Delivering our strategy

In this section we explain our business model and how we create value for our shareholders. We set out the main inputs and outputs of the business, as well as the key outcomes – the impact that we have on our stakeholders, on society and on the environment.

We describe the importance of our people, our physical assets and the research and development that we do. We report on the status of our brands and outline our relationships with our main stakeholders, including regulatory bodies. Finally we describe how we go about mitigating the principal risks and uncertainties that affect us.

The section starts with an overview of the Operating Committee, its members and their responsibilities.

Our people
Their commitment, expertise and diversity are key to the success of our business.

Our global reach
We offer services across 180 countries. We have more than 21,000 people based outside the UK, across 60 countries.

Our research activities
We invest extensively in R&D to find better ways of doing things and to offer new services. Innovation is an important part of our history and key to our brand and our future.

Operating Committee

This is our key management committee. It meets weekly and is chaired by the Chief Executive. Brief details of its members are set out on these pages.

The Operating Committee has collective responsibility for running our business and delivering our strategy. It monitors the group's financial, operational and customer service performance and has cross-business oversight of the lines of business.

It also reviews the group's principal risks and considers the potential threats to, and opportunities for, the business. It:

- develops BT's strategy and budgets for the Board's approval;
- recommends to the Board capital expenditure and investment budgets;
- allocates resources across BT within plans agreed by the Board;
- prepares and delivers major programmes; and
- reviews the senior talent base and succession arrangements.

It can approve, up to certain limits set by the Board, capital expenditure, disposals of fixed assets, investments and divestments. It has delegated some of these approvals to sub-committees, such as the Design Council (page 30), and to senior executives. The Company Secretary attends all meetings.

Nigel Stagg, formerly CEO, BT Wholesale and Joe Garner, formerly CEO, Openreach (an invitee to the Operating Committee) both left during the year.


Gavin Patterson

Chief Executive

appointed as Chief Executive in September 2013 and on the Board since June 2008.

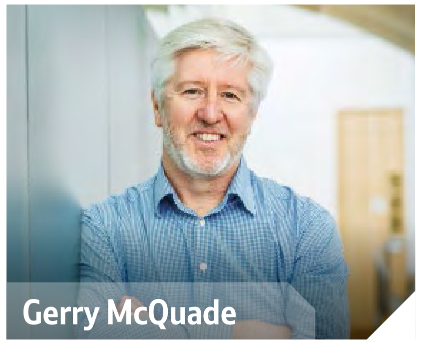
Gavin was previously CEO, BT Retail and from 2004 to 2008 was Managing Director, BT Consumer, BT Retail. Before joining BT, Gavin was managing director of the consumer division of Telewest (now Virgin Media). Prior to that, he spent nine years at Procter & Gamble, rising to become European marketing director.


Tony Chanmugam

Group Finance Director

appointed to the Board as Group Finance Director in December 2008.

Tony was formerly CFO, BT Retail, and Managing Director, BT Enterprises and, from 1997 to 2004, he was CFO and then Chief Operating Officer of BT Global Solutions. He is qualified as a Chartered Management Accountant.


Gerry McQuade

CEO, Wholesale and Ventures

appointed March 2016

Gerry was previously chief sales and marketing officer for EE Business, EE Business Wholesale businesses, and was responsible for all EE product development.

Gerry was chief development officer at Orange from January 2008, where he was key in overseeing the merger of Orange and T-Mobile. He was also one of the founding directors of Virgin Mobile and previously worked at Cellnet (now O2).


John Petter

CEO, Consumer

appointed September 2013

John was formerly Managing Director, BT Consumer, BT Retail and prior to that, Chief Operating Officer in BT Consumer. John was appointed chairman of the Plusnet Board in 2008 and has overseen its development as a key part of BT's strategy.

Prior to joining BT, John held roles as marketing and commercial director at Telewest (now Virgin Media) and brand manager at Procter & Gamble.


Graham Sutherland

CEO, Business and Public Sector

appointed September 2013

Graham was formerly Managing Director, BT Business, BT Retail, responsible for the small and medium-sized enterprises unit within BT Retail and prior to that, CEO of BT Ireland.

Before joining BT, Graham held a number of senior management positions including managing director of NTL in the Republic of Ireland. Graham is qualified as a Chartered Management Accountant.


Marc Allera

CEO, EE

appointed February 2016

Marc was formerly chief commercial officer for EE, responsible for all commercial activities across a multi-channel operation including digital, retail, telesales and customer base management. Prior to EE, Marc spent ten years at Three UK where he held a number of senior positions, including chief commercial officer and sales and marketing director.


Luis Alvarez

CEO, Global Services

appointed October 2012

Luis was formerly president of the European, Middle East, Africa and Latin America operations of BT Global Services serving some of our biggest global customers. Luis also led BT Global Services Telecom Markets unit, managing business with carriers and operators outside the UK.

Before joining BT, Luis worked at Ericsson, IBM and Group Santander. Luis has a telecommunications engineering degree.

Dan Fitz

Company Secretary

Dan is the Group General Counsel & Company Secretary of BT Group plc. He joined BT in April 2010 as its Group General Counsel and was appointed Company Secretary in November 2012. Dan previously spent six years at Misys and 12 years at Cable & Wireless.

Clive Selley

Invitee, CEO, Openreach

Clive was appointed CEO, Openreach in February 2016. He was formerly CEO, BT Technology, Service & Operations, CEO BT Innovate & Design and before that President, BT Global Services Portfolio & Service Design. He is an 'invitee' because the CEO of Openreach cannot be a member of the Operating Committee under the provisions of the Undertakings.


Howard Watson

CEO, Technology, Service & Operations

appointed February 2016

Howard was formerly chief architect and Managing Director global IT systems and led the technical teams behind the launch of BT Sport in 2013.

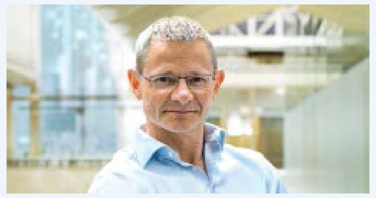
Howard joined BT in 2011 and has 30 years of telecoms experience having spent time at Telewest (now Virgin Media) and Cartesian, a telecommunications consultancy and software company.


Alison Wilcox

Group HR Director

appointed July 2015

Alison was formerly Regional HR Director for Vodafone Europe and prior to that, Regional HR Director for Vodafone's Africa, Middle East and Asia Pacific footprint. Alison joined Vodafone in 2006 as Group Director of Leadership following a career in consulting.



Simon Lowth

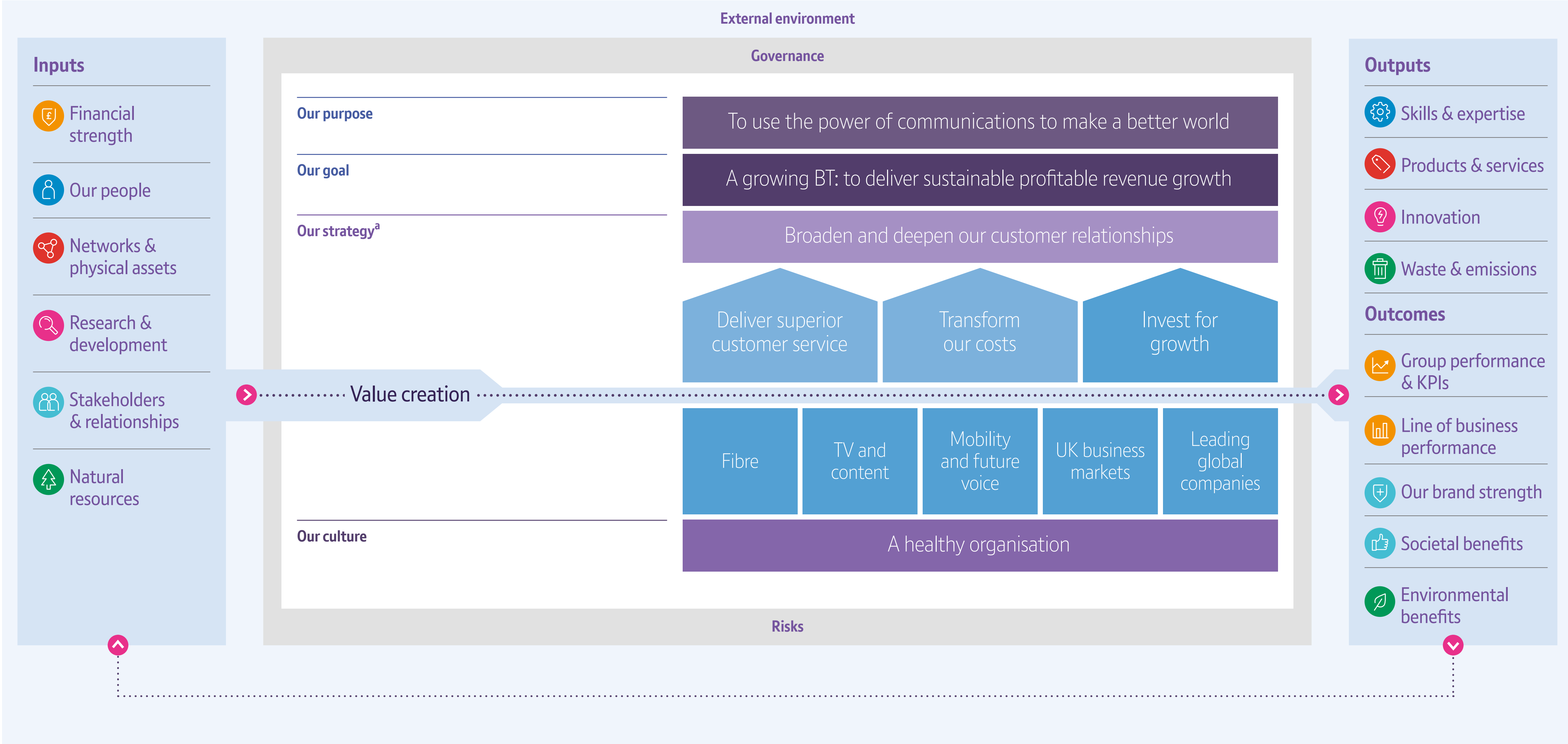
Group Finance Director designate

Simon will join BT on 4 July 2016 as Group Finance Director designate and an Operating Committee member.

Our business model

We create value for shareholders by developing and selling services that are important to our customers and that benefit communities, the environment and society as a whole.

We invest to build and maintain communications networks in the UK and overseas; we develop products and services that run over those networks; and then we sell them to consumers, businesses and the public sector. By selling these services, we're able to make a return on our investments. This means we can reinvest in the business to create value for our stakeholders over the short, medium and long term. A virtuous circle.



[a] For 2016/17 our strategy is evolving (see page 21).

In this Annual Report, coloured icons show the linkage between our business model inputs, outputs and outcomes (the impact that we have on our stakeholders, on society and on the environment).

You can find the inputs, outputs and outcomes for each of our lines of business from page 57.

This key provides a mapping to the 'capitals' of the IIRC's Integrated Reporting (IR) Framework.

IIRC capitals key

Financial	Intellectual
Human	Social
Manufactured	Natural

You can find out more about the IR Framework at: www.theiirc.org

Inputs

Financial strength
We're focused on growing our cash flow over the long term. Together with a prudent financial policy and a strong balance sheet, we can invest in our business and the things that set us apart from our competitors. Read more on page 31

Our people
We have 102,500 people. Their commitment, expertise and diversity are key to the success of our business. Read more from page 31

Networks & physical assets
Our networks and platforms are the foundations of the products and services we sell. We continue to invest in these to improve the service we offer our customers. Read more from page 34

Research & development
We're one of the largest investors in research and development in the UK. Read more from page 36

Stakeholders & relationships
Key stakeholders include our customers, communities, shareholders, lenders, our pension schemes, suppliers, government and regulators. Read more from page 38

Natural resources
We use some natural resources in doing business. Our energy use has declined for the seventh consecutive year. Read more from page 43

Outputs

Skills & expertise
We invest in our people so they can do their jobs better and are more engaged. And we encourage them to volunteer to benefit the communities we serve. Read more from page 31

Products & services
Our products range from fixed and mobile telephony, TV and broadband services for UK individuals and households, through to managing the networks and communications needs of some of the world's leading multinational companies. Read more from page 57

Innovation
We have a long history of innovation. It helps us offer new and improved products and services, find better ways of doing things and can generate valuable intellectual property for us. Read more from page 36

Waste & emissions
Our operations produce some waste and emissions; we're working to minimise these. Read more from page 43

Outcomes

Group performance & KPIs
The group's financial results and our progress against our KPIs are the key measurable outcomes of what we do. Read more from page 93

Line of business performance
Our lines of business sell our products and services and put our strategy into action. Read more from page 57

Our brand strength
Our brands are a key asset. Our investments in areas such as BT Sport have increased the value of the BT brand. And the EE brand gives us strength in mobile. Read more on page 37

Societal benefits
We're increasing digital inclusion and helping people get the most from being online. Our people and platforms support a number of good causes. Read more from page 38

Environmental benefits
We help our customers and suppliers reduce their waste and carbon emissions. Read more from page 43

Who we are

We're one of the world's leading communications services companies.

Where we operate

We're based in the UK but we serve customers across 180 countries (see page 59).

How we make money

The main output of our business is our portfolio of communications products and services. We make money by selling these in the UK and around the world through our customer-facing lines of business.

We sell through a range of channels including online, contact centres and account managers. And, following our acquisition of EE, we now have around 560 EE shops in the UK.

Our revenue is mostly subscription or contract-based. Individuals, households and SMEs pay for standalone or bundled services, typically on 12 to 24-month contracts. Large corporate and public sector customers usually buy managed networked IT services on contracts spanning several years. Our wholesale customer contracts range from one month in length for regulated products, to five years or more for major managed services deals.

But it's not just about the money

There's much more to what we do than just making money. What we do matters. We help millions of people communicate, be entertained, do business and generally live their lives. We help our customers reduce their carbon footprint. And we contribute directly to communities and the health of the UK by providing jobs, working with suppliers and paying tax, and through our employees' volunteering activities.

All of which contribute to the strength of our brands – which can influence whether a potential customer buys from us or one of our competitors.

Our approach

Our focus on delivering superior customer service, transforming our costs and investing for growth is central to what we do. They are key business activities. Better customer service means that we spend less time and money putting things right. These cost reductions, combined with savings from working more efficiently and the cash we generate from sales, mean we can invest in the future of our business.

Some investments, such as sports rights, have a lifespan of just a few years. Other investments, such as our fibre broadband network, are much longer term and can have 'pay-back' periods stretching to more than ten years.

Delivering our strategy is as much about how we do things, as what we do. That's why being a healthy organisation (see page 33) and living our values (page 31) are so important to us. And that's why our people are key to our success.

What sets us apart

We have a strong combination of people, technology, networks and other physical assets that set us apart from our competitors. Our research and development (R&D) activities are crucial to us – and to wider society. We have pioneered innovation in the telecoms arena, and our R&D supports new ways of doing things and advancements in our technology.

Importantly, we have the financial strength to invest in these areas to stay ahead of the competition.

A flexible and sustainable business model

Communications markets are dynamic and very competitive, particularly in the UK. There are risks and opportunities. Our Enterprise Risk Management framework (see page 46) helps us identify and mitigate the challenges and risks we face. And we do an annual materiality review to understand the societal and environmental issues that are important to our stakeholders.

We have a flexible and sustainable business model, enabling us to anticipate and respond to changes in our markets. It underpins our assessment of the future prospects and viability of the Group (see page 54).

We see more and more demand for our products and services because they play such an integral role in modern life. We use 'insight' teams to make sure we stay in tune with market developments and customer expectations. And we use governance committees, such as the Design Council, to make sure we're making the right investments. So we're confident that we'll be able to deliver value over the short, medium and long term.

Design Council

The Design Council is a sub-committee of the *Operating Committee* (page 26). It normally meets monthly. It is collectively responsible for aligning our capital investments in our networks, systems, platforms and products so that they are directed towards achieving our overall purpose and strategy, serve the needs of all of our customers and are delivered in a cost-effective manner.

Financial strength

We have the financial strength to make bold decisions and to invest in the things that set us apart.

Our goal is to deliver sustainable profitable revenue growth. Together with further transformation of our costs, we aim to grow our EBITDA and cash flow over the long term.

We have a prudent financial policy and strong governance over our decisions to make investments, manage our debt and grow our business, and over how we reward those who work for us and invest in us.

To build our business, we will continue to make bold decisions and be prepared to make strategic investments.

At the same time as investing in our five strategic growth areas (see page 24), we intend to reduce our net debt (which increased after our acquisition of EE).

We'll also continue to support the pension fund and to do so in a responsible way. And we'll pay progressive dividends to our shareholders.

Our financial strategy has been consistent for a number of years:

Deliver sustainable profitable revenue growth

Grow EBITDA

Grow free cash flow

Invest in business	Reduce net debt	Support pension fund	Pay progressive dividends

This approach gives us the financial flexibility to make long-term investments in the best interests of the company and our stakeholders; and also in the best interests of communities where we operate.

Our financial strength has underpinned the investments we've made in BT Sport in recent years, and which we'll continue to make in the years ahead. And it meant that in January 2016 we were able to complete the acquisition of EE, the leading mobile network operator in the UK.

It means we can invest over £3bn to help take fibre broadband to 95% of the country by the end of 2017, with plans to go even further. And with the right investment and regulatory environment, we'll invest in ultrafast broadband to 10m premises (with an ambition of reaching 12m) by the end of 2020.

It also means we can support the business in other ways. For example, by making sure we continue to innovate and stay at the forefront of a rapidly-changing industry. And by investing in the training, development and support we give to our people.

Our people[a]

Every day our people touch the lives of millions, providing products and services which are essential to the fabric of today's society – underpinning everything from global trade and industry to economic growth and social infrastructure.

They are at the heart of our ambition to deliver an excellent customer experience and sustainable profitable revenue growth.

Believing in what we do

A clear purpose guides everyone's contribution in BT. By bringing together the best networks, technology and products and services for our customers, we use the power of communications to make a better world.

With EE joining the group, we've embraced the opportunity to combine the best of both cultures. Creating possibilities for employees is at the heart of this and is a common theme across our employer brand pillars:

Making a better world together	Go anywhere, do anything	Bringing ideas to life	Simplifying complexity
Join a community dedicated to making a difference in the world	Find a world of diverse, exciting career opportunities	Be the best you can be and explore your inventiveness	Transform complex technology to make our customers' lives easier

During the year we had five values to guide our people: Customer, Team, Honesty, Change and Pride. But we're changing as a business so feel the time is right for a refreshed set of shared values. We asked our people what they thought. We asked our customers too – they said they want us to understand their needs, be easy to deal with and show we care. So from next year our values will be: Personal. Simple. Brilliant.

[a] Unless stated otherwise, figures in the Our people section exclude EE.

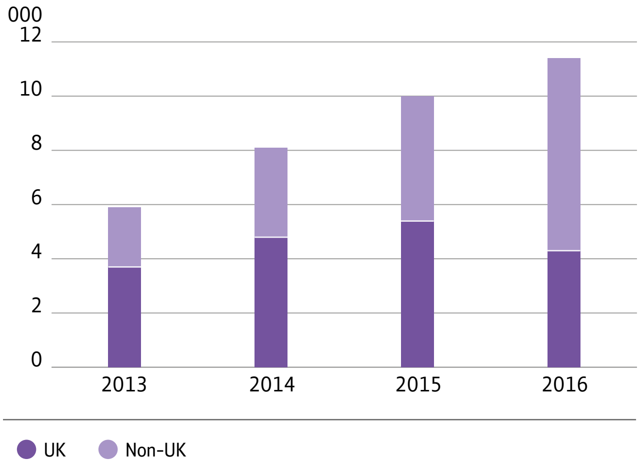
A global workforce

At 31 March 2016 we had 102,500 full-time equivalent (FTE) employees in 61 countries, with 81,400 of them based in the UK. This includes 12,800 who joined the group as part of EE.

We're one of the largest employers in the UK, supporting its economy by providing jobs and income.

This year, excluding acquisitions, we recruited nearly 11,400 people, bringing fresh ideas and new approaches to help us innovate, learn and improve. Of these, more than 4,200 are in the UK.

External hires (full-time equivalents)
Year ended 31 March



We continued to transform our HR function, reviewing our systems, processes, policies and services. This has allowed us to simplify further the way we work and to improve the service our HR team offers our people.

As our business evolves to meet the needs of our customers, we adapt our organisation, redeploying people through the BT transition centre. This helps us avoid redundancies. Last year in the UK, 1,000 people were redeployed, meaning that we retained experienced people with the skills we need for the future.

Recruiting talented people

A customer-connected workforce

Improving the quality of our customer relationships is at the heart of our people strategy.

We've built on previous years, recruiting 900 new field engineers and more than 900 new people to work in customer-facing roles – in our UK contact centres. We've also converted 600 agency workers to permanent employees, so that we keep their skills and experience in the organisation.

Highest-ever graduate intake

In 2015/16 we hired 300 graduates globally, our highest intake to date. We're planning on hiring around 300 again in 2016/17.

We were again in the top half of The Times Top 100 Graduate Employers. We're one of only four companies in the IT and telecoms sector to feature in the top 100.

Hiring more apprentices

We hired around 550 new apprentices into eight business operations, learning a range of skills. Demand for apprentices continues to grow so we expect to hire even more next year.

Investing for growth

Learning matters at BT. We create meaningful roles so that people understand what they are responsible for. We also invest in learning and development to allow our people to build skills and careers to deliver successfully for our customers. The BT Academy helps them do this.

The Academy is not a physical place or building, it's a combination of materials, events, and activities. It gives people easy access to the knowledge and skills they need, when they need it, changing the way they learn and develop. It is organised across four 'faculties'.

The Academy			
Business	Customer	Leadership	Technical

Each faculty supports a number of communities we call 'professions', providing both structured learning and ways to connect and share with others.

We're very pleased with how the Academy has done in its first full year. Across the world employees used the Academy website over 400,000 times. Over 20% of our people each month are now sharing information and ideas as well as accessing learning materials online.

The tools we've developed have won awards – gold for Internal Learning Solution of the Year at the Learning and Performance Institute Annual Learning Awards 2016, and silver for Best Use of Technology in Learning at the Training Journal Awards 2015.

This year has seen many success stories culminating in the National Apprenticeship Finals in January 2016 where we had two finalists. We also won the Scottish SDS Macro Apprentice Employer Of The Year Award.

Preparing young people for employment

With growing demand for digital skills in the UK, we feel well-placed to help create a future supply of suitably-skilled people, helping both our own business and the national economy, and creating a brighter future for the country's youth.

Our 2020 ambition

Help 5m children to receive better teaching in computer skills

5m

Creating a culture of tech literacy

We've made a long-term commitment to help build a culture of tech literacy. As our first goal, we want to help 5m children by the end of 2020.

We're doing this by:

- **Inspiring Kids** to connect with exciting and relevant tech concepts;
- **Enabling Teachers** to feel confident to teach young people about tech in computing lessons; and
- **Equipping Schools** to be able to use technology effectively.

We're working with our partners – the British Computer Society and the National Schools Partnership – to deliver the Barefoot Computing Programme, which helps primary school teachers across the country deliver the new computing curriculum. Over the 2014/15 school year we supported 12,500 teachers, helping to give around 340,000 children better teaching in computer science. We're on track to reach a further 15,000 teachers and 400,000 children by the end of the 2015/16 school year.

Getting young people 'Work Ready'

We're a founding partner of Movement to Work, a voluntary collaboration of UK employers committed to tackling youth unemployment. Our Work Ready programme helps 16–24 year-olds get better prepared for work, building both confidence and their core employability skills. It often supports people from disadvantaged backgrounds.

Our traineeship programme is at the heart of our strategy. Those not currently in education, employment or training can join BT for seven weeks of skills development and work experience. So far over 1,000 young people have taken part in this initiative, with more than 600 gaining recognised certificates in work skills and business administration. Many go on to get jobs, either in BT or elsewhere.

The Prince's Trust

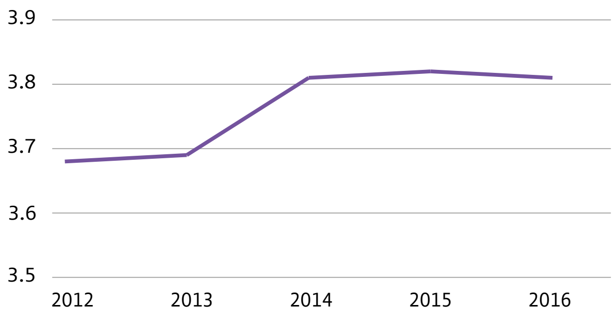
BT is part of The Prince's Trust Technology Leadership Group, which helps thousands of young people turn their lives around each year. We've donated use of the BT Tower as a venue for the Trust's annual ICT Leaders Dinner for the last ten years – raising £96,000 in 2015.

Engaging our people

We continue to focus on the health of our organisation. From the rapid expansion of our Academy, through to the business initiatives that are driving 'Continuous Improvement' across BT, we are investing in a culture of strong employee engagement.

This also benefits our customers. We believe that highly-engaged employees provide the best experience for customers, helping us to broaden and deepen our relationship with them.

Employee engagement index
Year ended 31 March



Challenge Cup

Challenge Cup is our key people engagement programme. It's an annual competition that started in 2003.

It encourages people to form teams and come up with insights and new initiatives, including ideas for changing business processes.

The aim of the Challenge Cup is to improve customer experience while generating ideas for creating growth and saving money for BT. This year over 4,300 people came together to form over 900 teams across 24 countries. The number of people participating has increased year on year, with 67% of those involved this year doing so for the first time.

Twice a year, more than 72,000 people provide feedback on working for BT through our employee engagement survey. It helps us develop a focused people strategy and support action planning at a local level. Engagement levels have remained stable for the last two years at just over 3.8 (out of a maximum of 5, with a telecoms benchmark of 3.95).

We keep our people informed about company results, major business decisions and other things that affect them using a variety of digital channels. Leaders regularly connect with their teams through roundtable meetings, town hall debates, site visits, webcasts and blogs.

We consult with our people or their representatives on a regular basis, taking their views into account on decisions that affect them. In the UK we recognise two main trade unions. The Communication Workers Union represents people in engineering, administration and clerical positions. Prospect represents managerial and professional people.

Diversity at work

Diversity is part of our heritage – as far back as 1880 Henry Fawcett, who was blind, was appointed Postmaster General.

Improving the mix of our people remains a priority and, in particular, we're encouraging more women to take up a career in technology. We're proud of our Tech Literacy programmes and events like the BT Young Scientist and Technology exhibition that target young women in education. We've run recruitment campaigns in Openreach to attract more women into engineering and redesigned our entry schemes to try to get rid of any unconscious bias.

19,000 women now work for us – many with flexible contracts. That's 21% of our workforce and there are more than 11,000 women in our management team (corresponding to 26%). We aim to have at least 25% female representation on our Board, and it currently sits at 27% (three out of 11 Board members). Our maternity return rate, measured one year after women come back, is 86%, well above the industry average.

Gender is only part of the story. Our aim is to create an inclusive culture that values all differences in people. Research shows that diverse teams are more innovative and can deliver a better experience to an equally diverse customer base.

This year we've focused on Inclusive Leadership training for senior management teams, specific programmes around working patterns and promoting our *#bettertogether* culture. The Race at Work report we sponsored with Business in the Community will set the direction for development programmes for our employees from black and minority ethnic backgrounds.

We are a 'Two Ticks'[a] employer and we actively encourage the recruitment, development and retention of disabled people. We'll automatically put an applicant with a disability or long-term health condition, who meets the minimum criteria for a vacancy, through to the first stage of a recruitment process. We're making progress on improving diversity but we recognise that there is a lot more we need to do.

Staying safe and well

We're committed to having no avoidable health and safety incidents. The 11% reduction in the rate of lost time due to injury brings us to our lowest-ever level. However, some of our activities are inherently hazardous and the risks, particularly in external engineering, remain challenging to manage. We've accepted some localised and historic failures raised by the Health and Safety Executive. We've done a lot to mitigate the risks highlighted and we still compare well with industry benchmarks.

We haven't done as well as we wanted on some indicators. Our sickness absence rate has risen by 5%, driven mainly by increasing levels of musculoskeletal and mental health conditions. We've measured our people's sense of wellbeing for some time. The long-term improvements we've seen were broadly flat this year, with a small increase of 0.5%. The pattern of sickness absence and wellbeing varies across the group and is strongly linked to the level of change taking place within a particular business area. We see the best results where changes have been well managed with a style that takes account of people's perceptions. We're sharing best practice on managing change across the lines of business and through the Academy.

We continue to focus on early intervention when people are sick or injured. Our company-funded schemes helped get 91% of people treated back into their role on full duties.

Volunteering

Our 2020 ambition

Inspire two-thirds of our people to volunteer some of their time

66%

Our people can use up to three working days a year on volunteering activities. As well as having a positive impact on society, our employee engagement survey (see page 33) shows higher engagement levels from those who volunteer than from those who don't.

Some people choose to help charities with particular issues needing their expert input and knowledge. Others use their energy and enthusiasm to make a practical difference in their local communities. That includes helping our tech literacy programme and promoting traineeships.

This year over 27% of our people spent nearly 45,000 days volunteering their time to support charities and community groups around the world. BT volunteers were involved in raising £8.5m for Children In Need and £2.9m for Sport Relief.

The EE business shares our passion for making a difference. It supports several charities through volunteering such as 'Apps for Good', in which young people use new technologies to design and make products that can make a difference to their world, gaining confidence and skills at the same time. Our combined contributions will benefit good causes in the years ahead.

Pay and benefits

We compare pay and benefits for our people with companies of similar size and complexity to ensure our remuneration is competitive.

In the UK, most of our engineering and support people are paid on terms and conditions negotiated through collective bargaining with our recognised trade unions, ensuring fair terms and conditions for all. Our managers' pay and any bonuses are determined by a combination of business performance and their personal contribution to the company.

Our executives may also receive long-term awards to reward the creation of shareholder value. The amount they ultimately receive is determined by the group's performance over a three-year period. Executive directors must retain incentive shares for a further two-year period.

In line with our regulatory obligations, incentives for people in Openreach are tied solely to a combination of personal contribution and Openreach's performance, rather than that of the wider group.

We support our people by providing a range of retirement savings plans. In the UK, our main defined benefit scheme is the BT Pension Scheme and our defined contribution scheme is the BT Retirement Saving Scheme. You can read more about these on page 107.

Sharing in success

Almost 60% of our people take part in one or more of our savings-related share option plans (saveshare), which operate in over 25 countries. In August 2015, almost 13,000 people in our 2010 saveshare plan were able to buy shares at 104p, representing an average gain of around £10,000 each.

Our networks and physical assets

Our networks, platforms and IT systems are the foundations of the products our customers rely on around the world.

Network platforms

Our global reach

Our global network provides service to 180 countries and is supported by in-country networks and infrastructure. Most of our network assets are in the UK and continental Europe. We continue to selectively expand the reach of our network to support multinational companies in other regions. And we use the expertise we gain from protecting BT's own networks, to help secure our customers' networks.

[a] Two Ticks is an accreditation that is given to organisations that are committed to employing disabled people.

The scale and reach of our global multi-protocol label switching (MPLS) network is a key competitive differentiator. This single IP-based network lets our lines of business launch products and services quickly and cost-effectively, without having to invest in dedicated infrastructure for each product.

To help our multinational customers connect their sites we offer virtual private network (VPN) services, which are integral to our 'Cloud of Clouds' vision (see page 60). VPNs provide the convenience and security of a private network, but over the public internet. We use our MPLS network together with a combination of owned and leased fibre connections to connect our points of presence (PoPs) around the world. For the final connection into the customers' premises, we either use our own circuits, or rent connections from telecoms operators in that country. We also have an extensive satellite network which provides customers with connectivity around the world, including remote locations.

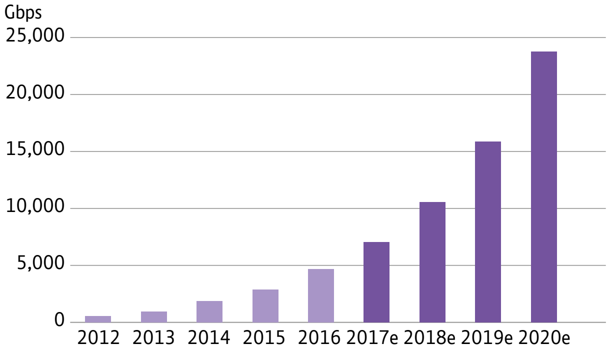
In-country networks

We have extensive networks in the UK, as well as in Germany, Italy, the Netherlands, the Republic of Ireland and Spain.

Our UK fixed-line network is one of our most valuable assets and our investment in fibre broadband is key to delivering modern, superfast services to UK consumers. To meet the demand from businesses, we're continuing to expand the availability of Ethernet. And when our customers are away from their home or office, they can use one of more than 5.6m BT Wi-fi hotspots.

Our research shows that over the last five years, at peak times, data traffic in the core network has grown by around 50% a year, and we expect growth to continue at a similar rate. So we're making sure that our core and access networks can cope with that demand.

Core network peak-time traffic
Year ended 31 March



As a result of buying EE, we now own the UK's largest mobile network. We'll continue to invest in its coverage and capability, to consolidate its position as the biggest and fastest in the UK. At the end of March 2016 outdoor coverage of the UK population was:

- over 99% for 2G;
- over 98% for 3G; and
- over 96% for 4G.

We want to expand 4G geographic coverage. This stands at 60% today, and we plan to get this to 95% by the end of 2020 with an ambition to go even further.

Between BT and EE, we have a combined 120MHz of paired mobile spectrum. This means we're able to offer speeds of up to 90Mbps in areas served by our 4G+ network.

We have access to over 18,500 basestation sites including those via the MBNL joint operation between EE and Hutchison 3G UK (see page 237).

Progress this year

This year we've:

- installed new, more cost-effective MPLS network routers in all 106 core exchanges in the UK;
- installed new Ethernet switches into 169 exchanges, so even more businesses can have access to BT Ethernet services;
- continued to roll out the latest technology, such as content caching so we can use network capacity better and speed up the delivery of TV and internet content; and
- integrated the technology to allow BT Global Services to offer a software-defined WAN service. This lets enterprise customers use different types of network together, and provide various services to their users seamlessly, as if over just one network.

Service platforms

We run a number of service platforms that combine our network and IT resources. They underpin many of the key products we offer.

One such platform is BT Conferencing, which provides audio and video conferencing services to customers around the world. Our audio conferencing service is called BT MeetMe and is available with Dolby Voice for higher quality sound and a better user experience.

Our BT TV platform supports a growing number of customers and we're increasing the range of services it delivers. We designed, developed and tested the new BT Ultra HD set-top box. We also launched our BT Sport app. It provides customers with functionality like goal replays, different camera angles and extra facts – all to enhance the viewing experience.

IT systems

Our IT systems let us manage our processes, handle customer information and deliver our products and services. They're critical to serving our customers and running our business.

For example, our customer management systems hold customer and billing information. They include the technology that works with our online customer portals. And the technology used when customers call a contact centre.

Progress this year

This year we've:

- delivered an integrated set of applications that we call Consumer.com. It's part of our focus on broadening and deepening our customer relationships. It means we've a much easier way for our customers and contact centre agents to manage customer accounts, and track orders and fault management. It has resulted in around 10,000 fewer calls to our contact centres each week;
- introduced 'View My Engineer' to help reduce missed appointments. A customer can use it to check details of scheduled engineer visits. It provides engineer contact details, indicates when the engineer is travelling to the appointment, when the work has been started and when the work has been done; and
- continued to innovate in our data centres – improving their performance and removing older server technology. For example, this year we started to roll out storage virtualisation which helps us store data more efficiently.

Properties

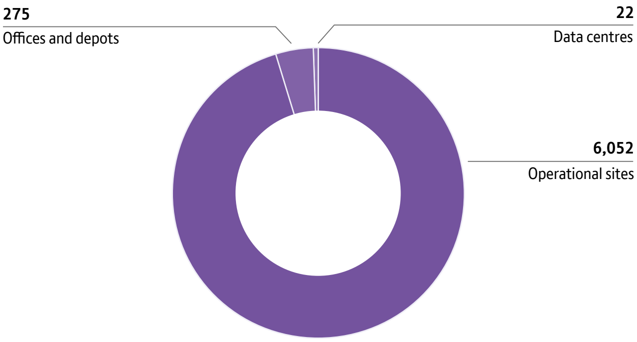
We have around 7,000 properties in the UK and 1,730 across the rest of the world. The number of properties in the UK is higher than the 6,350 we had last year, mainly reflecting our acquisition of EE in January 2016. Through this, we've added 635 properties, of which around 560 are EE shops. There are also around 40 former shops EE is in the process of disposing of.

We lease the majority of our UK properties from Telereal Trillium, part of the William Pears group. We signed a sale and leaseback arrangement with them in 2001. 88% of our UK properties are operational sites housing fixed and mobile telecoms and broadband equipment. The rest are retail outlets, offices, contact centres, depots and data centres. We also have our BT Sport TV studios in London.

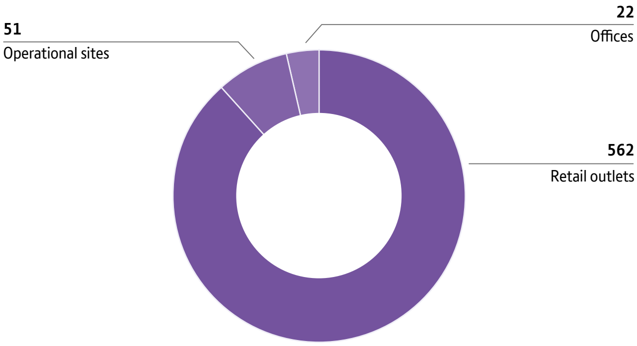
In the UK, we've been consolidating and disposing of surplus office space for several years and we're working on further opportunities to streamline our real estate. We continue to reduce the size of the operational estate as new fibre-based technologies mean we can dispose of buildings and make energy savings. This year we brought our property management activities back into BT from Telereal Trillium. This will reduce costs by simplifying how we manage our UK property portfolio.

Outside the UK, our offices in Gurgaon, Kolkata and Bengaluru in India are now home to our Central Business Services organisation. This provides support to our lines of business. As part of our strategy of investing in high-growth regions, we've expanded our offices in Budapest and Debrecen in Hungary – so we can support our global customers more effectively and efficiently.

BT property portfolio (UK)



EE property portfolio (UK)[a]



[a] Excludes leased cell sites.

Research and development

We invest in research and development (R&D) as we believe commercial success is ever more dependent on it. Our long history of innovation combines scientific breakthrough, practical engineering and commercial purpose. We call this 'purposeful innovation'.

Our innovation heritage

Our origins can be traced back to an entrepreneurial fusion of business and innovation. In 1837 Sir William Fothergill Cooke (a businessman) and Sir Charles Wheatstone (an academic) filed a patent for the world's first practical electric telegraph. This led to the founding of the Electric Telegraph Company in 1846, the seed company that eventually led to the formation of BT.

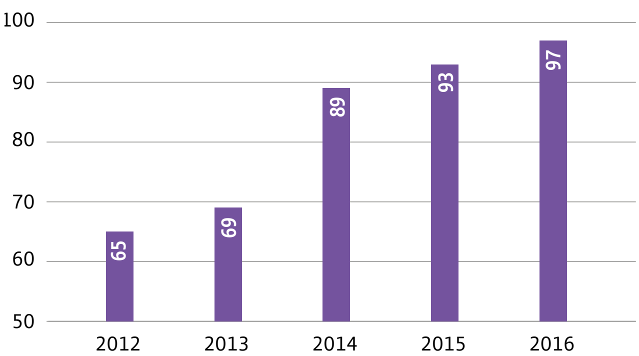
We've pioneered many of the technologies that we and customers now rely on. For example, in 1926 we established the world's first two-way, trans-Atlantic conversation by radio telephone, from our wireless station near Rugby. And in 1943 Tommy Flowers, working in the telecoms division of the GPO, developed the world's first programmable electronic computer, Colossus. In 1968, we installed the world's first digital telephone exchange. We laid the world's first, purpose-designed optical fibre submarine cable in Loch Fyne in 1980. And in 1984, we installed the world's first 140Mbps commercial single-mode optical fibre link. Our global IP Exchange platform (GIPX) was the result of one of our research projects. And more recently, we've led the industry in setting out our vision for widescale deployment of ultrafast broadband.

We sponsor the Information Age gallery at the Science Museum where many of our historical innovations can be seen, including parts from Colossus.

This year we invested around £470m (2014/15: around £500m) in research and development. Over the years we've been one of the largest investors in R&D of any company in the UK, and globally in the telecoms sector[b].

We've continued to grow the number of inventions we produce from our research activities. In 2015/16 we filed patent applications for 97 inventions (2014/15: 93).

Number of new invention filings
Year ended 31 March



We routinely seek patent protection in different countries, and at 31 March 2016 had a worldwide portfolio of around 4,700 patents and applications.

[b] Comparison based on total R&D spend over 2005/6 to 2014/15. Source: EU Industrial R&D Investment Scoreboard, http://iri.jrc.ec.europa.eu/scoreboard.html

Open innovation

We bring together expertise and resources (both our own and third-party) at our eight global development centres. Adastral Park in the UK is our technology headquarters. It's an innovation campus which we share with around 70 high-tech companies, and a workplace for around 3,700 people. This year we continued to grow our development centres in Kuala Lumpur and Bengaluru.

We're keen to work with people outside BT. We have extensive, long-standing, joint-research programmes with Cambridge University (UK), Massachusetts Institute of Technology (US), Tsinghua University (China), Khalifa University (UAE) and over 30 other universities globally.

Global innovation scouting

Our research teams work with customers and other companies in the US, Asia, Europe and the Middle East. And we've had people located at hotbeds of innovation such as Silicon Valley and Cambridge, Massachusetts for over 15 years.

These teams help us track the latest global developments in new technologies, business propositions and market trends. We've been finding new ways to support start-ups in Adastral Park and in London's Tech City. And through our BT Infinity Lab programme we partner with entrepeneurs to meet and co-innovate with start-ups from around the world.

Our people help us innovate. This year our internal New Ideas Scheme had more than 1,700 submissions. It's helping us provide a better service to our customers.

We run innovation showcases where business customers can discuss applications and solutions with our experts, and work with them on solving problems.

Under our communications programme, 'Ingenious', we're sharing BT's innovation story with thought-leaders, governments and the media. Examples of our research activities this year include:

G.fast speed improvements

We've been driving the standards for a new transmission system at the heart of our ultrafast broadband vision. This means we should be able to deploy ultrafast broadband far more quickly than previously thought possible.

XG-FAST trial

Working with Bell Labs, we've demonstrated speeds of 5.6Gbps over 35 metres of copper cable in lab conditions. This proves it's possible to achieve very high broadband speeds over existing infrastructure.

Long-reach VDSL

We've shown in the lab that we can take a 2km long copper line currently achieving 9Mbps with standard VDSL, and increase this to 24Mbps and beyond.

Future-proofing exchange operations

We've been improving the tools that our exchange-based engineering teams use for planning their work. We use artificial intelligence and mathematical modelling to better forecast, plan and schedule where people and equipment will be needed.

Quantum communications

We're also leading the world in demonstrating how quantum physics and optical engineering are on the cusp of providing much improved security for optical fibre systems. We've shown how a 200Gbps stream of encrypted data can be transmitted on the same 100km network link as a quantum encryption key. This work could offer enhanced security for the data networks of the future.

Brand and reputation

We own three strong brands: BT, EE and Plusnet. These are at the heart of our efforts to broaden and deepen our customer relationships. The experience our customers have is shaped not just by the service our front-line teams provide, but by everything we do: from the products and propositions we design, to the way we communicate with customers.

BT | EE | plusnet — We'll do you proud

The BT brand continues to go from strength to strength. Brand Finance has valued it at \$18.4bn, 14% more than a year ago. According to their analysis, BT is the 60th most valuable brand in the world and the third most valuable brand in the UK.

In March 2015, we re-entered the UK consumer mobile market, under the BT brand. In January 2016 we took ownership of the EE brand. Since its launch in 2012, the EE brand has achieved impressive results in terms of awareness and positive associations.

The Plusnet brand continues to offer a distinctive position of brilliant service at a great price. We'll continue to run all three of our brands in the UK consumer market, offering products that meet different customer needs.

We continue to innovate for our customers, further building the strength and breadth of our brands. For example:

- In August, we added to our BT Sport offering, showing exclusive UEFA Champions League and UEFA Europa League games. We enhanced this with the launch of Europe's first live Ultra HD sports TV channel.
- We also embarked on a multi-year strategic technology partnership with the Williams Martini Racing Formula One team. We're providing the team with innovative communications technology to help improve car performance with instant access to real-time data. Our collaboration is already helping Williams to work better – connecting race tracks around the world with its headquarters in Oxfordshire.

Using partnerships to raise awareness

Partnerships continue to play an important role in how we build our reputation and show our support for good causes. For example we:

- launched our BT Sport Infinity Lab competition to find start-ups and entrepreneurs with innovative digital media and production solutions;
- agreed multi-year sponsorship of the Institution of Engineering and Technology's new Diamond Jubilee Scholarship Programme;
- have continued to develop our Connecting Africa programme (see page 38); and
- continued to support good causes including Children in Need in November 2015 and Sport Relief in March 2016 (see page 34).

Stakeholders and relationships

As well as our people, our main stakeholders are: our customers; communities; shareholders; lenders; our pension schemes; suppliers; government; and regulatory authorities.

Our markets and customers

We sell fixed-voice, broadband, mobile and TV products and services to individuals and households in the UK. For small and medium-sized enterprises, as well as larger businesses in the UK, we offer fixed-voice, broadband, mobility, networking and IT services. In both the UK and globally we offer managed networked IT services to multinational corporations, domestic businesses and public sector organisations.

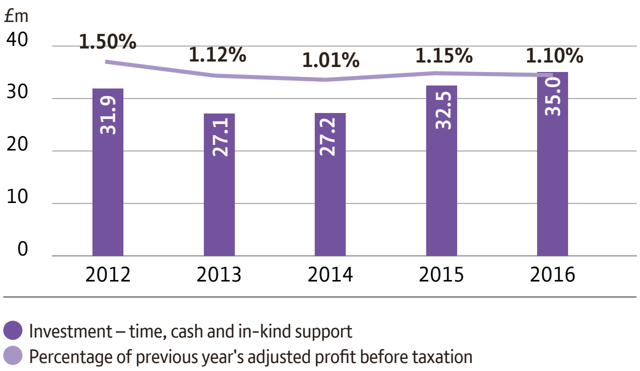
Some of our customers are also our competitors. This is because we sell wholesale products and services to other communications providers in the UK and overseas.

You can read about our markets, customers and the services we provide them in our lines of business section, from page 57.

Communities and society[a]

BT's purpose is embedded at the heart of our business, and has helped us to deliver economic growth and wider societal and environmental benefits. During the year we invested £35m to accelerate a number of environmental and societal priorities that help to bring our purpose to life (see page 43). This investment is a mixture of cash, time volunteered, and in-kind contributions. It is equivalent to 1.1% of our previous year's adjusted profit before tax. Over the last five years we've invested over £153m, an average of 1.18% of our adjusted profit before tax.

BT's total investment in society
Year ended 31 March



Creating a connected society

Our 2020 ambitions

More than 9 out of 10 people in the UK will have access to our fibre-based products and services — **9/10**

Help 10m people overcome social disadvantage through the benefits our products and services can bring — **10m**

This year, we extended our fibre footprint in the UK to more than 25m premises and – in line with our 2020 goal – this means around 8.5 out of 10 people can now access fibre-based products and services (see page 85). We plan to extend coverage even further so that fibre availability in the UK exceeds the Government's current target of 95% by the end of 2017.

We continue to push for greater digital inclusion, both by playing a leading role in the development of the Government's Digital Inclusion Outcomes Framework, and through the use of our own products.

We're helping low income groups to get online with two products: BT Basic + Broadband and our BT Business Digital Inclusion for Social Housing solution. The launch of the 'BT and Barclays Wi-Fi in Our Community' initiative is providing access, guidance and coaching to those who need it most.

Keeping people safe online remains a priority. Internet Matters, the website we co-founded in 2014 to help parents keep their children safe online, has now had over 2.5m visitors. The Right Click, our partnership with UNICEF UK, has seen BT volunteers deliver 280 workshops in schools, teaching children and parents how to use the internet safely.

This year we've developed a methodology to measure the social impact of our products and services. This has been successfully piloted on three propositions (BT Basic, Digital Inclusion for Social Housing and Mobile Health Worker) and has been used on a corporate contract through our work with the Colombian government (page 62). Having a way to measure the wider benefits our products and services can bring shows how valuable ICT, and what we do, has become in people's day-to-day lives. We can also use the methodology to influence how we develop our future products.

Outside the UK, our Connecting Africa programme has now successfully connected all 30 of the planned SOS Children's Villages, in 13 countries, using BT's satellite technology. We have used this in seven villages to provide a new Healthcare Management System, improving healthcare services for over 100,000 people.

We also continue to embed social and environmental criteria into our business processes, helping us to make better decisions, stimulate growth and spark innovation. In January we launched a BT Infinity Lab competition, in partnership with the Department of Transport, to stimulate social and environmental innovation in the SME sector.

[a] Data excludes EE.

Supporting charities and communities

Our 2020 ambition

Help generate more than £1bn for good causes, using our people, their skills and our technology

£1bn

This year we added £94m towards our £1bn target. £60m of this was raised via MyDonate, our commission-free online fundraising and donations platform. This takes our overall fundraising total to £327m.

As well as supporting a number of smaller charities and individual fundraisers, we again used MyDonate and our communications technology – with help from our volunteers – to support various large telethons (page 34). These included Comic Relief, Children in Need, and the Disasters Emergency Committee appeal after the earthquake in Nepal.

In the UK, we provide discounted calls and line rental charges to members of The Charities Club, saving those charities £1.2m on their phone bills.

We see sport as a positive vehicle for change in young people's lives. Through the donations of BT Sport customers, The Supporters Club funded nine new sports charities and community sports foundations this year (four in the UK). And we encourage people to take up sport through the Join In campaign.

Our shareholders

We have around 825,000 shareholders. As well as the Annual Report and Annual General Meeting, we keep our shareholders up to date with how we're doing through regular mailings. These often include offers on our products and services that are only available to shareholders. Our website includes press releases, newsletters, presentations and webcasts that can also keep our shareholders informed.

We held a general meeting in April 2015 at which our shareholders approved the acquisition of EE. And in January 2016 we published a prospectus for the issue of new BT shares that were part of the consideration for the acquisition.

Most of our shares are held by institutional investors. We have an extensive investor relations programme aimed at keeping existing investors informed and attracting new ones. This programme includes:

- reporting quarterly results, accompanied by a conference call or presentation from senior management;
- 'teach-ins' on key topics;
- site visits (for example this year we invited investors to an innovation event at Adastral Park); and
- meetings and conference calls with investors both in the UK and around the world.

In 2015/16, we held 353 meetings or events with institutional investors. This compares with 369 in 2014/15.

We were voted the best company for investor relations in England in the Extel Survey 2015, for the second year running. We also maintained our second place in the European telecoms sector. And we won the IR Magazine award for best investor relations in the European Technology & Communications sector.

Our lenders

Our lenders, mainly banking institutions and bondholders, play an important role in our treasury and funding strategy.

These relationships are vital for funding the business and meeting our liquidity requirements. We tell you more about this on page 102.

Our pension schemes

We operate defined benefit and defined contribution pension schemes. The largest is the BT Pension Scheme (BTPS) which has 301,500 members. You can read more about it on page 107.

Our suppliers

Our suppliers play a vital role; their products and services help us deliver our strategy. We source from across the world and currently have suppliers in over 150 countries. We spent around £10.2bn with our suppliers this year (2014/15: £9.4bn). Around 64% of our spend is with the top 100 suppliers.

We want to get the most from our suppliers – especially from their diversity, skills and innovation. The mix of suppliers keeps evolving as we expand into markets such as mobility, TV and televised sport. This year we've grown our supplier base in IT security, to support our growing investment in cyber security. But we've also removed over 2,800 suppliers from our procurement systems.

As part of integrating EE, we're working to identify opportunities for cost savings and efficiencies through our combined spend.

Our approach to procurement

We have around 330 BT people in 30 countries working with suppliers. As part of our cost transformation activities we've concentrated on making the most of our relationships with our largest suppliers to get even better value. In-life contract management of our top 130 suppliers has delivered savings of around £18m.

We've continued our Purchase Order (PO) Intercept programme, reviewing all POs over £1,000 to make sure that we're getting the best from our spend across BT. Our Central Business Services organisation has hired more people to support this programme. They've reviewed around 90,000 POs, accounting for £4bn of spend, and have saved us more than £15m.

The Procurement Profession, part of the BT Academy, has grown this year, developing a rich library of over 120 training modules. The website attracts nearly 250 visits a month on average.

Our ambition is to have all our buyers accredited and licensed. And for a few of our expert practitioners to be recognised externally as fellows of CIPS (Chartered Institute of Procurement and Supply).

We now have 198 licensed buyers. And there are now five fellows of CIPS (2014/15: two) leading our procurement activities in BT.

Choosing our suppliers

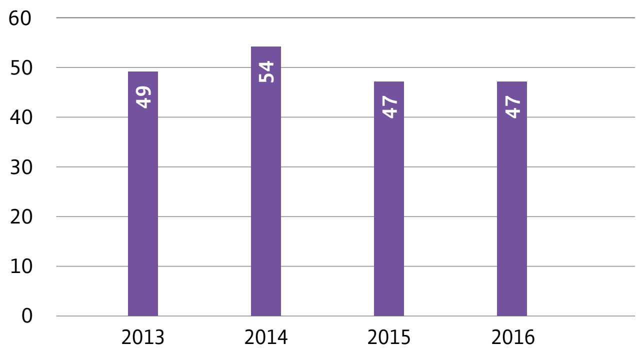
We want to know who we're doing business with and who is acting on our behalf. So we:

- choose suppliers using principles that make sure both we and the supplier act ethically and responsibly;
- check that the goods and services we buy are made, delivered and disposed of in a socially and environmentally responsible way; and
- measure things like suppliers' energy use, environmental impact and labour standards, and work with them to improve these.

Ethical standards in our supply chain

We want our suppliers' employees to experience working conditions that are safe and fair. We send all but our lowest-risk suppliers an ethical standards questionnaire. Based on their responses, we follow up with any suppliers identified as high or medium risk. This year we met our target to achieve 100% follow-up action within three months. We also visit supplier sites to make sure they meet our standards. This year we visited 47 sites around the world, the same as last year.

Number of on-site supplier assessments
Year ended 31 March



To comply with the Dodd-Frank Act and our Securities and Exchange Commission (SEC) obligations, we repeated our annual research asking our BT product suppliers whether their products contain certain minerals which may have been sourced from conflict areas such as the Democratic Republic of the Congo. As a result we have a better understanding of our suppliers' own supply chains but we're not yet at the point where we can declare an individual product to be entirely conflict mineral free.

In June 2015 we filed with the SEC our 2014 report describing our conflict minerals approach and reflecting the supplier responses we received. We will file the report for 2015 in May 2016.

The Modern Slavery Act, which came into effect in 2015, has meant that we're reviewing the processes we use with our suppliers to address human rights risks in our supply chain.

Paying our suppliers

This year the average number of days between invoice date and supplier payment was 62 days globally (2014/15: 60 days), with 54 days for UK invoices.

Suppliers can choose to use the BT Supplier Finance scheme which offers contracted suppliers the chance to be paid early. This reduces their financing costs.

We introduced it in September 2013 and it's now one of the largest supplier finance schemes in the UK, supporting over £1.4bn of spend. EE also operates a supplier finance scheme.

These schemes are attractive for SMEs (who make up around 40% of our supply base). They also support UK government initiatives to encourage small business growth.

We also follow the principles of the Better Payment Practice Code set up by the Government in partnership with business organisations.

Human rights

The human rights of our employees, people working in our supply chain, our customers and members of the communities where we operate could be affected by the way we do business. We think about what these effects could be and try to positively impact the experience and approach for those we work with. We also consider how we can remove or reduce potential negative impacts in accordance with the UN Guiding Principles on Business and Human Rights (UNGPs).

It's important that everyone in BT, and everyone who works with us, understands our commitment to the UNGPs. That's why we commit to them in The Way We Work, our statement of business practice.

We have other policies to address specific issues which might affect human rights, such as: supply chain standards; diversity and inclusion; and safety and wellbeing in the workplace.

We're in the process of drawing together our approach into one overarching human rights policy so that anyone can easily access our principles and understand how we put them into practice.

As we're a communications provider, the rights to privacy and freedom of expression are the human rights which could be most at risk from our operations:

- **Privacy** – because we must comply with laws on investigatory powers. These allow governments, in certain situations, to request information about how people use our services and the content of their communications.
- **Freedom of expression** – because although we don't host much online content ourselves, we do help people get online. So if we block content (which we do in very limited circumstances), that could clearly affect people's rights to express their views and receive information.

We support and respect people's rights to privacy and free expression, though we accept that sometimes there may need to be limitations on those rights, as international human rights standards allow. Any limitations should be within clear legal frameworks with the right checks and balances. In December 2015 we published our Privacy and Free Expression in UK Communications report which explains our approach to this in more detail.

Our Human Rights Steering Group, which is chaired by a member of the Operating Committee, meets quarterly. This year it considered a broad range of issues, including:

- our approach to an overarching human rights policy;
- our due diligence processes when it comes to winning business;
- the Modern Slavery Act 2015;
- our supply chain; and
- specific human rights issues arising from day-to-day business.

Find out more about the BT Supplier Finance scheme at:
www.selling2bt.bt.com

You can find out more about the Better Payment Practice Code at:
www.payontime.co.uk

www.btplc.com/TheWayWeWork

We're developing an enhanced human rights due diligence tool for our global sales team. We've also undertaken detailed human rights impact assessments on a number of potential business opportunities. As a result, we took a range of mitigating steps such as including detailed contractual provisions, integrating human rights considerations into customer training and ongoing project monitoring. We've also turned down business opportunities on the basis of human rights concerns.

Our relationship with HM Government

We're one of the largest suppliers of networked IT services to the UK public sector. We work with more than 1,400 organisations across central, local and devolved government, healthcare, police and defence to provide some of the UK's most vital services. For example:

- We run N3, the National Health Service's secure national network.
- We provide telecoms services to the Ministry of Defence and contact centre and conferencing services to the Department for Work and Pensions.
- We've recently started working with the NHS Islington Clinical Commissioning Group and the London Borough of Islington to provide a service that will help join up health and social care in Islington and improve the experience of care for the borough's residents.
- We're working with Bromley Council to deliver computer and data centre services which will help provide them with greater flexibility in running their IT services.
- We're working with the Government to extend fibre broadband to rural areas under the Broadband Delivery UK (BDUK) scheme.
- In December, EE was awarded a contract to provide the emergency services with nationwide 4G voice and data services.

We can be required by law to do certain things and provide certain services to the Government. For example, under the Communications Act, we (and others) can be required to provide or restore services during disasters. The Civil Contingencies Act 2004 also says that the Government can impose obligations on us (and others) at times of emergency or in connection with civil contingency planning.

The Secretary of State for the Home Department can also require us to take certain actions in the interests of national security.

Regulation

Communications and TV services are regulated by governmental and non-governmental bodies in the UK and around the world. This is to make sure that CPs and broadcasters comply with common standards and rules, and that nobody is disadvantaged by providers with strong positions in their markets.

European Union (EU) regulation

In EU countries, electronic communications networks and services are governed by directives and regulations set by the European Commission (EC). These create a Europe-wide framework (known as the European Common Regulatory Framework) covering services such as fixed and mobile voice, broadband, cable and satellite TV.

The directives include rules covering:

- access and interconnection;
- universal service obligations; and
- a requirement for national regulators to review markets for significant market power (SMP) every three years and to put appropriate and proportionate SMP remedies in place.

Companies with SMP typically have a market share of 40% or more and would, without regulation, be able to do things such as increase prices without losing business to competitors (as would happen in a fully competitive market). The directives also cover how regulators should impose remedies to prevent the exercise of SMP, for example by setting price controls. The rules require national regulators to consult with the EC on any remedies before they are finalised to make sure they're consistent with European regulations.

Functional separation of the access network from downstream businesses is included in the EU Common Regulatory Framework list of remedies. But it's positioned as an exceptional remedy, requiring a high burden of proof of market failure, and is subject to EC approval. Structural separation, unless self-imposed, is not included.

Review of the European Common Regulatory Framework

In May 2015, the EC announced its strategy for the Digital Single Market which includes a plan to review the European Common Regulatory Framework. As part of this review, the EC will assess how to encourage investment in infrastructure and how to make current telecoms and media rules fit for new challenges and new types of service provider. The EC is also reviewing copyright and content policy. Any changes are expected to be implemented by mid-2017.

UK regulation

The UK telecoms and broadcasting industries are regulated primarily by Ofcom (the UK's independent regulator) within the framework set by the various European directives, the Communications Act 2003 (the Communications Act) and other UK and EU regulations and recommendations.

The telecoms sector is subject to an extensive ex-ante regulatory framework set out under the European Common Regulatory Framework. By contrast, broadcasting and pay-TV is only currently subject to a mixture of separate, specific regulation and general competition law.

The Communications Act and Ofcom

The Communications Act gives Ofcom legal powers and sets out how electronic communications and broadcasting services should be regulated in the UK. It includes the conditions set by the European directives.

Ofcom's main duties

- To further the interests of citizens in relation to communications matters.
- To further the interests of consumers in relevant markets, where appropriate, by promoting competition.

Under the powers of the Communications Act, Ofcom sets conditions that CPs must comply with. Some conditions, known as General Conditions, apply to all CPs. These mainly deal with:

- protecting consumers;
- access and interconnection;
- planning for emergencies;
- providing information to Ofcom; and
- allocating and transferring phone numbers.

Other conditions apply to certain companies that are universal service providers or which Ofcom has decided have SMP in a particular market. We're the designated universal service provider for the UK (except for the Hull area where it is KCOM Group) and so we have certain obligations. The main one is to make sure that basic fixed-line services are available at an affordable price to all consumers. We're also obliged to provide public payphones, although we can remove those that are uneconomic (subject to local consultation and agreement by local authorities).

We have SMP in a number of markets including Business Connectivity (such as Ethernet and backhaul), Fixed Access (including LLU, GEA and WLR) and Wholesale Narrowband (such as Call Origination). Ofcom's market reviews are therefore very important for us.

Following a market review, if Ofcom decides that a CP has SMP, it can put controls in place, typically on the prices which the CP can charge. Ofcom will generally try to set charges that are reasonably based on costs and an appropriate return on the capital invested.

CPs affected by Ofcom decisions can appeal them through a number of routes, including to the Competition Appeal Tribunal (CAT) or to the High Court.

BT's Undertakings

In response to Ofcom's 2005 Strategic Review of Telecommunications we gave some legally-binding undertakings under the Enterprise Act 2002. These Undertakings (which included the creation of Openreach) began in September 2005. They aim to give clarity and certainty to the UK telecoms industry about the way we provide wholesale regulated products. This in turn supports effective and fair competition in related retail markets.

Ofcom's Strategic Review of Digital Communications

Ofcom announced in March 2015 that, ten years on from the last one, it would carry out a new strategic review, this time of the wider digital communications industry.

The review has looked at ways to improve investment, innovation and sustainable competition across fixed-line, broadband and mobile markets, and at ways to ensure that where regulation is necessary it is targeted, with deregulation elsewhere. Ofcom has also looked at ways of empowering consumers.

On 25 February 2016, Ofcom published its initial conclusions:

- Ofcom sees passive access to Openreach's underground ducts and telephone poles as key to its future competition policy, especially to encourage investment in fibre-to-the-premises by other companies. Ofcom wants an improved process for getting access to this infrastucture, including an online database of its location, condition and capacity.
- Ofcom wants a strengthened model of functional separation of Openreach so that it can take its own decisions on budget, investment and strategy, in consultation with the wider industry.
- Ofcom intends to introduce: tougher rules on faults, repairs and installations; transparent information on service quality; and automatic compensation for consumers when things go wrong.
- Ofcom will work with the Government to deliver a new universal right to fast, affordable broadband for every household and business in the UK. Also, when Ofcom releases spectrum for mobile operators, it intends to impose obligations to improve rural mobile coverage.

We've made a number of proposals to Ofcom to address its concerns. These include a new governance structure for Openreach and a clear commitment on investment. We're happy for other companies to use our ducts and poles which have been open to competitors since 2011.

Overseas regulation

The degree of regulation in international markets varies widely. This can hinder our ability to compete and provide the services our customers require. We're pressing incumbent operators around the world, and their national regulatory authorities, for fairer, cost-related wholesale access to their networks.

We're also in discussions with both EC and US regulatory authorities over what we believe to be premature deregulation of parts of the US telecoms market. This has made it more difficult for non-US CPs to enter and compete in the US, while European telecoms markets remain open to competition from US operators.

Price regulation of our main wholesale products

The following table shows the main wholesale products provided to CPs which are subject to price controls in markets where we have been found to have SMP.

Product	Annual charge control	Current charge control ends
Call origination	RPI–3.6%	30 September 2016
Call termination	RPI–3.1%	30 September 2016
Ethernet	CPI–13.5%	31 March 2019
PPCs	CPI–3.5%	31 March 2019
WLR rental	CPI–3.0%	31 March 2017
IPStream rental	CPI–4.4% in Market A[a] only	31 March 2017
MPF rental	CPI+0.3%	31 March 2017
SMPF rental	CPI–33.4%	31 March 2017

[a] Wholesale broadband services are regulated in Market A which covers 9.5% of UK premises. Market B covers the remaining premises and is competitive and unregulated.

Our wholesale fibre broadband product, GEA, is not currently subject to price regulation. This will be reviewed again in Ofcom's Wholesale Local Access market review, expected to begin later in 2016, with a final decision due by 1 April 2017.

Other regulatory decisions and activities

Business Connectivity market and cost attribution

In April 2016, Ofcom published its final statement on its Business Connectivity Market Review, Leased Lines Charge Control and Cost Attribution Review. The key measures Ofcom imposed are:

- charge controls to apply from 1 May 2016 until 31 March 2019;
- the introduction of minimum service levels for the provision of Ethernet services by Openreach;
- requiring Openreach to provide access to its fibre network for providers of high-speed leased lines for businesses ('dark fibre').

In setting the charge controls, Ofcom made a number of base year cost adjustments to reflect its Cost Attribution Review assessment that some of our attribution methodologies do not reflect the activity that drives the cost. This is also likely to affect future price controls, including in the Wholesale Local Access and Narrowband markets.

Ethernet dispute

In August 2015, the Court of Appeal granted us permission to appeal the CAT's August 2014 decision relating to a dispute on historical Ethernet pricing that was originally determined by Ofcom in 2012. Our appeal was granted on three legal grounds, including whether Ofcom had the power to require us to make the payments it determined in the dispute and if it has the power to award interest charges on these payments. Ofcom has deferred its final determination on the amount of interest payable until the Court hears the appeal, which we expect to take place in March 2017.

In November 2015, the Court of Appeal also granted TalkTalk permission to appeal the CAT's August 2014 decision.

Margin squeeze test

In May 2015, we lodged an appeal with the CAT against the design of Ofcom's regulatory margin squeeze test which requires BT Consumer to maintain a 'minimum margin' on newly-acquired fibre broadband customers.

In August 2015, Ofcom issued supplementary guidance on how the 'minimum margin' test in respect of fibre broadband would be impacted by a material change in circumstances (such as the launch of our UEFA Champions League and UEFA Europa League content). While we welcome this guidance, it still doesn't provide enough flexibility around how we recover our BT Sport costs. And we believe it doesn't address concerns previously raised by the European Commission around providing us sufficient flexibility to recover these costs.

In March 2016, the CAT issued its judgment on our appeal. The CAT found that Ofcom was entitled to impose a regulatory margin squeeze test as one of the remedies in its Fixed Access Market Review, and rejected our arguments that Ofcom had not met the legal or evidential tests to impose such a condition. Our appeal on the design of the margin squeeze test is being heard by the CMA and its provisional determination is expected in the coming months.

Pay-TV

We're appealing to the CAT Ofcom's November 2015 decision to remove Sky's Wholesale Must Offer obligation on Sky Sports. We believe that effective remedies are essential to address the failure of competition in the pay-TV market, where Sky has held a dominant position for more than a decade.

Broadband USO

In March 2016, the UK Government began a consultation on a broadband Universal Service Obligation (USO) that will require a minimum line speed of 10Mbps to be provided. In April 2016, at the Government's request, Ofcom began a consultation on the design of the USO including: whether there should be one or more designated USO providers; whether there should be a competitive process for designating USO providers; and whether the net costs of a USO should be funded by industry. Ofcom plans to report back to the Government by the end of 2016.

Regulatory approval of our acquisition of EE

In February 2015 we announced that we'd agreed definitive terms to acquire EE. This transaction was subject to approval by BT shareholders and merger clearance, in particular from the UK Competition and Markets Authority (CMA). In October 2015, the CMA gave its provisional clearance to the deal, announcing that it is not expected to result in a substantial lessening of competition in any market in the UK. The CMA gave formal approval, unconditionally without remedies, on 15 January 2016.

Protecting the environment

We believe that the Information and Communications Technology (ICT) industry plays a vital and ever-growing role in tackling climate change[a]. As set out in a report[b] published this year, we believe increased investment in ICT can reduce UK carbon emissions by 24% by 2030, while creating value for the UK economy (£122bn in that year). Reflecting our role in this area, we also organised and took part in working sessions at the UN climate negotiations in Paris (COP21).

We launched 100% Sport at Climate Week in New York, encouraging sports fans to switch to renewable energy and promoting our support for the global *#go100percent* campaign (created by the Renewables 100 Policy Institute).

Our 2020 ambition

Enable customers to reduce their carbon emissions by at least three times the end-to-end carbon impact of our business

3:1

[a] As a signatory to the Climate Disclosure Standards Board's (CDSB) fiduciary duty and climate change disclosure, we summarise our response to climate change through this Annual Report with more details in our Delivering Our Purpose report, www.btplc.com/Purposefulbusiness

[b] 'The Role of ICT in Reducing Carbon Emissions in the UK', www.btplc.com/Purposefulbusiness/Stories/Energyenvironment/UKcarbontargets/index.htm

Reducing our customers' carbon footprint[a,b]

We continue to progress towards our 3:1 goal, measuring the impact our products and services can have on reducing our customers' carbon emissions.

This year we generated £3.6bn of revenue from products that have contributed to carbon abatement – up from £3.4bn in 2014/15. As an example, our Field Force Automation services enable organisations with mobile teams to improve their productivity by automating fleet and driver scheduling and reporting. This means they can better manage their fleet of vehicles, saving fuel and reducing emissions.

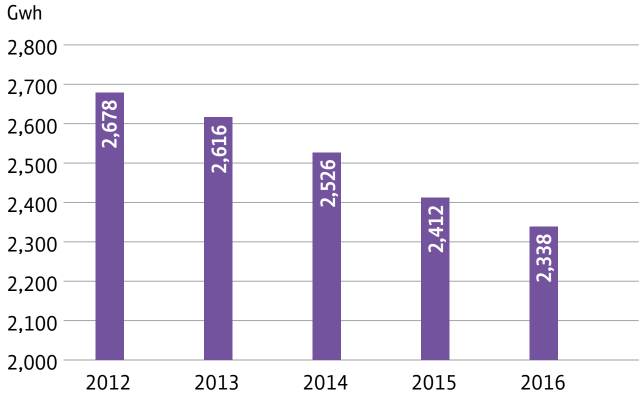
3:1 Goal	2015/16[b]	2014/15
Customer savings	7.6 Mt	7.1 Mt
Our impact	4.8 Mt	4.6 Mt
Ratio	1.6:1	1.5:1

Our own energy use and carbon footprint[a,b]

Reducing our energy use

We've reduced our worldwide energy use for the seventh consecutive year. In Great Britain we spent around £307m on energy and fuel this year (2014/15: £306m). We estimate that our energy savings programme has helped reduce our overall bill by £29m this year, and by £190m since 2009/10. 95% of the worldwide energy we buy comes from renewable sources and we're aiming to achieve 100% – where markets allow – by the end of 2020.

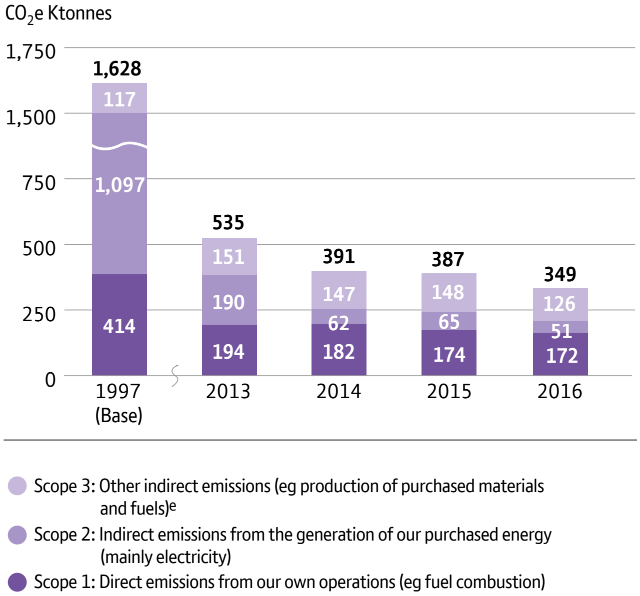
BT's worldwide energy use[a,b]
Year ended 31 March



Reducing our carbon footprint

We report all of the greenhouse gas (GHG) emission sources required under UK regulations[c]. The following chart shows the 10% reduction this year in our total operational worldwide CO_2 equivalent (CO_2e) emissions[d]:

BT's worldwide greenhouse gas emissions[a,b,c,e]
Year ended 31 March



Figures exclude third-party consumption and EE.

We also report two CO_2e intensity measures:

- Our climate stabilisation intensity (CSI) target: by 2020, we'll reduce our operational worldwide carbon emissions per unit of value-added (our contribution to GDP) by 80% compared to 1996/97. This year, we achieved 81%, exceeding our target. Next year, we'll incorporate EE into the numbers and set a new target.
- Our scope 1 & 2 emissions this year totalled 12.5 tonnes CO_2e per £m revenue, reflecting an 86% reduction since our base year of 1996/97.

Conserving natural resources[a,b]

Reducing water usage

Most of our water usage is for office and catering facilities, or to cool equipment (for example, in telephone exchanges). This year we reduced our UK water consumption by 10%. We'll continue to target and reduce leaks using our half-hourly meter readings, provided by our automatic monitoring and reporting programme.

Managing waste products

We try to minimise the amount of materials we use in our operations, and re-use them where we can. Otherwise our specialist contractors recycle them wherever possible, or manage their disposal – including hazardous materials such as oil and some types of light bulbs and batteries – in line with legislation.

[a] We restate previous years' data when subsequent information is deemed to be materially significant, such as replacing previous estimates with measured figures.
[b] EE data is excluded, in line with the GHG protocol below, pending next year's report when we will provide new baseline numbers.
[c] We use the GHG Protocol Corporate Accounting and Reporting Standard, with UK Government GHG Conversion Factors for Company Reporting 2015.
[d] We report on all our greenhouse gas emissions as a single total, by converting them to the equivalent amount of CO_2 using latest government conversion factors.
[e] Detailed emissions data is available from our Delivering Our Purpose website, www.btplc.com/Purposefulbusiness. To comply with revised GHG Protocol guidance this year, we now report both market and location-based Scope 2 data. This chart uses a market-based measure for 2015/16, consistent with the methodology used in previous years.

Our performance as a sustainable and responsible business

The first table below demonstrates our performance against our six 2020 ambitions. Below that, we report progress against seven foundation measures. Next year, we aim to maintain or improve on each of our ambitions and measures. To aid comparison against previous years, we exclude EE's contribution to the group this year, but we'll provide new baseline numbers in our 2016/17 Annual Report.

Our 2020 ambitions

	Our 2020 ambitions	2014/15 performance	2015/16 performance	Status	Page
Supporting charities and communities	Use our skills and technology to help generate more than £1bn for good causes	£86m raised for good causes Cumulative total: £234m since 2012	£94m raised for good causes Cumulative total: £327m since 2012	Ongoing	38
	Inspire 66% (two-thirds) of our people to volunteer	26% of BT people volunteering	27% of BT people volunteering	Ongoing	34
Creating a connected society	More than 9/10 people in the UK will have access to our fibre-based products and services	7.5 out of 10	8.5 out of 10	Ongoing	38
	Helping 10m people overcome social disadvantage through the benefits our products and services can bring	n/a – new target	2.6m people reached	Ongoing	38
Creating a culture of tech literacy	Help 5m children to receive better teaching in computer skills	n/a – new target	344,000 children reached	Ongoing	33
Delivering environmental benefits	Enable customers to reduce their carbon emissions by at least three times the end-to-end carbon impact of our business	1.5:1 achieved	1.6:1 achieved	Ongoing	44

Our foundation measures

	Our foundations	2014/15 performance	2015/16 performance	Status	Page
Our investment	Investment to accelerate our purposeful business approach; to be more than 1% of adjusted profit before tax (PBT)	1.15% of PBT invested	1.10% of PBT invested	Target met	38
Our customers	**Customer service:** to consistently improve RFT across our entire customer base	4.7% improvement	3.0% reduction (see page 22)	Target failed	22
Our employees	**Employee engagement index:** our relationship with our employees	3.82/5 achieved	3.81/5 achieved	Target met	33
	Sickness absence rate: % of calendar days lost to sickness	2.23% calendar days lost to sickness	2.33% calendar days lost to sickness	Target failed	34
	Ethical performance: our employees' awareness and training	4.33/5 achieved	4.31/5 achieved	Target met	52
Our suppliers	**Ethical Trading:** across our supply chain, with focus on Human Rights. Achieve 100% follow-up within three months, for all suppliers identified as high or medium risk, through our ethical standards questionnaire	96% follow-up within three months	100% follow-up within three months	Target met	40
Our environmental impact	**CO_2e emissions:** a measure of our climate change impact. We'll reduce our worldwide CO_2e emission intensity by 80% by December 2020	79% reduction in net CO_2e emission intensity vs. base levels (1996/97)	81% reduction in net CO_2e emission intensity vs. base levels (1996/97)	Target met	44

Target met   Target failed   Ongoing

To find out more about our 2020 ambitions, our methodologies and how our results are calculated, take a look at www.btplc.com/Purposefulbusiness

Our risks

We're affected by a number of risks and uncertainties. Some risks come from outside our business, others from within. Some we can't control. Many of our risks are similar to those felt by comparable businesses.

Principal risks and uncertainties

The principal risks and uncertainties that affect us could have an impact on our business, brand, assets, revenue, profits, liquidity or capital resources. The principal risks we described last year have evolved, and so has our response to them.

Our Enterprise Risk Management framework gives reasonable (but cannot give absolute) assurance that we've identified and addressed our biggest risks. However, there may be some risks which are unknown to us today. And there may be some that we consider less significant now but which become more important later.

Things that happen outside BT present both risks and opportunities, to our business and to others. We focus our efforts on predicting and mitigating those risks while aiming to take advantage of any opportunities that may emerge.

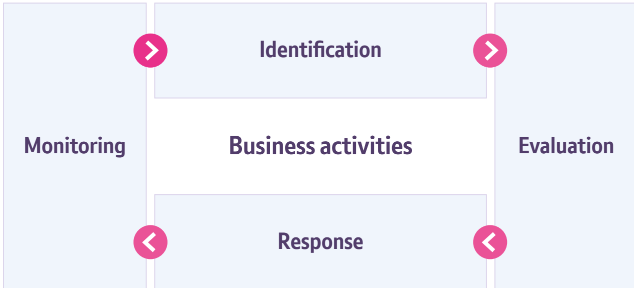
We recognise the particular uncertainty that political and geo-political risks present, both in the UK (like the forthcoming referendum on Britain's membership of the EU) and globally. We monitor these through a separate sub-committee of our Group Risk Panel.

In the section that follows, we talk about what we're doing to stop our main risks materialising, or to limit their impact. Our biggest risks and uncertainties should be considered alongside the risk management process, the forward-looking statements in this document and the cautionary statement on those statements (see page 248).

How we manage risk

To meet our objectives, build shareholder value and promote our stakeholders' interests, we must manage risk.

We have a group-wide risk management process with four stages. The directors believe our Enterprise Risk Management framework and process support a robust assessment of our principal risks.



Changes over the year

In 2014/15 we improved the way we manage risk by: strengthening our approach to managing it in projects and programmes; further developing our assessment of risk appetite; and identifying opportunities to develop our risk management culture. Specific improvements in 2015/16 included:

UK Corporate Governance Code

Responding to changes in the UK Corporate Governance Code, we've refreshed several aspects of our risk management framework. That included expanding our quantification methodology and reviewing our material controls.

Enhanced tools

This year we've trialled software which helps with modelling risk. We're also in the process of upgrading our core risk management software to make it easier for people to use.

Education and awareness

We believe risk management is an essential capability for our business. It'll therefore be a core skill across all the professions in our business with tailored training for everyone who works for BT.

Enterprise Risk Management framework

Line of business and BT TSO audit & risk committees

Line of business and BT TSO leadership teams

Our lines of business and BT TSO follow our process for managing risk as part of our Enterprise Risk Management framework. That means identifying and responding to the key risks to their business. They record the risks in a register for their leadership teams to review. Audit & risk committees in each line of business, BT TSO and our group functions, ensure this process is effective.

Group Risk Panel

The Group Risk Panel supports the Board and the *Operating Committee*. Every three months it reviews the Group Risk Register (which summarises those risks of greatest significance across our business), considers the inclusion of new or emerging risks, and recommends ways to tackle them. It also oversees the work of the group risk management function. Geo-political risks are reviewed by a sub-committee of the Panel.

Operating Committee

The *Operating Committee* identifies, evaluates, responds to and monitors risks. Significant risks are reported and monitored through the Group Risk Register. The *Operating Committee* assigns a management owner to take charge of monitoring and managing each risk. It monitors risks through regular detailed reviews as well as six-monthly reviews of the Group Risk Register.

Audit & Risk Committee

Board

The Board has overall responsibility for making sure we manage risks appropriately. It regularly reviews, either directly or through the *Audit & Risk Committee*, how we're doing across the group, in our lines of business and in BT TSO.

Strategic and financial risks

Growth in a competitive market

Our markets are characterised by:

- constant and rapid change;
- strong and new competition;
- falling prices and (in some markets) falling revenues;
- technology changes;
- market and product convergence;
- customers moving between providers; and
- regulation to promote competition and cut wholesale prices.

Potential impact

If we don't grow our revenue profitably and sustainably, our cash flows could be impacted. This could limit our ability to invest in the business or pay dividends.

Link to strategy and business model

- Invest for growth **Trend:**

What's changed over the last year?

Last year we did some big things as part of our growth strategy. We:

- acquired EE;
- won FA Premier League rights for the second time;
- launched our BT Sport Europe channel; and
- deployed more of our fibre broadband network.

Our competitors are beginning to react. CK Hutchison wants to buy Telefónica Europe plc (O2 UK). Virgin Media is expanding its network. Sky is being more aggressive in broadband. Vodafone has entered the consumer home phone market. The market is going to get more difficult – not only because of the moves of our traditional competitors but also from players in neighbouring markets, as the dividing lines between industries keep blurring.

There are also regulatory risks that could threaten revenue growth – particularly Ofcom's 'Business Connectivity Market Review' and 'Wholesale Must Offer' statement on pay-TV sports channels.

How we're mitigating the risks

We stick to our strategy, which means:

- broadening and deepening our customer relationships;
- delivering superior customer service;
- transforming our costs; and
- investing for growth.

If we do that, we'll grow our revenue profitably and sustainably.

We've been investing in areas like fibre, TV and content, voice and mobility, UK business markets, and our global corporate customers. Our cost transformation programmes are still delivering savings. We can also seek changes in regulation to make things fairer – so we can compete harder in neighbouring markets, which will be better for our customers.

Communications industry regulation

Regulation affects a lot of what we do.

In the UK, after market reviews, Ofcom can make us provide wholesale services on specified terms. Ofcom reviews the shape and size of that regulation every three years and can include controls on the price we charge for regulated products. It can investigate and enforce any regulatory rules in place and impose fines on us if we don't comply.

Ofcom also has powers to regulate the terms on which we get supplied with certain services – for instance, mobile call termination and wholesale access to certain pay-TV channels. This can increase our costs and affects the scope of services we can provide to customers. Ofcom can also sort out disputes between us and other communications providers about the terms on which services are supplied.

Trend indicates management's perception of how the pre-mitigation risk has moved year on year

Pre-mitigation risk is increasing/worsening | Pre-mitigation risk is at a similar level | Pre-mitigation risk is lessening/improving

Outside the UK, general licensing requirements can make it tough for us to enter markets and compete. Regulation will also define the terms on which we can buy wholesale services from others.

Potential impact

Regulatory rules can affect our ability to compete effectively and earn revenues. UK regulation has the biggest impact – because we have to supply wholesale access products on regulated terms.

Around £5.7bn of our revenue (£3.3bn of which is to downstream parts of BT) is from supplying wholesale services to markets where Ofcom has found us to have significant market power. Most of these revenues are from products with regulated prices which we also have to cut each year by a defined, real-term percentage. The regulatory controls usually last for three years and hold back revenues during that time.

Where other CPs ask Ofcom to sort out disputes with us, there's a risk that Ofcom may set the prices we supply services at, and/or make us provide specific services. In some circumstances, Ofcom can adjust past prices and make us pay back CPs.

Regulation outside the UK can hit our revenue too. For example, overly-restrictive licensing requirements or ineffective regulation of access to other networks mean we might not be able to compete fairly. Regulation can also define and control the terms of access to necessary regulated inputs, which raises our costs.

Link to strategy and business model

- Deliver superior customer service **Trend:**
- Transform our costs

What's changed over the last year?

There has been a lot of regulatory activity in different areas. We've summarised this in the Regulation section on page 41.

Alongside the standard cycle of market reviews, in March 2015 Ofcom announced an overarching strategic review of the digital communications market. In February 2016 it set out its initial conclusions. Some of these could impact our operations, revenues and costs if they're adopted, for example:

- strengthening Openreach's functional separation;
- keeping structural separation on the table;
- reducing regulation where it's no longer required; and
- relying on more end-to-end fibre-based competition.

How we're mitigating the risks

Our team of regulatory specialists include economists and accountants. Together with legal experts and external advisers they continuously check for potential disputes with other CPs and look for opportunities to change regulatory rules. They talk continually with regulators and other key influencers to understand the outlook and to make sure we make our positions clear.

We push for fair, proportionate, consistent and evidenced-based regulation everywhere we do business. Whenever there are market reviews, charge controls, and disputes or investigations we put forward evidence and analysis. This helps us manage the risks around decisions in any particular year.

We can appeal any regulatory decisions we think are wrong. We can also raise disputes or complain (under the relevant regulatory framework or competition law) where we have problems getting access to wholesale services – like to wholesale pay-TV channels or to other access networks.

Pensions

We have a large funding obligation to our main defined benefit pension scheme in the UK, the BT Pension Scheme (BTPS or Scheme). The BTPS faces similar risks to other defined benefit schemes. Things like future low investment returns, high inflation, longer life expectancy and regulatory changes may all mean the BTPS becomes more of a financial burden.

Potential impact

Our contributions to the BTPS are next due to be reviewed at the triennial funding valuation as at 30 June 2017. If there's an increase in the pension deficit, then we could have to increase deficit payments into the Scheme. That might affect our share price and credit rating. If our credit rating fell in future, it would cost us more to borrow money and we might not get such flexible borrowing terms. Higher deficit payments could mean less money available to invest, pay out as dividends or repay debt as it matures.

Link to strategy and business model

- Transform our costs **Trend:**
- Invest for growth

What's changed over the last year?

The last funding valuation of the BTPS, as at 30 June 2014, provided certainty over what we need to pay until the next triennial valuation is concluded.

Things like financial market conditions and expected future investment returns at the valuation date affect the funding position. When considering expected future returns, different factors are reviewed including yields (or returns) on government bonds, which have dropped significantly since 30 June 2014. If a lower future investment return is assumed at the next valuation our liabilities would likely go up, which may lead to bigger deficit payments.

EE operates the EE Pension Scheme (EEPS) which has a defined benefit section that was closed to future benefit accrual in 2014. The EEPS represents less than 2% of the group's retirement benefit obligation. The latest funding valuation for the EEPS is being performed as at 31 December 2015.

How we're mitigating the risks

The investment performance and liability experience are regularly reviewed by both us and the Trustee of the BTPS. We also consider the associated risks and possible mitigations. The assets of the BTPS are well diversified, softening the impact of sharp drops in the value of individual asset classes. This helps us maintain a reasonable balance of risk and return.

Our financial strength and cash generation provide a level of protection against the impact of changes in the funding position of the BTPS. The funding liabilities also include a buffer against future negative experience, as legislation requires that liabilities are calculated on a prudent basis.

Operational risks

Security and resilience

Resilient IT systems, networks and associated infrastructure are essential to our commercial success. There are a lot of different hazards that could significantly interrupt our services.

These include the evolving threat of cyber-attack, as hackers increasingly see Internet Service Providers (ISPs) as attractive targets. Others include component failure, physical attack, copper cable or equipment theft, fire, explosion, flooding and extreme weather, power failure, overheating or extreme cold, problems encountered during upgrades and major changes, and suppliers failing to meet their obligations.

Potential impact

A malicious cyber-attack or breach of security could mean our data is lost, corrupted, disclosed or ransomed, or that our services are interrupted. We might have to pay fines, contract penalties and compensation, and have to operate under sanctions or temporary arrangements while we recover and put things right.

A big interruption to our services, from cyber-attack or otherwise, could mean immediate financial losses from fraud and theft; contract cancellations; lost revenue from not being able to process orders and invoices; contractual penalties; lost productivity and unplanned costs to restore and improve our security; prosecution and fines. Ultimately individuals' welfare could be put at risk where we weren't able to provide services or personal data was misappropriated.

Our revenues, new business and cash flow could suffer, and restoring our reputation and re-building our market share might take an extended period of time.

Link to strategy and business model

- Deliver superior customer service **Trend:**

What's changed over the last year?

We've invested in scanning and monitoring tools and automated cyber defences. But the rate of major cyber-related incidents needing a manual response keeps rising. We've increased the size of our Cyber Defence Operations team accordingly. To probe for vulnerabilities they simulate cyber-attacks. When we learn of potential attack routes, or get intelligence about attacks on similar organisations, we treat the information proactively and resolve it with the same speed and rigour as a real attack.

We've reviewed the resilience and disaster recovery capability of our critical systems, main data centres and our most important exchanges. This has helped us make judgements on where to invest in better and stronger systems and infrastructure. We're also continuing to develop cross-site recovery for our critical systems where this didn't previously exist. There are also several major change programmes underway to intensify IT and network controls to meet new levels of risk.

How we're mitigating the risks

We use encryption to prevent unauthorised access to data travelling over our networks, or through direct access to computers and removable storage devices.

But encryption alone can't eliminate this risk. People can be tricked into downloading malware or giving away information by phone or email. So we also implement extra layers of access control, block as many malicious emails as we can, and run awareness campaigns for customers and employees to make sure they stay vigilant.

We ask suppliers for evidence of compliance with our security policies. We also run an audit programme to test this. We simulate cyber-attacks to test how well protected our websites, networks and internal controls are.

A control framework helps us prevent service interruptions, supported by tried and tested recovery capabilities. Proactive problem management helps us address the root causes of common incidents.

We continue to invest in resilience and recovery capabilities for critical IT systems, as well as addressing vulnerabilities in our physical estate as we become aware of them. We also have a rolling programme of major incident simulations to test and refine our procedures for crises.

By replacing equipment approaching the end of its service life, we're moving more of our legacy estate to new, more resilient facilities. We've also made sure that we have geographically-distributed locations that support cross-site recovery.

Major contracts

We have a number of complex and high-value national and multinational customer contracts. The revenue and profitability of these contracts are affected by things like: variation in cost; achieving cost savings anticipated in contract pricing (both in terms of scale and time); delays in delivering or achieving agreed milestones owing to factors either in or out of our control; changes in customers' requirements, their budgets, strategies or businesses; and our suppliers' performance. Any of these factors could make a contract less profitable or even loss-making.

The degree of risk varies with the scope and life of the contract and is typically higher in the early stages. Some customer contracts need investment in the early stages, which we then expect to recover over the life of the contract.

Major contracts often involve implementing new systems and communications networks, transforming legacy networks and developing new technologies. Delays or missed milestones might have an impact on us recovering these upfront costs. There is substantial performance risk in some of these highly-complex contracts.

Potential impact

If we don't manage and meet our commitments under these contracts – or if customers' needs, budgets, strategies or businesses change – then our expected future revenue, profitability and cash generation may go down. Unexpectedly high costs associated with delivering particular transformational contracts could also hit profitability. Earnings may drop. Contracts may even become loss-making through loss of revenue, changes to customers' businesses (due to, for example, mergers or acquisitions), business failure or contract termination.

We're still delivering lots of contracts with local authorities through regional fibre deployment programmes including the Broadband Delivery UK programme (BDUK). As with our other major contracts, if we failed to deliver these contracts successfully it might lead to reduced future revenue, profitability and cash generation.

As well as carrying a higher reputational risk, these contracts present specific risks around deployment, delivery and our ability to recover public funding. We also have an obligation to potentially either re-invest or repay grant funding depending on lots of different factors – including how many customers take up a new service.

Link to strategy and business model
- Deliver superior customer service
- Transform our costs
- Invest for growth

Trend:

What's changed over the last year?

Tough market conditions and competitive pressures continue in many global regions, while in some we're seeing bigger growth in volume of business because of our previous investments. The risk landscape changes accordingly, as does our focus of risk support and review.

Of particular note for 2015/16 has been the way the BDUK programme has helped UK broadband fibre implementation mature, cutting the associated delivery risks. But these risks have partly been replaced by new challenges from the next tranche of smaller contracts (with their associated geographic and technical risks). While our broadband contracts carry a different risk profile to other major corporate contracts, we apply our governance and reporting processes to make sure we identify risks and mitigation activities and report them to management.

How we're mitigating the risks

At both group and line of business-level we have governance, risk management and reporting processes in place. Independent audits and the checks and balances in individual contracts provide assurance through an independent review programme. To track progress, we monitor how we're doing on these risks and mitigation actions and report it to senior management. A separate, dedicated team provides assurance for our BDUK projects.

The BT Academy helps support skills development and learning initiatives. These help our Contract Management Profession to better identify and manage risk. We also update new training collateral whenever we learn something new. The scope and availability of training options continues to improve through BT-wide learning and development initiatives.

Supply chain

Our supply market is global, and there are often several links in our supply chains. So guaranteeing the integrity and continuity of those links is critical to our operations and therefore a big risk to our business.

Global markets expose us to global risks, including climate change. We weigh up and respond to any risks which crop up where geo-political and market forces could affect our suppliers' ability to support us.

A global supply market means better sourcing opportunities, but brings challenges if suppliers become more geographically and culturally diverse from our customers.

Our dealings with suppliers – from the way we choose them, to the contracts we sign, to how we pay them – follow our trading and ethical policies. For more detail, see Our suppliers on page 39.

Potential impact

If something goes wrong in our supply chain the level of impact can vary. But most of the time it means higher costs for us, and potential damage to our customer service, investments and ultimately our brand. We could lose a lot of money if a big or important supplier went out of business, especially if that meant us having to change a technology or system. And if we couldn't find an alternative supplier, it might compromise the commitments we make to our customers. And that might lead to breach of contract, lost revenue or penalties.

If any link in our supply chain falls foul of the law, or fails to meet our ethical expectations, that could damage our reputation – possibly leading to legal action and lost revenue.

Link to strategy and business model
- Deliver superior customer service
- Transform our costs

Trend:

What's changed over the last year?

We've spent time assessing several emerging geo-political threats and the impact they'd have on our supply chain. They include Greece's position in the Eurozone and the UK's position in the EU.

There's a continuing trend toward mergers and acquisitions in some of the global markets we source from. It highlights the risk of us depending on single or monopolistic suppliers – particularly those less constrained by regulation and who might charge us more than their domestic customers.

There's generally an increasing (and welcome) focus on human rights. The Modern Slavery Act 2015 means we must examine the potential risk of both modern slavery and human trafficking in our supply chain. Another ethical consideration is the risk of conflict minerals being in our supply chain, which would not only go against our ethical standard but could also harm our reputation.

How we're mitigating the risks

We have a few really critical suppliers. We keep a close eye on their performance and ability to meet their obligations. We tell the business when to prepare for the risk of a supplier failing. And our senior leaders continually review how ready we are for those types of events.

We make sure we put in place the right due diligence when it comes to introducing new suppliers and to continuing business with existing ones. That includes checks on company finances, business and quality management systems, accreditations, and ethical and sustainability practices. We manage our top suppliers according to the contracts they've signed. We work with them to drive better ways of working every day, reducing our exposure to risks around poor supplier practices.

Case study: Early intervention to deliver major contracts

If we don't establish strong contract and risk management at the start of a contract, it can have longer-term impacts on contract profitability and customer experience.

How we managed the risk

Contracts are generally getting more complex. To reduce contract risk, in 2015 we introduced a new team of contract mobilisation specialists. Their aim is to make sure large and complex contracts get off to a good start.

The team works exclusively on new contracts. They take a hands-on approach to improving and supplementing the way we manage contracts in their early stages. That helps make sure the in-life contract team has the level of planning and implementation capability it needs.

The result, and what we learned

There's a strong link between contracts beginning well and us meeting our customers' expectations. So our mobilisation specialists' job is to cut the service delivery risk and the likelihood of implementation delays.

Our contract leads don't begin new multi-year contracts that often, so they're not always familiar with the huge volume of very detailed and time-critical actions unique to the first few weeks. But given how many of those types of contract we sign each year, it helps having a team with the right expertise and skills solely focused on supporting this activity.

Compliance risks

Business integrity and ethics

We're proud of our high ethical standards. We don't tolerate bribery. We don't tolerate any forms of corruption. We follow a wide range of local and international anti-corruption and bribery laws – in particular the UK Bribery Act and US Foreign Corrupt Practices Act (FCPA). Both these pieces of legislation have extraterritorial reach, so cover our global operations. As we expand globally, we're increasingly operating in countries seen as having a higher risk of bribery and corruption. We also have to make sure we follow trade sanctions and import and export controls.

Potential impact

If BT people, or associated people like suppliers or agents break anti-corruption, bribery or sanctions legislation there could be big penalties, criminal prosecution and significant brand damage. This could have a major or minor impact on future revenue and cash flow depending on the nature of the breach, the legislation concerned and any penalties. If we were accused of corruption or bribery or violating sanctions regulations that could lead to reputational damage with investors, regulators and customers.

Link to strategy and business model

- Deliver superior customer service
- Transform our costs

Trend:

What's changed over the last year?

More and more countries are bringing in anti-corruption and bribery legislation. In the UK, the Serious Fraud Office is now able to bring in deferred prosecutions agreements for fraud, bribery and other economic crime. In terms of enforcement, there are yet to be any big cases stemming from the UK Bribery Act, but US FCPA generates a lot of enforcement actions.

How we're mitigating the risks

We've put a number of controls in place to address risk in this area. These include an anti-corruption and bribery programme and 'The Way We Work' (our statement of business practice, available in 14 languages). We ask all BT people to sign up to its principles and to our anti-corruption and bribery policy. We have policies covering gifts, hospitality, charitable donations and sponsorship. We run training for people in higher-risk roles like procurement and sales.

We regularly weigh up our business integrity risks to make sure we've got the right mitigation in place. 'Speak Up' (our confidential hotline) is operated by a third party with all reports passed straight to our Director of Ethics and Compliance for investigation.

Our internal audit team regularly runs checks on our business. External providers also assess areas we think are higher risk, to make sure people understand our policies and that controls are working. We do selective due diligence checks on third parties like suppliers, agents, resellers and distributors. Procurement contracts include anti-corruption and bribery clauses.

Our policy helps us follow all sanctions and export controls that apply to us. That policy means all bids involving a country with sanctions imposed by the EU and/or the US need approval. The policy also mandates everyone uses our internal shipping system to arrange international exports. That system runs compliance checks and flags any orders which need an export licence.

Processing our customers' data

We control and process huge quantities of customer data around the world. So sticking to data privacy laws is something we take extremely seriously. Every day we process the personal data of millions of customers. It's important that those individuals and businesses feel they can trust us to do the right thing with their data.

Being trusted with our customers' data goes further than making sure it's secure. It means preserving the integrity of the personal data we process. And only keeping the things we need to provide customers with the services they've signed up for. It also means being transparent around how we use that data, making sure the way we process personal data is legal, fair and in line with customers' rights and wishes.

As a communications provider we operate under a stringent 24-hour reporting regime to tell the UK Information Commissioner's Office (ICO) if we become aware of a personal data security breach. We must also tell any affected individuals as quickly as possible.

Different parts of the world approach privacy and data protection differently. Individuals' fundamental right to privacy is reflected in the fact that today data privacy laws are in force in over 100 countries. More and more we (and other multinationals) have to show that we're handling personal data in line with a complex tangle of national data laws and societal ethical expectations.

Potential impact

Failing to stick to data protection and privacy laws could result in possible regulatory enforcement action, fines, class-action, prison sentences and the regulator telling us to stop processing data.

On top of that, we could see huge reputational damage and big financial losses. Those losses could come from fines and damages if we fail to meet our legal requirements, as well as costs resulting from having to close customer contracts and the subsequent customer churn. Companies who've had high profile 'data incidents' have seen their share price hit hard, and suffered ongoing costs from their non-compliance.

Link to strategy and business model

- Deliver superior customer service **Trend:**

What's changed over the last year?

National regulators are more aggressively protecting their citizens' privacy and data protection rights. They're especially targeting companies who fail to do due diligence, or who knowingly accept (or ignore) a related risk for too long. This has been brought into sharp focus by the mushrooming of the data threat environment, with several big organisations suffering incidents.

There's been a general trend toward bigger financial penalties and more frequent public shamings for organisations that break global privacy and data protection laws. The UK Information Commissioner now issues more penalties than Ofcom.

How we're mitigating the risks

We've introduced governance to clarify accountabilities and responsibilities for data activities across the whole business. People, processes and technology have been our core areas of focus. By embedding this governance, we're reinforcing our expectations around personal data with our people, partners and third parties.

The cornerstone of our education and training programme is making sure our people understand our data governance culture and the impact of data risks on our business. Our mandatory data training focuses on individuals' roles, with relevant scenarios, helping highlight the varying data risks of different BT job families. By educating our technical and commercial units we've made a step change in understanding data risks across the group.

We want to give our people the tools they need to make everyday risk-based decisions around privacy and data protection without it being a burden or making their job more complicated. Because if we do that, there's a much better chance of data compliance being 'business as usual'. For example, using Privacy Impact Assessments when we develop new products and services makes sure everyone understands privacy issues from the start and builds in the right controls, without any operational impact.

Supporting the third-line assurance of our Internal Audit team, the Chief Privacy Officer and his team are a second line of defence. They undertake an annual cycle of audit and monitoring. That is overseen by the BT Compliance Programme Panel, who track and monitor everything until completion.

Health & safety

Our business – and in particular our vast engineering workforce – does a lot of work which is subject to health and safety regulation and enforcement by national authorities.

Potential impact

If we failed to implement and keep up effective health and safety management and governance, that could have a big impact on our people and our finances. It could lead to people getting injured, work-related sickness and service disruption for customers.

It could also lead to our people and third parties making compensation claims against us, or fines or other sanctions if we didn't stick to health and safety regulation. There could even be criminal prosecutions against us, our directors and our people – all of which would harm our brand and business.

And of course an unhappy or unhealthy workforce also leads to higher work absence rates and lower performance levels.

Link to strategy and business model

- Deliver superior customer service **Trend:**
- Transform our costs

What's changed over the last year?

The range and complexity of risks has gone up as we've offered new services to our customers. Those risks include us doing more construction and electrical engineering work on our own network, and the fact that we have new contracts which need our people to work to maintain and extend the UK's mobile network. We've taken a lot of steps to mitigate these risks – especially around how our people work with electricity or high off the ground.

We're building a plan to further embed health and safety into our operations. In the past year, we've seen major legislative change – particularly with the UK introducing Construction, Design and Management Regulations which place new responsibilities on organisations around making construction work safer. We've worked with the UK regulator and others in our sector to respond pragmatically to these demands. We've faced increased enforcement action against us this year, and also a few prosecutions initiated for past incidents.

How we're mitigating the risks

For the past five years we've busied ourselves implementing a Board-endorsed health, safety and wellbeing strategy. And each year, each line of business produces its own health and safety plan with its own targets and programmes.

Our people managers take responsibility for making sure their teams know how to comply with health and safety standards. We monitor compliance using annual licensing, scheduled refresher training, competency assessments and accreditation processes for higher risk groups. All BT people do training in basic health and safety.

Wherever we do business around the world, we put in place policies and programmes to make sure we stick to our own standards and that those standards meet or exceed minimum legal requirements.

Advice is provided to help management teams understand and control health and safety risks and help everyone feel involved in health, safety and wellbeing. We've created interventions to help promote good mental health and physical wellbeing. We also provide support and rehabilitation services for people who have mental or physical health issues. And we complement these measures with strong attendance management processes.

Case study: Privacy by design

Privacy by design is about building privacy into products and services. It helps organisations understand their privacy and data protection obligations. It also indicates a positive data compliance culture. The way we do privacy by design is through our Privacy Impact Assessment tool.

How we managed the risk

This year, we took a phased approach to embedding Privacy Impact Assessments within our various lines of business, starting with BT Consumer.

At the heart of our process is an online tool which each new product or service proposition must go through. It identifies what the proposition involves, what personal data is in scope and whether third parties will access that data. It also asks other tailored questions around marketing, big data analytics and customer communications. All that provides an initial insight into the risks.

Our privacy team follow this with an extra one-to-one review for more complex propositions. They must formally sign them off before they can move forward and get further development funding. This means our Privacy Impact Assessment process must be quick to make sure we can move fast to exploit commercial opportunities.

The result, and what we learned

From small system changes (for example in marketing) to large-scale projects (like our SmartTalk app) we've created Privacy Impact Assessments in line with industry best practice.

The Privacy team has had to learn to prioritise how they review Privacy Impact Assessments to meet launch timescales. The tool itself has been through various versions to make sure it meets the needs of people using it, with stage gates speeding up the flow of approval and sign off.

It's likely we'll need extra changes as we move to confirming the EU General Data Protection Regulation and what that'll mean for our business. But the Privacy Impact Assessment tool's flexibility will let us do that with minimal impact on the business.

Our viability statement

Assessment of prospects

An understanding of the group's business model and strategy are central to assessing its prospects, and details can be found on pages 21 to 30.

Our business model provides resilience that is relevant to any consideration of our prospects and viability. We have a broad spread of customers and suppliers across different geographic areas and market sectors, serving the needs of customers across 180 countries worldwide. In the UK, we benefit from diversification across a number of markets and products, which has increased in recent years, most notably through the launch of BT Sport and the acquisition of EE.

Our strategy of delivering superior customer service, transforming our cost base and investing for growth are all designed to support long term and sustainable cash flow growth.

We assess our prospects on a regular basis through our financial planning process. Our three-year Medium Term Plan forecasts the group's profitability, cash flows and funding requirements. The Medium Term Plan is reviewed by the Board twice during the year and the latest refresh includes forecasts related to our newly-acquired EE business. The Medium Term Plan is built from the 'bottom up' forecasts of each of our lines of business, supplemented by items managed at a group level and assumptions such as macro-economic activity and exchange rates. The performance of the group and our lines of business against these forecasts is monitored monthly and this is supplemented each quarter through a series of 'deep dive' Business Unit Reviews performed by the *Operating Committee*.

Viability statement

In accordance with provision C2.2 of the 2014 revision of the UK Corporate Governance Code, the directors have assessed the prospects and viability of the group.

Although the directors have no reason to believe that the group will not be viable over a longer period, the Board has chosen to conduct this review for a period of three years to 31 March 2019. The Board believes this is an appropriate timeframe as it aligns with the group's financial planning processes.

In support of this statement, we have stress tested our forecast cash flows by assessing the potential combined impact our most significant risks could have on these forecasts. This assessment was informed by our judgements as to the potential financial impact of these risks if they materialise, together with their likelihood of occurrence.

Our stress testing confirmed that in many of the scenarios tested, existing projected cashflows and cash management activities provide us with a buffer against the impact of these risks. In the most extreme scenarios we tested, where all of our principal risks are assumed to materialise over the three-year period, we have considered the further actions we could take to mitigate the negative cash flow impact and generate additional funding. These actions could include, for example, sale of assets, limiting or delaying discretionary capital expenditure and marketing activities, restricting share buy back programmes and reducing or ceasing dividend payments.

In our viability assessment we've adopted a number of assumptions designed to stress test our resilience. For example, in making our assessments of the impact and likelihood of our risks, we've only taken into account the control activities that we have in place today. We've not factored in any of the extensive future mitigation activity that we're undertaking to address these risks, thereby assuming such activity proves ineffective. We've also assumed that existing debt facilities which mature over the three-year period will not be renewed. While we don't expect this to happen, we've adopted these pessimistic assumptions to add greater stress to our viability testing.

Based on the results of this analysis, the directors have a reasonable expectation that the group will be able to continue in operation and meet its liabilities as they fall due over the three-year period of their assessment.

EE acquisition risks

Our acquisition of EE has introduced additional risks for BT beyond those captured in our principal risks and uncertainties. This year, given the acquisition has only recently completed, we've set out these risks separately. As the EE risks become more embedded in our Enterprise Risk Management framework, we'll integrate the reporting of these risks into our review of our principal risks and uncertainties.

Risks related to the acquisition

Although a number of the risks EE faces are similar in nature to those potentially impacting BT, there are also distinct risks that the group now faces that BT has not previously perceived to be significant threats.

This section outlines some of those new risks and uncertainties, but it is not exhaustive.

Realising acquisition synergies

We are targeting significant synergies from the acquisition, including operating cost savings and capital expenditure savings. Integrating the respective businesses is also expected to give rise to further benefits. These include fixed-mobile convergence, the ability to serve customers through a single, seamless platform supported by a single IP network, and being able to offer BT products to EE customers and EE products to BT customers.

The group's success will depend, in part, on the effectiveness of the integration process and the ability to realise the anticipated benefits and synergies from combining the businesses. Some of the potential challenges in integrating the businesses may not be known at this stage. If these challenges cannot be overcome, for example because of unforeseen difficulties in implementing fixed-mobile convergence or a lack of customer demand for the offerings, the anticipated benefits of the acquisition will not be fully achieved.

Realisation of synergies will depend partly on the rapid and efficient management and co-ordination of the activities of the group's businesses. We may experience difficulties in integrating EE with our existing businesses and may not realise, or it might take longer than expected to realise, certain or all of the perceived benefits of the acquisition. There's also a risk that synergy benefits and growth opportunities from the acquisition may fail to materialise, or may be materially lower than have been estimated. In addition, the costs of generating these synergies may exceed expectations. Further, we may not achieve the revenue or profitability that justify the original investment, which could result in material, non-cash write-downs. Failure to deliver the anticipated synergies and business opportunities could have a material adverse effect on our businesses, financial conditions and results of operations, including our ability to support our pension deficit, service our debt or to pay dividends.

Competition in the mobile market

Competition in the UK mobile telecommunications market is intense. Competition results from, among other things, the existence of established mobile network operators, market entry of alternative and lower cost carriers (such as mobile virtual network operators), technology developments (such as Voice over Internet Protocol (VoIP)), and the ability of other providers to bundle mobile phone services with different products and content (such as broadband and pay-TV). In particular, technologies such as VoIP and so-called 'over-the-top' platforms (such as iMessage, Facetime, Blackberry Messenger, WhatsApp and Facebook Messenger) could reduce voice and/or text messaging traffic on mobile networks, which could lead to significant price and revenue reductions.

Increased competition has led to a decline in the prices which EE charges for its mobile services and is expected to lead to further declines in pricing in the future. Competition could also lead to a reduction in the rate at which we add new mobile customers, a decrease in the size of our mobile market share and a decline in the group's service revenue as customers choose to receive telecommunications services or other competing services from other providers. Also, there's a risk of increased customer churn as a result of the transition away from the legacy T-Mobile and Orange brands and any potential changes to the branding in future. Churn could also increase as a result of potential Ofcom changes to the mobile switching regime in the UK. An increase in churn rates could adversely affect profitability because we would experience lower revenue and/or additional selling costs to replace customers or recapture lost revenue.

Delays in the deployment of new technologies

Our operations will depend partly on the successful deployment of continuously evolving telecommunications technologies, including handsets and network compatibility and components.

EE uses technologies from a number of vendors and incurs significant capital expenditure deploying these technologies. There can be no assurance that common standards and specifications will be achieved, that there will be interoperability across networks, that technologies will be developed according to anticipated schedules, that they'll perform according to expectations or that they will achieve commercial acceptance. The introduction of software and other network components may also be delayed. The failure of vendor performance or technology performance to meet our expectations or the failure of a technology to achieve commercial acceptance could result in additional capital expenditure, or a reduction in profitability.

Technology change and market acceptance

We may not succeed in making customers sufficiently aware of existing and future services or in creating customer acceptance of these services at the prices we would want to charge. Also, we may not identify trends correctly, or may not be able to bring new services to market as quickly or price-competitively as our competitors.

These risks exist in the mobile telecommunications area (eg mobile data services) and in non-mobile telecommunications areas (eg mobile payment services based on contactless technology) where there is a risk that differences in the regulatory treatment of different operators, based on their choice of technology, could put us at a competitive disadvantage.

Further, as a result of rapid technological progress and the trend towards technological convergence, new and established information and telecommunications technologies or products may not only fail to complement one another but in some cases, may even become a substitute for one another. An example of this is the risk that 'over-the-top' services (being those which are provided by a third party to the end-user device) develop substitutes for our own products and services. Another example is VoIP, a technology that is already established in the business customer market and which has now reached the consumer market. The availability of mobile handsets with VoIP functionality may adversely affect our pricing structures and market share in our mobile voice telephony business. If we don't appropriately anticipate the demand for new technologies, and adapt our strategies, service offering and cost structures accordingly, we may be unable to compete effectively, which may have an adverse effect on our business and operations.

Supplier and joint venture failure

EE has a number of suppliers identified as critical. EE is also party to a complex and critical network-sharing arrangement with Hutchison 3G UK Limited. The failure of this joint operation to fully support our interests and goals, or any material disruption to the operation of the EE network sharing arrangement, could cause significant harm to our business.

As demand for smartphone and tablet products increases around the world, there could be shortages in the volume of devices produced as a result of insufficient manufacturing capacity, the lack of availability of internal components such as processors or major supply chain disruptions. This may result in delays in the supply chain which in turn may have an adverse effect on our business and operations.

Regulation and spectrum

Regulators, including Ofcom, set annual licence fees for spectrum bands used by EE for voice calls, and data services. In future spectrum auctions, the costs of acquiring spectrum could increase or we may be unsuccessful in our bids. Any significant increases in spectrum pricing which apply to us could have a material adverse effect on our business and results of operations.

EE has been found to have significant market power in some areas of wholesale call termination following market reviews and, as is the case for all MNOs, EE's wholesale mobile termination rates are therefore regulated by Ofcom. The scope and form of the regulation is reviewed every three years.

EE is also subject to UK and European Union consumer-focused regulation in areas including: the international roaming services provided by EE; processes for consumer switching and non-geographic numbering call services. This regulation may affect the group's market share, competitive position, future profitability and cash.

As technology and market dynamics develop and as the mobile business of EE is integrated into BT, a wider range of existing regulations will apply to us and a broader range of new and/or modified regulations may be directed at us.

Network, licence and technology investment

EE (as well as the rest of BT to a lesser extent), has made substantial investments in the acquisition of licences and EE has invested in its mobile networks, including modernising its 2G network, the upgrade of its 3G network and the continued expansion of its 4G network. We expect to continue to make significant investments in our mobile networks due to increased usage and the need to offer new services and greater functionality. We may acquire new spectrum licences with licence conditions, which may include network coverage obligations or increased licence fees. Accordingly, the rate of our capital expenditure and costs in future years could increase and exceed those expected or experienced to date.

There can be no assurance that new services will be introduced according to anticipated schedules or that the level of demand for new services will justify the cost of setting them up (in particular, the cost of new spectrum licences and network infrastructure, for example, for 4G services and subsequent evolutions). Failure or a delay in completing networks and launching new services, or increases in the associated costs, could have an adverse effect on our business and operations and could result in significant write downs of the value of network spectrum or other licences or other network-related investments.

If the current economic climate worsens, we may decide, or be required, to scale back capital expenditure. A lasting reduction in capital expenditure levels below certain thresholds could affect our ability to invest in mobile telecommunications networks (including additional spectrum), new technology and other BT businesses and so could have an adverse effect on our future growth and the value of radio spectrum.

Transmission of radio waves from mobile telephones, transmitters and associated equipment

Media reports have suggested that radio frequency emissions from wireless mobile devices and mobile telecommunications sites may cause health issues, including cancer, and may interfere with some electronic medical devices, including hearing aids and pacemakers. Research and studies are ongoing. According to the World Health Organisation's Fact Sheet Number 193, last reviewed in October 2014, there are no known adverse effects on health from emissions at levels below internationally recognised health and safety standards. However, we cannot provide assurance that research in the future will not establish links between radio frequency emissions and health risks.

Whether or not research or studies conclude that there is a link between radio frequency emissions and health, popular concerns about radio frequency emissions may discourage the use of wireless devices, impairing our ability to retain customers and attract new customers, and may result in restrictions on the location and operation of mobile communications sites and the usage of our wireless technology. These concerns could also lead to litigation against us. Any restrictions on use or litigation could have an adverse effect on our business and operations.