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**BT Group plc  
ANNUAL REPORT & FORM 20-F  
2011**



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# FINANCIAL STATEMENTS

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# STATEMENT OF DIRECTORS' RESPONSIBILITIES

The directors are responsible for preparing the Annual Report, the Report on directors' remuneration and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the consolidated financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union, and the parent company financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law). In preparing the consolidated financial statements, the directors have also elected to comply with IFRSs, issued by the International Accounting Standards Board (IASB). Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the group and the company and of the profit or loss of the group for that period. In preparing these financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgments and accounting estimates that are reasonable and prudent;
- state whether IFRSs as adopted by the European Union and IFRSs issued by IASB and applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the consolidated and parent company financial statements respectively; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company and the group and enable them to ensure that the financial statements and the Report on directors' remuneration comply with the Companies Act 2006 and, as regards the consolidated financial statements, Article 4 of the IAS Regulation. They are also responsible for safeguarding the assets of the company and the group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Each of the directors, whose names and functions are listed on pages 60 to 61 confirm that, to the best of their knowledge:

- the consolidated financial statements, which have been prepared in accordance with IFRSs as adopted by the European Union, give a true and fair view of the assets, liabilities, financial position and profit of the group; and
- the Report of the directors on pages 59 to 86 includes a fair review of the development and performance of the business and the position of the group, together with a description of the principal risks and uncertainties that it faces.

# REPORT OF THE INDEPENDENT AUDITORS CONSOLIDATED FINANCIAL STATEMENTS

## United Kingdom opinion

### Independent Auditors' Report to the members of BT Group plc (the 'company')

We have audited the consolidated financial statements of BT Group plc for the year ended 31 March 2011 which comprise the Group income statement, the Group statement of comprehensive income, the Group statement of changes in equity, the Group cash flow statement, the Group balance sheet, the Accounting policies and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

### Respective responsibilities of directors and auditors

As explained more fully in the Statement of directors' responsibilities set out on page 88, the directors are responsible for the preparation of the consolidated financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the consolidated financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

### Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the group's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the BT Group plc Annual Report & Form 20-F for the year ended 31 March 2011 to identify material inconsistencies with the audited consolidated financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

### Opinion on financial statements

In our opinion the consolidated financial statements:

- give a true and fair view of the state of the group's affairs as at 31 March 2011 and of its profit and cash flows for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006 and Article 4 of the IAS Regulation.

### Separate opinion in relation to IFRSs as issued by the IASB

As explained in the Accounting policies section of the consolidated financial statements the group, in addition to complying with its legal obligation to apply IFRSs as adopted by the European Union, has also applied IFRSs as issued by the International Accounting Standards Board (IASB).

In our opinion the consolidated financial statements comply with IFRSs as issued by the IASB.

### Opinion on other matters prescribed by the Companies Act 2006

In our opinion the information given in the Report of the directors for the financial year for which the consolidated financial statements are prepared is consistent with the consolidated financial statements.

### Matters on which we are required to report by exception

We have nothing to report in respect of the following:

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Under the Listing Rules we are required to review:

- the directors' statement, set out on page 54, in relation to going concern;
- the part of the Corporate Governance Statement relating to the company's compliance with the nine provisions of the June 2008 Combined Code specified for our review; and
- certain elements of the Report on directors' remuneration.

### Other matter

We have reported separately on the parent company financial statements of BT Group plc for the year ended 31 March 2011 and on the information in the Report on directors' remuneration that is described as having been audited.

**Philip Rivett (Senior Statutory Auditor)**  
for and on behalf of PricewaterhouseCoopers LLP  
Chartered Accountants and Statutory Auditors  
London, United Kingdom  
11 May 2011

## United States opinion

### Report of Independent Registered Public Accounting Firm to the Board of Directors and Shareholders of BT Group plc (the ‘company’)

In our opinion, the accompanying Group income statements, Group statements of comprehensive income, Group statements of changes in equity, Group cash flow statements and Group balance sheets present fairly, in all material respects, the financial position of BT Group plc and its subsidiaries at 31 March 2011 and 2010 and the results of their operations and cash flows for each of the three years in the period ended 31 March 2011, in conformity with International Financial Reporting Standards (IFRSs) as issued by the International Accounting Standards Board. Also, in our opinion the company maintained, in all material respects, effective internal control over financial reporting as of 31 March 2011, based on criteria established in the Turnbull Guidance.

The company’s management is responsible for these financial statements, for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in management’s evaluation of the effectiveness of internal control over financial reporting as set out in the first three paragraphs of Internal control over financial reporting in the Report of the directors, Business Policies of the BT Group plc Annual Report & Form 20-F.

Our responsibility is to express opinions on these financial statements and on the company’s internal control over financial reporting based on our integrated audits. We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects.

Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and

significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company’s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company’s internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorisations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorised acquisition, use, or disposition of the company’s assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

**PricewaterhouseCoopers LLP**  
London, United Kingdom  
11 May 2011

# CONSOLIDATED FINANCIAL STATEMENTS

## Accounting policies

### (i) Basis of preparation and presentation of the financial statements

#### Compliance with applicable law and IFRS

These consolidated financial statements have been prepared in accordance with the Companies Act 2006, Article 4 of the IAS Regulation and International Accounting Standards (IAS) and International Financial Reporting Standards (IFRS) and related interpretations, as adopted by the European Union. The consolidated financial statements are also in compliance with IFRS as issued by the International Accounting Standards Board.

#### Accounting convention

The consolidated financial statements are prepared on the historical cost basis, except for certain financial and equity instruments that have been measured at fair value.

#### Presentation of specific items

The group's income statement and segmental analysis separately identify trading results before specific items. Specific items are those that in management's judgment need to be disclosed by virtue of their size, nature or incidence. In determining whether an event or transaction is specific, management considers quantitative as well as qualitative factors such as the frequency or predictability of occurrence. This is consistent with the way that financial performance is measured by management and reported to the Board and the *Operating Committee* and assists in providing a meaningful analysis of the trading results of the group. The directors believe that presentation of the group's results in this way is relevant to an understanding of the group's financial performance as specific items are identified by virtue of their size, nature or incidence. Furthermore, the group considers a columnar presentation to be appropriate, as it improves the clarity of the presentation and is consistent with the way that financial performance is measured by management and reported to the Board and the *Operating Committee*. Specific items may not be comparable to similarly titled measures used by other companies.

Items which have been considered to be specific items by virtue of their size, nature or incidence include disposals of businesses and investments, business restructuring programmes, asset impairment charges, property rationalisation programmes and the settlement of multiple tax years in a single payment. In 2011 net interest on pensions has been included in specific items because of its volatile nature, and also BT Global Services contract and financial review charges in 2009, by virtue of their size and nature. Accordingly, specific items for comparative periods have been re-presented to reflect this reclassification. The impact of subsequent changes to the contract and financial review charges from revisions in estimates and assumptions are included within trading results before specific items, and are separately disclosed if considered significant. Specific items for the current and prior years are disclosed in note 8.

#### Critical accounting estimates and key judgements

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed on pages 97 and 98 in **Critical accounting estimates and key judgements**.

#### Composition of the group

The group's principal operating subsidiaries and associate are detailed on page 155.

### (ii) Basis of consolidation

The group financial statements consolidate the financial statements of BT Group plc ('the company') and its subsidiaries, and they incorporate its share of the results of associated and joint ventures using the equity method of accounting.

#### Accounting for subsidiaries

A subsidiary is an entity that is controlled by another entity, known as the parent. Control is the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities generally accompanied by a shareholding of more than one half of the voting rights.

Non-controlling interests in the net assets of consolidated subsidiaries are identified separately from the group's equity. Non-controlling interests consist of the amounts of those interests at the date of the original business combination and non-controlling share of changes in equity since the date of the combination.

The results of subsidiaries acquired or disposed of during the year are consolidated from and up to the date of change of control. Where necessary, adjustments are made to the financial statements of subsidiaries, associates and joint ventures to bring the accounting policies used in line with those used by the group. All intra group transactions including any gains or losses, balances, income or expenses are eliminated in full on consolidation.

Changes in the group's ownership interests in subsidiaries that do not result in the group losing control over the subsidiaries are accounted for as equity transactions. The carrying amounts of the group's interests and the non-controlling interests are adjusted to reflect the changes in their relative interests in the subsidiaries. Any difference between the amount by which the non-controlling interests are adjusted and the fair value of the consideration paid or received is recognised directly in equity.

When the group loses control of a subsidiary, the profit or loss on disposal is calculated as the difference between (i) the aggregate of the fair value of the consideration received and the fair value of any retained interest and (ii) the previous carrying amount of the assets (including goodwill), and liabilities of the subsidiary and any non-controlling interests.

#### Interests in associates and joint ventures

An associate is an entity over which another entity has significant influence and that is neither a subsidiary nor an interest in a joint venture. Significant influence is the power to participate in the financial and operating policy decisions of an entity but is not control or joint control over those policies.

A joint venture is an entity that is jointly controlled by two or more entities. Joint control is the contractually agreed sharing of control over an economic activity, and exists only when the strategic financial and operating decisions relating to the activity require the unanimous consent of the parties sharing control.

Investments in associates and joint ventures are initially recognised at cost. Any excess of the cost of acquisition over the group's share of the net fair value of the identifiable assets, liabilities and contingent liabilities of an associate or joint venture at the date of acquisition is recognised as goodwill, which is included within the carrying amount of the investment.

Subsequent to acquisition, the carrying value of the group's investment in associates and joint ventures includes the group's share

of post acquisition reserves, less any impairment in the value of individual assets. The income statement reflects the group's share of the results of operations after tax of the associate or joint venture.

When a group entity transacts with its associate or a joint venture, profits and losses resulting from the transactions with the associate or joint venture are recognised in the consolidated financial statements only to the extent of interests in the associate that are not related to the group.

### (iii) Business combinations

Acquisitions of businesses are accounted for using the acquisition method of accounting. The consideration transferred is measured at fair value, which is the aggregate of the fair values of the assets transferred, liabilities incurred or assumed and the equity instruments issued in exchange for control of the acquiree. Acquisition related costs are generally expensed as incurred. The acquiree's identifiable assets and liabilities are recognised at their fair value at the acquisition date.

Goodwill arising on acquisition is recognised as an asset and measured at cost representing the excess of the aggregate of the consideration, the amount of any non-controlling interests in the acquiree, and the fair value of the acquirer's previously held equity interest in the acquiree (if any) over the net of the fair values of the identifiable assets and liabilities at the date of acquisition.

Non-controlling interests that entitle their holders to a proportionate share of the entity's net assets in the event of liquidation may be initially measured either at fair value or at the non-controlling interests' proportionate share of the recognised amounts of the acquiree's identifiable net assets. The choice of measurement basis is made on a transaction by transaction basis.

When the consideration in a business combination includes contingent consideration, it is measured at its acquisition date fair value. Changes in the fair value of the contingent consideration that qualify as measurement period adjustments are adjusted retrospectively, with corresponding adjustments against goodwill. Measurement period adjustments are adjustments that arise from additional information obtained during the 'measurement period', which cannot exceed one year from the acquisition date, about facts and circumstances that existed at the acquisition date.

The subsequent accounting for changes in the fair value of the contingent consideration that do not qualify as measurement period adjustments depends on how the contingent consideration is classified. Contingent consideration that is classified as equity is not remeasured and its subsequent settlement is accounted for within equity. Contingent consideration that is classified as an asset or a liability is remeasured with the corresponding gain or loss being recognised in profit or loss.

When a business combination is achieved in stages, the group's previously held equity interest in the acquiree is remeasured to fair value at the acquisition date and the resulting gain or loss, if any, is recognised in profit or loss.

Business combinations that took place prior to 1 April 2010 were accounted for in accordance with the previous version of IFRS 3.

### (iv) Revenue

Revenue represents the fair value of the consideration received or receivable for communication services and equipment sales, net of discounts and sales taxes. Revenue from the rendering of services and sale of equipment is recognised when it is probable that the economic benefits associated with a transaction will flow to the group and the amount of revenue and associated costs can be

measured reliably. Where the group acts as an agent in a transaction, it recognises revenue net of directly attributable costs.

#### Services

Revenue arising from separable installation and connection services is recognised when it is earned, upon activation. Revenue from the rental of analogue and digital lines and private circuits is recognised evenly over the period to which the charges relate. Revenue from calls is recognised at the time the call is made over the group's network.

Subscription fees, consisting primarily of monthly charges for access to broadband and other internet access or voice services, are recognised as revenue as the service is provided. Revenue arising from the interconnection of voice and data traffic between other telecommunications operators is recognised at the time of transit across the group's network.

#### Equipment sales

Revenue from the sale of peripheral and other equipment is recognised when all the significant risks and rewards of ownership are transferred to the buyer, which is normally the date the equipment is delivered and accepted by the customer.

#### Long-term contractual arrangements

Revenue from long-term contractual arrangements is recognised based on the percentage of completion method. The stage of completion is estimated using an appropriate measure according to the nature of the contract. For long-term services contracts, revenue is recognised on a straight line basis over the term of the contract. However, if the performance pattern is other than straight line, revenue is recognised as services are provided, usually on an output or consumption basis. For fixed price contracts, including contracts to design and build software solutions, revenue is recognised by reference to the stage of completion, as determined by the proportion of costs incurred relative to the estimated total contract costs, or other measures of completion such as the achievement of contract milestones and customer acceptance. In the case of time and materials contracts, revenue is recognised as the service is rendered.

Costs related to delivering services under long-term contractual arrangements are expensed as incurred. An element of costs incurred in the initial set up, transition or transformation phase of the contract is deferred and recorded within non-current assets. These costs are then recognised in the income statement on a straight line basis over the remaining contractual term, unless the pattern of service delivery indicates a different profile is appropriate. These costs are directly attributable to specific contracts, relate to future activity, will generate future economic benefits and are assessed for recoverability on a regular basis.

The percentage of completion method relies on estimates of total expected contract revenues and costs, as well as reliable measurement of the progress made towards completion. Unless the financial outcome of a contract can be estimated with reasonable certainty, no attributable profit is recognised. In such circumstances, revenue is recognised equal to the costs incurred to date, to the extent that such revenue is expected to be recoverable. Recognised revenue and profits are subject to revisions during the contract if the assumptions regarding the overall contract outcome are changed. The cumulative impact of a revision in estimates is recorded in the period in which such revisions become likely and can be estimated. Where the actual and estimated costs to completion exceed the estimated revenue for a contract, the full contract life loss is recognised immediately.

Where a contractual arrangement consists of two or more separate elements that have value to a customer on a standalone basis, revenue is recognised for each element as if it were an individual contract. The total contract consideration is allocated between the separate elements on the basis of relative fair value and the appropriate revenue recognition criteria are applied to each element as described above.

### (v) Other operating income

Other operating income is income generated by the group that arises from activities outside of the provision of communication services and equipment sales. Items reported as other operating income include income from repayment works, proceeds from scrap and cable recovery, income generated by our fleet operations, income from government grants, profits and losses on the disposal of business operations and property, plant and equipment and income generated from the exploitation of our intellectual property.

### (vi) Government grants

Government grants are recognised initially as deferred income at their fair value where there is a reasonable assurance that the grant will be received and the group will comply with the conditions associated with the grant. Grants that compensate the group for expenses incurred are recognised in the income statement within other operating income in the same periods in which the associated expenditure is recognised. Grants that compensate the group for the cost of an asset are recognised in the income statement in other operating income on a straight line basis over the useful life of the asset.

### (vii) Leases

The determination of whether an arrangement is, or contains, a lease is based on the substance of the arrangement and requires an assessment of whether the fulfilment of the arrangement is dependent on the use of a specific asset or assets and whether the arrangement conveys the right to use the asset.

Leases of property, plant and equipment where the group holds substantially all the risks and rewards of ownership are classified as finance leases.

Finance lease assets are capitalised at the commencement of the lease term at the lower of the present value of the minimum lease payments or the fair value of the leased asset. The obligations relating to finance leases, net of finance charges in respect of future periods, are recognised as liabilities. Leases are subsequently measured at amortised cost using the effective interest method. If a sale and leaseback transaction results in a finance lease, any excess of sale proceeds over the carrying amount is deferred and recognised in the income statement over the lease term.

Leases where a significant portion of the risks and rewards are held by the lessor are classified as operating leases. Rentals are charged to the income statement on a straight line basis over the period of the lease. If a sale and leaseback transaction results in an operating lease, any profit or loss is recognised in the income statement immediately, except where a proportion of the profit or loss is deferred or amortised because the sale price was not equal to fair value.

### (viii) Foreign currencies

Items included in the financial statements of each of the group's subsidiaries are measured using the currency of the primary economic environment in which the entity operates (the functional

currency). The consolidated financial statements are presented in Sterling, the presentation currency of the group.

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the date of the transaction. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation of monetary assets and liabilities denominated in foreign currencies at period end exchange rates are recognised in the income statement in the line which most appropriately reflects the nature of the item or transaction. Where monetary items form part of the net investment in a foreign operation and are designated as hedges of a net investment or as cash flow hedges, such exchange differences are recognised in equity.

On consolidation, assets and liabilities of foreign undertakings are translated into Sterling at year end exchange rates. The results of foreign undertakings are translated into Sterling at average rates of exchange for the year (unless this average is not a reasonable approximation of the cumulative effects of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions). Foreign exchange differences arising on retranslation are recognised directly in a separate component of equity, the translation reserve.

In the event of the disposal of an undertaking with assets and liabilities denominated in a foreign currency, the cumulative translation difference associated with the undertaking in the translation reserve is charged or credited to the gain or loss on disposal recognised in the income statement.

### (ix) Intangible assets

Identifiable intangible assets are recognised when the group controls the asset, it is probable that future economic benefits attributable to the asset will flow to the group and the cost of the asset can be reliably measured. All intangible assets, other than goodwill and indefinite lived assets, are amortised over their useful economic life. The method of amortisation reflects the pattern in which the assets are expected to be consumed. If the pattern cannot be determined reliably, the straight line method is used.

#### Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the group's share of the identifiable net assets (including intangible assets) of the acquired subsidiary. Goodwill is reviewed annually for impairment and carried at cost less accumulated impairment losses.

#### Computer software

Computer software comprises computer software purchased from third parties, and also the cost of internally developed software. Computer software purchased from third parties and internally developed software is initially recorded at cost.

#### Telecommunication licences

Licence fees paid to governments, which permit telecommunication activities to be operated for defined periods, are initially recorded at cost and amortised from the time the network is available for use to the end of the licence period.

#### Brands, customer lists and customer relationships

Intangible assets acquired through business combinations are recorded at fair value at the date of acquisition. Assumptions are used in estimating the fair values of acquired intangible assets and include management's estimates of revenue and profits to be generated by the acquired businesses.

**Subscriber acquisition costs**

Subscriber acquisition costs are expensed as incurred, unless they meet the criteria for capitalisation, in which case they are capitalised and amortised over the shorter of the expected customer life or contractual period.

**Estimated useful economic lives**

The estimated useful economic lives assigned to the principal categories of intangible assets are as follows:

Computer software	2 to 10 years
Telecommunication licences	1 to 5 years
Brands, customer lists and customer relationships	3 to 15 years

**(x) Research and development**

Research expenditure is recognised in the income statement in the period in which it is incurred.

Development expenditure, including the cost of internally developed software, is recognised in the income statement in the period in which it is incurred unless it is probable that economic benefits will flow to the group from the asset being developed, the cost of the asset can be reliably measured and technical feasibility can be demonstrated. Capitalisation ceases when the asset being developed is ready for use.

Research and development costs include direct and indirect labour, materials and directly attributable overheads.

**(xi) Property, plant and equipment**

Property, plant and equipment is included in the balance sheet at historical cost, less accumulated depreciation and any impairment losses. On disposal of property, plant and equipment, the difference between the sale proceeds and the net book value at the date of disposal is recorded in the income statement.

**Cost**

Included within the cost for network infrastructure and equipment are direct labour, contractors' charges, materials and directly attributable overheads.

**Depreciation**

Depreciation is provided on property, plant and equipment on a straight line basis from the time the asset is available for use, so as to write off the asset's cost over the estimated useful life taking into account any expected residual value. Freehold land is not subject to depreciation. The lives assigned to principal categories of assets are as follows:

<b>Land and buildings</b>	
Freehold buildings	40 years
Leasehold land and buildings	Unexpired portion of lease or 40 years, whichever is the shorter
<b>Network infrastructure and equipment</b>	
Transmission equipment:	
Duct	40 years
Cable	3 to 25 years
Fibre	5 to 20 years
Exchange equipment	2 to 13 years
Payphones and other network equipment	2 to 20 years
Other	
Motor vehicles	2 to 9 years
Computers and office equipment	3 to 6 years

Assets held under finance leases are depreciated over the shorter of the lease term or their useful economic life. Residual values and useful lives are reassessed annually and, if necessary, changes are recognised prospectively.

**(xii) Borrowing costs**

In respect of borrowing costs relating to qualifying assets which take more than 12 months to complete, the group capitalises borrowing costs during the construction phase as part of the cost of that asset.

**(xiii) Asset impairment (non financial assets)**

Intangible assets with finite useful lives and property, plant and equipment are tested for impairment if events or changes in circumstances (assessed at each reporting date) indicate that the carrying amount may not be recoverable. When an impairment test is performed, the recoverable amount is assessed by reference to the higher of the net present value of the expected future cash flows (value in use) of the relevant cash generating unit and the fair value less cost to sell.

Goodwill and intangible assets with indefinite useful lives are reviewed for impairment at least annually.

Impairment losses are recognised in the income statement.

If a cash generating unit is impaired, provision is made to reduce the carrying amount of the related assets to their estimated recoverable amount, normally as a specific item. Impairment losses are allocated firstly against goodwill, and secondly on a pro rata basis against intangible and other assets.

Where an impairment loss has been recognised against an asset, it may be reversed in future periods where there has been a change in the estimates used to determine the recoverable amount since the last impairment loss was recognised, but only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised. This does not apply for goodwill, for which an impairment loss may not be reversed in any circumstances.

**(xiv) Inventory**

Inventory mainly comprises items of equipment held for sale or rental and consumable items.

Equipment held and consumable items are stated at the lower of cost and estimated net realisable value, after provisions for obsolescence. Cost is calculated on a first-in-first-out basis.

**(xv) Termination benefits**

Termination benefits (leaver costs) are payable when employment is terminated before the normal retirement date, or when an employee accepts voluntary redundancy in exchange for these benefits. The group recognises termination benefits when it is demonstrably committed to the affected employees leaving the group.

**(xvi) Post retirement benefits**

The group operates a funded defined benefit pension plan, which is administered by an independent Trustee, for the majority of its employees.

The group's obligation in respect of defined benefit pension plans is calculated separately for each scheme by estimating the amount of future benefit that employees have earned in return for their service to date. That benefit is discounted to determine its present value, and the fair value of any plan assets is deducted to arrive at the net pension obligation or asset. The discount rate used is the

yield at the balance sheet date on AA credit rated bonds that have maturity dates approximating the terms of the group's obligations. The calculation is performed by a qualified actuary using the projected unit credit method. The net obligation or asset recognised in the balance sheet is the present value of the defined benefit obligation less the fair value of the plan assets.

The income statement charge is allocated between an operating charge and net finance expense or income. The operating charge reflects the service cost which is spread systematically over the working lives of the employees. The net finance charge reflects the unwinding of the discount applied to the liabilities of the plan, offset by the expected return on the assets of the plan, based on conditions prevailing at the start of the year.

Actuarial gains and losses are recognised in full in the period in which they occur and are presented in the statement of comprehensive income. During 2011 this includes the impact of the change from RPI to CPI as detailed in note 23 on page 131.

Actuarial valuations of the main defined benefit plan are carried out by an independent actuary as determined by the Trustee at intervals of not more than three years, to determine the rates of contribution payable. The pension cost is determined on the advice of the group's actuary, having regard to the results of these Trustee valuations. In any intervening years, the actuaries review the continuing appropriateness of the contribution rates.

The group also operates defined contribution pension schemes and the income statement is charged with the contributions payable.

### (xvii) Share-based payment

The group operates a number of equity settled share-based payment arrangements, under which the group receives services from employees as consideration for equity instruments (share options and shares) of the group. Equity settled share-based payments are measured at fair value (excluding the effect of non market-based vesting conditions) at the date of grant, but including any market-based performance criteria and the impact of non-vesting conditions (for example the requirement for employees to save). The fair value determined at the grant date is recognised on a straight-line basis over the vesting period, based on the group's estimate of the options or shares that will eventually vest and adjusted for the effect of non market-based vesting conditions.

Fair value is measured using either the Binomial options pricing model or Monte Carlo simulations, whichever is most appropriate to the award.

Service and performance conditions are vesting conditions. Any other conditions are non-vesting conditions which have to be taken into account to determine the fair value of equity instruments granted. In the case that an award or option does not vest as a result of a failure to meet a non-vesting condition that is within the control of either counterparty, this is accounted for as a cancellation. Cancellations must be treated as accelerated vesting and all remaining future charges are immediately recognised. As the requirement to save under an employee sharesave arrangement is a non-vesting condition, employee cancellations must be treated as an accelerated vesting.

### (xviii) Taxation

Current income tax is calculated on the basis of the tax laws enacted or substantively enacted at the balance sheet date in the countries where the company's subsidiaries, associates and joint ventures operate and generate taxable income. The group periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation, and the

group establishes provisions where appropriate on the basis of the amounts expected to be paid to tax authorities.

Deferred tax is recognised, using the liability method, in respect of temporary differences between the carrying amount of the group's assets and liabilities and their tax base, except to the extent that the deferred tax asset or liability arises from the initial recognition of goodwill or from the initial recognition of an asset or liability in a transaction which is not a business combination and affects neither accounting profit nor taxable profit.

Deferred tax liabilities are, where permitted, offset against deferred tax assets within the same taxable entity or qualifying local tax group. Any remaining deferred tax asset is recognised only when, on the basis of all available evidence, it can be regarded as probable that there will be suitable taxable profits, within the same jurisdiction, in the foreseeable future against which the deductible temporary difference can be utilised.

Deferred tax is determined using tax rates that are expected to apply in the periods in which the asset is realised or liability settled, based on tax rates and laws that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is provided on temporary differences arising on investments in subsidiaries, associates and joint ventures, except where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

Current and deferred tax are recognised in the income statement, except when the tax relates to items charged or credited directly in equity, in which case the tax is also recognised in equity.

### (xix) Dividends

Final dividends are recognised as a liability in the year in which they are declared and approved by the company's shareholders in the annual general meeting. Interim dividends are recognised when they are paid.

### (xx) Provisions

Provisions are recognised when the group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation and the amount can be reliably estimated. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability. Financial liabilities within provisions are initially recognised at fair value and subsequently carried at amortised cost using the effective interest method. Onerous lease provisions have been measured at the lower of the cost to fulfil the contract or the cost to exit it.

### (xxi) Financial instruments

#### Recognition and derecognition of financial assets and financial liabilities

Financial assets and financial liabilities are recognised when the group becomes party to the contractual provisions of the instrument. Financial assets are derecognised when the group no longer has rights to cash flows, the risks and rewards of ownership or control of the asset. Financial liabilities are derecognised when the obligation under the liability is discharged, cancelled or expires. In particular, for all regular way purchases and sales of financial assets, the group recognises the financial assets on the settlement date, which is the date on which the asset is delivered to or by the group.

## Financial assets

### Financial assets at fair value through income statement

A financial asset is classified in this category if acquired principally for the purpose of selling in the short-term (held for trading) or if so designated by management. Financial assets held in this category are initially recognised and subsequently measured at fair value, with changes in value recognised in the income statement in the line which most appropriately reflects the nature of the item or transaction. The direct transaction costs are recognised immediately in the income statement.

### Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market other than those for which the group may not recover substantially all of its initial investment, other than because of credit deterioration, which are classified as available-for-sale.

Loans and receivables are initially recognised at fair value plus transaction costs and subsequently carried at amortised cost using the effective interest method, with changes in carrying value recognised in the income statement in the line which most appropriately reflects the nature of the item or transaction.

### Available-for-sale financial assets

Non-derivative financial assets classified as available-for-sale are either specifically designated in this category or not classified in any of the other categories. Available-for-sale financial assets are initially recognised at fair value plus direct transaction costs and then re-measured at subsequent reporting dates to fair value, with unrealised gains and losses (except for changes in exchange rates for monetary items, interest, dividends and impairment losses, which are recognised in the income statement) recognised in equity until the financial asset is derecognised, at which time the cumulative gain or loss previously recognised in equity is taken to the income statement, in the line that most appropriately reflects the nature of the item or transaction.

### Trade and other receivables

Financial assets within trade and other receivables are initially recognised at fair value, which is usually the original invoiced amount, and are subsequently carried at amortised cost using the effective interest method less provisions made for doubtful receivables.

Provisions are made specifically where there is evidence of a risk of non payment, taking into account ageing, previous losses experienced and general economic conditions.

### Cash and cash equivalents

Cash and cash equivalents comprise cash in hand and current balances with banks and similar institutions, which are readily convertible to cash and which are subject to insignificant risk of changes in value and have an original maturity of three months or less.

For the purpose of the consolidated cash flow statement, cash and cash equivalents are as defined above net of outstanding bank overdrafts. Bank overdrafts are included within loans and other borrowings, in current liabilities on the balance sheet.

### Impairment of financial assets

The group assesses at each balance sheet date whether a financial asset or group of financial assets are impaired.

Where there is objective evidence that an impairment loss has arisen on assets carried at amortised cost, the carrying amount is reduced with the loss being recognised in the income statement. The impairment loss is measured as the difference between that asset's carrying amount and the present value of estimated future

cash flows discounted at the financial asset's original effective interest rate. The impairment loss is only reversed if it can be related objectively to an event after the impairment was recognised and is reversed to the extent that the carrying value of the asset does not exceed its amortised cost at the date of reversal.

If an available-for-sale asset is impaired, an amount comprising the difference between its cost (net of any principal payment and amortisation) and its fair value is transferred from equity to the income statement. Reversals of impairment losses on debt instruments are taken through the income statement if the increase in fair value of the instrument can be objectively related to an event occurring after the impairment loss was recognised in the income statement. Reversals in respect of equity instruments classified as available-for-sale are recognised directly in equity.

If there is objective evidence that an impairment loss has been incurred on an unquoted equity instrument that is not carried at fair value because its fair value cannot be objectively measured, or on a derivative asset that is linked to and must be settled by delivery of such an unquoted equity instrument, the amount of loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the current market rate of return for a similar financial asset.

## Financial liabilities

### Trade and other payables

Financial liabilities within trade and other payables are initially recognised at fair value, which is usually the original invoiced amount, and subsequently carried at amortised cost using the effective interest method.

### Loans and other borrowings

Loans and other borrowings are initially recognised at fair value plus directly attributable transaction costs. Where loans and other borrowings contain a separable embedded derivative, the fair value of the embedded derivative is the difference between the fair value of the hybrid instrument and the fair value of the loan or borrowing. The fair value of the embedded derivative and the loan or borrowing is recorded separately on initial recognition. Loans and other borrowings are subsequently measured at amortised cost using the effective interest method and, if included in a fair value hedge relationship, are revalued to reflect the fair value movements on the hedged risk associated with the loans and other borrowings. The resultant amortisation of fair value movements, on de-designation of the hedge, are recognised in the income statement.

### Financial guarantees

Financial guarantees are recognised initially at fair value plus transaction costs and subsequently measured at the higher of the amount determined in accordance with the accounting policy relating to provisions and the amount initially determined less, when appropriate, cumulative amortisation.

### Derivative financial instruments

The group uses derivative financial instruments mainly to reduce exposure to foreign exchange risks and interest rate movements. The group does not hold or issue derivative financial instruments for financial trading purposes. However, derivatives that do not qualify for hedge accounting are accounted for as trading instruments.

Derivative financial instruments are classified as held for trading and are initially recognised and subsequently measured at fair value. The gain or loss on re-measurement to fair value is recognised immediately in the income statement in net finance expense. However, where derivatives qualify for hedge accounting, recognition of any resultant gain or loss depends on the nature of the

hedge. Derivative financial instruments are classified as current assets or current liabilities where they have a maturity period within 12 months. Where derivative financial instruments have a maturity period greater than 12 months, they are classified within either non-current assets or non-current liabilities.

Derivatives embedded in other financial instruments or other host contracts are treated as separate derivatives when their risk and characteristics are not closely related to those of the host contract and the host contract is not carried at fair value. Changes in the fair value of embedded derivatives are recognised in the income statement in the line which most appropriately reflects the nature of the item or transaction.

### Hedge accounting

To qualify for hedge accounting, hedge documentation must be prepared at inception and the hedge must be expected to be highly effective both prospectively and retrospectively. The hedge is tested for effectiveness at inception and in subsequent periods in which the hedge remains in operation.

### Cash flow hedge

When a financial instrument is designated as a hedge of the variability in cash flows of a recognised asset or liability, or a highly probable transaction, the effective part of any gain or loss on the derivative financial instrument is recognised directly in equity.

For cash flow hedges of recognised assets or liabilities, the associated cumulative gain or loss is removed from equity and recognised in the same line in the income statement in the same period or periods during which the hedged transaction affects the income statement.

For highly probable transactions, when the transaction subsequently results in the recognition of a non financial asset or non financial liability the associated cumulative gain or loss is removed from equity and included in the initial cost or carrying amount of the non financial asset or liability.

If a hedge of a highly probable transaction subsequently results in the recognition of a financial asset or a financial liability, then the associated gains and losses that were recognised directly in equity are reclassified into the income statement in the same period or periods during which the asset acquired or liability assumed affects the income statement.

Any ineffectiveness arising on a cash flow hedge of a recognised asset or liability is recognised immediately in the same income statement line as the hedged item. Where ineffectiveness arises on highly probable transactions, it is recognised in the line which most appropriately reflects the nature of the item or transaction.

### Fair value hedge

When a derivative financial instrument is designated as a hedge of the variability in fair value of a recognised asset or liability, or unrecognised firm commitment, the change in fair value of the derivatives that are designated as fair value hedges are recorded in the same line in the income statement, together with any changes in fair value of the hedged asset or liability that is attributable to the hedged risk.

### Hedge of net investment in a foreign operation

Exchange differences arising from the retranslation of currency instruments designated as hedges of net investments in a foreign operation are taken to shareholders' equity on consolidation to the extent that the hedges are deemed effective.

Any ineffectiveness arising on a hedge of a net investment in a foreign operation is recognised in net finance expense.

### Discontinuance of hedge accounting

Discontinuance of hedge accounting may occur when a hedging instrument expires or is sold, terminated or exercised, or when the hedge no longer qualifies for hedge accounting or the group revokes designation of the hedge relationship but the hedged financial asset or liability remains or a highly probable transaction is still expected to occur.

Under a cash flow hedge, the cumulative gain or loss at that point remains in equity and is recognised in accordance with the above policy when the transaction occurs. If the hedged transaction is no longer expected to take place or the underlying hedged financial asset or liability no longer exists, the cumulative unrealised gain or loss recognised in equity is recognised immediately in the income statement. Under a hedge of a net investment, the cumulative gain or loss remains in equity when the hedging instrument expires or is sold, terminated or exercised, or when the hedge no longer qualifies for hedge accounting or the group revokes designation of the hedge relationship. The cumulative gain or loss is recognised in the income statement as part of the profit on disposal when the net investment in the foreign operation is disposed. Under a fair value hedge, the cumulative gain or loss adjustment associated with the hedged risk is amortised over the income statement using the effective interest method over the remaining term of the hedged item.

### Share capital

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of new shares are shown in equity as a deduction from the proceeds received. Shares in the parent company, BT Group plc, held by employee share ownership trusts and repurchased treasury shares are recorded in the balance sheet as a deduction from shareholders' equity at cost.

### Critical accounting estimates and key judgements

The preparation of financial statements in conformity with IFRSs requires the use of accounting estimates and assumptions. It also requires management to exercise its judgement in the process of applying the group's accounting policies. We continually evaluate our estimates, assumptions and judgements based on available information and experience. As the use of estimates is inherent in financial reporting, actual results could differ from these estimates. The areas involving a higher degree of judgement or complexity are described below.

### Long-term customer contracts

Long-term customer contracts can extend over a number of financial years. During the contractual period recognition of costs and profits may be impacted by estimates of the ultimate profitability of each contract. If, at any time, these estimates indicate that any contract will be unprofitable, the entire estimated loss for the contract is recognised immediately. If these estimates indicate that any contract will be less profitable than previously forecast, contract assets may have to be written down to the extent they are no longer considered to be fully recoverable. The group performs ongoing profitability reviews of its contracts in order to determine whether the latest estimates are appropriate. Key factors reviewed include:

- Transaction volumes or other inputs affecting future revenues which can vary depending on customer requirements, plans and market position and other factors such as general economic conditions;
- Our ability to achieve key contract milestones connected with the transition, development, transformation and deployment phases for customer contracts;
- The status of commercial relations with customers and the implication for future revenue and cost projections; and

- Our estimates of future staff and third party costs and the degree to which cost savings and efficiencies are deliverable.

The carrying value of assets comprising the costs of the initial set up, transition or transformation phase of long-term networked IT services contracts are disclosed in note 19.

#### Interconnect income and payments to other telecommunications operators

In certain instances, BT relies on other operators to measure the traffic flows interconnecting with our networks. Estimates are used in these cases to determine the amount of income receivable from, or payments we need to make to, these other operators. The prices at which these services are charged are often regulated and may be subject to retrospective adjustment by regulators, and estimates are used in assessing the likely effect of these adjustments.

#### Pension obligations

BT has a commitment, mainly through the BTPS, to pay pension benefits to approximately 327,500 people over approximately 60 years. The cost of these benefits and the present value of our pension liabilities depend on such factors as the life expectancy of the members, the salary progression of our current employees, the return that the pension fund assets will generate in the time before they are used to fund the pension payments, price inflation and the discount rate used to calculate the net present value of the future pension payments. We use estimates for all of these factors in determining the pension costs and liabilities incorporated in our financial statements. The assumptions reflect historical experience and our judgement regarding future expectations.

The value of the net pension obligation at 31 March 2011 and the key financial assumptions used to measure the obligation are disclosed in note 23.

#### Useful lives for property, plant and equipment and software

The plant and equipment in BT's networks is long lived with cables and switching equipment operating for over 10 years and underground ducts being used for decades. BT also develops software for use in IT systems and platforms that supports the products and services provided to our customers and that is also used within the group. The annual depreciation and amortisation charge is sensitive to the estimated service lives allocated to each type of asset. Asset lives are assessed annually and changed when necessary to reflect current thinking on their remaining lives in light of technological change, network investment plans (including the group's fibre roll-out programme), prospective economic utilisation and physical condition of the assets concerned. Changes to the service lives of assets implemented from 1 April 2010 had no significant impact in aggregate on the results for the year ended 31 March 2011.

The carrying values of software, property, plant and equipment are disclosed in notes 13 and 14, respectively. The useful lives applied to the principal categories of assets are disclosed on page 94.

#### Income tax

The actual tax we pay on our profits is determined according to complex tax laws and regulations. Where the effect of these laws and regulations is unclear, we use estimates in determining the liability for the tax to be paid on our past profits which we recognise in our financial statements. We believe the estimates, assumptions and judgements are reasonable but this can involve complex issues which may take a number of years to resolve. The final determination of prior year tax liabilities could be different from the estimates reflected in the financial statements and may result in the recognition of an additional tax expense or tax credit in the income statement.

The value of the group's income tax liability is disclosed on the balance sheet on page 104.

#### Deferred tax

Deferred tax assets and liabilities require management judgement in determining the amounts to be recognised. In particular, judgement is used when assessing the extent to which deferred tax assets should be recognised with consideration given to the timing and level of future taxable income.

The carrying value of the group's deferred tax assets and liabilities are disclosed in note 24.

#### Goodwill

The recoverable amount of cash generating units has been determined based on value in use calculations. These calculations require the use of estimates, including management's expectations of future revenue growth, operating costs and profit margins for each cash generating unit.

The carrying value of goodwill and the key assumptions used in performing the annual impairment assessment are disclosed in note 13.

#### Determination of fair values

Certain financial instruments such as investments, derivative financial instruments and certain elements of loans and borrowings, are carried on the balance sheet at fair value, with changes in fair value reflected in the income statement. Fair values are estimated by reference in part to published price quotations and in part by using valuation techniques.

The fair values of financial instruments are disclosed in note 29.

#### Providing for doubtful debts

BT provides services to consumer and business customers, mainly on credit terms. We know that certain debts due to us will not be paid through the default of a small number of our customers. Estimates, based on our historical experience, are used in determining the level of debts that we believe will not be collected. These estimates include such factors as the current state of the economy and particular industry issues.

The value of the provision for doubtful debts is disclosed in note 19.

#### Provisions

As disclosed in note 25, the group's provisions principally relate to obligations arising from property rationalisation programmes, restructuring programmes, claims and litigation, and regulatory risks.

Under our property rationalisation programmes we have identified a number of surplus properties. Although efforts are being made to sub-let this space, this is not always possible. Estimates have been made of the cost of vacant possession and of any shortfall arising from any sub-lease income being lower than the lease costs. Any such shortfall is recognised as a provision.

In respect of claims, litigation and regulatory risks, the group provides for anticipated costs where an outflow of resources is considered probable and a reasonable estimate can be made of the likely outcome. The ultimate liability may vary from the amounts provided and will be dependent upon the eventual outcome of any settlement.

## Accounting standards, interpretations and amendments to published standards adopted in the year ended 31 March 2011

The following new, revised and amended standards and interpretations were adopted in 2011. They have had no significant impact on the group's financial position or results of operations for the current or prior years but may impact the accounting for future transactions or arrangements.

- IFRS 3 (Revised) 'Business Combinations';
- IAS 27 (Revised) 'Consolidated and Separate Financial Statements';
- IFRIC 17 'Distributions of Non-cash Assets to Owners';
- Amendment to IAS 39 'Financial Instruments: Recognition and Measurement: Eligible Hedged items';
- Amendment to IAS 32 'Financial Instruments: Presentation – Classification of Rights Issues'; and
- Improvements to IFRSs 2009.

## Accounting standards, interpretations and amendments to published standards not yet effective

Certain new standards, interpretations and amendments to existing standards have been published that are mandatory for the group's accounting periods beginning on or after 1 April 2011 or later periods. Those which are considered to be relevant to the group's operations are set out below.

### IFRS 9 'Financial Instruments' (effective 1 April 2013)

IFRS 9 represents the first phase of the IASB's project to replace IAS 39 'Financial Instruments: Recognition and Measurement'. It sets out the classification and measurement criteria for financial assets and financial liabilities and requires all financial assets, including assets currently classified under IAS 39 as available-for-sale, to be measured at fair value through profit and loss unless the assets can be classified as held at amortised cost. Qualifying equity investments held at fair value may have their fair value changes taken through other comprehensive income by election. The group is currently assessing the impact of the standard on its results, financial position and cash flows.

Those standards, interpretations and amendments which are not currently expected to have a significant impact on the group's financial statements, are as follows:

### Amendments to IAS 24 'Related Party Disclosures' (effective 1 April 2011)

These amendments clarify the definition of a related party and provides some exemptions for government-related entities.

### Amendment to IFRIC 14 'Prepayments of a Minimum Funding Requirement' (effective 1 April 2011)

This amendment permits a voluntary prepayment of a minimum funding requirement to be recognised as an asset.

### IFRIC 19 'Extinguishing Financial Liabilities with Equity Instruments' (effective 1 April 2011)

This interpretation clarifies the accounting when an entity renegotiates the terms of its debt with the result that the liability is settled in part or in full by the debtor issuing its own equity instrument to the creditor.

### Improvements to IFRSs 2010 (effective 1 April 2011)

This is the third set of amendments published under the IASB's annual improvements process and incorporate minor amendments to seven standards and interpretations.

### Amendments to IFRS 1 'First-time Adoption of International Financial Reporting Standards' (effective 1 July 2011)

These amendments provide limited exemption from comparative IFRS 7 disclosures for IFRS first-time adopters.

### Amendments to IFRS 7 'Financial Instruments: Disclosures' (effective 1 April 2012)

These amendments are intended to provide greater transparency around risk exposures when a financial asset is transferred but the transferor retains some level of continuing exposure in the asset. The amendments also require disclosures where transfers of financial assets are not evenly distributed throughout the period.

## GROUP INCOME STATEMENT

Year ended 31 March 2011	Notes	Before specific items £m	Specific items <sup>a</sup> £m	Total £m
<b>Revenue</b>	1	<b>20,076</b>	–	<b>20,076</b>
Other operating income	2	373	–	373
Operating costs	3	(17,542)	(329)	(17,871)
<b>Operating profit</b>	1	<b>2,907</b>	<b>(329)</b>	<b>2,578</b>
Finance expense	9	(880)	(2,323)	(3,203)
Finance income	9	35	2,244	2,279
<b>Net finance expense</b>		<b>(845)</b>	<b>(79)</b>	<b>(924)</b>
Share of post tax profit of associates and joint ventures	17	21	–	21
Profit on disposal of interest in associate	8	–	42	42
<b>Profit before taxation</b>		<b>2,083</b>	<b>(366)</b>	<b>1,717</b>
Taxation	10	(452)	239	(213)
<b>Profit for the year</b>		<b>1,631</b>	<b>(127)</b>	<b>1,504</b>
<b>Attributable to:</b>				
Equity shareholders of the parent		1,629	(127)	1,502
Non-controlling interests	26	2	–	2
<b>Earnings per share</b>	11			
Basic				19.4p
Diluted				18.5p

<sup>a</sup> For a definition of specific items, see page 91. An analysis of specific items is provided in note 8.

Year ended 31 March 2010	Notes	Before specific items <sup>a</sup> £m	Specific items <sup>a</sup> £m	Total £m
<b>Revenue</b>	1	<b>20,911</b>	<b>(52)</b>	<b>20,859</b>
Other operating income	2	378	2	380
Operating costs	3	(18,689)	(427)	(19,116)
<b>Operating profit</b>	1	<b>2,600</b>	<b>(477)</b>	<b>2,123</b>
Finance expense	9	(902)	(2,211)	(3,113)
Finance income	9	12	1,943	1,955
<b>Net finance expense</b>		<b>(890)</b>	<b>(268)</b>	<b>(1,158)</b>
Share of post tax profit of associates and joint ventures	17	25	29	54
Loss on disposal of interest in associate	8	–	(12)	(12)
<b>Profit before taxation</b>		<b>1,735</b>	<b>(728)</b>	<b>1,007</b>
Taxation	10	(398)	420	22
<b>Profit for the year</b>		<b>1,337</b>	<b>(308)</b>	<b>1,029</b>
<b>Attributable to:</b>				
Equity shareholders of the parent		1,336	(308)	1,028
Non-controlling interests	26	1	–	1
<b>Earnings per share</b>	11			
Basic				13.3p
Diluted				12.9p

<sup>a</sup> In 2011 the group amended its definition of specific items. Comparatives for 2010 have been re-presented to be on a consistent basis. See page 91 for details.

## GROUP INCOME STATEMENT

Year ended 31 March 2009	Notes	Before specific items <sup>a</sup> £m	Specific items <sup>a</sup> £m	Total £m
<b>Revenue</b>	1	<b>21,431</b>	<b>(41)</b>	<b>21,390</b>
Other operating income	2	352	(13)	339
Operating costs	3	(19,435)	(1,993)	(21,428)
<b>Operating profit</b>	<b>1</b>	<b>2,348</b>	<b>(2,047)</b>	<b>301</b>
Finance expense	9	(964)	(2,308)	(3,272)
Finance income	9	31	2,621	2,652
<b>Net finance expense</b>		<b>(933)</b>	<b>313</b>	<b>(620)</b>
Share of post tax profit of associates and joint ventures		39	36	75
<b>Profit (loss) before taxation</b>		<b>1,454</b>	<b>(1,698)</b>	<b>(244)</b>
Taxation	10	(361)	414	53
<b>Profit (loss) for the year</b>		<b>1,093</b>	<b>(1,284)</b>	<b>(191)</b>
<b>Attributable to:</b>				
Equity shareholders of the parent		1,091	(1,284)	(193)
Non-controlling interests		2	–	2
<b>Loss per share</b>				
Basic	11			(2.5)p
Diluted				(2.5)p

<sup>a</sup> In 2011 the group amended its definition of specific items. Comparatives for 2009 have been re-presented to be on a consistent basis. See page 91 for details.

## GROUP STATEMENT OF COMPREHENSIVE INCOME

Year ended 31 March	Notes	2011 £m	2010 £m	2009 £m
<b>Profit (loss) for the year</b>		<b>1,504</b>	<b>1,029</b>	<b>(191)</b>
<b>Other comprehensive income (loss)</b>				
Actuarial gains (losses) relating to retirement benefit obligations	23	5,109	(4,324)	(7,037)
Exchange differences on translation of foreign operations	28	(140)	(119)	692
Fair value movements on available-for-sale assets	28	15	7	5
Fair value movements on cash flow hedges:				
– net fair value (losses) gains	28	(347)	(1,067)	2,719
– recognised in income and expense	28	333	496	(2,144)
– reclassified and reported in non-current assets	28	–	(4)	(5)
Tax on components of other comprehensive income	10	(1,521)	1,350	1,859
<b>Other comprehensive income (loss) for the year, net of tax</b>		<b>3,449</b>	<b>(3,661)</b>	<b>(3,911)</b>
<b>Total comprehensive income (loss) for the year</b>		<b>4,953</b>	<b>(2,632)</b>	<b>(4,102)</b>
<b>Attributable to:</b>				
Equity shareholders of the parent		4,951	(2,633)	(4,113)
Non-controlling interests		2	1	11
		<b>4,953</b>	<b>(2,632)</b>	<b>(4,102)</b>

## GROUP STATEMENT OF CHANGES IN EQUITY

	Shareholders' equity (deficit)						Non-controlling interests <sup>c</sup>	Total equity £m
	Share capital <sup>a</sup> £m	Share premium <sup>a</sup> £m	Capital reserve £m	Other reserves <sup>b</sup> £m	Retained earnings £m	Total £m		
<b>At 1 April 2008</b>	<b>420</b>	<b>62</b>	<b>15</b>	<b>(527)</b>	<b>5,439</b>	<b>5,409</b>	<b>23</b>	<b>5,432</b>
Loss for the year	–	–	–	–	(193)	(193)	2	(191)
Other comprehensive income – before tax	–	–	–	3,407	(7,037)	(3,630)	9	(3,621)
Other comprehensive income – tax	–	–	–	(164)	2,023	1,859	–	1,859
Transferred to the income statement	–	–	–	(2,144)	–	(2,144)	–	(2,144)
Transferred to non-current assets	–	–	–	(5)	–	(5)	–	(5)
Comprehensive income (loss)	–	–	–	1,094	(5,207)	(4,113)	11	(4,102)
Dividends to shareholders	–	–	–	–	(1,222)	(1,222)	–	(1,222)
Share-based payments	–	–	–	–	143	143	–	143
Tax on share-based payments	–	–	–	–	(12)	(12)	–	(12)
Issue of ordinary shares	–	–	–	797	(797)	–	–	–
Cancellation of shares	(12)	–	12	–	–	–	–	–
Net purchase of treasury shares	–	–	–	(63)	–	(63)	–	(63)
Other movements in non-controlling interests	–	–	–	–	–	–	(7)	(7)
<b>At 1 April 2009</b>	<b>408</b>	<b>62</b>	<b>27</b>	<b>1,301</b>	<b>(1,656)</b>	<b>142</b>	<b>27</b>	<b>169</b>
Profit for the year	–	–	–	–	1,028	1,028	1	1,029
Other comprehensive income – before tax	–	–	–	(1,179)	(4,324)	(5,503)	–	(5,503)
Other comprehensive income – tax	–	–	–	139	1,211	1,350	–	1,350
Transferred to the income statement	–	–	–	496	–	496	–	496
Transferred to non-current assets	–	–	–	(4)	–	(4)	–	(4)
Comprehensive income (loss)	–	–	–	(548)	(2,085)	(2,633)	1	(2,632)
Dividends to shareholders	–	–	–	–	(263)	(263)	–	(263)
Share-based payments	–	–	–	–	81	81	–	81
Tax on share-based payments	–	–	–	–	19	19	–	19
Net issuance of treasury shares	–	–	–	4	–	4	–	4
Other movements in non-controlling interests	–	–	–	–	–	–	(4)	(4)
<b>At 1 April 2010</b>	<b>408</b>	<b>62</b>	<b>27</b>	<b>757</b>	<b>(3,904)</b>	<b>(2,650)</b>	<b>24</b>	<b>(2,626)</b>
Profit for the year	–	–	–	–	1,502	1,502	2	1,504
Other comprehensive income – before tax	–	–	–	(472)	5,109	4,637	–	4,637
Other comprehensive income – tax	–	–	–	13	(1,534)	(1,521)	–	(1,521)
Transferred to the income statement	–	–	–	333	–	333	–	333
Comprehensive income (loss)	–	–	–	(126)	5,077	4,951	2	4,953
Dividends to shareholders	–	–	–	–	(543)	(543)	–	(543)
Share-based payments	–	–	–	–	68	68	–	68
Tax on share-based payments	–	–	–	–	91	91	–	91
Net issuance of treasury shares	–	–	–	27	(19)	8	–	8
<b>At 31 March 2011</b>	<b>408</b>	<b>62</b>	<b>27</b>	<b>658</b>	<b>770</b>	<b>1,925</b>	<b>26</b>	<b>1,951</b>

<sup>a</sup> For details of share capital and share premium, see note 27.

<sup>b</sup> For further analysis of other reserves, see note 28.

<sup>c</sup> For further analysis of non-controlling interests, see note 26.

## GROUP CASH FLOW STATEMENT

Year ended 31 March	Note	2011 £m	2010 £m	2009 £m
<b>Cash flow from operating activities</b>				
Profit (loss) before taxation <sup>a</sup>		1,717	1,007	(244)
Depreciation and amortisation		2,979	3,039	2,890
(Profit) loss on disposal of associates and businesses		(42)	10	13
Net finance expense		924	1,158	620
Other non cash charges		78	77	596
Share of profits of associates and joint ventures		(21)	(54)	(75)
(Increase) decrease in inventories		(17)	14	11
Decrease in trade and other receivables		408	524	1,063
(Decrease) in trade and other payables		(378)	(708)	(379)
(Decrease) increase in provisions and other liabilities <sup>b</sup>		(873)	(591)	439
<b>Cash generated from operations<sup>a</sup></b>		<b>4,775</b>	<b>4,476</b>	<b>4,934</b>
Income taxes paid		(209)	(76)	(232)
Income tax repayment for prior years		–	425	4
<b>Net cash inflow from operating activities</b>		<b>4,566</b>	<b>4,825</b>	<b>4,706</b>
<b>Cash flow from investing activities</b>				
Interest received		29	16	19
Dividends received from associates and joint ventures		7	3	6
Proceeds on disposal of interest in associates		72	–	–
Proceeds on disposal of businesses		–	2	–
Acquisition of subsidiaries, net of cash acquired		(8)	(70)	(227)
Proceeds on disposal of current financial assets <sup>c</sup>		9,267	8,739	6,316
Purchases of current financial assets <sup>c</sup>		(8,902)	(8,985)	(6,030)
Purchases of non-current financial assets		(18)	–	–
Proceeds on disposal of property, plant and equipment		15	29	44
Purchases of property, plant and equipment and software		(2,645)	(2,509)	(3,082)
<b>Net cash outflow from investing activities</b>		<b>(2,183)</b>	<b>(2,775)</b>	<b>(2,954)</b>
<b>Cash flow from financing activities</b>				
Equity dividends paid		(543)	(265)	(1,221)
Dividends paid to non-controlling interests		–	–	(1)
Interest paid		(973)	(956)	(956)
Repayment of borrowings <sup>d</sup>		(2,509)	(307)	(863)
Repayment of finance lease liabilities		(11)	(24)	(16)
Proceeds from finance leases		–	9	–
Net proceeds from (repayment of) commercial paper		69	(697)	606
Proceeds from bank loans		340	522	795
Cash flows from derivatives related to net debt		120	–	–
Repurchase of ordinary shares		–	–	(334)
Proceeds on issue of treasury shares		8	4	125
<b>Net cash used in financing activities</b>		<b>(3,499)</b>	<b>(1,714)</b>	<b>(1,865)</b>
Effect of exchange rate changes on cash and cash equivalents		(3)	(7)	54
<b>Net (decrease) increase in cash and cash equivalents</b>		<b>(1,119)</b>	<b>329</b>	<b>(59)</b>
Cash and cash equivalents at the start of the year		1,444	1,115	1,174
<b>Cash and cash equivalents at the end of the year</b>	16	<b>325</b>	<b>1,444</b>	<b>1,115</b>

<sup>a</sup> The reconciliation from the loss before taxation of £244m for 2009 to the cash generated from operations of £4,934m for 2009 includes BT Global Services contract and financial review charges of £1,639m, which were non-cash charges.

<sup>b</sup> Includes pension deficit payments of £1,030m (2010: £525m, 2009: £nil).

<sup>c</sup> Primarily consists of investment in and redemption of amounts held in liquidity funds.

<sup>d</sup> In 2011 the repayment of borrowings includes the impact of hedging. See page 144 for further details.

## GROUP BALANCE SHEET

At 31 March	Notes	2011 £m	2010 £m
<b>Non-current assets</b>			
Intangible assets	13	3,389	3,672
Property, plant and equipment	14	14,623	14,856
Derivative financial instruments	21	625	1,076
Investments	15	61	64
Associates and joint ventures	17	164	195
Trade and other receivables	19	286	336
Deferred tax assets	24	461	2,196
		<b>19,609</b>	<b>22,395</b>
<b>Current assets</b>			
Inventories	18	121	107
Trade and other receivables	19	3,332	3,696
Derivative financial instruments	21	108	624
Investments	15	19	406
Cash and cash equivalents	16	351	1,452
		<b>3,931</b>	<b>6,285</b>
<b>Current liabilities</b>			
Loans and other borrowings	20	485	3,269
Derivative financial instruments	21	62	166
Trade and other payables	22	6,114	6,531
Current tax liabilities		221	320
Provisions	25	149	134
		<b>7,031</b>	<b>10,420</b>
<b>Total assets less current liabilities</b>		<b>16,509</b>	<b>18,260</b>
<b>Non-current liabilities</b>			
Loans and other borrowings	20	9,371	9,522
Derivative financial instruments	21	507	533
Retirement benefit obligations	23	1,830	7,864
Other payables	22	831	804
Deferred tax liabilities	24	1,212	1,456
Provisions	25	807	707
		<b>14,558</b>	<b>20,886</b>
<b>Equity</b>			
Ordinary shares	27	408	408
Share premium	27	62	62
Capital redemption reserve		27	27
Other reserves	28	658	757
Retained earnings (loss)		770	(3,904)
<b>Total parent shareholders' equity (deficit)</b>		<b>1,925</b>	<b>(2,650)</b>
Non-controlling interests	26	26	24
<b>Total equity (deficit)</b>		<b>1,951</b>	<b>(2,626)</b>
		<b>16,509</b>	<b>18,260</b>

The consolidated financial statements on pages 91 to 150 and 155 were approved by the Board of Directors on 11 May 2011 and were signed on its behalf by

**Sir Michael Rake**  
Chairman

**Ian Livingston**  
Chief Executive

**Tony Chanmugam**  
Group Finance Director

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

## 1. Segment information

The group's operating segments are reported based on financial information provided to the *Operating Committee*, as detailed on page 64, which is the key management committee and represents the 'chief operating decision maker'. The *Operating Committee* is chaired by the Group Chief Executive and the other members are the Group Finance Director and the Chief Executives of BT Retail, BT Wholesale, BT Global Services, BT Innovate & Design and BT Operate. The Chief Executive of Openreach, the Company Secretary and the Group HR director also normally attend all meetings.

The group's organisational structure reflects the different customer groups to which it provides communications products and services via its four customer-facing lines of business, supported by two internal service units. The four customer-facing lines of business are the group's reportable segments and generate substantially all the group's revenue. Their operations are summarised as follows:

**BT Global Services** provides managed networked IT services to multinational corporations, domestic businesses and national and local government organisations operating in more than 170 countries worldwide.

**BT Retail** provides communication products and services to the consumer market and provides IT and communications services to SMEs. BT Retail includes BT Ireland which operates across the major corporate, SME, consumer and wholesale markets throughout the Republic of Ireland and Northern Ireland. BT Retail also includes BT Enterprises which comprises a number of individual businesses including BT Conferencing, BT Directories, BT Expedite, BT Redcare & Payphones and BT Openzone.

**BT Wholesale** provides products and a broad range of voice, broadband and data communications services, including managed services for fixed and mobile network operators, internet service providers and telecoms resellers in the UK.

**Openreach** is responsible for the 'last mile' of the UK access network – the copper wires and fibre connecting homes and businesses to their local telephone exchange via fixed-line local and backhaul connections. Openreach customers, which comprise UK communication providers and other BT lines of business, are offered fair, equal and open access to its networks.

BT Innovate & Design and BT Operate are internal service units which support the four customer-facing lines of business. BT Innovate & Design is responsible for the development, design and delivery of the platforms, systems and processes which support the provision of the group's products and services. BT Operate is responsible for managing BT's IT and network infrastructure platforms. BT Innovate & Design and BT Operate operate on a full cost recovery basis. The costs incurred by BT Innovate & Design and BT Operate are allocated to the customer-facing lines of business in line with the services they provide. The depreciation and amortisation incurred by BT Operate in relation to the networks and systems they manage and operate on behalf of the customer-facing lines of business are allocated to the lines of business based on their respective utilisation. Capital expenditure incurred by BT Innovate & Design for specific projects undertaken on behalf of the customer-facing lines of business is allocated based on the value of the directly attributable expenditure incurred. Where projects are not directly attributable to a particular line of business, capital expenditure is allocated based on the proportion of estimated future economic benefits. Capital expenditure incurred by BT Operate is allocated to the customer-facing lines of business in line with the proportion of operating cost recoveries. BT Innovate & Design and BT Operate and the group's centralised functions are not reportable segments as they did not meet the quantitative thresholds as set out in IFRS 8 'Operating Segments' for any of the years presented.

Intra group revenue generated from the sale of regulated products and services is based on market price. Intra group revenue from the sale of other products and services is agreed between the relevant lines of business and thus line of business profitability can be impacted by transfer pricing levels. The majority of the internal trading relates to Openreach and arises on rentals, and any associated connection or migration charges, of the UK access lines and other network products to the market-facing lines of business, both directly, and also indirectly, through BT Operate which is included within the 'Other' segment. Internal revenue arising in BT Retail relates primarily to BT Ireland and Enterprises. Internal revenue arising in BT Wholesale relates to the sale of line cards and access electronic services to Openreach.

In addition to the four customer-facing lines of business, the remaining operations of the group are aggregated and included within the 'Other' category to reconcile to the consolidated results of the group. The 'Other' category includes costs associated with the group's centralised functions including procurement and supply chain, fleet and property management. Provisions for the settlement of significant legal, commercial and regulatory disputes, which are negotiated at a group level, are initially recorded in the 'Other' segment. On resolution of the dispute, the full impact is recognised in the relevant lines of business results, offset in the group results by the utilisation of the provision previously charged to the 'Other' segment. Settlements which are particularly significant or cover more than one financial year may fall within the definition of specific items as detailed on page 91.

Information regarding the results of each reportable segment is provided below. Performance is measured based on adjusted EBITDA, defined as EBITDA before specific items, as included in the internal financial reports reviewed by the *Operating Committee*. EBITDA is defined as the operating profit or loss before depreciation, amortisation, net finance expense and taxation. Adjusted EBITDA is considered to be a useful measure of the operating performance of the lines of business because it reflects the underlying cash by eliminating depreciation and amortisation and also provides a meaningful analysis of trading performance by excluding specific items which are disclosed separately by virtue of their size, nature or incidence. Specific items are detailed in note 8 and are not allocated to the reportable segments as this reflects how they are reported to the *Operating Committee*. Finance expense and income is not allocated to the reportable segments as this activity is managed by the central treasury function which manages the overall net debt position of the group.

## 1. Segment information continued

### Segment revenue and profit

Year ended 31 March 2011	BT Global Services £m	BT Retail £m	BT Wholesale £m	Openreach £m	Other £m	Total £m
Segment revenue	8,047	7,748	4,210	4,930	38	24,973
Internal revenue	–	(446)	(980)	(3,471)	–	(4,897)
<b>Revenue from external customers<sup>a</sup></b>	<b>8,047</b>	<b>7,302</b>	<b>3,230</b>	<b>1,459</b>	<b>38</b>	<b>20,076</b>
<b>EBITDA<sup>b</sup></b>	<b>593</b>	<b>1,784</b>	<b>1,316</b>	<b>2,132</b>	<b>61</b>	<b>5,886</b>
Depreciation and amortisation	(734)	(443)	(619)	(877)	(306)	(2,979)
<b>Operating profit (loss)<sup>a</sup></b>	<b>(141)</b>	<b>1,341</b>	<b>697</b>	<b>1,255</b>	<b>(245)</b>	<b>2,907</b>
Specific items (note 8)						(329)
<b>Operating profit (loss)</b>						<b>2,578</b>
Net finance expense <sup>d</sup>						(924)
Share of post tax profit of associates and joint ventures						21
Profit on disposal of interest in associate						42
<b>Profit before tax</b>						<b>1,717</b>

Year ended 31 March 2010	BT Global Services £m	BT Retail <sup>e</sup> £m	BT Wholesale <sup>e</sup> £m	Openreach <sup>e</sup> £m	Other £m	Total £m
Segment revenue	8,513	8,124	4,592	5,164	40	26,433
Internal revenue	–	(373)	(1,226)	(3,923)	–	(5,522)
<b>Revenue from external customers<sup>a</sup></b>	<b>8,513</b>	<b>7,751</b>	<b>3,366</b>	<b>1,241</b>	<b>40</b>	<b>20,911</b>
<b>EBITDA<sup>b</sup></b>	<b>457</b>	<b>1,777</b>	<b>1,353</b>	<b>1,960</b>	<b>92</b>	<b>5,639</b>
Depreciation and amortisation	(815)	(459)	(680)	(856)	(229)	(3,039)
<b>Operating profit (loss)<sup>a</sup></b>	<b>(358)</b>	<b>1,318</b>	<b>673</b>	<b>1,104</b>	<b>(137)</b>	<b>2,600</b>
Specific items (note 8)						(477)
<b>Operating profit (loss)</b>						<b>2,123</b>
Net finance expense <sup>d</sup>						(1,158)
Share of post tax profit of associates and joint ventures						54
Loss on disposal of interest in associate						(12)
<b>Profit before tax</b>						<b>1,007</b>

Year ended 31 March 2009	BT Global Services £m	BT Retail <sup>e</sup> £m	BT Wholesale <sup>e</sup> £m	Openreach <sup>e</sup> £m	Other £m	Total £m
Segment revenue	8,628	8,491	4,800	5,231	41	27,191
Internal revenue	–	(343)	(1,228)	(4,189)	–	(5,760)
<b>Revenue from external customers<sup>a</sup></b>	<b>8,628</b>	<b>8,148</b>	<b>3,572</b>	<b>1,042</b>	<b>41</b>	<b>21,431</b>
<b>EBITDA<sup>b</sup></b>	<b>261</b>	<b>1,585</b>	<b>1,356</b>	<b>1,996</b>	<b>40</b>	<b>5,238</b>
Depreciation and amortisation	(776)	(426)	(686)	(778)	(224)	(2,890)
<b>Operating profit (loss)<sup>a</sup></b>	<b>(515)</b>	<b>1,159</b>	<b>670</b>	<b>1,218</b>	<b>(184)</b>	<b>2,348</b>
Specific items (note 8) <sup>c</sup>						(2,047)
<b>Operating profit (loss)</b>						<b>301</b>
Net finance expense <sup>d</sup>						(620)
Share of post tax profit of associates and joint ventures						75
<b>Loss before tax</b>						<b>(244)</b>

<sup>a</sup> Before specific items.

<sup>b</sup> EBITDA is stated before specific items and is a non-GAAP measure provided in addition to the disclosure requirements defined under IFRS. The rationale for using non-GAAP measures is explained on pages 56 to 58.

<sup>c</sup> Re-presented. See page 91.

<sup>d</sup> Net finance expense includes specific items of £79m (2010: £268m; 2009: £313m credit). See note 8.

<sup>e</sup> In 2011 the group moved certain customer accounts between lines of business. Comparatives for 2010 and 2009 have been restated to be on a consistent basis. The impact on line of business results in 2010 was to decrease revenue and EBITDA in BT Retail by £173m and £73m (2009: £172m and £79m), to increase revenue and EBITDA in BT Wholesale by £143m and £74m (2009: £142m and £79m), to increase revenue in Openreach by £30m (2009: £29m) with no impact on EBITDA. There is no impact on total group results.

## 1. Segment information continued

### Internal revenue and costs

Year ended 31 March 2011	Internal cost recorded by					Total £m
	BT Global Services £m	BT Retail £m	BT Wholesale £m	Openreach £m	Other £m	
<b>Internal revenue recorded by</b>						
BT Global Services	–	–	–	–	–	–
BT Retail	309	–	64	3	70	446
BT Wholesale	–	–	–	980	–	980
Openreach	241	1,780	198	–	1,252	3,471
<b>Total</b>	<b>550</b>	<b>1,780</b>	<b>262</b>	<b>983</b>	<b>1,322</b>	<b>4,897</b>

Year ended 31 March 2010	Internal cost recorded by					Total £m
	BT Global Services £m	BT Retail £m	BT Wholesale £m	Openreach £m	Other £m	
<b>Internal revenue recorded by</b>						
BT Global Services	–	–	–	–	–	–
BT Retail	231	–	51	2	89	373
BT Wholesale	–	–	–	1,226	–	1,226
Openreach	264	1,988	131	–	1,540	3,923
<b>Total</b>	<b>495</b>	<b>1,988</b>	<b>182</b>	<b>1,228</b>	<b>1,629</b>	<b>5,522</b>

Year ended 31 March 2009	Internal cost recorded by					Total £m
	BT Global Services £m	BT Retail £m	BT Wholesale £m	Openreach £m	Other £m	
<b>Internal revenue recorded by</b>						
BT Global Services	–	–	–	–	–	–
BT Retail	233	–	54	4	52	343
BT Wholesale	–	–	–	1,228	–	1,228
Openreach	398	2,159	141	–	1,491	4,189
<b>Total</b>	<b>631</b>	<b>2,159</b>	<b>195</b>	<b>1,232</b>	<b>1,543</b>	<b>5,760</b>

### Capital expenditure

Year ended 31 March 2011	Internal cost recorded by					Total £m
	BT Global Services £m	BT Retail £m	BT Wholesale £m	Openreach £m	Other £m	
Property, plant and equipment	338	355	246	982	169	2,090
Intangible assets	160	79	83	105	73	500
<b>Capital expenditure</b>	<b>498</b>	<b>434</b>	<b>329</b>	<b>1,087</b>	<b>242</b>	<b>2,590</b>

Year ended 31 March 2010	Internal cost recorded by					Total £m
	BT Global Services £m	BT Retail £m	BT Wholesale £m	Openreach £m	Other £m	
Property, plant and equipment	395	333	230	816	130	1,904
Intangible assets	204	84	95	91	155	629
<b>Capital expenditure</b>	<b>599</b>	<b>417</b>	<b>325</b>	<b>907</b>	<b>285</b>	<b>2,533</b>

## 1. Segment information continued

### Revenue by products and services

Year ended 31 March	2011 £m	2010 <sup>a</sup> £m	2009 <sup>a</sup> £m
ICT and managed networks	6,632	6,574	6,382
Broadband and convergence	2,767	2,677	2,618
Calls and lines	5,595	6,225	6,799
Transit	1,518	1,758	2,003
Conveyance, interconnect circuits, WLR, global carrier and other wholesale	1,471	1,451	1,506
Other products and services	2,093	2,226	2,123
<b>Revenue<sup>b</sup></b>	<b>20,076</b>	<b>20,911</b>	<b>21,431</b>

<sup>a</sup> In 2011 the group moved certain customer accounts between lines of business. This move has led to a change in the classification of revenue by the nature of products or services. Comparatives for 2010 and 2009 have been restated to be on a consistent basis. The impact on products and services in 2010 is to decrease ICT and managed services by £7m (2009: £8m), to decrease broadband and convergence by £1m (2009: £1m increase), to decrease calls and lines by £68m (2009: £63m), to increase conveyance, interconnect circuits, WLR, global carrier and other wholesale by £252m (2009: £265m) and to decrease other products and services by £176m (2009: £195m). There is no impact on total revenue.

<sup>b</sup> Before specific items.

### Geographic information

The UK is the group's country of domicile and the group generates the majority of its revenue from external customers in the UK. The geographic analysis of revenue is on the basis of the country of origin in which the customer is invoiced.

### Revenue from external customers

Year ended 31 March	2011 £m	2010 £m	2009 £m
UK	15,575	16,116	16,777
Europe, Middle East and Africa, excluding the UK	3,064	3,250	3,247
Americas	990	1,235	1,119
Asia Pacific	447	310	288
<b>Revenue<sup>a</sup></b>	<b>20,076</b>	<b>20,911</b>	<b>21,431</b>

<sup>a</sup> Before specific items.

### Non-current assets

At 31 March	2011 £m	2010 £m
UK	15,127	15,583
Europe, Middle East and Africa, excluding the UK	2,673	2,761
Americas	601	653
Asia Pacific	61	62
<b>Non-current assets</b>	<b>18,462</b>	<b>19,059</b>

Non-current assets, which exclude derivative financial instruments and investments and deferred tax assets, are based on the location of the assets.

## 2. Other operating income

Year ended 31 March	Notes	2011 £m	2010 £m	2009 £m
Profits on disposal of property, plant and equipment		103	75	52
Income from repayment works		62	74	72
Other operating income		208	229	228
<b>Other operating income before specific items</b>		<b>373</b>	<b>378</b>	<b>352</b>
Specific items	8	–	2	(13)
<b>Other operating income</b>		<b>373</b>	<b>380</b>	<b>339</b>

## 3. Operating costs

Year ended 31 March	Notes	2011 £m	2010 £m	2009 £m
<b>Costs by nature</b>				
<b>Staff costs</b>				
Wages and salaries		3,947	4,182	4,499
Social security costs		456	447	432
Pension costs	23	416	304	544
Share-based payment expense	6	68	71	141
<b>Total staff costs</b>		<b>4,887</b>	<b>5,004</b>	<b>5,616</b>
Own work capitalised		(718)	(575)	(673)
Net staff costs		4,169	4,429	4,943
Indirect labour costs		629	722	1,114
<b>Net labour costs</b>		<b>4,798</b>	<b>5,151</b>	<b>6,057</b>
Payments to telecommunications operators		3,740	4,083	4,266
Property and energy costs		1,149	1,284	1,292
Network maintenance and IT costs		706	781	742
Other operating costs <sup>a</sup>		2,786	2,927	2,710
General and administrative costs		1,384	1,424	1,478
Depreciation of property, plant and equipment				
Owned assets	14	2,255	2,260	2,200
Held under finance leases	14	33	44	49
Amortisation of intangible assets	13	691	735	641
<b>Total operating costs before specific items</b>		<b>17,542</b>	<b>18,689</b>	<b>19,435</b>
Specific items	8	329	427	1,993
<b>Total operating costs</b>		<b>17,871</b>	<b>19,116</b>	<b>21,428</b>
Operating costs before specific items include the following:				
Leaver costs <sup>b</sup>		57	142	204
Research and development expenditure <sup>c</sup>		833	935	1,021
Rental costs relating to operating leases		395	451	426
Foreign currency (gains) losses		(17)	7	30

<sup>a</sup> Other operating costs also include a net charge of £2m (2010: £1m charge, 2009: £8m credit) relating to fair value movements on derivatives recycled from the cash flow reserve.

<sup>b</sup> Leaver costs exclude leaver costs associated with the restructuring of BT Global Services during 2011, 2010 and 2009 and managed leaver costs associated with the group's transformation and reorganisation activities during 2009. These costs have been recorded as a specific item. Other leaver costs are included within wages and salaries and social security costs.

<sup>c</sup> Research and development expenditure includes amortisation of £444m (2010: £491m, 2009: £431m) in respect of internally developed computer software.

## 4. Employees

	2011		2010		2009	
	Year end '000	Average '000	Year end '000	Average '000	Year end '000	Average '000
Number of employees in the group <sup>a</sup>						
UK	75.7	77.1	79.8	82.9	86.5	89.5
Non UK	16.9	17.5	18.0	18.8	20.5	21.1
<b>Total employees</b>	<b>92.6</b>	<b>94.6</b>	<b>97.8</b>	<b>101.7</b>	<b>107.0</b>	<b>110.6</b>

	2011		2010		2009	
	Year end '000	Average '000	Year end '000	Average '000	Year end '000	Average '000
Number of employees in the group <sup>a</sup>						
BT Global Services	21.8	22.6	24.3	26.1	28.2	28.4
BT Retail	16.6	17.4	19.4	20.2	21.2	21.9
BT Wholesale	1.9	2.1	2.4	2.4	2.4	2.5
Openreach	31.3	30.9	30.8	31.4	32.3	33.1
Other	21.0	21.6	20.9	21.6	22.9	24.7
<b>Total employees</b>	<b>92.6</b>	<b>94.6</b>	<b>97.8</b>	<b>101.7</b>	<b>107.0</b>	<b>110.6</b>

<sup>a</sup> The numbers disclosed are the equivalent full-time employees including both full and part-time employees.

## 5. Related party transactions

Key management personnel comprise executive and non-executive directors and members of the *Operating Committee*. Key management personnel compensation is shown in the table below:

Year ended 31 March	2011 £m	2010 £m	2009 £m
Salaries and short-term benefits	11.4	10.3	8.4
Termination benefits	–	0.1	2.4
Post employment benefits	1.4	1.8	2.3
Share-based payments	5.3	2.6	3.6
	<b>18.1</b>	<b>14.8</b>	<b>16.7</b>

More detailed information concerning directors' remuneration, shareholdings, pension entitlements, share options and other long-term incentive plans is shown in the audited part of the **Report on directors' remuneration**, which forms part of the consolidated financial statements.

Amounts paid to the group's retirement benefit plans are set out in note 23. There were a number of transactions during the year between the company and its subsidiary undertakings, which are eliminated on consolidation and therefore not disclosed.

During 2011 the group purchased services in the normal course of business and on an arm's length basis from its principal associate, Tech Mahindra Limited. The net value of services purchased was £258m (2010: £301m, 2009: £296m) and the amount outstanding and payable for services at 31 March 2011 was £61m (2010: £65m, 2009: £89m). In 2010 a cash payment of £127m was made to Tech Mahindra Limited for the renegotiation of certain supply contracts as part of the rationalisation of procurement channels within BT Global Services.

## 6. Share-based payments

The company has an employee share investment plan and savings-related share option plans for its employees and those of participating subsidiaries, further share option plans for selected employees and an employee stock purchase plan for employees in the United States. It also has several share plans for executives. All share-based payment plans are equity settled and details of these plans and an analysis of the total charge by type of award is set out below.

Year ended 31 March	2011 £m	2010 £m	2009 £m
Employee Sharesave Plan	23	25	107
Allshare International Plan	2	2	2
Employee Stock Purchase Plan	1	1	–
Incentive Share Plan	37	29	18
Deferred Bonus Plan	5	13	12
Retention Share Plan	–	1	2
	<b>68</b>	<b>71</b>	<b>141</b>

### Share options

#### Employee Sharesave Plan

There is an HMRC approved savings related share option plan, under which employees save on a monthly basis, over a three or five year period, towards the purchase of shares at a fixed price determined when the option is granted. This price is usually set at a 20% discount to the market price for five year plans and 10% for three year plans. The options must be exercised within six months of maturity of the savings contract, otherwise they lapse. Similar plans operate for BT's overseas employees.

#### Employee Stock Purchase Plan

The BT Group Employee Stock Purchase Plan (ESPP), for employees in the United States, enables participants to purchase American Depository Shares (ADSs) quarterly at a price which is 85% of the fair market price of an ADS at the end of each quarterly purchase period.

### Share plans

#### Incentive Share Plan, Deferred Bonus Plan and Retention Share Plan

Under the BT Group Incentive Share Plan (ISP), participants are only entitled to these shares in full at the end of a three year period if the company has met the relevant pre-determined corporate performance measures and if the participants are still employed by the group. In 2010 the corporate performance measures for the ISP was amended. For all ISP awards made, 50% of each share award is linked to a total shareholder return target (TSR) for a comparator group of companies from the beginning of the relevant performance period and the remaining 50% is linked to a three-year cumulative free cash flow measure. The comparator group contains European telecommunications companies and companies which are either similar in size or market capitalisation and/or have a similar business mix and spread to BT. For ISP awards prior to 2010, a single corporate performance measure was used, being BT's TSR measured against a comparator group of companies from the European telecommunications sector.

Under the BT Group Deferred Bonus Plan (DBP) awards are granted annually to selected employees of the group. Shares in the company are transferred to participants at the end of three years if they continue to be employed by the group throughout that period.

Under the BT Group Retention Share Plan (RSP), the length of retention period before awards vest is flexible. Awards may vest annually in tranches. The shares are transferred at the end of a specified period, only if the employee is still employed by the group.

In accordance with the terms of the ISP, DBP and RSP, dividends or dividend equivalents earned on shares during the conditional periods are reinvested in company shares for the potential benefit of the participants.

#### Employee Share Investment Plan (ESIP)

The ESIP is an HMRC approved plan. It allows BT employees to buy shares with contributions of up to £1,500 per tax year out of gross pay (directshare) and allows BT to provide free shares to UK employees which are held in trust for at least three years (UK allshare). In 2008 UK allshare was replaced by free broadband for all BT employees in the UK. Employees outside the UK continued to receive awards of shares where practicable (Allshare International), otherwise they received cash awards equivalent to the value of free shares.

During 2011 9.2m directshare shares (2010: 13.7m directshare shares), were purchased by the Trustee of the ESIP on behalf of 19,169 (2010: 19,730) employees at a total cost of £13.8m (2010: £15.0m). A further 1.8m shares (2010: 1.0m shares) were purchased by the Trustee through dividend reinvestment on behalf of 19,392 (2010: 20,120) allshare and directshare employee participants. At 31 March 2011, 79.3m shares (2010: 79.2m shares) were held in trust on behalf of 64,643 participants (2010: 68,444).

## 6. Share-based payments continued

### Share option plans

Movements in share options during 2011, 2010 and 2009 are shown below.

Movement in the number of share options	Employee Sharesave			GSOP and GLOP <sup>a</sup>		
	2011 millions	2010 millions	2009 millions	2011 millions	2010 millions	2009 millions
Outstanding at the beginning of the year	534	136	281	38	42	46
Granted	78	490	339	–	–	–
Forfeited	(28)	(44)	(390)	(5)	(4)	(3)
Exercised	(3)	(1)	(80)	–	–	(1)
Expired	(14)	(47)	(14)	(4)	–	–
<b>Outstanding at the end of the year</b>	<b>567</b>	<b>534</b>	<b>136</b>	<b>29</b>	<b>38</b>	<b>42</b>
Exercisable at the end of the year	1	1	1	29	38	42
<b>Weighted average exercise price</b>						
Outstanding at the beginning of the year	76p	160p	180p	255p	256p	257p
Granted	107p	63p	135p	–	–	–
Forfeited	94p	107p	153p	325p	263p	199p
Exercised	163p	125p	155p	–	–	196p
Expired	175p	150p	178p	544p	–	–
<b>Outstanding at the end of the year</b>	<b>77p</b>	<b>76p</b>	<b>160p</b>	<b>207p</b>	<b>255p</b>	<b>256p</b>
Exercisable at the end of the year	111p	163p	195p	207p	255p	256p

<sup>a</sup> The BT Group Global Share Option Plan (GSOP) and BT Group Legacy Option Plan (GLOP) are legacy executive share option plans which are no longer operated. Options granted in previous years were exercisable on the third anniversary of the date of grant. Options must be exercised within 10 years of the original grant date.

The weighted average share price for options exercised during 2011 was 181p (2010: 136p, 2009: 180p).

The following table summarises information relating to options outstanding and exercisable under all share option plans at 31 March 2011, together with their exercise prices and dates:

Normal dates of vesting and exercise (based on calendar years)	Exercise price per share	Number of outstanding options millions	Number of exercisable options millions
<b>BT Group Employee Sharesave Plans</b>			
2011	137p–208p	11	1
2012	68p–262p	133	–
2013	104p–185p	36	–
2014	61p–111p	341	–
2015	104p–107p	46	–
<b>Total</b>		<b>567</b>	<b>1</b>
<b>BT Group Legacy Option Plan</b>			
2001–2011	318p	2	2
<b>Total</b>		<b>2</b>	<b>2</b>
<b>BT Group Global Share Option Plan</b>			
2004–2014	176p–199.5p	22	22
2005–2015	192p–263p	5	5
<b>Total</b>		<b>27</b>	<b>27</b>
<b>Total options</b>		<b>596</b>	<b>30</b>

## 6. Share-based payments continued

The options outstanding under all share option plans at 31 March 2011 have weighted average remaining contractual lives as follows:

Range of exercise prices	Employee Sharesave			Range of exercise prices	GSOP and GLOP		
	Weighted average exercise price	Number of outstanding options millions	Weighted average contractual remaining life		Weighted average exercise price	Number of outstanding options millions	Weighted average contractual remaining life
61p–68p	63p	447	36 months	176p–200p	198p	27	40 months
104p–185p	119p	112	42 months	215p–318p	302p	2	9 months
208p–262p	247p	8	19 months	–	–	–	–
<b>Total</b>	<b>77p</b>	<b>567</b>	<b>37 months</b>		<b>207p</b>	<b>29</b>	<b>38 months</b>

## Executive share plans

Movements in executive share plans during 2011 are shown below:

	Millions of shares			
	ISP	DBP	RSP	Total
At 1 April 2010	99.2	14.3	1.2	114.7
Awards granted	44.2	9.1	0.2	53.5
Awards vested	–	(3.8)	(0.9)	(4.7)
Awards lapsed	(34.2)	(1.8)	(0.2)	(36.2)
Dividend shares reinvested	5.3	0.9	–	6.2
<b>At 31 March 2011</b>	<b>114.5</b>	<b>18.7</b>	<b>0.3</b>	<b>133.5</b>

At 31 March 2011, 0.3m shares (2010: 1.1m) were held in trust and 133.2m shares (2010: 113.6m) were held in treasury for executive share plans.

## Fair value

The following table summarises the fair values and key assumptions used for valuing grants made under the Employee Sharesave plans and ISP in 2011, 2010 and 2009.

Year ended 31 March	2011		2010		2009	
	Employee Sharesave	ISP	Employee Sharesave	ISP	Employee Sharesave	ISP
Weighted average fair value	34p	108p	14p	106p	27p	47p
Weighted average share price	138p	134p	80p	131p	152p	199p
Weighted average exercise price	107p	–	63p	–	135p	–
Expected dividend yield	5.4%–5.8%	5.4%	5.7%–6.4%	6.5%	4.6%–6.4%	4.9%
Risk free rates	1.2%–2.2%	1.2%	2.2%–2.8%	2.5%	2.1%–5.5%	5.2%
Expected volatility	34.4%–41.4%	34.4%	26.9%–30.7%	38.5%	20.7%–28.4%	23.3%

Employee Sharesave grants, under the BT Group Employee Sharesave and the BT Group International Employee Sharesave option plans, are valued using a Binomial options pricing model. Awards under the ISP are valued using Monte Carlo simulations. TSRs were generated for BT and the comparator group at the end of the three-year performance period, using each company's volatility and dividend yield, as well as the cross correlation between pairs of stocks.

Volatility has been determined by reference to BT's historical volatility which is expected to reflect the BT share price in the future. An expected life of three months after vesting date is assumed for Employee Sharesave options and for all other awards the expected life is equal to the vesting period. The risk-free interest rate is based on the UK gilt curve in effect at the time of the grant, for the expected life of the option or award.

The fair values for the RSP and DBP were determined using the market price of the shares at the date of grant. The weighted average share price for RSP awards granted in 2011 was 163p (2010: 104p, 2009: 151p). The weighted average share price for DBP awards granted in 2011 was 131p (2010: 131p, 2009: 203p).

## 7. Audit and non-audit services

The following fees for audit and non-audit services were paid or are payable to the company's auditors, PricewaterhouseCoopers LLP, for the three years ended 31 March 2011.

Year ended 31 March	2011 £000	2010 £000	2009 £000
<b>Audit services</b>			
Fees payable to the company's auditor and its associates for the audit of parent company and consolidated financial statements	2,842	2,585	2,831
<b>Non-audit services</b>			
Fees payable to the company's auditor and its associates for other services:			
– The audit of the company's subsidiaries pursuant to legislation	4,636	4,732	4,675
– Other services pursuant to legislation	1,405	867	1,211
– Tax services	1,156	792	1,247
– Services relating to corporate finance transactions	–	–	32
– All other services	857	941	887
	<b>10,896</b>	<b>9,917</b>	<b>10,883</b>

Audit services – represent fees payable for services in relation to the audit of the parent company and the consolidated financial statements and also includes fees for reports under section 404 of the US Public Company Accounting Reform and Investor Protection Act of 2002 (Sarbanes-Oxley).

The audit of the company's subsidiaries pursuant to legislation – represents fees payable for services in relation to the audit of the financial statements of subsidiary companies.

Other services pursuant to legislation – represent fees payable for services in relation to other statutory filings or engagements that are required to be carried out by the appointed auditor. In particular, this includes fees for audit reports issued on the group's regulatory financial statements and comfort letters associated with the group's US debt shelf registration.

Tax services – represent fees payable for tax compliance and advisory services.

Services relating to corporate finance transactions – represent fees payable in relation to due diligence work completed on acquisitions and disposals.

All other services – represent fees payable for non-regulatory reporting on internal controls and other advice on accounting or financial matters.

The audit fee of the company was £41,000 (2010: £41,000, 2009: £41,000).

In order to maintain the independence of the external auditors, the Board has determined policies as to what non-audit services can be provided by the company's external auditors and the approval processes related to them. Under those policies, work of a consultancy nature will not be offered to the external auditors unless there are clear efficiencies and value-added benefits to the company. In this context, non-audit services in the ordinary sense of the words are considered to be those services that are not pursuant to legislation. As a proportion of the total fees this represents 18% of the total fees in 2011 (2010: 17%, 2009: 20%).

## 8. Specific items

The group separately identifies and discloses certain items by virtue of their size, nature or incidence (termed 'specific items'). This is consistent with the way that financial performance is measured by management and reported to the Board and the *Operating Committee* and it assists in providing a meaningful analysis of the trading results of the group. A definition of specific items is provided on page 91.

Year ended 31 March	2011 £m	2010 <sup>a</sup> £m	2009 <sup>a</sup> £m
<b>Revenue</b>			
Regulatory settlement <sup>b</sup>	–	52	–
BT Global Services contract and financial review charges	–	–	41
<b>Other operating income</b>			
(Profit) loss on disposal of a business	–	(2)	13
<b>Operating costs</b>			
BT Global Services restructuring charges <sup>c</sup>	192	301	280
Property rationalisation costs	88	121	–
Intangible asset impairment charges <sup>d</sup>	49	–	–
Costs associated with settlement of open tax years <sup>e</sup>	–	5	–
BT Global Services contract and financial review charges	–	–	1,598
Restructuring costs – group transformation and reorganisation activities	–	–	65
21CN asset impairment and related charge	–	–	50
	<b>329</b>	<b>427</b>	<b>1,993</b>
<b>Net finance expense</b>			
Interest expense on pension scheme liabilities <sup>f</sup>	2,323	2,211	2,308
Expected return on pension scheme assets <sup>f</sup>	(2,244)	(1,932)	(2,621)
Interest income on settlement of open tax years <sup>e</sup>	–	(11)	–
	<b>79</b>	<b>268</b>	<b>(313)</b>
<b>Share of results of associates and joint ventures</b>			
(Profit) loss on disposal of interest in associate <sup>g</sup>	(42)	12	–
Impact of renegotiated supply contracts on associate <sup>h</sup>	–	(29)	–
Reassessment of carrying value of associate	–	–	(36)
	<b>(42)</b>	<b>(17)</b>	<b>(36)</b>
<b>Net specific items charge before tax</b>	<b>366</b>	<b>728</b>	<b>1,698</b>
Tax credit on specific items above	(72)	(190)	(414)
Tax charge (credit) in respect of settlement of open tax years <sup>e</sup>	5	(230)	–
Tax credit on re-measurement of deferred tax <sup>i</sup>	(172)	–	–
	<b>(239)</b>	<b>(420)</b>	<b>(414)</b>
<b>Net specific items charge after tax</b>	<b>127</b>	<b>308</b>	<b>1,284</b>

<sup>a</sup> In 2011 the group amended its definition of specific items. Comparatives for 2010 and 2009 have been re-presented to be on a consistent basis. See page 91 for details.

<sup>b</sup> In 2010 a charge of £52m was recognised reflecting an Ofcom determination in relation to 2Mbps partial private circuits.

<sup>c</sup> The main components of the BT Global Services restructuring charges recognised in 2011, 2010 and 2009 were:

– Networks, products and procurement channels rationalisation charges of £41m (2010: £142m, 2009: £183m) from rationalising legacy networks, including the associated systems and processes. In 2010 this included a payment of £127m made to Tech Mahindra for the renegotiation of certain supply contracts as part of the rationalisation of procurement channels.

– People and property charges of £129m (2010: £132m, 2009: £51m) principally comprising leaver costs and property exit costs.

– Intangible asset impairments and other charges of £22m (2010: £27m; 2009: £46m).

<sup>d</sup> In 2011 the group recognised goodwill impairment charges of £39m mainly relating to an operational restructuring of a business acquired several years ago. In addition, intangible asset impairments of £10m

have been recognised relating to brands which are no longer in use.

<sup>e</sup> In 2010 the group agreed substantially all outstanding tax matters with HMRC relating to the 2008, 2007 and 2006 tax years. Specific items include a tax repayment of £230m and associated interest of

£11m on the repayment, and operating costs of £5m representing costs associated with reaching the agreement.

<sup>f</sup> See note 23 for more details.

<sup>g</sup> In 2011 a profit of £42m arose on the disposal of a 6.5% interest in the group's associate Tech Mahindra. In 2010 a loss of £12m arose on the disposal of an indirect interest in Tech Mahindra.

<sup>h</sup> In 2010 the group recognised a specific item credit of £29m in connection with the £127m payment to its associate Tech Mahindra, as described in c above.

<sup>i</sup> In 2011 a tax credit of £172m was recognised for the re-measurement of deferred tax balances as a result of the change in the UK statutory corporation tax rate from 28% to 26% effective in 2012.

## 9. Finance expense and finance income

Year ended 31 March	2011 £m	2010 <sup>a</sup> £m	2009 <sup>a</sup> £m
<b>Finance expense</b>			
Interest on listed bonds <sup>b,c</sup>	775	806	777
Interest on finance leases <sup>b</sup>	18	18	25
Interest on other borrowings <sup>b</sup>	56	58	130
Unwinding of discount on provisions <sup>b</sup>	3	4	3
Fair value movements on derivatives <sup>d</sup>	34	19	29
Finance expense <sup>e,f</sup>	886	905	964
Less: amounts included in the cost of qualifying assets <sup>g</sup>	(6)	(3)	–
<b>Total finance expense before specific items</b>	<b>880</b>	<b>902</b>	<b>964</b>
Specific items (note 8)	2,323	2,211	2,308
<b>Total finance expense</b>	<b>3,203</b>	<b>3,113</b>	<b>3,272</b>

<sup>a</sup> In 2011 the group amended its definition of specific items to include net interest on pensions due to its volatile nature. Comparatives have been re-presented to be on a consistent basis.

<sup>b</sup> Calculated using the effective interest rate method unless otherwise stated below.

<sup>c</sup> Includes a net charge of £38m (2010: £44m, 2009: £25m) relating to fair value movements on derivatives recycled from the cash flow reserve.

<sup>d</sup> Includes a charge of £28m (2010: £9m, 2009: £nil) arising from restructuring certain derivatives and £6m (2010: £10m, 2009: £29m) of fair value movements on derivatives not in a designated hedge relationship.

<sup>e</sup> Includes a net credit of £293m (2010: net credit of £451m, 2009: net charge of £2,161m) relating to foreign exchange movements on loans and borrowings and a net charge of £293m (2010: net charge of £451m, 2009: net credit of £2,161m) relating to fair value movements on derivatives recycled from the cash flow reserve. The items generating these foreign exchange movements are in designated hedge relationships.

<sup>f</sup> Includes a net credit of £3m (2010: net credit of £29m, 2009: net charge of £39m) relating to fair value movements arising on hedged items and net charge of £3m (2010: net charge of £29m, 2009: net credit of £39m) relating to fair value movements arising on derivatives designated as fair value hedges.

<sup>g</sup> The weighted average capitalisation rate on general borrowings was 7.8% in 2011 (2010: 7.9%).

Year ended 31 March	2011 £m	2010 <sup>a</sup> £m	2009 <sup>a</sup> £m
<b>Finance income</b>			
Interest on available-for-sale investments	9	5	14
Interest on loans and receivables	7	7	17
Other interest and similar income	19	–	–
<b>Total finance income before specific items</b>	<b>35</b>	<b>12</b>	<b>31</b>
Specific items (note 8)	2,244	1,943	2,621
<b>Total finance income</b>	<b>2,279</b>	<b>1,955</b>	<b>2,652</b>

<sup>a</sup> In 2011 the group amended its definition of specific items to include net interest on pensions due to its volatile nature. Comparatives have been re-presented to be on a consistent basis.

Year ended 31 March	2011 £m	2010 £m	2009 £m
<b>Net finance expense before specific items</b>	<b>845</b>	<b>890</b>	<b>933</b>
Specific items (note 8)	79	268	(313)
<b>Net finance expense</b>	<b>924</b>	<b>1,158</b>	<b>620</b>

## 10. Taxation

### Analysis of taxation (expense) credit for the year

Year ended 31 March	2011 £m	2010 £m	2009 £m
United Kingdom			
Corporation tax at 28% (2010: 28%, 2009: 28%)	(197)	(161)	–
Adjustments in respect of prior periods	(7)	204	50
Non UK taxation			
Current	(40)	(31)	(48)
Adjustments in respect of prior periods	11	–	10
<b>Total current tax (expense) credit</b>	<b>(233)</b>	<b>12</b>	<b>12</b>
Deferred tax			
Origination and reversal of temporary differences	(184)	(53)	77
Adjustments in respect of prior periods	32	63	(36)
Impact of change in UK corporation tax rate to 26%	172	–	–
<b>Total deferred tax credit</b>	<b>20</b>	<b>10</b>	<b>41</b>
<b>Total taxation (expense) credit</b>	<b>(213)</b>	<b>22</b>	<b>53</b>

### Factors affecting taxation (expense) credit

The taxation (expense) credit on the profit (loss) for the year differs from the amount computed by applying the corporation tax rate to the profit (loss) before taxation as a result of the following factors:

Year ended 31 March	2011		2010		2009	
	£m	%	£m	%	£m	%
<b>Profit (loss) before taxation</b>	<b>1,717</b>		<b>1,007</b>		<b>(244)</b>	
Expected taxation (expense) credit at UK rate of 28% (2010: 28%, 2009: 28%)	(481)	28.0	(282)	28.0	68	28.0
Effects of:						
Non deductible depreciation and amortisation	(15)	0.9	(18)	1.7	(27)	(11.0)
Non deductible (taxable) non UK losses (profits)	(13)	0.8	(26)	2.6	24	9.8
Overseas losses utilised	53	(3.1)	35	(3.4)	–	–
Higher (lower) taxes on non UK profits	(1)	–	(1)	0.1	9	3.7
Higher (lower) taxes on gain on disposal of business	12	(0.7)	–	–	(4)	(1.6)
Other deferred tax assets not recognised	(8)	0.4	(17)	1.6	(5)	(2.0)
Associates and joint ventures	6	(0.3)	11	(1.1)	21	8.6
Adjustments in respect of prior periods	36	(2.1)	37	(3.7)	24	9.8
Tax credit in respect of settlement of open tax years	–	–	230	(22.9)	–	–
Re-measurement of deferred tax balances at 26%	172	(10.0)	–	–	–	–
Adoption of the amendment to IFRS 2	–	–	–	–	(30)	(12.3)
Other	26	(1.5)	53	(5.1)	(27)	(11.1)
<b>Total taxation (expense) credit and effective tax rate</b>	<b>(213)</b>	<b>12.4</b>	<b>22</b>	<b>(2.2)</b>	<b>53</b>	<b>21.9</b>
Exclude specific items (note 8)	(239)		(420)		(414)	
<b>Total taxation (expense) before specific items and effective rate on profit before specific items</b>	<b>(452)</b>	<b>21.7</b>	<b>(398)</b>	<b>22.9</b>	<b>(361)</b>	<b>24.8</b>

### Factors that may affect future tax charges

The rate of UK corporation tax changed from 28% to 26% on 1 April 2011. The UK government has also indicated that it intends to enact future reductions in the corporation tax rate down to 23% by 1 April 2014.

### Tax credit (expense) recognised directly in equity

Year ended 31 March	2011 £m	2010 £m	2009 £m
Deferred tax credit (expense) relating to share-based payments	91	19	(12)
<b>Total taxation credit (expense) recognised directly in equity</b>	<b>91</b>	<b>19</b>	<b>(12)</b>

## 10. Taxation continued

### Tax components of other comprehensive income

The tax (expense) credit relating to components of other comprehensive income is as follows:

Year ended 31 March	2011			2010			2009		
	Before tax £m	Tax (expense) credit £m	After tax £m	Before tax £m	Tax (expense) credit £m	After tax £m	Before tax £m	Tax (expense) credit £m	After tax £m
Actuarial gains (losses) relating to retirement benefit obligations	5,109	(1,534)	3,575	(4,324)	1,211	(3,113)	(7,037)	1,959	(5,078)
Exchange differences on translation of foreign operations	(140)	18	(122)	(119)	(20)	(139)	692	64	756
Fair value movements on available-for-sale assets	15	–	15	7	–	7	5	–	5
Fair value movements on cash flow hedges									
– fair value (losses) gains	(347)	(124)	(471)	(1,067)	297	(770)	2,719	(766)	1,953
– recognised in income and expense	333	119	452	496	(139)	357	(2,144)	600	(1,544)
– reclassified and reported in non-current assets	–	–	–	(4)	1	(3)	(5)	2	(3)
	<b>4,970</b>	<b>(1,521)</b>	<b>3,449</b>	<b>(5,011)</b>	<b>1,350</b>	<b>(3,661)</b>	<b>(5,770)</b>	<b>1,859</b>	<b>(3,911)</b>
Current tax credit (expense)		25			(2)			–	
Deferred tax (expense) credit		(1,546)			1,352			1,859	
		<b>(1,521)</b>			<b>1,350</b>			<b>1,859</b>	

## 11. Earnings (loss) per share

Basic earnings (loss) per share is calculated by dividing the profit or loss attributable to equity shareholders by the weighted average number of shares in issue after deducting the group's shares held by employee share ownership trusts and treasury shares.

In calculating the diluted earnings (loss) per share, share options outstanding and other potential shares have been taken into account where the impact of these is dilutive. Options over 81m shares (2010: 138m shares, 2009: 158m shares) were excluded from the calculation of the total diluted number of shares as the impact of these is antidilutive.

Year ended 31 March	2011	2010	2009
Profit (loss) attributable to equity shareholders of the parent (£m)	1,502	1,028	(193)
Basic weighted average number of shares (millions)	7,750	7,740	7,724
Dilutive shares from share options (millions)	252	174	5
Dilutive shares held in trust (millions)	114	74	42
Diluted weighted average number of shares (millions)	8,116	7,988	7,771
Basic earnings (loss) per share	19.4p	13.3p	(2.5)p
Diluted earnings (loss) per share	18.5p	12.9p	(2.5)p

## 12. Dividends

Year ended 31 March	2011		2010		2009	
	pence per share	£m	pence per share	£m	pence per share	£m
Final dividend paid in respect of the prior year	4.6	357	1.1	85	10.4	804
Interim dividend paid in respect of the current year	2.4	186	2.3	178	5.4	418
	<b>7.0</b>	<b>543</b>	<b>3.4</b>	<b>263</b>	<b>15.8</b>	<b>1,222</b>

The Board recommends that a final dividend in respect of the year ended 31 March 2011 of 5.0p per share will be paid to shareholders on 5 September 2011, taking the full year proposed dividend in respect of the 2011 financial year to 7.4p (2010: 6.9p, 2009: 6.5p) which amounts to approximately £574m (2010: £534m, 2009: £503m). This dividend is subject to approval by shareholders at the Annual General Meeting and therefore the liability of approximately £388m (2010: £356m, 2009: £85m) has not been included in these financial statements. The proposed dividend will be payable to all shareholders on the Register of Members on 12 August 2011.

### 13. Intangible assets

	Goodwill £m	Brands, customer relationships and technology £m	Telecommunication licences and other £m	Internally developed software £m	Computer software £m	Total £m
<b>Cost</b>						
At 1 April 2009	1,489	376	307	2,348	1,204	5,724
Additions	–	–	–	585	44	629
Acquisitions through business combinations	1	–	–	–	–	1
Interest on qualifying assets <sup>a</sup>	–	–	–	2	–	2
Disposals and adjustments	(2)	(3)	(6)	(362)	9	(364)
Exchange differences	(56)	(16)	(11)	(5)	(16)	(104)
<b>At 1 April 2010</b>	<b>1,432</b>	<b>357</b>	<b>290</b>	<b>2,568</b>	<b>1,241</b>	<b>5,888</b>
Additions	–	–	–	435	65	500
Acquisitions through business combinations	6	–	–	–	–	6
Interest on qualifying assets <sup>a</sup>	–	–	–	4	–	4
Disposals and adjustments	–	–	–	(92)	(5)	(97)
Impairment charges <sup>b</sup>	(39)	(10)	–	–	–	(49)
Exchange differences	(42)	(9)	(2)	(2)	(3)	(58)
<b>At 31 March 2011</b>	<b>1,357</b>	<b>338</b>	<b>288</b>	<b>2,913</b>	<b>1,298</b>	<b>6,194</b>
<b>Amortisation</b>						
At 1 April 2009		153	156	739	888	1,936
Charge for the year		54	15	559	107	735
Disposals and adjustments		(1)	(4)	(366)	(53)	(424)
Exchange differences		(9)	(5)	(5)	(12)	(31)
<b>At 1 April 2010</b>		<b>197</b>	<b>162</b>	<b>927</b>	<b>930</b>	<b>2,216</b>
Charge for the year		47	14	544	86	691
Disposals and adjustments		–	–	(91)	(4)	(95)
Exchange differences		(2)	(1)	(1)	(3)	(7)
<b>At 31 March 2011</b>		<b>242</b>	<b>175</b>	<b>1,379</b>	<b>1,009</b>	<b>2,805</b>
<b>Carrying amount</b>						
<b>At 31 March 2011</b>	<b>1,357</b>	<b>96</b>	<b>113</b>	<b>1,534</b>	<b>289</b>	<b>3,389</b>
At 31 March 2010	1,432	160	128	1,641	311	3,672

<sup>a</sup> Additions to internally generated software in 2011 includes interest capitalised at a weighted average borrowing rate of 7.8% (2010: 7.9%).

<sup>b</sup> See note 8 for details.

### Goodwill impairment review

The group performs an annual goodwill impairment review, based on its cash generating units (CGUs). The CGUs that have associated goodwill are BT Global Services and BT Retail's business units: BT Consumer, BT Business, BT Ireland and BT Enterprises. These are the smallest identifiable groups of assets that generate cash inflows that are largely independent of the cash inflows from other groups of assets, and to which goodwill is allocated. Goodwill is allocated to the group's CGUs as follows:

	BT Global Services £m	BT Retail				Total £m
		BT Consumer £m	BT Business £m	BT Ireland £m	BT Enterprises £m	
At 1 April 2009	1,226	57	44	16	146	1,489
Acquisitions through business combinations	1	–	–	–	–	1
Disposals, adjustments and reclassifications	(3)	8	17	5	(29)	(2)
Exchange differences	(52)	–	–	–	(4)	(56)
<b>At 1 April 2010</b>	<b>1,172</b>	<b>65</b>	<b>61</b>	<b>21</b>	<b>113</b>	<b>1,432</b>
Acquisitions through business combinations	6	–	–	–	–	6
Reclassifications	–	–	(15)	–	15	–
Impairment charges <sup>a</sup>	(39)	–	–	–	–	(39)
Exchange differences	(37)	–	–	–	(5)	(42)
<b>At 31 March 2011</b>	<b>1,102</b>	<b>65</b>	<b>46</b>	<b>21</b>	<b>123</b>	<b>1,357</b>

<sup>a</sup> The goodwill impairment charges recognised in 2011 mainly relate to an operational restructuring of a business acquired several years ago.

### 13. Intangible assets continued

The key assumptions used in performing the value in use calculations in 2011 were as follows:

	BT Global Services	BT Retail			
		BT Consumer	BT Business	BT Ireland	BT Enterprises
Discount rate	10.0%	10.0%	10.0%	10.0%	10.0%
Perpetuity growth rate	2.5%	2.0%	2.0%	2.0%	2.0%

The key assumptions used in performing value in use calculations in 2010 were as follows:

	BT Global Services	BT Retail			
		BT Consumer	BT Business	BT Ireland	BT Enterprises
Discount rate	10.8%	10.8%	10.8%	10.8%	10.8%
Perpetuity growth rate	2.5%	2.0%	2.0%	2.0%	2.0%

#### Recoverable amount

The value in use of each CGU is determined using cash flow projections derived from financial plans approved by the Board covering a three-year period and a further two years approved by the line of business and group senior management team. They reflect management's expectations of revenue, EBITDA growth, capital expenditure, working capital and operating cash flows, based on past experience and future expectations of business performance. Cash flows are also adjusted downwards to reflect the different risk attributes of each CGU. Cash flows beyond the five-year period have been extrapolated using perpetuity growth rates.

#### Discount rate

The pre-tax discount rates applied to the cash flow forecasts are derived from the group's post-tax weighted average cost of capital. The assumptions used in the calculation of the group's weighted average cost of capital are benchmarked to externally available data.

#### Growth rates

The perpetuity growth rates are determined based on the long-term historical growth rates of the regions in which the CGU operates, and they reflect an assessment of the long-term growth prospects of the sector in which the CGU operates. The growth rates have been benchmarked against external data for the relevant markets. None of the growth rates applied exceed the long-term historical average growth rates for those markets or sectors.

#### Sensitivities

For the BT Retail CGUs, significant headroom exists in each CGU and, based on the sensitivity analysis performed, no reasonably possible changes in the assumptions would cause the carrying amount of the CGUs to exceed their recoverable amount.

For BT Global Services, the value in use exceeds the carrying value of the CGU by approximately £895m. The following changes in assumptions would cause the recoverable amount to fall below the carrying value:

- a reduction in the perpetuity growth rate from the 2.5% assumption applied to a revised assumption of a 0.7% decline or more
- an increase in the discount rate from the 10.0% assumption applied to a revised assumption of 12.2% or more
- a reduction in the projected operating cash flows across five years by 25% or more.

## 14. Property, plant and equipment

	Land and buildings <sup>a,b</sup> £m	Network infrastructure equipment <sup>b</sup> £m	Other <sup>c</sup> £m	Assets in course of construction £m	Total £m
<b>Cost</b>					
At 1 April 2009	1,294	41,558	2,374	910	46,136
Additions	22	254	144	1,441	1,861
Interest on qualifying assets <sup>d</sup>	–	–	–	1	1
Transfers	5	1,520	1	(1,526)	–
Disposals and adjustments	71	(1,121)	(346)	(14)	(1,410)
Exchange differences	(13)	(131)	(22)	(5)	(171)
<b>At 1 April 2010</b>	<b>1,379</b>	<b>42,080</b>	<b>2,151</b>	<b>807</b>	<b>46,417</b>
Additions	11	197	180	1,690	2,078
Interest on qualifying assets <sup>d</sup>	–	–	–	2	2
Transfers	17	1,729	1	(1,747)	–
Disposals and adjustments	(2)	(1,350)	(77)	(13)	(1,442)
Exchange differences	(6)	(39)	(8)	(3)	(56)
<b>At 31 March 2011</b>	<b>1,399</b>	<b>42,617</b>	<b>2,247</b>	<b>736</b>	<b>46,999</b>
<b>Accumulated depreciation</b>					
At 1 April 2009	590	28,413	1,756	–	30,759
Charge for the year	70	2,015	219	–	2,304
Disposals and adjustments	72	(1,124)	(255)	–	(1,307)
Exchange differences	(7)	(103)	(14)	–	(124)
<b>At 1 April 2010</b>	<b>725</b>	<b>29,201</b>	<b>1,706</b>	<b>–</b>	<b>31,632</b>
Charge for the year	63	2,019	206	–	2,288
Disposals and adjustments	(13)	(1,316)	(98)	–	(1,427)
Exchange differences	(3)	(24)	(7)	–	(34)
<b>At 31 March 2011</b>	<b>772</b>	<b>29,880</b>	<b>1,807</b>	<b>–</b>	<b>32,459</b>
<b>Carrying amount</b>					
<b>At 31 March 2011</b>	<b>627</b>	<b>12,737</b>	<b>440</b>	<b>736</b>	<b>14,540</b>
Engineering stores	–	–	–	83	83
<b>Total at 31 March 2011</b>	<b>627</b>	<b>12,737</b>	<b>440</b>	<b>819</b>	<b>14,623</b>
At 31 March 2010	654	12,879	445	807	14,785
Engineering stores	–	–	–	71	71
<b>Total at 31 March 2010</b>	<b>654</b>	<b>12,879</b>	<b>445</b>	<b>878</b>	<b>14,856</b>

	2011 £m	2010 £m
<sup>a</sup> The carrying amount of land and buildings, including leasehold improvements, comprised:		
Freehold	420	431
Long leases (over 50 years unexpired)	34	33
Short leases	173	190
<b>Total land and buildings</b>	<b>627</b>	<b>654</b>

<sup>b</sup> The carrying amount of the group's property, plant and equipment includes an amount of £140m (2010: £183m) in respect of assets held under finance leases, comprising land and buildings of £71m (2010: £74m) and network infrastructure and equipment of £69m (2010: £109m). The depreciation charge on those assets for 2011 was £33m (2010: £44m), comprising land and buildings of £3m (2010: £3m) and network infrastructure and equipment of £30m (2010: £41m).

<sup>c</sup> Other mainly comprises motor vehicles and computers.

<sup>d</sup> Additions to assets in the course of construction in 2011 includes interest capitalised at a weighted average borrowing rate of 7.8% (2010: 7.9%).

## 14. Property, plant and equipment continued

Year ended 31 March	2011 £m	2010 £m
Additions to property, plant and equipment comprised:		
Land and buildings	20	29
Network infrastructure and equipment		
Transmission equipment	985	902
Exchange equipment	43	29
Other network equipment	851	753
Other		
Computers and office equipment	92	115
Motor vehicles and other	87	33
<b>Total additions to property, plant and equipment</b>	<b>2,078</b>	<b>1,861</b>
Increase in engineering stores	12	43
<b>Total additions</b>	<b>2,090</b>	<b>1,904</b>

## 15. Investments

At 31 March	2011 £m	2010 £m
<b>Non-current assets</b>		
Available-for-sale	61	32
Loans and receivables	–	32
	<b>61</b>	<b>64</b>
<b>Current assets</b>		
Available-for-sale	1	258
Loans and receivables	7	148
Fair value through profit and loss	11	–
	<b>19</b>	<b>406</b>

The majority of current asset investments are held for periods ranging from one day to one year.

### Available-for-sale

Available-for-sale current assets consist of a US Dollar listed investment of £1m (2010: £nil) and floating rate liquidity fund deposits denominated in Sterling of £nil (2010: £185m), Euros of £nil (2010: £56m) and US Dollars of £nil (2010: £17m). Non-current assets include unlisted investments of £27m (2010: £12m) which are measured at the lower of cost and net realisable value.

### Loans and receivables

Loans and receivables mainly consist of term deposits denominated in Sterling with a fixed interest rate.

## 16. Cash and cash equivalents

At 31 March	2011 £m	2010 £m
<b>Cash at bank and in hand</b>	<b>141</b>	<b>197</b>
<b>Cash equivalents</b>		
Loans and receivables		
UK deposits	182	1,211
US deposits	20	37
European deposits	8	7
<b>Total cash equivalents</b>	<b>210</b>	<b>1,255</b>
<b>Total cash and cash equivalents</b>	<b>351</b>	<b>1,452</b>
Bank overdrafts	(26)	(8)
<b>Cash and cash equivalents per the cash flow statement</b>	<b>325</b>	<b>1,444</b>

The group has cross undertaking guarantee facilities across certain bank accounts which allow a legally enforceable right of set-off of the relevant cash and overdraft balances on bank accounts included within each scheme.

The group's cash at bank included restricted cash of £77m (2010: £54m), of which £59m (2010: £29m) were held in countries in which prior approval is required to transfer funds abroad. Such liquid funds are at the group's disposition within a reasonable period of time if it complies with these requirements. The remaining balance of £18m (2010: £25m) were held in escrow accounts.

Cash and cash equivalents are primarily fixed rate financial assets held for periods ranging from one day to three months.

## 17. Associates and joint ventures

	2011			2010		
	Associates £m	Joint ventures £m	Total £m	Associates £m	Joint ventures £m	Total £m
Non-current assets	28	6	34	49	7	56
Current assets	214	5	219	278	4	282
Current liabilities	(43)	(1)	(44)	(77)	(2)	(79)
Non-current liabilities	(45)	–	(45)	(64)	–	(64)
<b>Share of net assets at 31 March</b>	<b>154</b>	<b>10</b>	<b>164</b>	<b>186</b>	<b>9</b>	<b>195</b>
Revenue	263	22	285	298	14	312
Expenses	(233)	(26)	(259)	(266)	(14)	(280)
Taxation	(5)	–	(5)	(7)	–	(7)
<b>Share of post tax results before specific items</b>	<b>25</b>	<b>(4)</b>	<b>21</b>	<b>25</b>	<b>–</b>	<b>25</b>
Specific items (note 8)	–	–	–	29	–	29
<b>Share of post tax results</b>	<b>25</b>	<b>(4)</b>	<b>21</b>	<b>54</b>	<b>–</b>	<b>54</b>

## 17. Associates and joint ventures continued

	Associates £m	Joint ventures £m	Total £m
At 1 April 2009	123	9	132
Share of post tax profit	54	–	54
Additions	3	–	3
Disposals	(12)	–	(12)
Dividends received	(3)	–	(3)
Exchange differences and other	21	–	21
<b>At 1 April 2010</b>	<b>186</b>	<b>9</b>	<b>195</b>
Share of post tax profit (loss)	25	(4)	21
Additions	–	4	4
Disposals	(42)	–	(42)
Dividends received	(7)	–	(7)
Exchange differences	(8)	1	(7)
<b>At 31 March 2011</b>	<b>154</b>	<b>10</b>	<b>164</b>

At 31 March 2011 the fair value of the group's investments in associates and joint ventures for which published price quotations are available was £279m (2010: £473m). Details of the group's principal associate at 31 March 2011 are set out on page 155.

## 18. Inventories

At 31 March	2011 £m	2010 £m
Consumables	28	30
Work in progress	46	43
Finished goods	47	34
	<b>121</b>	<b>107</b>

## 19. Trade and other receivables

At 31 March	2011 £m	2010 £m
<b>Current</b>		
Trade receivables	1,770	1,937
Prepayments	570	549
Accrued income	788	1,010
Other receivables	204	200
	<b>3,332</b>	<b>3,696</b>

	2011 £m	2010 £m
<b>Non-current</b>		
Other assets <sup>a</sup>	<b>286</b>	<b>336</b>

<sup>a</sup> Other assets mainly represent costs relating to the initial set up, transition or transformation phase of long-term networked IT services contracts. At 31 March 2011 the balance was £249m (2010: £294m). Other assets also include prepayments of £37m (2010: £42m).

Trade receivables are stated after deducting allowances for doubtful debts, as follows:

	2011 £m	2010 £m
At 1 April	219	246
Expense	112	155
Utilised	(136)	(183)
Exchange differences	(3)	1
<b>At 31 March</b>	<b>192</b>	<b>219</b>

## 19. Trade and other receivables continued

Trade receivables are continuously monitored and allowances applied against trade receivables consist of both specific impairments and collective impairments based on the group's historical loss experiences for the relevant aged category and taking into account general economic conditions. Historical loss experience allowances are calculated by line of business in order to reflect the specific nature of the customers relevant to that line of business.

Trade receivables are due as follows:

	Not past due £m	Trade receivables specifically impaired net of provision £m	Past due and not specifically impaired:				Total £m
			Between 0 and 3 months £m	Between 3 and 6 months £m	Between 6 and 12 months £m	Over 12 months £m	
2011	967	127	461	93	71	51	1,770
2010	1,257	51	426	98	60	45	1,937

Gross trade receivables which have been specifically impaired amounted to £193m (2010: £130m).

Trade receivables not past due and accrued income are analysed below by line of business. The nature of customers associated with each line of business is disclosed in note 1.

At 31 March	2011 £m	2010 £m
BT Global Services	674	867
BT Retail	178	228
BT Wholesale	82	127
Openreach	25	27
Other	8	8
<b>Total trade receivables not past due</b>	<b>967</b>	<b>1,257</b>

At 31 March	2011 £m	2010 £m
BT Global Services	422	633
BT Retail	138	148
BT Wholesale	176	182
Openreach	47	44
Other	5	3
<b>Total accrued income</b>	<b>788</b>	<b>1,010</b>

Given the broad and varied nature of the group's customer base, the analysis of trade receivables not past due and accrued income by line of business is considered the most appropriate disclosure of credit concentrations. Cash collateral held against trade and other receivables amounted to £29m (2010: £25m).

## 20. Loans and other borrowings

At 31 March	2011 £m	2010 £m
US Dollar 9.375% bonds December 2010 (2010: 9.125%, minimum 8.125% <sup>a</sup> ) <sup>b</sup>	–	1,951
Euro 7.87% bonds February 2011 (2010: 7.87%, minimum 6.875% <sup>a</sup> ) <sup>b</sup>	–	1,015
US Dollar 5.15% bonds January 2013 <sup>b</sup>	537	566
Euro 5.25% bonds January 2013 <sup>b</sup>	898	902
Euro 5.25% bonds June 2014 <sup>b</sup>	693	696
Euro 6.125% bonds July 2014 <sup>a,d</sup>	557	561
Euro 6.5% bonds July 2015 <sup>b</sup>	930	935
Sterling 8.75% bonds December 2016 (2010: 8.5%, minimum 7.5% <sup>a</sup> )	715	715
Sterling 6.625% bonds June 2017 <sup>b</sup>	525	525
US Dollar 5.95% bonds January 2018 <sup>b</sup>	695	734
Sterling 8.625% bonds 2020	298	298
Sterling 3.5% index linked bonds April 2025	340	325
Sterling 5.75% bonds December 2028 <sup>c</sup>	605	602
US Dollar 9.875% bonds December 2030 (2010: 9.625%, minimum 8.625% <sup>a</sup> ) <sup>b</sup>	1,714	1,811
Sterling 6.375% bonds June 2037 <sup>b</sup>	521	521
<b>Total listed bonds</b>	<b>9,028</b>	<b>12,157</b>
<b>Finance leases</b>	<b>294</b>	<b>304</b>
Sterling 6.35% bank loan due August 2012	312	312
Other loans	125	10
Commercial paper <sup>e</sup>	71	–
Bank overdrafts (see note 16)	26	8
<b>Total other loans and borrowings</b>	<b>534</b>	<b>330</b>
<b>Total loans and borrowings</b>	<b>9,856</b>	<b>12,791</b>

<sup>a</sup> The interest rate payable on these bonds will be subject to adjustment from time to time if either Moody's or Standard & Poor's (S&P) reduce the rating ascribed to the group's senior unsecured debt below A3 in the case of Moody's or below A- in the case of S&P. In this event, the interest payable on the bonds and the spread applicable to the floating rate bonds will be increased by 0.25% for each ratings category adjustment by each ratings agency. In addition, if Moody's or S&P subsequently increase the ratings ascribed to the group's senior unsecured debt, then the interest rate will be decreased by 0.25% for each rating category upgrade by each rating agency, but in no event will the interest rate be reduced below the minimum interest rate reflected in the above table. In February 2010 S&P downgraded BT's credit rating by one ratings category to BBB-. At the next coupon date in 2011 the rate payable on these bonds increased by 0.25 percentage points.

<sup>b</sup> Hedged in a designated cash flow hedge.

<sup>c</sup> Hedged in a designated fair value hedge.

<sup>d</sup> The interest rate payable on this bond attracts an additional 1.25% for a downgrade by one credit rating category by either or both Moody's and S&P below Baa3/BBB- respectively.

<sup>e</sup> Commercial paper is denominated in Euros of £56m (2010: £nil) and US Dollars of £15m (2010: £nil).

The interest rates payable on loans and borrowings disclosed above reflect the coupons on underlying issued loans and borrowings and not the interest rates achieved through applying associated currency and interest rate swaps in hedge arrangements.

The carrying values disclosed above reflect balances at amortised cost adjusted for accrued interest and current fair value adjustments to the relevant loans or borrowings. This does not reflect the final principal repayment that will arise after taking account of the relevant derivatives in hedging relationships which is reflected in the table below. Apart from finance leases, all borrowings as at 31 March 2011 and 2010 were unsecured.

At 31 March	2011			2010		
	Carrying amount £m	Effect of hedging and interest <sup>a</sup> £m	Principal repayments at hedged rates £m	Carrying amount £m	Effect of hedging and interest <sup>a</sup> £m	Principal repayments at hedged rates £m
Repayments fall due as follows:						
<b>Within one year, or on demand</b>	<b>485</b>	<b>(266)</b>	<b>219</b>	<b>3,269</b>	<b>(737)</b>	<b>2,532</b>
Between one and two years	1,747	(66)	1,681	18	–	18
Between two and three years	10	–	10	1,763	(313)	1,450
Between three and four years	1,209	(48)	1,161	11	–	11
Between four and five years	901	(94)	807	1,213	(177)	1,036
After five years	5,507	(198)	5,309	6,523	(431)	6,092
<b>Total due for repayment after more than one year</b>	<b>9,374</b>	<b>(406)</b>	<b>8,968</b>	<b>9,528</b>	<b>(921)</b>	<b>8,607</b>
<b>Total repayments</b>	<b>9,859</b>	<b>(672)</b>	<b>9,187</b>	<b>12,797</b>	<b>(1,658)</b>	<b>11,139</b>
Fair value adjustments for hedged risk	(3)			(6)		
<b>Total loans and other borrowings</b>	<b>9,856</b>			<b>12,791</b>		

<sup>a</sup> Adjustments for hedging and interest reflect the impact of the currency element of derivatives and adjust the repayments to exclude interest recognised in the carrying amount.

## 20. Loans and other borrowings continued

As noted on page 126, the principal repayments of loans and borrowings at hedged rates amounted to £9,187m (2010: £11,139m). The table below reflects the currency risk and interest cash flow and fair value risk associated with these loans and borrowings after the impact of hedging.

At 31 March	2011			2010		
	Fixed rate interest £m	Floating rate interest £m	Total £m	Fixed rate interest £m	Floating rate interest £m	Total £m
Sterling	7,954	913	8,867	10,110	835	10,945
Euro	–	283	283	–	184	184
US Dollar	18	2	20	–	3	3
Other	–	17	17	–	7	7
<b>Total</b>	<b>7,972</b>	<b>1,215</b>	<b>9,187</b>	<b>10,110</b>	<b>1,029</b>	<b>11,139</b>
Weighted average effective fixed interest rate Sterling	7.4%			8.0%		

The floating rate loans and borrowings bear interest rates fixed in advance for periods ranging from one day to one year, primarily by reference to LIBOR and EURIBOR quoted rates.

Obligations under finance leases at the balance sheet date are analysed as follows:

At 31 March	2011		2010	
	Minimum lease payments £m	Repayment of outstanding lease obligations £m	Minimum lease payments £m	Repayment of outstanding lease obligations £m
Amounts payable under finance leases:				
Within one year	19	2	33	16
In the second to fifth years inclusive	128	57	119	48
After five years	513	235	535	240
	<b>660</b>	<b>294</b>	<b>687</b>	<b>304</b>
Less: future finance charges	(366)	–	(383)	–
<b>Total finance lease obligations</b>	<b>294</b>	<b>294</b>	<b>304</b>	<b>304</b>

Assets held under finance leases mainly consist of buildings and network assets. The group's obligations under finance leases are secured by the lessors' title to the leased assets.

## 21. Derivative financial instruments

At 31 March	2011		2010	
	Assets £m	Liabilities £m	Assets £m	Liabilities £m
<b>Cash flow hedges</b>				
Interest rate swaps	–	265	–	361
Cross currency swaps	622	29	1,571	30
Forward foreign exchange rate contracts	4	6	23	4
	<b>626</b>	<b>300</b>	<b>1,594</b>	<b>395</b>
<b>Fair value hedges</b>				
Interest rate swaps	4	2	–	6
	<b>4</b>	<b>2</b>	<b>–</b>	<b>6</b>
<b>Derivatives not in a formal hedge relationship</b>				
Interest rate swaps	99	267	106	295
Cross currency swaps	–	–	–	1
Forward foreign exchange rate contracts	4	–	–	2
	<b>103</b>	<b>267</b>	<b>106</b>	<b>298</b>
	<b>733</b>	<b>569</b>	<b>1,700</b>	<b>699</b>

For a further description of the group's derivative financial instruments and hedge designations, see note 29.

## 21. Derivative financial instruments continued

The maturity of derivative financial instruments is shown below:

At 31 March	2011		2010	
	Assets £m	Liabilities £m	Assets £m	Liabilities £m
Within one year or on demand	108	62	624	166
<b>Current</b>	<b>108</b>	<b>62</b>	<b>624</b>	<b>166</b>
Between one and two years	71	9	–	–
Between two and three years	–	–	211	–
Between three and four years	66	100	–	–
Between four and five years	73	–	222	128
After five years	415	398	643	405
<b>Non-current</b>	<b>625</b>	<b>507</b>	<b>1,076</b>	<b>533</b>
<b>Total</b>	<b>733</b>	<b>569</b>	<b>1,700</b>	<b>699</b>

## 22. Trade and other payables

At 31 March	2011 £m	2010 £m
<b>Current</b>		
Trade payables	3,250	3,668
Other taxation and social security	485	516
Other payables	530	506
Accrued expenses	505	498
Deferred income	1,344	1,343
	<b>6,114</b>	<b>6,531</b>
<b>Non-current<sup>a</sup></b>		
Other payables	762	734
Deferred income	69	70
	<b>831</b>	<b>804</b>

<sup>a</sup> Non-current payables mainly relate to operating lease liabilities and deferred gains on a prior period sale and finance leaseback transaction.

## 23. Retirement benefit plans

### Background

The group has both defined benefit and defined contribution retirement benefit plans.

The group's main plans are in the UK. The BTPS is a defined benefit plan which has been closed to new entrants since 31 March 2001. Subsequent to that date new entrants have been able to join a defined contribution plan, initially the BT Retirement Plan (BTRP) and since 1 April 2009 the BT Retirement Saving Scheme (BTRSS), a contract-based defined contribution arrangement, to which BTRP members were invited to transfer their accumulated assets.

A defined contribution plan is a pension arrangement under which both the company and participating members pay fixed contributions to an independently administered fund. Pension benefits for members of the plan are linked to contributions paid, the performance of each individual's chosen investments and the annuity rates at retirement. The income statement charge in respect of defined contribution plans represents the contribution payable by the group based upon a fixed percentage of employees' pay. The company has no exposure to investment and other experience risks.

A defined benefit plan is a pension arrangement under which participating members receive a pension benefit at retirement dependent on factors such as age, years of service and pensionable pay. Benefits are determined by the scheme rules and are not dependent upon actual contributions made by the company or members. The plan is administered by an independent trustee who is responsible for ensuring that the plan is sufficiently funded to meet current and future benefit payments and therefore must agree with the sponsoring company a funding plan for additional company contributions where it is estimated that the benefits will not be met from regular contributions and expected investment returns. The company is exposed to investment and other experience risks.

The membership of the BTPS is shown below:

At 31 March	2011 Number of members	2010 Number of members
Active members	51,000	55,000
Deferred members	88,500	93,000
Pensioners	188,000	185,000
<b>Total membership</b>	<b>327,500</b>	<b>333,000</b>

Since 1 April 2009, active BTPS members accrue benefits based upon a career average revalued earnings (CARE) basis and a normal pensionable age of 65. Pensionable service prior to that date entitles scheme members to benefits based upon their final salary and a normal pensionable age of 60. On a CARE basis, rather than being based upon final salary, benefits are built up based upon earnings in each year and the benefit accrued for each year is increased by the lower of inflation or the individual's actual pay increase in each year to retirement. Under the scheme rules, pension benefits are increased in line with inflation (see below for details).

BT Pension Scheme Trustees Limited (the "Trustee") administers and manages the scheme on behalf of the members in accordance with the terms of the Trust Deed of the scheme and relevant legislation. Under the terms of the Trust Deed of the BTPS, there are nine Trustee directors appointed by the group, five of which appointments are made with the agreement of the relevant trade unions, including the Chairman of the Trustee. Four Trustee directors, other than the Chairman, are appointed by BT on the nomination of the relevant trade unions. Two of the Trustee directors will normally hold senior positions within the group, and two will normally hold (or have held) senior positions in commerce or industry. Subject to there being an appropriately qualified candidate, there should be at least one current pensioner or deferred pensioner of the BTPS as one of the Trustee directors. Trustee directors are appointed for a three-year term, but are then eligible for re-appointment.

Further details of the governance of the BTPS, its financial position and performance of investments, and a summary of member benefits are available in the BTPS Annual Report published by the Trustee in June each year.

### Amounts recognised in the income statement in respect of the group's pension plans

Year ended 31 March	2011 £m	2010 £m	2009 £m
<b>Recognised in the income statement before specific items</b>			
Current service cost – defined benefit plans	297	206	459
– defined contribution plans	119	98	85
<b>Total operating charge</b>	<b>416</b>	<b>304</b>	<b>544</b>
<b>Specific items (note 8)</b>			
Expected return on pension plan assets	(2,244)	(1,932)	(2,621)
Interest expense on pension plan liabilities	2,323	2,211	2,308
<b>Net interest expense (income) included in specific items</b>	<b>79</b>	<b>279</b>	<b>(313)</b>
<b>Total recognised in the income statement</b>	<b>495</b>	<b>583</b>	<b>231</b>

## 23. Retirement benefit plans continued

The current service cost that will be recognised in the income statement in 2012 relating to defined benefit plans is estimated to be around £25m lower than in 2011, derived from market conditions at 1 April 2011. The net interest income, within specific items, is estimated to be around £200m in 2012, an improvement of around £280m. Subsequent changes in market conditions during 2012 will be reflected as actuarial gains or losses in the Group statement of comprehensive income.

£6m (2010: £6m, 2009: £4m) of contributions to defined contribution plans were outstanding at 31 March 2011.

### Defined benefit plans

#### Balance sheet position in respect of defined benefit plans – IAS 19

The net pension obligation is set out below:

At 31 March	2011			2010		
	Assets £m	Present value of liabilities £m	Deficit £m	Assets £m	Present value of liabilities £m	Deficit £m
BTPS	37,034	(38,715)	(1,681)	35,278	(43,018)	(7,740)
Other plans <sup>a</sup>	188	(337)	(149)	151	(275)	(124)
<b>Retirement benefit obligation</b>	<b>37,222</b>	<b>(39,052)</b>	<b>(1,830)</b>	<b>35,429</b>	<b>(43,293)</b>	<b>(7,864)</b>
Deferred tax asset			460			2,193
<b>Net pension obligation</b>			<b>(1,370)</b>			<b>(5,671)</b>

<sup>a</sup> Included in the present value of liabilities of other schemes is £70m (2010: £54m) related to unfunded pension arrangements.

#### Measurement of scheme assets – IAS 19

Scheme assets are measured at the bid market value at the balance sheet date.

The fair values of the assets of the BTPS analysed by asset category and the assumptions for the expected long-term rate of return on assets at 31 March were:

At 31 March	2011				2010			
	Expected long-term rate of return (per annum) %	Asset fair value <sup>b</sup> £bn	%	Target %	Expected long-term rate of return (per annum) %	Asset fair value <sup>b</sup> £bn	%	Target %
UK equities	7.9	3.2	8	9	8.5	3.6	10	11
Non UK equities	7.9	8.2	22	22	8.5	7.5	21	22
Fixed-interest securities	5.0	4.4	12	22	5.0	5.9	17	20
Index-linked securities	4.1	5.9	16	15	4.2	5.8	16	15
Property	7.0	3.9	11	11	7.7	3.8	11	12
Alternative assets <sup>a</sup>	6.7	7.3	20	21	6.9	5.9	17	20
Cash and other	3.6	4.1	11	–	4.2	2.8	8	–
	<b>6.35</b>	<b>37.0</b>	<b>100</b>	<b>100</b>	<b>6.50</b>	<b>35.3</b>	<b>100</b>	<b>100</b>

<sup>a</sup> Alternative asset classes include commodities, hedge funds, private equity, infrastructure and credit opportunities.

<sup>b</sup> At 31 March 2011 and 31 March 2010, the scheme's assets did not include any ordinary shares of the company. However, the scheme held £10m (2010: £52m) of bonds and £7m (2010: £6m) of index-linked bonds issued by the group. The group occupies two (2010: four) properties owned by the BTPS on which an annual rental of £0.1m is payable (2010: £0.2m).

#### Expected long-term return on assets – IAS 19

The expected long-term rate of return on assets does not affect the level of the obligation but does affect the expected return on pension scheme assets reported in the income statement as a specific item.

The expected returns on fixed-interest and index-linked securities are based on the gross redemption yields at the start of the year which assume that the security is held to maturity. Expected returns on equities, property and alternative asset classes are based on a combination of an estimate of the risk premium above yields on government bonds, consensus economic forecasts of future returns and historical returns.

## 23. Retirement benefit plans continued

### Asset allocation

The target allocation of assets between different classes of investment is reviewed regularly and is a key factor in the Trustee's investment policy. The Trustee's main investment objective is to ensure that over the long-term, and after allowing for all future income, the BTPS will have sufficient liquid resources to meet the cost of benefit payments as they fall due. The targets set reflect the Trustee's views on the appropriate balance to be struck between seeking returns and incurring risk, and on the extent to which the assets should be distributed to match liabilities. The targets are a long-term aim to be achieved over a period as and when favourable opportunities arise. Current market conditions and trends are continuously assessed and short-term tactical shifts in asset allocation may be made around the long-term target, for example, by using stock index future contracts. The BTPS also uses financial instruments to manage interest rate risk, liquidity risk and foreign currency risk.

The Trustee reports on investment performance against a target benchmark which is based on the target asset mix and the market returns for each asset class. BTPS performance against the benchmark for the periods to 31 December 2010 was as follows:

Period ending 31 December 2010	Target benchmark return %	Actual BTPS return %	Over/(under) performance return %
1 year	10.7	11.8	1.1
3 years	(0.2)	1.1	1.3
10 years	4.1	5.1	1.0

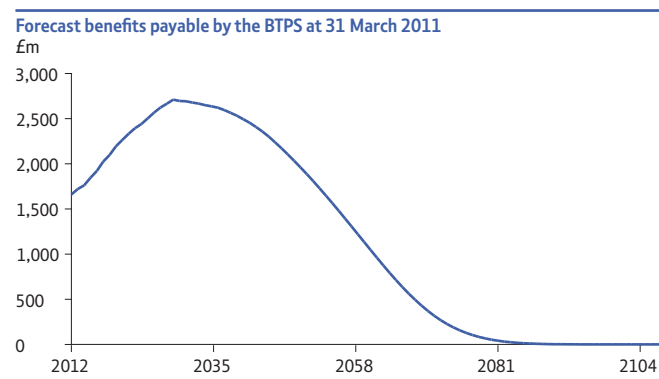
Further commentary on investment performance is provided in the Report by the Trustee in the BTPS Annual Report.

### Measurement of scheme liabilities – IAS 19

The liabilities of the BTPS are measured as the present value of the best estimate of future cash flows to be paid out by the scheme using the projected unit credit method. The present value of scheme liabilities is calculated by estimating future benefit payments, including allowance for benefits to increase with inflation and projected salary levels, and discounting the resulting cash flows.

### Principal assumptions used to measure BTPS liabilities

The estimated average duration of BTPS liabilities is 15 years (2010: 15 years) and the benefits payable by the BTPS are expected to be paid over more than 60 years as shown in the following graph:



The expected future benefit payments are based on a number of assumptions including future inflation, retirement ages, benefit options chosen and life expectancy and are therefore inherently uncertain. Sensitivities are set out below. Actual benefit payments in a given year may be higher or lower, for example if members retire sooner or later than assumed, or take more or less cash lump sum at retirement.

The rate of inflation influences the assumptions for salary and pension increases. In assessing the appropriate assumption for pension increases, management have considered the announcement in July 2010 by the UK Government that the Consumer Prices Index (CPI), rather than the Retail Prices Index (RPI), will be used as the basis for determining the rate of inflation for the statutory minimum rate of revaluation and indexation of occupational pension rights. Under the scheme rules the Government's decision has the following impact with effect for increases after 1 April 2011:

- members who commenced employment prior to 1 April 1986 – CPI will be used to revalue preserved pensions of deferred members and for the rate of inflationary increase applied to pensions in payment
- members who commenced employment on or after 1 April 1986 – CPI will be used to revalue preserved pensions of deferred members and RPI will continue to be used for inflationary increases to pensions in payment.

The Government's decision does not affect the accrual of benefits for employees while they are active members of the scheme for whom benefits accrue on a CARE basis that is linked to RPI.

## 23. Retirement benefit plans continued

The assumption for RPI has been assessed by reference to yields on long-term fixed interest and index-linked Government bonds and has regard to Bank of England published inflationary expectations. CPI is assessed at a margin below RPI taking into account long-term trends. The impact of using CPI instead of RPI is to reduce BTPS liabilities at 31 March 2011 by £3.5bn. In determining the most appropriate manner by which to reflect the impact of the change on the scheme liabilities, the directors have had regard to the UITF Abstract 48 "Accounting implications of the replacement of the Retail Prices Index with the Consumer Prices Index for retirement benefits" issued by the Urgent Issues Task Force of the UK Accounting Standards Board in December 2010. The Abstract states that, where the obligation is to pay pensions with increases based on a general measure of inflation rather than a measure linked specifically to RPI, a change in the inflation assumption represents an actuarial gain or loss rather than a cost relating to past service of employees. Accordingly, the gain on re-measurement of the liabilities of the BTPS to reflect CPI as the inflation measure is recorded as an actuarial gain in comprehensive income in 2011.

The key financial assumptions used to measure the liabilities of the BTPS under IAS 19 at 31 March 2011 are as follows:

At 31 March	Nominal rates (per annum)			Real rates (per annum)		
	2011 %	2010 %	2009 %	2011 %	2010 %	2009 %
Rate used to discount liabilities	5.50	5.50	6.85	2.03	1.83	3.84
Inflation – increase in RPI	3.40	3.60	2.90	n/a	n/a	n/a
Inflation – increase in CPI	2.40 <sup>a</sup>	n/a	n/a	n/a	n/a	n/a
Average future increases in wages and salaries	3.40	3.60	2.90	–	–	–

<sup>a</sup> There is a short-term reduction in CPI of 0.5% for one year.

IAS 19 requires that the discount rate used be determined by reference to market yields at the reporting date on high quality corporate bonds. The currency and term of these should be consistent with the currency and estimated term of the pension obligations. The discount rate has been assessed by reference to the duration of the BTPS's liabilities and by reference to the published iBoxx index of Sterling corporate bonds of duration greater than 15 years and investment grade AA and above. Allowance is made where the constituent bonds in the published index have been re-rated or new issues made. The nominal rate is used to discount the future expected benefit payments. The real rate is shown as a comparator to inflation.

The average life expectancy assumptions, after retirement at 60 years of age, are as follows:

At 31 March	2011	2010
	Number of years	Number of years
Male in lower pay bracket	25.3	25.2
Male in higher pay bracket	27.6	27.4
Female	28.2	28.1
Average improvement for a member retiring at age 60 in 10 years time	1.1	1.1

The assumptions about life expectancy have regard to information published by the UK actuarial profession's Continuous Mortality Investigation Bureau. However, due to the size of the membership of the BTPS it is considered appropriate for the life expectancy assumptions adopted to take into account the actual membership experience. Allowance is also made for future improvements in mortality. The BTPS actuary undertakes formal reviews of the membership experience every three years. The IAS 19 life expectancy assumptions reflect the 2008 triennial funding valuation basis.

### Sensitivity analysis of the principal assumptions used to measure BTPS liabilities

The assumed discount rate, inflation, salary increases and life expectancy all have a significant effect on the measurement of scheme liabilities. The following table shows the sensitivity of the valuation of the pension liability, and of the estimated income statement charge for 2012, to changes in these assumptions:

	Decrease (increase) in liability £bn	Decrease (increase) in service cost £m	(Decrease) increase in net finance income £m
0.25 percentage point increase to:			
– discount rate	1.4	15	–
– inflation rate (RPI)	(0.5)	(15)	45
– salary increases	(0.2)	(5)	(15)
Additional one year increase to life expectancy	(1.0)	(5)	(55)
0.1 percentage point increase in expected return on assets	–	–	35

## 23. Retirement benefit plans continued

### Movements in defined benefit plan assets and liabilities

	Assets £m	Liabilities £m	Deficit £m
At 1 April 2009	29,353	(33,326)	(3,973)
Current service cost	–	(206)	(206)
Expected return on pension plan assets <sup>a</sup> (interest expense on pension plan liabilities)	1,932	(2,211)	(279)
Actuarial gain (loss) <sup>a</sup>	5,157	(9,481)	(4,324)
Regular contributions by employer	391	–	391
Deficiency contributions by employer	525	–	525
Contributions by employees	15	(15)	–
Benefits paid	(1,948)	1,948	–
Exchange differences	4	(2)	2
<b>At 1 April 2010</b>	<b>35,429</b>	<b>(43,293)</b>	<b>(7,864)</b>
Current service cost	–	(297)	(297)
Expected return on pension plan assets <sup>a</sup> (interest expense on pension plan liabilities)	2,244	(2,323)	(79)
Actuarial gain <sup>a</sup>	234	4,875	5,109
Regular contributions by employer	283	–	283
Deficiency contributions by employer	1,030	–	1,030
Contributions by employees	15	(15)	–
Benefits paid	(2,011)	2,014	3
Other movements	–	(15)	(15)
Exchange differences	(2)	2	–
<b>At 31 March 2011</b>	<b>37,222</b>	<b>(39,052)</b>	<b>(1,830)</b>

<sup>a</sup> Actual return on plan assets in the year was £2,478m (2010: £7,089m).

### Amounts recognised in the statement of comprehensive income for actuarial gains or losses arising on defined benefit plans

Year ended 31 March	2011 £m	2010 £m	2009 £m
Actuarial (losses) gains at 1 April	(4,915)	(591)	6,446
Actuarial gains (losses) for the year:			
– arising on plan liabilities	4,875	(9,481)	2,414
– arising on plan assets	234	5,157	(9,451)
Net actuarial gains (losses) recognised for the year in other comprehensive income	5,109	(4,324)	(7,037)
<b>Actuarial gains (losses) at 31 March</b>	<b>194</b>	<b>(4,915)</b>	<b>(591)</b>

### History of experience gains and losses

At 31 March	2011 £m	2010 £m	2009 £m	2008 £m	2007 £m
Present value of defined benefit liabilities	(39,052)	(43,293)	(33,326)	(34,669)	(38,779)
Fair value of plan assets	37,222	35,429	29,353	37,448	38,390
<b>Net pension (obligation) asset</b>	<b>(1,830)</b>	<b>(7,864)</b>	<b>(3,973)</b>	<b>2,779</b>	<b>(389)</b>
Actuarial gain (loss) arising from assumptions used to value defined benefit liabilities	4,617	(11,113)	2,652	5,215	226
Actuarial gain (loss) arising from experience adjustments on defined benefit liabilities	258	1,632	(238)	(22)	190
<b>Total actuarial gain (loss) arising on defined benefit liabilities</b>	<b>4,875</b>	<b>(9,481)</b>	<b>2,414</b>	<b>5,193</b>	<b>416</b>
Total actuarial gain or loss arising on defined benefit liabilities as a percentage of the present value of defined benefit liabilities	12.5%	21.8%	7.2%	15.0%	1.1%
Actuarial gain (loss) arising from experience adjustment on plan assets	234	5,157	(9,451)	(2,572)	993
Actuarial gain or loss arising from experience adjustment on plan assets as a percentage of the plan assets	0.6%	14.6%	32.2%	6.9%	2.6%

Actuarial gain (loss) arising from assumptions used to value defined benefit liabilities represents the impact on the liabilities of changes to the assumptions used at the year end compared to the assumptions used at the prior year end. This includes both financial assumptions, which are based on market conditions at the year end, and non-financial assumptions such as life expectancy.

## 23. Retirement benefit plans continued

Actuarial gain (loss) arising from experience adjustments on defined benefit liabilities represents the impact on the liabilities of differences between actual experience during the year compared to the assumptions made. Such differences might arise, for example, from actual salary increases being different from those assumed, or members choosing different benefit options at retirement.

Actuarial gain (loss) arising from experience adjustment on plan assets represents the difference between the actual investment performance in the year and expected rate of return on assets assumed at the start of the year.

### BTPS funding valuation and future funding obligations

A triennial valuation is carried out for the independent Trustee by a professionally qualified independent actuary, using the projected unit credit method. The purpose of the valuation is to design a funding plan to ensure that the scheme has sufficient funds available to meet future benefit payments. The funding valuation is based on prudent assumptions and is performed at 31 December as this is the financial year end of the scheme.

The valuation basis for funding purposes is broadly as follows:

- assets are valued at market value at the valuation date; and
- liabilities are measured using a projected unit credit method and discounted to their present value.

The last two triennial valuations were determined using the following long-term assumptions:

	Nominal rates (per annum)		Real rates (per annum)	
	2008 valuation %	2005 valuation %	2008 valuation %	2005 valuation %
Discount rate				
Pre retirement liabilities	6.76	5.84	3.65	3.06
Post retirement liabilities	5.21	4.54	2.15	1.79
Average long-term increase in retail price index	3.00	2.70	–	–
Average future increases in wages and salaries	3.00	3.47	–	0.75
Average increase in pensions	3.00	2.70	–	–

The results of the two most recent triennial valuations based upon these prudent actuarial assumptions were:

	2008 valuation £bn	2005 valuation £bn
At 31 December		
BTPS liabilities	(40.2)	(37.8)
Market value of BTPS assets	31.2	34.4
Funding deficit	(9.0)	(3.4)
Percentage of accrued benefits covered by BTPS assets at valuation date	77.6%	90.9%
Percentage of members benefits that the BTPS assets could purchase from an insurance company at the valuation date	57.0%	70.0%

In the three years ended 31 December 2008, the decline in the market value of assets combined with longer life expectancy assumptions significantly increased the funding deficit, although the impact on the liabilities was reduced by the higher discount rate and favourable experience compared to other actuarial assumptions used at 31 December 2005.

The outcome of the 2008 valuation was announced in February 2010, together with the agreement between BT and the Trustee of the BTPS to a recovery plan to make good the £9.0bn funding deficit over 17 years. The agreement also determined that the ordinary contributions rate required to meet the benefits of current employed members for service after the valuation date reduce to 13.6% of pensionable salaries (including employee contributions) from 19.5%, reflecting the implementation of benefit changes with effect from 1 April 2009.

The group made the first two payments of £525m each in December 2009 and 2010, respectively, under the 17-year recovery plan and in March 2011 paid £505m representing the actuarial value of the £525m payment due to have been made in December 2011. The remaining payments are scheduled to be paid as follows:

Year ended 31 December	£m
2011	–
2012	583
2013–25	Increasing at 3% pa

### 23. Retirement benefit plans continued

Under the terms of the Trust Deed that governs the BTPS, the group is required to have a funding plan that should address the deficit over a maximum period of 20 years.

Other features of the February 2010 legal agreements with the Trustee for BT providing support to the scheme are:

- in the event that cumulative shareholder distributions exceed cumulative total pension contributions over the three-year period to 31 December 2011, then BT will make additional matching contributions to the scheme.
- in the event that BT generates net cash proceeds greater than £1bn from disposals and acquisitions in any 12-month period to 31 December 2011 then BT will make additional contributions to the scheme equal to one third of those net cash proceeds.
- a negative pledge that provides comfort to the scheme that future creditors will not be granted superior security to the scheme in excess of a £1.5bn threshold.

Since the valuation date the scheme's assets have increased by £5.8bn and the Trustee's initial estimate is that if the funding valuation was performed using the same methodology at 31 December 2010 the deficit would have been around £3.2bn on this prudent valuation basis, after allowing for the £0.5bn deficit payment made in March 2011.

The Pensions Regulator's review of the 2008 BTPS funding valuation and recovery plan is now on hold and not expected to recommence until the outcome of the final Court decision, including any potential appeals, is known on the Crown Guarantee. We do not expect this to be before the completion of the next triennial funding valuation as at 31 December 2011. As is usual, BT and the Trustee will engage with the Pensions Regulator regarding the 2011 valuation.

#### Payments made to the BTPS

Year ended 31 March	2011 £m	2010 £m
Ordinary contributions	266	384
Deficit contributions	1,030	525
<b>Total contributions in the year</b>	<b>1,296</b>	<b>909</b>

The group expects to contribute approximately £135m to the BTPS in 2012, being ordinary contributions only, as the deficit payment due in December 2011 was paid early in March 2011. The expected payments are reduced by £110m to recover overpayments of ordinary contributions paid in 2010 before the reduced rate of regular contributions was announced in February 2010.

#### Other protection of BTPS member benefits

If the group were to become insolvent there are additional protections available to members:

- the Crown Guarantee which was granted when the group was privatised in 1984 and applies upon the winding up of the group. The scope and extent of the Crown Guarantee is being clarified by the Trustee through the courts. The decision of the High Court issued in October 2010 was that the Crown Guarantee is not limited to those who were members of the scheme at the date of privatisation and that members who joined after privatisation are also capable of being covered. The Court confirmed that any payments to be made by the Government must be measured on an annuity basis. It was decided that the Crown Guarantee does not cover the benefits of members accrued while in service with companies that participate in the BTPS other than BT if the member concerned had not previously been employed by BT. The judgment was the first stage in the case and leaves further issues to be considered at future hearings and/or appeals. Until these issues are finally resolved it is not possible to say with complete precision what the scope of the Crown Guarantee is.
- the Pension Protection Fund (PPF) may take over the scheme and pay benefits to members not covered by the Crown Guarantee. There are limits on the amounts paid by the PPF and this would not give exactly the same benefits as those provided by the scheme.

## 24. Deferred taxation

	Excess capital allowances £m	Retirement benefit obligations <sup>a</sup> £m	Share-based payments £m	Other £m	Total £m
At 1 April 2009	1,811	(1,103)	(7)	(76)	625
(Credit) expense recognised in the income statement	(115)	118	(15)	2	(10)
(Credit) recognised in other comprehensive income	–	(1,211)	–	(143)	(1,354)
(Credit) expense recognised in equity	–	–	(19)	–	(19)
Transfer from current tax	–	–	–	18	18
<b>At 31 March 2010</b>	<b>1,696</b>	<b>(2,196)</b>	<b>(41)</b>	<b>(199)</b>	<b>(740)</b>
Deferred tax asset	–	(2,196)	–	–	(2,196)
Deferred tax liability	1,696	–	(41)	(199)	1,456
<b>At 1 April 2010</b>	<b>1,696</b>	<b>(2,196)</b>	<b>(41)</b>	<b>(199)</b>	<b>(740)</b>
(Credit) expense recognised in the income statement	(315)	201	(17)	111	(20)
Expense recognised in other comprehensive income	–	1,534	–	12	1,546
(Credit) recognised in equity	–	–	(91)	–	(91)
Transfer from current tax	56	–	–	–	56
<b>At 31 March 2011</b>	<b>1,437</b>	<b>(461)</b>	<b>(149)</b>	<b>(76)</b>	<b>751</b>
Deferred tax asset	–	(461)	–	–	(461)
Deferred tax liability	1,437	–	(149)	(76)	1,212
<b>At 31 March 2011</b>	<b>1,437</b>	<b>(461)</b>	<b>(149)</b>	<b>(76)</b>	<b>751</b>

<sup>a</sup> Includes a deferred tax asset of £1m (2010: £3m) arising on contributions payable to defined contribution schemes.

At 31 March 2011, all of the deferred tax asset of £461m (2010: £2,196m) is expected to be recovered after more than one year. At 31 March 2011, all of the deferred tax liability of £1,212m (2010: £1,456m) is expected to be settled after more than one year.

The rate of UK corporation tax changed from 28% to 26% on 1 April 2011. As deferred tax assets and liabilities are measured at the rates that are expected to apply in the periods of the reversal, deferred tax balances at 31 March 2011 have been calculated using a rate of 26%. The impact of the change of rate decreased deferred tax assets by £35m and deferred tax liabilities by £91m totalling a reduction in net liabilities of £56m. This reduction has been recognised as a deferred tax credit of £172m in the income statement (note 10) and a deferred tax expense of £116m in other comprehensive income.

The UK Government has also indicated that it intends to enact future reductions in the main rate of UK corporation tax to 23% by 1 April 2014. The future annual corporation tax reductions of 1% are expected to affect the group's financial statements. The actual impact will depend on the group's deferred tax position at that time.

At 31 March 2011 the group had operating losses, capital losses and other temporary differences carried forward in respect of which no deferred tax assets were recognised amounting to £23.5bn (2010: £29.5bn). The group's capital losses and other temporary differences have no expiry date restrictions. The expiry date of operating losses carried forward is dependent upon the tax law of the various territories in which the losses arose. A summary of expiry dates for losses in respect of which restrictions apply is set out below:

At 31 March	2011 £m	Expiry of losses
<b>Restricted losses:</b>		
Americas	254	2012-31
Europe	1,492	2012-26
Asia	14	2012-16
<b>Total restricted losses</b>	<b>1,760</b>	
<b>Unrestricted losses:</b>		
Operating losses	3,440	No expiry
Capital losses	17,771	No expiry
<b>Total unrestricted losses</b>	<b>21,211</b>	
Other temporary differences	536	
<b>Total</b>	<b>23,507</b>	

At 31 March 2011, the undistributed earnings of overseas subsidiaries was £5.3bn (2010: £5.5bn). No deferred tax liabilities have been recognised in respect of these unremitted earnings because the group is in a position to control the timing of the reversal of the temporary differences and it is probable that such differences will not reverse in the foreseeable future. Temporary differences arising in connection with interests in associates and joint ventures for which deferred tax liabilities have not been recognised are insignificant.

## 25. Provisions

	BT Global Services restructuring <sup>a</sup> £m	Property <sup>b</sup> £m	Other <sup>c</sup> £m	Total £m
At 1 April 2009	303	172	245	720
Income statement expense <sup>d</sup>	10	131	204	345
Unwind of discount	–	4	–	4
Utilised or released	(139)	(35)	(98)	(272)
Transfers	16	–	31	47
Exchange differences	(3)	–	–	(3)
<b>At 1 April 2010</b>	<b>187</b>	<b>272</b>	<b>382</b>	<b>841</b>
Income statement expense <sup>d</sup>	76	131	190	397
Unwind of discount	–	3	–	3
Utilised or released	(103)	(88)	(76)	(267)
Transfers	–	–	(15)	(15)
Exchange differences	(1)	–	(2)	(3)
<b>At 31 March 2011</b>	<b>159</b>	<b>318</b>	<b>479</b>	<b>956</b>
At 31 March			2011 £m	2010 £m
Analysed as:				
Current			149	134
Non-current			807	707
			<b>956</b>	<b>841</b>

<sup>a</sup> Amounts provided in relation to the BT Global Services restructuring programme and the contract and financial reviews in 2009. These are being utilised as the obligations are settled.

<sup>b</sup> Property provisions mainly comprise onerous lease provisions arising from the rationalisation of the group's property portfolio. The provisions will be utilised over the remaining lease periods, which range from one to 21 years. Financial liabilities comprise £280m (2010: £255m) of this balance.

<sup>c</sup> Other provisions include amounts provided for legal or constructive obligations arising from insurance claims, litigation and regulatory risk, which will be utilised as the obligations are settled.

<sup>d</sup> Includes specific items of £88m (2010: £121m) for property rationalisation costs and £24m (2010: £10m) relating to the BT Global Services restructuring programme.

## 26. Non-controlling interests

	2011 £m	2010 £m
At 1 April	24	27
Share of profits	2	1
Disposals	–	(4)
<b>At 31 March</b>	<b>26</b>	<b>24</b>

## 27. Share capital

	Number of shares	Share capital <sup>a</sup> £m	Share premium <sup>b</sup> £m
At 1 April 2010 and 31 March 2011	<b>8,151,227,029</b>	<b>408</b>	<b>62</b>

<sup>a</sup> The allotted, called up and fully paid ordinary share capital of the company at 31 March 2011 and 31 March 2010 was £408m, representing 8,151,227,029 ordinary shares of 5p each.

<sup>b</sup> The share premium account, representing the premium on allotment of shares, is not available for distribution.

## 28. Other reserves

	Treasury shares <sup>a</sup> £m	Merger reserve <sup>b</sup> £m	Other comprehensive income			Total other reserves £m
			Cash flow reserve <sup>c</sup> £m	Available-for-sale reserve <sup>d</sup> £m	Translation reserve <sup>e</sup> £m	
<b>At 1 April 2008</b>	<b>(1,843)</b>	<b>998</b>	<b>157</b>	<b>–</b>	<b>161</b>	<b>(527)</b>
Exchange differences	–	–	–	–	683	683
Net fair value gain on cash flow hedges	–	–	2,719	–	–	2,719
Recognised in income and expense	–	–	(2,144)	–	–	(2,144)
Reclassified and reported in non-current assets	–	–	(5)	–	–	(5)
Fair value movements on available-for-sale assets	–	–	–	5	–	5
Tax recognised in other comprehensive income	–	–	(164)	–	–	(164)
Net purchase of treasury shares	(63)	–	–	–	–	(63)
Cancellation of treasury shares	797	–	–	–	–	797
<b>At 1 April 2009</b>	<b>(1,109)</b>	<b>998</b>	<b>563</b>	<b>5</b>	<b>844</b>	<b>1,301</b>
Exchange differences	–	–	–	–	(119)	(119)
Net fair value loss on cash flow hedges	–	–	(1,067)	–	–	(1,067)
Recognised in income and expense	–	–	496	–	–	496
Reclassified and reported in non-current assets	–	–	(4)	–	–	(4)
Fair value movements on available-for-sale assets	–	–	–	7	–	7
Tax recognised in other comprehensive income	–	–	159	–	(20)	139
Net issue of treasury shares	4	–	–	–	–	4
<b>At 1 April 2010</b>	<b>(1,105)</b>	<b>998</b>	<b>147</b>	<b>12</b>	<b>705</b>	<b>757</b>
Exchange differences	–	–	–	–	(140)	(140)
Net fair value loss on cash flow hedges	–	–	(347)	–	–	(347)
Recognised in income and expense	–	–	333	–	–	333
Fair value movements on available-for-sale assets	–	–	–	15	–	15
Tax recognised in other comprehensive income	–	–	(5)	–	18	13
Net issue of treasury shares	27	–	–	–	–	27
<b>At 31 March 2011</b>	<b>(1,078)</b>	<b>998</b>	<b>128</b>	<b>27</b>	<b>583</b>	<b>658</b>

<sup>a</sup> The treasury shares reserve is used to hold BT Group plc shares purchased by the group. During 2011 the company purchased nil (2010: nil, 2009: 142,608,225) of its own shares of 5p each, representing nil% (2010: nil%, 2009: 2%) of the called-up share capital, for consideration (including transaction costs) of £nil (2010: £nil, 2009: £189m). In addition, 12,335,580 shares (2010: 8,320,766, 2009: 90,626,518) were issued from treasury to satisfy obligations under employee share schemes and executive share awards at a cost of £27m (2010: £4m, 2009: £126m), and nil treasury shares (2010 nil, 2009: 250,000,000) were cancelled at a cost of £nil (2010: £nil, 2009: £797m). At 31 March 2011, 388,570,539 shares (2010: 400,906,119, 2009: 409,226,885) with an aggregate nominal value of £19m (2010: £20m, 2009: £20m) were held as treasury shares at cost.

<sup>b</sup> The merger reserve arose on the group reorganisation that occurred in November 2001 and represented the difference between the nominal value of shares in the new parent company, BT Group plc, and the aggregate of the share capital, share premium account and capital redemption reserve of the prior parent company, British Telecommunications plc.

<sup>c</sup> The cash flow reserve is used to record the effective portion of the cumulative net change in the fair value of cash flow hedging instruments related to hedged transactions that have not yet occurred.

<sup>d</sup> The available-for-sale reserve is used to record the cumulative fair value gains and losses on available-for-sale financial assets. The cumulative gains and losses are recycled to the income statement on disposal of the assets.

<sup>e</sup> The translation reserve is used to record cumulative translation differences on the assets and liabilities of foreign operations. The cumulative translation differences are recycled to the income statement on disposal of the foreign operation.

## 29. Financial instruments and risk management

The group issues or holds financial instruments mainly to finance its operations; to finance corporate transactions such as dividends, share buy backs and acquisitions; for the temporary investment of short-term funds; and to manage the currency and interest rate risks arising from its operations and from its sources of finance. In addition, various financial instruments, for example trade receivables and trade payables, arise directly from the group's operations.

### Financial instruments by category

The accounting classification of each class of the group's financial assets and liabilities is set out in the tables below.

Financial assets		Loans and receivables	Fair value through profit and loss	Derivatives used for hedging	Available-for-sale	Total
At 31 March 2011	Notes	£m	£m	£m	£m	£m
Investments	15	7	11	–	62	80
Derivative financial instruments	21	–	103	630	–	733
Trade and other receivables <sup>a</sup>	19	2,558	–	–	–	2,558
Cash and cash equivalents	16	351	–	–	–	351
<b>Total financial assets</b>		<b>2,916</b>	<b>114</b>	<b>630</b>	<b>62</b>	<b>3,722</b>

		Loans and receivables	Fair value through profit and loss	Derivatives used for hedging	Available-for-sale	Total
At 31 March 2010	Notes	£m	£m	£m	£m	£m
Investments	15	180	–	–	290	470
Derivative financial instruments	21	–	106	1,594	–	1,700
Trade and other receivables <sup>a</sup>	19	2,947	–	–	–	2,947
Cash and cash equivalents	16	1,452	–	–	–	1,452
<b>Total financial assets</b>		<b>4,579</b>	<b>106</b>	<b>1,594</b>	<b>290</b>	<b>6,569</b>

Financial liabilities		Notes	Fair value through profit and loss	Derivatives used for hedging	Amortised cost	Total
At 31 March 2011			£m	£m	£m	£m
Loans and other borrowings	20	–	–	–	9,856	9,856
Derivative financial instruments	21	267	302	–	–	569
Trade and other payables <sup>b</sup>	22	–	–	–	4,285	4,285
Provisions <sup>c</sup>	25	–	–	–	280	280
<b>Total financial liabilities</b>			<b>267</b>	<b>302</b>	<b>14,421</b>	<b>14,990</b>

		Notes	Fair value through profit and loss	Derivatives used for hedging	Amortised cost	Total
At 31 March 2010			£m	£m	£m	£m
Loans and other borrowings	20	–	–	–	12,791	12,791
Derivative financial instruments	21	298	401	–	–	699
Trade and other payables <sup>b</sup>	22	–	–	–	4,672	4,672
Provisions <sup>c</sup>	25	–	–	–	255	255
<b>Total financial liabilities</b>			<b>298</b>	<b>401</b>	<b>17,718</b>	<b>18,417</b>

<sup>a</sup> Excludes prepayments of £570m (2010: £549m), other receivables £204m (2010: £200m) and other non-current assets of £286m (2010: £336m).

<sup>b</sup> Excludes other taxation and social security of £485m (2010: £516m), deferred income £1,344m (2010: £1,343m) and other non-current payables of £831m (2010: £804m).

<sup>c</sup> Excludes provisions of £676m (2010: £586m).

## 29. Financial instruments and risk management continued

### Financial risk management

The group's activities exposes it to a variety of financial risks: market risk (including interest rate risk and foreign exchange risk); credit risk and liquidity risk.

#### Funding and exposure management

The group finances its operations primarily by a mixture of issued share capital, retained profits and long-term and short-term borrowing. The group borrows in the major long-term bond markets in major currencies and typically, but not exclusively, these markets provide the most cost effective means of long-term borrowing. The group uses derivative financial instruments primarily to manage its exposure to changes in interest and foreign exchange rates against these borrowings. The derivatives used for this purpose are principally interest rate swaps, cross currency swaps and forward currency contracts. The group also uses forward currency contracts to hedge some of its currency exposures arising from funding its overseas operations, acquisitions, overseas assets, liabilities and forward purchase commitments. The group does not hold or issue derivative financial instruments for trading purposes. All transactions in derivative financial instruments are undertaken to manage the risks arising from underlying business activities.

#### Treasury operations

The group has a centralised treasury operation whose primary role is to manage liquidity, funding, investments and counterparty credit risk arising from transactions with financial institutions. The treasury operation also manages the group's market exposures, including risks from volatility in currency and interest rates. The treasury operation acts as a central bank to group entities providing central deposit taking, funding and foreign exchange management services. Funding and deposit taking is usually provided in the functional currency of the relevant entity. The treasury operation is not a profit centre and its objective is to manage financial risk at optimum cost.

#### Treasury policy

The Board sets the policy for the group's treasury operation. Group treasury activities are subject to a set of controls commensurate with the magnitude of the borrowing, investments and group-wide exposures. The Board has delegated its authority to operate these policies to a series of panels that are responsible for the management of key treasury risks and operations. Appointment to and removal from the key panels requires approval from two of the Chairman, the Chief Executive or the Group Finance Director.

The financial risk management of exposures arising from trading related financial instruments, primarily trade receivables and trade payables, is through a series of policies and procedures set at a group and line of business level. Line of business management apply these policies and procedures and perform review processes to assess and manage financial risk exposures arising from these financial instruments.

There has been no change in the nature of the group's risk profile between 31 March 2011 and the date of approval of these financial statements.

### Interest rate risk management

#### Management policy

The group has interest bearing financial assets and liabilities which may expose the group to either cash flow or fair value volatility. The group's policy, as prescribed by the Board, is to ensure that at least 70% of net debt is at fixed rates. Short-term interest rate management is delegated to the treasury operation while long-term interest rate management decisions require further approval from the Group Finance Director, Director Treasury, Tax and Risk Management or the Treasurer who have been delegated such authority from the Board.

#### Hedging strategy

In order to manage the group's interest rate mix profile, the group has entered into cross currency and interest rate swap agreements with commercial banks and other institutions to vary the amounts and periods for which interest rates on borrowings are fixed. The duration of the swap agreements matches the duration of the debt instruments. The majority of the group's long-term borrowings have been, and are, subject to fixed Sterling interest rates after applying the impact of these hedging instruments. Outstanding cross currency and interest rate swaps at 31 March 2011 are detailed in the Hedging activities and Other derivatives section below.

The group's fixed to floating interest rate profile, after hedging, on gross borrowings was:

	2011			2010		
	Fixed rate interest £m	Floating rate interest £m	Total £m	Fixed rate interest £m	Floating rate interest £m	Total £m
At 31 March						
Total borrowings <sup>a</sup>	7,972	1,215	9,187	10,110	1,029	11,139
Ratio of fixed to floating	87%	13%	100%	91%	9%	100%

<sup>a</sup> See note 20.

## 29. Financial instruments and risk management continued

### Sensitivities

#### Interest rates

The group is exposed to volatility in the income statement and shareholders' equity arising from changes in interest rates. To demonstrate this volatility, management have concluded that a 100 basis point increase in interest rates and parallel shift in yield curves across Sterling, US Dollar and Euro currencies is a reasonable benchmark for performing a sensitivity analysis.

After the impact of hedging, the group's main exposure to interest rate volatility in the income statement arises from fair value movements on derivatives, that are not in hedging relationships and on variable rate borrowing, investments and cash equivalents which are largely influenced by Sterling interest rates. With all other factors remaining constant and based on the composition of net debt at 31 March 2011, a 100 basis point increase in Sterling interest rates would increase the group's annual net finance expense by approximately £2m.

The group's main exposure to interest rate volatility within shareholders' equity arises from fair value movements on derivatives held in the cash flow reserve. The derivatives have an underlying interest exposure to Sterling, Euro and US Dollar rates. With all other factors remaining constant and based on the composition of derivatives included in the cash flow reserve at the balance sheet date, a 100 basis point increase in interest rates in each of the currencies would impact equity, before tax, as detailed below:

At 31 March	2011 £m Reduce (Increase)	2010 £m Reduce (Increase)
Sterling interest rates	426	496
US Dollar interest rates	(355)	(392)
Euro interest rates	(94)	(134)

A 100 basis points decrease in interest rates would have broadly the same impact in the opposite direction.

#### Credit ratings

The group's 2030 and 2016 bonds contain a covenant such that if the group's credit rating were downgraded below A3 in the case of Moody's or below A- in the case of Standard & Poor's (S&P), additional interest would accrue from the next coupon period at a rate of 0.25 percentage points for each ratings category adjustment by each agency. Based on the total debt outstanding of £2.4bn at 31 March 2011, the group's finance expense would increase/decrease by approximately £12m a year if BT's credit rating were to be downgraded/upgraded, respectively, by one credit rating category by both agencies from the current ratings.

The group's €600m 2014 bond attracts an additional 1.25 percentage points for a downgrade by one credit rating by either or both Moody's and S&P below Baa3/BBB-, respectively. This would result in an additional finance expense of approximately £7m a year.

As at 31 March the group's credit ratings were as detailed below:

At 31 March	2011		2010	
Rating agency	Rating	Outlook	Rating	Outlook
Standard & Poor's	BBB-	Positive	BBB-	Stable
Moody's	Baa2	Stable	Baa2	Negative

### Foreign exchange risk management

#### Management policy

The purpose of the group's foreign currency hedging activities is to protect the group from the risk that eventual future net inflows and net outflows will be adversely affected by changes in exchange rates. The Board's policy for foreign exchange risk management defines the type of transactions which should normally be covered, including significant operational, funding and currency interest exposures, and the period over which cover should extend for the different types of transactions. Short-term foreign exchange management is delegated to the treasury operation whilst long-term foreign exchange management decisions require further approach from the Group Finance Director, Director Treasury, Tax and Risk Management or the Treasurer who have been delegated such authority by the Board. The policy delegates authority to the Director Treasury, Tax and Risk Management to take positions of up to £100m and for the Group Finance Director to take positions of up to £1bn.

## 29. Financial instruments and risk management continued

### Hedging strategy

A significant proportion of the group's current revenue is invoiced in Sterling, and a significant element of its operations and costs arise within the UK. The group's overseas operations generally trade and are funded in their functional currency which limits their exposure to foreign exchange volatility. The group's foreign currency borrowing comprised:

At 31 March	2011 £m	2010 £m
Euro	3,361	4,294
US Dollar	2,966	5,065
Other	17	7
	<b>6,344</b>	<b>9,366</b>

These borrowings are used to finance the group's operations and have been predominantly swapped into Sterling using cross currency swaps. The currency profile of these borrowings after the impact of hedging is disclosed in note 20.

The group also enters into forward currency contracts to hedge foreign currency investments, interest expense, capital purchases and purchase and sale commitments on a selective basis. The commitments hedged are principally denominated in US Dollar, Euro and Asia Pacific region currencies. As a result, the group's exposure to foreign currency arises mainly on its non UK subsidiary investments and on residual currency trading flows.

### Sensitivities

After hedging, with all other factors remaining constant and based on the composition of assets and liabilities at the balance sheet date, the group's exposure to foreign exchange volatility in the income statement from a 10% strengthening/weakening in Sterling against other currencies would result in a credit/charge respectively of approximately £5m (2010: approximately £26m).

The group's main exposure to foreign exchange volatility within shareholders' equity (excluding translation exposures) arises from fair value movements on derivatives held in the cash flow reserve. The majority of foreign exchange fluctuations in the cash flow reserve are recycled immediately to the income statement to match the hedged item and therefore the group's exposure to foreign exchange fluctuations in equity were insignificant in both 2011 and 2010.

Outstanding cross currency swaps at 31 March 2011 are detailed in the Hedging activities and Other derivatives sections below.

## Credit risk management

### Treasury management policy

The group's exposure to credit risk arises from financial assets transacted by the treasury operation (primarily derivatives, investments, cash and cash equivalents) and from its trading related receivables. For treasury related balances, the Board's defined policy restricts exposure to any one counterparty by setting credit limits based on the credit quality as defined by Moody's and S&P and by defining the types of financial instruments which may be transacted. The minimum credit ratings permitted with counterparties are A3/A- for long-term and P1/A1 for short-term investments.

The treasury operation continuously reviews the limits applied to counterparties and will adjust the limit according to the nature and credit standing of the counterparty up to the maximum allowable limit set by the Board. Where multiple transactions are undertaken with a single counterparty, or group of related counterparties, the group may enter into netting arrangements to reduce the group's exposure to credit risk by making use of standard International Swaps and Derivative Association (ISDA) documentation. The group also seeks collateral or other security where it is considered necessary. The treasury operation regularly reviews the credit limits applied when investing with counterparties in response to market conditions and continues to monitor their credit quality and actively manages any exposures which arise.

### Exposures

The maximum credit risk exposure of the group's financial assets at the balance sheet date is as follows:

At 31 March	Notes	2011 £m	2010 £m
Derivative financial assets	21	733	1,700
Investments	15	80	470
Trade and other receivables <sup>a</sup>	19	2,558	2,947
Cash and cash equivalents	16	351	1,452
		<b>3,722</b>	<b>6,569</b>

<sup>a</sup> The carrying amount excludes £286m (2010: £336m) of non-current trade and other receivables which relate to non financial assets, and £774m (2010: £749m) of prepayments and other receivables.

## 29. Financial instruments and risk management continued

The credit quality and credit concentration of cash equivalents, current asset investments and derivative financial assets are detailed in the tables below. Where the opinion of Moody's and S&P differ, the lower rating is used.

At 31 March 2011	Moody's/S&P credit rating of counterparty						Total
	Aaa/AAA	Aa2/AA	Aa3/AA-	A1/A+	A2/A	A3/A-	
Cash equivalents	-	18	159	32	1	-	210
Current asset investments	-	-	-	7	12	-	19
Derivative financial assets	-	52	115	378	188	-	733
	-	70	274	417	201	-	962

At 31 March 2010	Moody's/S&P credit rating of counterparty						Total
	Aaa/AAA	Aa2/AA	Aa3/AA-	A1/A+	A2/A	A3/A-	
Cash equivalents	100	609	202	341	3	-	1,255
Current asset investments	258	-	35	105	8	-	406
Derivative financial assets	-	89	480	708	318	105	1,700
	358	698	717	1,154	329	105	3,361

The concentration of credit risk for trading balances of the group is provided in note 19, which analyses outstanding balances by line of business and reflects the nature of customers in each line of business.

The derivative financial assets were held with 14 counterparties at 31 March 2011 (2010: 18 counterparties). After applying the legal right of set-off under the group's ISDA documentation, the group had a net exposure to derivative counterparties of £549m (2010: £1,303m) of which 94% (2010: 85%) was with six counterparties (2010: six).

The group has credit support agreements with certain swap counterparties whereby on a weekly basis the fair value position on nominal £800m of long dated cross currency swaps and interest rate swaps is collateralised. As at 31 March 2011, the group had paid cash collateral of £14m (2010: £nil) in respect of fair value losses and had received cash collateral of £104m (2010: £nil) in respect of fair value gains. The collateral paid and received is recognised within cash and cash equivalents, and loans and other borrowings, respectively.

The majority of the group's derivatives are in designated cash flow hedges. With all other factors remaining constant and based on the composition of net derivative financial assets at 31 March 2011, a 100 basis point shift in yield curves across each of the ratings categories within which these derivative financial assets are classified would change their carrying values and impact equity, before tax, as follows:

At 31 March 2011	Moody's/S&P credit rating	Impact of 100	Impact of 100
		basis point increase	basis point decrease
		£m	£m
	Aa2/AA	(4)	5
	Aa3/AA-	(15)	20
	A1/A+	(75)	88
	A2/A	(101)	120
		(195)	233

### Operational management policy

The group's credit policy for trading related financial assets is applied and managed by each of the lines of business to ensure compliance. The policy requires that the creditworthiness and financial strength of customers is assessed at inception and on an ongoing basis. Payment terms are set in accordance with industry standards. The group will also enhance credit protection, when appropriate, taking into consideration the group's exposure to the customer, by applying processes which include netting and offsetting, and requesting securities such as deposits, guarantees and letters of credit. The group takes proactive steps including constantly reviewing credit ratings of relationship banks to minimise the impact of adverse market conditions on trading related financial assets.

### Capital risk management

The objective of the group's capital management policy is to reduce net debt over time whilst investing in the business, supporting the pension scheme and paying progressive dividends. In order to meet this objective, the group may issue or repay debt, issue new shares, repurchase shares, or adjust the amount of dividends paid to shareholders. The group manages the capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of the group. The Board regularly reviews the capital structure. No changes were made to these objectives and processes during 2011 and 2010.

## 29. Financial instruments and risk management continued

The group's capital structure consists of net debt and shareholders' equity. The following analysis summarises the components which the group manages as capital:

At 31 March	2011 £m	2010 £m
Net debt	8,816	9,283
Total parent shareholders' equity (deficit) <sup>a</sup>	1,925	(2,650)
	<b>10,741</b>	<b>6,633</b>

<sup>a</sup> See page 104.

### Net debt

Net debt consists of loans and other borrowings (both current and non-current), less current asset investments and cash and cash equivalents. Loans and other borrowings are measured at the net proceeds raised, adjusted to amortise any discount over the term of the debt. For the purpose of this measure, current asset investments and cash and cash equivalents are measured at the lower of cost and net realisable value. Currency denominated balances within net debt are translated to Sterling at swapped rates where hedged. Net debt is considered to be an alternative performance measure as it is not defined in IFRS. The most directly comparable IFRS measure is the aggregate of loans and other borrowings (current and non-current), current asset investments and cash and cash equivalents. A reconciliation from this measure, the most directly comparable IFRS measure, to net debt is given below.

At 31 March	2011 £m	2010 £m
Loans and other borrowings	9,856	12,791
Less:		
Cash and cash equivalents	(351)	(1,452)
Current asset investments	(19)	(406)
	<b>9,486</b>	<b>10,933</b>
Adjustments:		
To retranslate currency denominated balances at swapped rates where hedged	(408)	(1,326)
To remove fair value adjustments and accrued interest applied to reflect the effective interest method	(262)	(324)
<b>Net debt</b>	<b>8,816</b>	<b>9,283</b>

## Liquidity risk management

### Management policy

The group ensures its liquidity is maintained by entering into short, medium and long-term financial instruments to support operational and other funding requirements. The group determines its liquidity requirements by the use of both short and long-term cash forecasts. These forecasts are supplemented by a financial headroom analysis which is used to assess funding adequacy for at least a 12-month period. On at least an annual basis the Board reviews and approves the maximum long-term funding of the group and on an ongoing basis considers any related matters. Short and medium-term requirements are regularly reviewed and managed by the treasury operation within the parameters of the policies set by the Board.

During 2011 and 2010 the group issued commercial paper and held cash, cash equivalents and current investments in order to manage short-term liquidity requirements. In March 2011 the group signed a committed borrowing facility of £1.5bn, available for the period to March 2016. The committed facility replaces the £1.5bn January 2013 and £650m May 2012 facilities.

Refinancing risk is managed by limiting the amount of borrowing that matures within any specified period and having appropriate strategies in place to manage refinancing needs as they arise. In December 2010 the group's US Dollar 9.375% bond matured with a principal of \$2.88bn (£1.74bn at swapped rates) and in February 2011 a Euro 7.87% bond matured with a principal of €1.12bn (£0.76bn at swapped rates). Both bond maturities were financed through existing cash equivalents and investments which had been built up in anticipation of these maturities. The maturity profile of the group's term debt at 31 March 2011 is disclosed in note 20. The group has no term debt maturities until the 2013 financial year.

## 29. Financial instruments and risk management continued

### Maturity analysis

The group's remaining contractually agreed cash flows, including interest, associated with non-derivative and derivative financial liabilities on an undiscounted basis, which therefore differs from both the carrying value and fair value, is as follows:

	Due within 1 year £m	Due between 1 and 2 years £m	Due between 2 and 3 years £m	Due between 3 and 4 years £m	Due between 4 and 5 years £m	Due after 5 years £m	Total £m
At 31 March 2011 – Outflow (inflow) <sup>a</sup>							
<b>Non-derivative financial liabilities</b>							
Loans and other borrowings	221	1,747	10	1,209	901	5,507	9,595
Interest payments on loans and other borrowings	639	639	548	548	482	4,358	7,214
Trade and other payables	4,285	–	–	–	–	–	4,285
Provisions	57	38	38	18	16	223	390
<b>Derivative financial liabilities</b> (analysed by earliest payment date) <sup>b</sup>							
Net settled	132	553	234	276	63	(120)	1,138
Gross settled – outflow	919	411	4	4	103	–	1,441
Gross settled – inflow	(882)	(397)	(4)	(4)	(101)	–	(1,388)
	<b>5,371</b>	<b>2,991</b>	<b>830</b>	<b>2,051</b>	<b>1,464</b>	<b>9,968</b>	<b>22,675</b>
<b>Derivative financial liabilities</b> (analysed based on holding instrument to maturity)							
Net settled	62	62	62	62	62	828	1,138
Gross settled – outflow	397	427	20	20	20	557	1,441
Gross settled – inflow	(388)	(413)	(20)	(20)	(20)	(527)	(1,388)
	<b>71</b>	<b>76</b>	<b>62</b>	<b>62</b>	<b>62</b>	<b>858</b>	<b>1,191</b>
At 31 March 2010 – Outflow (inflow) <sup>a</sup>							
<b>Non-derivative financial liabilities</b>							
Loans and other borrowings	2,937	18	1,763	11	1,213	6,523	12,465
Interest payments on loans and other borrowings	833	581	581	484	484	4,016	6,979
Trade and other payables	4,672	–	–	–	–	–	4,672
Provisions	61	37	30	26	45	143	342
<b>Derivative financial liabilities</b> (analysed by earliest payment date) <sup>b</sup>							
Net settled	450	78	185	65	(215)	745	1,308
Gross settled – outflow	1,081	–	–	–	–	–	1,081
Gross settled – inflow	(1,074)	–	–	–	–	–	(1,074)
	<b>8,960</b>	<b>714</b>	<b>2,559</b>	<b>586</b>	<b>1,527</b>	<b>11,427</b>	<b>25,773</b>
<b>Derivative financial liabilities</b> (analysed based on holding instrument to maturity)							
Net settled	193	92	93	92	93	745	1,308
Gross settled – outflow	424	20	20	20	20	577	1,081
Gross settled – inflow	(413)	(21)	(21)	(21)	(21)	(577)	(1,074)
	<b>204</b>	<b>91</b>	<b>92</b>	<b>91</b>	<b>92</b>	<b>745</b>	<b>1,315</b>

<sup>a</sup> Foreign currency related cash flows were translated at closing rates as at the relevant reporting date. Future variable interest rate cash flows were calculated using the most recent rate applied at the relevant balance sheet date.

<sup>b</sup> Certain derivative financial instruments contain break clauses whereby either the group or bank counterparty can terminate the swap on certain dates and the mark to market position is settled in cash.

### Price risk

The group has limited exposure to price risk.

## 29. Financial instruments and risk management continued

### Hedging activities

Our hedging policies use derivative financial instruments to manage financial risk. Derivatives that are held as hedging instruments are formally designated as hedges as defined in IAS 39. Derivatives may qualify as hedges for accounting purposes if they meet the criteria for designation as fair value hedges or cash flow hedges in accordance with IAS 39.

#### Fair value hedges

Fair value hedges principally consist of interest rate and cross-currency swaps that are used to protect against changes in the fair value of fixed-rate, long-term financial instruments due to movements in market interest rates. For qualifying fair value hedges, all changes in the fair value of the derivative and changes in the fair value of the hedged item in relation to the risk being hedged are recognised in the income statement. If the hedge relationship no longer meets the criteria for hedge accounting, the fair value adjustment to the hedged item continues to be reported as part of the basis of the item and is amortised to the income statement as a yield adjustment over the remainder of the life of the hedged item.

#### Cash flow hedges

Exposure arises from the variability in future interest and currency cash flows on assets and liabilities which bear interest at variable rates and/or are in a foreign currency. Interest rate and cross-currency swaps are transacted, and where they qualify, designated as cash flow hedges, to manage this exposure. Fair value changes on derivatives designated as cash flow hedges are initially recognised directly in the cash flow hedge reserve, as gains or losses recognised in equity. Amounts are transferred from equity and recognised in the income statement as the income or expense is recognised on the hedged asset or liability.

Forward foreign currency contracts are used to hedge anticipated and committed future currency cash flows. Where these contracts qualify for hedge accounting they are designated as cash flow hedges. On recognition of the underlying transaction in the financial statements, the associated hedge gains and losses, deferred in equity, are transferred and included with the recognition of the underlying transaction.

The gains and losses on ineffective portions of such derivatives are recognised immediately in the income statement.

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity and is recognised when the forecast transaction is ultimately recognised in the income statement or on the balance sheet. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to the income statement.

The group had outstanding hedging arrangements as at 31 March 2011 as follows:

Hedged item	Hedging instruments	Hedge type	Derivative fair value <sup>b</sup>			Remaining term of hedging instruments	Weighted average interest rate on hedging instruments	Period over which forecast transaction arises
			Notional principal £m	Asset £m	Liability £m			
Euro and US Dollar denominated borrowings <sup>a</sup>	Interest rate swaps	Cash flow	1,014	–	265	20 years	Sterling receivable at 1.0% Sterling payable at 6.0% Euro receivable at 6.1% US Dollar receivable at 6.9% Sterling payable at 3.2%	
	Cross currency swaps	Cash flow	5,451	622	29	2 to 20 years		
Sterling denominated borrowings <sup>a</sup>	Interest rate swaps	Fair value	500	4	2	18 years	Sterling receivable at 5.8% Sterling payable at 2.6%	
Euro and US Dollar step up interest on currency denominated borrowings <sup>a</sup>	Forward currency contracts	Cash flow	245	1	4	3 months	20 years	
Euro and US Dollar commercial paper <sup>a</sup>	Forward currency contracts	Cash flow	70	1	–	1 to 6 months rolling basis		
Currency exposures on overseas purchases principally US Dollar and Asia Pacific currencies	Forward currency contracts	Cash flow	3	–	–	1 month rolling basis	12 months	
Purchase of US Dollar denominated retail devices	Forward currency contracts	Cash flow	213	2	2	1 to 6 months		
<b>Total</b>				<b>630</b>	<b>302</b>			

<sup>a</sup> See note 20.

<sup>b</sup> See note 21.

## 29. Financial instruments and risk management continued

The group had outstanding hedging arrangements as at 31 March 2010 as follows:

Hedged item	Hedging instruments	Hedge type	Derivative fair value <sup>b</sup>			Remaining term of hedging instruments	Weighted average interest rate on hedging instruments	Period over which forecast transaction arises
			Notional principal £m	Asset £m	Liability £m			
Euro and US Dollar denominated borrowings <sup>a</sup>	Interest rate swaps	Cash flow	2,913	–	361	9 months to 21 years	Sterling receivable at 0.8% Sterling payable at 5.9% Euro receivable at 6.1% US Dollar receivable at 7.6% Sterling payable at 6.3%	
	Cross currency swaps	Cash flow	7,612	1,571	30	9 months to 21 years		
Sterling denominated borrowings <sup>a</sup>	Interest rate swaps	Fair value	500	–	6	19 years	Sterling receivable at 5.8% Sterling payable at 2.2%	
Euro and US Dollar step up interest on currency denominated borrowings <sup>a</sup>	Forward currency contracts	Cash flow	247	16	–	3 to 9 months rolling basis		21 years
Currency exposures on overseas purchases principally US Dollar and Asia Pacific currencies	Forward currency contracts	Cash flow	161	–	4	1 month rolling basis		12 months
Purchase of US Dollar denominated retail devices	Forward currency contracts	Cash flow	180	7	–	1 to 9 months		
<b>Total</b>				<b>1,594</b>	<b>401</b>			

<sup>a</sup> See note 20.

<sup>b</sup> See note 21.

### Other derivatives

Our policy is not to use derivatives for trading purposes. However, due to the complex nature of hedge accounting under IAS 39 some derivatives may not qualify for hedge accounting, or are specifically not designated as a hedge where natural offset is more appropriate. Changes in the fair value of any derivative instruments that do not qualify for hedge accounting are recognised immediately in the income statement.

At 31 March 2011 the group held certain foreign currency forward and interest rate swap contracts which were not in hedging relationships in accordance with IAS 39. Foreign currency forward contracts were economically hedging operational purchases and sales. The interest rate swap contracts became ineffective on first time adoption of IFRS. The volatility arising from these swaps is recognised through the income statement but is limited due to a natural offset in their fair value movements.

The table below summarises these derivatives at 31 March 2011 and 2010:

At 31 March 2011	Notional principal £m	Derivative fair value <sup>a</sup>		Remaining term of derivatives	Weighted average %
		Asset £m	Liability £m		
Foreign currency forward contracts	464	4	–	2 months	
Interest rate swaps	1,887	99	267	3 to 20 years	Sterling receivable at 4.3% Sterling payable at 5.9%
<b>Total</b>		<b>103</b>	<b>267</b>		
At 31 March 2010	Notional principal £m	Derivative fair value <sup>a</sup>		Remaining term of derivatives	Weighted average %
Foreign currency forward contracts	189	–	2	1 month	
Interest rate swaps	1,887	106	295	4 to 21 years	Sterling receivable at 4.2% Sterling payable at 5.8%
Cross currency swaps	12	–	1	9 months	US Dollar receivable at 8.1% Sterling payable at 8.7%
<b>Total</b>		<b>106</b>	<b>298</b>		

<sup>a</sup> See note 21.

## 29. Financial instruments and risk management continued

### Fair value of financial instruments

The table below discloses the carrying amounts and fair values of all of the group's financial instruments which are not carried at an amount which approximates to their fair value on the balance sheet at 31 March 2011 and 2010. The carrying amounts are included in the group balance sheet under the indicated headings. The fair values of listed investments were estimated based on quoted market prices for those investments. The carrying amount of the short-term deposits and investments approximated to their fair values due to the short maturity of the investments held. The carrying amount of trade receivables and payables approximated to their fair values due to the short maturity of the amounts receivable and payable. The fair value of the group's bonds, finance leases and other long-term borrowings has been estimated on the basis of quoted market prices for the same or similar issues with the same maturities where they existed, and on calculations of the present value of future cash flows using the appropriate discount rates in effect at the balance sheet dates, where market prices of similar issues did not exist. The fair value of the group's outstanding swaps and foreign exchange contracts were the estimated amounts, calculated using discounted cash flow models taking into account market rates of interest and foreign exchange at the balance sheet date.

At 31 March	Carrying amount		Fair value	
	2011 £m	2010 £m	2011 £m	2010 £m
Financial liabilities				
Listed bonds	9,028	12,157	10,274	13,304
Finance leases	294	304	339	343
Other loans and borrowings	534	330	562	354

The table below shows certain financial assets and financial liabilities that have been measured at fair value, analysed by the level of valuation method. The three levels of valuation methodology used are:

- Level 1 – uses quoted prices in active markets for identical assets or liabilities
- Level 2 – uses inputs for the asset or liability other than quoted prices, that are observable either directly or indirectly
- Level 3 – uses inputs for the asset or liability that are not based on observable market data such as internal models or other valuation methods.

At 31 March 2011	Notes	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets at fair value					
Non-current and current derivative financial assets					
Derivatives designated as accounting hedges		–	630	–	630
Other derivatives		–	103	–	103
<b>Total current and non-current derivative financial assets</b>	21	–	<b>733</b>	–	<b>733</b>
Available-for-sale financial assets					
Non-current and current investments					
Liquid investments		–	1	–	1
Other investments		34	–	27	61
Fair value through profit and loss		11	–	–	11
Total non-current and current investments	15	45	1	27	73
<b>Total financial assets at fair value</b>		<b>45</b>	<b>734</b>	<b>27</b>	<b>806</b>
Financial liabilities at fair value					
Current and non-current derivative financial liabilities					
Derivatives designated as accounting hedges		–	302	–	302
Other derivatives		–	267	–	267
Total current and non-current financial liabilities	21	–	569	–	569
<b>Total financial liabilities at fair value</b>		–	<b>569</b>	–	<b>569</b>

## 29. Financial instruments and risk management continued

At 31 March 2010	Notes	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets at fair value					
Non-current and current derivative financial assets					
Derivatives designated as accounting hedges		–	1,594	–	1,594
Other derivatives		–	106	–	106
<b>Total current and non-current derivative financial assets</b>	<b>21</b>	<b>–</b>	<b>1,700</b>	<b>–</b>	<b>1,700</b>
Available-for-sale financial assets					
Non-current and current investments					
Liquid investments		–	258	–	258
Other investments		20	–	12	32
Fair value through profit and loss		–	–	–	–
Total non-current and current investments	15	20	258	12	290
<b>Total financial assets at fair value</b>		<b>20</b>	<b>1,958</b>	<b>12</b>	<b>1,990</b>
Financial liabilities at fair value					
Current and non-current derivative financial liabilities					
Derivatives designated as accounting hedges		–	401	–	401
Other derivatives		–	298	–	298
Total current and non-current financial liabilities	21	–	699	–	699
<b>Total financial liabilities at fair value</b>		<b>–</b>	<b>699</b>	<b>–</b>	<b>699</b>

Movements in financial instruments measured using Level 3 valuation methods are presented below:

	Other investments £m
At 1 April 2009	11
Additions	3
Disposals	(2)
At 1 April 2010	12
Additions	20
Disposals	(5)
<b>At 31 March 2011</b>	<b>27</b>

There were no losses recognised in the income statement in respect of Level 3 assets held at 31 March 2011.

### 30. Financial commitments and contingent liabilities

Capital expenditure contracted for at the balance sheet date but not yet incurred was as follows:

	2011 £m	2010 £m
Property, plant and equipment	467	368
Computer software	–	15
<b>Total</b>	<b>467</b>	<b>383</b>

Future minimum operating lease payments for the group were as follows:

	2011 £m	2010 £m
Payable in the year ending 31 March:		
2011	–	494
2012	464	460
2013	440	431
2014	413	400
2015	383	375
2016	373	367
Thereafter	5,119	5,160
<b>Total future minimum operating lease payments</b>	<b>7,192</b>	<b>7,687</b>

Operating lease commitments were mainly in respect of land and buildings which arose from a sale and operating leaseback transaction in a prior period. Leases have an average term of 21 years (2010: 22 years) and rentals are fixed for an average of 21 years (2010: 22 years).

At 31 March 2011, other than as disclosed below, there were no contingent liabilities or guarantees other than those arising in the ordinary course of the group's business and on these no material losses are anticipated. The group has insurance cover to certain limits for major risks on property and major claims in connection with legal liabilities arising in the course of its operations. Otherwise, the group generally carries its own risks.

The group has provided guarantees relating to certain leases entered into by Telefonica UK Limited prior to its demerger with O2 on 19 November 2001. mmO2 plc has given BT a counter indemnity for these guarantees. The maximum exposure was US\$128m as at 31 March 2011 (2010: US\$132m), approximately £80m (2010: £87m), although this could increase by a further US\$268m (2010: US\$304m), approximately £167m (2010: £200m), in the event of credit default in respect of amounts used to defease future lease obligations. The guarantee lasts until Telefonica UK Limited has discharged all its obligations, which is expected to be when the lease ends on 30 January 2017.

We do not believe that there is any single court action that would have a material adverse effect on the financial position or operations of the group. During 2011 the aggregate volume and value of legal actions to which the group is party has remained broadly the same as at the end of 2010, during which the levels had increased significantly.

The European Commission formally investigated the way the UK Government sets the rates payable on BT's infrastructure and those paid by KCOM, and whether or not the UK Government complied with EU rules on state aid. The Commission's decision in October 2006 that no state aid had been granted was appealed. In January 2011, the appeal was rejected as inadmissible.

# REPORT OF THE INDEPENDENT AUDITORS PARENT COMPANY FINANCIAL STATEMENTS

## Independent Auditors' Report to the members of BT Group plc (the 'company')

We have audited the parent company financial statements of BT Group plc for the year ended 31 March 2011 which comprise the BT Group plc company balance sheet, the BT Group plc company reconciliation of movement in equity shareholders' funds, the BT Group plc accounting policies and related notes. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

### Respective responsibilities of directors and auditors

As explained more fully in the Statement of directors' responsibilities set out on page 88, the directors are responsible for the preparation of the parent company financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit the parent company financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

### Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the parent company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the BT Group plc Annual Report & Form 20-F for the year ended 31 March 2011 to identify material inconsistencies with the audited financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

### Opinion on financial statements

In our opinion the parent company financial statements:

- give a true and fair view of the state of the company's affairs as at 31 March 2011;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

### Opinion on other matters prescribed by the Companies Act 2006

In our opinion:

- the part of the Report on directors' remuneration to be audited has been properly prepared in accordance with the Companies Act 2006; and
- the information given in the Report of the directors for the financial year for which the parent company financial statements are prepared is consistent with the parent company financial statements.

### Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent company financial statements and the part of the Report on directors' remuneration to be audited are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

### Other matter

We have reported separately on the consolidated financial statements of BT Group plc for the year ended 31 March 2011.

**Philip Rivett (Senior Statutory Auditor)**  
for and on behalf of PricewaterhouseCoopers LLP  
Chartered Accountants and Statutory Auditors  
London, United Kingdom  
11 May 2011

# FINANCIAL STATEMENTS OF BT GROUP PLC

## BT Group plc accounting policies

### (i) Accounting basis

As used in these financial statements and associated notes, the term 'company' refers to BT Group plc. These separate financial statements of the company are presented as required by the Companies Act 2006. The separate financial statements have been prepared in accordance with UK Generally Accepted Accounting Principles (UK GAAP).

The financial statements are prepared on a going concern basis and under the historical cost convention as modified by the revaluation of certain financial instruments at fair value.

As permitted by Section 408(3) of the Companies Act 2006, the company's profit and loss account has not been presented.

The BT Group plc consolidated financial statements for the year ended 31 March 2011 contain a consolidated statement of cash flows. Consequently, the company has taken advantage of the exemption in FRS 1, 'Cash Flow Statements', not to present its own cash flow statement.

The BT Group plc consolidated financial statements for the year ended 31 March 2011 contain related party disclosures. Consequently, the company has taken advantage of the exemption in FRS 8, 'Related Party Disclosures', not to disclose transactions with other members of the BT Group.

The BT Group plc consolidated financial statements for the year ended 31 March 2011 contain financial instrument disclosures which comply with FRS 29, 'Financial Instruments: Disclosures'. Consequently, the company is exempted from the disclosure requirements of FRS 29 in respect of its financial instruments.

### (ii) Investments in subsidiary undertakings

Investments in subsidiary undertakings are stated at cost and reviewed for impairment if there are indicators that the carrying value may not be recoverable.

### (iii) Taxation

Full provision is made for deferred taxation on all timing differences which have arisen but not reversed at the balance sheet date. Deferred tax assets are recognised to the extent that it is regarded as more likely than not that there will be sufficient taxable profits from which the underlying timing differences can be deducted. The deferred tax balances are not discounted.

### (iv) Dividends

Dividend distributions are recognised as a liability in the year in which the dividends are approved by the company's shareholders. Interim dividends are recognised when they are paid; final dividends when authorised in general meetings by shareholders.

### (v) Share capital

Ordinary shares are classified as equity. Repurchased shares of the company are recorded in the balance sheet as treasury shares and presented as a deduction from shareholders' equity at cost.

### (vi) Cash

Cash includes cash in hand and bank deposits repayable on demand.

### (vii) Share-based payments

The company does not incur a charge for share-based payments. However, the issuance by the company of share options and awards to employees of its subsidiaries represents additional capital contributions to its subsidiaries. An addition to the company's investment in subsidiaries is recorded with a corresponding increase in equity shareholders' funds. The additional capital contribution is determined based on the fair value of options and awards at the date of grant and is recognised over the vesting period.

## Other information

### (i) Dividends

The Board recommends that a final dividend in respect of the year ended 31 March 2011 of 5.0p will be paid to shareholders on 5 September 2011, taking the full year proposed dividend in respect of the 2011 financial year to 7.4p (2010: 6.9p). This dividend is subject to shareholder approval at the Annual General Meeting and therefore the liability of approximately £388m (2010: £356m) has not been included in these financial statements.

### (ii) Employees

The executive directors and the Chairman of BT Group plc were the only employees of the company during 2011. The costs relating to qualifying services provided to the company's principal subsidiary, British Telecommunications plc, are recharged to that company.

### (iii) Audit fees

The audit fee in respect of the parent company was £41,000 (2010: £41,000). Fees payable to PricewaterhouseCoopers LLP for non-audit services to the company are not required to be disclosed as they are included within note 7 to the consolidated financial statements of BT Group plc.

**BT Group plc company balance sheet**

At 31 March	2011 £m	2010 £m
<b>Fixed assets</b>		
Investments in subsidiary undertakings <sup>a</sup>	10,417	10,349
<b>Total fixed assets</b>	<b>10,417</b>	<b>10,349</b>
<b>Current assets</b>		
Cash at bank and in hand	–	11
<b>Total current assets</b>	<b>–</b>	<b>11</b>
Creditors: amounts falling due within one year <sup>b</sup>	722	186
<b>Net current liabilities</b>	<b>(722)</b>	<b>(175)</b>
<b>Total assets less current liabilities</b>	<b>9,695</b>	<b>10,174</b>
<b>Capital and reserves</b>		
Called up share capital	408	408
Share premium account	62	62
Capital redemption reserve	27	27
Treasury shares reserve	(1,078)	(1,105)
Profit and loss account	10,276	10,782
<b>Total equity shareholders' funds<sup>c</sup></b>	<b>9,695</b>	<b>10,174</b>

<sup>a</sup> Throughout 2011 and 2010, the company held a 100% investment in BT Group Investments Limited, a company registered in England and Wales. The increase in investments in subsidiary undertakings relates to additional capital contributions in respect of share-based payments of £68m in 2011 (2010: £71m).

<sup>b</sup> Creditors consists of amounts owed to subsidiary undertakings of £703m (2010: £166m) and other creditors of £19m (2010: £20m).

<sup>c</sup> The movements in total equity shareholders' funds shown on page 154.

The financial statements of the company on pages 152 to 155 were approved by the Board of the directors on 11 May 2011 and were signed on its behalf by

**Sir Michael Rake**  
Chairman

**Ian Livingston**  
Chief Executive

**Tony Chanmugam**  
Group Finance Director

## BT Group plc company reconciliation of movement in equity shareholders' funds

	Share capital <sup>a</sup> £m	Share premium account £m	Capital redemption reserve £m	Treasury reserve <sup>b</sup> £m	Profit and loss account <sup>b,c</sup> £m	Total £m
At 1 April 2009	408	62	27	(1,109)	10,980	10,368
Loss for the financial year	–	–	–	–	(6)	(6)
Dividends paid	–	–	–	–	(263)	(263)
Capital contribution in respect of share-based payment	–	–	–	–	71	71
Net issue of treasury shares	–	–	–	4	–	4
<b>At 1 April 2010</b>	<b>408</b>	<b>62</b>	<b>27</b>	<b>(1,105)</b>	<b>10,782</b>	<b>10,174</b>
Loss for the financial year	–	–	–	–	(12)	(12)
Dividends paid	–	–	–	–	(543)	(543)
Capital contribution in respect of share-based payment	–	–	–	–	68	68
Net issue of treasury shares	–	–	–	27	(19)	8
<b>At 31 March 2011</b>	<b>408</b>	<b>62</b>	<b>27</b>	<b>(1,078)</b>	<b>10,276</b>	<b>9,695</b>

<sup>a</sup> The allotted, called up and fully paid ordinary share capital of the company at 31 March 2011 and 2010 was £408m, representing 8,151,227,029 ordinary shares of 5p each.

<sup>b</sup> In 2011 12,335,580 shares (2010: 8,320,766) were issued from treasury to satisfy obligations under employee share schemes and executive share awards at a cost of £27m (2010: £4m). At 31 March 2011 388,570,539 shares (2010: 400,906,119) with an aggregate nominal value of £19m (2010: £20m) were held as treasury shares at cost.

<sup>c</sup> The loss for the financial year, dealt with in the profit and loss account of the company after taking into account dividends received from subsidiary undertakings, was £12m (2010: loss of £6m). As permitted by Section 408(3) of the Companies Act 2006, no profit and loss account of the company is presented.

# SUBSIDIARY UNDERTAKINGS AND ASSOCIATE

The tables below give brief details of the group's principal<sup>a</sup> operating subsidiaries<sup>b</sup> and associate at 31 March 2011. All subsidiaries are unlisted and held through an intermediate holding company, unless otherwise stated. No subsidiaries are excluded from the group consolidation.

Subsidiary undertakings	Activity	Group interest in allotted capital <sup>c</sup>	Country of operation <sup>d</sup>
British Telecommunications plc	Communications related services and products provider	100% ordinary	UK
BT Americas Inc <sup>d</sup>	Communications related services, systems integration and products provider	100% common	International
BT Australasia Pty Limited	Communications related services and products provider	100% ordinary 100% preference	Australia
BT Brasil Servicos de Telecomunicacoes Ltda <sup>b</sup>	Data communication services	100% common	Brazil
BT Business Direct Limited	Technology equipment retailer	100% ordinary	UK
BT Centre Nominee 2 Limited	Property holding company	100% ordinary	UK
BT Communications do Brasil Limitada <sup>b</sup>	Communications related services, technology consulting and products provider	100% common	Brazil
BT Communications Ireland Limited	Telecommunications service provider	100% ordinary	Republic of Ireland
BT Conferencing Inc	Audio, video and web collaboration services provider	100% common	US
BT Conferencing Video Inc	Audio, video and web collaboration services provider	100% common	US
BT Convergent Solutions Limited	Communications related services and products provider	100% ordinary	UK
BT Engage IT Limited	IT solutions provider	100% ordinary	UK
BT ESPANA, Compania de Servicios Globales de Telecomunicaciones, SA	Communications related services and products provider	100% ordinary	Spain
BT Fleet Limited	Fleet management company	100% ordinary	UK
BT France SA	Communications related services, systems integration and products provider	100% ordinary	France
BT Frontline Pte Ltd	Communications related services and products provider	100% ordinary	Singapore
BT (Germany) GmbH & Co. oHG	Communications related services and products provider	100% ordinary	Germany
BT Global Communications India Private Limited	Communications related services	100% ordinary	India
BT Global Services Limited	International telecommunications network systems provider	100% ordinary	UK
BT Holdings Limited	Investment holding company	100% ordinary	UK
BT Hong Kong Limited	Communications related services and products provider	100% ordinary 100% preference	Hong Kong
BT INS Inc	Information telecommunications consulting and software solutions provider	100% common	US
BT LatAm Brasil Ltda <sup>b</sup>	Data communication services	100% common	Brazil
BT Italia SpA	Communications related services and products provider	98.6% ordinary	Italy
BT Limited	International telecommunications network systems provider	100% ordinary	International
BT Managed Services Limited	Communications related services and products provider	100% ordinary	UK
BT Nederland NV	Communications related services and products provider	100% ordinary	Netherlands
BT Payment Services Limited	Payment services provider	100% ordinary	UK
BT Services SA	Technology consulting and engineering services	100% ordinary	France
BT Singapore Pte Ltd	Communications related services and products provider	100% ordinary	Singapore
BT Switzerland AG	Communications related services and products provider	100% ordinary	Switzerland
BT US Investments Limited <sup>b</sup>	Investment holding company	100% ordinary	Jersey
Business Integration S.L.	Technology consulting and engineering services	100% ordinary	Spain
Communications Global Network Services Limited <sup>d</sup>	Communications related services and products provider	100% ordinary	International
Communications Networking Services (UK)	Communications related services and products provider	100% ordinary	UK
dabs.com plc	Technology equipment retailer	100% ordinary	UK
Infonet Services Corporation	Global managed network service provider	100% common	US
Infonet USA Corporation	Global managed network service provider	100% common	US
Plusnet plc	Broadband service provider	100% ordinary	UK
Radianz Americas Inc	Global managed network service provider	100% common 100% preference	US

<sup>a</sup> The group comprises a large number of entities and it is not practical to include all of them in this list. The list therefore includes only those entities that have a significant impact on the revenue, profit or assets of the group. A full list of subsidiaries, joint ventures and associates will be annexed to the company's next annual return filed with the Registrar of Companies.

<sup>b</sup> The principal operating subsidiaries (listed above) have a reporting date of 31 March, except for BT US Investments Limited which has a reporting date of 31 October in order to meet its corporate objectives and entities domiciled in Brazil, due to regulatory requirements.

<sup>c</sup> The proportion of voting rights held corresponds to the aggregate interest percentage held by the holding company and subsidiary undertakings.

<sup>d</sup> All overseas undertakings are incorporated in their country of operations. Subsidiary undertakings operating internationally are all incorporated in England and Wales, except BT Americas Inc and Communications Global Network Services Limited which are incorporated in the US and Bermuda, respectively.

Associate	Activity	Share capital		Country of operation <sup>9</sup>
		Issued <sup>e</sup>	Percentage owned <sup>f</sup>	
Tech Mahindra Limited	Global systems integrator and business transformation consultancy provider	125,955,481	23.5%	India

<sup>e</sup> Issued share capital comprises ordinary or common shares unless otherwise stated.

<sup>f</sup> Held through an intermediate holding company.

<sup>9</sup> Incorporated in the country of operation.