

Notes to the Accounts

for the year ended 31 March 2004

1 Segmental reporting

Turnover has been analysed below between data and telecom services, Internet services, contact centre services and interactive services. The Directors consider these to be the same class of business and accordingly no segmental analysis of operating loss or net assets has been given.

	2004 £'000	2003 £'000
Turnover analysis from continuing operations		
Data and telecom services	198,644	160,556
Internet services	99,067	90,273
Contact centre services	21,694	24,631
Interactive services	12,967	15,776
	332,372	291,236

Turnover by origin

	2004 £'000	2003 £'000
United Kingdom	318,239	281,920
Europe	14,133	9,316
	332,372	291,236

Turnover by destination

	2004 £'000	2003 £'000
United Kingdom	314,687	278,503
Europe	17,685	12,134
USA	-	599
	332,372	291,236

2 Operating loss from continuing operations

	Notes	2004 £'000	2003 £'000
Operating loss is stated after charging/(crediting):			
Depreciation on tangible fixed assets			
- Owned assets		61,478	77,547
- Under finance leases		3,133	190
Amortisation of intangible fixed assets	9, 22	165	165
Profit on disposal of tangible fixed assets	22	-	(66)
Hire of assets under operating leases			
- Other operating lease rentals		8,681	9,861
Other operating income			
- Rents received		(289)	-
Auditor's remuneration for audit of	(i)		
- Group		175	160
- Company		-	-

(i) Fees paid to the auditors and their associates during the current and prior year are analysed below:

	2004 £'000	2003 £'000
All relate to the Group		
Audit services	201	180
Further assurance services	-	7
Tax services		
- Compliance services	7	-
- Advisory services	6	-
Other services	86	-
	300	187

The work included in Other Services comprises £77,000 for forensic work and £9,000 in connection with systems implementation work.

3 Earnings before interest, taxation, depreciation and amortisation (EBITDA)

	Notes	2004 £'000	2003 £'000
Operating loss		(21,213)	(50,799)
Depreciation charge for the year	5	64,611	77,737
Amortisation charge for the year	9	165	165
EBITDA		43,563	27,103

4 Employees

(a) Employee costs

	Note	2004 £'000	2003 £'000
Wages and salaries		57,407	63,085
Social security costs		6,115	6,615
Pension costs	24	3,117	3,144
Total employee costs		66,639	72,844
Less: amounts not charged to the Profit and Loss Account		(7,492)	(10,096)
Charged to the Profit and Loss Account		59,147	62,748

(b) Employee numbers

The year end and average number of employees (full-time and part-time) employed by the Group, including Executive Directors, were:

	At 31 March		Average	
	2004	2003	2004	2003
Operations	593	581	578	603
Selling and distribution	264	284	267	291
Administration and customer services	376	391	380	410
Contact centres	961	632	780	764
	2,194	1,888	2,005	2,068

The number of full-time equivalent staff was:

	2,089	1,858	1,942	2,034
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By location

	Average	
	2004	2003
United Kingdom	1,933	1,992
Europe	72	75
USA	-	1
	2,005	2,068

5 Depreciation charge

Depreciation is charged on network and non-network assets and is included within cost of sales and administration expenses on that basis as follows:

	Note	2004 £'000	2003 £'000
Cost of sales		47,152	43,977
Administration expenses		17,459	33,760
	22	64,611	77,737

The cost of sales depreciation charge includes asset impairment charges of £4,155,000 (2003: £2,694,000). The depreciation charge for administration expenses includes asset impairment charges of £612,000 (2003: £10,688,000).

6 Net interest payable and other similar charges

(a) Analysis of net interest payable and other similar charges

	2004 £'000	2003 £'000
Interest on overdrafts and other borrowings	5,278	6,879
Interest on finance leases	374	383
Total interest payable and other similar charges	5,652	7,262
Interest receivable	(382)	(347)
Net interest payable and other similar charges	5,270	6,915

(b) Analysis of total interest payable and other similar charges

	2004 £'000	2003 £'000
– Secured credit facilities	4,242	2,893
– Amortisation of loan costs	1,004	920
– Loan costs written off	–	2,469
– Other interest payable	32	597
– Finance leases	374	383
	5,652	7,262

7 Taxation charge on loss on ordinary activities

	2004 £'000	2003 £'000
Taxation on the loss for the year		
UK corporation tax charge at 30% (2003: 30%)	–	–
Overseas taxation	212	196
	212	196

The current tax charge is higher (2003: higher) than the standard rate of corporation tax in the UK (30%) applied to the loss for the year due to the following factors:

	2004 £'000	2003 £'000
Loss before taxation	(25,009)	(58,789)
Loss before tax at standard rate of 30% (2003: 30%)	(7,503)	(17,637)

Effects of:	2004 £'000	2003 £'000
Permanent differences	122	1,549
Fixed asset timing differences	6,769	15,888
Other timing differences	612	900
Prior year adjustments	–	(700)
Overseas taxation	212	196
	212	196

The future tax charge will be impacted by the reversal of the unrecognised deferred tax asset (see Note 18).

8 Loss per ordinary share

The loss and diluted loss per ordinary share have been calculated in accordance with Financial Reporting Standard 14 "Earnings per Share" (FRS 14) for both years. The loss for the financial year, divided by the weighted average number of ordinary shares in issue during the financial year, has been used to calculate both the loss and diluted loss per ordinary share.

	2004	2003
Loss for the financial year (£'000)	(25,221)	(58,985)
Basic and diluted weighted average share capital (number of shares, thousands)	1,329,973	1,329,347

The basic weighted average share capital excludes 17,600,525 (2003: 18,930,284) ordinary shares held by the Company under Trust in connection with the Employee Share Schemes.

9 Intangible fixed assets

Group	Note	Licences £'000	Other £'000	Total £'000
Cost				
At 1 April 2003 and 31 March 2004		500	2,077	2,577
Aggregate amortisation				
At 1 April 2003		363	1,913	2,276
Charge for the year	2	100	65	165
At 31 March 2004		463	1,978	2,441
Net book value at 31 March 2004		37	99	136
Net book value at 31 March 2003		137	164	301

Other intangible assets relates to costs associated with the development of new products or services.

10 Tangible fixed assets

Group	Notes	Land & leasehold buildings £'000	Plant & equipment £'000	Other assets £'000	Total £'000
Cost					
At 1 April 2003		12,462	497,997	140,502	650,961
Additions		385	28,615	12,118	41,118
Disposals		–	(313)	–	(313)
At 31 March 2004		12,847	526,299	152,620	691,766
Aggregate depreciation					
At 1 April 2003		4,643	115,400	94,410	214,453
Charge for the year	2, 5	1,167	44,992	18,452	64,611
Released on disposal		–	(94)	–	(94)
At 31 March 2004		5,810	160,298	112,862	278,970
Net book value at 31 March 2004					
		7,037	366,001	39,758	412,796
Net book value at 31 March 2003		7,819	382,597	46,092	436,508

The net book value of tangible fixed assets held under finance leases by the Group at 31 March 2004 was £95,000 (2003: £3,128,000). The charge for depreciation against these assets during the year was £3,133,000 (2003: £190,000) which includes asset impairment charges of £2,938,000 (Note 2).

Notes to the Accounts

for the year ended 31 March 2004

11 Investments

(a) Company

	Subsidiary undertakings
	2004 £'000
Cost and net book value	
At 1 April 2003 and 31 March 2004	56,963

The investment in subsidiary undertakings represents an investment in shares of £56,963,000.

Details of the Company's subsidiary undertakings at 31 March 2004 are as follows:

Company	Country of incorporation	Class of share	Proportion of shares held	Principal activity
THUS plc	Scotland	Ordinary	100%	Voice, data, Internet and contact centre services provider
Demon Internet, Inc*	USA	Ordinary	100%	US Internet peering management
THUS Profit Sharing Trustees Limited*	Scotland	Ordinary	100%	Trustee

* The investment in these companies is held by a subsidiary undertaking.

(b) Group

The number of own shares, held as fixed asset investments by the Group, as at 31 March 2004 was 17,600,525 (2003: 18,930,284). These shares were previously treated as a current asset investment and valued at the lower of cost and net realisable value, being mid-market price at the balance sheet date. Due to a general uplift in the market price of the Company's shares during the year a credit of £1,740,000 (2003: charge £1,325,000) has been recognised as amounts written back to investments in the Profit and Loss Account.

At the 31 March 2004 the Directors took the decision to reclassify the own shares held under Trust from current asset investments to fixed asset investments to reflect the fact that these shares will now be used to satisfy share options.

The nominal value of all shares held as fixed asset investments as at 31 March 2004 was £440,013 (2003: current asset investment £473,257).

12 Stocks

	Group		Company	
	2004 £'000	2003 £'000	2004 £'000	2003 £'000
Raw materials – replacement parts and consumables	3,125	2,867	–	–

13 Debtors

	Group		Company	
	2004 £'000	2003 £'000	2004 £'000	2003 £'000
Amounts falling due within one year:				
Trade debtors	64,395	63,982	–	–
Prepayments and accrued income	28,786	26,187	–	–
Other debtors	317	668	–	–
	93,498	90,837	–	–
Amounts falling due after more than one year:				
Trade debtors	3,471	–	–	–
Total debtors	96,969	90,837	–	–

14 Other creditors

	Group		Company	
	2004 £'000	2003 £'000	2004 £'000	2003 £'000
Trade creditors	43,844	36,346	–	–
Corporation tax	824	612	–	–
Taxation and social security	2,072	3,802	–	–
Capital creditors and accruals	7,126	3,852	–	–
Other creditors	3,488	1,736	87	87
Accruals and deferred income	42,880	49,163	–	–
Amounts due to subsidiary undertakings	–	–	540	540
	100,234	95,511	627	627

15 Loans and other borrowings

		Group		Company	
	Notes	2004 £'000	2003 £'000	2004 £'000	2003 £'000
Secured credit facilities	(a) (i)	53,987	35,983	–	–
Other loans		600	600	–	–
Finance leases	23	4,175	4,200	–	–
		58,762	40,783	–	–

Repayments fall due as follows:

Within one year, or on demand	1,583	117	–	–
After more than one year	(a) (i)	57,179	40,666	–
		58,762	40,783	–

Repayments due after more than one year are analysed as follows:

Between one and two years	12,203	1,728	–	–
Between two and five years	44,689	39,467	–	–
After five years	3,300	3,488	–	–
	60,192	44,683	–	–
Less: unamortised issue costs	(3,013)	(4,017)	–	–
	57,179	40,666	–	–

15 Loans and other borrowings continued

(a) Analysis of loans and other borrowings

	Note	Group		Company	
		2004 £'000	2003 £'000	2004 £'000	2003 £'000
Other borrowings:					
Secured credit facilities	(i)	53,987	35,983	-	-
Other loans		600	600	-	-
Finance lease obligations		4,175	4,200	-	-
		58,762	40,783	-	-

(i) The secured credit facilities are stated net of unamortised issue costs of £3,013,000 (2003: £4,017,000). The credit facilities are secured by a bond and floating charge over the undertaking and all property and assets, present and future, of the Group and by a fixed and floating charge over the properties, plant, machinery and assets of the Group.

Under the terms of the facility £90,000,000 was available for drawing down until 1 April 2004, however, during the year this facility was reduced to £60,000,000. The facility is refinanced by an amortising term loan facility commencing on 1 April 2004 and maturing on 31 March 2008.

A further £17,000,000 was drawn down during the year giving a total drawdown at 31 March 2004 of £57,000,000.

The first repayment of £1,425,000, which is calculated as 2.5% of the outstanding amount, is payable on 31 March 2005. Subsequent repayments are due on a quarterly basis with the last repayment falling due on 31 March 2008. The value of the last repayment is calculated as 10% of the outstanding amount.

The interest rate applied to the loan facility is calculated as being the aggregate of an applicable margin, LIBOR and a mandatory cost, if any. The mandatory cost is defined as an addition to the interest rate to compensate the lenders for certain compliance costs.

The average interest rate charged during the year was 9.26% (2003: 8.94%).

(b) Finance lease obligations

	Group		Company	
	2004 £'000	2003 £'000	2004 £'000	2003 £'000
Falling due:				
Within one year	158	117	-	-
Between one and two years	203	128	-	-
Between two and five years	514	467	-	-
After five years	3,300	3,488	-	-
Amounts falling due after one year	4,017	4,083	-	-
Total	4,175	4,200	-	-

16 Derivatives and other financial instruments

(a) Financial instruments and risk management

(i) Overview

The main financial risks faced by the Group are funding and liquidity, counterparty and credit risk, interest rate risk and exchange rate risk; the Board has reviewed and agreed policies for managing each of these risks as summarised below. Speculative trading activities are not permitted.

(ii) Risk management

Funding and liquidity management

The Group's objective is to maintain continuity of funding for its operations using committed facilities and overdrafts and to maximise interest on surplus funds. Finance leases are also used where considered cost effective. A revolving loan facility, refinanced by a term loan facility was the Group's main source of funding during the current year. Drawdowns under the facility are subject to various financial covenants.

Counterparty and credit risk management

Cash placements and derivative transactions give rise to credit risk on the potential default of counterparties. The Group monitors the exposures and the credit rating of its counterparties regularly and uses limits to mitigate the credit risk that the Group may have with any one counterparty. It is not anticipated that any existing counterparties will fail to meet their current obligations.

Interest rate management

The Group's policy is to have a floating rate interest profile, with the exception of finance leases. The Group's borrowing facilities and investments are all at a Sterling LIBOR floating rate of interest. Only the interest flows connected to the secured credit facility are hedged and this policy has been applied throughout the year. To comply with the Group's secured borrowing facilities, an interest rate hedge must be in place. The Group is required to hedge interest on at least 50% of the principal loan outstanding. The costs of interest rate hedges are expensed as incurred. The current arrangement in place caps LIBOR at a minimum of 4.23% and a maximum of 6%.

Foreign exchange management

THUS faces currency exposures in Euros and US Dollars (USD) from operating activities generated in the Netherlands and United States and has fixed asset expenditure in Euros and USD. In addition, on consolidation, THUS is exposed to risk from the translation of net assets and profits earned in its US subsidiary. THUS does not hedge either the currency exposure on the operating activities to date, which are not considered to be material, or the translation exposure on consolidation as this is considered to be an accounting rather than cash exposure.

(b) Borrowing facilities

THUS had a revolving £90,000,000 facility provided by the Royal Bank of Scotland, Société Générale, Toronto Dominion Bank Europe Limited and Rabobank which was reduced to £60,000,000 on 28 May 2003. The facility was available to 1 April 2004 when it was then refinanced by an amortising term loan facility on 1 April 2004 with the same banks and matures on 31 March 2008. Repayments on the term loan will commence on 31 March 2005, with repayments increasing over time to March 2008. The facility and loan are subject to financial covenants, principally relating to EBITDA.

The purpose of the bank facility is to finance capital expenditure, working capital requirements and for general corporate purposes. As at 31 March 2004 £57,000,000 had been drawn down and, under the terms of the facility, no further drawdowns are possible.

The Group has the following undrawn committed borrowing facilities at 31 March.

	2004 £'000	2003 £'000
Expiring between one and two years	-	50,000

Notes to the Accounts

for the year ended 31 March 2004

16 Derivatives and other financial instruments continued

(c) Financial assets and liabilities

The only significant financial assets are the cash at bank and in hand with a net book amount of £26,421,000 at 31 March 2004 (2003: £12,143,000) of which £25,612,000 was denominated in Sterling (2003: £11,519,000), £670,000 was denominated in Euros (2003: £597,000) and £139,000 was denominated in US Dollars (2003: £27,000) and the long-term trade debtor of £3,471,000 which was denominated in Sterling (2003: £Nil).

The financial liabilities of the Group at 31 March 2004 are secured credit facilities of £57,000,000 (2003: £40,000,000), finance leases of £4,175,000 (2003: £4,200,000), and other loans of £600,000 (2003: £600,000).

The maturities of the Group's financial liabilities at 31 March were as follows:

	Debt £'000	Finance leases £'000	Other financial liabilities £'000	Total 2004 £'000
In one year or less, or on demand	1,425	158	-	1,583
In more than one year, but not more than two years	12,000	203	-	12,203
In more than two years, but not more than five years	44,175	514	-	44,689
In more than five years	-	3,300	-	3,300
Total financial liabilities	57,600	4,175	-	61,775
Unamortised issue costs	(3,013)	-	-	(3,013)
	54,587	4,175	-	58,762

	Debt £'000	Finance leases £'000	Other financial liabilities £'000	Total 2003 £'000
In one year or less, or on demand	-	117	-	117
In more than one year, but not more than two years	1,600	128	-	1,728
In more than two years, but not more than five years	39,000	467	-	39,467
In more than five years	-	3,488	-	3,488
Total financial liabilities	40,600	4,200	-	44,800
Unamortised issue costs	(4,017)	-	-	(4,017)
	36,583	4,200	-	40,783

For the purpose of the disclosures which follow in this Note, short-term debtors and creditors which arise directly from the Group's operations have been excluded as permitted by Financial Reporting Standard 13 "Derivatives and Other Financial Instruments: Disclosures" (FRS 13).

(d) The interest rate risk profile of the Group's financial assets and financial liabilities was:

(i) Financial assets

	Total £'000	Floating rate financial assets £'000	Fixed rate financial assets £'000	Weighted average interest rate %	Average period for which rate is fixed years
At 31 March 2004:					
Currency: Sterling					
- Cash at bank and in hand	25,612	25,612	-		
- Long-term trade debtor	3,471	-	3,471	5.2	3
Currency: Euros					
- Cash at bank and in hand	670	670	-		
Currency: US Dollars					
- Cash at bank and in hand	139	139	-		
Gross financial assets	29,892	26,421	3,471		

	Total £'000	Floating rate financial assets £'000	Fixed rate financial assets £'000	Weighted average interest rate %	Average period for which rate is fixed years
At 31 March 2003:					
Currency: Sterling					
- Cash at bank and in hand	11,519	11,519	-		
Currency: Euros					
- Cash at bank and in hand	597	597	-		
Currency: US Dollars					
- Cash at bank and in hand	27	27	-		
Gross financial assets	12,143	12,143	-		

The floating rate financial assets, in the current and prior year, comprise Sterling denominated cash at bank and in hand, Euro denominated cash at bank and in hand and US Dollar denominated cash at bank and in hand. The Sterling denominated cash at bank and in hand attracts interest based on LIBOR less an applicable margin and the Euro denominated cash at bank and in hand attracts interest based on EURIBOR less an applicable margin.

(ii) Financial liabilities

	Total £'000	Floating rate financial liabilities £'000	Fixed rate financial liabilities £'000	Weighted average interest rate %	Average period for which rate is fixed years
At 31 March 2004:					
Currency: Sterling					
- Secured credit facilities	57,000	57,000	-		
- Other loans	600	600	-		
- Finance leases	4,175	-	4,175	10	20
Gross financial liabilities	61,775	57,600	4,175		

	Total £'000	Floating rate financial liabilities £'000	Fixed rate financial liabilities £'000	Weighted average interest rate %	Average period for which rate is fixed years
At 31 March 2003:					
Currency: Sterling					
- Secured credit facilities	40,000	40,000	-		
- Other loans	600	600	-		
- Finance leases	4,200	-	4,200	10	20
Gross financial liabilities	44,800	40,600	4,200		

The floating rate liabilities, in the current and prior year comprise Sterling denominated secured credit facilities and other loans. The Sterling denominated secured credit facilities bear interest at rates based on LIBOR plus an applicable margin.

16 Derivatives and other financial instruments continued

(e) Fair values of financial assets and financial liabilities

The following table provides a comparison by category of the carrying amounts and the fair values of the Group's financial assets and financial liabilities as at 31 March 2004 and 31 March 2003. Fair value is the amount at which a financial instrument could be exchanged in an arm's length transaction between informed and willing parties, other than a forced liquidation sale and excludes accrued interest. Where available, market values have been used to determine fair values.

Notes	2004		2003	
	Book value £'000	Fair value £'000	Book value £'000	Fair value £'000
Primary financial instruments held or issued to finance the Group's operations:				
Financial assets				
Cash at bank and in hand	26,421	26,421	12,143	12,143
Long-term trade debtor	13 3,471	3,210	-	-

Financial liabilities

Borrowings:					
- Short-term	15	1,583	1,583	117	117
- Long-term	15	60,192	60,359	44,683	44,683
		61,775	61,942	44,800	44,800
Less unamortised issue costs		(3,013)	(3,013)	(4,017)	(4,017)
		58,762	58,929	40,783	40,783

The following methods and assumptions were used to estimate the fair values shown above.

Short-term deposits and borrowings – The fair value of short-term deposits, loans and overdrafts approximate to the carrying amount because of the short maturity of these instruments.

Long-term trade debtors – The fair value of the long-term trade debtor has been based on the discounted value of the future cash flows expected to be received.

Long-term borrowings – In the case of the new finance lease the estimated fair value was based on the book value as the finance lease was negotiated during the year. The fair value of the other finance leases has been based on the discounted value of the future cash flows expected to be paid out by the Group. The fair value of the secured credit facility approximates to the carrying value as the loan falls due for repayment in one to five years and the Directors consider it unlikely that there would be a significant variation between the fair value and the settlement value as the Group is marked at LIBOR rates.

(f) Currency exposure

The table below shows the extent to which Group companies have net monetary assets and liabilities in currencies other than their local currency. Foreign exchange differences on retranslation of these assets and liabilities are taken to the Group's Profit and Loss Account.

Functional currency of operation	Net foreign currency monetary assets/(liabilities)		
	US Dollar £'000	Euro £'000	2004 £'000
Sterling	(1,005)	319	(686)

Functional currency of operation	Net foreign currency monetary assets/(liabilities)		
	US Dollar £'000	Euro £'000	2003 £'000
Sterling	(1,219)	941	(278)

(g) Hedge accounting

Hedge accounting is only applicable for the tangible fixed asset purchases that are denominated in a foreign currency. The Group also has an interest rate hedge in connection with the secured credit facilities.

17 Provisions for liabilities and charges

Group	At 1 April 2003 £'000	Provided in the year £'000	Utilised during the year £'000	At 31 March 2004 £'000
Property	264	500	(25)	739
Restructuring costs	352	-	(352)	-
Balance at the end of the year	616	500	(377)	739

The property provision represents costs associated with the centralisation of the Glasgow and London offices.

The restructuring costs provision related to anticipated severance costs advised at 31 March 2003 but not actioned at that date.

18 Deferred taxation

Total potential deferred tax assets computed at the rate of corporation tax at 31 March 2004 of 30% (2003: 30%) are noted below. These assets have not been recognised as their future recoverability is not certain.

	Group		Company	
	2004 £'000	2003 £'000	2004 £'000	2003 £'000
Accelerated capital allowances	(34,747)	(21,875)	-	-
Other timing differences	(10,209)	(15,700)	-	-
Total deferred tax assets not recognised	(44,956)	(37,575)	-	-

19 Share capital

	Group and Company	
	2004 £'000	2003 £'000
Authorised:		
1,974,788,625 (2003: 1,974,788,625) ordinary shares of 2.5p each	49,370	49,370
Allotted, called up and fully paid:		
1,348,613,156 (2003: 1,348,613,156) ordinary shares of 2.5p each	33,715	33,715

Notes to the Accounts

for the year ended 31 March 2004

20 Analysis of movements in shareholders' funds

(a) Group

	Notes	Number of shares 000's	Share capital £'000	Merger reserve £'000	Capital redemption reserve £'000	Other reserves £'000	Profit and loss account £'000	Total £'000
At 1 April 2003		1,348,613	33,715	566,560	23,248	18,840	(234,951)	407,412
Retained loss for the year		–	–	–	–	–	(25,221)	(25,221)
Unrealised gains on fixed asset disposals	(i)	–	–	–	–	839	–	839
Transfer	(ii)	–	–	–	–	(979)	979	–
Currency translation differences on overseas net assets		–	–	–	–	–	(38)	(38)
At 31 March 2004		1,348,613	33,715	566,560	23,248	18,700	(259,231)	382,992

(i) The unrealised gains on fixed asset disposals represent sales made under Indefeasible Rights of Use arrangements during the financial year.

(ii) The transfer from Other Reserves to the Profit and Loss Account reserve represents the element of previously unrealised gains on fixed asset disposals attributable to the current year.

(b) Company

	Share capital £'000	Capital redemption reserve £'000	Profit and loss account £'000	Total £'000
At 1 April 2003 and 31 March 2004	33,715	23,248	(540)	56,423

(c) As permitted by Section 230 of the Companies Act 1985, the Company has not presented its own Profit and Loss Account. The Company's Profit and Loss Account was approved by the Board on 30 April 2004. The Company did not make a profit or loss during the current or prior year.

21 Analysis of cash flows

(a) Returns on investments and servicing of finance

	Note	2004 £'000	2003 £'000
Interest received		232	346
Interest paid		(3,059)	(2,812)
Interest element of finance lease rental payments		(374)	(383)
Expenses paid in connection with issue of debt		(150)	(5,564)
Net cash outflow for returns on investments and servicing of finance		(3,351)	(8,413)

(b) Capital expenditure and financial investment

Purchase of tangible fixed assets		(37,744)	(54,825)
Sale of tangible fixed assets		1,058	463
Receipt from sale of own shares		22	–
Net cash outflow for capital expenditure and financial investment		(36,664)	(54,362)

(c) Financing

Secured credit facilities	23	17,000	40,000
Other loans		–	(500)
Capital element of finance lease rental payments	23	(125)	(106)
Increase in debt	23	16,875	39,394
Net cash inflow from financing		16,875	39,394

22 Reconciliation of operating loss to net cash inflow from continuing operating activities

	Notes	2004 £'000	2003 £'000
Operating loss		(21,213)	(50,799)
Depreciation on tangible fixed assets	5	64,611	77,737
Amortisation of intangible fixed assets	2	165	165
Profit on disposal of tangible fixed assets	2	–	(66)
Movements in provisions for liabilities and charges		123	(284)
(Increase)/decrease in stocks		(258)	2,456
Increase in debtors		(6,248)	(7,961)
Increase in creditors		238	4,828
Net cash inflow from continuing operating activities		37,418	26,076

23 Analysis of net debt

Note	At 1 April 2003 £'000	Cash flow £'000	Other non-cash changes £'000	At 31 March 2004 £'000
Cash at bank and in hand	12,143	14,278	–	26,421
Loans – due within one year	–	–	(1,425)	(1,425)
Loans – due after one year	21c (40,600)	(17,000)	1,425	(56,175)
Finance leases	21c (4,200)	125	(100)	(4,175)
	(44,800)	(16,875)	(100)	(61,775)
Total	(32,657)	(2,597)	(100)	(35,354)

24 Pensions

The pension charge for the year comprises:

	2004 £000	2003 £000
Defined benefit scheme	2,845	2,067
ScottishPower defined benefit schemes to 1 August 2002	–	901
Defined contribution arrangements	201	100
ScottishPower defined contribution arrangements	–	76
Others	71	–
	3,117	3,144

The Company operates two pension schemes:

- the THUS Group plc pension scheme (“the Scheme”), a funded defined benefit scheme. The assets of the Scheme are held in a Trust Fund which is independent of the Group’s own assets.
- the THUS Group Personal Pension Plan, a funded defined contribution arrangement.

In determining the level of contributions required to be made to the Scheme and the relevant charges to the Group’s Profit and Loss Account, the Group has been advised by Watson Wyatt LLP, Actuaries and Consultants. The most recently published formal valuation of the Scheme was an initial valuation at 1 August 2002. The main assumptions adopted in making this valuation were as follows:

	Rates per annum
Future price inflation	2.5%
Return on new investments	6.6%
Increases in earnings	4.0%
Increases in pensions	2.5%

The pension costs for accounting purposes have been calculated using the same assumptions as those adopted for the initial valuation. At the valuation date the Scheme had just commenced and therefore had no assets or liabilities. The regular pension charge, calculated using the projected unit method of valuation was 1.5% of pensionable salaries, or £2,845,000 for the year.

Until 31 July 2002, the Group participated in four defined benefit pension schemes and one defined contribution pension scheme operated by the ScottishPower Group. The amount payable in respect of all schemes by THUS Group plc was defined in the Pensions Agreement between THUS plc and Scottish Power UK plc and was known as the Adjusted Regular Pension cost. The calculation was based on the percentage of ordinary shares in THUS held by ScottishPower and the regular pension scheme rate determined by the actuary for each pension scheme. Contributions for the defined contribution scheme were based on age and ranged from 3% to 5% of pensionable salaries. A charge of 1% of salaries was added to cover administration expenses for all schemes and paid to Scottish Power UK plc.

The benefits accruing to members of the ScottishPower pension schemes were transferred to the THUS Group plc pension scheme during the year, following election by the members.

Notes to the Accounts

for the year ended 31 March 2004

24 Pensions continued

FRS 17

Disclosures in accordance with the transitional arrangements for the implementation of FRS 17 are set out below. This information is for disclosure purposes only. Pension costs have been recognised in line with SSAP 24 as described above. The results of the actuarial valuation of the THUS Group plc Pension Scheme as at 31 December 2002, updated by the actuary to take account of the requirements of FRS 17 and to assess the assets and liabilities of the Scheme as at 31 March 2004, have been used in assessing the FRS 17 disclosures.

Scheme assets are stated at their market value at 31 March 2004 and 31 March 2003. A bulk transfer payment of an amount known at 31 March 2003 was paid to the Scheme from the ScottishPower pension arrangements after the end of the prior year. The Scheme's assets and liabilities as at 31 March 2003 were increased to take account of the payment of this sum and the associated transfer of members' benefits. The liabilities of the Scheme under FRS 17 as at 31 March 2004 and 31 March 2003, and the current service cost for the periods ending on those dates, were calculated using the Projected Unit method and the following financial assumptions:

	Rates per annum 31 March 2004	Rates per annum 31 March 2003	Rates per annum 1 August 2002
Future price inflation	2.7%	2.3%	2.3%
Discount rate	5.7%	5.6%	5.9%
Rate of increase in salaries	4.2%	3.8%	3.8%
Rate of increase in pensions in payment*	2.7%	2.3%	2.3%

* Pre April 1997 pension increases are in respect of pensions in excess of Guaranteed Minimum Pensions.

The assumptions used by the actuary are the best estimates chosen from a range of possible actuarial assumptions which, due to the timescales covered, may not necessarily be borne out in practice.

The Scheme is closed to new entrants. Under the Projected Unit method, the current service cost will increase as members of the Scheme approach retirement.

The assets of the Scheme and the expected rates of return at 31 March were:

	Long-term expected rate of return per annum at 31 March 2004	Value at 31 March 2004 £'000	Long-term expected rate of return per annum at 31 March 2003	Value at 31 March 2003 £'000
Equities	8.2%	20,786	8.2%	20,565
Bonds	5.4%	17,059	4.8%	5,017
Property	-	-	6.5%	1,598
Other	3.6%	9	3.6%	253

The fair value of the Scheme's assets which are not intended to be realised in the short-term, and may be subject to significant change before they are realised, and the present value of the Scheme's liabilities, which are derived from cash flow projections over a long period and are thus inherently uncertain, were:

Total market value of assets	6.9%	37,854	7.4%	27,433
Present value of liabilities of the Scheme		(40,600)		(30,764)
Deficit in the Scheme		(2,746)		(3,331)
Potential deferred tax asset		824		999
Net pension liability		(1,922)		(2,332)

The amount of this net pension liability would have a consequent effect on reserves.

The movement in the deficit in the Scheme can be analysed as follows:

	Year ended 31 March 2004 £'000	Year ended 31 March 2003 £'000
Deficit in the Scheme at the start of the year		—*
Contributions paid	2,845	2,067
Current service cost	(3,880)	(2,685)
Other finance income	469	—
Actuarial gain/(loss)	1,151	(2,713)
Deficit in the Scheme at end of year	(2,746)	(3,331)

* The Scheme commenced on 1 August 2002 with no assets and no liabilities.

Components of defined benefit cost

	Year ended 31 March 2004 £'000	Year ended 31 March 2003 £'000
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Analysis of amount that would fall to be charged to operating profit

Current service cost	3,880	2,685
Past service cost	—	—
Total charged to operating profit	3,880	2,685

Analysis of amount that would fall to be charged to other finance income

Interest on pension scheme liabilities	1,721	—
Expected return on assets in pension scheme	(2,190)	—
Net credit to other finance income	(469)	—

Total Profit and Loss charge before deduction of tax

	3,411	2,685
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24 Pensions continued

FRS 17 continued

Analysis of amounts that would be recognised in the Statement of Total Recognised Gains and Losses (STRGL)

	Year ended 31 March 2004 £'000	Year ended 31 March 2003 £'000
(Gain)/loss on assets	(4,821)	–
Experience loss on liabilities	770	2,713
Loss on change of assumptions (financial and demographic)	2,900	–
Total (gain)/loss recognised in STRGL before adjustment for tax	(1,151)	2,713

History of experience gains and losses

	Year ended 31 March 2004	Year ended 31 March 2003
(Gain)/loss on Scheme assets		
Amount (£'000)	(4,821)	–
% of Scheme assets at end of year	13%	–%
Experience (gain)/loss on Scheme liabilities		
Amount (£'000)	770	2,713
% of Scheme liabilities at end of year	2%	9%
Total actuarial (gain)/loss recognised in STRGL		
Amount (£'000)	(1,151)	2,713
% of Scheme liabilities at end of year	3%	9%

25 Financial commitments

(a) Group analysis of annual commitments under operating leases

	2004 £'000	2003 £'000
Leases of land and buildings		
Expiring within one year	191	548
Expiring between two and five years inclusive	1,207	812
Expiring in over five years	7,086	7,008
	8,484	8,368

Other operating leases

Expiring within one year	–	–
Expiring between two and five years inclusive	–	–
Expiring in over five years	170	170
	170	170

(b) Group capital commitments

Contracted but not provided	8,835	4,437
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26 Employee share schemes

The Company operates the THUS Group Performance Share Plan and the THUS Group plc Discretionary Share Option Scheme, details of which are included in the Directors' Remuneration Report.

In addition, the Company also recognises the importance of encouraging share ownership amongst all employees and to that extent, the Company operates the THUS Group plc Sharesave Scheme which provides the opportunity for employees to exercise options at the end of a savings contract. Options are exercisable, in normal circumstances, on completion of a three or five year save-as-you-earn contract as appropriate. No performance criteria are attached to the exercise of these options.

Closed Schemes

Prior to the establishment of THUS Group plc on the demerger from Scottish Power plc, THUS plc operated a number of share incentive plans pursuant to which awards over shares in THUS Group plc continue to subsist. No further awards will be made under any of these Schemes.

THUS plc Employee Sharesave Scheme

Under this Scheme, in normal circumstances, share options are exercisable on completion of a three or five year save-as-you-earn contract as appropriate.

THUS plc Executive Share Option Scheme

Options under this Scheme did not meet the associated performance condition and have now lapsed.

THUS plc Discretionary Share Option Scheme (2000)

The performance conditions described under the THUS Group plc Discretionary Share Option Scheme also apply to this Scheme. In addition, a grant over 2,000 shares was made to each employee (excluding Executive Directors), on 6 December 2000 without any performance conditions applying.

Notes to the Accounts

for the year ended 31 March 2004

26 Employee share schemes continued

(a) Summary of movements in share options in THUS Group plc shares which will be satisfied by new issue shares

Note	THUS Group Performance Share Plan (number of shares 000's)	THUS Group plc Discretionary Share Option Scheme (number of shares 000's)	THUS Group plc Sharesave Scheme (number of shares 000's)	Total (number of shares 000's)
Outstanding at 1 April 2003	7,104	7,495	11,501	26,100
Granted	–	–	6,729	6,729
Exercised	(i)	–	(99)	(99)
Lapsed	(400)	(1,088)	(2,199)	(3,687)
Outstanding at 31 March 2004	6,704	6,407	15,932	29,043

(i) The shares exercised during the year were satisfied using lapsed shares from the Employee Benefit Trust.

(b) Analysis of share options outstanding at 31 March 2004 which will be satisfied by new issue shares

	Date of grant	Number of participants	Number of shares (000's)	Option price (pence)	Normal exercisable date
THUS Group Performance Share Plan	27.03.02	3	1,954	£1 total consideration	Mar 2005
	11.02.03	3	4,750	£1 total consideration	Feb 2006
THUS Group plc Discretionary Share Option Scheme	27.03.02	41	6,407	16.25	Mar 2005 – Mar 2009
THUS Group plc Sharesave Scheme	01.05.02	635	9,505	14	May 2005 – May 2007
	13.06.03	512	6,427	11.75	Aug 2006 – Feb 2007

All options are exercisable over THUS Group plc shares.

27 Contingent liabilities

A contingent liability exists in respect of an amount of corporation tax on chargeable gains calculated as the difference between the market value at 30 September 1999 of the assets and liabilities of the ScottishTelecom Businesses acquired by THUS plc on that date and the indexed base cost of those assets and liabilities as at 30 September 1999, multiplied by the percentage rate of corporation tax applicable to the profits of the Company in the accounting period in which THUS plc ceased to be a member of the ScottishPower Capital Gains Tax group. Management estimated that such liability would be up to £570 million. Management's estimate was subject to the following principal uncertainties:

- (i) The rate of corporation tax applicable at the time of exit from the ScottishPower Group; and
- (ii) The valuation attributable to the acquired businesses by the Inland Revenue as at 30 September 1999.

The contingent liability may crystallise in the event that THUS plc makes a "chargeable payment" to any member of the ScottishPower Group where there is parental holding of at least 75% of the ordinary share capital (which for capital gains tax purposes would include participating Preference Shares where applicable) or vice versa, a payment is made to THUS by any member of the ScottishPower Group, again where the above shareholding relationship applies. The contingent liability expires on 19 March 2007.

A "chargeable payment" is defined as any payment made otherwise than for bona fide commercial reasons or forming part of a scheme of arrangement the main purpose or one of the main purposes of which is the avoidance of tax and which has to be an amount significant enough to change the valuation of either party. Management of both THUS and ScottishPower have put in place procedures to monitor and minimise the exposure.

THUS and ScottishPower have jointly agreed that neither party will make or agree to make any chargeable payment within five years of the date of the demerger. This agreement is governed by a Tax Indemnity Deed entered into between ScottishPower and THUS whereby voluntary acts or omissions that result in a chargeable payment being made, will not be indemnified by the innocent party.