

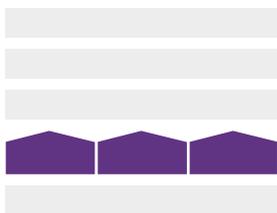
Review of the year

We announced that Jan du Plessis will join our Board on 1 June 2017 and become chairman of BT Group with effect from 1 November 2017.

 **PG106** to read more about our Board



Strategic progress



- Focused on improving customer experience across the group.
- EE integration is going well, we're ahead of target on first-year cost synergies.
- Restructuring announced, accelerating our cost transformation.
- Continued investment for growth and aspiration to become the UK's digital champion.

 **PG16** to read more about our strategy



Openreach

- Enduring and comprehensive agreement reached with Ofcom on future Openreach governance.
- Openreach board created with Mike McTighe appointed as Openreach chairman.
- Ofcom's investigation into the historical use of Deemed Consent by Openreach resulted in a £42m fine and c£300m of compensation payments that will be paid in 2017/18.

 **PG83** to read more about Openreach

Our investigation into our Italian business

£268m

prior years' adjustments

£260m

specific item charge

Adjustments relating to the investigation of our Italian business amount to £268m for errors in prior years, for which we've revised prior periods, and a specific item charge of £245m for changes in accounting estimates and investigation costs of £15m.

To respond, our actions have included:

- detailed balance sheet reviews in seven selected country operations in Global Services. Issue isolated to Italy;
- appointed a new CEO and CFO of our Italian business, as well as a new president of European operations; and
- reviewed and improved financial processes, systems and controls across the group.

 [PG6](#) to read more

Market environment

Headwinds in the UK public sector and international corporate markets.

Low interest rate environment increasing our IAS 19 pension deficit by £2.4bn net of tax.



EE integration

Cross-selling opportunities being realised

- Business mobile net adds up strongly over the year.
- Hundreds of thousands of EE customers taking BT Sport.
- Trial of selling BT products in EE stores has gone well.

c£150m per annum run-rate cost synergies achieved in first year

- Ahead of £100m target due to synergies being realised early.
- Early focus on renegotiating supplier terms, insourcing and estate rationalisation.

Taking the best of both cultures

 [PG93](#) to read more about the EE integration

100%

100% of EE calls now handled in UK and Ireland contact centres, and Consumer now at 86%

7.7m

premises connected to fibre broadband, 29% of those passed

53%

of retail broadband customers now on fibre

500,000

premises now built to with ultrafast broadband

30m

mobile customers using our network

18.6m

mobile customers using 4G

80%

UK's land mass now covered by 4G



BT Sport

BT Sport won exclusive rights to UEFA Champions League and UEFA Europa League until the end of 2020/21 season.



Global Services strategic review

We have undertaken a strategic review of Global Services, with the objectives of improving its market and financial performance, its risk profile, and the long-term value that it delivers to BT. Global Services is most differentiated with large, multinational customers, who demand high-quality, secure communications. Its product portfolio is industry-leading across a range of areas, including networking, security, cloud collaboration and contact centres.

Technology trends mean that we are now less dependent on owning physical local network access assets

around the world, creating the opportunity to reposition Global Services as a more focused digital business. We will prioritise innovation of cloud-based platforms that deliver our products and services, with BT's global network at the core, to support the digital transformation of our customers. As we implement this strategy, we will ensure that we optimise the value of our global and our local network assets.

To enable this strategic repositioning, we are restructuring our Global Services organisation to a simpler operating model. This will involve a two-year restructuring of our operations, the costs of which will be treated as a specific item.

Our investigation into our Italian business

What we found

In the summer of 2016 we received a whistle-blower report of inappropriate behaviours in our Italian business. We instigated an investigation, which included an independent review by KPMG LLP, with support and oversight from our Legal, Governance & Compliance function and Freshfields Bruckhaus Deringer, reporting directly to both the chair of the *Audit & Risk Committee* and BT Group chairman, and our own comprehensive balance sheet review, which revealed improper accounting practices and a complex set of improper sales, purchase, factoring and leasing transactions in our Italian business. The investigation identified collusion, circumvention and override of controls within our Italian business that was not identified by our monitoring controls thereby resulting in the misstatement of results going undetected for a number of years.

These activities resulted in the overstatement of profits amounting to £268m in our Italian business over a number of years. We concluded that the errors were not individually material to any of the group's previously issued financial statements; however, we did conclude that the correction of the full £268m in the current year would materially misstate the current year. To avoid this we corrected the errors by revising prior year income statements, balance sheets and cash flow statements. The effect of these revisions is set out in note 1 to the financial statements.

The findings from the investigation in Italy led us to review the carrying value of the assets and liabilities on the balance sheet, taking into account changes in facts or circumstances since 31 March 2016 and whether additional exposures had arisen due to events in the current year. This exercise required a level of judgement, in many cases taking a more cautious view based on our current understanding of circumstances surrounding each item. This exercise concluded that it was appropriate to write-down the value of our balance sheet assets and increase our balance sheet liabilities. The resulting charge of £245m is presented as a specific item in the current year.

Changes in facts or circumstance of items arising in the current year have been recorded in Global Services' current year trading results.

How we responded

The inappropriate behaviour in our Italian business is an extremely serious matter. It has no place in BT and we took immediate steps to improve the financial processes and controls in that business. We suspended a number of BT Italy's senior management team who have now left the business. The president of our European operations has also left the business.

We have appointed a new president of our European operations and a new CEO and CFO of BT Italy, from outside the Italian executive management team, and they are working hard to reposition and restructure the business for the future including implementing improvements to the governance, compliance and control culture and the capabilities of our people in the organisation.

To ensure independence, KPMG and our internal investigation team, with support and oversight from the Legal, Governance & Compliance function and Freshfields Bruckhaus Deringer, reporting directly to both the chair of the *Audit & Risk Committee* and

BT Group chairman, conducted an investigation of the systems and controls relating to our Italian business. We also conducted a broader review of financial processes, systems and controls across the group. We are acting on both the recommendations of KPMG and our own observations and have taken steps to improve our controls within Italy. We have also taken steps to enhance the wider controls that monitor our overseas operations in our shared service centres, Global Services and at a group level.

Beyond Italy, we have completed detailed balance sheet reviews in seven selected country operations in Global Services outside of the UK. These thorough reviews were supported by EY. Together with the investigation in Italy these covered around two-thirds by asset value of the operations outside the UK, representing 4% of the group's total assets. Our review did not identify any similar issues or areas of concern elsewhere giving us comfort that the inappropriate behaviours were isolated to Italy. This along with other additional substantive assurance activities that we have undertaken enables us to conclude that the financial results and balance sheet as of 31 March 2017 position give a true and fair view of the group.

As a result of our US listing we are required to make certain assessments of our controls as of 31 March 2017 for the purposes of the US Sarbanes-Oxley Act 2002 (Sarbanes-Oxley). Despite the remediation steps we took, the controls had not operated for sufficient time to allow assurance testing to confirm their effectiveness under Sarbanes-Oxley. We have therefore concluded for these purposes that our controls were ineffective as of 31 March 2017 due to a material weakness with regards to our Italian business.

The BT Group *Remuneration Committee* has also considered the wider implications of the BT Italy investigation; see page 122 for further details.

What we will do going forward

While we have taken steps to improve our control environment, we recognise we have more to do. We will continue to take steps to improve further our control, governance and compliance environment. These steps include increasing the resources and improving the capabilities of the controlling function and the audit function outside the UK, and further developing our integrated risk and assurance reporting processes. We are also enhancing our controls and compliance programme to strengthen awareness of the standards we expect, the capabilities of our people, and to reinforce the importance of doing business in an ethical, disciplined and standardised way.

The new CEO and CFO of BT Italy will continue to review the Italian management and finance teams and work with BT Group Ethics and Compliance to improve the governance, compliance and financial safeguards. Going forward, we will also continue to rotate senior management among countries to ensure an independently governed and rigorously controlled organisation throughout all parts of Global Services.

Deemed Consent

On 26 March 2017, Ofcom published the findings of its investigation into the historical use of Deemed Consent by Openreach. Deemed Consent is an agreed process between Openreach and its Communications Provider (CP) customers, which allows Openreach to halt the installation and reschedule the delivery date for providing dedicated business services (known as Ethernet) in a number of specific circumstances which are beyond its control. Ofcom found that Openreach had breached its contractual and regulatory obligations by inadequately and retrospectively applying Deemed Consent to reduce compensation payments to CPs between January 2013 and December 2014.

As a result of the findings, Openreach has agreed to compensate CPs and Ofcom has imposed a fine of £42m, reflecting the seriousness of the failings. This includes a 30% maximum discount for BT admitting its liabilities and agreeing to compensate the affected CPs in full. The precise amount of these compensation payments will result from discussions with the affected parties and is currently estimated at £300m. The fine and associated compensation payments are treated as a specific item charge in this year's income statement, with the cash expected to be paid in 2017/18.

We take this matter very seriously and we've put in place additional controls to safeguard against this happening again and to make sure that we're providing the highest standards in serving our customers.

Financial results

Proposed final dividend of 10.55p, up 10%, giving a full year dividend of 15.40p, also up 10%

	Year to 31 March 2017 £m	Change ^{a,b}
Reported measures		
Revenue	24,062	27%
Profit before tax	2,354	(19)%
Basic earnings per share	19.2p	(33)%
Adjusted measures		
Change in underlying revenue ^c excluding transit adjusted for the acquisition of EE	(0.2)%	
Adjusted ^d EBITDA	7,645	18%
Change in underlying EBITDA ^c adjusted for the acquisition of EE	(2.9)%	
Adjusted ^d profit before tax	3,532	5%
Adjusted ^d basic earnings per share	28.9p	(9)%
Normalised free cash flow ^e	2,782	£(316)m
Net debt	8,932	£(906)m

 **PG91** to read the Group Performance

 **PG20** to read our KPIs

Performance against 2016/17 outlook

In January we revised our outlook as a result of the pressures in the UK public sector and international corporate markets and the outcome of the investigation into our Italian business.

Outlook

Our outlook for 2017/18 is now as follows:

	2016/17 initial outlook	2016/17 revised outlook	2016/17 performance	2017/18 outlook
Change in underlying revenue ^c excluding transit	Growth	Broadly flat	(0.2)%	Broadly flat
Adjusted ^d EBITDA	c£7.9bn	c£7.6bn	£7,645m	£7.5bn - £7.6bn
Normalised free cash flow ^e	£3.1bn - £3.2bn	c£2.5bn	£2,782m	£2.7bn - £2.9bn
Dividend per share	≥10% growth	≥10% growth	15.40p, +10%	Progressive
Share buyback	c£200m	£206m	£206m	c£100m

^a The results for the period include EE which we acquired on 29 January 2016. Unless referred to as underlying adjusted for the acquisition of EE, comparatives only include EE from the date of acquisition.

^b Certain prior year results have been revised to reflect the outcome of the investigation into our Italian business. See note 1.

^c Excludes specific items, foreign exchange movements and disposals and is calculated as though EE had been part of the group from 1 April 2015. This differs from how we usually adjust for acquisitions as explained on page 252.

^d Before specific items, which are defined on page 252.

^e Before specific items, pension deficit payments and the cash tax benefit of pension deficit payments.

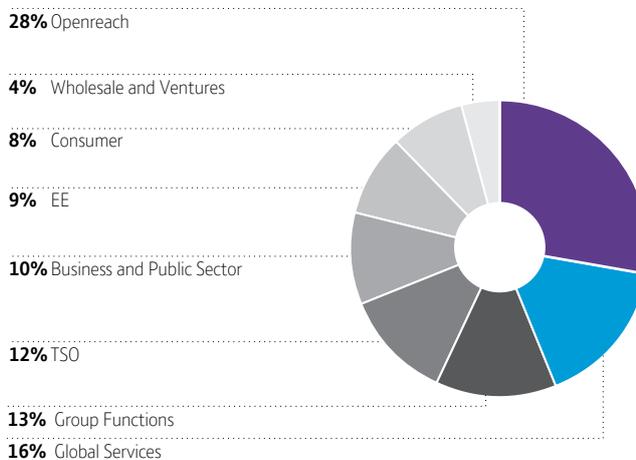
How we're organised

We have six customer-facing lines of business: Consumer, EE, Business and Public Sector, Global Services, Wholesale and Ventures, and Openreach.

They're supported by our internal service unit, Technology, Service and Operations as well as Group Functions.

 **PG56-90** to read more about our lines of business

Employees by division



Consumer

We're the largest provider of consumer fixed-line voice and broadband services in the UK.

We're also the second-largest provider of pay-TV sports channels in the UK and a leading innovator in broadcasting technology. During the year we secured an extension to our broadcast rights for the UEFA Champions League and the UEFA Europa League until 2021 which puts our business in a strong position.

2nd
largest provider of
pay-TV sports channels
in the UK



Openreach

We build the network that connects Britain's homes and businesses to the future.

We're responsible for providing services over the local access network, sometimes referred to as 'the last mile', as well as installing and maintaining the fibre and copper communications networks that connect homes and businesses.

26.5m

premises passed by
our fibre network



Business and Public Sector

We sell communications and IT services in the UK and the Republic of Ireland.

We've around 1.2m business and public sector customers and lead the field in fixed-voice, networking and broadband. We have three customer-facing units providing communications solutions and IT services to SMEs, corporates and public sector customers.

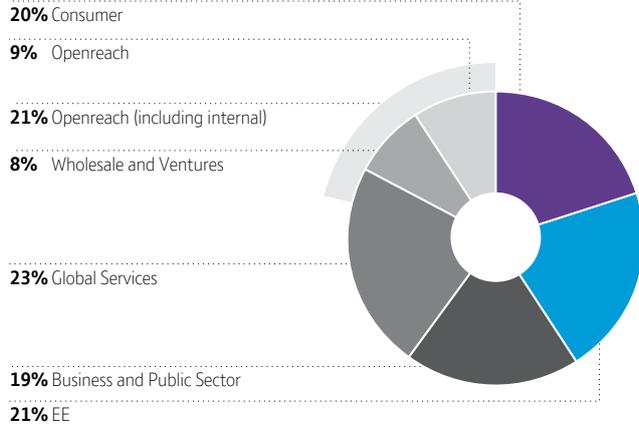
c1.2m

customers



Adjusted revenue^a by line of business

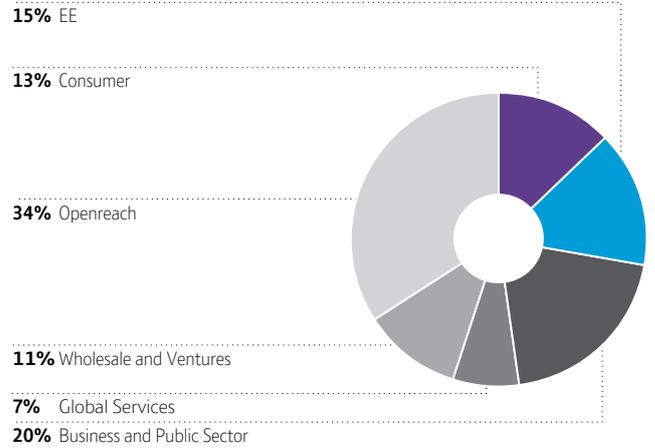
Year ended 31 March 2017



^a Before specific items.

Adjusted EBITDA^a by line of business

Year ended 31 March 2017



^a Before specific items.

EE

We're the UK's largest mobile network operator and we also offer fixed broadband and TV.

We employ 9,000 people with 67% directly helping customers through our shops and contact centres. Our 4G mobile network is the biggest and fastest in the UK.

80%

4G geographic coverage
(99% population coverage)



Wholesale and Ventures

We help other companies provide fixed or mobile telephony services, as well as running a number of BT's specialist business units.

We provide wholesale fixed network services to over 1,400 customers. We support 30 mobile virtual network operators. And our ventures provide mass market services such as directory enquiries and payphones, as well as enterprise services.

1,400

wholesale customers



Global Services

We're a leading global business communications provider, supplying ICT services to 5,500 multinational companies in 180 countries.

Our performance for the year has been impacted by the challenges in the international corporate markets and the outcome of our investigation into our Italian business. We will be implementing a new operating model in response to these challenges, explained on page 70.

180

countries served



Technology, Service and Operations

We're the internal technology unit responsible for creating and operating our global networks, platforms and IT systems.

We work closely with each of our lines of business, creating new products for them and making sure that services evolve to reflect the changing needs of their customers. And we make sure that BT's networks and systems are reliable and resilient. We also manage BT's research and development and our worldwide patent portfolio.

4,900

worldwide portfolio of patents and applications

