

Notes to Financial Statements

01 Accounting policies

The principal accounting policies are summarised below. All of these have been applied consistently throughout the year and the preceding year.

a) Basis of accounting

The financial statements have been prepared under the historical cost convention, modified to include the revaluation of certain investments, and in accordance with applicable United Kingdom financial reporting and accounting standards, including the adoption of Urgent Issues Task Force Abstract 38 "Accounting for ESOP trusts" ("UITF 38"), which has come into force since the previous year end.

UITF 38 requires that the Company's shares held by the Group's Employee Share Ownership Plan ("ESOP"), which were previously held within fixed asset investments, be presented as a deduction from shareholders' funds. In addition, the charge to the profit and loss account in relation to awards under the Long Term Incentive Plan ("LTIP"), the Key Contributor Plan ("KCP") and the Equity Bonus Plan ("EBP"), which was previously based on the cost of shares held by the ESOP, is now based on the difference between the market price on the date of grant and the exercise price.

The adoption of UITF 38 has been treated as a prior year adjustment with comparative figures being restated accordingly. The adoption has resulted in the restatement of the following primary statements and notes: the Consolidated Profit and Loss Account; the Consolidated Balance Sheet; Operating expenses, net; Profit on ordinary activities before taxation; Staff costs; Taxation; Earnings per share; Other fixed asset investments; Creditors: amounts falling due within one year; and the Reconciliation of movement in shareholders' funds. The impact of the prior year adjustment on brought forward net assets and the profit for the year to 30 June 2003 has been disclosed in note 23.

The Group has taken advantage of the exemption in Urgent Issues Task Force Abstract 17 (Revised 2003) "Employee share schemes" and has not applied the abstract to the Group's Inland Revenue approved Sharesave Scheme.

b) Basis of consolidation

The Group financial statements consolidate the financial statements of the Company and all of its subsidiary undertakings. All companies are consolidated using acquisition accounting, and all inter-company balances and transactions have been eliminated on consolidation.

The Group maintains a 52 or 53 week fiscal year ending on the Sunday nearest to 30 June in each year. In fiscal year 2004 this date was 27 June 2004, this being a 52 week year (2003: 29 June 2003, 52 week year).

The Company has taken advantage of the exemption in section 230 of the Companies Act 1985 not to present its own profit and loss account. The Company's result for the financial year determined in accordance with the Act is disclosed in note 23.

c) Acquisitions

On the acquisition of a business, fair values are attributed to the Group's share of separable net assets acquired. Subsidiary undertakings are accounted for from the effective date of acquisition until the effective date of disposal. Adjustments are also made to bring the accounting policies into line with those of the Group. Where statutory merger relief is applicable, the difference between the fair value of the shares issued as purchase consideration and the nominal value of the shares issued as purchase consideration has been treated as a merger reserve in the consolidated accounts. The results and cash flows relating to an acquired business are included in the consolidated profit and loss account and the consolidated cash flow statement from the date of acquisition.

d) Goodwill and other intangible assets

Where the cost of acquisition exceeds the fair values attributable to the net assets acquired, the difference is treated as purchased goodwill and capitalised on the Group balance sheet in the year of acquisition. Purchased goodwill arising on acquisitions from 1 July 1998 is capitalised. Prior to 1 July 1998, goodwill arising on acquisitions was eliminated against reserves. As permitted by FRS 10, this goodwill has not been restated on the balance sheet. On disposal or closure of a previously acquired business, any goodwill previously written off to reserves is included in calculating the profit or loss on disposal.

Other intangible assets, all of which have been acquired and are controlled through custody or legal rights and could be sold separately from the rest of the business, are capitalised where fair value can be reliably measured.

Where capitalised goodwill and intangible assets are regarded as having a limited useful economic life, the cost is amortised on a straight-line basis over that life of up to 20 years. Any amortisation or impairment write-downs are charged to the profit and loss account.

e) Tangible fixed assets

Tangible fixed assets are stated at cost, net of accumulated depreciation and any provision for impairment. Land and assets in the course of construction are not depreciated.

Depreciation is provided to write off the cost, less estimated residual value, of each asset on a straight-line basis over its estimated useful life. Principal annual rates used for this purpose are:

Freehold buildings	4%
Leasehold improvements	Lower of lease period or life of the asset
Equipment, fixtures and fittings:	
- Fixtures and fittings	10% - 20%
- Computer equipment	20% - 33 $\frac{1}{3}$ %
- Technical equipment	10% - 20%
- Motor vehicles	25%

f) Impairment of fixed assets and goodwill

Intangible fixed assets, goodwill and tangible fixed assets are reviewed for impairment if events or circumstances indicate that the carrying value may not be recoverable. Goodwill and intangible fixed assets are also reviewed for impairment at the end of the first full financial year after acquisition. Should an impairment review be required, this is performed in accordance with Financial Reporting Standard ("FRS") 11, "Impairment of fixed assets and goodwill".

g) Interests in joint ventures

Joint ventures are entities in which the Group holds a long-term interest and shares control under a contractual arrangement. These investments are dealt with by the gross equity method of accounting. Provision is made within creditors where the Group's share of a joint venture's loss exceeds the Group's funding to date.

h) Fixed asset investments

The Group's fixed asset investments are stated at cost, less any provision for permanent diminution in value.

In the Company's financial statements, investments in subsidiary undertakings are stated at cost, with the exception of the investment in Sky Television Limited which is stated at valuation. Provision is made for any impairment in value. Where statutory merger relief is applicable, the cost has been measured by reference to the nominal value only of the shares issued. Any premium has not been recognised.

i) Stocks

Acquired and commissioned television programme rights

Programme rights are stated at cost including, where applicable, estimated escalation payments, and net of accumulated amortisation. Provisions are made for any programme rights which are surplus to Group requirements or which will not be shown for any other reason.

Contractual obligations for programme rights not yet available for transmission are not included in the cost of programme rights, but are disclosed as contractual commitments (see note 24). Payments made upon receipt of commissioned and acquired programming, but in advance of the legal right to broadcast the programmes, are treated as prepayments. Programme rights are recorded in stock at cost when the programmes are available for transmission.

Amortisation is provided to write off the cost of programme rights. The principal rates used for this purpose are:

Sports - 100% on first showing, or, where contracts provide for sports rights for multiple seasons or competitions, the amortisation of each contract is based on anticipated revenue.

01 Accounting policies (continued)

Current affairs – 100% on first showing.

General entertainment – Straight-line basis on each transmission.

- One showing planned – 100%
- Two showings planned – 60%; 40%
- Three showings planned – 50%; 30%; 20%
- Four showings planned – 40%; 30%; 20%; 10%

Movies – Acquired movies are amortised on a straight-line basis over the period of transmission rights. Where acquired movie rights provide for a second availability window, 10% of the cost is allocated to that window. Own movie productions are amortised in line with anticipated revenue over a maximum of five years.

Set-top boxes and related equipment

Set-top boxes and related equipment includes digital set-top boxes, Low Noise Blockers (“LNBs”) and mini-dishes. These stocks are valued at the lower of cost and net realisable value (“NRV”), the latter of which reflects the value to the business of the set-top box and the related equipment in the hands of the customer. Any subsidy is expensed on enablement, which is the process of activating the viewing card once inserted in the set-top box upon installation, so as to enable a viewer to view encrypted broadcast services, and effectively represents the completion of the installation process for new subscribers.

Raw materials, consumables and goods held for resale

Raw materials, consumables and goods held for resale are valued at the lower of cost and NRV.

j) Transponder rental prepayments

Payments made in advance to secure satellite capacity have been recorded as prepaid transponder rentals. These payments are amortised on a straight-line basis to the profit and loss account from commencement of broadcasting to the end of the rental period, normally 10 years.

k) Taxation

Corporation tax payable is provided at current rates on all taxable profits.

l) Deferred taxation

Deferred tax is recognised in respect of 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.

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 against which carried forward tax losses can be offset and from which the future reversal of 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. Deferred tax is measured on a non-discounted basis.

m) Foreign currency

Trading activities denominated in foreign currencies are recorded in sterling at actual exchange rates as of the date of the transaction or at the contracted rate if the transaction is covered by a forward foreign exchange contract or other hedging instrument. Monetary assets, liabilities and commitments denominated in foreign currencies at the year end are reported at the rates of exchange prevailing at the year end or, if hedged, at the appropriate hedged rate.

n) Derivatives and other financial instruments

The Group uses a number of derivative financial instruments to hedge its exposures to fluctuations in interest and foreign exchange rates. Receipts and payments on interest rate instruments are recognised on an accruals basis over the life of the instrument. Gains and losses on those instruments which are designated as hedges are not recognised until the underlying creditor being hedged is recognised.

Cash flows associated with derivative financial instruments are classified in the cash flow statement in a manner consistent with those of the underlying transactions being hedged. If an instrument ceases to be designated as a hedge, for example, by the underlying hedged position being eliminated, the instrument is marked to market and any resulting gain or loss is recognised immediately in the profit and loss account.

The Group does not hold or issue derivative financial instruments for speculative purposes.

o) Turnover

Turnover, which excludes value added tax and sales between Group companies, represents the value of products and services sold. The Group's main sources of turnover are recognised as follows:

- Revenues from the provision of direct-to-home (“DTH”) subscription services are recognised as the services are provided. Pay-per-view revenue is recognised when the event, movie or football match is viewed.
- Cable revenues are recognised as the services are provided to the cable wholesalers and are based on the number of subscribers taking the Sky channels, as reported to the Group by the cable companies, and the applicable rate card.
- Advertising sales revenues are recognised when the advertising is broadcast.
- Interactive revenues include income from betting and gaming, on-line advertising, e-mail, e-commerce, telephony income from the use of interactive services (e.g. voting), text services and set-top box subsidy recovery revenues earned through conditional access and access control charges made to customers on the Sky digital platform. Betting and gaming revenues represent: a) amounts receivable in respect of bets placed on events which occur in the year; and b) net customer losses in the year in respect of the on-line casino operations. All other Interactive revenues are recognised when the goods or services are delivered.
- Other revenues principally include income from installations, Sky+ and Multiroom Digibox sales revenues, Sky Talk revenues, sales of set-top boxes, service call revenue, warranty revenue, customer management service fees, conditional access fees and access control fees. Other revenues are recognised, net of any discount given, when the relevant service has been provided.

Revenues derived from the sale of surplus programming and surplus transponder capacity are recognised net against programming and transmission and related functions costs respectively, since these revenues are not derived from transactions that the Group is in business to provide.

p) EBITDA

EBITDA (earnings before interest, taxation, depreciation and amortisation) is calculated as operating profit before depreciation and amortisation or impairment of goodwill and intangible fixed assets.

q) Pension costs

The Group provides pensions to eligible employees through the BSKyB Pension Plan, a defined contribution pension scheme. The amount charged to the profit and loss account in the year represents the cost of contributions payable by the Group to the scheme in that year. The assets of the BSKyB Pension Plan are held independently of the Group.

r) Leases

Assets held under finance leases, which confer rights and obligations similar to those attached to owned assets, are treated as tangible fixed assets. Depreciation is provided over the shorter of the lease term and the asset's useful economic life, and the deemed capital element of future rentals is included within creditors. Deemed interest is then taken to the profit and loss account as interest payable over the life of the lease.

The rental costs arising from operating leases are charged to the profit and loss account in the year in which they are incurred.