Company Registration Number 2650571

ALCATEL TELECOM LIMITED

Report and Financial Statements

31 December 2002

Deloitte & Touche LLP
Bristol

ALCATEL TELECOM LIMITED

REPORT AND FINANCIAL STATEMENTS 2002

CONTENTS

ALCATEL TELECOM LIMITED

OFFICERS AND PROFESSIONAL ADVISERS

DIRECTORS

M A Couzens
D Lewis
C Matthews

SECRETARY

M A Couzens

REGISTERED OFFICE

Christchurch Way
Greenwich
London
SE10 0AG

BANKERS

Barclays Bank PLC

AUDITORS

Deloitte & Touche LLP
Bristol

DIRECTORS' REPORT

The directors present their annual report and the audited financial statements for the year ended 31 December 2002.

PRINCIPAL ACTIVITIES

The principal activities of the company are the sale, distribution and maintenance of communications services and equipment primarily manufactured by members of the Alcatel S.A. group of companies, as well as related products.

BUSINESS REVIEW

On 1 January 2001, Alcatel Telecom Limited a company incorporated in England and Wales, entered into an agreement to acquire the entire issued share capital of Alcatel Networks Limited, which itself owned Alcatel Networks Services Limited, for a consideration of £79,000,000.

On 23 January 2002, Alcatel Telecom Limited acquired the trade and assets of Alcatel Networks Services Limited. The trade and assets of Alcatel Networks Limited and Alcatel Networks Services Limited were transferred to Alcatel Telecom Limited for a total consideration of £79,000,000.

On 1 April 2002, Alcatel Telecom Limited entered into an agreement to acquire the entire issued share capital of Alcatel Internetworking Limited. On the same date, the trade and assets of Alcatel Internetworking Limited were transferred to Alcatel Telecom Limited for a consideration of £855,000.

Details of significant events since the balance sheet date are contained in note 22 to the financial statements.

The directors expect the general level of activity to continue over the next 12 months.

RESULTS AND DIVIDENDS

The loss after taxation for the year ended 31 December 2002 was £137,618,000 (2001: loss of £62,573,000). The directors are unable to recommend the payment of a dividend (2001: nil).

DIRECTORS AND THEIR INTERESTS

The directors who served during the year were as follows:

M A Couzens
D Lewis
C Matthews
J W Baker (resigned 31 May 2002)

The directors held no interests requiring disclosure under Schedule 7 of the Companies Act 1985.

CHARITABLE AND POLITICAL CONTRIBUTIONS

The company contributed £2,500 to charities during the year (2001: £1,200).

DISABLED EMPLOYEES

Applications for employment by disabled persons are always fully considered, bearing in mind the aptitudes of the applicant concerned. In the event of members of staff becoming disabled, every effort is made to ensure that their employment with the company continues and that the appropriate training is arranged. It is the policy of the company that the training, career development and promotion of disabled persons should, as far as possible, be identical with that of other employees.

DIRECTORS' REPORT (continued)

EMPLOYEE CONSULTATION

The company places considerable value on the involvement of its employees and has continued its previous practice of keeping them informed on matters affecting them as employees and on the various factors affecting the performance of the company. This is achieved through formal and informal meetings. Employee representatives are consulted regularly on a wide range of matters affecting their current and future interests.

AUDITORS

Arthur Andersen resigned as auditors on 31 July 2002. On 1 August 2002 the directors appointed Deloitte & Touche to fill a casual vacancy. A resolution will be put before the annual general meeting to appoint auditors for the ensuing year.

On 1 August 2003, Deloitte & Touche transferred their business to Deloitte & Touche LLP, a limited liability partnership incorporated under the Limited Liability Partnerships Act 2000. The company's consent has been given to treating the appointment of Deloitte & Touche as extending to Deloitte & Touche LLP with effect from 1 August 2003 under the provisions of section 26(5) of the Companies Act 1989.

A resolution to re-appoint Deloitte & Touche LLP as the company's auditor will not be proposed at the forthcoming Annual General Meeting.

D Lewis
Director

26 September 2003

STATEMENT OF DIRECTORS' RESPONSIBILITIES

United Kingdom 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 of the company for that year. In preparing those financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the 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 enable them to ensure that the financial statements comply with the Companies Act 1985. They are also responsible for safeguarding the system of internal control, the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Deloitte
& Touche

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF

ALCATEL TELECOM LIMITED

We have audited the financial statements of Alcatel Telecom Limited for the year ended 31 December 2002 which comprise the profit and loss account, the balance sheet and the related notes 1 to 22. These financial statements have been prepared under the accounting policies set out therein.

This report is made solely to the company's members, as a body, in accordance with Section 235 of the Companies Act 1985. 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 auditors' 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 auditors

As described in the statement of directors' responsibilities, the company's directors are responsible for the preparation of financial statements which are required to be prepared in accordance with applicable United Kingdom law and accounting standards. Our responsibility is to audit the financial statements in accordance with relevant United Kingdom legal and regulatory requirements and auditing standards.

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 1985. We also report 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 our audit, or if information specified by law regarding directors' remuneration and transactions with the company is not disclosed.

We read the directors' report for the above year and consider the implications for our report if we become aware of any apparent misstatements.

Basis of audit opinion

We conducted our audit in accordance with United Kingdom 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 as at 31 December 2002 and of its loss for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

Deloitte & Touche LLP

DELOITTE & TOUCHE LLP
Chartered Accountants and Registered Auditors
Bristol

10 October 2003

PROFIT AND LOSS ACCOUNT
Year ended 31 December 2002

	Note	2002 £'000	2001 £'000
TURNOVER	2		
- existing operations		180,661	325,766
- acquisitions		33,110	-
Continuing operations		213,771	325,766
Cost of sales	3	(198,840)	(291,210)
GROSS PROFIT		14,931	34,556
Operating expenses	3	(117,220)	(64,883)
OPERATING LOSS			
- existing operations		(103,632)	(30,327)
- acquisitions		1,343	-
Continuing operations		(102,289)	(30,327)
Costs of a fundamental restructuring of continuing operations			
- redundancy costs	4	(5,170)	(17,285)
- vacant property costs	4	(10,285)	(13,089)
Loss on sale of investments in Alcatel eBusiness Distribution Ltd	12	(12,728)	-
LOSS ON ORDINARY ACTIVITIES BEFORE FINANCE CHARGES		(130,472)	(60,701)
Finance charges (net)	5	(8,014)	(7,022)
LOSS ON ORDINARY ACTIVITIES BEFORE TAXATION	6	(138,486)	(67,723)
Tax credit on loss on ordinary activities	9	868	5,150
RETAINED LOSS FOR THE FINANCIAL YEAR	19	(137,618)	(62,573)

There are no recognised gains and losses for the current or preceding financial year other than as stated in the profit and loss account. Accordingly, no separate statement of total recognised gains and losses is presented.

ALCATEL TELECOM LIMITED

BALANCE SHEET
At 31 December 2002

	Note	2002 £'000	2002 £'000	2001 £'000	2001 £'000
FIXED ASSETS					
Intangible assets - goodwill	10		33,546		97,312
Tangible assets	11		15,425		18,597
Investments	12		79,855		79,000
			128,826		194,909
CURRENT ASSETS					
Stocks	13	13,860		24,998	
Debtors: due within one year	14	66,418		106,171	
Debtors: due after one year	14	13,729		13,730	
Cash at bank and in hand		53		3,332	
		94,060		148,231	
CREDITORS: AMOUNTS FALLING DUE WITHIN ONE YEAR	15	(260,396)		(305,120)	
NET CURRENT LIABILITIES			(166,336)		(156,889)
TOTAL ASSETS LESS CURRENT LIABILITIES			(37,510)		38,020
PROVISIONS FOR LIABILITIES AND CHARGES	16		(22,588)		(20,500)
NET (LIABILITIES)/ASSETS			(60,098)		17,520
CAPITAL AND RESERVES					
Called up share capital	17		148,711		88,711
Share premium account	18		47,289		47,289
Profit and loss account	18		(256,098)		(118,480)
EQUITY SHAREHOLDERS' (DEFICIT)/FUNDS	19		(60,098)		17,520

The financial statements were approved by the Board of Directors on

Signed on behalf of the Board of Directors

D Lewis
Director
26 September 2003

NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 December 2002

1. ACCOUNTING POLICIES

The principal accounting policies are summarised below. They have all been applied consistently throughout the year and the preceding year with the exception of the policy for deferred tax which has been changed to comply with FRS 19 "Deferred taxation".

Basis of accounting

The financial statements have been prepared under the historical cost convention and in accordance with applicable accounting standards.

The consolidated financial statements of Alcatel S.A., the company's ultimate parent company, are publicly available and therefore the company is exempt under the provisions of FRS 1 (Revised) "Cash flow statements" from presenting its own cash flow statement.

Group financial statements have not been prepared as the company has taken advantage of the relief available under Section 228 of the Companies Act 1985, as the results of the company and its subsidiary undertakings are included within the consolidated financial statements of Alcatel S.A.

Intangible assets - goodwill

Goodwill arising on the acquisition of subsidiary undertakings and businesses, representing any excess of the fair value of the consideration given over the fair value of the identifiable assets and liabilities acquired, is capitalised and written off on a straight line basis over its useful economic life, which has been estimated as twenty years. Provision is made for any impairment.

Goodwill arising on acquisitions in the year ended 31 December 1997 and earlier periods was written off to reserves in accordance with the accounting standard then in force. As permitted by the current accounting standard the goodwill previously written off to reserves has not been reinstated in the balance sheet. On disposal or closure of a previously acquired business, the attributable amount of goodwill previously written off to reserves is included in determining the profit or loss on disposal.

Tangible fixed assets

Fixed assets are shown at original historical cost net of accumulated depreciation and provision for impairment.

Depreciation is provided on all fixed assets, other than freehold land, to write off the cost of the asset, less estimated residual value, on a straight-line basis over its estimated useful life, as follows:

Freehold buildings	35 years
Leasehold improvements	10 years or lease term
Plant and equipment	3 to 5 years
Motor vehicles	4 to 5 years

1. ACCOUNTING POLICIES *(continued)*

Stocks

Finished goods stock is stated at the lower of cost, calculated on a first-in first-out basis, and net realisable value, based on estimated normal selling price less further costs expected to be incurred to completion and disposal. Provision is made for obsolete, slow-moving or defective items where appropriate.

Spares stock is used by the company to meet obligations under service maintenance contracts and warranty agreements and is stated at cost, calculated on a first-in first-out basis, less provisions. Provisions are made to reflect the ageing of the spares stock and for obsolete, slow-moving or defective items, where appropriate.

Research and development

Research and development costs are written off as incurred.

Investments

Fixed asset investments are shown at cost less provision for impairment.

Foreign currency

Transactions denominated in foreign currencies are recorded in sterling at either the rates ruling at the dates of the transactions or, where appropriate, at the related forward exchange contract rates. Gains or losses are reported in the profit and loss account to reflect changes in exchange rates subsequent to the date of the transaction.

Monetary assets and liabilities which are denominated in foreign currencies at the year-end are translated at the rates of exchange ruling at the year-end or, where appropriate, at the related forward exchange contract rates, and resulting gains or losses are reported in the profit and loss account.

Taxation

Current tax is provided at amounts expected to be paid (or recovered) using the tax rates and laws that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date where transactions or events that result in an obligation to pay more tax in the future or a right to pay less tax in the future have occurred at the balance sheet date. Timing differences are differences between the group's taxable profits and its results as stated in the financial statements that arise from the inclusion of gains and losses in tax assessments in periods different from those in which they are recognised in the financial statements.

A net deferred tax asset is regarded as recoverable and therefore recognised only when, on the basis of all available evidence, it can be regarded as more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted.

Deferred tax is measured at the average tax rates that are expected to apply in the periods in which the timing differences are expected to reverse, based on tax rates and laws that have been enacted or substantively enacted by the balance sheet date.

NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 December 2002

1. ACCOUNTING POLICIES (continued)

Leases

The company enters into operating and finance leases.

Assets held under operating leases are not reported in the balance sheet. Rentals under operating leases are charged to the profit and loss account on a straight-line basis over the lease term.

Assets held under finance leases are initially reported at the present value of the minimum lease payments at the inception of the lease with an equivalent liability categorised under creditors falling due within one year and after one year. Each asset is depreciated over the shorter of the lease term and its useful economic life. Finance charges are allocated to accounting periods over the period of the lease to produce a constant rate of charge on the outstanding balance. Lease payments are apportioned between finance charges and reduction of liability.

Turnover

Turnover comprises the value of sales and services provided during the year (net of value added tax).

Revenues from service maintenance contracts which are invoiced in advance are deferred and released over the future periods to which they relate.

Pension costs

The company provides pension benefits based on final pensionable pay under a defined benefit scheme. The assets of the scheme are held independently of the company by trustees.

The amount charged to the profit and loss account is the estimated regular cost of providing the benefits accrued in the year, adjusted to reflect variations from that cost. The regular cost is calculated so that it represents a substantially level percentage of current and future pensionable payroll. Variations from regular cost are charged or credited to the profit and loss account over the estimated average remaining working lives of scheme members.

Any difference between amounts charged to the profit and loss account and contributions paid to the scheme is shown as a separately identified liability or asset in the balance sheet (see note 20).

2. SEGMENTAL INFORMATION

The analysis of turnover by geographical location is as follows:	**2002 £'000**	**2001 £'000**
United Kingdom	162,229	168,749
Continental Europe	37,253	128,749
North America	7,914	1,737
Other	6,375	26,531
	213,771	325,766

All of Alcatel Telecom Limited's turnover is derived from the sale, distribution and maintenance of communication services and equipment.

NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 December 2002

3. COST OF SALES AND OPERATING EXPENSES

	Existing operations £'000	Acquisitions £'000	*2002* Total £'000	*Continuing* operations £'000	*Discontinued* operations £'000	*2001* Total £'000
Cost of sales	167,385	31,455	198,840	99,152	192,058	291,210

	£'000	£'000	£'000	£'000	£'000	£'000
Selling and marketing costs	23,800	232	24,032	9,747	19,370	29,117
Research and development	7,788	-	7,788	4,669	7,786	12,455
Administrative expenses	19,451	80	19,531	7,066	16,245	23,311
Goodwill impairment	65,869	-	65,869	-	-	-
Operating expenses	116,908	312	117,220	21,482	43,401	64,883

During the year, the company undertook an impairment review of goodwill. This has resulted in an impairment of goodwill of £65,869,000 in the year.

4. COST OF A FUNDAMENTAL RESTRUCTURING OF CONTINUING OPERATIONS

	2002 £'000	2001 £'000
Redundancy costs	5,170	17,285
Vacant property costs	10,285	13,089
	15,455	30,374

During the year and the previous two years the company undertook a fundamental restructuring of its continuing operations. This led to a rationalisation of both the workforce and of certain properties and has a material impact on the nature and focus of the company's operations.

The effect of the exceptional items reported after operating losses on the amounts charged to the profit and loss account for taxation was to increase available tax losses in the year by £5,170,000.

NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 December 2002

5. FINANCE CHARGES (NET)

Investment income	2002 £'000	2001 £'000
Interest receivable and similar income	89	328
Other income	-	248
	89	576

Interest payable and similar charges	£'000	£'000
Bank loans and overdrafts	-	3,808
Finance leases and hire purchase contracts	3	24
Interest payable to other group undertakings	8,100	3,766
	8,103	7,598

Finance charges (net)	£'000	£'000
Interest payable and similar charges	8,103	7,598
Less: investment income	(89)	(576)
	8,014	7,022

6. LOSS ON ORDINARY ACTIVITIES BEFORE TAXATION

Loss on ordinary activities before taxation is stated after charging/(crediting):	2002 £'000	2001 £'000
Goodwill amortisation	6,096	5,275
Depreciation:		
- owned assets	4,705	5,203
- assets held under finance leases	3	452
Operating lease rentals:		
- plant and machinery	2,326	4,080
- other	7,443	11,172
Auditors' remuneration:		
- audit fees	100	140
- fees for non-audit services	47	118
Management charges:		
- group allocation for research and development	7,303	11,513
- other	485	942
Foreign exchange gain	(1,704)	(1,212)

The operating lease rentals – other figure of £7,443,000 (2001: £11,172,000) includes £5,820,000 (2001: £8,452,000) which is included within vacant property costs of £10,285,000 (2001: 13,089,000), see note 4.

NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 December 2002

7. STAFF COSTS

The average monthly number of persons employed by the company (including executive directors) during the year was as follows:

	2002 No.	2001 No.
Service and technical personnel	319	529
Sales and marketing	237	342
Administration	127	168
	683	1,039

Their aggregate remuneration comprised:	£'000	£'000
Wages and salaries	46,547	73,793
Social security costs	3,260	5,518
Other pension costs (see note 20)	2,895	3,940
	52,702	83,251

The wages and salaries costs include £5,170,000 of redundancy costs (see note 4).

8. DIRECTORS' REMUNERATION AND TRANSACTIONS

The remuneration of the directors was as follows:	2002 £'000	2001 £'000
Salaries and other emoluments	781	1,377

The number of directors who were members of pension schemes was as follows:	No.	No.
Defined benefit schemes	3	3

Pension contributions of £49,000 were made for the directors during the year (2001: £64,000).

The above amounts for remuneration include the following in respect of the highest paid director:	£'000	£'000
Emoluments	222	823
Pension contributions	26	10
	248	833

NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 December 2002

9. TAX CREDIT ON LOSS ON ORDINARY ACTIVITIES

	2002 £'000	2001 £'000
Current tax		
Adjustments in respect of prior years:		
- UK corporation tax	868	5,150

The differences between the total current tax shown above and the amount calculated by applying the standard rate of UK corporation tax to the profit before tax are as follows:

	2002 £'000	2001 £'000
Loss on ordinary activities before tax	(138,486)	(67,723)
Tax on profit on ordinary activities at standard UK corporation tax rate of 30% (2001: 30%)	41,546	20,317
Effects of:		
Expenses not deductible for tax purposes	(20,011)	(230)
Losses not recognised as a deferred tax asset	(21,535)	(20,087)
Adjustments to tax charge in respect of previous periods	868	5,150
Current tax credit for period	868	5,150

A deferred tax asset has not been recognised in respect of timing differences relating to tax losses due to the uncertainty of the profitability of the company in the foreseeable future. The amount of the asset not recognised is approximately £50,000,000 (2001: £41,000,000). The asset would be recovered if the company made sufficient profits in the future.

NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 December 2002

10. INTANGIBLE FIXED ASSETS

	Goodwill £'000
Cost	
At 1 January 2002	102,957
Additions	8,199
At 31 December 2002	111,156
Amortisation	
At 1 January 2002	5,645
Charge for the year	6,096
Impairment (see note 3)	65,869
At 31 December 2002	77,610
Net book value	
At 31 December 2002	33,546
At 31 December 2001	97,312

On 1 January 2001, Alcatel Telecom Limited a company incorporated in England and Wales, entered into an agreement to acquire the entire issued share capital of Alcatel Networks Limited, which itself owned Alcatel Networks Services Limited, for a consideration of £79,000,000.

On 23 January 2002, Alcatel Telecom Limited acquired the trade and assets of Alcatel Networks Services Limited. The trade and assets of Alcatel Networks Limited and Alcatel Networks Services Limited were transferred to Alcatel Telecom Limited, for a total consideration of £79,000,000.

On 1 April 2002, Alcatel Telecom Limited entered into an agreement to acquire the entire issued share capital of Alcatel Internetworking Limited. On the same date, the trade and assets of Alcatel Internetworking Limited were transferred to Alcatel Telecom Limited for a consideration of £855,000.

The following table explains the major categories of assets and liabilities acquired:

	Alcatel Networks *Services Limited* Book and fair value £'000	**Alcatel Internetworking *Limited*** Book and fair value £'000
Tangible fixed assets	-	2
Current assets	25,441	1,102
Creditors and provisions	(33,640)	(249)
Net (liabilities)/assets acquired	(8,199)	855
Goodwill	8,199	-
Consideration	-	855

NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 December 2002

11. TANGIBLE FIXED ASSETS

	Freehold land and buildings £'000	Leasehold improvements £'000	Plant and machinery £'000	Total £'000
Cost				
At 1 January 2002	5,915	602	22,206	28,723
Additions	3	-	3,096	3,099
Disposals	(79)	(47)	(9,572)	(9,698)
Transfers from subsidiary	-	-	2	2
At 31 December 2002	5,839	555	15,732	22,126
Depreciation				
At 1 January 2002	122	34	9,970	10,126
Charge for the year	124	38	4,546	4,708
Disposals	(3)	(13)	(8,117)	(8,133)
At 31 December 2002	243	59	6,399	6,701
Net book value				
At 31 December 2002	5,596	496	9,333	15,425
At 31 December 2001	5,793	568	12,236	18,597

Included within plant and machinery are assets held under finance leases with a net book value of £nil (2001: £51,000).

Freehold land amounting to £882,000 (2001: £882,000) has not been depreciated.

NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 December 2002

12. FIXED ASSET INVESTMENTS

	£'000
Cost and net book value	
At 1 January 2002	79,000
Additions	13,583
Disposals	(12,728)
At 31 December 2002	79,855

On 6 February 2002, the company increased its investment in Alcatel eBusiness Distribution Limited by £12,727,777 by purchasing 12,727,777 £1 ordinary shares.

On 19 February 2002, the investment in Alcatel eBusiness Distribution Limited was sold to Drivelec SAS, a group company wholly owned by Alcatel S.A. in France. The consideration received was 1 Euro. The loss on sale of the investment recorded was £12,727,776.

The balance of the additions figure represents the fair value of the consideration paid upon acquisition of the trade and assets of Alcatel Internetworking Limited (note 10).

The company had investments in the following subsidiary undertakings:

	Country of incorporation or principal business address	Principal activity	Holdings
Alcatel Internetworking Limited	United Kingdom	Telecoms services	100%
Alcatel Networks Limited	United Kingdom	Dormant	100%
Alcatel Networks Services Limited	United Kingdom	Dormant	100%

13. STOCKS

The following are included in the net book value of stocks:	2002 £'000	2001 £'000
Spares	2,124	3,478
Finished goods	11,736	21,520
	13,860	24,998

There is no material difference between the balance sheet value of stocks and their replacement cost.

NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 December 2002

14. DEBTORS

	2002 £'000	2001 £'000
Amounts falling due within one year:		
Trade debtors	23,281	29,417
Amounts owed by group undertakings	38,943	52,241
Prepayments and accrued income	4,194	24,513
	66,418	106,171
Amounts falling due after more than one year:		
Pension prepayments	-	5,326
Corporation tax	8,552	8,404
Amounts owed by group undertakings	5,177	-
	13,729	13,730
	80,147	119,901

15. CREDITORS: AMOUNTS FALLING DUE WITHIN ONE YEAR

	2002 £'000	2001 £'000
Obligations under finance leases and hire purchase contracts	-	8
Trade creditors	15,059	14,083
Amounts owed to other group undertakings	209,679	264,759
Other creditors:		
- social security and PAYE	1,075	937
- other creditors	5,117	290
Accruals and deferred income	29,466	25,043
	260,396	305,120

NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 December 2002

16. PROVISIONS FOR LIABILITIES AND CHARGES

	2002 £'000	2001 £'000
Provision for restructuring	121	2,093
Provision for warranties	475	1,047
Vacant property provision	21,992	17,360
	22,588	20,500

The movements in provision are as follows:

	Restructuring £'000	Warranties £'000	Vacant property provision £'000	2002 Total £'000	2001 Total £'000
At beginning of year	2,093	1,047	17,360	20,500	6,192
Charged to profit and loss account	5,170	-	10,285	15,455	30,374
Transferred from subsidiary undertaking	-	-	-	-	1,812
Utilised during the year	(7,142)	(572)	(5,653)	(13,367)	(17,878)
At end of year	121	475	21,992	22,588	20,500

Restructuring

The company has provided for the cost of redundancies resulting from a restructuring of the business. This is to be utilised within the next financial year.

Warranties

Warranty provisions represents expected warranty claims on products sold in the last three years. The majority of this expenditure will be incurred in the next financial year.

Vacant property provisions

This represents provisions for vacated properties. The leases expire within the next 15 years.

NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 December 2002

17. CALLED UP SHARE CAPITAL

	2002 £	2001 £
Authorised		
160,000,000 Ordinary shares of £1 each	160,000,000	100,000,000

	£	£
Issued, allotted, called up and fully paid		
Ordinary shares of £1 each	148,711,268	88,711,268

The authorised share capital was increased by 60,000,000 £1 ordinary shares on 23 December 2002. On that date 60,000,000 shares were issued at par for cash consideration.

18. RESERVES

	Share premium £'000	Profit and loss account £'000	2002 Total £'000
At beginning of year	47,289	(118,480)	(71,191)
Retained loss for the financial year	-	(137,618)	(137,618)
At end of year	47,289	(256,098)	(208,809)

19. RECONCILIATION OF MOVMENT IN SHAREHOLDERS' (DEFICIT)/FUNDS

	2002 £'000	2001 £'000
Loss for the financial year	(137,618)	(62,573)
Issue of share capital	60,000	31,711
Share premium	-	47,289
Net (decrease)/increase in shareholders' funds	(77,618)	16,427
Opening shareholders' funds	17,520	1,093
Closing shareholders' (deficit)/funds	(60,098)	17,520

NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 December 2002

20. GUARANTEES AND OTHER FINANCIAL COMMITMENTS

Capital commitments

At the end of the year capital commitments were:	**2002 £'000**	**2001 £'000**
Contracted for but not provided	18	654

Guarantees

The company has provided a £1,080,000 (2001: £1,080,000) guarantee to Royal Mail in respect of franking machines sold and serviced before the demerger of the franking machine business in 1992. It also has other guarantees of £6,063,000 (2001: £3,831,000) in respect of duty deferment guarantees and performance bonds.

Lease commitments

At 31 December 2002 the company had annual commitments under non-cancellable operating leases as follows:

	2002		**2001**	
	Plant and *machinery* £'000	**Land and *buildings* £'000**	**Plant and *machinery* £'000**	**Land and *buildings* £'000**
Expiry date:				
- within one year	412	807	616	-
- between two and five years	555	92	1,191	997
- after five years	-	3,864	-	3,658
	967	4,763	1,807	4,655

Pension arrangements

The company provides a defined benefit pension scheme for the majority of its employees. The assets of the scheme are held in a separate trustee administered fund and the scheme does not invest in the company.

The pension cost relating to the scheme is assessed in accordance with the advice of independent qualified actuaries and employer's contributions to the scheme are paid as recommended by the actuaries. Employees' normal contributions are paid to the scheme.

The scheme is valued at regular intervals, usually triennially. An actuarial valuation of the scheme was carried out as at 30 June 2000. The market value of the scheme's assets at that date was £207,400,000.

20. GUARANTEES AND OTHER FINANCIAL COMMITMENTS (continued)

Pension arrangements (continued)

The main assumptions were that the investment return would be 7.5% per annum, salary increases would average 5.3% per annum, and future pensions would increase by 2.7% per annum. Using these assumptions, the actuarial valuation showed that the actuarial value of the scheme's assets was sufficient to cover 96% of the value of benefits accrued to members after allowing for expected future increases in earnings. Having regard to the size of the deficit, the actuaries advised that the company contribute at the rate of 12.5% of pensionable earnings with effect from April 2001.

The projected unit method was used both for the funding of the scheme and in assessing pension costs for accounting purposes. Members retiring are assumed to be replaced by new entrants so that the average age of the membership remains constant.

FRS17 disclosure

Additional disclosures regarding the group defined benefit pension scheme are required under the transitional provisions of FRS17 "Retirement benefits". In accordance with FRS17, the company will account for its contributions to the scheme as if it were a defined contribution scheme because it is not possible to identify the company's share of the assets and liabilities in the scheme on a consistent and reasonable basis. The latest actuarial valuation of the scheme, prepared for the purposes of making the transitional disclosures in accordance with FRS17 in the financial statements of the parent company, shows a deficit of £4,045,000. Further details of this valuation can be found in the annual report of Alcatel (UK) Limited which can be obtained from Christchurch Way, Greenwich, London, SE10 0AG.

21. ULTIMATE PARENT COMPANY AND CONTROLLING PARTY

The company is a subsidiary undertaking of Alcatel S.A. incorporated in France.

The smallest and largest group of which Alcatel Telecom Limited is a member and for which group financial statements are drawn up is that headed by Alcatel S.A.

The consolidated financial statements of this group are available to the public and may be obtained from the corporate offices at 54 rue La Boétie, 75008 Paris, France.

As a wholly owned subsidiary of Alcatel S.A., in accordance with FRS8 "Related party disclosures", the company is not required to disclose transactions with other members of the group.

NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 December 2002

22. SUBSEQUENT EVENTS

On 1 January 2003, Alcatel Telecom Limited entered into an agreement to acquire the entire issued share capital of Alcanet International UK Limited. On the same date, the trade and assets of Alcanet International UK Limited were transferred to Alcatel Telecom Limited for a consideration of £524,000. The following table explains the major categories of assets and liabilities acquired:

	Book and fair value £'000
Fixed assets	127
Current assets	1,192
Creditors and provisions	(795)
	524

On 1 January 2003, Alcatel Telecom Limited purchased certain assets and liabilities from Alcatel Ireland Limited at net book value, for cash consideration. The following table explains the major categories of assets and liabilities acquired:

	Book and fair value £'000
Current assets	10,329
Creditors and provisions	(4,361)
	5,968

On 1 April 2003, Alcatel Canada Inc. sold all but one of its shares in Alcatel Telecom Limited to Alcatel UK Limited.

On 23 May 2003, Alcatel Telecom Limited purchased certain assets from Thirdspace Living Limited. The following table explains the major categories of assets acquired:

	Book and fair value £'000
Tangible fixed assets	458
Intangible fixed assets	3,661
Fixed asset investments	31
	4,150

On 15 September 2003, Alcatel Telecom Limited increased its authorised share capital from 160,000,000 to 225,000,000 £1 ordinary shares. On the same date, Alcatel Telecom Limited issued 65,000,000 £1 ordinary shares, at par, to Alcatel UK Limited.