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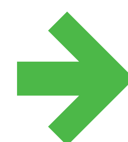
BT Group plc

Annual Report & Form 20-F 2010



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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 judgements 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 58 to 59 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 57 to 82 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

We have audited the consolidated financial statements of BT Group plc for the year ended 31 March 2010 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 84, 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 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.

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 2010 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 for 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; and
- 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.

Other matter

We have reported separately on the parent company financial statements of BT Group plc for the year ended 31 March 2010 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
12 May 2010

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 2010 and 2009 and the results of their operations and cash flows for each of the three years in the period ended 31 March 2010, 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 2010, 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 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.

As disclosed in note 30 to the consolidated financial statements, the company adopted an amendment to IFRS 2 'Share-based payment' and accordingly changed the manner in which it accounts for vesting conditions and cancellations.

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
12 May 2010

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 have been prepared under the historical cost convention, modified for the revaluation of certain financial assets and liabilities at fair value.

Presentation of specific items

The group's income statement and segmental analysis separately identify trading results before significant one-off or unusual items (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 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 significant one-off or unusual in nature and have little predictive value. 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 significant one-off or unusual in nature 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 settlement. Specific items for the current and prior years are disclosed in note 5.

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 93 and 94 in **'Critical accounting estimates and key judgements'.**

Implementation of new accounting standards

With effect from 1 April 2009, the group adopted the amendment to IFRS 2 'Share-based payment – Vesting Conditions and Cancellations', IFRS 8 'Operating Segments', IAS 1 (Revised) 'Presentation of Financial Statements', IAS 23 (Revised) 'Borrowing costs', minor amendments to a number of other accounting standards and several new interpretations. The adoption of the amendment to IFRS 2 and IAS 1 (Revised) has resulted in the restatement of comparative information. Further details are provided on pages 94 and 95.

Composition of the group

The group's principal operating subsidiaries and associate are detailed on page 149.

(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 joint ventures and associates using the equity method of accounting.

- 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.
- 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.
- 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.

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, balances, income and expenses are eliminated on consolidation.

Investments in associates and joint ventures are initially recognised at cost. 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.

(iii) 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 are 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.

(iv) 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.

(v) 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 on a straight line basis over the useful life of the asset.

(vi) 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.

(vii) 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.

(viii) Business combinations

The purchase method of accounting is used for the acquisition of subsidiaries, in accordance with IFRS 3 'Business Combinations'. On transition to IFRS, the group elected not to apply IFRS 3 retrospectively to acquisitions that occurred before 1 April 2004. Goodwill arising on the acquisition of subsidiaries is therefore treated as follows:

- Goodwill which arose after 1 April 2004: included in the balance sheet at original cost, less any provisions for impairment. This goodwill is not amortised.
- Goodwill which arose between 1 January 1998 and 1 April 2004: included in the balance sheet at original cost, less accumulated amortisation to the date of transition to IFRS and less any provisions for impairment. This goodwill is not amortised after the date of transition to IFRS.
- Goodwill which arose before 1 January 1998: written off directly to retained earnings.

On acquisition of a subsidiary, fair values are attributed to the identifiable net tangible and intangible assets acquired. The excess of the cost of the acquisition over the fair value of the group's share of the identifiable net assets acquired is recorded as goodwill. If the cost of the acquisition is less than the fair value of the group's share of the identifiable net assets acquired, the difference is recognised directly in the income statement. On disposal of a subsidiary, the gain or loss on disposal includes the carrying amount of goodwill relating to the subsidiary sold. Goodwill previously written off to retained earnings is not recycled to the income statement on disposal of the related subsidiary.

(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 5 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 labour, contractors' charges, 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:

Land and buildings	
Freehold buildings	40 years
Leasehold land and buildings	Unexpired portion of lease or 40 years, whichever is the shorter

▶ Network infrastructure and equipment	
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 for which the commencement date for capitalisation is on or after 1 April 2009, and 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. Previously, the group immediately recognised all borrowing costs as an expense in the income statement. The change in accounting policy was due to the adoption of IAS 23 'Borrowing Costs (Revised)'.

(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.

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 pricing model or the Monte Carlo model, whichever is most appropriate to the award.

The group adopted IFRS 2 'Share-based payment – vesting conditions and cancellations', with effect from 1 April 2009. The amendment clarifies that only 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 share save 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) Advertising and marketing

The costs associated with the group's advertising and marketing activities are recognised within other operating costs as incurred.

(xx) 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.

(xxi) 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.

(xxii) 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 are not designated in a hedging relationship or have a maturity period within 12 months. Where derivative financial instruments have a maturity period greater than 12 months and are designated in a hedge relationship, 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 to 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 17.

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 BT Pension Scheme, to pay pension benefits to approximately 333,000 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 and the rate at which the future pension payments are discounted. 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 2010 and the key financial assumptions used to measure the obligation are disclosed in note 29.

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 2009 had no significant impact in aggregate on the results for the year ended 31 March 2010.

The carrying values of software, property, plant and equipment are disclosed in notes 12 and 13, respectively. The useful lives applied to the principal categories of assets are disclosed on pages 89 and 90.

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 100.

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 notes 29 and 22, respectively.

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 12.

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 32.

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 17.

Provisions
As disclosed in note 21, 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 given the current regulatory environment. 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 2010

The following new, revised and amended standards and interpretations have been adopted in 2010 and have affected the amounts reported in these financial statements or have resulted in a change in presentation or disclosure.

Amendment to IFRS 2 'Share-based payment – Vesting Conditions and Cancellations'
The adoption of the amendment to IFRS 2 'Share-based payment – Vesting Conditions and Cancellations' has resulted in a change in the group's accounting policy for share-based payments. The amendment clarifies that only 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 the equity instruments granted. In the case that the award does not vest as a result of a failure to meet a non-vesting condition that is within the control of either the group or the counterparty, this must be treated as a cancellation. Cancellations are treated as accelerated vestings and all remaining future charges are immediately recognised in the income statement with the credit recognised directly in equity. Prior to the adoption of the amendment to IFRS 2, the monthly savings requirement under the group's all employee sharesave plans was classified as a vesting condition and any cancellations made by employees prior to the normal vesting date resulted in the reversal of all charges recognised to date.

The amendment to IFRS 2 requires retrospective adoption and hence prior period comparatives have been restated resulting in an increase of £110m in the share-based payment charge for 2009 (2008: £nil) and a reduction of 1.4p in basic and diluted loss per share for 2009 (2008: nil). There was no impact on net assets and cash flow. There was no material impact on the share-based payment charge in 2010, following the adoption of the amendment.

IAS 1 (Revised) 'Presentation of Financial Statements'
IAS 1 (Revised) introduced some changes in the format and content of the financial statements. In addition, the revised standard requires the presentation of a third balance sheet as at 1 April 2008 because the group has applied two new accounting policies retrospectively.

The adoption of the amendment to IAS 1 (Revised) arising from the Annual Improvements to IFRSs 2007 has also resulted in a change in accounting policy applied to the classification of derivatives which have not been allocated to a specific hedge relationship. Where such derivatives have a maturity of and are expected to be held for more than twelve months after the reporting period, they are now presented as non current assets or liabilities. Prior period balance sheets have been reclassified to be on a consistent basis. The impact of these changes on the balance sheet line items is an increase in non current assets as at 31 March 2009 of £86m (31 March 2008: £6m) and a reduction in current assets as at 31 March 2009 of £86m (31 March 2008: £6m), and a reduction in current liabilities as at 31 March 2009 of £284m (31 March 2008: £209m) and an increase in non current liabilities of £284m (31 March 2008: £209m).

IAS 23 (Revised) 'Borrowing costs'
In respect of borrowing costs relating to qualifying assets for which the commencement date for capitalisation is on or after 1 April 2009, the group capitalises borrowing costs during the construction phase as part of the cost of that asset. Previously, the group immediately recognised all borrowing costs as an expense in the income statement. The change in accounting policy was due to the adoption of IAS 23 (Revised) 'Borrowing Costs'. The change in accounting policy has had no material impact on earnings per share. In 2010, the group capitalised borrowing costs of £3m with respect to property, plant and equipment under construction (note 13) and software development costs (note 12).

Amendment to IFRS 7 'Financial Instruments: Disclosures'
The amendment to IFRS 7 expands the disclosures required in respect of fair value financial instruments measurements and liquidity risk. The group has elected not to provide comparative information for these expanded disclosures in 2010, as set out in note 32, in accordance with the transitional relief offered in the amendment.

IFRS 8 'Operating Segments'
IFRS 8 is a new disclosure standard which has not changed the group's reportable segments but has introduced certain new disclosures as set out in note 1.

As part of the Annual Improvements to IFRSs 2009 the IASB modified the requirement to disclose total assets for each reportable segment. This disclosure is now required only if a measure of total assets by segment is reported to the 'chief operating decision maker' (CODM). For BT, such a measure is not included in the information regularly provided to the CODM. The amendment to IFRS 8 is effective for accounting periods commencing on or after 1 January 2010. The amendment was endorsed by the EU on 23 March 2010 and the group has chosen to adopt it early for 2010.

The following new and revised standards and interpretations have also been adopted in these financial statements. Their adoption has not had any significant impact on the amounts reported.

- IFRIC 12 'Service concession arrangements';
- IFRIC 13 'Customer loyalty programmes';
- IFRIC 16 'Hedges of a net investment in a foreign operation'; and
- IFRIC 18 'Transfer of assets from customers'.

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 2010 or later periods, which the group has not adopted early, with the exception of the amendment to IFRS 8 as described above. Those which are considered to be relevant to the group's operations, but which are not currently expected to have a significant impact on the group's financial statements, are as follows:

IFRS 3 (Revised) 'Business Combinations' (effective 1 April 2010)
IFRS 3 (Revised) revises certain aspects of accounting for business combinations. Revisions include the requirement to expense all transaction costs and the requirement for all payments to acquire a business to be recorded at fair value at the acquisition date, with future contingent consideration subsequently re-measured at fair value through the income statement. IFRS 3 (Revised) is applied prospectively to business combinations entered into on or after the effective date.

IAS 27 (Revised) 'Consolidated and Separate Financial Statements' (effective 1 April 2010)
IAS 27 (Revised), which is applied prospectively, requires the effects of all transactions with non-controlling interests to be recorded in equity if there is no overall change in control. Such transactions will no longer result in goodwill or gains or losses being recorded. IAS 27 (Revised) also specifies that when control is lost, any remaining interest should be re-measured to fair value and a gain or loss recorded through the income statement.

IFRIC 17 'Distributions of Non-cash Assets to Owners' (effective 1 April 2010)
IFRIC 17 provides guidance on how an entity should measure distributions other than cash when it pays dividends to its owners. The interpretation requires the dividend payable to be measured at the fair value of the assets to be distributed, and any difference between the fair value and the book value of the assets is recorded in the income statement.

Amendment to IAS 39 'Financial Instruments: Recognition and Measurement: Eligible Hedged items' (effective 1 April 2010)
This clarifies two aspects of hedge accounting relating to hedging with options and the identification of inflation as a hedged risk.

Amendment to IAS 32 'Financial Instruments: Presentation-Classification of Rights Issues' (effective 1 April 2010)
This requires an issue to all existing shareholders of rights to acquire additional shares to be recognised in equity, regardless of the currency in which the exercise price is denominated.

Annual Improvements to IFRSs 2009 (effective 1 April 2010)
These improvements relate to a number of standards including changes in presentation, recognition and measurement, terminology and editorial changes. It incorporates minor amendments to a number of standards in areas including operating segments, leases, intangible assets and financial instruments.

IAS 24 (Revised) 'Related Party Disclosures' (effective 1 April 2011)
The revised standard clarifies 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, which is applied retrospectively, 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.

IFRS 9 'Financial Instruments' (effective 1 April 2013)
IFRS 9 is the first phase of the IASB's three phase project to replace IAS 39 'Financial Instruments: Recognition and Measurement'. It is applicable to financial assets and requires classification and measurement in either the amortised cost or the fair value category. IFRS 9 is applied prospectively with transitional arrangements depending on the date of application.

GROUP INCOME STATEMENT

Year ended 31 March 2010	Notes	Before specific items £m	Specific items[a] £m	Total £m
Revenue	1	**20,911**	(52)	**20,859**
Other operating income	2	378	2	380
Operating costs	3	(18,689)	(427)	(19,116)
Operating profit	1	**2,600**	**(477)**	**2,123**
Finance expense	6	(3,113)	–	(3,113)
Finance income	6	1,944	11	1,955
Net finance expense		**(1,169)**	**11**	**(1,158)**
Share of post tax profit of associates and joint ventures	15	25	29	54
Loss on disposal of associate	15	–	(12)	(12)
Profit before taxation		**1,456**	(449)	1,007
Taxation	8	(320)	342	22
Profit for the year		**1,136**	**(107)**	**1,029**
Attributable to:				
Equity shareholders of the parent		1,135	(107)	1,028
Minority interests	23	1	–	1
Earnings per share	9			
Basic				13.3p
Diluted				12.9p

a For a definition of specific items, see page 87. An analysis of specific items is provided in note 5.

Year ended 31 March 2009	Notes	Before specific items[b] £m	Specific items[a] £m	Total[b] £m
Revenue	1	**21,390**	**–**	**21,390**
Other operating income	2	352	(13)	339
Operating costs	3	(21,033)	(395)	(21,428)
Operating profit	1	**709**	**(408)**	**301**
Finance expense	6	(3,272)	–	(3,272)
Finance income	6	2,652	–	2,652
Net finance expense		**(620)**	**–**	**(620)**
Share of post tax profit of associates and joint ventures	15	39	36	75
Profit (loss) before taxation		**128**	**(372)**	**(244)**
Taxation	8	10	43	53
Profit (loss) for the year		**138**	**(329)**	**(191)**
Attributable to:				
Equity shareholders of the parent		136	(329)	(193)
Minority interests	23	2	–	2
Loss per share	9			
Basic				(2.5)p
Diluted				(2.5)p

a For a definition of specific items, see page 87. An analysis of specific items is provided in note 5.
b Restated. See page 94.

GROUP INCOME STATEMENT

Year ended 31 March 2008	Notes	Before specific items[b] £m	Specific items[a] £m	Total[b] £m
Revenue	1	**20,704**	**–**	**20,704**
Other operating income	2	359	(10)	349
Operating costs	3	(18,168)	(529)	(18,697)
Operating profit	1	**2,895**	**(539)**	**2,356**
Finance expense	6	(2,891)	–	(2,891)
Finance income	6	2,513	–	2,513
Net finance expense		**(378)**	**–**	**(378)**
Share of post tax loss of associates and joint ventures		(11)	–	(11)
Profit on disposal of associate		–	9	9
Profit before taxation		**2,506**	**(530)**	**1,976**
Taxation	8	(581)	343	(238)
Profit for the year		**1,925**	**(187)**	**1,738**
Attributable to:				
Equity shareholders of the parent		1,924	(187)	1,737
Minority interests		1	–	1
Earnings per share	9			
Basic				21.5p
Diluted				21.1p

[a] For a definition of specific items, see page 87. An analysis of specific items is provided in note 5.
[b] Restated. See page 94.

GROUP STATEMENT OF COMPREHENSIVE INCOME

Year ended 31 March	Notes	**2010** £m	2009[a] £m	2008[a] £m
Profit (loss) for the year		1,029	(191)	1,738
Other comprehensive (loss) income				
Actuarial (losses) gains relating to retirement benefit obligations	29	(4,324)	(7,037)	2,621
Exchange differences on translation of foreign operations	25	(119)	692	213
Fair value movements on available-for-sale assets	25	7	5	–
Fair value movements on cash flow hedges:				
– fair value (losses) gains	25	(1,067)	2,719	446
– reclassified and reported in net profit (loss)	25	496	(2,144)	(294)
– reclassified and reported in non current assets	25	(4)	(5)	11
Tax on components of other comprehensive income	8	1,350	1,859	(832)
Other comprehensive (loss) income for the year, net of tax		**(3,661)**	**(3,911)**	**2,165**
Total comprehensive (loss) income for the year		**(2,632)**	**(4,102)**	**3,903**
Attributable to:				
Equity shareholders of the parent		(2,633)	(4,113)	3,899
Minority interests		1	11	4
		(2,632)	(4,102)	3,903

[a] Restated. See page 94.

GROUP STATEMENT OF CHANGES IN EQUITY

	Shareholders' equity (deficit)							
	Share capital[a] £m	Share premium[a] £m	Capital reserve £m	Other reserves[b] £m	Retained earnings £m	Total £m	Minority interests[c] £m	Total Equity £m
At 1 April 2007	432	31	2	88	3,685	4,238	34	4,272
Change in accounting policy for adoption of the amendment to IFRS 2 (see page 94)	–	–	–	–	–	–	–	–
Total comprehensive income[d]	–	–	–	344	3,555	3,899	4	3,903
Dividends to shareholders	–	–	–	–	(1,241)	(1,241)	–	(1,241)
Share-based payments	–	–	–	–	55	55	–	55
Tax on share-based payments	–	–	–	–	(45)	(45)	–	(45)
Issue of ordinary shares	1	31	–	–	–	32	–	32
Cancellation of shares	(13)	–	13	570	(570)	–	–	–
Net purchase of treasury shares	–	–	–	(1,529)	–	(1,529)	–	(1,529)
Other movements in minority interests	–	–	–	–	–	–	(15)	(15)
At 1 April 2008	420	62	15	(527)	5,439	5,409	23	5,432
Total comprehensive (loss) income[d]	–	–	–	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 minority interests	–	–	–	–	–	–	(7)	(7)
At 1 April 2009	408	62	27	1,301	(1,656)	142	27	169
Total comprehensive (loss) income[d]	–	–	–	(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 minority interests	–	–	–	–	–	–	(4)	(4)
At 31 March 2010	**408**	**62**	**27**	**757**	**(3,904)**	**(2,650)**	**24**	**(2,626)**

[a] For details of share capital and share premium, see note 24.
[b] For further analysis of Other reserves, see note 25.
[c] For further analysis of minority interests, see note 23.
[d] The group statement of comprehensive income is on page 97.

GROUP CASH FLOW STATEMENT

Year ended 31 March	Note	2010 £m	2009[a] £m	2008[a] £m
Cash flow from operating activities				
Profit (loss) before taxation[b]		1,007	(244)	1,976
Depreciation and amortisation		3,039	2,890	2,889
Loss on sale of associates and group undertakings		10	13	1
Net finance expense		1,158	620	378
Other non cash charges		77	596	60
Share of (profits) losses of associates and joint ventures		(54)	(75)	11
Decrease in inventories		14	11	23
Decrease (increase) in trade and other receivables		524	1,063	(498)
(Decrease) increase in trade and other payables		(708)	(379)	451
(Decrease) increase in provisions and other liabilities[d]		(591)	439	(104)
Cash generated from operations[b]		**4,476**	**4,934**	**5,187**
Income taxes paid		(76)	(232)	(222)
Income tax repayment for prior years		425	4	521
Net cash inflow from operating activities		**4,825**	**4,706**	**5,486**
Cash flow from investing activities				
Interest received		16	19	111
Dividends received from associates and joint ventures		3	6	2
Proceeds on disposal of property, plant and equipment		29	44	62
Proceeds on disposal of businesses		2	–	–
Proceeds on disposal of associates and joint ventures		–	–	13
Proceeds on disposal of non current financial assets		–	–	1
Proceeds on disposal of current financial assets[c]		8,739	6,316	4,779
Acquisition of subsidiaries, net of cash acquired		(70)	(227)	(377)
Purchases of property, plant and equipment and software		(2,509)	(3,082)	(3,315)
Purchases of non current financial assets		–	–	(2)
Purchases of current financial assets[c]		(8,985)	(6,030)	(4,938)
Net cash outflow from investing activities		**(2,775)**	**(2,954)**	**(3,664)**
Cash flow from financing activities				
Equity dividends paid		(265)	(1,221)	(1,236)
Dividends paid to minority interests		–	(1)	–
Interest paid		(956)	(956)	(842)
Repayment of borrowings		(307)	(863)	(913)
Repayment of finance lease liabilities		(24)	(16)	(284)
Net proceeds (repayment) of issued commercial paper		(697)	606	(681)
New bank loans raised		522	795	3,939
Proceeds from finance leases		9	–	–
Repurchase of ordinary shares		–	(334)	(1,498)
Proceeds on issue of treasury shares		4	125	85
Net cash used in financing activities		**(1,714)**	**(1,865)**	**(1,430)**
Effect of exchange rate changes on cash and cash equivalents		(7)	54	25
Net increase (decrease) in cash and cash equivalents		**329**	**(59)**	**417**
Cash and cash equivalents at the start of the year		1,115	1,174	757
Cash and cash equivalents at the end of the year	10	**1,444**	**1,115**	**1,174**

a Restated. See page 94.
b 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.
c Primarily consists of investment in and redemption of amounts held in liquidity funds.
d Includes pension deficit payment of £525m (2009: £nil, 2008: £320m).

GROUP BALANCE SHEET

At 31 March	Notes	2010 £m	2009[a] £m	2008[a] £m
Non current assets				
Intangible assets	12	3,672	3,788	3,355
Property, plant and equipment	13	14,856	15,405	15,307
Derivative financial instruments	19	1,076	2,542	316
Investments	14	64	55	31
Retirement benefit asset	29	–	–	2,887
Associates and joint ventures	15	195	132	85
Trade and other receivables	17	336	322	854
Deferred tax assets	22	2,196	1,103	–
		22,395	**23,347**	**22,835**
Current assets				
Inventories	16	107	121	122
Trade and other receivables	17	3,696	4,185	4,449
Derivative financial instruments	19	624	158	71
Investments	14	406	163	440
Cash and cash equivalents	10	1,452	1,300	1,435
		6,285	**5,927**	**6,517**
Current liabilities				
Loans and other borrowings	18	3,269	1,542	1,524
Derivative financial instruments	19	166	56	58
Trade and other payables	20	6,531	7,215	7,591
Current tax liabilities		320	1	241
Provisions	21	134	254	81
		10,420	**9,068**	**9,495**
Total assets less current liabilities		**18,260**	**20,206**	**19,857**
Non current liabilities				
Loans and other borrowings	18	9,522	12,365	9,818
Derivative financial instruments	19	533	711	1,014
Retirement benefit obligations	29	7,864	3,973	108
Other payables	20	804	794	707
Deferred tax liabilities	22	1,456	1,728	2,513
Provisions	21	707	466	265
		20,886	**20,037**	**14,425**
Equity				
Ordinary shares	24	408	408	420
Share premium	24	62	62	62
Capital redemption reserve		27	27	15
Other reserves	25	757	1,301	(527)
Retained (loss) earnings		(3,904)	(1,656)	5,439
Total parent shareholders' (deficit) equity		**(2,650)**	**142**	**5,409**
Minority interests	23	24	27	23
Total (deficit) equity[b]		**(2,626)**	**169**	**5,432**
		18,260	**20,206**	**19,857**

[a] Restated. See page 94.
[b] The Group statement of changes in equity is on page 98.

The consolidated financial statements on pages 87 to 144 and 149 were approved by the Board of Directors on 12 May 2010 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 has implemented IFRS 8 'Operating segments' with effect from 1 April 2009. IFRS 8 requires operating segments to be identified on the basis of internal reports about components of the group which are regularly reviewed by the 'chief operating decision maker' in order to allocate resources to the segments and to assess their performance. As a result of the adoption of IFRS 8, the group's reportable segments have not changed. The group's operating segments are reported based on financial information provided to the *Operating Committee,* as detailed on page 61, 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 also normally attends 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 functional 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 serves multinational corporations, domestic businesses, government departments and other communications providers across the world, providing networked IT services.

BT Retail serves consumer customers and small and medium enterprises (SMEs) in the UK, providing a range of innovative communications products and services. BT Retail also includes BT Ireland, which operates across the major corporate, SME, consumer and wholesale markets throughout the Republic of Ireland and Northern Ireland, and BT Enterprises, which comprises a number of individual businesses including BT Conferencing, BT Directories, BT Expedite, BT Redcare and BT Payphones.

BT Wholesale provides services to UK communications providers through a diverse portfolio ranging from nationally available broadband, voice and data connectivity services and interconnect to bespoke, fully managed network outsourcing and value-added solutions.

Openreach is responsible for the crucial 'first mile' connecting communications providers' customers to their local telephone exchange, giving them equal, open and economic access to the UK network. Openreach products are sold on an equivalent basis to BT lines of business and other communications providers at the same arm's length prices, with the BT lines of business being treated no differently than any other customer with regard to terms and conditions or access to systems and data.

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 design and build of the platforms, systems and processes which support the provision of the group's products and services, and BT Operate is responsible for their operation. 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 do not meet the quantitative thresholds as set out in IFRS 8 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.

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 87.

Information regarding the results of each reportable segment is provided below. Performance is measured based on EBITDA before specific items and contract and financial review charges recognised in BT Global Services in 2009 (defined as 'adjusted EBITDA'), 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 significant, one-off or unusual in nature and have little predictive value. Specific items are detailed in note 5 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 treasury function which manages the overall net debt position of the group.

Restatements

Comparatives have been restated for the adoption of the amendment to IFRS 2, which has been dealt with in the 'Other' category and detailed on page 94. Comparatives have also been restated for the impact of customer account moves between BT Global Services and BT Retail and other internal trading model changes effective from 1 April 2009 and has had no impact on the total results of the group.

1. Segment information continued

Segment revenue and profit

Year ended 31 March 2010	BT Global Services £m	BT Retail £m	BT Wholesale £m	Openreach £m	Other £m	Total £m
Total segment revenue	8,513	8,297	4,450	5,164	40	26,464
Internal revenue	–	(373)	(1,227)	(3,953)	–	(5,553)
Revenue from external customers	**8,513**	**7,924**	**3,223**	**1,211**	**40**	**20,911**
Adjusted EBITDA[b]	**457**	**1,850**	**1,279**	**1,960**	**93**	**5,639**
Depreciation and amortisation	(815)	(459)	(680)	(856)	(229)	(3,039)
Adjusted operating profit (loss)[b]	(358)	1,391	599	1,104	(136)	2,600
Specific items (note 5)	–	–	–	–	(477)	(477)
Operating (loss) profit	**(358)**	**1,391**	**599**	**1,104**	**(613)**	**2,123**
Share of post tax profits of associates and joint ventures						54
Loss on disposal of associate						(12)
Net finance expense						(1,158)
Profit before tax						1,007

Year ended 31 March 2009[a]	BT Global Services £m	BT Retail £m	BT Wholesale £m	Openreach £m	Other £m	Total £m
Total segment revenue	8,628	8,663	4,658	5,231	40	27,220
Internal revenue	–	(343)	(1,228)	(4,218)	–	(5,789)
Adjusted revenue from external customers[b]	**8,628**	**8,320**	**3,430**	**1,013**	**40**	**21,431**
Contract and financial review charges	(41)	–	–	–	–	(41)
Revenue from external customers	8,587	8,320	3,430	1,013	40	21,390
Adjusted EBITDA[b]	**261**	**1,664**	**1,277**	**1,996**	**40**	**5,238**
Depreciation and amortisation	(776)	(426)	(686)	(778)	(224)	(2,890)
Adjusted operating profit (loss)[b]	(515)	1,238	591	1,218	(184)	2,348
Specific items (note 5)	–	–	–	–	(408)	(408)
Contract and financial review charges	(1,639)	–	–	–	–	(1,639)
Operating (loss) profit	**(2,154)**	**1,238**	**591**	**1,218**	**(592)**	**301**
Share of post tax profits of associates and joint ventures						75
Net finance expense						(620)
Loss before tax						(244)

[a] Restated. See pages 94 and 101.

Year ended 31 March 2008[a]	BT Global Services £m	BT Retail £m	BT Wholesale £m	Openreach £m	Other £m	Total £m
Total segment revenue	7,664	8,682	4,959	5,266	28	26,599
Internal revenue	–	(265)	(1,252)	(4,378)	–	(5,895)
Revenue from external customers	**7,664**	**8,417**	**3,707**	**888**	**28**	**20,704**
Adjusted EBITDA[b]	**808**	**1,529**	**1,406**	**1,911**	**130**	**5,784**
Depreciation and amortisation	(744)	(445)	(893)	(689)	(118)	(2,889)
Adjusted operating profit[b]	64	1,084	513	1,222	12	2,895
Specific items (note 5)	–	–	–	–	(539)	(539)
Operating profit (loss)	**64**	**1,084**	**513**	**1,222**	**(527)**	**2,356**
Share of post tax losses of associates and joint ventures						(11)
Profit on disposal of associate						9
Net finance expense						(378)
Profit before tax						1,976

[a] Restated. See pages 94 and 101.
[b] Adjusted revenue, adjusted EBITDA and adjusted operating profit (loss) are stated before specific items and BT Global Services contract and financial review charges in 2009 and are non-GAAP measures provided in addition to the disclosure requirements defined under IFRS. The rationale for using non-GAAP measures is explained on pages 54 to 56.

1. Segment information continued

Capital expenditure

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

Year ended 31 March 2009	BT Global Services £m	BT Retail £m	BT Wholesale £m	Openreach £m	Other £m	Total £m
Property, plant and equipment	576	386	310	823	154	2,249
Intangible assets	310	85	125	128	191	839
Capital expenditure	**886**	**471**	**435**	**951**	**345**	**3,088**

Revenue by products and services

Year ended 31 March	**2010** £m	2009 £m	2008 £m
Managed solutions	6,581	6,390	5,293
Broadband and convergence	2,678	2,617	2,549
Calls and lines	6,293	6,862	7,405
Transit, conveyance, interconnect services, WLR, global carrier and other wholesale products	2,957	3,244	3,327
Other products and services	2,402	2,318	2,130
Total adjusted revenue	**20,911**	**21,431**	**20,704**
Specific items	(52)	–	–
Contract and financial review charges	–	(41)	–
Total revenue	**20,859**	**21,390**	**20,704**

Geographic information

The UK is the group's country of domicile and 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	**2010** £m	2009 £m	2008 £m
UK	16,064	16,736	17,186
Europe, Middle East and Africa, excluding the UK	3,250	3,247	2,510
Americas	1,235	1,119	847
Asia Pacific	310	288	161
Total revenue	**20,859**	**21,390**	**20,704**

Non current assets

At 31 March	**2010** £m	2009 £m
UK	15,583	16,110
Europe, Middle East and Africa, excluding the UK	2,761	3,046
Americas	653	421
Asia Pacific	62	70
Total	**19,059**	**19,647**

Non current assets other than 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	**2010 £m**	2009 £m	2008 £m
Profits on disposal of property, plant and equipment	75	52	50
Income from repayment works	74	72	74
Other operating income	229	228	235
Other operating income before specific items	**378**	**352**	**359**
Specific items (note 5)	2	(13)	(10)
Other operating income	**380**	**339**	**349**

3. Operating costs

Year ended 31 March	Notes	**2010 £m**	2009[a] £m	2008[a] £m
Costs by nature				
Staff costs:				
Wages and salaries		4,182	4,499	4,242
Social security costs		447	432	417
Pension costs	29	304	544	626
Share-based payment expense	30	71	141	73
Total staff costs		**5,004**	**5,616**	**5,358**
Own work capitalised		(575)	(673)	(724)
Net staff costs		**4,429**	**4,943**	**4,634**
Depreciation of property, plant and equipment:				
Owned assets	13	2,260	2,200	2,324
Held under finance leases	13	44	49	86
Amortisation of intangible assets	12	735	641	479
Payments to telecommunications operators		4,083	4,266	4,237
Other operating costs[b]		7,138	8,934	6,408
Total operating costs before specific items		**18,689**	**21,033**	**18,168**
Specific items	5	427	395	529
Total operating costs		**19,116**	**21,428**	**18,697**
Operating costs before specific items include the following:				
Contract and financial review charges[e]		–	1,598	–
Leaver costs[c]		142	204	127
Research and development expenditure[d]		1,177	1,021	857
Rental costs relating to operating leases		451	426	423
Foreign currency losses		7	30	8

[a] Restated for the adoption of the amendment to IFRS 2. See page 94.
[b] Other operating costs also include a net charge of £1m (2009: £8m credit, 2008: £nil) relating to fair value movements on derivatives recycled from the cash flow reserve.
[c] Leaver costs exclude leaver costs associated with the restructuring of BT Global Services during 2010 and 2009 and manager leaver costs associated with the group's transformation and reorganisation activities during 2009 and 2008. These costs have been recorded as a specific item. Other leaver costs are included within wages and salaries and social security costs.
[d] Research and development expenditure includes amortisation of £733m (2009: £431m, 2008: £325m) in respect of internally developed computer software.
[e] In 2009, the group recognised contract and financial review charges of £1,639m, of which £1,598m was recognised within other operating costs and £41m was recognised as a reduction to revenue. The total charge of £1,639m was allocated against the following assets and liabilities: intangible assets £241m; non current trade and other receivables £913m; prepayments £52m; accrued income £41m; provisions £256m; £136m was allocated against a number of other balance sheet categories and the individual amounts were insignificant.

4. Employees

	2010		2009		2008	
	Year end 000	Average 000	Year end 000	Average 000	Year end 000	Average 000
Number of employees in the group[a]:						
UK	79.8	82.9	86.5	89.5	91.3	93.0
Non UK	18.0	18.8	20.5	21.1	20.6	15.5
Total employees	**97.8**	**101.7**	**107.0**	**110.6**	**111.9**	**108.5**

	2010		2009[b]		2008[b]	
	Year end 000	Average 000	Year end 000	Average 000	Year end 000	Average 000
Number of employees in the group[a]:						
BT Global Services	24.3	26.1	28.2	28.4	29.7	26.8
BT Retail	19.4	20.2	21.2	21.9	21.9	21.5
BT Wholesale	2.4	2.4	2.4	2.5	2.8	3.1
Openreach	30.8	31.4	32.3	33.1	33.6	33.8
Other	20.9	21.6	22.9	24.7	23.9	23.3
Total employees	**97.8**	**101.7**	**107.0**	**110.6**	**111.9**	**108.5**

a The numbers disclosed include both full and part-time employees.
b Restated for the impact of customer account moves and other internal trading model changes. See page 101.

5. Specific items

The group separately identifies and discloses significant one off or unusual items (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 87.

Year ended 31 March	**2010** £m	2009 £m	2008 £m
Revenue			
Regulatory settlement[a]	52	–	–
Other operating income			
(Profit) loss on disposal of a business[b]	(2)	13	10
Operating costs			
BT Global Services restructuring charges:			
– Networks, products and procurement channels rationalisation[c]	142	183	–
– People and property[c]	132	51	–
– Intangible asset impairments and other charges[c]	27	46	–
	301	280	–
Property rationalisation costs[d]	121	–	–
Costs associated with settlement of open tax years[e]	5	–	–
Restructuring costs – group transformation and reorganisation activities[f]	–	65	402
21CN asset impairment and related charges[g]	–	50	–
Creation of Openreach and delivery of the Undertakings[h]	–	–	53
Write off of circuit inventory and other working capital balances[i]	–	–	74
	427	**395**	**529**
Finance income			
Interest on settlement of open tax years[e]	(11)	–	–
Share of results of associates and joint ventures			
Impact of renegotiated supply contracts on associate[j]	(29)	–	–
Reassessment of carrying value of associate[k]	–	(36)	–
Loss (profit) on disposal of associates and joint ventures[l]	12	–	(9)
	(17)	**(36)**	**(9)**
Net specific items charge before tax	**449**	**372**	**530**
Tax credit in respect of settlement of open tax years[e]	(230)	–	(40)
Tax credit on re-measurement of deferred tax[m]	–	–	(154)
Tax credit on specific items above	(112)	(43)	(149)
Net specific items charge after tax	**107**	**329**	**187**

[a] In 2010 a charge of £52m was recognised reflecting an Ofcom determination in relation to 2Mb/s partial private circuits.
[b] In 2010 a profit of £2m arose on disposal of a business. In 2009 and 2008 respectively, a £13m and £10m loss on disposal arose from exiting businesses.
[c] In 2010 and 2009 respectively, the group recognised BT Global Services restructuring charges of £301m and £280m. The main components of the charges are set out below:
– Networks, products and procurement channels rationalisation charges of £142m (2009: £183m and 2008: £nil). 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 £132m (2009: £51m and 2008: £nil) principally comprising leaver costs and property exit costs.
– Intangible asset impairments and other charges of £27m (2009: £46m and 2008: £nil) reflecting the costs associated with rationalising the services that are offered to customers and the brands under which customers are served.
[d] In 2010 £121m (2009 and 2008: £nil) of property rationalisation charges were recognised in relation to the rationalisation of the group's UK property portfolio. The charge recognised relates to properties which have been vacated and as a result of which, the associated leases have become onerous. This programme is expected to continue over the next two years. Including the charge recognised in 2010, the total cost of the rationalisation programme is expected to be around £300m.
[e] In 2010 the group agreed substantially all outstanding tax matters with HMRC relating to the 2006, 2007 and 2008 tax years. Specific items include a tax credit of £230m, associated interest of £11m and costs of £5m in connection with reaching the agreement. In 2008 the group agreed an outstanding tax matter relating to a business disposed of in 2001, the impact of which was a tax credit of £40m.
[f] In 2009 and 2008 respectively, the group incurred costs of £65m and £402m in respect of the group's transformation and reorganisation activities. The costs mainly comprised leaver costs, property exit and transformation programme costs.
[g] In 2009 a £50m charge was recognised comprising £31m of asset impairments and £19m of associated costs, following the group's review of its 21CN programme and associated voice strategy in the light of the move to a customer-led roll out strategy and focus on next generation voice service developments of fibre-based products.
[h] In 2008 a charge of £53m was recognised in relation to further estimated costs to create Openreach and deliver the Undertakings agreed with Ofcom.
[i] In 2008 a charge of £74m was recognised as a result of the completion of a review of circuit inventory and other working capital balances.
[j] In 2010 the group recognised a specific item credit of £29m in connection with the £127m payment to its associate Tech Mahindra, as described above.
[k] In 2009 a credit of £36m was recognised in respect of a reassessment of the value of the group's share of the net assets of an associate.
[l] In 2010 a £12m loss on disposal of an indirect interest in Tech Mahindra was recognised. In 2008, a £9m profit on the sale of an associate was recognised.
[m] In 2008 a tax credit of £154m was recognised for the re-measurement of deferred tax balances as a result of the change in the UK statutory corporation tax rate from 30% to 28% effective in 2009.

6. Finance expense and finance income

Year ended 31 March	2010 £m	2009 £m	2008 £m
Finance expense			
Interest on listed bonds, debentures and notes[a,b]	806	777	629
Interest on finance leases[a]	18	25	31
Interest on other borrowings[a]	58	130	159
Unwinding of discount on provisions[a]	4	3	3
Fair value loss on derivatives not in a designated hedge relationship[e]	19	29	41
Interest on pension scheme liabilities	2,211	2,308	2,028
Finance expense[c,d]	3,116	3,272	2,891
Less: amounts included in the cost of qualifying assets[f]	(3)	–	–
Total finance expense	**3,113**	**3,272**	**2,891**

a Calculated using the effective interest rate method unless otherwise stated below.
b Includes a net charge of £44m (2009: £25m, 2008: £77m) relating to fair value movements on derivatives recycled from the cash flow reserve.
c Includes a net credit of £29m (2009: net charge of £39m, 2008: net credit of £6m) relating to fair value movements arising on hedged items and net charge of £29m (2009: net credit of £39m, 2008: net charge of £6m) relating to fair value movements arising on derivatives designated as fair value hedges.
d Includes a net credit of £451m (2009: net charge of £2,161m, 2008: net charge of £373m) relating to foreign exchange movements on loans and borrowings and a net charge of £451m (2009: net credit of £2,161m, 2008: net credit of £373m) relating to fair value movements on derivatives recycled from the cash flow reserve. The items generating this foreign exchange are in designated hedge relationships.
e Includes a loss of £nil (2009: £nil, 2008: £2m) recycled from the cash flow reserve arising on de-designation of derivatives from a hedge relationship and includes a charge of £9m arising from the negotiation of swap break dates on certain derivatives.
f The weighted average capitalisation rate on general borrowings was 7.9% in 2010.

Year ended 31 March	2010 £m	2009 £m	2008 £m
Finance income			
Other interest and similar income			
Interest on available-for-sale investments	5	14	25
Interest on loans and receivables	7	17	40
Other interest and similar income[a]	11	–	–
Expected return on pension scheme assets	1,932	2,621	2,448
Total finance income	**1,955**	**2,652**	**2,513**

a 2010 includes £11m relating to interest on settlement of tax matters disclosed as a specific item (see note 5).

Year ended 31 March	2010 £m	2009 £m	2008 £m
Net finance expense before specific items and pensions	890	933	798
Net interest expense (income) on pensions	279	(313)	(420)
Net finance expense before specific items	**1,169**	**620**	**378**
Specific items	(11)	–	–
Net finance expense	**1,158**	**620**	**378**

7. Dividends

Year ended 31 March	2010 pence per share	2010 £m	2009 pence per share	2009 £m	2008 pence per share	2008 £m
Final dividend paid in respect of the prior year	1.10	85	10.40	804	10.00	810
Interim dividend paid in respect of the current year	2.30	178	5.40	418	5.40	431
	3.40	**263**	**15.80**	**1,222**	**15.40**	**1,241**

The Board recommends that a final dividend in respect of the year ended 31 March 2010 of 4.6p per share will be paid to shareholders on 6 September 2010, taking the full year proposed dividend in respect of the 2010 financial year to 6.9p (2009: 6.5p, 2008: 15.8p) which amounts to approximately £534m (2009: £503m, 2008: £1,236m). This dividend is subject to approval by shareholders at the Annual General Meeting and therefore the liability of approximately £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 13 August 2010.

8. Taxation

Analysis of taxation (credit) expense for the year

Year ended 31 March	2010 £m	2009 £m	2008 £m
United Kingdom			
Corporation tax at 28% (2009: 28%, 2008: 30%)	161	–	214
Adjustments in respect of prior periods	(204)	(50)	18
Non UK taxation			
Current	31	48	42
Adjustments in respect of prior periods	–	(10)	(88)
Total current tax (credit) expense	**(12)**	**(12)**	**186**
Deferred tax			
Origination and reversal of temporary differences	53	(77)	78
Adjustments in respect of prior periods	(63)	36	(26)
Total deferred tax (credit) expense	**(10)**	**(41)**	**52**
Total taxation (credit) expense	**(22)**	**(53)**	**238**

Factors affecting taxation (credit) expense

The taxation (credit) expense 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:

	2010		2009[a]		2008[a]	
Year ended 31 March	£m	%	£m	%	£m	%
Profit (loss) before taxation	**1,007**		**(244)**		**1,976**	
Notional taxation expense (credit) at UK rate of 28% (2009: 28%, 2008: 30%)	282	28.0	(68)	28.0	592	30.0
Effects of:						
Non deductible depreciation and amortisation	18	1.7	27	(11.0)	23	1.1
Non deductible (taxable) non UK losses (profits)	26	2.6	(24)	9.8	(7)	(0.3)
Overseas losses utilised	(35)	(3.4)	–	–	–	–
Higher (lower) taxes on non UK profits	1	0.1	(9)	3.7	7	0.3
Higher (lower) taxes on gain on disposal of non current investments and group undertakings	–	–	4	(1.6)	–	–
Other deferred tax assets not recognised	17	1.6	5	(2.0)	(13)	(0.6)
Associates and joint ventures	(11)	(1.1)	(21)	8.6	(2)	(0.1)
Adjustments in respect of prior periods	(37)	(3.7)	(24)	9.8	(56)	(2.8)
Tax credit settlement of open tax years	(230)	(22.9)	–	–	(40)	(2.0)
Re-measurements of deferred tax balances at 28%	–	–	–	–	(154)	(7.8)
Adoption of the amendment to IFRS 2	–	–	30	(12.3)	–	–
Other	(53)	(5.1)	27	(11.1)	(112)	(5.8)
Total taxation (credit) expense and effective tax rate	**(22)**	**(2.2)**	**(53)**	**21.9**	**238**	**12.0**
Specific items	342		43		343	
Total taxation (credit) expense before specific items and effective rate on profit before specific items	**320**	**22.0**	**(10)**	**(7.8)**	**581**	**23.2**

[a] Restated. See page 94.

8. Taxation continued

Tax components of other comprehensive income

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

Year ended 31 March	2010 Before tax £m	2010 Tax credit (expense) £m	2010 After tax £m	2009 Before tax £m	2009 Tax credit (expense) £m	2009 After tax £m	2008 Before tax £m	2008 Tax credit (expense) £m	2008 After tax £m
Actuarial (losses) gains relating to retirement benefit obligations	(4,324)	1,211	(3,113)	(7,037)	1,959	(5,078)	2,621	(804)	1,817
Exchange differences on translation of foreign operations	(119)	(20)	(139)	692	64	756	213	1	214
Fair value movements on available-for-sale assets	7	–	7	5	–	5	–	–	–
Fair value movements on cash flow hedges									
– fair value gains (losses)	(1,067)	297	(770)	2,719	(766)	1,953	446	(108)	338
– reclassified and reported in net (loss)profit	496	(139)	357	(2,144)	600	(1,544)	(294)	82	(212)
– reclassified and reported in non current assets	(4)	1	(3)	(5)	2	(3)	11	(3)	8
	(5,011)	**1,350**	**(3,661)**	(5,770)	1,859	(3,911)	2,997	(832)	2,165
Current tax (expense) credit		(2)			–			2	
Deferred tax credit (expense)		1,352			1,859			(834)	
		1,350			1,859			(832)	

Tax on items recognised directly in equity

Year ended 31 March	2010 £m	2009 £m	2008 £m
Current tax credit relating to share-based payments	–	–	17
Deferred tax credit (expense) relating to share-based payments	19	(12)	(62)
Total taxation credit (expense) on items recognised directly in equity	**19**	**(12)**	**(45)**

9. 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 ordinary shares have been taken into account where the impact of these is dilutive. Options over 138m shares (2009: 158m shares, 2008: 58m shares) were excluded from the calculation of the total diluted number of shares as the impact of these is antidilutive.

The weighted average number of shares in the years was:

Year ended 31 March	2010 millions of shares	2009[a] millions of shares	2008[a] millions of shares
Basic	**7,740**	**7,724**	**8,066**
Dilutive ordinary shares from share options	174	5	106
Dilutive ordinary shares held in trust	74	42	51
Diluted	**7,988**	**7,771**	**8,223**
Profit (loss) attributable to equity shareholders of the parent (£m)	**1,028**	(193)	1,737
Basic earnings (loss) per share (p)	**13.3p**	(2.5)p	21.5p
Diluted earnings (loss) per share (p)	**12.9p**	(2.5)p	21.1p

[a] Restated. See page 94.

9. Earnings (loss) per share continued

Adjusted basic and diluted earnings (loss) per share, and the per share impact of the adjustments, is as follows:

Year ended 31 March	2010 pence per share	2010 £m	2009[a] pence per share	2009[a] £m	2008[a] pence per share	2008[a] £m
Basic earnings (loss) per share/profit (loss)[b]	**13.3**	**1,028**	**(2.5)**	**(193)**	**21.5**	**1,737**
Net specific items charge after tax	1.4	107	4.3	329	2.4	187
Net pension interest expense (income) after tax	2.6	201	(3.0)	(225)	(3.7)	(294)
BT Global Services contract and financial review charges after tax	–	–	15.3	1,178	–	–
Adjusted basic earnings (loss)per share/profit (loss) attributable to adjustments[b]	4.0	308	16.6	1,282	(1.3)	(107)
Adjusted basic earnings per share/profit[b]	**17.3**	**1,336**	**14.1**	**1,089**	**20.2**	**1,630**
Diluted earnings (loss) per share/profit (loss)[b]	**12.9**	**1,028**	**(2.5)**	**(193)**	**21.1**	**1,737**
Adjusted diluted earnings (loss) per share/profit (loss)attributable to adjustments[b]	3.9	308	16.5	1,282	(1.3)	(107)
Adjusted diluted earnings per share/profit[b]	**16.8**	**1,336**	**14.0**	**1,089**	**19.8**	**1,630**

a Restated. See page 94.
b The stated profit (loss) amounts are the component of the total profit (loss) which is attributable to equity shareholders excluding minority interests.

10. Cash and cash equivalents

At 31 March	2010 £m	2009 £m
Cash at bank and in hand	**197**	**562**
Cash equivalents		
Available-for-sale		
Listed	–	7
Loans and receivables		
UK deposits	1,211	711
European deposits	7	5
US deposits	37	15
Total cash equivalents	**1,255**	**738**
Total cash and cash equivalents	**1,452**	**1,300**
Bank overdrafts	(8)	(185)
Cash and cash equivalents per the cash flow statement	**1,444**	**1,115**

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. Included within overdrafts at 31 March 2010 were balances of £nil (2009: £160m) which had a legally enforceable right of set off against cash balances of £nil (2009: £96m).

The group's cash at bank included restricted cash of £54m (2009: £52m), of which £29m (2009: £27m) 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 £25m (2009: £25m) were held in escrow accounts.

10. Cash and cash equivalents continued

The credit rating of counterparties with which cash equivalents were held is detailed in the table below.

At 31 March	2010 £m	2009 £m
Moody's/S&P credit rating[a]		
Aaa/AAA	100	90
Aa2/AA	609	124
Aa3/AA–	202	271
A1/A+	341	251
A2/A	3	2
Total cash equivalents	**1,255**	**738**

[a] Cash equivalent balances with counterparties have been classified at the lower of their Moody's and S&P rating.

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

11. Net debt

Net debt consists of loans and other borrowings 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 analysis, 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.

This definition of net debt measures balances at the expected value of future undiscounted cash flows due to arise on maturity of financial instruments and removes the adjustments made for the re-measurement of hedged risks under fair value hedges and accrued interest applied to reflect the effective interest method as required by IAS 39. In addition, the gross balances are adjusted to take account of netting arrangements amounting to £nil (2009: £160m). Net debt is a non-GAAP measure since it is not defined in accordance with IFRS, but it is a key indicator used by management in order to assess operational performance and balance sheet strength.

Analysis of net debt	2010 £m	2009 £m
Loans and other borrowings (current and non current)	12,791	13,907
Less:		
Cash and cash equivalents	(1,452)	(1,300)
Current asset investments	(406)	(163)
	10,933	12,444
Adjustments:		
To retranslate currency denominated balances at swapped rates where hedged	(1,326)	(1,766)
To remove fair value adjustments and accrued interest applied to reflect the effective interest method	(324)	(317)
Net debt at 31 March	**9,283**	**10,361**

After allocating the element of the adjustments which impacts loans and other borrowings, as defined above, gross debt at 31 March 2010 was £11,139m (2009: £11,663m).

Reconciliation of movement in net debt	2010 £m	2009 £m
At 1 April	10,361	9,460
(Decrease) increase in net debt resulting from cash flows	(1,079)	921
Net debt assumed or issued on acquisitions	–	(2)
Currency movements	–	(36)
Other non cash movements	1	18
At 31 March	**9,283**	**10,361**

12. Intangible assets

	Goodwill £m	Telecommunication licences and other £m	Brands, customer relationships and technology £m	Internally developed software £m	Computer software £m	Total £m
Cost						
At 1 April 2008	1,088	266	248	1,896	1,281	4,779
Additions	–	–	–	712	127	839
Acquisitions through business combinations	131	–	46	–	–	177
Disposals and adjustments	1	(3)	20	(225)	(12)	(219)
Impairments[a]	–	–	(26)	(48)	(261)	(335)
Exchange differences	269	44	88	13	69	483
At 1 April 2009	**1,489**	**307**	**376**	**2,348**	**1,204**	**5,724**
Additions	–	–	–	585	44	629
Acquisitions through business combinations[c]	1	–	–	–	–	1
Interest on qualifying assets[b]	–	–	–	2	–	2
Disposals and adjustments	(2)	(6)	(3)	(362)	9	(364)
Exchange differences	(56)	(11)	(16)	(5)	(16)	(104)
At 31 March 2010	**1,432**	**290**	**357**	**2,568**	**1,241**	**5,888**
Amortisation						
At 1 April 2008		121	67	520	716	1,424
Charge for the year		14	62	433	132	641
Disposals and adjustments		(1)	–	(225)	(9)	(235)
Exchange differences		22	24	11	49	106
At 1 April 2009		**156**	**153**	**739**	**888**	**1,936**
Charge for the year		15	54	559	107	735
Disposals and adjustments		(4)	(1)	(366)	(53)	(424)
Exchange differences		(5)	(9)	(5)	(12)	(31)
At 31 March 2010		**162**	**197**	**927**	**930**	**2,216**
Carrying amount						
At 31 March 2010	**1,432**	**128**	**160**	**1,641**	**311**	**3,672**
At 31 March 2009	**1,489**	**151**	**223**	**1,609**	**316**	**3,788**

a Impairment charges of £335m were recognised in 2009, comprising BT Global Services restructuring charges of £81m, BT Global Services contract and financial review charges of £241m (see note 3) and £13m in relation to the review of the 21CN programme and associated voice strategy. All impairment losses were recognised in the income statement. The recoverable amount of the impaired assets was equal to their value in use.
b Additions to internally generated software in 2010 includes interest capitalised at a weighted average borrowing rate of 7.9%.
c Additional earnout payment in respect of investment in BT Leasing Limited.

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 the following business units within BT Retail: 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 2008	936	47	34	16	55	1,088
Acquisitions through business combinations	37	10	10	–	74	131
Disposals, adjustments and reclassifications	1	–	–	–	–	1
Exchange differences	252	–	–	–	17	269
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)
At 31 March 2010	**1,172**	**65**	**61**	**21**	**113**	**1,432**

12. Intangible assets continued

The key assumptions used in performing value in use calculations in 2010 are 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%

The key assumptions used in performing the value in use calculations in 2009 were as follows:

	BT Global Services	BT Retail			
		BT Consumer	BT Business	BT Ireland	BT Enterprises
Discount rate	11.1%	11.1%	11.1%	11.1%	11.1%
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 margins, 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 £725m. 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 0.5% or less
- an increase in the discount rate from the 10.8% assumption applied to a revised assumption of 12.2% or more
- a reduction in the projected operating cash flows across five years by 15% or more.

13. Property, plant and equipment

	Land and buildings[a,b] £m	Network infrastructure equipment[b] £m	Other[c] £m	Assets in course of construction £m	Total £m
Cost					
At 1 April 2008	1,209	39,117	2,194	1,240	43,760
Additions	8	238	187	1,813	2,246
Acquisition through business combinations	–	–	2	–	2
Transfers	16	2,045	19	(2,080)	–
Disposals and adjustments	3	(373)	(169)	(71)	(610)
Impairments[d]	–	(121)	(8)	(18)	(147)
Exchange differences	58	652	149	26	885
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[e]	–	–	–	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)
At 31 March 2010	**1,379**	**42,080**	**2,151**	**807**	**46,417**
Accumulated depreciation					
At 1 April 2008	500	26,404	1,574	–	28,478
Charge for the year	56	1,928	265	–	2,249
Disposals and adjustments	4	(395)	(209)	–	(600)
Exchange differences	30	476	126	–	632
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)
At 31 March 2010	**725**	**29,201**	**1,706**	**–**	**31,632**
Carrying amount					
At 31 March 2010	**654**	**12,879**	**445**	**807**	**14,785**
Engineering stores	–	–	–	71	71
Total at 31 March 2010	**654**	**12,879**	**445**	**878**	**14,856**
At 31 March 2009	704	13,145	618	910	15,377
Engineering stores	–	–	–	28	28
Total at 31 March 2009	**704**	**13,145**	**618**	**938**	**15,405**

	2010 £m	2009 £m
[a] The carrying amount of land and buildings, including leasehold improvements, comprised:		
Freehold	431	451
Long leases (over 50 years unexpired)	33	30
Short leases	190	223
Total land and buildings	**654**	**704**

[b] The carrying amount of the group's property, plant and equipment includes an amount of £183m (2009: £216m) in respect of assets held under finance leases, comprising land and buildings of £74m (2009: £76m) and network infrastructure and equipment of £109m (2009: £140m). The depreciation charge on those assets for 2010 was £44m (2009: £49m), comprising land and buildings of £3m (2009: £3m) and network infrastructure and equipment of £41m (2009: £46m).
[c] Other mainly comprises motor vehicles and computers.
[d] Impairment charges of £147m were recognised in 2009, comprising BT Global Services restructuring charges of £129m and £18m in relation to the review of the 21CN programme and associated voice strategy. All impairment losses were recognised in the income statement. The recoverable amount of the impaired assets was equal to their value in use.
[e] Additions to assets in the course of construction in 2010 includes interest capitalised at a weighted average borrowing rate of 7.9%.

13. Property, plant and equipment continued

Year ended 31 March	**2010** **£m**	2009 £m
Additions to property, plant and equipment comprised:		
Land and buildings	29	23
Network infrastructure and equipment		
Transmission equipment	902	1,067
Exchange equipment	29	44
Other network equipment	753	899
Other		
Computers and office equipment	115	140
Motor vehicles and other	33	73
Total additions to property, plant and equipment	**1,861**	**2,246**
Increase in engineering stores	43	3
Total additions	**1,904**	**2,249**

14. Investments

At 31 March	**2010** **£m**	2009 £m
Non current assets		
Available-for-sale	32	23
Loans and receivables	32	32
	64	**55**
Current assets		
Available-for-sale	258	153
Loans and receivables	148	10
	406	**163**

The credit rating of counterparties with which current asset investments were held is detailed in the table below.

At 31 March	**2010** **£m**	2009 £m
Moody's/S&P credit rating[a]		
Aaa/AAA	258	153
Aa3/AA-	35	–
A1/A+	105	10
A2/A	8	–
Total current asset investments	**406**	**163**

[a] Current asset investment balances with counterparties have been classified at the lower of their Moody's and S&P rating.

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 floating rate liquidity fund deposits denominated in Sterling of £185m (2009: £97m), Euros of £56m (2009: £43m) and US Dollars of £17m (2009: £13m) which are immediately accessible to the group to manage liquidity.

Loans and receivables

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

15. Associates and joint ventures

	2010			2009		
	Associates £m	Joint ventures £m	Total £m	Associates £m	Joint ventures £m	Total £m
Non current assets	49	7	56	41	7	48
Current assets	278	4	282	168	4	172
Current liabilities	(77)	(2)	(79)	(86)	(2)	(88)
Non current liabilities	(64)	–	(64)	–	–	–
Share of net assets at 31 March	**186**	**9**	**195**	**123**	**9**	**132**
Revenue	298	14	312	308	15	323
Expenses	(266)	(14)	(280)	(262)	(15)	(277)
Taxation	(7)	–	(7)	(7)	–	(7)
Share of post tax results before specific items	**25**	**–**	**25**	**39**	**–**	**39**
Specific items (note 5)						
– impact of renegotiated supply contracts on associate	29	–	29	–	–	–
– reassessment of carrying value of associate	–	–	–	36	–	36
Share of post tax results	**54**	**–**	**54**	**75**	**–**	**75**

	Associates £m	Joint ventures £m	Total £m
At 1 April 2008	79	6	85
Share of post tax profit	75	–	75
Dividends received	(6)	–	(6)
Exchange differences and other	(25)	3	(22)
At 1 April 2009	**123**	**9**	**132**
Share of post tax profit	54	–	54
Additions	3	–	3
Disposals (note 5)	(12)	–	(12)
Dividends received	(3)	–	(3)
Exchange differences and other	21	–	21
At 31 March 2010	**186**	**9**	**195**

At 31 March 2010 the fair value of the group's investments in associates and joint ventures for which published price quotations are available was £473m (2009: £153m). Details of the group's principal associate at 31 March 2010 are set out on page 149.

16. Inventories

At 31 March	2010 £m	2009 £m
Consumables	30	23
Work in progress	43	57
Finished goods	34	41
	107	**121**

17. Trade and other receivables

At 31 March	**2010** £m	2009 £m
Current		
Trade receivables	1,937	1,966
Prepayments	549	825
Accrued income	1,010	1,135
Other receivables	200	259
	3,696	**4,185**

	2010 £m	2009 £m
Non current		
Other assets[a]	**336**	**322**

[a] Other assets mainly represents costs relating to the initial set up, transition or transformation phase of long-term networked IT services contracts. At 31 March 2010 the balance was £294m (2009: £322m). Other assets also include prepayments of £42m (2009: £nil).

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

	2010 £m	2009 £m
At 1 April	246	209
Expense recognised in the income statement	155	151
Utilised in the year	(183)	(139)
Acquisitions	–	4
Exchange differences	1	21
At 31 March	**219**	**246**

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:

			Past due and not specifically impaired:				
	Not past due £m	Trade receivables specifically impaired net of provision £m	Between 0 and 3 months £m	Between 3 and 6 months £m	Between 6 and 12 months £m	Over 12 months £m	Total £m
2010	**1,257**	**51**	**426**	**98**	**60**	**45**	**1,937**
2009	1,263	1	474	90	65	73	1,966

Gross trade receivables which have been specifically impaired amounted to £230m (2009: £30m).

17. Trade and other receivables continued

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	**2010** £m	2009 £m
BT Global Services	867	878
BT Retail	228	308
BT Wholesale	127	64
Openreach	27	3
Other	8	10
Total trade receivables not past due	**1,257**	**1,263**

At 31 March	**2010** £m	2009 £m
BT Global Services	633	635
BT Retail	148	274
BT Wholesale	182	195
Openreach	44	26
Other	3	5
Total accrued income	**1,010**	**1,135**

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 £25m (2009: £23m).

18. Loans and other borrowings

At 31 March	2010 £m	2009 £m
Sterling 6.375% bonds June 2037[b]	521	521
US Dollar 9.625% (2009: 9.125%) notes December 2030 (minimum 8.625%[a])[b]	1,811	1,914
Sterling 5.75% bonds December 2028[c]	602	608
Sterling 3.5% indexed linked notes April 2025	325	330
Sterling 8.625% bonds March 2020	298	298
US Dollar 5.95% bonds January 2018[b]	734	777
Sterling 6.625% bonds June 2017[b]	525	524
Sterling 8.5% (2009: 8.0%) notes December 2016 (minimum 7.5%[a])	715	713
Euro 6.5% bonds July 2015[b]	935	973
Euro 6.125% bonds July 2014[b,f]	561	–
Euro 5.25% bonds June 2014[b]	696	723
Euro 5.25% bonds January 2013[b]	902	935
US Dollar 5.15% bonds January 2013[b]	566	599
Euro 7.87% (2009: 7.375%) notes February 2011 (minimum 6.875%[a])[b]	1,015	1,051
US Dollar 9.125% (2009: 8.625%) notes December 2010 (minimum 8.125%[a])[b]	1,951	2,074
US Dollar 8.765% bonds August 2009[d]	–	149
Total listed bonds, debentures and notes	**12,157**	**12,189**
Finance leases	**304**	**332**
Commercial paper[b,e]	–	715
Sterling 6.35% bank loan due August 2012	312	312
Sterling 10.4% bank loan due September 2009	–	140
Sterling floating rate note 2009-2010	–	28
Other loans 2009-2012	10	6
Bank overdrafts (of which £nil (2009: £160m) had a legally enforceable right of set off – see note 10)	8	185
Total other loans and borrowings	**330**	**1,386**
Total loans and other borrowings	**12,791**	**13,907**

a The interest rate payable on these notes will be subject to adjustment from time to time if either Moody's or Standard and 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 rate payable on the notes and the spread applicable to the floating notes will be increased by 0.25% for each ratings category adjustment by each rating 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 then payable on notes and the spread applicable to the floating notes 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– as detailed on page 138. At the next coupon date in the 2011 financial year, the rate payable on these bonds will therefore increase by 0.25 percentage points.
b Hedged in a designated cash flow hedge.
c Hedged in a designated fair value hedge.
d Hedged in a designated cash flow and fair value hedge.
e Commercial paper is denominated in Sterling of £nil (2009: £209m) and Euros of £nil (2009: £506m).
f The group's €600m bond issued in June 2009 would attract an additional 1.25 percentage points for a downgrade by one credit rating category by both Moody's and S&P below Baa3/BBB– respectively.

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 deferred and current fair value adjustments to the relevant loans or borrowings' hedged risk in a fair value hedge. 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 2010 and 2009 were unsecured.

	2010			2009		
At 31 March	Carrying amount £m	Effect of hedging and interest[a] £m	Principal repayments at hedged rates £m	Carrying amount £m	Effect of hedging and interest[a] £m	Principal repayments at hedged rates £m
Repayments fall due as follows:						
Within one year, or on demand	**3,269**	**(737)**	**2,532**	**1,542**	**(352)**	**1,190**
Between one and two years	18	–	18	3,098	(551)	2,547
Between two and three years	1,763	(313)	1,450	10	–	10
Between three and four years	11	–	11	1,829	(380)	1,449
Between four and five years	1,213	(177)	1,036	14	–	14
After five years	6,523	(431)	6,092	7,412	(799)	6,613
Total due for repayment after more than one year	**9,528**	**(921)**	**8,607**	**12,363**	**(1,730)**	**10,633**
Total repayments	**12,797**	**(1,658)**	**11,139**	**13,905**	**(2,082)**	**11,823**
Fair value adjustments for hedged risk	(6)			2		
Total loans and other borrowings	**12,791**			**13,907**		

a 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.

18. Loans and other borrowings continued

As noted on page 119, the principal repayments of loans and borrowings at hedged rates amounted to £11,139m (2009: £11,823m). 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.

			2010			2009
At 31 March	Fixed rate interest £m	Floating rate interest £m	Total £m	Fixed rate interest £m	Floating rate interest £m	Total £m
Sterling	10,110	835	10,945	10,239	1,373	11,612
Euro	–	184	184	–	204	204
US Dollar	–	3	3	–	2	2
Other	–	7	7	–	5	5
Total	**10,110**	**1,029**	**11,139**	**10,239**	**1,584**	**11,823**
Weighted average effective fixed interest rate						
Sterling	8.0%			8.1%		

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.

	2010	2009	**2010**	2009
	Minimum lease payments		Repayment of outstanding lease obligations	
At 31 March	£m	£m	£m	£m
Amounts payable under finance leases:				
Within one year	33	32	16	14
In the second to fifth years inclusive	119	135	48	66
After five years	422	456	240	252
	574	**623**	**304**	**332**
Less: future finance charges	(270)	(291)	–	–
Total finance lease obligations	**304**	**332**	**304**	**332**

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.

19. Derivative financial instruments

		2010		2009[a]		2008[a]
At 31 March	Assets £m	Liabilities £m	Assets £m	Liabilities £m	Assets £m	Liabilities £m
Interest rate swaps – cash flow hedge	–	361	–	446	1	207
Interest rate swaps – fair value hedge	–	6	–	–	–	–
Other interest rate swaps	106	295	107	316	25	239
Cross currency swaps – cash flow hedge	1,571	30	2,541	1	340	605
Cross currency swaps – fair value hedge	–	–	18	–	–	20
Other cross currency swaps	–	1	–	–	–	–
Forward foreign exchange contracts – cash flow hedge	23	4	27	1	20	1
Other forward foreign exchange contracts	–	2	7	2	1	–
Credit default swaps	–	–	–	1	–	–
	1,700	699	2,700	767	387	1,072
Analysed as:						
Current	624	166	158	56	71	58
Non current	1,076	533	2,542	711	316	1,014
	1,700	**699**	**2,700**	**767**	**387**	**1,072**

[a] Restated. See page 94.

19. Derivative financial instruments continued

The credit rating of counterparties with which derivative financial assets were held is detailed in the table below.

At 31 March	**2010** £m	2009 £m
Moody's/S&P credit rating[a]		
Aa2/AA	89	200
Aa3/AA–	480	650
A1/A+	708	1,030
A2/A	318	719
A3/A–	105	101
	1,700	**2,700**

[a] Derivative financial instrument balances with counterparties have been classified at the lower of their Moody's and S&P rating.

In 2010 derivative financial assets were held with 18 counterparties (2009: 19 counterparties). After applying the legal right of set off under the group's International Swaps and Derivative Association (ISDA) documentation, the group had a net exposure to derivative counterparties of £1,303m (2009: £2,282m). Of this, 85% (2009: 85%) was with 6 counterparties (2009: 6). Details of hedges in which the derivative financial instruments are utilised are disclosed in note 32.

20. Trade and other payables

At 31 March	**2010** £m	2009 £m
Current		
Trade payables	3,668	4,367
Other taxation and social security	516	489
Other payables	506	527
Accrued expenses	498	460
Deferred income	1,343	1,372
	6,531	**7,215**

At 31 March	**2010** £m	2009 £m
Non current		
Other payables	734	718
Deferred income	70	76
	804	**794**

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

21. Provisions

	BT Global Services provisions[a] £m	Property provisions[b] £m	Other provisions[c] £m	Total £m
At 1 April 2009	303	172	245	720
Charged to the income statement[d]	10	131	204	345
Unwind of discount	–	4	–	4
Utilised in the year	(139)	(35)	(98)	(272)
Transfers	16	–	31	47
Exchange differences	(3)	–	–	(3)
At 31 March 2010	**187**	**272**	**382**	**841**

At 31 March	**2010** £m	2009 £m
Analysed as:		
Current	134	254
Non current	707	466
	841	**720**

[a] Amounts provided in relation to the BT Global Services restructuring programme and the contract and the financial reviews in 2009. These will be utilised as the obligations are settled.
[b] 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 22 years. Financial liabilities comprise £255m (2009: £166m) of this balance.
[c] Other provisions includes:
– Amounts provided for incremental and directly attributable costs arising from the group's obligation to deliver the Undertakings, which will be utilised within one year.
– Amounts provided for legal or constructive obligations arising from insurance claims, litigation and regulatory risk, which will be utilised as the obligations are settled.
[d] Includes specific items of £121m for property rationalisation costs and £10m relating to the BT Global Services restructuring programme.

22. Deferred taxation

	Excess capital allowances £m	Retirement benefit obligations[a] £m	Share-based payments £m	Other £m	Total £m
At 1 April 2008	1,969	778	(51)	(183)	2,513
(Credit) expense recognised in the income statement	(158)	78	32	7	(41)
(Credit) expense recognised in equity	–	(1,959)	12	100	(1,847)
At 31 March 2009	1,811	(1,103)	(7)	(76)	625
Deferred tax asset	–	(1,103)	–	–	(1,103)
Deferred tax liability	1,811	–	(7)	(76)	1,728
At 1 April 2009	1,811	(1,103)	(7)	(76)	625
(Credit) expense recognised in the income statement	(115)	118	(15)	2	(10)
(Credit) expense recognised in equity	–	(1,211)	(19)	(143)	(1,373)
Transfer from current tax	–	–	–	18	18
At 31 March 2010	**1,696**	**(2,196)**	**(41)**	**(199)**	**(740)**
Deferred tax asset	–	(2,196)	–	–	(2,196)
Deferred tax liability	1,696	–	(41)	(199)	1,456
At 31 March 2010	**1,696**	**(2,196)**	**(41)**	**(199)**	**(740)**

[a] Includes a deferred tax asset of £3m (2009: £nil) arising on contributions payable to defined contribution schemes.

At 31 March 2010, all of the deferred tax asset of £2,196m (2009: £1,103m) is expected to be recovered after more than one year. At 31 March 2010, all of the deferred tax liability of £1,456m (2009: £1,728m) is expected to be settled after more than one year.

22. Deferred taxation continued

At 31 March 2010 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 £29.5bn (2009: £24.3bn). 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	2010 £m	Expiry of losses
Restricted losses:		
Americas	284	2010-2029
Europe	1,719	2010-2025
Total restricted losses	**2,003**	
Unrestricted losses:		
Operating losses	3,278	No expiry
Capital losses	23,439	No expiry
Other	775	No expiry
Total unrestricted losses	**27,492**	
Total	**29,495**	

At 31 March 2010, the undistributed earnings of overseas subsidiaries was £5.5bn (2009: £10.1bn). 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.

23. Minority interests

	2010 £m	2009 £m
At 1 April	27	23
Share of profits	1	2
Disposals	(4)	(9)
Minority share of dividend paid	–	(1)
Acquisitions through business combinations	–	3
Exchange differences	–	9
At 31 March	**24**	27

24. Share capital

	Number of shares	Share capital[a] £m	Share premium[b] £m
At 1 April 2008	8,401,227,029	420	62
Cancelled[c]	(250,000,000)	(12)	–
At 1 April 2009 and 31 March 2010	**8,151,227,029**	**408**	**62**

[a] The authorised share capital of the company up to 1 October 2009 was £13,463m, representing 269,260,253,468 ordinary shares of 5p each. The allotted, called up and fully paid ordinary share capital of the company at 31 March 2010 and 31 March 2009 was £408m, representing 8,151,227,029 ordinary shares of 5p each.
[b] The share premium account, representing the premium on allotment of shares, is not available for distribution.
[c] In 2010 the group cancelled nil treasury shares (2009: 250,000,000) with a nominal value of £nil (2009: £12m).

25. Other reserves

	Treasury shares[a] £m	Cash flow reserve[b] £m	Available-for-sale reserve[c] £m	Translation reserve[d] £m	Merger reserve[e] £m	Total other reserves £m
At 1 April 2007	(884)	23	–	(49)	998	88
Exchange differences	–	–	–	210	–	210
Net fair value gain on cash flow hedges	–	446	–	–	–	446
Recognised in income and expense in the year	–	(294)	–	–	–	(294)
Reclassified and reported in non current assets	–	11	–	–	–	11
Tax recognised in other comprehensive income	–	(29)	–	–	–	(29)
Net purchase of treasury shares	(1,529)	–	–	–	–	(1,529)
Cancellation of treasury shares	570	–	–	–	–	570
At 1 April 2008	(1,843)	157	–	161	998	(527)
Exchange differences	–	–	–	683	–	683
Net fair value gain on cash flow hedges	–	2,719	–	–	–	2,719
Recognised in income and expense in the year	–	(2,144)	–	–	–	(2,144)
Reclassified and reported in non current assets	–	(5)	–	–	–	(5)
Gains on available-for-sale investments	–	–	5	–	–	5
Tax recognised in other comprehensive income	–	(164)	–	–	–	(164)
Net purchase of treasury shares	(63)	–	–	–	–	(63)
Cancellation of treasury shares	797	–	–	–	–	797
At 1 April 2009	(1,109)	563	5	844	998	1,301
Exchange differences	–	–	–	(119)	–	(119)
Net fair value loss on cash flow hedges	–	(1,067)	–	–	–	(1,067)
Recognised in income and expense in the year	–	496	–	–	–	496
Reclassified and reported in non current assets	–	(4)	–	–	–	(4)
Gains on available-for-sale investments	–	–	7	–	–	7
Tax recognised in other comprehensive income	–	159	–	(20)	–	139
Net issue of treasury shares	4	–	–	–	–	4
At 31 March 2010	**(1,105)**	**147**	**12**	**705**	**998**	**757**

a The treasury shares reserve is used to hold BT Group plc shares purchased by the group. During 2010 the company purchased nil (2009: 142,608,225, 2008: 539,657,691) of its own shares of 5p each, representing nil% (2009: 2%, 2008: 6%) of the called-up share capital, for consideration (including transaction costs) of £nil (2009: £189m, 2008: £1,626m). In addition, 8,320,766 shares (2009: 90,626,518, 2008: 53,250,144) were issued from treasury to satisfy obligations under employee share schemes and executive share awards at a cost of £4m (2009: £126m, 2008: £97m), and nil treasury shares (2009 and 2008: 250,000,000) were cancelled at a cost of £nil (2009: £797m, 2008: £570m). At 31 March 2010, 400,906,119 shares (2009: 409,226,885, 2008: 607,285,178) with an aggregate nominal value of £20m (2009: £20m, 2008: £30m) were held as treasury shares at cost.
b 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.
c 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. The gross gain in the year amounted to £7m (2009: £5m, 2008: £nil).
d 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.
e 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.

26. 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	**2010** £m	2009[a] £m	2008[a] £m
Salaries and short-term benefits	10.3	8.4	8.3
Termination benefits	0.1	2.4	–
Post employment benefits	1.8	2.3	1.0
Share-based payments	2.6	3.6	5.0
	14.8	**16.7**	**14.3**

a Restated to include the Chairman and non-executive directors.

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 (pages 73 to 77), which forms part of the consolidated financial statements.

Amounts paid to the group's retirement benefit plans are set out in note 29. 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 2010, 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 £301m (2009: £296m, 2008: £305m) and the amount outstanding and payable for services at 31 March 2010 was £65m (2009: £89m, 2008: £125m). In addition 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. In 2008, a cash payment of £55m was received from Tech Mahindra Limited, which was recognised as income in 2008 (£28m) and 2009 (£27m).

27. Financial commitments and contingent liabilities

Capital expenditure contracted for at the balance sheet date but not yet incurred was as follows:	2010 £m	2009 £m
Property, plant and equipment	368	414
Computer software	15	37
Total	**383**	**451**

Future minimum operating lease payments for the group were as follows:	2010 £m	2009 £m
Payable in the year ending 31 March:		
2010	–	484
2011	494	455
2012	460	430
2013	431	403
2014	400	377
2015	375	356
Thereafter	5,527	5,499
Total future minimum operating lease payments	**7,687**	**8,004**

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 22 years (2009: 23 years) and rentals are fixed for an average of 22 years (2009: 23 years).

At 31 March 2010, 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 O_2 UK Limited prior to its demerger with O_2 on 19 November 2001. O_2 plc has given BT a counter indemnity for these guarantees. The maximum exposure was US$132m as at 31 March 2010 (2009: US$110m), approximately £87m (2009: £77m), although this could increase by a further US$304m (2009: US$399m), approximately £200m (2009: £278m), in the event of credit default in respect of amounts used to defease future lease obligations. The guarantee lasts until O_2 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 current court action that would have a material adverse effect on the financial position or operations of the group. However the aggregate volume and value of legal actions to which the group is party has increased significantly during 2010.

There have been criminal proceedings in Italy against 21 defendants, including a former BT employee, in connection with the Italian UMTS (universal mobile telecommunication system) auction in 2000. Blu, in which BT held a minority interest, participated in that auction process. On 20 July 2005, the former BT employee was found not culpable of the fraud charge brought by the Rome Public Prosecutor. All the other defendants were also acquitted. The Public Prosecutor has appealed the court's decision. The appeal was unsuccessful and no damages follow.

The European Commission formally investigated the way the UK Government set the rates payable on BT's infrastructure and those paid by Kingston Communications, and whether or not the UK Government complied with European Community Treaty rules on state aid. The Commission concluded in October 2006 that no state aid had been granted. The Commission's decision was appealed. Judgement on the appeal has not yet been given but we continue to believe that any allegation of state aid is groundless and that the appeal will not succeed.

28. Acquisitions

There were no acquisitions made in 2010. A summary of the acquisitions made in 2009 is set out below.

Year ended 31 March 2009	BT Global Services £m	BT Retail £m	Other £m	Total £m
Fair value of consideration	13	98	75	186
Less: fair value of net assets acquired	3	24	28	55
Goodwill arising	**10**	**74**	**47**	**131**
Consideration:				
Cash	13	98	65	176
Deferred consideration	–	–	10	10
Total	**13**	**98**	**75**	**186**
The outflow of cash and cash equivalents was as follows:				
Cash consideration	13	98	65	176
Less: cash acquired	1	3	5	9
	12	**95**	**60**	**167**

BT Global Services

During 2009 the group acquired 100% of Stemmer GmbH and SND GmbH. The purchase consideration was £13m. The net assets acquired and the goodwill arising were as follows:

	Book value £m	Fair value adjustments £m	Fair value £m
Receivables	6	–	6
Cash and cash equivalents	1	–	1
Payables	(4)	–	(4)
Net assets acquired	**3**	**–**	**3**
Goodwill			**10**
Total consideration			**13**

During 2010 the determination of fair values has been finalised. No adjustments have been made to the balances previously reported.

BT Retail

During 2009 the group acquired 100% of the issued share capital of Wire One Holdings Inc and Ufindus Ltd for a total consideration of £98m. The combined net assets acquired in these transactions and the goodwill arising were as follows:

	Book value £m	Fair value adjustments £m	Fair value £m
Intangible assets	2	21	23
Property, plant and equipment	2	–	2
Receivables	20	(1)	19
Cash and cash equivalents	3	–	3
Payables	(22)	(1)	(23)
Net assets acquired	**5**	**19**	**24**
Goodwill			**74**
Total consideration			**98**

Intangible assets recognised in respect of these acquisitions comprised customer relationships, brand names and proprietary technology. Goodwill arising on these acquisitions principally related to anticipated cost and revenue synergies and the assembled workforce. During 2010 the determination of fair values has been finalised. No adjustments have been made to the balances previously reported.

28. Acquisitions continued

Other

During 2009 the group acquired 100% of the issued share capital of Moorhouse Consulting and Ribbit Corporation, for a total consideration of £75m including £10m of deferred, contingent consideration. The combined net assets acquired in these transactions and the goodwill arising were as follows:

	Book value £m	Fair value adjustments £m	Fair value £m
Intangible assets	–	25	25
Receivables	2	–	2
Cash and cash equivalents	5	–	5
Payables	(4)	–	(4)
Net assets acquired	**3**	**25**	**28**
Goodwill			**47**
Total consideration			**75**

Intangible assets recognised in respect of these acquisitions comprised internally developed technology. Goodwill on the acquisitions principally related to cost savings and other synergies. During 2010 the determination of fair values has been finalised and adjustments have been made to the balances previously reported. Prior year balances have not been restated as the amount is not significant to the group.

29. Retirement benefit plans

Background

The group offers retirement benefit plans to its employees. The group's main scheme, the BT Pension Scheme (BTPS), is a defined benefit scheme. This scheme has been closed to new entrants since 31 March 2001 when it was replaced by a defined contribution scheme, the BT Retirement Plan (BTRP) which was closed on 31 March 2009. On 1 April 2009 BT set up the BT Retirement Saving Scheme, a contract based defined contribution arrangement, to which BTRP members were invited to transfer their accumulated assets. The total pension cost of the group for 2010, included within staff costs, was £304m (2009: £544m, 2008: £626m). The total cost associated with the group's defined benefit pension schemes for 2010 was £206m (2009: £459m, 2008: £576m).

Defined contribution schemes

The income statement charge in respect of defined contribution schemes represents the contribution payable by the group based upon a fixed percentage of employees' pay. The total pension cost for 2010 in respect of the group's main defined contribution scheme was £66m (2009: £47m, 2008: £37m) and £6m (2009: £4m, 2008: £3m) of contributions were outstanding at 31 March 2010.

Defined benefit schemes

BT Pension Scheme Trustees Limited 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.

Measurement of scheme assets and liabilities – IAS 19

Scheme assets are measured at the bid market value at the balance sheet date. The liabilities of the BTPS are measured by discounting the best estimate of future cash flows to be paid out by the scheme using the projected unit credit method. Estimated future cash flows are discounted at the current rate of return on high quality corporate bonds of an equivalent term to the liability. Actuarial gains and losses are recognised in full in the year in which they occur in the statement of comprehensive income.

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 rate of inflation influences the assumptions for salary and pension increase. This has been assessed by reference to yields on long-term fixed and index-linked Government bonds and has regard to Bank of England published inflationary expectations. Salary increases are assumed to be in line with inflation.

29. Retirement benefit plans continued

The financial assumptions used to measure the net pension obligation of the BTPS under IAS 19 at 31 March 2010 are as follows:

	Real rates (per annum)			Nominal rates (per annum)		
At 31 March	**2010** %	2009 %	2008 %	**2010** %	2009 %	2008 %
Rate used to discount liabilities	1.83	3.84	3.24	5.50	6.85	6.85
Average future increases in wages and salaries	–	–	0.75[a]	3.60	2.90	4.28[a]
Average increase in pensions in payment and deferred pensions	–	–	–	3.60	2.90	3.50
Inflation – average increase in retail price index	n/a	n/a	n/a	3.60	2.90	3.50

[a] There is a short-term reduction in the real salary growth assumption to 0.5% for the first three years.

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 (333,000 members at 31 December 2009) it is considered appropriate for the life expectancy assumptions adopted to take in to 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.

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

	2010 Number of years	2009 Number of years
Male in lower pay bracket	25.2	24.8
Male in higher pay bracket	27.4	27.1
Female	28.1	27.7
Future improvement every 10 years	1.1	1.0

Amounts recognised in respect of defined benefit schemes

The net pension obligation is set out below:

			2010			2009
At 31 March	Assets £m	Present value of liabilities £m	Obligation £m	Assets £m	Present value of liabilities £m	Obligation £m
BTPS	35,278	(43,018)	(7,740)	29,227	(33,070)	(3,843)
Other schemes[a]	151	(275)	(124)	126	(256)	(130)
	35,429	**(43,293)**	**(7,864)**	**29,353**	**(33,326)**	**(3,973)**
Deferred tax asset			2,193			1,103
Net pension obligation			**(5,671)**			**(2,870)**

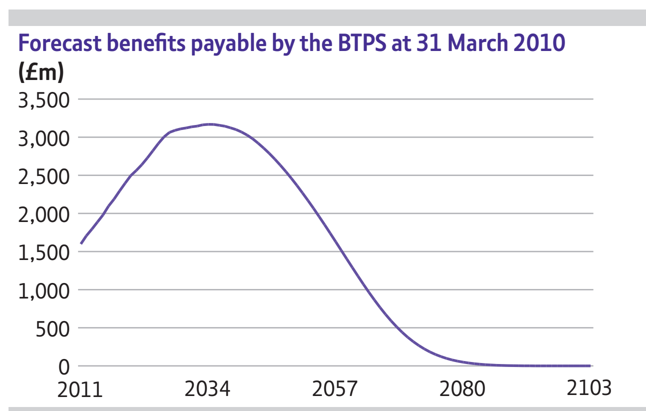
[a] Included in the present value of liabilities of other schemes is £54m (2009: £52m) related to unfunded schemes.

Amounts recognised in the income statement in respect of the group's pension schemes were as follows:

Year ended 31 March	**2010** £m	2009 £m	2008 £m
Current service cost (including defined contribution schemes)	304	544	626
Total operating charge	304	544	626
Expected return on pension scheme assets	(1,932)	(2,621)	(2,448)
Interest expense on pension scheme liabilities	2,211	2,308	2,028
Net finance expense (income)	**279**	**(313)**	**(420)**
Total recognised in the income statement	**583**	**231**	**206**

29. Retirement benefit plans continued

The present value of the obligation is derived from long-term cash flow projections and is thus inherently uncertain. The benefits payable by the BTPS are expected to be paid as follows:



An analysis of actuarial gains and losses and the actual return on plan assets is shown below:

Year ended 31 March	**2010** £m	2009 £m	2008 £m
Actuarial (loss) gain recognised in the year	(4,324)	(7,037)	2,621
Cumulative actuarial (losses) gains	(4,915)	(591)	6,446
Actual return on plan assets	7,089	(6,830)	(124)

Changes in the present value of the defined benefit pension obligation are as follows:

Year ended 31 March	**2010** £m	2009 £m
Opening defined benefit pension obligation	(33,326)	(34,669)
Current service cost	(206)	(459)
Interest expense	(2,211)	(2,308)
Contributions by employees	(15)	(18)
Actuarial (loss) gain	(9,481)	2,414
Business combinations	–	(4)
Benefits paid	1,948	1,741
Exchange differences	(2)	(23)
Closing defined benefit pension obligation	**(43,293)**	**(33,326)**

Changes in the fair value of plan assets are as follows:

Year ended 31 March	**2010** £m	2009 £m
Opening fair value of plan assets	29,353	37,448
Expected return	1,932	2,621
Actuarial gain (loss)	5,157	(9,451)
Regular contributions by employer	391	441
Deficiency contributions by employer	525	–
Contributions by employees	15	18
Benefits paid	(1,948)	(1,741)
Exchange differences	4	17
Closing fair value of plan assets	**35,429**	**29,353**

29. Retirement benefit plans continued

The BTPS assets are invested in UK and overseas equities, UK and overseas properties, fixed interest and index-linked securities, alternative assets, deposits and short-term investments. At 31 March 2010 and 31 March 2009, the scheme's assets did not include any ordinary shares of the company. However, the scheme held £52m (2009: £65m) of bonds and £6m (2009: £5m) of index-linked notes issued by the group. The group occupies four (2009: two) properties owned by the BTPS on which an annual rental of £0.2m is payable (2009: £0.1m).

The Trustee's main investment objective is to ensure that over the long-term, and after allowing for all future income, the BTPS will always have sufficient liquid resources to meet the cost of benefit payments to be made as they fall due. The strategic allocation of assets between different classes of investment is reviewed regularly and is a key factor in the Trustee's investment policy. The targets set reflect the Trustee's views on the appropriate balance to be struck between seeking high returns and incurring risk, and on the extent to which the assets should be distributed to match its 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 strategic target, for example, by using stock index future contracts.

The BTPS uses financial instruments to manage interest rate risk, liquidity risk and foreign currency risk. Exposure to interest rate fluctuations on its borrowings and deposits is managed by using interest rate swaps. Liquidity risk is managed by maintaining a balance between continuity of funding and flexibility through the use of borrowings with a range of maturities. The BTPS has significant investments overseas, as a result of which the value of the scheme's assets can be significantly affected by movements in foreign currencies against Sterling. A portion of the exposure to foreign currencies embedded in the overseas assets is hedged back into Sterling to remove some of the currency risk.

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

	At 31 March 2010				At 31 March 2009			
	Expected long-term rate of return (per annum) %	Asset fair value £bn	Asset fair value %	Target %	Expected long-term rate of return (per annum) %	Asset fair value £bn	Asset fair value %	Target %
UK equities	8.5	3.6	10	11	8.5	3.2	11	11
Non-UK equities	8.5	7.5	21	22	8.5	5.9	20	22
Fixed-interest securities	5.0	5.9	17	20	5.9	6.6	22	20
Index-linked securities	4.2	5.8	16	15	4.0	4.4	15	15
Property	7.7	3.8	11	12	7.0	3.2	11	12
Alternative assets	6.9	5.9	17	20	7.0	5.2	18	20
Cash and other	4.2	2.8	8	–	3.5	0.8	3	–
	6.5	**35.3**	**100**	**100**	**6.7**	**29.3**	**100**	**100**

The assumption for the expected return on scheme assets is a weighted average based on the assumed expected return for each asset class and the proportions held of each asset class at the beginning of the year. The expected returns on fixed interest and index-linked securities are based on the gross redemption yields at the start of the year. 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. Alternative asset classes include commodities, hedge funds, private equity, infrastructure and credit opportunities. The long-term expected rate of return on investments does not affect the level of the obligation but does affect the expected return on pension scheme assets within the net finance expense.

The history of experience gains and losses are as follows:

	2010 £m	2009 £m	2008 £m	2007 £m	2006 £m
Present value of defined benefit obligation	(43,293)	(33,326)	(34,669)	(38,779)	(38,187)
Fair value of plan assets	35,429	29,353	37,448	38,390	35,640
Net pension (obligation) asset	(7,864)	(3,973)	2,779	(389)	(2,547)
Experience adjustment on defined benefit obligation – gain (loss)	1,632	(238)	(22)	190	(527)
Percentage of the present value of the defined benefit obligation	3.8%	0.7%	0.1%	0.5%	1.4%
Experience adjustment on plan assets – gain (loss)	5,157	(9,451)	(2,572)	993	4,855
Percentage of the plan assets	14.6%	32.2%	6.9%	2.6%	13.6%

The group expects to contribute approximately £669m to the BTPS in 2011, including deficiency contributions of £525m.

29. Retirement benefit plans continued

Sensitivity analysis of the principal assumptions used to measure BTPS liabilities

The assumed discount rate, life expectancy and salary increases all have a significant effect on the measurement of scheme liabilities. The following table shows the sensitivity of the valuation of the pension obligations, and of the prospective 2011 income statement charge, to changes in these assumptions:

	Decrease (increase) in liability £bn	Decrease (increase) in service cost £m	Decrease (increase) in net finance expense £m
0.25 percentage point increase to:			
– discount rate	1.6	15	(15)
– salary increases	(0.2)	–	(15)
Additional 1 year increase to life expectancy	(1.0)	(10)	(55)
0.1 percentage point increase in expected return on assets	–	–	35

The sensitivities relating to the discount rate, inflation rate and expected return on assets in respect of the pension cost elements in the income statement are shown for information only. The amounts that will be recognised in the income statement in 2011 are derived from market conditions at 1 April 2010. Subsequent changes in market conditions will have no effect on the income statement in 2011 and will be reflected as actuarial gains and losses in the Statement of comprehensive income.

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 present and future contributions should be sufficient to meet future liabilities. The funding valuation is based on prudent assumptions and is performed at 31 December as this is the financial year end of the BTPS.

The valuation basis for funding purposes is broadly as follows:

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

The outcome of the latest triennial actuarial funding valuation at 31 December 2008 was announced on 11 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. Whilst the valuation and the recovery plan have been agreed with the Trustee, they are currently under review by the Pensions Regulator. However, the Pensions Regulator's initial view is that they have substantial concerns with certain features of the agreement. BT and the Trustee continue to work with the Pensions Regulator to help them complete their detailed review. The Pensions Regulator has indicated it will discuss its position with us once they have completed their review. Accordingly, as matters stand, it is uncertain as to whether the Pensions Regulator will take any further action. This uncertainty is outside of our control. Since the valuation date the scheme's assets have increased by £4.1bn and the Trustee estimates that if the funding valuation was performed at 31 December 2009 the deficit would have been about £7.5bn on this prudent valuation basis.

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

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

At 31 December 2008 the assets of the BTPS had a market value of £31.2bn (2005: £34.4bn) and were sufficient to cover 77.6% (2005: 90.9%) of the benefits accrued by that date. This represented a funding deficit of £9.0bn compared with £3.4bn at 31 December 2005. The funding valuation uses prudent assumptions. 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.

Following the agreement of the valuation the ordinary contributions rate reduced to 13.6% of pensionable salaries (including employee contributions) from 19.5%, reflecting the implementation of benefit changes with effect from 1 April 2009, following the UK pensions review. In addition, the group will make deficit payments of £525m per annum for the first three years of the 17 year recovery plan, the first payment of which was made in December 2009. The payment in the fourth year will be £583m, then increasing at 3% per annum. The payments in years four to 17 are equivalent to £533m per annum in real terms. Under the 2005 valuation deficit contributions were £280m per annum for 10 years. In 2010, the group made regular contributions of £384m (2009: £433m) and deficit contributions of £525m. No deficit contributions were made in 2009 as they were paid in advance during 2008.

29. Retirement benefit plans continued

Other features of the 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. Total pension contributions (including regular contributions) are expected to be approximately £2.4bn over the three financial years.
- 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.

The intention is for there to be sufficient assets in the scheme to pay pensions now and in the future. Without any further contribution from the company, it is estimated that at 31 December 2008, the assets of the scheme would have been sufficient to provide around 57% of the members' benefits with an insurance company.

If the group were to become insolvent, however, there are a number of additional protections available to members. Firstly, there is the Crown Guarantee which was granted when the group was privatised in 1984. The scope and extent of the Crown Guarantee is being confirmed by the Trustee through the courts. This applies, on a winding up of the group, as a minimum to pension entitlements for anyone who joined the scheme before 6 August 1984, and to payments to beneficiaries of such persons. Secondly, the Pension Protection Fund (PPF) may take over the scheme and pay certain benefits to members. 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.

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. The BTPS was closed to new entrants on 31 March 2001 and the age profile of active members will consequently increase. Under the projected unit credit method, the current service cost, as a proportion of the active members' pensionable salaries, is expected to increase as the members of the scheme approach retirement. Despite the scheme being closed to new entrants, the projected payment profile extends over more than 60 years.

30. Share-based payments

The total charge recognised in 2010 in respect of share-based payments was £71m (2009: £141m, 2008: £73m).

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	**2010** £m	2009[a] £m	2008[a] £m
Employee Sharesave Plan	25	107	29
Allshare International	2	2	2
Employee Stock Purchase Plan	1	–	1
Incentive Share Plan	29	18	26
Deferred Bonus Plan	13	12	12
Retention Share Plan	1	2	3
	71	**141**	**73**

[a] Restated for the adoption of the amendment to IFRS 2 'Share-based payment – vesting conditions and cancellations'. See page 94.

Share options

BT Group Employee Sharesave Plans

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 US, enables participants to purchase American Depositary 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.

30. Share-based payments continued

The following are legacy option plans which are no longer operated by the group:

BT Group Global Share Option Plan (GSOP)

The options granted in previous years were exercisable on the third anniversary of the date of grant, subject to continued employment and meeting corporate performance targets. Options must be exercised within ten years of the grant date.

BT Group Legacy Option Plan (GLOP)

On the demerger of 0_2, BT's share option plans ceased to operate and were replaced by similar BT Group Employee Sharesave plans and the BT Group GSOP. The BT GLOP was launched on 17 December 2001 following the scheme of arrangement and demerger of 0_2 in November 2001, and is therefore outside the scope of IFRS 2. The options were exercisable subject to continued employment and meeting corporate performance targets. Options must be exercised within 10 years of the original grant date.

Share plans

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 (allshare). In 2008, allshare was replaced by free broadband for all BT employees in the UK. Employees outside the UK continue to receive awards of shares where practicable, otherwise they will receive awards equivalent to the value of free shares.

During 2010, 13.7m directshare shares (2009: 10.7m directshare shares), were purchased by the Trustee of the ESIP on behalf of 19,730 (2009: 20,384) employees at a total cost of £15.0m (2009: £16.4m). A further 1.0m shares (2009: 3.3m shares) were purchased by the Trustee through dividend reinvestment on behalf of 20,120 (2009: 21,782) allshare and directshare employee participants. At 31 March 2010 79.2m shares (2009: 75.9m shares) were held in trust on behalf of 68,444 participants (2009: 76,678).

Incentive Share Plan, Retention Share Plan and Deferred Bonus 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 measure and if the participants are still employed by the group. In 2010, the corporate performance measure for the ISP was amended. For all ISP awards made in 2010, 50% of each share award is linked to a total shareholder return target (TSR) for a revised 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 revised 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 in prior periods, 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 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.

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.

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

30. Share-based payments continued

Share option plans

Activity relating to share options during 2010, 2009 and 2008 is shown below.

	Employee Sharesave			GSOP and GLOP		
Movement in the number of share options:	**2010 millions**	2009 millions	2008 millions	**2010 millions**	2009 millions	2008 millions
Outstanding at the beginning of the year	136	281	272	42	46	103
Granted	490	339	54	–	–	–
Forfeited	(44)	(390)	(15)	(4)	(3)	(10)
Exercised	(1)	(80)	(28)	–	(1)	(14)
Expired	(47)	(14)	(2)	–	–	(33)
Outstanding at the end of the year	**534**	**136**	**281**	**38**	**42**	**46**
Exercisable at the end of the year	**1**	**1**	**2**	**38**	**42**	**46**
Weighted average exercise price:						
Outstanding at the beginning of the year	160p	180p	165p	256p	257p	227p
Granted	63p	135p	269p	–	–	–
Forfeited	107p	153p	208p	263p	199p	251p
Exercised	125p	155p	188p	–	196p	198p
Expired	150p	178p	179p	–	–	199p
Outstanding at the end of the year	**76p**	**160p**	**180p**	**255p**	**256p**	**257p**
Exercisable at the end of the year	**163p**	**195p**	**158p**	**255p**	**256p**	**257p**

The weighted average share price for options exercised during the year was 136p (2009: 180p, 2008: 293p). The following table summarises information relating to options outstanding and exercisable under all share option plans at 31 March 2010, 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
BT Group Employee Sharesave Plans			
2010	171p–294p	16	1
2011	137p–208p	12	–
2012	68p–262p	143	–
2013	185p	8	–
2014	61p–111p	355	–
Total		**534**	**1**
BT Group Legacy Option Plan			
2001-2011	318p–648p	8	8
Total		**8**	**8**
BT Group Global Share Option Plan			
2004-2014	176p–199.5p	24	24
2005-2015	179p–263p	6	6
Total		**30**	**30**
Total options		**572**	**39**

30. Share-based payments continued

The options outstanding under all share option plans at 31 March 2010, have weighted average remaining contractual lives as follows:

	Employee Sharesave				GSOP and GLOP		
Range of exercise prices	Weighted average exercise price	Number of outstanding options millions	Weighted average contractual remaining life	Range of exercise prices	Weighted average exercise price	Number of outstanding options millions	Weighted average contractual remaining life
61p–68p	63p	465	48 months	–	–	–	–
100p – 199p	143p	57	32 months	150p-317p	198p	30	52 months
200p – 300p	242p	12	26 months	318p-650p	424p	8	8 months
Total		**534**				**38**	

Executive share plans

Movements in executive share plans during 2010 are shown below:

	Millions of shares			
	ISP	DBP	RSP	Total
At 1 April 2009	75.2	15.5	1.5	92.2
Awards granted	50.0	4.5	0.3	54.8
Awards vested	–	(5.0)	(0.6)	(5.6)
Awards lapsed	(28.4)	(1.1)	–	(29.5)
Dividend shares reinvested	2.4	0.4	–	2.8
At 31 March 2010	**99.2**	**14.3**	**1.2**	**114.7**

At 31 March 2010 1.1m shares (2009: 1.3m) were held in trust and 113.6m shares (2009: 90.9m) were held in treasury for executive share plans.

Fair value

The following table summarises the fair values and key assumptions used for grants made under the Employee Sharesave plans and ISP in 2010, 2009 and 2008.

	2010		2009		2008	
Year ended 31 March	Employee Sharesave	ISP	Employee Sharesave	ISP	Employee Sharesave	ISP
Weighted average fair value	14p	106p	27p	47p	71p	182p
Weighted average share price	80p	131p	152p	199p	329p	306p
Weighted average exercise price	63p	–	135p	–	269p	–
Expected dividend yield	5.7%–6.4%	6.5%	4.6%-6.4%	4.9%	5.5%	5.5%
Risk free rates	2.2%–2.8%	2.5%	2.1%-5.5%	5.2%	5.8%	5.8%
Expected volatility	26.9%–30.7%	38.5%	20.7%-28.4%	23.3%	22.0%	18.0%

Employee Sharesave grants, under the BT Group Employee Sharesave and the BT Group International Employee Sharesave option plans, are valued using a Binomial option 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 2010 was 104p (2009: 151p, 2008: 310p). The weighted average share price for DBP awards granted in 2010 was 131p (2009: 203p, 2008: 319p).

31. 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 2010.

Year ended 31 March	**2010** **£000**	2009 £000	2008 £000
Audit services			
Fees payable to the company's auditor and its associates for the audit of parent company and consolidated financial statements	2,585	2,831	2,990
Non-audit services			
Fees payable to the company's auditor and its associates for other services:			
– The audit of the company's subsidiaries pursuant to legislation[a]	4,732	4,675	3,848
– Other services pursuant to legislation[a]	867	1,211	1,590
– Tax services	792	1,247	727
– Services relating to corporate finance transactions[b]	–	32	549
– All other services	941	887	527
	9,917	**10,883**	**10,231**

[a] These services are audit services as defined by the Public Company Accounting Oversight Board AU Section 550 (PCAOB AU Section 550).
[b] These services are audit related services as defined by the PCAOB AU Section 550.

Audit services represents 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 represents 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.

Tax services represents 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 represents 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 (2009: £41,000, 2008: £40,000).

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.

32. 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.

Funding and exposure management

The group finances its operations primarily by a mixture of issued share capital, retained profits, deferred taxation 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. This treasury operation also manages the group's market risk exposures, including risks arising from volatility in currency and interest rates. The treasury operation acts as a central bank to members of the group 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 and its activities are subject to a set of controls commensurate with the magnitude of the borrowings and investments and group wide exposures under its management. The Board has delegated its authority to operate these polices 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 key policies defined by the Board are highlighted in each of the sections below.

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 2010 and the date of approval of these financial statements.

Capital management

The objective of the group's capital management policy is to reduce net debt whilst investing in the business, supporting the pension scheme and delivering 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 the group's objectives and processes during 2010 and 2009.

The group's capital structure consists of net debt, committed facilities and shareholders' equity (excluding the cash flow reserve). The following analysis summarises the components which the group manages as capital:

At 31 March	**2010** £m	2009 £m	2008 £m
Total parent shareholders' (deficit) equity (excluding cash flow reserve)	(2,797)	(421)	5,252
Net debt	9,283	10,361	9,460
Committed facilities	1,500	2,300	2,335
Total capital	**7,986**	**12,240**	**17,047**

Interest rate risk management

Management policy

The group has interest bearing financial assets and financial 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 whilst 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 by the Board.

32. Financial instruments and risk management continued

Hedging strategy

In order to manage the group's interest rate mix profile, the group has entered into swap agreements with commercial banks and other institutions to vary the amounts and periods for which interest rates on borrowings are fixed. Under cross currency swaps, the group agrees with other parties to exchange, at specified intervals, US Dollar and Euro fixed rates into either fixed or floating Sterling interest amounts calculated by reference to an agreed notional principal amount. Under Sterling interest rate swaps, the group agrees with other parties to exchange, at specified intervals, the differences between fixed rate and floating rate Sterling interest amounts calculated by reference to an agreed notional principal amount. The group uses a combination of these derivatives to primarily fix its interest rates.

The majority of the group's long-term borrowings have been, and are, subject to fixed Sterling interest rates after applying the impact of hedging instruments. Outstanding currency and interest rate swaps at 31 March 2010 are detailed in the Hedging activities and Other derivatives sections below.

At 31 March 2010 the group's fixed floating interest rate profile, after hedging, on gross debt was 91:9 (2009: 87:13).

Sensitivities

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 (2009: 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. All adjustments to interest rates for the impacted financial instruments are assumed to take effect from the respective balance sheet date.

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 not in hedging relationships and on variable rate borrowings and investments which are largely influenced by Sterling interest rates. Trade payables, trade receivables and other financial instruments do not present a material exposure to interest rate volatility. With all other factors remaining constant and based on the composition of net debt at 31 March 2010, a 100 basis point increase (2009 and 2008: 100 basis point increase) in Sterling interest rates would decrease the group's annual net finance expense by approximately £17m (2009: £5m, 2008: £5m).

The group's main exposure to interest rate volatility within shareholders' equity, as defined in IFRS 7, arises from fair value movements on derivatives held in the cash flow reserve. The derivatives have an underlying interest rate 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 (2009 and 2008: 100 basis point increase) in interest rates in each of the currencies would impact equity, before tax, as detailed below:

At 31 March	**2010** £m Charge (credit)	2009 £m Charge (credit)	2008 £m Charge (credit)
Sterling interest rates	496	550	470
US Dollar interest rates	(392)	(538)	(347)
Euro interest rates	(134)	(149)	(90)

The impact as a result of a 100 basis point decrease in interest rates would have broadly the same impact in the opposite direction.

The long-term debt instruments which the group issued in December 2000 and February 2001 both contained covenants providing that if the BT Group 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 ratings agency. In February 2010 S&P downgraded BT's credit rating to BBB–. Prior to this in March 2009, Moody's and S&P downgraded BT's credit rating to Baa2 and BBB, respectively. Based on the total debt of £4.4bn outstanding on these instruments at 31 March 2010, the group's finance expense would increase/decrease by approximately £9m in the year ending 31 March 2011 if BT's credit rating were to be downgraded/upgraded respectively by one credit rating category by both agencies below a long-term debt rating of Baa2/BBB–.

In addition, the group's €600m 2014 bond issued in June 2009 would attract an additional 1.25 percentage points for a downgrade by one credit rating category by both Moody's and S&P below Baa3/BBB–, respectively. This would result in an additional finance expense of £5m in the year ending 31 March 2011.

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 the eventual 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 types 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 approval 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.

32. Financial instruments and risk management continued

Exposure and hedging

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 borrowings, which totalled £9.4bn at 31 March 2010 (2009: £9.9bn), are used to finance its operations and have been predominantly swapped into Sterling using cross currency swaps. 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 £26m (2009: approximately £20m).

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 would be insignificant in both 2010 and 2009.

Outstanding cross currency swaps at 31 March 2010 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 Standard and Poor's 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. Management review significant utilisations on a regular basis to determine the adjustments required, if any, and actively manage any exposures which may arise. 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. The group makes use of standard International Swaps and Derivative Association (ISDA) documentation. In addition, where possible the group will seek a combination of a legal right of set off and net settlement. 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 manage any exposures which arise.

Exposures

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

At 31 March	**2010** £m	2009 £m	2008 £m
Derivative financial assets	1,700	2,700	387
Investments	470	218	471
Trade and other receivables[a]	2,947	3,101	3,193
Cash and cash equivalents	1,452	1,300	1,435
Total	**6,569**	**7,319**	**5,486**

[a] The carrying amount excludes £749m (2009: £1,084m, 2008: £1,256m) of current and £336m (2009: £322m, 2008: £854m) of non current trade and other receivables which relate to non financial assets.

Note 19 discloses the credit concentration and credit quality of derivative financial assets. The majority of these 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 2010, 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 2010	Impact of 100 basis point increase £m	Impact of 100 basis point decrease £m
Moody's/S&P credit rating		
Aa2/AA	(3)	4
Aa3/AA–	(26)	30
A1/A+	(89)	104
A2/A	(102)	122
	(220)	**260**

The credit quality of other treasury related financial assets is disclosed in notes 10 and 14.

32. Financial instruments and risk management continued

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 customer's exposure to the group, by applying processes which include netting and off setting, and requesting securities such as deposits, guarantees and letters of credit. The group takes proactive steps to minimise the impact of adverse market conditions on trading related financial assets. The concentration of credit risk for trading balances of the group is provided in note 17 which analyses outstanding balances by line of business and reflects the nature of customers in each line of business.

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. 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.

The group's liquidity and funding management process includes projecting cash flows and considering the level of liquid assets in relation thereto, monitoring balance sheet liquidity and maintaining a diverse range of funding sources and back up facilities. The Board reviews forecasts, including cash flow forecasts, on a quarterly basis. The treasury operation reviews cash flows more frequently to assess the short and medium-term requirements. These assessments ensure the group responds to possible future cash constraints in a timely manner. Liquid assets surplus to the immediate operating requirements of the group are generally invested and managed by the treasury operation. Requests from group companies for operating finance are met whenever possible from central resources.

Liquidity position

At 31 March	**2010** £m	2009 £m	2008 £m
Net debt	9,283	10,361	9,460

During 2010, the group's net debt decreased from £10.4bn to £9.3bn primarily driven by higher free cash flow partially offset by the pension deficit payment of £525m in December 2010. During 2010, debt amounting to £1bn matured consisting of £0.7bn of commercial paper and £0.3bn of long-term debt. This was offset by new issuance of a €600m bond at 6.125% repayable in 2014 which was swapped into £520m at a fixed semi-annual rate of 6.8%. During 2009, the group's net debt increased from £9.5bn to £10.4bn primarily driven by lower free cash flow being exceeded by dividend and share buy back payments. During 2009, debt amounting to £0.9bn matured consisting of bank notes and Sterling floating notes. This was offset by new issuances of £1.5bn mainly consisting of a €1bn bond at 6.5% repayable in 2015, which was swapped into £0.8bn at an average annualised Sterling interest rate of 7.7%, and commercial paper. In addition, investments of £0.3bn matured.

During 2010 and 2009 the group issued commercial paper and held cash, cash equivalents and current asset investments in order to manage short-term liquidity requirements. At 31 March 2010 the group had an undrawn committed borrowing facility of £1.5bn (2009: £1.5bn). The facility is available for the period to January 2013. The group had an additional undrawn committed borrowing facility of £900m which expired in March 2010.

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. The group has two significant term debt maturities during the 2011 financial year. In December 2010 the group's US Dollar 8.625% note matures with a principal of $2,883m (£1,742m at swapped rates) and in February 2011 a Euro 7.375% note matures with a principal of €1,125m (£758m at swapped rates). The group has built up significant liquidity in anticipation of these maturities which, alongside cash flows generated from operations and the group's financing strategy, will fund this requirement. In May 2010, the group entered into a £650m two-year facility arrangement. There are no term debt maturities in the 2012 financial year. At 31 March 2010, the group's credit rating was BBB– with stable outlook with S&P and Baa2 with negative outlook with Moody's respectively (2009: BBB with stable outlook/Baa2 with negative outlook).

32. Financial instruments and risk management continued

The group's remaining contractually agreed cash flows, including interest, associated with financial liabilities based on undiscounted cash flows are as follows:

Outflow (inflow)[d]	Carrying amount £m	Within one year, or on demand £m	Between one and two years £m	Between two and three years £m	Between three and four years £m	Between four and five years £m	After five years £m
At 31 March 2010							
Loans and borrowings	12,791						
Principal		2,937	18	1,763	11	1,213	6,523
Interest		833	581	581	484	484	4,016
Trade and other payables[a]	4,672	4,672	–	–	–	–	–
Provisions[b]	255	61	37	30	26	45	143
Derivative financial instrument liabilities analysed based on earliest payment date[c]							
Net settled	662	450	78	185	65	(215)	745
Gross settled	37						
Outflow		1,081	–	–	–	–	–
Inflow		(1,074)	–	–	–	–	–
Total		**8,960**	**714**	**2,559**	**586**	**1,527**	**11,427**
Derivative financial instrument liabilities analysed based on holding instrument to maturity							
Net settled	662	193	92	93	92	93	745
Gross settled	37						
Outflow		424	20	20	20	20	577
Inflow		(413)	(21)	(21)	(21)	(21)	(577)

Outflow (inflow)[d]	Carrying amount £m	Within one year, or on demand £m	Between one and two years £m	Between two and three years £m	Between three and four years £m	Between four and five years £m	After five years £m
At 31 March 2009							
Loans and borrowings	13,907						
Principal		1,227	3,098	10	1,829	14	7,412
Interest		906	900	649	650	550	5,333
Trade and other payables[a]	5,354	5,354	–	–	–	–	–
Provisions[b]	166	59	17	15	13	8	119
Derivative financial instrument liabilities analysed based on earliest payment date[c]							
Net settled	762	244	338	28	50	19	30
Gross settled	5						
Outflow		414	113	–	–	–	–
Inflow		(409)	(113)	–	–	–	–
Total		**7,795**	**4,353**	**702**	**2,542**	**591**	**12,894**
Derivative financial instrument liabilities analysed based on holding instrument to maturity							
Net settled	762	117	117	60	60	60	634
Gross settled	5						
Outflow		414	113	–	–	–	–
Inflow		(409)	(113)	–	–	–	–

[a] The carrying amount excludes £1,859m (2009: £1,861m) of current and £804m (2009: £794m) of non current trade and other payables which relate to non financial liabilities.
[b] The carrying amount excludes £73m (2009: £195m) of current and £513m (2009: £359m) of non current provisions which relate to non financial liabilities.
[c] Certain derivative financial instrument liabilities 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.
[d] Foreign currency related cash flows were translated at the closing rate 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.

32. Financial instruments and risk management continued

Price risk management

The group has limited exposure to price risk.

Hedging activities

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

Hedged item	Hedging instruments	Hedge type	Notional principal £m	Derivative fair value[b] Asset £m	Derivative fair value[b] Liability £m	Remaining term of hedging instruments	Weighted average interest rate on hedging instruments	Period over which forecast transaction arises
Euro and US Dollar denominated borrowings[a]	Interest rate swaps	Cash flow	2,913	–	361	9 months to 21 years	Sterling receivable at 0.8% Sterling payable at 5.9%	
	Cross currency swaps	Cash flow	7,612	1,571	30	9 months to 21 years	Euro receivable at 6.1% US Dollar receivable at 7.6% Sterling payable at 6.3%	
Sterling denominated borrowings[a]	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[a]	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		

a See note 18.
b See note 19.

The group had outstanding hedging activities as at 31 March 2009 as follows:

Hedged item	Hedging instruments	Hedge type	Notional principal £m	Derivative fair value[b] Asset £m	Derivative fair value[b] Liability £m	Remaining term of hedging instruments	Weighted average interest rate on hedging instruments	Period over which forecast transaction arises
Euro and US Dollar denominated borrowings[a]	Interest rate swaps	Cash flow	2,913	–	446	2 to 22 years	Sterling receivable at 3.0% Sterling payable at 5.9%	
	Cross currency swaps	Cash flow and fair value	7,227	2,559	1	5 months to 22 years	Euro receivable at 6.0% US Dollar receivable at 7.7% Sterling payable at 7.2%	
Euro and US Dollar step up interest on currency denominated borrowings[a]	Forward currency contracts	Cash flow	223	9	–	3 to 5 months rolling basis		22 years
Euro and US Dollar commercial paper[a]	Forward currency contracts	Cash flow	490	17	–	Less than 3 months rolling basis		
Purchase of US Dollar denominated fixed assets	Forward currency contracts	Cash flow	48	–	1	Less than 1 month		4 years
Euro deferred consideration on acquisition	Forward currency contracts	Cash flow	50	1	–	Less than 5 months		

a See note 18.
b See note 19.

Other derivatives

At 31 March 2010, 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 and had a notional principal amount of £189m for purchases of currency (2009: £533m) and had a maturity period of under one month (2009: under nine months). Interest rate swaps not in hedging relationships under IAS 39 had a notional principal amount of £1.9bn (2009: £1.9bn) and mature between 2014 and 2030 (2009: 2014 and 2030). The interest receivable under these swap contracts is at a weighted average rate of 4.2% (2009: 6%) and interest payable is at a weighted average rate of 5.8% (2009: 7.6%). 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. In 2009 the group entered into credit default swap contracts to economically hedge part of its US Dollar denominated derivative financial assets, which had a notional principal of $90m. These derivatives matured in 2010.

32. 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 2010, 2009 and 2008. 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, debentures, notes, 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.

	Carrying amount			Fair value		
At 31 March	**2010** £m	2009 £m	2008 £m	**2010** £m	2009 £m	2008 £m
Financial liabilities						
Listed bonds, debentures and notes	12,157	12,189	9,298	13,304	11,384	9,436
Finance leases	304	332	320	343	366	347
Other loans and borrowings	330	1,386	1,724	354	1,338	1,690

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 2010	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
Total current and non current derivative financial assets (note 19)	–	1,700	–	1,700
Available-for-sale financial assets				
Non current and current investments				
Liquid investments	–	258	–	258
Other investments	20	–	12	32
Total non current and current investments (note 14)	20	258	12	290
Total financial assets at fair value	**20**	**1,958**	**12**	**1,990**
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 (note 19)	–	699	–	699
Total financial liabilities at fair value	**–**	**699**	**–**	**699**

32. Financial instruments and risk management continued

Movements in 2010 for financial instruments measured using Level 3 valuation methods are presented below:

	Other investments £m
At 1 April 2009	11
Additions	3
Disposals	(2)
At 31 March 2010	**12**

There were no losses recognised in the income statement in respect of Level 3 assets held at 31 March 2010.

REPORT OF THE INDEPENDENT AUDITORS – PARENT COMPANY FINANCIAL STATEMENTS

We have audited the parent company financial statements of BT Group plc for the year ended 31 March 2010 which comprise the BT Group plc company balance sheet, the BT Group plc company reconciliation of movement in equity shareholders' funds, the related notes and the BT Group plc accounting policies. 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 84, 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.

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 2010;
- 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 2010.

Philip Rivett (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
London, United Kingdom
12 May 2010

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 2010 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 2010 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 2010 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.

The company has adopted the amendment to FRS 20 (IFRS 2) 'Share-based payment' – Vesting Conditions and Cancellations with effect from 1 April 2009. The amendment requires retrospective adjustment and therefore prior period comparatives have been restated. This has resulted in an increase of £110m in the carrying value of investments in subsidiary undertakings in the year ended 31 March 2009. A corresponding increase to equity shareholders' funds representing the additional capital contribution has also been recognised.

Other information

(i) Dividends

The Board recommends that a final dividend in respect of the year ended 31 March 2010 of 4.6p will be paid to shareholders on 6 September 2010, taking the full year proposed dividend in respect of the 2010 financial year to 6.9p (2009: 6.5p). This dividend is subject to shareholder approval at the Annual General Meeting and therefore the liability of approximately £356m (2009: £85m) 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 2010. 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 (2009: £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 31 to the consolidated financial statements of BT Group plc.

BT Group plc company balance sheet

At 31 March	**2010** **£m**	2009[e] £m
Fixed assets		
Investments in subsidiary undertakings[a]	10,349	10,278
Total fixed assets	**10,349**	**10,278**
Current assets		
Debtors[b]	–	142
Cash at bank and in hand	11	13
Total current assets	**11**	**155**
Creditors: amounts falling due within one year[c]	186	65
Net current (liabilities) assets	**(175)**	**90**
Total assets less current liabilities	**10,174**	**10,368**
Capital and reserves		
Called up share capital	408	408
Share premium account	62	62
Capital redemption reserve	27	27
Treasury shares reserve	(1,105)	(1,109)
Profit and loss account	10,782	10,980
Total equity shareholders' funds[d]	**10,174**	**10,368**

[a] Throughout 2010, the company held a 100% investment in BT Group Investments Limited, a company registered in England and Wales. The change to investments in subsidiary undertakings relates to additional capital contributions in respect of share-based payments of £71m in 2010 (2009: £141m).
[b] Debtors consists of amounts owed by subsidiary undertakings of £nil (2009: £142m).
[c] Creditors consists of amounts owed to subsidiary undertakings of £166m (2009: £15m) and other creditors of £20m (2009: £50m).
[d] The movements in total equity shareholders' funds shown on page 148.
[e] Restated. See page 146.

The financial statements of the company on pages 146 to 149 were approved by the Board of the directors on 12 May 2010 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[a] £m	Share premium account £m	Capital redemption reserve £m	Treasury reserve[b] £m	Profit and loss account[b,c] £m	Total £m
At 1 April 2008	420	62	15	(1,843)	12,356	11,010
Profit for the financial year	–	–	–	–	502	502
Dividends paid	–	–	–	–	(1,222)	(1,222)
Change in accounting policy for adoption of the amendment to FRS 20 (see page 6)	–	–	–	–	110	110
Capital contribution in respect of share-based payment	–	–	–	–	31	31
Net purchase of treasury shares	–	–	–	(63)	–	(63)
Cancellation of shares	(12)	–	12	797	(797)	–
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
At 31 March 2010	**408**	**62**	**27**	**(1,105)**	**10,782**	**10,174**

[a] The authorised share capital of the company up to 1 October 2009 was £13,463m, representing 269,260,253,468 ordinary shares of 5p each. The allotted, called up and fully paid ordinary share capital of the company at 31 March 2010 was £408m (2009: £408m), representing 8,151,227,027 ordinary shares of 5p each (2009: 8,151,227,029).

[b] During 2010, the company repurchased nil (2009: 142,608,225) of its own shares of 5p each, nil % (2009: 2%) of the called-up share capital, for consideration (including transaction costs) of £nil (2009: £189m). In addition, 8,320,766 shares (2009: 90,626,518) were issued from treasury to satisfy obligations under employee share schemes and executive share awards at a cost of £4m (2009: £126m), and nil treasury shares (2009: 250,000,000) were cancelled at a cost of £nil (2009: £797m). At 31 March 2010, 400,906,119 shares (2009: 409,226,885) with an aggregate nominal value of £20m (2009: £20m) were held as treasury shares at cost.

[c] 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 £6m (2009: profit of £502m). 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[a] operating subsidiaries[b] and associate at 31 March 2010. 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[c]	Country of operation[d]
British Telecommunications plc	Communications related services and products provider	100% ordinary	UK
BT Americas Inc[d]	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 Centre Nominee 2 Limited	Property holding company	100% ordinary	UK
BT Communications do Brasil Limitada	Communications related services, technology consulting and products provider	100% ordinary	Brazil
BT Communications Ireland Limited	Telecommunications service provider	100% ordinary	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 Italia SpA	Communications related services and products provider	98.6% ordinary	Italy
BT Limited	International telecommunications network systems provider	100% ordinary	International
BT Nederland NV	Communications related services and products provider	100% ordinary	Netherlands
BT Payment Services Limited	Payment services provider	100% ordinary	UK
BT Professional Services Nederland BV	Systems integration and application development	100% ordinary	Netherlands
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 US Investments Limited[b]	Investment holding company	100% ordinary	Jersey
Communications Global Network Services Limited[d]	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% preference 100% common	US

[a] 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.
[b] 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.
[c] The proportion of voting rights held corresponds to the aggregate interest percentage held by the holding company and subsidiary undertakings.
[d] 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 Issued[e]	Share capital Percentage owned[f]	Country of operation[g]
Tech Mahindra Limited	Global systems integrator and business transformation consultancy provider	122,320,114	30.9%	India

[e] Issued share capital comprises ordinary or common shares unless otherwise stated.
[f] Held through an intermediate holding company.
[g] Incorporated in the country of operation.

QUARTERLY ANALYSIS OF REVENUE AND PROFIT

Year ended 31 March 2010	**Quarters**	Unaudited 1st £m	Unaudited 2nd £m	Unaudited 3rd £m	Unaudited 4th £m	Total £m
Revenue		5,235	5,070	5,198	5,356	**20,859**
Other operating income		79	93	80	128	**380**
Operating costs		(4,767)	(4,613)	(4,805)	(4,931)	**(19,116)**
Operating profit		547	550	473	553	**2,123**
Net finance expense		(283)	(284)	(292)	(299)	**(1,158)**
Share of post tax profits of associates and joint ventures		8	9	28	9	**54**
Loss on disposal of associate		–	–	–	(12)	**(12)**
Profit before taxation		272	275	209	251	**1,007**
Taxation		(58)	153	(31)	(42)	**22**
Profit for the period		214	428	178	209	**1,029**
Basic earnings per share		2.8p	5.5p	2.3p	2.7p	**13.3p**
Diluted earnings per share		2.7p	5.4p	2.2p	2.6p	**12.9p**
Profit before specific items and taxation		313	370	339	434	**1,456**
Adjusted basic earnings per share[a]		3.8p	4.3p	4.1p	5.0p	**17.3p**

Year ended 31 March 2009	Quarters	Unaudited 1st £m	Unaudited 2nd £m	Unaudited 3rd £m	Unaudited 4th £m	Total[b] £m
Revenue		5,177	5,303	5,437	5,473	**21,390**
Other operating income		90	107	71	71	**339**
Operating costs		(4,641)	(4,762)	(5,299)	(6,726)	**(21,428)**
Operating profit (loss)		626	648	209	(1,182)	**301**
Net finance expense		(130)	(159)	(180)	(151)	**(620)**
Share of post tax profits of associates and joint ventures		1	5	52	17	**75**
(Loss) profit before taxation		497	494	81	(1,316)	**(244)**
Taxation		(115)	(116)	(19)	303	**53**
(Loss) profit for the period		382	378	62	(1,013)	**(191)**
Basic (loss) earnings per share		4.9p	4.9p	0.8p	(13.1)p	**(2.5)p**
Diluted (loss) earnings per share		4.8p	4.9p	0.8p	(13.0)p	**(2.5)p**
Profit (loss) before specific items and taxation		524	532	45	(973)	**128**
Adjusted basic earnings per share[a]		4.4p	4.5p	2.7p	2.4p	**14.1p**

Year ended 31 March 2008	Quarters	Unaudited 1st £m	Unaudited 2nd £m	Unaudited 3rd £m	Unaudited 4th £m	Total[b] £m
Revenue		5,033	5,095	5,154	5,422	**20,704**
Other operating income		66	73	74	136	**349**
Operating costs		(4,441)	(4,647)	(4,646)	(4,963)	**(18,697)**
Operating profit		658	521	582	595	**2,356**
Net finance expense		(55)	(92)	(134)	(97)	**(378)**
Share of post tax losses of associates and joint ventures		(3)	(3)	(2)	(3)	**(11)**
Profit (loss) on disposal of associate		–	9	1	(1)	**9**
Profit before taxation		600	435	447	494	**1,976**
Taxation		8	(96)	(82)	(68)	**(238)**
Profit for the period		608	339	365	426	**1,738**
Basic earnings per share		7.4p	4.2p	4.5p	5.4p	**21.5p**
Diluted earnings per share		7.2p	4.1p	4.4p	5.3p	**21.1p**
Profit before specific items and taxation		650	617	581	658	**2,506**
Adjusted basic earnings per share[a]		5.0p	4.8p	4.8p	5.5p	**20.2p**

[a] Adjusted results refer to the amounts before BT Global Services contract and financial review charges in 2009, specific items and net interest on pensions.
[b] Restated. See page 94.

SELECTED FINANCIAL DATA

Summary group income statement

Year ended 31 March	**2010 £m**	2009[a] £m	2008[a] £m	2007[a] £m	2006[a] £m
Revenue					
Adjusted[b]	20,911	21,431	20,704	20,223	19,514
Specific items	(52)	–	–	–	–
Contract and financial review charges	–	(41)	–	–	–
	20,859	**21,390**	**20,704**	**20,223**	**19,514**
Other operating income					
Adjusted[b]	378	352	359	236	227
Specific items	2	(13)	(10)	(3)	–
	380	**339**	**349**	**233**	**227**
Operating costs					
Adjusted[b]	(18,689)	(19,435)	(18,168)	(17,746)	(17,108)
Specific items	(427)	(395)	(529)	(169)	(138)
Contract and financial review charges	–	(1,598)	–	–	–
	(19,116)	**(21,428)**	**(18,697)**	**(17,915)**	**(17,246)**
Operating profit					
Adjusted[b]	2,600	2,348	2,895	2,713	2,633
Specific items	(477)	(408)	(539)	(172)	(138)
Contract and financial review charges	–	(1,639)	–	–	–
	2,123	**301**	**2,356**	**2,541**	**2,495**
Net finance expense					
Adjusted[b]	(890)	(933)	(798)	(653)	(726)
Specific items	11	–	–	139	
Net interest on pensions	(279)	313	420	420	254
	(1,158)	**(620)**	**(378)**	**(94)**	**(472)**
Share of post tax profits (losses) of associates and joint ventures					
Adjusted[b]	25	39	(11)	15	16
Specific items	29	36	–	–	–
	54	**75**	**(11)**	**15**	**16**
(Loss) profit on disposal of associates and joint ventures – specific items[a]	**(12)**	**–**	**9**	**22**	**1**
Profit (loss) before taxation					
Adjusted[b]	1,735	1,454	2,086	2,075	1,923
Specific items	(449)	(372)	(530)	(11)	(137)
Contract and financial review charges	–	(1,639)	–	–	–
Net interest on pensions	(279)	313	420	420	254
	1,007	**(244)**	**1,976**	**2,484**	**2,040**
Taxation					
Adjusted[b]	(398)	(361)	(455)	(485)	(457)
Specific items	342	43	343	979	41
Contract and financial review charges	–	459	–	–	–
Net interest on pensions	78	(88)	(126)	(126)	(76)
	22	**53**	**(238)**	**368**	**(492)**
Profit (loss) for the year					
Adjusted[b]	1,337	1,093	1,631	1,590	1,466
Specific items	(107)	(329)	(187)	968	(96)
Contract and financial review charges	–	(1,180)	–	–	–
Net interest on pensions	(201)	225	294	294	178
	1,029	**(191)**	**1,738**	**2,852**	**1,548**
Basic earnings (loss) per share					
Adjusted[b]	17.3p	14.1p	20.2p	19.1p	17.4p
Specific items	(1.4)p	(4.3)p	(2.4)p	11.7p	(1.1)p
Contract and financial review charges	–	(15.3)p	–	–	–
Net interest on pensions	(2.6)p	3.0p	3.7p	3.6p	2.1p
Total basic (loss) earnings per share	**13.3p**	**(2.5)p**	**21.5p**	**34.4p**	**18.4p**

[a] Restated. See page 94.

[b] Adjusted revenue, adjusted other operating income, adjusted operating costs, adjusted operating profit, adjusted net finance expense, adjusted share of post tax profits (losses) of associates and joint ventures, adjusted (loss) profit on disposal of associates and joint ventures, adjusted profit (loss) before taxation, adjusted taxation credit (charge), adjusted profit (loss) for the year and adjusted basic earnings (loss) per share are non-GAAP measures provided in addition to the disclosure requirements defined under IFRS. The rationale for using non-GAAP measures is explained on pages 54 to 56.

Summary group income statement continued

Year ended 31 March	**2010**	2009[a]	2008[a]	2007[a]	2006[a]
Average number of shares used in basic earnings per share (millions)	7,740	7,724	8,066	8,293	8,422
Average number of shares used in diluted earnings per share (millions)	7,988	7,771	8,223	8,479	8,537
Basic earnings (loss) per share	13.3p	(2.5)p	21.5p	34.4p	18.4p
Diluted earnings (loss) per share	12.9p	(2.5)p	21.1p	33.6p	18.1p
Dividends per share[b]	6.9p	6.5p	15.8p	15.1p	11.9p
Dividends per share, cents[b,c]	10.5c	9.3c	31.4c	29.7c	20.7c

[a] Restated. See page 94.
[b] Dividends per share represents the dividend paid and proposed in respect of the relevant financial year. Under IFRS, dividends are recognised as a deduction from shareholders' equity when they are paid.
[c] Based on actual dividends paid and/or year end exchange rate on proposed dividends.

Summary group cash flow statement

Year ended 31 March	**2010 £m**	2009 £m	2008 £m	2007 £m	2006 £m
Net cash inflow from operating activities	4,825	4,706	5,486	5,210	5,387
Net cash (outflow) inflow from investing activities	(2,775)	(2,954)	(3,664)	(2,778)	214
Net cash used in financing activities	(1,714)	(1,865)	(1,430)	(2,898)	(5,278)
Effect of exchange rate changes on cash and cash equivalents	(7)	54	25	(35)	–
Net increase (decrease) in cash and cash equivalents	**329**	**(59)**	**417**	**(501)**	**323**
Cash and cash equivalents at the start of the year	1,115	1,174	757	1,258	935
Cash and cash equivalents at the end of the year	**1,444**	**1,115**	**1,174**	**757**	**1,258**

Summary group balance sheet

At 31 March	**2010 £m**	2009[a] £m	2008[a] £m	2007[a] £m	2006[a] £m
Intangible assets	3,672	3,788	3,355	2,584	1,908
Property, plant and equipment	14,856	15,405	15,307	14,997	15,222
Retirement benefit asset	–	–	2,887	–	–
Other non current assets	3,867	4,154	1,286	780	1,175
	22,395	**23,347**	**22,835**	**18,361**	**18,305**
Current assets less current liabilities	(4,135)	(3,141)	(2,978)	(3,746)	(3,052)
Total assets less current liabilities	**18,260**	**20,206**	**19,857**	**14,615**	**15,253**
Non current loans and other borrowings	(9,522)	(12,365)	(9,818)	(6,387)	(7,995)
Retirement benefit obligations	(7,864)	(3,973)	(108)	(389)	(2,547)
Other non current liabilities	(3,500)	(3,699)	(4,499)	(3,567)	(3,104)
Total assets less liabilities	**(2,626)**	**169**	**5,432**	**4,272**	**1,607**
Called up share capital	408	408	420	432	432
Share premium account	62	62	62	31	7
Capital redemption reserve	27	27	15	2	2
Other reserves	757	1,301	(527)	88	364
Retained (loss) earnings	(3,904)	(1,656)	5,439	3,685	750
Total parent shareholders' (deficit) equity	**(2,650)**	**142**	**5,409**	**4,238**	**1,555**
Minority interests	24	27	23	34	52
Total (deficit) equity	**(2,626)**	**169**	**5,432**	**4,272**	**1,607**

[a] Restated. See page 94.

Other selected financial data

	2010 £m	2009[a] £m	2008[a] £m	2007[a] £m	2006[a] £m
Adjusted EBITDA[b]	**5,639**	5,238	5,784	5,633	5,517
Free cash flow[c]	**1,933**	737	1,823	1,874	1,612
Net debt[d]	**9,283**	10,361	9,460	7,914	7,534

[a] Restated. See page 94.
[b] Adjusted EBITDA is stated before specific items and BT Global Services contract and financial review charges in 2009 and is defined on page 55.
[c] Free cash flow is defined on page 55.
[d] Net debt is defined on page 56.

FINANCIAL STATISTICS

Year ended 31 March	**2010**	2009[a]	2008[a]	2007[a]	2006[a]
Financial ratios					
Adjusted basic earnings per share[b] – pence	17.3	14.1	20.2	19.1	17.4
Reported basic (loss) earnings per share – pence	13.3	(2.5)	21.5	34.4	18.4
Adjusted return on capital employed[b, c] (unaudited)	16.0	14.5	17.7	17.6	18.1
Reported return on capital employed[c] (unaudited)	13.3	2.3	14.4	16.5	17.1
Adjusted interest cover before net pension interest[d] – times (unaudited)	2.9	2.5	3.6	4.2	3.6
Reported interest cover[e] – times (unaudited)	0.3	0.5	6.2	27.0	5.3

Year ended 31 March	**2010** £m	2009 £m	2008 £m	2007 £m	2006 £m
Expenditure on research and development					
Research and development expense	444	590	532	378	326
Amortisation of internally developed computer software	733	431	325	314	161
Total	**1,177**	**1,021**	**857**	**692**	**487**

Year ended 31 March	**2010** £m	2009 £m	2008 £m	2007 £m	2006 £m
Capital expenditure					
Plant and equipment					
Transmission equipment	902	1,067	1,117	1,209	1,429
Exchange equipment	29	44	83	118	80
Other network equipment	753	899	1,060	854	727
Computers and office equipment	115	140	181	149	138
Motor vehicles and other	662	912	876	877	715
Land and buildings	29	23	33	61	68
	2,490	**3,085**	**3,350**	**3,268**	**3,157**
Increase (decrease) in engineering stores	43	3	(11)	(21)	(15)
Total capital expenditure	**2,553**	**3,088**	**3,339**	**3,247**	**3,142**
(Decrease) increase in payables	(24)	(6)	(24)	51	(202)
Cash outflow on capital expenditure	**2,509**	**3,082**	**3,315**	**3,298**	**2,940**

a Restated. See page 94.
b Adjusted results refer to the results before specific items, the BT Global Services contract and financial review charges in 2009, and net interest on pensions.
c The ratio is based on profit before taxation and net finance expense to average capital employed. Capital employed is represented by total assets less current liabilities (excluding corporation tax, current borrowings, derivative financial liabilities and finance lease creditors) less deferred tax assets, retirement benefit asset, cash and cash equivalents, derivative financial assets and investments.
d The number of times net finance expense before net pension interest and specific items is covered by adjusted operating profit.
e The number of times reported net finance expense is covered by reported operating profit.

OPERATIONAL STATISTICS

All values (000) unless otherwise stated.	Unaudited				
Year ended 31 March	**2010**	2009	2008	2007	2006
BT Global Services					
12 month rolling[a] order intake (£m)	6,631	7,917[a]	7,835[a]	9,101[a]	8,787[a]
BT Retail					
BT's retail share of broadband[b] installed base	35%	34%	35%	34%	33%
BT Vision installed base	467	423	214	–	–
Call minutes (bn)					
Non geographic	11.86	14.73	19.18	25.03	34.66
Geographic	37.31	42.06	46.84	51.92	58.35
Total	49.17	56.79	66.02	76.95	93.01
Active consumer lines[c]	11,113	11,789	12,600	13,634	14,587
Average annual revenue per consumer user (ARPU)[d] (£)	309	287	274	262	251
BT Group					
Total employees[e]	97.8	107.0	111.9	106.2	104.4
Broadband lines (UK)					
BT Retail	5,132	4,757	4,402	3,659	2,668
BT Wholesale (external)	2,926	3,305	3,983	5,168	5,092
Openreach	6,620	5,750	4,300	1,910	356
Total broadband lines	14,678	13,812	12,685	10,737	8,116
Exchange lines (UK)					
Consumer	13,051	14,514	15,793	16,636	17,912
Business	5,367	5,992	6,750	7,264	7,797
External WLR lines	6,028	5,647	4,666	4,227	2,874
Total exchange lines	24,446	26,153	27,209	28,127	28,583

[a] Restated for impact of customer account moves. See page 101.
[b] DSL and LLU.
[c] Active consumer lines represents the number of lines over which BT is the call provider (excluding Northern Ireland but including Plusnet in 2010).
[d] Rolling 12 month consumer revenue, less mobile POLOs, divided by average number of primary lines.
[e] The numbers disclosed include both full-time and part-time employees.