

Registered Number: 2833330

VIRGIN NET LIMITED

DIRECTORS' REPORT AND FINANCIAL STATEMENTS

31 JULY 2000



VIRGIN NET LIMITED

DIRECTORS' REPORT AND FINANCIAL STATEMENTS

For the year ended 31 July 2000

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DIRECTORS' REPORT

The directors present their report and audited financial statements for the year ended 31 July 2000.

RESULTS AND ACTIVITIES

The results for the year are set out on page 4. The loss has been transferred to reserves.

DIVIDENDS

The directors do not recommend the payment of a dividend on the ordinary share capital.

DIRECTORS

The directors of the company, and, where a director at the year-end, their interests in its shares at the beginning and end of the year, are shown in the table and note below:

	Notes	Number of share options at the beginning and end of the year	Exercise price	Date from which exercisable
R Branson (resigned 20 December 2000)	1	-	-	-
KRA Ibbett		44,813	£1.00	10 Aug 98
		14,937	£1.00	10 Aug 00
J Gregg	2	43,050	£1.00	10 Aug 98
		14,350	£1.00	10 Aug 00
B Knapp (resigned 20 December 2000)	2	-	-	-
Gordon McCallum (resigned 20 December 2000, reappointed 24 January 2001)		-	-	-
D Johnson (alternate to R Branson, resigned 8 September 1999)		-	-	-
L Wood (alternate to B Knapp, resigned 19 December 2000)		-	-	-

1. Sir R Branson is interested in the whole of the issued A ordinary shares by virtue of his interest in Virgin Group Investments, the ultimate owner of the shares, registered in British Virgin Islands.
2. Mr B Knapp and Mr J Gregg are interested in the whole of the issued B ordinary shares and Cumulative redeemable preference shares by virtue of their interest in the share capital of Cabelfel Ventures Limited (which is 100% owned by NTL Inc), the owner of the shares, a corporation organised under the laws of the state of Delaware.

The options expire seven years after the grant date. None of the options have lapsed or been exercised during the year. None of the other directors had any disclosable interests in the shares of the company during the year.

BUSINESS REVIEW AND PROSPECTS

This financial year witnessed continuing strong growth in the business on all operating metrics. The number of Internet service subscribers increased by 50% to c.570,000 at the year-end; the number of unique users of the www.virgin.net portal grew to over 1 million; the number of staff deployed in the business grew to over 150 people.

During the year, the Company also launched a service for small businesses (virginbiz.net) and entered into a joint venture with Alba Plc to build and manage a portal for the next generation of internet enabled TV's.

In financial terms, the increased investment in growth and new ventures was, however, accompanied by a deterioration in ISP operating margin as a result of the move from a subscription product to a "Free" model, supported only by a share in the

VIRGIN NET LIMITED

inter-connect revenue generated from subscribers telephone calls. The renegotiated supply arrangement with NTL did not fully recoup that margin and as a result, the operating loss increased in the year from £8.7 million to £18.1 million on increased revenues of £13.4 million.

In early 2000, the ISP environment became even more volatile with the onset of unmetered access at very low prices or even on a "Free" basis. The financial outlook in April 2000 was for a business incurring mounting losses in the shortterm and requiring cross-subsidisation from e-commerce or other activities to remain viable.

The underlying economic prospects are, however, improving with wholesale rates for unmetered access products reducing and a renegotiated supply arrangement with NTL likely to result in the ISP business breaking even by the end of calendar 2001 and the Portal business breaking even by end 2002.

STATEMENT OF DIRECTORS' RESPONSIBILITIES

Company law requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the company and of the profit or loss for that year. In preparing those financial statements the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements that are reasonable and prudent; and
- prepare financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the company and to enable them to ensure that the financial statements comply with the Companies Act 1985. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the company and to prevent and detect fraud and other irregularities.

AUDITORS

In accordance with Section 385 of the Companies Act 1985, a resolution for the re-appointment of KPMG as auditors of the company is to be proposed at the forthcoming Annual General Meeting.

On behalf of the board


PG GRAM
Secretary

22 August 2001
120 Campden Hill Road
London W8 7AR

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REPORT OF THE AUDITORS, KPMG

to the members of Virgin Net Limited

We have audited the financial statements set out on pages 4 to 13.

Respective responsibilities of directors and auditors

The directors are responsible for preparing the director's report and, as described on page 2, the financial statements in accordance with applicable United Kingdom law and accounting standards. Our responsibilities, as independent auditors, are established in the United Kingdom by statute, the Auditing Practices Board and by our profession's ethical guidance.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act. We also report to you if, in our opinion, the directors' report is not consistent with the financial statements, if the company has not kept proper accounting records, if we have not received all the information and explanations we require for the audit, or if information specified by law regarding directors' remuneration and transactions with the company is not disclosed.

Basis of Audit Opinion

We conducted our audit in accordance with Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion

In our opinion the financial statements give a true and fair view of the state of the company's affairs at 31 July 2000 and of its loss for the year then ended and have been properly prepared in accordance with the Companies Act 1985.



KPMG
Chartered Accountants
Registered Auditors
London

Date

24 August 2001

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PROFIT AND LOSS ACCOUNT for the year ended 31 July 2000

	Notes	Year ended 31 July 2000 £	Year ended 31 July 1999 £
Turnover - continuing activities	1	13,414,013	12,478,665
Cost of sales		<u>(11,321,417)</u>	<u>(10,266,978)</u>
Gross profit		2,092,596	2,211,687
Administrative expenses		(20,154,882)	(9,177,386)
Exceptional item	16	<u>-</u>	<u>(1,743,081)</u>
Operating loss - continuing activities	2,3	(18,062,286)	(8,708,780)
Interest payable - bank interest		(330,588)	(13,628)
Interest receivable - bank interest		<u>143,600</u>	<u>69,032</u>
Loss on ordinary activities before taxation	4	(18,249,274)	(8,653,376)
Taxation	5	<u>-</u>	<u>-</u>
Loss on ordinary activities after taxation		(18,249,274)	(8,653,376)
Dividend on preference shares	11	<u>(200,000)</u>	<u>(200,000)</u>
Retained loss for the year	12	<u>(18,449,274)</u>	<u>(8,853,376)</u>

There were no material recognised gains and losses in the current or previous year other than those reported in the above profit and loss account.

There is no difference between the company's historical cost loss to that reported in the profit and loss account.

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BALANCE SHEET

as at 31 July 2000

	Notes	2000 £	1999 £
FIXED ASSETS			
Tangible fixed assets	6	1,216,795	1,090,324
Investments	7	<u>2</u>	<u>-</u>
		<u>1,216,797</u>	<u>1,090,324</u>
CURRENT ASSETS			
Debtors	8	9,966,182	1,632,388
Cash at bank		<u>6,192,836</u>	<u>2,806,253</u>
		16,159,018	4,438,641
CREDITORS:			
Amounts falling due within one year	9	<u>(5,736,612)</u>	<u>(7,340,897)</u>
NET CURRENT ASSETS/(LIABILITIES)		<u>10,422,406</u>	<u>(2,902,256)</u>
TOTAL ASSETS LESS CURRENT LIABILITIES		11,639,203	(1,811,932)
PROVISION FOR LIABILITIES AND CHARGES	10	<u>(10,000)</u>	<u>(1,448,106)</u>
NET ASSETS/(LIABILITIES)		<u>11,629,203</u>	<u>(3,260,038)</u>
CAPITAL AND RESERVES			
Called up share capital	11	8,099,035	7,707,978
Share premium account	12	33,343,970	5,792,023
Shares to be issued	12	3,060,036	-
Profit and loss account	12	<u>(32,873,838)</u>	<u>(16,760,039)</u>
SHAREHOLDERS' FUNDS/(DEFICIT)		<u>11,629,203</u>	<u>(3,260,038)</u>
Shareholders' funds / (deficit) are split:			
Equity interests		8,791,596	(5,847,645)
Non-equity interests		<u>2,837,607</u>	<u>2,587,607</u>
		<u>11,629,203</u>	<u>(3,260,038)</u>

The financial statements were approved by the board of directors on 22 August 2001 and signed on its behalf by:



K IBBETT
Director

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**CASH FLOW STATEMENT
for the year ended 31 July 2000**

	Notes	Year ended 31 July 2000	Year ended 31 July 1999
RECONCILIATION OF OPERATING PROFIT TO NET CASH FLOW FROM OPERATING ACTIVITIES			
Operating loss		(18,062,286)	(8,708,780)
Depreciation charges		923,606	607,938
Increase in debtors		(8,333,794)	(845,390)
(Decrease)/increase in creditors		(1,604,285)	2,002,622
(Decrease)/increase in provision for liabilities		(1,438,106)	1,448,106
Deferred compensation expense		<u>2,135,475</u>	<u>709,593</u>
Net cash outflow from operating activities		(26,379,390)	(4,785,911)
Returns on investments and servicing of finance	17	(186,988)	55,404
Capital expenditure and financial investment	17	<u>(1,050,079)</u>	<u>(640,486)</u>
Cash outflow before management of liquid resources and financing		(27,616,457)	(5,370,993)
Financing	17	31,003,040	5,750,001
Increase in cash in the year		<u>3,386,583</u>	<u>379,008</u>
RECONCILIATION OF NET CASH FLOW TO MOVEMENT IN NET FUNDS			
Increase in cash in the year		3,386,583	379,008
Net funds at the start of the year		2,806,253	2,427,245
Net funds at the end of the year	18	<u>6,192,836</u>	<u>2,806,253</u>

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Notes to the accounts For the year ended 31 July 2000

1 ACCOUNTING POLICIES

The financial statements have been prepared in accordance with applicable accounting standards and on the basis of the following accounting policies, which have been applied consistently during the year.

a) Basis of accounting

The accounts have been prepared under the historical cost convention, and on a going concern basis in view of an undertaking from the company's ultimate shareholders, Virgin Group Investments Limited and NTL Inc. to provide sufficient funding to enable the company to meet its liabilities as and when they fall due for the next twelve months.

The directors have no reason to believe that the shareholders will not be in a position to provide the support referred to above and, accordingly, they have prepared the financial statements on the going concern basis.

b) Fixed assets and depreciation

Depreciation is provided on a straight-line basis over the following periods to write off the cost of each tangible fixed asset over its estimated useful life:

Computer equipment	: 3 years
Fixtures and fittings	: 3-4 years
On-line operating system	: over first three years of full service
Leasehold improvements	: over 21 months

c) Leases

Where the company enters into a lease which entails taking all of the risks and rewards of ownership of an asset the lease is treated as a "finance lease". There are no finance leases in the year.

All other leases are accounted for as "operating leases" and the rental charges are charged to the profit and loss account on a straight-line basis over the life of the lease.

d) Taxation

The charge for taxation is based on the result for the year and takes into account taxation deferred because of timing differences between the treatment of certain items for taxation and accounting purposes. Provision for taxation is made for deferred tax only to the extent that it is probable that an actual liability will crystallise.

e) Turnover

Turnover represents the amounts (excluding value added tax) derived from the provision of services to customers.

Turnover and loss before taxation all arose from the principal activity of the company within the United Kingdom.

f) Pensions

The company operates a defined contribution scheme for its employees and executives. The assets of the scheme are held separately from those of the company in independently administered funds. The pension cost represents contributions payable by the company to the funds.

g) Employee share options

Employee share options are accounted for in accordance with UITF No 17 Employee Share Schemes. The difference between the exercise price and the market value at date of grant, if any, is recognised as a charge in the profit and loss account on a straight-line basis over the vesting period.

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Notes to the accounts
For the year ended 31 July 2000

2 DIRECTORS' REMUNERATION

None of the directors received any remuneration from the company either this year or last year. Mr K Ibbett is an employee of Virgin Management Limited ('VML') and management charges are made to the company by VML to cover certain emoluments and other costs. It is not possible to allocate a proportion of the charge to the emoluments of Mr Ibbett.

3 STAFF NUMBERS AND COSTS

There were on average 112 (1999: 80) employees in the year.

The aggregate payroll costs of these employees for the year were:

	2000 £	1999 £
Wages and salaries	4,101,000	2,891,250
Social security costs	446,111	280,316
Other pension costs	59,323	72,397
Compensation expense	<u>2,135,475</u>	<u>709,593</u>
	<u><u>6,741,909</u></u>	<u><u>3,953,556</u></u>

Compensation expense represents the difference between the exercise price of options granted and the market value of the options at the date of grant and is recognised in accordance with the stated accounting policy.

4 LOSS ON ORDINARY ACTIVITIES BEFORE TAX

The loss on ordinary activities before tax is stated after charging:

Rentals payable under operating leases – building	352,000	199,479
Depreciation	923,606	607,938
Auditors' remuneration	<u>15,000</u>	<u>14,250</u>

5 TAXATION ON LOSS ON ORDINARY ACTIVITIES

No liability to taxation arises on the company's loss for the year due to the availability of losses (1999: £nil).

6 TANGIBLE FIXED ASSETS

	Leasehold Improvements £	Fixtures & fittings £	Computer equipment £	On-line operating system £	Total £
<u>Cost</u>					
At 1 August 1999	457,321	48,127	948,192	836,587	2,290,227
Additions	77,208	47,327	987,671	-	1,112,206
Disposals	<u>-</u>	<u>-</u>	<u>(62,129)</u>	<u>-</u>	<u>(62,129)</u>
At 31 July 2000	<u><u>534,529</u></u>	<u><u>95,454</u></u>	<u><u>1,873,734</u></u>	<u><u>836,587</u></u>	<u><u>3,340,304</u></u>
<u>Depreciation</u>					
At 1 August 1999	310,679	19,902	479,074	390,248	1,199,903
Charge for year	<u>132,195</u>	<u>16,981</u>	<u>378,091</u>	<u>396,339</u>	<u>923,606</u>
At 31 July 2000	<u><u>442,874</u></u>	<u><u>36,883</u></u>	<u><u>857,165</u></u>	<u><u>786,587</u></u>	<u><u>2,123,509</u></u>
<u>Net book value</u>					
At 31 July 2000	<u><u>91,655</u></u>	<u><u>58,571</u></u>	<u><u>1,016,569</u></u>	<u><u>50,000</u></u>	<u><u>1,216,795</u></u>
At 31 July 1999	<u><u>146,642</u></u>	<u><u>28,225</u></u>	<u><u>469,118</u></u>	<u><u>446,339</u></u>	<u><u>1,090,324</u></u>

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Notes to the accounts
For the year ended 31 July 2000

7 FIXED ASSET INVESTMENTS

Shares in
group undertakings
£

Shares

Cost

At beginning of year

Additions

-

2

At end of year

2

The following is the principal subsidiary undertaking of Virgin Net Limited as at 31 July 2000:

	Country of incorporation	Principal activity	Class and percentage of shares held
<i>Subsidiary undertakings</i>			
Virgin Biznet Limited	United Kingdom	Application service provider	100%

8 DEBTORS

2000
£

1999
£

Trade debtors

3,990,513

294,743

Amounts owed by fellow Subsidiary companies

3,169,822

-

Other debtors

218,609

496,019

Prepayments and accrued income

2,209,174

274,635

Other taxation

378,064

566,991

9,966,182

1,632,388

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Notes to the accounts For the year ended 31 July 2000

9	CREDITORS	2000	1999
	Amounts falling due within one year:	£	£
	Trade creditors	1,650,875	1,297,033
	Deferred income	571,293	536,264
	Other creditors	2,309,785	4,522,783
	Owed to group companies	293,555	57,787
	Accruals	<u>911,104</u>	<u>927,030</u>
		<u><u>5,736,612</u></u>	<u><u>7,340,897</u></u>

There is no interest payable on amounts owed to group companies.

10	PROVISION FOR LIABILITIES AND CHARGES	2000	1999
	The provision for liabilities and charges is made up as follows:	£	£
	At beginning of the year	1,448,106	-
	(Released)/charged in	<u>(1,438,106)</u>	<u>1,448,106</u>
		<u><u>10,000</u></u>	<u><u>1,448,106</u></u>

This provision related to the estimated write-off required for the call centre which had been established during the previous financial year. This was utilised during the current financial year.

11	SHARE CAPITAL	2000	1999
		£	£
	<u>Authorised</u>		
	A Ordinary shares of £1 each	5,865,000	5,865,000
	B Ordinary shares of £1 each	5,635,000	5,635,000
	Non-Voting Ordinary Shares of £1	455,650	455,650
	Cumulative redeemable preference shares of £1 each	<u>2,100,000</u>	<u>2,100,000</u>
		<u><u>14,055,650</u></u>	<u><u>14,055,650</u></u>
	<u>Allotted, called up and fully paid</u>		
	A Ordinary shares of £1 each	3,018,037	2,885,569
	B Ordinary shares of £1 each	2,977,998	2,772,409
	Nom voting Ordinary shares of £1 each	3,000	-
	Cumulative redeemable preference shares of £1 each	<u>2,100,000</u>	<u>2,050,000</u>
		<u><u>8,099,035</u></u>	<u><u>7,707,978</u></u>

In October 1999, 25,500 cumulative redeemable preference shares were issued at £100 each. In November 1999, 24,500 cumulative redeemable preference shares were issued at £100 each. In December 1999, 3,000 non-voting Ordinary shares were issued at £1 each. In March 2000, 132,468 "A" Ordinary shares and 127,273 "B" Ordinary shares were issued at £77 each. In June 78,316 "B" Ordinary shares were issued at £37.54 each. In all cases the shares were issued in order to increase the working capital of the company.

The cumulative preference shares attract a dividend of 10% net, per annum. A provision is made in the profit and loss account for the dividend of £200,000 (1999: £200,000) relating to the financial year, although it is not due for payment. The total cumulative dividend accruing at the year-end is £737,607 (1999: £537,607).

Shares to be issued

In September 2000 81,514 "A" Ordinary shares of £1 each were issued at £37.54 each, in accordance with a share allotment agreement of June 2000.

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Notes to the accounts For the year ended 31 July 2000

Share options

At 31 July 2000, the company had granted options to subscribe for 603,860 options over non-voting ordinary shares at prices ranging between £1 and £77.00 per share. Options to subscribe for 200,660 were granted in the year ending 31 July 2000. The options granted do not contain any specific performance conditions. 136,731 of the share options were exercisable at 31 July 2000, the remainder are exercisable between August 2000 and March 2003.

12 RECONCILIATION OF MOVEMENTS IN SHAREHOLDERS' DEFICIT

	Share capital £	Share Premium £	Share to be issued £	Profit and loss account £	Total £
As at 1 August 1999	7,707,978	5,792,023	-	(16,760,039)	(3,260,038)
Shares issued in year	391,057	27,551,947	-	-	27,943,004
Shares to be issued	-	-	3,060,036	-	3,060,036
Unpaid dividend	-	-	-	200,000	200,000
Loss for the year	-	-	-	(18,449,274)	(18,449,274)
Write back of options compensation charge	-	-	-	2,135,475	2,135,475
As at 31 July 2000	<u>8,099,035</u>	<u>33,343,970</u>	<u>3,060,036</u>	<u>(32,873,838)</u>	<u>11,629,203</u>

13 COMMITMENTS

At 31 July 2000, the company had contracted capital commitments of **£nil** (1999: **£nil**).

Annual Commitments under non-cancellable operating leases are as follows:	2000	1999
	£	£
Operating leases relating to buildings which expire in the second to fifth years inclusive	<u>-</u>	<u>522,356</u>

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Notes to the accounts
For the year ended 31 July 2000

14 TRANSACTIONS WITH RELATED PARTIES

During the year ended 31 July 2000, the company had the following related party transactions and balances at the year-end:

	Transactions during the year £	Balance outstanding at the year-end £
Sales to:		
Virgin Direct	10,280	4,346
Virgin Atlantic	2,157	-
Virgin.Com	22,448	22,031
Virgin Megastores	11,306	-
Virgin Management	21,162	21,162
Virgin Biznet	5,875	5,875
Virgin Wines	8,812	8,812
Virgin Energy	3,525	3,525
NTL Internet	11,715,687	2,438,808
Virgin Biznet	3,127,923	3,127,923
 Management and Service Fees payable to:		
Isisfine Limited	105,000	192,500
 Trademark Fees payable to:		
Virgin Enterprises Limited	69,747	134,772
 Purchases from		
NTL Internet	12,808,709	943,159
Virgin Atlantic	20,030	15,990
Virgin Vouchers	42,967	-
Virgin Radio	297,500	23,500
Virgin Projects	75,321	14,975
Virgin Limobikes	329	-
Virgin Media	550,000	-

15 ULTIMATE HOLDING COMPANY

On 16 December 1998, a majority of the shares were purchased by Virgin Holdings SA, a company registered in Switzerland, which itself is ultimately owned by Virgin Group Investments Limited, registered in British Virgin Islands, which is now the company's ultimate holding company.

The largest and smallest group in which the results of the company are consolidated is that headed by Virgin Group Investments Limited. The consolidated accounts of this company are not available to the public.

16 EXCEPTIONAL ITEM

The exceptional item in the previous year related to an aborted project to build a call centre. All irrecoverable costs were provided for the last year. This provision has been utilised in the current year.

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Notes to the accounts
For the year ended 31 July 2000

17 ANALYSIS OF CASH FLOWS

	Year ended 31 July 2000	Year ended 31 July 1999
Returns on investment and servicing of finance		
Interest received	143,600	69,032
Interest paid	(330,588)	(13,628)
	<u>(186,988)</u>	<u>55,404</u>
 Capital expenditure and financial investment		
Purchase of tangible fixed assets	(1,112,206)	(640,486)
Purchase of investment	2	-
Sale of tangible fixed assets	62,129	-
	<u>(1,050,079)</u>	<u>(640,486)</u>
 Financing		
Issue of ordinary share capital	27,943,004	6,000,001
Shares to be issued	3,060,036	-
Loan from Isisfine Limited	-	(250,000)
	<u>31,003,040</u>	<u>5,750,001</u>

18 ANALYSIS OF NET FUNDS

	At beginning of year £	Cash flow £	At end of year £
Cash in hand, at bank	<u>2,806,253</u>	<u>3,386,583</u>	<u>6,192,836</u>