

# METALÚRGICA GERDAU S.A.

## BALANCE SHEET AT DECEMBER 31 (IN THOUSANDS OF REAIS)

### ASSETS

		Company		Consolidated	
		2005	2004	2005	2004
<b>CURRENT ASSETS</b>					
Cash and cash equivalents.....	note 5	49,312	95,800	5,395,463	2,003,945
Trade accounts receivable.....	note 6	-	-	2,101,137	2,564,192
Inventories.....	note 7	-	-	4,018,629	4,236,642
Tax credits.....	note 8	6,181	11,247	206,714	251,858
Deferred income tax and social contribution on net income.....	note 9	-	-	152,283	329,797
Dividends receivable.....	note 11	80,163	120,508	-	-
Other accounts receivable.....		1,969	3,801	303,942	267,058
Total current assets.....		<u>137,625</u>	<u>231,356</u>	<u>12,178,168</u>	<u>9,653,492</u>
<b>LONG-TERM RECEIVABLES</b>					
Related parties.....	note 21	-	-	171	1,231
Tax credits.....	note 8	-	-	242,792	69,992
Deposit for future investment in subsidiary.....	note 4	-	-	34,703	182,158
Deferred income tax and social contribution on net income.....	note 9	14,819	9,702	472,417	623,722
Judicial deposits and other.....	note 10	2,725	3,189	165,657	185,983
Total long-term receivables.....		<u>17,544</u>	<u>12,891</u>	<u>915,740</u>	<u>1,063,086</u>
<b>PERMANENT ASSETS</b>					
Investments.....	note 11	3,925,401	3,018,021	113,216	112,547
Fixed assets.....	note 12	1,448	1,593	8,694,958	7,928,973
Deferred charges.....	note 13	-	-	61,041	33,858
Total permanent assets.....		<u>3,926,849</u>	<u>3,019,614</u>	<u>8,869,215</u>	<u>8,075,378</u>
Total assets.....		<u>4,082,018</u>	<u>3,263,861</u>	<u>21,963,123</u>	<u>18,791,956</u>

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

### LIABILITIES AND SHAREHOLDERS' EQUITY

		Company		Consolidated	
		2005	2004	2005	2004
<b>CURRENT LIABILITIES</b>					
Suppliers.....		12	63	1,665,862	1,921,424
Loans.....	note 14	-	-	1,329,651	2,027,865
Debentures.....	note 15	-	-	2,719	2,986
Taxes and contributions payable.....	note 18	464	2,247	312,359	391,185
Related parties.....	note 21	137	266	-	-
Deferred income tax and social contribution on net income.....	note 9	-	-	86,879	180,166
Salaries payable.....		-	4,218	271,855	259,919
Dividends payable.....	note 24	85,082	158,374	209,683	338,972
Other accounts payable.....		13,582	10,630	324,466	222,741
Total current liabilities.....		<u>99,277</u>	<u>175,798</u>	<u>4,203,474</u>	<u>5,345,258</u>
<b>LONG-TERM LIABILITIES</b>					
Loans.....	note 14	-	-	5,352,420	3,490,374
Debentures.....	note 15	-	-	679,186	573,504
Provision for contingencies.....	note 20	664	664	192,858	240,964
Deferred income tax and social contribution on net income.....	note 9	86,619	85,540	613,920	699,119
Post-employment benefits.....	note 22	-	-	263,778	294,478
Other accounts payable.....	note 23	35,890	40,825	282,584	292,664
Total long-term liabilities.....		<u>123,173</u>	<u>127,029</u>	<u>7,384,746</u>	<u>5,591,103</u>
<b>MINORITY INTEREST</b>					
		-	-	6,515,335	4,894,561
<b>SHAREHOLDERS' EQUITY</b>					
Capital.....	note 24	2,496,000	1,664,000	2,496,000	1,664,000
Capital reserves.....		10,842	10,842	10,842	10,842
Revenue reserves.....		1,352,166	1,285,632	1,352,166	1,285,632
Retained earnings.....		560	560	560	560
Total shareholders' equity.....		<u>3,859,568</u>	<u>2,961,034</u>	<u>3,859,568</u>	<u>2,961,034</u>
<b>SHAREHOLDERS' EQUITY INCLUDING MINORITY INTEREST</b>					
		-	-	10,374,903	7,855,595
Total liabilities and shareholders' equity.....		<u>4,082,018</u>	<u>3,263,861</u>	<u>21,963,123</u>	<u>18,791,956</u>

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

**STATEMENT OF INCOME**  
**YEARS ENDED DECEMBER 31**  
 (IN THOUSANDS OF REAIS)

	Company		Consolidated	
	2005	2004	2005	2004
SALES REVENUES.....	-	-	25,485,818	23,407,573
Taxes on sales.....	-	-	(2,642,225)	(2,456,568)
Freight and discounts.....	-	-	(1,597,845)	(1,353,743)
<b>NET SALES REVENUES</b> ..... note 30	-	-	21,245,748	19,597,262
COST OF SALES.....	-	-	(15,519,861)	(13,352,238)
<b>GROSS PROFIT</b> .....	-	-	5,725,887	6,245,024
SELLING EXPENSES.....	-	-	(514,443)	(455,175)
FINANCIAL INCOME..... note 17	7,360	10,239	483,231	249,261
FINANCIAL EXPENSES..... note 17	(4,893)	(6,852)	(441,080)	(397,642)
GENERAL AND ADMINISTRATIVE EXPENSES				
Management fees.....	(2,248)	(3,168)	(34,624)	(50,654)
General expenses.....	(9,647)	(28,891)	(1,132,456)	(1,000,299)
EQUITY IN THE EARNINGS (LOSSES) OF SUBSIDIARIES..... note 11	1,281,519	1,342,842	(157,903)	(344,628)
OTHER OPERATING INCOME (EXPENSES), NET..... note 27	4,684	96	140,383	191,043
<b>OPERATING PROFIT</b> .....	1,276,775	1,314,266	4,068,995	4,436,930
NON-OPERATING INCOME (EXPENSES), NET..... note 28	-	170,953	304,738	144,102
PROFIT BEFORE TAXES AND PROFIT SHARING.....	1,276,775	1,485,219	4,373,733	4,581,032
PROVISION FOR INCOME TAX AND SOCIAL CONTRIBUTION ON NET INCOME..... note 9				
Current.....	(2,982)	(2,624)	(932,420)	(957,000)
Deferred.....	4,038	(42,352)	(142,882)	(238,405)
MANAGEMENT PROFIT SHARING..... note 25	(2,247)	(3,168)	(29,587)	(44,530)
<b>NET INCOME BEFORE MINORITY INTEREST</b> .....	1,275,584	1,437,075	3,268,844	3,341,097
MINORITY INTEREST.....			(1,993,260)	(1,904,022)
<b>NET INCOME FOR THE YEAR</b> .....			1,275,584	1,437,075
Net income per share - R\$.....	10.34	17.42		
Net equity per share - R\$.....	31.30	35.90		

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

**STATEMENT OF CHANGES IN FINANCIAL POSITION**  
**YEARS ENDED DECEMBER 31**  
 (IN THOUSANDS OF REAIS)

	Company		Consolidated	
	2005	2004	2005	2004
<b>FINANCIAL RESERVES WERE PROVIDED BY</b>				
Operations				
Net income for the year.....	1,275,584	1,437,075	3,268,844	3,341,097
Expenses/income not affecting working capital				
Depreciation and amortization.....	145	145	838,760	766,819
Cost of permanent asset disposals.....	-	79,158	38,332	360,816
Equity in the (earnings) losses of subsidiaries..... note 11	(1,281,519)	(1,342,842)	157,903	344,628
Gain on change in shareholding.....	-	(125,969)	(305,839)	-
Monetary and exchange variations on long-term liabilities.....	-	3,707	241,343	(131,822)
Monetary and exchange variations on long-term receivables.....	-	-	-	(526)
From operations.....	(5,790)	51,274	4,239,343	4,681,012
Third parties				
Capital increase/changes in treasury shares..... note 24	(12,992)	(14,441)	520,048	451,704
Contributions to capital reserve.....	-	32,666	29,785	16,246
Increase (decrease) of long-term liabilities.....	(3,855)	183	1,735,534	768,045
Net working capital of consolidated subsidiaries.....	-	-	22,965	-
Foreign exchange offset on working capital of foreign subsidiaries.....	-	-	(282,861)	(86,946)
Working capital - purchase of assets.....	-	-	111,818	669,445
Dividends not included in income for the year..... note 11	382,777	404,325	3,964	-
Total funds provided.....	360,140	474,007	6,380,596	6,499,506
<b>FINANCIAL RESERVES WERE USED FOR</b>				
Investments.....	8,638	3,214	64,313	41,619
Purchase of assets.....	-	-	-	924,457
Fixed assets.....	-	-	1,641,230	1,262,707
Deferred charges.....	-	-	27,905	18,654
Increase (reduction) of long-term receivables.....	4,653	(5,254)	27,453	(13,500)
Dividends/interest on own capital..... note 24	364,059	433,879	953,235	966,119
Total funds used.....	377,350	431,839	2,714,136	3,200,056
<b>INCREASE (DECREASE) IN WORKING CAPITAL</b> .....	(17,210)	42,168	3,666,460	3,299,450
Working capital				
At the beginning of the year.....	55,558	13,390	4,308,234	1,008,784
At the end of the year.....	38,348	55,558	7,974,694	4,308,234
<b>INCREASE (DECREASE) IN WORKING CAPITAL</b> .....	(17,210)	42,168	3,666,460	3,299,450

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

**STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY**  
**YEARS ENDED DECEMBER 31**  
 (IN THOUSANDS OF REAIS)

	Capital Reserves			Revenue Reserves			Total shareholders' equity
	Premium on shares	Others	Total	Investments and working capital	Legal	Total	
At December 31, 2003.....	1.280.000	1.973	10.659	572.937	107.940	680.877	1.972.096
Net income for the year.....	-	-	-	-	-	560	1.437.075
Capital increase.....	384.000	-	-	(384.000)	-	-	-
Investment subsidy.....	-	183	183	(14.441)	-	-	183
Treasury shares.....	-	-	-	(14.441)	-	(14.441)	(14.441)
Distributions proposed for the Annual General Meeting:							
Legal reserve.....	-	-	-	-	71.855	71.855	(71.855)
Reserve for investments and working capital.....	-	-	-	931.341	931.341	931.341	(931.341)
Dividend/interest on own capital.....	-	-	-	1.105.837	1.105.837	1.285.632	(433.879)
At December 31, 2004.....	1.664.000	2.156	10.842	1.105.837	179.795	1.285.632	2.961.034
Net income for the year.....	-	-	-	(832.000)	-	(832.000)	1.275.584
Capital increase.....	832.000	-	-	(12.991)	-	(12.991)	-
Treasury shares.....	-	-	-	-	-	-	-
Distributions proposed for the Annual General Meeting:							
Legal reserve.....	-	-	-	-	63.778	63.778	(63.778)
Reserve for investments and working capital.....	-	-	-	847.747	-	847.747	(847.747)
Dividend/interest on own capital.....	-	-	-	-	-	-	(364.059)
At December 31, 2005.....	2.496.000	2.156	10.842	1.108.599	243.573	1.352.166	3.859.568

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

**STATEMENTS OF CASH FLOWS**  
**YEARS ENDED DECEMBER 31**  
 (IN THOUSANDS OF REAIS)

	Company		Consolidated	
	2005	2004	2005	2004
Net income for the year.....	1.275.584	1.437.075	3.268.844	3.341.097
Equity in the (earnings) losses of subsidiaries.....	(1.281.519)	(1.342.842)	157.903	344.628
Provision for credit risks.....	-	-	(12.339)	7.647
Gain on disposal of fixed assets.....	-	-	10.642	9.058
Gain (loss) on disposal/merger of investments.....	-	(170.953)	(317.827)	(164.058)
Monetary and exchange variations (1).....	4.422	5.198	(77.587)	(94.087)
Depreciation and amortization.....	145	145	838.760	766.819
Income tax and social contribution on net income.....	(9.809)	47.393	43.656	505.551
Interest on loans.....	4	778	473.421	412.152
Contingencies/judicial deposits.....	(372)	(940)	(67.216)	4.351
Changes in trade accounts receivable.....	-	-	492.287	(720.363)
Changes in inventories.....	-	-	144.981	(1.402.408)
Changes in suppliers.....	(51)	58	(128.858)	477.292
Changes in operating activity accounts.....	1.233	(33.737)	134.564	(100.288)
Net cash provided by (used in) operating activities.....	(10.363)	(57.825)	4.961.231	3.387.391
Purchase/disposal of fixed assets.....	-	-	(1.641.230)	(1.173.491)
Increase in deferred charges.....	-	-	(27.905)	(18.006)
Acquisition/disposal of investments.....	(8.791)	155.144	(129.282)	362.905
Purchase of assets.....	-	-	-	(924.457)
Receipt of dividends/interest on own capital.....	434.156	351.884	-	-
Net cash provided by (used in) investing activities.....	425.365	507.028	(1.798.417)	(1.753.049)
Suppliers of fixed assets.....	-	-	(28.636)	144.573
Loans for working capital.....	(8.549)	(7.778)	1.175.121	(133.006)
Debentures.....	-	(586)	12.235	85.305
Receipt of loans for permanent assets.....	-	-	711.495	762.766
Payment of loans for permanent assets.....	-	-	(476.266)	(677.357)
Payment of loan interest.....	(4)	-	(426.284)	(379.801)
Loans with related parties.....	(129)	2.839	11.590	35.944
Capital increase/changes in treasury shares.....	(12.992)	(14.441)	520.048	451.704
Payment of dividend/interest on own capital and profit sharing.....	(439.816)	(358.623)	(1.102.601)	(853.710)
Net cash provided by (used in) financing activities.....	(461.490)	(378.589)	396.702	(563.582)
Increase (decrease) in cash and cash equivalents.....	(46.488)	70.614	3.559.516	1.070.760
Cash and cash equivalents				
At the beginning of the year.....	95.800	25.186	2.003.945	1.015.726
Changes in cash and cash equivalents opening balance.....	-	-	(210.426)	(82.541)
Opening balance of companies consolidated in the year.....	-	-	42.428	-
At the end of the year.....	49.312	95.800	5.395.463	2.003.945

<sup>(1)</sup> Includes gain and/or loss on swaps

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

## NOTES TO THE FINANCIAL STATEMENTS AT DECEMBER 31, 2005 AND 2004

(ALL AMOUNTS IN THOUSANDS OF REAIS UNLESS OTHERWISE INDICATED)

### 1 - OPERATIONS

Metalúrgica Gerdau S.A., with Head Office in the city of Porto Alegre, Brazil, is a holding company in the Gerdau Group, which is principally dedicated to the production of common and special steel rods and sale of general steel products (plates and rods), in plants located in Brazil, Uruguay, Chile, Canada, Colombia, Argentina and the United States of America.

The Gerdau Group has an installed capacity of 16.5 million tons of crude steel per year, producing steel in electrical furnaces from scrap and pig iron purchased, for the most part, in the region near each plant (mini-mill concept). Gerdau also operates plants which are capable of producing steel from iron ore (through blast furnaces and direct reduction) and has a unit used exclusively to produce special steels. It is the largest scrap recycling group in Latin America and is among the largest in the world.

The industrial sector is the most important market, including manufacturers of consumer goods such as vehicles and household and commercial equipment that basically use profiled steel in various available specifications. The next most important market is the civil construction sector, which demands a high volume of bars and wires for concrete. There are also numerous customers for nails, staples and wires, commonly used in the agribusiness sector.

### 2 - PRESENTATION OF THE FINANCIAL STATEMENTS

The financial statements have been prepared and are presented in accordance with accounting practices adopted in Brazil, which are based on the provisions of Brazilian Corporate Law, together with the rules established by the Brazilian Securities Commission (CVM).

### 3 - SIGNIFICANT ACCOUNTING PRACTICES

**a) Cash and cash equivalents** - financial investments are recorded at cost plus income accrued up to the balance sheet date, applying the interest rates agreed with the financial institutions, and do not exceed market value;

**b) Trade accounts receivable** - are stated at realizable values, and accounts receivable from foreign customers are adjusted based on the exchange rates effective at the balance sheet date. The provision for credit risks is calculated based on a credit risk analysis, which includes the history of losses, the individual situation of each customer and the economic group to which it belongs, the collateral and guarantees and the legal advisors' opinion, and is considered sufficient to cover any losses on realization;

**c) Inventories** - are stated at the lower of market value and average production or purchase cost;

**d) Investments** - are recorded on the equity method of accounting and the equity in the earnings or loss is recorded in an income statement account. Capital gains or losses resulting from changes in the percentage ownership in subsidiaries are recorded as non-operating income or loss.

**e) Fixed assets** - are recorded at cost, net of depreciation. Depreciation is calculated on the straight-line basis at the rates stated in Note 12, which take into consideration the estimated useful lives of the assets. Interest on loans obtained to finance construction in progress is added to the cost of the constructions;

**f) Deferred charges** - amortization is calculated on the straight-line basis at rates determined based on the production of the implemented projects in relation to their installed capacities;

**g) Loans** - are stated at the contract value plus the contracted charges, including interest and monetary or foreign exchange variations. Swap contracts, which are linked to the loan agreements, are classified together with the related loans;

**h) Income tax and social contribution on net income** - current and deferred income tax and social contribution on net income are calculated in conformity with current legislation;

**i) Post-employment benefits** - the actuarial liabilities relating to the pension benefits and retirement plans and actuarial liabilities relating to the healthcare plan are provided according to procedures established by the CVM Deliberation 317/00, on the basis of an actuarial calculation made every year by an independent actuary, using the projected unit credit method, net of the assets that guarantee the plan, when applicable, and the costs associated to the increase of the present value of the liabilities resulting from the service rendered by the employee, is recognized over the employees' working lives.

The projected unit credit method considers each period of service as the generating factor of an additional unit of benefit, which are accumulated to calculate the total liabilities. Other actuarial assumptions are also used, such as estimates of the increase of healthcare costs, biological and economic hypotheses and, also, the historical experience of costs incurred and the employee contributions.

**j) Other current and long-term assets and liabilities** - are recorded at their realizable amounts (assets) and at their known or estimated amounts plus accrued charges and indexation adjustments (liabilities), when applicable;

**k) Related parties** - loan agreements between Brazilian companies are restated by the weighted average interest rate for market funding. The agreements with foreign companies are restated by charges (LIBOR plus 3% p.a.) plus foreign exchange variation. Sales and purchases of inputs and products are made under terms and conditions similar to those of unrelated third parties;

**l) Determination of the results of operations** - the results of operations are determined on the accrual basis of accounting;

**m) Use of estimates** - the preparation of financial statements requires estimates to record certain assets, liabilities and other transactions. The financial statements therefore include various estimates related to the useful lives of fixed assets, provisions for contingent liabilities, for income taxes and other similar matters. Actual results may differ from those estimated;

**n) Environmental investments** - expenses related to compliance with environmental regulations are considered as cost of production or capitalized when incurred;

**o) Translation of foreign currency balances** - asset and liability balances of transactions in foreign currency are translated to local currency (R\$) at the foreign exchange rate effective at the balance sheet date and at the quarterly average rate for income statement accounts;

**p) Additional information to the financial statements** - the statement of cash flows is being presented, prepared in accordance with the Accounting Rule and Procedure - NPC 20 issued by the Institute of Independent Auditors of Brazil (IBRACON), in order to provide additional information.

#### 4 – CONSOLIDATED FINANCIAL STATEMENTS

a) The consolidated financial statements at December 31, 2005 and 2004 were prepared in accordance with accounting practices adopted in Brazil, based on the provisions of Corporate Law and the regulations issued by the Brazilian Securities Commission. They include the financial statements of Metalúrgica Gerdau S.A. and its directly or indirectly controlled subsidiaries listed below:

Consolidated company	Percentage Consolidation	Shareholders' equity	Percentage ownership	
			Total capital	Voting capital
Gerdau S.A.	100	8,042,186	44.81	75.73
Gerdau Ameristeel Corporation e subsidiaries (*)	100	3,747,086	66.78	66.78
Gerdau Internacional Empreendimentos Ltda. - Grupo Gerdau	100	3,229,356	100.00	100.00
Gerdau GTL Spain S.L.	100	3,227,984	100.00	100.00
Gerdau Açominas S.A.	100	3,094,596	89.55	89.56
Gerdau Aços Longos S.A.	100	2,494,218	89.55	89.56
Gerdau Steel Inc.	100	2,245,575	100.00	100.00
Gerdau América do Sul Participações S.A.	100	736,422	90.64	90.65
Axol S.A.	100	591,809	100.00	100.00
Gerdau Chile Inversiones Ltda.	100	585,644	99.99	99.99
Indústria Del Acero S.A. - Indac	100	585,501	99.98	99.98
Santa Felicidade Com. Imp. e Exp. de Produtos Siderúrgicos Ltda.	100	579,602	100.00	100.00
Gerdau Comercial de Aços S.A.	100	530,031	89.55	89.56
Gerdau Aza S.A.	100	487,953	100.00	100.00
Gerdau Aços Especiais S.A.	100	447,912	89.55	89.56
Diaco S.A. e subsidiaries (**)	100	276,382	57.11	57.11
Seiva S.A. - Florestas e Indústrias	100	237,380	97.06	99.73
Itaguaí Com. Imp. e Exp. Ltda.	100	224,654	100.00	100.00
Aramac S.A.	100	142,328	100.00	100.00
GTL Equity Investments Corp.	100	142,267	100.00	100.00
Sipar Aceros S.A.	100	95,356	89.50	88.87
Sipar Gerdau Inversiones S.A.	100	84,754	83.77	83.77
Margusa - Maranhão Gusa S.A.	100	83,978	100.00	100.00
Gerdau Laisa S.A.	100	71,815	99.90	99.90
Banco Gerdau S.A.	100	40,540	99.00	99.00
Açominas Com. Imp. Exp. S.A. - Açotrading	100	22,565	100.00	100.00
Salomon Sack S.A.	100	22,043	99.00	99.00
Gerdau Açominas Overseas Ltd.	100	16,016	100.00	100.00
Siderúrgica Del Pacifico S.A.	100	13,524	100.00	100.00
Distribuidora Matco S.A.	100	12,281	99.00	99.00
Armacero Industrial y Comercial S.A.	100	10,566	50.00	50.00
Aceros Cox Comercial S.A.	100	10,293	99.00	99.00
Siderco S.A.	100	7,223	100.00	100.00
Florestal Itacambira S.A.	50	6,624	100.00	100.00
GTL Financial Corp.	100	4,349	100.00	100.00
Gerdau Hungria Holdings Limited Liability Company	100	367	100.00	100.00
GTL Trade Finance Inc.	100	23	100.00	100.00
Dona Francisca Energética S.A.	52	(4,753)	51.82	51.82

(\*) Subsidiaries: Gerdau Ameristeel MRM Special Sections Inc., Gerdau USA Inc., AmeriSteel Bright Bar Inc., Gerdau AmeriSteel US Inc., Gerdau Ameristeel Perth Amboy Inc., Gallatin Steel Company (50%) and Gerdau Ameristeel Sayreville Inc.

(\*\*) Subsidiaries: Ferrer Ind. Corporation, Laminados Andinos S.A., Laminadora Diaco S.A. and Ferrofigurados Lasa S.A. (55%).

b) The more significant accounting practices used in preparing the consolidated financial statements are as follows:

i) Metalúrgica Gerdau S.A. and its subsidiaries adopt consistent practices to record their transactions and value their

assets and liabilities. The financial statements of foreign subsidiaries were translated using the exchange rate in effect at the balance sheet date and were adjusted to conform with accounting practices adopted in Brazil. The income statement accounts were translated by the average exchange rate every quarter;

ii) Asset, liability and income statement balances arising from transactions between consolidated companies have been eliminated; and

iii) Holdings of minority shareholders in subsidiaries are shown separately.

c) The following transactions occurred during the year ended December 31, 2005:

i) As part of the corporate reorganization of the Gerdau companies, the Extraordinary General Meeting of shareholders' the subsidiary Gerdau Açominas S.A. held on May 9, 2005 approved the merger of Gerdau Participações S.A. The shareholders' equity, adjusted in accordance with CVM Instruction No. 349/01, corresponding to the assets and liabilities transferred to Gerdau Açominas S.A., was R\$ 1,224,646 comprised as follows:

#### ASSETS

CURRENT ASSETS	550,136
PERMANENT ASSETS	
Investments	
Gerdau Internacional Empreendimentos Ltda. - 22.8%	673,401
Other Investments	1,195
Total permanent assets	674,596
Total assets	1,224,732

#### LIABILITIES

LONG-TERM LIABILITIES	86
Total liabilities	86
TOTAL ADJUSTED NET ASSETS (*)	1,224,646

(\*) The merged net assets are adjusted the investment held by Gerdau Participações S.A. in Gerdau Açominas S.A.

ii) Up to July 28, 2005, Gerdau Açominas S.A. was the company that carried out the steel operations in Brazil, in addition to holding 22.8% of the capital of Gerdau Internacional Empreendimentos Ltda. On July 29, 2005, certain assets and liabilities of Gerdau Açominas S.A. were spun off into four new companies: Gerdau Aços Longos S.A., Gerdau Aços Especiais S.A., Gerdau Comercial de Aços S.A. and Gerdau América do Sul Participações S.A. As a result, these assets and liabilities were grouped in separate companies in accordance with the lines of business of each company, as follows:

Company	Business
Gerdau Açominas S.A.	Production of steel at the Ouro Branco plant
Gerdau Aços Longos S.A.	Production of long steel at the other plants in Brazil
Gerdau Aços Especiais S.A.	Production of special steel in Brazil
Gerdau Comercial de Aços S.A.	Distribution of steel products in Brazil
Gerdau América do Sul Participações S.A.	Investment in 22.8% of the capital of Gerdau Internacional Empreendimentos Ltda.

The assets and liabilities of Gerdau Açominas S.A. that were spun off into other companies are still recorded at their original purchase/formation cost, and no gain or loss arose as a result of this transaction.

III) On September 15, 2005, the Gerdau Group signed an agreement for the acquisition of 35.98% of the shares issued by Sipar Aceros S.A., a steel rod rolling mill located in Province of Santa Fé, Argentina. This investment, when added to the 38.46% already owned by Gerdau, represents 74.44% of the share capital of Sipar Aceros. The disbursement for this additional investment will be R\$ 94,800 (equivalent to US\$ 40.5 million) payable over the next three years. Goodwill of R\$ 59,367 arose on this acquisition, based on expected future profitability, to be amortized in 10 years. Also, as a result of this acquisition, Sipar Aceros S.A. is being fully included in the consolidated financial statements as from September 30, 2005.

Shareholders of Sipar Aceros S.A., holders of approximately 14.4% of its capital, have the right of sale of this investment to the Gerdau Group (sale option) for a period of up to two years, as from September 2005, and for a fixed price subject to restatement.

IV) On September 30, 2005, in continuity of the agreement with the Mayaguez Group and with The Latinamerican Enterprise Steel Holding, the Gerdau Group completed the acquisition of a 57.11% holding in Diaco S.A., the largest manufacturer of steel and rods in Colombia, for R\$ 124,367, paid through an advance made in 2004. A negative goodwill of R\$ 27,469 was recorded on the transaction, as a result of the overvaluation of Diaco S.A.'s fixed assets, to be amortized proportionally to the depreciation of the assets that originated the negative goodwill, over an estimated period of 10 years.

In accordance with the agreement, the Gerdau Group must purchase in up to 8 years, 40.27% of the capital of Diaco S.A. still in possession of the Mayaguez Group, for US\$ 51,795 thousand (equivalent to R\$ 121,236 at December 31, 2005), restated as defined in the agreement. Also, in view of this purchase, an advance was made to the vendors of US\$ 14,825 thousand (equivalent to R\$ 34,703 at December 31, 2005) recorded in long-term receivables as a deposit for future investment in subsidiary.

V) On November 15, 2005, the Gerdau Group signed, together with two Spanish companies, a contract for the purchase of all the shares of Corporación Sidenor, S.A. (Sidenor), located in Spain.

The ownership of the capital of Corporación Sidenor, S.A. will be as follows: 40% will belong to Gerdau Hungria Holdings Limited Liability Company, 40% to Carpe Diem Salud, SL, (Carpe Diem), a company of the Santander Group, and 20% to Bogey Holding Company Spain, S.L., a holding company of the Sidenor executives.

The contracted value for the purchase of all the shares is € 443,820 thousand (equivalent to R\$ 1,228,960 at December 31, 2005) plus a variable portion to be calculated in the future, estimated at € 19,500 thousand (equivalent to R\$ 53,996 at December 31, 2005), to be paid by Gerdau Hungria Holdings Limited Liability Company. Each shareholder will pay the amount corresponding to its investment from its own funds.

Carpe Diem has the right to sell its investment in Sidenor to the Gerdau Group after a 5-year period (sale option), for a fixed price subject to restatement. When and if Carpe Diem exercises this option, Gerdau shall have the right, if it sees fit, to indicate a third party to purchase this investment.

Corporación Sidenor, S.A. is a holding company that controls Sidenor Industrial, S.L., the largest manufacturer of special steel rods and forged and cast parts in Spain, as well as one of the major manufacturers in Spain of die forged products.

Sidenor Industrial has three steel production units, located in Basauri, Vitoria and Reinosa. In 2004, the company sold 688 thousand tons of finished products. Sidenor Industrial also has the subsidiary Forjanor, S.L. for the production of forged steel for die forging, with plants in Madrid and Elgeta. In 2004, Forjanor sold 25 thousand tons of products. Corporación

Sidenor, S.A., in Brazil, by means of its subsidiary Sidenor International, S.L., has a 58,44% interest in the capital of Aços Villares S.A., producer of special steel rods and rolling cylinders, with units in Mogi das Cruzes, Pindamonhangaba and Sorocaba, all of them in the state of São Paulo, having sold 646 thousand tons of finished products in 2004.

This transaction was completed in January 2006 when the shares were transferred to the buyers. The financial statements of Corporación Sidenor S.A. and its subsidiaries will be included in the consolidated financial statements of the Gerdau Group (proportional consolidation) as from that date.

VI) On December 19, 2005, the Gerdau Group completed the purchase of 97.01% of the capital of Siderúrgica del Pacífico S.A. - Sidelpa, the only special steel producer in Colombia. This transaction resulted in a negative goodwill of R\$ 30,605 as a result of the overvaluation of Sidelpa's fixed assets, to be amortized proportionally to the depreciation of the assets that originated the negative goodwill, over an estimated period of 10 years.

d) The consolidated financial statements also include the financial statements of the jointly-owned subsidiary Dona Francisca Energética S.A. consolidated proportionally to the direct interest, and of the jointly-owned subsidiaries Armacero Industrial y Comercial Ltda. and Gallatin Steel Company, proportionally to the indirect interest of the parent company in the capital of the subsidiaries. As a result of the increased investment in Sipar Aceros S.A. as stated in c) III) above, the results of operations of this company, up to September 30, 2005, were consolidated proportionally to the interest previously held.

The principal financial statement balances of these companies, on which the corresponding consolidation percentage is applied, are as follows:

	Dona Francisca Energética S.A.		Gallatin Steel Company		Sipar Aceros S.A. Consolidated (*)		Armacero Ind. Com. Ltda. (**)
	2005	2004	2005	2004	2005	2004	2005
<b>Assets</b>							
Current assets.....	135,777	116,627	412,954	586,106	-	144,251	29,952
Long-term receivables.....	122,618	128,427	454	-	-	-	1,437
Permanent assets.....	172,664	180,984	513,296	612,762	-	18,929	37,816
Total assets.....	<u>431,059</u>	<u>426,038</u>	<u>926,704</u>	<u>1,198,868</u>	<u>-</u>	<u>163,180</u>	<u>69,205</u>
<b>Liabilities</b>							
Current liabilities.....	40,817	29,381	140,664	131,580	-	80,787	27,348
Long-term liabilities.....	394,995	413,006	47,512	54,190	-	4,356	20,725
Shareholder's equity.....	(4,753)	(16,349)	738,528	1,013,098	-	78,037	21,132
Total liabilities and equity.....	<u>431,059</u>	<u>426,038</u>	<u>926,704</u>	<u>1,198,868</u>	<u>-</u>	<u>163,180</u>	<u>69,205</u>
<b>Income statement</b>							
Net sales revenues.....	46,326	42,780	1,948,736	2,372,850	284,120	350,605	87,437
Cost of sales.....	(19,647)	(19,424)	(1,456,182)	(1,626,650)	(220,105)	(285,566)	(80,761)
Gross profit.....	26,679	23,356	492,554	746,200	64,015	65,039	6,676
General, administrative and selling expenses.....	(1,739)	(2,110)	(25,832)	(51,234)	(25,040)	(24,863)	(5,365)
Other financial income (expenses).....	(7,506)	(17,882)	(86,095)	(14,030)	(4,801)	(8,101)	(17)
Other operating income (expenses), net..	-	-	-	-	(71)	(76)	695
Operating profit (loss).....	17,434	3,364	380,627	680,936	34,103	31,999	1,989
Non-operating income, net.....	4	380	-	10,225	236	759	-
Provision for income tax and social contribution on net income.....	(5,841)	(1,249)	(237)	(797)	(11,290)	(10,188)	(366)
Net income for de year.....	<u>11,597</u>	<u>2,495</u>	<u>380,390</u>	<u>690,364</u>	<u>23,049</u>	<u>22,570</u>	<u>1,623</u>

(\*) Includes the subsidiary Siderco S.A.

(\*\*) Company included in the consolidation in 2005.

e) The Company and its direct and indirect subsidiaries have goodwill and negative goodwill, which are amortized as the assets that generated them are realized or based on the realization of the projected future profits, limited to ten years, as follows:

	Amortization period	Consolidated
<b>Goodwill included in the investment accounts</b>		
Balance at December 31, 2004 (based on projected future profitability).....		52,854
(+) Foreign exchange adjustment.....		2,774
(+) Sipar Aceros S.A (Note 4c - III).....		59,367
(-) Amortization during the year .....	10 years	(23,341)
Balance at December 31, 2005 (based on projected future profitability).....		91,654
Analysis of the goodwill by subsidiary		
Margusa - Maranhão Gusa S.A. ....		8,242
Dona Francisca Energética S.A.....		17,074
Distribuidora Matco S.A. ....		5,368
Sipar Aceros S.A. (Note 4c - III).....		60,970
		91,654

	Amortization period	Consolidated
<b>Goodwill included in the fixed asset accounts</b>		
Balance at December 31, 2004 (based on undervaluation of assets).....		144,959
(-) Foreign exchange adjustment.....		(17,131)
(-) Amortization during the year .....	10 years	(20,315)
Balance at December 31, 2005 (based on undervaluation of assets).....		107,513
The goodwill resulted from the assets of the subsidiary Gerdau Ameristeel US Inc.		
<b>Negative goodwill included in the fixed asset accounts</b>		
Balance at December 31, 2004 (based on undervaluation of assets).....		(243,277)
(-) Foreign exchange adjustment.....	10 years	26,897
(+) Diaco S.A. (Note 4c - IV).....		(27,469)
(+) Siderúrgica del Pacífico S.A. (Note 4c - VI).....		(30,605)
Balance at December 31, 2005.....		(274,454)

The negative goodwill at December 31, 2004 mainly resulted from the assets of the subsidiary Gerdau Açominas S.A..

The goodwills based on future profitability were supported by projections of profits of each subsidiary, calculated on the discounted cash flow method and at an average interest rate equivalent to the TJLP (Long-term Interest Rate), for a period of 10 years.

The equity accounting loss in the consolidated statement of income refers, basically, to the effects of foreign exchange rate variations on the foreign investments, to goodwill amortization and the tax incentive reserves arising from the reduction of income tax on the exploitation profit of the subsidiaries Gerdau Açominas S.A. and Margusa - Maranhão Gusa S.A., both located in the Northeastern region of Brazil, as well as to benefits arising from state tax financing.

## 5 - CASH AND CASH EQUIVALENTS

	Company		Consolidated	
	2005	2004	2005	2004
Cash .....	10	98	273,285	337,767
Financial investment fund.....	2,743	-	3,328,902	527,102
Fixed income securities.....	46,559	95,702	1,736,105	1,101,388
Equities .....	-	-	57,171	37,688
	49,312	95,800	5,395,463	2,003,945

The financial investments are, basically, in federal public securities and bank certificates of deposit (CDB) at market prices and rates, and are adjusted according to the income accrued proportionally up to the financial statement date, not exceeding their respective market values.

Of the existing balance, R\$ 2,238,294 - Consolidated (R\$ 1,004,550 - Consolidated in 2004), refer to investments in foreign currency, principally in U.S. dollars.

## 6 - TRADE ACCOUNTS RECEIVABLE

	Consolidated	
	2005	2004
Customers in Brazil.....	799,831	880,557
Brazilian export receivables.....	160,157	543,954
Receivables from customers of foreign subsidiaries.....	1,223,317	1,232,095
Provision for credit risks .....	(82,168)	(92,414)
	2,101,137	2,564,192

## 7 - INVENTORIES

	Consolidated	
	2005	2004
Finished products.....	1,656,123	1,728,652
Products in progress.....	585,014	679,167
Raw materials .....	977,800	1,112,467
Storeroom material.....	723,301	649,892
Advances to suppliers.....	76,391	66,464
	4,018,629	4,236,642

The inventories are insured against fire and overflow. Cover is determined based on the amounts and the risks involved.





## 12 - FIXED ASSETS

	Annual depreciation/ depletion rate %	Consolidated			
		Cost	Accumulated depreciation and depletion	2005	2004
				Net	Net
Land, buildings and structures.....	0 a 4	4,919	(3,471)	1,448	1,593
		<u>4,919</u>	<u>(3,471)</u>	<u>1,448</u>	<u>1,593</u>

	Annual depreciation/ depletion rate %	Consolidated			
		Cost	Accumulated depreciation and depletion	2005	2004
				Net	Net
Land, buildings and structures.....	0 a 10	3,466,847	(1,190,478)	2,276,369	2,232,444
Machinery, equipment and installations.....	5 a 10	8,599,988	(4,467,396)	4,132,592	4,326,483
Furniture and fixtures.....	5 a 10	135,078	(76,851)	58,227	40,797
Vehicles.....	20 a 33	69,152	(35,095)	34,057	10,566
Electronic data equipment/rights/licences.....	20 a 33	332,139	(221,927)	110,212	96,724
Construction in progress.....	-	1,889,512	-	1,889,512	1,065,583
Forestation/reforestation.....	Felling plan	250,528	(56,539)	193,989	156,376
		<u>14,743,244</u>	<u>(6,048,286)</u>	<u>8,694,958</u>	<u>7,928,973</u>

a) **Insured amounts** - the assets are insured against fire, electrical damage and explosion. The cover is based on the amounts and risks involved. The plants of the North and South American subsidiaries and the subsidiary Gerdau Açominas S.A. are also insured against loss of profits. The total cover amounts to R\$ 18,548,459 at December 31, 2005.

b) **Capitalization of interest and financial charges** - financial income was credited during 2005 totaling R\$ 10,070 - Consolidated (R\$ 2,021 - Consolidated in 2004) as a result of the appreciation of the Brazilian real against the U.S. dollar.

c) **Guarantees offered** - fixed assets were pledged as collateral for loans of R\$ 837,996 - Consolidated (R\$ 688,034 - Consolidated in 2004).

d) **Summary of changes in fixed assets:**

	Company		Consolidated	
	2005	2004	2005	2004
Balance at the beginning of the year.....	1,593	1,738	7,928,973	7,380,838
( + ) Purchases/sales for the year.....	-	-	1,698,794	1,167,022
( - ) Depreciation and depletion in cost of sales.....	-	-	(756,386)	(692,609)
( - ) Depreciation and depletion in administrative expenses.....	(145)	(145)	(82,374)	(69,594)
( + ) Companies consolidated in the year.....	-	-	252,280	-
( + ) Purchase of North Star and others.....	-	-	-	267,948
( - ) Foreign exchange rate effect on fixed assets of foreign subsidiaries.....	-	-	(346,329)	(124,632)
Balance at end of the year.....	<u>1,448</u>	<u>1,593</u>	<u>8,694,958</u>	<u>7,928,973</u>

## 13 - DEFERRED CHARGES

The deferred charges (Consolidated) comprise pre-operating expenses in the construction of a hydroelectric plant, reforestation projects and research, development and reorganization projects.

## 14 - LOANS

	Annual Current loans stated in reais charges (*)	Consolidated	
		2005	2004
<b>Current loans stated in reais</b>			
Working capital.....	CDI (**)	20,903	60,197
Investment.....		-	4,500
Fixed assets financing.....		-	446
<b>Current loans stated in foreign currency</b>			
Working capital (US\$).....	5.26%	592,887	1,174,094
Fixed assets and others (US\$).....	7.90%	34,676	1,387
Export advances (US\$).....	2.88%	3,082	43,891
Working capital (Cip\$).....	5.38%	50,133	31,905
Working capital (Cop\$).....	7.00%	11,810	-
Working capital (PA\$).....	8.27%	4,880	19,956
		<u>718,371</u>	<u>1,336,376</u>
Plus: current portion of long-term loans.....		611,280	691,489
Current loans.....		<u>1,329,651</u>	<u>2,027,865</u>
<b>Long-term loans in reais</b>			
Working capital.....	TJLP + 3,50%	124,125	52,625
Fixed assets.....	TJLP + 3,50%	812,691	619,668
Investment.....	IGP - M + 8,50%	22,510	42,686
<b>Long-term loans in foreign currency</b>			
Working capital (US\$).....	7.70%	226,104	167,795
Bearer Bonds (Perpetual Bonds and Senior Notes) (US\$).....	9.48%	2,337,845	1,056,486
Açominas Export Notes (US\$).....	7.34%	543,739	627,908
Export advances (US\$).....	2.88%	761,896	778,258
Investments (US\$).....	4.04%	162,945	182,943
Fixed assets and others.....	4.30%	844,318	605,092
Fixed assets (Cdn\$).....	5.25%	5,606	3,485
Working capital (Cip\$).....	5.38%	19,495	16,254
Fixed assets (Cip\$).....		-	27,000
Working capital (Cop\$).....	11.22%	102,300	-
Working capital (PA\$).....	8.27%	126	1,663
		<u>5,963,700</u>	<u>4,181,863</u>
Minus: current portion.....		(611,280)	(691,489)
Long-term loans.....		<u>5,352,420</u>	<u>3,490,374</u>
Total loans.....		<u>6,682,071</u>	<u>5,518,239</u>

(\*) Weighted average rate at December 31, 2005.

(\*\*) CDI - Interbank Deposit Certificate interest rate.

The loans stated in reais are indexed by the TJLP (Long-term Interest Rate), established by the Brazilian Government and used for restatement of long-term loans granted by BNDES (National Bank for Economic and Social Development), determined quarterly, or by the IGP-M (General Price Index - Market): Brazilian inflation rate, calculated by the Getúlio Vargas Foundation).

Summary of loans by currency:

	Consolidated	
	2005	2004
Real (R\$).....	980,229	780,121
American dollar (US\$).....	5,507,492	4,637,855
Canadian dollar (Cdn\$).....	5,606	3,485
Colombian peso (Cip\$).....	114,110	-
Argentinean peso (PA\$).....	5,006	21,619
Chilean peso (Clp\$).....	69,628	75,159
	<u>6,682,071</u>	<u>5,518,239</u>

Maturity of long-term loans:

	Consolidated
2007.....	803,329
2008.....	823,083
2009.....	539,881
2010.....	379,590
2011.....	1,126,736
After 2011.....	1,679,801
	<u>5,352,420</u>

#### a) Events during the year

**I)** Gerdau S.A. concluded the private issue of Guaranteed Perpetual Notes (Notes) on September 15, 2005 in the total amount of US\$ 600 million with annual interest of 8.875%. These Notes are guaranteed by the Brazilian operating companies Gerdau Açominas S.A., Gerdau Aços Longos S.A., Gerdau Aços Especiais S.A. and Gerdau Comercial de Aços S.A. The Notes have no maturity but may become due in certain specific circumstances (as defined in the terms of the Notes), which are not under total control of the Company. The Company has the option of redeeming these Notes after 5 years of their issue, the first option for redemption therefore being in September 2010. Interest is payable quarterly and each quarterly payment date after September 2010 is also a redemption option date.

**II)** The third issue of Euro commercial paper was concluded on December 12, 2005 in the amount of US\$ 200 million, with final maturity on October 11, 2006 and interest of 5.0% p.a..

#### b) Guarantees

The loans contracted under the FINAME/BNDES program (financing for the purchase of machinery and equipment through the BNDES) are guaranteed by the financed assets, in the amount of R\$ 469,708. The other loans are guaranteed by the controlling companies, on which the Company pays a fee of 1% p.a. on the amount guaranteed.

#### c) Covenants

In replacement of the tangible guarantees usually required, the loans are being contracted with certain financial covenants, as follows:

**I)** *Consolidated interest coverage ratio* - measures the debt service payment capacity in relation to EBITDA (Earnings before Interest, Taxes, Depreciation and Amortization), as described in Note 28;

**II)** *Consolidated leverage ratio* - measures the debt coverage capacity in relation to EBITDA, as described in Note 28;

**III)** *Required Minimum Net Worth* - measures the minimum net worth required in financial agreements; and

**IV)** *Current Ratio (current liquidity ratio)* - measures the capacity to pay current liabilities.

All the covenants mentioned above are calculated on a consolidated basis, except for item IV which refers to the parent company Metalúrgica Gerdau S.A., and have been complied with. The penalty for non-compliance is the prepayment of the contracts.

#### d) Credit lines

In October 2005, the subsidiaries Gerdau Açominas S.A., Gerdau Aços Longos S.A., Gerdau Aços Especiais S.A. and Gerdau Comercial de Aços S.A. obtained a pre-approved credit line from BNDES - National Bank for Economic and Social Development of R\$ 900,000 for the purchase of equipment and for expenses. These funds will be provided as the subsidiaries carry out their own investment plans and submit proof of expenditures to BNDES. At December 31, 2005, this line had not yet been used and the applicable interest rates will be the ones in force on the dates the funds are released. The contracts are guaranteed by Indac - Ind. Adm. e Comércio S.A. and by financial covenants offered by Metalúrgica Gerdau S.A.

The subsidiary Gerdau Açominas S.A. also has the following credit lines:

- US\$ 240 million (R\$ 561,768 at December 31, 2005) from ABN AMRO Bank N.V., The Bank of Tokyo-Mitsubishi and UFJ Bank Limited, whose guarantee was given by Nippon Export and Investment Insurance (NEXI), with a term of seven years, of which two are the grace period and the remaining five for payment. At December 31, 2005, US\$ 32,7 million (R\$ 76,541) of this credit line had been drawn down. The funds will be used for the modernization of the Ouro Branco plant and there is no relation to imports or export receivables.

- US\$ 69 million (R\$ 161,508 at December 31, 2005) from Export Development Canada, whose guarantee was given by KFW IPEX - Bank and by Gerdau S.A., with a term of six years, of which two are the grace period and the remaining four for payment. At December 31, 2005, US\$ 33.66 million (R\$ 78,788) of this credit line had been drawn down. The interest rate is 7.02 % per year. The funds will be applied in the supply of blooms continuous casting and beam blank.

- US\$ 50 million (R\$ 117,035 at December 31, 2005) from BNP Paribas Brasil, whose guarantee was given by Gerdau S. A., with a term of five years, of which three are the grace period and the remaining two for payment. At December 31, 2005, US\$ 50 million of this credit line had been drawn down. The interest rate is 5.93% p.a. The funds will be used to finance 15% of the supply plus the Credit Insurance of the blast furnace, coking mill and sintering facilities.

- US\$ 201 million (R\$ 470,480 at December 31, 2005) from BNP Paribas - France (50%) and the Industrial and Commercial Bank of China (50%), whose guarantee was given by SINOSURE (China Export & Credit Insurance Corporation), credit agency for Chinese exports, and by Gerdau S. A., with a term of 12 years, for which three are the grace period and the remaining nine for payment. At December 31, 2005, there had been no use of funds from this credit line. The interest rate is 6.97% p.a. The funds will be used to finance 85% of the supply for the blast furnace, coking mill and sintering facilities.

The North American subsidiaries have a credit line in the amount of US\$ 650 million, equivalent to R\$ 1,521,455 at December 31, 2005, falling due in October 2010, which can be drawn in U.S. dollars (at the LIBOR rate plus interest of between 2.25% and 2.75% p.a. or US Prime/FED Funds plus interest of 0.5% p.a.) or in Canadian dollars (at the Bankers Acceptance (BA) rate plus interest of between 2.35% and 2.85% p.a., or Canadian Prime plus interest of 1.00% p.a.). The distribution of this credit line among the companies is made in proportion to the working capital of each North American subsidiary. This credit line had not been used up to December 31, 2005. The inventories and accounts receivable of subsidiaries were given as guarantee for this credit line.

The subsidiary Gerdau Aza S.A. has a line of credit for working capital of Clp\$ 40.9 billion (R\$ 186,388 at December 31, 2005), bearing interest of 3.60% p.a., and a credit line for fixed assets of Clp\$ 146 million (R\$ 674 at December 31, 2005) bearing interest of 6.12% p.a. This line was not being used at December 31, 2005.

## 15 - DEBENTURES

Issue	General Meeting	Number		Maturity	Annual rate	2005		2004	
		Issued	In portfolio						
Gerdau S.A.									
3ª - A e B.....	05/27/1982	144,000	60,250	06/01/2011	CDI	160,315	156,387		
7ª.....	07/14/1982	68,400	36,192	07/01/2012	CDI	74,959	121,068		
8ª.....	11/11/1982	179,964	25,774	05/02/2013	CDI	234,455	145,878		
9ª.....	06/10/1983	125,640	57,528	09/01/2014	CDI	158,519	170,954		
11ª - A e B.....	06/29/1990	150,000	78,270	06/01/2020	CDI	158,258	98,189		
Gerdau Ameristeel Corp.....	04/23/1997	125,000	-	04/30/2007	6.50%	228,816	232,618		
						1,015,322	925,094		
Debentures held by consolidated subsidiaries.....						(286,938)	(252,982)		
Debentures in possession of the company.....						(46,479)	(95,622)		
<b>Consolidated</b> .....						<u>681,905</u>	<u>576,490</u>		
Current.....						2,719	2,986		
Long-term.....						679,186	573,504		

### Debentures issued by Gerdau S.A.

The debentures are stated in reais, with variable interest at a percentage of the CDI (Interbank Deposit Certificate) rate. The nominal annual interest rate was 18.99% and 16.17% for the years ended December 31, 2005 and 2004, respectively.

### Debentures issued by Gerdau Ameristeel Corp.

The debentures of Gerdau Ameristeel Corporation are convertible into common shares of the subsidiary at a conversion price of Cdn\$ 26.25 per share, up to their maturity.

The controlling shareholders hold, directly or indirectly, R\$ 543,383 at December 31, 2005 (R\$ 523,546 at December 31, 2004) of the outstanding debentures.

## 16 - FINANCIAL INSTRUMENTS

**a) General comments** - Metalúrgica Gerdau S.A. and its subsidiaries enter into transactions with financial instruments whose risks are managed by means of financial positions and exposure limit controls. All instruments are fully recorded in the books of account and mainly relate to the instruments listed below:

- **financial investments** - are recorded at their redemption value as of the financial statement date and are explained and presented in Note 5;
- **investments** - are explained and presented in Note 11;
- **related parties** - are explained and presented in Note 21;
- **loans** - are explained and presented in Note 14;
- **debentures** - are explained and presented Note 15; and
- **financial derivatives** - in order to minimize the effects of fluctuations in foreign exchange rates on their liabilities, the subsidiaries Gerdau Açominas S.A. and Dona Francisca Energética S.A. entered into swap contracts that were converted

into Brazilian reais on the contract date and linked to changes in the CDI interest rate and the General Market Price Index (IGP-M), plus additional interest. The subsidiaries Gerdau Açominas S.A and Gerdau Ameristeel Corporation also entered into swap contracts linked to LIBOR.

The swap contracts are listed below:

Consolidated				
Contract date	Purpose	Amount - US\$ thousand	Annual rate	Maturity
07.16.2001 to 07.18.2001	Prepayment	7,902	85.55% to 92.80% of the CDI	01.13.2006 to 03.01.2006
04.17.2003	Fixed assets	5,263	IGP-M + 12.95% p.a.	05.15.2006 to 11.16.2010
04.17.2003	Fixed assets	11,253	97.00% to 100.90% of the CDI	05.15.2006 to 11.16.2010
10.30.2003 to 11.03.2003	Bank notes	200,000	LIBOR + 6.09% to 6.13% interest	07.15.2011
01.31.2005	Fixed assets	240,000	5.64%	11.30.2011
11.22.2005	Fixed assets	40,000	5.97%	12.15.2008
11.22.2005	Fixed assets	43,125	7.05%	08.18.2008

**b) Market value** - the market values of the financial instruments are as follows:

	Company			
	2005		2004	
	Book value	Market value	Book value	Market value
Financial investments.....	49,302	49,302	95,702	95,702
Investments.....	3,925,401	6,832,003	3,018,021	5,979,482
Related parts (liabilities).....	137	137	266	266
Treasury stock - note 24.....	34,481	70,189	21,490	45,967

	Consolidated			
	2005		2004	
	Book value	Market value	Book value	Market value
Financial investments.....	5,122,178	5,122,178	1,666,178	1,666,178
Securitization financing.....	543,739	543,739	627,908	627,908
Importation financing.....	844,318	844,318	619,883	619,883
Prepayment financing.....	777,447	777,682	808,983	804,724
Resolution 2770 financing.....	-	-	263,060	256,585
Resolution 4131 financing.....	-	-	20,893	20,755
Bank Notes Financing.....	937,361	1,049,893	1,050,835	1,260,376
Fixed Assets.....	41,393	41,592	45,837	45,686
Perpetual bonuses.....	1,407,190	1,439,531	-	-
Others financing.....	2,130,623	2,130,623	2,080,840	2,080,840
Debentures.....	681,905	713,254	576,490	576,490
Investments.....	113,216	113,216	112,547	112,547
Related parties (assets).....	171	171	1,231	1,231
Stock options (liabilities) - note 26.....	-	14,241	-	13,663
Swap contracts - fixed assets (assets).....	5,462	5,462	-	-
Swap contracts - investment (liabilities).....	374	374	4,500	4,500

The market values of the swap contracts of subsidiaries in Brazil were obtained based on future income projections for each contract, calculated based on the present value of the forward U.S. dollar plus coupon rates (assets) and CDI/IGPM future rates (liabilities) and adjusted to present value on the financial statement date using the projected future CDI/IGPM rate for each maturity. The same methodology is applied for the calculation of the market values of the swap contracts of the subsidiary Gerdau Ameristeel Corporation, using the LIBOR rate.

Swap contracts related to financing contracts are classified together with the related financing, as a contra entry to the "Financial expenses/income, net" account, and are stated at cost plus accrued charges up to the financial statement date. Contracts not linked to such financing have been recorded at their market value under the heading "Judicial deposits and other" (assets) and "Other accounts payable" (liabilities).

The Company and its subsidiaries believe that the balances of the other financial instruments, which are recognized in the books at net contracted values, are substantially similar to those that would be obtained if they were negotiated in the market. However, because the markets for these instruments are not active, differences could exist if they were settled in advance.

### c) Risk factors that could affect the Company's and its subsidiaries' business

**Price risk:** this risk is related to the possibility of price variations of the products that the subsidiaries sell or in the raw material prices and other inputs used in the production process. Since the subsidiaries operate in a commodity market, their sales revenues and cost of sales may be affected by the changes in the international prices of their products or materials. In order to minimize this risk, the subsidiaries constantly monitor the price variations in the local and international markets.

**Interest rate risk:** this risk arises as a result of the possibility of losses (or gains) due to fluctuations in interest rates relating to its assets invested and liabilities raised in the market. In order to minimize possible impacts resulting from interest rate fluctuations, the Company and its subsidiaries have adopted a policy of diversification, alternating between fixed rates and variable rates (such as LIBOR and the CDI) and periodically renegotiating contracts to adjust them to market.

**Exchange rate risk:** this risk is related to the possibility of fluctuations in foreign exchange rates affecting financial expenses (or income) and the liability (or asset) balance of contracts denominated in a foreign currency. In addition to the foreign investments which are a natural hedge, the Company and its subsidiaries use hedge instruments, usually swap contracts, as described in item "a" above, to manage the effects of these fluctuations.

**Credit risk:** this risk arises from the possibility of the subsidiaries not receiving amounts arising from sales or investments with financial institutions. In order to minimize this risk, the subsidiaries adopt the procedure of analyzing in detail the financial and equity position of their customers, establishing a credit limit and constantly monitoring their balances. In relation to financial investments, the Company and its subsidiaries invest solely in institutions with low credit risk, as assessed by rating agencies. In addition, each institution has a maximum limit for investment, determined by the Credit Committee.

## 17 – FINANCIAL INCOME/EXPENSES

	Company		Consolidated	
	2005	2004	2005	2004
<b>Financial income</b>				
Financial investments.....	6,030	1,227	390,069	136,413
Interests.....	-	15	30,684	29,934
Monetary variation.....	17	1	3,161	3,327
Foreign exchange variation.....	-	-	(12,636)	(34,671)
Foreign exchange swap.....	-	-	-	3,915
Other financial income.....	1,313	8,996	71,953	110,343
<b>Total income</b> .....	<u>7,360</u>	<u>10,239</u>	<u>483,231</u>	<u>249,261</u>
<b>Expenses</b>				
Interest on loans.....	(4)	(844)	(459,936)	(417,041)
Monetary variations.....	(4,422)	(5,147)	(27,387)	(22,983)
Foreign exchange variations.....	-	-	236,372	197,607
Foreign exchange swap.....	-	-	(57,222)	(44,127)
Interest rate swap.....	-	-	(681)	-
Others financial expenses.....	(467)	(861)	(132,226)	(111,098)
<b>Total expenses</b> .....	<u>(4,893)</u>	<u>(6,852)</u>	<u>(441,080)</u>	<u>(397,642)</u>

## 18 – TAXES AND SOCIAL CONTRIBUTIONS PAYABLE

	Company		Consolidated	
	2005	2004	2005	2004
Income tax and social contribution on net income.....	-	843	113,295	202,962
Social charges on payroll.....	93	149	52,830	49,368
ICMS - Value-added tax on sales and services.....	-	-	34,355	32,131
COFINS - Tax for social security Financing.....	247	1,014	19,266	33,622
IPI - Excise Tax.....	-	-	21,599	14,114
PIS - Social Integration Program.....	54	220	4,193	6,903
Withholding income tax and social contribution.....	66	-	7,320	8,211
Tax payable in installments.....	-	-	4,196	11,819
Others.....	4	21	55,305	32,055
	<u>464</u>	<u>2,247</u>	<u>312,359</u>	<u>391,185</u>

## 19 – SPECIAL INSTALLMENT PAYMENT PROGRAM (PAES)

The proportionally consolidated (52%) subsidiary Dona Francisca Energética S.A. enrolled in the PAES, established by Law 10684/03, at the Federal Revenue Secretariat, to settle Corporate Income Tax (IRPJ), Social Contribution on Net Income (CSLL), Social Integration Program (PIS) and Social Contribution on Revenues (COFINS) liabilities. The balances of these tax liabilities are recorded in Taxes and contributions payable, in current liabilities, and in Other accounts payable, in long-term liabilities. The balances of the renegotiated taxes, which were divided into 180

installments of which 149 are not yet due, are restated by the Long-term Interest Rate (TJLP) and are as follows at the year end:

	Consolidated					
	2005			2004		
	Principal	Interest	Total	Principal	Interest	Total
IRPJ.....	18,790	4,756	23,546	20,303	3,160	23,463
CSLL.....	6,812	1,724	8,536	7,360	1,145	8,505
PIS.....	666	169	835	720	112	832
COFINS.....	3,078	779	3,857	3,326	518	3,844
	<u>29,346</u>	<u>7,428</u>	<u>36,774</u>	<u>31,709</u>	<u>4,935</u>	<u>36,644</u>
Current.....	2,363	599	2,962	2,364	368	2,732
Long-term.....	26,983	6,829	33,812	29,345	4,567	33,912

Dona Francisca Energética S.A. pays its taxes, contributions and other liabilities on their due dates, which is a basic requirement to remain eligible for the PAES program.

## 20 - PROVISION FOR CONTINGENCIES

The Company and its subsidiaries are parties to labor, civil, and tax lawsuits. Based on the opinion of its legal advisors, management believes that the provision for contingencies is sufficient to cover probable and reasonably estimable losses from unfavorable court decisions, and that the final decisions will not have significant effects on the financial position of the Company at December 31, 2005.

The balances of the contingencies, net of the corresponding judicial deposits, are:

### l) Contingent liabilities provided

	Company		Consolidated	
	2005	2004	2005	2004
a) Tax Contingencies				
Value-added tax on sales and services (ICMS).....	(a.1)	-	44,879	17,300
Social contribution on net income.....	(a.2)	-	7,333	7,333
Corporate income tax.....	(a.3)	-	19,993	19,993
National Institute of Social Security (INSS).....	(a.4)	-	29,924	24,900
Social Integration Program (PIS).....	(a.5)	469	2,373	2,372
Social Contribution on Revenues (COFINS).....	(a.5)	-	6,910	6,935
Compulsory loans Eletrobrás.....	(a.6)	-	-	50,456
Social Investment Fund (FINSOCIAL).....	(a.6)	-	-	6,898
Emergency capacity charge.....	(a.7)	-	33,896	25,563
Extraordinary reposition.....	(a.7)	-	19,675	13,037
Government Severance Indemnity				
Fund for Employee (FGTS) and other.....	(a.8)	-	986	1,503
Import Tax/IPI - Drawback.....	(a.9)	-	76,402	-
( - ) Judicial deposits.....	(a.10)	-	(93,848)	(73,938)
		<u>469</u>	<u>148,523</u>	<u>102,352</u>
b) Labor Contingencies.....	(b.1)	-	50,101	49,798
( - ) Judicial deposits.....	(b.2)	-	(10,899)	(10,538)
		-	<u>39,202</u>	<u>39,260</u>
c) Civil Contingencies.....	(c.1)	195	6,207	100,559
( - ) Judicial deposits.....	(c.2)	-	(1,074)	(1,207)
		<u>195</u>	<u>5,133</u>	<u>99,352</u>
Total liabilities provided.....		<u>664</u>	<u>192,858</u>	<u>240,964</u>

### a) Tax Contingencies

**a.1)** Lawsuits relating to value-added tax on sales and services (ICMS), the majority of which relates to credit rights, mostly under judgment by the Finance Secretariat and the Courts of First Instance of the State of Minas Gerais.

A provision for R\$ 28,483 was recorded in 2005 by the subsidiary Gerdau Aços Longos S.A. to cover possible losses in the motion seeking to reverse a final and irrevocable judgment in a tax assessment brought by the State of Minas Gerais to collect tax on shipments of merchandise to an exclusively exporting company. The company understands that the judgment breached a provision of law and that there was also a refusal of judgment in the decision. Although the company understands that ICMS is not payable on shipments to an exporting company, this provision was recorded in an amount considered to be sufficient to cover the entire alleged liability and additional fines and interest.

**a.2)** Social Contribution on Net Income. The amounts refer to challenges of the constitutionality of the contribution in 1989, 1990 and 1992. Some of these lawsuits are pending judgment, most of them in the Higher Courts.

**a.3)** Matters concerning Corporate Income Tax (IRPJ) in discussion at the administrative level.

**a.4)** Social security contributions due to the INSS, with lawsuits for annulment by the subsidiary Gerdau S.A., with judicial deposits of practically the whole amount involved, in progress in the Federal Court of the First Instance in the state of Rio de Janeiro.

In the Consolidated financial statements, the additional provision refers to lawsuits questioning the position of the INSS charging INSS contributions on profit sharing payments made by the subsidiary Gerdau Açominas S.A., as well as on payments for services rendered by third parties, in which the INSS calculated charges for the last ten years and assessed the company because it understands that it is jointly liable. The assessments were maintained at the administrative level, and Gerdau Açominas S.A. filed annulment actions with the judicial deposit of the corresponding amount, based on the understanding that the right to assess part of the charge had prescribed and that there is no such liability.

**a.5)** Contributions to the Social Integration Program (PIS), and the Social Contribution on Revenues (COFINS) in connection with lawsuits challenging the constitutionality of Law no 9,718, which changed the calculation basis of these contributions. These lawsuits are in progress at the Federal Regional Court of the 2nd Region and the Federal Supreme Court.

**a.6)** Tax contingencies relating to the Eletrobrás compulsory loan (R\$ 50,456) and FINSOCIAL (R\$ 6,891) were reversed by the subsidiary Gerdau S.A. in 2005, considering, respectively, the implementation by Eletrobrás of the 3rd conversion in shares of the compulsory loans and the closing of the respective lawsuits.

**a.7)** Emergency Capacity Charge (ECE) and Extraordinary Tariff Recomposition (RTE), charges included in the electric energy bills of the plants of the Company's subsidiaries. According to the Company, these charges are of a tax nature and, as such, are incompatible with the National Tax System provided in the Federal Constitution. For this reason, the constitutionality of these charges is being challenged in court. The lawsuits are in progress in the Federal Justice of the First Instance of the states of Pernambuco, Ceará, Minas Gerais, Rio de Janeiro, São Paulo, Paraná, and Rio Grande do Sul, as well as in the Federal Regional Courts of the 1st, 2nd and 5th Regions. The companies have fully deposited in court the amounts of the disputed charges.

**a.8)** The provision recorded by Gerdau Açominas S.A. relating to the increased charges for FGTS, arising from the changes introduced by Complementary Law No. 110/01, was eliminated since the legal dispute referred to in the corresponding Injunction was finally and irrevocably judged against the company, following the judgment by the Federal Supreme Court in a similar case. There was a subsequent discussion since, at the time of payment of the principal as a result of the decision

of the Injunction, Caixa Econômica Federal insisted on charging a fine. Consequently, the company deposited the principal in a Court Payment and the amount of the fine in a Judicial Appeal. The principal was drawn by the Caixa Econômica Federal and the dispute about the fine is pending judgment of the appeal brought by the company.

**a.9)** The provision made in the last quarter of 2005 by the subsidiary Gerdau Açominas S.A is intended to cover amounts requested by the Federal Revenue authorities for Import Tax, Excise Tax and resulting additional charges on transactions made under a drawback granted which was subsequently annulled by the Foreign Trade Operations Department (DECEX). The company does not agree with the administrative decision that annulled the grant and defends the legality of the transactions made. The matter is the object of a Request for Injunction under consideration in the Superior Court of Justice (STJ).

**a.10)** The judicial deposits relate to amounts deposited and maintained in court by the Company and its subsidiaries until the resolution of the related litigation. The balances of these credits are classified as a reduction of the provision for tax contingencies.

**b) Labor Contingencies:**

**b.1)** The Company's subsidiaries are also parties to labor claims. None of these claims involve significant amounts and the lawsuits mainly involve overtime pay, health and danger hazards, among others.

**b.2)** The judicial deposits relate to amounts deposited and maintained in court until the resolution of the related litigation and are classified as a reduction of the provision for labor contingencies.

**c) Civil Contingencies**

**c.1)** The Company and its subsidiaries are also a party to civil claims arising in the normal course of their operations, including claims arising from work accidents, which total at December 31, 2005 the amount shown as the contingent liability for these matters. Certain provisions were reversed in 2005 because of changes in the prospect of loss and/or closing of the lawsuits.

**c.2)** The judicial deposits are classified as a reduction of the provision for civil contingencies.

**II) Contingent liabilities not provided**

**a) Tax contingencies**

**a.1)** The subsidiary Gerdau S.A. is a defendant in assessments filed by the state of Minas Gerais demanding ICMS tax payments arising mainly from the sales of products to commercial exporters. The restated amount of the lawsuits totals R\$ 32,425. The Company has not made any provision for contingency in relation to these claims since it considers that this tax is not payable, because products for export are exempted from ICMS.

**a.2)** The subsidiaries Gerdau S.A. and Gerdau Açominas S.A. are defendants in assessments filed by the state of Minas Gerais which demand ICMS tax payments on the export of semi-finished manufactured products. The subsidiary Gerdau Açominas S.A. has also filed a lawsuit for the annulment of an action of the same nature. The total amount demanded is R\$ 271,997. The companies have not recorded any provision for contingency in relation to these claims since they consider that this tax is not payable because the products cannot be considered semi-finished manufactured products as defined by the federal complementary law and, therefore, are not subject to ICMS.

**a.3)** On December 6, 2000, the subsidiary Gerdau S.A. enrolled in the Tax Recovery (REFIS) Program to pay the Social Integration Program (PIS) and the Social Contribution on Revenues (COFINS) contributions in installments. The constitutionality of the use of credits of R\$ 40,118 acquired from third parties to settle the company's own interest and penalties is being challenged in court. This occurred because the Federal Revenue authorities understand that tax credits

must first be used to offset the assignor's own debts, only transferring the excess to the assignee. This understanding, based solely on a REFIS Management Committee Resolution, edited subsequent to the company's enrollment in the Program, does not have a legal basis. In fact, the law which established the Program authorized, with no conditions, the purchase of third party tax credits for offset against own liabilities.

**b) Civil Contingencies**

**b.1)** Antitrust lawsuit involving the subsidiary Gerdau S.A. brought by two civil construction unions in the state of São Paulo alleging that Gerdau S.A. and other long steel producers in Brazil share customers among them, violating the antitrust legislation. After investigations carried out by the National Secretariat of Economic Law (SDE) and based on public hearings, the SDE is of the opinion that a cartel exists. This conclusion was also supported by an earlier opinion by the Secretariat for Economic Monitoring (SEAE). The lawsuit was therefore forwarded to the Administrative Council for Economic Defense (CADE) for judgment.

However, its course was suspended from May 2004 to August 16, 2005 due to a legal protection granted within a new lawsuit brought by Gerdau S.A. with the purpose of annulling the administrative proceeding grounded on formal irregularities found in its discovery. The annulment of the legal protection by the Federal Regional Court occurred as a result of appeals brought by CADE and the Federal Government.

CADE, regardless of the request for submission of negative evidence of cartel made by Gerdau S.A., judged the merits of the administrative proceedings on September 23, 2005 and, by a majority of votes, fined the company and other long steel producers an amount equivalent to 7% of their revenues in the year before the Administrative Proceeding was commenced, excluding taxes, for formation of a cartel. A request for amendment of judgment was made regarding this decision, which is still pending judgment.

Despite the CADE decision, the legal action through by Gerdau S.A. follows its normal course and, at present, awaits judgment in the lower court. In the event the processual irregularities alleged by Gerdau S.A. are recognized by the court, the CADE decision may be annulled.

It should be noted that just prior to the CADE decision, the Federal Public Ministry of the state of Minas Gerais issued a judgment on a Public Civil Action, based on the above mentioned SDE decision, and, without mentioning any new elements, alleged that the company was involved in activities which contravened the antitrust legislation. Gerdau S.A. contested this allegation on July 22, 2005.

The company denies having engaged in any type of anti-competitive conduct and believes, based on information available, including the opinion of its legal advisors, that the administrative process until now includes many irregularities, some of which are impossible to resolve. In relation to the merit, Gerdau S.A. is sure that it did not practice the alleged conduct and, in this regard, its convictions are supported by renowned experts and the company, consequently, believes in the possibility of its conviction being reversed.

**b.2)** A civil lawsuit has been filed against Gerdau Açominas S.A. regarding the termination of a contract for the supply of slag and indemnities for losses and damages. At December 31, 2005, the lawsuit amounted to approximately R\$ 47,954. Gerdau Açominas S.A. contested all bases for the lawsuit and filed a counterclaim for termination of the contract and indemnity for breach of contract. The judge declared the contract to be terminated, since this demand was common to both parties. With regards to the remaining discussion, the judge understood that both parties were at fault and judged the requests for indemnity unfounded. This decision was maintained by the Court of Civil Appeals of the State of Minas Gerais (TAMG), and the court decision is based on expert evidence and interpretation of the contract.

As regards the termination and the fact that the indemnity claimed by the supplier is not payable, the Court of Civil Appeals of the state of Minas Gerais confirmed the termination of the contract and granted the appeal by Gerdau Açominas to charge the supplier for the costs of removal of the slag, maintaining that the latter's claim has no grounds.

A Special Appeal was initially brought against TAMG's decision, whose continuation was denied, against which a Bill of Review was filed in which the Superior Court of Justice (STJ) determined TAMG to complement the judgment challenged, which occurred in 2005. In this judgment, the previous decision was maintained and a new Special Appeal filed, which was also denied. A new Bill of Review was filed, which was denied by the STJ in a decision published on October 18, 2005. Gerdau Açominas has not been notified of any subsequent appeal.

The company believes that any loss is remote since it is of the opinion that any change in judgment is unlikely, as the judgment was based on the analysis of evidence and interpretation of the contract, which practically precludes the chances of success of the Itabira appeals, which has been confirmed by the successive judgments against Itabira.

**b.3)** A civil lawsuit has been filed by Sul America América Cia. Nacional de Seguros against Gerdau Açominas S.A. and Ban Westdeutsche Landesbank Girozentrale, New York Branch (WestLB), for the payment of R\$ 34,383 to settle an indemnity claim, which has been deposited in court. The insurance company pleads doubt in relation to whom the payment should be made and alleges that the subsidiary is resisting in receiving and settling the amount. The lawsuit was challenged both by the Bank (which claims to have no right over the amount deposited, which resolves the doubt raised by Sul América) and by the subsidiary (which claims that there is no such doubt and that there is justification to refuse payment since the amount owed by Sul América is higher than the amount involved). Subsequently, Sul América claimed fault on the Bank's representation, and this matter is therefore already settled, which resulted in the withdrawal in December 2004 of the amount deposited. The process should enter the expert evidence phase, mainly for calculation of the amount due.

Based on the opinion of its legal advisors, the subsidiary expects a loss to be remote and that the sentence will declare the amount payable within the amount stated in the pleading. Also, Gerdau Açominas S.A. filed, prior to this lawsuit, a lawsuit for the payment of the amount recognized by the insurance companies. The lawsuits are pending. The subsidiary expects a favorable outcome in this lawsuit.

The civil lawsuits arise from an accident on March 23, 2002 with the blast furnace regenerators of the Ouro Branco steel plants, which resulted in the stoppage of several activities, with material damages to the steel mill equipment and loss of profits. The equipment, as well as the loss of profits arising from the accident, was covered by an insurance policy. The report on the event, as well as the loss claim, was filed with IRB - Brasil Resseguros, and an advance payment of R\$ 62,000 was received in 2002.

In 2002, a preliminary and conservative estimate of indemnities related to the coverage of loss of profits and material damages, in the total amount of approximately R\$ 110,000, was recorded based on the amount of fixed costs incurred during the period of partial stoppage of the steel mill activities and the immediate expenses to be incurred to recover the equipment temporarily. This estimate approximates the advance amount received (R\$ 62,000) plus the amount proposed by the insurance company as a complement to settle the indemnity (R\$ 34,383). Subsequently, new amounts were added to the dispute as stated in the subsidiary's plea, although not yet recorded. In addition to these amounts, the subsidiary also incurred other costs for the recovery of the damage resulting from the accident, as well as other related losses that were listed in its challenge to the lawsuit in progress and which will be confirmed during the discovery phase, when they will be recorded.

Based on the opinion of its legal advisors, the Company considers that losses from other contingencies that may affect the results of operations or the Company's consolidated financial position are remote.

### III) Contingent gains not recorded

#### a) Tax contingencies

**a.1)** The Company believes that the realization of certain contingent gains is possible. Among them is a court-order debt security issued in 1999 in the amount of R\$ 26,580 in favor of the subsidiary Gerdau S.A., arising from an ordinary lawsuit against the state of Rio de Janeiro for non-compliance with the Loan Agreement for Periodic Execution in Cash under the Special Industrial Development Program (PRODI). Due to the default by the state of Rio de Janeiro and the non-regulation of Constitutional Amendment 30/00 (which granted the government a ten-year moratorium for payment of securities issued to cover court-order debts not related to food), the realization of this credit is not expected in 2005 and following years. For this reason, this gain is not recorded in the financial statements.

**a.2)** A final and irrevocable favorable decision was granted on December 7, 2005 against the restatement of the calculation basis of the half-yearly PIS under Complementary Law 07/70, as a result of the decision of unconstitutionality of Decree Laws 2445/88 and 2449/88, in the last lawsuit of the subsidiary Gerdau S.A. still under examination. Accordingly, the company has recorded the corresponding credit, in December 2005, which, added to the credits recorded in the first quarter of the year relating to the same lawsuit, totaled R\$ 70,332.

**a.3)** Also, the subsidiaries Gerdau S.A., Gerdau Açominas S.A. and Margusa - Maranhão Gusa S.A. expect to recover IPI premium credits. Gerdau S.A. and the subsidiary Margusa Maranhão Gusa S.A. have filed administrative appeals for recovery, which are pending judgment. With regards to the subsidiary Gerdau Açominas S.A., the proceedings were judged unfavorably. Currently, the process awaits judgment of the appeal filed by the subsidiary. The Company estimates the credits at R\$ 394,002 (Consolidated) but no accounting recognition has been made thereof because of uncertainty as to their realization.

### 21 - RELATED PARTIES

#### a) Analysis of loan balances

	Company		Consolidated	
	2005	2004	2005	2004
Gerdau Açominas S.A. ....	-	(381)	-	-
Gerdau Aços Longos S.A. ....	(137)	-	-	-
Fundação Gerdau .....	-	-	294	1,305
Gerdau S.A. ....	-	115	-	-
Florestal Rio Largo Ltda. ....	-	-	(119)	-
Sipar Aceros S.A. e outras .....	-	-	-	(74)
Others .....	-	-	(4)	-
	<u>(137)</u>	<u>(266)</u>	<u>171</u>	<u>1,231</u>
Net financial income (expenses) .....	-	(817)	27,874	19,638

**b) Commercial transactions -** the Company entered into transactions with its parent company Indac - Ind. Adm. e Comércio S.A. Such transactions were the payment (R\$ 466) and receipt (R\$ 4,500) of guarantees received and given as collateral in contracts. The Company also made payments for the use of the Gerdau brand to the associated company Grupo Gerdau Empreendimentos Ltda., of R\$ 300 (R\$ 300 on 2004).

**c) Guarantees granted -** The Company is the guarantor of the subsidiary GTL Financial Corp., in the amount of US\$ 50,000, equivalent to R\$ 117,035 at December 31, 2005. The Company is also guarantor of its parent company Indac - Ind. Adm. e Comércio S.A. in contracts totaling R\$ 660,249. The subsidiary Gerdau S.A. is the guarantor of loan agreements of the

jointly-owned subsidiary Dona Francisca S.A. in the amount of R\$ 90,489, corresponding 51,82% of the joint agreement. Gerdau S.A. is also the guarantor of the Euro Commercial Paper program of the subsidiary GTL Trade Finance Inc., of US\$ 200 million, equivalent to R\$ 468,140 at December 31, 2005. This subsidiary is also the guarantor of the securitization operations of the subsidiary Gerdau Açominas Overseas Ltda., of US\$ 228.610 thousand, equivalent to R\$ 535,107 on December 31, 2005. The subsidiaries Gerdau Açominas S.A. and Gerdau Comercial de Aços S.A. are the guarantors of the vendor financing loan agreements of the associated company Banco Gerdau S.A., in the amounts of R\$ 17,097 and R\$ 15,440, respectively.

## 22 - POST-EMPLOYMENT BENEFITS

Considering all the benefits granted to employees by the Company and its subsidiaries, the assets and liabilities on December 31 are as follows:

	Company		Consolidated	
	2005	2004	2005	2004
Actuarial liabilities with pension plan-defined benefit.....	-	-	135,695	154,199
Actuarial liabilities with post-employment health benefits.....	-	-	119,687	130,283
Liabilities with retirement and severance benefits.....	-	-	8,395	9,996
Total do liabilities.....	-	-	263,777	294,478
Unrecorded actuarial assets.....	1,539	1,964	211,586	165,510

### a) Pension plan - defined benefit

The Company and other Group subsidiaries in Brazil are the co-sponsors of defined benefit pension plans that cover substantially all employees in Brazil ("Açominas Plan" and "Gerdau Plan").

The Açominas Plan is managed by Fundação Açominas de Seguridade Social - Aços, a closed supplementary pension entity to complement the social security benefits of employees and retired employees of the Ouro Branco unit of Gerdau Açominas S.A. The assets of the Açominas Plan mainly comprise investments in bank deposit certificates, federal public securities, marketable securities and properties.

The Gerdau Plan is managed by Gerdau - Sociedade de Previdência Privada, a closed supplementary pension entity to complement the social security benefits of employees and retired employees of the Company, of the other units of Gerdau Açominas S.A. and of other subsidiaries in Brazil. The assets of the Gerdau Plan comprise investments in bank deposit certificates, federal public securities and marketable securities.

Also, the Canadian and American subsidiaries sponsor defined benefit plans (Canadian Plan and American Plan) that cover substantially all of their employees. The Canadian and American plans are managed by CIBC Mellon and Wells Fargo, respectively, to complement the social security benefits of employees of Gerdau Ameristeel Corporation and its subsidiaries. The assets of the Plans mainly comprise marketable securities.

The sponsors' contributions to these pension plans were R\$ 6 in 2005 (R\$ 13 in 2004) for the Company and R\$ 67,157 in 2005 (R\$ 68,288 in 2004) Consolidated.

The current expense of the defined benefit pension plans is as follows:

	Company		Consolidated	
	2005	2004	2005	2004
Cost of current service.....	47	39	64,452	49,884
Interest cost.....	136	124	134,725	125,054
Return expected from the plan's assets.....	(238)	(204)	(223,818)	(162,001)
Amortization of unrecognized liability.....	-	-	438	462
Amortization of past service costs.....	4	-	3,692	778
Amortization of (gain) loss.....	(31)	(18)	12,483	2,550
Contribution expected from employees.....	-	-	(5,997)	(4,383)
Pension plan net costs (benefits), net.....	(82)	(59)	(14,025)	12,344

The reconciliation of the assets and liabilities of the plans is as follows:

	Company		Consolidated	
	2005	2004	2005	2004
Total liabilities.....	(4,182)	(7,065)	(1,953,332)	(1,790,639)
Fair value of plan assets.....	9,545	14,993	2,041,184	1,867,506
Net assets.....	5,363	7,928	87,852	76,867
Unrecorded gain (losses).....	(3,824)	(5,964)	(40,904)	(96,827)
Past service costs.....	-	-	24,910	26,342
Others.....	-	-	4,033	4,929
Total net assets.....	1,539	1,964	75,891	11,311
Actuarial assets.....	1,539	1,964	211,586	165,510
Pension plan liability recorded in the books of accounts.....	-	-	(135,695)	(154,199)
Net assets.....	1,539	1,964	75,891	11,311

The changes in plan assets and actuarial liabilities were as follows:

	Company		Consolidated	
	2005	2004	2005	2004
<b>Changes in benefit liabilities</b>				
Benefit liabilities at the beginning of the year.....	7,065	6,223	1,790,639	1,623,000
Cost of service.....	47	39	64,452	49,884
Interest cost.....	136	124	134,725	125,054
Actuarial loss (gain).....	(1,551)	794	131,754	88,360
Payment of benefits.....	(123)	(115)	(62,115)	(69,534)
Past service due to change in the plan.....	-	-	-	10,516
Foreign exchange effect on foreign subsidiaries.....	-	-	(110,173)	(45,000)
Transfer of participants.....	(1,392)	-	-	-
Initial liability recognition adjustment.....	-	-	4,050	8,359
Benefit liabilities at the end of the year.....	4,182	7,065	1,953,332	1,790,639
<b>Change in plan assets</b>				
Fair value of the plan assets at the beginning of the year.....	14,993	12,366	1,867,506	1,663,567
Return on plan assets.....	(2,195)	2,729	248,239	232,043
Contributions from sponsors.....	6	13	67,157	68,288
Contributions from participants.....	-	-	6,045	5,202
Payment of benefits.....	(123)	(115)	(62,115)	(69,534)
Transfer of participants.....	(3,136)	-	-	-
Foreign exchange effect on foreign subsidiaries.....	-	-	(85,648)	(32,060)
Fair value of the plan assets at the beginning of the year.....	9,545	14,993	2,041,184	1,867,506

The amount of the actuarial gains and losses to be recognized as income or expense is the unrecognized amount that exceeds, in each period, the higher of the following limits: (i) 10% of the present value of the total actuarial liability of the defined benefit plan and (ii) 10% of the fair value of the plan assets. The resulting amount will be amortized annually based on the average remaining years of service estimated for the employees that participate in the plan.

The table below shows a summary of the assumptions made to calculate and record the defined benefit plan for both the Company and Consolidated:

	<b>Gerdau Plan</b>	<b>Açominas Plan</b>	<b>North American Plan</b>
Average discount rate.....	11.30%	11.30%	5.00% - 5.75%
Increase in composition.....	9.20%	8.68%	2.50% - 4.25%
Expected rate of return on assets.....	15.54%	12.35%	7.50% - 8.40%
Mortality chart.....	GAM 83 (-1 year)	AT-2000	GAM 83
Disabled mortality chart.....	RRB 1944	AT-2000	RRB 1977
Turnover rate.....	Based on service and salary level	Null	Based on age and service (plan experience)

#### b) Pension plan – defined contribution

The Company and its subsidiaries in Brazil are also the co-sponsors of a defined contribution pension plan administered by Gerdau - Sociedade de Previdência Privada. Contributions are based on a percentage of the compensation of the employees.

The foreign subsidiary Gerdau AmeriSteel US Inc. has a defined contribution plan, the contributions to which are equivalent to 50% of the amount paid by the participants, limited to 4% of salary. The other companies do not have this type of pension plan.

The total cost of this plan was R\$ 22 in 2005 (R\$ 55 in 2004) for the Company and R\$ 16,742 in 2005 (R\$ 12,005 in 2004) Consolidated.

#### c) Other post-employment benefits

The Company estimates that the amount payable to executives on their retirement or discharge totals R\$ 8,396 (Consolidated) on December 31, 2005 (R\$ 9,996 in 2004 - Consolidated).

The American Plan includes, in addition to pension benefits, specific health benefits for employees who retire after a certain age and with a certain number of years of service. The American subsidiary has the right to change or eliminate these benefits, and the contributions are based on amounts actuarially calculated.

The composition of the net periodic cost for the post-employment health benefits is as follows:

	<b>Consolidated</b>	
	<b>2005</b>	<b>2004</b>
Cost of service.....	3,394	3,007
Interest cost.....	6,404	5,715
Amortization of past service costs.....	(770)	(563)
Amortization of loss.....	229	80
Net-expense for post-employment benefits.....	<u>9,257</u>	<u>8,239</u>

The status of the fund for post-employment health benefits is as follows:

	<b>Consolidated</b>	
	<b>2005</b>	<b>2004</b>
Plan assets at market value.....	-	-
Projected benefit liabilities.....	(139,400)	(130,559)
Fund status.....	(139,400)	(130,559)
Unrecorded gains and losses, net.....	30,960	8,101
Past service costs.....	(11,247)	(7,825)
Liabilities for post-employment health benefits recorded in the financial statements.....	<u>(119,687)</u>	<u>(130,283)</u>

The changes in plan assets and actuarial liabilities were as follows:

	<b>Consolidated</b>	
	<b>2005</b>	<b>2004</b>
<b>Change in projected benefit liabilities</b>		
Projected benefit liabilities at the beginning of the years.....	130,559	111,390
Purchase of North Star.....	-	23,136
Cost of service.....	3,394	3,007
Interest cost.....	6,404	5,715
Contributions of participants.....	2,160	1,946
Actuarial cost.....	19,671	4,759
Benefits and administrative expenses paid.....	(5,215)	(6,639)
Foreign exchange effect.....	(12,642)	(4,364)
Initial liability recognition adjustment.....	(4,931)	(8,391)
Projected benefit liabilities at the end of the year.....	<u>139,400</u>	<u>130,559</u>

	<b>Consolidated</b>	
	<b>2005</b>	<b>2004</b>
<b>Changes in plan assets</b>		
Plan assets at the beginning of the year.....	-	-
Contributions from sponsors.....	3,055	4,693
Contributions from participants.....	2,160	1,946
Benefits and administrative expenses paid.....	(5,215)	(6,639)
Plan assets at the end of the year.....	<u>-</u>	<u>-</u>

The assumptions adopted in the accounting for post-employment health benefits were as follows:

	<b>North American Plans</b>
Average discount rate.....	5.75% - 6.00%
Health treatment - assumed rate for next year.....	9.50% - 12.00%
Health treatment - assumed cost decline rate to be reached in the years from 2010 to 2013.....	5.50%

#### 23 – OTHER ACCOUNTS PAYABLE (LONG-TERM)

Other accounts payable in the company's long-term liabilities refers to the debt with the National Treasury arising from the privatization project.

## 24 – SHAREHOLDERS' EQUITY

**a) Capital Stock** – The Board of Directors may, regardless of changes to the by-laws, issue new shares (authorized capital), including the capitalization of profits and reserves up to the authorized limit of 100,000,000 common shares (50,000,000 at December 31, 2004) and 200,000,000 preferred shares (100,000,000 at December 31, 2004), all of them with no par value, in accordance with the amendment approved by the Extraordinary General Meeting of shareholders held on April 4, 2005. The right of preference shall be exercised before the deadline for prescription of 30 days, except in the case of a public offer, when the deadline for prescription shall not be less than 10 days.

On April 11, 2005, as approved in a meeting of the Board of Directors held on March 31, 2005, Metalúrgica Gerdau S.A. increased capital by R\$ 832,000 through the capitalization of the reserve for investments and working capital, with a bonus of 50% on the share position on April 11, 2005, date of capitalization of the reserve, representing 41,584,395 new shares (13,861,465 common shares and 27,722,930 preferred shares).

At December 31, 2005, 41,584,395 common shares (27,722,930 at December 31, 2004) and 83,168,790 preferred shares (55,445,860 at December 31, 2004) are subscribed and paid up, totaling a paid up capital of R\$ 2,496,000 (R\$ 1,664,000 at December 31, 2004). Preferred shares do not have voting rights and cannot be redeemed, but have the same rights as common shares in terms of profit sharing.

**b) Legal reserve** – Under Brazilian legislation, Metalúrgica Gerdau is required to transfer 5% of the annual net income determined in accordance with corporate legislation to legal reserve until this reserve is equivalent to 20% of the paid up capital. The legal reserve can be used to increase capital or to absorb losses, but cannot be used for payment of dividends.

**c) Statutory reserve** – The Board of Directors may propose to the shareholders the transfer of at least 5% of the net income of each year to a statutory reserve (Reserve for Investments and Working Capital). The reserve is created only if it does not affect the minimum dividend requirement and its balance cannot exceed the total paid up capital. The reserve can be used to absorb losses, if necessary, and for capitalization, payment of dividends or repurchase of shares.

**d) Treasury shares** – at December 31, 2005 the Company had 1,447,200 preferred shares (682,000 preferred shares at December 31, 2004) held in treasury, totaling R\$ 34,481 (R\$ 21,490 at December 31, 2004), of which 1,023,000 shares related to the share repurchase program announced on November 17, 2003, and 424,200 shares to the share repurchase program announced on May 30, 2005, to be held in treasury for subsequent cancellation. The average cost of these shares is R\$ 23.83, the lowest purchase price being R\$ 15.54 and the highest R\$ 32.06. During 2005, 424,200 shares were purchased at an average cost of R\$ 30.59.

**e) Dividends and interest on own capital** – the shareholders have the right to receive, each year, a minimum mandatory dividend of 30% of the adjusted net income. In 2004, the Company calculated interest on own capital in accordance with the terms established by Law 9249/95. The corresponding amount was recorded as a financial expense for tax purposes. For presentation purposes, this amount was recorded as a dividend, not affecting net income. The related tax benefit through the reduction of the income tax and social contribution on net income charge for 2004 was R\$ 55,250.

The dividends credited in 2005 amounted to R\$ 364,059, shown as follows:

	2005	2004
Net income for the year .....	1,275,584	1,437,075
Legal reserve constitution.....	(63,778)	(71,855)
Adjusted net income.....	<u>1,211,80</u>	<u>1,365,220</u>

## Payments during the year

Period	Nature	R\$/share	Credit	Payment	2005	2004
1 <sup>st</sup> quarter .....	Interest	-	-	-	-	45,368
	Dividends	0.72	05/13/2005	05/24/2005	89,086	-
2 <sup>nd</sup> quarter.....	Interest	-	-	-	-	51,142
	Dividends	0.79	08/15/2005	08/24/2005	97,412	37,944
3 <sup>rd</sup> quarter.....	Interest	-	-	-	-	65,990
	Dividends	0.75	11/18/2005	11/30/2005	92,479	75,061
4 <sup>th</sup> quarter.....	Dividends	0.69	02/17/2006	03/02/2006	85,082	158,374
Interest on own capital and dividends.....					<u>364,059</u>	<u>433,879</u>
% interest/dividends paid or credited .....					30%	32%
Amount per share (R\$).....					2.95	5.26
Shares in circulation.....					123,306	82,487

The remaining income for the year was transferred to the statutory reserve for investments and working capital in accordance with the by-laws.

## 25 – PROFIT SHARING

**a)** The management profit sharing is limited to 10% of net income for the year, after income tax and management fees, as stated in the Company's by-laws;

**b)** The employees' profit sharing is linked to the attainment of operating goals and was charged to cost of production and general and administrative expenses, as applicable.

## 26 – LONG-TERM INCENTIVE PLANS

### I) Metalúrgica Gerdau S.A.

The Extraordinary General Meeting of shareholders held on April 30, 2003 decided, based on a plan approved at the meeting and within the limit of the authorized capital, to grant options for the purchase of preferred shares to management, employees or persons who render services to the Company or its subsidiaries, and approved the formation of the Long-Term Incentive Program that represents a new form of compensation of the strategic executives of the Company. Although the plan was approved, no options have been granted to date.

### II) Gerdau S.A.

The Extraordinary General Meeting of shareholders held on April 30, 2003 decided, based on a previously agreed plan and within the limit of the authorized capital, to grant options for the purchase of preferred shares to management, employees or persons who render services to the Company or its subsidiaries, and approved the formation of the Long-Term Incentive Program that represents a new form of compensation of the strategic executives of the Company. The options should be exercised in a maximum of five years after the grace period.

**a) Summary of changes in the plan:**

	Grant (Quantity of shares)						Total
	2003	2003	2004	2004	2005	2005	
Opening balance on 12/31/2004.....	806,457	561,680	4,859	342,250	-	-	1,715,246
Grants.....	-	-	-	-	211,128	285,336	496,464
Stock bonuses on 04/11/2005.....	399,097	278,086	2,430	168,870	105,563	142,668	1,096,714
Cancelled.....	(8,259)	(5,513)	-	(21,504)	(5,806)	(3,600)	(44,682)
Exercised.....	(28,171)	(18,781)	-	(7,353)	-	-	(54,305)
Final balance on 12/31/2005.....	<u>1,169,124</u>	<u>815,472</u>	<u>7,289</u>	<u>482,263</u>	<u>310,885</u>	<u>424,404</u>	<u>3,209,437</u>
Price for exercise in R\$.....	7.96	7.96	20.33	20.33	31.75	31.75	
Grace period.....	3 years	5 years	3 years	5 years	3 years	5 years	

At December 31, 2005, the company has a total of 3,045,695 preferred shares in treasury. These shares may be used for this plan.

**b) Plan status at December 31, 2005:**

	Grant			
	2003	2004	2005	Average
Total granted shares purchase options.....	1,984,596	489,552	735,289	
Price of exercise - R\$ (adjusted by bonuses).....	7.96	20.33	31.75	15.30
Fair value of options on the grant date - R\$ per option (*).....	2.48	5.77	5.31	3.63
Average option exercise period on grant date (years).....	3.8	4.9	4.2	4.1

(\*) calculated considering the Black-Scholes model

The percentage of dilution of interest that the current shareholders may experience if all options are exercised is approximately 0.7%.

**III) Gerdau Ameristeel Corporation - ("Gerdau Ameristeel")**

Gerdau Ameristeel Corporation and its subsidiaries have stock compensation plans for their employees, as follows:

**a) Former Co-Steel Plan**

According to the terms of the Co-Steel Plan, the Stock-Based Option Plan, the company was authorized to grant purchase options to employees and directors up to the limit of 3,041,335 common shares. The exercise price was based on the closing price of the common shares in the market on the day prior to the issue of the option. The options have a maximum term of ten years and are granted during various periods, as determined by the administrator of the plan at the date of the grant, up to April 13, 2008.

**b) Gerdau AmeriSteel US Inc. ("AmeriSteel") Plans**

According to the terms of the Transaction Agreement relating to the acquisition of Co-Steel, the minority shareholders of AmeriSteel exchanged their shares and stock options for shares and stock options of Ameristeel at the ratio of 9,4617 shares and stock options for each share or stock option of AmeriSteel. This exchange occurred on March 31, 2003.

**b.1) AmeriSteel Plan**

AmeriSteel has a long-term incentive plan for the executive officers (the "AmeriSteel Plan") to ensure that the interests of the AmeriSteel senior management are in line with those of the AmeriSteel shareholders. The awards are determined by a formula based on the return on employed capital of AmeriSteel in a given year of the plan. The awards are granted and paid over a period of four years. The participants may choose payment in cash or in shares of AmeriSteel and Gerdau, for which a premium of 25% is given, if chosen. Expenses related to the benefits for the years ended December 31, 2005 and 2004 totaled US\$ 6,000 thousand (R\$ 14,044) and US\$ 1,300 thousand (R\$ 3,450), respectively.

**b.2) 2004 Stakeholder Plan**

For the year ended December 31, 2004, the Gerdau Ameristeel Human Resources Committee established the long-term incentive plan of 2004 (the "2004 Stakeholder Plan") based on the AmeriSteel Plan. The 2004 Stakeholder Plan was designed to award the executive officers with a share in the profits of Gerdau AmeriSteel. The awards earned are granted and paid over a period of four years, based on the closing price of the Gerdau Ameristeel Shares in the New York Stock Exchange. A total award of approximately US\$ 14,000 thousand (equivalent to R\$ 37,161) was calculated at December 31, 2004 and was granted on March 1, 2005. This award is being provided for in accordance with the payment term established in the plan.

**b.3) 2005 Stakeholder plan**

For the year beginning January 1, 2005, the Human Resources Committee established the 2005 long-term incentive plan (the "2005 Stockholder plan"). The 2005 Stockholder plan was established to award employees with bonuses based on attaining goals related to the return of capital invested. The bonuses will be granted at the end of the year in cash and/or options. The payment of the cash portion option will be made in the form of shares (phantom stock). The number of shares will be determined by the market price of the common share on the date of grant, based on the average negotiation price on the New York Stock Exchange. The shares will be paid in April each year at the ratio of 25% in a period of 4 years. The number of options granted to the participants is determined by dividing the portion of the bonus not paid in cash by the market value of the common share on the date of grant and indexed by a factor determined by the option value on the same date (the option value is determined by the Committee based on the Black Scholes model or other method). The options may be exercised at the rate of 25% p.a. during four years from the date of grant and prescribe after 10 years. The maximum number of options that will be granted based on this plan is 6,000,000.

**b.4) SAR Plan**

In July 1999, the Board of Directors of AmeriSteel approved the SAR/Shares Purchase Plan (SAR Plan) available to basically all employees. The SAR Plan authorizes the sale of 946,170 common shares to the employees during three offer periods, from July to September in 1999, 2002 and 2005. The employees who purchase the shares are rewarded with stock appreciation rights (SARs) equal to four times the number of shares purchased. SARs at market value were granted at the date of grant, determined on the basis of an independent appraisal at the end of the prior year. SARs can be exercised at 25% annually as from the date of grant, and may be exercised in up to ten years from the date of grant. The SARs are recorded as liabilities and the benefits recorded as costs based on this plan for the years ended December 31, 2005 and 2004 amounted to US\$ 1,500 thousand (R\$ 3,511) and US\$ 6.4 million (R\$ 16,985), respectively.

In July 2002, the Board of Directors of AmeriSteel approved the issue of new purchase options under the SAR Plan, which were granted to the executive directors, with the exercise price determined by the fair value at the date of grant. A total of 6,244,722 SARs were authorized and issued. One-third of all awarded options and common shares are vested two years as from the date of grant, and one-third after each subsequent two-year period. The options may be exercised in up to ten years after the date of grant.

At December 31, 2005, the expense related to this plan, recorded in the Consolidated financial statements, was US\$ 1,500 thousand, equivalent to R\$ 3,511 (US\$ 14,300 thousand, equivalent to R\$ 37,952 in 2004).

**b.5) Equity ownership**

In September 1996, the Board of Directors of AmeriSteel approved the Equity Ownership Plan of AmeriSteel Corporation (the "Equity Ownership" Plan), which grants common shares, purchase options for common shares and SARs. The maximum

number of shares that may be issued under this plan is 4,152,286. AmeriSteel granted 4,667,930 incentive stock options and 492,955 common shares under the Equity Ownership Plan up to December 31, 2004. One-third of all options and common shares issued become vested two years from the date of the grant, and one-third after each subsequent two-year period. All grants were carried out at the market value of the common shares at the date of grant, determined on the basis of an independent appraisal at the end of the prior year. The options may be exercised for ten years as from the date of the grant.

#### b.6) Purchase plan

In May 1995, the Board of Directors of AmeriSteel approved an option/purchase plan (the "Purchase Plan"), available to essentially all employees. The employees who purchased shares were rewarded with options for six times the number of shares purchased. A total of 356,602 shares were sold under the Purchase Plan at a purchase price of US\$ 1.12 per share. The options were granted at market value at the date of the grant, determined on the basis of an independent appraisal at the end of the prior year. A total of 2,139,612 options were granted under the Purchase Plan. No options are available for future grant. All options granted can already be exercised, which may occur for ten years as from the date of the grant.

A summary of the Gerdau Ameristeeel plans is as follows:

	2005			2004		
	Number of shares	Average exercise price		Number of shares	Average exercise price	
		US\$	R\$		US\$	R\$
Available at the beginning of the year....	2,833,288	5.94	13.90	3,606,570	6.41	17.01
Options exercised .....	(443,371)	1.86	4.35	(375,261)	1.90	5.04
Options cancelled.....	(26,341)	1.85	4.33	(76,321)	1.92	5.10
Options expired.....	(99,000)	19.00	44.47	(321,700)	19.46	51.65
Available at the end of the year.....	<u>2,264,576</u>	6.42	15.03	<u>2,833,288</u>	5.94	15.77
Exercisable shares.....	<u>2,128,241</u>			<u>2,350,378</u>		

The table below summarizes the information on the purchase options of Gerdau Ameristeeel shares available on December 31, 2005:

Exercise price	Number available	Average grace period	Average exercise price		Number exercisable at December 31,2005
			US\$	R\$	
US\$ 1.32 to US\$ 1.43 (R\$ 3.09 to R\$ 3.35).....	545,482	3.80	1.39	3.25	545,482
US\$ 1.80 to US\$ 1.90 (R\$ 4.21 to R\$ 4.45).....	671,369	5.20	1.84	4.31	535,034
US\$ 2.11 to US\$ 2.96 (R\$ 4.94 to R\$ 6.93).....	454,725	3.50	2.61	6.11	454,725
US\$ 15.45 to US\$ 18.69 (R\$ 36.16 to R\$ 43.75).....	297,500	1.50	17.41	40.75	297,500
US\$ 20.06 to US\$ 20.15 (R\$ 46.95 to R\$ 47.65).....	295,500	0.90	20.91	48.94	295,500
	<u>2,264,576</u>				<u>2,128,241</u>

The effect on net income for the year and shareholders' equity would have been as follows had the expenses for the option plans of Gerdau S.A. and Gerdau Ameristeeel Corporation been recorded:

	Net income	Consolidated Shareholders' equity
Balances according to the financial statements (*).....	3,268,844	3,859,568
Expense (**).....	(3,125)	(11,040)
Pro forma balances.....	<u>3,265,719</u>	<u>3,848,528</u>

(\*) Net income includes minority interest.

(\*\*) Applying the fair value method (Black Scholes model).

#### 27 - OTHER OPERATING INCOME

Other operating income refers mainly to the amount of R\$ 70,332 (Company and Consolidated) recorded following the favorable outcome of the litigation for incorrect payment of PIS (Social Integration Program), according to Note 20.III item a.2, and reversals and new provisions for contingencies commented in Note 20.

#### 28 - NON-OPERATING INCOME

Non-operating income refers mainly to the gain on change in percentage ownership of R\$ 305,839 (Consolidated), resulting from the merger of Gerdau Participações S.A. by Gerdau Açominas S.A..

#### 29 - CALCULATION OF EBITDA

	Consolidated	
	2005	2004
Gross profit .....	5,725,887	6,245,024
Selling expenses .....	(514,443)	(455,175)
General and administrative expenses.....	(1,167,080)	(1,050,953)
Depreciation and amortization.....	838,760	766,819
EBITDA.....	<u>4,883,124</u>	<u>5,505,715</u>

## 30 – INFORMATION BY GEOGRAPHICAL AREA AND BUSINESS SEGMENT

	Geographical Area							
	Brazil		South America (*)		North America		Consolidated	
	2005	2004	2005	2004	2005	2004	2005	2004
Net sales revenues.....	9,997,575	9,975,760	1,194,089	763,865	10,054,084	8,857,637	21,245,748	19,597,262
Cost of sales.....	(6,211,632)	(5,668,217)	(831,440)	(488,120)	(8,476,789)	(7,195,901)	(15,519,861)	(13,352,238)
Gross profit.....	3,785,943	4,307,543	362,649	275,745	1,577,295	1,661,736	5,725,887	6,245,024
Selling expenses.....	(447,342)	(400,317)	(33,395)	(7,079)	(33,706)	(47,779)	(514,443)	(455,175)
General and administrative expenses.....	(776,605)	(751,200)	(79,902)	(45,934)	(310,573)	(253,819)	(1,167,080)	(1,050,953)
Financial income (expenses), net.....	189,867	33,673	(22,836)	(4,491)	(124,881)	(177,563)	42,150	(148,381)
Operating profit.....	2,790,631	3,022,950	222,198	219,272	1,056,166	1,194,708	4,068,995	4,436,930
Net income (**)	2,417,389	2,270,548	166,337	174,240	685,118	896,309	3,268,844	3,341,097
EBITDA (***)	3,110,287	3,657,500	292,430	250,983	1,480,407	1,597,232	4,883,124	5,505,715

(\*) Does not include Brazilian operations.

(\*\*) Net income for the year before minority interest.

(\*\*\*) Profit before financial expenses, income tax and social contribution on net income, depreciation and amortization as shown in Note 28.

The segments shown below correspond to the business units through which the Gerdaul Executive Committee manages its operations: Aços Longos Brasil, Açominas (corresponding to the operations of the plants located in Ouro Branco, Minas Gerais), Aços Especiais, South America (excluding Brazilian operations) and North America (Gerdaul Ameristeel):

	Business Segments											
	Longos Brasil		Açominas		South America (*)		Consolidated					
	2005	2004	Ouro Branco	Aços Especiais	2005	2004	2005	2004				
Net sales revenues.....	6,246,464	6,456,351	2,681,077	2,646,752	1,070,034	872,657	1,194,089	763,865	10,054,084	8,857,637	21,245,748	19,597,262
Identifiable assets (**)	3,999,504	3,916,049	3,735,219	3,482,517	538,456	462,370	1,349,088	668,351	5,192,457	6,131,526	14,814,724	14,660,813
Capital expenditures.....	656,946	611,779	524,681	265,851	78,427	36,291	359,068	27,367	318,017	1,156,660	1,937,139	2,097,948
Depreciation/amortization.....	246,738	208,868	272,398	265,707	29,155	26,899	43,078	28,251	247,391	237,094	838,760	766,819

(\*) Does not include Brazilian operations.

(\*\*) Identifiable assets: Accounts receivable, inventories and fixed assets.

## CONSELHO DE ADMINISTRAÇÃO

### Presidente

JORGE GERDAU JOHANNPETER

### Vice-Presidentes

GERMANO H. GERDAU JOHANNPETER

KLAUS GERDAU JOHANNPETER

CARLOS JOÃO PETRY

### Conselheiros

AFFONSO CELSO PASTORE

ANDRÉ PINHEIRO DE LARA RESENDE

OSCAR DE PAULA BERNARDES NETO

### Secretário-Geral

EXPEDITO LUZ

## DIRETORIA

### Comitê Executivo

#### Diretor Presidente

JORGE GERDAU JOHANNPETER

#### Diretores Vice-Presidentes

FREDERICO C. GERDAU JOHANNPETER, Vice-Presidente Sênior

CARLOS JOÃO PETRY, Vice-Presidente Sênior

ANDRÉ BIER JOHANNPETER

CLAUDIO JOHANNPETER

FILIPE AFFONSO FERREIRA

MÁRIO LONGHI FILHO

OSVALDO BURGOS SCHIRMER

RICARDO GEHRKE

#### Secretário-Geral

EXPEDITO LUZ

#### Diretores

EXPEDITO LUZ

GERALDO TOFFANELLO

PAULO FERNANDO BINS DE VASCONCELLOS

## REPORT OF INDEPENDENT AUDITORS

To the Board of Directors and Stockholders  
Metalúrgica Gerdau S.A.

1. We have audited the accompanying balance sheets of Metalúrgica Gerdau S.A. and the consolidated balance sheets of Metalúrgica Gerdau S.A. and its subsidiaries as of December 31, 2005 and 2004, and the related statements of income, of changes in stockholders' equity and of changes in financial position of Metalúrgica Gerdau S.A., as well as the related consolidated statements of income and of changes in financial position for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements. The audits of the financial statements of the jointly-owned indirect subsidiary Gallatin Steel Company and of the indirect subsidiaries Diaco S.A. and its subsidiaries and of Siderúrgica del Pacífico S.A. were conducted by other independent auditors and our report, insofar as it relates to the income derived from these companies, equivalent to 5.74% of the profit before taxes of Metalúrgica Gerdau S.A. and 4.41% of the profit before taxes and minority interest of Metalúrgica Gerdau S.A. and its subsidiaries for the year ended December 31, 2005, and to the consolidated assets as of that date equivalent to 4.97% of the total consolidated assets, is based solely on the reports of these other auditors.

2. We conducted our audits in accordance with approved Brazilian auditing standards, which require that we perform the audit to obtain reasonable assurance about whether the financial statements are fairly presented in all material respects. Accordingly, our work included, among other procedures: (a) planning our audit taking into consideration the significance of balances, the volume of transactions and the accounting and internal control systems of the companies, (b) examining, on a test basis, evidence and records supporting the amounts and disclosures in the financial statements, and (c) assessing the accounting practices used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

3. In our opinion, based on our audits and on the reports of the other auditors, the financial statements audited by us present fairly, in all material respects, the financial position of Metalúrgica Gerdau S.A. and of Metalúrgica Gerdau S.A. and its subsidiaries at December 31, 2005 and 2004, and the results of operations, the changes in stockholders' equity and the changes in financial position of Metalúrgica Gerdau S.A., as well as the consolidated results of operations and of changes in financial position, for the years then ended, in accordance with accounting practices adopted in Brazil.

4. Our audits were conducted for the purpose of forming an opinion on the basic financial statements, taken as a whole. The statement of cash flows is presented for purposes of additional analysis and is not a required part of the basic financial statements. This information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly presented in all material respects in relation to the financial statements taken as a whole.

Porto Alegre, February 21, 2006

**PRICEWATERHOUSECOOPERS** 

Auditores Independentes  
CRC 2SP000160/O-5 "F" RS

Carlos Alberto Sousa  
Accountant CRC 1RJ056561/O-0 "S" RS

## OPINION OF THE STATUTORY AUDIT BOARD

The Statutory Audit Board of Metalúrgica Gerdau S.A., in compliance with legal and statutory provisions, has examined the Management Report and the Financial Statements for the year ended December 31, 2005. Based on the examinations made and also considering the opinion of the independent auditors - PricewaterhouseCoopers Auditores Independentes, dated February 21, 2006, as well as the information and explanations received during the year, the Statutory Audit Board is of the opinion that these documents are suitable for presentation to the Annual General Meeting of shareholders.

Porto Alegre, February 21, 2006

DOMINGOS MATIAS URROZ LOPES  
CARLOS ROBERTO SCHRÖDER  
MARIO MAGALHÃES DE SOUSA