Annual Report
2012

TalkTalk Group

TalkTalk Telecom Group PLC

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We are one of the leading fixed line voice and broadband telecoms businesses in the UK. We provide services to homes and businesses throughout the UK using our state-of-the-art backhaul network.

For more information visit:
www.talktalkgroup.com

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Chairman's statement

TalkTalk's second year as a stand alone company has once again been one of intense activity that has delivered an excellent financial performance with strong progress in the Group's profitability driving Headline earnings per share growth of 33% and dividend per share growth of 61%.

Following the completion of the complex integration of Tiscali in FY2011 TalkTalk made significant progress in FY2012 in simplifying the business and reducing costs to become more efficient. This has helped the Group's profitability and created a strong platform from which to invest in future growth opportunities. Equally importantly, simplifying how we operate and making our processes more efficient has given our customers an even better experience.

TalkTalk Business has seen a year of good progress against the backdrop of an ongoing decline in legacy voice revenues and substantial increase in orders for our Ethernet data services.

At the heart of TalkTalk is our commitment to be the UK's best value for money provider of broadband, voice and television services. Broadband is now an essential service, and we will be absolutely true to our heritage of giving customers consistently the best value for money products in the market.

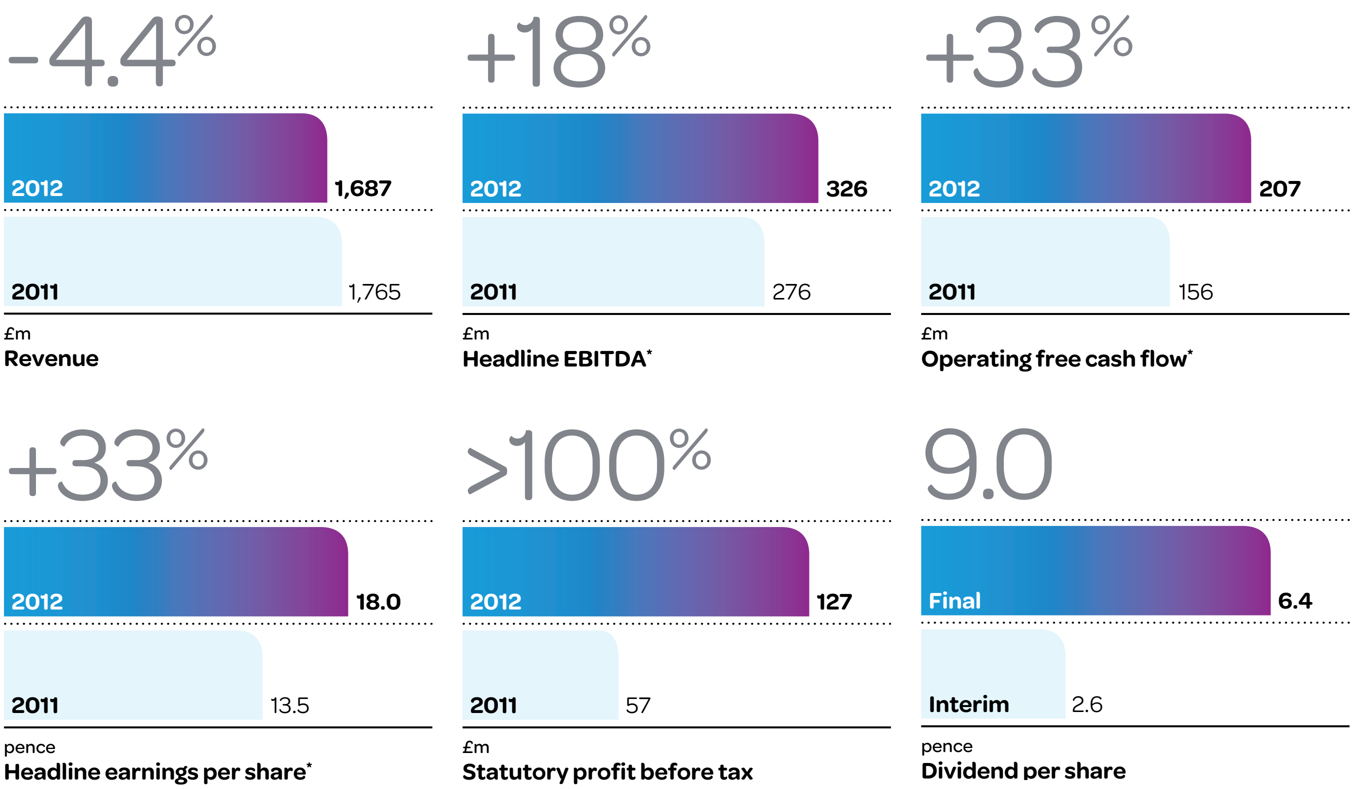
This includes being competitively priced in fibre, which we now offer our customers at up to speeds of 80Mbps. Later this year we will be transforming our customers' television viewing experience with the launch of YouView from TalkTalk, allowing them to access value for money TV packages that are just not available in the market now.

At the end of FY2011, we put in place a policy to distribute 50% of our Headline earnings per share every year in the form of regular dividends. I am pleased to report therefore that for FY2012 the Board has declared a final dividend of 6.4p that, in addition to our interim dividend of 2.6p, gives a total payout for the year of 9.0p.

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 continuing commitment to TalkTalk and our customers.

Charles Dunstone
Chairman
16 May 2012

Financial highlights



* We use adjusted measures where measures are not defined under IFRS or IFRS numbers have been adjusted. For details see page 75.

What we do

We are the UK's leading value for money provider of fixed line broadband and voice telephony services to residential and business customers.

Over the past six years, we have built one of the UK's largest broadband and voice customer bases, attracting customers looking for significant bill savings. More recently, we have started to extend into mobile services, and in FY2012, we plan to launch great value television services.

Our network gives us a strong value for money advantage

We are able to offer our customers voice and broadband services at significantly lower cost than our cable and incumbent competitors. This is because we operate the UK's most extensive Next Generation Network, which has our own advanced, highly cost effective equipment.

Our NGN now covers 91% of UK homes, operating in 2,508 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.

This investment enables us to take control of the telephone line from the exchange to the customer's premises, and to manage all of the voice and broadband services. This process is known as 'local loop unbundling', and 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 groundbreaking HomeSafe™ technology, which protects children from seeing inappropriate content online, is built into this network.

Services to Consumers

TalkTalk is strongly positioned as the leading value for money broadband and voice provider for UK homes. We are differentiated by our clear and simple tariff structure, low prices, and groundbreaking safety features.

We are delivering a steady stream of innovations to augment our broadband and voice offering to customers, with the aim of increasing our customers' savings, their loyalty to TalkTalk, and our revenue potential.

In the beginning of 2011 we launched HomeSafe™, a network based security service that, when activated, protects all the devices in the home from viruses and inappropriate content. We believe online safety is a right, and we therefore offer this service free of charge. We have seen strong engagement among our customers, who appreciate our commitment to family online safety.

We have also seen strong performance in our value for money SIM mobile offering, which launched at the end of 2011. We plan to extend our mobile range with a launch into handsets in the Summer of 2012. Again, our handsets will be clearly positioned as offering strong value for money, with low prices and a commitment to bill control.

We also launched superfast broadband in 2012, and have seen steady uptake among specific customer groups who require faster speeds.

We are partnering with the BBC, ITV, BT and several other companies to launch YouView in FY2013. YouView is a broadband based television service with differentiated catch-up and on-demand services, and an open platform for future application driven innovations. We believe customers will have strong demand for value for money services in the television sector.

Market overview

At the end of December 2011 there were 20.7 million household broadband connections in the UK, 6.2% more than at the same time the previous year. It is estimated that more than 70% of UK households now have a fixed line broadband connection.

There are four key players in the broadband market. BT Retail is the largest broadband service provider, with Virgin Media, the cable provider, the second largest player. BSkyB is the fourth largest player behind 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 deep discounts to customers who take all three products with them.

Within this context, TalkTalk is clearly positioned as the leading provider for customers seeking a best value, reliable voice and broadband. We believe this reputation for value for money will improve further as we are able to offer more television and mobile services.

For more information visit:
www.talktalkgroup.com

46.3%

TalkTalk share of UK unbundled network

million
On-net base

92%

TalkTalk unbundled customer percentage

%
On-net customers

UK telecoms regulation

The UK telecoms market is regulated by Ofcom, which sets the charges for wholesale access to infrastructure and associated services owned by BT Openreach, where BT 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.

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:

LLU Charges

On 7 March 2012, Ofcom made its statement regarding the level of BT Openreach ('Openreach') charges for LLU for the period until 31 March 2014, which covers MPF charges, SMPF charges 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. Pursuant to this decision, MPF rental prices reduced to £87.41 on 1 April 2012 (from £91.50 previously) and will reduce again by RPI – 5.9% on 1 April 2013. TalkTalk has appealed the statement since it believes that the prices are still set too high. BT also appealed the decision. The outcome of these appeals are likely in early 2013.

Next Generation Access

Openreach's NGA infrastructure, currently mainly comprising its FTTC network is now being rolled out. Openreach is required to offer a wholesale NGA product on equivalent terms and conditions for all communications providers. The current wholesale product is GEA, which TalkTalk is using to provide customers with its Fibre Optic Boost product. At present GEA is not subject to formal price controls. The development of GEA is the subject of discussions between TalkTalk, other service providers, Openreach and Ofcom, aiming to improve the customer experience and to make its economics more attractive for providers and customers. The future regulation of GEA will be reconsidered in the upcoming Wholesale Local Access Market Review (which will be effective from April 2014).

Treatment of BT's pension deficit

BT's wholesale charges currently do not include any contribution to BT's pension deficit repair payments. In 2009 and 2010, Ofcom consulted on whether, as demanded by BT, these costs should be included. Ofcom concluded that deficit repair payments should continue to be excluded. BT appealed Ofcom's approach. BT's appeal also challenged two aspects of the way cost of capital was calculated. We expect the final determination of the Competition Commission in June 2012.

Other regulation and legislation

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

Digital Economy Act

This Act was enacted in 2010 and requires ISPs to send notifications to customers whose connections have been identified as being used for illegal file sharing. The Act also includes reserve powers to require the ISP to disconnect these customers. TalkTalk, along with BT, was given permission for a judicial review of these provisions of the Act. In judgments by the High Court (April 2011) and Court of Appeal (March 2012) the majority of the challenge was rejected though the amount ISPs needed to contribute to the costs of the scheme was reduced. Further secondary legislation and regulation is required and the Government now projects that letters will be sent out in early 2014.

The Act had provisions that could require ISPs to block certain websites that promote illegal file sharing. The Government has decided not to pursue these. However, the MPA has been granted a court order (under the Copyright Act) requiring TalkTalk to block access to the Newzbin website and the BPI has been granted the same in respect of The Pirate Bay website.

Net Neutrality

A number of parties have lobbied vocally at national and EU level for the introduction of rules to prevent certain forms of data traffic management by ISPs. However, the EU, UK Government and Ofcom all appear to be committed currently to allow market transparency and competition to protect consumers' interests, rather than prescriptive regulation. In order to ensure that the market works effectively, TalkTalk has committed to a code of practice regarding traffic management transparency and we are developing a code regarding 'open internet' principles.

Government consultation on parental controls

In June 2011 the Government published the Bailey Review into the commercialisation and sexualisation of children. One of the key recommendations was that parents should be offered an 'active choice' by ISPs about whether or not they wanted to use parental controls.

In March, TalkTalk became the first, and so far only, ISP to implement the Government's policy of offering new customers a 'yes' or 'no' decision about whether they wanted to turn on the parental controls element of HomeSafe™, the UK's only network level security system. TalkTalk also announced its commitment to roll out 'active choice' to existing customers with trials beginning later in the year.

Alongside the Bailey Review, an independent Parliamentary Inquiry was convened to examine Online Child Protection, chaired by Claire Perry, MP. The review, published in April, praised TalkTalk's HomeSafe™ for its ability to protect all devices using the home broadband connection and called for other ISPs to introduce similar systems. The Inquiry also concluded that 'default blocking' of pornography, where customers have to 'opt in' to view this content, was preferred.

On 4 May 2012, the Prime Minister announced that the Government would hold a formal consultation into whether pornography should be blocked by default.

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

Business strategy and objectives

Significant opportunity to deliver customer and shareholder value

We see significant opportunities ahead of us to grow both revenues and profitability.

We have a strong, long term position in the UK telecoms industry, underpinned by our value for money positioning, large installed customer base, advanced NGN and cost efficient operating model. We are well placed to take advantage of a number of key industry trends such as the proliferation of connected devices in the home and the growing appetite for on-demand content from both consumers and businesses. These trends are driving demand for reliable and uncontended bandwidth in what increasingly, is becoming an essential service.

Fixed line networks are significantly advantaged over mobile networks in this context, as the incremental costs of bringing additional capacity onstream are much lower. Our network, with its deeply embedded points of connectivity into the UK core, both for consumers and for businesses, is therefore a key competitive asset.

In November 2010, we set out a framework of strategic priorities for delivering medium term revenue and margin growth:

1. Extending our network and its benefits to 700 more exchanges
2. Increasing efficiency by simplifying our operating systems and processes
3. Developing compelling new value for money services for consumers
4. Using our network to expand our range of advanced data services for businesses
5. Preparing for a fibre future

Network expansion

By the end of FY2013 we will have unbundled 2,700 local exchanges (2012: 2,508), taking our coverage to 91% of UK households. Unbundled exchanges, in which we install our own equipment, are linked to our core national NGN by high capacity, low cost backhaul circuits. This all IP network allows us to manage multiple services efficiently, control service quality, and develop new services rapidly and cost effectively.

Fully unbundled customers on our network are able to access more services from us, save more money, and enjoy a superior user experience. They also deliver the most value for us as a business because they buy more services from us and cost less to serve.

Over the next five years, we plan to increase our network capacity by over 100 times (within our capex run rate of 6% of revenue). Primarily this will take the form of cost efficient backhaul scaling against a sustainable exchange footprint. In addition, we will continue to optimise our network for video content, security and access to cloud services. This network advantage will enable us to grow revenues, by providing additional services to our consumer and business customers.

Increasing efficiency

We have targeted £50m of operating efficiencies over the medium term, to be delivered through a programme of improving our end-to-end processes and simplifying our operating systems. Simpler, more efficient processes allow us to deliver better customer service that in turn allows us to reduce customer service costs. As the achievements of the last 18 months have demonstrated, this is one of our key organisational capabilities.

New services for consumers and businesses

We have clear pipelines for growth in our consumer and business customers that will enable us to leverage industry trends, our network assets and our processes.

We are committed to providing an expanding range of clear, value for money services to our customers. Customers who buy more than one service from us save more money, deliver greater value, and stay with us for longer. To date, our customer value journey for consumers has included upselling customers from single play (broadband only) to dual play (broadband and voice), on to our Plus product, an expanding range of paid Boosts and a competitive SIM-only mobile offering.

For consumers, the launch of a TV proposition will be a key element in the implementation of our strategy of building a compelling quad play offer to deliver ARPU growth and lower churn i.e. more valuable customers. Also during 2012, we will launch a series of handsets to extend our mobile offering.

We also have clear revenue and margin growth opportunities in TalkTalk Business. Our network gives us a significant capability to meet efficiently the changing needs of business customers as they migrate from legacy voice services to data-driven traffic. We aim to build upon the success of our Ethernet products to create a best value connectivity business that also provides voice and data hosted applications to deliver value added solutions to our customers.

Superfast broadband

We are confident about our role in fibre, which we see as a profitable and low capital driver of incremental ARPU over time. As the number of devices our customers use to access the internet, and as they increasingly require higher speeds to support their data consumption, so the delivery of our core broadband service needs to evolve. A 'future-proof' network to deliver NGA is therefore at the heart of our broadband strategy.

We aim to offer a simple to understand and competitively priced fibre product to our customers, as BT Openreach rolls out its fibre network. Following the launch of our 40Mbps fibre boost in 2011, we have recently launched an 80Mbps product that an increasing number of customers will be able to access.

A key element of our fibre strategy is to maintain regular and close dialogue with both BT Openreach and the UK regulator (Ofcom), to ensure that consumers continue to enjoy a choice of fairly and competitively priced services. We believe the UK regulator will, in due course, reaffirm its responsibility for maintaining strong retail competition, which will support our fibre strategy.

2013 Financial guidance

We have already delivered on key elements of the medium term strategy we set out 18 months ago. Our operating and financial performance in the last financial year has delivered a materially more profitable and stable customer base and a leaner, more efficient cost structure. As a result we have entered the new financial year in a position of strength, from which to invest in growth opportunities such as YouView, and to deliver further shareholder value.

The majority of our investment in TV will take the form of variable SAC and marketing costs with minimal capital expenditure requirement. The guidance below excludes these costs, further details on which, together with details of our proposition, will be provided in due course.

Revenue

We are confident of achieving our target of a return to positive net adds in the first quarter of FY2013. We expect that this, together with ongoing progress in ARPU from an improving customer mix on our fully unbundled base, will drive a return to revenue growth.

Operating expenses

We expect operating expenses to be broadly flat in FY2013 as customer service improvements and back office simplification cost reductions, enable us to reinvest in increased network footprint and resilience.

EBITDA margin

We expect ARPU growth and stronger margins from improved customer mix to generate an EBITDA margin of 20%-21% in FY2013.

Cash flow items

We do not expect material net exceptional cash expenditure in FY2013, as the costs of contact centre consolidation are expected to be offset by a credit relating to an historical BT dispute. Capex is expected to be in line with our stated policy of 6% of revenue. We expect our tax cash rate to be less than 10%.

Dividend

We are firmly committed to growing our dividend whilst also investing for growth, a commitment that is supported by the increasing profitability of our core business, our cash generation and overall financial strength. Thus, although FY2013 and FY2014 will see us absorb the costs of investing in TV, we expect to grow the dividend by a minimum of 15% in each of these years.

Chief Executive Officer's statement

Our operational focus during the year has been on continuing to implement the five core elements of the strategy we set out in November 2010:

1. Extending our network and its benefits to 700 more exchanges
2. Increasing efficiency by simplifying our operating systems and processes
3. Developing compelling new value for money services for consumers
4. Using our network to expand our range of advanced data services for businesses
5. Preparing for a fibre future

We have made significant progress on each of these elements and as a result have delivered an extremely strong financial performance with Headline EBITDA growing 18% to £326m, operating free cash flow by 33% to £207m and Headline EPS by 33% to 18.0p.

1. Largest unbundled UK network

We unbundled 501 exchanges during the year, taking our total network coverage to 2,508 exchanges and 91% customer coverage, by some distance the largest unbundled estate in the UK. Our plans to extend our unbundled footprint further, to around 2,700 exchanges will take us to over 93% customer coverage by the end of FY2013. More than 200 further exchanges are currently scheduled to come on stream before the end of FY2013.

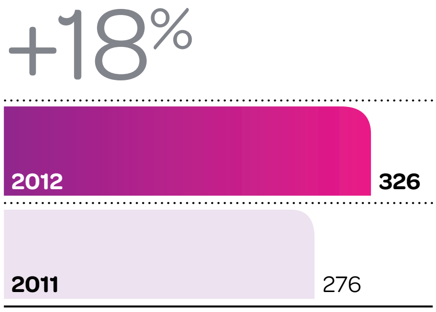
We ended the year with 3.755 million customers on our network, accounting for 92% of our total broadband customer base, compared to 86% at the end of last year. Of these 3.066 million were fully unbundled customers, taking both phone and broadband services delivered through our MPF equipment. The remaining 689k customers were partially unbundled, taking only broadband, served through our SMPF equipment. Unbundling and the resulting customer mix improvement was a key driver of our ARPU growth during the year, to £25.6 in Q4 from £25.0 at the same time last year.

Unbundling delivers major benefits for our customers, such as better prices, optimised broadband speed and service quality, and access to our growing range of additional products and services, such as Plus, HomeSafe™ and Boosts. Investment in unbundling delivers significant financial benefits, including higher ARPU and lower churn across the base, access to inbound call termination revenue, lower regulated charges (MPF and SMPF), and lower backhaul costs due to our investment in a highly efficient, high capacity NGN.

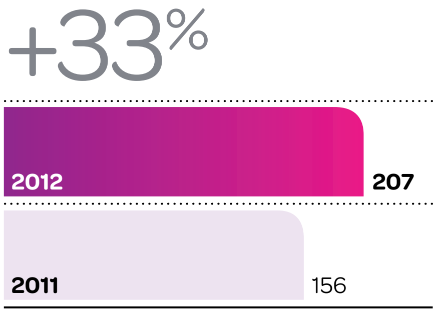
2. Operating efficiencies

In November 2010 we announced our target to deliver a total of £40-50m of operating efficiencies over the medium term, by providing a better customer experience through simplifying our business processes, eliminating significant duplication, and creating a leaner operational structure. We have aimed, through these initiatives, to improve significantly the quality of the end-to-end experience we deliver to our customers and therefore to also reduce our overall customer service costs.

We have delivered significant improvements in our customer experience over the last 12 months with a 31% year on year reduction in calls into our contact centres, a 36% reduction in complaints to Ofcom and 76% of our customers now benefiting from first time resolution of their query.



£m
Headline EBITDA



£m
Operating free cash flow

Better diagnostic processes and tools and greater network stability, following completion of our customer migration programme, were reflected in a substantial reduction in technical support calls during the period. Improved self-serve capabilities and higher first time query resolution resulted in lower volumes of general service calls, including billing queries.

More than 70% of our total customer contacts are now online, compared to around 65% last year. This improves both customer experience and future profitability.

We have now identified the full £50m of the £40-50m targeted range of efficiencies ahead of plan. A total saving of £23m was delivered during FY2012. We expect a further £22m to be realised in FY2013 and further £5-10m in the following year.

3. Value for money quad play

Our firm commitment to consistently provide clear, value for money services for our customers was reflected in a series of new prices and products, to maintain our positioning as the best value provider in the market. These initiatives included the repricing of our line rental offer, the reduction of headline pricing of our Essentials and Plus broadband packages and the launch of both our unique HomeSafe™ service and a 500 Mobile Minute Boost.

By the end of FY2012, 1 million customers have joined or been upsold to Plus, our inclusive calls product, reflecting its unbeatable value and appeal to customers in these challenging economic times. Plus customers now comprise c.25% of our total customer base. A further 250,000 customers are now also benefiting from a capped cost of calling mobiles through our innovative 200 and 500 Mobile Minute Boosts.

HomeSafe™, our network level security and safety service that protects all devices using the internet connection in the home, is unique to TalkTalk. HomeSafe™ gives customers the ability to block inappropriate content as well as protect devices from viruses and appeals strongly to parents in particular. HomeSafe™ is an excellent example of our ability to bring innovative new services to our customers that also create value for us. While the service is provided at no charge, the cost of provision is far outweighed by the benefit to us in the form of materially reduced churn.

Our triple play proposition that will feature YouView, is on track for launch during Q2 of FY2013. YouView will bring to our customers all of the 'plug-in-and-watch' simplicity of Freeview, plus the UK's leading internet catch-up and video on-demand services, all instantly available through one simple, intuitive set-top box and proprietary electronic programme guide.

Development within the YouView team is progressing well and within TalkTalk we are making great progress on provisioning capability, as well as operational and CRM readiness to support our TV service within our existing operational structures. We began 'Friends and Family' trials focusing on the end-to-end customer experience in April 2012 and will be extending the trial to our customers soon.

Our mobile base continues to grow with over 70,000 customers now taking mobile in addition to their phone and broadband service. We have built an impressive 7.5% share of the UK SIM-only market since launch and as expected, have seen significantly lower churn on this customer base. We plan to launch a handset proposition later this year in addition to our existing SIM-only and data products.

4. TalkTalk Business services

TalkTalk Business generates approximately 20% of the revenue of the Group and comprises three main areas; business data services, voice services and carrier services through a direct team and channel community.

Taking full advantage of the UK's most extensive NGN, the re-branded TalkTalk Business is a leading player in developing and delivering converged voice and data services across four distinct markets, small and medium sized enterprises (SME), larger corporates, system integrators and direct to other carriers.

Our network coupled with hosted services provides the flexibility, reliability, capacity and geographic coverage required to meet our customers' growing demand for high quality data services. Our product range extends from simple business broadband propositions for sole traders and home workers, through to complex, integrated connectivity solutions for larger organisations delivered direct or through our vibrant partner community.

After the introduction in FY2011 of our fibre-based Ethernet connectivity service aimed at large carriers and systems integrators we have expanded our offerings with a launch in April 2011 of our EFM solution into our partner channel. This product captures the advantages of both Ethernet technology and the underlying copper-based broadband service, delivering guaranteed symmetrical connectivity up to 10Mbps across bonded copper pairs. EFM bridges the gap between ADSL and fibre-based Ethernet, and presents a major growth opportunity as a compelling low cost, business grade alternative. Across our Ethernet offerings in the second half we have seen substantial increase in orders as we scale for growth.

As anticipated, and in line with wider secor trends, voice revenues in the B2B business continued to be under pressure driven by the impact of mobile termination rates and declining fixed line voice minutes through the year. Carrier service operations, which leverage our interconnected voice network and scale of customer base, traded broadly in line with last year.

At the beginning of the year we acquired Executel, a regional unified communications solutions business with a strong presence in North East England. Executel was a long-standing TalkTalk Business channel partner, and the acquisition strengthened our capabilities in the all important PBX systems market.

5. Fibre access

Early in FY2012 we launched our first NGA product, a fibre optic Boost that delivers download speeds of 15-40Mbps for our customers who are located within the BT Openreach fibre network footprint. Priced at £10 per month, plus a one off connection fee, this product delivers a value for money, high-speed broadband service. Demand for superfast broadband amongst our customer base remains modest as our current copper-based ADSL technology already delivers average download speeds of 7-8Mbps, which satisfies most customers' present requirements.

We saw accelerating demand for our 40Mbps fibre boost during Q4, with an additional 4,000 customers being provisioned, to leave a closing base of 9,000. We expect demand for NGA to grow over the medium term and we have spent much of the last year on laying the groundwork both commercially and operationally, to be able to take advantage of customers' growing demand for faster speeds when they need it.

Accordingly, after reaching agreement on commercial terms with BT Openreach, we launched an 80Mbps (20Mbps upload) product in April 2012. Priced at £15 per month, plus a one off connection fee, this product also delivers a value for money service that allows our customers to save money versus comparable products in the market.

We are continuing to work with BT Openreach to develop the NGA product further, and in particular to improve the customer connection experience and reduce both the initial set-up and ongoing provisioning costs. Currently all new fibre connections necessitate a visit by a BT Openreach engineer and supply of separate new access and inter-connection equipment within the home. Trials on a simpler installation process are underway and we continue to believe that the experience must become more flexible, and its end-to-end costs reduced, before NGA products will gain mass-market customer acceptance.

Dido Harding
Chief Executive Officer
16 May 2012

Business review

Overview

In our second year we have delivered another strong performance, continuing to generate material growth in profitability (Headline EBIT up 21%) and cash generation (Operating free cash flow up 33%). We have also achieved our medium term objective of 20% Headline EBITDA margin in the second half of the year, significantly ahead of schedule. Our focus this year has been twofold; to continue to increase the size of our on-net base and to drive further improvements through our Operating Efficiencies programmes.

By the end of the year, 92% of our customer base were on our own network, up from 86% the year before. Not only do we provide these customers with better value, but they also take more services from us, resulting in broadband ARPU growing from £25.0 in Q4 FY2011 to £25.6 in Q4 FY2012.

We have now actioned our target operating annualised cost savings of £40-£50m. Of these annualised savings, £40m, have been successfully delivered during this year, and are captured in our EBITDA exit run rate, and we anticipate that the remainder will be implemented during the first half of the FY2013 financial year. The savings have been delivered through a simplification of our back office functions and through rationalising our in-house contact centres and outsource partners.

All figures presented within the Business review are presented on a Headline basis as this is the way in which management reviews the business. Our Statutory results are presented in the Finance review.

Customer base and ARPU

	2012	2011	Growth (decline)
On-net base (k)	**3,755**	3,607	148
Of which:			
MPF base (k)	**3,066**	2,751	315
SMPF base (k)	**689**	856	(167)
Off-net base (k)	**311**	592	(281)
Total broadband (k)	**4,066**	4,199	(133)
Non-broadband (k)	**476**	678	(202)
ARPU	**Q4 2012**	Q4 2011	
Broadband	**£25.6**	£25.0	2.4%
Non-broadband	**£19.4**	£17.7	9.6%

Broadband customer base and ARPU

We continued to grow our on-net customer base this year, increasing by 4% year on year to 3.755 million, representing 92% of our broadband customers.

During the year we have expanded our exchange footprint by a further 501 exchanges as our exchange unbundling programme continued, representing material progress towards our medium term goal of unbundling 2,700 exchanges. Unbundling exchanges brings our network closer to the customer's home or office, allowing us to offer more competitively priced products to attract new customers and provide better value to existing customers as well as the opportunity to migrate existing IP stream customers onto our own network. As a result, we have continued to grow the proportion of our broadband base on our own network.

The proportion of customers taking voice, broadband and line rental from us also grew, increasing to 75% at the end of the year, from 66% at the start of the year. These customers have a higher monthly spend, are more valuable and have a lower propensity to churn.

We continued to acquire new broadband and voice customers under the TalkTalk brand during the year. Our higher value Plus product represents 30% of new acquisitions and almost a quarter of our total broadband base at the end of the year, up from 14% in the previous year. Improving customer mix has been one of the key drivers in growing our ARPU from £25.0 in Q4 FY2011 to £25.6 in Q4 FY2012.

As expected, our off-net base has reduced as we migrate more of our customers on-net and focus on delivering value for money products to this base.

Non-broadband customer base and ARPU

Our non-broadband base declined in the year to 476k at the year end from 678k at the start of the year, as the trend towards customers taking bundled packages with broadband services continues. Non-broadband ARPU improved from £17.7 at the start of the year to £19.4 at the year end due to the mix of customers and price changes for voice and line rental products.

Headline financial information

£m	2012	2011	Growth (decline)
Broadband	**1,242**	1,247	(0.4)%
Non-broadband	**129**	189	(31.7)%
Corporate	**316**	329	(4.0)%
Total revenue	**1,687**	1,765	(4.4)%
Headline EBITDA	**326**	276	18.1%
Sale of freehold site	**9**	–	
Underlying EBITDA	**317**	276	14.9%
EBITDA margin	**19.3%**	15.6%	
Underlying EBITDA margin	**18.8%**	15.6%	
Depreciation and amortisation*	**(93)**	(84)	
EBIT	**233**	192	21.4%

* Includes share of results of joint venture.

Revenue

Our revenue is principally derived from the provision of voice and broadband and data services to UK consumers and businesses. A customer is treated as a broadband customer when they receive a broadband service. If a customer takes another service such as voice, or a mobile SIM, this revenue is also included in the broadband line. A customer is classified as non-broadband where they do not take broadband and receive voice only or narrowband services. Our revenue is a function of the mix of services received by the customer, their usage and the size of the relevant base. ARPU is an indicator of the average value of the services we supply to each customer.

Corporate revenue represents revenue generated by TalkTalk Business in the provision of voice and data services to corporate customers and resellers.

Revenue decreased by 4.4% to £1,687m (2011: £1,765m), principally driven by the continued reduction in the size of the non-broadband customer base.

Broadband revenue was broadly flat year on year at £1,242m (2011: £1,247m) reflecting the increasing ARPU throughout the year offsetting the reduction in the total base in the second and third quarters of the year.

In line with the reduction in the base size, revenue from non-broadband customers reduced to £129m (2011: £189m).

Revenue from our Corporate services decreased 4% to £316m (2011: £329m), as the decline in both traditional voice minutes services and mobile termination rates continued throughout, partially offset by the Executel and Greystone acquisitions during the year and growth in new data services products such as Ethernet.

Headline profit

Our Headline EBITDA continued to grow, increasing by 18.1% to £326m (2011: £276m) and EBITDA margin improved to 19.3% (2011: 15.6%). Our current year EBITDA includes the profit made on the disposal of a freehold site in Birmingham during the year of £9m. Excluding this profit, the underlying EBITDA margin was 18.8%. The increase in underlying EBITDA reflects the ongoing benefit of the Operating Efficiencies programmes undertaken during the current and prior year, and the increased on-net and Plus penetration of our broadband base.

Over the year we focused on our operating model to drive further efficiencies in our business. We have delivered benefits of £38m during the year, of which £18m related to our back office simplification announced in January 2011, £5m to our contact centres rationalisation programme announced in September 2011, and £15m related to the full year benefit of the One Company Integration.

Headline EBIT increased by 21.4% to £233m (2011: £192m) resulting from the growth in EBITDA and this takes into account an increase in depreciation and amortisation resulting from continued investment in our network build programme and our billing systems.

Operating free cash flow and net debt

£m	2012	2011	Growth
Headline EBITDA	**326**	276	18.1%
Working capital	**(14)**	(10)	
Capex	**(105)**	(110)	
Operating free cash flow	**207**	156	32.7%
Net debt	**(434)**	(438)	

In our second year we have delivered another significant increase in cash generation, growing our operating free cash flow 32.7% to £207m (2011: £156m). This has been driven by the growth in Headline EBITDA alongside control over investment in capital expenditure in line with our guidance to focus on delivering our unbundling strategy and unified billing system. Net debt has remained broadly flat at £434m (2011: £438m), as the increase in our cash generation has funded both an enhanced dividend payout to shareholders of £58m (2011: £15m) and the purchase of £54m (2011: £nil) of shares by our Group ESOT to satisfy future anticipated share option exercises.

Finance review

Reconciliation of Headline to Statutory information Income statement

£m	2012	2011	Growth (decline)
Revenue	**1,687**	1,765	(4.4)%
Gross margin	**884**	888	(0.5)%
Operating expenses excluding amortisation and depreciation	**(558)**	(612)	
Headline EBITDA	**326**	276	18.1%
Exceptional items – One Company[2]	**–**	(36)	
Exceptional items – Operating Efficiencies[2]	**(27)**	(12)	
EBITDA	**299**	228	31.1%
Depreciation and amortisation			
Operating[1]	**(93)**	(84)	
Exceptional[2]	**–**	(7)	
Non-operating amortisation[2]	**(61)**	(62)	
Operating profit	**145**	75	93.3%
Finance costs	**(18)**	(18)	
Profit before tax	**127**	57	>100%
Tax	**11**	(22)	
Profit after tax	**138**	35	>100%

(1) Includes share of results of joint venture.
(2) Excluded from Headline results.

Revenue
Revenue decreased by 4.4% to £1,687m (2011: £1,765m). As discussed in the Business review, this was principally driven by the continued reduction in the non-broadband customer base.

Gross margin
We have delivered an improvement in our gross margin percentage to 52.4% (2011: 50.3%) in the year as a result of the increasing percentage of customers who are unbundled. As a result, gross margin for the year has remained flat at £884m (2011: £888m).

Operating expenses
Operating expenses in the year reduced by £54m from £612m in the prior year to £558m. This reflects the full year benefits of the One Company Integration programme, the cost savings generated by our Operating Efficiencies programme, and the profit realised on the sale of a freehold site in Birmingham during the year partially offset by the investment in our network.

Exceptional items
Investment in our Operating Efficiencies programme was £25m for the year, principally in relation to redundancy and site exit costs. We undertook this reorganisation in two phases; phase one focused on restructuring back office functions to deliver annualised benefits of approximately £25m at a cost of £11m (2011: £12m). The second phase, announced in September 2011, rationalised our customer services footprint, resulting in the closure of our Waterford contact centre, to deliver a further £15m of annualised savings at a cost of £14m. Operating cost savings of £23m have been realised in the current year as a result of these reorganisation programmes. A credit of £1m was recognised in respect of the One Company Integration programme for a provision no longer required.

In addition, we received a fine from Ofcom in the year of £3m relating to billing issues that arose as a result of the integration of the Tiscali business.

EBITDA
EBITDA after exceptional items has grown by 31.1% to £299m (2011: £228m). Exceptional costs within EBITDA have reduced significantly year on year to £27m (2011: £48m), as the One Company Integration programme was completed. The improvement in EBITDA principally reflects the benefits of the Operating Efficiencies programmes and the full year benefits of the One Company Integration programme.

Amortisation of acquisition intangibles
The amortisation charge in respect of acquisition intangibles was flat year on year at £61m (2011: £62m).

Profit before tax
Statutory profit before tax more than doubled to £127m (2011: £57m), reflecting the significant increase in Headline earnings and the decrease in exceptional costs year on year.

Earnings per share

	2012	2011	Growth
Headline earnings (£m)	**159**	122	30.3%
Basic EPS	**18.0p**	13.5p	33.3%
Diluted EPS	**17.2p**	12.8p	34.4%
Statutory earnings (£m)	**138**	35	>100%
Basic EPS	**15.6p**	3.9p	>100%
Diluted EPS	**14.9p**	3.7p	>100%

In order to provide a meaningful comparison and to remove the impact of exceptional items, EPS is provided on a Headline basis as well as a Statutory basis. A full reconciliation of Headline to Statutory results can be found in note 10 to the financial statements.

We have had another year of strong EPS growth, with Headline EPS increasing 33.3% to 18.0p (2011: 13.5p), and Statutory EPS growth even stronger, growing fourfold to 15.6p (2011: 3.9p), as a result of the growth in profit before tax and the recognition of deferred tax assets in relation to acquired losses.

Basic EPS has been calculated based on a weighted average number of shares of 885 million (2011: 907 million). During August and September our Group ESOT purchased 41.7 million shares to settle anticipated future share option exercises. This has led to a decrease in the weighted average number of shares in issue during the year. Dilution of 40 million shares (2011: 45 million) has been applied for the purposes of calculating diluted EPS resulting from employee share option plans, the details of which can be found in note 5 to the financial statements.

Cash flow and net debt

£m	2012	2011	Growth
Headline EBITDA	**326**	276	18.1%
Working capital	**(14)**	(10)	
Capex	**(105)**	(110)	
Operating free cash flow	**207**	156	32.7%
Exceptional items – Operating Efficiencies	**(35)**	–	
Exceptional items – Ofcom fine	**(3)**	–	
Exceptional items – One Company	**(7)**	(43)	
Exceptional items – demerger	**–**	(16)	
Acquisitions and disposals(1)	**(20)**	7	
Dividends paid	**(58)**	(15)	
Interest and Tax	**(26)**	(19)	
Share purchase	**(54)**	–	
Net cash flow	**4**	70	
Opening net debt(2)	**(438)**	(508)	
Closing net debt(2)	**(434)**	(438)	

(1) In 2011, includes £2m of sundry items.
(2) Including loans to related parties, closing net debt was £432m (2011: £436m).

Capital expenditure

Capital expenditure in the year was £105m (2011: £110m), representing 6.2% of revenue (2011: 6.2%). During the year we expanded our network footprint by unbundling a further 501 exchanges, and completed the migration of consumer customers onto our strategic billing system. We also enhanced our network capacity to efficiently manage increased bandwidth demands of our customers.

Working capital

The working capital outflow of £14m (2011: £10m) reflects our decreasing cost base and the continued unwind of fair value provisions arising on the acquisition of Tiscali.

Exceptional and demerger costs

Exceptional cash spend totalled £45m in the year (2011: £59m) of which £35m was in relation to the Operating Efficiencies reorganisation programme and £7m in relation to the One Company Integration programme, which was completed during 2011. In addition we received a fine from Ofcom in the year of £3m relating to billing issues that arose on the integration of Tiscali.

Acquisitions

The cash outflow in relation to acquisitions was £20m comprising strategic B2B acquisitions of £16m and a payment of £4m in relation to our continued investment in the YouView joint venture.

Dividends

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

Dividends paid in the year of £58m (2011: £15m) comprised the final dividend for FY2011 of 3.9p per share and the interim dividend for FY2012 of 2.6p per share.

The Board has declared a final dividend of 6.4p per share, which will be paid, subject to shareholder approval at the AGM, on 27 July 2012 for shareholders on the register at 6 July 2012. The total declared dividend for the year was 9.0p, which provides dividend cover of 2.0 times.

Net debt

Our net cash inflow was £4m (2011: £70m). Net debt, including loans to related parties, was £432m (2011: £436m). Excluding loans to related parties net debt was £434m (2011: £438m).

Taxation and treasury

	2012		2011	
£m	Headline	Statutory	Headline	Statutory
Operating profit	**233**	**145**	192	75
Finance costs	**(18)**	**(18)**	(18)	(18)
Profit before tax	**215**	**127**	174	57
Tax	**(56)**	**11**	(52)	(22)
Profit after tax	**159**	**138**	122	35
Headline tax rate	**26%**		30%	

Finance costs

Net finance costs charged to the income statement were £18m (2011: £18m). This comprised the blended interest rate charged on debt of 3.17% (2011: 3.07%) and an amortisation charge of £1m in relation to facility fees incurred when we refinanced our debt in November 2011.

Net interest paid in the year increased to £24m (2011: £17m), principally as a result of the fees paid for refinancing during the year.

Finance review
continued

Taxation
The effective Headline tax rate for the year was 26% (2011: 30%) representing a tax charge of £56m (2011: £52m) on Headline profit before tax of £215m (2011: £174m).

The tax credit for the year on statutory earnings was £11m (2011: charge of £22m). The principal differences 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 year in the corporation tax rate from 26% to 24% from April 2012, created a charge through the income statement of £10m resulting from the downward revaluation of deferred tax assets. This has been partially offset by prior year credits of £4m relating to the recognition of additional tax losses and capital allowances.

During the year we 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 has resulted in the recognition of deferred tax assets of £45m in addition to those recognised at the acquisition date. The associated tax credit has been treated as an exceptional item in the income statement.

There have been tax payments in the year of £2m (2011: £2m), which relate to the final corporation tax assessment of our AOL Luxembourg entity prior to its liquidation.

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

During the year we refinanced our £550m revolving credit facility that matured in March 2013. The Group has £520m revolving credit facility, £70m of bilateral facilities used for working capital purposes and a term loan of £100m. The revolving credit facility matures in November 2015, the bilateral facilities in March 2015 and November 2015, and the term loan in March 2015.

The terms of all the facilities are similar and the covenants are identical. We were in compliance with the covenant conditions on all funding facilities at the year end. As at 31 March 2012, £435m (2011: £395m) had been drawn down on these combined facilities. It is our policy to refinance our facilities significantly in advance of maturity dates.

Policy
We are exposed to limited cross border transactional commitments but where significant, these are hedged using forward currency contracts. 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 financial statements, considers that our medium term target gearing is 75% to 100%. Gearing at 31 March 2012 was 98% (2011: 106%).

Accounting developments
The adoption of standards in the year, as disclosed in note 1 to the financial statements, has had no material effect on the 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 6 to 7 and Business review on pages 8 to 9. Our financial position, cash flows and borrowing facilities are described within this Finance review. In addition, note 19 in the financial statements describes how we manage financial risk, including foreign exchange risk, interest rate risk, credit and liquidity risk.

Whilst the current economic climate remains uncertain, the breadth of our customer base, our value for money proposition, improved operating efficiency and the largest unbundled network in the UK together with our development of a competitive quad play offering means that the Directors are confident of our ability to continue to compete effectively in the UK telecoms sector.

We have £690m of committed credit facilities and as at 31 March 2012 the headroom on these facilities was £255m. Our forecasts and projections, taking into account reasonably possible changes in trading performance, indicate that there is sufficient headroom on 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 in preparing the 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 broadband market may impact financial performance.

Mitigation: We regularly monitor the product offerings of key competitors in the market. This results in an ongoing review of the customer proposition and the overall value of our products.

2

Regulatory environment

Potential impact: Changes in regulated prices can significantly impact the Group's performance. In particular, demand for fibre access could grow significantly before a wholesale product with acceptable economics is available for the Group to market to customers.

Mitigation: We actively participate in pricing consultations by Ofcom, including the use of independent experts to provide assistance and evidence as required. The Group is working with Openreach to develop fibre products that incur lower set up and provisioning costs. There is close liaison with Ofcom to ensure there is regulatory support for development of fibre products suitable for mass-market adoption.

3

Regulatory compliance

Potential impact: Failure to operate effective processes across the Group may lead to customer churn, and non-compliance with regulatory requirements. Disruption to business operations and back office functions may impact financial performance and our customers.

Mitigation: The Group's Compliance Committee regularly monitors the level and reason for customer complaints.

4

Network stability and reliability

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

Mitigation: We focus continually on improving network resilience and performance, and continue to invest to ensure we keep pace with customers' growing demands.

5

Change management

Potential impact: We are undertaking a strategic review of our IT structure and systems in the next financial year. Disruption to business operations and back office functions may impact financial performance and our customers.

Mitigation: We have a Group Change Forum comprised of senior managers that is responsible for centrally monitoring Group wide change. Teams are established to run the component projects of the overall change, with clear plans in place for each area. Regular progress reports are provided to ensure key dates are met.

6

Data integrity and security

Potential impact: Failure to accurately capture and securely store customer data could lead to data protection breaches causing damage to our reputation and fines.

Mitigation: The Group continually reviews its data security and implements new solutions as they become available.

7

Television

Potential impact: Provision of television services could become a more important driver of competitive advantage in the broadband market.

Mitigation: The Group is part of the YouView joint venture, along with the BBC and other parties, which is developing a television service that includes internet-based catch-up and video-on-demand services.

8

Key suppliers

Potential impact: Failure of key suppliers could affect the Group's ability to operate its business.

Mitigation: We manage these risks by ensuring we have a strong supplier selection process with appropriate ongoing management and monitoring.

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 better and more sustainable place by motivating our people and suppliers, and by producing innovative products for our customers.

Digital society

We aim to improve society through innovation and motivating our customers, people and partners. We do this through the following programmes:

Digital safety

We think it is important to maintain the freedoms that the internet age brings. However, we realise that parents want to protect their children online, and keep them focused during homework time. We also want to empower all customers to protect all of their internet devices from security risks.

We were first, in 2011, to develop a service that can automatically protect every device on a home broadband connection. We call it HomeSafe™ and we offer it free with our consumer broadband packages. It is built into our network and, once enabled on a connection, 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.

We are the only broadband provider with such a service.

It won the 2012 uSwitch Award for Broadband Innovation, and helped us to win a Mumsnet Family Friendly Silver Award.

We also offer customers an additional layer of protection with security software for up to three PCs, and this is free as part of our TalkTalk Plus package.

Safety and security are specialist areas, so we collaborate with several experts in the field. This includes F-Secure, the UK Council for Child Internet Safety (UKCCIS) and the Mumsnet Family Friendly programme.

Digital inclusion

Most of us have internet access and enjoy the educational, entertainment and savings opportunities that it brings. Yet, over eight million people in the UK have never been online, and so we are committed to helping them overcome their barriers, be they confidence or financial, and harness the power of the internet.

Go ON UK and Race Online 2012

TalkTalk is a founding sponsor of the new charity Go ON UK, alongside Age UK, the BBC and Big Lottery Fund. The charity is led by Martha Lane Fox. Together we pledge to work with the Government to help make the UK the world's most digitally capable nation. We were a partner of its predecessor, Race Online 2012. Aside from lending our online safety and digital inclusion expertise, we have donated office space above our Customer Experience Centre in central London, as well as funding.

A good example of our involvement in FY2012 was our support for the Go ON Liverpool initiative, where we offered local families, who had never been online at home before, a broadband and phone package free for 12 months.

TalkTalk Digital Heroes Awards 2011

We have sponsored these awards, run in conjunction with charity Citizens Online and The Daily Mirror, since 2009. The awards aim to reward amazing individuals, nominated by their communities, who use digital technology in the most socially positive way. This year we had 190 entries, an increase on last year, nominated by the public and their MPs. We awarded £65,000 in grants to 12 regional finalists, including £10,000 to the 2011 TalkTalk Digital Hero.

The judges were our Chairman – Charles Dunstone, the UK Digital Champion – Martha Lane Fox and the Editor of The Daily Mirror – Richard Wallace. They judged the 2011 TalkTalk Digital Hero to be Chris Dredger of the charity, Storybook Dads, a project that helps maintain the vital emotional bond between prisoners and their children by helping offenders to record bedtime stories on CD or DVD. The grant will buy Storybook Dads new video equipment to roll the project out to more prisons, as well as helping their planned project with the Armed Forces. For more on Storybook Dads, visit storybookdads.org.uk.

Environmental sustainability

This year we have stepped up our focus on measuring and reducing our environmental impact: in particular the CO_2 emissions related to our consumption of energy. This is by far our biggest impact.

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

CO_2 emissions

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.

Despite growing the network in line with customer usage and volume, we have increased energy efficiency and therefore our CO_2 emissions intensity has fallen.

tCO_2e/Gb	2012	2011
Energy[(1)], transport[(2)] and lodging	**193**	317

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

As customers' broadband usage grows, we will further invest in expanding our network capacity to meet demand, and energy efficiency initiatives.

We are members of the UK Government's Carbon Reduction Commitment Energy Efficiency Scheme league table. In 2011, the Environment Agency ranked us in the top performance quartile: at position 381, from over 2,000 UK organisations. To achieve this, we attained the Carbon Saver Gold Standard and initiated a programme of fitting digital 'half-hourly' energy meters, linked to our energy management software platform. In addition, we installed sub-metering, to allow us to better monitor energy usage and identify target areas for further improvements.

100% renewable electricity
In November 2011, we switched our procurement of electricity, by far our main energy source, so that 100% of the units consumed by our NGN, offices and UK call centres come from renewable sources.

Sustainable forestry
Another focus in FY2012 was sustainable paper. We began displaying 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. The printed version of this report is our first to be printed on certified 100% recycled paper and we have used a lighter stock and lower ink coverage than previously.

Community

Fundraising and volunteering
In FY2012, the Group was responsible for generating £357,909 of income for registered charities in the year, including £129,576 of direct cash donations (2011: £240,455). In addition, we invested over £150,000 in community projects, in towns and villages that we added to our NGN footprint. We 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 new communities
FY2012 saw us bring our NGN to several hundred additional telephone exchanges as part of our local loop unbundling programme. Each new addition sees our best value 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, be it a junior football team (for example Pangbourne Youth Football Club), improvements to a community centre or a Town in Bloom project.

In FY2012, we supported over 300 local communities in this way, directly investing over £150,000 in projects. This included support for over 150 youth and ladies' football teams, 60 community centres, 40 rugby and cricket clubs, 16 sport and leisure centres, 40 Christmas lights ceremonies and numerous allotments and gardening projects.

Engaging with our customers
We ran two customer driven fundraising campaigns in FY2012. 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.

FY2012 also saw the introduction of an initiative to reward customers who return to us routers that have been diagnosed as end-of-life. We pay for the postage, before refurbishing or safely recycling the equipment, and donate £1 to charity. Among those to benefit in this first year was Cool Earth, a charity supported by Sir David Attenborough and Professor Lord Stern. Cool Earth is the only charity dedicated to protecting endangered rainforests, one of the most effective ways to minimise CO_2 reaching our atmosphere.

Engaging with our colleagues
FY2012 saw us introduce our Give Something Back initiative, which offers our people an extra day of paid leave, every year, to volunteer or fundraise for a charity of their choice. We also offer fundraising matching. The first year was a success, with over 300 team and individual events taking place. One team of 20 alone raised over £20,000 for Ambitious about Autism by cycling from London to our office in Greater Manchester.

Our charity partner of ten years, Ambitious about Autism is the national charity for children and young people with autism. They provide specialist education, through the TreeHouse School as well as raising awareness and understanding, and influencing policy. It is their ambition to make the ordinary possible for more children and young people with autism.

We also collaborated with Marie Curie Cancer Care and Sport Relief as part of Give Something Back, with our people participating in their organised challenges. This included making over cancer sufferers' gardens and team fundraising challenges such as taking over charity shops for the day.

Engaging with our suppliers
November 2011 saw our Directors host the Night of Ambition, our second annual fundraising auction on behalf of Ambitious about Autism. A record number of our suppliers generously took tables and donated unique lots for Nicholas Bonham to auction. Over £200,000 was raised for the cause.

Looking ahead
In FY2013 we will expand our charity efforts by establishing partnerships with organisations that work in the communities surrounding our major sites. We will start with Irlam in Greater Manchester, Warrington and West London.

Other achievements in FY2012
- Through demonstrating our approach to responsible business, 2011 saw us admitted to the Corporate Responsibility Group. Members pledge to share best practice on community involvement, business ethics and environmental protection with fellow members, even competitors.
- We retained both our FTSE4Good Index membership and Carbon Saver Gold Standard certification.

Corporate Responsibility Group

FTSE4Good

For more detail
Our first Sustainability Report will be available on our website in 2012, and we are aiming for compliance with the Global Reporting Initiative (GRI) standard.

To read more on our Sustainability strategy and progress, visit:
www.talktalkgroup.com/sustainability

People

Our people are at the heart of TalkTalk and in this year of significant change our people agenda has been more important than ever. We encourage honesty, ideas and action and we acknowledge that our people are the key to the success of the business.

In January 2011, we announced a Group wide restructure across TalkTalk that had a significant impact on our people and transformed the way that we operate, making us a simpler, more effective organisation.

Being Brighter – employee development programme
Our people plan for the year clearly focused on development and engagement following the launch of our Brighter Basics last year. They are a set of values that capture our personality and the ambition of TalkTalk. They are centred around five key areas: Customer, Value, Innovate, People and Community. It is important that these values become embedded across the organisation and we held a series of one day events across the country, which every single employee attended, including many of our outsource partners in the UK and overseas. First and foremost it was a day for our employees' personal development, where they learnt some tools to use both at work and in their personal life. The tools they experienced brought the Brighter Basics to life and also will form the basis of future training and development events across the Group.

Leading a Brighter Business
We recognise that the quality of our managers is vital to our future success. In January this year we launched our new Leadership Development Programme, 'Leading a Brighter Business', to empower our people managers as leaders and provide them with the tools to drive the business forward to even greater success. Over 550 people managers are taking part in the programme over the coming year.

Involvement and recognition
Recognising our people who are driving our culture by actively demonstrating our Brighter Basics is extremely important to us. We introduced a manager-led recognition initiative where managers can reward their employees with an 'On-the-Spot' award. We also continue our highly popular 'TalkTalk Heroes' scheme, again in line with the Brighter Basics, where people are nominated by their colleagues for their outstanding contribution in a whole range of subjects, from charity work to customer engagement.

Employee benefits
We have a comprehensive range of benefits that we offer to our employees and this year we were able to extend this once again to include a Sharesave scheme to enable our employees to participate in the performance of the Group. To ensure that our employees can enjoy the power of the internet at home, we are also continuing to offer their broadband and phone services for free.

Great Getaway
We held our first ever Company-wide employee event, the 'Great Getaway' in September last year, which was really popular and a great success. We decided to make it a family friendly event and extend the invitation to 3,500 TalkTalk colleagues and their families. The event was shaped by our people from a comprehensive cross-section from across the business who formed the Organising Committee. After the success of last year we will be continuing with this event later on this year.

TalkTalk Employee Forum – ONE Voice
As part of our transformation journey we have re-launched our employee forum, ONE Voice, a consultation and information forum consisting of 80 nominated employee representatives, management and members of our People Services team. We are committed to involving our people in the key issues and challenges we face as a Group.

Employee communication
We have developed a range of channels and methods to improve communication with our people. We hold regular 'All-Hands' events at each of our sites and also include our offshore partners where members of the senior leadership team provide business updates to everyone. We also communicate on a weekly basis via 'TeamTalk', a newsletter that incorporates various updates from across the business. We have also recently developed a better way of communicating with our People Managers by having a bespoke newsletter and website on our intranet to inform them first about matters that affect them or their teams. The weekly 'Dido's blog' continues to be popular with employees regularly feeding back on key issues.

Employee engagement – MySay
At the end of last year we held our new engagement survey, MySay. This is to help us explore more about what it's like to work at TalkTalk and how we can be a great place to work. We achieved a response rate of 72% and it has provided valuable insights into what we're doing well and also where we need to improve in order to make TalkTalk a brighter place for everyone.

Our engagement survey and plan enable us to listen and respond to what our people are saying and help us to create and sustain an environment where employees are motivated, stay with us and enjoy doing great work.

Disabled employees
We have an equal opportunities policy, which ensures that disabled persons are provided with the same opportunities for employment, career development, training and promotion along with all other employees. 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.

Board of Directors and advisors

Chairman:

Charles Dunstone (47)

Charles founded the Carphone Warehouse, and created TalkTalk in 2002. Since that date he has directed the development of TalkTalk to become one of the leading fixed line telecoms businesses in the UK. Charles is chairman of the Prince's Trust, chairman of Carphone Warehouse Group PLC and a Non-Executive Director of The Daily Mail and General Trust PLC and Independent Media Distribution PLC.

Executives:

Dido Harding (44)

Dido has been Chief Executive Officer of TalkTalk since February 2010. Prior to that date 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.

Amy Stirling (42)

Amy has been the Chief Financial Officer of TalkTalk since 2006, having been with CPW since 2000. Amy has played a key role in the management and integration of the significant businesses acquired by TalkTalk over the past seven years. Amy has no external director appointments.

David Goldie (48)

David joined TalkTalk when the Opal business was acquired by CPW in 2002. 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 and was a Board member of the Northwest Regional Development Agency until he resigned in December 2011. The Agency was closed on 31 March 2012.

Non-Executives:

Roger Taylor (47)

Roger was Chief Financial Officer of CPW from January 2000, and played a key role in the creation and growth of its group, including TalkTalk. Roger is also Chief Executive Officer of Carphone Warehouse Group PLC.

John Gildersleeve (67)

John was an Executive Director of Tesco PLC, and joined the Board of CPW in June 2000 before becoming Chairman in July 2005. John is a Non-Executive Director of Carphone Warehouse Group PLC and The British Land Company PLC.

Ian West (48)

Ian has been involved in the TMT sector for over 20 years. Ian held numerous roles at British Sky Broadcasting over 11 years, including managing director of the Sky Digital subscription business and co-founded Top Up TV in 2003.

John Allwood (60)

John was the Chief Operating Officer and latterly Group Finance Director of Mecom Group PLC, and prior to this he was managing director of Telegraph Media Group Limited, Chief Executive of Orange UK and of Mirror Group PLC. John is a member of Exeter University Council and a Non-Executive Director of Carphone Warehouse Group PLC.

Brent Hoberman (43)

Brent co-founded lastminute.com in 1998, and was their Chief Executive Officer until it was sold in 2005, during which time he oversaw its flotation on the London Stock Exchange in March 2000. Brent has subsequently founded mydeco, the innovative online service for home design and furniture. Brent is Governor of the University of the Arts, London, a Non-Executive Director of Guardian Media Group, Non-Executive Chairman of Where are we now? Limited, a member of the Business Council for Britain and a Young Global Leader for the World Economic Forum.

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 6LG

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.

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 nine members, four of whom, excluding the Chairman and deputy Chairman, are considered independent Non-Executive Directors. These are John Gildersleeve, our Senior Independent Director, John Allwood, Brent Hoberman and Ian West. Roger Taylor, the deputy Chairman, is not considered independent given he was previously Chief Financial Officer of CPW from the which the Company was demerged in March 2010. Although the Board believes it currently has the right balance and level of independence, the Board is also considering a proposal to appoint another independent Non-Executive Director during FY2013 in order to provide certain additional experience to the Board. Such appointment will be carried out by the Nomination Committe.

Therefore, at least half of the Board (excluding the Chairman) are independent and this has been the situation for all of the financial year.

The Chairman and Executive Directors have service contracts that can be terminated by either the Company or the Director on 12 months' notice.

The Non-Executive Directors have three year periods of appointment, all of which commenced from 20 January 2010 (with the exception of Ian West, who was appointed on 8 February 2011). All the independent Directors have a three month notice period with no compensation for loss of office. Roger Taylor has a six month notice period.

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**	**7**	**1**

Director	Board	Audit	Remuneration	Nomination
Charles Dunstone, Chairman	6	–	–	–
Dido Harding	6	–	–	–
Amy Stirling(1)	5	–	–	–
David Goldie(2)	5	–	–	–
Roger Taylor	6	–	–	1
John Gildersleeve(3)	5	2	7	1
Ian West	6	3	7	1
John Allwood	6	3	–	–
Brent Hoberman(4)	6	–	4	–

(1) Amy Stirling was unable to attend a Board meeting due to illness.
(2) David Goldie was unable to attend a Board meeting due to a prior business commitment.
(3) John Gildersleeve was unable to attend a Board meeting and an Audit Committee meeting due to a prior business commitment.
(4) Brent Hoberman was unable to attend three Remuneration Committee meetings due to prior business commitments.

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 form a good knowledge of how the Group operates.

The Chairman meets regularly with just the Non-Executive Directors, usually in the evening 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 also 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.

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 the FY2014.

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 as required by the Code, the fourth to ensure the compliance of the Group within the regulatory environment in which it operates and the fifth to focus on the Group's work in relation to its forthcoming television proposition.

Audit Committee

The Committee currently comprises the following independent Non-Executive Directors: John Allwood (Chairman), John Gildersleeve and Ian West. Roger Taylor is not a member but attends the Committee by invitation.

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 and other senior management attend the Committee meetings by invitation of the Committee. 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 auditor has 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.

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 period, 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 their 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 12 months include:

- review of the financial statements in the Annual Report 2011 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;

Corporate governance
continued

- 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.

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:

£m	2012	2011
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	**0.6**	0.7
Audit services provided to all Group companies	**0.7**	0.8
Taxation services	**0.1**	0.1
Other services	**0.2**	0.1
All other services	**0.3**	0.2
Total Group auditor's remuneration	**1.0**	1.0

Certain non-audit services are pre-approved by the Committee depending upon the nature and size of the service. Tax services principally comprise technical advice associated with relevant UK and international fiscal laws and regulations and, in particular, assessment of the potential implications of proposed corporate transactions or restructuring. Other services principally represent advice provided and project management support received for the set up of the Group's human resources and finance shared service functions. Having undertaken a review of the non-audit related work, the Committee has satisfied itself that the services undertaken during the period 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 of any 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 have expressed their willingness to continue in office as auditor and a resolution to re-appoint them 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 and Ian West. Roger Taylor is not a member but the attends the Committee by invitation.

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 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 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.

Television Committee

The Board has established a Committee delegated with managing the Group's future plans for television. 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.

The risk management programme is supported by the Business Assurance and Internal Audit functions.

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, counter-parties 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 and Audit Committee 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 and financial statements. 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 and financial statements. This was approved by the Audit Committee and the Board.

This is supported by the Business Assurance 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.

During the year the Group launched a new discretionary share option plan. Prior to the launch of the plan, significant shareholders were consulted.

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 FY2012.

Introduction
The Group's remuneration continues to be focused on enabling it 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.

The 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.

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 strongly 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. The Company may, in calculating this percentage, take into account Executive Directors' participation shares issued under the TalkTalk Group Value Enhancement Scheme, a summary of which is set out later in this report.

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 into account 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 PricewaterhouseCoopers and Towers Watson was received in relation to share schemes and executive remuneration respectively. 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:

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

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

Component	Aim	Description	Further Detail
Fixed Basic salary	To attract and retain talent by ensuring base salaries are 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 salary for Executive Directors remains at market median levels. 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.
Affinity benefits	Benefits may vary dependent on the role of the individual.	These include car allowances/ company car provision, voluntary benefits arrangements 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 the year ended 31 March 2012 was based on a 'balanced scorecard' that was comprised of financial measures, customer measures and 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 they feel that this course of action is appropriate.
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.	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

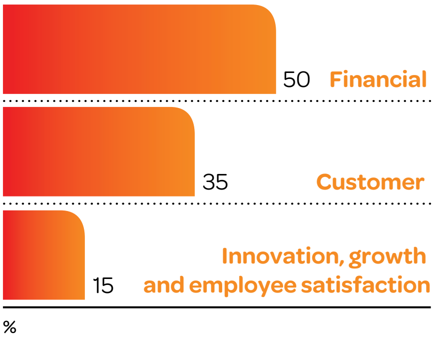
Annual performance bonus

For the year ending 31 March 2012, the annual performance bonus was based on a 'balanced scorecard' blend of financial measures (Group Headline EBITDA, Group operating free cash flow, revenue), customer measures (On-net customer base and churn), employee satisfaction measures and innovation. Executives had an incentive opportunity in the range of 0% to 200% of base salary. Performance for the year achieved 40% of the maximum bonus potential resulting in a bonus of 80% of salary.

Director	2012 £000	2011 £000
D Harding	**400**	199
A Stirling	**300**	149
D Goldie	**260**	130
Total	**960**	478

Cash awards will be paid in June 2012.

Annual Performance Bonus Scheme – executive performance measures



Weighting of FY2012 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 being at the start of the financial year ending 31 March 2010. 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').

When the performance conditions have been 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.

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 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.

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 financial statements.

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 out performance in bear market conditions and under performance 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 payout 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%.

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, three or five years.

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 2012. The options are exercisable from 1 July 2013 at an exercise price of £1.02 per share. The options expire on 1 January 2014.

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.

Further details of the features and operations of the TTG VES, DSOP and SAYE can be found in note 5 to the 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	Other(3) £000	2012 Total £000	2011 Total £000
Executive						
D Harding	**500**	**16**	**400**	**–**	**916**	716
A Stirling	**375**	**9**	**300**	**144**	**828**	533
D Goldie	**325**	**20**	**260**	**144**	**749**	470
Non-Executive						
C Dunstone	**360**	**1**	**–**	**–**	**361**	362
R Taylor	**75**	**–**	**–**	**–**	**75**	75
J Gildersleeve	**85**	**–**	**–**	**–**	**85**	73
J Allwood	**60**	**–**	**–**	**–**	**60**	60
B Hoberman	**50**	**–**	**–**	**–**	**50**	50
I West(1)	**74**	**–**	**–**	**–**	**74**	8
J Burley(2)	**–**	**–**	**–**	**–**	**–**	40
Aggregate emoluments	**1,904**	**46**	**960**	**288**	**3,198**	2,387

(1) Appointed in February 2011.
(2) Resigned in November 2010.
(3) Amy Stirling and David Goldie 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.

Total remuneration for 2012 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 either a fixed proportion by the Director or no contribution 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 was a member 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 financial statements.

Director	2012 £000	2011 £000
D Harding	**51**	51
A Stirling	**19**	19
D Goldie	**60**	65
Total	**130**	135

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	2012 £000
D Harding	British Land PLC, The Jockey Club	**67**
D Goldie	Northwest Regional Development Agency(1)	**7**
Total		**74**

(1) Resigned at the end of December 2011, the Northwest Regional Development Agency was closed on 31 March 2012.

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 with the exception of Roger Taylor, who has a six month notice period. The Company has no age limit for Directors. The dates of each contract are set out below 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
C Dunstone	TV
R Taylor	Remuneration, Nomination
J Gildersleeve(1)	Audit, Remuneration, Nomination, Compliance
J Allwood	Audit
B Hoberman	Remuneration
I West(1,2)	Audit, Remuneration, Nomination, TV
J Burley(3)	Audit, Remuneration, Nomination

(1) Fees in respect of the TV and Regulatory Compliance Committees were paid effective from 1 April 2011.
(2) Appointed February 2011.
(3) Resigned in November 2010.

Directors' Remuneration Report
continued

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 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 (the 'TTG VES') and the CPW TTG VES (the 'CPW TTG VES').

The Directors had the following percentage shares in the TTG VES pool at 31 March 2012:

Director	**2012 % Share**	2011 % Share
A Stirling	**6**	6
D Goldie	**6**	6
D Harding	**10**	10

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 2012:

Director	**2012 £000**	2011 £000
A Stirling	**433**	295
D Goldie	**433**	295
D Harding	**1,606**	480
	2,472	1,070

During the year, agreement was received from HMRC for the basis of calculation used to determine market value of the Participation Shares. Participant loans have increased to take this into account.

Interest on outstanding loans was charged at 4% during the year (2011: 4%).

The Directors had the following percentage share in the CPW TTG VES at 31 March 2012:

Director	2012 % Share	2011 % Share
R Taylor	53.5	53.5

The remaining percentage share in the CPW TTG VES pool is held by other senior management of Carphone Warehouse Group PLC.

Based on the weighted average share price for the year, and as disclosed in note 5 to the financial statements, the number of shares in the combined TTG VES pool and CPW VES pool at 31 March 2012 is 30.5 million (2011: 32.8 million).

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 2011 or date of appointment	Granted during the year	Exercised during the year	Lapsed during the year	**At 31 March 2012**	Exercise price per share £	Exercisable from	Expiry date
D Harding	236,220	–	–	–	**236,220**	–	01/09/2012	04/12/2020
	236,220	–	–	–	**236,220**	–	01/09/2013	04/12/2020
	–	1,024,590	–	–	**1,024,590**	–	May 2015	07/02/2022
Total for D Harding	472,440	1,024,590	–	–	**1,497,030**			
A Stirling	–	614,754	–	–	**614,754**	–	May 2015	07/02/2022
Total for A Stirling	–	614,754	–	–	**614,754**			

For awards made in September 2010 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 financial statements.

For awards made in February 2012 the performance conditions are based on an equal split of achieving a compound TSR measure and a compound EPS measure over the performance period. Full details of the scheme are disclosed in note 5 to the financial statements.

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

a. CSOP

Director	At 31 March 2011 or date of appointment	Granted during the year	Exercised during the year	Lapsed during the year	At 31 March 2012	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
R Taylor	444,444	–	444,444	–	**–**	0.52	06/06/2006	06/06/2013
	250,000	–	250,000	–	**–**	0.48	11/06/2005	11/06/2012
Total for R Taylor	694,444	–	694,444	–	**–**			

The market price at the date of exercise was 136p per share.

The market price was 137p as at 31 March 2012 (2011: 134p), and the range during the year was 150p to 119p.

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 2011 or date of appointment	Granted during the year	Exercised during the year	Lapsed during the year	At 31 March 2012	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**			
R Taylor	213,856	–	213,856	–	**–**	–	11/06/2005	11/06/2012
	675,000	–	675,000	–	**–**	–	28/07/2007	28/07/2014
	675,000	–	675,000	–	**–**	–	28/07/2008	28/07/2015
Total for R Taylor	1,563,856	–	1,563,856	–	**–**			

The market price at the date of exercise was 136p per share.

Directors' interests in shares and dates of service contracts
Both the Directors' interests in the Group at 31 March 2012 and the effective dates of their contract are set out below:

	Ordinary shares of 0.1p		
Director	**31 March 12**	31 March 11	Date of contract
C Dunstone	**295,209,396**	295,209,396	20-Jan-10
D Harding	**–**	–	20-Jan-10
A Stirling	**536,687**	536,687	20-Jan-10
D Goldie	**945,460**	945,460	20-Jan-10
R Taylor	**2,587,932**	1,083,698	20-Jan-10
J Gildersleeve	**246,000**	246,000	20-Jan-10
J Allwood	**10,000**	–	20-Jan-10
B Hoberman	**–**	–	20-Jan-10
I West	**346,023**	164,323	08-Feb-11

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.

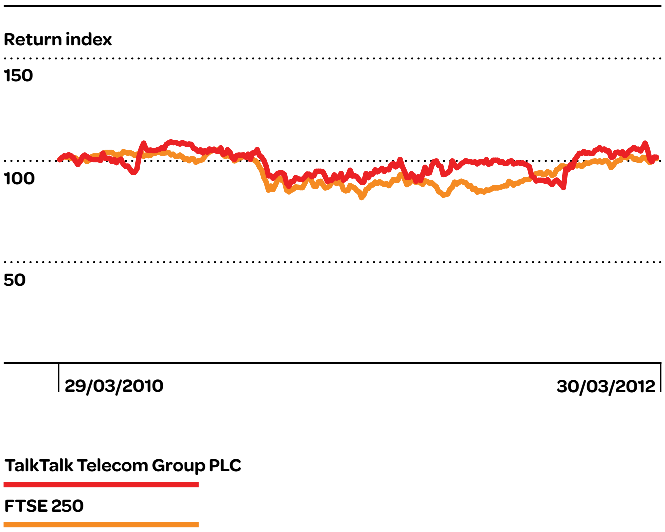
In framing its remuneration policy the Committee has given full consideration to the matters set out in Schedule A of the Code. As required by the Regulations, a resolution to approve this report will be proposed at the AGM to be held on 27 July 2012.

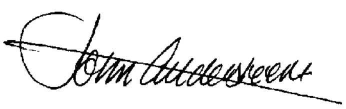
Performance graph

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





John Gildersleeve
Senior Independent Non-Executive Director
16 May 2012

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 average credit period taken on trade payables was 32 days (2011: 24 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 2011, the Directors were granted the right to acquire 91,410,825 shares. This right expires on the date of the 2012 AGM or 28 October 2012 (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.

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 16 May 2012 the Company had been notified of the following interests in the Company's shares:

Name	Number of shares	Percentage of share capital
Charles Dunstone	295,209,396	32.29%
David Ross	116,160,528	12.71%
Capital Research and Management Company	68,558,100	7.50%
Jupiter Asset management	47,609,919	5.21%
Invesco Asset Management (UK)	43,092,820	4.71%
Group ESOT	41,731,830	4.57%
M&G Investment Management	27,779,209	3.04%

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 finance review on page 12.

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

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 s418 of the Companies Act 2006.

By order of the Board

TalkTalk Telecom Group PLC
11 Evesham Street
London W11 4AR

TS Morris
Company Secretary
16 May 2012

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 Group 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 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.

In preparing the Group 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.

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
16 May 2012

A Stirling
Chief Financial Officer
16 May 2012

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 2012, 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 26. 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 2012 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 financial statements, 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 matters

We have reported separately on the Parent Company financial statements of TalkTalk Telecom Group PLC for the year ended 31 March 2012 and on the information in the Directors' Remuneration Report that is described as having been audited.

Peter O'Donoghue (Senior Statutory Auditor)
for and on behalf of Deloitte LLP
Chartered Accountants and Statutory Auditor
London, United Kingdom
16 May 2012

Group income statement

For the year ended 31 March 2012

	Notes	Before amortisation of acquisition intangibles and exceptional items 2012 £m	Amortisation of acquisition intangibles and exceptional items* 2012 £m	After amortisation of acquisition intangibles and exceptional items 2012 £m	Before amortisation of acquisition intangibles and exceptional items 2011 £m	Amortisation of acquisition intangibles and exceptional items* 2011 £m	After amortisation of acquisition intangibles and exceptional items 2011 £m
Revenue	2	**1,687**	**–**	**1,687**	1,765	–	1,765
Cost of sales		**(803)**	**–**	**(803)**	(877)	–	(877)
Gross profit		**884**	**–**	**884**	888	–	888
Operating expenses excluding amortisation and depreciation		**(558)**	**(27)**	**(585)**	(612)	(48)	(660)
EBITDA		**326**	**(27)**	**299**	276	(48)	228
Depreciation	3, 12	**(65)**	**–**	**(65)**	(57)	(3)	(60)
Amortisation	3, 11	**(27)**	**(61)**	**(88)**	(26)	(66)	(92)
Share of results of joint venture	14	**(1)**	**–**	**(1)**	(1)	–	(1)
Operating profit	3	**233**	**(88)**	**145**	192	(117)	75
Finance costs	6	**(18)**	**–**	**(18)**	(18)	–	(18)
Profit before taxation		**215**	**(88)**	**127**	174	(117)	57
Taxation	7	**(56)**	**67**	**11**	(52)	30	(22)
Profit for the year		**159**	**(21)**	**138**	122	(87)	35
Attributable to the equity holders of the Parent Company		**159**	**(21)**	**138**	122	(87)	35
Earnings per share							
Basic (pence)	10	**18.0**		**15.6**	13.5		3.9
Diluted (pence)	10	**17.2**		**14.9**	12.8		3.7

* 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 2012

	Notes	2012 £m	2011 £m
Profit for the year[1]		**138**	35
Other comprehensive income for the year			
Exchange differences on translation of foreign operations[1]		**–**	1
Currency translation and cash flow hedges[2]		**–**	(1)
Total comprehensive income for the year		**138**	35
Attributable to the equity holders of the Parent Company		**138**	35

(1) Recognised within retained earnings and other reserves.
(2) Recognised within the translation and hedging reserve.

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 2012

	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	5	-	**–**	**–**	**–**	**(2)**	**(2)**
Equity dividends	8	**–**	**–**	**–**	**–**	**(58)**	**(58)**
At 31 March 2012		**1**	**586**	**(65)**	**(513)**	**435**	**444**

	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 2010		1	586	(60)	(513)	378	392
Total comprehensive income for the year		–	–	(1)	–	36	35
Taxation of items recognised directly in reserves	7	–	–	–	–	2	2
Recycling of translation and hedging reserve		–	–	(4)	–	–	(4)
Settlement of Group ESOT shares		–	–	–	–	1	1
Share-based payments reserve credit	5	–	–	–	–	4	4
Equity dividends	8	–	–	–	–	(15)	(15)
At 31 March 2011		1	586	(65)	(513)	406	415

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

Group balance sheet

For the year ended 31 March 2012

	Notes	2012 £m	2011 £m
Non-current assets			
Goodwill	11	**480**	471
Other intangible assets	11	**202**	255
Property, plant and equipment	12	**292**	290
Non-current asset investments	13	**1**	1
Investment in joint venture	14	**7**	4
Deferred tax assets	7	**120**	116
		1,102	1,137
Current assets			
Cash and cash equivalents	18	**2**	1
Inventories	15	**3**	3
Trade and other receivables	16	**184**	155
Loans to related parties	16	**2**	2
		191	161
Total assets		**1,293**	1,298
Current liabilities			
Trade and other payables	17	**(379)**	(376)
Loans and other borrowings	18	**(26)**	(44)
Corporation tax liabilities		**(16)**	(22)
Provisions	20	**(8)**	(32)
		(429)	(474)
Non-current liabilities			
Loans and other borrowings	18	**(410)**	(395)
Provisions	20	**(10)**	(14)
		(420)	(409)
Total liabilities		**(849)**	(883)
Net assets		**444**	415
Equity			
Share capital	21, 22	**1**	1
Share premium	22	**586**	586
Translation and hedging reserve	22	**(65)**	(65)
Demerger reserve	22	**(513)**	(513)
Retained earnings and other reserves	22	**435**	406
Total equity		**444**	415

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

These financial statements were approved by the Board on 16 May 2012. They were signed on its behalf by:

D Harding
Chief Executive Officer
16 May 2012

A Stirling
Chief Financial Officer
16 May 2012

Group cash flow statement

For the year ended 31 March 2012

	Notes	2012 £m	2011 £m
Operating activities			
Operating profit		**145**	75
Adjustments for non-cash items:			
Share-based payments	5	**4**	4
Depreciation and impairment	3, 12	**65**	60
Amortisation and impairment	3, 11	**88**	92
Share of losses of joint venture	14	**1**	1
Recycling of translation reserve	9	**–**	(4)
Profit on disposal of property, plant and equipment		**(9)**	–
Profit on disposal of customer base		**(3)**	–
Fair value gain on step acquisition	13	**–**	(1)
Operating cash flows before movements in working capital		**291**	227
(Increase) decrease in trade and other receivables		**(20)**	11
Increase in inventory		**–**	(1)
Increase (decrease) in trade and other payables		**13**	(28)
Decrease in provisions		**(29)**	(4)
Cash generated by operations		**255**	205
Income taxes paid		**(2)**	(2)
Net cash flows generated from operating activities		**253**	203
Investing activities			
Acquisition of subsidiaries and joint ventures, net of cash acquired	13, 14	**(20)**	5
Disposal of customer base	13	**3**	–
Disposal of subsidiaries, net of cash disposed	13	**–**	4
Acquisition of intangible assets		**(28)**	(27)
Acquisition of property, plant and equipment		**(78)**	(83)
Disposal of property, plant and equipment		**9**	–
Cash flows used in investing activities		**(114)**	(101)
Financing activities			
Settlement of Group ESOT shares	22	**1**	1
Net purchase of own shares	22	**(54)**	–
Drawdown (repayment) of borrowings	23	**5**	(72)
Refinancing fees	6	**(7)**	–
Interest paid		**(17)**	(17)
Net decrease in loans to related parties	23	**–**	1
Dividends paid	8	**(58)**	(15)
Cash flows used in financing activities		**(130)**	(102)
Net increase in cash and cash equivalents		**9**	–
Cash and cash equivalents at the start of the year		**(8)**	(8)
Cash and cash equivalents at the end of the year		**1**	(8)
Cash and cash equivalents for the purpose of this statement comprise:			
Cash and cash equivalents	18	**2**	1
Bank overdrafts*	18	**(1)**	(9)
		1	(8)

* 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 the United Kingdom 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.

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 12 within the Finance Review.

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.

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.

Revenue
Turnover is stated net of VAT and other sales related taxes, and comprises revenue generated from the provision of fixed line 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;
- voice usage 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.

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	
	2012	2011	**2012**	2011
Euro	**1.16**	1.17	**1.20**	1.13
United States dollar	**1.60**	1.56	**1.60**	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.

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

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.

Notes to the consolidated financial statements
continued

1. Accounting policies and basis of preparation (continued)

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 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 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 provide 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, or 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 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.
- Level 3: Fair values measured using inputs for the asset or liability that are not based on observable market data.

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)
- Impairment of goodwill (note 11)
- Capitalisation and useful economic lives of assets (notes 11, 12)
- Impairment of assets (notes 11, 12)
- Trade receivables (note 16).

Application of significant new or amended EU endorsed accounting standards
In the current year, the following new and revised Standards and Interpretations have been adopted with no significant impact:

Accounting Standard	Requirement
Amendment to IFRS 1 'Limited Exemption from Comparative IFRS 7 Disclosures for First-time Adopters'	The amendment provides a limited exemption for first-time adopters from providing comparative fair-value hierarchy disclosures under IFRS 7.
Amendment to IAS 32 'Classification of Rights Issues'	Under the amendment, rights issues of instruments issued to acquire a fixed number of an entity's own non-derivative equity instruments for a fixed amount in any currency and which otherwise meet the definition of equity are classified as equity.
IFRIC 19 'Extinguishing Financial Liabilities with Equity Instruments'	The Interpretation provides guidance on the accounting for 'debt for equity swaps' from the perspective of the borrower.
The following amendments were made as part of 'Improvements to IFRSs (2010)'	
Amendment to IFRS 3 'Business Combinations'	IFRS 3 has been amended such that only those non-controlling interests which are current ownership interest and which entitle their holders to a proportionate share of net assets upon liquidation can be measured at fair value or the proportionate share of net identifiable assets. Other non-controlling interests are measured at fair value, unless another measurement basis is required by IFRS.
Amendment to IFRS 7 'Financial Instruments: Disclosures'	The amendment clarifies the required level of disclosure around credit risk and collateral held and provides relief from disclosure of renegotiated financial assets. The impact of this amendment has been to reduce the level of disclosure provided on collateral that the entity holds as security on financial assets that are past due or impaired.

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):

- IFRS 1 (amended) 'Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters'
- IFRS 7 (amended) 'Disclosures – Transfers of Financial Assets'
- IFRS 9 'Financial Instruments'
- IFRS 10 'Consolidated Financial Statements'
- IFRS 11 'Joint Arrangements'
- IFRS 12 'Disclosure of Interests in Other Entities'
- IFRS 13 'Fair Value Measurement'
- IAS 1 (amended) 'Presentation of Items of Other Comprehensive Income'
- IAS 12 (amended) 'Deferred Tax: Recovery of Underlying Assets'
- IAS 19 (revised) 'Employee Benefits'
- IAS 27 (revised) 'Separate Financial Statements'
- IAS 28 (revised) 'Investments in Associates and Joint Ventures'

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 9 will impact both the measurement and disclosure of Financial Instruments; and
- IFRS 12 will impact the disclosure of interest the Group has in other entities.

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.

	Year ended 31 March 2012 £m	Year ended 31 March 2011 £m
Revenue	**1,687**	1,765
Headline EBITDA	**326**	276
Depreciation	**(65)**	(57)
Amortisation of operating intangibles	**(27)**	(26)
Share of results of joint ventures	**(1)**	(1)
Headline profit before interest and taxation (note 9)	**233**	192
Amortisation of acquisition intangibles and exceptional amortisation*	**(61)**	(66)
Exceptional items – Operating expenses (note 9)	**(27)**	(48)
Exceptional items – Depreciation (note 9)	**–**	(3)
Operating profit	**145**	75

* In the prior year this comprised £62m amortisation on acquisition intangibles and £4m of exceptional amortisation (note 9).

The Group's revenue is split by broadband, non-broadband and corporate products. Broadband and non-broadband comprise Consumer and business customers that receive similar services.

	2012 £m	2011 £m
Broadband	**1,242**	1,247
Non-broadband	**129**	189
Corporate	**316**	329
	1,687	1,765

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. Profit before interest and taxation

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

	2012 £m	2011 £m
Depreciation of property, plant and equipment	**65**	57
Amortisation of acquisition intangibles	**61**	62
Amortisation of internally generated operating intangible fixed assets	**6**	6
Amortisation of other operating intangible fixed assets	**21**	20
Impairment of property, plant and equipment	**–**	3
Profit on disposal of property, plant and equipment	**(9)**	–
Profit on disposal of customer base	**(3)**	–
Impairment of operating intangible fixed assets	**–**	4
Impairment loss recognised on trade receivables	**38**	33
Share-based payments	**4**	4
Staff costs, excluding share-based payments	**137**	154
Cost of inventories recognised in expenses	**19**	19
Rentals under operating leases – property	**9**	9
Rentals under operating leases – other	**64**	57
Auditor's remuneration*	**1**	1

* A breakdown of auditor's remuneration is disclosed within the Corporate governance section on page 20.

4. Employee costs

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

	2012 Number	2011 Number
Administration	**1,545**	1,988
Sales and customer management	**1,561**	2,089
	3,106	4,077

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

	2012 £m	2011 £m
Wages and salaries	**120**	135
Social security costs	**14**	16
Other pension costs	**3**	3
	137	154
Share-based payments (note 5)	**4**	4
	141	158

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.

	2012 £m	2011 £m
Salaries and fees	**4.1**	3.4
Performance bonuses	**2.4**	2.4
Benefits	**0.1**	0.1
Pension costs	**0.2**	0.2
Share-based payments	**3.2**	2.3
Compensation for loss of office*	**1.0**	–
Other**	**0.3**	–
	11.3	8.4

* 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 is reversed.

Notes to the consolidated financial statements
continued

5. Share-based payments (continued)

Charges arise on loans that are provided to employees to fund the purchase of shares in the Group as part of long-term incentives 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. Where loans are granted for the purchase of shares under a LTIP, interest is charged on these loans.

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 Discretionary Share Option Plan ('DSOP') and Save-As-You-Earn scheme ('SAYE').

In addition, the Group has a number of legacy Carphone Warehouse Group 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 £1.36 (2011: £1.38).

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.

Summary of share schemes

	IFRS 2 charge	Dilutive effect	Options outstanding at end of the year
Year ended 31 March 2012	**£m**	**millions**	**millions**
TalkTalk Telecom Group PLC schemes			
DSOP – 2012 grant	**–**	**1.6**	**11**
DSOP – 2010 grant	**2**	**0.3**	**20**
SAYE	**1**	**0.9**	**6**
Total TalkTalk Telecom Group PLC schemes	**3**	**2.8**	**37**
Legacy Carphone Warehouse schemes			
TTG VES and CPW TTG VES*	**1**	**30.5**	**–**
Performance share plan	**–**	**3.7**	**2**
ESOS	**–**	**1.5**	**1**
Other employee share option schemes	**–**	**1.2**	**1**
Total Legacy Carphone Warehouse schemes	**1**	**36.9**	**4**
Total	**4**	**39.7**	**41**

	IFRS 2 charge	Dilutive effect	Options outstanding at end of the year
Year ended 31 March 2011	£m	millions	millions
TalkTalk Telecom Group PLC schemes			
DSOP – 2010 grant	2	0.5	24
SAYE	1	0.6	7
Total TalkTalk Telecom Group PLC schemes	3	1.1	31
Legacy Carphone Warehouse schemes			
TTG VES and CPW TTG VES*	1	32.8	–
Performance share plan	–	5.6	4
ESOS	–	2.4	3
Other employee share option schemes	–	3.5	3
Total Legacy Carphone Warehouse schemes	1	44.3	10
Total	4	45.4	41

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

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TalkTalk Telecom Group PLC schemes

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

(i) DSOP – 2012 grant

Nil priced share option awards were first granted in February 2012 and are subject to the 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 Annual Report and accounts for the year ended 31 March 2015. Options are forfeited if an employee leaves the Group before the options vest.

(ii) DSOP – 2010 grant

Awards made under the DSOP – 2010 grant are subject to TSR performance targets and are measured over an initial performance period to 29 March 2013 and a subsequent performance period to 29 March 2014. Options are forfeited if an employee leaves the Group before the options vest.

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

	DSOP – 2012 grant
Valuation method	Monte Carlo
Share price (pence)	122
Exercise price (pence)	–
Expected volatility	30.44%
Expected exercise (years)	3.3
Risk free rate	0.60%
Expected dividend yield	3.5%
Fair value of options granted (£m)	3

DSOP – 2010 grant	2012 Number million	2012 WAEP £	2011 Number million	2011 WAEP £
Outstanding at the beginning of the year	24	1.24	–	–
Granted during the year	–	–	29	1.25
Forfeited during the year	(4)	1.27	(5)	1.27
Outstanding at the end of the year	**20**	**1.24**	24	1.24
Exercisable at the end of the year	–	–	–	–

The weighted average remaining contractual life of DSOP – 2012 grant is 13.0 years, and the DSOP – 2010 grant is 7.7 years. No options were exercisable either during the year or at the year end. Of the DSOP – 2010 grant, 472,000 options were nil priced.

Notes to the consolidated financial statements
continued

5. Share-based payments (continued)

(iii) 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 and for employees based in Ireland range from €12 to €500 per month. Options may be exercised at the end of the three or five year period at an exercise price of £1.02 per share. The scheme is available for a period each year for employees to join. During the year, employees based in Ireland forfeited their options due to the closure of the Waterford site (note 9).

	2012 Number million	**2012 WAEP £**	2011 Number million	2011 WAEP £
Outstanding at the beginning of the year	**7**	**1.02**	–	–
Granted during the year	**1**	**1.19**	8	1.02
Lapsed during the year	**–**	**–**	–	–
Forfeited during the year	**(2)**	**1.03**	(1)	1.02
Outstanding at the end of the year	**6**	**1.05**	7	1.02
Exercisable at the end of the year	**–**	**–**	–	–

	SAYE – 2012 grant
Valuation method	**Black Scholes**
Share price (pence)	**145**
Exercise price (pence)	**119**
Expected volatility	**27.2%**
Expected exercise (years)	**4.5**
Risk free rate	**1.62%**
Expected dividend yield	**4.67%**
Fair value of options granted (£m)	**0.3**

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

(iv) 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%.

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 5 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.

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. These performance conditions are measured over an initial performance period to September 2012, at which point participants have a put option over 60% of their shares, and a subsequent performance period to September 2013, at which point participants have a put option over the remainder of their shares. If the performance criteria are not met, the A and C shares will have no value.

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.

The following assumptions were used in the Monte Carlo model for the A shares awarded in the year:

- volatility of 22%;
- a risk free rate ranging from 0.5% to 2.7%; and
- a dividend yield of between 0% and 5% in each of the three years to September 2013.

The following assumptions were used in the Black Scholes model for the A shares awarded in the year:

- equity volatility of 149.9% and 139.0% for September 2012 and September 2013 options respectively;
- a risk free rate of 1.9% and 2.3% for September 2012 and September 2013 options respectively; and
- a dividend yield of nil.

No C shares were awarded in the year.

6. Finance costs and investment revenue

Finance costs are analysed as follows:

	2012 £m	2011 £m
Interest on bank loans and overdrafts	**14**	13
Facility fees and similar charges	**3**	3
Unwinding of discount on provisions	**1**	2
	18	18

During the year the Group refinanced its revolving credit facility and paid £7m in respect of facility fees. This will be 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, and on the tax legislation then in force, and as such the value of associated deferred tax assets is uncertain.

Tax – Income statement
The tax charge comprises:

	2012 £m	2011 £m
Current tax:		
UK Corporation tax	**–**	–
Adjustments in respect of prior years:		
UK Corporation tax	**(4)**	(18)
Total current tax credit	**(4)**	(18)
Deferred tax:		
Origination and reversal of timing differences	**(13)**	18
Effect of change in tax rate	**10**	9
Adjustments in respect of prior years – reclassification from current tax	**–**	18
Adjustments in respect of prior years – deferred tax recognised	**(4)**	(5)
Total deferred tax	**(7)**	40
Total tax (credit) charge	**(11)**	22

Notes to the consolidated financial statements
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7. Taxation (continued)

The tax charge on Headline earnings for the year ended 31 March 2012 is £56m (2011: £52m) representing an effective tax rate on pre-tax profits of 26% (2011: 30%). The tax credit on Statutory earnings for the year ended 31 March 2012 is £11m (2011: £22m charge). The reconciliation between the Headline and Statutory tax charge is shown in note 9.

In the prior year there was a reclassification of £18m from current tax to deferred tax to better reflect expected utilisation of losses.

The principal differences between the tax charge and the amount calculated by applying the standard rate of UK corporation tax of 26% (2011: 28%) to the profit before tax are as follows:

	2012 £m	2011 £m
Profit before tax	**127**	57
Tax at 26% (2011: 28%)	**33**	16
Items attracting no tax relief or liability	**(2)**	2
Effect of change in tax rate	**10**	9
Adjustments in respect of prior years	**(4)**	(5)
Movement in unrecognised tax losses during the year	**(3)**	–
Recognition of additional Tiscali losses	**(45)**	–
Total tax (credit) charge through income statement	**(11)**	22

Tax – retained earnings and other reserves
Tax on items recognised directly in retained earnings and other reserves are as follows:

	2012 £m	2011 £m
Deferred tax credit	**–**	(2)
Total tax (credit) charge through retained earnings and other reserves	**(11)**	20

The movement for the year ended 31 March 2011 relates to share-based payments.

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

	Share-based payments	Timing differences on capitalised costs	Tax losses	Timing differences on acquisition intangibles	Other timing differences	Total
	£m	**£m**	**£m**	**£m**	**£m**	**£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**

	Share-based payments	Timing differences on capitalised costs	Tax losses	Timing differences on acquisition intangibles	Other timing differences	Total
	£m	£m	£m	£m	£m	£m
At 1 April 2010	2	85	85	(19)	2	155
(Charge) credit to the income statement	(1)	(9)	(40)	8	2	(40)
Credit to reserves	2	–	–	–	–	2
Acquisition of subsidiaries	–	–	–	(1)	–	(1)
At 31 March 2011	3	76	45	(12)	4	116

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. During the year a reduction in the UK Statutory rate of corporation tax was enacted bringing the rate down from 26% to 24%. Accordingly the tax assets and liabilities recognised at 31 March 2012 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 has been reduced. The Government intends to enact further reductions in the main tax rate of 1% each year, down to 23% effective from 1 April 2013 and to 22% by 1 April 2014. As these tax rates were not substantively enacted at the balance sheet date, the rate reduction is not reflected in these financial statements in accordance with IAS10 'Events after the Reporting Period', as it is a non-adjusting event occurring after the reporting period.

During the 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 has resulted in the recognition of deferred tax assets of £45m, in addition to those that were recognised at the acquisition date. The associated tax credit has been treated as an exceptional item in the income statement (note 9).

At 31 March 2012, the Group had unused tax losses of £873m (2011: £1,016m) available for offset against future taxable profits. A deferred tax asset of £56m (2011: £45m) has been recognised in respect of £232m (2011: £173m) of such losses, based on expectations of recovery in the foreseeable future.

No deferred tax asset has been recognised in respect of the remaining £641m (2011: £843m) 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.

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:

	2012 £m	2011 £m
Ordinary dividends		
Interim dividend for the year ended 31 March 2011 of 1.7p per ordinary share	**–**	15
Final dividend for the period 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**	–
Total ordinary dividends	**58**	15

The final dividend for the year ended 31 March 2012 is 6.4p per ordinary share on approximately 873 million shares (£56m), which was approved by the Board on 16 May 2012 and has not been included as a liability as at 31 March 2012.

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.

	EBITDA	Profit before interest and tax	Profit before tax	Profit for the year
Year ended 31 March 2012	**£m**	**£m**	**£m**	**£m**
Headline results	**326**	**233**	**215**	**159**
Exceptional items – Operating expenses (a)	**(11)**	**(11)**	**(11)**	**(8)**
Exceptional items – Operating expenses (b)	**(14)**	**(14)**	**(14)**	**(11)**
Exceptional items – Operating expenses (c)	**(3)**	**(3)**	**(3)**	**(3)**
Exceptional items – Operating expenses (d)	**1**	**1**	**1**	**1**
Amortisation of acquisition intangibles (e)	**–**	**(61)**	**(61)**	**(45)**
Exceptional items – taxation (f)	**–**	**–**	**–**	**45**
Statutory results	**299**	**145**	**127**	**138**

	EBITDA	Profit before interest and tax	Profit before tax	Profit for the year
Year ended 31 March 2011	£m	£m	£m	£m
Headline results	276	192	174	122
Exceptional items – Operating expenses (a)	(12)	(12)	(12)	(9)
Exceptional items – Operating expenses (d)	(36)	(36)	(36)	(28)
Exceptional items – Depreciation (d)	–	(3)	(3)	(2)
Exceptional items – Amortisation (d)	–	(4)	(4)	(3)
Amortisation of acquisition intangibles (e)	–	(62)	(62)	(45)
Statutory results	228	75	57	35

Notes to the consolidated financial statements
continued

9. Reconciliation of Headline information to Statutory information (continued)

(a) 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. A credit of £1m has been recognised in the year in respect of accruals relating to property costs which are no longer required. The total charge incurred in the year ended 31 March 2012 was £11m (2011: £12m).

A total taxation credit of £3m has been recognised in the year ended 31 March 2012 (2011: £3m).

(b) Operating efficiencies – Phase II (Contact centre rationalisation)
On 7 September 2011, the Group announced the consolidation of the Group's contact centre operations, which has resulted in redundancy, consultancy and onerous property lease costs, principally in relation to the closure of the Group's contact centre in Waterford, Ireland. The total charge incurred in the year ended 31 March 2012 was £14m (2011: £nil).

A total taxation credit of £3m has been recognised in the year ended 31 March 2012 (2011: £nil).

(c) Ofcom fine
During the year Ofcom fined the Group £3m as a result of contravention of General Condition 11 under section 94 of The Communication Act 2003. No tax credit has been recognised in respect of the fine.

(d) One Company integration
The One Company integration was implemented during the year ended 31 March 2010 following the acquisition of Tiscali UK on 3 July 2009. The Group revisited its overall operating structure in order to both integrate the Tiscali business and deliver efficiencies in existing operations. The programme has generated significant synergies, through the elimination of duplicated costs and migration of customers onto the Group's unbundled network and is largely complete.

A credit of £1m was recognised in the year in respect of a provision release for costs no longer anticipated to be incurred. In the prior year operating reorganisation costs of £40m were incurred, principally comprising redundancies and site closures, an integration project team and consulting costs and costs of £7m were incurred in respect of redundant software and fixed asset write-downs.

A total taxation credit of £nil in year ended 31 March 2012 (2011: £10m).

A credit of £4m was recognised in respect of recycling of translation reserves in the year ended 31 March 2011 in relation to legal entities, which were liquidated. No taxation has been recognised in respect of this credit.

(e) Amortisation of acquisition intangibles
An amortisation charge in respect of acquisition intangibles of £61m was incurred in the year (2011: £62m). A tax credit at 26% (2011: 28%) has been recognised in respect of the amortisation of acquisition intangibles, net of any adjustments in respect of prior periods: this was £16m for the year ended 31 March 2012 (2011: £17m).

(f) 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 has resulted in the recognition of deferred tax assets of £45m, in addition to those recognised at the acquisition date.

The recognition of the deferred tax asset has been recognised in exceptional items as it is both material and one-off in nature, and does not relate to the underlying performance of the business.

10. Earnings per share

Earnings per share is shown on both a Headline and Statutory basis to assist in the understanding of the underlying performance of the Group.

	2012 £m	2011 £m
Headline earnings (note 9)	**159**	122
Statutory earnings	**138**	35
Weighted average number of shares (millions):		
Shares in issue	**914**	914
Less weighted average holdings by Group ESOT	**(29)**	(7)
For basic EPS	**885**	907
Dilutive effect of share options	**40**	45
For diluted EPS	**925**	952

	2012 pence	2011 pence
Basic earnings per share		
Headline	**18.0**	13.5
Statutory	**15.6**	3.9

	2012 pence	2011 pence
Diluted earnings per share		
Headline	**17.2**	12.8
Statutory	**14.9**	3.7

The number of shares that could be issued but that are not considered to be dilutive at 31 March 2012 is 20 million (2011: 27 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 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 value in use of the CGUs to which the goodwill has been allocated.

Notes to the consolidated financial statements
continued

11. Goodwill and other intangible assets (continued)

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.

Impairment 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 three year plan and extrapolated out for the following 17 years based on the UK's long-term growth rate. This is discounted by the CGU's weighted average cost of capital 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 segment 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.

	2012 £m	2011 £m
Opening cost and net book value	**471**	470
Acquisition of subsidiaries (note 13)	**9**	3
Disposals (note 13)	**–**	(2)
Closing cost and net book value	**480**	471

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:

	2012 £m	2011 £m
Consumer	**337**	337
TalkTalk Business	**143**	134
	480	471

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 1.8% (2011: 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 8.2% (2011: 9.1%). 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.

(b) Other intangible assets

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.

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.

Notes to the consolidated financial statements
continued

11. Goodwill and other intangible assets (continued)

(b) Other intangible assets (continued)

Other intangible assets are analysed as follows:

	Operating intangibles	Acquisition intangibles	Total other intangibles
	£m	**£m**	**£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	Acquisition intangibles	Total other intangibles
	£m	£m	£m
Opening balance at 1 April 2010	126	190	316
Additions	28	3	31
Amortisation	(26)	(62)	(88)
Impairment charges	(4)	–	(4)
Closing balance at 31 March 2011	124	131	255
Cost (gross carrying amount)	207	328	535
Accumulated amortisation	(83)	(197)	(280)
Closing balance at 31 March 2011	124	131	255

Operating intangibles includes internally generated assets of net book value £26m (2011: £25m), which are amortised over a period of up to eight years. This includes additions of £7m (2011: £8m) and an amortisation charge of £6m (2011: £6m) in year ended 31 March 2012.

Included within Operating intangibles are the following assets which are material to the Group:

- TRIO, the customer billing system, which has a net book value of £90m (2011: £91m). TRIO is amortised over a period of up to eight years depending on the release date of relevant component. The weighted average remaining useful economic life of the components of TRIO is five years (2011: six years).

Acquisition intangibles are removed from cost in the analysis above once fully amortised.

(b) Other intangible assets (continued)

Acquisition intangibles are analysed as follows:

	Customer bases	Other	Total
	£m	**£m**	**£m**
Opening balance at 1 April 2011	**131**	**–**	**131**
Acquisition of subsidiaries	**9**	**–**	**9**
Amortisation	**(61)**	**–**	**(61)**
Closing balance at 31 March 2012	**79**	**–**	**79**
Cost (gross carrying amount)	**326**	**–**	**326**
Accumulated amortisation	**(247)**	**–**	**(247)**
Closing balance at 31 March 2012	**79**	**–**	**79**

	Customer bases	Other	Total
	£m	£m	£m
Opening balance at 1 April 2010	188	2	190
Acquisition of subsidiaries	3	–	3
Amortisation	(60)	(2)	(62)
Closing balance at 31 March 2011	131	–	131
Cost (gross carrying amount)	328	–	328
Accumulated amortisation	(197)	–	(197)
Closing balance at 31 March 2011	131	–	131

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.

Other acquisition intangibles primarily represent licences to continue to use the AOL and Tiscali brands, valued using the relief from royalty method.

Included within Acquisition intangibles are the following assets which are material to the Group and their remaining useful economic life at 31 March 2012:

- AOL broadband customer base which has a net book value of £32m (2011: £69m) and a remaining useful economic life of 10 months (2011: 22 months); and
- Tiscali customer base which has a net book value of £41m (2011: £59m) and a remaining useful economic life of 27 months (2011: 39 months).

Acquisition intangibles are removed from cost in the analysis above once fully amortised.

Notes to the consolidated financial statements
continued

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).

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	Network equipment and computer hardware	Fixtures and fittings	Total
	£m	**£m**	**£m**	**£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**

	Leasehold improvements	Network equipment and computer hardware	Fixtures and fittings	Total
	£m	£m	£m	£m
Opening balance at 1 April 2010	7	254	1	262
Additions	–	87	1	88
Depreciation	(1)	(55)	(1)	(57)
Impairment charges	–	(3)	–	(3)
Closing balance at 31 March 2011	6	283	1	290
Cost (gross carrying amount)	6	442	6	454
Accumulated depreciation and impairment charges	–	(159)	(5)	(164)
Closing balance at 31 March 2011	6	283	1	290

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 1 April 2010, 31 March 2011 and 31 March 2012	**1**

Non-current asset investments at 31 March 2012 and at 31 March 2011 relate to a 8.4% (2011: 11.3%) interest in Shared Band Limited, a telecommunications technology provider. The Group holds a strategic, non-controlling interest. These shares are not held for trading and accordingly are classified as available for sale. The fair value of the shares is based on cost less any provision for impairment, as the shares are not listed on an exchange, and therefore a market price cannot be reliably measured. This fair value measurement is classified as level three, derived from valuation techniques using data that are not based on observable market data.

(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
TalkTalk Direct Limited	England and Wales	Telecommunications
TalkTalk UK Communication Services Limited	England and Wales	Telecommunications
GIS Telecoms Limited	England and Wales	Telecommunications
CPW Network Services Limited	England and Wales	Telecommunications
Tiscali UK Limited	England and Wales	Telecommunications

* Directly held by the Company.

(b) Acquisitions and disposals

(i) Acquisitions
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.

Notes to the consolidated financial statements
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13. Non-current asset investments (continued)

The Group paid cash consideration of £1m in respect of deferred consideration for TalkTalk Business (2CCH) Limited and Southern Communications Limited and dealer buyouts. The acquisition of dealer buyouts resulted in acquisition intangibles of £1m.

In the year ended 31 March 2011:

- The Group agreed a net adjustment in respect of working capital and customer numbers with Tiscali S.p.A. in respect of the Group's acquisition on Tiscali UK on 3 July 2009. This resulted in an adjustment to goodwill of £14m.
- The Group acquired TalkTalk Business (2CCH) Limited and Southern Communications Limited for cash consideration net of cash acquired of £2m and deferred consideration of £2m, which resulted in acquisition intangibles of £2m and goodwill of £3m. The impact of these acquisitions on the results of the Group for the year ended 31 March 2011 had the businesses been acquired on 31 March 2010, is immaterial. The Group has recognised a gain of £1m within its income statement in respect of the increase in fair value of the equity interest held in Opal 2CCH Limited at the acquisition date. The goodwill of £3m was recognised relating to the future opportunities arising from the nature of the businesses and fit with the Group's existing operations.
- The Group paid cash consideration of £1m in respect of V Networks Limited deferred consideration and dealer buyouts which resulted in goodwill and acquisition intangibles of £1m.

(ii) Disposals
On 5 July 2011, Group disposed of its Valuecall operations for cash consideration of £3m. There was no associated goodwill or acquisition intangibles in respect of this business, resulting in a £3m profit on disposal.

In the year ended 31 March 2011 the Group entered into an agreement to sell its operations in Ireland for a consideration of £4m. The profit on sale of the business was offset by the impairment of goodwill recognised on the acquisition of Tele2 Ireland in 2006 of £2m and closure costs for the business of £2m, resulting in £nil profit or loss 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 has been set up in order to develop a new free-to-air internet-connected TV service to UK homes in 2012. The table below sets out the net additions in the year.

	Net assets £m
Opening balance at 1 April 2011	**4**
Additions	**4**
Share of results	**(1)**
Closing balance at 31 March 2012	**7**

	Net assets £m
Opening balance at 1 April 2010	–
Additions	5
Share of results	(1)
Closing balance at 31 March 2011	4

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	2012 £m	2011 £m
Revenue	–	–
Expenses	(1)	(1)
Loss before taxation	(1)	(1)
Taxation	–	–
Loss after taxation	(1)	(1)

Group share of net assets of joint ventures	2012 £m	2011 £m
Non-current assets	7	3
Cash and overdrafts (net)	–	2
Other liabilities	–	(1)
Net assets	7	4

At 31 March 2012 the Group had committed to pay £13m (2011: £14m) 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 and consists of modems 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.

	2012 £m	2011 £m
Goods for resale	3	3

The difference between the balance sheet value of inventory and its replacement cost is considered by the Directors not to be material.

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:

	2012 £m	2011 £m
Current – trade and other receivables		
Trade receivables – gross	133	109
Less provision for impairment	(29)	(31)
Trade receivables – net	104	78
Other receivables	31	44
Prepayments and accrued income	49	33
Trade and other receivables	184	155
Loans to related parties	2	2
	186	157

Notes to the consolidated financial statements
continued

16. Trade and other receivables (continued)

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

Loans to related parties comprise a loan to Future Office Communications Limited, an associated company of the Group.

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, adjusted to take account of the timing of acquisitions, was 24 days (2011: 19 days).

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

	2012 £m	2011 £m
UK sterling	**111**	102
Other	**22**	7
	133	109

The ageing of gross trade receivables is as follows:

	2012 £m	2011 £m
Not yet due	**80**	59
0 to 2 months	**21**	20
2 to 4 months	**14**	10
Over 4 months	**18**	20
	133	109

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

	2012 £m	2011 £m
Not yet due	**(3)**	(3)
0 to 2 months	**(5)**	(5)
2 to 4 months	**(8)**	(6)
Over 4 months	**(13)**	(17)
	(29)	(31)

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

	2012 £m	2011 £m
Opening balance	**(31)**	(37)
Charged to the income statement	**(38)**	(33)
Receivables written off as irrecoverable	**40**	39
	(29)	(31)

Trade receivables of £27m (2011: £22m) 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:

	2012 £m	2011 £m
0 to 2 months	**16**	15
2 to 4 months	**6**	4
Over 4 months	**5**	3
	27	22

17. Trade and other payables

	2012 £m	2011 £m
Trade payables	**135**	112
Other taxes and social security costs	**21**	33
Other payables	**26**	34
Accruals and deferred income	**197**	197
	379	376

The average credit period taken on trade payables, calculated by reference to the amounts owed at the balance sheet date as a proportion of the amounts invoiced by suppliers in the year, adjusted to take account of the timing of acquisitions, was 32 days (2011: 24 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:

	2012 £m	2011 £m
Cash at bank and in hand	**2**	1

The effective interest rate on bank deposits and money market funds was 0.5% (2011: 0.6%).

(b) Loans and other borrowings comprise:

	2012 £m	2011 £m
Current		
Bank overdrafts	**1**	9
Term loan (2011: uncommitted bank loan)	**25**	35
	26	44

	Maturity	2012 £m	2011 £m
Non-current			
Term loan	2014, 2015	**75**	100
Bilateral loan	2015	**30**	–
£520m revolving credit facility (2011: £550m)	2015	**305**	295
		410	395

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.

£100m term loan:
The Group has a committed Term Loan of £100m, £25m matures in March 2013, £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 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. During the year the final maturity date on the loan was extended from 2013 to 2015.

Notes to the consolidated financial statements
continued

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

£520m revolving credit facility ('RCF') and £70m bilateral agreement:
During the year, the Group refinanced the £550m RCF that was due to mature in March 2013. On 11 November 2011, the Group signed a new £520m 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 signed £70m of bilateral agreements which mature in March 2015 and November 2015.

The Group's facilities total £690m. The Group was in compliance with these covenants throughout the current and prior year.

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	**2012 £m**	2011 £m
Undrawn available committed facilities	2015	**255**	255
		255	255

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

	2012 £m	2011 £m
Less than 1 year	**26**	44
1 to 2 years	**25**	295
2 to 3 years	**80**	–
3 to 4 years	**305**	100
	436	439

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 above, are as follows:

	Book and fair value	
	2012 £m	2011 £m
Cash and cash equivalents	**2**	1
Trade and other receivables	**184**	155
Non-current investments and investment in joint venture	**8**	5
Trade and other payables*	**(379)**	(376)
Loans to related parties	**2**	2

* 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.

(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.

(a) Financial instruments (continued)

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 two, 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 2012 is £nil (2011: £nil). An expense of £nil (2011: £nil) has been recognised in other comprehensive income in the year ended 31 March 2012. As the hedges were fully effective there has been no income statement impact.

(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 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 2012, the sterling value of outstanding currency contracts was £2m (2011: £23m).

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) as follows:

	2012 £m	2011 £m
10% movement in the UK sterling/Euro exchange rate		
Income statement movement	**–**	2
Other equity movement	**–**	–

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

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

	UK Sterling £m	Euro £m	Total £m
2011			
Borrowings before derivatives	439	–	439
Derivative	(23)	23	–
	416	23	439

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.

(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.

	2012 £m	2011 £m
1% movement in the UK sterling interest rate		
Income statement movement	**2**	5
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 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	1 to 2 years	2 to 3 years	3 to 4 years	4 to 5 years	More than 5 years	Total
	£m	**£m**	**£m**	**£m**	**£m**	**£m**	**£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)**

	Less than 1 year	1 to 2 years	2 to 3 years	3 to 4 years	4 to 5 years	More than 5 years	Total
	£m	£m	£m	£m	£m	£m	£m
2011							
Loans and other borrowings	(54)	(305)	(3)	(103)	–	–	(465)
Derivative financial instruments – payable	(23)	–	–	–	–	–	(23)
Derivative financial instruments – receivable	23	–	–	–	–	–	23
Trade and other payables	(376)	–	–	–	–	–	(376)

(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 Finance review on page 12.

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 2012 of 98% (2011: 106%) was within the stated medium term target.

The gearing ratio at the year end is as follows:

	2012 **£m**	2011 £m
Debt	**(436)**	(439)
Cash and cash equivalents	**2**	1
Net debt	**(434)**	(438)
Equity	**444**	415
Net debt to equity ratio	**98%**	106%

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 12 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 12 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 seven 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 are expected to be utilised over the next 12 months.

The below tables analyse the Group's provisions:

	2012 £m	2011 £m
Operating efficiencies	**1**	12
One Company integration	**2**	10
Property	**9**	9
Contract and other	**6**	15
	18	46

	2012 £m	2011 £m
Current	**8**	32
Non-current	**10**	14
	18	46

Notes to the consolidated financial statements
continued

20. Provisions (continued)

	Operating efficiencies	One Company integration	Property	Contract and other	Total
	£m	**£m**	**£m**	**£m**	**£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**

	Operating efficiencies	One Company integration	Property	Contract and other	Total
	£m	£m	£m	£m	£m
2011					
Opening balance	–	14	9	24	47
Charged to income statement	12	6	1	–	19
Utilised in the year	–	(10)	(2)	(10)	(22)
Unwinding of discount	–	–	1	1	2
	12	10	9	15	46

21. Share capital

	2012 million	2011 million	**2012 £m**	2011 £m
Allotted, called-up and fully paid				
Ordinary shares of 0.1p each	**914**	914	**1**	1

Redeemable preference shares of £50,000 were issued as part of the demerger transaction and were redeemed in the prior year.

22. Reserves

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

	Share capital	Share premium	Translation and hedging reserve	Demerger reserve	Retained earnings and other reserves	Total
	£m	£m	£m	£m	£m	£m
At 1 April 2010	1	586	(60)	(513)	378	392
Net profit for the year	–	–	–	–	35	35
Exchange differences on translation of foreign operations	–	–	–	–	1	1
Recycling of translation and hedging reserve	–	–	(4)	–	–	(4)
Currency translation and cash flow hedges	–	–	(1)	–	–	(1)
Tax on items recognised directly in reserves (note 7)	–	–	–	–	2	2
Settlement of Group ESOT shares	–	–	–	–	1	1
Share-based payments reserve credit (note 5)	–	–	–	–	4	4
Equity dividends	–	–	–	–	(15)	(15)
At 31 March 2011	1	586	(65)	(513)	406	415

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.

Net purchase of own shares
The Group ESOT held 41 million shares at 31 March 2012 (2011: 5 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 the year end the shares had a market value of £56m (2011: £7m).

During the year ended 31 March 2012 the Group ESOT purchased 42 million shares at a cost of £54m.

23. Analysis of changes in net debt

	Opening	Net cash flow	Exchange movements	Closing
	£m	**£m**	**£m**	**£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)**

Notes to the consolidated financial statements
continued

23. Analysis of changes in net debt (continued)

	Opening	Net cash flow	Exchange movements	Closing
	£m	£m	£m	£m
2011				
Cash and cash equivalents	1	–	–	1
Bank overdrafts	(9)	–	–	(9)
	(8)	–	–	(8)
Current loans and other borrowings	(10)	(25)	–	(35)
Non-current loans and other borrowings	(490)	97	(2)	(395)
	(500)	72	(2)	(430)
Total net debt	(508)	72	(2)	(438)
Loans to related parties	3	(1)	–	2
Total net debt including loans to related parties	(505)	71	(2)	(436)

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.

The Group had outstanding commitments for future minimum payments due as follows:

	2012 £m	2011 £m
Less than 1 year	**37**	38
2 to 5 years	**73**	83
Greater than 5 years	**75**	56
	185	177

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:

	2012 £m	2011 £m
Expenditure contracted, but not provided for in the financial statements	**21**	14

26. Related party transactions

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

	Other related parties
	£m
2012	
Loans owed to the Group	**2**
2011	
Loans owed to the Group	2

Other related parties comprises loans to Future Office Communications Limited, associated undertakings of the Group.

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.

Independent auditor's report to the Directors of TalkTalk Telecom Group PLC

We have audited the Parent Company financial statements of TalkTalk Telecom Group PLC for the year ended 31 March 2012 which comprise the Parent Company balance sheet, the Parent Company reconciliation of movements in shareholders' funds and the related notes 1 to 9. 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 2012;
- 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 matters

We have reported separately on the Group financial statements of TalkTalk Telecom Group PLC for the year.

Peter O'Donoghue (Senior Statutory Auditor)
for and on behalf of Deloitte LLP
Chartered Accountants and Statutory Auditor
London, United Kingdom
16 May 2012

Company balance sheet

As at 31 March 2012

	Notes	2012 £m	2011 £m
Fixed assets			
Fixed asset investments	4	**1,004**	996
		1,004	996
Current assets			
Debtors: amounts due within one year	5	**505**	487
		505	487
Total assets		**1,509**	1,483
Current liabilities			
Creditors: amounts due within one year	6	**(128)**	(122)
Loans	7	**(25)**	–
		(153)	(122)
Non-current liabilities			
Loans	7	**(410)**	(395)
		(410)	(395)
Total liabilities		**(563)**	(517)
Net assets		**946**	966
Equity			
Share capital	8, 9	**1**	1
Share premium	9	**586**	586
Retained earnings and other reserves	9	**359**	379
Equity shareholders' funds		**946**	966

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

These financial statements were approved by the Board of Directors on 16 May 2012. They were signed on its behalf by:

D Harding
Chief Executive Officer
16 May 2012

A Stirling
Chief Financial Officer
16 May 2012

Company reconciliation of movement in shareholders' funds

	2012 £m	2011 £m
Profit (loss) for the period (note 2)	**34**	(10)
Equity dividends (note 3)	**(58)**	(15)
Retained loss for the period	**(24)**	(25)
Issue of share capital	**–**	987
Share-based payments reserve credit	**4**	4
Net movement in shareholders' funds	**(20)**	966
Opening shareholders' funds	**966**	–
Closing shareholders' funds	**946**	966

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 prior period comparatives have been prepared for the 15 months from 15 December 2009 to 31 March 2011 as the Company was incorporated on 15 December 2009.

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 12 within the Finance Review.

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 Group 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 note 19 to the Group's Annual Report and accounts.

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2. Profit (loss) for the period

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 period. The Company reported a profit of £34m for the year ended 31 March 2012 (2011: £10m loss).

The auditor's remuneration for audit and other services is disclosed in the Corporate governance report on page 20.

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

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.

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.

	2012 £m	2011 £m
Interim dividend for the period ended 31 March 2011 of 1.70p per ordinary share	**–**	15
Final dividend for the period ended 31 March 2011 of 3.90p per ordinary share	**35**	–
Interim dividend for the year ended 31 March 2012 of 2.6p per ordinary share	**23**	–
Total ordinary dividends	**58**	15

The final dividend for the year ended 31 March 2012 is 6.4p per ordinary share on approximately 873 million shares (£56m), which was approved by the Board on 16 May 2012 and has not been included as a liability as at 31 March 2012.

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.

	2012 £m	2011 £m
Subsidiaries	**995**	991
Joint venture	**9**	5
	1,004	996

	2012 £m	2011 £m
Opening net book value	**996**	–
Additions	**8**	996
Closing net book value	**1,004**	996

Notes to the Company financial statements
continued

4. Fixed asset investments (continued)

Joint ventures
The Company 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. Further details relating to the joint venture are disclosed within note 14 to the consolidated financial statements.

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

5. Debtors: amounts due within one year

	2012 £m	2011 £m
Amounts owed by Group undertakings	**496**	485
Other debtors	**9**	2
	505	487

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, usually through the Group's netting system, within 30 to 60 days.

6. Creditors: amounts due within one year

	2012 £m	2011 £m
Amounts owed to Group undertakings	**127**	122
Other creditors	**1**	–
	128	122

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, usually through the Group's netting system, within 30 to 60 days.

7. Loans

	2012 £m	2011 £m
Current		
Loans	**25**	–
Non-current		
Loans	**410**	395
	435	395

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

	2012 million	2011 million	2012 £m	2011 £m
Allotted, called-up and fully paid				
Ordinary shares of 0.1p each	**914**	914	**1**	1

In the prior period redeemable preference shares of £50,000 were issued as part of the demerger transaction and were redeemed in the prior year.

9. Reserves

	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**

	Share capital £m	Share premium £m	Profit and loss and other reserves £m	Total £m
At 15 December 2009	–	–	–	–
Issue of share capital	1	986	–	987
Capital reduction	–	(400)	400	–
Loss for the period	–	–	(10)	(10)
Net cost of share-based payments	–	–	4	4
Equity dividends	–	–	(15)	(15)
At 31 March 2011	1	586	379	966

In the prior period, on 29 March 2010, the Group became a separately listed entity on the London Stock Exchange, under a court approved scheme of arrangement under part 26 of the Companies Act. Both the share capital and share premium in the Company arose as a result of the issuance of new shares in the Group to ordinary shareholders of CPW. As these shares were issued for nil consideration, both the share capital of £1m and share premium of £986m have been treated as arising from the demerger reserve.

On 29 March 2010 the share premium relating to the ordinary shares was reduced by £400m by way of a court approved capital reduction. This had the effect of creating distributable reserves, which are available at the discretion of the Board for dividend payments as required.

Five year record (unaudited)

	2012 £m	2011 £m	2010 £m	2009 Unaudited £m	2008 Unaudited £m
Headline results					
Revenue	**1,687**	1,765	1,686	1,385	1,424
Net profit for the year	**159**	122	106	95	12
Net assets employed					
Non-current assets	**1,102**	1,137	1,204	1,319	928
Net current liabilities before provisions	**(230)**	(281)	(275)	(184)	(235)
Provisions	**(18)**	(46)	(47)	(8)	(10)
Non-current liabilities	**(410)**	(395)	(490)	(425)	(895)
Net assets employed	**444**	415	392	702	(212)
Headline earnings per share					
Basic	**18.0**	13.5	11.8	10.7	1.3
Diluted	**17.2**	12.8	11.2	10.4	1.3

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, 31 March 2009 and 31 March 2008 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 stand alone 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
RCF	Revolving Credit Facility

Glossary
continued

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
wifi	Trademark of the wifi 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:	27 July 2012
Ex-dividend date:	4 July 2012
Record date:	6 July 2012
Dividend payment date:	3 August 2012

About this report
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