SPIRENT PLC
Form 20-F/A
March 31, 2005

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As filed with the Securities and Exchange Commission on March 31, 2005

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 20-F/A

AMENDMENT No. 1

o **REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) or (g) OF THE SECURITIES EXCHANGE ACT OF 1934**

or

ý **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended December 31, 2003

or

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from [______] to [______]

Commission file number: 001-15206

SPIRENT PLC

(Exact name of Registrant as specified in its charter)

England and Wales

(Jurisdiction of incorporation or organization)

Spirent House
Crawley Business Quarter
Fleming Way, Crawley
West Sussex RH10 9QL
United Kingdom

(Address of principal executive offices)

+44 (0)1293 767676

(Registrant's telephone number, including area code)

Securities registered or to be registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange
American Depositary Shares	**New York Stock Exchange**
Ordinary Shares*	**New York Stock Exchange***

* Listed, not for trading, but only in connection with the registration of American Depositary Shares, pursuant to the requirements of the Securities and Exchange Commission.

Securities registered or to be registered pursuant to Section 12(g) of the Act: None.

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act: None.

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the annual report: 944,031,413 Ordinary shares of $3^1/_3$p.

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days: Yes ý No o

Indicate by check mark which financial statement item the registrant has elected to follow:

Item 17 o Item 18 ý

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You should rely only on the information contained in this Amendment. We have not authorized anyone to provide you with information that is different. The information in this Amendment may only be accurate on the date of this Amendment.

EXPLANATORY NOTE

In accordance with Rule 12b-15 under the United States Securities Exchange Act of 1934 (the "Exchange Act"), Spirent plc (the "Company", "we", "us" or "our") hereby amends its Annual Report on Form 20-F for the fiscal year ended December 31, 2003 (this "Amendment") as filed with the United States Securities and Exchange Commission on June 29, 2004 (the "Original Filing") by restating its financial results and shareholders' equity presented under accounting principles generally accepted in the United States ("US GAAP"). The restatements reflect our re-evaluation of revenue recognition and deferral of revenue relating to multiple-element arrangements with customers in the Service Assurance division of our Communications group for the purposes of the reconciliations of our financial statements to US GAAP.

The Company's financial statements presented under accounting principles generally accepted in the United Kingdom ("UK GAAP") are not affected by these restatements.

The Company's Consolidated Financial Statements at December 31, 2003 and 2002 and for each of the three years in the period ended December 31, 2003 included in Item 18 have been restated and amended by:

- restating Note 34 Differences between United Kingdom and United States Generally Accepted Accounting Principles to the Company's consolidated financial statements, and

- the inclusion of an updated report of the Company's independent registered public accounting firm.

This Amendment also amends Item 3. "Key Information Selected Consolidated Financial Information of Spirent", Item 5. "Operating and Financial Review and Prospects Differences Between UK GAAP and US GAAP", Item 15. "Controls and Procedures", and Item 19. "Exhibits" to reflect the filing of new certifications by each of the Chief Executive Officer and the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, and the furnishing of a new certification of the Chief Executive Officer and the Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 as well as filing new consents by our independent registered public accounting firm and independent auditors.

Other than items expressly set forth above, this Amendment does not, and does not purport to, amend, update or restate any other information in the Original Filing or reflect any events that have occurred after the date of the Original Filing.

ITEM 3. KEY INFORMATION

Selected Consolidated Financial Information of Spirent

The selected consolidated profit and loss account data for each of the three years in the period ended December 31, 2003 and balance sheet data as of December 31, 2003 and 2002 set forth below are derived from our audited consolidated financial statements, which are included elsewhere in this amendment. The profit and loss account data for the years ended December 31, 2000 and 1999 and the balance sheet data as of December 31, 2001, 2000 and 1999 are derived from our audited consolidated financial statements. All of these financial statements have been audited by Ernst & Young LLP, our independent registered public accounting firm. The selected consolidated financial data set forth below should be read in conjunction with "Item 5. Operating and Financial Review and Prospects," and our consolidated financial statements and notes thereto included elsewhere in this amendment.

We prepare our consolidated financial statements in accordance with accounting principles generally accepted in the United Kingdom, or UK GAAP, which differ in certain respects from those generally accepted in the United States, or US GAAP. A description of the significant differences applicable to us and reconciliations of net income, shareholders' equity and cash flows are set forth in Note 34 of Notes to the Financial Statements.

We evaluate performance for each reportable segment based on turnover and operating profit before goodwill amortization and exceptional items. Operating profit and return on sales are used by the Group as key measures of operating performance and are stated before the effect of goodwill amortization and exceptional items so that period on period comparisons are not distorted. Free cash flow, meaning cash flow before acquisitions, disposals, equity dividends and financing, is also a key measure of operating performance used by the Group. Headline earnings per share is considered by the Group and our investors to be a key measure of overall earnings performance. The calculation is based on reported earnings adjusted for goodwill amortization and exceptional items including tax.

Consolidated Profit and Loss Account Data

	Year ended December 31				
	2003	Restated(1)(2) 2002	Restated(1)(2) 2001	Restated(2) 2000	Restated(2) 1999
	(£ millions, except per share and per ADS amounts)				
Amounts in accordance with UK GAAP					
Turnover	466.2	558.9	801.8	696.7	544.5
Operating profit/(loss)	18.8	(970.6)	(734.3)	110.0	81.4
Other Information					
Exceptional items					
Goodwill impairment		923.3	724.6		
Other	7.5	41.6	34.9	2.2	
Goodwill amortization	9.7	56.1	86.6	25.7	8.6
Operating profit before goodwill amortization and exceptional items	36.0	50.4	111.8	137.9	90.0
Income from interests in					
Joint ventures	2.7	7.4	9.6	13.3	9.5
Associates	2.1	1.0	1.3	2.7	2.3
Amortization of goodwill on associates		(0.2)	(0.1)		
Profit/(loss) on disposal and closure of operations	3.6	(48.4)	14.5	(18.1)	(6.7)
Profit on disposal of tangible fixed assets				3.2	
Profit/(loss) before interest	27.2	(1,010.8)	(709.0)	111.1	86.5
Net interest payable	(9.3)	(12.3)	(22.8)	(29.3)	(12.8)
Exceptional interest expense	(16.1)				
Other finance (expense)/income	(1.5)	(0.3)	0.4		
Profit/(loss) before taxation	0.3	(1,023.4)	(731.4)	81.8	73.7
Taxation	(0.6)	(26.9)	(32.4)	(30.6)	(30.2)
Minority interest equity and joint venture	(0.2)	(0.4)	(0.2)	(0.5)	
(Loss)/profit for the financial period	(0.5)	(1,050.7)	(764.0)	50.7	43.5
Basic (loss)/earnings per share (pence)	(0.05)	(113.90)	(83.49)	7.40	6.67
Headline earnings per share (pence)	2.31	3.36	7.70	12.61	9.18
Diluted (loss)/earnings per share (pence)	(0.05)	(113.90)	(83.49)	7.18	6.39
Dividend per share (pence)		1.35	4.35	4.35	4.13
Dividend per share (US cents)		2.10	6.36	6.33	6.38
Dividend per ADS (pence)		5.40	17.40	17.40	16.52
Dividend per ADS (US cents)		8.40	25.44	25.32	25.52
Turnover by segment					
Continuing operations					

	Year ended December 31				
Performance Analysis	148.7	184.0	241.4	280.0	111.5
Service Assurance	91.7	131.4	189.2	9.2	3.2
Communications	240.4	315.4	430.6	289.2	114.7
Network Products	174.4	164.7	170.4	181.4	158.1
Systems	51.4	78.8	124.0	135.4	149.6
	466.2	558.9	725.0	606.0	422.4
Discontinued operations			76.8	90.7	122.1
	466.2	558.9	801.8	696.7	544.5
Operating profit before goodwill amortization and exceptional items					
Continuing operations					
Performance Analysis	4.4	10.0	38.6	97.0	42.8
Service Assurance	9.4	20.8	44.8	1.6	0.2
Communications	13.8	30.8	83.4	98.6	43.0
Network Products	16.7	15.0	14.9	25.3	21.8
Systems	5.5	4.6	5.4	2.7	10.8
	36.0	50.4	103.7	126.6	75.6
Discontinued operations			8.1	11.3	14.4
	36.0	50.4	111.8	137.9	90.0

(1) Restated for the adoption of Financial Reporting Standard ("FRS") 17 "Retirement Benefits" and of Urgent Issues Task Force ("UITF") Abstract 38 "Accounting for ESOP Trusts".

(2) The results for the Communications group have been restated to reflect the transfer of our field test activities from the Performance Analysis to the Service Assurance division.

Amounts in accordance with US GAAP

	Year ended December 31				
	Restated(1) 2003	**Restated(1) 2002**	**Restated(1) 2001**	**2000**	**1999**
	(£ millions, except per share and per ADS amounts)				
Income/(loss) from continuing operations					
As previously reported		(774.3)	(816.0)	(41.8)	(7.5)
Restatement	5.7	(3.6)	(55.5)		
As restated	5.7	(777.9)	(871.5)	(41.8)	(7.5)
Income/loss from discontinued operations			42.3	2.2	9.7
Net income/(loss) as restated	5.7	(777.9)	(829.2)	(39.6)	2.2
Net income/(loss) per share					
Basic (pence):					
Continuing operations					
As previously reported		(83.93)	(89.17)	(6.10)	(1.15)
Restatement	0.61	(0.40)	(6.06)		
As restated	0.61	(84.33)	(95.23)	(6.10)	(1.15)
Discontinued operations			4.62	0.32	1.49
Net income/(loss)	0.61	(84.33)	(90.61)	(5.78)	0.34
Diluted (pence):					
Continuing operations					
As previously reported		(83.93)	(89.17)	(6.10)	(1.11)
Restatement	0.60	(0.40)	(6.06)		
As restated	0.60	(84.33)	(95.23)	(6.10)	(1.11)
Discontinued operations			4.62	0.32	1.44
Net income/(loss)	0.60	(84.33)	(90.61)	(5.78)	0.33
Dividend per share (pence)		4.35	4.35	4.24	3.91
Dividend per share (US cents)		6.49	6.33	6.29	6.22
Net income/(loss) per American Depositary Share ("ADS")					
Basic (pence):					
Continuing operations					
As previously reported		(335.72)	(356.68)	(24.40)	(4.60)
Restatement	2.44	(1.60)	(24.24)		
As restated	2.44	(337.32)	(380.92)	(24.40)	(4.60)
Discontinued operations			18.48	1.28	5.96
Net income/(loss)	2.44	(337.32)	(362.44)	(23.12)	1.36

	Year ended December 31				
Diluted (pence):					
Continuing operations					
As previously reported		(335.72)	(356.68)	(24.40)	(4.44)
Restatement	2.40	(1.60)	(24.24)		
As restated	2.40	(337.32)	(380.92)	(24.40)	(4.44)
Discontinued operations			18.48	1.28	5.76
Net income/(loss)	2.40	(337.32)	(362.44)	(23.12)	1.32
Dividend per ADS (pence)		17.40	17.40	16.96	15.64
Dividend per ADS (US cents)		25.96	25.32	25.16	24.88

(1) Restated for revenue recognition, see Note 34 of Notes to the Financial Statements.

Consolidated Cash Flow Data

	Year ended December 31				
	2003	2002	2001	2000	1999
	(£ millions)				
Amount in accordance with UK GAAP					
Net cash inflow from operating activities	68.2	76.9	141.2	125.7	101.7
Acquisitions and disposals	60.4	6.4	149.6	(536.6)	(232.9)
Financing	(143.6)	53.8	(152.8)	480.2	284.2
Amounts in accordance with US GAAP					
Cash inflow from operating activities	54.1	60.7	96.4	83.9	72.9
Cash inflow/(outflow) on investing activities	44.6	(17.9)	91.9	(596.1)	(272.7)
Cash (outflow)/inflow from financing activities	(143.6)	13.8	(192.6)	452.5	258.7

Consolidated Balance Sheet Data

	At December 31				
	2003	Restated(1) 2002	Restated(1) 2001	Restated(1) 2000	Restated(1) 1999
	(£ millions)				
Amounts in accordance with UK GAAP					
Intangible assets	101.6	113.6	987.7	1,816.8	321.3
Tangible fixed assets	90.2	110.0	137.6	136.2	107.0
Current assets	179.5	242.4	263.0	375.5	270.5
Total assets	386.2	529.4	1,450.9	2,382.1	745.6
Current liabilities	113.1	109.3	178.0	219.4	269.6
Creditors due after more than one year	95.6	248.3	205.6	355.6	233.4
Total liabilities (including pension liability)	264.1	432.2	400.7	577.1	503.7
Shareholders' funds	119.9	95.1	1,047.8	1,801.3	238.0
Share capital	31.5	31.3	31.1	30.9	20.8
	Restated(2)	Restated(2)	Restated(2)	Restated(2)	
Amounts in accordance with US GAAP					
Intangible assets	79.0	94.4	907.8	1,841.4	430.0
Tangible fixed assets	90.2	110.0	137.6	136.2	107.0
Current assets	220.1	283.1	314.1	408.7	275.8
Total assets	431.7	579.5	1,450.4	2,458.3	874.8
Current liabilities	186.1	179.1	234.2	246.9	213.4
Creditors due after more than one year	135.2	298.1	252.4	380.8	266.9
Total liabilities	388.4	566.9	538.1	669.3	480.3
Shareholders' funds	41.1	10.5	909.9	1,785.3	390.6
Share capital	31.5	31.3	31.1	30.9	20.8

(1) Restated for the adoption of FRS 17 for 2002 and 2001 and of UITF 38.

(2) Restated for revenue recognition, see note 34 of Notes to the Financial Statements.

Exchange Rate Information

We present our financial statements in pounds sterling. The financial statements of the WAGO joint venture are presented in euro. The information set forth below with respect to pounds sterling to US dollar exchange rates is based on the noon buying rate for pounds sterling in The City of New York for cable transfers in pounds sterling as certified for customs purposes by the Federal Reserve Bank of New York. Also set forth below is exchange rate information pertaining to the euro, being the closing middle market price against pounds sterling. These rates are provided solely for the convenience of the reader and are not the exchange rates used by us in the preparation of our consolidated financial statements included in this annual report.

US Dollar

The noon buying rate on June 2, 2004 was $1.84 = £1.00. The following table sets forth the high and low rate for each month of the previous six months.

	High	Low
	(US dollars per pound sterling)	
May 2004	1.84	1.75
April 2004	1.86	1.77
March 2004	1.87	1.79
February 2004	1.90	1.82
January 2004	1.85	1.79
December 2003	1.78	1.72

The following table sets forth information about the noon buying rate for the last five years. The average rates for each year are calculated by using the rate on the last business day of each month during the relevant year.

Year ended December 31	High	Low	Average	End of year
	(US dollars per pound sterling)			
2003	1.78	1.55	1.64	1.78
2002	1.61	1.41	1.51	1.61
2001	1.50	1.37	1.44	1.45
2000	1.65	1.40	1.51	1.50
1999	1.68	1.55	1.61	1.62

Fluctuations in the exchange rate between pounds sterling and US dollars affect the US dollar equivalent of the pound sterling denominated prices of our shares and, as a result, affect the market price of our ADSs in the United States.

Euro

The euro rate on June 2, 2004 was €1.50 = £1.00. The following table sets forth the high and low rate for each month of the previous six months.

	High	Low
	(euro per pound sterling)	
May 2004	1.50	1.47
April 2004	1.52	1.48
March 2004	1.51	1.47
February 2004	1.50	1.46
January 2004	1.46	1.42
December 2003	1.44	1.41

The following table sets forth information about the euro rate for the last five years. The average rates for each year are calculated by using the rate on the last business day of each month during the relevant year.

Year ended December 31	High	Low	Average	End of year
		(euro per pound sterling)		
2003	1.54	1.38	1.45	1.42
2002	1.64	1.53	1.59	1.53
2001	1.67	1.56	1.61	1.64
2000	1.74	1.56	1.64	1.60
1999	1.61	1.40	1.52	1.60

Risk Factors

You should carefully consider the risks and uncertainties described below and the other information in this Amendment, including the discussions set forth in "Item 4. Information on the Company" and "Item 5. Operating and Financial Review and Prospects" as well as our consolidated financial statements and related notes included elsewhere in this annual report.

Risks Related to Our Business

Our business, operating results and financial condition could be harmed if the economy, and particularly the telecommunications industry into which we sell our products, fails to recover or recovers at a slower pace than anticipated.

Generally weak prevailing market conditions worldwide during 2001, 2002 and continuing through 2003 resulted in worldwide reduced purchasing and capital spending in many of the industries and markets into which we sell our products, in particular the telecommunications industry. As a result we experienced diminished product demand. The decline in demand for our products and services has had and may continue to have an adverse effect on the results of operations and we continue to be affected by challenging conditions in the global telecommunications market. Another downturn in our customers' markets or in general market conditions would be likely to result in a further reduction in demand for our products and services and could further harm our business, operating results and financial condition.

We operate in rapidly changing industries and if we do not keep up with these rapid changes, and continue significant investment in research and development, our turnover and operating results will suffer.

We sell our products and systems in several industries that are characterized by rapid technological changes, frequent product and service introductions and evolving industry standards. We anticipate that our current products and services will become technologically obsolete over time and technological developments may eliminate whole markets or the need for individual products. Entire product lines may be threatened by new technologies or market trends which may reduce the value of these product lines. If we fail to keep up with changes in these industries, our turnover and operating results will suffer.

We believe that the continued success of our communications business is dependent on our ability to advance next-generation technologies and services, to deliver integrated, easy-to-use, end-to-end customer solutions, to increase our presence internationally and to extend our products into web services and applications for the enterprise sector. For instance, our Service Assurance division is extending its existing capabilities in the next-generation IP services sector, which we believe represents an important growth opportunity. If we do not succeed in anticipating changes in technology and customer requirements and in developing and introducing new products, our business, operating results and financial condition will suffer.

The loss of key managers and skilled employees may result in inefficiencies in managing and operating our business and our business will suffer if we are not able to hire and retain appropriately qualified personnel.

Our success is dependent on attracting and retaining highly qualified and skilled employees. We face intense competition for personnel from other companies, establishments and organizations and the loss of our key employees, or our failure to attract and retain other highly skilled employees, may impair our ability to run and expand our business effectively.

In order for us to continue to expand and develop new technologies and products we will need to attract and retain employees with the necessary skills base and to ensure that our incentive plans are competitive.

We face aggressive competition and if we fail to compete effectively our business, operating results and financial condition will suffer.

We face aggressive competition in all of our businesses. Our competitors are numerous, including highly specialized firms as well as in-house capability within customers, and new competitors may emerge. Some of our competitors have greater name recognition, larger customer bases, and greater financial, marketing, sales and other resources. To stay competitive we will need to introduce successful new products and also may have to adjust prices of some of our products and manage financial returns effectively. Our business, operating results and financial condition will suffer if we do not compete effectively.

Fluctuations in exchange rates and heavy exposure to a weak US dollar could materially harm our operating results.

Since we conduct operations globally, a substantial portion of our assets, liabilities, revenues and expenses are denominated in various currencies, principally the US dollar and pounds sterling. Because our financial statements are denominated in pounds sterling, fluctuations in exchange rates, especially if the US dollar continues to weaken against the pound, could have a material impact on our reported results. In recent periods, the value of the US dollar has declined significantly in comparison with the pound sterling.

We may at times engage in currency hedging in an effort to cover any transaction exposure. Under such circumstances, this currency hedging could have an adverse effect on our financial condition.

The terms of our debt obligations may affect our ability to operate our business.

During 2003 we renegotiated our borrowing terms. The renegotiated terms increased our weighted average interest payments and placed restrictions and tests on us, constraining our ability to make dividend payments, incur further debt, provide further security and make acquisitions and disposals. Such restrictions and tests will continue to apply until certain financial requirements are met. We are unable to give guidance as to when we are likely to meet these financial requirements and can give no assurance that they will indeed be achieved and, therefore, whether or when our operations will be freed from such restrictions and tests.

The risk of a breach of financial covenants remains.

The borrowing terms we renegotiated in 2003 provided us with more headroom under certain of our financial covenants (see "Liquidity and Capital Resources" in Item 5 and "Material Contracts" in Item 10 below for a more detailed discussion of the renegotiated borrowing terms). However, we can provide you with no assurance that the covenants will not be breached and that further renegotiation of our borrowing terms will not be needed to further increase our level of headroom if there is another downturn in our business due to industry conditions or otherwise.

We rely on a limited number of customers in some of our businesses, and therefore any cancellation, reduction or delay in orders from them could significantly harm our business, operating results and financial condition.

In some of our businesses we continue to rely on a limited number of customers, which makes our relationships with these customers critical to the success of our business. We can provide you with no assurance that we will be able to retain this client base, that we will be able to increase our sales to our other existing customers or that we will be able to attract additional customers. The loss of one or more of our largest customers, any reduction or delay in sales to these customers, or inability to successfully develop and maintain relationships with existing and new customers could significantly harm our business, operating results and financial condition.

Because of our significant international operations, we are exposed to a variety of risks, many of which are beyond our control, that could adversely affect our business.

Our international operations are subject to a variety of potential risks arising out of the global economy, the political outlook, currency fluctuations, exchange control restrictions, investment in capital, the ability to enforce intellectual property rights, language and certain cultural differences in countries where we have operations.

Events such as the continued military involvement in Iraq, the tensions in the Middle East, the threat of terrorism and associated political instability and the effect of heightened security concerns on travel and commerce may trigger unforeseen economic conditions and cause market demand to fluctuate in an unpredictable manner which could adversely affect our business, operating results and financial condition.

The retirement of our Chief Executive Officer may disrupt the effective management of our business and create uncertainty among our employees.

On February 25, 2004 our Chief Executive Officer, Nicholas Brookes, informed us of his intention to retire as Chief Executive Officer of the Company. His retirement is due to become effective at the end of June 2004 at which time he will step down from the Board. A formal process to find a successor is under way. Any delay in our securing the services of a successor Chief Executive Officer may result in difficulties in the effective management of our business.

Our pension fund deficit may become a further burden on our financial resources.

The latest actuarial valuation of our UK defined benefit scheme as at April 1, 2003 identified a deficit of £50.7 million before taxation representing a funding deficit of 39%. In order to comply with minimum funding requirements we will make annual pension contributions of £3.5 million commencing on July 1, 2004 and have increased the rate of our employer pension contribution from 13.4% to 16% of pay with effect from January 1, 2004. While these increased contributions are intended to reduce the funding deficit over time, it is possible that a future actuarial valuation will reveal that the increased contributions are insufficient to do so and will need to be increased. The UK defined benefit scheme is required to have an actuarial valuation every three years. These additional funding costs, both the current increased contributions and any further increases required by future actuarial valuations, may have an adverse effect on the financial condition of our business.

Acquisitions undertaken could be difficult to integrate, disrupt our business and harm our operating results.

Acquisitions have historically been an important part of our business strategy and we evaluate strategic opportunities from time to time and may acquire businesses, products or technologies in the future. Acquisitions are inherently risky and no assurance can be given that our previous or future acquisitions will be successful or will not adversely affect our business, operating results or financial condition. Currently our renegotiated borrowing terms restrict our ability to make acquisitions.

Third parties may claim we are infringing their intellectual property rights and as a result our business may be harmed.

Third parties may claim that we are infringing their intellectual property rights. While we do not believe that any of our products infringe the valid intellectual property rights of third parties, we may be unaware of intellectual property rights of others that may cover some of our technology, products and services. We could suffer litigation or licensing expenses, or could be prevented from selling certain products as a result of third-party infringement claims. The complexity of the technology involved and the uncertainty of intellectual property litigation increase these risks. Claims of intellectual property infringement might also require us to enter into costly royalty or license agreements. Indeed, we may not be able to obtain royalty or license agreements on terms acceptable to us, or at all. We may also be subject to significant damages or injunctions against development and sale of certain of our products. We often rely on obtaining licenses of intellectual property. We cannot assure you that these licenses will be available in the future on favorable terms or at all.

If third parties infringe our intellectual property rights, our business may be harmed.

Our success depends in part on our proprietary technology. If we fail to maintain or enforce our intellectual property rights, or if competitors design around our technology or develop competing technologies, our competitive position could suffer and our operating results may be harmed. We may not be able to detect infringement and our competitive position may be harmed before we do so. Intellectual property rights may also be unavailable or limited in some foreign countries, which could make it easier for competitors to capture market share.

If our products are defective, we may be held responsible for liabilities caused by malfunctions of equipment in which our products are used or have to bear some of the cost of recalling this equipment, which would harm our turnover and our reputation.

Some of our products are incorporated as component parts by manufacturers into sophisticated equipment and machinery or are used in critical applications or are stand-alone solutions. If our products are defective, we may be held responsible for the personal, property and financial damages that result and the costs associated with recalling the products themselves and products in which our defective products were incorporated. Although we carry product liability insurance customary for companies of our size, such available insurance cover may not be sufficient to cover a catastrophic loss or the costs of recall. In addition, our reputation with customers may be damaged as a result of any such event. Product liabilities or the costs of implementing a recall could hurt our profitability, and the damage to our reputation if one or more of our products proves defective could cause us to lose customers.

Many of our businesses are dependent on third-party manufacturers. If we cannot obtain sufficient services or products from these manufacturers, we may lose customers and suffer a reduction in turnover and profits.

Many of our businesses contract out certain manufacturing processes. If there were a failure of such a manufacturer because of, for example, insolvency or catastrophic loss, the services or products to our operations might be disrupted or even terminated. It might not be possible to find an alternative manufacturer in an acceptable timeframe on the same economic terms as the original manufacturer. If we cannot obtain sufficient quantities of these products or services at an acceptable cost, we may not be able to meet customer demands in the desired timeframe at a commercially acceptable cost, which may result in the loss of customers and a reduction in turnover and profits.

Some of our businesses are dependent on key component suppliers. If we cannot obtain sufficient components from these suppliers, we may lose customers and suffer a reduction in turnover and profits.

Some of our businesses, particularly in the Communications group, may be dependent on some components from suppliers who experience greater demand for their products than they can meet. In some instances these suppliers have introduced allocation systems to divide their available stock among potential customers. We may be affected because the allocation to our business is too small or because suppliers change the way they apportion their available stock to our disadvantage. If we cannot obtain sufficient quantities of these products at an acceptable cost, we may not be able to meet customer demands in the desired timeframe at a commercially acceptable cost, which may result in the loss of customers and a reduction in turnover and profits.

Prices for some of the commodity raw materials we use to manufacture our products fluctuate, and we may not be able to pass on increased costs of these raw materials to our customers.

Prices fluctuate for some of the commodity raw materials our Network Products group uses to manufacture its products. If prices for commodities such as PVC and Nylon 66 increase significantly and we are not able to pass on the increased prices to our customers, our profitability will be reduced and our business, operating results and financial condition may be adversely affected.

Remaining liabilities from discontinued businesses could adversely affect our results.

We have concluded a number of divestments of our non-core businesses, but we may, despite divesting of these non-core businesses, have contingent liabilities arising out of those businesses that could adversely affect our business, operating results and financial condition. In addition, the time periods for bringing claims in relation to representations, warranties and indemnities that we have given on recent divestments have not yet expired.

A significant portion of our telecommunications operations are located in California where they may be subject to the risks of earthquakes and other natural disasters.

A significant portion of our telecommunications operations are located in California which has experienced natural disasters, including earthquakes, in the past. A significant natural disaster, such as an earthquake, could disrupt our ability to conduct our telecommunications business and could have a material adverse impact on the Group's business, operating results and financial condition.

Events described by our forward-looking statements may not occur.

This annual report includes forward-looking statements concerning our business, operations and financial performance and condition. We have based these forward-looking statements on our current expectations and projections about future events. These forward-looking statements are subject to risks, uncertainties, and assumptions about us, including, among other things, those discussed above as well as under "Item 5. Operating and Financial Review and Prospects." You can identify these statements by words such as "anticipate", "assume", "believe", "estimate", "expect", "intend", "may", "plan", "positioned", "should", "will", "would" and other similar expressions which are predictions of or indicate future trends and future events. In light of these risks, uncertainties and assumptions, the forward-looking events discussed in this annual report might not occur. We undertake no obligation to update publicly or revise any forward-looking statements, whether as a result of new information, future events or otherwise. Given these considerations, readers are cautioned not to place undue reliance on such forward-looking statements.

Risks Relating to an Investment in our Ordinary Shares and ADSs

The price of our Ordinary shares and ADSs may be volatile and may decrease significantly below your purchase price.

The market price of our Ordinary shares is significantly affected by market forces. The market prices of securities of technology companies on the London Stock Exchange, the New York Stock Exchange and other exchanges have fluctuated significantly in the last three years. The prices for securities of companies involved in telecommunications and other technologies, have been particularly volatile. A significant portion of our activities is based on telecommunications and thus the market price of our Ordinary shares and ADSs is likely to remain highly volatile.

In addition to general factors, the following specific factors may have a significant effect on the market price of our Ordinary shares and ADSs:

- speculation on the risks associated with the telecommunications industry;

fluctuations in our operating results and speculation on the robustness of our financial condition;

announcements regarding awards of major contracts;

announcements of technological innovations by us or our competitors; and

speculation regarding acquisitions and divestments.

As a result, you may only be able to resell our Ordinary shares or ADSs at a price significantly below your purchase price. See "Item 9. The Offer and Listing" for historical pricing data on our shares.

Fluctuations in the exchange rate between the pound sterling and the US dollar may affect the price at which our ADSs trade on United States securities markets.

For any particular price in pounds sterling at which our shares are trading on the London Stock Exchange, fluctuations in the exchange rate between the pound sterling and the US dollar may affect the price in US dollars at which our ADSs trade on the New York Stock Exchange. For example, a fall in the value of the pound sterling against the US dollar is likely to reduce the price of our ADSs in the United States market.

The availability of sufficient purchasers and sellers for our shares, whether in the form of Ordinary shares or ADSs, cannot be guaranteed and therefore you may not be able to purchase or sell our shares or ADSs at any particular time.

The volume of our stock traded on the London Stock Exchange can vary from day to day and is affected by events and circumstances out of our control. This also applies to the ADSs traded on the New York Stock Exchange. You may not be able to purchase or sell our Ordinary shares or ADSs at any particular time because of the lack of sufficient purchasers or sellers.

Your ability to bring an action and enforce judgments against us may be limited under English law.

We are a public limited company incorporated under the laws of England and Wales. The rights of holders of Ordinary shares and, therefore, many of the rights of ADS holders, are governed by English law and by our Memorandum and Articles of Association. These rights differ from the rights of shareholders in typical United States corporations. In particular, English law significantly limits the circumstances under which shareholders of English companies may bring actions on the company's behalf. Under English law generally, only we can bring a claim in proceedings in respect of wrongful acts committed against us. In addition, it may be difficult for you to prevail in a claim against us under, or to enforce liabilities relying upon, United States securities laws. See "Item 4. Information on the Company Enforcement of Civil Liabilities".

ITEM 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS

The following discussion and analysis relates to our financial condition as of December 31, 2003 and the results of operations for the years ended December 31, 2003, 2002 and 2001. This discussion should be read in conjunction with our Selected Consolidated Financial Information and our Audited Consolidated Financial Statements included elsewhere in this Amendment. You should also read the description of our business included in "Item 4. Information on the Company."

The following discussion and analysis by segment is based on the Consolidated Financial Statements of Spirent plc and its subsidiaries, together with its share of profits of its joint ventures and associates, which we refer to as the Group. These Consolidated Financial Statements are prepared in accordance with UK GAAP. A summary of the main differences between UK GAAP and US GAAP as they relate to us is set out in Note 34 of Notes to the Financial Statements.

We evaluate performance for each reportable segment based on turnover and operating profit before goodwill amortization and exceptional items. Operating profit and return on sales are used by the Group as key measures of operating performance and are stated before the effect of goodwill amortization and exceptional items so that period on period comparisons are not distorted. Free cash flow, meaning cash flow before acquisitions, disposals, equity dividends and financing, is also a key measure of operating performance used by the Group. Headline earnings per share is considered by the Group and our investors to be a key measure of overall earnings performance. The calculation is based on reported earnings adjusted for goodwill amortization and exceptional items including tax.

Unless otherwise stated, operating profit and return on sales are stated before goodwill amortization and exceptional items.

We have implemented Financial Reporting Standard ("FRS") 17 "Retirement Benefits" at December 31, 2003 to bring us in line with latest UK GAAP and to move towards the adoption of International Financial Reporting Standards in 2005. Prior year amounts have been restated to reflect the change in accounting policy.

The Group has also implemented Urgent Issues Task Force ("UITF") Abstract 38 "Accounting for ESOP Trusts" which requires that the cost of own shares, previously reported as a fixed asset investment, be shown as a deduction from shareholders' funds. A prior year adjustment has been made to reflect this change.

Overview

Spirent is a leading communications technology company focused on delivering innovative systems and services to meet the needs of customers worldwide. Our Communications group is a global provider of performance analysis and service assurance solutions that enable the development and deployment of next-generation networking technologies such as broadband services, Internet telephony, 3G wireless and web applications and security testing. Our Network Products business is a developer and manufacturer of innovative solutions for fastening, identification, protection and connectivity in electrical and communications networks marketed under the global brand HellermannTyton. The Systems group comprises PG Drives Technology, which develops power control systems for specialist electrical vehicles in the mobility and industrial markets, and an aerospace business that provides ground-based logistics support software systems for the aviation market.

Our results for the year were affected by the challenging conditions in the global telecommunications market and the generally weak market conditions worldwide with turnover of £466.2 million and operating profit of £36.0 million down 17% and 29%, respectively, compared with 2002. However, our performance in the second half of 2003 saw an increase in both turnover and operating profit over the first half reflecting a modest increase in activity levels.

We have maintained our commitment to product development, investing £66.0 million or 14% of turnover in 2003 (2002 £77.7 million and 14%).

Due to a strong focus on cash management we generated £68.2 million of operating cash in 2003. Net debt has been significantly reduced to £57.5 million at the year end compared with £161.8 million at the end of 2002 principally through cash generated by the businesses and the proceeds from the sale of the WAGO joint venture.

Acquisitions and Disposals

Acquisitions

Acquisitions and disposals are discussed in "Item 4. Information on the Company" and in Notes 32 and 33 of Notes to the Financial Statements.

We did not make any acquisitions in 2003. In August 2002 we completed the acquisition of Caw Networks, Inc. ("Caw") for an initial cash consideration of $49 million with a provision for deferred consideration of up to $60 million dependent on certain technical and financial milestones being met. Caw has achieved a certain level of the earn-out targets. The Company has satisfied the deferred consideration due through the issue of 4.4 million new Spirent shares in 2004 and provided for a liability of £2.7 million in respect of this at December 31, 2003.

Disposals

On April 4, 2003 we completed the divestment of our 51% interests in WAGO, our interconnection joint venture, to the joint venture partners (the Hohorst family) for a cash consideration, net of expenses, of £58.8 million.

On June 30, 2003 we completed the divestment of our AIS businesses from within the Systems group's aerospace activities for a net cash consideration of £3.2 million.

Recent Developments

On February 25, 2004 it was announced that Nicholas Brookes had informed the Board of his intention to retire as Chief Executive of the Company on June 30, 2004. A formal process to find a successor is under way.

At December 31, 2003 no amounts were drawn under our committed bank facility of £60 million and we held £37.6 million of cash. We determined that this £60 million bank facility was in excess of our business requirements. Consequently, at the end of 2003 we entered into negotiations with a small group of lending banks and agreed a £30 million, 364-day working capital facility with a six-month term-out option which became effective on February 18, 2004 to replace the £60 million facility. We have applied some of our excess cash, including the net proceeds from the disposal of AIS, to make a partial prepayment on our senior notes ("notes") to reduce the cost of borrowing going forward. The partial prepayment of $14.4 million (£8.1 million) was made on February 18, 2004 and an associated make-whole amount of $3.3 million (£1.8 million) has been incurred. This make-whole amount and the costs associated with this transaction were accrued in the 2003 financial year.

At the Annual General Meeting of shareholders held on May 11, 2004, we stated that "Spirent's overall trading performance in the first quarter of 2004 was in line with expectations after allowing for the impact of the continuing weakness of the US dollar to sterling exchange rate. On an organic, constant currency basis Group turnover was up 9% compared with the first quarter of last year.

"In the Communications group we have started to see some more encouraging trends in spending by our customers. The Performance Analysis division has benefited from our broad portfolio of products, particularly in next-generation broadband and wireless technologies, with quarterly order intake up appreciably over the same period last year. We have also seen some signs of a return of confidence among network service providers but as previously stated we expect the Service Assurance division's performance to lag a recovery. We continue to extend our existing capabilities in IP services and expand our product offering internationally.

"Our Network Products group delivered a good performance in the first quarter benefiting from the introduction of new products and applications in its principal markets. As anticipated our Systems group's exports in the first quarter of 2004 have been impacted by the weakness of the US dollar.

"The satisfactory start to 2004 we reported in our 2003 preliminary results announcement in February has continued into April. While we have seen indications of a pick up in spending by our customers, we continue to be cautious as to the extent of this recovery."

Results of Operations

Turnover for 2003 of £466.2 million was 17% lower than 2002. Turnover for ongoing businesses of £237.0 million for the second half of 2003 improved by 6% over the first half reflecting modestly improved levels of activity in the latter part of the year.

Operating profit before goodwill amortization and exceptional items was £36.0 million for the year, down 29% on 2002. Operating profit for ongoing businesses for the second half of 2003 improved by 31% over the first half reflecting the modest increase in activity and the effect of cost savings.

Return on sales for the year was lower at 7.7%, 1.3 percentage points below 2002. Return on sales in the second half of 2003 showed an improvement over the first half of 2.0 percentage points.

The Communications group contributed £240.4 million of turnover (2002 £315.4 million) and £13.8 million of operating profit (2002 £30.8 million), representing 52% (2002 56%) of Group turnover and 38% (2002 61%) of Group operating profit.

As anticipated, the telecommunications market remained challenging throughout 2003. 2003 saw further reductions in capital spending of approximately 20% by our NEM and NSP customers. Spirent Communications' turnover was down 24% compared with 2002, but turnover for the second half of 2003 was up 5% compared with the first half due to modestly improved levels of activity. Compared with 2002, operating profit for 2003 was down 55%, however operating profit in the second half of 2003 improved by 71% over the first half. Return on sales for the Communications group for 2003 reduced to 5.7% from 9.8% in 2002.

Our Network Products and Systems groups delivered improved performances over the prior year. Network Products reported growth in turnover of 6% and in operating profit of 11% compared with 2002. The Systems group reported growth of 8% in turnover and 32% in operating profit excluding the effect of divestments. These businesses supply a broad range of industries and therefore have provided some protection from the volatile conditions in the telecommunications market. The Network Products group contributed turnover of £174.4 million (2002 £164.7 million), representing 37% (2002 30%) of the Group's turnover and £16.7 million (2002 £15.0 million) of operating profit being 47% (2002 30%) of the Group's operating profit. The Systems group, including divestments, contributed £51.4 million (2002 £78.8 million), representing 11% of the Group's turnover (2002 14%) and £5.5 million (2002 £4.6 million) of operating profit, representing 15% (2002 9%) of the Group's operating profit.

The weakness of the US dollar in the second half of the year has been offset to some extent by the strength of the euro throughout 2003. The effect of currency translation for 2003 compared with 2002 was to reduce turnover by £16.6 million and operating profit by £0.2 million. In relation to profit before taxation, goodwill amortization and exceptional items, currency translation resulted in an increase of £0.7 million as our interest costs are largely denominated in US dollars and a higher proportion of profits this year were denominated in euro.

Reported profit before taxation was £0.3 million after charging exceptional items of £20.0 million compared with a loss of £1,023.4 million in 2002 after charging exceptional items of £1,013.3 million. Reported loss per share for 2003 was 0.05 pence (2002 loss 113.90 pence).

In 2002 we took a large exceptional charge for goodwill impairment of £923.3 million which was principally in relation to the Communications group. After carrying out the appropriate valuation exercises, no further impairment charges were required in 2003.

Spirent continued to generate cash in all its operating groups during 2003. Operating cash flow of £68.2 million was 11% down on the previous year of £76.9 million. Cash flow before acquisitions, disposals, equity dividends and financing, or free cash flow, before the cash cost of exceptional items, was higher at £62.8 million compared with £44.1 million for 2002. The second half of the year was particularly strong in cash generation terms with £39.9 million of free cash flow before exceptional items being generated.

Turnover

Our revenues, which we refer to as turnover, are derived from:

- communications: performance analysis and service assurance solutions;
- solutions for fastening, identification, protection and connectivity in electrical and communications networks;
- power control systems for specialist electrical vehicles and software systems for the aviation market;
- hardware systems for the aerospace market until the disposal of AIS on June 30, 2003; and
- temperature, humidity, pressure and gas sensing products until the disposal of Sensing Solutions in November 2001.

Turnover is generally recognized upon shipment of the product unless there are significant post-delivery obligations or collection is not considered probable at the time of sale. When significant post-delivery obligations exist, turnover is deferred until such obligations are fulfilled. Turnover from service obligations is deferred and generally recognized ratably over the period of the obligation.

During the year ended December 31, 2003 turnover by source in Europe was 36% (2002 28%), of which the United Kingdom comprised 16% (2002 13%), and in North America 56% (2002 66%). This reflects the reduction in turnover in North America following the deterioration seen in our Communications group which is predominantly North American based. The proportion of turnover generated in North America is expected to remain at these levels in the near term.

No single customer accounted for more than 10% of total turnover in any of the three years in the period ended December 31, 2003.

Cost of sales

Cost of sales is comprised of direct costs associated with product sales including product development and all attributable overheads. Of our three operating groups, our Communications group has historically experienced the lowest cost of sales as a percentage of turnover and has consequently earned the highest margins, however these margins have been significantly reduced during the telecommunications downturn. Our Network Products group has typically experienced more stable returns.

Operating expenses

Operating expenses consist of selling and distribution expenses, administration expenses and other operating income. Selling and distribution expenses consist primarily of salaries and related costs for sales and marketing personnel and promotional expenditures. Administration expenses include goodwill amortization, impairment expense and other operating exceptional items. For both categories of expenses excluding goodwill amortization and exceptional items, the principal variable is headcount.

Income from interest in joint venture

This represents our share of operating profit from the WAGO joint venture which was sold in April 2003, and our share of the costs of our Spirent DM Limited joint venture which was established in 2003.

Interest receivable and similar income

Interest receivable and similar income is comprised of interest from cash and cash equivalents.

Interest payable

Interest payable primarily comprises interest on loans and bank overdrafts, as well as finance charges on finance leases. Finance charges associated with debt issuances are charged to the profit and loss account over the life of the instrument and included in interest expense. An exceptional interest charge, comprising the make-whole amount on the notes and related bank fees arose in 2003.

Other finance expense/income

Other finance expense or income arises in connection with the application of FRS 17 "Retirement Benefits" and represents the expected return on the schemes' assets net of the charge for the increase during the period in the net present value of the schemes' liabilities because the benefits are one year closer to settlement.

Critical Accounting Policies

The fundamental objective of financial reporting is to provide useful information that allows a reader to comprehend the business activities of Spirent. To aid in that understanding, management has identified Spirent's "critical accounting policies". These policies are considered "critical" because they have the potential to have a material impact on Spirent's financial statements, and because they require judgments and estimation due to the uncertainty involved in measuring, at a specific point in time, events which are continuous in nature.

Goodwill and intangibles

Goodwill arising on the acquisition of subsidiaries, and representing the excess of cost over the fair value of the attributable assets and liabilities acquired, is capitalized as an intangible asset and amortized over its estimated useful economic life up to a maximum of 20 years. Goodwill is reviewed for impairment at the end of the first full financial year following acquisition and in other periods if events or changes in circumstances indicate the carrying value may not be recoverable. US GAAP requires that goodwill is reviewed at least annually for impairment.

The deterioration in the telecommunications market in the second half of 2002 together with the significant fall in the Spirent share price resulted in a review of our businesses for impairment in that year. This review resulted in impairment losses of £923.3 million being recognized during 2002. A similar impairment loss of £724.6 million was recognized in 2001. These losses were the aggregate from the impairment reviews of each individual income generating unit and were determined in accordance with FRS 11 "Impairment of Fixed Assets and Goodwill". The impairment loss restated the assets to value in use using estimated cash flows which included assumptions on future growth rates, margins, product developement spend and other expenditure in these businesses. The resulting cash flows were discounted at pre-tax discount rates of between 15% and 20%, which were considered appropriate to those businesses based on their perceived risk compared to Spirent's weighted average cost of capital.

In addition, independent valuations were obtained for the purpose of impairment reviews in accordance with US GAAP to determine the fair value of the businesses and any necessary impairment charges. These valuations were based on management's estimates of the future cash flows of the businesses and have been considered in determining the fair values of the businesses.

The appropriate valuation exercises were carried out in 2003 under UK and US GAAP, the result being that no further impairment charges were identified.

The impairment reviews for UK and US GAAP have been performed using a number of assumptions which management considers most appropriate given the market conditions at that time. These assumptions underpin the cash flows upon which the calculations are performed. The discount rates applied were chosen based on the perceived risk within each business. Given the significance of the impairments identified in 2001 and 2002, varying any of these assumptions could have materially changed the impairment charges reported.

In implementing our amortization policy various judgments and assumptions have been made in relation to the estimated useful economic lives of the goodwill and intangibles concerned and their recoverability. Using a different useful economic life could materially affect the amortization charges under UK GAAP or US GAAP.

Stocks and debtor provisions

Spirent makes provisions against inventories, which we refer to as stocks, in excess of 12 months' usage and for doubtful debts. Spirent's policy is to reserve against both excess and obsolete inventories. Inventory is assessed and reserved if in excess of 12 months' usage. Obsolete inventories are identified on an itemized basis. Debtors are reserved based on exposures on specific customer accounts and reserved as soon as the exposure is identified by management through the process of regular reviews. Use of a different policy in respect of inventory and debtors could result in materially different provisions being made.

Revenue recognition

Revenue from product sales of hardware and software is recognized at time of delivery and acceptance. Terms of acceptance are dependent upon the specific contractual arrangement agreed with the customer. Where the sale is to a new customer and installation is to be performed, revenue recognition is deferred until acceptance has occurred. Revenue recognition is also deferred until acceptance where a new product is supplied to an existing customer.

Revenue from multiple element contracts is allocated based on prices charged for each individual element when sold separately. Revenue from services is recognized ratably over the period of performance.

The Group does not enter into a significant number of long-term sales contracts. Revenue and estimated profits on long-term contracts are recognized under the percentage-of-completion method of accounting. When estimates of total contract revenues and costs indicate a loss, a provision for the entire amount of the contract loss is recognized in the period in which the loss becomes evident.

The Group does not enter into bill and hold transactions and revenue is only recognized when collectability is probable.

Pensions

We have implemented FRS 17 "Retirement Benefits" at December 31, 2003 to bring us in line with latest UK GAAP and to move towards the adoption of International Financial Reporting Standards in 2005. Prior year amounts have been restated to reflect the change in accounting policy.

Under FRS 17, the assets of the defined benefit plans are measured at their market value at the balance sheet date and the liabilities are measured using the projected unit method. The discount rate used to measure the scheme liabilities is the current rate on an AA corporate bond of equivalent term and currency to the liabilities. The extent to which the schemes' assets exceed or fall short of the schemes' liabilities is shown as a surplus or deficit in the balance sheet net of deferred tax.

The regular service cost of providing retirement benefits to employees in defined benefit schemes is charged to the operating profit in the year together with the cost of providing benefit improvements in respect of past service and gains or losses arising on settlements and curtailments.

A credit for the expected return on the schemes' assets and a charge for the increase in the period in the present value of the schemes' liabilities because the benefits are one year closer to settlement, are included in other finance income or expense in the profit and loss account. Differences arising between the actual and expected return on the schemes' assets together with changes in the actuarial assumptions are included in the statement of recognized gains and losses.

The funding position of the defined benefit plans reported at December 31, 2003 was a deficit of £43.4 million (2002 £41.9 million) before taxation, representing a funding deficit of 31% (2002 32%).

The various assumptions used in this valuation are detailed in Note 10 of Notes to the Financial Statements. Changing any one, or a combination of these assumptions will result in a change to the deficit reported. Varying the assumptions will also have an impact on the profit and loss account and statement of total recognized gains and losses.

Deferred taxation

The reduction in activity levels and the resulting deterioration in operating profits necessitated a reassessment of the carrying value of £19.0 million of deferred tax assets in 2002. These assets had previously been recognized on the acquisition of businesses, on prior years' exceptional items, and on timing differences. We continue, in 2003, not to recognize deferred tax assets, other than in relation to the pension fund deficit, as there is currently insufficient evidence to support recognition under accounting standards.

Deferred tax assets of £18.3 million (2002 £20.1 million) arising principally on timing differences in the United States and United Kingdom have not been recognized. In addition, the Group has tax losses arising in the United States of £70.1 million (2002 £23.1 million) and in the United Kingdom of £24.8 million (2002 £10.2 million) that are available for offset against future taxable profits and which have not been recognized.

We have not recognized these deferred tax assets based on current forecasts and estimates prepared by management. A change to these forecasts and estimates could result in recognition of some of the assets currently unrecognized. Given the significance of the assets that remain unrecognized this could materially affect the deferred tax assets reported and the resulting credit to the profit and loss or statement of unrecognized gains and losses.

Year Ended December 31, 2003 Compared with the Year Ended December 31, 2002

	First half 2003	Second half 2003	Year ended December 31 2003	Year ended December 31 Restated(1)(2) 2002
	(£ millions)			
Turnover				
Continuing operations				
Performance Analysis	71.3	77.4	148.7	184.0
Service Assurance	46.2	45.5	91.7	131.4
Communications	117.5	122.9	240.4	315.4
Network Products	85.9	88.5	174.4	164.7
Systems	25.8	25.6	51.4	78.8
	229.2	237.0	466.2	558.9
Operating profit before goodwill amortization and exceptional items				
Continuing operations				
Performance Analysis	0.5	3.9	4.4	10.0
Service Assurance	4.6	4.8	9.4	20.8
Communications	5.1	8.7	13.8	30.8
Network Products	8.1	8.6	16.7	15.0
Systems	2.2	3.3	5.5	4.6
	15.4	20.6	36.0	50.4

(1) Restated for the adoption of FRS 17 "Retirement Benefits".

(2) The results for the Communications group have been restated to reflect the transfer of our field test activities from the Performance Analysis to the Service Assurance division.

Turnover and operating profit

Comparisons by segment are given below for ongoing operations (excluding divestments which cannot be classified as discontinued operations). Operating profit and return on sales are stated before goodwill amortization and exceptional items.

Communications

	First half 2003	Second half 2003	2003	2002 Restated	Annual change
		(£ millions)			%
Turnover					
Performance Analysis	71.3	77.4	**148.7**	184.0	(19)
Service Assurance	46.2	45.5	**91.7**	131.4	(30)
	117.5	122.9	**240.4**	315.4	(24)
Operating profit before goodwill amortization and exceptional items					
Performance Analysis	0.5	3.9	**4.4**	10.0	(56)
Service Assurance	4.6	4.8	**9.4**	20.8	(55)
	5.1	8.7	**13.8**	30.8	(55)
Return on sales before goodwill amortization and exceptional items		(%)			
Performance Analysis	0.7	5.0	**3.0**	5.4	
Service Assurance	10.0	10.5	**10.3**	15.8	
Communications group	4.3	7.1	**5.7**	9.8	

The results for the Communications group for 2002 and the first half of 2003 have been restated to reflect the transfer of our field test activities from the Performance Analysis to the Service Assurance division.

As anticipated, the telecommunications market remained challenging throughout 2003. 2003 saw further reductions in capital spending of approximately 20% by our NEM and NSP customers. Spirent Communications' turnover was down 24% compared with 2002, but turnover for the second half of 2003 was up 5% compared with the first half due to modestly improved levels of activity. Compared with 2002, operating profit for 2003 was down 55%, however operating profit in the second half of 2003 improved by 71% over the first half. Return on sales for the group for 2003 reduced to 5.7% from 9.8% in 2002.

Quarterly order intake in the Performance Analysis division has increased since the first half reflecting the modest improvement in activity levels and the normal seasonality of the business. Due to the lower levels of spending and change in ordering patterns by the US ILECs, the Service Assurance division's order book declined from $59.2 million (£36.8 million) at the end of 2002 to $44.4 million (£25.0 million) at the end of 2003.

Performance Analysis

Due to the drop in spending by NEMs and NSPs globally during 2003, turnover in this division fell 19% compared with 2002 to £148.7 million. Operating profit for 2003 was down 56% compared with 2002 at £4.4 million. However our performance in the second half of 2003 showed an improvement with turnover up 9% and operating profit up by £3.4 million due to a modest increase in activity levels in the latter part of the year. Return on sales for the second half recovered to 5.0%, but was 3.0% for the year compared with 5.4% in 2002.

Our customer base for this division remains broadly spread and includes some of the largest NEMs and NSPs worldwide. We have benefited from the direct sales presence we established in China in 2002 and our increased sales and marketing efforts throughout the rest of Asia. In Europe, a continuing focus on the development and roll-out of DSL networks and services by customers helped sales of our broadband test equipment and we saw encouraging interest in our web applications and security testing products.

While turnover for the year reduced overall we saw improvements in sales from our web applications and security testing activities and an increase in sales to the government sector. Growth in data traffic continues to drive the need for increased broadband access and our broadband solutions continue to represent the largest part of this division's sales. We believe we have been able to capitalize on the trend towards VoIP and have launched several new products that are aimed at this growth area. Interest in IPv6, which provides broader address space for the next phase of the Internet, was also good this year as the technology moves closer to deployment.

In the wireless sector, we benefited from our acquisition in 2002 of W-CDMA expertise. During the year we launched a W-CDMA network emulator for testing the interoperability of mobile handsets and networks and versions of our position location test system to support GSM and W-CDMA. In the CDMA sector, we launched several products in 2003 aimed at testing the performance of mobile data services and enhanced voice services such as "push-to-talk".

Service Assurance

We are a leading provider of monitoring systems to the US ILECs' continuing broadband service roll-out programs. However during the year our core customers continued to reduce their overall capital spending and as a result sales were adversely affected with turnover for the division declining 30% to £91.7 million compared with £131.4 million in 2002. While we continue to be a leading supplier of monitoring systems for DSL services, systems for digital leased line services remain the largest part of our Service Assurance business, accounting for approximately half the sales in 2003. Operating profit of £9.4 million for 2003 was down 55% for the year. Return on sales for 2003 fell to 10.3% from 15.8% in 2002. In order to capitalize on potential engineering and customer synergies we have transferred our field test business into the Service Assurance division. At the end of the year actions were taken to extend our existing capabilities in the IP services sector which we believe represents an important growth opportunity.

During 2003 we expanded our product range with test probes and OSS for next-generation DSL variants which allow higher speed broadband access for the residential and enterprise markets. A number of our existing customers have announced the introduction of next-generation IP services and we have won initial orders in this market for gigabit Ethernet, virtual local area network and IP virtual private network services. We intend to expand our capabilities and product functionality in this area in the future. We have also extended our product line through the launch of FieldOp , an operations management solution that integrates service assurance and workforce management capabilities onto a single platform for use in the field.

Network Products

	First half 2003	**Second half 2003**	**2003**	**2002 Restated**	**Annual change**
		(£ millions)			**%**
Turnover	85.9	88.5	**174.4**	164.7	6
Operating profit before goodwill amortization and exceptional items	8.1	8.6	**16.7**	15.0	11
Return on sales (%) before goodwill amortization and exceptional items	9.4	9.7	**9.6**	9.1	

The business delivered a sound performance in 2003 with turnover up 6% at £174.4 million and operating profit up 11% at £16.7 million compared with 2002. Turnover in the second half of 2003 was up 3% which is a positive indicator given that the second half of the year is usually weaker than the first. Return on sales at 9.6% in 2003 was up over the previous year.

The main improvement in turnover in 2003 over 2002 came from our European automotive sales where we have increased market penetration.

The automotive sector remains our most important with sales to this market accounting for 34% of turnover in 2003 compared with 30% in 2002. Despite global vehicle production declining modestly year on year, the trend to replace metal parts with plastic and the increasing complexity of electronic systems within cars has resulted in more of our products being specified on new vehicle platforms than on their predecessors.

Our range of automated systems, including "Autotools", continues to generate sales of the high volume consumables they require, such as cable ties and identification labels and markers. We now have a broad installed base of these systems at cable and wire harness manufacturers worldwide.

Sales of our local area network connectivity products were lower in the United Kingdom in 2003 compared with 2002 reflecting the continued decline in the market but we were able to continue to increase sales in the United States. The market for our broadband products remained depressed due to continuing cuts in spending by telecommunications service providers worldwide.

Systems

	First half 2003	**Second half 2003**	**2003**	**2002 Restated**	**Annual change**
		(£ millions)			**%**
Turnover	21.0	25.6	**46.6**	43.0	8
Operating profit before goodwill amortization and exceptional items	2.5	3.3	**5.8**	4.4	32
Return on sales (%) before goodwill amortization and exceptional items	11.9	12.9	**12.4**	10.2	

Figures in the above table relate to ongoing businesses only. Divested businesses contributed £4.8 million (2002 £35.8 million) of turnover and a £0.3 million operating loss (2002 £0.2 million operating profit).

On an ongoing business basis the Systems group saw an 8% increase in turnover to £46.6 million and a 32% increase in operating profit to £5.8 million compared with 2002. The improvement was mainly in PG Drives Technology, our power controls business. During 2003 we completed the divestment of our AIS businesses from within the Systems group's aerospace activities for net proceeds of £3.2 million in cash.

The continuing success of our established VSI systems for powered wheelchairs and our S-Drive systems for mobility scooters enabled us to increase customer penetration and win new business in the mobility vehicles market in 2003. During 2003 we also made further progress in the small industrial vehicles market, with the I-Drive and TRIO+ products being well received by customers.

In our aerospace business, in 2003, sales of GOLD , a leading contractor logistics support software system to the military market, were up compared with 2002 largely due to increased sales to leading defense manufacturers. The continued weak conditions in the civil aviation market affected sales of AuRA , our ground-based MRO software system.

Divested operations

In 2003 we divested of our AIS businesses from within the Systems group's aerospace activities which contributed £4.8 million of turnover and an operating loss of £0.3 million in 2003.

We also divested the WAGO interconnection joint venture which contributed £2.9 million of income in 2003.

Cost of sales

Cost of sales was £279.8 million for the year ended December 31, 2003 compared with £340.8 million for the year ended December 31, 2002, a reduction of 18% and a result of reduced sales activity. Cost of sales as a percentage of turnover was slightly lower at 60% compared with 61% for 2002 however cost of sales includes an exceptional charge of £4.4 million in 2002 in respect of inventories in excess of 12 months' usage which was caused by the deterioration in the technology industry.

Product development expenditure was £66.0 million compared with £77.7 million for the year ended December 31, 2002, a decrease of 15%. Product development expenditure represented 14% of turnover in both years. Of the total product development expenditure £57.8 million was incurred by the Communications group (2002 £66.2 million).

Operating expenses

Total operating expenses, which include goodwill amortization and exceptional items, were £167.6 million for the year ended December 31, 2003 compared with £1,188.7 million for the year ended December 31, 2002. Total operating expenses in 2002 were impacted by goodwill amortization and exceptional items as discussed below.

Selling and distribution expenses were £110.0 million for the year ended December 31, 2003, compared with £124.6 million for the year ended December 31, 2002, a decrease of 12%. As a percentage of turnover selling and distributions costs were 24% compared to 22% in 2002. The absolute decrease was due to cost reduction actions taken in 2002 and in 2003, the effect of the divestments and exchange.

Administration expenses were £58.3 million for the year ended December 31, 2003, compared with £1,064.7 million for the year ended December 31, 2002 which included £923.3 million of goodwill impairment. There is no impairment charge arising in 2003. Administration expenses for the year ended December 31, 2003 included £7.5 million of exceptional costs (2002 £37.2 million) and £9.7 million of goodwill amortization (2002 £56.1 million). Excluding exceptional items and goodwill amortization, administration costs are £41.1 million and represented 9% of turnover in 2003 compared with £48.1 million, also representing 9% of turnover, in 2002. The reduction in costs in absolute terms can be attributed to the cost reduction actions taken as well as the effect of divestments and exchange. The significant reduction in the goodwill amortization charge to £9.7 million compared with £56.1 million in 2002 is due to the goodwill impairment charge taken in 2002.

Operating exceptional items of £7.5 million charged as administration costs include £2.3 million in respect of the renegotiation of our borrowing terms and £3.8 million for the cost reduction actions within the Communications group. We were able to sublet two of our vacant locations and an amount of £1.8 million has been released in respect of these. Further properties were vacated in 2003 that gave rise to a charge of £1.0 million, resulting in a net release of £0.8 million for lease provisions in the year. In addition, a charge of £2.2 million has been taken for tangible fixed asset write-downs connected with the vacated space.

The cash cost of operating exceptional items was £10.9 million in 2003 (2002 £7.7 million).

Turnover and income from interest in joint venture

In 2003 our share of turnover from the WAGO joint venture decreased to £22.4 million (2002 £75.6 million) and our share of operating profit decreased to £2.9 million (2002 £7.4 million). The significant reduction is due to the disposal of the WAGO joint venture on April 4, 2003, as we are reporting our share of the result from the joint venture only up to the date of disposal. Our share of the Spirent DM Limited joint venture was a £0.2 million operating loss for 2003.

Income from interests in associates

Income from interests in associates, consisting of Tyton Company of Japan and 3M/ECC in the Netherlands amounted to £2.1 million for the year ended December 31, 2003 compared with £1.0 million in the year ended December 31, 2002. The improvement was due to the strong sales experienced by our Japanese associate.

Profit/(loss) on disposal and closure of operations

The divestment of our interests in the WAGO joint venture and of AIS from within the Systems group's aerospace activities resulted in a net profit of £3.6 million after charging £2.6 million of goodwill previously written off to reserves and now reinstated in accordance with FRS 10.

Net interest payable and other finance (expense)/income

Net interest payable has reduced from £12.3 million in 2002 to £9.3 million for the year to December 31, 2003. This reduction is principally a result of the reduction in net debt. A charge of £1.5 million arose in connection with the application of FRS 17 "Retirement Benefits".

Exceptional interest expense

An exceptional interest cost of £16.1 million has been charged in 2003. This charge comprises the make-whole amount and related bank fees of £14.3 million charged in the first half of the year, together with a make-whole amount of £1.8 million accrued in respect of the prepayment of loan notes in February 2004 and negotiated at the end of 2003.

The cash cost of the exceptional interest expense was £13.7 million in 2003.

Taxation

The Group's effective tax rate for 2003 was 7.7% compared with 18.3% in 2002 being significantly reduced by a prior year adjustment of £6.0 million recognizing the utilization of losses and the release of provisions. Excluding this the effective tax rate was 27.7%.

The exceptional tax credit of £1.7 million is in respect of the tax effect of the exceptional items in 2003. In 2002 we reported a net exceptional tax charge of £18.5 million which was principally due to the re-evaluation of the recovery of deferred tax assets under FRS 19. We continue not to recognize deferred tax assets as there is currently insufficient evidence to support recognition under accounting standards, other than in relation to the pension fund deficit in 2003.

Year Ended December 31, 2002 Compared with the Year Ended December 31, 2001

The previous year's presentation of segmental information has been restated to comply with current year presentation due to the implementation of FRS 17 "Retirement Benefits" and UITF 38 "Accounting for ESOP Trusts". In addition our field test activities within our Communications group have been transferred from our Performance Analysis division to our Service Assurance division.

	Year ended December 31	
	Restated(1)(2) 2002	**Restated(1)(2) 2001**
	(£ millions)	
Turnover		
Continuing operations		
Performance Analysis	184.0	241.4
Service Assurance	131.4	189.2
Communications	315.4	430.6
Network Products	164.7	170.4
Systems	78.8	124.0
	558.9	725.0
Discontinued operations		
Sensing Solutions		76.8
	558.9	801.8
Operating profit before goodwill amortization and exceptional items		
Continuing operations		
Performance Analysis	10.0	38.6
Service Assurance	20.8	44.8
Communications	30.8	83.4
Network Products	15.0	14.9
Systems	4.6	5.4
	50.4	103.7
Discontinued operations		
Sensing Solutions		8.1
	50.4	111.8

(1) Restated for the adoption of FRS 17 "Retirement Benefits".

(2) The results for the Communications group have been restated to reflect the transfer of our field test activities from the Performance Analysis to the Service Assurance division.

Turnover and operating profit

Comparisons by segment are given below for ongoing operations (excluding divestments which cannot be classified as discontinued operations).

Communications

	Year ended December 31		
	Restated 2002	Restated 2001	Change
	(£ millions)		%
Turnover			
Performance Analysis	184.0	241.4	(24)
Service Assurance	131.4	189.2	(31)
Communications group	315.4	430.6	(27)
Operating profit before goodwill amortization and exceptional items			
Performance Analysis	10.0	38.6	(74)
Service Assurance	20.8	44.8	(54)
Communications group	30.8	83.4	(63)

Return on sales before goodwill amortization and exceptional items	(%)	
Performance Analysis	5.4	16.0
Service Assurance	15.8	23.7
Communications group	9.8	19.4

Throughout 2002 our major customers, the NEMs and NSPs, continued to restructure their operations in response to the significantly reduced overall market. This coupled with certain regulatory issues for our customers in the United States resulted in a reduction in spending on our products, particularly in the third quarter. By taking immediate cost-saving actions in October 2002 we were able to return to profitability in our Communications group in the fourth quarter after delivering a small loss in the third quarter.

The Communication group's turnover was £315.4 million for the year ended December 31, 2002, compared with £430.6 million for the year ended December 31, 2001, a decrease of 27%. Operating profit was £30.8 million for the year ended December 31, 2002, compared with £83.4 million for the year ended December 31, 2001, a decrease of 63%.

Return on sales, before goodwill amortization and exceptional items, decreased to 9.8% for the year ended December 31, 2002, compared with 19.4% for the year ended December 31, 2001. Return on sales was reduced in both divisions and the most significant reduction was seen in the Performance Analysis division where return on sales dropped to 5.4% compared with 16.0% in 2001. The Service Assurance division's return on sales reduced to 15.8% compared with 23.7% in 2001.

During the year we maintained investment in the development of our products. Product development expenditure in 2002 of £66.2 million (2001 £73.0 million) represented 21% of the Communications group turnover and was invested in key areas such as gigabit and 10-gigabit Ethernet in the access and metro networks, VoIP, IPv6, Internet infrastructure and security testing, storage area networks and 3G wireless technologies. This investment resulted in numerous new products and enhancements to existing product lines being launched during the year including the first end-to-end performance analysis and radio frequency channel emulation system for the wireless local area network ("LAN") market, a fully automated system for testing W-CDMA mobile handsets, a system for the analysis of Internet infrastructures simultaneously from the physical layer to the applications layer, and a test system for storage area networks.

In the Performance Analysis division turnover fell in 2002 to £184.0 million from £241.4 million due to decreased spending by our major customers in the United States and Europe. The return on sales declined to 5.4% due to a combination of the drop in trading levels and the timing of the associated cost reductions in this business. Despite the overall reduction there were areas of growth, in particular our wireless test products, which increased strongly with turnover up 57% and our position location test products, which performed well.

In the Service Assurance division turnover fell in the third quarter as our major customers, the US ILECs, reduced investment in their networks in response to financial constraints and regulatory pressures. As a result of lower volume, return on sales was affected falling to 15.8% from 23.7% in 2001. Return on sales was also affected by the product mix which included a higher hardware content (lower margin) in the second half of the year as compared with the first half which had a higher software element (higher margin). Additionally, sales of monitoring systems for digital leased line services having a lower margin, represented a higher proportion of turnover in 2002 compared with 2001, which had a predominance of DSL business.

Network Products

	Year ended December 31		
	Restated 2002	Restated 2001	Change
	(£ millions)		%
Turnover	164.7	170.4	(3)
Operating profit before goodwill amortization and exceptional items	15.0	14.9	1
Return on sales (%) before goodwill amortization and exceptional items	9.1	8.7	

Turnover in our Network Products group was down marginally by 3% and operating profit before goodwill amortization and exceptional items was up 1% on the prior year. In the United States, improved sales to the heavy vehicles market and growth of our LAN "Network Sciences" product line were off-set by reduced sales to the telecommunications service providers. Our European sales showed a small increase overall and in Japan sales were broadly flat. In South America the recession led by the severe economic collapse in Argentina negatively affected the group. The restructuring actions taken in 2001 to consolidate and extend customer-facing activities and reduce administrative and back office activities became fully effective in the first half of 2002 and return on sales improved to 9.1% compared to 7.3% in the second half of 2001.

Sales to the automotive sector contributed 30% to turnover in 2002 compared with 27% in 2001. While global vehicle production was broadly flat in 2002 the trend towards increasing electronic/electrical systems content and lighter vehicles requiring increased use of plastics provided underlying market growth. As a result we were able to increase our penetration with vehicle manufacturers, their first tier suppliers and major vehicle harness manufacturers worldwide. Our sales in the United States heavy vehicles market recovered showing 23% growth after the significant market downturn in 2001.

The market for our broadband products and structured cabling products remained very weak in the United States and the United Kingdom throughout the year due to depressed conditions in the telecommunications market and reductions in enterprise information technology spending.

Systems

	Year ended December 31		
	Restated 2002	Restated 2001	Change
	(£ millions)		%
Turnover	53.8	48.6	11
Operating profit before goodwill amortization and exceptional items	3.3	(0.2)	>100
Return on sales (%) before goodwill amortization and exceptional items	6.1		

Figures in the above table relate to ongoing businesses only. Divested businesses contributed £25.0 million of turnover (2001 £75.4 million) and £1.3 million of operating profit (2001 £5.6 million).

On an ongoing business basis the Systems group saw an increase in revenues from £48.6 million to £53.8 million and in operating profit from a loss of £0.2 million to a profit of £3.3 million. Return on sales improved to 6.1%. These improvements were achieved through increased customer penetration, product launches (including the new airborne file server) and the successful entrance into new markets. The impact of cost reductions taken in the first half of 2002 in the aerospace business coupled with increased sales resulted in improved trading in the Systems group in the second half of 2002.

The power controls business saw good growth in turnover over 2001 mainly due to increased penetration of the mobility vehicles market. Sales to the industrial market, a new market for the business, also contributed to the improvement.

Divested operations

During 2002 Spirent sold three businesses all from within the Systems group. In April, May and September, we completed the divestment of our aerospace component businesses, Switching Systems International and Monitor Labs Incorporated, respectively. Combined revenues from these businesses were £25.0 million in 2002 with operating profit of £1.3 million.

Cost of sales

Cost of sales was £340.8 million for the year ended December 31, 2002 compared with £490.7 million for the year ended December 31, 2001, a reduction of 31% as a result of reduced activity. Cost of sales as a percentage of turnover was unchanged at 61%. Cost of sales includes an exceptional charge of £4.4 million in respect of inventories in excess of 12 months' usage (2001 £14.2 million) which was caused by the deterioration in the technology industry.

Product development expenditure was £77.7 million compared with £95.9 million for the year ended December 31, 2001, a decrease of 19%. Product development expenditure represented 14% of turnover, as compared with 12% in 2001. Of the total product development expenditure £66.2 million was incurred by the Communications group (2001 £73.0 million).

Operating expenses

Total operating expenses were £1,188.7 million for the year ended December 31, 2002 compared with £1,045.4 million for the year ended December 31, 2001, impacted by goodwill amortization and exceptional items as discussed below.

Selling and distribution expenses were £124.6 million for the year ended December 31, 2002, compared with £156.0 million for the year ended December 31, 2001, a decrease of 20%. As a percentage of turnover, selling and distribution costs were 22% compared with 19% in 2001. The absolute decrease was due to cost reductions taken in late 2001 and in 2002 and to the effect of the divestments.

Administration expenses were £1,064.7 million for the year ended December 31, 2002, compared with £890.6 million for the year ended December 31, 2001. Included within administration expenses are £923.3 million of goodwill impairment (2001 £724.6 million), £37.2 million of exceptional costs (2001 £20.7 million) and £56.1 million of goodwill amortization (2001 £86.6 million). Excluding exceptional items and goodwill amortization, administration costs are £48.1 million and represented 9% of turnover in 2002 compared with £58.7 million and 7% in 2001. The reduction in costs in absolute terms can be attributed to the cost reductions taken as well as the effect of divestments. The reduction in the goodwill amortization charge to £56.1 million compared with £86.6 million in 2001 is due to the goodwill impairment charge taken in 2001.

Other operating income, consisting of non-trading income net of any specific expenses relating to that income, amounted to £0.6 million for the year ended December 31, 2002 compared with £1.2 million for the year ended December 31, 2001.

Exceptional items of £37.2 million other than goodwill impairment and included in administrative expenses are as follows:

Restructuring costs of £8.6 million were charged in respect of redundancy payments and other costs incurred in the restructuring of the business. Tangible fixed assets have been written down by £3.6 million relating to the down-sizing in our Communications group.

After the reduction in workforce in the fourth quarter we relocated certain employees to make more efficient use of our facilities and this resulted in certain leased properties being vacated. Provisions of £20.2 million have been recognized in the period in relation to our continuing obligations under these leases.

Acquisition retention bonuses arising from acquisitions made in 2000 of £4.8 million were charged in 2002.

The cash cost of these operating exceptional items was £7.7 million in 2002 (2001 £11.9 million).

Turnover and income from interest in joint venture

In 2002 our share of turnover from the WAGO joint venture decreased by 3% to £75.6 million (2001 £78.3 million) and our share of operating profit decreased by 23% to £7.4 million (2001 £9.6 million). The decline was due to the continuing depressed conditions WAGO experienced in most of its geographic markets during the year. Our share of interest payable and of taxation from WAGO were £0.7 million and £2.7 million, respectively, giving a profit after taxation of £4.0 million.

We announced on March 12, 2003 the divestment of our interests in WAGO to our joint venture partners. The transaction completed on April 4, 2003.

Income from interests in associates

Income from interests in associates, consisting of Tyton Company of Japan, 3M/ECC in the Netherlands, and Caw in the United States, amounted to £1.0 million for the year ended December 31, 2002 compared with £1.3 million in the year ended December 31, 2001. The majority holding of Caw was acquired by Spirent in August 2002, from which date Caw was fully consolidated.

Profit/(loss) on disposal and closure of operations

We continued to divest our non-core businesses and realized £37.6 million in net proceeds from the sale of our aerospace component businesses from within our Systems group to Curtiss-Wright Corporation in April 2002. Other divestments, also within our Systems group realized a further £18.0 million.

A net loss of £48.4 million is reported in 2002 on divestments after charging £70.8 million representing goodwill written off against reserves in previous years and now reinstated in accordance with FRS 10.

Net interest payable and other finance (expense)/income

Net interest payable was reduced from £22.8 million in 2001 to £12.3 million in 2002, as we benefited from the reduction in interest rates, primarily on our US dollar borrowings. Benefit was also obtained from the reduction in borrowings following receipt of the proceeds from the sale of Sensing Solutions in November 2001.

A charge of £0.3 million arises in 2002 (2001 income £0.4 million) on the application of FRS 17 "Retirement Benefits".

Taxation

The tax charge amounted to £26.9 million in the year ended December 31, 2002 compared with £32.4 million in the year ended December 31, 2001. The charge for 2002 includes an exceptional tax charge of £18.5 million arising principally through the re-evaluation of the recovery of deferred tax assets under FRS 19. The effective tax rates after adjusting for goodwill amortization, exceptional items and the loss on disposal of operations and the exceptional tax charge were 18.3% and 29.4%, respectively, in the years ended December 31, 2002 and 2001.

Liquidity and Capital Resources

Our policy is to finance operations through a combination of retained earnings and external financing raised principally by the parent company. Debt is largely sourced from the syndicated bank market and the United States private placement market.

In order to provide the Group with an increase in the level of headroom available in relation to certain of the financial covenants, amendments to the terms of our notes and syndicated bank facility were agreed in March 2003. These amendments were conditional on the divestment of our interests in the WAGO joint venture and the application of the net proceeds to partially pre-pay our notes. On completion of the divestment of WAGO in April 2003, £47.0 million of our notes were pre-paid and an associated make-whole amount of £12.5 million was paid. Following this prepayment $144.2 million of notes remained outstanding. These notes mature in 2006 ($6.4 million) and in 2009 ($137.8 million). Further details on our notes are contained in Note 28 of Notes to Financial Statements and in "Item 10. Material Contracts".

At December 31, 2003 no amounts were drawn under our committed bank facility of £60 million and we held £37.6 million of cash. We determined that this £60 million bank facility was in excess of our business requirements. Consequently at the end of 2003 we entered into negotiations with a small group of lending banks and agreed a £30 million, 364-day working capital facility with a six-month term-out option which became effective on February 18, 2004 to replace the £60 million facility. We have applied some of our excess cash, including the net proceeds from the disposal of AIS, to make a partial prepayment on our notes to reduce the cost of borrowing going forward. The partial prepayment of $14.4 million (£8.1 million) was made on February 18, 2004 and an associated make-whole amount of $3.3 million (£1.8 million) has been incurred. This make-whole amount and the costs associated with this transaction were accrued in the 2003 financial year. Further details on the bank facility can be found in "Item 10. Material Contracts".

In our opinion these facilities provide sufficient liquidity for our present requirements. We believe that the present requirements of our existing businesses and future investment can be met through funds generated internally, divestment of businesses and external financing we expect to be available to us.

At December 31, 2003 net debt reduced significantly to £57.5 million from £161.8 million at the end of 2002 due to cash generation and the proceeds of divestments of non-core businesses. The weak US dollar benefited the net debt position on translation by £6.1 million.

At December 31, 2003 Spirent was well within its existing borrowing covenants. Net interest cover was 3.7 times (covenant ratio: greater than or equal to 2.5 times) and net debt to EBITDA (Earnings before interest, taxation, depreciation, amortization and exceptional items) was 0.96 times (covenant ratio: less than or equal to 2.25 times).

At December 31, 2003, gross borrowings amounted to £95.1 million, comprising £84.2 million of US dollar borrowings and £10.3 million of euro borrowings with the balance in a variety of other currencies.

At December 31, 2003, we held £37.6 million of cash. Cash is held in the United Kingdom or in the United States. There are no material amounts subject to restriction on repatriation to the parent company. Dividends are remitted through to the Company as appropriate having considered the working capital needs of the individual subsidiaries. At December 31, 2003 £18.2 million is held in US dollars, £8.9 million in sterling and the balance in other currencies.

At December 31, 2003 the Group's borrowings were composed of 57% of fixed rate debt. This excludes $72.1 million of notes which have been swapped into floating rates through the use of an interest rate swap, callable at the counterparties' option at six-monthly intervals.

Spirent continued to generate cash in all its operating groups during 2003. Operating cash flow of £68.2 million was 11% down on the previous year of £76.9 million. Cash flow before acquisitions, disposals, equity dividends and financing, or free cash flow, before the cash cost of exceptional items, was higher at £62.8 million compared with £44.1 million for 2002. The second half of the year was particularly strong in cash generation terms with £39.9 million of free cash flow before exceptional items being generated.

Net interest payments of £9.5 million, excluding the exceptional interest expense, were lower by £1.3 million compared to the previous year due to lower levels of debt.

We received tax refunds net of tax charges of £8.9 million in 2003 compared with a net tax payment of £4.2 million in 2002. Most of these refunds fell into the second half of the year and were due to the carry back of prior year tax losses in the United States.

We have substantially reduced our capital expenditure over the last two financial years and in 2003 spent a net £15.8 million compared with £25.8 million in 2002. This rate of capital spending is well below the depreciation charge of £29.3 million. We are planning to increase the rate of capital spending in 2004 to some £30.0 million largely in respect of renewing and increasing capacity in the Network Products group.

Off-Balance Sheet Arrangements

Spirent had no off-balance sheet arrangements at December 31, 2003.

Contractual Obligations

The following table summarizes the Group's contractual cash obligations and commitments at December 31, 2003, and the effect such obligations are expected to have on liquidity and cash flows in future periods.

	Payments due by period				
	Total	Less than 1 year	1 3 years	3 5 years	More than 5 years
			(£ millions)		
Senior notes	121.5	7.8	19.1	11.4	83.2
Bank and other loans	5.7	0.7	1.5	2.6	0.9
Finance lease obligations	16.6	1.6	3.0	4.1	7.9
Operating lease obligations	56.0	10.4	17.4	11.4	16.8
UK defined benefit plans (see "Pension Fund" below)	35.0	3.5	7.0	7.0	17.5
Unfunded unapproved retirement benefit	3.7	3.7			
Capital commitments	1.5	1.5			
Total	240.0	29.2	48.0	36.5	126.3

Pension Fund

The valuation of the defined benefit United Kingdom pension plans at April 1, 2003 showed a funding deficit of £50.7 million. In order to comply with the minimum funding requirements Spirent will make annual pension contributions of £3.5 million commencing on July 1, 2004 and has increased the rate of employer pension contribution from 13.4% to 16.0% of pay with effect from January 1, 2004.

As previously discussed we have implemented in full FRS 17 "Retirement Benefits". The funding position at December 31, 2003 under FRS 17 has improved as a result of the performance of equity markets since the valuation date and the deficit has reduced to £43.4 million.

Spirent has a contractual liability, as disclosed in our annual reports, to pay Nicholas Brookes an unfunded unapproved retirement benefit ("UURB") as agreed when he joined the Company in 1995. At December 31, 2003 the provision in respect of this UURB stood at £4.5 million. Conditionally upon him remaining in employment until June 30, 2004, Nicholas Brookes and the Company have agreed that he will commute all of his pension entitlement under the UURB in exchange for a lump sum payment of £3.7 million in cash, payable to him on July 1, 2004.

Foreign Exchange

See "Item 11. Quantitative and Qualitative Disclosures about Market Risk" for a description of our funding and treasury policies.

Currency exposures arise from trading transactions undertaken by subsidiaries in foreign currencies and on the translation of the operating results and net assets of our overseas subsidiaries.

Group treasury, by means of forward foreign exchange contracts, carries out the majority of the transactional hedging activity.

Transaction exposures of the operating results or net assets of our overseas subsidiaries are not actively hedged since these are accounting, not cash, exposures. To provide a partial hedge, we match, as far as possible, the currency of our borrowings with the currency profile of operating results and net assets.

Details of the currencies of borrowings are set out in "Liquidity and Capital Resources" above.

At the year end the balance sheet translation exposure was 61% hedged (2002 70%).

During the year the pound sterling strengthened against the US dollar, the main currency to which we are exposed.

Research and Development

With our continued commitment to innovation, investment in product development spend for 2003 was £66.0 million (2002 £77.7 million; 2001 £95.9 million) and represents 14% of turnover (2002 14%; 2001 12%).

In 2003, our Communications group devoted 24% of its turnover to product development, which amounted to £57.8 million (2002 £66.2 million: 2001 £73.0 million). A further £4.4 million (2002 £7.9 million: 2001 £14.5 million) was invested by our Systems group and £3.8 million (2002 £3.6 million; 2001 £3.6 million) was spent by the Network Products group. Discontinued operations accounted for the remaining £4.8 million of product development in 2001.

Factors That May Affect Future Results

We operate globally in a dynamic and rapidly changing environment that involves numerous trends, risks and uncertainties. The risks and uncertainties facing our business are discussed more fully in the section entitled "Item 3. Key Information Risk Factors". The following section lists some of those trends that have occurred and that we expect to have an effect on our business, financial condition or results of operations.

Our operating results could be harmed if the economy, and particularly the telecommunications industry into which we sell our products fails to recover or recovers at a pace slower than anticipated.

We rely on a limited number of customers in some of our businesses, and therefore any cancellation, reduction or delay in orders from them could significantly harm our business, operating results and financial condition.

Because of our significant international operations, we are exposed to a variety of risks, many of which are beyond our control, that could adversely affect our business.

We operate in rapidly changing industries and, if we do not keep up with these rapid changes, and continue significant investment in research and development, our turnover and operating results will suffer.

Fluctuations in exchange rates and heavy exposure to a weak US dollar could materially harm our operating results.

Future Spirent Stock Option Plan ("SSOP") awards will be granted as Stock Appreciation Rights ("SARs"). Under current accounting standards, the Company will recognize a non- cash charge to the Company's profit and loss account in 2004 to reflect the use of SARs. Additionally, in response to the introduction of International Financial Reporting Standards ("IFRS") in 2005, the Company will recognize a non-cash charge to reflect the use of all our share-based incentives.

Inflation

Inflation has not had a significant impact on our results of operations during any of the periods reported.

Differences Between UK GAAP and US GAAP

The accounting policies under which the consolidated financial statements of our group are prepared conform with accounting principles generally accepted in the United Kingdom, or UK GAAP. Such principles differ from those generally accepted in the United States, or US GAAP. The principal differences applicable to us relate to the accounting treatment of goodwill, share-based compensation, pension costs, derivative financial instruments, goodwill on businesses sold and deferred taxation. The differences are described in more detail in Note 34 of Notes to the Financial Statements included elsewhere in this Amendment. The effect of these differences on profit attributable to shareholders is summarized below:

		Year ended December 31		
		Restated(1) 2003	Restated(1)(2) 2002	Restated(1)(2) 2001
			(£ millions)	
Loss attributable to shareholders in accordance with UK GAAP		(0.5)	(1,050.7)	(764.0)
Adjustments:				
Revenue recognition	deferred revenues	12.2	(2.1)	(48.6)
	deferred costs	(3.0)	(3.8)	21.7
Goodwill and other intangible assets		(0.7)	197.6	(109.3)
Stock-based compensation		(0.9)	0.2	18.3
Pension costs		2.2	(2.2)	0.1
Profit on disposal		(1.0)	49.4	35.8
Vacation payroll costs			0.5	0.4
Derivative financial instruments		(1.9)	2.1	(1.2)
Income from interest in joint venture			0.2	0.3
Deferred taxation on above adjustments		(0.7)	30.9	17.3
Total adjustments		6.2	272.8	(65.2)
Net income/(loss) in accordance with US GAAP		5.7	(777.9)	(829.2)

(1) Restated for revenue recognition, see Note 34 of Notes to the Financial Statements.

(2) Restated for the adoption of FRS 17 and UITF 38.

Newly Adopted Accounting Standards

UK Standards

We have implemented FRS 17 "Retirement Benefits" at December 31, 2003 to bring us in line with latest UK GAAP and to move towards the adoption of International Financial Reporting Standards in 2005. Prior year amounts have been restated to reflect the change in accounting policy. Under FRS 17 profit before taxation for 2003 is £0.6 million higher than it would have been under Statement of Standard Accounting Practice ("SSAP") 24. Under FRS 17 £1.5 million of the pension charge for 2003 has been classified as other finance expense. Actuarial changes are recorded in the statement of total recognized gains and losses. A pension fund liability net of deferred taxes at December 31, 2003 of £35.2 million (2002 £46.2 million) is reflected in the balance sheet.

The Group has also implemented UITF Abstract 38 "Accounting for ESOP Trusts" which requires that the cost of own shares, previously reported as a fixed asset investment, be shown as a deduction from shareholders' funds. A prior year adjustment has been made to reflect this change.

US Standards

For purposes of the US GAAP reconciliations presented in Note 34 of Notes to the Financial Statements and above, the following new US accounting standards have been implemented:

In June 2001, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 143, "Accounting for Asset Retirement Obligations" ("SFAS No. 143"). SFAS No. 143 addresses financial accounting and reporting for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. SFAS No. 143

applies to legal obligations associated with the retirement of long-lived assets that result from the acquisition, construction, development and the normal operation of a long-lived asset, except for certain obligations of lessees. SFAS No. 143 amends FASB Statement No. 19, "Financial Accounting and Reporting by Oil and Gas Producing Companies", and is effective for fiscal years beginning after June 15, 2002. The adoption of the provisions of SFAS No. 143, effective January 1, 2003, did not have a material impact on the financial position or results of operations of the Group.

In June 2002, the FASB issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities" ("SFAS No. 146"). SFAS No. 146 addresses financial accounting and reporting for costs associated with exit or disposal activities and nullifies Emerging Issues Task Force ("EITF") Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring)." The adoption of the provisions of SFAS No. 146, effective for exit or disposal activities initiated after December 31, 2002, did not have a material impact on the financial position or results of operations of the Group.

Impact of Recently Issued Accounting Standards Not Yet Adopted

UK GAAP

International Financial Reporting Standards

The Council of the European Union announced in June 2002 that listed companies would adopt International Financial Reporting Standards ("IFRS"), formerly known as International Accounting Standards, from January 1, 2005. The adoption of IFRS will be first reflected in the Group's financial statements for the half year ending June 30, 2005 and the year ending December 31, 2005.

The Company is in the process of assessing the impact the conversion to IFRS will have on the Group's financial statements and on its financial processes and systems.

It is a complex task to assess the differences between current accounting policies and IFRS, not least since many of the IFRS have only recently been revised, and it is clear that a number of accounting policies and some presentational aspects of the financial statements will continue to change. As a result it is not possible to quantify the impact at this time.

For the Spirent Group, the main areas which the Company anticipates will be impacted by the adoption of IFRS will be the reporting and treatment of amortization and impairment of goodwill and intangible assets, share based payments, deferred taxation and financial instruments.

US GAAP

Consolidation of Variable Interest Entities

In January 2003, the FASB issued Interpretation No. ("FIN") 46, Consolidation of Variable Interest Entities, an Interpretation of Accounting Research Bulletin No. 51, which requires a variable interest entity ("VIE") to be consolidated by its primary beneficiary. The primary beneficiary is the party that absorbs a majority of the VIE's expected losses and/or receives a majority of the expected residual returns.

In December 2003, the FASB revised FIN 46 ("FIN 46-(R)"), delaying the effective date for certain entities created before February 1, 2003 and making other amendments to clarify the application of guidance. In anticipation of the adoption of FIN 46-(R), the Group has identified and evaluated arrangements that may be subject to its provisions to determine whether they are VIEs.

The Group has adopted FIN 46 for entities created subsequent to February 1, 2003 as of December 31, 2003 and will adopt FIN 46-(R) for the year ending December 31, 2004. The adoption of FIN 46 did not result in the consolidation of any VIEs. The adoption of FIN 46-(R) is not expected to have a material impact on amounts reported under U.S. GAAP.

ITEM 15 CONTROLS AND PROCEDURES

As of December 31, 2003, we evaluated, under the supervision, and with the participation, of the Company's management, including the Chief Executive Officer and Chief Financial Officer, the effectiveness of the design and operation of the Group's disclosure controls and procedures (as defined in Exchange Act rules 13a-15(e) and 15d-15(e)). Based on that evaluation, the Company's management, including the Chief Executive Officer and Chief Financial Officer, concluded that the Group's disclosure controls and procedures were effective in all material regards to ensure that the information required to be disclosed in the reports the Company files and submits under the Exchange Act are recorded, processed, summarized and reported within the time periods specified in the rules and procedures of the SEC.

However, in 2004, as part of our on-going assessment of internal control over financial reporting, the Company's management, including the Chief Executive Officer and Chief Financial Officer, undertook a review of the controls over the Group's methods of revenue recognition in relation to certain complex arrangements with customers entered into in 2004 in the Service Assurance division of our Communications group. The terms of these arrangements with customers included, among other terms, ongoing customer support for hardware and software and the provision, in some instances, of product roadmaps, which contain expected release dates of planned updates and enhancements. The existence of a particular item on a roadmap does not, in itself, create a contractual obligation to deliver that item; however, under US GAAP an implied obligation is deemed to exist. In the light of this US GAAP requirement we conducted an extensive review of these arrangements with customers to determine whether the revenue had been correctly recognized in previous years in accordance with Statement of Position (SOP) 97-2 "Software Revenue Recognition" and related US GAAP. This further review covered how multiple-element arrangements with customers are accounted for under US GAAP and the basis for determining Vendor Specific Objective Evidence (VSOE) for each element. From this further review we concluded that, contrary to our prior determination, we did not have sufficient VSOE for certain elements of some of the multiple-element arrangements with customers in the Service Assurance division.

As a result of our review, we have restated, under US GAAP, the revenues and related costs arising from these arrangements as discussed more fully in note 34 of Notes to the Financial Statements. This has resulted in the Group restating its net income/(loss) and shareholders' equity under US GAAP in respect of the fiscal years 2001, 2002 and 2003. There are no changes to the Group's financial statements for any of the fiscal years 2001, 2002 and 2003 and related notes prepared in accordance with UK GAAP.

In conjunction with the decision to restate our financial statements, we have re-evaluated our internal controls over financial reporting. We have concluded that there was a material weakness in our internal control over financial reporting and disclosure controls and procedures at December 31, 2003 regarding the Group's selection and application of accounting policies in respect of revenue recognition under US GAAP. We are taking steps to further strengthen our internal control over financial reporting under US GAAP, in particular, our control processes and procedures over accounting for revenue recognition including employing specialized consultants, providing additional training and supplementing existing internal revenue recognition policies and procedures to clarify certain complex areas.

We believe the changes to controls mentioned above will be adequate to provide reasonable assurance that the objectives of these control systems will be met. However, because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues within the Company have been detected.

Change in Internal Control Over Financial Reporting

Except as disclosed above, there were no changes in the Company's internal control over financial reporting that occurred during the Company's last fiscal year that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

ITEM 18. FINANCIAL STATEMENTS

The following audited financial statements, together with the related auditors' reports and financial statement schedule of Spirent are filed as part of this annual report:

Financial Statements

ITEM 19. EXHIBITS

All exhibits except those marked * (which are exhibits to this Amendment) were filed as exhibits to our Registration Statement on Form 20-F filed with the SEC on June 27, 2001 or our Annual Reports on Form 20-F for the years ended December 31, 2003, December 31, 2002 or December 31, 2001 filed with the SEC and are incorporated herein by reference.