Elements of Remuneration

Basic salary

Basic salaries for executive Directors are reviewed by the Remuneration Committee usually annually taking into account individual performance, skills and competitiveness. In assessing competitiveness, the Committee considers comparator groups in both Europe and the US, but weighted towards Europe. Comparator groups include both companies in similar sectors and companies with similar levels of turnover. Performance assessment of executive Directors includes the performance of the Company and the achievement of individual objectives. No increases in basic salaries were awarded to executive Directors at the normal review date of 1 July 2001, except in the case of promotion. With effect from 1 April 2002, Mr Parton's base salary was increased from £400,000 to £525,000 but as part of a wider review of his remuneration, a payment of £125,000 per annum made to Mr Parton in respect of his pension arrangements was discontinued.

Short term incentive bonus

No short term incentive bonus scheme for executive Directors operated in the year ended 31 March 2002 and accordingly no performance-related bonuses were awarded to executive Directors for the year ended 31 March 2002.

Longer term incentives

The Company, has since its formation, operated two main discretionary plans, the 1999 Stock Option Plan and the Long Term Incentive Plan.

Options may be granted under the 1999 Stock Option Plan for a period of up to ten years from 30 November 1999. At the July 2001 Annual General Meeting, shareholders approved amendments to the plan rules giving the Remuneration Committee discretion to grant options which become exercisable over varying periods of time and which are subject to performance conditions appropriate to the markets in which the Company operates. In previous years, the Company's policy on the granting of options has been to make phased awards to key employees, based on business and personal performance, with the value of options granted normally ranging from 50 per cent to 150 per cent of basic salary per annum. Reductions in the Company's share price meant both, that option holdings built up over a number of years (with the minimum exercise value of any option granted under the Plan having been £6.70) had lost any value as an incentive, and that grants based on these multiples of salary would result in an unacceptable level of dilution. In granting options to around 600 key executive, technical, and sales and marketing staff (including executive Directors) in November 2001, the Committee sought to balance an appropriate level of dilution with the need to provide a meaningful level of incentive. In exercising its discretion in respect of performance targets, the Committee recognised the need for the Company to achieve its short term objectives in order to deliver longer term performance. Of each option granted in November 2001, 50 per cent is subject to the achievement of targets for the reduction in the Company's net debt, and 50 per cent subject to Marconi's Total Shareholder Return being better than that of the company at the fiftieth percentile for FTSE 100 companies. In order to provide a progressive incentive, options become exercisable, subject to the achievement of the performance conditions, over four years.

Under the rules of the Long Term Incentive Plan, executive Directors can receive an annual award of notional shares up to a maximum value of 50 per cent of base salary. Three years after the award, participants may be granted a nil cost option to acquire Marconi shares, up to the number covered by the award, subject to a demanding performance condition. For executive Directors this requires Marconi's Total Shareholder Return to be at or above that of the top 50 companies in the FTSE 100 share index, for other executives the requirement is for Total Business Return to be above 17 per cent. To the extent that the awards vest, the nil cost options are normally exercisable in three equal tranches on date of grant and one and two years thereafter. In respect of awards made in 1998, nil cost options to acquire Marconi shares were granted to executive Directors on 18 June 2001 as follows: Mr M W J Parton – 28,405; Mr M J Donovan – 6,036; Mr S Hare – 17,394. Owing to changed circumstances, no awards were made in 2001 and the Company is currently reviewing the future operation of the plan.

In addition, the Company also operates the Marconi UK Sharesave Plan and the Marconi Launch Share Plan (under which participants are eligible to receive 1,000 nil cost options in the event of the Company's share price reaching £16.03 before November 2004) in which the executive Directors and all eligible employees may participate. No award was made under the UK Sharesave Plan in 2001/02.

The Company has previously operated a personal shareholding policy in order to assist further in aligning the interests of executives and shareholders. The policy requires executive Directors to build up, over a period of time, a target shareholding of Marconi shares with a market value equal to three times annual basic salary. The policy was not applied to the November 2001 option grant as it was not considered to be practical to do so, given the Company's share price.

Retirement Benefits

All executive Directors are members of the Group's pension scheme, The G.E.C. 1972 Plan. Members contribute at the rate of 3 per cent of salary subject to limits imposed by the Inland Revenue. Company contributions made during the year ended 31 March 2002 amounted to 6.6 per cent of salary similarly restricted (2001 6.6 per cent). The Company has announced that, with effect from 6 April 2002, it will increase employers' contributions to 14.2 per cent of salary. Basic salary is the only element of remuneration that is pensionable other than for Mr Hare whose bonuses are pensionable in accordance with the terms of The G.E.C. 1972 Plan. As with all employees who joined the Plan prior to the introduction of the statutory earnings cap on pensions introduced in April 1989, Mr Hare's bonus is pensionable. Further details about the Directors' benefits under the G.E.C. 1972 Plan are given below.

Funded unapproved retirement benefit schemes ("FURBS") were operated during the year for five executive Directors – Lord Simpson, Mr J C Mayo, Mr M J Donovan, Mr R I Meakin and Mr M W J Parton. The Company makes contributions to each of the FURBS on the advice of the actuary; such contributions are calculated to produce a capital sum targeted to provide benefits at the normal retirement age equivalent to a two-thirds pension. The targeted benefit takes into account the capital value of benefits arising from membership of The G.E.C. 1972 Plan and any relevant benefit in payment or otherwise arising from previous employment. Normal retirement age is 62 for executive Directors. In the event of cessation of employment before normal retirement age, or at retirement age, each of the Directors is entitled to the amount held in the FURBS established for him. The Remuneration Committee has reviewed the cost of such arrangements and has decided that it is not appropriate to the Company's changed circumstances and will seek to change the basis of the FURBS it provides for executive Directors and senior employees. In future, with the exception of the FURBS established for the benefit of Mr Donovan, all FURBS will be based upon "defined contribution" rather than the present "defined benefit" arrangements.

In accordance with the requirements of the Listing Rules, the disclosures required for the year ended 31 March 2002 are set out below.

In previous years, the contributions made to the Directors' FURBS have been disclosed on a defined contribution basis. For the current year, owing to certain guarantees from the Company which underpin the Directors' pension entitlements, the Directors believe that it is more appropriate to disclose the FURBS arrangements on a defined benefit basis in accordance with Actuarial Guidance Note GN11. This is consistent with the treatment of benefits accrued under The G.E.C. 1972 Plan.

In addition to this disclosure, the Directors' remuneration table above also discloses within pension contributions, the contributions paid by the Company in respect of these FURBS arrangements and all other pension arrangements, including The G.E.C. 1972 Plan.

(a) the pension benefits earned by the Directors of Marconi plc under the FURBS arrangements for the period to 31 March 2002

Name of Director	Length of pensionable service (years)	Increase in gross unapproved accrued pension during the year £000	Net cost of unapproved pension benefits accrued during the year £000	Accumulated total gross unapproved accrued pension at 31 March 2002 £000
M J Donovan	3	10	54	68
J C Mayo*	3	25	107	159
R I Meakin*	5	7	66	102
M W J Parton	11	12	58	52

* at the date of cessation of employment

The pension entitlement shown above is that which would be paid annually at normal retirement age based on service to 31 March 2002. The increase in accrued pension during the year excludes any increase for inflation. Mr Mayo resigned as a Director of Marconi plc on 6 July 2001 and Mr Meakin resigned from the Company on 31 March 2002. During the year, the Company made the following payments to the Trustee of the FURBS in respect of individual Directors: Mr J C Mayo £633,000 (2001 £374,000); Mr M J Donovan £63,966 (2001 £63,181); Mr R I Meakin £290,000 (2001 £290,000); and Mr M W J Parton £147,000 (2001 £147,000). No entry is shown for Lord Simpson as, in his case, his defined contribution entitlement due under the FURBS was completed in the year by the payment of £212,000 to the trustee of the FURBS. The contributions are determined each year based on actuarial advice to be sufficient to meet the obligations. Periodically the contributions are reviewed by the actuary.

(b) the pension benefits earned by the Directors under the G.E.C. 1972 Plan

Name of Director	Length of pensionable service (years)	Increase in accrued pension during the year £000	Cost of pension benefits accrued during the year net of member's contributions £000	Accumulated total accrued pension at 31 March 2002 £000
M J Donovan	3	2	2	6
S Hare	13	18	100	67
J C Mayo*	3	7	58	12
R I Meakin*	5	2	11	9
M W J Parton	11	3	11	24
Lord Simpson*	4	1	8	8

* at the date of cessation of employment

The pension entitlement shown above is that which would be paid annually at normal retirement age based on service to 31 March 2002. The increase in accrued pension during the year excludes any increase for inflation. The cost of pension benefits accrued during the year net of member's contributions has been calculated on the basis of actuarial advice in accordance with Actuarial Guidance Note GN11. The cost of pension benefits accrued during the year net of member's contributions is a measure of the capital cost of providing future pension payments and accordingly is a liability of the Group's pension arrangements and not a sum paid or due to the Directors of the Company.

The ability of the Company to satisfy pension obligations for Directors subject to the earnings cap from the Company's approved pension scheme, rather than unapproved schemes, is influenced by benefits payable from other approved pension schemes from their previous employment. In respect of Mr Parton, benefits accrued under approved plans from previous employment are lower than previously anticipated. Consequently, a higher proportion of his accrued pension benefit can be paid from the Plan, as opposed to FURBS arrangements and his accrued pension under the Plan has been increased as a result. His entitlement under the FURBS arrangements has been reduced by a corresponding amount.

Members of the plan have the option to make contributions to the Selected Benefit Scheme (an additional voluntary contribution scheme); neither the contributions nor the resulting benefits are included in the above table.

Death in service benefits

In the event of death in service, a lump sum of four times pensionable salary, plus additional benefits for a surviving spouse and/or children, inclusive of any death benefits arising from The G.E.C. 1972 Plan, will be held in trust for the benefit of dependants of each of Mr M J Donovan, Mr S Hare and Mr M W J Parton.

Directors' Interests

The Directors' interests as defined by the Companies Act 1985 (which include trustee holdings and family interests incorporating holdings of minor children) in shares of the Company and its subsidiaries are as follows:

(a) Ordinary shares

	As at 31 March 2002 Beneficial	As at 1 April 2001 (or later appointment) Beneficial
D C Bonham	156,000	6,000
Sir William Castell	10,000	10,000
The Rt Hon The Baroness Dunn	10,000	10,000
M J Donovan	169,591	67,601
S Hare	30,121	1,660
M W J Parton	128,122	28,860
Sir Alan Rudge	20,000	10,000
Hon Raymond G H Seitz	11,099	11,095
N J Stapleton	21,572	13,572

None of the Directors held any non-beneficial interests in the shares of the Company during the year.

There have been no other changes in the interests of Directors between 31 March 2002 and 15 May 2002.

(b) Options

The following table shows the interests of Directors in options over ordinary shares of 5 pence each in the Company:

	At 1 April 2001		Granted in the year		Exercised in the year		Lapsed in the year		At 31 March 2002		Exercisable	
	No.	Average exercise price pence	No.	Exercise price pence	No.	pence	No.	pence	No.	Average exercise price pence	From	To
M J Donovan	1,000	nil	6,036	nil	737	nil	–	–	6,299	nil	Jun 2001	Nov 2009
	800,000	662	2,500,000	35	–	–	–	–	3,300,000	187	Oct 2001	Dec 2010
S Hare	1,000	nil	17,394	nil	5,798	nil	–	–	12,596	nil	Jun 2001	Nov 2009
	484,034	586	2,000,000	35	–	–	–	–	2,484,034	142	Feb 1997	Nov 2010
M W J Parton	1,000	nil	28,405	nil	–	–	–	–	29,405	nil	Jun 2001	Nov 2009
	1,456,591	603	3,000,000	35	8,497	203	3,136	538	4,444,958	221	Oct 2000	Dec 2010

Notes

1 All options have exercise prices that exceed the market price of a Marconi share as at 28 March 2002, other than nil cost options granted under the Launch Share Plan (1,000 shares at nil cost) and the Long Term Incentive Plan.

2 Mr S Hare was appointed a director of Marconi plc on 10 April 2001 and his options are shown at that date.

3 Gains totalling £1,747 were made by Mr M J Donovan in the exercise of share options during the period 1 April 2001 to 31 March 2002. Gains totalling £6,436 were made by Mr S Hare in the exercise of share options during the period 10 April 2001 to 31 March 2002. Gains totalling £11,811 were made by Mr M W J Parton in the exercise of share options during the period 1 April 2001 to 31 March 2002.

4 The mid-market price of a Marconi share as at 28 March 2002 was 6.96 pence with a range during the year of 6.25 pence to 424 pence.

5 The options set out above relate to those granted under the Manager's 1984 Share Option Scheme, the 1997 Executive Share Option Scheme, the Marconi 1999 Stock Option Plan, the Phantom Option Schemes, the Marconi Launch Plan, the Long-Term Incentive Plan, the Employee 1992 Savings-Related Share Option Scheme and the Marconi UK Sharesave Plan.

6 The information provided above is a summary and full details of Directors' shareholdings and options are contained in the Company's Register of Directors' Interests.

Service Contracts

With effect from 1 December 2001, the terms of employment of each executive Director are covered by a service contract with Marconi plc, subject to termination by either party giving not less than one year's notice or, if not already terminated on reaching the age of 62 years. Other than Mr M J Donovan, none of the Directors offering themselves for re-election at the forthcoming Annual General Meeting has a service contract with the Company or any of its subsidiaries.

When considering compensation payable in respect of termination of service contracts of executive Directors, the Committee would pay due regard to the need for mitigation.

Non-executive Directors serve for a period of three years, subject to renewal by agreement with the Board.

External Appointments

With the approval of the Chairman of the Company, executive Directors are permitted to hold appointments outside the Company. Any fees payable in connection with such appointments are retained by Directors unless otherwise agreed.

Membership and Framework of the Remuneration Committee
The Remuneration Committee consists of wholly independent non-executive Directors. During the year, the members of the Committee were:

Sir William Castell (Chairman)
D C Bonham
Sir Alan Rudge
Hon Raymond G H Seitz
N J Stapleton

D C Bonham was appointed to the Committee on 16 May 2001 and as its Chairman on 18 July 2001. Sir William Castell was appointed Chairman of the Committee with effect from 22 November 2001 in place of Mr Bonham on his appointment as Interim Chairman of the Company.

The Committee meets at least three times a year and makes decisions on behalf of the Board on the contracts of service and the remuneration packages of the Interim Chairman and executive Directors. The Committee also determines the framework within which executive remuneration is more generally determined and in its review of executive Directors' pay takes account of the remuneration of the other employees. The Committee has access to and takes professional advice from inside and outside Marconi. During the year, the Company has used the services of a number of external advisers. The Committee also takes the advice of the Interim Chairman and Chief Executive, as appropriate, on the performance of the executive Directors. The fees of non-executive Directors are reviewed and determined by the Board.

In preparing this report, the Remuneration Committee has given full consideration to the provisions set out in Schedule B to the Combined Code.

On behalf of the Board of
Marconi plc

Sir William Castell
Chairman of the Remuneration Committee
15 May 2002

Corporate Social Responsibility

During the year, work has continued on developing policies, procedures and verification in the areas of social, environmental, and ethical matters, which can affect the Group's business. The Group has undergone substantial change in its circumstances but the Board of Marconi remains committed to achieving the highest standards of corporate social responsibility commensurate with the Group's other objectives.

Policies

Marconi has identified 6 main areas of focus for the implementation of its policies across the Group's activities:

1 Corporate Social Responsibility;
2 Environmental;
3 Health and Safety;
4 Human Rights;
5 Product Safety; and
6 Ethics.

Existing policies covering environment, product safety and ethics have been reviewed during the year and where appropriate amended to reflect the Group's changed circumstances. New policies including those covering human rights have been developed and are presently under review.

Managing the risks

From January 2002, the Executive Committee of the Board also acted as the Group's Business Risk Committee and assumed Board responsibility for the business risk management process.

An Environment and Health & Safety Council has been established which will meet quarterly to review audits carried out by the Marconi Environment and Health & Safety department. Reporting through the Executive Committee, this will permit the Board to assess the ongoing management of social, environmental and ethical issues. Marconi considers that presently, those areas do not present any significant risks to the business in either the short or long term.

Major developments during the year

During the year, Marconi established a central environment and health & safety department (replacing the former Safety and Environment Unit) to support Marconi's commitment to world class standards in environmental and health & safety matters. This increases the Group's focus on the operational environment and health & safety whilst maintaining a strategic overview. The Group's network of regional experts are shared across all of Marconi's businesses whilst at the same time ensuring that each geographic region receives the necessary support. New policies are being introduced which set best in class practices that will be benchmarked against key performance indicators.

Audits continue to be undertaken on all of the Group's businesses and this year no significant instances of non-compliance with the Group's policies were identified.

Marconi has continued to work closely with its customers, suppliers, trade and industry associations and standards organisations during the year to develop and promote sustainable management systems and business solutions. 11 Marconi businesses are now registered to ISO 14001 covering the key operational sites in the UK, Germany and Italy with more expected to gain registrations during the year to 31 March 2003.

Social, environmental and ethical standards

Through the development of its policies, implementation of programmes supporting those policies and the monitoring of the results, Marconi aims to achieve world class social, environmental and ethical standards which in turn, it believes should have a positive impact on the Group's business.

Treasury Policies and Organisation
The Group's Treasury activities are co-ordinated by the Director of Treasury and Risk Management. In addition to the treasury function, the department is responsible for insurance risk management, and monitors the exposures arising from the various Marconi employee share plans. Overall responsibility for the customer financing activities of Marconi Finance plc rests with the Director of Treasury and Risk Management.

The department does not operate as a profit centre and its operations are conducted within a framework of policies and procedures approved by the Board. Treasury advises operational management on treasury matters and undertakes all derivative transactions except certain forward exchange contracts relating to the hedging of foreign currency transaction exposures arising in the operating businesses.

Financial Instruments
The Group uses financial instruments, including derivatives (principally interest rate swaps, cancellable interest rate swaps, currency swaps and forward foreign currency contracts) to manage interest rate and currency risk exposures. More information on financial instruments is provided in note 29 to the Accounts.

It is policy that there is no trading in financial instruments, and all financial instruments are used for the purpose of financing or hedging identified exposures of the Marconi group.

The main risks faced by the Group in the financial markets are liquidity risk, interest rate risk, foreign currency risk, counterparty risk and share price risk. The Board reviews and agrees policies for managing each of these, which are summarised below.

Liquidity Risk
The Group has funded its activities through cash generated from its operational activities, the proceeds of disposals, bank borrowings and the debt capital markets.

The Group's gross borrowings as at 31 March 2002 were £4,239 million (£3,677 million at 31 March 2001) and reflected operating cash outflows and financing transactions in the first half of the year, offset by debt reductions funded from disposal proceeds.

Marconi's net debt was £2,865 million at 31 March 2002, and decreased from £3,167 million at 31 March 2001.

At 31 March 2002, the Group's cash and liquid resources totalled £1,374 million, of which £278 million was denominated in sterling, £738 million in US dollars, £239 million in euro and the balance of £119 million in other currencies.

At 31 March 2001, Marconi had €7.0 billion of bank facilities, €4.5 billion maturing in March 2003 and €2.5 billion maturing in June 2002. In May 2001, the €2.5 billion facility was replaced by a new €3.0 billion facility, with the total facility outstanding rising to €7.5 billion.

Discussions were commenced in October 2001 with the Group's syndicate banks on replacing the existing facilities with a new facility, which would mature in June 2005. The intention of the Group was to secure the medium-term financing required beyond the current market downturn.

On 22 March 2002 Marconi announced that in the light of the Group's revised market outlook, it had decided not to proceed with the new bank facility it had been negotiating with its lending banks to refinance its two existing syndicated loan facilities. The Group further announced that as a result of this decision, it had agreed to cancel the undrawn commitments under these facilities and to place on demand the drawn portion of the €4.5 billion facility, which matures in March 2003. The Group now has a single facility with total commitment of €3.6 billion (£2.2 billion) and this was fully drawn as at 31 March 2002.

In recent weeks, Marconi has developed a revised business plan which has been presented to representatives of the Group's lending banks and bondholders. The plan, currently being reviewed by independent accountants, demonstrates a sustainable Core business which generates operating cash flow and returns to operating profit in the early stages of the 5-year plan period. In parallel, Marconi continues discussions with representatives of its lending banks and bondholders in order to reach an agreement, as rapidly as possible, on a financial restructuring proposal that is acceptable to all stakeholders. As part of this process, the Marconi Board has agreed that it will accept certain restrictions on financial and corporate activities while it continues its restructuring negotiations with the bank syndicate and bondholders. On 25 April 2002, the Group agreed that certain restrictions will apply to £850 million of its cash balances and liquid resources that will continue to be held with banks independent of the bank syndicate. Currently, these arrangements may be terminated at any time after 27 May 2002, with 5 business days' notice. In addition, the Group has agreed to increase the margin above LIBOR on its syndicated loan facility to 225 basis points per annum with effect from 1 April 2002. If the current levels of drawings were outstanding for the current financial year, the interest charge would increase by £46 million.

In December 2001, and January 2002, Marconi reduced the total bond debt outstanding through the repurchase by Ancrane Limited of sterling equivalent £375 million of principal of bonds at 53 per cent of face value, plus fees and accrued interest, funded from the Group's cash resources.

Interest Rate Risk
The Group's policy is to maintain at least 50 per cent of debt at fixed rates of interest. This may be varied in the context of a financial restructuring. At 31 March 2002, 53 per cent of the Group's interest-bearing borrowings were at fixed rates after taking account of interest rate swaps. Of this total, 43 per cent were at fixed dollar rates of interest and 10 per cent were at fixed euro rates of interest.

In the year ended 31 March 2002, the average interest rate received on cash and liquid investments was approximately 5.2 per cent per annum. The largest proportion of investments was in US dollar deposits – the

Group held an average of $413 million in US dollar deposits, earning an average interest rate of 1.9 per cent per annum. These US dollar deposits match in part the US dollar borrowings referred to below.

Due to the proportion of fixed rate debt, the Group's interest charge has limited exposure to interest rate movements. Consequently, an increase in market interest rates of one percentage point would have increased loss before taxation in the fiscal year 2002 by approximately £12 million.

Foreign Exchange Risk
The Group is exposed to movements in foreign exchange rates against sterling for both trading transactions and the translation of net assets and the profit and loss accounts of overseas subsidiaries. The main trading currencies of the Group are the US dollar, sterling and the euro.

The foreign currency management policy of the Group seeks to minimise the impact of fluctuations in exchange rates on future cash flows and requires subsidiaries to hedge firm transaction exposures against their local currency at the time the exposure is identified. These exposures are hedged by the use of spot and forward foreign exchange contracts.

The Group has overseas subsidiaries that earn profits or incur losses in their local currencies. It is not the Group's policy to hedge the exposures arising from the translation of these overseas results into sterling.

Gross borrowings at year end were £4,239 million, and 85 per cent of these were denominated in foreign currencies in order to form a hedge for the Group's investments in currencies other than sterling. Of these, 63 per cent denominated in US dollars formed a hedge for the Group's investment in the US, and 20 per cent denominated in euros formed a hedge for the Group's investments in the eurozone.

Marconi has subsidiaries in most of the European countries which have converted to the euro, and the major subsidiaries are located in Italy and Germany. The programme to ensure that all eurozone subsidiaries convert in a timely and efficient manner has now been brought to a successful conclusion.

Counterparty Risk
All deposits are made with creditworthy and authorised counterparties. All forward contracts, swaps and other derivative contracts, as described above, are similarly managed to ensure that the benefits of such financial hedging are subject to controlled counterparty risk.

As at 31 March 2002, the Group had vendor finance commitments of approximately £100 million ($142 million), of which £58 million ($82 million) had been drawn. In addition, Marconi has provided a $90 million counter-indemnity to Philips relating to the sale of Medical Systems. Approximately $42 million was paid out against this indemnity during the period to 31 March 2002. Management has no present intention of extending any significant further financing using the Group's own funds. Instead, through its in-house vendor finance specialists, it will continue to provide innovative and structured financing solutions for its customers through third party financing institutions.

In addition the Group uses export credit agencies to assist in managing political and credit risks on major contracts and makes extensive use of export credit insurance in respect of small to medium-sized contracts.

Contract Bonding Facilities
Some customers in the telecommunications market require that bank bonds or surety bonds (issued by insurance companies) are provided to guarantee performance of the supplier. Marconi had £500 million of bonds outstanding as at 31 March 2002 with both banks and insurance companies worldwide. Some of these facilities were covered by blanket indemnities and others required individual indemnities on a per bond basis. These facilities are normally provided on an uncommitted basis. All bonds currently have to be cash collateralised, under a bonding facility agreed with some of Marconi's relationship banks.

Insurance Risk Management
Marconi manages centrally the purchase of global insurance policies in respect of major insurable risks, including property (material damage/business interruption) and public and products liability. The use of global policies and centrally appointed brokers allows the Group to improve internal control and optimise the overall level of retained risk. Risk management and insurance spend are concentrated on those insurable risks which are considered potentially catastrophic to the Group as a whole. The Group continues to work with its insurers and advisers to improve its loss prevention and mitigation processes, with a particular emphasis on business continuity. Insurance market conditions are currently very challenging and premium rates have increased substantially. However, the Group benefits from good relationships with its major insurers and from some long-term deals.

Marconi Share Price Risk
Marconi has issued share options to employees under a number of different option plans. Options may be satisfied by a transfer of existing Marconi ordinary shares acquired on the market by the Marconi Employee Trust or other vehicle, or by an issue of new Marconi shares. It is intended to use existing shares to satisfy options under some of the plans. In order to hedge some of the potential cost of the acquiring existing shares, the Marconi Employee Trust has entered into contracts to purchase shares in the future at prices which were fixed at the date of contract. It has become apparent that, due to the reduction in the share price, it is unlikely that the options outstanding under the plans that were hedged by these equity hedging transactions, will be exercised.

Exchange rate sensitivity

10 per cent reduction in the value of:	Percentage reduction in Group reported sterling operating loss before goodwill amortisation and exceptional items
US dollar	(3.6)
Euro-traded currencies	(0.6)
Other	(0.4)
Total	(4.6)

The Directors have overall responsibility for Marconi's system of internal control and for reviewing its effectiveness. Any system of internal control can only manage and not eliminate the risk of failing to achieve business objectives and can only provide reasonable and not absolute assurance against material misstatement or loss.

For the period from 1 April 2001 until the date of the approval of the financial statements on 15 May 2002, the Group has applied the Marconi Business Risk Management Process. This continuing process is designed to identify, evaluate and manage the significant risks faced by the Group. The significant risks include strategic, operational, commercial and financial matters. As part of this process the Board, Audit Committee and key members of the executive management team have received and assessed reports and notifications of any identified weaknesses with the system of internal control.

Business Planning

Historically, the Group has operated a forecasting process that was based mainly upon data from market commentators and analysts. These plans assumed significant growth in the overall market place for telecommunications equipment and services. In this context, the Group had geared its operations and, in particular, its supply-chain capacity, towards an industry that it expected to continue to grow.

During the year, Marconi experienced a rapid and significant deterioration in its operating and financial environment, which the forecasting process failed to predict. Although the Group identified this change as a potential risk, the pace of the change, when it occurred, was far greater than any reasonable expectation at the time.

The Group has taken steps to improve its forecasting process but continues to operate in an environment characterised by significant short-term uncertainty. The Group's ability to forecast activity accurately within this environment is a continuing risk. To address this issue, its systems have been refocused to adapt to this environment by providing more regular information that highlights changes anticipated to occur in the short-term.

As a result of this decline in performance the Group carried out substantial organisational restructuring to adapt to its changed circumstances.

Corporate process controls

Corporate review and approval procedures have been put in place to cover major risk areas such as acquisitions and disposals, capital expenditure, contract tenders, research and development, litigation, industrial relations, treasury management, insurance, risk management, taxation, outsourcing and environmental issues.

The Group has also centralised the purchase of insurance in relation to major insurable risks in order to improve control and reduce overall cost. The specialist function assesses exposures and risk tolerance and selects the optimum means of mitigating losses.

Risk Management Process

The paragraphs below set forth the risk management measures employed for both periods up to and after 4 September 2001.

Period Prior to 4 September 2001

Historically, each Division (Networks, Services, Mobile, Systems and Capital) of the Group maintained a Business Audit Committee which met four times a year. These committees were responsible for facilitating the identification of key risks across all aspects of the division's activities, which would prevent the divisions and operating units from achieving their objectives. This involved an assessment of the impact and likelihood of these risks occurring and the development of a related mitigation strategy. These committees also worked with Marconi Internal Audit to develop a programme of assurance over relevant risks.

This process continued during the first quarter, ended 30 June 2001, when a revised organisational structure was introduced with three divisions (Networks, Enterprise, Wireless) supported by a number of global functions. Appropriate delegated authority levels and procedures were implemented within the revised structure, which gave major decision-making responsibility to the divisional chief executives, who were accountable for the conduct and performance of their divisions within the overall strategy.

The Executive Committee reviewed the risks being faced by the Group in April 2001. The Group's Operational Review that commenced in July 2001 superseded a further review of the detailed action plans initially scheduled to take place at that time.

The conclusions and actions arising from the Operational Review were announced on 4 September. These included a further change to the Group's organisational structure and a series of cost and debt reduction actions:

Organisation – the three former Divisions were replaced by a single integrated structure based around a functional structure. In addition a new senior management team was established.

Cost reduction actions – as a result of the rapid deterioration in the Group's operating environment, the Group implemented a series of cost reduction actions designed to align its cost base with current forecast sales.

This rationalisation of the Group is ongoing and management has taken and continues to take all necessary measures to maintain adequate internal controls over the operation of the business throughout this process.

Period from 4 September 2001

As a result of the organisational changes, the Group revised its Business Risk Management Process and refocused its priorities on key areas of immediate risk.

Under the new structure, responsibility for operational performance and control has been reassigned to the head of each function. The delegated authorities have also been reviewed and re-established at levels that are more appropriate for the expected scope and scale of the Group's activities.

A Business Risk Committee has been established as a sub-committee of the Board. The sub-committee has responsibility for reviewing the risk assessments of functional management and for identifying the key risks facing the Group. Minutes of its meetings are forwarded to the Board for its consideration. Key risks have been identified and a member of the Executive Committee nominated to identify and execute a strategy to mitigate each risk.

Where necessary, the Business Risk Committee will be supported by Functional Audit Committees specific to each function. These Functional Audit Committees will report to the Business Risk Committee.

Financial Reporting
Financial results are monitored and reported according to comprehensive systems and procedures. Actual results and cash flows are reviewed each month by the Executive Committee and reported to the Board. Given the continuing poor visibility of market demand, the monthly reviews of forecast and actual results are the key methods of evaluating performance. In addition, key performance indicators are used to help identify areas where additional focus is required as a result of the group's current situation.

Review of Internal Controls
The Audit Committee reports regularly the findings of its review of the effectiveness of the Group's systems of internal control for consideration by the Board. To review the effectiveness of internal control, the Audit Committee meets with management and the internal and external auditors to discuss and review:

- The key risks facing the Group and the progress being made to address them.
- The external and internal audit plans and related reports.
- Letters of assurance, which are received from the executive management responsible for the various specialist activities. These letters certify compliance with Group procedures covering areas such as delegation of authority, ethics and risk and controls amongst others.
- The operations of the Group treasury function, which works within appropriate limits approved by the Board.
- Insurance risks and the levels of protection purchased from the insurance market.

Where any significant weaknesses have been identified in the system of internal control as a result of any reviews, new procedures are put in place to strengthen them. This is a process of continuous improvement as new challenges arise in the Group's operating environment.

The Committee has considered the adequacy of internal controls both before and after the organisational changes of September 2001. The Directors confirm that the effectiveness of the system of internal control for the year ended 31 March 2002 and the period up to 15 May 2002 has been reviewed in line with the criteria set out by the Internal Control working party of the Institute of Chartered Accountants in England and Wales issued in September 1999 (the Turnbull committee report).

Statement of Directors' Responsibilities

The Directors are required by the Companies Act 1985 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 Group and of the profit or loss of the Group for the financial year.

The Directors consider that the financial statements have been prepared on a going concern basis (as discussed further in note 1 to the accounts), appropriate accounting policies have been used and applied consistently, reasonable and prudent judgements and estimates have been made and applicable accounting standards have been followed.

The Directors are responsible for ensuring that the Company keeps accounting records which disclose with reasonable accuracy the financial position of the Company and which enable them to ensure that the financial statements comply with the Companies Act 1985.

The Directors have a general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Company and the Group and to prevent and detect fraud and other irregularities.

To the members of Marconi plc
We have audited the financial statements of Marconi plc for the year ended 31 March 2002 which comprise the profit and loss account, the balance sheets, the cash flow statement, the reconciliation of net cash flow to movements in net monetary debt, the consolidated statement of total recognised gains and losses, the reconciliation of movements in equity shareholders' (deficit)/funds and the related notes 1 to 30. These financial statements have been prepared under the accounting policies set out therein.

Respective responsibilities of Directors and Auditors
As described in the Statement of Directors' Responsibilities, the Company's Directors are responsible for the preparation of the financial statements 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, auditing standards, and the Listing Rules of the Financial Services Authority.

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 or the Listing Rules regarding directors' remuneration and transactions with the Company and other members of the Group is not disclosed.

We review whether the corporate governance statement reflects the Company's compliance with the seven provisions of the Combined Code specified for our review by the Listing Rules and we report if it does not. We are not required to consider whether the Board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the Group's corporate governance procedures or its risk and control procedures.

We read the Directors' Report and the other information contained in the Annual Report for the above year as described in the contents section and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements.

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 circumstances of the Company and the Group, 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.

Going Concern – fundamental uncertainty
In forming our opinion, we have considered the adequacy of the disclosures made in note 1 of the accounts concerning the Group's current borrowing facilities and ongoing negotiations with its bankers and bondholders. As indicated in note 1, the going concern assumption is dependent on the Directors reaching a satisfactory resolution of the re-financing negotiations with the Group's bankers and bondholders. Should the Group's bankers and bondholders not continue to provide support until a re-financing of the Group is achieved, the going concern basis of preparation would no longer be applicable and adjustments to the Group profit and loss account and Group balance sheet would be required to record additional liabilities and write down assets to their recoverable amount. Furthermore, the contingent liabilities relating to the indebtedness and obligations guaranteed by Marconi plc described in note 28 (a) to the accounts would crystallise, resulting in additional liabilities in the Company balance sheet. It is not practicable to quantify these potential adjustments. In view of the significance of this fundamental uncertainty, we consider that it should be drawn to your attention. Our opinion is not qualified in this respect.

Opinion
In our opinion, the financial statements give a true and fair view of the state of affairs of the Company and the Group as at 31 March 2002 and of the loss of the Group for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

Deloitte & Touche

Deloitte & Touche
Chartered Accountants and Registered Auditors
Hill House
1 Little New Street
London EC4A 3TR

15 May 2002

Consolidated Profit and Loss Account

For the year ended 31 March

	Note	2002 £ million	2001 (restated) £ million
Turnover			
Continuing operations	5	**3,222**	4,892
Discontinued operations	5	**1,088**	1,761
Group	5	**4,310**	6,653
Share of joint ventures		**257**	289
	4	**4,567**	6,942
Operating (loss)/profit			
Group operating (loss)/profit			
Excluding goodwill amortisation and exceptional items		**(474)**	732
Goodwill amortisation		**(431)**	(671)
Operating exceptional items	6a	**(5,210)**	(32)
	5	**(6,115)**	29
Continuing operations		**(6,160)**	(114)
Discontinued operations		**45**	143
	5	**(6,115)**	29
Share of operating profit of joint ventures			
Excluding goodwill amortisation and exceptional items		**11**	22
Goodwill amortisation		**(2)**	(2)
Operating exceptional items	6a	**(6)**	–
		3	20
		(6,112)	49
Group and joint venture operating (loss)/profit before goodwill amortisation and exceptional items		**(463)**	754
Share of operating (loss)/profit of associates			
Excluding goodwill amortisation and exceptional items		**(1)**	8
Goodwill amortisation		**(7)**	–
Operating exceptional items		**(173)**	–
		(181)	8
Operating (loss)/profit	4	**(6,293)**	57
Non-operating exceptional items			
Gain on disposal of discontinued operations		**358**	–
Gain/(loss) on disposal of fixed assets and investments in continuing operations		**18**	(38)
Merger/demerger items		**291**	20
	6b	**667**	(18)
		(5,626)	39
Net interest payable			
Group		**(240)**	(151)
Share of joint ventures and associates		**2**	1
	7	**(238)**	(150)
Net finance income			
Group excluding exceptional items		**34**	41
Exceptional gain on repurchase of bonds	6b, 8	**166**	–
	8	**200**	41
(Loss)/profit on ordinary activities before taxation			
Excluding goodwill amortisation and exceptional items		**(668)**	653
Goodwill amortisation and exceptional items		**(4,996)**	(723)
	4	**(5,664)**	(70)
Tax credit/(charge) on loss on ordinary activities			
Excluding tax on goodwill amortisation and exceptional items		**21**	(195)
Tax on goodwill amortisation and exceptional items		**(231)**	(17)
	9	**(210)**	(212)
Loss on ordinary activities after taxation		**(5,874)**	(282)
Equity minority interests	10	**(1)**	(5)
Loss on ordinary activities attributable to the shareholders		**(5,875)**	(287)
Equity dividends	11	**–**	(148)
Retained loss for the financial year		**(5,875)**	(435)
Basic and diluted loss per share	12	**(210.6)p**	(10.4)p
(Loss)/earnings per share excluding goodwill amortisation and exceptional items	12	**(23.2)p**	15.1p

	Note	Group 2002 £ million	Group 2001 (restated) £ million	Company 2002 £ million	Company 2001 £ million
Fixed Assets					
Goodwill	14	**877**	5,395	**–**	–
Tangible assets	15	**522**	1,142	**–**	–
Investments:	16				
Joint ventures					
Share of gross assets		**71**	178		
Share of gross liabilities		**(11)**	(90)		
		60	88		
Associates		**137**	45		
Other investments		**53**	458		
Shares in Group companies				**602**	439
		250	591	**602**	439
		1,649	7,128	**602**	439
Current Assets					
Stocks and contracts in progress	17	**720**	1,721	**–**	–
Debtors	18	**1,297**	2,683	**275**	526
Investments	19	**59**	56	**–**	–
Cash at bank and in hand	19	**1,330**	454	**1**	141
		3,406	4,914	**276**	667
Creditors: amounts falling due within one year	20	**(4,068)**	(3,920)	**(207)**	(115)
Net current (liabilities)/assets		**(662)**	994	**69**	552
Total assets less current liabilities		**987**	8,122	**671**	991
Creditors: amounts falling due after more than one year	20	**(1,902)**	(2,574)	**–**	–
Provisions for liabilities and charges	22	**(505)**	(714)	**–**	–
Net (liabilities)/assets before retirement benefit surpluses and deficits		**(1,420)**	4,834	**671**	991
Retirement benefit scheme surpluses	27	**19**	240	**–**	–
Retirement benefit scheme deficits	27	**(145)**	(120)	**–**	–
Net (liabilities)/assets after retirement benefit surpluses and deficits		**(1,546)**	4,954	**671**	991
Capital and reserves					
Called up share capital		**140**	139	**140**	139
Shares to be issued	23	**45**	310	**45**	310
Share premium account	23	**500**	489	**500**	489
Capital reserve	23	**375**	375	**–**	–
Revaluation reserve	23	**–**	267	**–**	–
Profit and loss account	23	**(2,618)**	3,359	**(14)**	53
Equity shareholders' interests		**(1,558)**	4,939	**671**	991
Equity minority interests		**12**	15	**–**	–
		(1,546)	4,954	**671**	991

These accounts were approved by the Board of Directors on 15 May 2002.
Signed on behalf of the Board of Directors

D C Bonham
M W J Parton } Directors

Cash Flow Statement

For the year ended 31 March

	Note	2002 £ million	2001 £ million
Net cash inflow/(outflow) from operating activities before exceptional items	24a	**10**	(67)
Exceptional cash flows from operating activities	6c	**(368)**	(39)
Net cash outflow from operating activities after exceptional items – continuing operations		**(418)**	(269)
Net cash inflow from operating activities after exceptional items – discontinued operations		**60**	163
Net cash outflow from operating activities after exceptional items		**(358)**	(106)
Dividends from joint ventures and associates		**29**	68
Returns on investments and servicing of finance	24b	**(262)**	(134)
Tax paid	24c	**(13)**	(137)
Capital expenditure and financial investment	24d	**(196)**	(34)
Acquisitions and disposals	24e	**1,025**	(203)
Non-operating exceptional cash flows related to merger/demerger	6c	**–**	(56)
Equity dividends paid to shareholders		**(95)**	(146)
Cash inflow/(outflow) before use of liquid resources and financing		**130**	(748)
Net cash inflow from management of liquid resources	24f	**186**	166
Net cash inflow from financing			
Issues of ordinary shares		**7**	36
Other	24g	**972**	316
Increase/(decrease) in cash and net bank balances repayable on demand		**1,295**	(230)

Reconciliation of Net Cash Flow to Movements in Net Monetary Debt

For the year ended 31 March

	Note	2002 £ million	2001 £ million
Increase/(decrease) in cash and net bank balances repayable on demand		**1,295**	(230)
Net cash inflow from management of liquid resources		**(186)**	(166)
Net cash inflow from increase in debt and lease financing		**(972)**	(316)
Change in net monetary debt resulting from cash flows		**137**	(712)
Net debt acquired with subsidiaries		**(3)**	(23)
Other non-cash changes		**162**	(31)
Effect of foreign exchange rate changes		**6**	(256)
Movement in net monetary funds in the period		**302**	(1,022)
Net monetary debt at 1 April	25	**(3,167)**	(2,145)
Net monetary debt at 31 March	25	**(2,865)**	(3,167)

Consolidated Statement of Total Recognised Gains and Losses

For the year ended 31 March

	2002 £ million	2001 (restated) £ million
(Loss)/profit on ordinary activities attributable to the shareholders		
Group	(5,701)	(306)
Share of joint ventures	9	13
Share of associates	(183)	6
	(5,875)	(287)
Listed fixed asset investments		
Deficit due to movement in share price	(30)	(375)
Exchange rate adjustments	–	6
	(30)	(369)
Unrealised gain on exchange of businesses	9	–
Exchange differences on translation		
Group	(66)	240
Share of associates	–	3
	(66)	243
Actuarial loss recognised on retirement benefit schemes		
Difference between the expected and actual return on scheme assets	(277)	(186)
Changes in assumptions underlying the present value of the scheme liabilities – (losses)/gains	(83)	164
Experience gains and (losses) on scheme liabilities	9	(51)
	(351)	(73)
Tax credit on net retirement benefit items debited in the statement of total recognised gains and losses	68	38
Total recognised gains and losses related to the year	(6,245)	(448)
Prior period adjustment	317	
Total gains and losses recognised since the last annual report	(5,928)	

Reconciliation of Movements in Equity Shareholders' (Deficit)/Funds

For the year ended 31 March

	2002 £ million	2001 (restated) £ million
Total recognised gains and losses related to the year	(6,245)	(448)
Equity dividends	–	(148)
Release of provision in respect of shares to be issued	(260)	–
Shares to be issued	–	71
Issues of ordinary shares	8	491
Total movement in the year	(6,497)	(34)
Equity shareholders' interests at 1 April as previously reported	4,622	4,630
Prior period adjustment	317	343
Equity shareholders' interests at 1 April as restated	4,939	4,973
Equity shareholders' interests at 31 March	(1,558)	4,939

1 Fundamental uncertainty in respect of the application of the going concern basis

In the year to 31 March 2002, the Group met its day-to-day working capital requirements through syndicated banking facilities, certain bilateral bank facilities and its own cash resources. In addition, it has in issue bonds with a face value of £1.8 billion, issued in order to finance acquisitions that occurred in the year to 31 March 2000. As at 31 March 2002, net debt stood at £2.9 billion.

The Group's existing syndicated bank facility expires on 25 March 2003. From October 2001, the Group has been in negotiations with these banks to provide facilities that would extend beyond this date. However, on 22 March 2002, the Group announced that in the light of the Group's revised view of the extended market downturn, it no longer believed that the refinancing proposal provided the Group with an appropriate capital structure. Accordingly, the Group decided that it was unable to enter into the proposed new bank facility. The bank coordinators indicated that the banks reserve all their rights under the existing bank facilities. In order to preserve the support of its syndicate banks, the Group announced that as a result of this decision, it had agreed to cancel the undrawn commitments under its syndicated facilities and to place on demand the drawn portion of the €4.5 billion facilities. The final maturity of the €4.5 billion syndicated bank facility remains 25 March 2003.

The Group has developed a revised business plan and is in discussion with its banks and bondholders in order to secure a capital structure that is appropriate to that business plan.

The Company has guaranteed certain derivative transactions related to the exercise of share options previously granted to employees of the Group, the borrowings of its subsidiary, Marconi Corporation plc under the syndicated bank facilities and the bonds issued by Marconi Corporation plc. The aggregate amount of these guarantees is disclosed in note 28 (a). If the guarantees are called, the extent to which the Company ultimately bears the liabilities will depend on the extent to which the liabilities are satisfied by other Group companies. Given the current state of the negotiations with its bankers and bondholders, the Directors have assessed whether it is probable that these guarantees will become actual liabilities and decided that the guarantees are currently not likely to crystallise. Consequently, these guarantees are not recorded in the Company balance sheet, but are disclosed as a contingent liability.

In the light of the information currently available to them, the Directors believe that the Group's bankers and bondholders will support it in achieving an appropriate capital structure. On this basis, the Directors consider it appropriate to prepare the accounts on a going concern basis. Should the Group's bankers and bondholders not support the Group in achieving an appropriate capital structure, adjustments would be necessary to record additional liabilities and to write down assets to their recoverable amount. It is not practicable to quantify these possible adjustments.

2 Accounting policies

The financial statements have been prepared in accordance with applicable accounting standards.

The more important Marconi Group accounting policies are summarised below to facilitate the interpretation of the financial statements.

Accounting convention
The financial statements are prepared under the historical cost convention, as modified by the valuation of listed fixed asset investments.

Basis of consolidation
The financial statements consolidate the accounts of Marconi plc and all of its subsidiary undertakings (Group companies or subsidiaries).

All accounts for Group companies are made up to 31 March.

Turnover
Turnover, excluding VAT, comprises sales to outside customers, and the Group's percentage interest in sales of joint ventures. The Group records transactions as sales when the delivery of products or performance of services takes place in accordance with the terms of sale.

Currency translation
Profits and losses of overseas subsidiaries, joint ventures and associates and cash flows of overseas subsidiaries are translated at the average rates of exchange during the year. Non-sterling net assets are translated at year-end rates of exchange. Key rates used are as follows:

	Average rates		Year-end rates	
	2002	2001	**2002**	2001
US dollar	**1.43**	1.48	**1.42**	1.42
Italian lira	**3,152**	3,153	**3,161**	3,114
Euro	**1.63**	1.63	**1.63**	1.61