TalkTalk Telecom Group PLC

Annual report 2013

TalkTalk Group

We are the UK's leading value for money provider of fixed line broadband, voice telephony, mobile and television services.

In this report

Chairman's statement

This has been a year of significant progress for TalkTalk. We successfully introduced value for money pay TV to the UK mass market and in the six months since launch have built a base of nearly a quarter of a million subscribers. We also launched a mobile handset proposition for existing customers that has proved extremely popular for its range, value and simplicity. TalkTalk Business has also had a good year, delivering strong growth in new, competitively priced data products such as Ethernet and EFM.

This is quite simply, TalkTalk doing what it should – creating disruptive and value for money propositions that make our customers' lives better.

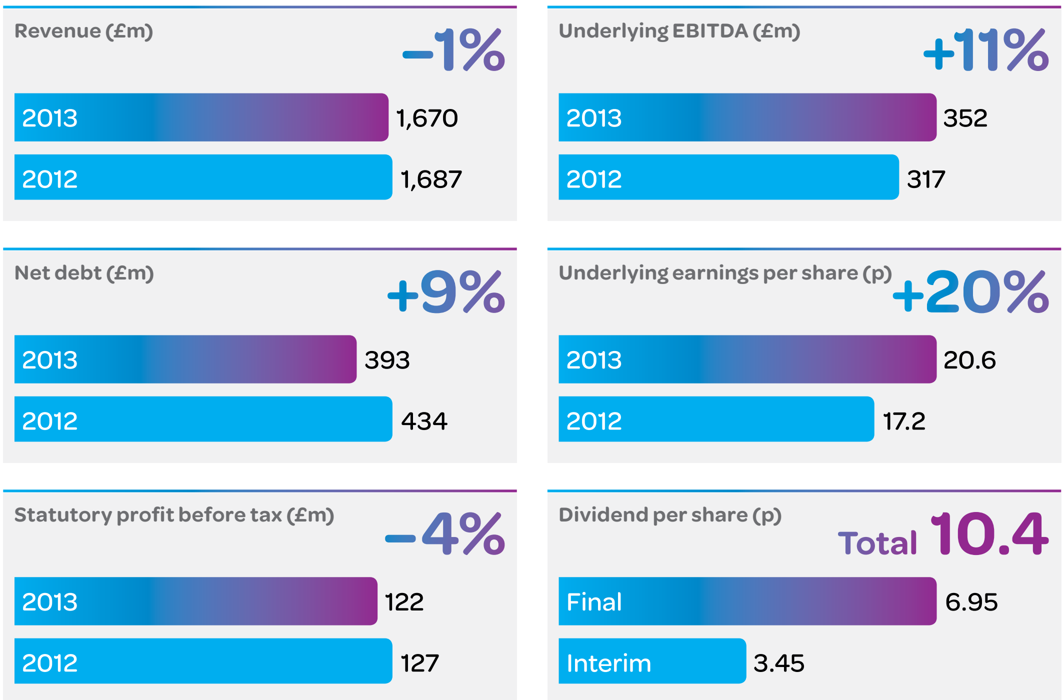
Most importantly, we continue to make great progress in simplifying our business and making our processes more efficient. The most tangible benefits of this are happier customers and reduced churn.

As a result we delivered a substantial improvement in underlying profitability which, despite our investment in TV, allowed us to grow the dividend by the 15% we committed to last year. I am pleased to report therefore that for FY13 the Board has declared a final dividend of 6.95p that, in addition to our interim dividend of 3.45p, gives a total pay-out for the year of 10.4p.

It has been another year of significant change and challenge for our employees. The Board and I would like to thank them for their efforts and for their continuing commitment to TalkTalk and to our customers.

Sir Charles Dunstone
Chairman

Financial highlights



What we do

Over the past seven years, we have built one of the UK's largest broadband and voice customer bases, attracting those looking for significant bill savings. FY13 saw us successfully implement our quad play strategy with the launch of mobile handsets for Consumer customers and an innovative, value for money TV proposition, built on the YouView platform.

Our network gives us a strong value for money advantage

We are able to offer our Consumer and Business customers services at significantly lower cost than our cable and incumbent competitors. This is because we operate the UK's most extensive Next Generation Network (NGN), which is comprised of our own advanced, highly cost effective equipment.

Our NGN now covers approximately 95% of UK homes, operating in 2,724 exchanges. These exchanges are connected via our own high-speed, high capacity all-IP national network, enabling us to carry all of our customers' voice and data traffic efficiently and cost effectively. Our customers benefit through optimised broadband speeds and quality and access to our growing range of lower cost, value add products and services. For example, our all-IP Content Delivery Network which runs over our NGN puts content closer to the end user to increase the quality of experience for our TV customers.

Services to Consumers

TalkTalk is strongly positioned as the leading value for money phone, broadband, and TV provider for UK homes. We are differentiated by our clear and simple tariff structure, low prices, flexibility and groundbreaking safety features, namely HomeSafe™, our unique network based security service which is available free of charge for all customers on our network and protects the whole home from viruses and inappropriate content.

In FY13 we successfully launched our TV proposition for Plus customers, which included a free YouView set top box. TalkTalk is one of seven partners behind YouView including the BBC, ITV and BT. YouView is a broadband based television service with differentiated catch-up and on-demand services, and an open platform for future application driven innovation. Our TV offering is proving to be a powerful proposition for mass market value seekers who want flexible access to premium content without the need to enter into costly long term subscriptions.

We also extended our TalkTalk Mobile offering from SIM-only into mobile contract handsets. Available exclusively to TalkTalk customers, TalkTalk Mobile offers simplicity, range and some of the most competitive prices in the market. As a result our mobile offering has gained strong traction amongst our base.

The launch of TV and mobile handsets are key to our aim of increasing our customers' savings, their loyalty to TalkTalk, and our revenue potential.

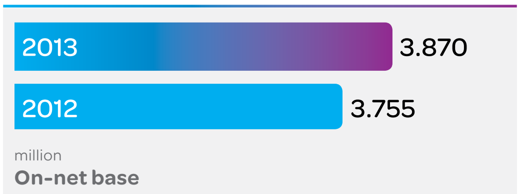
Services to Businesses

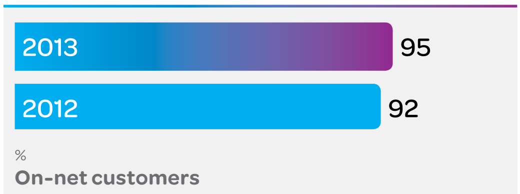
TalkTalk Business continues to drive innovation and competitive product development that leverages our NGN capability. We believe there is significant opportunity to use our network to grow all our Next Generation products within TalkTalk Business.

In January 2013, we began offering an Ethernet over Fibre service which delivers high-speed symmetrical services at a significantly lower price point than traditional Ethernet technologies. We also launched an 80Mbps fibre product with generous data allowances and network prioritisation. The year also saw us launch a very competitive Next Generation Voice service for businesses requiring high performance data and voice services, which we have made widely available to channel partners.

Market overview

At the end of December 2012 there were 22.2 million Consumer and SME fixed broadband connections in the UK, 8.5% more than at the same time the previous year. It is estimated that around 85% of UK households now have a broadband connection.





There are four key players in the broadband and TV market. BT Retail is the largest broadband service provider, followed by BSkyB. Virgin Media, the cable provider, is the third largest player followed by TalkTalk. TalkTalk is the largest unbundler.

BT Retail and Virgin Media are positioned at the premium end of the market, with significantly higher price points. They focus on speed and reliability of broadband connection. BSkyB's focus is on cross selling broadband and voice to its pay television base, providing discounts to customers who take all three products with them. BT Retail is also now competing with BSkyB on pay TV content rights, specifically sports.

Within this context, TalkTalk is clearly positioned as the leading provider for customers seeking a best value, reliable voice, broadband and TV service. Especially in TV, we have a unique proposition for those homes who want flexible access to premium content without costly long term subscriptions. We believe this reputation for value for money puts TalkTalk in a strong position and will only improve further as we grow our TV and mobile bases.

UK telecoms regulation

The UK telecoms market is regulated by Ofcom, which sets the charges and other terms for wholesale access to infrastructure and associated services owned by BT Openreach (Openreach), where Openreach is deemed to enjoy 'Significant Market Power'. Ofcom's objective is to ensure that these wholesale products enable effective competition in the market, so that consumers and businesses benefit from a choice of services and retail service providers.

Compliance with regulation is monitored by the Regulatory Compliance Committee as detailed on page 20.

The areas regulated by Ofcom that are most material for TalkTalk are:

Next Generation Access

Openreach provides wholesale access to its NGA infrastructure (predominantly FTTC), on an equivalent basis to all communication providers. The current Openreach wholesale product is GEA. TalkTalk uses GEA to provide its fibre broadband products. At present neither the price of GEA nor the margin between the GEA price and the retail price are regulated. In June 2013, Ofcom is expected to publish its Wholesale Local Access Market Review which will include proposals for regulation which would take effect from April 2014.

LLU Charge Control

On 7 March 2012, Ofcom made its statement regarding the level of Openreach charges for LLU for the period until 31 March 2014, which covers MPF, SMPF and WLR charges. It takes account of a range of factors, including Openreach's cost of capital, the regulatory valuation of local loop infrastructure, and potential efficiency gains.

TalkTalk appealed Ofcom's 2012 LLU Charge Control decision (as did BT). The Competition Commission found in favour of some of TalkTalk's grounds and some of Openreach's grounds. The net adjustment was a 78p reduction in the MPF rental charge and a £1.47 reduction in the WLR rental charge which has been implemented from 1 May 2013.

In June 2013, Ofcom is expected to publish its LLU Charge Control which will include proposed charges for the period from April 2014.

Openreach service performance

Openreach is a critical supplier to TalkTalk and we strive to work closely with them to deliver the best service for our customers, for example, the timely delivery of connections. As part of the Wholesale Local Access Market Review and LLU Charge Control, Ofcom will set new regulations in order to provide effective incentives for Openreach to provide a high quality service.

Ethernet dispute appeal

In December 2012, Ofcom published its determination to resolve a dispute regarding Openreach's pricing for various Ethernet services in the period from April 2006 to July 2009 which required Openreach to repay TalkTalk for their overcharging. Openreach have appealed that decision to the Competition Appeal Tribunal (CAT). TalkTalk (and others) have also appealed the decision arguing that the determination was too low. Further detail is provided in notes 9 and 27 to the consolidated financial statements.

Other regulation and legislation

Several other areas of current or potential legislation are significant for TalkTalk:

New Communications Bill

The Government has stated that they plan to introduce a new Communications Bill by the end of Parliament. The Department for Culture, Media and Sport (DCMS) is leading a 'Communications Review', looking at all the law and rules that affect the communications industry. DCMS has stated that they plan to publish their recommendations for any changes in the first half of 2013.

Digital Economy Act

This Act, enacted in 2010, requires ISPs to send notifications to customers (and log) whose connections have been used for illegal file sharing. Expectations are that the earliest notifications could be sent is 2015. In parallel, TalkTalk and other ISPs are discussing with rights holders alternative approaches.

Pursuant to various court orders, TalkTalk is required to block access to certain sites that are used for illegal file sharing.

Government consultation on parental controls

Between June and September 2012 the Government held a consultation into parental controls. This followed the recommendations of an independent Parliamentary Inquiry, chaired by Claire Perry MP, that pornography should be blocked by default to protect children online.

On 14 December 2012 the Government published their response to the consultation. This concluded that ISPs should actively encourage parents to switch on parental controls and take measures to ensure the person setting up the controls is over 18. TalkTalk began offering all new customers an unavoidable 'yes' or 'no' decision about whether they wanted to turn on the parental controls element of HomeSafe™ in March 2012 and will soon be extending this same unavoidable active choice to existing customers from mid 2013.

As a Board member of the UK Council for Child Internet Safety, TalkTalk continues to engage actively with Government about its policy for protecting children online.

Glossary

FTTC: Fibre to the Cabinet
GEA: Generic Ethernet Access
ISP: Internet Service Provider
LLU: Local Loop Unbundling
MPF: Full unbundling
NGA: Next Generation Access
NGN: Next Generation Network
RPI: Retail Price Index
SMPF: Partial unbundling
WLR: Wholesale Line Rental

Chief Executive Officer's statement

This has been a momentous year for TalkTalk, which is now a fundamentally better business than it was three years ago. In the year we have returned our customer base to growth, successfully launched TV and mobile handsets, grown TalkTalk Business and returned to year-on-year revenue growth in the final quarter. We have the UK's fastest growing new TV business and our customers clearly appreciate its comprehensive content and value for money pricing. We will continue to invest in growth and remain confident that having more customers who buy more products and who stay with us longer puts us firmly on track to achieve our medium term financial targets.

FY13 Business Review

We returned to growth in FY13 and have made strong progress in our key strategic priorities.

Returned customer base to growth in H2

We returned our customer base to growth in the second half of the year. Resilient demand for our value for money proposition and reducing churn has offset the decline in our legacy base.

We added 66,000 net new On-net customers in H2, comprising strong growth of 133,000 in our core MPF broadband and voice product, offset by the net loss of 67,000 legacy SMPF broadband-only customers. Over 81% of our broadband customers are now fully unbundled and able to benefit from our added value products such as Plus TV, mobile, fibre and HomeSafe™. The Off-net broadband base, which now comprises less than 5% of our total base, continued to decline, with a reduction in the second half of the year of 46,000. As a result our total broadband base grew by 20,000 during the second half of the year.

For the year as a whole, we added 115,000 net new On-net customers, comprising growth of 229,000 in fully unbundled phone and broadband customers and a net loss of 114,000 broadband-only customers. With the Off-net broadband base reducing by 118,000, we ended the year with a total broadband base of 4.063 million customers.

We have continued to deliver significant improvements to our customers' experience during the year with a 14% year-on-year reduction in calls into our contact centres, over 70% of customers now benefiting from first time resolution of their query and a substantially reduced number of complaints to Ofcom during the year – down 41% year-on-year. As a result, we delivered improvements in churn through every quarter with monthly On-net churn in Q4 of 1.5% (Q4 FY12: 1.7%).

Strong momentum in value for money quad play

230,000 TV customers in first six months and strong install momentum

We launched our TV proposition for Plus customers at the end of September 2012, featuring a free YouView set top box and no additional monthly fee. In addition to the excellent content on the YouView platform (including seven day catch up and over 70 Freeview channels including some in HD), our service features search, pause and recording of live TV and a huge library of the best films and shows from the US and UK. Our proposition also offers simply priced, easy and flexible access to bundles of over 50 premium channels including all Sky Sports channels (1, 2 ,3, 4, 5 and Formula 1) and all Sky Movie channels available for one month at a time, with no costly annual subscriptions.

Since launch we have enhanced our proposition with a wide range of transactional and on-demand content through LoveFilm Box Office and other studios and access to blockbuster movies, international on-demand and subscription content, such as Star, Star+ and StarOD, and specialist channels, such as the Digital Theatre Channel and the Karaoke Channel.

In addition to our popular engineer install which gives customers security and peace of mind, we launched a self-install option in Q4, offering free and faster installation for customers. Early feedback on the ease of installation from those customers who have opted to do it themselves is highly positive.

Since launch, when we focused initially on our existing customers, the base has grown rapidly and we ended the year with an installed base of 230,000 customers, around 25% of whom are new to TalkTalk.

Momentum towards the end of the year benefited from the availability of a self-install option and we exited the year with connections running at 12,000 per week.

Targeted at mass market value-seeking customers

Our TV proposition is targeted firmly at value-seeking customers who want a little more TV, not a lot. There is a potentially large (c. 8 million) base of customers who currently take Freeview or Freesat, many of whom do not wish to enter into costly long term Pay TV subscriptions. Our proposition is proving to be a powerful new way of watching TV for this segment of the market.

Early data from our installed base is providing strong evidence of the segmented nature of the UK TV market:

- customers who have previously been Freeview or Freesat users comprise 72% of the people taking our TV product;
- the majority of viewing by our customers is of the excellent free to air and catch-up content on YouView (c. 19.5 hours per week on average), with the balance (c. 2.5 hours) on paid-for content; and
- 20% of our TV customers have bought one or more paid-for boosts (mainly family and kids' entertainment packages and popular films) with many showing a significant propensity to buy content beyond the initial sign-up. We have seen particular success with transactional video on-demand for blockbuster movies such as The Hobbit and Life of Pi.

Positive feedback from installed base and lower churn

Survey* results from our customers reveal high levels of satisfaction with the sign-up process, installation and functionality of TalkTalk TV:

- integrated catch-up TV on the YouView platform is proving to be the most valuable feature for customers from both Pay TV and Freeview backgrounds;
- customers with previous experience of Pay TV cite the wide range of paid-for content boosts and the flexibility of purchasing without long term subscriptions as very attractive; and
- content browsing and purchasing reflects the core demographic of our family and value orientated customer base, with Entertainment and Children's packages, and transactional video on-demand proving the most popular.

* ICM Research, May 2013, 1,025 respondents.

As a result, these customers are significantly more likely to recommend TalkTalk than dual play customers, reporting a c. 20 point higher Net Promoter Score. They are also showing more loyalty and the churn from customers taking TV is materially lower than the churn on our dual play base, with seven out of ten customers who upgraded from phone and broadband saying they were more likely to stay with TalkTalk beyond their contract terms than they would have been before taking TV.

Strong pipeline of product and content development

Looking ahead, in FY14, we plan to broaden our proposition to appeal to all our customers by launching a value for money Essentials TV product. This will enable us to provide an even better value for money route for Freeview upgraders. The Essentials TV product will consist of a smaller, lower cost set top box with no PVR and only one tuner.

We will also extend our content offering for all customers with a range of specialist channels including foreign language titles, education and entertainment.

175,000 mobile customers with lower churn

In August 2012, we launched our TalkTalk Mobile contract handset proposition. Available exclusively to TalkTalk customers, TalkTalk Mobile offers simplicity, range and great value plans. All handsets, of which there is a broad range available, are completely free with 24 month contract plans starting from £5 a month. Mobile handset contracts are designed to pay back within the 24 month contract term and are ARPU and EBITDA accretive.

Three plans are available – Small, Medium and Large with different prices depending on the choice of handset. Customers can buy online or over the phone, with those buying online getting double the data allowance. This simplicity, coupled with low running costs, means that we can offer the most popular handsets at competitive prices, ranging from basic feature phones to smartphones.

As a result our mobile offering has gained strong traction, with 175,000 customers now taking advantage of our innovative mobile-to-fixed calling offers, competitive call rates and handsets. As with TV, the feedback from our mobile customers is highly encouraging:

- mobile customers are significantly more likely to recommend TalkTalk than dual play customers, reporting a c. 20 point higher Net Promoter Score; and
- churn from customers taking TalkTalk Mobile is materially lower than the churn on our dual play base, with seven out of ten customers saying they were more likely to stay with TalkTalk beyond their contract terms than they would have been before taking mobile.

We will continue to develop our mobile proposition with further innovative tariff and bundle offers and see real opportunities to build a growing and profitable scale base.

Fibre building gradually

Demand for fibre grew gradually during FY13 with 65,000 more customers choosing to take paid-for speed uplifts (versus 8,000 in FY12), taking our base of fibre customers to 73,000.

As expected, overall fibre demand among our customer base remains modest. We expect this will continue until the customer benefits of much higher bandwidth, and the value of accessing that bandwidth, become clearer. Nevertheless, there are certain segments of our customer base that can derive clear value today from upgrading to fibre, for example those who are interested in taking TV from us and live in a fibre-enabled area but whose copper speed is currently lower than 3Mbps.

We remain actively engaged with Ofcom and the Government to promote greater competition in fibre through a tighter regulatory framework. We are pleased to see Ofcom taking the importance of a level playing field increasingly seriously, with the recent opening of an investigation into BT's pricing of fibre.

Chief Executive Officer's statement continued

TalkTalk Business delivering margin accretive growth

Our TalkTalk Business customers take our On-net and Off-net basic phone and broadband products and Corporate products and services (data, carrier and voice products). Corporate revenue grew by 1.9% year-on-year to £322m as strong growth in data services (29%) and carrier (10%) offset a 5% decline in lower margin legacy voice related revenues.

Data services, which include Ethernet, managed networks and co-location, has built momentum rapidly through the year, as we continued to expand our product set and scale up our volume capability. We connected over 6,000 Ethernet circuits during the year, taking our total base to over 10,000. Revenues from this high margin product family tripled during the year to over £15m (FY12: £5m) and we expect continued strong demand through FY14.

We made significant progress in our partner channel as we continued to drive innovative and competitive product development that leverages our network reach. In May 2012, as part of a consortium led by Fujitsu, we were awarded a contract to provide network services for the phone and broadband customers of the Post Office. The contract, worth over £100m over five years, is on track for services to go live during the second half of FY14.

In December 2012, we reached an agreement with Virgin Media Business on a five year contract worth over £40m to provide additional choice for its Off-net Ethernet connectivity.

Towards the end of the year, we were awarded a six year contract by the Iceland retail group to support their data and voice requirements across the UK, demonstrating our ability to provide Corporate customers with complete data and voice solutions.

In addition to the continued growth of margin accretive data products, we are realising opportunities to grow our carrier revenues and next generation voice products. Together, this is allowing us to offset the established decline in low margin legacy voice revenues.

We also have an opportunity, with our business customers, to simplify operations and leverage the cost and technology advantage of our network. The combination of gross margin expansion through data revenue growth and generating cost savings through simplification will contribute meaningfully to the Group's medium term revenue and margin targets.

Largest unbundled network in the UK

Our unbundling programme continued with 216 new exchanges added during the year, extending the reach of our value for money proposition to 2,724 exchanges and approximately 95% of the UK population. We plan to unbundle another 300 exchanges in FY14 and now see the potential to extend the programme beyond that as the cost of unbundling exchanges falls and On-net customer ARPU grows, allowing us to continue to profitably extend our geographic reach.

In conjunction with our unbundling programme, we continue to expand the capacity of our network, which we expect to grow by 50–100 times over the next three to five years. The favourable economics of our network, which allows us to lease dark fibre at very competitive rates, means that we will be able to achieve this capacity expansion within our long run capex guideline of 6% of revenues.

Driving operating efficiencies

During the year we completed our Operating Efficiencies programme which has delivered £50m of annualised cost savings, a more efficient business and a better experience for our customers. The financial benefit of this programme in FY13 was a reduction in overheads of £25m.

We see further opportunity to make TalkTalk simpler to operate, which in turn will improve our customers' experience and reduce our costs, through driving process and efficiency improvements over the medium term. These are a key component of our medium term plan to achieve a 25% EBITDA margin.

During FY13 we began our new Making TalkTalk Simpler programme. We expect that combined initiatives under this programme will drive incremental savings of £30m–£50m over the next three to five years, of which £10m has been actioned during 2013. During this first phase of the programme we: began the process of restructuring the systems and processes that service our TalkTalk Business customers to remove duplication and better align our sales and service model with our growth ambitions; completed the closure of our Stoke Mandeville site; consolidated the development of our IT systems under one partner; and continued to improve online functionality across the business. These initiatives have delivered £3m of savings during the year.

Summary

In summary, FY13 has been a momentous year for TalkTalk. We have returned the business to growth, successfully launched the fastest growing triple play proposition in the UK and a mobile base with real traction and delivered strong growth in margin accretive data products. At the same time we have continued to make the business simpler to operate and successfully begun to deliver on our third cost saving programme.

FY14 Financial guidance

We have entered the new financial year with growing revenues, a higher gross margin, lower overheads and significant headroom to invest further in growth.

- Revenue
  We expect FY14 revenues to grow by at least 2%.
- Overheads
  After benefiting from some acceleration of the savings from Making TalkTalk Simpler in FY13, we expect overheads as a percentage of revenues to remain broadly flat in FY14.
- SAC and Marketing
  We expect total SAC as a percentage of revenues to peak in FY14 as we invest in building a scale base of TV subscribers, drive further penetration of mobile and fibre into our customer base and continue to grow TalkTalk Business. SAC per customer, both for TV and non-TV customers, is expected to continue to reduce through the year.
- Net debt
  Capex is expected to be within our guideline of 6% of revenue and working capital is expected to show outflows of £15m–£20m as we grow the business.

  Cash exceptional items are expected to be in line with the incremental annualised savings benefits from our Making TalkTalk Simpler programme of £10m.

  The costs of repurchasing shares to satisfy incentive schemes is expected to be similar to that incurred in FY13.

  We expect to begin making modest cash tax payments during FY14.
- Dividend
  We remain firmly committed to dividend growth whilst also investing in the business. This commitment is supported by the profitability of our core business, underlying cash generation and overall financial strength. While we plan to invest substantially in growing our business during FY14, we are reiterating our commitment to grow the dividend by a minimum of 15%.

FY15 and beyond

We are on track to achieve our medium term targets of 2% CAGR in revenue and 25% EBITDA margin.

We expect the components of our revenue growth strategy (improving On-net customer mix, growing TV and mobile penetration and growth in TalkTalk Business) also to contribute to our profitability target, through gross margin over the medium term.

We expect the balance of our profitability target to be delivered through both overhead reduction (driven, amongst other things, by our Making TalkTalk Simpler programme) and SAC declining from its FY14 peak (driven by reducing churn and falling costs per addition).

As a result we expect to deliver strong EBITDA growth in FY15 and subsequent years, which we expect to support continued dividend growth at a similar rate to FY14.

Chief Financial Officer's statement

Overview

We have delivered another strong performance this year, with a return to revenue growth in the final quarter of the year and significant increases in both our underlying profitability and cash generation.

Revenue growth in the latter half of the year has been driven primarily by growth in ARPU, our Broadband customer base returning to growth and the launch of new products for both our Consumer and TalkTalk Business customers.

In launching our new TalkTalk TV service this year we have invested £62m incorporating both the incremental SAC for those taking the service and one-off launch costs. To enable year-on-year comparisons we have included a measure of Underlying EBITDA, which shows our results before the investment in TV.

Our gross margin has increased as more of our customers are On-net and take both their broadband and voice from TalkTalk. Strengthening gross margin and delivery on our cost efficiency programmes has increased underlying profitability. The business continues to be strongly cash generative and has this year generated £41m net cash flow after funding a 15.6% growth in the divided and the additional investment in TV.

Net debt has reduced to £393m (FY12: £434m) providing significant headroom to invest in driving continued growth.

Underlying and Headline financial information

	2013 £m	2012 £m	Growth
On-net	**1,170**	1,084	8%
Off-net	**178**	287	(38)%
Corporate	**322**	316	2%
Revenue	**1,670**	1,687	(1)%
Gross margin	**919**	884	4%
%	**55.0%**	52.4%	
Operating expenses excluding amortisation and depreciation	**(567)**	(567)	–
Underlying EBITDA	**352**	317	11%
%	**21.1%**	18.8%	
Investment in TV	**(62)**	–	
Sale of freehold property	**–**	9	(100)%
Headline EBITDA	**290**	326	(11)%
Exceptional items	**9**	(27)	>(100)%
EBITDA	**299**	299	–
Depreciation and amortisation	**(102)**	(92)	(11)%
Non-operating amortisation	**(52)**	(61)	15%
Share of joint venture	**(4)**	(1)	>(100)%
Operating profit	**141**	145	(3)%
Finance costs	**(19)**	(18)	(6)%
Profit before tax	**122**	127	(4)%
Tax	**(22)**	11	>(100)%
Profit after tax	**100**	138	(28)%

Revenue

We returned to year-on-year revenue growth in the year, with revenue up 1.4% in the last quarter primarily driven by strong On-net ARPU progress; growth in the customer base and take up of our new products. Our full year revenue decreased 1% to £1,670m (FY12: £1,687m), with continued growth in On-net and Corporate offsetting the expected decline in our legacy Off-net business.

Growth in On-net revenues, which increased to £1,170m (FY12: £1,084m), has been driven by both the growth in our base and the growth in our On-net ARPU, which increased to £26.37 in Q4 (Q4 FY12: £25.47). This has resulted from upsell activity and price inflation, offsetting planned promotional spend and the continued decline in voice usage.

Our Corporate revenue grew in the year to £322m (FY12: £316m), driven by the growth of our new data products and carrier services which more than offset the continued decline in legacy voice services.

In line with the expected decline in our Off-net base, Off-net revenues decreased to £178m (FY12: £287m). Price inflation during the year partly offset the base and usage decline.

Gross margin

We expanded our gross margin by 260 basis points to 55.0% (FY12: 52.4%) and £919m (FY12: £884m) driven by the improved mix of higher value On-net broadband and voice customers, price inflation, growth in our TalkTalk Business data services revenue, offset by the decline in lower margin Off-net revenues.

Operating expenses

Operating expenses comprising customer service costs, Network and IT and management overheads have reduced to £395m (FY12: £415m) and represent 23.7% of revenues (FY12: 24.6%), reflecting the delivery of cost savings from our Operating Efficiency programmes, offset by the continued investment in our network.

During the year we completed our Operating Efficiency programmes delivering a total saving of £50m of which £25m was realised in the year.

SAC and Marketing (excluding TV)

We successfully launched handsets with our Mobile proposition this year, saw a gradual increase in the number of customers taking fibre, and our Broadband base returned to growth. TalkTalk Business also had a year of growth driving incremental SAC. The investment in SAC and Marketing resulted in an increase in spend yea-on-year of £20m to £172m (FY12: £152m). Our total operating expenses for the year were therefore flat overall at £567m (FY12: £567m).

Underlying EBITDA

We have had strong growth in Underlying EBITDA and our margin has increased to 21.1% (FY12: 18.8%), resulting in an 11% increase in our full year result to £352m (FY12: £317m). In FY12 we disposed of a freehold property at a profit of £9m that was excluded from Underlying EBITDA.

Investment in TV

We have made a significant investment this year to deliver the highly successful launch of our TV service. We have invested £62m, of which £39m is the specific, incremental SAC cost of acquiring the TV customers, and £23m represents the one-off, fixed costs of launch, being the cost of the trial, the project team employed to deliver our TV product, the cost of ramp up of our installation engineers, the marketing spend and content offered to support the launch and other similar costs.

Headline EBITDA

As a result of our investment in TV, Headline EBITDA has decreased £36m to £290m (FY12: £326m).

Exceptional items

The net exceptional credit in the year of £9m, comprised a credit of £27m received from BT in settlement for the overcharging of certain Ethernet circuits between April 2006 and July 2009, offset by the investment in the second phase of our Operating Efficiencies programme (£11m) and the beginning of our Making TalkTalk Simpler programme (£7m). The exceptional costs principally comprise redundancy, site exit and dual running costs incurred in streamlining our IT systems and processes and improving our Consumer and TalkTalk Business service model.

EBITDA

EBITDA after exceptional items is flat year-on-year at £299m as savings seen in our operating costs and the decrease in spend on exceptional items has been offset by the increased investment in our new products, TV, Mobile, Fibre and Ethernet.

Depreciation and amortisation

The charge for depreciation and amortisation has increased by £10m (10.9%) to £102m (FY12: £92m) as a result of a further year of capital investment in both our network and our IT systems.

Amortisation of acquisition intangibles

The amortisation charged on acquisition intangibles decreased to £52m (FY12: £61m) as the customer base acquired with the acquisition of AOL in December 2006 became fully amortised during the year.

Profit before tax

Profit before tax decreased £5m in the year reflecting the reduction in Headline earnings due to the investment in TV.

EPS

	2013	2012	Growth
Underlying earnings[(1)] (£m)	**182**	152	20%
Basic EPS	**20.6p**	17.2p	20%
Diluted EPS	**19.4p**	16.4p	18%
Headline earnings (£m)	**132**	159	(17)%
Basic EPS	**14.9p**	18.0p	(17)%
Diluted EPS	**14.0p**	17.2p	(19)%
Statutory earnings (£m)	**100**	138	(28)%
Basic EPS	**11.3p**	15.6p	(28)%
Diluted EPS	**10.6p**	14.9p	(29)%

(1) Underlying earnings for the year ended 31 March 2013 of £182m is defined as Headline earnings excluding costs of £62m relating to the investment in TV less an allocation of taxation of £12m based on the Group's Headline effective tax rate. In the year ended 31 March 2012, Underlying earnings of £152m was defined as Headline earnings excluding the profit on sale of a freehold property of £9m less an allocation of taxation of £2m based on the Group's Headline effective tax rate.

We provide EPS on an Underlying and Headline basis alongside our Statutory measures to allow easier comparison year-on-year due to the impact of exceptional items, the investment in TV and the disposal of a freehold property in FY12. A full reconciliation to Statutory results can be found in note 9 to the consolidated financial statements.

Chief Financial Officer's statement continued

EPS continued

Our Underlying Basic EPS, which is stated before the investment in TV and exceptional costs, has grown significantly year-on-year, increasing 20% to 20.6p (FY12: 17.2p). Our Headline Basic EPS decreased 17% to 14.9p (FY12: 18.0p), with the growth in our Underlying EBITDA offset by the investment in TV.

Statutory Basic EPS decreased 28% to 11.3p (FY12: 15.6p), principally due to the investment in TV and a tax credit that was recognised in the prior year.

Cash flow and net debt

	2013	2012	Growth
Headline EBITDA	**290**	326	(11)%
Working capital	**(11)**	(14)	(21)%
Capex	**(104)**	(105)	(1)%
Operating free cash flow	**175**	207	(15)%
Exceptional items – BT credit	**27**	–	
Exceptional items – Operating efficiencies	**(19)**	(35)	(46)%
Exceptional items – Ofcom fine	**–**	(3)	(100)%
Exceptional items – One Company	**–**	(7)	(100)%
Acquisitions and disposals	**(4)**	(20)	(80)%
Dividends paid	**(87)**	(58)	50%
Interest and tax	**(16)**	(26)	(38)%
Share purchase	**(35)**	(54)	(35)%
Net cash flow	**41**	4	>100%
Opening net debt	**(434)**	(438)	(1)%
Closing net debt	**(393)**	(434)	(9)%

Capital expenditure

Capital expenditure in the year of £104m (FY12: £105m) is broadly flat year-on-year, and represented 6.2% of revenue (FY12: 6.2%). During the year, we have continued to invest in our network and have rolled out a further 216 exchanges, significantly increased capacity across the network and invested in improved resilience. We have also continued to invest in our IT systems to support our growing product offerings.

Working capital

Our working capital outflow of £11m was broadly in line with the prior year (FY12: £14m), and resulted from our return to revenue growth in H2, the decrease in our cost base and the continued unwind of Tiscali fair value provisions.

Exceptional items

We had net inflow on exceptional items this year of £8m (FY12: outflow of £45m) driven by the £27m of cash received from BT in settlement for the overcharging of certain Ethernet circuits between April 2006 and July 2009. Exceptional spend of £14m was incurred in respect of the completion of our Operating Efficiencies programmes and £5m relating to the Making TalkTalk Simpler programme.

Acquisitions and disposals

Acquisitions in the year of £4m (FY12: £20m) represent a £6m investment in the YouView joint venture offset by £2m of proceeds on the sale of Southern Communications Networks Limited, an immaterial subsidiary company, at the end of the year.

Dividends

Our dividend policy is to return to shareholders 50% of our basic Headline earnings per share in the form of ordinary dividends.

In May 2012, we committed that during 2013 and 2014, when the business will be investing in growing the TV base, our dividend will grow by a minimum of 15%.

Dividends of £87m paid in the year (FY12: £58m), comprised the final dividend for FY12 of 6.4p and the interim dividend for FY13 of 3.45p, which reflects our 15% dividend growth commitment.

The Board has declared a final dividend of 6.95p per share which will be paid on 2 August 2013, subject to approval at the AGM on 24 July 2013 for shareholders on the register at 5 July 2013. The total declared dividend for the year was 10.4p, which provides dividend cover (based on Headline earnings per share) of 1.4 times (FY12: 2 times).

Share purchases

In September 2012 the first tranche of both the TalkTalk Group Value Enhancement Scheme and the Carphone Warehouse TalkTalk Group Value Enhancement Scheme (together referred to as "the VES schemes") vested. Settlement took the form of purchasing the participants' VES shares in return for a combination of the issue of new PLC shares and cash, resulting in a cash outflow of £35m. In the prior year, share repurchases totalling £54m (42 million shares) were made by the Group ESOT in order to cover anticipated future options exercises.

Net debt

Net debt in the year reduced by £41m (FY12: £4m) to £393m (FY12: including loans to related parties £432m, excluding loans to related parties £434m) as a result of the continuing improvement in the operating cash generation of the business and a reduction in exceptional spend.

Taxation and treasury

	2013		2012	
	Headline	Statutory	Headline	Statutory
Operating profit	**184**	**141**	233	145
Finance costs	**(19)**	**(19)**	(18)	(18)
Profit before tax	**165**	**122**	215	127
Tax	**(33)**	**(22)**	(56)	11
Profit after tax	**132**	**100**	159	138
Headline tax rate	**20%**		26%	

Finance costs

Net finance costs charged to the income statement were £19m (FY12: £18m). This comprised the blended interest charge on debt of 3.58% (FY12: 3.17%) and a full year of the amortisation charge in relation to the facility fees incurred on our November 2011 debt refinancing of £3m (FY12: £1m).

Net interest paid (including refinancing fees) in the year decreased to £16m (FY12: £24m), principally due to the facility fees paid in the prior financial year for the refinancing and an overall decrease in our interest charges as a result of lower average debt.

Taxation

Our effective Headline tax rate for the year was 20% (FY12: 26%), representing a tax charge of £33m (FY12: £56m). The tax charge for the year on statutory earnings was £22m (FY12: credit of £11m). The principal difference between the tax charge and the standard rate of corporation tax is the recognition of deferred tax assets in relation to acquired losses.

A reduction in the rate of corporation tax from 24% to 23% in April 2013 has created a charge through the income statement of £5m resulting from the downward revaluation of our deferred tax assets.

During the prior year the Group reached agreement with HMRC over the utilisation of brought forward losses acquired with the Tiscali UK business in 2009, including those of Video Networks Limited. This resulted in the recognition of deferred tax assets of £45m, in addition to those that were recognised at the acquisition date.

We have made minimal corporation tax payments during the year. Payments of £2m made in the prior year related to the final corporation tax assessment for our AOL Luxembourg entity prior to its liquidation.

Funding

We finance our operations with committed bank facilities, retained profits and equity. During the year, we were able to make use of overdrafts and uncommitted facilities to assist with working capital management. Our subsidiaries are funded centrally, with an emphasis on efficient cash management.

Our total Group funding of £665m comprises £560m revolving credit facilities, which mature in November 2015, £30m of bilateral loan facilities that mature in March 2015 and November 2015, and a £75m term loan that matures in March 2015. The terms of our facilities are similar and the covenants are identical. At 31 March 2013 £400m (FY12: £436m) had been drawn down under these facilities.

We are in compliance with the covenant conditions on all funding facilities at the year end. It is our policy to refinance our facilities significantly in advance of maturity dates.

Hedging policy

We are exposed to limited cross border transactional commitments, but where significant these are hedged using forward currency contracts. Interest rate risk is managed by the use of interest rate swaps. The Group aims to fix the interest cost on a proportion of its net debt over a weighted average period. The Group Treasury function operates within the framework approved by the Board, in line with best practice, to ensure effective management of our interest and foreign exchange risk.

Capital structure

The Board reviews the capital structure of the Group on an annual basis and, as discussed in note 19 to the consolidated financial statements, considers that our medium term target gearing is 75% to 100%. Gearing at 31 March 2013 was 89% (FY12: 98%).

Accounting developments

The adoption of accounting standards in the year, as disclosed in note 1 to the consolidated financial statements, has had no material effect on the consolidated financial statements.

Going concern

The Directors have acknowledged the guidance 'Going Concern and Liquidity Risk: Guidance for Directors of UK Companies 2009', published by the FRC in October 2009.

Our business activities, together with the factors likely to affect our future development, performance and position are set out in the Chief Executive Officer's statement on pages 4 to 7. Our financial position, cash and borrowing facilities are described within this Chief Financial Officer's Statement. In addition, note 19 in the financial statements describes how we manage financial risk, including foreign exchange risk, interest risk and liquidity risk.

Whilst the current economic climate remains uncertain, the breadth of our base, our value for money proposition, continuing improvements in operating efficiency and the largest unbundled network in the UK together with the launch of our competitive TV and Mobile offerings means that the Directors are confident in our ability to continue to compete effectively in the UK telecoms sector.

We have £665m of committed credit facilities and as at 31 March 2013 the headroom on these facilities was £265m. Our forecasts and projections, taking into account reasonably possible changes in trading performance, indicate that there is sufficient headroom to our facilities and that this, together with our market positioning, means that we are well placed to manage our business risks successfully and have adequate resources to continue in operational existence for the foreseeable future. The Directors have therefore adopted the going concern basis of accounting when preparing the consolidated financial statements.

Principal risks and uncertainties

In common with other organisations, we are affected by a number of risks, not all of which are in our control. Some risks, such as UK macroeconomic factors, are likely to affect the performance of UK businesses generally, while others are particular to our operations. This section sets out the material risks to the Group and how we seek to mitigate them in the day to day running of our business.

1 Competitive environment

Potential impact: Increased competition in the UK voice, broadband and TV market may impact financial performance.

Mitigation: We regularly monitor the product offerings of our key competitors as well as the latest market and consumer trends. This ensures we identify opportunities to strengthen our competitive position by broadening and enriching the products and services we offer and by finding ways to deliver greater benefits for our value-seeking customers. This financial year, TalkTalk successfully launched both a new TV and mobile handset proposition. These new product offerings will enable TalkTalk to differentiate ourselves from other triple and quad play providers in the marketplace.

2 Regulatory environment

Potential impact: Changes in regulation can significantly impact the Group's performance.

Mitigation: We actively participate in pricing consultations by Ofcom, including the use of independent experts to provide assistance and evidence as required. Current reviews are underway of the Wholesale Local Access Market Review, LLU Change Control and the Wholesale Broadband Access Market Review. There is close liaison with Ofcom to ensure that the Group's views on the future of regulation are well represented.

3 Regulatory compliance

Potential impact: Failure to operate effective processes and controls across the Group may have an adverse impact on the services we deliver to our customers, leading to churn, and non-compliance with regulatory requirements.

Mitigation: The Group's Regulatory Compliance Committee convenes at least quarterly to monitor the mitigation of operational risks which could give rise to customer complaints and regulatory breaches. This financial year, a new Consumer Quality & Compliance department has been established with responsibility for the independent monitoring of compliance for Consumer customers. The Director of Quality & Compliance chairs a weekly operational Compliance Committee meeting which is attended by senior executives.

4 Change management

Potential impact: We continue to review, rationalise and integrate our IT infrastructure and to simplify the way in which we operate our business. Disruption to our operations could have an adverse impact on the services we provide to our customers and on our financial performance.

Mitigation: The Executive Committee regularly monitors the progress of our significant change programmes and their associated risks. TalkTalk's Group Change Forum, comprised of senior executives, is responsible for establishing and monitoring adherence to the governance framework which determines how change is managed.

5 Data security

Potential impact: Failure to prevent the loss or exploitation of personally identifiable or commercially sensitive information could result in loss of competitive advantage, regulatory fines, damage to the brand and ultimately churn.

Mitigation: We continually review the Group's data security, investing in and implementing new solutions, both to prevent and detect security breaches, as they become available. In addition, the Data Governance Council, chaired by the Chief Technology Officer, meets fortnightly throughout the year to review data security risks and progress with their mitigation.

6 Network stability and reliability

Potential impact: Failure to provide a stable and reliable service may cause customer churn.

Mitigation: We have continued to invest heavily in our network to improve resilience and performance and to ensure we keep pace with our customers' growing demands.

7 Key suppliers

Potential impact: The Group has a number of critical suppliers. Failure of any of these suppliers could significantly affect the Group's ability to continue operations and to maintain its financial performance.

Mitigation: We continue to review our processes and controls around supplier selection and in-life risk management. This helps to reduce the likelihood and potential impact of business interruption due to supplier failure.

8 Customer experience

Potential impact: Failure to deal with customer queries, resolve service faults and other issues in line with our customers' expectations could lead to complaints, damage to our brand and customer churn.

Mitigation: We are committed to continuously reviewing and improving the level of customer service we provide. In FY13 we have launched a number of initiatives to i) reduce the likelihood of customers experiencing service issues, ii) improve the ability of our customers to self-help via new online tools and iii) delivering better training and tools to our Customer Service teams so that queries and complaints can be handled more effectively.

9 Scaling TV

Potential impact: Having successfully launched a TV service with YouView, there is a risk that TalkTalk is unable to maximise competitive advantage through its failure to scale its network, operations and supply chain efficiently.

Mitigation: There are a number of areas of focus: i) YouView continues to invest in innovation and to roll-out its strategic product roadmap, ii) TalkTalk has recently launched a TV self-install proposition to support our TV rollout, iii) the Group continues to invest in the network and to plan for future capacity requirements, iv) TalkTalk continues to work closely with the major content providers to secure distribution rights for the most popular content, v) the Group and its strategic partners are focused on and have plans in place to continually improve the resilience of the supply chain.

Sustainability review

Leading the way to a digital society, environmental sustainability and community.

We believe that innovative digital communications can improve our society and environment.

Our strategy is to help make our community a brighter and more sustainable place by motivating our people, customers and supply partners, and by creating innovative services that empower our customers.

Our efforts this year were focused on the following programmes:

Digital safety

Households and businesses are connecting ever more devices to the internet, and we want to empower customers to protect themselves from security risks and inappropriate content.

We offer HomeSafe™, which automatically protects every device on a home broadband connection, free with all our Consumer broadband packages. HomeSafe™ is built into our network and prevents users from reaching sites in categories deemed inappropriate by the account holder. It is also capable of automatically blocking access to sites that are believed to harbour viruses or other threats.

TalkTalk is the only broadband provider to offer such a service, and nearly three quarters of a million homes across the country have enabled HomeSafe™.

In FY13 we tailored a similar service specifically for Business customers called WorkSafe. This service is free with all Business broadband and Superpowered Fibre Business broadband services.

Digital inclusion

Talk Digital Heroes Awards 2012

We continue to sponsor these awards, run in conjunction with charity Citizens Online and The Daily Mirror. The awards aim to reward individuals, nominated by their communities, who use digital technology in the most socially positive way. In FY13 we awarded over £70,000 in grants and prizes to twelve regional finalists, including £10,000 to the 2012 TalkTalk Digital Hero.

The judges were our Chairman (Sir Charles Dunstone), the UK Digital Champion (Baroness Lane-Fox) and the Editor of The Daily Mirror (Lloyd Embley). They judged the 2012 TalkTalk Digital Hero to be Clare Sutcliffe of Code Club, an organisation aimed at giving children the chance to learn computer programming for free. Their mission is to give every child in the UK the chance to learn to code, and they want a Code Club in 25% of primary schools in the UK by 2016. The clubs are free to both the schools and the pupils.

The new category of Young Digital Hero, open to anyone under 18, was won by May Gabriel, founder of 'It's OK', a campaign which tackles the stigma around depression.

TalkTalk Digital Champions

The year saw the Group launch its enhanced Give Something Back programme that gives all our people paid time off to volunteer and fundraise for good causes. In FY13 our people were given the opportunity to be trained by the Online Centres Foundation, to become TalkTalk Digital Champions. Once trained, the Digital Champions were matched with their local UK Online Centre, so that they could pass on their learnings.

Go ON UK

The Group is a Founder Partner of the charity Go ON UK, with the likes of Age UK, the BBC and Big Lottery Fund. The charity is chaired by Baroness Lane-Fox. Together we work with the Government to help make the UK the world's most digitally capable nation. Aside from funding, we lend our online safety and digital inclusion expertise and central London office space.

A key piece of collaborative work in 2012 was the publication of a study – in partnership with Booz & Company – that concluded that there is a £63bn potential GDP uplift in the UK achieving its full digital potential. For more visit go-on-uk.org.

Talk about autism

This year we continued our support for long term partner Ambitious about Autism, the national charity that makes the ordinary possible for children and young people with autism, including Asperger's Syndrome. Talk about Autism is the safe, friendly, online community where affected families can share their experiences, get support and help others to understand the condition. For more on autism visit talkaboutautism.org.uk.

North Kensington Estate project

We have continued to fund the IntoWork programme of North Kensington-based charity The ClementJames Centre. We focus our support on IT outreach by taking broadband to the local housing estates and community centres. The project has been able to help individuals, most often immigrant women, who are typically unsure about engaging online. Next year our focus will be on training local women as IT Ambassadors, empowering them to run IT classes for beginners.

Brownie Computer Badge

This year we've worked with Girlguiding, in support of the Brownie Computer Badge, specifically to help ensure that girls are supported in using the internet safely. In addition to lending our expertise in this area, we also provided funding for the project.

Sustainability review continued

Environmental sustainability

CO_2 emissions

This year we have continued our focus on measuring and reducing our environmental impact. In particular: the CO_2 emissions related to our consumption of energy – by far our biggest impact.

Our continuing strategy to reduce our CO_2 emissions is twofold. Firstly, to reduce our energy consumption and secondly, to carefully consider the energy's provenance.

Our NGN is one of the biggest and most advanced in the UK. It grows in line with our customer volume and their rapidly expanding broadband consumption habits. We therefore measure our CO_2 emissions relative to the network's scale, so that we stay focused on improving our efficiency or 'emissions intensity'.

In 2011, our Chief Executive Officer set our objective: to reduce our CO_2 emissions intensity, in tonnes of CO_2 equivalent per Gigabit (tCO_2e/Gb), by 25% by April 2021, relative to 2010.

This focus on improving our emissions intensity has produced tangible results. We participate in the Government's CRC Energy Efficiency Scheme, and were 148th out of 2,097 participants (2012: 381st).

Our internal tracking also shows that our approach is working, as despite growing the network in line with customer usage and volume, we have improved energy intensity for the second year running:

tCO_2e/Gb	2013	2012	2011
Energy(1), transport(2) and hotels	145	193	317

(1) Primarily electricity, but also some natural gas and back-up generator fuel.
(2) Includes rail, air and car travel.

100% renewable electricity

All of the units of electricity consumed by our NGN, offices and UK call centres come from renewable sources.

Sustainable forestry

We display FSC and PEFC certification marks on the envelopes of our consumer direct marketing and bills, recognising our decision to source paper from certified sustainable sources. In fact, where possible, we replace printed materials with an online equivalent. This Annual Report is printed on certified 100% recycled paper.

Community investment

During the year, the Group was responsible for generating £517,700 (2012: £357,900) of income for Registered Charities, including £283,200 of direct cash donations (2012: £129,600). In addition, we invested over £75,000 in community projects that we added to our NGN footprint. The Group did not make any political donations in the current or prior year.

We focus primarily on providing time and money via engagement with four key stakeholder groups:

Engaging with our supply partners

In November our Directors hosted the Night of Ambition, our third annual fundraising auction on behalf of Ambitious about Autism. Over 250 of our supply partners and senior managers attended, with many donating unique lots for the auction. A total of £220,000 was raised for children and young people with autism.

Engaging with our customers

We continued three customer driven cause-related fundraising campaigns throughout the year. The first was the continuation of our pledge to donate to Ambitious about Autism for every call made to our UK directory enquiries number: 118 111.

We also continued the initiative to reward customers who return to us routers that have been diagnosed as end-of-life. We pay for the postage, refurbish or safely recycle the equipment and then donate £1 to charity on their behalf.

The year also saw the introduction of a donation to the unique charity Cool Earth, when customers added our unique Global Minutes Boost option to their phone package. Supported by Sir David Attenborough and Professor Lord Stern, Cool Earth is the only charity dedicated to protecting endangered rainforests through engagement with indigenous communities, one of the most effective ways to minimise CO_2 reaching our atmosphere.

Engaging with our colleagues

The Group's Give Something Back initiative includes matched donations for our people who raise funds for a Registered Charity. Hundreds of people took part in fundraising over the year.

Engaging with our new communities

The year saw us bring our NGN to additional exchanges as part of our LLU programme. Each new addition sees our broadband and phone services become available to thousands of families and businesses for the first time.

To celebrate our arrival in these communities, we make an investment in something important to them, for example, improvements to the community centre. This year, we supported over 100 communities, investing over £75,000.

Other achievements in the year

We retained both our FTSE4Good Index membership and Carbon Saver Gold Standard certification

Corporate Responsibility Group

CARBON SAVER CERTIFIED

FTSE4Good

People

We have an ambitious and progressive approach to engaging with our employees.

We have protected and developed our unique culture, expressed in our 'Brighter Basics' – Customer, Innovate, Value, People and Community.

In FY13 we issued every employee with a one-off gift of 1,000 nil priced share options, created a consistent set of employment terms and saw a significant increase in employee engagement; all key contributors to our success as a business.

Harmonisation programme

During FY13, following an extensive period of consultation, we created a simple banded job structure with consistent terms, conditions and benefits for all our employees. This programme is delivering consistency, transparency and the foundation from which our employee development programmes can operate. It also offers a clearer proposition to help us attract and retain the best talent.

Leadership development

We recognise that the quality of our managers is vital to our future success and we have continued our commitment to leadership development through our on-going programme, 'Leading a Brighter Business'. 550 of our managers have now been through the first parts of the modular programme and showing improvements in leadership capability. The programme will continue in FY14.

Employee engagement

Our engagement survey and plan enable us to listen and respond to our employees and help us to create and sustain an environment where they are motivated, stay with us and enjoy working for TalkTalk.

Following our first survey in December 2011, we committed to specific actions that would enable higher levels of employee engagement. The survey was repeated in January 2013 with significantly greater participation (89% vs. 72%) and an 11% increase in overall engagement.

Employee performance and development

In the past twelve months, we have delivered a number of new tools to support employee development. TalkTalkU is our online hub for all learning and development and includes extensive face-to-face and eLearning options. We have also delivered interactive tools to enable employees to chart career progression routes through TalkTalk. Our annual performance management process has continued to provide a mechanism to drive performance and development with all employees participating in a performance related variable bonus pay scheme.

Employee recognition

Recognising employees who drive our culture by actively demonstrating our Brighter Basics is extremely important to us. Our 'On-the-Spot' award scheme enables Senior Managers to give instant recognition to employees, while our highly popular 'TalkTalk Heroes' scheme allows employees to nominate colleagues for their outstanding contribution in a wide range of areas, from charity work to customer engagement. TalkTalk Heroes are publicly recognised at company events.

Employee benefits and share ownership

We offer a comprehensive range of flexible employee benefits which we are continually improving, so employees can make choices to suit their lifestyles.

Share ownership is an important part of our culture. In September 2012 we issued every employee, who was not currently part of another share option plan, with a one-off gift of 1,000 nil priced share options through the 'All Employee Share Option Award.' This is in addition to the employee share ownership already promoted through the annual TalkTalk SAYE Scheme, in which over 40% of our employees participate.

We believe in our employees being users of, and advocates for, our products. In FY13, we extended our employee offers to include free home phone, fibre and TV, as well as half-price mobile packages.

Great Getaway

In September 2012, we held our family friendly summer event the Great Getaway again, which was for all employees and their families, with over 2,000 people attending.

Employee consultation – One Voice forum

One Voice, is a consultation and information forum consisting of 80 nominated employee representatives, management and members of our People Services team. The forum meets regularly to discuss how the key issues we face as a business might affect our employees and to discuss relevant employee matters.

Employee communication

We communicate with all employees on a weekly basis via 'TeamTalk', a newsletter that incorporates various updates from across the business. We also produce a bespoke online newsletter for our people managers, informing them about matters that affect them or their teams. The weekly blog from Dido Harding continues to be popular with employees allowing for communication and feedback on topical issues in the Group.

Every six months, Senior Managers provide a face-to-face update on the performance of the business to all our employees, including those employed by our partners. In June 2012, we brought every UK based employee together for a one day conference, following which 87% of attendees said that they had a better understanding of TalkTalk's strategic priorities. We will be repeating the event in FY14.

Board of Directors and advisors

Chairman:

Sir Charles Dunstone

Sir Charles is the founder of Carphone Warehouse and created TalkTalk in 2002. He was appointed Chairman of TalkTalk in 2010. Sir Charles has directed the development of TalkTalk to become one of the leading fixed line telecommunication businesses in the UK. Sir Charles is Chairman of the Prince's Trust, YouView TV Limited and Carphone Warehouse Group PLC.

Executives:

Dido Harding

Dido has been Chief Executive Officer of TalkTalk since February 2010. Prior to that, Dido was Sainsbury's convenience Director, having been appointed to Sainsbury's operating board in March 2008. Dido joined Sainsbury's from Tesco PLC where she held a variety of senior roles. Dido is a Non-Executive Director of The British Land Company PLC and is a Trustee of Go On UK.

Amy Stirling

Amy has been Chief Financial Officer of TalkTalk since 2006 and was appointed to the Board in 2010 prior to its demerger and listing on the London Stock Exchange. She has held a variety of senior commercial and finance positions as the business has developed. Amy joined TalkTalk in 2000 from The Rank Group PLC where she held finance and business development roles. Amy is a chartered accountant.

David Goldie

David joined the Board in January 2010. David has over 25 years' experience in the telecoms industry and has been instrumental in the establishment and growth of the Group. David holds a Non-Executive role at The Fulwood Academy.

Non-Executives:

John Gildersleeve

John joined the Board in January 2010. He is currently Chairman of The British Land Company PLC and deputy Chairman of Carphone Warehouse Group PLC. Previously he was an Executive Director of Tesco PLC.

Ian West

Ian joined the Board in February 2011. He has been involved in the TMT sector for around 25 years as a Manager, Director and Investor. Ian held numerous roles at British Sky Broadcasting over 11 years, ending up as Managing Director of the Sky Digital subscription business. Ian is also currently an investor in a range of small and medium sized businesses and co-founded Top Up TV in 2003. Ian is a supervisory board member of Kabel Deutschland.

John Allwood

John joined the Board of TalkTalk in 2010. He has spent his entire career in Media and Telecoms and held a number of senior executive positions in these sectors including Chief Executive of Orange UK, between 2000-2004. Prior to that John spent eight years at Mirror Group PLC as Finance Director and Chief Executive. After leaving Orange he was Managing Director of Telegraph Media Group, and Chief Operating Officer and Finance Director of Mecom Group PLC. John is Non-Executive Director of Carphone Warehouse Group PLC and a Governor of Exeter University.

Brent Hoberman

Brent joined the board of TalkTalk in January 2010. Brent co-founded lastminute.com in 1998, and was its Chief Executive Officer until it was sold in 2005. He has subsequently founded and is Chairman of mydeco and made.com, and also co-founded PROfounders and Founders Forum. Brent is a Director of easyCar.com and is a Non-Executive Director of Guardian Media Group, Time Out Group and Shazam.

Sir Howard Stringer

Sir Howard joined the Board in July 2012. He is (until June 2013) Chairman of the Board of Directors of Sony Corporation. Prior to his appointment as Chairman, Sir Howard was President and CEO of Sony Corporation. Before Sony Corporation, Sir Howard had a distinguished 30 year career as a journalist, producer and executive at CBS Inc. After seven years as President of CBS Inc, Sir Howard was Chairman and CEO of TELE–TV, the media and technology company formed by Bell Atlantic NYNEX and Pacific Telesis.

James Powell

James joined the Board in July 2012. James is Chief Technology Officer of Thomson Reuters. In his 14 years at Reuters, James held a number of senior leadership positions including CTO for Enterprise; CTO and global head of product development; head of technology strategy and CTO for the Reuters Financial division. He has also held senior leadership positions at Solace Systems, Citadel Investment Group and TIBCO Finance Technology.

Company Secretary

Tim Morris

Advisors

Principal bankers:

Royal Bank of Scotland Group PLC
DNB Bank ASA
Barclays PLC
HSBC Bank PLC
Lloyds TSB Bank PLC

Corporate brokers:

Credit Suisse (Europe) Limited
1 Cabot Square, London E14 4QJ

Barclays Capital
5 The North Colonnade
Canary Wharf, London E14 4BB

Registrars:

Equiniti Limited
Aspect House, Spencer Road
Lancing, West Sussex BN99 6DA

Auditor:

Deloitte LLP
2 New Street Square
London EC4A 3BZ

Corporate governance

Introduction

The Board is committed to the highest standards of corporate governance and in accordance with the Listing Rules of the UK Listing Authority the Board confirms that the Company has throughout the year and as at the date of this Annual Report, complied with the provisions set out in the UK Corporate Governance Code (the 'Code').

This section of the Annual Report, together with the Directors' Report and Directors' Remuneration Report, provides details of how the Company has applied the principles and complied with the provisions of the Code. In particular, this section summarises the Board's compliance with the five key principles of the Code, namely: leadership, effectiveness, remuneration, accountability and relations with shareholders.

Board balance and independence

The Board has ten members, six of whom, excluding the Chairman, are considered independent Non-Executive Directors. These are John Gildersleeve, the Senior Independent Director, John Allwood, Brent Hoberman, Ian West, Sir Howard Stringer and James Powell.

Therefore, at least half of the Board (excluding the Chairman) are independent and, notwithstanding the changes to the Board composition, this has been the situation for all of FY13.

The following changes to the Board have been announced during the year: Roger Taylor stepped down in July 2012, and Sir Howard Stringer and James Powell were appointed as Non-Executive Directors with effect from the same date. On 4 March 2013, it was announced that Stephen Makin will become an Executive Director with effect from 31 May 2013, replacing Amy Stirling who will step down. His biographic details will be made available at the 2013 AGM, where he will stand for election.

The Chairman and Executive Directors have service contracts that can be terminated by either the Company or the Director on twelve months' notice.

The Non-Executive Directors have three year periods of appointment, all of which commenced from 20 January 2010, with the following exceptions: Ian West (8 February 2011); Sir Howard Stringer (26 July 2012); and James Powell (26 July 2012). Once these periods end, their appointments become rolling until each AGM where they stand for re-election. All the independent Directors have a three month notice period with no compensation for loss of office.

Leadership

How the Board operates

The Board has reserved certain matters, and delegated others, to the Group's Executive Committee, which comprises Dido Harding (Chief Executive Officer), Amy Stirling (Chief Financial Officer), David Goldie (Group Commercial Director) and other senior employees drawn from across the Group. Reserved matters include approving the Group's strategy, annual budgets and other longer term planning.

Number of meetings attended

	Board	Audit	Remuneration	Nomination
Number of meetings	6	3	6	1

Director	Board	Audit	Remuneration	Nomination
Sir Charles Dunstone, Chairman	6	–	–	–
Dido Harding	6	–	–	–
Amy Stirling	6	–	–	–
David Goldie(1)	5	–	–	–
Roger Taylor(2)	2	–	–	1
John Gildersleeve	6	3	6	1
Ian West	6	3	6	1
John Allwood	6	3	–	–
Brent Hoberman	6	–	6	–
Sir Howard Stringer(3)	3	–	3	–
James Powell(4)	4	1	–	–

(1) David Goldie was unable to attend a Board meeting due to a prior business commitment.
(2) Roger Taylor stepped down as a Director on 26 July 2012.
(3) Sir Howard Stringer was appointed on 26 July 2012 and was unable to attend one Board meeting due to illness.
(4) James Powell was appointed on 26 July 2012. He was unable to attend one Audit Committee meeting due to personal reasons.

Corporate governance continued

Leadership continued

As well as the formal meetings during the year, the Board met at other times appropriate for approving certain announcements to shareholders.

It is important to the Board that Non-Executive Directors have the ability to influence and challenge appropriately. To this end all Non-Executive Directors are given a thorough induction to the Group and take priority in Board discussions. All Directors receive papers in advance of meetings. They also receive regular reports and members of the Group's executive team are invited to present at Board meetings so that the Non-Executive Directors keep abreast of developments in the Group.

The Chairman meets regularly with just the Non-Executive Directors prior to every other Board meeting. This ensures that any concerns can be raised and discussed outside of formal Board meetings. The Senior Independent Director also attends these sessions where it is possible, if required, to discuss any matters with the other independent Non-Executive Directors.

The Senior Independent Director also takes responsibility for performance evaluation of the Board; succession planning for the Chairman; and chairing Non-Executive Director only meetings. In addition, he is an alternative point of contact for shareholders in the event that normal executive channels are not appropriate. Details of the Senior Independent Director's role are set out on the Group's website (www.talktalkgroup.com).

It is important to the Group that all Directors understand external views of the Group. To this end regular reports are provided to the Board by the Group's Investor Relations Director, covering broker reports and the output of meetings with significant shareholders.

As stated below, the Board has also delegated certain matters to a number of Board Committees.

Effectiveness

Performance evaluation and continued development

Each Board member has been subject to an internal performance review during the year, where the balance of skills, knowledge and experience of each Director was reviewed. This was undertaken by each member of the Board completing detailed questionnaires. The results of these were analysed by the Chairman, Senior Independent Director and the Board as a whole against the broad criteria of overall Board effectiveness and individual contributions.

As part of the performance review the ability of each Director, in particular the Non-Executive Directors, to demonstrate the required time commitment to the role was assessed.

As a result of this performance evaluation the Chairman confirms that each of the Directors seeking re-election at the AGM continues to be effective and has demonstrated the appropriate commitment to the role.

The Senior Independent Director also met with the other Non-Executive Directors to assess the Chairman's effectiveness, taking into account the views of Executive Directors.

In line with the Code, an external performance evaluation of the Board will be conducted during FY14.

The Company Secretary ensures that the Board is made aware of new laws, regulations and other information appropriate to the Group to ensure that all Directors continually update their skills, knowledge and familiarity of the Group in order to fulfil their roles. Additionally each Director has access to the advice and services of the Company Secretary and also has the ability to take independent external advice if required.

Board Committees

The Board has established five Committees: Audit, Remuneration, Nomination, Regulatory Compliance and Television; the first three are as required by the Code, the fourth is to ensure the compliance of the Group within the regulatory environment in which it operates, and the fifth is to focus on the Group's work in relation to its television offering.

Audit Committee

The Committee currently comprises the following independent Non-Executive Directors: John Allwood (Chairman), John Gildersleeve, Ian West and James Powell (with effect from July 2012). Roger Taylor was not a member but attended the Committee by invitation until he stepped down on 26 July 2012.

The Chairman of the Committee updates the Board on any significant issues that may have arisen at the Board meeting following each Committee meeting. In addition, the Chairman of the Committee is happy to make himself available to investors on request. During the year, all requirements of the Code in respect of the Committee were met. The work undertaken by the Committee is described within the following sections of this report.

The Group's Chief Financial Officer as well as representatives of the Company's external auditor and other senior executives from Finance, Tax and Treasury, Legal and Business Assurance also attend these meetings by invitation of the Committee. The external and internal auditors have direct access to the Committee during formal meetings and time is set aside for them to have private discussion with the Committee, in the absence of management attendees.

Effectiveness continued

Board Committees continued

Audit Committee continued

John Allwood remains the member of the Committee with relevant and recent financial experience (as recognised by the Consultative Committee of Accountancy bodies), although all members are expected to be financially literate and have an understanding of:

- the principles of, contents of and developments in financial reporting, accounting standards and statements of recommended practice;
- key aspects of the Company's operations;
- matters that influence or distort the presentation of accounts and key financial information;
- the principles of, and developments in, key applicable company law and other legislation relevant to the Company;
- the role of internal and external auditing and risk management;
- the regulatory framework of the Company's business; and
- environmental and social responsibility best reporting practices.

During the year, the formal calendar of items considered at each Audit Committee meeting within each annual cycle embraced the Code requirements to:

- monitor the integrity of the financial statements of the Company and any formal announcements relating to the Company's financial performance, including reviewing significant financial reporting judgements contained in them;
- review the Company's internal financial controls and its internal control and risk management systems and to make recommendations to the Board;
- review the Company's arrangements by which employees may raise concerns in confidence;
- monitor and review the effectiveness of the Company's internal audit function;
- make recommendations to the Board in relation to the appointment, re-appointment and removal of the external auditor and to approve its remunerations and terms of engagement;
- review and monitor the external auditor's independence and objectivity and the effectiveness of the audit process, taking into consideration relevant UK professional and regulatory requirements; and
- review the Company's policy on the engagement of the external auditor to supply non-audit services.

The Committee's remit requires it to report to the Board, identifying any matters in respect of which it considers that action or improvement is needed and to make recommendations as to the steps to be taken.

The actions taken by the Committee over the last twelve months include:

- review of the financial statements in the Annual Report 2012 and received reports from the external auditor on the same;
- review of the non-audit work undertaken by the external auditor during the year and the non-audit fees paid to the auditor;
- review of the external auditor's performance;
- receipt of reports on internal audit work undertaken, key findings and implementation of actions and approval of the internal audit plan for the year;
- review of the effectiveness of the Group's internal controls and disclosures made in the Annual Report on this matter; and
- review of updates on Group accounting, tax and treasury matters, including going concern, goodwill impairment review and tax.

The Committee is responsible for the development, implementation and monitoring of the Company's policy on external audit, which assigns responsibility for monitoring the independence, objectivity and compliance by the external auditor to the Committee.

The policy relating to the provision of non-audit services by the external auditor specifies the types of work from which the external auditor is excluded; for which the external auditor can be engaged without referral to the Committee; and for which a case by case decision is required. In order to safeguard the auditor's objectivity and independence, the ratio of non-audit fees to audit fees is monitored by the Committee. Any work proposed in excess of 50% of the audit fee is referred to the Committee. Amounts below this are discussed with the Chairman of the Committee.

A statement of fees paid or accrued for services from the external auditor during the period is set out below:

	2013 £m	2012 £m
Fees payable to the Company's auditor for the audit of the Company's annual accounts	**0.1**	0.1
Audit of the Group and its subsidiaries pursuant to legislation	**0.4**	0.6
Audit services provided to all Group companies	**0.5**	0.7
Taxation and other services	**0.1**	0.3
Total Group auditor's remuneration	**0.6**	1.0

Corporate governance continued

Effectiveness continued

Board Committees continued

Audit Committee continued

In the current year, the Group incurred non-audit fees of £53,000. Fees relating to tax services of £39,000 principally comprised technical advice associated with relevant UK and international fiscal law and regulations. Other fees of £14,000 mainly represented advice for corporate restructure projects and HR consultancy. Having undertaken a review of the non-audit related work, the Committee has satisfied itself that the services undertaken during the year did not prejudice the external auditor's independence.

At each of its meetings the Committee reviewed and considered reports on risk and business assurance on the status of the Group's risk management systems, findings from the internal audit function concerning internal controls, and reports on the status and recommended necessary actions for the remedying of any significant failings or weaknesses in internal controls identified by the internal or external auditor.

The Chairman of the Committee updates the Board following each Committee meeting.

The Committee's terms of reference, which are available on request from the Company Secretary and are published on the Group's website (www.talktalkgroup.com), comply with the Code.

In light of the assessments and review undertaken, the Committee recommended to the Board that Deloitte LLP be retained as the auditor of the Company. This recommendation was endorsed by the Board.

Deloitte LLP has expressed its willingness to continue in office as auditor and a resolution to re-appoint Deloitte LLP will be proposed at the forthcoming AGM.

Remuneration

Remuneration Committee

The Committee currently comprises the following independent Non-Executive Directors: John Gildersleeve (Chairman), Brent Hoberman, Ian West and Sir Howard Stringer (with effect from July 2012). Roger Taylor was not a member but attended the Committee by invitation until he stepped down on 26 July 2012.

Other Directors including the Chief Executive Officer, the Company Secretary, the Group Human Resources Director and advisors attended by invitation of the Committee. A detailed description of the Committee's remit and work during the period is contained in the Directors' Remuneration Report on pages 22 to 28.

The Chairman of the Committee updates the Board following each Committee meeting.

The Committee's terms of reference, which are available on request from the Company Secretary and are published on the Group's website (www.talktalkgroup.com), comply with the Code.

Accountability

Nomination Committee

During the year the Committee comprised the following Non-Executive Directors: John Gildersleeve (Chairman), Roger Taylor (until 26 July 2012, when he stepped down and was replaced by John Allwood) and Ian West.

The Committee is responsible for succession planning at Board level, overseeing the selection and appointment of Directors, regularly reviewing the structure, size and composition of the Board and making its recommendations to the Board. It assists in evaluating the commitments of individual Directors and the balance of skills, knowledge and experience on the Board.

The Committee has overseen the appointment of Sir Howard Stringer and James Powell as Non-Executive Directors and also the appointment of Stephen Makin as an Executive Director and Chief Financial Officer with effect from 31 May 2013, when Amy Stirling will stand down as an Executive Director and Chief Financial Officer. All will stand for election at the 2013 AGM.

The Chairman of the Committee updates the Board following each Committee meeting.

The Committee's terms of reference, which are available on request from the Company Secretary and are published on the Group's website (www.talktalkgroup.com), comply with the Code.

Regulatory Compliance Committee

The members of this Committee are John Gildersleeve (Chairman), Dido Harding (Chief Executive Officer), David Goldie (Group Commercial Director) and Tim Morris (Company Secretary).

Other senior executives of the Group attend by invitation of the Committee.

The purpose of the Committee is to provide the Board with visibility of how the Group remains compliant with those regulations affecting its businesses from time to time. Its members therefore include those senior executives who are operationally responsible for implementing permanent changes necessary to ensure the Group remains compliant.

Such members are accountable to the Committee and the Board for the successful delivery of such changes.

This Committee meets at least four times a year and reports to the Board accordingly. The Group also operates a weekly Compliance Committee made up of those senior executives (including the Chief Executive Officer) responsible for all key areas of compliance across the Group and is chaired by the Company Secretary. Targets set at these meetings are monitored against a weekly scorecard.

Accountability continued

Television Committee

The Board has established a Committee, which is delegated with managing the Group's television proposition. The Board retains strategic decision making capacity in relation to television. The Committee is chaired by Ian West and its members are drawn from the Executive Directors and other senior executives of the Group. Terms of reference for the Committee are available from the Company Secretary on request.

Risk management and internal control

The Company has established a risk management programme that assists management throughout the Company to identify, assess and mitigate business, financial, operational and compliance risks. The Board views management of risk as integral to good business practice. The programme is designed to support management's decision making and to improve the reliability of business performance.

To ensure that all parts of the Group have a good understanding of risk, members of this team have conducted risk workshops and reviews within each of the main functions in the past year, culminating in an assessment of key business risks by the Executive Directors and key management. These risk assessments have been wide-ranging, covering risks arising from the regulatory environment, strategy, counterparties and organisational change associated with major projects. The risk management process operates throughout the Group, being applied equally to the main business units and corporate functions. A risk report and update is provided at each Board meeting.

The output of each assessment is a list of key strategic, financial, operational and compliance risks. Associated action plans and control to mitigate identified risks are put in place where this is possible and to the extent considered appropriate by the Board taking account of costs and benefits. Changes in the status of the key risks and updates on mitigation are reported regularly at each Board meeting.

The Directors have overall responsibility for the Group's system of internal controls and for reviewing their effectiveness. The Board delegates to executive management the responsibility for designing, operating and monitoring these systems. The systems are based on a process of identifying, evaluating and managing key risks and include the risk management processes set out above.

The systems of internal control were in place throughout the period and up to the date of approval of the Annual Report. The effectiveness of these systems is periodically reviewed by the Audit Committee in accordance with the revised guidance in the Turnbull Report. These systems are also refined as necessary to meet changes in the Group's business and associated risks. The systems of internal control are designed to manage rather than eliminate the risk of failure to achieve business objectives. They can only provide reasonable and not absolute assurance against material errors, losses, fraud or breaches of law and regulations.

The Board has conducted an annual review of the effectiveness of the systems of risk management and internal control in operation during the year and up to the date of the approval of the Annual Report. This was approved by the Audit Committee and the Board. The Audit Committee also adopts an internal audit charter each year in accordance with international internal auditing standards.

This is supported by the Business Assurance and Internal Audit function through an ongoing process for identifying, evaluating and managing the risks faced by the Group.

Relations with shareholders

The Board believes it is important to explain business developments and financial results to the Company's shareholders and to understand any shareholder concerns. The principal communication media used to impart information to shareholders are news releases (including results announcements) and Company publications. In all such communications, care is taken to ensure that no price sensitive information is released.

The Chief Executive Officer and Chief Financial Officer have lead responsibility for investor relations. They are supported by a dedicated Investor Relations Director who, amongst other matters, organises presentations for analysts and institutional investors. There is a full programme of regular meetings and dialogue with major institutional shareholders, fund managers, analysts, retail brokers and credit investors, upon which the Chairman ensures that the Board receives regular updates at Board meetings. The Board also receives periodic reports on investors' views of the performance of the Company. All the Non-Executive Directors and, in particular, the Chairman and Senior Independent Director, are available to meet with major shareholders, if such meetings are required. The Company plans also to communicate with shareholders through the AGM, at which the Chairman will give an account of the progress of the business over the last year, and a review of current issues, and provides the opportunity for shareholders to ask questions.

The Company's AGM provides all shareholders with the opportunity to vote on the resolutions put to shareholders (whether personally or by proxy). Information relating to votes cast will, following the AGM, be available on the Company's website (www.talktalkgroup.com).

Further financial and business information is available on the Group's website (www.talktalkgroup.com).

Directors' Remuneration Report

On behalf of the Board, I am pleased to present the Directors' report on remuneration for FY13.

The current regulations require the Company's auditor to report to the members on the 'auditable part' of this report (marked*) and to state, in their opinion, that this part of the report has been properly prepared in accordance with the Companies Act.

Introduction

The Group's Remuneration Committee continues to be focused on its ability to attract, motivate and retain high quality talent required for the delivery of its strategy and ensuring that remuneration is linked to the long term performance of the Group. The Committee ensures that it is up to date with the ongoing evolution of corporate governance practice and Government guidance in the design of its remuneration policy and framework. Over the course of the next twelve months, the Committee will continue to plan for the forthcoming revised remuneration reporting regulations which will be reflected in my report for FY14.

Remuneration policy

The aim of the remuneration policy is to support the Group in:

- aligning individual and business performance with those of shareholders through the delivery of clear and stretching targets;
- strengthening the link between employee output and the delivery of shareholder value;
- supporting the Group's overarching philosophy, to maintain its 'value player' positioning in the marketplace;
- attracting, motivating and retaining high quality talent;
- maintaining a stable, efficient cost base;
- enabling the Group's remuneration strategy to be tailored to its changing circumstances; and
- reflecting corporate governance best practice.

The Company firmly believes that remuneration should be structured in a fair and competitive way, in order to incentivise individuals to achieve the highest levels of performance.

Packages are designed to be market competitive with fixed remuneration set at market median levels. Variable rewards, which are linked to challenging objectives based on the performance of the Group, are designed to reward exceptional performance and for the delivery of shareholder value creation. These variable rewards can provide individuals with significant overall levels of remuneration.

To ensure that the interests of the Executive Directors are closely aligned to those of its shareholders, the Company requires Executive Directors to build and retain a shareholding in the Company of at least 200% of their annual salary.

Remuneration Committee

The Remuneration Committee is responsible for making recommendations to the Board in relation to the individual remuneration packages for the Executive Directors and the Chairman. These recommendations comply with the remuneration policy, which is set by the Board, and the terms of reference of the Committee are available on the Group's website (www.talktalkgroup.com) or on request from the Company Secretary. The Committee works with the Board to determine the balance of allocation of profits between employee incentives, shareholder dividends and reinvestment into the Group.

Remuneration for Non-Executive Directors is set by the Board, taking account of the commitments and responsibilities of the role and their participation in the various governance committees of the Company.

Except when matters concerning their own positions are being considered, the Chief Executive Officer and the Group Human Resources Director are normally invited to attend the meetings of the Remuneration Committee to assist the Committee. The Committee may discuss any matter affecting the Chairman without the Chairman being present.

The Committee has access to independent advisors where it considers it appropriate. Advice from Towers Watson was received in relation to share schemes and executive remuneration in the course of the year. The Committee expects its external advisors to comply with the Remuneration Consultants Group Code of Conduct.

Components of remuneration

The main fixed and performance related elements of remuneration that can be awarded to Executive Directors are as follows:

- base pay, benefits and pension contribution (fixed);
- annual performance bonus (variable); and
- share options and performance shares (variable).

Harmonisation programme

Over the course of the last twelve months, the Group has undertaken the task of aligning the terms, conditions and benefits of all employees, managers and executives. The Committee has been fully consulted on this harmonisation programme, with employees voluntarily accepting a new single set of terms and conditions.

Following an extensive period of consultation, the Group created a simple banded job structure with consistent terms, conditions and benefits. This programme is delivering consistency, transparency and the foundations for our employee, manager and executive development programmes to operate from. It also offers a clearer proposition to help attract and retain high quality talent, supporting the remuneration policy of the Group.

Summary of reward components of Executive Directors and other members of the Executive Committee

Component	Aim	Description	Further detail
Fixed Base pay	To attract and retain talent by ensuring base pay is competitive in the market.	Paid monthly.	Reviewed annually. Benchmarked against external market data from external specialists and the Company's approach to the all employee salary review. Base pay for Executive Directors remains at market median levels for D Goldie, but is within the lower quartile for both D Harding and A Stirling. Any increase typically takes effect from 1 July annually.
Fixed Core benefits	Designed to be competitive in the market.	Core benefits typically include a defined contribution pension scheme (or cash alternative), life assurance, income protection, annual leave and private medical insurance.	Reviewed periodically relative to the market.
Fixed Voluntary benefits	Benefits may vary dependent on the role of the individual.	These include car allowances/company car provision, voluntary benefits arrangements including the purchase of additional holiday days and the ability to participate in all employee share plans.	Reviewed periodically relative to the market.
Variable Annual performance bonus	Designed to focus executives on the business priorities for the financial year ahead and to align an individual's reward with future shareholder value creation.	The bonus scheme for FY13 was based on a 'balanced scorecard' that comprised financial, customer as well as employee satisfaction measures and innovation.	Annual performance bonuses are satisfied in cash each year on the achievement of stretching performance conditions set by the Remuneration Committee. Any payment is typically made in June annually. The Remuneration Committee retains the discretion to adjust payments up or down in exceptional circumstances, where it feels that this course of action is appropriate. Maximum awards for executives have been reduced from 200% to 170% of base pay for FY13.
Variable Share-based incentive plans	Designed to reward and retain executives over the longer term whilst aligning an individual's interests with those of TalkTalk Telecom Group's shareholders.	Awards are granted over TalkTalk Telecom Group shares. Level of vesting is dependent on stretching performance conditions, usually over a three year performance period from the date of grant. No awards were made to executives in the period.	Awards are discretionary. Awards do not normally vest until the third anniversary of the date of grant and may have a deferral element. If employment ceases during the vesting period, awards will normally lapse in full.

Directors' Remuneration Report continued

Annual performance bonus

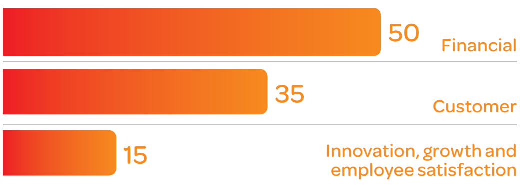
For the year ended 31 March 2013, the annual performance bonus was based on a 'balanced scorecard' blend of financial measures (Underlying Group EBITDA[1], Underlying Group operating free cash flow[1], ARPU and revenue), customer measures (TV launch and customer experience and churn), employee satisfaction measures and innovation. Executives had an incentive opportunity in the range of 0% to 170% of base salary. Performance for the year achieved 39.2% of the maximum bonus potential resulting in a bonus of 66.8% of salary.

(1) Before investment in TV.

Director	2013 £000	2012 £000
D Harding	**334**	400
A Stirling	**250**	300
D Goldie	**133**	260
Total	**717**	960

Cash awards will be paid in June 2013.

Annual Performance Bonus Scheme – executive performance measures



% Weighting of FY13 performance measures

The Remuneration Committee is satisfied that this bonus has provided an excellent link between reward and operating performance and the creation of further shareholder value.

Share-based incentive plans

Aggregate emoluments shown do not include any amounts for the value of options to acquire ordinary shares in the Company granted to or held by the Directors. Details of the options for the Directors who served during the year are as follows:

The TalkTalk Group Value Enhancement Scheme

The TalkTalk Group Value Enhancement Scheme (TTG VES) was designed to enable participants to share in the incremental value of the Group in the excess of an opening valuation, as determined by the Remuneration Committee and agreed with HMRC, with the first opening valuation on 1 April 2009. Each award entitles the participant to purchase a fixed number of separate shares in the subsidiary company, TalkTalk Group Limited, the holding company for the TalkTalk business ('Participation Shares').

As the performance conditions are satisfied and the award vests, the Participation shares may be purchased by TalkTalk by the issue of TalkTalk shares or satisfied by shares held by the Group ESOT. Participation Shares that are purchased by participants were acquired at market value and participants offered a loan from TalkTalk at a commercial rate of interest in order to fund such a purchase.

The scheme partially vested in the year as set out on page 26. The vesting of the remaining 40% will be determined in September 2013 as set out in note 5 to the consolidated financial statements.

TalkTalk Discretionary Shares

The TalkTalk Discretionary Share Option Plan (DSOP) is designed to provide a long term incentive plan for certain employees of the TalkTalk Group businesses. It is the intention of the Committee that, generally in any one year, participants may only receive an award under one of such schemes.

2010 grant

The DSOP awarded in 2010 is approved by HMRC and the exercise of the options is subject to continuing employment and performance conditions as set out in note 5 to the consolidated financial statements. No employee will be granted options over 200% of base salary, unless the TalkTalk Board determines that exceptional circumstances exist which justify exceeding this limit, in which case options shall not exceed 300% of base salary. The options granted under this award vested on 28 March 2013 and are exercisable following the announcement of the preliminary results on 16 May 2013.

2012 grant

The DSOP granted in February 2012, under the DSOP rules approved by shareholders in 2010, is an unapproved scheme and is designed to provide a long term incentive plan for Executive Directors, senior executives and certain employees of the TalkTalk Group businesses. The exercise of the options is subject to continuing employment and performance conditions as set out in note 5 to the consolidated financial statements.

Awards are triggered within a range from 10% to 19% for compound annual growth of TSR and EPS. 25% of the part of an award relative to either EPS or TSR will vest for the minimum target, rising to 40% for target performance, 70% for stretch performance and 100% for super stretch performance.

In order to protect shareholder interests and to ensure that participants of the DSOP are rewarded for performance related value creation under volatile market conditions, a 'Cap and Collar' mechanism has been introduced into the scheme for the 2012 grant.

- This mechanism would address outperformance in bear market conditions and underperformance in bull market conditions.
- The mechanism adjusts the market cap of the Group downwards when the FTSE 250 performance is above the normal range cap and adjusts the market cap upwards when the FTSE 250 performance falls below the normal range.
- There would be no pay-out below a 5% TSR CAGR floor.
- The normal range of the FTSE 250 has been analysed by PricewaterhouseCoopers. The Remuneration Committee has set this as between +10% and -10%.

Share-based incentive plans continued

All Employee Share Option Award

The All Employee Share Option Award was granted in September 2012, under the DSOP rules approved by shareholders in 2010. The award is designed to reward all employees not currently part of another share option plan to foster all employee share ownership. Each qualifying employee was awarded 1,000 nil priced share options. No awards were made to executives or senior managers. The exercise of the options is subject to continuing employment on the vesting date in September 2013 and there are no performance conditions in relation to this grant. These options lapse on resignation of an employee.

TalkTalk SAYE Scheme

The TalkTalk SAYE Scheme is a Save-As-You-Earn share option scheme and is approved by HMRC. The SAYE Scheme is administrated by a duly authorised committee of the Board. All UK Executive Directors and employees of TalkTalk and participating companies within the Group are eligible to participate in the SAYE Schemes as long as they have been employed for a qualifying period. To participate in the SAYE Scheme, an eligible employee must enter into an SAYE contract and agree to make monthly contributions between £5 and £250 for a specified period of three or five years.

Options granted to acquire TalkTalk shares under the SAYE Scheme have an option price determined by the TalkTalk Board, which will be not less than the higher of 80% of the middle market quotation price or their nominal value.

Dido Harding, Amy Stirling and David Goldie each had 8,897 options available to buy shares in the Company under the TalkTalk SAYE Scheme at 31 March 2013. These options are exercisable from 1 July 2013 at an exercise price of £1.02 per share. The options expire on 1 January 2014.

Further details of the features and operations of the TTG VES, DSOP and SAYE can be found in note 5 to the consolidated financial statements.

Aggregate remuneration*

The total amounts of Directors' remuneration and other benefits (excluding pension contributions) were as follows:

Director	Basic £000	Taxable benefits £000	Bonuses £000	2013 Total £000	2012 Total £000
Executive					
D Harding	**500**	**16**	**334**	**850**	916
A Stirling	**375**	**9**	**250**	**634**	828
D Goldie(1)	**200**	**55**	**133**	**388**	749
Non-Executive					
C Dunstone	**360**	**1**	**–**	**361**	361
R Taylor(2)	**25**	**–**	**–**	**25**	75
J Gildersleeve	**85**	**–**	**–**	**85**	85
J Allwood	**60**	**–**	**–**	**60**	60
B Hoberman	**50**	**–**	**–**	**50**	50
I West	**73**	**–**	**–**	**73**	74
H Stringer(3)	**34**	**–**	**–**	**34**	–
J Powell(3)	**34**	**–**	**–**	**34**	–
Aggregate emoluments	**1,796**	**81**	**717**	**2,594**	3,198

(1) D Goldie reduced his working hours to three days per week from June 2012.
(2) Stepped down on 26 July 2012.
(3) Appointed on 26 July 2012.

Total remuneration for FY13 above relates only to that paid to Directors for their role as Directors of the Company.

Pension contributions*

The schedule below sets out payments by the Group to defined contribution money purchase pension schemes on behalf of Executive Directors. A fixed proportion of salary is paid by the Company together with a fixed proportion by the Director and both amounts are invested on behalf of the Director. Pension benefits are then funded by the total investment. Levels are reviewed by the Committee annually against published market data. None of the Directors were members of a defined benefit pension scheme during the year. Pension entitlements are based on basic salary only. The pension schemes provided for other employees of the Group are set out in note 4 to the consolidated financial statements.

Director	2013 £000	2012 £000
D Harding	**51**	51
A Stirling	**19**	19
D Goldie	**–**	60
Total	**70**	130

Directors' Remuneration Report continued

External appointments

The Board supports Executive Directors holding Non-Executive Directorships of other companies and believes that any such appointments are part of the continuing development of the Executive Directors from which the Company will ultimately benefit. The Board has reviewed all such appointments and those appointments that the Board believes require disclosure pursuant to the Code are set out below. The Board has also agreed that the Directors may retain their fees from such appointments.

Fees for external appointments

Director	Organisation	2013 £000
D Harding	British Land PLC, The Jockey Club	**70**

Sir Charles Dunstone is also Chairman of Carphone Warehouse Group PLC, which the Company believes is a significant other commitment for him.

Fees for Non-Executive Directors

The Non-Executive Directors do not take part in discussions on their remuneration. Each of the Non-Executive Directors has a letter of appointment substantially in the form suggested by the Code, and each has a three month notice period with no compensation for loss of office. The Company has no age limit for Directors. The dates of each contract are set out on page 28.

The fees for Non-Executive Directors are set out in the aggregate remuneration table. The Committees that they serve on are set out below.

Non-Executive Director	Committees
R Taylor(1)	Remuneration, Nomination
J Gildersleeve	Audit, Remuneration, Nomination, Compliance
J Allwood	Audit, Nomination(3)
B Hoberman	Remuneration
I West	Audit, Remuneration, Nomination, Television
H Stringer(2)	Remuneration
J Powell(2)	Audit

(1) Stepped down on 26 July 2012.
(2) Appointed on 26 July 2012.
(3) Replaced R Taylor from 26 July 2012.

Directors' interest in shares and dates of service contracts*

Details of Directors' interests in options to buy shares in the Company are as follows:

1. TalkTalk Group schemes

a. Value Enhancement Scheme

As set out in note 5 to the consolidated financial statements, prior to the demerger two value enhancement schemes were introduced to provide long term incentives to senior management. These were called the TTG VES and the CPW TTG VES ('the VES schemes').

On 17 September 2012, the Group's Remuneration Committee determined that the relevant performance conditions of the VES schemes (including the 5% TSR requirement) had been satisfied meaning the VES participants were entitled to exercise 60% of their VES options. The remaining 40% will vest in September 2013 subject to ongoing performance conditions being met. Further details on the VES schemes are set out in note 5 to the consolidated financial statements. The participants' options were acquired by the Company for new ordinary shares in the Company and cash resulting in a cash outflow of £35m. The net issue of 17 million shares in the Company was at a price of £1.86 per share being the average closing price of the Company's shares on 18 and 19 September 2012.

Vesting of the first 60% of the TTG VES resulted in the Directors receiving the following share holdings:

Director	2013 number of shares
D Harding	**2,149,688**
A Stirling	**1,464,046**
D Goldie	**1,464,046**
	5,077,780

The Directors had the following percentage share of the TTG VES pool at 31 March 2013:

Director	2013 % share	2012 % share
D Harding	**10**	10
A Stirling	**6**	6
D Goldie	**6**	6

The remaining percentage of allocated shares in the TTG VES pool is held by other senior management of the Group.

The Directors have the following interest bearing loans outstanding to the Group in relation to the TTG VES at 31 March 2013:

Director	2013 £000	2012 £000
D Harding	**668**	1,606
A Stirling	**180**	433
D Goldie	**180**	433
	1,028	2,472

Interest on outstanding loans was charged at 4% during the year (2012: 4%).

Directors' interest in shares and dates of service contracts* continued

1. TalkTalk Group schemes

b. Discretionary Share Option Plan

Details of Executive Directors' conditional right to receive nil priced options in the Company are shown in the following table:

Director	At 31 March 2012 or date of appointment	Granted during the year	Exercised during the year	Lapsed during the year	At 31 March 2013	Exercise price per share £	Exercisable from	Expiry date
D Harding	236,220(1)	–	–	–	**236,220**	–	01/09/2012	04/12/2020
	236,220(1)	–	–	–	**236,220**	–	01/09/2013	04/12/2020
	1,024,590(2)		–	–	**1,024,590**	–	May 2015	07/02/2022
Total for D Harding	1,497,030	–	–	–	**1,497,030**			
A Stirling	614,754(2)	–	–	–	**614,754**	–	May 2015	07/02/2022
Total for A Stirling	614,754	–	–	–	**614,754**			

(1) Awarded in FY11
(2) Awarded in FY12

For awards made in FY11 the performance conditions are based on achieving a compound TSR of 5% over the performance period. Full details of the scheme are disclosed in note 5 to the consolidated financial statements.

For awards made in FY12 the performance conditions are based on an equal split of achieving a compound TSR measure and a compound EPS measure over the performance period. The awards made to Dido Harding and Amy Stirling were equivalent to 250% and 200% of base pay respectively. Full details of the scheme are disclosed in note 5 to the consolidated financial statements.

2. CPW legacy schemes

The performance conditions for all CPW legacy schemes have been met.

a. CSOP

Director	At 31 March 2012 or date of appointment	Granted during the year	Exercised during the year	Lapsed during the year	At 31 March 2013	Exercise price per share £	Exercisable from	Expiry date
A Stirling	106,668	–	–	–	**106,668**	0.52	06/06/2006	06/06/2013
Total for A Stirling	106,668	–	–	–	**106,668**	0.52	06/06/2006	06/06/2013

b. Performance Shares

Details of Executive Directors' conditional right to receive nil priced options in the Company are shown in the following table:

Director	At 31 March 2012 or date of appointment	Granted during the year	Exercised during the year	Lapsed during the year	At 31 March 2013	Exercise price per share £	Exercisable from	Expiry date
A Stirling	52,734	–	–	–	**52,734**	–	28/07/2007	28/07/2014
	52,734	–	–	–	**52,734**	–	28/07/2008	28/07/2014
Total for A Stirling	105,468	–	–	–	**105,468**			
D Goldie	200,000	–	–	–	**200,000**	–	28/07/2008	28/07/2015
Total for D Goldie	200,000	–	–	–	**200,000**			

The market price was 272p as at 31 March 2013 (FY12: 137p) and the range during the year was 127p to 274p.

Directors' Remuneration Report continued

Directors' interests in shares and dates of service contracts

Both the Directors' interests in the Group at 31 March 2013 and the effective dates of their contract are set out below:

Director	Ordinary shares of 0.1p 31 March 2013	31 March 2012	Date of contract
C Dunstone	**294,059,396**	295,209,396	20/01/2010
D Harding	**2,149,688**	–	20/01/2010
A Stirling	**2,000,733**	536,687	20/01/2010
D Goldie	**2,409,506**	945,460	20/01/2010
J Gildersleeve	**246,000**	246,000	20/01/2010
J Allwood	**10,000**	10,000	20/01/2010
B Hoberman	**12,882**	–	20/01/2010
I West	**346,023**	346,023	08/02/2011
H Stringer	**–**	–	26/07/2012
J Powell	**–**	–	26/07/2012

Roger Taylor held 2,587,932 ordinary shares in the Group at 31 March 2012. He stepped down from the Board on 26 July 2012.

This Remuneration Report has been prepared in accordance with the Large and Medium sized Companies and Groups (Accounts and Reports) Regulations 2008 ('Regulations') issued under the Companies Act, the UK Corporate Governance Code and the Executive Remuneration Guidelines published by the Association of British Insurers in September 2011. The constitution and operation of the Remuneration Committee are in compliance with the Code.

In framing its remuneration policy the Committee has given full consideration to the matters set out in Schedule A of the Code. As required by the Regulations, a resolution to approve this report will be proposed at the AGM to be held on 24 July 2013.

Performance graph

The graph below shows the Group's performance compared to the TSR performance of the FTSE 250 from the date of the Group's listing, 29 March 2010.

The FTSE 250 was selected as it is a broad market index of which the Group is a member.

Performance Return Index

J Gildersleeve
Senior Independent Non-Executive Director
15 May 2013

Other statutory information

Suppliers payment policy

It is the Company's policy to develop and maintain key commercial relationships with its suppliers, one aspect of which is payment timing to obtain mutually agreed payment terms. The Company has commercially agreed longer credit terms with certain suppliers. Excluding these suppliers, the average credit period taken on trade payables was 39 days (FY12: 32 days). Including these suppliers, the average credit period taken was 48 days (FY12: 32 days).

Contracts with controlling shareholders

There are no material contracts with controlling shareholders, except as disclosed in the Directors' Remuneration Report on pages 22 to 28. No Director is entitled to any compensation for loss of office on a takeover or change of control of the Company.

Details of employee share schemes are set out in note 5 to the financial statements. Shares held by the Group ESOT abstain from voting.

Share capital

The rights and obligations relating to the Company's shares are set out in the Articles of Association. The Articles of Association can be requested from the Company Secretary at the Company's registered office.

There are no restrictions on the transfer of ordinary shares in the capital of the Company other than those which may be imposed by law from time to time. In accordance with the Disclosure and Transparency Rules, certain employees are required to seek approval to deal in the Company's shares. The Company is not aware of any agreements between shareholders that may result in restrictions on the transfers of securities and/or voting rights.

There is a general right of the Company to purchase its own shares, as set out at Article 16 of the Company's Articles of Association. In addition, at the AGM in 2012, the Directors were granted the right to acquire 91,410,825 shares. This right expires on the date of the 2013 AGM or 28 October 2013 (whichever is the sooner).

The Articles of Association may be changed by special resolution.

Details in the movements in authorised and issued share capital during the period are provided in notes 21 and 22 to the financial statements.

Appointment of Directors

The rules relating to the appointment and/or removal of Directors are contained in Section O of the Company's Articles of Association. The powers of the Directors are set out in the Company's Articles of Association.

Property, plant and equipment

Movements in property, plant and equipment are set out in note 12 to the financial statements.

Dividends

The Company may, by resolution in a general meeting, declare dividends in accordance with the respective rights of the members, but no dividend can exceed the amount recommended by the Board.

Significant shareholdings

At 15 May 2013 the Company had been notified of the following interests in the Company's shares:

Name	Number of shares	Percentage of share capital
Sir Charles Dunstone	294,059,396	31.58
David Ross	116,160,528	12.47
Capital Research Global Investors	62,933,100	6.76
Jupiter Asset Management Limited	42,764,602	4.59
Group ESOT	38,728,388	4.16
Schroder Investment Management Ltd (SIM)	29,369,033	3.15
Invesco Asset Management Limited	28,158,815	3.02

The total interests of the Directors are detailed in the Directors' Remuneration Report on pages 22 to 28.

Going concern

On the basis of current financial projections and facilities available, the Directors are satisfied that the Group has adequate resources to continue in operation for the foreseeable future and consequently the financial statements continue to be prepared on the going concern basis, as discussed in the Chief Financial Officer's Statement on page 11.

Director's indemnities

Director's liability insurance is provided for Directors. In addition, there is an existing indemnity to Amy Stirling in her capacity as a Director of CPW Support Services (India) Private Limited.

Equal opportunities

We celebrate diversity and have an equal opportunities policy, which ensures that everyone is provided with the same opportunities for employment, career development, training and promotion. As part of this policy, applications for employment by disabled persons are fully considered, bearing in mind the abilities of the applicant concerned. In the event of employees becoming disabled during employment a thorough process is followed and support provided (including income support insurance) to try to secure their employment.

Audit information

Each of the persons who is a Director at the date of approval of this Annual Report confirms that:

- so far as the Director is aware, there is no relevant audit information of which the Company's auditor is unaware; and
- the Director has taken all the steps that he/she ought to have taken as a Director in order to make himself/herself aware of any relevant audit information and to establish that the Company's auditor is aware of the information.

This confirmation is given and should be interpreted in accordance with the provisions of Section 418 of the Companies Act 2006.

By order of the Board

TalkTalk Telecom Group PLC
11 Evesham Street
London W11 4AR

TS Morris
Company Secretary
15 May 2013

Directors' responsibilities statement

The Directors are responsible for preparing the Annual Report 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 are required to prepare the consolidated financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union and Article 4 of the IAS Regulation and have elected to prepare the Parent Company financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law). Under company law the Directors must not approve the accounts unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period.

In preparing the consolidated financial statements, International Accounting Standard 1 requires that Directors:

- properly select and apply accounting policies;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- provide additional disclosures when compliance with the specific requirements in IFRSs are insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance; and
- make an assessment of the Company's ability to continue as a going concern.

In preparing the Parent Company 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 applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements; 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 enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Responsibility statement

We confirm that to the best of our knowledge:

- the financial statements, prepared in accordance with the relevant financial reporting framework, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and the undertakings included in the consolidation taken as a whole; and
- the management report, which is incorporated into the Directors' Report, includes a fair review of the development and performance of the business and the position of the Company and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

By order of the Board

D Harding
Chief Executive Officer
15 May 2013

A Stirling
Chief Financial Officer
15 May 2013

Independent auditor's report

to the members of TalkTalk Telecom Group PLC

We have audited the Group financial statements of TalkTalk Telecom Group PLC for the year ended 31 March 2013 which comprise the Group income statement, the Group statement of comprehensive income, the Group statement of changes in equity, the Group balance sheet, the Group cash flow statement and the related notes 1 to 27. 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.

This report is made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of Directors and auditor

As explained more fully in the Directors' Responsibilities Statement, the Directors are responsible for the preparation of the Group financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the Group 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.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of:

- whether the accounting policies are appropriate to the Group's circumstances and have been consistently applied and adequately disclosed;
- the reasonableness of significant accounting estimates made by the Directors; and
- the overall presentation of the financial statements.

In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on financial statements

In our opinion the Group financial statements:

- give a true and fair view of the state of the Group's affairs as at 31 March 2013 and of its profit 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 note 1 to the Group 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 Group financial statements comply with IFRSs as issued by the IASB.

Opinion on other matter prescribed by the Companies Act 2006

In our opinion the information given in the Directors' Report for the financial year for which the Group financial statements are prepared is consistent with the Group 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, contained within the Chief Financial Officer's review, in relation to going concern;
- the part of the Corporate Governance Statement relating to the Company's compliance with the nine provisions of the UK Corporate Governance Code specified for our review; and
- certain elements of the report to shareholders by the Board on Directors' remuneration.

Other matter

We have reported separately on the Parent Company financial statements of TalkTalk Telecom Group PLC for the year ended 31 March 2013 and on the information in the Directors' Remuneration Report that is described as having been audited.

Peter O'Donoghue BA FCA (Senior Statutory Auditor)
for and on behalf of Deloitte LLP
Chartered Accountants and Statutory Auditor
London, United Kingdom
15 May 2013

Group income statement

For the year ended 31 March

	Notes	2013			2012		
		Before amortisation of acquisition intangibles and exceptional items £m	Amortisation of acquisition intangibles and exceptional items*** £m	After amortisation of acquisition intangibles and exceptional items £m	Before amortisation of acquisition intangibles and exceptional items £m	Amortisation of acquisition intangibles and exceptional items*** £m	After amortisation of acquisition intangibles and exceptional items £m
Revenue	2	**1,670**	**–**	**1,670**	1,687	–	1,687
Cost of sales		**(751)**	**–**	**(751)**	(803)	–	(803)
Gross profit		**919**	**–**	**919**	884	–	884
Operating expenses excluding amortisation and depreciation*		**(567)**	**9**	**(558)**	(567)	(27)	(594)
Underlying EBITDA**		**352**	**9**	**361**	317	(27)	290
Sale of freehold property		**–**	**–**	**–**	9	–	9
Investment in TV		**(62)**	**–**	**(62)**	–	–	–
Headline EBITDA		**290**	**9**	**299**	326	(27)	299
Depreciation	3, 12	**(76)**	**–**	**(76)**	(65)	–	(65)
Amortisation	3, 11	**(26)**	**(52)**	**(78)**	(27)	(61)	(88)
Share of results of joint venture	14	**(4)**	**–**	**(4)**	(1)	–	(1)
Operating profit	3	**184**	**(43)**	**141**	233	(88)	145
Finance costs	6	**(19)**	**–**	**(19)**	(18)	–	(18)
Profit before taxation		**165**	**(43)**	**122**	215	(88)	127
Taxation	7	**(33)**	**11**	**(22)**	(56)	67	11
Profit for the year		**132**	**(32)**	**100**	159	(21)	138
Attributable to the equity holders of the Parent Company		**132**	**(32)**	**100**	159	(21)	138
Earnings per share							
Underlying							
Basic (pence)	10	**20.6**			17.2		
Diluted (pence)	10	**19.4**			16.4		
Headline/Statutory							
Basic (pence)	10	**14.9**		**11.3**	18.0		15.6
Diluted (pence)	10	**14.0**		**10.6**	17.2		14.9

* Operating expenses excluding amortisation and depreciation also includes other exceptional income (note 9).
** Underlying EBITDA is defined as Headline EBITDA excluding any costs relating to the investment in TV (2012: excluding the profit on sale of a freehold property).
*** A reconciliation of Headline information to Statutory information is provided in note 9 to the financial statements.

The accompanying notes are an integral part of this Group income statement. All amounts relate to continuing operations.

Group statement of comprehensive income

For the year ended 31 March

	2013 £m	2012 £m
Profit for the year*	**100**	138
Other comprehensive income for the year		
Derivative financial instruments*	**(2)**	–
Total comprehensive income for the year	**98**	138
Attributable to the equity holders of the Parent Company	**98**	138

* Recognised within retained earnings and other reserves.

The accompanying notes are an integral part of this Group statement of comprehensive income.

Group statement of changes in equity

For the year ended 31 March

	Notes	Share capital £m	Share premium £m	Translation and hedging reserve £m	Demerger reserve £m	Retained earnings and other reserves £m	Total £m
At 1 April 2012		**1**	**586**	**(65)**	**(513)**	**435**	**444**
Total comprehensive income for the year		**–**	**–**	**–**	**–**	**98**	**98**
Issues of own shares*	22	**–**	**32**	**–**	**–**	**(63)**	**(31)**
Taxation of items recognised directly in reserves		**–**	**–**	**–**	**–**	**11**	**11**
Share-based payments reserve credit	5	**–**	**–**	**–**	**–**	**6**	**6**
Equity dividends	8	**–**	**–**	**–**	**–**	**(87)**	**(87)**
Currency translation differences		**–**	**–**	**1**	**–**	**–**	**1**
At 31 March 2013		**1**	**618**	**(64)**	**(513)**	**400**	**442**

	Notes	Share capital £m	Share premium £m	Translation and hedging reserve £m	Demerger reserve £m	Retained earnings and other reserves £m	Total £m
At 1 April 2011		1	586	(65)	(513)	406	415
Total comprehensive income for the year		–	–	–	–	138	138
Net purchase of own shares	22	–	–	–	–	(54)	(54)
Settlement of Group ESOT shares		–	–	–	–	1	1
Share-based payments reserve credit	5	–	–	–	–	4	4
Share-based payments reserve debit		–	–	–	–	(2)	(2)
Equity dividends	8	–	–	–	–	(58)	(58)
At 31 March 2012		1	586	(65)	(513)	435	444

* On 17 September 2012, the Group's Remuneration Committee determined that the relevant performance conditions of the VES schemes (including the 5% TSR requirement) had been satisfied, meaning the VES participants were entitled to exercise 60% of their options as set out in note 5. The settlement of the schemes resulted in the recognition of share premium of £32m and a £63m movement in retained earnings and other reserves.

The accompanying notes are an integral part of this Group statement of changes in equity.

Group balance sheet

As at 31 March

	Notes	2013 £m	2012 £m
Non-current assets			
Goodwill	11	**479**	480
Other intangible assets	11	**154**	202
Property, plant and equipment	12	**295**	292
Non-current asset investments	13	**–**	1
Investment in joint venture	14	**9**	7
Deferred tax assets	7	**109**	120
		1,046	1,102
Current assets			
Cash and cash equivalents	18	**7**	2
Inventories	15	**23**	3
Trade and other receivables	16	**226**	184
Loans to related parties	16	**–**	2
		256	191
Total assets		**1,302**	1,293
Current liabilities			
Trade and other payables	17	**(431)**	(379)
Loans and other borrowings	18	**(25)**	(26)
Corporation tax liabilities		**(16)**	(16)
Provisions	20	**(5)**	(8)
		(477)	(429)
Non-current liabilities			
Loans and other borrowings	18	**(375)**	(410)
Provisions	20	**(8)**	(10)
		(383)	(420)
Total liabilities		**(860)**	(849)
Net assets		**442**	444
Equity			
Share capital	21, 22	**1**	1
Share premium	22	**618**	586
Translation and hedging reserve	22	**(64)**	(65)
Demerger reserve	22	**(513)**	(513)
Retained earnings and other reserves	22	**400**	435
Total equity		**442**	444

The accompanying notes are an integral part of this Group balance sheet.

These financial statements were approved by the Board on 15 May 2013. They were signed on its behalf by:

D Harding
Chief Executive Officer
15 May 2013

A Stirling
Chief Financial Officer
15 May 2013

Group cash flow statement

For the year ended 31 March

	Notes	2013 £m	2012 £m
Operating activities			
Operating profit		**141**	145
Adjustments for non-cash items:			
Share-based payments	5	**6**	4
Depreciation	3, 12	**76**	65
Amortisation	3, 11	**78**	88
Share of losses of joint venture	14	**4**	1
Profit on disposal of property, plant and equipment		**–**	(9)
Profit on disposal of customer base		**–**	(3)
Profit on disposal of subsidiaries		**(1)**	–
Operating cash flows before movements in working capital		**304**	291
Increase in trade and other receivables		**(37)**	(20)
Increase in inventory		**(20)**	–
Increase in trade and other payables		**46**	13
Decrease in provisions		**(6)**	(29)
Cash generated by operations		**287**	255
Income taxes paid		**–**	(2)
Net cash flows generated from operating activities		**287**	253
Investing activities			
Acquisition of subsidiaries and joint ventures, net of cash acquired	13, 14	**(6)**	(20)
Disposal of subsidiaries and customer bases	13	**2**	3
Acquisition of operating intangible assets		**(34)**	(28)
Acquisition of property, plant and equipment		**(70)**	(78)
Disposal of property, plant and equipment		**–**	9
Cash flows used in investing activities		**(108)**	(114)
Financing activities			
Settlement of Group ESOT shares		**–**	1
Purchase of own shares		**(35)**	(54)
(Repayment) drawdowns of borrowings	23	**(35)**	5
Refinancing fees	6	**–**	(7)
Interest paid		**(16)**	(17)
Dividends paid	8	**(87)**	(58)
Cash flows used in financing activities		**(173)**	(130)
Net increase in cash and cash equivalents		**6**	9
Cash and cash equivalents at the start of the year		**1**	(8)
Cash and cash equivalents at the end of the year		**7**	1
Cash and cash equivalents for the purpose of this statement comprise:			
Cash and cash equivalents	18	**7**	2
Bank overdrafts*	18	**–**	(1)
		7	1

* Bank overdrafts are disclosed within loans and other borrowings less than one year.

The accompanying notes are an integral part of this Group cash flow statement.

Notes to the consolidated financial statements

1. Accounting policies and basis of preparation

Basis of preparation

TalkTalk Telecom Group PLC is incorporated in England and Wales under the Companies Act.

The consolidated financial statements of the Company have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted for use in the European Union (EU) and as applied in accordance with the provisions of the Companies Act 2006. These financial statements therefore comply with Article 4 of the European Union International Accounting Standard regulation. The Company elected to prepare its Parent Company financial statements in accordance with UK GAAP.

The financial statements have been prepared on the historical cost basis, except for the revaluation of certain financial instruments and investments. The financial statements are presented in Sterling, rounded to the nearest million, because that is the currency of the principal economic environment in which the Group operates.

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company, entities controlled by the Company (its subsidiaries) and entities which are joint ventures accounted for using the equity method made up to 31 March each year. Control is achieved where the Company has the power to govern the financial and operating policies of an investee entity so as to obtain benefits from its activities.

The results of subsidiaries acquired or sold during the year are included from or to the date on which control passed to or was relinquished by the Group. Intercompany transactions and balances between subsidiaries are eliminated on consolidation.

Where necessary, adjustments are made to the financial statements of subsidiaries and the results of joint ventures to bring accounting policies in line with those used by the Group.

Going concern

The financial statements have been prepared on the going concern basis. Details of the considerations undertaken by the Directors in reaching this conclusion are set out on page 11 within the Chief Financial Officer's Statement.

Accounting policies

The Group's principal accounting policies, which relate to the financial statements as a whole are set out below. Where an accounting policy is specific to one note, the policy is described in the note to which it relates. This section also shows new EU endorsed accounting standards, amendments and interpretations, whether these are effective in the current or later years. In both cases it is explained how they are expected to impact the performance of the Group.

Revenue

Revenue is stated net of VAT and other sales related taxes and represents the gross inflow of economic benefit generated from the provision of fixed line and mobile telecommunications services. All such revenue is recognised as the services are provided:

- line rental is recognised in the period to which it relates;
- voice and broadband subscriptions are recognised in the period to which they relate;
- usage including voice and TV content is recognised in the period in which the customer takes the service;
- promotional discounts are amortised on a straight line basis over the minimum contract period subject to an adjustment for in contract churn;
- connection charges are recognised in the period in which the connection is made; and
- data service solutions and other service contracts are recognised as the Group fulfils its performance obligations.

Revenue is measured at fair value of the consideration received or receivable. When the Group sells a number of products within a bundled transaction, the total consideration from the arrangement is allocated to each element based on their relative fair values. The amount of revenue the Group recognises for delivered elements is limited to the cash received.

Subscriber acquisition costs

Subscriber acquisition costs, being third party costs of recruiting and retaining new customers, are expensed as incurred.

Investment in TV

Investment in TV includes the one-off launch costs and incremental subscriber acquisition costs relating to the TV proposition.

Foreign currency translation and transactions

Material transactions in foreign currencies are hedged using forward purchases or sales of the relevant currencies and are recognised in the financial statements at the exchange rates thus obtained. Unhedged transactions are recorded at the exchange rate on the date of the transaction. Hedge accounting as defined by IAS 39 'Financial Instruments: Recognition and Measurement' has been applied in the current and preceding financial year by marking to market the relevant financial instruments at the balance sheet date and recognising the gain or loss in equity in respect of cash flow hedges.

The principal exchange rates against UK Sterling used in these financial statements are as follows:

	Average		Closing	
	2013	2012	**2013**	2012
Euro	**1.23**	1.16	**1.19**	1.20
United States Dollar	**1.58**	1.60	**1.52**	1.60

Where a foreign operation is sold, the gain or loss on disposal recognised in the income statement is determined after taking into account the cumulative currency translation differences that are attributable to the operation.

Notes to the consolidated financial statements continued

1. Accounting policies and basis of preparation continued

Leases

Rental payments under operating leases are charged to the income statement on a straight line basis over the period of the lease. Lease incentives and rent free periods are amortised through the income statement over the period of the lease.

Gains or losses from sale and leaseback transactions are deferred over the life of the new lease to the extent that the rentals are considered to be above or below market rentals. The remaining gain or loss is recognised within operating expenses in the year in which the sale is completed.

Financial instruments

Financial assets and financial liabilities, in respect of financial instruments, are recognised in the Group's balance sheet when the Group becomes a party to the contractual provisions of the instrument.

Trade and other receivables

Trade receivables, loans and other receivables that have fixed or determinable payments that are not quoted in an active market are classified as loans and receivables. Loans and receivables are measured at amortised cost using the effective interest rate method, less any impairment. Interest income is recognised by applying the effective interest rate, except for short term receivables when the recognition of interest would be immaterial.

Cash and cash equivalents

Cash and cash equivalents and bank deposits consists of cash in hand.

Trade payables

Trade payables are other financial liabilities initially measured at fair value and subsequently measured at amortised cost.

Financial liabilities and equity instruments

Financial liabilities and equity instruments issued by the Group are classified according to the substance of the contractual arrangements entered into and the definitions of a financial liability and an equity instrument. An equity instrument is any contract that evidences a residual interest in the assets of the Group after deducting all of its liabilities and includes no obligation to deliver cash or other financial assets. The accounting policies adopted for specific financial liabilities and equity instruments are set out below.

Loans and other borrowings

Loans and other borrowings represent committed and uncommitted bank loans, bank overdrafts and loans from related parties. These are initially measured at fair value (which is equal to cost at inception) and are subsequently measured at amortised cost, using the effective interest rate method.

Bank fees and legal costs associated with the securing of external financing are capitalised and amortised over the term of the relevant facility. All other borrowing costs are recognised in the income statement in the period in which they are incurred.

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.

Equity instruments

Equity instruments issued by the Group are recorded at the proceeds received, net of direct issuance costs.

Shares in the Company held by the Group ESOT are shown as a reduction in shareholders' funds. Other assets and liabilities held by the trust are consolidated with the assets of the Group.

Derivative financial instruments and hedge accounting

The Group's activities expose it to the financial risks of changes in foreign exchange rates and interest rates. The use of financial derivatives is governed by the framework approved by the Board, which provides written principles on the use of financial derivatives consistent with the Group's risk management strategy. Changes in values of all derivatives of a financing nature are included within investment income and financing costs in the income statement. The Group does not use derivative financial instruments for speculative purposes.

Derivative financial instruments are initially measured at fair value on the contract date and are subsequently remeasured to fair value at each reporting date.

Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated, exercised, or no longer qualifies for hedge accounting, or the Company chooses to end the hedging relationship.

Cash flow hedges

The Group uses derivative instruments (primarily interest rate swaps) to manage its interest rate risk. The Group designates these as cash flow hedges. The effective portion of changes in the fair value of these instruments is recognised in other comprehensive income. The gain or loss relating to the ineffective portion is recognised immediately in the income statement.

Measurement

The financial instruments included on the Group's balance sheet are measured at fair value or amortised cost. The measurement of this fair value can in some cases be subjective and can depend on the inputs used in the calculations. The different valuation methods are called 'hierarchies' and are described below:

- Level 1: Fair values measured using quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2: Fair values measured using inputs, other than quoted prices included within Level 1 that are observable for the asset or liability either directly or indirectly; and
- Level 3: Fair values measured using inputs for the asset or liability that are not based on observable market data.

1. Accounting policies and basis of preparation continued

Accounting estimates and judgements

The preparation of financial statements requires management to exercise judgement in applying the Group's accounting policies. Estimates and assumptions used in the preparation of the financial statements are continually reviewed and revised as necessary. Whilst every effort is made to ensure that such estimates and assumptions are reasonable, by their nature they are uncertain, and as such changes in estimates and assumptions may have a material impact.

The areas involving the most sensitive estimates and assumptions that are significant to the financial statements are set out in more detail in the related notes:

- tax (note 7);
- exceptional items (note 9);
- impairment of goodwill (note 11);
- capitalisation and useful economic lives of assets (notes 11 and 12);
- impairment of assets (notes 11 and 12); and
- trade receivables (note 16).

Application of significant new or amended EU endorsed accounting standards

New and revised standards and interpretations that have been endorsed for the financial year have no impact on the Group.

Future accounting developments

At the date of authorisation of these financial statements the following significant standards and interpretations that have not been applied in these financial statements were in issue, but not yet effective (and in some cases had not yet been adopted by the EU):

- IAS 1 (amended) 'Presentation on Financial Statements'
- IFRS 1 (amended) 'Government Loans'
- IFRS 7 (amended) 'Disclosures – Offsetting Financial Assets and Financial Liabilities'
- IFRS 9 'Financial Instruments'
- IFRS 10 'Consolidated Financial Statements'
- IFRS 10, IFRS 12 and IAS 27 (amended) 'Investment Entities'
- IFRS 11 'Joint Arrangements'
- IFRS 12 'Disclosure of Interests in Other Entities'
- IFRS 13 'Fair Value Measurement'
- IAS 27 (revised) 'Separate Financial Statements'
- IAS 28 (revised) 'Investments in Associates and Joint Ventures'
- IAS 32 (amended) 'Offsetting Financial Assets and Financial Liabilities'
- IAS 19 (revised) 'Employee Benefits'

The Directors do not expect that the adoption of these standards will have a material impact on the financial statements of the Group in future periods, except as follows:

- IFRS 7 (amended) will increase the disclosure requirements where netting arrangements are in place for financial assets and financial liabilities.
- IFRS 9 will impact the:
  - measurement and disclosure of financial instruments; and
  - the disclosure of interest the Group has in other entities.
- IFRS 10 will impact the consolidation of the financial statements.
- IFRS 12 will impact the disclosure of interests the Group has in other entities.
- IFRS 13 will impact the measurement of fair value for certain assets and liabilities as well as the associated disclosures.

Beyond the information above, it is not practicable to provide a reasonable estimate of the effect of these standards until a detailed review has been completed.

Notes to the consolidated financial statements continued

2. Segmental reporting

Accounting policy

IFRS 8 'Operating Segments' requires the segmental information presented in the financial statements to be that used by the chief operating decision maker to evaluate the performance of the business and decide how to allocate resources. The Group has identified the Board as its chief operating decision maker. The Board considers the results of the business as a whole when assessing the performance of the business and making decisions about the allocation of resources. Accordingly the Group has one operating segment.

	2013 £m	2012 £m
Revenue	**1,670**	1,687
Underlying EBITDA	**352**	317
Sale of freehold property	**–**	9
Investment in TV	**(62)**	–
Headline EBITDA	**290**	326
Depreciation	**(76)**	(65)
Amortisation of operating intangibles	**(26)**	(27)
Share of results of joint ventures	**(4)**	(1)
Headline profit before interest and taxation (note 9)	**184**	233
Amortisation of acquisition intangibles and exceptional amortisation	**(52)**	(61)
Exceptional items (note 9)	**9**	(27)
Operating profit	**141**	145

The Group's revenue is split by On-net, Off-net and Corporate products as this information is provided to the Group's chief operating decision maker. On-net and Off-net comprise Consumer and Business customers that receive similar services.

	2013 £m	2012* £m
On-net	**1,170**	1,084
Off-net	**178**	287
Corporate	**322**	316
	1,670	1,687

* As restated. During the year, the Group changed its revenue disclosure by product from Broadband, Non-broadband and Corporate to On-net, Off-net and Corporate as the information provided to the Group's chief operating decision maker to run the business was changed.

The Group has no material overseas operations; as a result a split of revenue and total assets by geographical location has not been disclosed.

3. Operating profit before interest and taxation

Group profit before interest and taxation is stated after charging (crediting):

	2013 £m	2012 £m
Depreciation of property, plant and equipment	**76**	65
Amortisation of acquisition intangibles	**52**	61
Amortisation of other operating intangible fixed assets	**26**	27
Profit on disposal of property, plant and equipment	**–**	(9)
Profit on disposal of subsidiaries and customer bases	**(1)**	(3)
Impairment of Shared Band Limited	**1**	–
Impairment loss recognised on trade receivables	**33**	38
Staff costs	**133**	141
Cost of inventories recognised in expenses	**67**	19
Rentals under operating leases	**79**	73
Auditor's remuneration*	**1**	1

* A breakdown of auditor's remuneration is disclosed within the Corporate governance section on page 19.

4. Employee costs

The average number of employees (including Executive Directors) was:

	2013 Number	2012 Number
Administration	**1,517**	1,545
Sales and customer management	**998**	1,561
	2,515	3,106

The aggregate remuneration recognised in respect of these employees in the income statement comprised:

	2013 £m	2012 £m
Wages and salaries	**110**	120
Social security costs	**14**	14
Other pension costs	**3**	3
	127	137
Share-based payments (note 5)	**6**	4
	133	141

The Group provides various defined contribution pension schemes for the benefit of a significant number of its employees. These are charged to the income statement as they become payable in accordance with the rules of the schemes.

Compensation earned by Key Management Personnel is analysed below. The Key Management Personnel comprised the TalkTalk Group Executive Board and Board of Directors.

	2013 £m	2012 £m
Salaries and fees	**4.0**	4.1
Performance bonuses	**1.9**	2.4
Benefits	**0.1**	0.1
Pension costs	**0.2**	0.2
Share-based payments	**2.2**	3.2
Compensation for loss of office*	**–**	1.0
Other**	**–**	0.3
	8.4	11.3

* Included within exceptional items (Operating efficiencies – Phase I) (note 9).
** Certain Directors had interest bearing loans to settle tax liabilities arising as a result of a share gift given in December 2008 by CPW. These were forgiven in the year ended 31 March 2012.

5. Share-based payments

Accounting policy

The Group issues equity settled share-based payments to certain employees. Equity settled share-based payments are measured at fair value at the date of grant and expensed over the vesting period, based on an estimate of the number of shares that will eventually vest.

Fair value is measured by use of a dividend discount or Binomial model for share-based payments with internal, non-market performance criteria (for example, EPS targets) and a Black Scholes or Monte Carlo model for those with external, 'market' performance criteria (for example, TSR targets).

For schemes with non-market performance criteria, the number of options expected to vest is recalculated at each balance sheet date, based on expectations of performance against target and of leavers prior to vesting. The movement in cumulative expense since the previous balance sheet date is recognised in the income statement, with a corresponding entry in reserves.

For schemes with market performance criteria, the number of options expected to vest is adjusted only for expectations of leavers prior to vesting. The movement in cumulative expense since the previous balance sheet date is recognised in the income statement, with a corresponding entry in reserves.

If a scheme is cancelled, any remaining part of the fair value of the scheme is expensed immediately. If a scheme is forfeited, no further expense is recognised and any charges previously recognised are reversed.

Notes to the consolidated financial statements continued

5. Share-based payments continued

Accounting policy continued

Charges arise on loans that are provided to employees to fund the purchase of shares in the Group as part of long term incentive plans. To the extent to which the loans are not, in certain circumstances, repayable, the cost of such loans is expensed over the course of the relevant incentive plans. Charges are also recognised on loans provided to employees to settle personal tax liabilities; to the extent to which the loans are not, in certain circumstances, repayable, the cost of such loans is expensed on grant.

In accordance with IFRS 2 'Share-based Payment' no cost has been recognised in respect of the options granted before November 2002.

Group share schemes

The Group's share schemes are the All Employee Share Option Award – 2012, the Discretionary Share Option Plan (DSOP) and Save-As-You-Earn Scheme (SAYE).

In addition, the Group has a number of legacy CPW schemes.

In order to aid the user of the accounts, the dilutive effect on EPS of each of the Group schemes and legacy CPW schemes has been presented. This has been calculated using an average share price for the financial year of £1.98 (2012: £1.36).

For the CPW legacy schemes, with no IFRS 2 charge in current or prior year, the disclosures are limited to the dilutive effect on EPS and the number of options outstanding at the end of the year.

In September 2012, 60% of the TTG VES and the CPW TTG VES vested. Further information is set out in section (v). In March 2013, the DSOP – 2010 grant vested. Further information is set out in section (iii).

Summary of share schemes

Year ended 31 March 2013	IFRS 2 charge £m	Dilutive effect millions	Options outstanding at end of the year millions
TalkTalk Telecom Group PLC schemes			
All Employee Share Option Award – 2012	**2**	**1**	**2**
DSOP – 2012 grant	**1**	**5**	**12**
DSOP – 2010 grant	**1**	**7**	**17**
SAYE	**1**	**3**	**6**
Total TalkTalk Telecom Group PLC schemes	**5**	**16**	**37**
Legacy Carphone Warehouse schemes			
TTG VES and CPW TTG VES*	**1**	**38**	**–**
Other employee share option schemes	**–**	**2**	**1**
Total legacy Carphone Warehouse schemes	**1**	**40**	**1**
Total	**6**	**56**	**38**

Year ended 31 March 2012	IFRS 2 charge £m	Dilutive effect millions	Options outstanding at end of the year millions
TalkTalk Telecom Group PLC schemes			
DSOP – 2012 grant	–	2	11
DSOP – 2010 grant	2	–	20
SAYE	1	1	6
Total TalkTalk Telecom Group PLC schemes	3	3	37
Legacy Carphone Warehouse schemes			
TTG VES and CPW TTG VES*	1	31	–
Performance share plan	–	4	2
ESOS	–	1	1
Other employee share option schemes	–	1	1
Total legacy Carphone Warehouse schemes	1	37	4
Total	4	40	41

* No options are shown as outstanding in respect of the VES schemes at the end of the year as the number of options available is not known until the vesting date.

5. Share-based payments continued

TalkTalk Telecom Group PLC schemes

(i) All Employee Share Option Award – 2012

The All Employee Share Option Award – 2012 was granted in September 2012 under the approved DSOP rules. The award of 1,000 nil priced share options per qualifying employee is designed to reward all employees who are not currently part of another share option plan and to promote all employee share ownership. The exercise of options is subject to continuing employment on the vesting date in September 2013 and there are no performance conditions in relation to this award. These options lapse on resignation of an employee.

	2013	
	Number million	WAEP £
Outstanding at the beginning of the year	–	–
Granted during the year	2	–
Outstanding at the end of the year	**2**	**–**
Exercisable at the end of the year	**–**	**–**

Valuation method	Black Scholes
Share price (pence)	1.92
Exercise price (pence)	nil
Expected volatility	15.58%
Expected exercise (years)	1.5
Risk free rate	0.16%
Expected dividend yield	4.69%
Fair value of options granted (£m)	4.3

The weighted average remaining contractual life of the All Employee Share Option Award – 2012 is 0.9 years (2012: nil).

The TalkTalk DSOP is designed to provide a long term incentive plan for senior employees of the Group.

(ii) DSOP – 2012 grant

Nil priced share option awards were first granted in February 2012 and are subject to absolute TSR and EPS performance targets with a cap and collar to address volatility in the market, as detailed in the Directors' Remuneration Report. The options are measured over a performance period to 31 March 2015 and will vest on the publication of the Group's 2015 Annual Report. A total of 60% of the vested options are exercisable from the vesting date, with the remaining 40% of options being exercisable twelve months later. Options are forfeited if an employee leaves the Group before the options vest. Awards are triggered within a range from 10% to 19% for compound annual growth of TSR and EPS. A total of 25% of the part of an award relative to either EPS or TSR will vest for the minimum target rising to 40% for target performance, 70% for stretch performance and 100% for super stretch performance.

	2013		2012	
DSOP – 2012 grant	Number million	WAEP £	Number million	WAEP £
Outstanding at the beginning of the year	11	–	–	–
Granted during the year	1	–	11	–
Outstanding at the end of the year	**12**	**–**	11	–
Exercisable at the end of the year	**–**	**–**	–	–

During the year, the Group granted a further 523,000 options under the DSOP – 2012 grant to a number of new senior employees. A separate fair value exercise was conducted for each grant using the Monte Carlo method, the total fair value of the options granted totalled £105,000. Detailed assumptions are not included here for each of the grants due to the fact that they are immaterial to the Group.

(iii) DSOP – 2010 grant

Awards made under the DSOP – 2010 grant are subject to TSR performance targets and were measured over a performance period to 28 March 2013. Options were forfeited if an employee left the Group before the options vested. On 28 March 2013, 16 million options vested but they are not exercisable until after the preliminary announcement on 16 May 2013. The original date of vesting of 29 March 2013 was amended to 28 March 2013 due to a bank holiday.

Notes to the consolidated financial statements continued

5. Share-based payments continued

TalkTalk Telecom Group PLC schemes continued

(iii) DSOP – 2010 grant continued

DSOP – 2010 grant	2013 Number million	2013 WAEP £	2012 Number million	2012 WAEP £
Outstanding at the beginning of the year	**20**	**1.24**	24	1.24
Forfeited during the year	**(3)**	**1.27**	(4)	1.27
Outstanding at the end of the year	**17**	**1.24**	20	1.24
Exercisable at the end of the year	**–**	**–**	–	–

The weighted average remaining contractual life of DSOP – 2012 grant is 8.9 years (2012: 13.0 years), and the DSOP – 2010 grant is 7.0 years (2012: 7.7 years). Of the DSOP – 2010 grant, 472,000 options were nil priced, of which 236,000 vested on 1 September 2012 but have not yet been exercised.

(iv) SAYE

The scheme permits the granting of options to employees linked to a bank SAYE contract for a term of three or five years. Contributions from UK employees range from £5 to £250 per month. Options may be exercised at the end of the three or five year period at an exercise price determined at the invitation date. The scheme is available for a period each year for employees to join.

Exercise prices for the schemes are set out below:

2012 grant	123p per share
2011 grant	119p per share
2010 grant	102p per share

	2013 Number million	2013 WAEP £	2012 Number million	2012 WAEP £
Outstanding at the beginning of the year	**6**	**1.05**	7	1.02
Granted during the year	**1**	**1.23**	1	1.19
Forfeited during the year	**(1)**	**1.11**	(2)	1.03
Outstanding at the end of the year	**6**	**1.08**	6	1.05
Exercisable at the end of the year	**–**	**–**	–	–

	SAYE – 2012 grant
Valuation method	Black Scholes
Share price (pence)	1.91
Exercise price (pence)	1.23
Expected volatility	13.17%
Expected exercise (years)	3.8
Risk free rate	0.75%
Expected dividend yield	4.72%
Fair value of options granted (£m)	0.6

The weighted average remaining contractual life of SAYE options is 1.6 years (2012: 2.2 years). No options were exercisable either during the year or at the year end.

(v) TTG VES and CPW TTG VES

The TTG VES enables participants to share in up to 7% of any increase in the value of the Group over an opening valuation representing invested capital at 1 April 2009, adjusted as relevant for changes in invested capital since that date. The incremental value is measured after a minimum annual rate of return of 7% on this invested capital. The Group advanced loans to participants to enable them to purchase A shares in TalkTalk Group Limited, the holding company of the Group's operating business. The CPW TTG VES enables participants to share in 2.24% of any increase in the value of the Group over an opening valuation representing invested capital at 1 April 2009, adjusted for the change in the Group's opening share price since 1 April 2009. In line with the TTG VES, the invested capital is adjusted for changes in invested capital since 1 April 2009 and the incremental value is measured after a minimum annual rate of return of 7%. For the vesting in September 2013, this is capped at the September 2012 amount.

The Group's opening share price for this purpose represents an allocation of the share price of CPW at that rate, based on the market capitalisation of the Group and Carphone Warehouse Group PLC in the five days following demerger. CPW advanced loans to participants to enable them to purchase C shares in TalkTalk Group Limited, the holding company of the Group's operating businesses.

5. Share-based payments continued

TalkTalk Telecom Group PLC schemes continued

(v) TTG VES and CPW TTG VES continued

The Group has an obligation to acquire the A and C shares if performance conditions are met, to provide to participants the share of value described above.

The fair value of the schemes, which has performance targets based on the growth of the market capitalisation of the Group, was estimated at the date of grant using a Monte Carlo model to initially value the A shares and then a Black Scholes model to calculate the option value. The model combines the valuation price of a share at the date of grant with the probability of meeting performance criteria, based on the expected value of the Group at the date of grant discounted for the lack of marketability of the shares.

On 17 September 2012, the Group's Remuneration Committee determined that the relevant performance conditions of these VES schemes (including the 5% TSR requirement) had been satisfied, meaning the VES participants were entitled to exercise 60% of their VES options. The remaining 40% will vest in September 2013 subject to ongoing performance conditions being met. The participants' options were acquired by the Company for new ordinary shares in the Company and cash resulting in a cash outflow of £35m. The net issue of 17 million shares in the Company was at a price of £1.86 per share being the average closing price of the Company's shares on 18 and 19 September 2012. The settlement of the schemes resulted in a net movement in reserves of £31m, being the recognition of share premium of £32m and a £63m debit in retained earnings and other reserves. The £63m debit to reserves represents a total cash outflow of £35m and the value of new PLC shares issued of £32m net of the repayment of the associated VES loans, interest and a reduction in the Group's liability to settle the schemes.

6. Finance costs

Finance costs are analysed as follows:

	2013 £m	2012 £m
Interest on bank loans and overdrafts	**14**	14
Facility fees and similar charges	**4**	3
Unwinding of discount on provisions	**1**	1
	19	18

During the prior year the Group refinanced its revolving credit facility and paid £7m in respect of facility fees. This is being amortised over the expected life of the loan and is included within facility fees and similar charges above.

7. Taxation

Accounting policy

Current tax, including UK corporation tax and overseas tax, is provided at amounts expected to be paid or recovered using the tax rates and laws that have been enacted or substantively enacted at the balance sheet date.

Deferred tax is provided on temporary differences between the carrying amount of an asset or liability in the balance sheet and its tax base.

Deferred tax liabilities represent tax payable in future periods in respect of taxable temporary differences. Deferred tax assets represent tax recoverable in future periods in respect of deductible temporary differences, and the carry-forward of unused tax losses and credits. Deferred tax is determined using the tax rates that have been enacted or substantively enacted at the balance sheet date and are expected to apply when the deferred tax asset is realised or the deferred tax liability is settled.

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. Current and deferred tax is recognised in the income statement except where it relates to an item recognised directly in reserves, in which case it is recognised directly in reserves.

Deferred tax assets and liabilities are offset where there is a legal right to do so in the relevant jurisdictions.

Critical judgements in applying the Group's accounting policy

The extent to which tax losses can be utilised depends on the extent to which taxable profits are generated in the relevant jurisdictions for the foreseeable future, on the tax legislation then in force, and as such the value of associated deferred tax assets is uncertain.

Notes to the consolidated financial statements continued

7. Taxation continued

Tax – income statement

The tax charge comprises:

	2013 £m	2012 £m
Current tax		
UK Corporation tax	–	–
Adjustments in respect of prior years:		
UK Corporation tax	–	(4)
Total current tax charge (credit)	–	(4)
Deferred tax		
Origination and reversal of timing differences	18	(13)
Effect of change in tax rate	5	10
Adjustments in respect of prior years – deferred tax recognised	(1)	(4)
Total deferred tax charge (credit)	22	(7)
Total tax charge (credit)	**22**	**(11)**

The tax charge on Headline earnings for the year ended 31 March 2013 is £33m (2012: £56m) representing an effective tax rate on pre-tax profits of 20% (2012: 26%). The tax charge on Statutory earnings for the year ended 31 March 2013 is £22m (2012: £11m credit). The reconciliation between the Headline and Statutory tax charge is shown in note 9.

The principal differences between the tax charge and the amount calculated by applying the standard rate of UK corporation tax of 24% (2012: 26%) to the profit before tax are as follows:

	2013 £m	2012 £m
Profit before tax	122	127
Tax at 24% (2012: 26%)	29	33
Items attracting no tax relief or liability	1	(2)
Effect of change in tax rate	5	10
Adjustments in respect of prior years	(1)	(4)
Movement in unrecognised tax losses during the year	(12)	(3)
Recognition of additional Tiscali losses	–	(45)
Total tax charge (credit) through income statement	22	(11)

Tax – retained earnings and other reserves

	2013 £m	2012 £m
Total tax charge (credit) through income statement	22	(11)
Deferred tax (credit) charge recognised directly in retained earnings and other reserves	(11)	–
Total tax charge (credit) through retained earnings and other reserves	**11**	**(11)**

The deferred tax credit recognised directly in retained earnings and other reserves for the year ended 31 March 2013 relates to share-based payments.

7. Taxation continued

Tax – balance sheet

The deferred tax assets recognised by the Group and movements thereon during the year are as follows:

	Share-based payments £m	Timing differences on capitalised costs £m	Tax losses £m	Timing differences on acquisition intangibles £m	Other timing differences £m	Total £m
At 1 April 2012	**1**	**71**	**56**	**(11)**	**3**	**120**
(Charge) credit to the income statement	**–**	**(9)**	**(16)**	**5**	**(2)**	**(22)**
Credit to reserves	**11**	**–**	**–**	**–**	**–**	**11**
At 31 March 2013	**12**	**62**	**40**	**(6)**	**1**	**109**

	Share-based payments £m	Timing differences on capitalised costs £m	Tax losses £m	Timing differences on acquisition intangibles £m	Other timing differences £m	Total £m
At 1 April 2011	3	76	45	(12)	4	116
(Charge) credit to the income statement	(2)	(5)	11	3	(1)	6
Acquisition of subsidiaries	–	–	–	(2)	–	(2)
At 31 March 2012	1	71	56	(11)	3	120

No deferred tax assets and liabilities have been offset in either year, except where there is a legal right to do so in the relevant jurisdictions. On 3 July 2012 a reduction in the UK Statutory rate of Corporation tax was substantively enacted, bringing the tax rate down from 24% to 23% with effect from 1 April 2013. Accordingly the tax assets and liabilities recognised at 31 March 2013 take account of this change. This has resulted in a tax charge to the income statement as the value of the Group's tax assets have been reduced.

The Government intends to enact further reductions in the main tax rate, down to 21% effective from 1 April 2014 and to 20% from 1 April 2015. As these tax rates were not substantially enacted at the balance sheet date, the rate reduction is not reflected in these financial statements.

The asset also reflects the annual recognition of a further tranche of the tax losses acquired with Tiscali UK Limited, including Video Networks Limited, based on the Group's rolling forecast. This is in line with the Group's agreement with HMRC, reached in the previous year, following which the immediate increase in the deferred tax asset of £45m was recognised as an exceptional credit (note 9).

At 31 March 2013, the Group had unused tax losses of £759m (2012: £873m) available for offset against future taxable profits. A deferred tax asset of £40m (2012: £56m) has been recognised in respect of £172m (2012: £232m) of such losses, based on expectations of recovery in the foreseeable future.

No deferred tax asset has been recognised in respect of the remaining £587m (2012: £641m) as there is insufficient evidence that there will be suitable taxable profits against which these losses can be recovered. All losses may be carried forward indefinitely.

Notes to the consolidated financial statements continued

8. Dividends

Accounting policy

Dividend income is recognised when payment has been received. Final dividend distributions are recognised as a liability in the financial statements in the year in which they are approved by the relevant shareholders. Interim dividends are recognised in the year in which they are paid.

The following dividends were paid by the Group to its shareholders:

	2013 £m	2012 £m
Ordinary dividends		
Final dividend for the year ended 31 March 2011 of 3.9p per ordinary share	–	35
Interim dividend for the year ended 31 March 2012 of 2.6p per ordinary share	–	23
Final dividend for the year ended 31 March 2012 of 6.4p per ordinary share	56	–
Interim dividend for the year ended 31 March 2013 of 3.45p per ordinary share	31	–
Total ordinary dividends	**87**	58

The proposed final dividend for the year ended 31 March 2013 is 6.95p per ordinary share on approximately 892 million shares (£62m), which was approved by the Board on 15 May 2013 and has not been included as a liability as at 31 March 2013.

The Group ESOT has waived its rights to receive dividends in the current and prior year and this is reflected in the analysis above.

9. Reconciliation of Headline information to Statutory information

Accounting policy

Headline results are stated before the amortisation of acquisition intangibles and exceptional items. Exceptional items are those that are considered to be one-off, non-recurring in nature and so material that the Directors believe that they require separate disclosure to avoid distortion of underlying performance and should be separately presented on the face of the income statement.

Year ended 31 March 2013	EBITDA £m	Profit before interest and tax £m	Profit before tax £m	Profit for the year £m
Headline results	290	184	165	132
Exceptional items – (a)	(7)	(7)	(7)	(5)
Exceptional items – (b)	(11)	(11)	(11)	(8)
Exceptional items – (d)	27	27	27	21
Amortisation of acquisition intangibles – (f)	–	(52)	(52)	(40)
Statutory results	299	141	122	100

Year ended 31 March 2012	EBITDA £m	Profit before interest and tax £m	Profit before tax £m	Profit for the year £m
Headline results	326	233	215	159
Exceptional items – (b)	(14)	(14)	(14)	(11)
Exceptional items – (c)	(11)	(11)	(11)	(8)
Exceptional items – (e)	(2)	(2)	(2)	(2)
Amortisation of acquisition intangibles – (f)	–	(61)	(61)	(45)
Exceptional items – (g)	–	–	–	45
Statutory results	299	145	127	138

Headline information is provided because the Directors consider that it provides assistance in understanding the Group’s underlying performance.

9. Reconciliation of Headline information to Statutory information continued

Accounting policy continued

a) Operating efficiencies – Phase III (Making TalkTalk Simpler)
During the year ended 31 March 2013, the Group has continued a review of operating structure to drive process and efficiency improvements over the medium term. The initiatives that form part of the Group's Making TalkTalk Simpler programme implemented in the year were: a restructuring of the systems and processes in TalkTalk Business to remove duplication and better align the sales and service model for future growth; and a review and consolidation of the outsourcing partners and rebalancing of the Group's on-shore footprint. This has resulted in redundancy, dual running, property and project management costs. The total charge incurred in the year ended 31 March 2013 was £7m (2012: £nil).

A total taxation credit of £2m in respect of this item has been recognised in the year ended 31 March 2013 (2012: £nil).

b) Operating efficiencies – Phase II (Consumer contact centre rationalisation)
On 24 April 2012, the Group announced the second stage of its contact centre rationalisation. This resulted in consolidating and outsourcing operations in Preston and Northampton. Costs were incurred in respect of redundancy, dual running and consultancy. The total charge incurred in the year ended 31 March 2013 was £11m (2012: £nil).

On 7 September 2011, the Group announced the closure of the Group's contact centre in Waterford, Ireland, which resulted in redundancy, consultancy and onerous property lease costs. The total charge incurred in the year ended 31 March 2012 was £14m.

A total taxation credit of £3m in respect of this item has been recognised in the year ended 31 March 2013 (2012: £3m).

c) Operating efficiencies – Phase I (Back office restructuring)
On 26 January 2011 a major restructure of the Group was announced to integrate technology and IT capabilities and consolidate back office functions. The reorganisation principally resulted in a reduction in headcount and required project management and consulting costs to deliver these benefits. The programme also resulted in onerous contract and dual running costs relating to a number of technology contracts where services previously provided externally are now being provided in-house. The total charge incurred in the year ended 31 March 2013 was £nil (2012: £11m).

A total taxation credit of £nil in respect of this item has been recognised in the year ended 31 March 2013 (2012: £3m).

d) Wholesale Ethernet services overcharges
In December 2012, Ofcom determined that BT had overcharged the Group for certain wholesale Ethernet services. Accordingly, BT was required to make repayments to the Group for these overcharges. A total of £27m has been recognised as an exceptional credit in the year ended 31 March 2013 (note 27).

A total taxation charge in respect of this item of £6m has been recognised in the year ended 31 March 2013 (2012: £nil).

e) Other
In April 2013, Ofcom fined the Group £750,000 as a result of a contravention of certain provisions of The Communication Act 2003 relating to abandoned and silent calls. The full amount has been recouped from the call centres that made the calls with a net impact of £nil on the Group's results. This has been accounted for in the year ended 31 March 2013 in accordance with IAS 10 'Events After the Reporting Period'. No tax credit was recognised in respect of this fine.

During the prior year Ofcom fined the Group £3m as a result of a contravention of General Condition 11 under Section 94 of The Communication Act 2003. No tax credit was recognised in respect of this fine. In addition a credit of £1m was recognised in the year ended 31 March 2012 in respect of a provision release for costs no longer anticipated to be incurred.

Notes to the consolidated financial statements continued

9. Reconciliation of Headline information to Statutory information continued

Accounting policy continued

f) Amortisation of acquisition intangibles

An amortisation charge in respect of acquisition intangibles of £52m was incurred in the year ended 31 March 2013 (2012: £61m).

A total tax credit of £12m has been recognised in the year ended 31 March 2013 (2012: £16m).

g) Exceptional items – taxation

During the year ended 31 March 2012, the Group reached agreement with HMRC over the utilisation of brought forward tax losses acquired with the Tiscali UK business in 2009, including those of Video Networks Limited. This resulted in the recognition of deferred tax assets of £45m, in addition to those recognised at the acquisition date.

10. Earnings per share

Earnings per share is shown on an Underlying, Headline and Statutory basis to assist in the understanding of the performance of the Group.

	2013 £m	2012 £m
Underlying earnings*	**182**	152
Headline earnings (note 9)	**132**	159
Statutory earnings	**100**	138
Weighted average number of shares (millions):		
Shares in issue	**924**	914
Less weighted average holdings by Group ESOT	**(40)**	(29)
For basic EPS	**884**	885
Dilutive effect of share options	**56**	40
For diluted EPS	**940**	925

	2013 pence	2012 pence
Basic earnings per share		
Underlying	**20.6**	17.2
Headline	**14.9**	18.0
Statutory	**11.3**	15.6

	2013 pence	2012 pence
Diluted earnings per share		
Underlying	**19.4**	16.4
Headline	**14.0**	17.2
Statutory	**10.6**	14.9

* Underlying earnings for the year ended 31 March 2013 of £182m is defined as Headline earnings excluding costs of £62m relating to the investment in TV less an allocation of taxation of £12m based on the Group's Headline effective tax rate. In the year ended 31 March 2012, Underlying earnings of £152m was defined as Headline earnings excluding the profit on sale of a freehold property of £9m less an allocation of taxation of £2m based on the Group's Headline effective tax rate.

The number of shares that could be issued but are not considered to be dilutive at 31 March 2013 is 5 million (2012: 20 million).

11. Goodwill and other intangible assets

(a) Goodwill

Accounting policy

Goodwill arising on the acquisition of subsidiary undertakings and businesses, representing the excess of the fair value of the consideration given over the fair value of the identifiable assets and liabilities acquired, is recognised initially as an asset at cost and is subsequently measured at cost less any accumulated impairment losses.

On disposal of a subsidiary undertaking, the relevant goodwill is included in the calculation of the profit or loss on disposal.

Critical judgements in applying the Group's accounting policy

The Group has two Cash Generating Units (CGUs) – Consumer and TalkTalk Business. For the purpose of impairment testing, at the acquisition date, goodwill is allocated to each of the CGUs expected to benefit from the synergies of the acquisition. The Group's shared costs and assets relating mainly to infrastructure and central overheads are allocated across the two CGUs based on the relative future cash flows that those shared costs support.

Determining whether goodwill is impaired requires estimation of the recoverable amount which is determined by estimating the value in use of the CGUs to which the goodwill has been allocated.

Impairment of goodwill

Goodwill is not subject to amortisation but is tested for impairment annually or whenever there is an indication that the asset may be impaired; this review is performed at a CGU level.

The recoverable amount is determined by assessing the future cash flows of the CGU to which the goodwill relates. The future cash flows of the Group are taken from the Board or Management approved five year plan and extrapolated out to 20 years based on the UK's long term growth rate. This is discounted by the CGU's weighted average cost of capital pre-tax to give the net present value of that CGU. Where the net present value of future cash flows is less than the carrying value of the unit, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the CGU and then to the other assets of the CGU pro-rata on the basis of the carrying amount of each asset in the unit. Any impairment loss is recognised in the income statement and is not subsequently reversed.

Sensitivity analysis is performed using reasonably possible changes in the key assumptions.

	2013 £m	2012 £m
Opening cost and net book value	**480**	471
Acquisition of subsidiaries (note 13)	**–**	9
Disposal (note 13)	**(1)**	–
Closing cost and net book value	**479**	480

The goodwill acquired in business combinations is allocated at acquisition to the CGUs that are expected to benefit from that business combination. The allocation of goodwill across the CGUs is as follows:

	2013 £m	2012 £m
Consumer	**337**	337
TalkTalk Business	**142**	143
	479	480

Notes to the consolidated financial statements continued

11. Goodwill and other intangible assets continued

(b) Other intangible assets

Impairment of goodwill continued

Impairment review

The key assumptions used in the Group's goodwill impairment review are as follows:

- Long term growth rates
  Long term revenue growth rates applied are based on the growth rate for the UK per the OECD. The rate applied in the current year was 1.1% (2012: 1.8%).
- Discount rate
  The underlying discount rate for each CGU is based on the UK ten year gilt rate adjusted for an equity risk premium and the systematic risk of the CGU. The average pre-tax rate for both CGUs used to discount the forecast cash flows is 8.1% (2012: 8.2%). The assumptions used in the calculation of the CGU's discount rate are benchmarked to externally available data. The same discount rate has been applied to both CGUs due to the similarity of risk factors and geographical location.
- Capital expenditure
  Forecast capital expenditure is based on senior management expectations of future required support of the network and current run rate of expenditure.
- Customer factors
  The key assumptions for the forecast cash flows of each of the CGUs are based on expected customer growth rates, ARPU, direct costs, including acquisition costs and change in product mix. The value assigned to each of these assumptions has been determined based on the extrapolation of historical trends in the Group and external information on expected trends of future market developments.

Sensitivity analysis has been performed for each key assumption and the Directors have not identified any reasonably possible material changes in the key assumptions that would cause the carrying value of goodwill to exceed the recoverable amount.

Accounting policy

Operating intangibles

Operating intangibles include internal infrastructure and design costs incurred in the development of software for internal use. Internally generated software is recognised as an intangible asset only if it can be separately identified, it is probable that the asset will generate future economic benefits, and the development cost can be measured reliably. Where these conditions are not met, development expenditure is recognised as an expense in the year in which it is incurred. Operating intangibles are amortised on a straight line basis over their estimated useful economic lives of up to eight years.

Acquisition intangibles

Acquired intangible assets such as customer bases and other intangible assets acquired through a business combination are capitalised separately from goodwill and amortised over their expected useful lives of up to six years on a straight line basis. The value attributed to such assets is based on the future economic benefit that is expected to be derived from them, calculated as the present value of future cash flows after a deduction for contributory assets.

Critical judgements in applying the Group's accounting policy

Impairment

At the acquisition date, acquisition intangibles are allocated to each of the CGUs expected to benefit from the synergies of the combination. The Group's shared costs and assets relating mainly to infrastructure and central overheads are allocated across the two CGUs based on the relative future cash flows.

Determining whether the carrying amount of operating and acquisition intangibles have any indication of impairment requires judgement. If an indication of impairment is identified, further judgement is required to assess whether the carrying amount can be supported by the value in use of the CGU that the asset is allocated to.

The value in use calculation involves estimation of both the future cash flows of the CGUs and the selection of appropriate discount rates, to use to calculate present values.

Useful economic lives

The assessment of the useful economic lives of these operating and acquisition intangibles requires judgement. Amortisation is charged to the income statement based on the useful economic life selected. This assessment requires estimation of the period over which the Group will benefit from the assets.

11. Goodwill and other intangible assets continued

(b) Other intangible assets continued

Impairment of assets

The Group reviews the carrying amounts of its intangible assets to determine whether there is any indication that those assets have suffered an impairment loss at each reporting date. Where an indicator of impairment exists, the Group makes a formal estimate of the asset's recoverable amount and the extent of any impairment loss.

The recoverable amount is the higher of an asset's fair value less costs to sell and its value in use. In assessing value in use, the estimated cash flows are discounted to their present value using a pre-tax discount rate that reflects the current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset is estimated to be less than the carrying amount, the carrying amount of the asset or CGU is reduced to its recoverable amount.

Other intangible assets are analysed as follows:

	Operating intangibles £m	Acquisition intangibles £m	Total other intangibles £m
Opening balance at 1 April 2012	**123**	**79**	**202**
Additions	**30**	**–**	**30**
Amortisation	**(26)**	**(52)**	**(78)**
Closing balance at 31 March 2013	**127**	**27**	**154**
Cost (gross carrying amount)	**260**	**326**	**586**
Accumulated amortisation	**(133)**	**(299)**	**(432)**
Closing balance at 31 March 2013	**127**	**27**	**154**

	Operating intangibles £m	Acquisition intangibles £m	Total other intangibles £m
Opening balance at 1 April 2011	124	131	255
Additions	26	9	35
Amortisation	(27)	(61)	(88)
Closing balance at 31 March 2012	123	79	202
Cost (gross carrying amount)	230	326	556
Accumulated amortisation	(107)	(247)	(354)
Closing balance at 31 March 2012	123	79	202

Operating intangibles include internally generated assets of net book value £31m (2012: £26m), which are amortised over a period of up to eight years. This includes additions of £10m (2012: £7m) and an amortisation charge of £5m (2012: £6m) in the year ended 31 March 2013.

Notes to the consolidated financial statements continued

11. Goodwill and other intangible assets continued

(b) Other intangible assets continued

Impairment of assets continued

Included within operating intangibles is the following asset which is material to the Group:

- TRIO, the customer billing system, which has a net book value of £86m (2012: £90m). TRIO is amortised over a period of up to eight years depending on the release date of the relevant component. The weighted average remaining useful economic life of the components of TRIO is five years (2012: five years).

Acquisition intangibles are removed from cost in the analysis in the year after they are fully amortised.

All acquisition intangibles relate to customer bases.

The customer bases relate primarily to the AOL UK internet access business which was acquired in December 2006 and the Tiscali UK internet access business which was acquired in July 2009. The valuation of customer bases is derived from the discounted future cash flows expected from them, after a deduction for contributory assets.

The following customer base is material to the Group at 31 March 2013:

- Tiscali customer base which has a net book value of £23m (2012: £41m) and a remaining useful economic life of 15 months (2012: 27 months).

In addition, the following customer base was material to the Group at 31 March 2012:

- AOL broadband customer base which had net book value of £32m and a remaining useful economic life of ten months.

12. Property, plant and equipment

Accounting policy

Property, plant and equipment are stated at cost, net of depreciation and any provision for impairment. Depreciation is provided on all property, plant and equipment at rates calculated to write off the cost, less estimated residual value, of each asset on a straight line basis over its expected useful life from the date it is brought into use, as follows:

Short leasehold costs	10% or the lease term if less than ten years
Network equipment and computer hardware	12.5–50% per annum
Fixtures and fittings	20–25% per annum

Critical judgements in applying the Group's accounting policy

The assessment of the useful economic lives of these assets requires judgement. Depreciation is charged to the income statement based on the useful economic life selected. This assessment requires estimation of the period over which the Group will benefit from the assets.

Determining whether the carrying amount of these assets has any indication of impairment also requires judgement. If an indication of impairment is identified, further judgement is required to assess whether the carrying amount can be supported by the value in use of the CGU that the asset is allocated to. The value in use calculation involves estimation of both the future cash flows of the CGUs and the selection of appropriate discount rates, to use to calculate present values (note 11).

12. Property, plant and equipment continued

Impairment of assets

Property, plant and equipment

The Group reviews the carrying amounts of its fixed assets to determine whether there is any indication that those assets have suffered an impairment loss at each reporting date. The Group uses the same methodology as set out in note 11 for operating and acquisition intangibles.

	Leasehold improvements £m	Network equipment and computer hardware £m	Fixtures and fittings £m	Total £m
Opening balance at 1 April 2012	**6**	**286**	**–**	**292**
Additions	**–**	**79**	**–**	**79**
Depreciation	**(1)**	**(75)**	**–**	**(76)**
Closing balance at 31 March 2013	**5**	**290**	**–**	**295**
Cost (gross carrying amount)	**6**	**584**	**6**	**596**
Accumulated depreciation and impairment charges	**(1)**	**(294)**	**(6)**	**(301)**
Closing balance at 31 March 2013	**5**	**290**	**–**	**295**

Assets are removed from cost and depreciation in the above analysis once they are fully depreciated and are no longer in use.

	Leasehold improvements £m	Network equipment and computer hardware £m	Fixtures and fittings £m	Total £m
Opening balance at 1 April 2011	6	283	1	290
Additions	–	68	–	68
Disposals	–	(1)	–	(1)
Depreciation	–	(64)	(1)	(65)
Closing balance at 31 March 2012	6	286	–	292
Cost (gross carrying amount)	6	509	6	521
Accumulated depreciation and impairment charges	–	(223)	(6)	(229)
Closing balance at 31 March 2012	6	286	–	292

13. Non-current asset investments

Accounting policy

Investments, other than subsidiaries, are initially recognised at cost, being the fair value of the consideration given plus any transaction costs associated with the acquisition.

Investments are categorised as available for sale and are then recorded at fair value. Changes in fair value, together with any related taxation, are taken directly to equity and recycled to the income statement when the investment is sold or determined to be impaired.

	£m
Cost and net book value at 31 March 2012	**1**
Impairment	**(1)**
Cost and net book value at 31 March 2013	**–**

Non-current asset investments at 31 March 2013 related to an 8.4% (2012: 8.4%) interest in Shared Band Limited, a telecommunications technology provider. During the year the Group impaired its investment to £nil.

Notes to the consolidated financial statements continued

13. Non-current asset investments continued

Accounting policy continued

(a) Principal investments

The Parent Company has investments in the following subsidiary undertakings, which principally affected the profits or losses or net assets of the Group. To avoid a statement of excessive length, details of investments that are not significant have been omitted. All holdings are in equity share capital and give the Group an effective holding of 100% on consolidation.

Name	Country of incorporation or registration	Nature of business
TalkTalk Group Limited	England and Wales	Holding company
TalkTalk Telecom Holdings Limited*	England and Wales	Holding company
TalkTalk Communications Limited	England and Wales	Telecommunications
TalkTalk Telecom Limited	England and Wales	Telecommunications
CPW Network Services Limited	England and Wales	Telecommunications

* Directly held by the Company.

(b) Acquisitions and disposals

(i) Acquisitions

During the prior year, the Group:

- acquired Executel Limited and Greystone Telecom Limited for cash consideration net of cash acquired of £15m, which resulted in acquisition intangibles of £8m, goodwill of £9m and the corresponding deferred tax liability of £2m. The impact of these acquisitions on the results of the Group for the year ended 31 March 2012 had the business been acquired on 31 March 2011 is immaterial. The goodwill of £9m was recognised relating to the future opportunities arising from the nature of the businesses and fit with the Group's existing operations; and
- paid cash consideration of £1m in respect of deferred consideration for TalkTalk Business (2CCH) Limited and Southern Communications Networks Limited and dealer buyouts. The acquisition of dealer buyouts resulted in acquisition intangibles of £1m.

(ii) Disposals

On 28 March 2013, the Group disposed of its investment in Southern Communications Networks Limited for cash consideration of £2m. Associated goodwill of £1m was written off resulting in a £1m profit on disposal. There was no associated acquisition intangible remaining in respect of this business.

In the prior year, the Group disposed of its ValueCall operations for cash consideration of £3m. There was no associated goodwill or acquisition intangible in respect of this business resulting in a £3m profit on disposal.

14. Interest in joint venture

Accounting policy

Interests in joint ventures are accounted for using the equity method. The Group income statement includes the Group's share of the post-tax profits or losses of the joint ventures based on their financial statements for the year. In the Group balance sheet, the Group's interest in joint ventures are shown as a non-current asset in the balance sheet, representing the Group's investment in the share capital of the joint ventures, as adjusted by post-acquisition changes in the Group's share of the net assets or liabilities less provision for any impairment.

When a joint venture has net liabilities, any loans advanced to the venture are included in the Group's equity accounted investment in it. When a venture has net assets, any loans advanced to it are shown separately in the balance sheet, as a receivable to the Group.

The Group holds 14.3% of the ordinary share capital of YouView TV Limited, a joint venture with The British Broadcasting Corporation, ITV Broadcasting Limited, British Telecom PLC, Channel Four Television Corporation, Arqiva Limited and Channel 5 Broadcasting Limited. The joint venture was set up in order to develop a free-to-air internet connected TV service to UK homes. The table below sets out the net additions in the year.

	2013 £m	2012 £m
Opening balance at 1 April	**7**	4
Additions	**6**	4
Share of results	**(4)**	(1)
Closing balance at 31 March	**9**	7

The Group has renewed the carrying value of YouView and has concluded that there is no indication of impairment.

14. Interest in joint venture continued

Accounting policy continued

The Group's share of the results, assets and liabilities of its joint ventures are as follows:

Group share of results of joint ventures	2013 £m	2012 £m
Expenses	**(4)**	(1)
Loss before taxation	**(4)**	(1)
Taxation	**–**	–
Loss after taxation	**(4)**	(1)

Group share of net assets of joint ventures	2013 £m	2012 £m
Non-current assets	**9**	7
Net assets	**9**	7

At 31 March 2013 the Group had committed to pay £5m (2012: £13m) to YouView TV Limited, payable over the period to 31 March 2014.

15. Inventories

Accounting policy

Inventories are stated at the lower of cost and net realisable value, valued on a FIFO basis, and consist predominantly of set top boxes, handsets and routers. Net realisable value is based on estimated selling price, less costs expected to be incurred. A provision is made for obsolete items where appropriate.

	2013 £m	2012 £m
Goods for resale	**23**	3

16. Trade and other receivables

Critical judgements in applying the Group's accounting policy

Judgement is required in order to evaluate the likelihood of collection of customer debt after revenue has been recognised and hence the value of the bad and doubtful debt. These provisions are based on historical trends in the percentage of debts which are not recovered.

Trade and other receivables comprise:

	2013 £m	2012 £m
Current – trade and other receivables		
Trade receivables – gross	**156**	133
Less provision for impairment	**(33)**	(29)
Trade receivables – net	**123**	104
Other receivables	**41**	31
Prepayments and accrued income	**62**	49
Trade and other receivables	**226**	184
Loans to related parties (note 26)	**–**	2
	226	186

The Directors estimate that the carrying amount of trade receivables approximates to their fair value.

The average credit period taken on trade receivables, calculated by reference to the amount owed at the year end as a proportion of total revenue in the year, was 28 days (2012: 24 days).

The Group's trade receivables are denominated in the following currencies:

	2013 £m	2012 £m
UK Sterling	**123**	111
Other	**33**	22
	156	133

Notes to the consolidated financial statements continued

16. Trade and other receivables continued

Critical judgements in applying the Group's accounting policy continued

The ageing of gross trade receivables is as follows:

	2013 £m	2012 £m
Not yet due	**94**	80
0 to 2 months overdue	**18**	21
2 to 4 months overdue	**19**	14
Over 4 months overdue	**25**	18
	156	133

The ageing of the provision for impairment of trade receivables is as follows:

	2013 £m	2012 £m
Not yet due	**(3)**	(3)
0 to 2 months overdue	**(3)**	(5)
2 to 4 months overdue	**(7)**	(8)
Over 4 months overdue	**(20)**	(13)
	(33)	(29)

Movements in the provisions for impairment of trade receivables are as follows:

	2013 £m	2012 £m
Opening balance	**(29)**	(31)
Charged to the income statement	**(33)**	(38)
Receivables written off as irrecoverable	**29**	40
	(33)	(29)

Trade receivables of £32m (2012: £27m) were past due but not impaired. These balances primarily relate to Consumer and Corporate fixed line customers. The Group has made provisions based on historical rates of recoverability and all unprovided amounts are considered to be recoverable. The ageing analysis of these trade receivables is as follows:

	2013 £m	2012 £m
0 to 2 months	**15**	16
2 to 4 months	**12**	6
Over 4 months	**5**	5
	32	27

17. Trade and other payables

	2013 £m	2012 £m
Trade payables	**210**	135
Other taxes and social security costs	**10**	21
Other payables	**21**	26
Accruals and deferred income	**190**	197
	431	379

The Company has commercially agreed longer credit terms with certain suppliers. Excluding these suppliers the underlying average credit period taken on trade payables was 39 days (2012: 32 days). Including these suppliers, the average credit period taken was 48 days (2012: 32 days).

The Directors consider that the carrying amount of trade and other payables approximates to their fair value.

18. Cash and cash equivalents, loans and other borrowings

(a) Cash and cash equivalents are as follows:

	2013 £m	2012 £m
Cash at bank and in hand	**7**	2

The effective interest rate on bank deposits and money market funds was 0.7% (2012: 0.5%).

(b) Loans and other borrowings comprise:

	2013 £m	2012 £m
Current		
Bank overdrafts	**–**	1
Term loan	**25**	25
	25	26

	Maturity	2013 £m	2012 £m
Non-current			
Term loan	2014, 2015	**50**	75
Bilateral loan	2015	**30**	30
£560m revolving credit facility	2015	**295**	305
		375	410

Details of the current and non-current borrowing facilities of the Group for the year are set out below.

Bank overdrafts
Overdraft facilities are used to assist in short term cash management; these uncommitted facilities bear interest at a margin over the Bank of England base rate.

£75m Term loan
The Group has a committed Term loan of £75m (2012: £100m), of which a further £25m matures in March 2014 and the remainder matures in March 2015. The interest rate payable in respect of drawings under this facility is at a margin over Sterling LIBOR for the relevant currency and for the appropriate period. The actual margin applicable to any drawing depends on the ratio of net debt to EBITDA calculated in respect of the most recent accounting period. Covenants included in this facility restrict the ratio of net debt to EBITDA and require minimum levels of interest cover and fixed charges (interest and operating lease expenditure) cover.

£560m revolving credit facility (RCF) and £30m bilateral agreement
The Group has a £560m RCF which matures in November 2015. The interest rate payable in respect of drawings under this facility is at a margin over Sterling LIBOR and for the appropriate period. The actual margin applicable to any drawing depends on the ratio of net debt to EBITDA calculated in respect of the most recent accounting period. Covenants included in this facility restrict the ratio of net debt to EBITDA and require minimum levels of interest cover and fixed charges (interest and operating lease expenditure) cover. In addition to the RCF the Group also has £30m of bilateral agreements which mature in March 2015.

The Group's facilities total £665m. The Group was in compliance with its covenants throughout the current and prior year.

Notes to the consolidated financial statements continued

18. Cash and cash equivalents, loans and other borrowings continued

(b) Loans and other borrowings comprise continued:

Borrowing facilities

The Group had undrawn committed borrowing facilities at the end of the year, in respect of which all conditions precedent had been met, as follows:

	Maturity	2013 £m	2012 £m
Undrawn available committed facilities	2015	**265**	255

The book value and fair value of the Group's loans and other borrowings, all of which are in Sterling, are as follows:

	2013 £m	2012 £m
Less than 1 year	**25**	26
1 to 2 years	**80**	25
2 to 3 years	**295**	80
3 to 4 years	**–**	305
	400	436

Securities and guarantees

Committed borrowings are guaranteed by Group companies which make up 75% EBITDA and 75% of gross assets excluding internal transactions.

19. Financial risk management and derivative financial instruments

The book value and fair value of the Group's financial assets, liabilities and derivative financial instruments, excluding the Group's loans and other borrowings shown in note 18, are as follows:

	Book and fair value	
	2013 £m	2012 £m
Cash and cash equivalents	**7**	2
Trade and other receivables	**226**	184
Non-current investments and investment in joint venture	**9**	8
Trade and other payables*	**(428)**	(379)
Derivative financial instruments**	**(3)**	–
Loans to related parties	**–**	2
	(189)	(183)

* Deferred income has been included within the financial liabilities above so as to give completeness over the Group's contractual commitments on future cash outflows.

** Derivative financial instruments are included with other payables in note 17.

(a) Financial instruments

The Group's activities exposed it to a variety of financial risks including market risk (such as currency risk and interest rate risk), credit risk and liquidity risk. The Group Treasury function used certain financial instruments to mitigate potential adverse effects on the Group's financial performance from these risks. These financial instruments primarily consisted of bank loans and interest rate swaps. Other products, such as currency options, can also be used depending on the risks to be covered but have not been used in the current or preceding financial year. The Group does not trade or speculate in any financial instruments.

The Group has cash flow hedges in place that swap the interest rate risk on the RCF from floating to fixed. These hedges have been fully effective from inception. The fair value measurement is classified as Level 2, derived from other observable market data; this means that their fair value is based upon the mark to market valuation at the balance sheet date. The fair value of these instruments at 31 March 2013 is £3m (2012: £nil). An expense of £2m (2012: £nil) has been recognised in other comprehensive income in the year ended 31 March 2013. As the hedges were fully effective there has been no income statement impact.

19. Financial risk management and derivative financial instruments continued

(b) Embedded derivatives

No contracts with embedded derivatives have been identified and accordingly no such derivatives have been accounted for separately.

(c) Foreign exchange risk

The Group uses spot and forward foreign exchange trading to hedge transactional exposures, which arise mainly through cost of sales and operating expenses, and are primarily denominated in Euro and US Dollar. In the prior year the Group also used short term currency swaps for liquidity management. At 31 March 2013, the Sterling value of outstanding currency contracts was £17m (2012: £2m).

Borrowings and foreign exchange contracts are sensitive to movements in foreign exchange rates; this sensitivity can be analysed in comparison to year end rates (adjusted for funding to related parties and assuming all other variables remain constant). There was no material impact of a 10% movement in the UK Sterling/Euro exchange rate on either the income statement or other equity as non-Sterling debtors are broadly offset by non-Sterling creditors.

The effect of foreign exchange derivatives on borrowings at the year end was as follows:

	UK Sterling £m	Euro £m	Other £m	Total £m
2013				
Borrowings before derivatives	**400**	**–**	**–**	**400**
Derivatives	**(17)**	**19**	**(2)**	**–**
	383	**19**	**(2)**	**400**

	UK Sterling £m	Euro £m	Other £m	Total £m
2012				
Borrowings before derivatives	436	–	–	436
Derivatives	(2)	2	–	–
	434	2	–	436

During the year the Group used derivatives for management of foreign currency cash balances held by overseas subsidiaries, which were inherited from CPW on demerger, and foreign currency trading balances.

(d) Interest rate risk

The Group's interest rate risk arises primarily from cash, cash equivalents and borrowings, all of which are at floating rates of interest and thus expose the Group to cash flow interest rate risk. These floating rates are linked to LIBOR and other interest rate bases as appropriate to the instrument and currency. Future cash flows arising from these financial instruments depend on interest rates and periods for each loan or rollover. As detailed in section (a) the Group has cash flow hedges in place to mitigate its interest rate risk on its borrowings.

Cash and borrowings, as well as some foreign exchange products, are sensitive to movements in interest rates and such movements have been analysed in the table below by calculating the effect on the income statement and equity of one percentage point movement in the interest rate for the currencies in which most Group cash and borrowings are denominated. Funding to related parties has been offset against gross borrowings in calculating these sensitivities. This annualised analysis has been prepared on the assumption that the year end positions prevail throughout the year and therefore may not be representative of fluctuations in levels of borrowings.

	2013 £m	2012 £m
1% movement in the UK Sterling interest rate		
Income statement movement	**2**	2
Other equity movement	**–**	–

Notes to the consolidated financial statements continued

19. Financial risk management and derivative financial instruments continued

(e) Liquidity risk

The Group manages its exposure to liquidity risk by regularly reviewing the long and short term cash flow projections for the business against facilities and other resources available to it. Headroom is assessed based on historical experience as well as by assessing current business risks, including foreign exchange movements. Existing facilities do not expire until March 2015 and November 2015; it is Group policy to refinance debt maturities significantly ahead of maturity dates.

The table below analyses the Group's financial liabilities into relevant maturity groupings. The amounts disclosed in the table are the contractual undiscounted cash flows assuming year end interest rates remain constant and that borrowings are paid in full in the year of maturity.

	Less than 1 year £m	**1 to 2 years £m**	**2 to 3 years £m**	**3 to 4 years £m**	**4 to 5 years £m**	**More than 5 years £m**	**Total £m**
2013							
Loans and other borrowings	**(25)**	**(80)**	**(295)**	**–**	**–**	**–**	**(400)**
Derivative financial instruments – payable	**(17)**	**–**	**–**	**–**	**–**	**–**	**(17)**
Derivative financial instruments – receivable	**17**	**–**	**–**	**–**	**–**	**–**	**17**
Trade and other payables	**(431)**	**–**	**–**	**–**	**–**	**–**	**(431)**
	(456)	**(80)**	**(295)**	**–**	**–**	**–**	**(831)**

	Less than 1 year £m	1 to 2 years £m	2 to 3 years £m	3 to 4 years £m	4 to 5 years £m	More than 5 years £m	Total £m
2012							
Loans and other borrowings	(26)	(25)	(80)	(305)	–	–	(436)
Derivative financial instruments – payable	(2)	–	–	–	–	–	(2)
Derivative financial instruments – receivable	2	–	–	–	–	–	2
Trade and other payables	(379)	–	–	–	–	–	(379)
	(405)	(25)	(80)	(305)	–	–	(815)

(f) Credit risk

The Group's exposure to credit risk is regularly monitored. Debt, investments, foreign exchange and derivative transactions are all spread amongst a number of banks all of which have short or long term credit ratings appropriate to the Group's exposures. Trade receivables primarily comprise balances due from Consumer and TalkTalk Business fixed line customers, and provision is made for any receivables that are considered to be irrecoverable.

(g) Capital risk management

The Group manages its capital to ensure that entities in the Group will be able to continue as a going concern while maximising the return to stakeholders through the optimisation of the debt and equity balance. Further detail is provided in the Chief Financial Officer's Statement on page 11.

The capital structure of the Group consists of debt, which includes the borrowings disclosed in note 18, cash and cash equivalents and equity attributable to equity holders of the parent, comprising issued capital, reserves and retained earnings as disclosed in notes 21 to 22.

The Group's Board reviews the capital structure on an annual basis. As part of this review, the Board considers the cost of capital and the risks associated with each class of capital. The Group has a medium term target gearing ratio of 75% to 100% determined as a proportion of net debt to equity. The gearing ratio at 31 March 2013 of 89% (2012: 98%) was within the stated medium term target.

The gearing ratio at the year end is as follows:

	2013 £m	2012 £m
Debt	**(400)**	(436)
Cash and cash equivalents	**7**	2
Net debt	**(393)**	(434)
Equity	**442**	444
Net debt to equity ratio	**89%**	98%

20. Provisions

Accounting policy

Provisions are recognised when a legal or constructive obligation exists as a result of past events and it is probable that an outflow of resources will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Provisions are discounted where the time value of money is considered to be material.

Provisions are categorised as follows:

Operating efficiencies

Operating efficiencies provisions relate principally to redundancy costs and are only recognised where plans are demonstrably committed and where appropriate communication to those affected has been undertaken at the balance sheet date. These provisions are expected to be utilised over the next twelve months.

One Company integration

These provisions relate principally to redundancy costs and are only recognised where plans are demonstrably committed and where appropriate communication to those affected has been undertaken at the balance sheet date, and onerous contract costs where a commitment has been made to exit a contract as part of the One Company reorganisation. These provisions are expected to be utilised over the next twelve to 24 months.

Property

Property provisions relate to dilapidations and similar property costs, and costs associated with onerous property contracts. All such provisions are assessed by reference to the terms and conditions of the contract and market conditions at the balance sheet date. Onerous property contracts are expected to be utilised over the next six years. Dilapidation provisions are expected to be utilised as and when properties are exited.

Contract and other

Contract and other provisions relate to onerous contracts and contracts with unfavourable terms arising on the acquisition of businesses and anticipated costs of unresolved legal disputes. All such provisions are assessed by reference to the best available information at the balance sheet date. Contract and other provisions were utilised in the year ended 31 March 2013.

The below tables analyse the Group's provisions:

	2013 £m	2012 £m
Current	5	8
Non-current	8	10
	13	18

	Operating efficiencies £m	One Company integration £m	Property £m	Contract and other £m	Total £m
2013					
Opening balance	1	2	9	6	18
Charged to income statement	2	–	1	–	3
Utilised in the year	(1)	(1)	(1)	(6)	(9)
Unwinding of discount	–	1	–	–	1
	2	2	9	–	13

	Operating efficiencies £m	One Company integration £m	Property £m	Contract and other £m	Total £m
2012					
Opening balance	12	10	9	15	46
Charged to income statement	10	–	1	–	11
Utilised in the year	(21)	(7)	(1)	(8)	(37)
Released in the year	–	(1)	–	(2)	(3)
Unwinding of discount	–	–	–	1	1
	1	2	9	6	18

Notes to the consolidated financial statements continued

21. Share capital

	2013 million	2012 million	2013 £m	2012 £m
Allotted, called-up and fully paid				
Ordinary shares of 0.1p each	**931**	914	**1**	1

On 21 September 2012 the Company issued a further 17,135,825 ordinary shares of 0.1p each to settle the VES schemes (note 5).

22. Reserves

	Notes	Share capital £m	Share premium £m	Translation and hedging reserve £m	Demerger reserve £m	Retained earnings and other reserves £m	Total £m
At 1 April 2012		**1**	**586**	**(65)**	**(513)**	**435**	**444**
Total comprehensive income for the year		**–**	**–**	**–**	**–**	**98**	**98**
Issues of own shares*		**–**	**32**	**–**	**–**	**(63)**	**(31)**
Taxation of items recognised directly in reserves		**–**	**–**	**–**	**–**	**11**	**11**
Share-based payments reserve credit	5	**–**	**–**	**–**	**–**	**6**	**6**
Equity dividends	8	**–**	**–**	**–**	**–**	**(87)**	**(87)**
Currency translation differences		**–**	**–**	**1**	**–**	**–**	**1**
At 31 March 2013		**1**	**618**	**(64)**	**(513)**	**400**	**442**

	Notes	Share capital £m	Share premium £m	Translation and hedging reserve £m	Demerger reserve £m	Retained earnings and other reserves £m	Total £m
At 1 April 2011		1	586	(65)	(513)	406	415
Total comprehensive income for the year		–	–	–	–	138	138
Net purchase of own shares		–	–	–	–	(54)	(54)
Settlement of Group ESOT shares		–	–	–	–	1	1
Share-based payments reserve credit	5	–	–	–	–	4	4
Share-based payments reserve debit		–	–	–	–	(2)	(2)
Equity dividends	8	–	–	–	–	(58)	(58)
At 31 March 2012		1	586	(65)	(513)	435	444

* On 17 September 2012, the Group's Remuneration Committee determined that the relevant performance conditions of the VES schemes (including the 5% TSR requirement) had been satisfied meaning the VES participants were entitled to exercise 60% of their options as set out in note 5. The settlement of the schemes resulted in the recognition of share premium of £32m and a £63m movement in retained earnings and other reserves. The £63m debit to reserves represents a total cash outflow of £35m and the value of the new PLC shares issued of £32m net of the repayment of the associated VES loans, interest and a reduction in the Group's liability to settle the schemes.

Group ESOT

The Group ESOT held 39 million shares at 31 March 2013 (2012: 41 million) in the Company for the benefit of employees and former CPW employees. The Group ESOT has waived its rights to receive dividends and none of its shares have been allocated to specific schemes. At 31 March 2013 the shares had a market value of £107m (2012: £56m).

During the prior year the Group ESOT purchased 42 million shares at a cost of £54m.

Demerger reserve

The demerger reserve primarily reflects the profits or losses arising on the transfer of investments and net assets of CPW on demerger.

Translation and hedging reserve

The results of overseas operations are translated at the average foreign exchange rates for the year, and their balance sheets are translated at the rates prevailing at the balance sheet date. Exchange differences arising on the translation of opening net assets and results of overseas operations are recognised in the translation and hedging reserve. All other exchange differences are included in the income statement.

23. Analysis of changes in net debt

	Opening £m	Net cash flow £m	Closing £m
2013			
Cash and cash equivalents	**2**	**5**	**7**
Bank overdrafts	**(1)**	**1**	**–**
	1	**6**	**7**
Current loans and other borrowings	**(25)**	**–**	**(25)**
Non-current loans and other borrowings	**(410)**	**35**	**(375)**
	(435)	**35**	**(400)**
Total net debt	**(434)**	**41**	**(393)**
Loans to related parties	**2**	**(2)**	**–**
Total net debt including loans to related parties	**(432)**	**39**	**(393)**

	Opening £m	Net cash flow £m	Closing £m
2012			
Cash and cash equivalents	1	1	2
Bank overdrafts	(9)	8	(1)
	(8)	9	1
Current loans and other borrowings	(35)	10	(25)
Non-current loans and other borrowings	(395)	(15)	(410)
	(430)	(5)	(435)
Total net debt	(438)	4	(434)
Loans to related parties	2	–	2
Total net debt including loans to related parties	(436)	4	(432)

24. Commitments under operating leases

The Group leases network infrastructure and offices under non-cancellable operating leases. The leases have varying terms, purchase options, escalation clauses and renewal rights. There were no leases which were individually significant to the Group.

As at 31 March 2013 the Group had outstanding commitments for future minimum payments due as follows:

	2013 £m	2012 £m
Less than 1 year	**37**	37
2 to 5 years	**69**	73
Greater than 5 years	**68**	75
	174	185

25. Capital commitments

The Group had entered into the following amount of contractual commitments for the acquisition of property, plant and equipment at the year end:

	2013 £m	2012 £m
Expenditure contracted, but not provided for in the financial statements	**21**	21

Notes to the consolidated financial statements continued

26. Related party transactions

The Group's related party transactions are made on terms equivalent to those that prevail in arm's length transactions.

During the year, the Group had the following disclosable transactions:

	Other related parties £m
2013	
Loans owed to the Group	–
2012	
Loans owed to the Group	2

Other related parties comprised a loan to Future Office Communications Limited, an associated undertaking of the Group at 31 March 2012.

The remuneration of the Directors, who are some of the Key Management Personnel of the Group, is set out in the Directors' Remuneration Report on pages 22 to 28. The remuneration of all Key Management Personnel is disclosed in note 4.

27. Contingent liabilities

Included within the Group's results for the year is a credit of £29m relating to an Ofcom determination that BT had overcharged for certain wholesale Ethernet services. The full amount has been paid to the Group by 31 March 2013.

BT has appealed Ofcom's determination in the Competition Appeal Tribunal (CAT). However, the Group and other parties have also appealed the decision arguing that the original Ofcom determination was too low.

Independent auditor's report

to the members of TalkTalk Telecom Group PLC

We have audited the Parent Company financial statements of TalkTalk Telecom Group PLC for the year ended 31 March 2013 which comprise the Company balance sheet, the Company reconciliation of movements in shareholders' funds and the related notes 1 to 10. 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).

This report is made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of Directors and auditor

As explained more fully in the Directors' Responsibilities Statement, 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 and express an opinion on 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.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of:

- whether the accounting policies are appropriate to the Parent Company's circumstances and have been consistently applied and adequately disclosed;
- the reasonableness of significant accounting estimates made by the Directors; and
- the overall presentation of the financial statements.

In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on financial statements

In our opinion the Parent Company financial statements:

- give a true and fair view of the state of the Company's affairs as at 31 March 2013;
- 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 Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006; and
- the information given in the Directors' Report for the financial year for which the 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 Directors' Remuneration Report 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 Group financial statements of TalkTalk Telecom Group PLC for the year.

Peter O'Donoghue BA FCA (Senior Statutory Auditor)
for and on behalf of Deloitte LLP
Chartered Accountants and Statutory Auditor
London, United Kingdom
15 May 2013

Company balance sheet

As at 31 March

	Notes	2013 £m	2012 £m
Fixed assets			
Fixed asset investments	4	**1,082**	1,004
		1,082	1,004
Current assets			
Debtors: amounts due within one year	5	**303**	505
		303	505
Total assets		**1,385**	1,509
Current liabilities			
Creditors: amounts due within one year	6	**(81)**	(128)
Loans	7	**(25)**	(25)
		(106)	(153)
Non-current liabilities			
Loans	7	**(375)**	(410)
		(375)	(410)
Total liabilities		**(481)**	(563)
Net assets		**904**	946
Equity			
Share capital	8, 9	**1**	1
Share premium	9	**618**	586
Retained earnings and other reserves	9	**285**	359
Equity shareholders' funds		**904**	946

The accompanying notes are an integral part of this Company balance sheet.

These financial statements were approved by the Board of Directors on 15 May 2013. They were signed on its behalf by:

D Harding
Chief Executive Officer
15 May 2013

A Stirling
Chief Financial Officer
15 May 2013

Company number: 07105891

Company reconciliation of movement in shareholders' funds

For the year ended 31 March

	2013 £m	2012 £m
Profit for the period (note 2)	**12**	34
Equity dividends (note 3)	**(87)**	(58)
Retained loss for the year	**(75)**	(24)
Issue of own shares*	**32**	–
Share-based payments reserve credit	**6**	4
Share-based payments reserve debit*	**(3)**	–
Derivative financial instruments	**(2)**	–
Net movement in shareholders' funds	**(42)**	(20)
Opening shareholders' funds	**946**	966
Closing shareholders' funds	**904**	946

* These amounts arose as a result of settlement of the Group's VES schemes; further detail is set out in note 9.

Notes to the Company financial statements

1. Accounting policies

Basis of preparation

The separate financial statements of the Company are presented as required by the Companies Act 2006. They have been prepared under the historical cost convention and in accordance with applicable United Kingdom Accounting Standards and law.

The financial statements have been prepared on the going concern basis. Details of the considerations undertaken by the Directors in reaching this conclusion are set out on page 11 within the Chief Financial Officer's Statement.

Accounting policies

The Company's principal accounting policies, which relate to the financial statements as a whole, are set out below. Where an accounting policy is specific to one note, the policy is described in the note to which it relates.

Financial liabilities and equity instruments

Financial liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into. An equity instrument is any contract that evidences a residual interest in the assets of the Company after deducting all of its liabilities. The accounting policies adopted for specific financial liabilities and equity instruments are set out below.

Loans and other borrowings

Loans and other borrowings represent committed and uncommitted bank loans, and bank overdrafts.

These are initially measured at fair value (which is equal to cost at inception) and are subsequently measured at amortised cost, using the effective interest rate method, except where they are identified as a hedged item in a fair value hedge. Any difference between the proceeds net of transaction costs and the settlement or redemption of borrowings is recognised over the term of the borrowing.

Bank fees and legal costs associated with the securing of external financing are capitalised and amortised over the term of the relevant facility. All other borrowing costs are recognised in the income statement in the period in which they are incurred.

Equity instruments

Equity instruments issued by the Company are recorded at the proceeds received, net of direct issuance costs.

Share-based payments

The Company issues equity settled share-based payments to certain employees. Share-based payments issued by the Company to its subsidiary undertakings are treated as additions to investments based on the fair value of the grant, spread over the relevant vesting period, with corresponding credit to reserves. Where the Company recharges the cost of share-based payments to its subsidiary undertaking the investment is reduced accordingly.

Further details are provided in note 5 to the consolidated financial statements.

Taxation

Current tax is provided at amounts expected to be paid or recovered using the tax rates and laws that have been enacted or substantively enacted at the balance sheet date.

Deferred tax is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date where transactions or events that result in an obligation to pay more, or a right to pay less tax in the future have occurred at the balance sheet date, with the following exception:

Deferred tax assets are recognised only to the extent that the Directors consider that it is more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted.

Deferred tax is measured on a non-discounted basis with the tax rates that are expected to apply in the periods in which the timing differences reverse, based on tax rates and laws enacted or substantively enacted at the balance sheet date.

The taxation liabilities of certain Group companies are reduced wholly or in part by the surrender of losses by fellow Group companies.

Exemptions

The Company has taken advantage of the exemption under FRS 8 'Related Party Disclosures' not to provide details of related party transactions with other Group companies, as the Company financial statements are presented together with the consolidated financial statements.

The Company has applied the exemption under FRS 29 'Financial Instruments: Disclosures' so as not to disclose details of financial instruments held by the Company. Full disclosure of the Group's financial instruments recognised under FRS 29 (IFRS 7) 'Financial Instruments: Disclosures' and IAS 39 'Financial Instruments: Recognition and Measurement' is provided in notes 1 and 19 to the consolidated financial statements.

2. Profit for the year

As permitted by Section 408 of the Companies Act 2006, the Company has elected not to present its own profit and loss account for the year. The Company reported a profit of £12m for the year ended 31 March 2013 (2012: £34m profit).

The auditor's remuneration for audit and other services is disclosed in the Corporate Governance Report on page 19.

Detailed disclosures of the Directors' remuneration and share-based payments are given in the audited section of the Directors' Remuneration Report on pages 22 to 28 and should be regarded as an integral part of this note.

In the prior year the Directors' remuneration was borne by another Group company and not recharged.

The Company has no employees other than Directors.

3. Dividends

Accounting policy

Dividends receivable from the Company's subsidiaries and joint venture investments are recognised only when they are approved or paid by shareholders.

Final dividend distributions to the Company's shareholders are recognised as a liability in the financial statements in the period in which they are approved by the Company's shareholders. Interim dividends are recognised in the period in which they are paid.

	2013 £m	2012 £m
Final dividend for the year ended 31 March 2011 of 3.9p per ordinary share	**–**	35
Interim dividend for the year ended 31 March 2012 of 2.6p per ordinary share	**–**	23
Final dividend for the year ended 31 March 2012 of 6.4p per ordinary share	**56**	–
Interim dividend for the year ended 31 March 2013 of 3.45p per ordinary share	**31**	–
Total ordinary dividends	**87**	58

The proposed final dividend for the year ended 31 March 2013 is 6.95p per ordinary share on approximately 892 million shares (£62m), which was approved by the Board on 15 May 2013 and has not been included as a liability as at 31 March 2013.

The expected cost of this dividend reflects the fact that the Group ESOT has agreed to waive its rights to receive dividends.

4. Fixed asset investments

Accounting policy

Fixed asset investments in subsidiaries and joint ventures are recorded at cost, being the fair value of consideration, acquisition charges associated with the investment and capital contributions by way of share-based payments, less any provision for impairment.

	2013 £m	2012 £m
Subsidiaries	**1,067**	995
Joint venture	**15**	9
	1,082	1,004

	2013 £m	2012 £m
Opening net book value	**1,004**	996
Additions	**78**	8
Closing net book value	**1,082**	1,004

Joint ventures

The Company holds 14.3% of the ordinary share capital of YouView TV Limited, incorporated in England and Wales, a joint venture with The British Broadcasting Corporation, ITV Broadcasting Limited, British Telecom PLC, Channel Four Television Corporation, Arqiva Limited and Channel 5 Broadcasting Limited. Further details relating to the joint venture are disclosed within note 14 to the consolidated financial statements.

Notes to the Company financial statements continued

4. Fixed asset investments continued

Principal Group investments

The Company's significant investments in subsidiary undertakings are set out within note 13 to the consolidated financial statements.

Additions

The additions in the year comprises:

- £68m relating to the settlement of the VES schemes (note 9);
- £4m relating to share-based payment schemes issued by the Company; and
- £6m relating to the YouView TV Limited.

5. Debtors: amounts due within one year

	2013 £m	2012 £m
Amounts owed by Group undertakings	**299**	496
Other debtors	**4**	9
	303	505

Interest on intercompany funding is calculated at the Bank of England base rate plus 2%; intercompany deposits receive interest at the Bank of England base rate with no margin. Interest is either paid or capitalised monthly as appropriate. Where they exist, currency balances are calculated at similar rates.

Interest is not charged on balances arising between Group companies as a result of intercompany trading; such balances are settled regularly in line with agreed terms of trade within 30 to 60 days.

6. Creditors: amounts due within one year

	2013 £m	2012 £m
Amounts owed to Group undertakings	**78**	127
Other creditors	**3**	1
	81	128

Interest on intercompany funding is calculated at the Bank of England base rate plus 2%; intercompany deposits receive interest at the Bank of England base rate with no margin. Interest is either paid or capitalised monthly as appropriate. Where they exist, currency balances are calculated at similar rates.

Interest is not charged on balances arising between Group companies as a result of intercompany trading; such balances are settled regularly in line with agreed terms of trade within 30 to 60 days.

7. Loans

	2013 £m	2012 £m
Current		
Loans	**25**	25
Non-current		
Loans	**375**	410
	400	435

The details of the loans are disclosed within note 18 to the consolidated financial statements and should be regarded as an integral part of these financial statements.

8. Share capital

	2013 million	2012 million	**2013 £m**	2012 £m
Allotted, called-up and fully paid				
Ordinary shares of 0.1p each	**931**	914	**1**	1

On 21 September 2012 the Company issued a further 17,135,825 ordinary shares of 0.1p each to settle the VES schemes (note 9).

9. Reserves

	Share capital £m	Share premium £m	Profit and loss and other reserves £m	Total £m
At 1 April 2012	**1**	**586**	**359**	**946**
Profit for the period	**–**	**–**	**12**	**12**
Issue of own shares*	**–**	**32**	**–**	**32**
Share-based payment credit	**–**	**–**	**6**	**6**
Share-based payment debit*	**–**	**–**	**(3)**	**(3)**
Derivative financial instruments	**–**	**–**	**(2)**	**(2)**
Equity dividends	**–**	**–**	**(87)**	**(87)**
At 31 March 2013	**1**	**618**	**285**	**904**

	Share capital £m	Share premium £m	Profit and loss and other reserves £m	Total £m
At 1 April 2011	1	586	379	966
Profit for the period	–	–	34	34
Net cost of share-based payments	–	–	4	4
Equity dividends	–	–	(58)	(58)
At 31 March 2012	1	586	359	946

* On 17 September 2012, the Group's Remuneration Committee determined that the relevant performance conditions of the VES schemes (including the 5% TSR requirement) had been satisfied, meaning the VES participants were entitled to exercise 60% of their options as set out in note 5 to the consolidated financial statements. The settlement of the scheme resulted in a net increase of £68m in investments (note 4), the recognition of share premium of £32m and a decrease in the net cost of share-based payments previously recognised in reserves of £3m.

10. Audit exemption

The Company's subsidiaries are entitled to an exemption from audit for its subsidiaries under Section 479A of the Companies Act 2006 for the year ending 31 March 2013.

The Directors have applied this exemption for the following subsidiaries:

Company name	Company number
Onetel Telecommunications Limited	04226697
TalkTalk Direct Limited	05303195
TalkTalk UK Communication Services Limited	05714293
Opal Business Solutions Limited	05990928
Opal Connect Limited	05727462
UK Telco (GB) Limited	04341230
V Networks Limited	05475260

The Directors acknowledge their responsibility for complying with the requirements of the Companies Act 2006 with respect to accounting records and the preparation of accounts.

Five year record (unaudited)

	2013 £m	2012 £m	2011 £m	2010 £m	2009 £m
Headline results					
Revenue	**1,670**	1,687	1,765	1,686	1,385
Net profit for the year	**132**	159	122	106	95
Net assets employed					
Non-current assets	**1,046**	1,102	1,137	1,204	1,319
Net current liabilities before provisions	**(216)**	(230)	(281)	(275)	(184)
Provisions	**(13)**	(18)	(46)	(47)	(8)
Non-current liabilities	**(375)**	(410)	(395)	(490)	(425)
Net assets employed	**442**	444	415	392	702
Underlying earnings per share					
Basic	**20.6**	17.2	13.5	11.8	10.7
Diluted	**19.4**	16.4	12.8	11.2	10.4
Headline earnings per share					
Basic	**14.9**	18.0	13.5	11.8	10.7
Diluted	**14.0**	17.2	12.8	11.2	10.4
Statutory earnings per share					
Basic	**11.3**	15.6	3.9	(0.3)	(4.1)
Diluted	**10.6**	14.9	3.7	(0.3)	(4.1)

Underlying earnings for the year ended 31 March 2013 is defined as Headline earnings excluding costs relating to investment in TV less an allocation of taxation based on the Group's Headline effective tax rate. Underlying earnings for the year ended 31 March 2012 is defined as Headline earnings excluding the profit on sale at a freehold property less an allocation of taxation based on the Group's Headline effective tax rate.

There was no difference between Underlying and Headline earnings for the years ended 31 March 2011, 31 March 2010 and 31 March 2009.

Headline earnings represents the Group's income statement stated before the amortisation of acquisition intangibles and exceptional items.

On 26 March 2010 CPW demerged into Carphone Warehouse Group PLC and the Group. The Company and Carphone Warehouse Group PLC were separately listed on the London Stock Exchange.

The consolidated financial information of the Group for the years ended 31 March 2010 and 31 March 2009 have been prepared with the objective of presenting the results, net assets and cash flows of the Group in the form that arose on completion of the demerger, as if it had been a standalone business during those periods.

Glossary

ADSL	Asymmetric Digital Subscriber Line technology enables data transmission over existing copper wiring at data rates several hundred times faster than analogue modems, providing for simultaneous delivery of voice, video and data
ARPU	Average Revenue Per User on a monthly basis
CAGR	Compound Annual Growth Rate
CGU	Cash generating unit
Churn	A measure of the number of subscribers moving into or out of a product or service over a specific period of time
The Company	TalkTalk Telecom Group PLC
Companies Act	Companies Act 2006
CPW	The Carphone Warehouse Group PLC, its subsidiary companies, joint ventures and investments
CRM	Customer Relationship Management
Demerger	The demerger of the The Carphone Warehouse Group PLC into TalkTalk Telecom Group PLC and Carphone Warehouse Group PLC effective on 26 March 2010
EBIT	Earnings Before Interest and Taxation
EBITDA	Earnings Before Interest, Taxation, Depreciation and Amortisation
EFM	Ethernet in the First Mile
EPS	Earnings Per Share
Ethernet	Ethernet is a protocol that controls data transmission over a communications network often referred to as a family of frame-based computers
FRC	Financial Reporting Council
Gb	Gigabits per second
GPS	Global Positioning System
The Group	The Company, its subsidiaries and entities which are joint ventures
Group ESOT	TalkTalk Telecoms Holdings Employee Share Option Trust
Headline information	Headline information represents the Group's income statement, stated before the amortisation of acquisition intangibles and exceptional items that are considered to be one-off, non-recurring in nature and so material that the Directors believe that they require separate disclosure to avoid distortion of underlying performance and should be separately presented on the face of the income statement
HD	High Definition
IP	Internet Protocol is the packet data protocol used for routing and carriage of messages across the internet and similar networks. IP performs the addressing function and contains some control information to allow packets to be routed through networks
ISP	Internet Service Provider
LLU	Local Loop Unbundling
Mbit/s/Mbps	Unit of data transfer rate equal to 1,000,000 bits per second
MPF	Metallic Path Facility provides both broadband and telephony services to customers from TalkTalk Group exchange infrastructure
MVNO	Mobile Virtual Network Operator
Narrowband	Telecommunication service that carries voice information in a narrowband of frequencies
Net debt	Borrowings net of cash held on deposit at financial institutions
NGN	Next Generation Network
On-net	The Group's unbundled network
Operating free cash flow	Cash generated from operations before exceptional items, interest, taxation, dividend payments and investments
Operating profit	Profit before finance costs and taxation
Quad play	A customer that takes voice, broadband, TV and MVNO services from the Group

Glossary continued

RCF	Revolving Credit Facility
SMPF or partial unbundling	Shared Metallic Path Facility provides broadband services to customers from TalkTalk Group exchange infrastructure
SME	Small and Medium sized Enterprises
Triple play	A customer that takes voice, broadband and TV services from the Group
UK Corporate Governance Code	UK Corporate Governance Code published by the FRC in May 2011
Unbundling	Process by which BT makes available its local network to third party broadband service providers
VoIP	Voice over Internet Protocol
WAEP	Weighted Average Exercise Price
Wi-Fi	Trademark of the Wi-Fi Alliance often used as a general term for wireless networking technology that uses radio waves to provide wireless high-speed internet and network connections

Financial calendar

AGM	24 July 2013
Ex-dividend date	3 July 2013
Record date	5 July 2013
Dividend payment date	2 August 2013

About this report

This report was printed in the UK by CPI Colour, a Carbon Neutral printing company. The report was printed using vegetable-based inks and produced on one site, avoiding the need for transportation between processes.

The material used in this report is Amadeus 100 Offset, which comprises 100% post-consumer waste. The paper mill and printer are certified to the environmental standard, ISO 14001. Both are also Forest Stewardship Council (FSC) chain-of-custody certified.

TalkTalk Telecom Group PLC

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