prior year by more than 40% (equal to 20,974 thousand Euro). Said increase was also due, in addition to the price factor, also to the effect of quantity, tied to the growth of flight hours, and the diverse mix of the fleet and destinations.

The increase of the impact of the cost of jet fuel on total revue increased from 22.3% in 2004 to 26.8% in 2005.

- **Personnel**

Personnel costs decreased in terms of impact on revenue from sales and services (from 15.2% in 2004 to 14.4% in 2005). The growth of the absolute value principally reflects an increase of the average workforce, from 530 employees in 2004 to 589 in 2005. Personnel issues will be examined in a specific paragraph later in this Report.

- **Materials, maintenance services**

Maintenance costs decreased in absolute value with respect to the prior year. Said decrease, both in absolute value as well as with regard to percentage of revenue, can be attributed to the different expirations for the maintenance of the Airbus fleet, tied to the updating of the constructor's maintenance program (lengthening of the maintenance intervals), the in-house performance of maintenance activity that had previously been entrusted to third parties, and to the different mix of fleet (specifically the lower presence of MD80/82, which have average maintenance costs that exceed those of the Airbus fleet). Among the costs for materials the reduction of the impact of catering costs is noted, prevalently due to renegotiation of the supply contracts.

- **Other operating costs and wet leases**

In order to better comprehend the trend in absolute value and in terms of impact on total revenue of said costs, it is opportune to indicate the trend of wet lease costs with respect to other costs:

| | 2005 | % on revenues | 2004 | % on revenues | Variation | Variation % |
|---|---|---|---|---|---|---|
| Other operating costs | 71,465 | 26.3 | 67,102 | 28.9 | 4,363 | 6.5 |
| Wet Lease | 12,984 | 4.8 | 7,907 | 3.4 | 5,077 | 64.2 |
| | **84,449** | **31.1** | **75,009** | **32.3** | **9,440** | **12.6** |

The wet lease costs grew both in percentage as well as in absolute terms, following the greater use in 2005 of third party capacity, both in Long as well as Mid Range.

The other operative costs, even though increasing in absolute value subsequent to the growth of activity, demonstrate a diminution of their impact due to the substitution of the MD 80/82 fleet in 2004 and which is characterized by greater variable costs, as well as managerial and contractual interventions aimed at recovering efficiency.

- **Other commercial costs and corporate costs**

Their increase is tied to support of the Company's development initiatives, to dimensional growth and completion of the organization of management processes subsequent to the separation from Alitalia. As confirmation, their impact on revenue is aligned to that of the prior fiscal year.

## EBITDAR

The strong growth of revenues ensures an increase of the margin, amounting to 6,562 thousand Euro (+27.0%) with respect to 2004, although there are some growing cost factors, such as jet fuel and the use of capacity acquired in wet lease. The percentage impact of EBITDAR on revenues grew from 10.5% in 2004 to 11.4% in 2005.

- **Rentals**

The impact of the cost on revenues, amounting to 10.8%, grew strongly with respect to 2004. Said increase is due to the growth of the fleet, already analyzed above, the trend of interest rates (in that some contracts are indexed), as well as by the fact that in 2004 the MD 80/82 fleet was owned by the Company.

## EBITDA

The increase of lease costs is more than proportional to the growth of EBITDAR and results in a decrease of EBITDA.

The impact of EBITDA (amounting to 1,392 thousand Euro) on total revenues worsened, diminishing from 3.5% in 2004 to 0.5% in 2005.

- **Depreciation, amortization and provisions for risks and charges**

The othe provision reflects the impact of an increased allocation to the bad debt reserve, related to some specific positions as well as to the general deterioration of the capacity of the Tour Operators to comply with their obligations, subsequent to events that characterized the sector during the course of the fiscal year. In particular, commercial conflicts increased with the initiation of some lawsuits regarding the interpretation of contractual clauses.

## EBIT

The growth of depreciation, amortization and provisions further eroded the margins, resulting in an operative loss of 4,689 thousand Euro.

## Financial and extraordinary revenues and charges

Financial revenues indicate a positive result of 775 thousand Euro, primarily due to profits on exchange rates.

The result of the disinvestment of assets during the fiscal year refers almost exclusively to the gains realized by the sale of 8 MD80/82, in the context of the disinvestment of such fleet initiated during the second half of 2004.

Extraordinary net proceeds prevalently regard the release of accruals for invoices to be received prior to 2003, that were deemed to be excessive with regard to needs.

## Tax charges

The tax charges regard current taxes for 1,994 thousand Euro (2,018 thousand Euro in 2004), represented by the allocation for IRAP in the amount of 1,809 thousand Euro and IRES in the amount of 185 thousand Euro, as well as deferred tax assets in the amount of 493 thousand Euro (949 thousand Euro in 2004).

## 4. PERSONNEL

The Company's workforce as of 31 December 2005 is set forth in the following table, where the variation with respect to the same data of the previous year is also indicated. The decrease prevalently refers to cabin flight crew, due to a different trend of operative activity during the period.

| Categories | 2005 | 2004 | Variation |
|---|---|---|---|
| Managers | 8 | 8 | – |
| Office workers | 182 | 188 | (6) |
| **Total ground force** | **190** | **196** | **(6)** |
| Pilots | 125 | 124 | 1 |
| Flight Assistants | 306 | 328 | (22) |
| **Total flight force** | **431** | **452** | **(21)** |
| **Company's Total** | **621** | **648** | **(27)** |

The average workforce for the year 2005 is set forth in the following table, together with the comparison of the same information referred to the previous year.

| Categories | 2005 | 2004 | Variation |
|---|---|---|---|
| Managers | 7,85 | 6,60 | 1.25 |
| Office workers | 187,33 | 149,80 | 37.53 |
| **Total ground force** | **195,18** | **156,40** | **38.78** |
| Pilots | 128,24 | 120,08 | 8.16 |
| Flight Assistants | 266,06 | 254,00 | 12.06 |
| **Total flight force** | **394,30** | **374,08** | **20.22** |
| **Company's Total** | **589,48** | **530,48** | **59.00** |

The increase of the average remunerated workforce is due, with regard to the ground force, to completion of the process of autonomy and independence from Alitalia and, with regard to flight crew, to the increase of the flight activity during the course of the year with respect to the prior fiscal year. With regard to the latter case, however, it should be noted that the increase of staff was not done proportionally with respect to the increase of flight hours due to improvement of the average productivity of the aircraft.

During the course of 2005, the Company consolidated its organizational structure by means of reinforcing the units that support operative activities and the functions of the staff. In order to deal more efficiently with the activities related to the status of being a company listed on a Stock Exchange, new organizational positions were created and some of the Company's key procedures were reviewed. The Management Committee was created, in which the Chief Executive Officer and the principal managers participate on a permanent basis, in order to analyze the trend of management indicators, identify the necessary actions to realign the results achieved with respect to the anticipated objectives, approve the most significant business initiatives and analyze the trend of the projects contained in the Industrial Plan.

During the course of 2005, initiatives were taken for the specialist education and training of the flight crew necessary to maintain the high standard of professional qualification required by law and by corporate policy in this regard. Further, the pilot certification programs continued on all of the fleet's aircraft, in order to allow the use of the same resources both for the Long Range fleet as well as for the Mid Range fleet – the so-called "Mixed Fleet". Finally, the training programs for flight crew continued regarding aeronautical security and workplace safety.

With regard to the ground crew, specialized educational and training programs aimed at the personnel used to maintain the aircraft continued, in order to guarantee an ever increasing efficiency of the maintenance of the line and to achieve the necessary competence to be able to perform part of the basic maintenance. For personnel belonging to the operative areas, the safety courses required to be able to perform work within the airport areas were also performed, and training and informational programs for personnel continued on the specific risks of each category of work.

With regard to the contracts, during the course of 2005 the cabin crews' contracts were renewed, according to the same philosophy already utilized for the prior renewal of the pilots. The contractual increases only regard the variable part of the remuneration, thus tying eventual remunerative increases to greater flight activity. On 31/12/2005 the economic part of the contract for the ground crew expired, with regard to which the Company has already initiated consultations with the unions, and the contract with the pilots has also expired.

The relationship with the Unions was characterized by a constant confrontation, both with regard to issues inherent to the company's development, as well as the conditions of work and the search for flexible forms of employment. The level of conflict was very contained and the general climate positive and aimed at the maximum collaboration, even though at a very difficult time for air transportation.

Some initiatives were taken during the course of the year regarding internal communications aimed at involving all of the personnel in the Company's activities. In particular, this was done at the time of the Company's listing on the Stock Exchange, in order to illustrate the industrial objectives of the operation and provide all of the personnel with the necessary information on the Company's trend and its strategic objectives.

## 5. FINANCIAL OPERATIONS

The development of the Company's net financial position in fiscal year 2005 is represented as follows:

| *Amounts Euro/000* | **31.12.2005** | **30.09.2005** | **30.06.2005** | **31.12.2004** |
|---|---|---|---|---|
| Financial Receivables Classified as Finacial Fixed Assets | 18,906 | 18,489 | 18,462 | 10,452 |
| Financial Receivables Classified as Current Financial Assets | – | – | – | 4,302 |
| Cash and Cash Equivalent | 32,272 | 5,386 | 1,346 | 2,023 |
| Bank Overdrafts | (18,529) | (25,605) | (22,790) | (6,886) |
| Due to Factoring Companies | – | (5,860) | – | – |
| Due to Shareholders | (4,500) | – | – | – |
| Due to Lenders other than bank | (4,761) | (4,761) | (5,000) | (5,000) |
| **Net financial position** | **23,387** | **(12,351)** | **(7,982)** | **4,891** |

The Company's financial position grew, generated by funds received subsequent to the increase of capital due to the listing on the Stock Exchange.

On the basis of a comparison of the financial positions of June and September 2005 with those of the end of the year, net of the listing proceeds, there was a substantial improvement which took place during the second part of the year. Such improvement is due both to the pro soluto (without recourse) assignment of receivables regarding the Ministry of Defense as well as to a more careful management of the cycle of collections and payments.

As of 31 December 2005, the residual amount of the cash and cash equivalent deriving from the IPO amounted to 30,306 thousand Euro. In fact, the liquidity was partially utilized during the fiscal year for the payment of costs related to the listing and the first tranche of the payment plan for the purchase of the A350.

The reconciliation between the Company's net financial position and net cash and cash equivalent/net short term financial indebtedness is as follows:

| *Amounts in Euro/000* | **31.12.2005** | **31.12.2004** | **Variations** |
|---|---|---|---|
| **Net financial position** | **23,387** | **4,891** | **18,496** |
| Financial receivables classified as finacial fixed assets | (18,906) | (10,452) | (8,454) |
| Due to shareholders | 4,500 | – | 4,500 |
| Due to lenders other than bank | | | |
| Non current portion | 4,270 | 4,760 | (490) |
| **Cash and cash equivalent net/(net financial indebtedness)** | **13,251** | **(801)** | **14,052** |

## Analysis of financial receivables included in financial fixed assets or in current financial assets

- **Financial receivables included in financial fixed assets**

As of 31 December 2005, the financial receivables included among financial fixed assets, amounting to 18,906 thousand Euro, include a capitalization contract with a lump sum premium paid in advance in the amount of 10,841 thousand Euro (10,452 thousand Euro as of 31 December 2004). The capitalization contract was classified among financial fixed assets starting from January 2004, as it was restricted starting from such date to guarantee bank lines of credit granted by Banca Profilo.

Said financial receivables also include a restricted bank deposit care of Unicredit, amounting to 8,065 thousand Euro, pledged for the issue by the cited bank of a bank guarantee as security for the finance leasing stipulated in May 2005 with Locat S.p.A. for the purchase of the above mentioned A319 CJ/LR. The bank guarantee remains in duration until the thirtieth day subsequent to the expiration of the finance leasing, which has a ten year duration.

- **Financial receivables included among current financial assets**

During the month of February 2005 Eurofly sold its share of 40% of the capitalization contract with a lump sum premium paid in advance with La Venezia Assicurazione, policy no. 1.259.750, for a value aligned to that of the registered value as of 31 December 2004.

- **Cash and cash equivalent**

Cash and cash equivalent as of 31 December 2005 consisted of bank accounts which, as already noted, were positively affected by the liquidity generated by the listing operation and by the loan received from Spinnaker Luxembourg S.A. discussed in chapter 10 of this Report.

## Analysis of bank overdrafts due to shareholders for financing and to other lenders

The contractual relationships underlying the liabilities in object are analyzed in the explanatory notes.

## Cash flow statement

The analysis of cash flows is represented as follows:

| Cash Flow Statement | | 31.12.2005 | 31.12.2004 | Variations |
|---|---|---|---|---|
| **A.** | **INITIAL CASH AND CASH EQUIVALENT, NET** | **(801)** | **26,070** | **(26,871)** |
| **B.** | **CASH FLOWS (TO) / FROM OPERATIONS** | | | |
| | Profits (loss) for the year | (3,123) | 6,835 | (9,958) |
| | Depreciation and amortization | 2,821 | 2,368 | 453 |
| | Gains from fixed assets disposal | (1,581) | (1,264) | (317) |
| | Write-down of fixed assets | – | 227 | (227) |
| | Net change in working capital | (6,999) | 955 | (7,954) |
| | Net variations of staff leaving indemnity | 121 | 348 | (227) |
| | | **(8,760)** | **9,470** | **(18,230)** |
| **C.** | **CASH FLOWS FOR INVESTMENTS IN FIXED ASSETS** | | | |
| | Investments in fixed assets: | | | |
| | – Intangible | (8,263) | (2,723) | (5,540) |
| | – Tangible | (13,654) | (31,887) | 18,233 |
| | – Financial | (17,290) | (14,004) | (3,286) |
| | Proceed from the sale of fixed assets | 25,193 | 7,512 | 17,681 |
| | | **(14,014)** | **(41,102)** | **27,088** |
| **D.** | **CASH FLOWS FROM FINANCIAL ACTIVITY** | | | |
| | Loan underwriting | – | 4,761 | (4,761) |
| | Shareholder loans | 4,500 | – | 4,500 |
| | | **4,500** | **4,761** | **(261)** |
| **E.** | **CASH FLOWS FROM OPERATIONS ON EQUITY** | | | |
| | Increase of share capital | 5,900 | – | 5,900 |
| | Dividends | (5,000) | – | (5,000) |
| | Paid in capital | 31,426 | – | 31,426 |
| | | **32,326** | **–** | **32,326** |
| **F.** | **CASH FLOWS DURING THE PERIOD (B+C+D+E)** | **14,052** | **(26,871)** | **40,924** |
| **G.** | **FINAL CASH AND EQUIVALENT, NET (A+F)** | **13,251** | **(801)** | **14,052** |

The year 2005 was characterized by cash flow originating from the listing operation, compared with an absorption of financial resources by the operative management and investment activity.

The cash flow components for the period are analyzed below.

### • Cash flow to/from operations

Such flow was negative for the year 2005 in the amount of 8,760 thousand Euro, primarily due to the dynamics of variations of the net working capital and the result of the year. The variation is commented on hereinafter in the Report.

### • Cash flow resulting for investment activity

The additions made by the Company during the course of the fiscal year, net of disinvestments, absorbed financial resources in the amount of 14,014 thousand Euro.

The detail of the additions to tangible, intangible and financial fixed assets is presented further on in a specific chapter of the Report. It is noted that the significant amount of disinvestments, amounting to 25,193 thousand Euro, refers both to the completion of the sales program for the MD 80/82 fleet, initiated during the second half of 2004, as well as to the sale to Airbus of components related to the interiors of the A319 CJ/LR aircraft.

### • Cash flow from financial activity

The cash flow from financial activity in 2005 was positive in the amount of 4,500 thousand Euro due to the non-interest bearing shareholders' loan.

- **Cash flows from operations on equity**

The cash flow generated by the activity regarding equity was positive in the amount of 32,326 thousand Euro. On 29 June 2005, the Company paid out 5,000 thousand Euro as dividends to the shareholder Spinnaker Luxembourg S.A.

On 12 September 2005, as better explained above, the Company approved an increase of capital up to 7,000 thousand Euro to be reserved as support to the offer aimed at listing the Company's shares on the Telematic Stock Market organized and managed by Borsa Italiana S.p.A.

With regard to the approved increase of share capital, the amount of 5,900 thousand Euro was subscribed to. The operation generated a paid in capital infusion amounting to 31,426 thousand Euro.

## Reclassified balance sheet

| *Amounts in Euro/000* | **31.12.2005** | **31.12.2004** | **Variations** |
|---|---|---|---|
| Tangible fixed assets | 16,647 | 35,742 | (19,095) |
| Other intangibles | 11,257 | 5,043 | 6,213 |
| Other long term financial investments | 34,981 | 19,084 | 15,897 |
| Deferred Tax assets | 1,523 | 1,030 | 493 |
| **Total non current assets** | **64,407** | **60,899** | **3,508** |
| Stock | 2,140 | 1,781 | 359 |
| Trade receivables and other receivables | 45,978 | 54,978 | (9,000) |
| Other assets | 15,372 | 3,328 | 12,044 |
| Cash and cash equivalent | 32,272 | 2,023 | 30,249 |
| **Total current assets** | **95,762** | **62,110** | **33,652** |
| Non current assets to be divested | – | 4,302 | (4,302) |
| **Total assets** | **160,169** | **127,311** | **32,858** |
| Share capital | 12,965 | 6,667 | 6,298 |
| Reserves | 35,585 | 2,722 | 32,863 |
| Profits (losses) brought forward | (3,123) | 6,835 | (9,958) |
| **Total net equity** | **45,427** | **16,224** | **29,203** |
| Long term loans | 8,770 | 4,761 | 4,009 |
| Provisions for risk and charges non current | 3,049 | 2,927 | 121 |
| **Total non current liabilities** | **11,819** | **7,688** | **4,130** |
| Trade Receivables and other liabilities | 80,590 | 93,886 | (13,297) |
| Short term loans | 18,529 | 6,886 | 11,644 |
| Current portion of long term loans | 491 | 239 | 252 |
| Provisions for risk and charges current | 3,313 | 2,387 | 926 |
| **Total current liabilities** | **102,923** | **103,398** | **(475)** |
| **Total net equity and liabilities** | **160,169** | **127,311** | **32,858** |

The trend of the net working capital can be analyzed as follows:

| | **31.12.2005** | **31.12.2004** | **Variations** |
|---|---|---|---|
| Total current liabilities | (102,923) | (103,398) | 475 |
| (Bank overdarfts and current portion of long term loans) | 19,020 | 7,125 | 11,895 |
| **Liabilities** | **(83,903)** | **(96,273)** | **12,370** |
| Receivables / payables with Alitalia | – | 14,057 | (14,057) |
| **Adjusted liabilities** | **(83,903)** | **(82,216)** | **(1,687)** |
| Total current assets | 95,762 | 62,110 | 33,652 |
| Deferred tax assets | 1,523 | 1,031 | 492 |
| Reversal of deferred liability for “maxi rent” A319 | (9,266) | – | (9,266) |
| (Cash and cash equivalent) | (32,272) | (2,023) | (30,249) |
| **Assets** | **55,747** | **61,118** | **(5,371)** |
| Receivables / payables with Alitalia | – | (14,057) | 14,057 |
| **Adjusted assets** | **55,747** | **47,061** | **8,686** |
| **Net working capital** | **(28,156)** | **(35,155)** | **6,999** |

The Company's net working capital is structurally negative, in that the collection of receivables from tour operator generally occurs in advance with respect to the flight and in any event prior to the payment of trade payables to suppliers. Added to this is the progressive growth of scheduled flight activity, which contributes to such phenomenon. With respect to the prior year, the increase of the net working capital in 2005 results from an increase of positive items for 8,683 thousand Euro. In order to enhance the comparison, trade liabilities and receivables as of 31 December 2004 were adjusted by the amount of 14,057 thousand Euro, related to the offset (which occurred in June 2005) of receivables from Alitalia, in relation to the code share contract that expired in March 2005, with liabilities to suppliers for services that were invoiced by Alitalia. In particular, among the positive items affecting the increase of net working capital, the growth is noted of trade receivables amounting to 5,057 thousand Euro, net of the above offset.

## 6. RESEARCH AND DEVELOPMENT ACTIVITY

The Company did not perform research and development activity in a strict sense.

## 7. INVESTMENTS

The details of the value of intangible fixed assets, tangible fixed assets and long term financial assets as of 31 December 2005 are set forth below, whose movements are better detailed in the Notes to Financial Statements.

| *Amounts in Euro/000* | **31.12.2004** | **31.12.2005** |
|---|---|---|
| ***Intangible fixed assets*** | | |
| Start up costs | 1,913 | 6,099 |
| Research, development and advertising | 309 | 272 |
| Concessions, licenses, trademarks and similar | 544 | 1,358 |
| Fixed assets under construction | 396 | 32 |
| Other assets | 1,881 | 3,497 |
| **Total Intangible fixed assets** | **5,043** | **11,257** |
| ***Tangible fixed assets*** | | |
| Land and buildings | 7,858 | 8,112 |
| Plant and machinery | 14,421 | 2,155 |
| Industrial and commercial equipment | 429 | 474 |
| Other assets | 1,015 | 939 |
| Fixed assets under construction | 12,019 | 4,967 |
| **Total tangible fixed assets** | **35,742** | **16,647** |
| ***Financial fixed assets*** | | |
| Financial Receivables | 8,632 | 24,140 |
| Other securities | 10,452 | 10,841 |
| **Total Financial Fixed Assets** | **19,084** | **34,981** |

Additions to intangible fixed assets, which amount overall to 8,263 thousand Euro, include the costs sustained for the listing process, those relative to the launch of the projects for New York and Egypt, as well as for the training of the flight crew. It is also noted that the costs sustained included the implementation of new management software for maintenance activities and the spare parts warehouse, as well as the costs for purchasing the trademark. Investments for modifications made to leased aircraft are also included in this category.

Additions to tangible fixed assets amount to 13,654 thousand Euro and refer to the completion of the purchases related to the MD80 fleet, to work on the real property that houses the registered office, and the first tranche of the payments due for the purchase of the A350 aircraft. Greater details are provided in the Notes to Financial Statements.

With regard to financial fixed assets, the net variations amount to 15,897 thousand Euro, explained both by the payment of security deposits to lessors for the new aircraft acquired for the fleet or required contractually, as well as the above mentioned restricted deposit of 8,065 thousand Euro opened at Unicredit for the issue of the bank guarantee as security for the finance leasing for the new AIRBUS A319-CJ/LR. With regard to the security deposits, the operative rentals with CIT and ILFC for the two new A330 that will be delivered the end of 2006 and April 2007 resulted in payments amounting to a total of 5,472 thousand USD.

## 8. IMPACT OF THE ADOPTION OF INTERNATIONAL ACCOUNTING PRINCIPLES (IAS/IFRS)

The entry into effect of EC Community Regulation no. 1606/2002, issued by Parliament and the European Council in July 2002, requires companies with shares traded on stock exchanges of States that are members of the European Union to prepare their consolidated financial statements, starting from 2005, in accordance with what is provided by the accounting principles (IAS/IFRS) issued by the IASB (International Accounting Standards Board), if homologated in the Community and included in the Official Journal of the European Community (OJEC).

A company that does not prepare a consolidated financial statements is required to prepare the financial statements applying the international accounting principles (IAS/IFRS) starting from the preparation of the financial statements ended 31 December 2006.

The present paragraph provides:

- The description of the principal differences among the Italian principles used in preparing financial statements ended 31 December 2005 and the IAS/IFRS principles;
- The accounting applications that Eurofly will presumably use in the context of the accounting options provided by the IAS/IFRS principles;
- The optional exemptions provided by IFRS 1 and presumably used by Eurofly.

With the exception of the above considerations, Eurofly's transition to IAS/IFRS principles will, in substance, lead to a restatement – according to new classifications – of the asset and economic dimensions previously classified according to the provisions of Legislative Decree 127/1991.

The qualitative and quantitative analysis of the differences among the previous accounting principles and the IAS/IFRS principles will be subject to refinement; it should be noted, in fact, that a new version or interpretations of the IFRS might be issued prior to the publication of the Company's financial statements as of 31 December 2006, eventually with retroactive effects. Therefore, the recording and valuation of said dimensions could be subject to changes in view of the preparation of comparative data and the first complete financial statements prepared according to the IAS/IFRS homologated by the European Commission.

### *Principal differences between the Italian Principles previously used and the IAS/IFRS principles*

The IAS/IFRS principles do not differ from those used for the preparation of financial statements and infra-annual financial statements, prepared – until 31 December 2005 – using the Italian accounting principles, except for the following cases:

<u>Derivatives:</u> according to the Italian accounting principles the use of derivatives to manage the risk of fluctuations in the exchange rate were represented as items "outside of the financial statements", whereas according to IAS 39 they must be reflected in the financial statements and valued at their relative "fair value" even when they have the nature of hedging instruments. In particular, the outstanding derivatives that Eurofly has, intended to manage the risk of fluctuations in the Euro/USD exchange rate, are classified in the category "Cash flow hedge"; and thus:

- the profits and losses deriving from the adjustment to "fair value" of the derivatives (for the effective portion of the coverage relationship) will be registered directly as net assets;
- the remainder (ineffective) will be immediately registered in the income statement;
- the amounts recorded among net assets will be reported in the income statement of the period in which contracts and transactions that are expected manifest their effects to the income statement.

In particular, with regard to Accounting Principle no. 26 of Consiglio Nazionale dei Dottori Commercialisti e dei Ragionieri, IAS 39 – finding formalized policies and procedures for risk management in the strategy of hedging declared by the Directors, as well as mechanisms to measure the effectiveness of the risk management instrument and the parameters to identify the conditions for "hedging" – treats risk management operations for exchange rate risks as "trading operations", which according to the previous principles could have been treated as "hedged operations" on the sole basis of the generic intent to manage the risk of exchange rate fluctuations, as long as correlated due to expiration and amount to the notional underlying assets or liabilities to which they refer.

Intangible assets: on the basis of IAS 38, the following reclassifications and adjustments of intangible fixed assets will be made:

- improvements to aircraft in operative rental will be subject to reclassification among tangible fixed assets, without modification to the previous amortization criteria, deemed to be adequate also on the basis of the IAS/IFRS principles;
- research and development and advertising costs relative to the new development initiatives of multi-channel distribution and mandatory pilot training will be classified as "development costs" and depreciated for the previous periods of depreciation, deemed to be representative of the multi-year benefit brought to the Company's activities.
- The costs connected to the listing operation on the Stock Exchange, registered in the financial statements for the fiscal year ended 31 December 2005 among intangible fixed assets according to the previous accounting principles on the basis of criteria of capitalization, in accordance with the IAS/IFRS principles will be classified as reduction of net equity.

Assets in finance lease: on the basis of the provisions set forth in IAS 17, the A319 CJ/LR aircraft – available in accordance with a finance lease contract – will be registered among net assets in the item "Fleet" at the current value of the rent (inclusive of the initial lump sum rent registered in the item "Deferred liabilities" according to the previous accounting principles) regarding liability for the rents to be paid to the lessor. With regard to the rents registered according to the previous accounting principles on the basis of the accrual principle, the depreciation of the fleet and interest charges on the financial liability will be registered in the income statement.

The depreciation of the aircraft will be determined – on the basis of the components approach – depreciating the motors over six years and the components of the airframes over twenty-five years.

Provisions risks and charges: On the basis of IAS 37, the risks and charges provision will be registered at current value of the liabilities for which they were allocated in the financial statements, in the event the occurrence of the liability for which they were allocated is not foreseeable within the subsequent fiscal year. According to the previous principles, no discounting of the liability is reflected in the financial statements.

The treatment of employee's leaving indemnity (TFR): on the basis of IAS 19, TFR can be assimilated to a "defined benefit plan" and the liability will therefore be determined applying the actuary methodology called "Projected Unit Method" rather than on the basis of the provisions of art. 2120 of the Civil Code. The total of the rights matured during the course of the fiscal year will be registered in the income statement in the item "Costs of the work" whereas the figurative cost (of a financial nature) that the Company would sustain if it requested the market for a loan in an amount equal to TFR would be chargeable among financial revenue/costs. The actuarial profits and losses that reflect the effects deriving from modifications of the actuarial hypothesis underlying the calculation have been transferred to the income statement.

### *Accounting options that Eurofly will presumably use in the context of the accounting options provided by the IAS/IFRS principles.*

Coherently with the valuation criteria already adopted for the statements according to Italian accounting principles:

- Stock: the method presumably chosen for the configuration of costs is that of the average weighted cost.
- Valuation of tangible and intangible assets and real property investments: the Company will opt for the registration of said assets subsequent to the initial registration, the costs model ("Costs model"), net of depreciation and eventual losses of the derivative value.

### *Optional exemptions provided by IFRS1 that will presumably be used by Eurofly*

In the transition to IAS/IFRS principles, Eurofly will presumably use the following optional exemption provided by IFRS 1:

- Valuation of tangible and intangible fixed assets: Eurofly will take advantage of the right to utilize the book value of said assets, determined on the basis of the above accounting principles, as a substitute of the costs as of the date of 1° January 2005, in that it has the pre-requisites required by IFRS principle 1.

In view of completeness of the information provided, it should be noted that the depreciation of the building in Via Bugatti 15, which in 2004 was determined on the basis of a useful life of 33 years, was determined in fiscal year 2005 by separately identifying the components attributable to the value of the land with respect to that of the building and relative installations. Said components are therefore subject to differentiated depreciation and, in particular, the component relating to the land is not depreciated, whereas that relating to the building is depreciated over a period of 50 years and that relating to the installations over a period of 10 years.

## 9. TREASURY OWNED SHARES

During the course of the fiscal year there were no purchases or sales, either direct or indirect, of treasury owned shares.

## 10. RELATIONSHIPS WITH SUBSIDIARIES, AFFILIATES, PARENT COMPANIES AND COMPANIES SUBJECT TO THEIR CONTROL

As of 31 December 2005, the Company did not have subsidiaries or affiliates, however it is subject to the management and coordination of Spinnaker Luxembourg S.A. (previously Effe Luxembourg S.A).

On 21 November 2005, Spinnaker Luxembourg S.A resolved a non-interest bearing loan in the amount of 4,500 thousand Euro having a 24 month duration, reimbursable upon expiration, in order to meet financial needs that emerged during the month of October 2005, primarily tied to the down payments related to contracts having as their object the entry in the fleet of new A330 and A350 aircraft.

## 11. RELATIONSHIPS WITH RELATED PARTIES

Your Company does not have relationships with related parties.

## 12. RELATIONSHIPS WITH BANCA PROFILO

In consideration of the relationship with companies of the Banca Profilo Group or with its Directors, it has been deemed opportune to provide a summary of the amount and nature of the transactions performed.

It is noted that the Company is exclusively controlled, indirectly, by Profilo Spinnaker Investment Fund, a closed Luxembourg investment fund managed by the company Profilo Management Company S.A., in which Banca Profilo S.p.A. has a shareholding of approximately 9.9%.

Profilo Spinnaker Investment Fund – of which Banca Profilo directly holds a share of 57.9% - is in fact the owner of a shareholding of 99.68% of the share capital of Spinnaker Holding S.A., in turn the owner of a shareholding of 99.68% of the share capital of Spinnaker Luxembourg S.A. which, in turn, owns 44.71% of the Company's share capital.

| **Banca Profilo Group** | **31.12.2004** | **31.12.2005** |
|---|---|---|
| Trade receivables | 105,301 | 39,883 |
| Trade payables | (1,117,500) | (300,000) |
| Financial receivables | 29,325 | 30,306,078 |
| Financial payables | – | (10,102,756) |
| Bank loan | (5,000,000) | (4,761,128) |
| Other revenue | (92,100) | (71,482) |
| Costs for services | 1,117,500 | 992,029 |
| Financial charges | 888 | 392,059 |

Said transactions are performed on market conditions and are analyzed below.

- **Trade receivables/payables and costs for services, other revenues:**

The costs for services sustained by Eurofly refer both to specific consulting activity for the listing process as well as to the activity performed as Joint Global Coordinator, together with Centrobanca. The residual liability as of 31 December 2005 relative to said services amounted to 300 thousand Euro and was paid during the month of January 2006.

The other revenue and relative receivables claimed by Eurofly refer to the lease of a flight that was made. Said credit was paid during the course of the month of January 2006.

- **Financial receivables/payables and financial charges:**

Banca Profilo has financial receivables with regard to the Company. In particular, the credit line granted to the Company by Banca Profilo amounted to 15,000 thousand Euro as of 31 December 2005, inclusive of a cash credit line in the amount of 10,000 thousand Euro (revocable at any time, at an interest rate amounting to Euribor at 3 months increased by 1 percentage point and, on amounts beyond the credit line, amounting to Euribor at 3 months increased by 3.5 percentage points), guaranteed by a pledge on a capitalization contract with the lump sum premium paid in advance, already cited above. In addition there is a loan in the amount of 5,000 thousand Euro. It is noted that the credit line in the amount of 10,000 thousand Euro and the loan in the amount of 5,000 thousand Euro do not contain financial covenants or negative pledges clauses. As of 31 December 2005, the 10,000 thousand Euro credit line had been utilized to the extent of 10,102 thousand Euro. The greater value of the credit line granted was justified by the fact that the passive interest for the period had already been included at the end of the year.

The interest paid during the course of 2005 for use of the credit line amounted to 232 thousand Euro, whereas the interest charge for the outstanding loan amounted to 160 thousand Euro.

During the course of the month of February 2006, the Company decided to extinguish the cash credit line in that the differential between the cost of money for the use of the funds and the yield of the capitalization contract pledged for the credit line did not justify the operation. The Company therefore decided to realize the sale of the above contract. Banca Profilo was interested in sub-entering in it and liquidated the counter-value on market conditions. The funds received from the sale of the policy were utilized to extinguish the above 10,000 thousand Euro credit line.

Banca Profilo made a stand-by credit line available to the Company, with an 18 month minus one day expiration and reimbursable upon expiration in the amount of 2,500 thousand Euro, partially utilized during the first months of 2006. As of 23 March 2006 the line had not been utilized.

The funds generated by the listing were temporarily deposited in a special account with Banca Profilo, having a EONIA credit rate. As of 31 December 2005 the funds deposited amounted to 30,306 thousand Euro. During the course of the first trimester transfers of funds were made to the accounts the Company holds with other financial institutes in order to improve the management of its treasury. Overall, therefore, Eurofly's position towards Banca Profilo as of 31 December 2005 was positive in the amount of 20,203 thousand Euro, from which it is necessary to deduct the loan, whose residual liability amounted to 4,761 thousand Euro.

During the course of 2005 the Company purchased forward foreign exchange contracts from Banca Profilo to cover the fluctuation of the exchange rate risk for a total counter-value amounting to 30,500 thousand Euro. In view of completeness, it is also noted that as of 31 December 2005, the Company has forward foreign exchange contracts with Banca Profilo, again as coverage of the exchange rate risk, for a total counter-value of 10,500 thousand USD.

## 13. MAIN EVENTS THAT TOOK PLACE AFTER THE CLOSURE OF THE FISCAL YEAR AND OUTLOOK OF THE FOLLOWING YEAR

### 13.1 Development of relationships with Teorema Tour S.p.A.

#### *Negotiations for the renewal of the winter contracts and reconciliation*

As known, over the past years Teorema Tour represented Eurofly's principal client Tour Operator with an impact on total invoiced sales in 2005 amounting to approximately 21%.

The management strategy of commercial risk, enunciated in the context of the industrial plan, as well as the investment risk indicated in the listing Prospectus, is to reduce the impact of the Eurofly's first total business clients, and in this context the negotiation with Teorema for the renewal of the contracts for subsequent years had the objective of a progressive reduction of its volumes in exchange for the growth of the Company's overall invoiced sales.

More specifically, with regard to the Winter (end December '05 – April '06), during the course of the month of November 2005 a substantial programming agreement was expected corresponding to invoiced sales of more than 17 million Euro, of which almost 11 million Euro on Long Range. With regard to Mid Range they were prevalently rotations in V/P (empty / full) of an entire aircraft from Malpensa for the destinations Red Sea and the Canary Islands; for Long Range Teorema's undertaking regarded two rotations Santo Domingo in V/P for an entire aircraft and three rotations (Maldives, Cancun, Africa) with an allotment (3) amounting to approximately 50% of the aircraft's total capacity.

During the course of the negotiations for the renewal of the winter contract, the normal activities of reconciliation of the accounting items between Teorema and Eurofly were made. Such process required an accurate verification of a vast number of events and documents, which was prolonged throughout the month of December. Eurofly's net receivables with regard to Teorema amount to approximately 3 million Euro and 3 million US$.

Teorema Tour, by means of an unexpected letter received by Eurofly on 25 January 2006, contested the credit balance and requested acknowledgment of amounts for various reasons amounting to 1,2 million Euro.

The Company, deeming said letter to be purely instrumental and pretentious, used the assistance of a law firm, which examined the contracts and correspondence between the parties, confirming Eurofly's proper conduct in the contractual and accounting management of the relationship and, on 6 February 2006, contested Teorema's claims claiming, in addition to the payment of the above mentioned credit, also penalties matured subsequent to the cancellation of flights amounting to more than 14 million Euro. As further confirmation of its activity, Eurofly, together with the law firm that represents it on this occasion, requested a primary Auditing firm to verify the proper application of the contract with regard to invoicing and the determination of the credit positions, as well as the determination of the value of the penalties claimed to the opposing party. The analysis performed confirmed the correctness of the receivables registered in the financial statements and the accuracy of the determination of the penalties.

Subsequent to the above, after having explored the possibility of an amicable settlement of the relationship that by now had become confrontational without a positive result, and having verified the groundlessness and the lack of support for opposing party's arguments, the Company decided to initiate arbitration, as contractually provided, as well as take every opportune legal action aimed at the collection of its credit and award of the above penalties.

#### *The commercial strategies implemented*

The interruption of the relationship with Teorema while the "Winter" season had already initiated – it is noted that the sales in Empty/Full to Tour Operators are generally concluded a few months prior to the initiation of the season of reference – evidently induced Eurofly to implement urgent strategies and initiatives to recover invoiced sales that had been expected from Teorema.

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(3) Allotment: share of seats of the aircraft acquired "empty in exchange for full".

More specifically, the following lines of action were taken:

- Acceleration of the purchase process of new Tour Operator clients;
- Reinforcement of the relationships with Tour Operators in the high and mid range who are already clients, to increase the market share intercepted by Eurofly. Various important Tour Operators increased their contractual undertakings with Eurofly in a significant manner with respect to the previous year;
- Offer to Tour Operators of greater flexibility of access to Eurofly's capacity (purchase of seats upon request in the course of the season as well as in Empty/Full), by means of a more highly developed distributional instrumentation than with regard to the past (possibility for Tour Operator clients and those who are "authorized" to reserve seats via Internet and/or call center);
- Strong push of sales to the channels of travel agencies and direct channels to stimulate the "flight only" segment.

It is felt that the results achieved are more than satisfactory: revenues during the first two months of 2006 were aligned with the Plan's objectives. More specifically:

- Mid Range commercial performance exceeded the Plan's expectations with recoveries that, therefore, more than offset Teorema Tour's absence; in particular, the resumption of the destination Egypt, where Eurofly has competitive advantages, strongly contributed to such result;
- In Long Range, the two rotations planned by Teorema in Empty/Full for the entire aircraft were cancelled, whereas Eurofly decided to maintain the 3 rotations where Teorema had forecast significant - but not total - presence. Eurofly focused its sales efforts on these flights, fully using multi-channel distribution and, with the exception of the month of January, the recovery was significant, with the average Load Factor (sales in Empty/Full + sales by means of various channels "on request") amounting to 78% in the month of February 2006.

### *The summer contractual season*

In view of the lack of agreement with Teorema Tour, Eurofly:

- anticipated the programming of the Summer '06 season and the consequent sales campaign for the part regarding the Tour Operator channel;
- waived the hypothesis, provided by the Plan, of acquiring Mid Range aircraft in "wet lease" from third party operators. It decided that it is risky to acquire extra capacity for the six summer months given the termination of the activity with Teorema, the low margin expected for such operation, as well as the more stringent rules issued by ENAC for the use of the capacity of other airline carriers;
- move part of its Long Range capacity from traditional charter routes (exotic sea destinations) to new scheduled destinations.

The sales campaign to Tour Operator for the Summer season has substantially ended with good results in terms of the contracts concluded. Overall, the orders in its portfolio – adding those regarding the Winter season in course and those already signed for the Summer season – amount to a sum in excess of 195,000 thousand Euro.

Further, the sales of the activities on the New York band were initiated both from Italy as well as from the USA; while it is early to draw conclusions, as of today it is noted that the total reservations during 2005 have been exceeded (even though the capacity offered is greater and includes, as well as the high season, also periods of less favorable traffic).

### *Effects on 2006 deriving from the interruption of the relationship with Teorema Tour*

In synthesis, the effects of a commercial nature on the entire year 2006 of the interruption of the relationship with Teorema Tour are estimated as follows:

- In 2006 growth is forecast with respect to 2005, but at a lower rate than that set forth in the Plan; a significant part of the diminished revenue is attributable to the waiver of performing summer Mid Range operations by means of the use of third party aircraft in wet lease.
- The client portfolio and channels will be much more balanced, with a strong reduction of the impact of the first 5 clients on total invoiced sales and growth of the percentage of sales of scheduled flights or in any event in of a kind that is not Empty/Full (estimated to be at least 20% of the total).

– On the other hand, the activity will be subject to minor variations during the course of the season, with positive implications in terms of programming resources, because Teorema made frequent requests for modifications (cancellations, modifications of schedules and routing, additional flights) with respect to what was initially planned.

### 13.2 Incorporation of a newco to manage maintenance services in joint venture with a primary industrial partner

Eurofly and EADS Sogerma Services, world leader in the sector of maintenance and aircraft, are negotiating an agreement for the incorporation of a company, based at Malpensa, to offer maintenance services to all carriers present at the airport, among whom Eurofly and Livingston Aviation Group. Said project will allow the Company to increase the efficiency and quality of the maintenance services to its fleet, for lower costs.

### 13.3 Extension of the active leasing of the A319 CJ aircraft and relationships with the MiMa association

During the month of December 2005, a contractual extension was negotiated for the lease of the A319 CJ to the Saudi company NAS, as described above. Said contract shall terminate on 5 April 2006 and, after a brief phase of "repossession of the property" and maintenance, the aircraft will be used in the context of a lease that is being stipulated with the association Club Milano – Manhattan (MiMa) starting from 8 May 2006.

MiMa is a non-profit cultural association, whose primary objective is that of promoting exchanges and networking between the business community of Milan and New York; among the most significant services that the association intends to offer to its members is the possibility of using private flights of general aviation between Milan Linate and New York for a cost compatible with the segment "business travel".

In said context, Eurofly will act as the association's carrier of reference, making its 48 seat A319 CJ aircraft available.

The aircraft, in the context of its activity for MiMa, will be based in Milan Linate at the general aviation terminal of ATA. Although the prevalent activity will regard the Milan – New York route, it is not excluded that MiMa might request Eurofly to operate different routes on behalf of its members.

### 13.4 Request for tenders for the company unit Volare in temporary joint venture with Meridiana S.p.A.

On 17 March 2006, the Ministry of Productive Affairs determined the outcome of the request for tenders for the sale of the "Volare Group" company unit, with the award to Alitalia SpA.

On 20 March 2006, the Ministry of Productive Affairs notified Eurofly, as another interested party, of the initiation of an administrative proceeding to evaluate AirOne's request, presented on 17 March 2006, to view the administrative documentation relative to the request for tenders for the sale of Volare.

Since AirOne's request is in substance aimed at having a copy of all of the documentation related to the tender, including the offer made by Meridiana - Eurofly, the Company entrusted an attorney with filing an opposition so that information of a confidential and private nature contained in Meridiana – Eurofly's offer is not communicated to AirOne.

### 13.5 Restructuring of financial relationships

As specified in the above paragraphs, during the course of the month of February 2006, the Company decided to extinguish the cash credit line in the amount of 10,000 thousand Euro granted by Banca Profilo, in that the differential between the cost of the money for the use of the funds and the yield of the capitalization contract having a sole premium pledged for the credit line did not justify the operation that had previously been created.

Negotiations are in course with the various suppliers for the release of the security deposits currently existing, in particular those given to the owners of the aircraft in leasing. For such purpose, new credit lines were granted by some financial institutes for receivables upon request, with regard to which the release of 2,700 thousand Euro of security deposits is in a phase of completion.

A request was made to LOCAT S.p.A. for the extinction/reduction of the outstanding bank guarantee in the amount of 14,000 thousand Euro, as guarantee of the lease finance contract for the A319-CJ/LR aircraft, counter-guaranteed by a pledge on a credit line in the amount of 8,000 thousand Euro with Unicredit S.p.A.. The reduction of the guarantee will permit the diminution of the pledge with the contemporaneous release of financial resources for the Company.

### 13.6 Manifestation of interest for the purchase of Livingston Aviation Group

On 17 March 2006 the Company presented a manifestation of interest in purchasing the Livingston Aviation Group, a carrier that operates in the same market segment as Eurofly. On the same date the Board of Directors of I Viaggi del Ventaglio S.p.A. acknowledged such manifestation of interest and granted an exclusive twenty day option.

On 27 March the Company approved a preliminary "term sheet" for the signing of a letter of intent in view of the stipulation of a sales contract. Such operation might result in an integration between the two carriers, with significant potential to create value.

### 13.7 Development initiatives in Egypt

Eurofly wishes to consolidate its leadership in Egypt, accept some commercial opportunities, including for new connections to the Red Sea from other European countries, and improve its efficiency, both with regard to the operations of the fleet, as well as the cost structure.

After having postponed hypothesis of local cooperation, not possible for the time being or in any event complex, the Company looked with interest to the new Egyptian law in this sector, which allows the creation of a charter carrier with foreign capital, as well as the local political climate, favorable to such initiative.

A preliminary feasibility and convenience study was therefore undertaken, whose results will be submitted to the Company's Board of Directors in order to initiate, in the case of approval, the procedure for the creation of an Egyptian company controlled by Eurofly.

The times for said procedure should be between 8 and 12 months, in order to allow the new carrier to become operative, in the best of cases, for the winter 2006/2007 season. The preliminary analysis will be completed within 4/6 weeks with the support of local consultants and the supervision of PWC Advisory Services.

### 13.8 Legislative Decree 69/2006

With regard to consumer protection, the Italian legislator issued Legislative Decree no. 69 of 27 January 2006, having as its object "Sanctions for the violation of (EC) Regulation no. 261/2004, which creates common rules in matters of compensation and assistance to passengers in the case of refused boarding, flight cancellation or prolonged delay".

Such measure establishes that the air carrier, in the event it breaches the provisions set forth in EC Regulation no. 261/2004, can be punished by means of administrative sanctions of various amounts.

It therefore reinforces, with respect to the previous situation, all of the necessary measures so that passenger rights are respected and guaranteed by the carrier.

ENAC is appointed as the organism responsible for the application of the Regulation and the eventual issuance of administrative sanctions.

Some verifications are underway – through Assaereo – to evaluate the manner by which ENAC intends to proceed with the application of the above Regulation.

### 13.9 Regulation of the time limits of flights and service

By means of a sentence published on 2 March 2006, the TAR of Lazio, with a final decision on the merits, partially granted the appeal filed by Eurofly (and others), annulling the Regulation, however limited to the part that regulates the length of flights and services for Flight Assistants, for whom, therefore, the pre-existing normative will remain in effect.

### 13.10 The operational outlook

The trend of the first two months of 2006, which has already felt the effect of the commercial actions aimed at reducing the impact of the termination of the relationship with Teorema Tour, demonstrates how the final flight hours and total revenues are aligned with what was originally forecast. On the other hand, the external variables represented by the cost of jet fuel and interest rates present negative trends with respect to expectations. The reasonable expectation that the trend of the above external variables will be confirmed during the entire current fiscal year leads to the belief that, although in the presence of the positive effects on profitability determined by the commercial actions described above, operative profitability and, consequently, the year result, might be less than the original forecast.

The comments on the management trend, further, must be revised further in the event the purchase of Livingston Aviation Group is finalized.

### Appropriation of fiscal year results and consequent resolutions

Dear Shareholders,

Eurofly S.p.A.'s financial statements for fiscal year 2005 ends with a loss of 3,123,097 Euro and a net equity of 45,427,110 Euro.

We propose that the draft financial statements for the fiscal year ended 31 December 2005 be submitted to the Ordinary Shareholders' Meeting with the following proposal:

– approval of Eurofly S.p.A.'s financial statements as of 31 December 2005, which indicates a loss of 3,123,097 Euro and a net equity of 45,427,110 Euro and defer coverage of the loss to the next fiscal year.

Milan, 27 March 2006

On behalf of the Board of Directors

The President
**Giuseppe Bonomi**

The Managing Director
**Augusto Angioletti**

# THE FINANCIAL STATEMENTS AS OF 31 DECEMBER 2005

## BALANCE SHEET

| ASSETS<br>*Amounts in euro* | 31.12.2005 | 31.12.2004 |
|---|---|---|
| **A) CAPITAL DUE FROM SHAREHOLDERS** | | |
| **Total due from shareholders** | **–** | **–** |
| | | |
| **B) FIXED ASSETS** | | |
| **I. *INTANGIBLE FIXED ASSETS*** | | |
| 1. Start up costs | 6,098,776 | 1,913,231 |
| 2. Research, development and advertising costs | 271,794 | 309,107 |
| 4. Concessions, licenses, trademarks and similar rights | 1,357,931 | 544,155 |
| 6. Fixed assets under construction | 31,500 | 395,591 |
| 7. Other assets | 3,496,710 | 1,881,340 |
| | 11,256,710 | 5,043,424 |
| **II. *TANGIBLE FIXED ASSETS*** | | |
| 1. Land and buildings | 8,111,984 | 7,856,768 |
| 2. Plant and machinery | 2,154,620 | 14,420,929 |
| 3. Industrial and commercial equipment | 474,201 | 428,369 |
| 4. Other assets | 938,695 | 1,016,369 |
| 5. Fixed assets under construction | 4,967,436 | 12,019,339 |
| | 16,646,935 | 35,741,774 |
| **III. *FINANCIAL FIXED ASSETS*** | | |
| 2. Financial Receivables | | |
| a. receivables over 12 months | 22,469,123 | 8,631,195 |
| b. receivables within 12 months | 1,670,939 | – |
| 3. Other securities | 10,840,810 | 10,452,502 |
| | 34,980,872 | 19,083,697 |
| **Total fixed assets** | **62,884,518** | **59,868,896** |
| | | |
| **C) CURRENT ASSETS** | | |
| **I. *STOCK*** | | |
| 1. Raw materials, subsidiary materials and consumables | 2,104,221 | 1,781,275 |
| 5. Payments on account | 35,905 | – |
| | 2,140,126 | 1,781,275 |
| **II. *RECEIVABLES*** | | |
| 1. from customers | 37,961,098 | 49,933,059 |
| 4-bis Receivables from tax Authorities | 2,810,430 | 2,117,003 |
| 4-ter Deferred tax assets | 1,522,591 | 1,029,541 |
| 5. Other receivables | 5,206,024 | 2,929,066 |
| | 47,500,143 | 56,008,669 |
| **III. *CURRENT FINANICAL ASSETS*** | | |
| 6. Other securities | – | 4,301,575 |
| **IV. *AVAILABLE LIQUIDITY*** | | |
| 1. Bank and post-office deposits | 32,254,618 | 1,995,785 |
| 3. Cash-in-hand and cash equivalents | 17,184 | 27,253 |
| | 32,271,802 | 2,023,038 |
| **Total Current Assets** | **81,912,071** | **64,114,557** |
| | | |
| **D) ACCRUED INCOME AND DEFERRED EXPENSES** | | |
| b. Prepayments | 15,372,096 | 3,327,640 |
| **Total Prepayments-Accruals Income** | **15,372,096** | **3,327,640** |
| **TOTAL ASSETS** | **160,168,685** | **127,311,093** |

*Translated from the original version in Italian*

| LIABILITIES<br>*Amounts in euro* | 31.12.2005 | 31.12.2004 |
|---|---|---|
| **A) NET EQUITY** | | |
| I. Share capital | 12,965,302 | 6,666,922 |
| II. Share premium reserve | 31,425,895 | – |
| III. Revaluation reserve | – | – |
| IV. Legal reserve | 478,258 | 136,497 |
| V. Reserve for treasury stock | – | – |
| VI. Statutory reserve | 3,680,752 | 2,585,681 |
| VII. Other reserves, separately indicated | – | – |
| VIII. Profits (losses) brought forward | – | – |
| IX. Result for the fiscal year | | |
| Profits (losses) for the fiscal year | (3,123,097) | 6,835,212 |
| **Total Net Equity** | **45,427,110** | **16,224,312** |
| **B) PROVISION FOR RISKS AND CHARGES** | | |
| 3. Other provisions | 3,312,692 | 2,387,372 |
| **Total provision for risks and charges** | **3,312,692** | **2,387,372** |
| **C) STAFF LEAVING INDEMNITY** | **3,048,694** | **2,927,341** |
| **Total staff leaving indemnity** | **3,048,694** | **2,927,341** |
| **D) DEBTS** | | |
| 3. Due to shareholders | 4,500,000 | – |
| 4. Due to banks | 18,529,399 | 6,885,870 |
| 5. Debts to lenders other than banks | | |
| within 12 months | 491,108 | 238,872 |
| over 12 months | 4,270,020 | 4,761,128 |
| 6. Payment received on account | 2,017,242 | 2,277,336 |
| 7. Due to suppliers | 52,826,110 | 64,199,960 |
| 12. Due to Tax Authorities | 3,009,295 | 2,565,550 |
| 13. Due to social security and insurance | 1,615,007 | 1,041,468 |
| 14. Other debts | 4,862,825 | 3,139,301 |
| **Total debts** | **92,121,007** | **85,109,485** |
| **E) ACCRUED EXPENSES AND DEFERRED INCOME** | | |
| b. Other accruals and deferred income | 16,259,182 | 20,662,583 |
| **Total accruals and deferred income** | **16,259,182** | **20,662,583** |
| **Total liabilities** | **160,168,685** | **127,311,093** |

| MEMORANDUM ACCOUNTS | | |
|---|---|---|
| **4) COMMITTMENTS AND GUARANTEES** | **199,920,407** | **94,974,656** |

*Translated from the original version in Italian*

# INCOME STATEMENT

| *Amounts in Euro* | | **31.12.2005** | | **31.12.2004** |
|---|---|---|---|---|
| **A) VALUE OF PRODUCTION** | | | | |
| 1. Revenue from sales and services | | 271,474,519 | | 245,340,085 |
| 5. Other revenues and income | | 6,511,822 | | 2,037,041 |
| **Total** | | **277,986,340** | | **247,377,126** |
| **B) COSTS OF PRODUCTION** | | | | |
| 6. for raw materials, subsidiary materials, consumables and goods | | 83,375,971 | | 62,430,174 |
| 7. for services | | 108,932,227 | | 105,310,864 |
| 8. for use of property of third parties | | 44,736,413 | | 36,556,767 |
| 9. for personnel | | 39,142,684 | | 35,195,415 |
| a) wages and salaries | *30,750,202* | | *28,018,094* | |
| b) social charges | *6,545,167* | | *5,549,098* | |
| c) staff leaving indemnity | *1,404,168* | | *1,243,774* | |
| e) other charges | *443,148* | | *384,449* | |
| 10. Depreciation and devaluation | | 4,821,447 | | 2,759,639 |
| a) depreciation of intagible fixed assets | *2,049,605* | | *1,526,777* | |
| b) depreciation of tagible fixed assets | *771,842* | | *841,665* | |
| c) write-down of tangible and intagible fixed assets | – | | *227,168* | |
| d) bad debt reserve accrual | *2,000,000* | | *164,028* | |
| 11. Variations in stocks of raw materials, subsidiary materials, consumables and goods | | (322,946) | | (773,912) |
| 13. Other provisions | | 1,259,427 | | 1,304,808 |
| 14. Other charges | | 730,123 | | 557,599 |
| **Totale Costs** | | **282,675,345** | | **243,341,353** |
| **Difference** | | **(4,689,005)** | | **4,035,773** |
| **C) INCOME AND FINANCIAL CHARGES** | | | | |
| 16. Other Financial Income | | | | |
| b) Securities classified under financial fixed asstets | | 399,335 | | 452,452 |
| c) Securities classified under current fixed asstes | | – | | 199,693 |
| d) Income other than described in the preceding subparagraph | | 161,725 | | 108,505 |
| 17. Interest payable and other financial charges | | | | |
| d) Other interest and commission | | (1,651,930) | | (120,287) |
| 17. Exchange differences | | 1,866,211 | | (268,927) |
| **Total** | | **775,340** | | **371,437** |
| **E) EXTRAORDINARY INCOME AND CHARGES** | | | | |
| 20. Income | | | | |
| a) Gains from disposals of fixed assets | | 1,595,486 | | – |
| c) Other | | 775,654 | | 4,646,347 |
| | | 2,371,140 | | 4,646,347 |
| 21. Costs | | | | |
| a) Losses from disposals of fixed assets | | (14,609) | | – |
| c) Other | | (64,553) | | (1,149,560) |
| | | (79,162) | | (1,149,560) |
| **Total** | | **2,291,978** | | **3,496,787** |
| **Results before taxes** | | **(1,621,686)** | | **7,903,996** |
| 22. a) Current taxes | | (1,994,461) | | (2,018,317) |
| b) Deferred taxes | | 493,050 | | 949,533 |
| **26. Profit (Loss) of the year** | | **(3,123,097)** | | **6,835,212** |

*Translated from the original version in Italian*


# NOTES TO THE FINANCIAL STATEMENTS

## NOTES TO THE FINANCIAL STATEMENTS AS OF 31 DECEMBER 2005

### EXPLANATION ADDED FOR ENGLISH TRANSLATION PURPOSES

The Financial statements as of December 31, 2005 have been translated into English from the original version in Italian. They have been prepared in accordance with the accounting principles established by the Italian law related to quarterly financial accounts, which may not conform with accounting principles in other countries.

### PREMISES

The financial statements as of 31 December 2005, consisting of the statement of balance sheet, income statement and explanatory notes, was prepared in compliance with the requirements of the Civil Code, which implemented the provisions introduced by Legislative Decree 127/91, and the subsequent modifications and/or integrations interpreted and disclosed by the Italian Accounting Organism. Further, all of the complementary information was prepared that was considered to be necessary in order to provide a broader informational picture of the Company's economic-financial position, in particular, a cash flow statement was prepared.

The information relative to the Company's activity, to the significant facts that took place after the end of the fiscal year, as well as operations with affiliates and with significant other parties are discussed in the Management Report of Operations.

### DIRECTION AND COORDINATION ACTIVITY

As of 31 December 2005, the majority shareholder was Spinnaker Luxembourg S.A. (previously Effe Luxembourg S.A.), having a registered office in Luxembourg, via Cote d'Eich no. 73, with a share capital of 31,000.00 entirely paid-in, and a shareholding of 44.17%. With reference to the information set forth in art. 2497-bis, paragraph 4 of the Civil Code (direction and coordination activity), it should be noted that the Company, during the fiscal year 2005 and untill the date of admission to the stock exchange, is subject to direction and coordination activity by said entity.

The main items of the financial statements ended 31 December 2004 of the Company Spinnaker Luxembourg S.A. (previously Effe Luxembourg S.A.) are represented as follows:

| **Balance sheet** | |
|---|---|
| **Assets** | |
| Intangible fixed assets | 4,085 |
| Financial fixed assets | 13,785,011 |
| Current assets | 85,655 |
| Fiscal year loss | 16,065 |
| **Total assets** | **13,890,816** |
| **Liabilities** | |
| Share Capital and Reserves | 24,770 |
| Long term liabilities | 13,760,000 |
| Short term liabilities | 106,046 |
| **Total Liabilities** | **13,890,816** |
| **Income statement** | |
| Earned interest | 1,786 |
| General Expenses and other costs | (17,851) |
| **Fiscal year loss** | **(16,065)** |

### PREPARATION CRITERIA

The financial statements corresponds to the results of the accounting records regularly maintained and has been prepared in compliance with the laws set forth in articles 2423 et seq. of the Civil Code.

In particular, the general clauses regarding preparation of the financial statements (art. 2423 Civil Code), the principles for its preparation (art. 2423 bis Civil Code) and the valuation criteria established for its individual items (art. 2426 Civil Code), integrated by the Principi Contabili dei Dottori Commercialisti e dei Ragionieri, were all strictly complied with.

The formal structures, developed in articles 2424 and 2425 of the Civil Code regarding the schemes of balance sheet and income statements, were complied with, both with reference to the order in which each group of items is listed, as well as with reference to the sequence of the individual items that make up such groups.

The variations occurred to assets and liabilities balances are explained when significant.

With particular regard to provision for risks and charges, the provision and utilizations occurred during the year are indicated.

## VALUATION CRITERIA

The valuation criteria used for the preparation of the financial statements as of 31 December 2005 have remained unchanged with respect to those used for the comparative financial statements as of 31 December 2004.

During the course of the period no exceptional cases were verified that required the use of the derogations set forth in art. 2423 Civil Code, 4° paragraph.

The valuation of the financial statements items was done with reference to the general principles of prudence and competence and from the perspective of the continuation of the Company's activity.

The risks and losses of competence to the period were considered, even if they became known after its closure.

The criteria adopted and the contents of the principal financial statements items can be summarized as follows:

### a) **Intangible fixed assets**

They represent goods, costs and expenses that have a multi-year utility and are registered – upon the consent of the Board of Statutory Auditors when required – at cost, and which were not subject to legally required or voluntary monetary revaluations, inclusive of directly chargeable accessory costs.

Said costs are listed among balance sheet assets net of amortization accumulated during prior fiscal years, starting from the time they were available for use. The relative amortization periods were determined in relation to their residual possibility of use. In particular:

- start-up costs were amortized over a period of five years;
- research costs were amortized over a period of three years, whereas those of advertising – capitalized limited to those costs related to the phases of the launch of new products/services from which future long-lasting effects are expected – for a period of five years;
- concessions, licenses, trademarks and similar rights are amortized over a period of five years;
- other intangible fixed assets have been amortized as follows:
  - the costs related to the preparation of Eurofly's web site have been amortized over five years;
  - the modifications and standardizations made on the aircraft in the fleet have been amortized on the basis of the residual duration of the operating lease contracts.

In the event that, independently of the amortization already registered, there is a lasting loss of value, the fixed asset will be correspondingly devaluated; if there are no longer any reasons for the devaluation in subsequent periods, the original value will be restored, in the limit of the accrued amortization.

### b) **Tangible fixed assets**

These assets are registered at purchase or manufacturing cost, inclusive of eventual accessory costs. Said assets are listed among the balance sheet assets net of the accumulated depreciation related to them. The cost was not subject to either legally required or voluntary monetary revaluations.

Ordinary maintenance and repair costs are charged to the income statement in the fiscal year in which they were sustained. Those that have an added value nature, in that they prolong the useful life of the tangible fixed assets or result in a significant increase of capacity, are registered as an increase of the same.

In the case in which, independently of the depreciation that has already been registered, there is a lasting loss of value, the fixed asset will be correspondingly devalued; if the reasons no longer exist for the devaluation in subsequent periods, the original value is restored, in the limit of the accrued depreciation.

Depreciation of homogeneous classes of tangible fixed assets have been calculated at constant rates, starting from the fiscal year in which they were available for use, on the basis of the residual possibilities of use of the assets to which they refer. In particular, the following rates, reduced by half for the fiscal year investments, area reasonably represented by the useful life of the relative assets:

| | | |
|---|---|---|
| – land | not depreciated | |
| – buildings, | 50 years | 2% |
| – lightweight constructions, | 10 years | 10% |
| – plant, | 10 years | 10% |
| – equipment, | 7 years | 14% |
| – rolling components, | 12 years | 8,33% |
| – computers, | 5 years | 20% |
| – office furnishings and machinery, | 8.3 years | 12% |
| – means of internal transport, | 5 years | 20% |
| – motor vehicles, | 4 years | 25% |
| – communication systems, | 5 years | 20% |

The MD80/82 aircraft in the fleet at the end of fiscal year 2004 were depreciated on the basis of the flight hours during the period in relation to the days of possession, determined with reference to a useful life of approximately 8 years.

The depreciation rates for the assets were not modified with the following exceptions:

- the modification – made in fiscal year 2004 – of the depreciation rate of rolling components, determined to be 8.33%, equal to a period of 12 years, rather than on the basis of the duration of the leases for the aircraft, which are for 5 years, in that it was found that the useful life of the rolling components is greater than the contractual duration of the leases of the aircraft themselves.
- the modification – made during the first six months of 2005 – of the depreciation rate for the property in Via Bugatti 15, for which different depreciation rates were used for its components of land, building and installations, as specified above. Said building, whose delivery took place mid-December 2004, had been depreciated in the financial statements as of 31 December 2004, using the criterion of daily pro-rata temporis of the annual rate of 3.33%, in order to consider the period that said property was effectively availability. Due to the effect of the modification of the criteria of estimating the useful life of the property, the depreciation in 2005 was less by 36,924 Euro with respect to that determined using the previous depreciation criteria.

## c) **Financial fixed assets**

Financial fixed assets relative to capitalization contracts are valued at nominal value and increased by matured interest; said value is not lower than the value represented by the insured initial capital, increased by the minimum guaranteed yield. Financial fixed assets related to security deposits for obligations have been registered at nominal value, coinciding with the presumed net realizable value.

Receivables for security deposits for utilities have been valued at nominal value, coinciding with that of net realizable value, whereas receivables for deposits for third party contractual commitments are registered at nominal value and eventually adjusted in order to adapt the amount towards the presumed recovery value.

## d) **Stock**

Stock, consisting of supplies of technical materials, catering materials and tickets for scheduled flights have been registered at their specific purchase cost, or the realizable value inferable from the market trend, if lower. Said lower value is not maintained in subsequent if the reasons for it are no longer applying and the restoration of values is made, if the pre-requisites are present, within the limits of the original purchase cost.

## e) Receivables

Receivables are disclosed at presumed net realizable value, adjusting their nominal value by means of the special devaluation reserve determined on the basis of the estimate of the risk of irrecoverableness.

## f) Financial current assets

The financial receivables for capitalization contracts have been registered at a value that is at least that of the initial insured capital, increased by the minimum guaranteed yield.

## g) Cash and cash equivalent

This is listed at its nominal value.

## h) Accruals and prepaid/deferred expenses and incomes

The portion of revenue and costs, common to two or more periods, have been registered in said items, in accordance with the accrual method.

## i) Provisions for risks and charges

The provision for risks and charges include expenses and costs of a specific nature, that are certain or likely, whose precise amount or date of occurrence had not been determined as of the close of the fiscal year.

The provision reflects the best possible estimate on the basis of available elements. The risks for which the manifestation of a liability is only possible are indicated in the notes to the financial statements, without making an appropriation to a risk fund. Remote risks are not considered.

## l) Items in foreign currency or subject to the “exchange rate risk”

Receivables and payables originally expressed in foreign currency of countries not belonging to the area of the Euro have been converted in Euro at the average exchange of the month prior to that in which the transaction occurred, until August 2004, subsequently at the exchange rate of the date of the relative operations. The differences in exchange rate realized at the time of collection of receivables and payment of payables in foreign currency are registered in the income statement. Fixed assets in foreign currency, with the exception of those of a monetary nature, have been registered at the exchange rate existing at the time of their purchase or the lower rate as of the date of closure of the fiscal year if the reduction is deemed to be lasting.

Assets and liabilities originally in foreign currency of countries not belonging to the area of the Euro still in existence at the end of the period, with the exception of fixed assets, have been aligned – starting from the 2004 financial statements – at the exchange rate as of the date of closure of the period and the relative gains and losses on the exchange rates have been registered in the income statement and the net gain, where existing, has been designated to a special equity reserve that will not be distributable until realization.

## m) Staff leaving indemnity

The staff leaving indemnity is adequate for the wages and salaries matured at the end of the period according to provisions of law and contracts in effect, net of advance payments made to employees. Such liability is subject to revaluation by means of indexes.

## n) Accounts payable

Account payables have been registered at their nominal value. Said item includes payables that are certain and specific both with regard to their amount as well as the date of their occurrence.

o) **Costs and revenues**

These are listed in the financial statements in compliance with the principles of prudence and accrual basis, net of the relative discounts and allowances. Revenue is recognized at the time of the performance of the service, which normally coincides with the transport of passengers. The commissions paid to agencies for the sale of airline tickets are charged to the income statement at the time of the recognition of the related revenue.

Contributions are credited to the income statement on the basis of the charge of the costs and expenses which they refer to, on the accrual basis principle, when they are certain and liquid.

p) **Income tax**

The current income taxes are determined on the basis of a realistic forecast of the taxes to be paid, as application of outstanding tax laws, and are recorded in the balance sheet, net of advance payments made and withholdings.

Deferred tax assets and liabilities have also been accounted on the temporary differences between the fiscal year result and the fiscal taxable amount. In particular, as application of accounting principle no. 25 of Registered Accountants and Bookkeepers, the deferred tax assets - with regard to fiscal year losses carried forward and the temporary differences between taxable income and the economic result, are considered until they match eventual deferred taxes and, with regard to the exceeding part, are registered within the limits in which the basis exists for the reasonable certainty that they will be recovered.

q) **Memorandum accounts**

These indicate the amount of the guarantees, commitments and risks at their nominal value or value of the obligations undertaken, existing as of the end of the fiscal year.

They are valued as follows:

1) the commitments related to the assets used in operative leasing are registered on the basis of the contracts existing at the end of the fiscal year for the amount of the residual rents as of the date of the financial statements;
2) the commitments related to the assets available in finance lease are registered for an amount equal to the nominal amount of the rents to be paid, increased by the redemption value of the asset;
3) third party property held by the Company is registered at current value;
4) guarantees given are registered at the nominal value of the guarantees issued to third parties;
5) purchases of forward foreign currency contracts to cover the generic risk of exchange rates are registered in the memorandum accounts at the time they are stipulated and for the nominal amount of the contract. The costs deriving from their valuation at “fair value” are registered in the income statement in that said instruments are not considered, for valuation purposes, as being hedged but as trading. The proceeds are, for prudence, deferred until realization.

## OTHER INFORMATION

### Comparison of the financial statements

The financial statements as of 31 December 2004 has been reclassified in order to allow comparison with that of the fiscal year ended as of 31 December 2005:

- Reclassification of receivables for deferred tax assets existing as of 31 December 2004 for an amount of 80 thousand Euro from the item “Receivables from tax Authorities” to the item “Deferred tax assets”.
- Reclassification of cost debited to the lessor for the recovery of maintenance costs on engines for an amount of 4,843 thousand Euro, from the item “Other revenue and income”, deducted from the item “Costs for services- Maintenance and reconditioning of fleet”.
- Reclassification of the cost relative to the allocation to the devaluation fund of penalties that arose during the year, from the item of the income statement account “Depreciation and devaluation - bad debt reserve accrual” to the item “Other revenues and income”, amounting to 245 thousand Euro.
- Reclassification of the cost related to the purchase of the technical manuals on board in the amount of 851 thousand Euro from the item “Other charges” to the item “Costs for raw materials, subsidiary materials, consumables and goods”.

Said reclassifications have not led to variations to net equity and the economic result indicated in the financial statements approved by the Board of Directors.

### Explanation of the information

The amounts indicated in the present note to the financial statements, unless otherwise specified, are in thousands of Euro.

## ITEMS OF THE BALANCE SHEET

An analysis of the contents and variations of the balance sheet items and memorandum accounts refers to the final items contained in the financial statements as of 31 December 2005. The comparison of the asset items was made with the financial statements of the fiscal year closed as of 31 December 2004.

## ASSETS

## A) RECEIVABLES FROM SHAREHOLDERS FOR PAYMENTS DUE

No amount is due from the shareholders as of 31 December 2005 and 2004 for payments to be made to the share capital account.

## B) FIXED ASSETS

I) **"Intangible fixed assets"** amount to 11,257 thousand Euro and register a net increase with respect to 31 December 2004 of 6,213 thousand Euro; the chages are detailed in the table in Annex 1.

As of 31 December 2005, an analysis by their nature is as follows:

– "start-up costs" consist of the costs sustained by the Company for its listing on the Stock Exchange (3,641 thousand Euro), training costs for pilots of the Airbus fleet and personnel of the technical-maintenance area (1,287 thousand Euro), costs sustained for the start up of the route to New York and for the opening of a technical unit at the airport of Sharm El Sheikh (899 thousand Euro), the costs sustained to outfit the offices rented at Malpensa (125 thousand Euro), as well as the costs to implement the e-Fly project for the sales of scheduled flights by means of the Internet (147 thousand Euro);
– "research, development and advertising costs" consist of the costs sustained for the research for the Eurofly logo (1 thousand Euro) and by the advertising costs for the launch of the new e-Fly project for the sales of scheduled flights using the Internet (271 thousand Euro);
– "concessions, licenses, trademarks and similar rights" substantially refer to the purchase of software (861 thousand Euro) and the Eurofly trademark (497 thousand Euro);
– "fixed assets under construction" refer to the costs sustained for new company projects that have not yet been concluded, related to the development of Eurofly's image and the Eurofly brand;
– "other assets" include the costs related to the preparation of Eurofly's web site (204 thousand Euro), as well as the modifications and standardizations made to the aircraft in the fleet amounting to 3,293 thousand Euro.

The principal capitalizations of the year refer to:

– start-up costs in the amount of 5,196 thousand Euro, primarily related to the costs sustained for the listing on the Stock Exchange in the amount of 3,663 thousand Euro, the costs sustained for the start-up of the Sharm El Sheikh and New York projects in the total amount of 1,073 thousand Euro (of which 322 thousand Euro as a fiscal year reclassification from "fixed assets under construction"), investments in pilot training and maintenance in the amount of 400 thousand Euro, and costs for outfitting the rented offices at the Malpensa airport amounting to 60 thousand Euro.
– concessions, licenses, trademarks and similar rights: amounting to 1,034 thousand Euro, primarily related to the implementation of a new warehouse and maintenance software (528 thousand Euro), as well as to the cost, inclusive of accessory costs, sustained to purchase the Eurofly trademark for consideration, amounting to 506 thousand Euro. Prior to such purchase, the Eurofly trademark was granted as a gratuitous, perpetual and non-exclusive license by Eurofly Service S.p.A., a third party company.
– Other assets in the amount of 2,353 thousand Euro primarily refer to the modifications made to the A330 and A320 aircraft, for a total of 1,978 thousand Euro as well as to aircraft purchase costs in the amount of 281 thousand Euro, of which 42 thousand Euro relating to reclassifications from the item "Fixed Assets under construction".

Amortization of the period in the amount of 2,050 thousand Euro benefits from the 3 year extension of the operative rental contracts related to the three Airbus 320, contractually agreed-upon during the course of 2005.

II) **“Tangible fixed assets”**, net of the respective accumulated depreciation, amount to 16,647 thousand Euro and registered, with respect to 31 December 2004, a net decrease of 19,095 thousand Euro. The changes of this item are detailed in Annex 2.

The various components and variations of investments and disinvestments are analyzed below:

- The item “land and buildings” refers to the building located in Via Ettore Bugatti no.15, Milan, where the Company’s registered office was transferred in December 2004. During the year investments amounting to 497 thousand Euro were made related to installations and light constructions.
- The item “plant and machinery” which as of 31 December 2004 referred to the MD 80/82 fleet and rolling components was represented, as of 31 December 2005, exclusively by rolling components of aircraft subsequent to the disinvestment of the MD 80/82 fleet, with the realization of 1,580 thousand Euro in capital gains. The investments of the year in rolling components amount to 717 thousand Euro, whereas the residual amount of investments refers to the purchase of an MD80/82, later sold in May 2005.
- The item “equipment” refers to equipment and workshop tools. Investments were made during the year in the amount of 131 thousand Euro.
- The item “other assets” prevalently refers to furnishings and decor for 478 thousand Euro and to hardware for 400 thousand Euro. The investments of the year amount to 169 thousand Euro prevalently related to hardware; during the year there were disinvestments of motor vehicles amounting to 36 thousand Euro and hardware for 41 thousand Euro.
- “Fixed assets under construction”, amounting to 4,967 thousand Euro, primarily refer to the down payment given to the supplier Airbus for the purchase of the A350 (4,870 thousand Euro); between 2006 and 2013 it is expected that further payments will be made as advances on the price of a total of approximately 120 million USD (of which approximately 16 million USD to be paid within April 2007), whereas the purchase price of the three A350, estimated by the Company as being a total of approximately 230 million USD, will be paid upon the delivery of the above aircraft.

  In addition to the above down payment for the A350, the residual increases primarily refer to down payments to suppliers to outfit the A319 LR aircraft (2,120 thousand Euro); the decreases of a total of 14,139 thousand Euro refer to:
  - the reclassification to the item “Prepaid expenses” of the advance payment of 9,757 thousand Euro paid to the builder and considered as a maxi-rent in the context of the finance leasing stipulated with Locat S.p.A. with reference to the above-cited aircraft;
  - the reclassification of 246 thousand Euro to the item “plant and machinery” of the purchase options of two MD 80/82 aircraft subsequently sold during the first six month period;
  - o the sale to the builder Airbus of investments amounting to 4,136 thousand Euro of outfitting (purchased from third party suppliers) for the A319 aircraft, later acquired in finance leasing from Locat S.p.A.

The effect of the application of the financial methodology in registering the finance lease for the A319LR aircraft results in an improvement of the year’s net result and the net equity as of 31 December 2005 in the amount of 110 thousand Euro, as detailed in Annex 4.

The depreciation of the period amounts to 772 thousand Euro and benefits from the effect of the change of estimate of the useful life of the building, as better described in the paragraph related to valuation criteria.

III) **“Financial fixed assets”**

The financial fixed assets as of 31 December 2005 can be analyzed as follows:

| | **31.12.2005** | **31.12.2004** |
|---|---|---|
| Long term financial assets | 18,906 | 10,452 |
| Security deposits to guarantee operative rentals | 10,869 | 6,541 |
| Various security deposits | 5,206 | 2,091 |
| **Total financial fixed assets** | **34,981** | **19,084** |

The net variation amounting to 15,897 thousand Euro consists of increases of 17,290 thousand Euro and decreases of 1,393 thousand Euro.

Financial receivables include a capitalization contract having a lump sum premium paid in advance for 10,841 thousand Euro (10,452 thousand Euro as of 31 December 2004) and a restricted bank deposit with Unicredit, amounting to 8,065 thousand Euro, opened during the course of 2005 and contemporaneously pledged for the issue by Unicredit of a bank guarantee as security for the already cited finance leasing contract stipulated in May 2005 with Locat S.p.A. for the purchase of the A319. The capitalization contract with the lump sum premium had as its object an insurance policy (number 1.280.611) with "La Venezia Assicurazioni" of the Generali Group. As of 31 December 2004 and as of 31 December 2005, said capitalization contract had an effective yield equal, respectively, to approximately 4.5% and 3.8%. Earned interest matured in 2005 amounted to 397 thousand Euro (of which 9 thousand Euro accrued, as of 31 December 2005, to accrued revenues). Said contract, pledged starting from April 2005 to Banca Profilo for the granting of a credit line of 10,000 thousand Euro, was released in February 2006 by "La Venezia Assicurazione" and sold by the Company to Banca Profilo at market value, aligned to the book value from the financial statements as of December 31, 2005.

The security deposits, as guarantee of the operative rentals, increased by 4,328 thousand Euro.

The variation was primarily caused by the opening of new security deposits as guarantee of the operative rental contracts for new A330. Moreover, prior to the delivery of the above two aircraft it is expected additional security deposits will be paid for a total of 600 thousand USD. The durations of the operative rental contracts for the above aircraft are respectively eight and seven years, with a total expected undertaking amounting to approximately 120 million USD.

The variation of the security deposits also reflects reimbursements, in particular from the supplier of STAR wet lease services (approximately 1,000 thousand Euro), as well as the adjustment related to the exchange rates.

The increase of the security deposits refers to the opening of new contracts for the performance of services by operative providers.

## C) CURRENT ASSETS

Current assets, amounting to 81,912 thousand Euro, presents an overall increase of 17,797 thousand Euro with respect to the balance indicated in the financial statements as of 31 December 2004.

The comment to the principal items of current assets are as follows:

**"Stock"** amounting to 2,140 thousand Euro, prevalently refers to aeronautical consumables.

**"Receivables from customers"** amounting to 37,961 thousand Euro (net of the receivables devaluation fund of 7,514 thousand Euro), diminished with respect to the balance as of 31 December 2004 of 11,972 thousand Euro. Said decrease can be principally traced to the offset that was made – determined in June 2005 – of receivables from Alitalia, in relation to the code share contract that expired in March 2005, with liabilities to suppliers for the services that are invoiced by Alitalia totaling 14,057 thousand Euro, as well as the factoring operation related to trade receivables from the Ministry of Defense that was performed during the course of the second six month period of 2005 for a total of 14,398 thousand Euro. It is noted that the fiscal year registered a worsening in the collection times of receivables from some clients. During the year a provision to the bad debt reserve was made of 2,000 thousand Euro, as well as the devaluation of receivables for penalties in the amount of 835 thousand Euro. This significant provision derives from an increased risk of unrecoverableness of some specific positions and from the revision of the estimate of the generic risk of unrecoverableness connected to the worsening of client solvency due to the crisis determined by the catastrophic and terrorist events of the year.

In particular, as discussed in the section "Main events that took place after the close of the fiscal year and outlook of the following year", on 25 January 2006 the Company received written notice from Teorema Tour with regard to the alleged groundlessness of the credit balance claimed by the Company (approximately 3 million Euro and 3 million USD) and the corresponding request for damages for approximately 1.2 million Euro. The Company, supported by its attorneys, after verification – entrusted to independent auditors specifically appointed – of the proper application of the contract for the purposes of the invoicing and determination of the credit position as well as determination of the value of the penalties requested to the opposing party, confirms the groundlessness of opposing party's arguments – who further has not provided sufficient support for its claims – and therefore deems that the credit from the same is liquid and enforceable. To protect its rights, the Company decided to initiate arbitration as contractually provided, as well as proceed with every opportune legal action aimed at the recovery of the credit and recognition of the penalties due to flight cancellations, amounting to 14,728 thousand Euro, not indicated in the financial statements in that they are contested by opposing party.

In the context of the controversies that arose at the end of the fiscal year it is noted that, by means of a summons and complaint served on 2 November 2005, the Company summonsed Italy Aviation Service S.r.l. for claims related to commercial relationships with the same, claiming in addition to the payment of its credits – amounting to 1.4 million Euro – also the payment of damages of approximately 1.7 million Euro. On 30 December 2005, opposing party, in addition to requesting that the claim made by the Company be rejected, in turn requested that the Company be ordered to pay damages of approximately 2.1 million Euro. In this case as well the Company, supported by its attorneys, considers the risk of losing the controversy in exam to be remote.

**"Receivables from Tax Authorities"** amounting to 2,810 thousand Euro, primarily refer to receivables for VAT in the amount of 787 thousand Euro, as well as the advance for IRAP and tax withholdings in the amount of 2,023 thousand Euro.

**"Deferred tax assets"** amounting to 1,523 thousand Euro, refer to variations in increase of the taxable income due to time differences. The following table indicates the detail of the deferred tax assets for the fiscal year and the movement that was made with respect to 31 December 2004:

| | Values as 31.12.2004 | | | | Values as 31.12.2005 | | |
|---|---|---|---|---|---|---|---|
| | **Temp. diffe-rences** | **Rate** | **Taxes paid in advance** | **2005 move-ments** | **Temp. diffe-rences** | **Rate** | **Taxes paid in advance** |
| Provision for risks and charges | 1,587 | 37.25% | 591 | 864 | 2,451 | 37.25% | 913 |
| Bad debt reserve | 409 | 33.00% | 135 | 2,825 | 3,235 | 33.00% | 1,067 |
| Tax losses carried forward | 226 | 33.00% | 75 | (226) | – | 33.00% | – |
| Other timimg differences for IRAP purposes | 1,883 | 4.25% | 80 | (1,156) | 727 | 4.25% | 31 |
| Unpaid remuneration of Directors | 425 | 33.00% | 140 | (381) | 44 | 33.00% | 15 |
| Remuneration statutory and external auditors | 7 | 37.25% | 3 | 50 | 57 | 37.25% | 21 |
| Expenses for public relations and gifts | 15 | 37.25% | 6 | 15 | 31 | 37.25% | 11 |
| Net penalty interest | – | 33.00% | – | (5) | (5) | 33.00% | (2) |
| Unrealized profits and losses on exchange rates | – | 33.00% | – | (1,617) | (1,617) | 33.00% | (534) |
| **Total** | **4,553** | | **1,030** | | **4,923** | | **1,523** |

The remaining items of current assets are represented by:

**"Other receivables"**, amounting to 5,206 thousand Euro, primarily refer to advanced payments made to service providers for 1,720 thousand Euro, receivables for 1,935 Euro relative to maintenance costs for two A330 aircraft sustained on behalf of the lessor, receivables from employees for 400 thousand Euro related to advanced payments for trips and 880 thousand Euro for receivables from the factor for the assignment of receivables from the Ministry of Defense.

**"Current financial assets"** as of 31 December 2004 refer to a capitalization contract with lump sum premium paid in advance, paid during the course of the first month of 2005 at values aligned with those of its registration value.

**"Cash and cash equivalent"**, amounting to 32,272 thousand Euro, whose variation with respect to 31 December 2004 is analyzed in the cash flow statement.

## D) ACCRUED INCOME AND DEFERRED EXPENSES

Accrued income and deferred expenses, as of 31 December 2005, show an increase of 12,044 thousand Euro primarily related to the payment of the initial lump sum rent paid at the time of stipulation of the finance leasing for the A319LR, discussed in the item "Tangible fixed assets". The details of said item are as follows:

| | **31.12.2005** | **31.12.2004** |
|---|---|---|
| Accrued income: | | |
| – interest earned on other securities and bank interest | 10 | 4 |
| Deferred expenses: | | |
| – insurance premiums | 114 | – |
| – rent for aircraft already paid | 954 | 1,328 |
| – initial lump sum rent for lease of the A319LR | 9,549 | 70 |
| – miscellaneous | 4,745 | 1,926 |
| **Total** | **15,372** | **3,328** |

The item “miscellaneous” primarily refers to the payment of costs of airport assistance and software fees, consulting, advertising and promotional services, painting and maintenance of the aircraft. The increase of the year is primarily due to the increased activity and the new aircraft introduced in the fleet.

## LIABILITIES

### A) NET EQUITY

Reference is made to Annex 3 for the details of the changes of the past 2 fiscal years.

The items that make up the net equity as of 31 December 2005 are therefore:

“**Share capital**”, in the amount of 12,965,302, represented by 12,965,302 ordinary shares having a nominal value of 1.00 Euro each. The Share Capital has been entirely paid-in and 44.17% is held by the majority shareholder Spinnaker Luxembourg S.A.

The variation with respect to the amount of 6,666,922 as of 31 December 2004 was generated by the following two events:

*a)* On 26 May 2005, the Company’s Extraordinary Shareholders’ Meeting voted to attribute the Board of Directors, in accordance with article 2443 of the Civil Code, with the right to increase the share capital on a gratuitous basis, on one or more occasions within July 31, 2005, for a maximum nominal value of 500,000 Euro, by means of the issue of a maximum number of 500,000 ordinary shares enjoying regular rights, to be assigned to the Company’s employees in accordance with article 2349 of the Civil Code and in accordance with article 29 of the By-laws.

In performance of said authority, on July 1, 2005 the Board of Directors voted to increase the share capital from 6,666,922 Euro to 7,065,302 Euro, and therefore by 398,380 Euro by means of the use, for a corresponding amount, of the special reserve that the Ordinary Shareholders’ Meeting of 11 May 2005 had set up for the occasion, and to gratuitously assign some employees 398,380 newly issued shares having a nominal value of 1.00 Euro each, with regular enjoyment of rights relative to fiscal year 2005.

*b)* On 21 December 2005 Eurofly S.p.A. was admitted to trading on the Telematic Stock Market, organized and managed by Borsa Italiana S.p.A.. The admission to the Stock Exchange occurred by means of a public offer and the subscription and sale whose result is summarized below:

| Type of investor | Nr shares subscribed | Subscription Price | Share premium |
|---|---|---|---|
| Eurofly employees | 84,600 | 5.44 | 375,624 |
| Public offer and institutional placement | 5,264,011 | 6.40 | 28,425,659 |
| Private placement | 551,389 | 5.76 | 2,624,612 |
| **Totals** | **5,900,000** | | **31,425,895** |

The “**Share premium reserve**” amounts to 31,426 thousand Euro and was set up as specified in the above table.

The “**Legal reserve**” amounts to 478 thousand Euro and was increased by the destination of the profits of fiscal year 2004.

The “**Statutory reserve**” amounting to 3,681 thousand Euro, was increased subsequent to the destination of the profits of fiscal year 2004 for 6,493 thousand Euro and subsequent distribution of dividends for 5,000 thousand Euro, as well as the use of 398 thousand Euro subsequent to the resolution of the Board of Directors of 1° July 2005.

The “**Loss**” of the year amounts to 3,123,097 Euro.

The analysis of the composition of Net Equity with reference to the availability and capability of being distributed of the reserves is as follows (amounts in Euro):

| Nature/Description | Amount | Possibility of use | Available share | Distributable Share | Summary of uses made in the three previous fiscal years | |
|---|---|---|---|---|---|---|
| | | | | | to cover losses | for other reasons |
| **Share capital** | 12,965,302 | B | – | – | 6,011,520 | |
| **Capital Reserves:** | | | | | | |
| Payments increases of Capital | – | | – | – | | 5,000,362 |
| Share premium reserve | 31,425,895 | A,B | | | | |
| **Profit Reserves** | | | | | | |
| – Legal Reserve | 478,258 | B | – | – | | |
| – Statutory reserve | 3,680,752 | C | 3,680,752 | – | 2,881 | (5,398,380) |
| – Profits (losses) of the period | (3,123,097) | | (3,123,097) | – | | |
| **Total** | **45,427,110** | | **557,655** | **–** | | |

Index:
A: for increase of share capital
B: for coverage of losses
C: for distribution to shareholders

As of 31 December 2005, in virtue of the start-up costs with a net accounting value amounting to 6,099 thousand Euro, research and advertising costs having a net accounting value of 271 thousand Euro, as well as net profits on exchange rates that were not realized amounting to 1,617 thousand Euro, there are no residual portions of the reserves that can be distributed.

The effect of the year result and on Net Equity as of 31 December 2005 resulting from the application of the financial methodology in the registration of the finance lease contract for the A319LR aircraft is indicated in Annex 4 to the present notes to the financial statements.

## B) PROVISIONS FOR RISKS AND CHARGES

The provisions for risks and charges, amounting to 3,313 thousand Euro, show a net increase of 925 thousand Euro primarily due to the effect of the provisions accrued to the periodic maintenance reserve in the amount of 1,260 thousand Euro, net of the use of other risk provisions in the amount of 365 thousand Euro.

In detail, during the course of the year, provisions were subject to the following variations:

- **periodic maintenance reserve for the A320 and A330**, amounting to 3,146 thousand Euro, includes the estimate of the cost for periodic maintenance that must be born at the time of the technical expiration for such work, or in any event at the time of the redelivery to lessor of the Airbus 320 and 330 included in the fleet. At present, the reserve gathers cumulative allocations for:
  - **Fleet phase-out reserve:** amounting to 1,730 thousand Euro, with an increase for the year of 604 thousand Euro, refers to A320 aircraft for 384 thousand Euro and to A330 aircraft for 220 thousand Euro. Such reserve was accrued for reconditioning costs upon the termination of the contract.
  - **Extra maintenance reserve**, amounting to 1,416 thousand Euro, increased by allocations during the year in the amount of 623 thousand Euro, refers to the A330 aircraft for 527 thousand Euro and to the A319 aircraft for 96 thousand Euro; it refers to the share of periodic maintenance costs to be borne by the Company during the course of the leases.
- **other reserves:** amounting to 166 thousand Euro, refers for 53 thousand Euro to commercial controversies in course and for 113 thousand Euro to the accrual of the risk for noise tax. Said provision is due to the fact that said tax was decreed by means of a Law, but at present the implementing decree has still not been issued.

In view of completeness of information, it is noted that a there is an outstanding labor dispute; the preliminary hearing, set for 1° February 2006, did not take place. The amount of the petitum related to said controversy amounts to 300 thousand Euro. Further, there are normal management activities of commercial controversies, both as plaintiff and defendant, from which at present no further liabilities beyond those appropriated in the financial statements are foreseeable. In particular, among the commercial controversies in which the Company is defendant, we note a summons and complaint served on the Company in August 2005 by a tour operator for the payment of 1.1 million Euro for alleged breaches and violations committed by the Company. With regard to the cited controversies, the financial statements does not reflect any allocation due to the indeterminate nature and uncertainty of the risk of loosing.

## C) STAFF LEAVING INDEMNITY

The net increase of 121 thousand Euro in the staff leaving indemnity is justified by:

- accrual of 1,403 thousand Euro for indemnities to personnel, determined in conformity with law and outstanding employment contracts;
- utilization amounting to 1,282 thousand Euro subsequent to terminations of employment or advance payments made during the year; among these, there are advance amounting to 155 thousand Euro issued to some employees related to the listing operation.

## D) DEBTS

Debts, amounting to 92,121 thousand Euro, indicate an increase amounting to 7,012 thousand Euro.

With reference to the composition of the item the following is noted:

1. "**Debts due to shareholders**" amount to 4,500 thousand Euro and refers to the non-interest bearing loan having a 24 month duration obtained from Spinnaker Luxembourg S.A. and cashed on 18 November 2005 in order to reinforce the Company's asset and financial situation in view of its being listed on the Stock Exchange.
2. "**Debts due to banks**" amount to 18,529 Euro and are represented by bank overdrafts. As of 31 December 2005 the total credit lines amounted 52,300 thousand Euro (of which 10,000 thousand with Banca Profilo); said credit lines were utilized to cover bank overdrafts in the amount of 10,075 thousand Euro, to anticipate invoices in the amount of 6,403 thousand Euro, for bank guarantees in the amount of 16,878 thousand Euro and for advances for the assignment of receivables in the amount of 9,000 thousand Euro.
3. "**Debts due to lenders other than bank**" amounted to 4,761 thousand Euro, of which 491 thousand Euro are enforceable within 12 months, and consist of a loan with Banca Profilo during the month of December 2003 for the purchase of the property located in via Bugatti 15, Milan. Said loan has a ten year duration and provides for the payment of 20 twice-yearly instalments paid in advance. The interest rate is 1% per year fixed until the second instalment and subsequently is the Euribor rate at 6 months increased by 130 Bp per year. Said liability is secured by a first mortgage on said property for the value of 10,000 thousand Euro. The variation with respect to 31 December 2004 is explained by the payment of the first instalment, amounting to 238 thousand Euro. The portion of the liability expiring beyond five years amounts to 2,078 thousand Euro.
4. "**Payment received on account**", amounting to 2,017 Euro, primarily refer to security deposits obtained by tour operators as advances against contractual commitments.
5. "**Debts due to suppliers**" amount to 52,826 thousand Euro, with a net decrease amounting to 11,374 thousand Euro, attributable on the one hand to the effect of the Alitalia offset previously mentioned and on the other to the physiological increase of liabilities to suppliers connected with the increased activity.
6. "**Debts due to Tax Authorities**" amount to 3,009 thousand Euro, with an increase of 444 thousand Euro with respect to 31 December 2004. They consist for 1,809 thousand Euro of the IRAP liability (2,018 thousand Euro as of 31 December 2004), 1,006 thousand Euro for IRPEF tax withholdings (538 thousand Euro as of 31 December 2004), 185 thousand Euro for IRES liability (amounting to zero in 2004) and 9 thousand Euro for sundry tax liabilities.
7. "**Debts due to Social Security and insurance**" amount to 1,615 thousand Euro and refer to the amount of 1,513 thousand Euro as liabilities to the Italian Social Security Office (INPS).

8. “**Other debts**” amount to 4,863 thousand Euro, with an increase amounting to 1,724 thousand Euro. The item includes the funds set aside for the thirteenth month payment and matured vacation pay not taken, as well as bonuses to employees with the relative contributions.

## E) ACCRUED EXPENSES AND DEFERRED INCOMES

Accruals expenses and deferred incomes, amounting to 16,259 thousand Euro, registered a decrease of 4,403 thousand Euro.

They are analysed as follows:

| | 31.12.2005 | 31.12.2004 |
|---|---|---|
| Accrued expenses: | | |
| – accrued expenses (insurance, bank expenses and mortgage for the building) | 131 | 249 |
| Deferred incomes: | | |
| – contribution reconditioning of the Long Range fleet | 767 | 1,172 |
| – contribution to training for fleet maintenance | 1,370 | – |
| – payment invoices for sales of MD80/82 | – | 3,969 |
| – pre-invoiced sales | 13,320 | 15,273 |
| – other | 671 | – |
| **Total accrued expenses and deferred incomes** | **16,259** | **20,663** |

The variation of accrued expenses and deferred incomes is principally traced to the component of invoices issued in 2004 in advance of the stipulation of the notarial act for the sale of two MD80/82, whose transfer of ownership took place during the course of the year 2005, as well as to a reduction of pre-invoiced sales. In fiscal year 2005, it is noted that there was the payment of 1,370 thousand Euro of contributions received from Airbus for training courses for Eurofly’s personnel that will be held in 2006.

## MEMORANDUM ACCOUNTS

The memorandum accounts amount to 199,920 thousand Euro as of 31 December 2005 (94,975 thousand Euro as of 31 December 2004), with an increase amounting to 104,945 thousand Euro. The significant increase is explained by three year renewals for 3 A320 aircraft, the initiation of the finance leasing relative to the A319 and the introduction in the fleet of another two aircraft.

In fact, the memorandum accounts consist of:

– commitments for rent, amounting to 132,981 thousand Euro (76.541 thousand Euro as of 31 December 2004), assumed by the Company relative to operating leases for aircraft currently in the fleet. Some of these rents are regulated by contracts in currency and have been indexed at the Libor rate;
– commitments for finance lease in the amount of 37,127 thousand Euro relating to installments that have not yet expired, increased by the value of the purchase option at contract end (amounting to 7,657 thousand Euro) of the finance lease for the A319LR (stipulated during the first six months) and to computer components;
– commitments for rent to be paid to the lessor of the building in Sesto San Giovanni, while waiting to find a new tenant, in the amount of 220 thousand Euro;
– commitments for leasing of the server and cars for a total of 532 thousand Euro;
– guarantees issued to third parties for a total of 18,651 thousand Euro, for the contract lease of the A319LR and given to suppliers for the purchase of jet fuel and for the payment of airport taxes due at some airports;
– purchases of forward foreign exchange contracts for an amount of 8,477 thousand Euro, in order to purchase US Dollars with a monthly expiration from January through March 2006. Said operations were performed with the intent of hedging, even though they are considered, for purposes of the registration of the value as of 31 December 2005, as trading contracts in the absence of formalized strategies, procedures and policies. Since the fair value of said contracts as of 31 December 2005 was positive, the connected gain was not recognized on the income statement and was postponed to the time of realization;
– third party assets stored at our technical unit at Malpensa, amounting to 85 thousand Euro.

In particular, the above mentioned commitments for operating and finance leases of aircraft are timed as follows:

| | Within 2006 | 2007 | 2008 | Beyond | Total |
|---|---|---|---|---|---|
| **Operating leases** | | | | | |
| In US$/000 | 41,229 | 41,313 | 36,490 | 37,846 | 156,877 |
| counter-value in Euro | 34,949 | 35,020 | 30,931 | 32,081 | 132,981 |
| **Finance lease** (*) | | | | | |
| In EUR/000 | 3,157 | 3,157 | 3,157 | 19,997 | 29,470 |

(*) The rents are understood as being net of the redemption value of 7,657 thousand Euro.

Further, there are agreements with Airbus that allow Eurofly to order – for the same price conditions as the first aircraft (adjusted on the basis of Airbus' standard adjustment formula) - an additional A319 CJ/LR aircraft within the first six months of 2006, with delivery in 2007.

@On 11 August 2005 the Company stipulated two letters of intent having as their object two operative rentals related to two Airbus A330-200 aircraft, whose deliveries are forecast for November 2006 and April 2007. The durations provided by the 2 operative rental contracts are respectively 8 and 7 years, and the total amount of the rent due amounts to 129,780 thousand Euro.

On 30 December 2005, the Company subscribed to a final purchase contract for three Airbus A350; with regard to the total price agreed upon, reference is made to what was discussed in the notes to the comment to tangible fixed assets in course.

## ITEMS OF THE INCOME STATEMENT

The analysis of the contents and variations of the income statement refers to the final results set forth in the financial statements as of 31 December 2005. The comparison of the economic items was made with the financial statements for the fiscal year ended 31 December 2004.

### A) **PRODUCTION VALUE**

A1) "**Revenues from sales and services**", amount to 271,475 thousand Euro, against a value for fiscal year 2004 of 245,340 thousand Euro, registering an increase of 26,135 thousand Euro.

The principal categories of activity are sub-divided as follows:

| | 2005 | 2004 |
|---|---|---|
| Revenues | | |
| – revenues charter and accessories | 184,640 | 228,498 |
| – revenues A.C.M.I. flights | 3,806 | 1,156 |
| – revenues scheduled flights | 81,356 | 14,991 |
| – revenues finished products | 1,673 | 695 |
| **Total** | **271,475** | **245,340** |

The increase registered in invoiced sales, as better analyzed in the Management Report on Operations, is due to various factors, among which the increase of flight hours (which increased from 38,202 in 2004 to 42,060 in 2005, with a percentage increase of 10.1%) and the reinforcement of the Company's fleet, also due to the use of aircraft in wet lease.

A 5) "**Other revenue and income**" amounts to 6,512 thousand Euro against 2,037 thousand Euro in 2004, with an increase of 4,475 thousand Euro. It primarily refers to revenue for training courses performed on behalf of other airline companies, revenue for the lease of aircraft, penalties due from clients (net of devaluation, which in 2005 amounted to 835 thousand Euro) and to Airbus's contribution for the introduction in the fleet of the last A330 in May 2005 (for 1,357 thousand Euro). The increase with respect to 2004 is primarily due to income deriving from the rent received for the A319 amounting to 2,712 thousand Euro.

### B) **PRODUCTION COSTS**

The costs for "**raw materials, subsidiary materials, consumables and goods**", subsequent to the increased activities performed, show an increase of 20,946 thousand Euro, passing from 62,430 thousand Euro to 83,376 thousand Euro.

They primarily consist of the costs of jet fuel for 72,725 thousand Euro which, with respect to a value of 51,778 thousand Euro in fiscal year 2004, increased by 20,947 thousand Euro (+40.4%) due, in addition to the noticeable increase in consumption generated by the increase of the flight activity, to the increase of the average cost of Jet Fuel.

The supplies of catering material totaled 8,293 thousand Euro, in line with a total of 8,249 thousand Euro in fiscal year 2004; the purchases of technical consumables tied to direct maintenance of the Long Range activity reached the amount of 982 thousand Euro, substantially in line with the data of 2004, amounting to 994 thousand Euro.

The costs "**for services**" show an increase amounting to 3,621 thousand Euro and amount to 105,311 thousand Euro in 2004 and to 108,932 thousand Euro in 2005.

They are analyzed by nature:

| | 2005 | 2004 |
|---|---|---|
| **Costs for services** | | |
| – Expenses for traffic and airport | 65,521 | 61,839 |
| – Maintenance and reconditioning of the fleet | 23,665 | 25,538 |
| – Consulting and various services | 2,484 | 4,353 |
| – Transportation and housing of personnel | 5,080 | 5,287 |
| – Expenses for sales and advertising | 6,093 | 2,812 |
| – Insurance | 2,174 | 1,754 |
| – Selection/Training of flight crew | 1,772 | 2,107 |
| – Transportation and shipments | 285 | 145 |
| – Postal and telephone expenses | 1,477 | 1,201 |
| – Other costs for services | 380 | 275 |
| **Total costs for services** | **108,932** | **105,311** |

The increase of expenses for traffic and airport (+6%) are justified by the increased activity performed.

Containment of maintenance costs and reconditioning of the fleet is tied, among others, to the decreased use of external maintenance providers and to completion of the disinvestment of the MD80 fleet, which had higher maintenance costs.

The expenses for the transportation and housing of personnel are in line and thus were contained notwithstanding the increase of activity.

The expenses for sales and advertising was subject to a significant increase (3,263 thousand Euro amounting to +116%), explainable by the increase of advertising costs on average and sponsorships aimed at promotion of the scheduled flight activity and in particular the launch of New York, as well as the increase of costs tied to reservation services using a call center, and to commissions to travel agents and Tour Operating services.

The costs "**for use of property of third parties**", amounting to 44,736 thousand Euro, show an increase of 8,180 thousand Euro with respect to fiscal year 2004 (36,557 thousand Euro).

The detail is as follows:

| | 2005 | 2004 |
|---|---|---|
| **Costs for use of property of third parties** | | |
| – Aircraft rents due to Third parties | 13,111 | 19,061 |
| – Aircraft A330 rents due to Third parties | 9,435 | 7,449 |
| – Aircraft A320 rents due to Third parties | 17,547 | 8,625 |
| – Finance Leasing A319 | 2,450 | – |
| – Other rents and leasing | 2,193 | 1,422 |
| **Total** | **44,736** | **36,557** |

In 2005 the Company increased its rental of A320 aircraft with respect to fiscal year 2004, due to the effect of the introduction in the fleet of three new aircraft during the months of December 2004 and February 2005.

During the course of the month of May 2005, a new A330-200 was introduced in the fleet leased from the company ILFC, which brings the number of Long Range aircraft to three.

The costs "for personnel" evidence an increase, with respect to the prior year, of 3,947 thousand Euro, passing from 35,195 thousand Euro to 39,143 thousand Euro, and is made up as follows:

| | 2005 | 2004 |
|---|---|---|
| **Costs for personnel** | | |
| – Gross remuneration | 30,750 | 28,018 |
| – Social security | 6,545 | 5,549 |
| – Leaving indemnity | 1,404 | 1,244 |
| – Other personnel costs | 443 | 384 |
| **Total personnel costs** | **39,142** | **35,195** |

The numerical evidence of the personnel employed over the years in review is analyzed in the final part of the present report. The increase of the cost for personnel is substantially related to the increase of the average workforce.

"**Depreciation, amortization and write-down**" made during the course of fiscal year 2005 amount to 4,821 thousand Euro, with an increase with respect to the same period of the prior fiscal year of 2,061 thousand Euro (+74.7%).

The detail of said item is as follows:

| | 2005 | 2004 |
|---|---|---|
| **Depreciation, amortization and write-down** | | |
| – Depreciation intangible fixed assets | 2,049 | 1,527 |
| – Depreciation tangible fixed assets | 772 | 842 |
| – Other write-down of fixed assets | – | 227 |
| – Bad debt provision on trade receivables | 2,000 | 164 |
| **Total depreciation, amortization and write-down** | **4,821** | **2,760** |

The significant provision for bad debt reserve of trade receivables derives from an increased risk of unrecoverableness of some specific positions and from the general increase of the estimate of generic risk, primarily related to the deterioration of the solvency of clients due to the crisis determined by natural disasters and terrorist attacks during the year.

As a precautionary measure, as in the past, receivables that are contested or tied to clients subject to bankruptcy procedures were totally devalued.

"**Other provisions**" amounting to 1,259 thousand Euro are analyzed by nature in the note "Provisions for risk and charges".

"**Other charges**" amounts to 730 thousand Euro, with an increase of 173 thousand Euro with respect to fiscal year 2004 (557 thousand Euro)f. The most significant amounts are:

| | 2005 | 2004 |
|---|---|---|
| **Other charges** | | |
| – Association fees | 58 | 45 |
| – Municipal real property tax (ICI) | 29 | 29 |
| – Stamp duty | 45 | 43 |
| – Printed materials and other manuals | 124 | 151 |
| – Bank expenses on bank accounts | 184 | 79 |
| – Fines and penalties | 85 | 53 |
| – Other | 205 | 157 |
| **Total other charges** | **730** | **557** |

## C) **INCOME AND FINANCIAL CHARGES**

16) "**Other financial income**" amounts to 561 thousand Euro, showing a decrease with respect to the balance of fiscal year 2004 (761 thousand Euro) of 200 thousand Euro. The balance was principally determined by proceeds from the capitalization contract with a sole premium and penalty interest for late payments.

Financial income consisted of the following:

| | 2005 | 2004 |
|---|---|---|
| **Other financial income** | | |
| – Earned interest on bank accounts | 123 | 109 |
| – Earned interest on securities | 399 | 652 |
| – Other financial income | 39 | – |
| **Total other financial income** | **561** | **761** |

17) "**Interest payable and other financial charges**" amounts to 1,652 thousand Euro, with a significant upwards variation of 1,531 thousand Euro with respect to the prior fiscal year (121 thousand Euro).

They can be analysed as follows:

| | 2005 | 2004 |
|---|---|---|
| **Financial charges** | | |
| – commissions on bank guarantees | 323 | 42 |
| – Passive interest on the mortgage | 160 | 3 |
| – Passive interest on bank accounts | 930 | 26 |
| – Interest on debts due to suppliers | 218 | 30 |
| – Other passive interest | 21 | 20 |
| **Total financial charges** | **1,652** | **121** |

The increase of financial charges is primarily explained by the loan operations performed during the year subsequent to investments made by the Company (purchase of the building in via Bugatti 15, and purchase of the A319 in finance leasing).

17-bis) "**Exchange differences**" amounts to a gain of 1,866 thousand Euro, against a loss of 269 thousand Euro in 2004. The positive differences of the exchange rate amounting to 4,346 thousand Euro consist of gains recorded during the course of the year. The part that was not realized, amounting to 3,151 thousand Euro, refers to the adjustment of receivables and liabilities and monetary items in currency at the exchange rate of 31 December 2005.

The negative exchange rate differences amounting to 2,479 thousand Euro consist of losses recorded during the course of the fiscal year. The amount of the unrealized loss relative to the adjustment of the receivables and liabilities and monetary items in currency at the exchange rate of 31 December 2005 amounts to 1,533 thousand Euro.

As indicated above, it is specified that the net effect of the adjustment of receivables and liabilities in short term currency at the exchange rate as of 31 December 2005 resulted in a net gain that was not realized of 1,617 thousand Euro.

| | 2005 | 2004 |
|---|---|---|
| **Gains and Losses on exchange rates** | | |
| – Gains on exchange rates | 4,346 | 1,570 |
| – Losses on exchange rates | (2,478) | (1,839) |
| **Total gains and losses on exchange rates** | **1,868** | **(269)** |

## E) **EXRAORDINARY INCOME AND CHARGES:**

Extraordinary income and charges, amounting to 2,292 thousand in 2005 as opposed to 3,497 thousand in 2004 (decrease of 1,205 thousand Euro), primarily refer to the net gains from the sale of 8 MD80/82 and 2 purchase options for MD 80/82 in the amount of 1,595 thousand Euro, as well as contingent assets in the amount of 775 thousand Euro for the release of prior accruals on invoices to be received referring to previous years, deemed to be excessive with respect to actual need.

22) "**Current and deferred taxes**", refer to current taxes of 1,994 thousand Euro (2,018 thousand Euro in 2004), represented by the allocation for the Regional Tax on Productive Activity (IRAP) in the amount of 1,809 thousand and IRES in the amount of 185 thousand Euro, and to deferred tax assets in the amount of 493 thousand Euro (950 thousand Euro in 2004).

The Company, by means of a total amnesty in accordance with Law 289/2002, closed fiscal years from 1997 through 2001 for direct taxes and from 1998 through 2001 for VAT. The subsequent fiscal years are thus subject to tax assessment by the competent organs.

## SUPPLEMENTAL REPORT - Other information

### Remuneration for Directors and Statutory Auditors

The amount of approved remuneration for Directors and Statutory Auditors cumulatively for each category was as follows during the period:

| Remuneration | 2005 | 2004 |
|---|---|---|
| – Directors | 62 | 472 |
| – Statutory Auditors | 62 | 28 |

### Average number of registered employees

During fiscal years 2004 and 2005, the average number of employees was as follows:

| | 2005 | 2004 |
|---|---|---|
| **Employees** | | |
| Managers | 7.85 | 6.60 |
| Office workers | 187.33 | 149.80 |
| **Total Ground Personnel** | **195.18** | **156.40** |
| Pilots | 128.24 | 120.08 |
| Cabin flight crew | 266.06 | 254.00 |
| **Total Flight Crew** | **394.30** | **374.08** |
| **Overall total** | **589.48** | **530.48** |

# ANNEX TO THE 2005 FINANCIAL STATEMENTS

## Table of changes of intangible fixed assets and relative accumulated amortization

*Annex 1*

| *Amounts in Euro* | Gross value | | | | Accumulated Amortizations | | | |
|---|---|---|---|---|---|---|---|---|
| | **Gross value as of 31/12/04** | **Increases** | **Reclassi-fications** | **Gross value as of 31/12/05** | **Accumulated amortization 31/12/04** | **Amortization of the year** | **Accumulated amortization 31/12/05** | **Net intangible fixed assets** |
| 1) Start-up costs | 4,032,185 | 4,873,402 | 322,310 | 9,227,897 | 2,118,954 | 1,010,167 | 3,129,121 | **6,098,776** |
| 2) Research, development, and advertising costs | 386,920 | 45,000 | – | 431,920 | 77,813 | 82,313 | 160,126 | **271,794** |
| 3) Concessions, licenses, trademarks and similar rights | 897,758 | 1,033,644 | – | 1,931,402 | 353,603 | 219,869 | 573,472 | **1,357,931** |
| 6) Fixed assets under construction | 395,591 | – | (364,091) | 31,500 | – | – | – | **31,500** |
| 7) Other intangible fixed assets | 3,063,491 | 2,310,845 | 41,781 | 5,416,117 | 1,182,151 | 737,256 | 1,919,407 | **3,496,710** |
| **Totale intangible fixed assets** | **8,775,945** | **8,262,891** | **–** | **17,038,836** | **3,732,521** | **2,049,605** | **5,782,126** | **11,256,710** |

## Table of changes of tangible fixed assets and relative accumulated depreciation

*Annex 2*

| *Amounts in Euro* | Gross value | | | | | Accumulated Depreciation | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | **Gross value as at 31/12/04** | **Reclassi-fications** | **Increases** | **Decreases** | **Gross value as at 31/12/05** | **Accumulated depreciation 31/12/04** | **Depreciation of the year** | **Decreases** | **Accumulated depreciation 31/12/05** | **Net tangible fixed assets** |
| 1) Land and buildings | 7,929,400 | – | 496,833 | – | 8,426,232 | 72,632 | 241,617 | – | 314,249 | **8,111,984** |
| 2) Installations and machinery | 16,215,037 | 246,219 | 5,769,171 | 18,389,037 | 3,841,391 | 1,794,107 | 216,302 | 323,639 | 1,686,771 | **2,154,620** |
| 3) Equipment | 686,026 | – | 131,266 | – | 817,293 | 257,657 | 85,434 | – | 343,091 | **474,201** |
| 4) Other assets | 1,980,900 | – | 168,823 | 76,758 | 2,072,964 | 964,529 | 228,489 | 58,748 | 1,134,270 | **938,695** |
| 5) Fixed tangible in course | 12,019,339 | (10,003,653) | 7,087,569 | 4,135,819 | 4,967,436 | – | – | – | – | **4,967,436** |
| **Total tangible fixed assets** | **38,830,701** | **(9,757,433)** | **13,653,662** | **22,601,613** | **20,125,316** | **3,088,926** | **771,842** | **382,387** | **3,478,381** | **16,646,935** |

## Changes in the accounts of net equity for the year ended 31 December 2004 and 2005

*Annex 3*

| *Amounts in euro* | Share capital | Share premium reserve | Legal reserve | Statutory reserve | Reserve future increases of capital | Profits (losses) of fiscal year | Total |
|---|---|---|---|---|---|---|---|
| **Balance as of December 2003** | **6,666,922** | **–** | **409** | **–** | **–** | **2,721,769** | **9,389,100** |
| Allocation of 2003 profits | | | 136,088 | 2,585,681 | | (2,721,769) | – |
| Profits for fiscal year 2004 | – | | – | – | | 6,835,212 | **6,835,212** |
| **Balance as of December 2004** | **6,666,922** | **–** | **136,497** | **2,585,681** | **–** | **6,835,212** | **16,224,312** |
| Allocation of 2004 profits | | | 341,761 | 6,493,451 | | (6,835,212) | **–** |
| Distribution of dividends to sole shareholder | | | | (5,000,000) | | | **(5,000,000)** |
| Other movements | | | | (500,000) | 500,000 | | **–** |
| Increase of share capital | 398,380 | | | 101,620 | (500,000) | | **–** |
| Effect of listing on Stock Exchange | 5,900,000 | 31,425,895 | | | | | **37,325,895** |
| Losses of fiscal year | | | | | | (3,123,097) | **(3,123,097)** |
| **Balance as of 31 December 2005** | **12,965,302** | **31,425,895** | **478,258** | **3,680,752** | **–** | **(3,123,097)** | **45,427,110** |

In conformity with the indications provided by Document OIC 1 – THE PRINCIPAL EFFECTS OF THE REFORM OF COMPANY LAW ON THE PREPARATION OF THE FISCAL YEAR FINANCIAL STATEMENT, the table set forth below provides information regarding the effects that might be produced on Net Equity and the Income Statement recording the finance leasing of the A319 according to what is required by application of IAS 17.

| | | Euro/000 |
|---|---|---|
| **The effect on Net Equity can be represented as follows:** | | |
| **A** | **ASSETS** | |
| **A1** | **Contracts in course** | |
| | + Assets acquired in finance leasing during the course of the fiscal year | 38,285 |
| | – Share of depreciation pertaining to the fiscal year | (1,337) |
| | Net value of assets in finance leasing at the end of the fiscal year | 36,948 |
| **A2** | **Redeemable assets** | |
| | Overall added value of redeemed assets, determined according to the financial methodology, with respect to their net accounting value at the end of the fiscal year | – |
| **A3** | **Treatment of the initial maxi-rent** | |
| | – Reclassification of the payable relative to the residual initial maxi-rate | (8,957) |
| **B** | **Liabilities** | |
| | + Implicit liabilities that arose during fiscal year | 38,285 |
| | – Reduction for reimbursement of Share capital (including initial maxi rate) | (10,469) |
| | Implicit liabilities for finance leasing at the end of the fiscal year | 27,816 |
| | – expiring in subsequent fiscal year | 1,712 |
| | – expiring between 1 to 5 years | 7,838 |
| **C** | **Overall gross effect at end of fiscal year (A1+A2+A3-B)** | **175** |
| **D** | Net tax effect | (65) |
| **E** | **Net effect on Net Equity at the end of the fiscal year (C-D)** | **110** |
| **The effect on Income Statement can be represented as follows:** | | |
| Reclassification of rents on finance leasing | | 1,842 |
| Reclassification of annual portion of maxi rent | | 555 |
| Recording of financial costs on finance leasing | | (885) |
| Recording of: | | |
| – | Depreciation | |
| | – on existing contracts | (1,337) |
| **Effect on result prior to taxes** | | **175** |
| Recording of fiscal effect (37.25%) | | (65) |
| **Net effect on result at the end of the fiscal year** | | **110** |

# REPORT OF THE BOARD OF STATUTORY AUDITORS

**REPORT OF THE BOARD OF STATUTORY AUDITORS TO EUROFLY S.p.A.'S SHAREHOLDERS' MEETING IN ACCORDANCE WITH ART. 2429, PAR. 2, OF THE ITALIAN CIVIL CODE AND ART. 153 OF LEGISLATIVE DECREE NO. 58/98 RELATIVE TO THE FINANCIAL STATEMENTS FOR THE FISCAL YEAR ENDED 31 DECEMBER 2005**

Dear Shareholders,

Over the course of the fiscal year that ended 31/12/2005, and during the first months of 2006, the Board of Statutory Auditors has performed its duties in accordance with law and the principles recommended by the National Councils of Accountants and Bookkeepers regarding the activity of a Board of Statutory Auditors.

**1.**

**SUMMARY OF THE AUDITING ACTIVITY**

The Board audited:

- compliance with law and the deed of incorporation;
- adequacy of the organizational structure and administrative system;
- compliance with proper management principles.

The auditing activity set forth above was performed by the Board in seven meetings during 2005 and in four meetings during 2006, through today, and during fiscal year 2005 it participated in eleven meetings of the Board of Directors, almost always in the presence of the entirety of auditors.

During the course of said meetings we repeatedly met with the directors responsible for the various functional areas and with the Auditing Firm entrusted with the audit.

2.

## COMPLIANCE WITH LAW AND WITH THE DEED OF INCORPORATION

The resolutions of the Board of Directors and the operations performed by the delegated Body which, in accordance with law, periodically advised us of the general trend of the activity performed, its foreseeable development, as well as the main economic, financial and patrimonial transactions occurred, allow us to acknowledge the material compliance of the management activity with law and the corporate by-laws.

We can reasonably observe that the actions that were approved and implemented are not in conflict of interest or in contrast with resolutions approved by the Shareholders' Meeting, do not create particular risks for the Company and do not compromise the integrity of its net worth.

We verified, in particular, that the procedure for the admission of its ordinary shares to the listing on the telematic stock market managed by Borsa Italiana S.p.A. was approved and implemented in compliance with the laws and regulations issued for this kind of transactions and complied with the recommendations received by the Company from such Authorities.

We acknowledge that, by means of a resolution of the extraordinary shareholders' meeting of 12 September 2005, the corporate by-laws were amended in order to comply with the specific provisions set out for Companies issuing listed securities in regulated markets.

Furthermore, during the course of said meetings we checked that the activity be performed in compliance with the specific provisions of laws and regulations issued at European Community and national level regarding the sector in which the Company operates.

3.

**ADEQUACY OF THE ORGANIZATIONAL STRUCTURE**

During periodic meetings with managers of the relative functions, we obtained the information required to evaluate the adequacy of the Company's organizational structure and compliance with proper management principles.

We verified, with regard to what falls within our competence, the adequacy of the administrative–accounting system during meetings with the service managers, with whom there was always a relationship of full cooperation, and we met with the internal controller who was recently hired.

This position was created upon the listing of the shares on the Telematic Stock Market managed by Borsa Italiana S.p.A. and, in the corporate organization chart, it is not subordinate to any manager of an operative area.

During the meetings that took place, we noted the initiation of some processes that make up the internal control system aimed at overseeing risks, redefining the processes previously implemented, improving computer equipment as well as creating and reinforcing some staff functions.

In this context, it should be noted that the Company, according to the provisions set out in the Prospectus relative to the offer for the subscription, sale and admission to the listing on the telematic stock market, has created the following functions:

- a management committee, whose purpose is to analyze the trend of the main management indicators, as well as to identify the actions that might be necessary to realign the results with respect to specific objectives;
- an internal control committee, whose purpose is to assist the Board of Directors with the orientation, verification and monitoring of the internal control system, with the objective of ensuring management effectiveness and efficiency, the

credibility and integrity of the economic-financial results, the compliance with current law and protection of the Company's assets;

- a remuneration committee, whose purpose is to propose and control remuneration criteria and incentive mechanisms.

With reference to Corporate Governance, we hereby confirm that the Company's Board of Directors has complied with the Self-Regulation Code for Listed Companies in the terms already indicated in the cited Prospectus, updated during the meeting of the Board of Directors held 4 April 2006.

Furthermore, it should be noted that the Company continued its undertaking regarding the internal development of its training programs for flight crews.

In its report, the Board provided information on the procedures related to compliance with Legislative Decree no. 626/1994, on the health of employees, and with privacy provisions (Italian Privacy Act, Legislative Decree 196/2003).

During the course of its auditing activity, as described above, no significant facts, omissions and/or censurable facts and/or irregularities emerged that would require advising the Supervisory Bodies and mention in this Report.

**4.**

**COMPLIANCE WITH PROPER MANAGEMENT PRINCIPLES**

The information acquired during the course of the year from the Company's managers and from the Auditing Firm confirmed the compliance of the administrative-accounting system with the proper accounting and entry of management activity in the Company's interim and year-end financial statements, and the due performance of administrative and fiscal compliances.

We have met with members of the Auditing Firm, and exchanged constructive comments, observations and information with regard to the Company's organization, reporting system and every other control performed in the context of our respective mandates.

**5.**

**INTERGROUP RELATIONSHIPS AND RELATIONSHIPS WITH RELATED PARTIES**

We note in this regard that the Company is not part of any group, and does not have any majority stakes in or connections with other Companies or Entities.

Furthermore, we did not find any relationships with related parties to be in contrast with the Company's interests, or which were atypical, unusual, or in any event regulated by non-competitive conditions.

**6.**

**OTHER INFORMATION**

During the course of the fiscal year we did not receive any complaints from shareholders in accordance with art. 2408 of the Italian Civil Code, nor complaints from third parties.

We acknowledge that during the course of 2005, the Company prepared a Six-Month Report, in the terms established by law, which was submitted to the review of the Auditing Firm Deloitte & Touche S.p.A.

The Report was sent to the Board of Statutory Auditors and did not require any comments from us. Upon the express directors' representation, and as confirmed by the Auditing Firm, we note that, in addition to the audit of the financial statements for the three-year period 2005-2007 and audit of the six-month reports for 2005, 2006 and 2007, during the course of the fiscal year the Auditing Firm was entrusted with the following assignments:

- determination of the qualitative and quantitative impact deriving from the application of the IAS/IFRS rules to accounting principles, reporting systems, administrative processes and the year-end financial statements;
- issuance of comfort letters related to the admission procedures for the listing of ordinary shares on the telematic stock market managed by Borsa Italiana S.p.A.

We note that the plan to gratuitously award shares to some employees, approved by the Board of Directors on 1° July 2005 in conformity with the mandate received in accordance with art. 2443 of the Italian Civil Code from the Extraordinary Shareholders' Meeting of 26 May 2005, was duly performed. We received adequate information regarding it from the Board.

In its Management Report, the Board of Directors provided adequate information with regard to the items in the financial statements whose valuation will be affected by the use of the IAS/IFRS international accounting principles, applicable to the Company starting from 2006.

We note that in par. 13 of the above Report, the Board of Directors discussed the significant facts that occurred after the end of the fiscal year, and in particular, the development of its relationship with the client Teorema Tour S.p.A. and the effects of the interruption of said relationship on fiscal year 2006 .

Furthermore, we note the agreement entered into by Spinnaker Luxembourg S.A., Mr. Augusto Angioletti and Singings Consultadoria Economica e Marketing Lda, fully dealt with on page 121 of the Prospectus, aimed at regulating their mutual relationships and containing significant provisions in accordance with art. 122 of the Italian Consolidated Finance Act (T.U.F.).

**7.**

**FINANCIAL STATEMENTS AND MANAGEMENT REPORT**

The Board of Directors timely provided us with the financial statements and management report, which contain all of the information required by law.

The Company ended fiscal year 2005 with a loss of 3,123,097 Euro.

Net worth, inclusive of the fiscal year results, amounted to 45,427,110 Euro.

Information related to the most significant economic, fiscal and asset transactions regarding fiscal year 2005 and those subsequent to the year end, provided in the management report and clarified in the notes to the financial statements, was attentively examined by us.

As we have not been entrusted with the analytical audit on the merits of the financial statements contents, we audited its general framework and its compliance with current laws, and we found that it corresponds to the facts and information the Board of Statutory Auditors is already aware of following its participation in the meetings of the Company's internal bodies, the supervisory tasks performed and the information gathered from the Auditing Firm.

We were timely informed by the Auditing Firm on the results of the financial statements audits.

In accordance with art. 2426, par. 1, clause 5) of the Italian Civil Code, we agree with the financial statements entry of start-up costs as well as research, development and advertising costs.

## 8.

## CONCLUSIONS

The Board of Statutory Auditors has no proposals in accordance with art. 153, par. 2 of Legislative Decree 58/98 regarding what is set forth above, and expresses its favorable opinion to the approval of the financial statements and management report.

**THE BOARD OF STATUTORY AUDITORS**

Dott. Guido Mongelli

Dott. Maurizio Dattilo

Dott. Michele Saracino

Milan, 11 April 2006

*(This report has been translated into the English language solely for the convenience of international readers)*

# REPORT OF INDEPENDENT AUDITORS

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www.deloitte.it

## AUDITOR'S REPORT IN ACCORDANCE WITH ARTICLE 156 OF LEGISLATIVE DECREE N. 58 OF FEBRUARY 24, 1998

**To the Shareholders of**
**EUROFLY S.p.A.**

1. We have audited the financial statements of Eurofly S.p.A. as of and for the year ended December 31, 2005. These financial statements are the responsibility of the Directors of the Company. Our responsibility is to express an opinion on these financial statements based on our audit.

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

   For the opinion on the prior year's financial statements, which are presented for comparative purposes as required by law, reference should be made to our auditors' report dated April 15, 2005.

3. In our opinion, the financial statements present fairly the financial position of Eurofly S.p.A. as of December 31, 2005, and the results of its operations for the year then ended in accordance with the Italian regulations governing financial statements.

4. For a better understanding of the financial statements, we draw attention to the following information, already set forth in the report on operations and in the explanatory notes to the financial statements with reference to the commercial relationships with the client Teorema Tour S.p.A. and to the related impact of the Company's operations.

5. Pursuant to Article 2497-bis, first paragraph, of the Italian Civil Code, the Company has disclosed that it is subject to management and coordination by Spinnaker Luxembourg S.A. (already named Effe Luxembourg S.A.) and, therefore, has indicated in the notes to the financial statements the key financial data from the most recent financial statements of such company. Our opinion on the financial statements of Eurofly S.p.A. does not extend to such data.

DELOITTE & TOUCHE S.p.A.

*Signed by*
Ernesto Lanzillo
Partner

Milan, Italy
April 12, 2006

*(This report has been translated into the English language solely for the convenience of international readers)*