

Telecom *plus* PLC

Adoption of International Financial Reporting Standards

The purpose of this document is to provide guidance on the impact of International Financial Reporting Standards as adopted for use in the EU (IFRS) on the financial results of Telecom *plus* PLC when they are adopted for the year ending 31 March 2006.

This document is for guidance only and the effects detailed may be amended as a result of further interpretive guidance from the International Accounting Standards Board (IASB) or to reflect industry practice.

The financial information presented in this document is unaudited.

The principal changes to Telecom *plus* PLC's reported financial information under UK GAAP arising from the adoption of IFRS are summarised below. The financial impact of these changes are detailed in the Appendices.

Background

The Group currently prepares its financial statements under UK Generally Accepted Accounting practice ('UK GAAP'). For the year ending 31 March 2006, the Group will be required to prepare its interim and annual reports, including comparatives, for previous periods under IFRS.

This document details the principal differences arising from this transition on the opening balance sheet as at 1 April 2004 ('date of transition') and on the income statement (previously the profit and loss account under UK GAAP), balance sheet and cash flow statements for the six months ended 30 September 2004 and the year ended 31 March 2005.

The revised accounting policies are also detailed in this document.

IFRS 1 exemptions

IFRS 1, First-time Adoption of International Financial Reporting Standards, establishes exemptions from the full requirements of IFRS for companies complying with them for the first time. Telecom *plus* PLC intends to elect to use the following exemptions and the financial information in this document has been prepared on this basis.

- (a) Business combinations: those prior to the transition date have not been restated onto an IFRS basis.
- (b) Share based payments: the Group is not applying the IFRS requirements to equity instruments such as share options granted on or before 7 November 2002.
- (c) Financial instruments: the Group has not restated its comparatives to reflect the requirements of IAS39 – Financial Instruments: Recognition and Measurement.

Financial Summary

	UK GAAP £'000	IFRS adjustment £'000	IFRS £'000
6 months to 30 September 2004			
Profit before tax	6,443	116	6,559
Profit after tax	4,598	144	4,742
Shareholders' equity	14,905	2,939	17,844
Basic earnings per share	7.4p	0.3p	7.7p
Diluted earnings per share	7.3p	0.2p	7.5p
Year ended 31 March 2005			
Profit before tax	10,052	405	10,457
Profit after tax	7,264	384	7,648
Shareholders' equity	13,629	4,150	17,779
Basic earnings per share	11.7p	0.7p	12.4p
Diluted earnings per share	11.5p	0.6p	12.1p

IFRS Adjustments

The main differences for the Group between reporting on the basis of IFRS compared with current UK GAAP are as follows:

(a) Goodwill amortisation

Under UK GAAP, goodwill is amortised over its expected useful economic life, whereas under IFRS goodwill is considered to have an indefinite life and is not amortised, but is tested for impairment annually.

No impairment provisions were required since the date of transition. This adjustment reverses the goodwill amortisation charged under UK GAAP since the date of transition.

(b) Share options

Under UK GAAP there was no charge to the profit and loss account for share options granted at the market price since they have no intrinsic value. IFRS requires that the fair value of such options at the date of grant is charged to the income statement. The fair value has been determined using the binomial model and is being charged to profit evenly over the vesting period of 3 years. A deferred tax asset has been recognised in respect of share options to reflect the difference between the market value and the exercise price at the Balance Sheet dates.

(c) Dividend accrual

Dividends relating to an accounting period were dealt with in that period under UK GAAP. IFRS does not recognise a dividend until it is declared, usually after the accounting period to which it relates. This adjustment writes back the accrual for the interim and final dividend as appropriate.

(d) Associated Companies

Under IFRS it is considered that the Group has the power to exercise significant influence over its investment in Oxford Power Holdings Limited and as such, the investment is now classified as an associate. This investment is accounted for using the equity method.

Accounting policies under IFRS

The restated financial information for the six months to 30 September 2004, the year ended 31 March 2005 and the opening balance sheet at 1 April 2004 (the transition date for the Group) have been prepared on a basis consistent with the Group's anticipated International Financial Reporting Standards (IFRS) accounting policies.

The accounts are prepared under the historical cost convention, except for the revaluation of certain properties and financial instruments.

Basis of consolidation

The Group's financial statements consolidate the financial statements of Telecom *plus* PLC and all its subsidiaries. Subsidiaries are consolidated from the date on which control transfers to the Group and are included until the date on which the Group ceases to control them. Transactions between Group companies are eliminated on consolidation.

Business combinations

The acquisition of subsidiaries is accounted for using the purchase method. On acquisition, the assets, liabilities and contingent liabilities of a subsidiary are measured at their fair value at the date of acquisition. Any excess of the cost of acquisition over the fair value of the identifiable net assets acquired is recorded as goodwill. Goodwill is reviewed for impairment at least annually and any impairment is recognised immediately in the income statement. Any deficiency of the cost of acquisition below the fair value of the identifiable net assets acquired is credited to the income statement on acquisition. Goodwill recorded on business combinations prior to IFRS transition has not been restated and has either been written off to reserves or capitalised according to the UK GAAP accounting standards then in force.

Goodwill

Goodwill arising on the acquisition of a business, representing the difference between the cost of acquisition and the fair value of the separable net assets acquired is capitalised and subject to impairment review, both annually and when there are indications that the carrying value may not be recoverable. Prior to 1 April 2004, goodwill was amortised over its expected useful economic life up to a maximum of 10 years.

Other intangible asset

The Group's intangible asset relates to the Billing System. It is stated at cost less a provision for depreciation, which has been calculated so as to write off the cost less estimated residual value of the asset in equal instalments over its expected useful life. Depreciation is provided over five years.

The carrying value of the intangible asset is reviewed for impairment when there is an indication that it may be impaired.

Investments in associates

An associate is an entity over which the Group 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 the investee but is not control or joint control over those policies.

The results and assets and liabilities of associates are incorporated in these financial statements using the equity method of accounting. Under the equity method, investments in associates are carried in the consolidated balance sheet at cost as adjusted for post-acquisition changes in the Group's share of the net assets of the associate, less any impairment in the value of individual investments. Losses of an associate in excess of the Group's interest in that associate are not recognised.

Revenue recognition

Revenue is the invoiced value of goods and services supplied to external customers excluding value added tax and other sales related taxes. Transactions are recorded as sales when the delivery of products or performance of services takes place in accordance with the contract terms of sale.

Leases

Payments on operating leases are charged to the income statement on a straight line basis over the lease term.

Taxation

Income tax on the profit or loss for the year comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantially enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognised, based on the balance sheet liability method, on temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

Property, plant and equipment

Property, plant and equipment are stated at cost less a provision for depreciation. Depreciation is calculated so as to write off the cost less estimated residual value of the assets in equal instalments over their expected useful lives. No depreciation is provided on freehold land. Depreciation is provided on other assets at the following rates:

Freehold buildings	- twenty five years
Leasehold improvements	- three years
Computer and office equipment	- three to five years
Motor vehicles	- four years

The carrying values of property, plant and equipment are reviewed for impairment when there is an indication that they may be impaired.

Inventories

Inventories are valued at the lower of cost, including related overheads, and net realisable value. Cost is measured on a first in, first out basis. Net realisable value represents the estimated selling price less all estimated costs of completion and costs to be incurred in marketing, selling and distribution.

Commodity contracts

The Group uses forward contracts for key energy commodities to minimise the risk of the effect of fluctuations in their cost. These forward contracts are accounted for in the accounting period in which they mature, as they are entered into and are held for the purpose of the delivery of the commodity in accordance with the Group's expected purchase requirements. The amount of any commitments under such contracts are disclosed in the Annual Report.

Research and development

Research costs are written off as incurred. Development costs incurred in the development of new or substantially improved products and processes are capitalised as intangible assets if it is probable that the expenditure will generate future economic benefits and costs can be measured reliably.

Share based payments

The fair value at the date of grant of share based remuneration, principally share options, is calculated using a binomial pricing model and charged to the income statement on a straight line basis over the vesting period of the award. The charge to the income statement takes account of the estimated number of shares that will vest. All share based remuneration is equity settled.

Segmental reporting

A segment is a distinguishable component of the Group that is engaged either in providing products or services (business segment), or in providing products or services within a particular economic environment (geographical segment), which is subject to risks and rewards that are different from those of other segments. The Group's primary reporting format is business segments

Provisions

Provisions are recognised when the Group has a present obligation as a result of a past event, and it is probable that the Group will be required to settle that obligation. Provisions are measured at the directors' best estimate of the expenditure required to settle the obligation at the balance sheet date, and are discounted to present value where the effect is material.

Pensions

The Group makes contributions to certain employees' personal pension plans. These are charged to the income statement in the year in which they become payable.

Receivables

Trade and other receivables are stated at cost less impairment losses.

Payables

Trade and other payables are stated at cost.

Cash and cash equivalents

Cash includes cash in hand and at banks. Bank overdrafts that are repayable on demand and form an integral part of the Group's cash management are included as a component of cash and cash equivalents for the purpose of the statement of cash flows. Cash equivalents comprise fixed term deposits or call deposits with an original term of less than 90 days

Interest

Net financing costs comprise interest payable on borrowings calculated using the effective interest rate method and interest receivable on funds invested. Interest income is recognised in the income statement as it accrues, using the effective interest method.

Impairment

The carrying amounts of the Group's assets, other than inventories and deferred tax assets, are reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount is estimated. The recoverable amount of assets is the greater of their net selling price and value in use.

An impairment loss is recognised whenever the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. Impairment losses are recognised in the income statement.

An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation, if no impairment loss had been recognised.

Appendices

	UK GAAP £'000	Intangible Assets IFRS3 £'000	Share based payments IFRS2 £'000	Investments in Associates IAS28 £'000	IFRS £'000
1. Unaudited Consolidated Income Statement 6 months to 30 September 2004					
Revenue	42,778				42,778
Cost of sales	(29,423)				(29,423)
Gross profit	13,355	-	-	-	13,355
Other income					-
Distribution costs	(2,854)		(48)		(2,902)
Administrative expenses	(4,326)	228	(78)		(4,176)
Other expenses					-
Operating profit	6,175	228	(126)	-	6,277
Share of profit in associates after tax				20	20
Finance income less costs	268				268
Profit before tax	6,443	228	(126)	20	6,565
Income taxes	(1,845)		22		(1,823)
Share of deferred tax of associates					-
Profit for the period	4,598	228	(104)	20	4,742
Basic earnings per share	7.4p				7.7p
Diluted earnings per share	7.3p				7.5p

	UK GAAP £'000	Intangible Assets IFRS3 £'000	Share based payments IFRS2 £'000	Investments in Associates IAS28 £'000	IFRS £'000
2. Unaudited Consolidated Income Statement					
Year to 31 March 2005					
Revenue	102,467				102,467
Cost of sales	(77,747)				(77,747)
Gross profit	<u>24,720</u>	-	-	-	<u>24,720</u>
Other income					-
Distribution costs	(5,966)		(191)		(6,157)
Administrative expenses	(9,221)	456	(111)		(8,876)
Other expenses					-
Operating profit	<u>9,533</u>	<u>456</u>	<u>(302)</u>	<u>-</u>	<u>9,687</u>
Share of profit in associates after tax	-			66	66
Finance income less costs	519				519
Profit before tax	<u>10,052</u>	<u>456</u>	<u>(302)</u>	<u>66</u>	<u>10,272</u>
Income taxes	(2,788)		164		(2,624)
Share of deferred tax of associates					-
Profit for the period	<u>7,264</u>	<u>456</u>	<u>(138)</u>	<u>66</u>	<u>7,648</u>
Basic earnings per share	11.7p				12.4p
Diluted earnings per share	11.5p				12.1p

	UK GAAP £'000	Intangible Assets IAS38 £'000	Share based payments IFRS2 £'000	Investments in Associates IAS28 £'000	Dividends IAS10 £'000	IFRS £'000
3. Unaudited Balance Sheet						
As at 1 April 2004						
Assets						
Non-current assets						
Property, plant and equipment	1,903	(384)				1,519
Goodwill	3,742					3,742
Other intangible assets	-	384				384
Investments in associates	1,038			(692)		346
Deferred tax	-		435			435
Other receivables	2,666					2,666
	<u>9,349</u>	<u>-</u>	<u>435</u>	<u>(692)</u>	<u>-</u>	<u>9,092</u>
Current assets						
Inventories	1,146					1,146
Trade receivables	1,586					1,586
Prepayments and accrued income	7,578					7,578
Cash and cash equivalents	9,857					9,857
	<u>20,167</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>20,167</u>
Total assets	<u>29,516</u>	<u>-</u>	<u>435</u>	<u>(692)</u>	<u>-</u>	<u>29,259</u>
Equity and liabilities						
Current liabilities						
Trade and other payables	(4,240)					(4,240)
Current portion of long term borrowings	(98)					(98)
Current tax payable	(1,794)					(1,794)
Other taxation and social security	-					-
Accrued expenses and deferred income	(10,370)				3,394	(6,976)
	<u>(16,502)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>3,394</u>	<u>(13,108)</u>
Total liabilities	<u>(16,502)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>3,394</u>	<u>(13,108)</u>
Total assets less total liabilities	<u>13,014</u>	<u>-</u>	<u>435</u>	<u>(692)</u>	<u>3,394</u>	<u>16,151</u>
Share capital						
Share capital	3,076					3,076
Share premium	6,625					6,625
Share option reserve	-		160			160
Retained earnings	3,313		275	(692)	3,394	6,290
	<u>13,014</u>	<u>-</u>	<u>435</u>	<u>(692)</u>	<u>3,394</u>	<u>16,151</u>
Total equity	<u>13,014</u>	<u>-</u>	<u>435</u>	<u>(692)</u>	<u>3,394</u>	<u>16,151</u>

	UK GAAP £'000	Intangible Assets IAS38 £'000	Share based payments IFRS2 £'000	Investments in Associates IAS28 £'000	Dividends IAS10 £'000	IFRS £'000
4. Unaudited Balance Sheet						
As at 30 September 2004						
Assets						
Non-current assets						
Property, plant and equipment	2,203	(349)				1,854
Goodwill	3,514	228				3,742
Other intangible assets	-	349				349
Investments in associates	1,038			(678)		360
Deferred tax	-		287			287
Other receivables	2,799					2,799
	9,554	228	287	(678)	-	9,391
Current assets						
Inventories	1,092					1,092
Trade receivables	2,761					2,761
Prepayments and accrued income	5,906					5,906
Cash and cash equivalents	13,393					13,393
	23,152	-	-	-	-	23,152
Total assets	32,706	228	287	(678)	-	32,543
Equity and liabilities						
Current liabilities						
Trade and other payables	(4,109)					(4,109)
Current portion of long term borrowings	-					-
Current tax payable	(2,356)					(2,356)
Other taxation and social security	-					-
Accrued expenses and deferred income	(11,336)				3,102	(8,234)
Total liabilities	(17,801)	-	-	-	3,102	(14,699)
Total assets less total liabilities	14,905	228	287	(678)	3,102	17,844
Share capital						
Share capital	3,100					3,100
Share premium	6,996					6,996
Share option reserve	-		286			286
Retained earnings	4,809	228	1	(678)	3,102	7,462
Total equity	14,905	228	287	(678)	3,102	17,844

	UK GAAP £'000	Intangible Assets IAS38 £'000	Share based payments IFRS2 £'000	Investments in Associates IAS28 £'000	Dividends IAS10 £'000	IFRS £'000
5. Unaudited Balance Sheet						
As at 31 March 2005						
Assets						
Non-current assets						
Property, plant and equipment	2,006	(283)				1,723
Goodwill	3,286	456				3,742
Other intangible assets	-	283				283
Investments in associates	1,038			(441)		597
Deferred tax	200		36			236
Other receivables	2,912					2,912
	9,442	456	36	(441)	-	9,493
Current assets						
Inventories	1,134					1,134
Trade receivables	2,939					2,939
Prepayments and accrued income	12,866					12,866
Cash and cash equivalents	6,275					6,275
	23,214	-	-	-	-	23,214
Total assets	32,656	456	36	(441)	-	32,707
Equity and liabilities						
Current liabilities						
Trade and other payables	(5,832)					(5,832)
Current portion of long term borrowings	-					-
Current tax payable	(1,592)					(1,592)
Other taxation and social security	-					-
Accrued expenses and deferred income	(11,603)				4,099	(7,504)
Total liabilities	(19,027)	-	-	-	4,099	(14,928)
Total assets less total liabilities	13,629	456	36	(441)	4,099	17,779
Share capital						
Share capital	3,108					3,108
Share premium	7,145					7,145
Share option reserve	-		464			464
Retained earnings	3,376	456	(428)	(441)	4,099	7,062
Total equity	13,629	456	36	(441)	4,099	17,779

6. Effect of IFRS adoption on the Cash Flow Statement

IFRS require Cash Flow Statements to present changes in cash and cash equivalents. Under UK GAAP, Cash Flow Statements presented changes in cash only. The Group did not have any cash equivalents at any Balance Sheet date presented and accordingly its cash flows are unchanged.