

Registered Number: 2604354

O2 Holdings Limited

Annual Report and Financial Statements for the year ended 31 December 2011

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O2 Holdings Limited
Company information

Registered No 2604354

Directors

Robert Harwood
Maria Pilar López Alvarez
Enrique Medina Malo
David Melcon
Jesus Perez de Urquien (appointed on 23 August 2012)

Secretary

O2 Secretaries Limited

Registered office

260 Bath Road
Slough
Berkshire
SL1 4DX
UK

Auditor

Ernst & Young LLP
1 More London Place
London
SE1 2AF

O2 Holdings Limited Directors' report

Registered No 2604354

The Directors present their annual report and the audited financial statements for the year ended 31 December 2011

CORPORATE STRUCTURE

O2 Holdings Limited (the "Company") is a private limited company registered in England and Wales under the number 2604354. The registered address is 260 Bath Road, Slough, Berkshire SL1 4DX. It is a wholly owned subsidiary of mmO2 plc, a company incorporated in England and Wales. mmO2 plc is a wholly owned subsidiary of Telefónica S A, a company incorporated in Spain.

PRINCIPAL ACTIVITY

The principal activity of the Company during the year was to act as an intermediate holding company providing services to the Telefonica Europe Group. References to 'the Group' in this report refer to Telefonica Europe plc and its subsidiaries, of which the Company is a part.

The Company is expected to continue as an intermediate holding company for the foreseeable future.

BUSINESS REVIEW

Financial performance of the Company for the year ended 31 December 2011

The operating loss for the company has increased by £17 million year on year to £27 million in 2011 (31 December 2010: loss of £10 million).

The profit before tax of £125 million in 2011 has decreased by £35 million compared to the prior year. This reduction has been driven by lower interest income due from group companies, offset by higher interest payments due to group companies on intercompany loans.

Financial position of the Company as at 31 December 2011

The net assets of the Company at 31 December 2011 were £3,786 million compared to £12,427 million at 31 December 2010. Details of significant movements have been detailed below.

Other non-current assets have decreased by £6,557 million in 2011. The movement is wholly attributable to the repayment of an existing internal loan in full by Telefonica Europe plc, a related party.

Current liabilities have decreased by £149 million in 2011 to £8,656 million. This decrease has resulted mainly from the repayment of internal loans due to mmO2 Plc, an immediate parent company of O2 Holdings Limited and O2 Europe Plc, a related party, offset by interest accruing on outstanding internal loan balances with various companies within the Group.

Financial risk management objectives, policies and exposure

Details of the Group's approach to financial risk management are set out in the financial statements in note 20 "Financial instruments"

Going Concern

The Company's business activity is to act as an intermediate holding company within the Telefónica Group. The financial position of the Company is described in this report. In addition, note 20 to the financial statements includes the Company's objectives, policies and processes for managing its financial risk management objectives, details of its financial instruments and its exposures to credit risk and liquidity risk. As a consequence, the Directors believe that the Company is well placed to manage its business risk successfully despite the current uncertain economic outlook.

The Directors have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future; thus they continue to adopt the going concern basis of accounting in preparing the annual financial statements.

Risks and uncertainties

From the perspective of the Company, the principal risks and uncertainties are integral to the principal risks and uncertainties of the Group and are not managed separately. A comprehensive analysis of the principal risks and uncertainties which impact the Group are disclosed in the consolidated Annual Report and financial statements of mmO2 plc, the Company's immediate parent Company.

Results

The audited financial statements are presented on pages 11 to 38.

DIVIDENDS

During the year ended 31 December 2011 the directors declared and paid interim dividends totalling £8,775,305,718 (year ended 31 December 2010: £nil).

SUBSEQUENT EVENT

On 23 August 2012 Jesus Perez de Urquien was appointed a director of the Company.
On 31 August 2012 Edward Smith resigned as director of the Company.
On 18 September 2012, O2 Holdings transferred its total number of shares (10 shares) in Cellular Radio Ltd to O2 Networks Limited (8 shares) and O2 Cedar Limited (2 shares). O2 Networks Limited is 100% owned by O2 Holdings Limited and O2 Cedar Limited is 100% indirect investment.

DIRECTORS AND SECRETARIES

The Directors who held office during the year and currently, except where shown otherwise are as follows:

| | |
|---------------------------|---|
| Antonio Martí Ciruelos | (appointed 6 September 2011 and resigned 1 October 2011) |
| Robert Harwood | |
| Katherine Ann Jarvis | (resigned 17 November 2011) |
| Maria Pilar López Álvarez | (resigned 31 July 2011 and re-appointed 1 October 2011) |
| Enrique Medina Malo | (appointed 17 November 2011) |
| David Melcon | |
| Edward Smith | (appointed 17 November 2011 and resigned on 31 August 2012) |

O2 Secretaries Limited served as secretary throughout the year.

DIRECTORS' LIABILITY INSURANCE AND INDEMNITY

Telefonica Europe plc, the Company's ultimate UK parent company, has granted an indemnity in the form permitted by UK Company Law to Directors appointed to subsidiary companies. This indemnity remains in place and continues until such time as any relevant limitation periods for bringing claims (as defined in the indemnity) against the Director has expired, or for so long as the past Director, where relevant, remains liable for any losses (as defined in the indemnity).

SHARE CAPITAL

Details of the issued share capital of the Company at 31 December 2011 are given in note 17 to the financial statements.

REDUCTION OF CAPITAL

On 17 October 2011 the amount standing in credit in the share premium account being £15,718,000,000 was reduced to nil, in accordance with Section 642 of the Companies Act 2006 reduction of capital by special resolution supported by solvency statement.

INTEREST OF MANAGEMENT IN CERTAIN TRANSACTIONS

During and at the end of the year ended 31 December 2011, none of the Company's Directors had a significant interest in any material transaction in relation to the Group's business.

EMPLOYEES

The Company has a wide range of communication channels with employees including face-to-face meetings, team briefings, audio conferences and a comprehensive intranet with tailored content dependent on employee segmentation. The aim of all these channels is to ensure employees fully understand the Company's objectives and its operational and financial performance as well as our latest products and services, whilst creating an inclusive employee culture. In addition the Company conducts an annual engagement survey with additional regular temperature checks and maintains a constructive dialogue with unions, employee representative bodies and works councils.

The employee experience is paramount and the Company continues to be committed to the development of all people in the organisation, actively promoting this through many training and development initiatives. People are encouraged and supported in maintaining personal development plans. The Company has invested in e-learning technology to give people better access to a wide range of learning opportunities.

The Company is committed to employment policies that follow best practice, based on equal opportunities for all, and recognises the diversity of its people. This approach includes the fair treatment of people with disabilities in relation to their recruitment, training and development. The Company has also invested in researching age, gender and disability diversity across the organisation, seeking to support all employees and their career development at every level of the organisation.

COMMUNITY INVOLVEMENT

During the year ended 31 December 2011, the mmO2 plc group, of which O2 Holdings is a part, made donations to charitable and community organisations totalling £2,085,525 of which £1,435,400 was made from UK based companies. As in previous years, no political donations were made.

POLICY ON THE PAYMENT OF SUPPLIERS

The Company aims to pay all of its creditors promptly. The payment terms for major contracts are agreed at the same time as other terms are negotiated with individual suppliers.

STATEMENT OF DIRECTORS' RESPONSIBILITIES

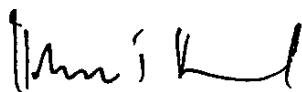
A statement by the Directors of their responsibilities for preparing the annual report and the financial statements is included on page 8.

AUDITOR

Pursuant to a shareholders' resolution passed on 4 February 2002, the Company is not obliged to re-appoint its auditor annually.

So far as each Director is aware, there is no relevant audit information of which the Company's auditor was unaware. The Directors have taken all the steps that they ought to have taken as Directors in order to make themselves aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

By Order of the Board



Robert Harwood
For and on behalf of
O2 Secretaries Limited
Company Secretary
26 September 2012

O2 Holdings Limited
Statement of Directors' responsibilities

Registered No 2604354

The Directors are responsible for preparing the Annual Report and the Company financial statements in accordance with applicable United Kingdom law and those International Financial Reporting Standards as adopted by the European Union

Under Company Law the Directors must not approve the Company financial statements unless they are satisfied that they present fairly the financial position, financial performance and cash flows of the Company for that period. In preparing the Company financial statements the Directors are required to

- select suitable accounting policies in accordance with IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors and then apply them consistently,
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information,
- provide additional disclosures when compliance with the specific requirements in IFRSs is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the Company's financial position and financial performance,
- state that the Company has complied with IFRSs, subject to any material departures disclosed and explained in the financial statements, and
- make judgements and estimates that are reasonable and prudent

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the Company financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Independent Auditor's Report to the members of O2 Holdings Limited

We have audited the financial statements of O2 Holdings Limited for the year ended 31 December 2011 which comprise the Statement of Comprehensive Income, the Statement of Financial Position, the Statement of Changes in Equity, the Statement of Cash Flows and the related notes 1 to 26. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

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

Respective responsibilities of directors and auditor

As explained more fully in the Statement of Directors' responsibilities set out on page 8, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of whether the accounting policies are appropriate to the company's circumstances and have been consistently applied and adequately disclosed, the reasonableness of significant accounting estimates made by the directors, and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the annual report and financial statements to identify material inconsistencies with the audited financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on financial statements

In our opinion the financial statements

- give a true and fair view of the state of the company's affairs as at 31 December 2011 and of its loss for the year then ended,
- have been properly prepared in accordance with IFRSs as adopted by the European Union, and
- have been prepared in accordance with the requirements of the Companies Act 2006

O2 Holdings Limited

Registered No 2604354

**Independent Auditor's Report to the members of O2 Holdings Limited
(continued)**

Opinion on other matter prescribed by the Companies Act 2006

In our opinion the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us, or
- the financial statements are not in agreement with the accounting records and returns, or
- certain disclosures of directors' remuneration specified by law are not made, or
- we have not received all the information and explanations we require for our audit

ERNST & YOUNG LLP

Marcus Butler (Senior statutory auditor)
for and on behalf of Ernst & Young LLP, Statutory Auditor
London

27 September 2012

Statement of Comprehensive Income
Year ended 31 December 2011

| | Note | Year ended 31 December 2011 £m | Year ended 31 December 2010 £m |
|---|------|---|---|
| Other operating income | | 94 | 161 |
| Administrative expenses | | (121) | (171) |
| Operating loss | 2 | (27) | (10) |
| Financial income | 3 | 246 | 262 |
| Financial expense | 3 | (94) | (92) |
| Profit before taxation | | 125 | 160 |
| Taxation charge | 4 | 9 | (26) |
| Profit for the year attributable to equity shareholders of the parent | | 134 | 134 |
| Other Comprehensive Income | | | |
| Actuarial gain/(loss) on defined benefit pension plans | 15 | - | - |
| Deferred tax on amounts recognised in reserves | 16 | - | 1 |
| Other comprehensive income for the year, net of tax | | - | 1 |
| Total comprehensive income for the year attributable to the equity holders of the parent | | 134 | 135 |

The accompanying notes are an integral part of these financial statements

**Statement of Financial Position
As at 31 December 2011**

| | | 31 December 2011 £m | 31 December 2010 £m |
|--|------|---------------------------|---------------------------|
| | Note | | |
| Non-current assets | | | |
| Investments in subsidiary undertakings | 5 | 11,422 | 11,422 |
| Property, plant and equipment | 7 | - | 1 |
| Other intangible assets | 8 | 35 | 28 |
| Deferred tax assets | 16 | 5 | 5 |
| Other non-current assets | 9 | - | 6,557 |
| | | 11,462 | 18,013 |
| Current assets | | | |
| Trade and other receivables | 10 | 1,001 | 3,128 |
| Cash and cash equivalents | 11 | 1 | 118 |
| | | 1,002 | 3,246 |
| Current liabilities | | | |
| Borrowings | 12 | (8,330) | (8,493) |
| Trade and other payables | 13 | (317) | (293) |
| Provisions | 14 | (9) | (19) |
| | | (8,656) | (8,805) |
| Net current liabilities | | (7,654) | (5,559) |
| Total assets less current liabilities | | 3,808 | 12,454 |
| Non-current liabilities | | | |
| Retirement benefit obligations | 15 | (5) | (5) |
| Borrowings | 12 | (12) | - |
| Provisions | 14 | (5) | (22) |
| | | (22) | (27) |
| Net assets | | 3,786 | 12,427 |
| Equity | | | |
| Ordinary share capital | 17 | 12 | 12 |
| Share premium | | 0 | 15,718 |
| Retained earnings | | 3,774 | (3,303) |
| Total equity | | 3,786 | 12,427 |

The accompanying notes are an integral part of these financial statements

These financial statements were approved by the Board of Directors on 26 September 2012 and were signed on its behalf by



David Melcon Sanchez-Friera

Director

Statement of Changes in Equity
Year ended 31 December 2011

| Company | Ordinary share capital £m | Share premium £m | Retained earnings £m | Total Equity £m |
|---|---------------------------------|------------------------|----------------------------|--------------------|
| At 1 January 2010 | 12 | 15,718 | (3,438) | 12,292 |
| Total comprehensive income for the year | - | - | 135 | 135 |
| At 31 December 2010 | 12 | 15,718 | (3,303) | 12,427 |
| Share capital reduction | | (15,718) | 15,718 | 0 |
| Dividend paid | | | (8,775) | (8,775) |
| Total comprehensive income for the year | | | 134 | 134 |
| At 31 December 2011 | 12 | 0 | 3,774 | 3,786 |

On 17th October 2011, in accordance with section 642 of the Companies Act 2006, the Company reduced to nil the amount standing in credit in the share premium account being £15,718m by special resolution supported by solvency statement

The accompanying notes are an integral part of these financial statements

Statement of Cash Flows
Year ended 31 December 2011

| | | Year ended 31 December 2011 £m | Year ended 31 December 2010 £m |
|---|------|---|---|
| | Note | | |
| Operating loss | | (27) | (10) |
| Depreciation and amortisation charges | 7, 8 | 12 | 6 |
| Decrease / (Increase) in trade and other receivables | 10 | (2) | 55 |
| Increase in trade and other payables | 13 | 24 | (3) |
| Decrease in Provisions | 14 | (27) | - |
| Net cash flow generated / (used) by operating activities | | (20) | 48 |
| Increase in intangible assets | 8 | (17) | (16) |
| Dividends (paid)/received | 6 | (8,775) | 5 |
| Net cash flow used in investing activities | | (8,792) | (11) |
| Proceeds from repayment of loans/ Increase in borrowings | | 8,713 | 505 |
| Interest paid | | (18) | (3) |
| Net cash flow generated / (used) by financing activities | | 8,695 | 502 |
| Net increase/(decrease) in cash and cash equivalents | | (117) | 539 |
| Cash and cash equivalents at start of the year | 11 | 118 | (421) |
| Cash and cash equivalents at end of the year | 11 | 1 | 118 |

The accompanying notes are an integral part of these financial statements

1. Accounting policies

Basis of preparation

These financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") and International Financial Reporting Interpretations Committee ("IFRIC") interpretations, as adopted for use in the EU. In addition the financial statements have been prepared in accordance with those parts of the Companies Act 2006 applicable to companies reporting under IFRS. The financial statements have been prepared using historical cost principles except that, as disclosed in the accounting policies below, certain items are measured at fair value.

The principal accounting policies of the Company applied in the preparation of these financial statements are set out below. The IFRS accounting policies have been applied consistently to all periods presented.

Consolidated financial statements

In accordance with s400 of the Companies Act 2006, consolidated financial statements have not been prepared as the Company and its subsidiaries are included in the group financial statements of Telefónica S.A.

The principal accounting policies of the Company applied in the preparation of these financial statements are set out below. The IFRS accounting policies have been applied consistently to all periods presented.

Property, plant and equipment

Property, plant and equipment are stated at historical cost less depreciation and any accumulated impairment losses, where applicable. The cost of property, plant and equipment includes directly attributable incremental costs incurred in its acquisition and installation and also the initial estimate of costs of dismantling, removing the item and restoring the site on which it is located. Subsequent costs are included in the assets' carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Company and the cost of the item can be measured reliably. Interest and other financial expenses incurred and directly attributable to the acquisition or construction of qualifying assets are capitalised.

Depreciation is provided on property, plant and equipment from the date they are available for use over their estimated useful lives on a straight-line basis. The lives assigned to property, plant and equipment are:

| | |
|--------------------------------|--------------|
| Computers and office equipment | 2 to 6 years |
|--------------------------------|--------------|

The assets' useful lives and residual values are reviewed, and adjusted if appropriate, at each statement of financial position date.

Other intangible assets

Software

Software is capitalised and measured at the cost incurred to acquire and bring into use the specific software. These costs are amortised over their estimated useful lives of between 2 and 6 years on a straight line basis. Costs that are directly associated with the production of identifiable unique software products controlled by the Company, which are expected to generate economic benefits over a period of more than one year, are recognised as intangible assets. Computer software development costs recognised as intangible assets are amortised over their estimated useful lives not exceeding 6 years on a straight line basis.

1. Accounting policies (continued)

Investments

Investments are stated at cost less provision for impairment. An impairment loss is recognised for the amount by which the investment's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an investment's fair value less costs to sell and value in use.

Impairment of non financial assets

Assets that have an indefinite useful life are not subject to amortisation and are tested annually for impairment. Assets with a definite useful life are reviewed for impairment whenever events or changes in circumstances indicate that their carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows ("cash-generating units").

Foreign currencies

Transactions denominated in foreign currencies are translated at the exchange rate on the day the transaction occurred to the functional currency of the entity. Monetary assets and liabilities denominated in foreign currencies are translated at the rates ruling at the statement of financial position date.

Foreign exchange differences arising on translation are recognised in the income statement. Non-monetary assets and liabilities denominated in foreign currency are translated at the foreign currency exchange rate ruling at the dates the non-monetary assets and liabilities are recognised.

Employee benefits

Employee benefits - Pension obligations

The Company operates both defined benefit and defined contribution plans. A defined benefit plan generally provides pensions based on the employee's length of service and their final pensionable salary. A defined contribution plan offers employees individual funds which are converted into pension benefits on retirement.

The company participates in the Telefonica Pension Plan ("Telefonica PP"), a scheme sponsored by Telefonica Europe plc that provides benefits for the majority of the UK employees in the Telefonica Europe plc group. The Telefonica PP has both defined benefit and defined contributions sections and covers all employees of the Group. The defined benefit sections are closed to new entrants. The assets of the schemes are held independently of the Company's finances.

In its capacity as a participating employer in the defined contribution section of the Telefonica PP, the Company pays contributions into the Plan on behalf of the employees. The Company has no further payment obligations once the contributions have been paid. The contributions are recognised as an asset to the extent that a cash refund or a reduction in the future payments is available.

Companies within the Group account for the defined benefit sections of the Telefonica Pension Plan as though it were a defined contribution plan as there is no arrangement for charging out the net defined benefit cost between participating employers. The net defined benefit cost of the defined benefit sections, as assessed in accordance with the advice of a qualified, independent actuary using the projected unit method and taking assets at market value, is recognised by the sponsoring employer. Accordingly the defined benefit liability or asset of the Telefonica PP is not recognised on the statement of financial position of the Company as the sponsoring employer is Telefonica Europe plc. Disclosures of the defined benefit sections of the Telefonica PP are provided in note 14. Additional disclosure in line with the requirements of IAS 19 for both the current and previous accounting periods is provided in the consolidated Annual Report and financial Statements of mmO2 plc for the year ended 31 December 2011.

1. Accounting policies (continued)

Share based payments

The Group recognises an expense for share awards and share options, which are both equity and cash settled, based on the fair value of the share awards or share options granted as compensation for the services rendered by employees. The fair value is calculated at the grant date using an adjusted statistical model and excludes the impact of non-market conditions. Instead, the expense is adjusted for the effect of non-market conditions at each reporting date through the number of share awards or share options expected to be exercisable. The effect of market and non-vesting conditions is included in the fair value at the date of grant and is recognised as an expense irrespective of whether the market or non-vesting condition is satisfied. Any proceeds received are credited to share capital and share premium when the share option or award are exercised. In addition, for cash-settled share based payment transactions, the Group measures the services received and the liability incurred at the fair value of the liability. Until the liability is settled, the Group remeasures the fair value of the liability at each reporting date and at the date of settlement, with any changes in fair value recognised in the consolidated statement of comprehensive income for the period.

Taxation

The charge for current tax is based on the results for the year as adjusted for items which are non-assessable or disallowed.

Deferred income tax is provided in full, using the balance sheet liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred tax liabilities are recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable future taxable profits will be available against which deductible temporary differences can be utilised.

Deferred income tax is provided on temporary differences arising on investments in subsidiaries and associates, except where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred income tax and current tax is determined using tax rates (and laws) that have been enacted or substantively enacted by the date of the statement of financial position and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Income tax relating to items recognised directly in other comprehensive income is also recognised directly in other comprehensive income.

Cash and cash equivalents

Cash and cash equivalents are carried in the statement of financial position at cost. Cash and cash equivalents includes cash in hand, deposits held at call with banks, and other short-term highly liquid investments with original maturities of three months or less, and bank overdrafts. Bank overdrafts are shown within borrowings in current liabilities on the statement of financial position.

Provisions

Provisions are recognised when the Company has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation and a reliable estimate of the amount can be made. If the effect of the time value of money is material, provisions are discounted using a current pre-tax rate that reflects, where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognised as a finance cost.

The Company recognises a provision for exceptional contractual costs when the expected benefits to be derived from a contract are less than the unavoidable costs of meeting the obligations under the contract. Restructuring provisions comprise employee termination payments, and these are recognised in the period in which the Company becomes legally or constructively committed to payment.

1 Accounting policies (continued)

Borrowings

Borrowings are recognised initially at fair value. Subsequent to initial recognition, borrowings are stated at amortised cost with any difference between the cost and the redemption value being recognised in the income statement over the period of the borrowings on an effective interest basis. Accrued interest on borrowings is included within the carrying value.

Dividends

Dividend distributions to the Company's shareholders are recognised as a liability in the Company's financial statements in the period in which the dividends are approved by the Company's shareholders.

New IFRS and interpretations of the International Financial Reporting Interpretations Committee (IFRIC)

The accounting policies adopted are consistent with those of the previous financial year.

At the date of preparation of the financial statements the following IFRS and IFRIC interpretations have been published, but their application is not mandatory.

| Title | Effective date (annual periods beginning on or after) |
|---|---|
| Effective for annual periods (and interim periods therein) ending 30 June 2012 or thereafter | |
| IFRS 9 - Financial Instruments | 1 January 2015 |
| Amendments to IFRS 7 - Disclosures - Transfers of financial assets | 1 July 2011 |
| Amendments to IAS 12 - Deferred Tax Recovery of Underlying Assets | 1 January 2012 |
| IFRS 10 - Consolidated Financial Statements | 1 January 2013 |
| IFRS 11 - Joint Arrangements | 1 January 2013 |
| IFRS 12 - Disclosure of Interests in Other Entities | 1 January 2013 |
| IFRS 13 - Fair Value Measurement | 1 January 2013 |
| IAS 27 (Revised) - Separate Financial Statements | 1 January 2013 |
| IAS 28 (Revised) - Investments in Associates and Joint Ventures | 1 January 2013 |
| Amendment to IAS 1 - Presentation of Items of Other Comprehensive Income | 1 July 2012 |
| IAS 19 (Revised) - Employee Benefits | 1 January 2013 |
| Amendment to IAS 32 - Offsetting Financial Assets and Financial Liabilities | 1 January 2014 |
| Amendments to IFRS 7 - Offsetting Financial Assets and Financial Liabilities | 1 January 2013 |

1 Accounting policies (continued)

Critical accounting estimates and judgements

The preparation of financial statements in accordance with IFRS requires the use of certain critical accounting estimates and assumptions. It also requires management to exercise judgement in the process of applying the Company's accounting policies. A significant change in the facts and circumstances on which these estimates are based could have a material negative impact on the Company's earnings and financial position. The areas involving a higher degree of judgement or complexity and areas where assumptions and estimates are significant to the financial statements are discussed below.

Provisions

Provisions are recognised when an event in the past gives rise to a current obligation for the Company, the settlement of which requires an outlay that is considered probable and can be estimated reliably. This obligation may be legal or constructive, deriving from regulations, contracts, normal practices or public commitments that lead third parties to reasonably expect that the Company will assume certain responsibilities. The amount of the provision is determined based on the best estimate of the outflow of resources required to settle the obligation, taking into account all available information.

No provision is recognised if the amount of liability cannot be estimated reliably. In this case, the relevant information is disclosed in the notes to the financial statements.

Given the uncertainties inherent in the estimates used to determine the amount of provision, actual outflows of resources may differ from the amounts recognised originally on the basis of the estimates.

Impairment of investments

An impairment exists when the carrying value of a cash generating unit exceeds its recoverable amount, which is the higher of its fair value less costs to sell and its value in use. The value in use calculation is based on a discounted cash flow model. The cash flows are derived from forecasts. The recoverable amount is most sensitive to the discount rate used in the discounted cash flow model as well as the expected cash inflows and the growth rate used for extrapolation purposes.

2. Operating loss

| | Year ended 31 December 2011 £m | Year ended 31 December 2010 £m |
|--|---|---|
| Operating loss is stated after charging / (crediting) | | |
| Total amortisation of other intangible assets (note 8) | 10 | 6 |
| Management charges to Group undertakings | (90) | (161) |
| Employee benefit expense (note 23) | 30 | 3 |

Management charges to Group undertakings represent recharges for services provided to fellow group companies within the Group. These services include use of the brand and other centrally provided services. Further details of intercompany loans and trading balances are included within note 18.

3. Net financial income

| | Year ended 31 December 2011 £m | Year ended 31 December 2010 £m |
|--|---|---|
| Interest income on loans to subsidiaries and other related parties (note 18) | 183 | 182 |
| Interest income on loans to immediate parent company (note 18) | 50 | 52 |
| Dividends received from subsidiary companies | - | 5 |
| Foreign exchange differences | 13 | 23 |
| Financial income | 246 | 262 |
| Interest expense on borrowings from subsidiaries and other related parties (note 18) | (86) | (85) |
| Interest expense on borrowings from immediate parent company (note 18) | (6) | (5) |
| Foreign exchange differences | (2) | (2) |
| Financial expense | (94) | (92) |
| Net financial income | 152 | 170 |

4. Taxation

The analysis of charge for the year is as follows

| | Year ended 31-Dec-11 £m | Year ended 31-Dec-10 £m |
|--|-------------------------------|-------------------------------|
| Current tax - UK tax | (3) | 10 |
| Current tax - adjustments in respect of prior periods | (6) | 15 |
| Deferred tax - origination and reversal of temporary differences | 2 | 1 |
| Deferred tax - adjustments in respect of prior periods | (2) | - |
| Taxation – charge / (credit) for the year | (9) | 26 |

4. Taxation (continued)

The tax assessed for the period varied from the amount computed by applying the corporation tax standard rate to profit on ordinary activities before taxation. The difference was attributable to the following factors

| | Year ended 31-Dec-11 £m | Year ended 31-Dec-10 £m |
|---|-------------------------------|-------------------------------|
| Profit before taxation | 125 | 160 |
| Profit on ordinary activities multiplied by the effective rate of UK corporation tax of 26.5% (2009 28%) | 33 | 45 |
| Expenses not deductible for tax purposes | 1 | 12 |
| Non-taxable income | - | (2) |
| UK-UK transfer pricing adjustments | (35) | (44) |
| Adjustments in respect of prior periods | (8) | 15 |
| Taxation – charge/(credit) for the year | (9) | 26 |

The statutory rate of corporation tax in the UK will reduce to 24% from 26% with effect from 1 April 2012. Deferred tax assets and liabilities in the UK have been re-calculated at the tax rate appropriate to when they are expected to reverse.

5. Investments in subsidiary undertakings

| | Shares in subsidiary undertakings £m |
|---|---|
| Cost | |
| At 1 January 2010 and 31 December 2010 | 14,323 |
| Additions | - |
| At 31 December 2011 | 14,323 |
| Impairment | |
| At 1 January 2010, 31 December 2010, 31 December 2011 | (2,901) |
| Net book value | |
| At 31 December 2011 | 11,422 |
| At 31 December 2010 | 11,422 |

The Directors consider that disclosing full particulars of all subsidiary undertakings would lead to a statement of excessive length. A list of principal subsidiary undertakings is given in note 19.

6. Dividends paid

| | Year ended 31-Dec 2011 £m | Year ended 31-Dec 2010 £m |
|---|--|--|
| Interim dividend for year ended 31 December 2011 £731 per share | 8,775 | - |
| Interim dividend for year ended 31 December 2010 | - | - |
| | 8,775 | - |

The interim dividends were declared and approved by the Company during the year ended 31 December 2011. The total cash dividend amount was £8,775 million. No other dividends were approved or paid in the year ended 31 December 2011.

7. Property, plant and equipment

| | Computer Equipment £m |
|---|--------------------------------------|
| Cost | |
| <i>At 1 January 2010 and 31 December 2010</i> | 5 |
| <i>Additions</i> | - |
| At 31 December 2011 | 5 |
| Amortisation and impairment | |
| <i>At 1 January 2010 and 31 December 2010</i> | 4 |
| <i>Charge for the year</i> | 1 |
| At 31 December 2011 | 5 |
| Net book value | |
| At 31 December 2011 | 0 |
| <i>At 31 December 2010</i> | 1 |

8 Other intangible assets

| | Software | Assets in course of construction | Other | Total |
|------------------------------------|-----------|--|----------|-----------|
| | £m | £m | £m | £m |
| Cost | | | | |
| At 1 January 2010 | 13 | 16 | - | 29 |
| Additions | - | 16 | - | 16 |
| Reclassifications | 11 | (13) | 2 | - |
| At 31 December 2010 | 24 | 19 | 2 | 45 |
| Additions | 17 | 0 | - | 17 |
| Reclassifications | 15 | -15 | - | - |
| At 31 December 2011 | 56 | 4 | 2 | 62 |
| Amortisation and impairment | | | | |
| At 1 January 2010 | 11 | - | - | 11 |
| Charge for the year | 5 | - | 1 | 6 |
| At 31 December 2010 | 16 | - | 1 | 17 |
| Charge for the year | 10 | - | 1 | 11 |
| At 31 December 2011 | 26 | - | 1 | 27 |
| Net book value | | | | |
| At 31 December 2011 | 30 | 4 | - | 35 |
| At 31 December 2010 | 8 | 19 | 1 | 28 |

9. Other non-current assets

| | 31 December 2011 £m | 31 December 2010 £m |
|---|---------------------------|---------------------------|
| Amounts owed by other related parties (note 18) | - | 6,557 |
| | - | 6,557 |

During the year the existing loan to Telefonica Europe plc, was repaid. This was a sterling denominated loan with an effective interest rate of 2.8% (31 December 2010 2.8%).

O2 Holdings Limited
Notes to the financial statements (continued)

Registered No 2604354

10. Trade and other receivables

| | 31 December 2011 £m | 31 December 2010 £m |
|--|---------------------------|---------------------------|
| Amounts owed by immediate parent company (note 18) | - | 2,129 |
| Amounts owed by subsidiaries (note 18) | 802 | 858 |
| Amounts owed by other related parties (note 18) | 170 | 102 |
| Prepayments | 29 | 39 |
| | 1,001 | 3,128 |

During the year the existing several loans to mmO2 plc, were repaid. These loans were denominated in Sterling, EUR and USD.

11 Cash and cash equivalents

| | 31 December 2011 £m | 31 December 2010 £m |
|----------------------------------|---------------------------|---------------------------|
| Short term deposits | 1 | 118 |
| Cash and cash equivalents | 1 | 118 |

The Company's short term deposits are funds deposited with Telefónica Finanzas S A, a related party. The Company's bank accounts are swept daily and deposited over night with the related party. If the short term deposits account is overdrawn at year end, the balance is included within borrowings in current liabilities on the statement of financial position.

12 Borrowings

| | 31-Dec 2011 £m | 31-Dec 2010 £m |
|--|----------------------|----------------------|
| <i>Current unsecured borrowings</i> | | |
| Amounts owed to immediate parent company (note 18) | - | 62 |
| Amounts owed to subsidiaries (note 18) | 8,330 | 8,278 |
| Amounts owed to other related parties (note 18) | - | 153 |
| | 8,330 | 8,493 |
| <i>Non-Current unsecured borrowings</i> | | |
| Amounts owed to immediate parent company (note 18) | - | - |
| Amounts owed to subsidiaries (note 18) | - | - |
| Amounts owed to other related parties (note 18) | 12 | - |
| | 12 | - |

The Company listed a £4,030 million floating rate bond in October 2005 on the Irish Stock Exchange with a maturity date of July 2006 which was subsequently extended to December 2007. Interest was based on 12 month Sterling LIBOR plus 42 basis points per annum on the outstanding principal amount (compounded annually), but was subject to a maximum 3 month Sterling LIBOR plus 200 basis points per annum.

On 14 December 2007 the bond was delisted from the Irish Stock Exchange. The bond was wholly held by an indirect subsidiary of the Company, O2 Third Generation Holdings Limited. From the date of delisting the bond reverted to an interest free intercompany balance.

The non current borrowings balance is made up of intra-group interest free payable to O2 Communications Ireland.

13. Trade and other payables

| | 31 December 2011 £m | 31 December 2010 £m |
|--|---------------------------|---------------------------|
| Trade payables | - | - |
| Amounts owed to immediate parent company (note 18) | - | 82 |
| Amounts owed to subsidiaries (note 18) | 45 | 5 |
| Amounts owed to other related parties (note 18) | 143 | 108 |
| Other payables | 11 | 5 |
| Accrued expenses | 118 | 93 |
| | 317 | 293 |

14. Provisions

A breakdown of the Company's current and non-current provisions is as follows

| | 31 December 2011 £m | 31 December 2010 £m |
|-------------|---------------------------|---------------------------|
| Current | 9 | 19 |
| Non-current | 5 | 22 |
| | 14 | 41 |

| | Contractual £m | Other £m |
|--|-------------------|-------------|
| At 1 January 2010 and 31 December 2010 | 39 | 2 |
| Charge for the year | (27) | - |
| At 31 December 2011 | 12 | 2 |

15 Pension costs

The Company participates in the Telefonica Pension Plan (Telefonica PP) and an unfunded defined benefit scheme. In addition, Telefónica Europe plc, its ultimate UK parent company, sponsors a group-wide defined benefit scheme, the Telefónica Pension Plan, in which employees of the Company are members and therefore the Company has been recharged the contributions payable into the scheme for the period. The retirement benefit obligation of the defined benefit scheme is recorded on the statement of financial position of Telefónica Europe plc.

The Telefonica Pension Plan

The Telefonica Pension Plan (Telefonica PP) provides the pension benefits for the majority of UK employees and is divided into defined contribution and defined benefit sections. Since 14 March 2005, the sponsoring employer of the scheme has been Telefonica Europe plc, prior to this the sponsoring employer was mmO2 plc. As mmO2 plc was the sponsoring employer of the Telefonica PP until 14 March 2005, the full net defined benefit cost and defined benefit liability was recognised by mmO2 plc until this date. After 14 March 2005 the defined benefit liability was transferred to Telefonica Europe plc, the new sponsoring employer.

The defined benefit sections of the Telefonica PP are closed to new entrants and therefore the current service cost is likely to increase, as a percentage of payroll, as the members approach retirement.

15. Pension costs (continued)

Companies within the mmO2 Group account for the defined benefit sections of the Telefonica PP as though it were a defined contribution plan as there is no contractual arrangement or stated policy for charging out the net defined benefit cost between participating employers. The net defined benefit cost of the defined benefit sections, as assessed in accordance with the advice of a qualified, independent actuary, measuring actuarial liabilities using the projected unit method and taking assets at market value, is recognised by the sponsoring employer. Accordingly the defined benefit liability or assets of the Telefonica PP is not recognised on the statement of financial position of the Group as the sponsoring employer is Telefonica Europe plc.

Actuarial valuation

A full valuation of the defined benefit sections of the Telefonica PP was undertaken as at 30 September 2008 by a suitably qualified independent actuary. The valuation used the projected unit method and set a future funding plan to ensure that contributions to the Plan meeting future liabilities and past service liabilities are adequately funded.

The valuation was completed in conjunction with a change in the investment strategy of the Plan from a predominantly performance asset basis to a predominantly corporate bond basis. As a result of the investment changes, inter-valuation experience and the development of actuarial assumptions the ongoing contribution rate was increased to 26.7% of defined benefit members' payroll. Based on the difference between the September 2008 pension asset value and the technical provisions a past service deficit of £187 million resulted. It was agreed that this deficit will be recovered by additional contributions over the period to 2015 totalling £243 million. £40.5 million is required to be contributed annually over the period 2012 to 2015 inclusive (2011: £45.2 million, 2010: £36 million) in accordance with the schedule of contributions contract dated 19 July 2011. These contributions are in line with the preceding schedule of contributions contract dated 24 December 2009.

The expected amount to be paid to the Telefonica PP defined benefit scheme by the mmO2 group during 2012 is £69 million.

Disclosures – Telefonica PP

Disclosures of the defined benefit sections of the Telefonica PP are provided below. Additional disclosure in line with the requirements of IAS 19 for both the current and previous accounting period is provided in the Annual Report and Financial Statements of Telefonica Europe plc for the year ended 31 December 2011.

The actuarial valuation of the Telefonica PP as at 30 September 2008 has been updated to 31 December 2011 by an independent qualified actuary in accordance with the requirements of IAS 19. In accordance with IAS 19, the defined benefit liabilities have been measured using the projected unit method. Plan assets are stated at fair value.

15 Pension costs (continued)

Movements in the present value of the Telefonica PP's defined benefit (funded) obligations in the current and preceding period were as follows

| | 31 December 2011 | 31 December 2010 |
|--------------------------------------|-----------------------------|-----------------------------|
| | £m | £m |
| At start of year | 785 | 765 |
| Total current service cost | 22 | 25 |
| Interest cost | 44 | 45 |
| Vested past service costs | - | (30) |
| Actuarial (gains) / losses | (23) | (10) |
| Curtailment (gain) / settlement loss | (1) | 1 |
| Benefits paid | (17) | (11) |
| At end of year | 810 | 785 |

The main assumptions adopted for the Telefonica PP (funded and Un-funded) under IAS 19 are as follows

| | Year ended 31 December 2011 | Year ended 31 December 2010 |
|--|--|--|
| | % | % |
| Nominal rate of increase in salaries | 4.0 | 4.5 |
| Nominal rate of increase of pensions in payment | | |
| – Pension increases with inflation | 3.0 | 3.5 |
| – Pension increases with inflation limited to 5 per cent p a | 2.9 | 3.4 |
| Discount rate | 4.9 | 5.6 |
| Inflation assumption | | |
| – RPI | 3.0 | 3.5 |
| – CPI | 2.0 | 2.5 |
| Expected long-term return for | | |
| – Equities | 7.0 | 7.5 |
| – UK Government bonds | - | - |
| – Other bonds | 4.9 | 5.2 |
| – Hedge funds | - | - |
| – Active currency | - | - |
| – Real estate | - | - |
| – Other | 3.0 | 4.2 |

Mortality tables called the "00 series" have been used in both years and are based on analysis of death rates over the 4 year period from 1999 to 2002. A floor has been applied to these tables giving a minimum rate of future improvement in males and females of 0.5% per annum. These tables are considered to be the most prudent available.

The defined benefit sections of the Telefonica PP are closed to new entrants and therefore the current service cost is likely to increase, as a percentage of payroll, as the members approach retirement.

In July 2010, the Government announced that it would, in future, link statutory minimum pension indexation to the Consumer Prices Index (CPI) rather than the, historically, higher Retail Price Index, therefore the Telefonica Europe Group has assessed that this change will act to reduce the Group's pension liabilities. To reflect this, in 2010 the Telefonica Europe Group has recognised a vested past service cost gain of £30m in its statement of comprehensive income.

15. Pension costs (continued)

Movements in fair value of the Telefonica PP's (funded) defined benefit scheme assets in the current and preceding period were as follows

| | 31 December 2011 £m | 31 December 2010 £m |
|----------------------------------|------------------------------------|------------------------------------|
| At start of year | 721 | 625 |
| Expected return on scheme assets | 42 | 45 |
| Actuarial (losses) / gains | (12) | (1) |
| Employer contributions | 77 | 63 |
| Benefits paid | (17) | (11) |
| At end of year | 811 | 721 |

The amount included in the consolidated statement of financial position of Telefonica Europe plc arising from its obligations in respect of the funded defined benefit sections of the Telefonica PP, as well as the analysis of the schemes assets, is as follows

| | 31 December 2011 £m | 31 December 2010 £m |
|---|------------------------------------|------------------------------------|
| Fair value of assets comprises | | |
| – Equities | 160 | 160 |
| – Other bonds | 644 | 532 |
| – Other | 7 | 29 |
| Fair value of assets | 811 | 721 |
| Present value of defined benefit obligations | (810) | (785) |
| Net (deficit)/asset recognised in statement of financial position of Telefonica Europe plc | 1 | (64) |

The defined benefit sections of the Telefonica PP are closed to new entrants and therefore the current service cost is likely to increase, as a percentage of payroll, as the members approach retirement

Other Group pension plans

The Company also operates an unfunded defined benefit scheme. The assumptions used for this scheme are generally consistent with those used for the Telefonica PP.

The expected rate of return on pension plan assets is determined as management's best estimate of the long-term return on the relevant equities and bonds that constitute plan assets weighted by the actual allocation of assets among the categories at the measurement date.

15. Pension costs (continued)

The actuarial gain/(loss) recognised in the statement of comprehensive income in respect of the unfunded defined benefit obligations is £nil (2010 £nil)

The amount included in the statement of financial position arising from the Company's obligations in respect of its unfunded defined benefit schemes is as follows

| | 31 December 2011 £m | 31 December 2010 £m |
|--|------------------------------------|------------------------------------|
| Present value of defined benefit obligations | (5) | (5) |
| Net liability recognised in statement of financial position | (5) | (5) |

Movements in the present value of defined benefit obligations in the current and preceding period were as follows

| | 31 December 2011 £m | 31 December 2010 £m |
|-------------------------|------------------------------------|------------------------------------|
| At start of period | 5 | 5 |
| Actuarial loss | - | - |
| At end of period | 5 | 5 |

| | Year ended 31 December 2011 £m | Year ended 31 December 2010 £m |
|--|---|---|
| History of experience gains and losses | | |
| Experience gains and losses on plan liabilities | | |
| Amount – gain/(loss) | (0.5) | 0.1 |
| Percentage of the present value of plan liabilities | 9% | 2% |
| Total amount recognised in the other comprehensive income statement | | |
| Amount – gain/(loss) | - | - |
| Percentage of the present value of plan liabilities | - | - |

The estimated amount of contributions expected to be paid to the schemes during the year ended 31 December 2011 is nil (31 December 2010 nil)

The five year summarised history of the Group's defined benefit pension plans is as follows

| | 31 Dec 2011 £m | 31 Dec 2010 £m | 31 Dec 2009 £m | 31 Dec 2008 £m | 31 Dec 2007 £m |
|--|-------------------------------|-------------------------------|-------------------------------|-------------------------------|-------------------------------|
| Present value of defined benefit obligation | (5) | (5) | (5) | (4) | (11) |
| Net liability recognised in the statement of financial position | (5) | (5) | (5) | (4) | (11) |

16. Deferred taxation

| | Year ended 31 December 2011 £m |
|---|---|
| Provision for deferred tax | |
| Accelerated tax depreciation | 1 |
| Pension provision | 1 |
| Other temporary differences | 3 |
| Total provision for deferred tax | 5 |

Deferred tax assets

| | £m |
|--|----------|
| At 1 January 2010 | 5 |
| Charge to the comprehensive income statement | (1) |
| Credit to other comprehensive income | 1 |
| At 31 December 2010 | 5 |
| Charge to the comprehensive income statement | - |
| Credit to other comprehensive income | - |
| At 31 December 2011 | 5 |

The deferred income tax credited to equity during the year was as follows

| | Year ended 31 December 2011 £m | Year ended 31 December 2010 £m |
|---------------|---|---|
| Share options | 0 | 1 |
| | 0 | 1 |

There were no unrecognised deferred tax assets or liabilities at 31 December 2011 (31 December 2010 £nil)

In the UK Budget of 23 March 2011, it was announced that the main rate of corporation tax would reduce from 28% to 26% effective from 1 April 2011 and 25% effective from 1 April 2012. These changes were enacted on 19 July 2011. As a result the disclosure of deferred tax has been adjusted to reflect the enactment with no significant impact on these financial statements.

The UK Budget of 21 March 2012 announced that the main rate of corporation tax will be 24% effective from 1 April 2012 instead of 25% as previously enacted, with reductions to the main rate of corporation tax proposed to reduce the rate by a further 1% each 1 April until 1 April 2014. As this legislation was not enacted or substantively enacted by the balance sheet date it has not been reflected within these financial statements. However it is expected that the changes would not have a significant impact on the value of the company's deferred tax balances at the balance sheet date.

17. Share capital

| | 31 December | | 31 December |
|---|--------------------|-------------|--------------------|
| | Number of | 2011 | Number of |
| | shares | £m | shares |
| | | | 2010 |
| | | | £m |
| Called up, allotted and fully paid | | | |
| Ordinary shares of £1 each | 12,000,600 | 12 | 12,000,600 |
| | | | 12 |

The Company has a single class of share capital, comprising ordinary shares of £1 each. Subject to the Company's articles of association, and applicable law, the Company's ordinary shares confer on the holder, the right to receive notice of and vote at general meetings of the Company, the right to receive any surplus assets on a winding up of the Company and an entitlement to receive any dividend declared on ordinary shares but not the right of redemption of shares.

18. Related party disclosures

Details of the nature of related party relationships are included in note 19.

During the year ended 31 December 2011, the Company entered into transactions with related parties as follows:

| | Year ended | Year ended |
|-------------------------------|--------------------|--------------------|
| | 31 December | 31 December |
| | 2011 | 2010 |
| | £m | £m |
| Financial income | | |
| Parent company | 50 | 52 |
| Subsidiary companies | 15 | 13 |
| Other related parties | 168 | 169 |
| | 233 | 234 |
| Financial expense | | |
| Parent company | (6) | (5) |
| Subsidiary companies | (86) | (78) |
| Other related parties | - | (7) |
| | (92) | (90) |
| Total net transactions | 141 | 144 |

18. Related party disclosures (continued)

At 31 December 2011 the Company had the following balances arising from transactions with related parties

| | 31 December 2011 £m | 31 December 2010 £m |
|---|------------------------------------|---------------------------|
| Receivables from related parties | | |
| Parent company | - | 2,129 |
| Subsidiary companies | 802 | 858 |
| Other related parties | 170 | 6,659 |
| | 972 | 9,646 |
| Payables to related parties | | |
| Parent company | - | (144) |
| Subsidiary companies | (8,375) | (8,283) |
| Other related parties | (155) | (261) |
| | (8,530) | (8,688) |

During the year the existing loans receivable and payable with mmO2 plc, were repaid

Included within receivables from subsidiary companies is an outstanding balance due from O2 Networks Limited. The interest rate of this loan was 2% at 31 December 2011 (31 December 2010 1.7%)

Included within payables to subsidiary companies are a £4,030 million floating rate bond held by O2 Third Generation Holdings Limited and a sterling denominated loan from O2 Networks Limited of £2,169 million (31 December 2010 £2,131 million) with an interest rate of 2% (31 December 2010 1.8%)

There is a balance due to O2 Limited included within payables to subsidiary companies, which represents intercompany loan balances with an interest rate of 2% at 31 December 2011 (31 December 2010 1.8%)

Related party transactions with Directors and key management are detailed in note 22

19 Principal subsidiary undertakings, joint ventures and associates

The principal operating subsidiary undertakings are detailed below

| Name | Country of incorporation | Activity | Portion of shares held % |
|---|---------------------------------|---|---------------------------------|
| Telefonica UK Limited ¹ | England and Wales | Mobile cellular telephone system | 100 |
| Be Un Limited ¹ | England and Wales | Internet services provider | 100 |
| Giffgaff Limited ¹ | England and Wales | Mobile communications network | 100 |
| Telefonica Financial Services UK Limited ¹ | England and Wales | Financial services for O2 portfolio products | 100 |
| Telefónica O2 Ireland Limited ¹ | Ireland | Mobile cellular telephone system provider and operator | 100 |
| O2 Mobiles Limited | England and Wales | Intermediate holding company | 100 |
| O2 Networks Limited | England and Wales | Intermediate holding company | 100 |
| O2 Investments Ireland | Ireland | Intermediate holding company | 100 |
| O2 Pine Limited | England and Wales | Intermediate holding company | 100 |
| O2 Willow Limited | England and Wales | Intermediate holding company | 100 |
| Kilmaine Limited | Isle of Man | Intermediate holding company | 100 |
| O2 International Holdings Limited | England and Wales | Intermediate holding company | 100 |
| O2 Credit Vouchers Limited | England and Wales | Selling of Mobile phone credit vouchers | 100 |
| Telefonica UK Pension Trustee Limited | England and Wales | Corporate Trustee of the O2 Pension Plan | 100 |
| Telefonica O2 UK Limited | England and Wales | Dormant entity | 100 |
| Cellular Radio Limited | England and Wales | Dormant entity | 100 |
| Movistar Limited | England and Wales | Dormant entity | 100 |
| Telefonica Digital Communications Limited | England and Wales | Dormant entity | 100 |
| O2 Secretaries Limited | England and Wales | Dormant entity | 100 |
| O2 Communications Limited | England and Wales | Intermediate holding company | 100 |
| Telefonica Europe People Services Limited | Ireland | European HR services, support functions and administration provider | 100 |

¹Investments are indirect

The accounting reference date of the principal operating subsidiary undertakings is 31 December 2011. No subsidiary undertakings are listed on any public exchange.

20. Financial instruments

Financial risk factors and management

The Company's operations expose it to a variety of financial risks including foreign currency risk, fair value risk, interest rate risk, credit risk and liquidity risk

The principal financial risks of the Company and how the Company managed these risks are discussed below

Credit risk

The Company does not have a significant exposure to credit risk. The Company's main credit balances are held with group companies within the Telefónica S A group. The Company does not have external trade receivable balances with companies outside of the Telefónica Group.

Liquidity risk

Management of the Company's liquidity risk is achieved mostly through being a part of the larger Telefónica group, which operates group wide policies in this area. The Company also maintains its own committed borrowing facilities, and holds financial assets primarily in short-term deposits with a central Telefónica group company that are readily convertible to known amounts of cash. These measures help keep liquidity risk low.

Foreign currency risk

The Company operates primarily in the United Kingdom and therefore there is low exposure to transactional foreign currency risk. The Company has foreign currency assets and liabilities held with group companies which expose it to translation risk. This risk is managed through being part of the larger Telefónica group, which operates group wide policies in this area. If the Pound Sterling lost 10 percent against the Euro at 31 December 2011, this would have no material impact on the statement of comprehensive income of the Company.

Interest rate risk

The Company's interest rate risk arises primarily from the effects of movements in interest rates on the value of the Company's borrowings and financial assets. During the period it was a policy to fix or protect expected interest flows where Company profits or key financial ratios would be materially at risk from interest rate movements.

Fair value of financial instruments

The carrying value and fair value of the Company's financial assets and financial liabilities are not deemed to be materially different at 31 December 2011 and 31 December 2010.

Capital management

The Company's capital comprises share capital and retained earnings.

The Company's objectives when managing capital are to safeguard the Company's ability to continue to operate as a going concern, to maintain optimal capital structure commensurate with risk and return and to reduce the cost of capital.

In order to maintain or adjust the capital structure, the Company may pay dividends to its shareholder, return capital to its shareholder, issue new shares or sell assets to reduce debt or draw down more debt.

21. Auditors' remuneration

Audit fees for the company were borne by another company within the Telefónica S A group and have not been allocated across the group

22 Key management and director compensation

The key management of the Company are deemed to be the key management of the Telefonica Europe plc group. The compensation of key management for the year ended 31 December 2011 was as follows

| | Year ended 31 December 2011 £000 | Year ended 31 December 2010 £000 |
|---|---|---|
| Salaries and short-term employee benefits | 9,001 | 8,643 |
| Post-employment benefits | 206 | 182 |
| Share based payments | 2,956 | 2,330 |
| Termination benefits | - | 1,906 |
| Total key management compensation | 12,163 | 13,061 |

The key management compensation analysed above represents compensation earned by senior managers

No emoluments were paid to the Directors during the year for their services to the Company (31 December 2010 £nil). The Directors are remunerated for their services to the Group as a whole

23 Employees

| | Year ended 31 December 2011 No | Year ended 31 December 2010 No |
|---|---|---|
| Average number of full time employee equivalents (including Directors) by class of business | | |
| Finance | 37 | 30 |
| Other businesses and administration | 138 | 79 |
| Total employees | 175 | 109 |

The benefit expenses incurred in respect of these employees were

| | Year ended 31 December 2011 £m | Year ended 31 December 2010 £m |
|---------------------------------------|---|---|
| Wages and salaries | 20 | 17 |
| Social security costs | 3 | 3 |
| Share based payments (note 24) | 7 | 7 |
| Pension costs (note 15) | - | (24) |
| Total employee benefit expense | 30 | 3 |

24. Share based payments

There are three share schemes currently in operation in O2 Holdings Limited, the Telefónica Performance Share Plan, the Telefonica Performance Cash Plan and the Global Employee Share Plan. These are described in more detail below.

The costs of share awards are charged to the statement of comprehensive income over the vesting period, based upon the fair value of the share award at the award date adjusted for the likelihood of vesting under the share award.

The amounts recognised in operating income for share based payment transactions with employees for the year ended 31 December 2011 was as follows:

| | Year ended 31 December 2011 £m | Year ended 31 December 2010 £m |
|--|---|---|
| Equity settled share based payments | 4 | 3 |
| Cash settled share based payments ¹ | 3 | 4 |
| Total share based payments | 7 | 7 |

¹ In the year ended 31 December 2011, of the £3 million (2010 - £4 million) cash settled share based payments recognised in the statement of comprehensive income, £2 million (2010 - £3 million) was charged to group undertakings and included in the £94 million (2010 - £161 million) management charge credit.

The liability recognised in the statement of financial position for share based payments at 31 December 2011 totalled £8 million (31 December 2010: £10 million).

In 2011 the total charge to equity for the unvested share based payments amounted to £4 million, there was also a reversal of £2 million arising from the 2008 share grant which vested in the year. The overall impact on equity in 2011 arising from share based payments was £2 million (2010: £nil).

Share award plans

The share award plans operated by the company during the year ended 31 December 2011 are:

Telefónica Performance Share Plan

The Telefónica Performance Share Plan was approved at the Telefónica S.A. AGM held on 21 June 2006 and awards shares in Telefónica S.A. to participants subject to the achievement of certain performance criteria.

The plan has an expected duration of seven years which is divided into five cycles of three years each, with the first cycle commencing on 1 July 2006. At the inception of each cycle, a number of shares are awarded to each participant in the plan, with the final number of shares vesting being based on the level of achievement against the performance criteria.

The performance criteria is the Total Shareholder Return (TSR) of Telefónica S.A. against a comparator group, over a fixed three year period as follows:

| TSR ranking | % Shares Vest |
|----------------|---------------|
| Below median | 0% |
| Median | 30% |
| Upper quartile | 100% |

Vesting occurs on a straight line basis between median and upper quartile performance.

The number of shares Telefónica S.A. granted under this plan to directors and senior management in the year ended 31 December 2011 is 390,918 (31 December 2010: 333,015).

24. Share based payments (continued)

As this plan will be settled by the physical delivery of Telefónica, S A shares to employees, the charge for the year ended 31 December 2011 of £4 million has been recognised against equity (31 December 2010 £3 million)

The fair value of the rights granted to the participants at the 2011 grant date is €8.28 per share (2010 grant €9.08). This value has been established by reference to the price of an instrument with the same conditions and requirements of the plan, which was acquired by Telefónica, S A from a financial institution. This is the best estimate of the fair value of the rights granted to the employees, as it results from a current market transaction.

In July 2011 the tranche of share awards granted in 2008 vested. At the date of vesting the weighted average share price was €13.39. The total number of shares which vested were 352,955.

Telefonica Performance Cash Plan

This plan mirrors the conditions of the Telefónica Performance Share Plan and awards employees a given number of notional shares in Telefónica S A. These notional shares entitle the beneficiary to a cash payment equivalent to their market value on vesting. The cash payment is capped at three times the value of the notional shares at the date of award. The value of the notional shares is set using a weighted average trading price for the 30 days prior to the start of each cycle. As an exception, the value of those notional shares awarded in the first cycle was determined using the weighted average share price for the 30 days prior to 11 May 2006. As such their notional value is €12.83.

This plan also has an expected duration of 7 years with 5 cycles of 3 years each commencing on 1 July.

As with the Telefónica Performance Share Plan, the entitlement to a payment at the end of each cycle is dependent on the TSR of Telefónica S A in relation to the comparator group over a fixed three year period as follows:

| TSR ranking | % Shares Vest |
|--------------------|----------------------|
| Below median | 0% |
| Median | 30% |
| Upper quartile | 100% |

Vesting occurs on a straight line basis between median and upper quartile performance.

The number of notional shares awarded in 2011 was 62,500 (2010 25,877).

The fair value of the rights granted to the participants in the 2011 scheme was €13.39 per share at 31 December 2011 (2010 €16.97). This value has been established based on the market value of Telefónica S A shares at the measurement date, taking into consideration the expected TSR performance of Telefónica S A. This fair value is updated at each statement of financial position date to reflect current market values.

In July 2011 the tranche of share awards granted in 2008 vested. At the date of vesting the weighted average share price at vesting was €15.72. The total number of shares vesting in the tranche was 27,001.

24. Share based payments (continued)

Global Employee Share Plan

The Annual General Meeting of Shareholders of Telefónica, SA held on 23 June 2009, approved the implementation of a share plan open to all employees of the Telefónica Group worldwide, with certain exceptions. The Plan offers employees the opportunity to acquire shares in Telefónica, SA with the latter's commitment to deliver free of charge a certain number of shares in Telefónica, SA, subject to certain conditions.

The total duration of the plan is initially planned for two years. Employees enrolled in the Plan may acquire shares in Telefónica, SA through monthly contributions of up to €100 (or local currency equivalent), with a maximum of €1,200 over a period of twelve months (time of purchase). The shares will be matched, after the vesting date of the plan, effective 1 September 2012, and are subject to the following:

The continuation of employment during the two-year program (consolidation period), subject to certain conditions.

- The actual number of shares awarded at the end of the vesting period depends on the number of shares purchased and retained by each employee. Thus, employees enrolled in the Plan that have retained the shares acquired for a further period of twelve months following the end of the period of purchase, shall be entitled to receive one free share for every share they have acquired.

25. Parent company and controlling party

At 31 December 2011 the immediate parent company was mmO2 plc, a company incorporated in England and Wales, which prepares consolidated financial statements. Due to this, O2 Holdings Limited presents only stand-alone financial statements whereas the mmO2 plc consolidated financial statements may be obtained from The Secretary, mmO2 plc, 260 Bath Road, Slough, Berkshire, SL1 4DX.

The ultimate parent company and controlling party at 31 December 2011 was Telefónica, S A, a company incorporated in Spain. Copies of the financial statements of Telefónica, S A may be obtained from Gran Vía 28, Madrid, Spain.

26. Subsequent event

On 23 August 2012 Jesus Perez de Urquien was appointed a director of the Company.

On 31 August 2012 Edward Smith resigned as director of the Company.

On 18 September 2012, O2 Holdings transferred its total number of shares (10 shares) in Cellular Radio Ltd to O2 Networks Limited (8 shares) and O2 Cedar Limited (2 shares). O2 Networks is 100% owned by O2 Holdings Limited and O2 Cedar is 100% indirect investment.