NATS (En Route) plc

Financial statements
for the year ended 31 March 2010

Company Number: 04129273

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Company Secretary

Andrew Picton

Registered office

5th Floor, Brettenham House South,
Lancaster Place, London WC2E 7EN

Registered in England and Wales
Company No. 04129273

Auditors

Deloitte LLP

This review presents a summary of the operating performance and results, financial position and cash flows of NATS (En Route) plc ("NERL") for the year ended 31 March 2010.

Highlights

- The company had another successful year of operational performance: it maintained its safety record; achieved its two-centre strategy by delivering the new Prestwick centre into service; and provided customers with good operational service.
- Average delay per flight was at an historical low of 4.3 seconds (2009: 19.3 seconds) and 99.5% of flights handled experienced no attributable delay.
- However, it was a challenging year financially because of the impact of the economic recession on traffic volumes, the increasing costs of staff pension benefits and the costs of restructuring the cost base.
- NERL handled 2.2m flights during the year, a decrease of 8.4% on last year. This was reflected in a 4.4% fall in revenues to £599.7m (2009: £627.1m).
- NERL reported a profit before tax of £75.1m (2009: £118.0m), before exceptional items. After exceptional items, profit before tax was £54.9m (2009: £66.8m).
- Net debt increased by £12.3m to £624.2m (2009: £611.9m) reflecting a modest increase in borrowings and a fall in cash balances.

Volcanic ash disruption

The eruption of the Eyjafjallajökull volcano in Iceland in April 2010, coupled with unseasonal winds, created an ash cloud which rose to 35,000 feet and covered much of the UK's controlled airspace. Through this period, we worked hard with others to ensure flights could resume safely and swiftly.

The urgency behind this imperative meant working around the clock with our safety regulator, the Civil Aviation Authority (CAA), the Met Office, the airlines, the government and the rest of Europe to learn more about the cloud which had covered much of the continent's airspace. In doing so, a new understanding of how to deal with this risk was developed, both technically, and operationally, to minimise the impact to our customers. Throughout this period of uncertainty all parties remained focused on the industry's priority: to resume operations whilst at all times ensuring safety.

The airspace restrictions meant a 21% reduction in flights for April 2010 alone (compared with 2009 figures) and the industry has suffered intermittent disruptions since then. This will have an impact on NERL's results for the year

ending 31 March 2011, with the cash shortfall estimated at around £10m, though the revenue loss will be c.£5m reflecting protections provided by the economic regulatory formula.

CP3 Review

Since the Public Private Partnership in 2001, NERL's charges have been economically regulated by the CAA. The CAA is currently reviewing NERL's charges for Control Period 3 (CP3), which starts in January 2011. As part of the CP3 review, the CAA agreed in 2009 to NERL's suggestion of 'Customer Consultation', by which NERL consulted customers on its draft business plan for CP3. This process has enabled NERL to develop a better understanding of customer requirements and offered deeper insights into their priorities for safety, service quality, flight efficiency and the environment, airspace capacity, investment and cost effectiveness. This consultation has helped to shape NERL's strategy in each of these areas. In addition to Customer Consultation, the CAA has scrutinised elements of NERL's draft business plan for CP3, including projected operating costs, pensions and capital expenditure using benchmarking and other techniques and has proposed a level of cost of capital.

The CAA published its proposals on charges in May 2010. For our UK en route business the CAA proposes a one-off price increase in January 2011 of 6.2% primarily to reflect higher pension costs and lower traffic than was assumed in CP2. From then on, prices would reduce by an average of some 4% each year for the next three years of CP3. For North Atlantic en route services, the CAA proposes a one-off price increase in January 2011 of 18.6% and then a similar average reduction of some 4% each year for the rest of CP3.

We welcome the CAA's recognition of our high level of performance and financial resilience in CP2 which reflects immense hard work and effort across the company; and we are pleased that the CAA has accepted our proposals for capital expenditure and pensions protection for all our employees in the defined benefit scheme.

We will study very carefully the CAA's methodology around their proposals on operating costs and cost of capital and respond accordingly during the consultation period.

Single European Sky

One of the major challenges that our industry faces is the Single European Sky (SES) initiative which aims to reform European air traffic control and improve the performance of the European aviation system. We are an active participant in, and strongly support, SES and believe that the performance improvements demanded by our customers are only possible

through co-operation with our European partners.

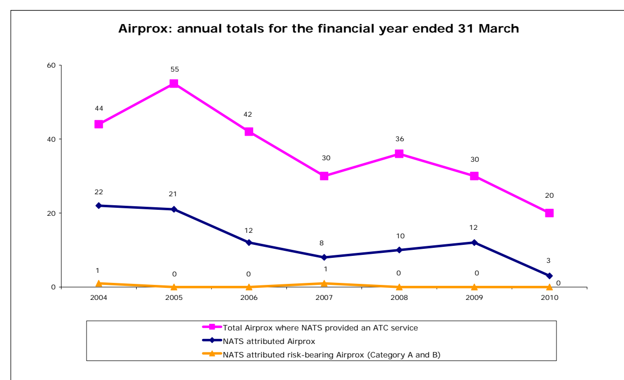
We are also playing an important role in SESAR (SES ATM Research) - the industry-wide programme to develop the new generation of air traffic management tools. The aim is to give Europe a high performance air traffic control infrastructure to deliver the SES goals in terms of performance, safety and sustainability.

It is vital that we play a leading role in influencing the outcome and we are well placed to lead on a number of important projects which make up SESAR, including the terminal manoeuvre area work package and the transverse package on the environmental component, which is a common thread running through the programme to deliver a 10% environmental efficiency improvement.

Proactive in Safety

Safety is at the heart of our business and our strategy remains to continue to improve our own safety performance, as well as playing a leading role in galvanising the industry to anticipate and prevent safety-related incidents. Our strategic targets are to achieve zero risk-bearing airprox and to reduce our safety risk index by 20% by March 2011 and then by 10% per year through the rest of CP3, with particular emphasis on the London Terminal Control operation and other safety hotspots. We have shared our strategic plan for safety with our customers and they support our plans. They agree that safety is our first and foremost priority and that the target will provide us with the momentum to ensure safety improvements against recovering traffic in future.

For the year, there were no risk-bearing airprox attributable to NERL. This result is testament to the continuing hard work of our operations and safety teams.



Note: Safety statistics for 2010 include NATS assessment of the outcome of the UK Airprox Board reviews

NERL continues to act beyond its remit to make lasting connections with the general aviation community as part of its commitment to being proactive in safety. In a bid to improve safety NERL has developed a low-cost, GPS-based navigation device for light aircraft called Aware. The tool gives pilots greater visibility of the boundaries of controlled airspace. This initiative should help drive down the risk of infringements in controlled airspace.

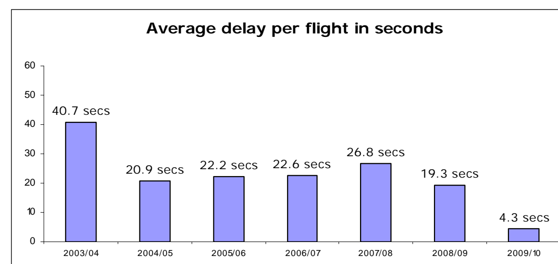
Another pioneering safety enhancement is the Callsign Confusion Identification Application (CCIA). This software

programme enables airlines to automatically filter out similar callsigns that could cause confusion and generates an alternative callsign before the aircraft takes off. NERL absorbed the cost of creating the software and has passed on the application to its customers, free of charge.

Tuned in to Customers and Driving Efficiency

Our focus continues to be on maintaining consistent service performance for our customers, implementing our capital investment programme with minimal disruption to this service and providing our service cost-effectively. Through Customer Consultation, NERL's customers re-affirmed these priorities. Customers require the low levels of delay achieved in 2010 to be sustained in future with a specific focus on early morning delay, long delays and day-to-day service consistency. To this end, we expect the CP3 review to establish performance metrics with demanding targets, including average delay per flight, a measure of the delay impact on customers (based on duration and time of day) and service consistency. The CAA's proposals include a proposed average delay per flight target of 12.5 seconds per flight, compared with 45 seconds for CP2 per flight.

For 2010, delay was at an historical low with just 4.3 seconds of air traffic related delay per flight, compared to 19.3 last year. This was achieved with improved operational performance but was also helped by lower traffic volumes.



We are also developing our contingency capability to ensure that service recovers quickly should we lose one of our two main centres, Swanwick in Hampshire or Prestwick in Ayrshire.

In May 2010 we completed a joint project with the military and airline customers and started providing an air traffic control service outside of controlled airspace. This service will be further developed in 2010 to enable us to operate up to 85% capacity within 48 hours of such a loss.

A major achievement for the year was the completion of our two-centre strategy when the doors opened to the new Prestwick Centre in January. Delivered on time and to budget, this project required the effort, professionalism and dedication of hundreds of people from across our business. Their significant contribution was formally recognised when HRH The Princess Royal opened the new centre in February. The opening of the new

Prestwick centre and closure of Manchester was achieved with minimal disruption to service and will provide operational synergies and economies of scale that will contribute to our overall efficiency in future, for the benefit of our customers.

We continued to make good progress with other key projects that will deliver cutting-edge tools into our operations rooms and control towers and increase efficiency.

Our project to introduce interim Future Area Control Tools Support (iFACTS) at Swanwick has reached a critical phase. This pioneering system will revolutionise the way we provide air traffic control by introducing automatic trajectory prediction and in doing so, deliver significant benefits both in terms of enhanced safety and a reduced controller workload. The system is now operating on certain sectors for a limited period of time and is on track for a launch in 2011.

NERL's strategic target for CP3 is to provide the lowest efficient cost base consistent with meeting customer and shareholder requirements. Its plans for CP3 include a target reduction in real unit operating expenditure of c. 2% per annum, compared to the projection for the year ending 31 March 2011. Over CP3 this represents cumulative savings in real terms for the four year period of c. £35m over a period when traffic levels are projected to increase. This will need to be considered in light of the CAA's May 2010 proposals.

During 2010, realising the severe difficulties that airline customers were experiencing in the current economic climate, NERL offered a three-fold response. First, a focus on service performance and minimising delay, which aids airline operations; second, continued cost efficiencies which will mean future prices are lower than they would otherwise be; and third, a one-off discount on the 2010 UK en route unit rate of £0.37 per chargeable service unit (depending on traffic volumes, this may be c. £3.7m). The discount was offset against the service performance bonus earned for the 2009 calendar year, recognising that a part of this performance related to lower traffic volumes.

Great Partners to Work With

It is clear that partnership is central to our environment strategy – to engage and influence industry partners. It is also at the heart of our safety strategy, our capital investment programme, and our response to SES and key to future business growth. We are often a unifying factor in a highly competitive industry and can act as a spur to enrol disparate interests.

Our work with the Irish Aviation Authority on Europe's first Functional Airspace Block (FAB) continues. The two businesses are working collaboratively to explore the potential of streamlining routes and making more efficient use of the UK and Irish airspace to deliver benefits to our airline customers in terms of fuel savings and reduced CO_2 emissions.

We have a strong partnership with Indra Sistemas of Spain, which has extensive experience of developing operational ATM systems, and with DFS and Aena, the German and Spanish air traffic controllers, in the development of the next generation flight data processing system (iTEC). This will help NERL support the vision of a single European sky by providing interoperability with our German and Spanish partners and other EU systems and by collaborating in this way we are able to share both the risks of development and the costs of the new system.

Our second biggest capital expenditure project, the 13-year programme to refurbish and replace our radar network reached its ten-year anniversary and is being carried out with Raytheon. By 2012, 23 radar sites will have been upgraded.

NERL prides itself on building strong relationships with industry partners to deliver advances in air traffic control.

Our ability to work collaboratively with other organisations was recognised in the year by The British Standards Institution (BSI).

Coupled with our active membership of CANSO (Civil Air Navigation Services Organisation) and ICAO (International Civil Aviation Organisation), the company's reach and influence now extends far beyond just the airspace it controls.

Acting Responsibly

When we became the world's first air traffic control organisation to set a target to reduce average ATM CO_2 emissions by an average of 10% per flight by 2020, it was seen by many in the industry as a daring step. However, this long-term project is now at the centre of our business planning and service provision with both our main centres working towards more environmentally friendly management of air traffic.

Customers have confirmed their very high priority for flight profiles that reduce fuel burn and emissions and strongly support our targets. This target represents potential fuel burn and financial savings for the airlines: a one per cent reduction in emissions across our network at today's fuel prices (and £/$ exchange rates) would mean today's fleet saving around £36m per year. NERL is committed to working with the

industry to turn this aspiration into a reality.

What is also clear is that the measurement and achievement of ATM environmental performance is still an emerging science and one our experts continue to work on. In the meantime, initiatives like night-time fuel-saving routes, allowing aircraft to fly more direct routes at quieter times, are already delivering an environmental benefit. We are also developing continuous climb departure profiles to contribute to the total benefit.

Our experts continue to engage with Sustainable Aviation (SA), the cross-industry effort which we helped to found. This coalition of UK airlines, airports, airframe and engine manufacturers and air traffic controllers was established in 2005 to address the future sustainability of the UK aviation industry. Its roadmap is to curb CO_2 emissions by 2050 to 2000 levels. SA's primary objective is to engage with policy makers and key influencers in order to ensure that aviation issues are taken seriously and factored properly and responsibly into environmental policy development.

NERL is also playing its part in helping the UK achieve its targets on renewable energy as part of a government initiative to work in partnership to solve obstacles to the construction of windfarms. Aviation – both military and civil – has been one of the principal objectors to large-scale projects because of the "clutter" effect wind turbines potentially cause on radar screens. Together with Raytheon, NERL is managing a contract for £5.2m awarded by government and industry, to research a software solution to mitigate this effect and, potentially, release planning restrictions on wind turbine proposals. In this area, we have gone from being one of the biggest obstacles to one of the central partners to unlocking the potential of this natural energy source.

Liberating and Inspiring People

Our performance stands or falls on the commitment, ingenuity and hard work of our people. We measure their engagement with the business each year through our talkback survey to which there was a healthy 66% response this year. Once again the results showed another good improvement, especially in relation to questions about how people are managed. Developing leadership and management capability continues to be a priority in order that we can deliver exceptional results through our people.

The company maintains a constructive relationship with its union colleagues and regards working together as important in maintaining good industrial relations. During the year, both parties agreed to strengthen the 'Working Together' relationships by introducing

specific training programmes for managers and union representatives to enhance understanding of industrial relations principles. In addition, we have also jointly established a key performance indicator that allows us to monitor the strength of this important relationship.

Overview of Financial Performance

The company's results for this and the last financial year included certain revenue and expense items that were material in terms of their size and incidence and which have been reported as exceptional items. The table below shows the underlying result, before these items, as well as the impact of these items on the result.

	2010 £m	2009 £m
Turnover	**599.7**	627.1
Operating profit		
- Operating profit before exceptional items	112.5	162.6
- Exceptional items	(20.2)	(51.2)
	92.3	111.4
Profit before taxation		
- Profit before tax and exceptional items	75.1	118.0
- Exceptional items	(20.2)	(51.2)
	54.9	66.8
Profit after tax		
- Profit after tax before exceptional items	55.6	85.1
- Exceptional items (net)	(14.5)	(50.5)
	41.1	34.6

The underlying result was a profit before tax of £75.1m (2009: £118.0m), £42.9m lower than last year, and reflects a challenging 2010 financial year. Revenues fell because of the impact of the economic recession on traffic volumes and operating costs increased due mainly to higher pension costs and a below inflation pay award. Pension cash contributions were also increased in the year and are set to rise further in future.

Our response to these factors has been to make significant reductions in operating costs, especially in non-operational areas. Non-controller headcount is planned to fall by 22% by the end of CP2, compared with the position at 31 March 2009, whilst maintaining our service to customers. In the year we achieved cost savings of £20m (most of which are sustainable) driven mainly by fewer staff and contractors. Further operating cost efficiencies are planned in CP3 for NERL leading to non-controller headcount reductions of up to a further 5%.

We have also strongly argued our case to the economic regulator and to its customers for the continued recovery of pension contributions through revenue allowances in CP3, given that we have taken all mitigating actions to control the cost and risks of the pension scheme through the reforms announced last year. The CAA's May 2010 proposals adopt NERL's March 2010 pension cost projections for CP3 and propose the continuation of the pass-through arrangements for CP3 for all employees currently enrolled in the defined benefit scheme.

In addition, mindful of the volatility and risk to revenues from the economic recession and other external factors

(most recently volcanic ash), the size of the pension scheme relative to that of the company and the previously high level of borrowings, NERL has been consistently strengthening its financial position over recent years and lowering its gearing to ensure that it remains robust to these challenges.

Exceptional items

The result for 2010 included: staff redundancy costs of £19.0m (2009: £25.2m) incurred in response to the economic downturn; £6.3m (2009: £26.0m) for the costs of relocating staff following site rationalisations; net of a refund of business rates for Swanwick of £5.1m relating to previous years.

	2010 £m	2009 £m
Redundancy costs	**(19.0)**	(25.2)
Relocation costs	**(6.3)**	(26.0)
Rates rebate	**5.1**	-
	(20.2)	(51.2)

Revenues

Overall traffic volumes were 8.4% lower than the previous year as airlines adjusted their flight schedules in response to the global economic slowdown.

	2010 ('000s)	2009 ('000s)	% change in year
Chargeable Service Units	**9,564**	10,601	(9.8%)
Chargeable Distance (km)	**693,702**	771,270	(10.1%)
Total UK traffic (flights):			
Domestic	**429**	470	(8.7%)
Transatlantic	**307**	336	(8.6%)
Other	**1,436**	1,566	(8.3%)
Total	**2,172**	2,372	(8.4%)
Oceanic traffic (flights)			
Total flights	**386**	416	(7.2%)

As a result, revenues fell by £27.4m to £599.7m (2009: £627.1m). Revenues are explained in more detail by business segment below.

Operating costs

Before exceptional items and asset-related charges, operating costs increased by £15.1m to £402.8m (2009: £387.7m). Operating costs for the year are analysed as follows:

	2010 £m	2009 £m
Before exceptional items:		
Employee costs	**(278.4)**	(256.9)
Services and materials	**(44.7)**	(46.0)
Repairs and maintenance	**(29.0)**	(25.1)
External research and development	**(0.3)**	(0.3)
Other operating charges (net)	**(50.4)**	(59.4)
	(402.8)	(387.7)
Depreciation, amortisation and impairment	**(86.1)**	(79.7)
Deferred grants	**1.7**	2.1
Profit on disposal of non-current assets	**-**	0.8
Operating costs	**(487.2)**	(464.5)

Employee costs of £278.4m (2009: £256.9m) increased by 8.4% on the previous year and accounted for 57% (2009: 55%) of the company's total operating costs. Through its cost savings programme the company reduced staff numbers, saving £8.7m in the year. The average number of staff employed during the year was 3,741 (2009: 3,913) and those in post at 31 March 2010 fell by 290 (7.4%) to 3,610 (2009: 3,900). Other staff cost savings of £2.3m were also achieved and a lower valuation for employee shares reduced costs further by £1.8m. However, these savings were more than offset by a higher charge (by £27.8m) for pensions (see below), due to a higher accrual rate (2010: 31.6% before salary sacrifice, 2009: 18.3%), and the costs of a below inflation pay award and salary progression of £8.4m.

Non-staff costs at £124.4m (2009: £130.8m) fell by £6.4m or 4.9%. reflecting the benefit of cost savings, including 55 fewer contractors, as well as lower charges for airline bad debts. These were partly offset by higher maintenance costs.

Depreciation, amortisation and impairment charges of £86.1m (2009: £79.7m) were £6.4m higher than the previous year, including charges relating to the new Prestwick Centre.

Net finance costs

Net finance costs, before exceptional items, at £37.4m (2009: £44.6m) were £7.2m lower than last year. This mainly reflected lower charges of £6.3m (2009: £11.5m) from marking to market the index-linked swap. The value of the latter is dependent on market expectations of inflation and gilt yields. Net interest payable was £2.0m lower than last year.

Taxation

The tax charge, before exceptional items, of £19.5m (2009: £32.9m) represents an effective rate of 26.0% (2009: 27.9%). This is lower than the headline rate of corporation tax of 28% due to research and development tax credits and deductions for the costs of a staff share award. After exceptional items, the tax charge of £13.8m (2009: £32.2m) represents an effective rate of 25.1% (2009: 48.2%).

Factors affecting the tax charge for the year are set out in note 10 to the accounts.

Dividends

In May 2010 the Board approved and paid an interim dividend for the year ending 31 March 2011 of £15m, to its parent company NATS Limited.

UK air traffic services

	2010 £m	2009 £m
Turnover	**577.5**	603.6
Operating costs	**(385.3)**	(368.4)
Depreciation, amortisation, impairment and deferred grants	**(80.6)**	(74.8)
Exceptional items	**(19.5)**	(50.2)
Operating profit	**92.1**	110.2
Chargeable Distance (millions km)	**693.7**	771.3
Chargeable Service Units (000)	**9,564**	10,601

UK air traffic services (UKATS) are provided by NERL and comprise UK en route services, services provided under contract with the MoD, London Approach services and services to North Sea helicopter operators. Revenues from these sources can be analysed as follows:

	2010 £m	2009 £m
UK en route services	**502.0**	527.0
Support services to MoD	**44.0**	44.9
London approach services	**8.3**	8.4
North Sea helicopters	**7.1**	7.3
	561.4	587.6
Services to other group companies	**16.1**	16.0
	577.5	603.6

Income from UK en route services, which are provided to traffic operating in those parts of UK airspace which constitute controlled airspace, decreased by £25.0m in the year to £502.0m (2009: £527.0m) mainly due to the

significant reduction in volume of air traffic handled (down 10.1% to 693.7m kilometres flown). The volume impact was offset in part by higher charges which, for calendar year 2009, were derived from higher RPI in August 2008 built into the annual adjustment to charges under the RPI minus "X" economic regulatory formula.

The volume risk sharing mechanism in the economic regulatory formula has provided some protection against the traffic downturns, enabling NERL to recover 50% of the shortfall below a regulatory baseline through an upward revision to charges for the subsequent year. This mechanism also provides for further protection against even more severe traffic downturns. No protection is provided against deflation, with charges from 1 January 2010 being based on August 2009 RPI of -1.3%.

NERL recognised a service performance bonus in the year of £6.4m (2009: £6.9m), which was net of the estimated discount to NERL's regulatory price cap, explained above.

London Approach services, which are provided to aircraft arriving at or departing from Heathrow, Gatwick and Stansted airports, generated £8.3m (2009: £8.4m). Revenues from these services are combined with those from UK en route services and capped by the economic regulatory formula. The specific charge for London Approach is levied based on aircraft landed tonnage. Landed tonnage decreased by 5.1% to 51.1m tonnes (2009: 53.9m tonnes). This effect was partly offset by a 1 pence rate increase to 21 pence per tonne for aircraft weights up to 100 tonnes. The charge per tonne for aircraft weights above 100 tonnes remained at 8 pence.

NERL has a contract to provide services and support infrastructure to the MoD for military air traffic services. Revenues generated under the contract amounted to £44.0m (2009: £44.9m) with the decrease reflecting the sharing of operating cost savings under the contract.

Charges for services to North Sea helicopter operators are levied on the basis of a charge per round trip flight. Revenues fell by £0.2m to £7.1m (2009: £7.3m), reflecting a fall in the volume handled to 37,335 (2009: 40,728), which was partly offset by an increase in the rate charged.

The costs of UK air traffic services, including asset-related charges and exceptional items, fell by £8.0m to £485.4m (2009: £493.4m) as the benefit of operating cost savings, lower charges for staff restructuring and a rebate of business rates offset the impact of higher pension costs and asset depreciation.

Overall, UK air traffic services generated an operating profit of £92.1m (2009: £110.2m), £18.1m lower than the prior year.

North Atlantic air traffic services

	2010 £m	2009 £m
Turnover	**22.2**	23.5
Operating costs	**(17.5)**	(18.5)
Depreciation, amortisation, impairment and deferred grants	**(3.8)**	(2.8)
Exceptional items	**(0.7)**	(1.0)
Operating profit	**0.2**	1.2
Total flights (000)	**386**	416
Chargeable flights (000)	**386**	414

North Atlantic air traffic services are en route services provided by NERL in the Shanwick Oceanic Control Area (part of the North Atlantic where the UK provides navigation services by international agreement and where communications are provided by the Republic of Ireland). The charges for these services are levied on a per flight basis and are subject to a separate economic regulatory formula that allows for the annual adjustment of prices by the movement in the RPI less a specified percentage. Revenues at £22.2m (2009: £23.5m) were £1.3m lower than the prior year. Flight volumes fell by 6.6% to 386,118 (2009: 413,600) and more than offset a 0.8% increase in price controlled rate per flight from £55.73 to £56.18. The rate per flight for 2011 is £53.20, reflecting the effect of deflation when applied to the economic regulatory formula.

Costs, including asset-related charges and exceptional items, fell by £0.3m to £22.0m (2009: £22.3m) due mainly to lower staff numbers and economies of scale following the transfer of operations to Prestwick.

Overall, North Atlantic air traffic services generated an operating profit of £0.2m, £1.0m lower than the previous year (2009: £1.2m).

Balance sheet

The company's balance sheet can be summarised as follows:

	2010 £m	2009 £m
Goodwill	**351.0**	351.0
Tangible and intangible fixed assets	**817.0**	765.5
Other non-current assets	**1.0**	1.4
Cash and short term deposits	**79.6**	83.4
Other net current assets/(liabilities)	**16.2**	(10.8)
Derivatives	**(87.3)**	(82.5)
Pension scheme surplus/(deficit)	**59.7**	(51.8)
Borrowings	**(703.8)**	(695.3)
Provisions and other non-current liabilities	**(137.3)**	(92.4)
Net assets	**396.1**	268.5

Shareholders' funds increased by £127.6m from £268.5m last year. This increase was primarily due to retained profit of £41.1m and the improvement in the pension scheme's financial position of £80.3m (net of deferred tax) as measured on an accounting basis – see below.

The increase in other net current assets/(liabilities) reflects higher accrued UK en route income. The fair value liability of derivative financial instruments increased in the year principally due to the change in the mark to market of the index-linked swap. The valuation of the swap is driven primarily by market expectations

of future inflation, which have increased since the prior year, leading to an increase in expected payments under the swap contract.

Provisions and other non-current liabilities of £137.3m (2009: £92.4m) include deferred tax provisions which, at £131.2m, were £49.9m higher than the prior year mainly due to the increase in the valuation of the pension fund.

Changes in intangible and tangible fixed assets, pensions and cash and borrowings are explained below.

Capital expenditure

The company invested £137.7m in the year, £8.3m less than the previous year, in the following areas:

	2010 £m	2009 £m
Airspace development	5.4	3.4
Business systems	4.5	4.6
Future centres programme	55.0	47.2
Communications, navigation and surveillance	6.5	8.4
Radar site services	12.2	13.8
Current software systems	29.2	35.3
Prestwick/Manchester programme	24.4	31.7
Swanwick/West Drayton programme	-	0.4
Other	0.5	1.2
Total	137.7	146.0

The company continued to increase investment in its future centres systems which include: the development of the next generation flight data processing system which will be compatible with European systems; the interim future area control tools based on trajectory prediction and conflict detection; and Electronic Flight Data which replaces paper flight data strips by electronic strips. The company also incurred further significant expenditure in completing the final stages of the new Prestwick centre and related systems, the development of voice communication systems and the ongoing development of its operational platforms. Airspace developments included the provision of air traffic services outside of controlled airspace and an improved contingency capability.

Pensions

At 31 March 2010, measured under international accounting standards requiring best estimate assumptions, the company's share of the NATS group's pension scheme was a surplus, with assets exceeding liabilities by £59.7m. This compared with its share of a deficit of £51.8m at 31 March 2009. The increase in the valuation was mainly due to the performance of the scheme's investments, with the company's share of these being £539m higher, reflecting the rise in global stock markets over the year. This effect was partly offset by an increase in its share of pension obligations of £427m due to a reduction in the discount rate to 5.65% from 6.4%.

The pension scheme actuary's triennial valuation performed as of 31 December 2009 was approved by Trustees on 27 April 2010. This valuation, which is for funding purposes, uses assumptions which include a margin for prudence and leads to a lower valuation than under international accounting standards. The

valuation reported a deficit of £351.1m in scheme assets to liabilities (equivalent to a funding ratio of 89%) and a future service cost of 36.7%. NERL's share of this deficit is c.75% or £263m. The future service cost represents a reduction on the rate reported at the 31 December 2006 valuation (of 37.3%), reflecting the benefit of pension reforms introduced in 2009, which included limiting increases in pensionable pay to RPI plus 0.5%.

During the year the company paid cash contributions to the scheme of £79.5m (2009: £52.0m). This amount included £12.0m (2009: £nil) of wages and salaries sacrificed by employees in return for pension contributions. Excluding the effect of salary sacrifice, employer cash contributions were paid at a rate of 27.5% (2009: 22.0%) of pensionable pay. The company is increasing these cash contributions from May 2010 to 36.7% of pensionable pay, equivalent to the future service cost. In response to the triennial valuation, the company has also agreed a deficit recovery plan with Trustees and from January 2011 it will make further contributions of c.£1.5m per month (for calendar year 2011), increasing these by 3.5% each January thereafter.

Treasury management

The gross borrowings of the company at £703.8m were £8.5m higher than the previous year (2009: £695.3m). Cash and short-term investments fell by £3.8m to £79.6m (2009: £83.4m). Overall, net debt increased by £12.3m to £624.2m (2009: £611.9m).

Movements in net debt

	Cash and short term investments	Borrowings	Net debt
	£m	£m	£m
Balance at 31 March 2009	83.4	(695.3)	(611.9)
Cash flow	(3.7)	(7.9)	(11.6)
Short term investments	(0.1)	-	(0.1)
Non-cash movements:	-	(0.6)	(0.6)
Balance at 31 March 2010	**79.6**	**(703.8)**	**(624.2)**

Cash flow

Overall, the company's balance of cash and cash equivalents fell by £3.7m in the year to £64.1m (2009: £67.8m).

	2010 £m	2009 £m
Cash generated from operations	**158.0**	181.6
Taxation	**(0.1)**	(14.4)
Net cash from operating activities	**157.9**	167.2
Interest received	**1.1**	4.5
Capital expenditure	**(139.1)**	(140.3)
Sales of property, plant and equipment	**0.1**	1.0
Change in short-term investments	**0.1**	1.6
Net cash outflow from investing activities	**(137.8)**	(133.2)
Interest paid	**(34.8)**	(39.6)
Interest received on derivative financial instruments	**3.4**	3.4
Bank drawings and other loans	**10.6**	(0.3)
Inter-company loan	**(3.0)**	3.4
Dividends paid	**-**	(9.1)
Net cash outflow from financing costs	**(23.8)**	(42.2)
Decrease in cash and equivalents	**(3.7)**	(8.2)

Net cash from operating activities at £157.9m was £9.3m lower than 2009 (2009: £167.2m) and remains robust. The reduction was mainly due to the effects of lower traffic levels on cash receipts, higher cash contributions to the pension scheme and higher staff redundancy and relocation payments, offset in part by lower tax payments.

Cash outflows from investing activities were funded by operating cash flows. Capital expenditure outflows were slightly lower than previously. Net cash outflows from financing activities were

lower at £23.8m (2009: £42.2m), reflecting the payment of a dividend in 2009.

Risks and uncertainties

The principal operational risks and uncertainties of the company are described in the business review above. Specifically, these are:

- the risk of aircraft collision;
- a loss of service from an air traffic control centre;
- the pension scheme's funding position;
- industrial relations;
- the "Single Skies" European regulatory framework;
- the delivery of capital investment projects;
- the outcome of NERL's CP3 review; and
- the security of assets and systems.

The main financial risks of the company relate to the availability of funds to meet business needs (including meeting obligations to the pension scheme), the risk of default by counter-parties to financial transactions, and fluctuations in interest and foreign exchange rates. The Treasury function is mandated by the Board to manage the financial risks that arise in relation to underlying business needs. The function has clear policies and operating parameters, and its activities are routinely reviewed and agreed by the Treasury Committee. The function does not operate as a profit centre and the undertaking of speculative transactions is not permitted.

The main risks arising from the company's financing activities are set out below:

- ♦ currency risk: the company's objective is to reduce the effect of exchange rate volatility on short-term profits. Transactional currency exposures that could significantly impact the Income Statement are hedged, typically using forward sales of foreign currencies. The company's most significant currency exposure arises because UK en route charges, which contribute 83% (2009: 84%) of total turnover, are set in sterling but are billed and collected in euro by applying a conversion rate determined monthly by Eurocontrol, which administers the UK en route revenue collection. The resultant currency risk is materially eliminated by entering into forward foreign exchange contracts. At the year end, forward foreign currency transactions entered into to buy and sell sterling, designated as cash flow hedges, equivalent to £83.0m (net) were outstanding (2009: £66.9m net) as detailed in note 18.
- ♦ interest rate and inflation risk: the group's policy is to achieve an efficient mix of funding at fixed rates of interest, floating rates of interest

and rates indexed to retail prices. NERL's strategy is to hedge net debt in order to reduce its exposure to interest rate risk on its cash holdings.

To achieve an economic hedge of NERL's regulated revenue, most of which is linked to the movement in the retail price index ("RPI"), an index-linked swap with a notional principal of £200m was entered into in August 2003 whereby NERL receives fixed interest and pays interest at a rate adjusted for the movement in RPI. The swap does not qualify for hedge accounting under IFRS and is classified as held for trading. As such, movements in the fair value are taken to the Income Statement.

As at 31 March 2010 (after derivatives), approximately 94.7% (2009: 96.7%) of NERL's net debt was either at fixed rates or at rates indexed to inflation.

- counterparty risk: as at 31 March 2010 the company had cash and deposits (shown as short-term investments) totalling £79.6m (2009: £83.4m). To minimise risk, funds may only be invested in high quality liquid investments. Credit risk associated with the investment of surplus funds (and from the use of interest rate and currency hedging derivatives) is managed by setting limits for counterparties based on their credit rating. An aggregate limit has also been established for each counterparty.
- liquidity risk: in addition to undrawn committed bank facilities totalling £126.9m, as at 31 March 2010 the company had cash and short-term deposits totalling £79.6m. Included in cash of £64.1m is a liquidity reserve account balance of £21.3m held to provide liquidity in the event of certain pre-defined circumstances, particularly to ensure compliance with financial covenants. The short-term deposit of £15.5m represents a debt service reserve account to fund interest and fees scheduled for payment in the 6 months ending 30 September 2010. The company's policy is to hold free cash equivalent to between one and two months' of projected UK en route services revenue (of between £43m and £86m) for the year ending 31 March 2011 and to use surplus cash to reduce borrowings.
- funding risk: the policy of the company is to ensure that committed funding is available at a competitive cost to meet its anticipated needs for the period covered by its business plan. This is achieved by maintaining a portfolio of debt diversified by source and maturity and ensuring it has access to long-term funding to finance its long-term assets. Hence, the company's borrowings include a £600m amortising bond issued by

NERL with a final maturity date of 2026 and bank facilities totalling £216.2m of which £11m matures in 2010, £34.25m in 2011 and c. £170.95m in 2012.

Going concern

The company's business activities, together with the factors likely to affect its performance and the financial position of the company, its cash flows, liquidity position and borrowings are set out in the Business and Financial Review above. In addition, note 18 to the financial statements describes the company's objectives, policies and processes for managing its capital; its financial risk management objectives; details of its financial instruments and hedging activities; and its exposure to credit risk and liquidity risk.

The company has significant undrawn committed bank facilities, the majority of which do not expire until 2012, and adequate levels of cash holdings. The company's forecasts and projections, taking account of reasonably possible changes in trading performance and the company's view of the outcome of the CP3 review of its charges, show that the company should be able to operate within the level of its existing facilities. The UK en route business also benefits from some protections against traffic volume risk afforded by its regulatory charge control conditions. Other sources of income are generated mainly from long-term contracts. The company is also actively seeking to reduce its operating cost base through the cost saving programmes described above to provide mitigation for future revenue shortfalls and cost pressures from legacy pension arrangements. As a result, the directors believe that the company is well placed to manage its business risks successfully despite the uncertain current economic outlook.

After making enquiries, the directors have formed a judgement that taking into account the financial resources available to the company, it has adequate resources to continue to operate for the foreseeable future and have therefore adopted the going concern basis in the preparation of the financial statements for the year ended 31 March 2010.

Ian Mills
Managing Director, NERL

Report of the directors

The directors present their report and audited accounts for the year ended 31 March 2010.

Principal activities and business review

The company's principal activity is the provision of air traffic services in the UK.

On 26 July 2001, the company's parent, National Air Traffic Services Limited, now NATS Limited, (NATS) hived down certain of its assets and liabilities to the company under a statutory transfer scheme established under the Transport Act 2000 to implement the Public Private Partnership (PPP) of NATS. The company commenced trading on 1 August 2001.

The company is subject to regulation in accordance with the Air Traffic Services Licence which was originally issued in March 2001 and has been modified on a number of occasions. The company generates revenues from UK air traffic services and North Atlantic air traffic services. The former comprises domestic en route services charged by Eurocontrol based on chargeable service units (a function of average weight of the aircraft and distance flown through UK airspace), support services provided to the Ministry of Defence, London Approach services and services provided to North Sea Helicopters.

The directors consider that the year-end financial position was satisfactory and that the company is well placed to develop its activities in the foreseeable future.

A review of the company's activities and performance during the year, including key performance indicators and comments on principal risks and uncertainties, is contained in the Business and Financial Review on pages 1–17.

Results and dividends

The results for the period are shown in the income statement on page 24. The board recommends a final dividend of £nil (2009: interim dividend of £9.1m).

In May 2010 the board approved and paid an interim dividend for the year ending 31 March 2011 of £15m to the company's parent, NATS Limited.

Use of financial instruments

The company uses financial instruments to manage financial risk. The accounting policies and notes to the financial statements, set out below, explain the financial risk management objectives and policies of the company and describe exposures to credit and other risks.

Employees

Contracts of employment with staff are held by the company's parent company, NATS. NATS continues its commitment to the involvement of employees in the decision making process through effective leadership at all levels in the organisation. Staff are frequently involved through direct discussions with their managers, cross company work groups and local committees. Regular staff consultations cover a range of topics affecting the workforce, including such matters as unit and corporate performance and business plans. The NATS CEO maintains high visibility with staff through annual visits to each NATS location where he talks to them about current business issues and takes questions in an open and straightforward manner. Also, employees views are represented through an open dialogue with Prospect and the Public and Commercial Services Union (PCS), the recognised unions on all matters affecting employees. This has been enhanced through the 'Working Together' programme aimed at working towards partnership principles as the basis for our relationship. Formal arrangements for consultation with staff exist through a local and company-wide framework agreed with the Trade Unions.

It is NATS' policy to establish and maintain competitive pay rates which take full account of the different pay markets relevant to its operations. In return, employees are expected to perform to the required standards and to provide the quality and efficiency of service expected by its customers.

NATS is an equal opportunities employer. Its policy is designed to ensure that no applicant or employee receives less favourable treatment than any other on the grounds of sex, age, disability, marital status, colour, race, ethnic origin, religious belief or sexual orientation, nor is disadvantaged by conditions or requirements applied to any post which cannot be shown to be fair and reasonable under relevant employment law or codes of practice.

NATS is also committed to improving employment opportunities for disabled people. The company will continue to promote policies and practices which provide suitable training and retraining and development opportunities for disabled staff, including any individuals who become disabled, bearing in mind their particular aptitudes and abilities and the need to maintain a safe working environment.

NATS strives to maintain the health and safety of employees through an appropriate culture, well-defined processes and regular monitoring. Line managers are accountable for ensuring health and safety is maintained; responsibility for ensuring compliance with both legal requirements and

company policy rests with the HR Director.

Policy and practice on payment of creditors

It is the company's policy to pay suppliers within the payment terms of the contract, which is normally 30 to 60 days, based upon the timely receipt of an accurate invoice.

The average number of days taken to pay suppliers calculated in accordance with the requirements of the Companies Act 2006 is 44 days (2009: 38 days).

Directors and their interests

The directors of the company who served during the year and to the date of this report are set out below:

John Devaney
Paul Barron (resigned 31 March 2010)
Richard Deakin (appointed 1 April 2010)
Nigel Fotherby
Ian Hall
Lawrence Hoskins (resigned 30 April 2010)
Ian Mills

None of the directors had any interests in the share capital of the company. The following directors held interests in ordinary shares of the company's parent undertaking NATS Holdings Limited at 31 March 2010: Nigel Fotherby - 1,977; Ian Hall - 1,977; Lawrence Hoskins – 200 and Ian Mills – 200.

None of the directors has, or has had, a material interest in any contract of significance in relation to the company's business.

Directors' responsibilities

The Directors are responsible for preparing the Annual Report and the accounts. The Directors have prepared the accounts for the company in accordance with International Financial Reporting Standards (IFRS).

International Accounting Standard 1 requires that financial statements present fairly for each financial year the company's financial position, financial performance and cash flows. This requires the faithful representation of the effects of transactions, other events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the International Accounting Standards Board's 'Framework for the preparation and presentation of financial statements'. In virtually all circumstances, a fair presentation will be achieved by compliance with all applicable International Financial Reporting Standards.

Directors are also required to:

- properly select and apply accounting policies;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;

- provide additional disclosures when compliance with the specific requirements in IFRS is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance; and
- prepare the financial statements on the going concern basis, unless it is inappropriate to presume that the company will continue in business.

The Directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the company, for safeguarding the assets, for taking reasonable steps for the prevention and detection of fraud and other irregularities and for the preparation of a Directors' report which comply with the requirements of the Companies Act 2006.

Each of the Directors at the date of approval of this report confirms that so far as the director is aware, there is no relevant audit information of which the company's auditors are unaware; and the director has taken all the steps that he ought to have taken as a director in order to make himself aware of any relevant audit information and to establish that the company's auditors are aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of s418 of the Companies Act 2006.

The financial statements have been prepared on a going concern basis, as explained in note 2 to the accounts.

Auditors

Deloitte LLP have expressed their willingness to continue in office as auditors and a resolution to reappoint them will be proposed at the Annual General Meeting.

By order of the Board

Andrew Picton
Secretary
1 July 2010

Registered office

5th Floor, Brettenham House South,
Lancaster Place, London WC2E 7EN

Registered in England and Wales
Company Number: 04129273

Independent auditors' report to the members of NATS (En Route) plc

We have audited the financial statements of NATS (En Route) plc for the year ended 31 March 2010 which comprise the Income Statement, the Statement of Comprehensive Income, the Balance Sheet, the Statement of Changes in Equity, the Cash Flow Statement and the related notes 1 to 27. The financial reporting that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

As explained more fully in the directors' responsibilities statement, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view.

Our responsibility is to audit the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's (APB's) Ethical Standards for Auditors.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of whether the accounting policies are appropriate to the company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements.

Opinion on the financial statements

In our opinion:

- the financial statements give a true and fair view of the state of the company's affairs as at 31 March 2010 and of its profit for the year then ended;
- the financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the company's financial statements, Article 4 of the IAS Regulation.

Separate opinion in relation to IFRS as issued by the IASB

As explained in note 2 to the financial statements, the company in addition to complying with its legal obligation to comply with IFRSs as adopted by the European Union, has applied IFRSs as issued by the International Accounting Standards Board (IASB).

In our opinion the financial statements comply with IFRSs as issued by the IASB.

Opinion on other matters prescribed by the Companies Act 2006

In our opinion:

- the information given in the Report of the Directors for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which we are required to report by exception

We have nothing to report in respect of the following:

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- adequate accounting records have not been kept by the company; or
- the company's financial statements are not in agreement with the accounting records and returns; or
- we have not received all the information and explanations we require for our audit.

John Clennett (Senior Statutory Auditor)
For and on behalf of Deloitte LLP
Chartered Accountants and Statutory Auditors
Southampton, United Kingdom
1 July 2010

Income statement

for the year ended 31 March 2010

	Notes	Year ended 31 March 2010 Before exceptional items £m	Exceptional items (Note 6a) £m	Total £m	Year ended 31 March 2009 Before exceptional items £m	Exceptional items (Note 6a) £m	Total £m
Revenue	4	599.7	-	599.7	627.1	-	627.1
Staff costs	7	(278.4)	(19.0)	(297.4)	(256.9)	(25.2)	(282.1)
Services and materials		(44.7)	5.1	(39.6)	(46.0)	-	(46.0)
Repairs and maintenance		(29.0)	-	(29.0)	(25.1)	-	(25.1)
External research and development		(0.3)	-	(0.3)	(0.3)	-	(0.3)
Depreciation, amortisation and impairment	6b	(86.1)	-	(86.1)	(79.7)	-	(79.7)
Profit on disposal of non-current assets		-	-	-	0.8	-	0.8
Other operating charges		(50.4)	(6.3)	(56.7)	(59.8)	(26.0)	(85.8)
Other operating income		-	-	-	0.4	-	0.4
Deferred grants released	6b	1.7	-	1.7	2.1	-	2.1
Net operating costs		(487.2)	(20.2)	(507.4)	(464.5)	(51.2)	(515.7)
Operating profit/(loss)	6	112.5	(20.2)	92.3	162.6	(51.2)	111.4
Investment revenue	8	1.2	-	1.2	4.7	-	4.7
Finance costs	9	(38.6)	-	(38.6)	(49.3)	-	(49.3)
Profit/(loss) before tax		75.1	(20.2)	54.9	118.0	(51.2)	66.8
Tax	10	(19.5)	5.7	(13.8)	(32.9)	0.7	(32.2)
Profit/(loss) for the year attributable to equity shareholders		55.6	(14.5)	41.1	85.1	(50.5)	34.6

All revenue and profit from operations have been derived from continuing operations.

Statement of comprehensive income

for the year ended 31 March 2010

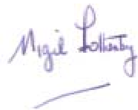
	Notes	Year ended 31 March 2010 £m	Year ended 31 March 2009 £m
Profit for the year after tax		41.1	34.6
Other comprehensive income/(expense) for the year net of tax			
Actuarial gain/(loss) on defined benefit pension scheme	24	119.8	(370.1)
Change in fair value of hedging derivatives		1.5	2.5
Transfer to income statement on cash flow hedges		(1.1)	(1.7)
Deferred tax relating to components of other comprehensive income/(expense)	20	(33.7)	103.4
		86.5	(265.9)
Total comprehensive income/(expense) for the year attributable to equity shareholders		127.6	(231.3)

Balance sheet
at 31 March 2010

	Notes	2010 £m	2009 £m
Non-current assets			
Goodwill	12	351.0	351.0
Other intangible assets	13	199.8	149.8
Property, plant and equipment	14	617.2	615.7
Retirement benefit asset	24	59.7	-
Trade and other receivables	15	1.0	1.4
		1,228.7	1,117.9
Current assets			
Trade and other receivables	15	129.8	114.1
Short term investments	18	15.5	15.6
Cash and cash equivalents	18	64.1	67.8
Derivative financial instruments	17	0.8	-
		210.2	197.5
Total assets		1,438.9	1,315.4
Current liabilities			
Trade and other payables	19	(113.1)	(121.9)
Borrowings	16	(0.5)	(1.2)
Current tax liabilities		(0.5)	(3.0)
Derivative financial instruments	17	(88.1)	(82.5)
		(202.2)	(208.6)
Net current assets/(liabilities)		8.0	(11.1)
Non-current liabilities			
Borrowings	16	(703.3)	(694.1)
Trade and other payables	19	(6.1)	(11.1)
Retirement benefit obligations	24	-	(51.8)
Deferred tax liability	20	(131.2)	(81.3)
		(840.6)	(838.3)
Total liabilities		(1,042.8)	(1,046.9)
Net assets		396.1	268.5
Equity			
Called up share capital	21	10.0	10.0
Hedge reserve		0.5	0.2
Special reserves		33.7	33.7
Other reserves		24.8	31.0
Retained earnings		327.1	193.6
Total equity		396.1	268.5

The financial statements (Company No. 04129273) were approved by the Board of directors and authorised for issue on 1 July 2010 and signed on its behalf by

Chairman John Devaney

Finance Director  Nigel Fotherby

Statement of changes in equity

for the year ended 31 March 2010

	Equity attributable to equity holders of the Company					
	Share capital £m	Special reserve £m	Hedge reserve £m	Other reserves £m	Retained earnings £m	Total £m
At 1 April 2008	10.0	33.4	(0.4)	37.4	428.5	508.9
Profit for the year	-	-	-	-	34.6	34.6
Other comprehensive income/(expense) for the year net of tax	-	0.3	0.6	(6.4)	(260.4)	(265.9)
Total comprehensive income/(expense) for the year	-	0.3	0.6	(6.4)	(225.8)	(231.3)
Dividends paid	-	-	-	-	(9.1)	(9.1)
At 31 March 2009	10.0	33.7	0.2	31.0	193.6	268.5
At 1 April 2009	10.0	33.7	0.2	31.0	193.6	268.5
Profit for the period	-	-	-	-	41.1	41.1
Other comprehensive income/(expense) for the period	-	-	0.3	(6.2)	92.4	86.5
Total comprehensive income/(expense) for the year	-	-	0.3	(6.2)	133.5	127.6
At 31 March 2010	10.0	33.7	0.5	24.8	327.1	396.1

Other reserves arose on completion of the PPP transaction in July 2001. The special reserve arose from a capital reduction in May 2003.

Cash flow statement

for the year ended 31 March 2010

	Notes	Year ended 31 March 2010 £m	Year ended 31 March 2009 £m
Net cash inflow from operating activities	22	157.9	167.2
Cash flows from investing activities			
Interest received		1.1	4.5
Purchase of property, plant and equipment and other intangible assets		(139.1)	(140.3)
Sales of property, plant and equipment		0.1	1.0
Changes in short term investments		0.1	1.6
Net cash outflow from investing activities		(137.8)	(133.2)
Cash flows from financing activities			
Interest paid		(34.8)	(39.6)
Interest received on derivative financial instruments		3.4	3.4
Bank and other loans		10.6	(0.3)
Inter-company loan		(3.0)	3.4
Dividends paid		-	(9.1)
Net cash outflow from financing activities		(23.8)	(42.2)
Decrease in cash and cash equivalents during the year		(3.7)	(8.2)
Cash and cash equivalents at 1 April		67.8	76.0
Cash and cash equivalents at 31 March		64.1	67.8
Net debt (representing borrowings net of cash and short term investments)		(624.2)	(611.9)

1 General information

NATS (En Route) plc is a company incorporated in England and Wales and domiciled in the United Kingdom and acting under the Companies Act 2006. The address of the registered office is on page 21. The nature of the company's operations and its principal activities are set out in the Report of the Directors and in the business and financial review.

These financial statements are presented in pounds sterling because that is the currency of the primary economic environment in which the company operates.

2 Accounting policies

The following accounting policies have been applied consistently in dealing with items which are considered material in relation to the company's financial statements.

Basis of preparation and accounting

The financial statements have been prepared on the going concern basis (see page 17). The financial information has been prepared in accordance with International Financial Reporting Standards (IFRSs). The financial statements have also been prepared in accordance with IFRSs and International Financial Reporting Interpretation Committee (IFRIC) interpretations as endorsed by the European Union and therefore the financial statements comply with Article 4 of the EU IAS Regulation.

Two interpretations issued by the International Financial Reporting Interpretations Committee become effective for this period. These are: IFRIC 13: *Customer Loyalty Programmes* and; IFRIC 15: *Agreements for the Construction of Real Estate.* The adoption of these Interpretations has not led to any changes in the company's accounting policies.

In addition, the company adopted IAS 1 (Revised): *Presentation of Financial Statements* for the first time. This has resulted in a number of changes in presentation and disclosure. The revised presentation requirements of IAS 1 permit a choice of presenting one or two performance statements; the company has elected to present two statements. The Statement of Changes in Equity is now presented as a primary statement. The revised standard has no impact on the reported results or financial position of the company. The company also adopted IFRS 7 (Revised): *Financial instruments: Disclosures*. The impact of the revised standard is additional disclosures on the fair value measurement and liquidity risk within notes 17 and 18. The company also adopted IAS 23 (Revised): *Borrowing Costs.* Previously the company adopted the option to expense borrowing costs on qualifying capital assets. The revised standard has removed this option, therefore, the company has capitalised all qualifying borrowing costs in the year. The impact of this change has been to capitalise £0.1m of borrowing costs in the current year.

The following interpretations, revisions and amendments to IFRSs which are not yet effective but have been adopted early in the current year and have had no effect on the accounting policies of the company: Amendments to IFRS 1 and IAS 27: *Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate;* Amendments to IFRS 2: S*hare-based Payment-vesting Conditions,* IFRS 2: *Group Cash-settled Share-based payment transaction* and Cancellations and Revisions to IFRS 3 and IAS 27: *Business Combinations and Consolidated and Separate Financial Statements;* Amendments to IAS 32 and IAS 1: *Puttable Financial Instruments and Obligations Arising on Liquidation;* IFRIC 16: *Hedges of a Net Investment in a Foreign Operation;* Amendments to IAS 39: *Eligible Hedged Items;* IFRIC 17: *Distributions of Non-cash Assets to Owners*; Improvements to IFRSs (May 2008); Amendments to IFRIC 9 and IAS 39: *Embedded Derivatives* and Revisions to IAS 39, IFRS 7: *Reclassification of Financial Assets (updated)* and IFRIC 18: *Transfers of Assets from Customers.*

At completion of the Public Private Partnership (PPP) transaction on 26 July 2001, a transfer scheme hived down certain of the operating assets

and liabilities of National Air Traffic Services Ltd (now NATS Limited) to this company.

In addition, the company entered into a Management Services Agreement with NATS Limited on 25 July 2001. This agreement provides for the provision by NATS Limited of personnel and central services to the company. The cost of central services is recharged on the basis of a fair allocation of costs taking into account the most important drivers for the services provided. The company is responsible for paying to NATS Limited an amount equal to the aggregate of all costs incurred by NATS Limited in connection with the employment of the personnel together with appropriate staff related costs and expenses and disbursements.

NATS (En Route) plc (NERL) also entered into an Inter-company Services Agreement on 25 July 2001 with NATS (Services) Limited (NATS Services). Under this agreement this company provides NATS Services with the following services:

- approach control service for London Luton airport;
- training services;
- radar data services at NATS Services airports;
- engineering and software support services;
- research and development for NATS Services airports division and business development division; and
- other services to NATS Services business development division (for example - consultancy and engineering services).

The range of services provided by NATS Services to NERL under the agreement includes:

- North Sea helicopter advisory service;
- air traffic services in certain sectors;
- services to London Approach service (engineering services and use of communications facilities);
- accommodation and support services to NERL units sited on NATS Services Heathrow premises; and
- miscellaneous other services.

The company commenced trading from 26 July 2001.

The financial information has been prepared on the historical cost basis. The principal accounting policies adopted are set out below.

Operating profit
Operating profit is stated after charging restructuring costs but before investment income and finance costs.

Revenue recognition
Revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for goods or services provided in the normal course of business, net of discounts, VAT and other sales related taxes. Revenue is recognised as follows:

- Income from the rendering of services is recognised when the outcome can be reliably estimated and then by reference to the stage of completion of the transaction at the balance sheet date and in accordance with NATS (En Route) plc's air traffic services licence (including volume risk sharing and performance incentives) and other contracts. Amounts receivable include revenue allowed under the charge control conditions of the air traffic services licence.
- Sales of goods are recognised when they are delivered and title has passed.
- Interest income is recognised on a time-proportion basis using the effective interest method. This is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount.
- Dividend income is recognised when the shareholder's rights to receive payment have been established.

Goodwill
Goodwill arising on consolidation in relation to NATS (En Route) plc, being the excess of

consideration over the values of the net assets acquired at the date of the Public Private Partnership (PPP), is recognised as an asset and reviewed for impairment at least annually. Any impairment is recognised immediately in the income statement and is not subsequently reversed. For the purpose of impairment testing the company assesses the carrying value of goodwill against the recoverable amount of the cash generating unit to which goodwill has been allocated. Where the recoverable amount is less than the carrying value, the impairment loss is allocated to goodwill.

Recoverable amount is the higher of fair value and the value in use. In assessing value in use the estimated future cash flows are discounted to their present value using the pre-tax nominal regulated rate of return.

Leases

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other items are classified as operating leases.

The company does not have any finance leases.

Rentals payable under operating leases are charged to income on a straight-line basis over the term of the relevant lease.

Benefits received and receivable as an incentive to enter into an operating lease are also spread on a straight-line basis over the lease term.

Property, plant and equipment

Property, plant and equipment are stated at cost less accumulated depreciation and any provision for impairments in value. The cost of property, plant and equipment includes internal and contracted labour costs directly attributable to bringing the assets into working condition for their intended use. Depreciation is provided on a straight-line basis to write off the cost, less estimated residual value, of property plant and equipment over their estimated useful lives as follows:

- Leasehold land: over the term of the lease.
- Freehold buildings: 10-40 years.
- Leasehold buildings: over the remaining life of the lease to a maximum of 20 years.
- Air traffic control systems: 8-15 years.
- Plant and other equipment: 3-15 years.
- Furniture, fixtures and fittings: 10 years.
- Vehicles: 5-8 years.

Freehold land and assets in the course of construction and installation are not depreciated.

The gain or loss arising on the disposal or retirement of an asset is determined as the difference between the sale proceeds and the carrying amount of the asset and is recognised in income.

Borrowing costs

Following the introduction of IAS 23: *Borrowing Costs*, the costs of borrowings directly attributable to the acquisition, construction or production of a qualifying asset are capitalised as part of the cost of the asset (i.e. there is no longer a choice to expense such costs). Qualifying assets are those which take a substantial time to get ready for intended use. These do not include assets which are ready for use when acquired.

For NERL this assumes qualifying assets relate to any additions to new projects that begin from 1 April 2009, included in assets under construction, and excludes acquisitions that are acquired in a state ready for use.

When funds are borrowed specifically for the purpose of acquiring or constructing a qualifying asset, the amount of borrowing costs eligible for capitalisation is the actual cost of borrowing incurred in the period. IAS 23 requires that where a qualifying asset is funded from a pool of general borrowings, the amount of borrowing costs eligible for capitalisation should be determined by applying an appropriate capitalisation rate (based on the weighted average of borrowing costs applicable to the general outstanding borrowings during the period) to the expenditure during the period, to

determine the borrowing costs eligible for capitalisation.

For NERL, the percentage rate for interest capitalisation is calculated as a proportion of the interest costs to the average level of borrowings in the period that relate to qualifying capital expenditure. All qualifying capital expenditure is then inflated by this percentage which has the effect of capitalising related interest costs.

Deferred grants and other contributions to property, plant and equipment

Government grants as contributions to non-current assets are treated as deferred income which is credited to the income statement by equal annual instalments over the expected useful economic lives of the related assets.

Grants of a revenue nature are credited to income in the period to which they relate.

Internally-generated intangible assets – research and development expenditure

Expenditure on research activities is recognised as an expense in the period in which it is incurred.

An internally-generated intangible asset arising from the company's development activities is recognised only if all of the following conditions are met:

- an asset is created that can be identified (such as software and new processes);
- it is probable that the asset created will generate future economic benefits; and
- the development cost of the asset can be measured reliably.

Internally-generated intangible assets are amortised on a straight-line basis over their useful lives, typically over 3 to 12 years. Assets in the course of construction are not amortised. Where no internally-generated intangible asset can be recognised, development expenditure is recognised as an expense in the period in which it is incurred.

Impairment of tangible and intangible assets, excluding goodwill

At each balance sheet date, the company reviews the carrying amounts of its tangible and intangible assets, including those in the course of construction, to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment (if any). Where the asset does not generate cash flows that are independent from other assets, the company estimates the recoverable amount of the cash-generating unit to which the asset belongs.

Recoverable amount is the higher of net realisable value less costs to sell and the value in use. In assessing value in use the estimated future cash flows are discounted to their present value using the pre-tax nominal regulated rate of return.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognised as an expense immediately.

Where an impairment loss on an intangible or tangible asset, excluding goodwill, subsequently reverses, the carrying amount of the asset (cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (cash-generating unit) in prior years. A reversal of an impairment loss is recognised in the income statement immediately.

Emissions allowances

Consistent with the withdrawal of IFRIC 3, emissions allowances previously recognised at valuation are now recognised at cost. Emission allowances granted free of charge are recognised at zero value on the balance sheet as an intangible asset. As carbon is produced and an obligation to submit allowances arises, a provision is created.

The provision is measured at book value ("nil" or carrying amount of purchased emission certificates) of the recognised emission certificates. If there is an obligation that is not covered by allowances already on the balance sheet, the corresponding provision made is measured at current market prices.

Share-based payments
The company has applied the requirements of IFRS 2: *Share-based payments*.

In 2001, the company established an All Employee Share Ownership Plan for the benefit of its employees to hold 5% of the share capital of NATS Holdings Limited. The Plan was initially established through the transfer of shares by the Crown Shareholder at the PPP to NATS Employee Sharetrust Limited ("NESL"), a trustee company. The employee ordinary shares may only be owned by employee shareholders and can only be sold to the trust company.

The cost of performance related awards to employees that take the form of rights to acquire or receive shares is recognised over the period of the employees' related performance. Where there are no performance criteria, the cost is recognised over the period from gift or grant to when the employee becomes unconditionally entitled to the shares. In respect of the award schemes and certain share option grants, the company provides finance to NESL to enable the trust company to meet its obligations to repurchase vested or eligible shares from employees.

The company's share of the costs of running the employee share trust are charged to the income statement.

In March 2010, employees were offered the option of subscribing to partnership shares at fair value by deductions from gross salary over a 12 month accumulation period. At the end of the accumulation period employees will receive partnership shares at a share price which is the lower of the share price at point of offer or the share price at the end of the accumulation period. In addition, staff will receive one free matching share for every partnership share purchased. At the end of the accumulation period, and after the shares are awarded, the extent to which the company has a liability to staff for their holdings of partnership and matching shares will be re-assessed in the light of subsequent share valuations.

Taxation
The tax expense represents the sum of the tax currently payable and deferred tax.

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

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying values of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the tax profit nor the accounting profit.

The carrying value of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted by the balance sheet date. Deferred tax in the income

statement is charged or credited, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current liabilities and when they relate to taxes levied by the same taxation authority and the company intends to settle its current tax assets and liabilities on a net basis.

Foreign currency translation
Transactions in currencies other than pounds sterling are recorded at the rates of exchange prevailing on the dates of the transactions. At each balance sheet date, monetary assets and liabilities that are denominated in foreign currencies are retranslated at the rates prevailing on the balance sheet date. Non-monetary assets and liabilities carried at fair value that are denominated in foreign currencies are translated at the rates prevailing at the date when the fair value was determined. Gains and losses arising on retranslation are included in the income statement for the period.

In order to hedge its exposure to certain foreign exchange risks, the company enters into forward contracts (see below for details of the company's accounting policies in respect of such derivative financial instruments).

Retirement benefit costs
NATS Ltd, the company's immediate parent undertaking, has entered into a deed of Pension Fund adherence with the CAA and the Trustees of the Civil Aviation Authority Pension Scheme whereby the company was admitted to participate in the Civil Aviation Authority Pension Scheme from 1 April 1996. At 31 March 2001, the business of NATS was separated from the CAA. As a consequence, NATS has become a 'non associated employer' which requires the assets relating to the liabilities of NATS active employees at 31 March 2001 to be separately identified within the Pension Scheme. The Pension Scheme has been divided into two sections to accommodate this and a series of common investment funds established in which both sections participate for investment purposes.

In January 2009, the company introduced a number of pension reforms, as explained in note 24. This included closing the defined benefit scheme to new entrants with effect from 1 April 2009, introducing a limit on increases in pensionable pay and establishing a defined contribution scheme for new entrants effective from 1 April 2009.

The Civil Aviation Authority Pension Scheme is a funded defined benefit scheme providing benefits based on final pensionable pay. The assets of the scheme are held in a separate trustee administered fund. Pension costs are assessed in accordance with the advice of a qualified actuary using the Projected Unit Credit Method. Actuarial valuations are carried out at each balance sheet date. Actuarial gains and losses are recognised in full in the period in which they occur. They are recognised outside the income statement and presented in the statement of recognised income and expense.

Past service cost is recognised immediately to the extent that the benefits are already vested, and otherwise is amortised on a straight-line basis over the average period until the benefits become vested.

The retirement benefit obligation recognised in the balance sheet represents the fair value of scheme assets as reduced by the present value of the defined benefit obligation as adjusted for unrecognised past service cost and as reduced by the fair value of scheme assets. Any asset resulting from this calculation is limited to past service cost, plus the present value of available refunds and reductions in future contributions to the scheme.

Provisions
Provisions are recognised when the company has a present obligation as a result of a past event, and it is probable that the company will be required to settle that obligation. Provisions are measured at the directors' best estimate of expenditure

required to settle the obligation at the balance sheet date, and are discounted to present value where the effect is material.

Financial instruments
Financial assets and financial liabilities are recognised on the company's balance sheet when the company becomes a party to the contractual provisions of the instrument. Detailed disclosures are set out in notes 15 to 19.

Financial Assets
Financial assets, other than hedging instruments, can be divided into the following categories;

- Loans and receivables
- Financial assets at fair value through the profit and loss
- Available for sale financial assets
- Held to maturity investments

Financial assets are assigned to different categories on initial recognition. The classification depends upon the nature and purpose of the financial asset. A financial instrument's category is relevant to the way it is measured and whether the resulting income is recognised through the income statement or directly in equity. Subsequent to initial recognition financial assets are measured at either fair value or at amortised cost according to the category in which they are classified.

Investments are recognised and derecognised on a trade date where the purchase or sale of an investment is under a contract whose terms require delivery of the investment within the time frame established by the market concerned, and are initially measured at fair value plus transaction costs.

Loans and receivables
Trade receivables and other receivables that have fixed or determinable payments that are not quoted in an active market are classified as loans and receivables. Receivables are measured at amortised cost using the effective interest method, less any impairment.

Impairment of financial assets
Financial assets are rigorously assessed for indicators of impairment at half year and year-end. Financial assets are impaired where there is objective evidence that, as a result of one or more events that occurred after initial recognition of the financial asset, the estimated future cash flows of the investment have been impacted.
Impairment losses on trade receivables are recognised using allowance accounts. When a trade receivable is considered irrecoverable, it is written off against the allowance account, any subsequent recoveries are credited to the allowance account. Changes in the allowance account are recognised in the income statement.

Cash and cash equivalents
Cash and cash equivalents comprise cash on hand and demand deposits and other highly liquid investments (with a maturity of 3 months or less) that are readily convertible to a known amount of cash and are subject to an insignificant risk of changes in value.

Financial liabilities
Financial liabilities are classified according to the substance of the contractual arrangements entered into. Financial liabilities are either financial liabilities at "fair value through the profit and loss" or "other financial liabilities".

Fair value through the profit and loss
Financial liabilities at fair value through the profit and loss are measured initially at fair value and subsequently stated at fair value, with any resultant gain or loss recognised in the income statement. The net gain or loss recognised in the income statement incorporates any interest paid on the financial liability.

Other Financial liabilities: including bank, other borrowings, loan notes and debt securities
Interest-bearing bank loans, other borrowings, loan notes and debt securities are recorded at the proceeds received, net of direct issue costs. Finance charges, including premiums payable on settlement or redemption and direct issue costs, are accounted for on an accrual basis in the income statement using the effective interest method and are added to the carrying amount of the instrument to the extent that they are not settled in the period in which they arise.

Effective interest method
The effective interest method is a method of calculating amortised cost of a financial asset or financial liability and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts the estimated future cash receipts through the expected life of the financial asset.

Equity
Equity instruments are also classified according to the substance of the contractual arrangements entered into. An equity instrument is any contract that evidences a residual interest in the assets of the company after deducting all of its liabilities. Equity instruments issued by the company are recorded at the proceeds received, net of direct issue costs.

Derivative financial instruments and hedging activities
The company's activities expose it primarily to the financial risks of changes in interest rates, inflation and foreign currency exchange rates. The company uses interest rate and index-linked swap contracts and forward foreign exchange contracts to hedge these exposures. These are disclosed in note 18 to the accounts.

Under IFRS derivatives are initially recognised at fair value on the date a derivative contract is entered into and are subsequently measured at their fair value. The method of recognising the resulting gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged.

The use of financial derivatives is governed by the company's policies approved by the board of directors, which provides written principles on the use of financial derivatives. The company documents at the inception of the transaction the relationship between hedging instruments and the hedged items, as well as its risk management objectives and strategy for undertaking various hedge transactions. The company also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items.

Changes in the fair value of derivative financial instruments that are designated and effective as hedges of future cash flows are recognised directly in equity and the ineffective portion is recognised immediately in the income statement. If a hedge of a forecast transaction subsequently results in the recognition of a financial asset or a financial liability, the associated gains or losses that were recognised directly in equity are reclassified into the income statement in the same period or periods during which the asset acquired or liability assumed affects profit or loss. For hedges that do not result in the recognition of an asset or a liability, amounts deferred in equity are recycled to the income statement in the same period in which the hedged item affects the income statement.

Changes in the fair value of derivative financial instruments that do not qualify for hedge accounting are recognised in the income statement as they arise.

Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated, or exercised, or no longer qualifies for hedge accounting. At that time, any cumulative gain or loss on the hedging instrument recognised in equity is retained in equity until the forecast transaction occurs. If a hedging transaction is no longer expected to occur, the net cumulative gain or loss recognised in equity is transferred to net income or expense for the period.

Derivatives embedded in other financial instruments or other host contracts are treated as separate derivatives when their risks and characteristics are not closely related to those of host contracts and the host contracts are not carried at fair value with unrealised gains or losses reported in the income statement.

3. Critical judgements and key sources of estimation uncertainty.

Impairment of goodwill, intangible and tangible assets

In carrying out impairment reviews of goodwill, intangible and tangible assets, (including assets in the course of construction), a number of significant assumptions have to be made when preparing cash flow projections and assessing net realisable values. These include air traffic growth, service performance, future cash flows, the value of the regulated asset base, market premiums for regulated businesses and the outcome of the regulatory price control determination for Control Period 3 (2011-2015). If the actual outcome should differ or changes in expectations arise, impairment charges may be required which would materially impact on operating results. A reduction in value in use of 6% or a reduction in market premium of 3% would result in recoverable amount being equal to the carrying amount of goodwill. Refer to notes 12, 13 and 14.

Retirement benefits

The company accounts for its defined benefit pension scheme such that the net pension scheme asset or liability is reported on the balance sheet with actuarial gains and losses being recognised directly in equity through the statement of comprehensive income. To the extent that there is a net pension scheme asset, this assumes that economic benefit will arise, at least to the extent shown, from contributions to the pension scheme at a rate below the future cost of pension benefits.

A number of key assumptions have been made in calculating the fair value of the company's defined benefit pension scheme which affect the balance sheet position and the company's reserves and income statement. Refer to note 24 of the notes to the accounts for a summary of the main assumptions. Actual outcomes may differ materially from the assumptions used and may result in volatility in the net pension scheme asset/liability.

Capital investment programme

The company is undertaking a significant capital investment programme to upgrade existing air traffic control infrastructure. This programme requires the company to enter into substantial contracts for the development of infrastructure assets and information systems. Whilst covered by contractual arrangements, it is in the nature of such complex projects that, from time to time, variations to the original specifications may necessitate the renegotiation of original contract scope or price and affect amounts reported in these accounts.

4 Revenue

An analysis of the company's revenue is provided as follows:

	Year ended 31 March 2010 £m	Year ended 31 March 2009 £m
UK air traffic services	561.4	587.6
North Atlantic air traffic services	22.2	23.5
Inter-company income	16.1	16.0
	599.7	627.1

All revenue is derived from continuing operations. Note 5 summarises the source of revenues by business and geographical segment. Other revenue is described on the face of the income statement and is included in note 8.

A portion of the company's revenue from the sale of goods denominated in foreign currencies is cash flow hedged. Included in revenue is the recycling of the effective amount of foreign currency derivatives that are used to hedge foreign currency revenue. The amount included in revenue is £1.1m (2009: £2.4m).

5 Business and geographical segments

Business segments

For management reporting purposes, the company is currently organised into two business areas.

Principal activities are as follows:

UK air traffic services represent the provision of en-route air traffic services within UK air space, including air traffic services for helicopters operating in the North Sea, approach services for London airports and services to the Ministry of Defence. North Atlantic air traffic services provide en-route air traffic services for the North Atlantic, including an altitude calibration service.

Inter-segment transfers are allocated to business areas on the basis of a fair allocation of costs taking into account the most important drivers for the services provided.

Information about each business area is presented below.

Year ended 31 March 2010	UK air traffic services £m	North Atlantic air traffic services £m	Total £m
Revenue			
Revenue from external customers	561.4	22.2	583.6
Revenue from internal customers	16.1	-	16.1
	577.5	22.2	599.7
Segmental operating profit	92.1	0.2	92.3
Investment revenue			1.2
Finance costs			(38.6)
Profit before tax			54.9
Tax			(13.8)
Profit for the period			41.1
Other information			
Exceptional costs	19.5	0.7	20.2
Capital expenditure	135.0	2.7	137.7
Depreciation and amortisation	79.9	3.8	83.7
Impairment losses recognised in income	2.4	-	2.4
Deferred grants released	(1.7)	-	(1.7)
Balance Sheet			
Segmental assets	1,324.5	34.1	1,358.6
Unallocated corporate assets			80.3
Total assets			1,438.9
Segmental liabilities	(115.1)	(3.9)	(119.0)
Unallocated corporate liabilities			(923.8)
Total liabilities			(1,042.8)

5 Business and geographical segments (continued)

Year ended 31 March 2009	UK air traffic services	North Atlantic air traffic services	Total
	£m	£m	£m
Revenue			
Revenue from external customers	587.6	23.5	611.1
Revenue from internal customers	16.0	-	16.0
	603.6	23.5	627.1
Segmental operating profit	110.2	1.2	111.4
Investment revenue			4.7
Finance costs			(49.3)
Profit before tax			66.8
Tax			(32.2)
Profit for the period			34.6
Other Information			
Exceptional costs	50.2	1.0	51.2
Capital expenditure	142.9	3.1	146.0
Depreciation and amortisation	74.2	2.8	77.0
Impairment losses recognised in income	2.7	-	2.7
Deferred grants released	(2.1)	-	(2.1)
Balance Sheet			
Segmental assets	1,200.8	31.2	1,232.0
Unallocated corporate assets			83.4
Total assets			1,315.4
Segmental liabilities	(177.0)	(7.6)	(184.6)
Unallocated corporate liabilities			(862.3)
Total liabilities			(1,046.9)

All assets are allocated to reportable segments with the exception of taxation, derivative financial instruments, interest receivables short term investments and cash and cash equivalents.

All liabilities are allocated to reportable segments with the exception of taxation, borrowings, derivatives financial instruments, interest payable and dividends payable.

Geographical segments

The following table provides an analysis of the company's revenue by geographical area, based on the geographical location of its customers:

	Year ended 31 March 2010	Year ended 31 March 2009
	£m	£m
UK	262.0	274.2
Rest of Europe	199.5	209.5
North America	100.6	106.1
Other	37.6	37.3
Total	599.7	627.1

Capital expenditure and company assets are all located within the UK.

Information about major customers

Included in revenues arising from UK air traffic services are revenues of £51.9m (2009: £65.5m) which arose from the company's largest customer.

6 Operating profit for the year

Operating profit for the year has been arrived at after charging/(crediting):

a Exceptional items

Redundancy and relocation costs

During the year staff relocation costs were incurred following the closure of the air traffic control centre at West Drayton in 2008 and Manchester in 2010, and the relocation of staff from the Hurn training college. To the extent that staff could not be redeployed, termination terms were agreed.
In response to the economic downturn and changes in technology, voluntary redundancy was also offered to staff in some areas of the business.

	Year ended 31 March 2010 £m	Year ended 31 March 2009 £m
Voluntary redundancy costs	19.0	25.2
Relocation of staff and offices to Swanwick area	5.3	11.4
Relocation of staff to the Prestwick area	(0.1)	14.6
Relocation of staff from Hurn to the Corporate Technical Centre	1.1	-
Swanwick business rates rebate relating to prior years	(5.1)	-
	20.2	51.2

The tax effect of the items above and the effects of the abolition of industrial building allowances in 2009 (see note 10) are shown as exceptional on the face of the income statement.

b Other items

Operating profit for the year has been arrived at after charging/(crediting):

	Year ended 31 March 2010 £m	Year ended 31 March 2009 £m
CAA regulatory charges	5.8	4.4
Depreciation of property, plant and equipment	73.8	68.8
Impairment of property, plant and equipment	0.7	2.6
Amortisation of internally generated intangible assets	9.9	8.2
Impairment of internally generated intangible assets	1.7	0.1
Deferred grants released	(1.7)	(2.1)
Research and development costs	8.5	3.9
Auditors remuneration for audit services (see below)	-	-

Fees payable to Deloitte LLP and their associates for non-audit services to the company are not required to be disclosed because the consolidated financial statements are required to disclose such fees on a consolidated basis.

Government grants relating to the purchase of property, plant and equipment and Ministry of Defence (MoD) contributions received prior to 1 April 2001 are treated as deferred income which is credited to the income statement by equal annual instalments over the expected useful lives of the related assets.

Transactions with group companies	Year ended 31 March 2010 £m	Year ended 31 March 2009 £m
Net charges for services provided by parent undertaking	10.9	10.9
Charges for services provided by other group companies	15.7	15.8

In addition to the staff costs referred to in note 7a below, NERL is responsible under the Management Services Agreement (MSA) for reimbursing NATS Limited for all other staff related costs which it incurs on behalf of the employees seconded to NERL. Under the Inter Company Services Agreement NATS Services provides certain services to NERL. The MSA and Inter Company Services Agreement are explained in more detail in note 2.

7 Staff costs

a Staff costs

	Year ended 31 March 2010 £m	Year ended 31 March 2009 £m
Salaries and staff costs, including directors' remuneration, were as follows:		
Wages and salaries*	225.4	252.2
Social security costs	21.5	22.6
Pension costs (note 7b)	88.0	44.1
	334.9	318.9
Less: amounts capitalised	(37.5)	(36.8)
	297.4	282.1

* Includes redundancy costs, other allowances and holiday pay.

NATS Limited, the immediate parent company, is responsible for employing the staff engaged in the activities carried out by NERL. Under the terms of the MSA dated 25 July 2001 the services of certain employees are seconded to NERL by NATS Limited. NERL is responsible for paying to NATS Limited an amount equal to the aggregate of all costs incurred by NATS Limited in connection with the employment of the seconded employees (including all taxes and social security and pension costs) together with appropriate staff related costs and expenses and disbursements.

b Pension costs

	Year ended 31 March 2010 £m	Year ended 31 March 2009 £m
Defined benefit pension scheme costs (note 24)	87.8	44.1
Defined contribution pension scheme costs	0.2	-
	88.0	44.1

Wages and salaries and pension costs reflect the implementation of pension salary sacrifice arrangements for staff with effect from 1 April 2009.

7 Staff costs (continued)

c Staff numbers

	Year ended 31 March 2010 No.	Year ended 31 March 2009 No.
The monthly average number of employees (including executive directors) was:		
Air traffic controllers	1,421	1,420
Air traffic service assistants	748	793
Engineers	894	984
Others	678	716
	3,741	3,913

8 Investment revenue

	Year ended 31 March 2010 £m	Year ended 31 March 2009 £m
Interest on bank deposits	1.2	4.4
Other loans and receivables	-	0.3
	1.2	4.7

9 Finance costs

	Year ended 31 March 2010 £m	Year ended 31 March 2009 £m
Interest on bank overdrafts, loans and hedging instruments	1.4	5.3
Bond and related costs including financing expenses	30.3	30.3
Other	0.2	0.7
Interest payable on intercompany loans	0.4	1.5
	32.3	37.8
Loss on derivatives not qualifying for hedge accounting	6.3	11.5
	38.6	49.3

10 Tax

	Year ended 31 March 2010 £m	Year ended 31 March 2009 £m
Current tax (including a credit of £3.0m in respect of prior years, 2009: £1.5m charge)	2.4	(11.8)
Deferred tax (See note 20. Including a charge of £2.6m in respect of prior years, 2009: £1.6m credit)	(16.2)	(20.4)
	(13.8)	(32.2)

Included in the prior year deferred tax charge above is a charge of £13.6m for the tax effect of the abolition of industrial building allowances. This is presented in the income statement as an exceptional item.

Corporation tax is calculated at 28% (2009: 28%) of the estimated assessable profit for the year.

The charge for the year can be reconciled to the profit per the income statement as follows:	Year ended 31 March 2010 £m	Year ended 31 March 2010 %	Year ended 31 March 2009 £m	Year ended 31 March 2009 %
Profit on ordinary activities before tax	54.9		66.8	
Tax on profit on ordinary activities at standard rate in the UK of 28% (2009:28%)	(15.4)	(28.0%)	(18.7)	(28.0%)
Tax effect of abolition of industrial building allowances	-	0.0%	(13.6)	(20.3%)
Tax effect of prior year adjustments	0.4	0.7%	0.1	0.1%
Tax effect of other permanent differences	1.2	2.2%	-	0.0%
Tax charge for year at the effective tax rate of 25.1% (2009: 48.2%)	(13.8)	(25.1%)	(32.2)	(48.2%)
Deferred tax charge/(credit) taken directly to equity (see note 20)	33.7		(103.4)	

11 Dividends

	Year ended 31 March 2010 £m	Year ended 31 March 2009 £m
Amounts recognised as distributions to equity holders in the year		
Interim dividend for the year of £nil per ordinary share (2009: £0.91).	-	9.1

In May 2010, the Board declared and paid an interim dividend for 2011 of £1.50 per share (totalling £15m) which was paid to the company's parent, NATS Limited.

12 Goodwill

	£m
At 31 March 2010 and 31 March 2009	351.0

The company tests goodwill annually for impairment, or more frequently if there are indications that goodwill might be impaired.

The carrying value is determined by reference to value in use calculations and the net realisable value of the regulated asset bases of the company's business segments, including market premiums for regulated businesses (assumed at 10%, 2009: 10%). The key assumptions for value in use calculations are the discount rate, future cash flows to the end of the second regulatory control period (31 December 2010 for UK air traffic services and 31 March 2011 for North Atlantic air traffic services) as assumed in the company's business plans, and a terminal value at that date, reflecting the regulated asset bases and market premiums. The company's business plans reflect the impact of the challenging economic environment on traffic volumes and the activities which the company is taking to mitigate this. The discount rate is a pre-tax nominal rate of 10.26% (2009: 7.07%). See note 3.

13 Other intangible assets

	Operational software £m	Non-operational software £m	Airspace and resectorisation £m	Assets in course of construction £m	Total £m
Cost					
At 1 April 2008	35.0	27.4	12.4	79.8	154.6
Additions internally generated	1.0	0.2	2.6	9.4	13.2
Additions externally acquired	2.0	0.6	-	28.2	30.8
Disposals during the year	-	(1.5)	-	-	(1.5)
Transfers during the year	0.1	2.0	2.5	(4.7)	(0.1)
At 1 April 2009	38.1	28.7	17.5	112.7	197.0
Additions internally generated	0.6	0.2	0.6	13.4	14.8
Additions externally acquired	1.3	2.5	0.2	42.9	46.9
Disposals during the year	-	-	-	(12.5)	(12.5)
Transfers during the year	8.3	0.4	0.3	(9.1)	(0.1)
At 31 March 2010	48.3	31.8	18.6	147.4	246.1
Accumulated amortisation					
At 1 April 2008	10.9	8.3	5.1	16.1	40.4
Charge for the year	4.1	2.7	1.4	-	8.2
Impairment provision recognised in income statement	-	-	-	0.1	0.1
Disposals during the year	-	(1.5)	-	-	(1.5)
At 1 April 2009	15.0	9.5	6.5	16.2	47.2
Charge for the year	5.0	3.3	1.6	-	9.9
Impairment provision recognised in income statement	-	-	-	1.7	1.7
Utilisation of impairment provision	-	-	-	(12.5)	(12.5)
At 31 March 2010	20.0	12.8	8.1	5.4	46.3
Carrying amount					
At 31 March 2010	28.3	19.0	10.5	142.0	199.8
At 31 March 2009	23.1	19.2	11.0	96.5	149.8

The accumulated amortisation of assets in the course of construction represents impairment provisions.

14 Property, plant and equipment

	Freehold land & buildings £m	Improvements to leasehold land & buildings £m	Air traffic control systems, plant and equipment £m	Vehicles, furniture & fittings £m	Assets in course of construction and installation £m	Total £m
Cost						
At 1 April 2008	213.9	46.1	1,027.6	13.2	131.0	1,431.8
Additions during the year	1.8	1.0	37.6	0.3	61.3	102.0
Disposals during the year	-	(11.4)	(81.6)	-	-	(93.0)
Other transfers during the year	5.1	1.9	32.3	1.0	(40.2)	0.1
At 1 April 2009	220.8	37.6	1,015.9	14.5	152.1	1,440.9
Additions during the year	1.1	0.2	35.2	0.1	39.4	76.0
Disposals during the year	-	-	(16.2)	-	(1.1)	(17.3)
Other transfers during the year	0.9	0.4	66.8	0.1	(68.1)	0.1
At 31 March 2010	222.8	38.2	1,101.7	14.7	122.3	1,499.7
Accumulated depreciation and impairment						
At 1 April 2008	70.6	32.0	736.9	6.1	1.3	846.9
Provided during the year	6.6	1.3	59.8	1.1	-	68.8
Provisions for impairment	-	-	-	-	2.6	2.6
Disposals during the year	(0.1)	(11.4)	(81.6)	-	-	(93.1)
At 1 April 2009	77.1	21.9	715.1	7.2	3.9	825.2
Provided during the year	6.9	1.4	64.3	1.2	-	73.8
Provisions for impairment	-	-	0.3	-	0.4	0.7
Utilisation of impairment provision	-	-	-	-	(1.1)	(1.1)
Disposals during the year	-	-	(16.1)	-	-	(16.1)
At 31 March 2010	84.0	23.3	763.6	8.4	3.2	882.5
Carrying amount						
At 31 March 2010	138.8	14.9	338.1	6.3	119.1	617.2
At 31 March 2009	143.7	15.7	300.8	7.3	148.2	615.7

The group conducts annual reviews of the carrying values of its property, plant, equipment and intangible assets. During the year, impairment charges of £2.4m (2009: £2.7m) were made in respect of operational assets and assets in the course of construction reflecting a reassessment of certain projects and the likelihood of benefits being realised in full.

During the year the company capitalised £0.1m of interest costs at a capitalisation rate of 0.7%, in accordance with IAS 23: Borrowing costs, adopted prospectively for the first time this year.

15 Financial and other assets

The company had balances in respect of financial and other assets as follows:

Trade and other receivables

	2010 £m	2009 £m
Non-current		
Other debtors	1.0	1.4
Current		
Receivable from customers gross	39.6	39.9
Allowance for doubtful debts	(5.0)	(5.3)
	34.6	34.6
Other debtors	2.6	5.4
Prepayments	7.6	13.0
Accrued income	85.0	61.1
	129.8	114.1

The average credit period taken on sales of services is 32 days (2009: 28 days). Interest is charged by Eurocontrol to UK en route customers at 11.58% (2009: 9.86%) on balances outstanding after more than 30 days. All other balances are non-interest bearing. An allowance has been made for estimated irrecoverable amounts from sales to customers of £5.0m (2009: £5.3m). Full provision is made for receivables from UK en route customers that are overdue. Debts that are neither impaired nor overdue are assessed for credit quality and reviewed periodically. Receivables in respect of other customers are provided for where there is an identified loss event, such as administration, receivership or liquidation which is evidence of a reduction in the recoverability of the cash flows.

15 Financial and other assets (continued)

Ageing of past due but not impaired trade receivables

	2010 £m	2009 £m
30-90 days	0.1	0.9

Movement in the allowance for doubtful debts

	2010 £m	2009 £m
Balance at the beginning of the year	5.3	2.1
Increase in allowance recognised in the income statement	-	3.6
Amounts written off as irrecoverable	(0.3)	(0.4)
Balance at end of year	5.0	5.3

As of 31 March 2010, of the allowance for doubtful debts, £1.0m was deferred to the balance sheet in respect of 2009 doubtful debts in accordance with the licence which limits NERL's exposure to bad debts from UK en route services to £1.5m arising in relation to a calendar year.

In determining the recoverability of a trade receivable the company considers any change in credit quality of the trade receivable from the date credit was initially granted up to the reporting date. Credit risk is mitigated in part by regulatory price control conditions that protect revenues from losses exceeding £1.5m a year. Accordingly, the directors believe that there is no further credit provision required in excess of the allowance for doubtful debts.

Included in the allowance for doubtful debts are individually impaired trade receivables with a balance of £4.4m (2009: £4.5m) which are in administration, receivership or liquidation. The impairment recognised represents the carrying amount of these trade receivables. The company does not hold any collateral over these balances.

Ageing of impaired receivables

	2010 £m	2009 £m
Current	-	-
30-90 days	0.2	0.4
90-365 days	1.0	3.8
more than 365 days overdue	3.8	1.1
	5.0	5.3

The directors consider that the carrying amount of trade and other receivables approximates to their fair value.

Cash and cash equivalents
Cash and cash equivalents comprise cash held by the company and short-term bank deposits with an original maturity of three months or less. The directors consider that the carrying amount of these assets approximates to their fair value.

Overall, the maximum credit risk for the items discussed above would be £202.8m (2009: £198.9m).

16 Borrowings

	2010 £m	2009 £m
Unsecured loans		
Intercompany loan	23.0	25.9
Other loans (non interest bearing)	-	1.2
Total unsecured loans	23.0	27.1
Secured loans		
£600m 5.25% Guaranteed Secured Amortising Bonds due 2026	597.6	597.4
Bank overdraft	1.2	-
Bank loans (revolving term loan and revolving credit facility expiring 2010-2012)	88.1	77.5
Gross borrowings	709.9	702.0
Unamortised bond issue costs	(6.1)	(6.7)
	703.8	695.3
Amounts due for settlement within 12 months	0.5	1.2
Amounts due for settlement after 12 months	703.3	694.1

The £600m 5.25% Guaranteed Secured Amortising Bond is secured by way of a debenture by which NERL grants its lenders a first legal mortgage over certain properties in England and Wales, a first fixed charge over all other real estate, plant and equipment and a floating charge over all other assets. Drawings of £89.3m made by NERL under its £216.2m committed bank facilities are similarly secured. Further security provisions are also provided by NATS Holdings Limited and NATS Limited. The carrying amount of the collateral provided as security for the £600m bond and bank borrowings is circa £1,257m (2009: £1,135m).

The average effective interest rate on the bank loans in the year was 1.6% (2009: 6.50%) and was determined based on LIBOR rates plus a margin.

Costs associated with the issue of the £600m bond are being amortised over the life of the bond.

Undrawn committed facilities	2010 £m	2009 £m
Less than one year	11.0	-
Between one and two years	34.3	11.0
Expiring in more than two years	81.6	127.7
	126.9	138.7

NERL has outstanding drawings of £89.3m on its committed facilities. The bank facilities expire as follows: £11.0m in November 2010; £34.25m in November 2011 and the balance of c.£170.95m in November 2012.

17. Derivative financial instruments

Fair value of derivative financial instruments

	2010 £m	2009 £m
Current assets		
Derivative financial instruments in designated hedge accounting relationships		
Forward foreign exchange contracts (cash flow hedges)	0.8	-
Current liabilities		
Derivative financial instruments in designated hedge accounting relationships		
Forward foreign exchange contracts (cash flow hedges)	(1.1)	(1.8)
Derivative financial instruments classified as held for trading		
Index-linked swaps	(87.0)	(80.7)
	(88.1)	(82.5)

Further details on derivative financial instruments are provided in note 18. The index-linked swap is classified under international accounting standards as held for trading as it does not qualify for hedge accounting. The index-linked swap was taken out in August 2003 to hedge against the risk of low inflation and previously qualified as a hedge under UK generally accepted accounting principles prior to the group's adoption of international accounting standards.

17. Derivative financial instruments (continued)

Fair value measurements recognised in the balance sheet
The following table provides an analysis of financial instruments that are measured subsequent to initial recognition at fair value, grouped into Levels 1 to 3 based on the degree to which the fair value is observable.

Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2 fair value measurements are those derived from inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).

Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).

	2010				2009			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Financial Assets								
Derivative instruments in designated hedge accounting relationships	-	0.8	-	0.8	-	-	-	-
Financial Liabilities								
Derivative instruments in designated hedge accounting relationships	-	(1.1)	-	(1.1)	-	(1.8)	-	(1.8)
Derivative financial instruments classified as held for trading	-	(87.0)	-	(87.0)	-	(80.7)	-	(80.7)
	-	(88.1)	-	(88.1)	-	(82.5)	-	(82.5)

There were no transfers between individual levels in the period.

18 Financial instruments

Capital risk management
The company manages its capital to ensure that it is able to continue as a going concern, to meet its obligations under its air traffic services licence and to provide returns to stakeholders. The capital structure of the company consists of debt, as disclosed in note 16, cash and cash equivalents and short term investments, as explained in this note and equity attributable to shareholders as disclosed in the statement of changes in equity.

External capital requirements
The air traffic services licence requires the company to use reasonable endeavours to maintain an investment grade issuer credit rating (BBB-/Baa3 or better). Separately, it is the objective of the company to target a credit profile that exceeds BBB-/Baa3.

As at 31 March 2010, the company had a credit rating of AA- (negative outlook) from Standard & Poor's and A2 (stable outlook) from Moody's (2009: A+ (stable outlook)/ (A2 stable outlook)).

Gearing ratio
Consistent with seeking to maintain an investment grade credit rating, the company sets a gearing target, measured as the ratio of Net Debt to the Regulatory Asset Base (RAB).

Significant accounting policies
Details of the significant accounting policies and methods adopted, including the criteria for recognition, the basis of measurement and the basis on which income and expenses are recognised, in respect of each class of financial asset, financial liability and equity instrument are disclosed in note 2 to the financial statements.

Categories of financial instrument
The carrying values of financial instruments by category at 31 March was as follows:

	2010 £m	2009 £m
Financial assets		
Trade and other receivables, excluding prepayments and accrued income	38.2	41.4
Cash and cash equivalents and short term investments	79.6	83.4
Derivative instruments in designated hedge accounting relationships	0.8	-
	118.6	124.8
Financial liabilities		
Derivative instruments in designated hedge accounting relationships	(1.1)	(1.8)
Derivative financial instruments classified as held for trading	(87.0)	(80.7)
Other financial liabilities at amortised cost	(762.7)	(761.9)
	(850.8)	(844.4)

Amortised cost includes balances for trade and other payables, the £600m bond, bank borrowings and other loans.

The index-linked swap is categorised as held for trading. The movement in its market value of £6.3m has been recorded in the income statement in the year (2009: £11.5m).

Financial risk management objectives
The treasury function is mandated by the Board of NATS (Holdings) Limited to manage financial risks that arise in relation to underlying business needs. The function provides services to the business, co-ordinates access to financial markets and monitors and manages financial risks relating to the operations of the company. The function has clear policies and operating parameters. The Treasury Committee provides oversight and meets three times a year to approve strategy and to monitor compliance with Board policy. The Treasury function does not operate as a profit centre and the undertaking of speculative transactions is not permitted. The principal financial risks arising from the company's activities include market risk (including currency risk, cash flow interest rate risk and inflation risk), credit risk and liquidity risk.

18 Financial instruments (continued)

Market risk
The company's activities expose it primarily to the financial risks of changes in foreign currency exchange rates, interest rates and inflation rates. These risks are explained below. The company enters into a variety of derivative financial instruments to manage its exposure to these risks, including:

- forward foreign exchange contracts to hedge the exchange risk arising on services provided to UK en route customers that are billed in Euro, and purchases from foreign suppliers settled in foreign currencies;
- interest rate swaps to mitigate the risk of rising interest rates; and
- index-linked swaps to mitigate the risk of low inflation.

Foreign currency risk management
The company's principal exposure to foreign currency transaction risk is in relation to UK en route services revenues, accounting for 83% of turnover (2009: 84%). Charges for this service are set in sterling, but are billed and collected in Euro by applying a conversion rate determined monthly by Eurocontrol, who administer the UK en route revenue collection. The conversion factor used is the average of the daily closing rates for the month prior to the billing period. To mitigate the risk that exchange rates move between the date of billing and the date on which the funds are remitted to the company, forward foreign currency contracts are entered into. The company seeks to hedge 90% of the UK en route income that is forecast to arise by entering into forward foreign exchange contracts on a quarterly basis.

Contracts for the supply of goods and services with overseas suppliers who invoice in foreign currency are also entered into. To mitigate currency risk the contract value is hedged when a firm commitment arises, either through the use of forward foreign currency contracts or by purchasing foreign currency at spot rates on the date the commitment arises or by setting aside already available foreign currency.

The carrying amount of the company's foreign currency denominated monetary assets and monetary liabilities at 31 March was as follows:

	Assets		Liabilities	
	2010	2009	2010	2009
	£m	£m	£m	£m
Euro	112.7	91.6	(3.3)	(1.1)
US Dollar	0.2	0.2	-	(0.1)
Canadian Dollars	0.1	0.1	(0.1)	(0.1)
Danish Krone	0.4	0.5	-	(0.1)
	113.4	92.4	(3.4)	(1.4)

Foreign currency sensitivity analysis
The company holds foreign currency cash balances in Euro, US Dollars, Canadian Dollars and Danish Krone.

The following table details the sensitivity to a 10% increase or decrease in the value of sterling against relevant foreign currencies. 10% is the sensitivity rate that represents management's assessment of the reasonably possible change in foreign currency exchange rates in a financial year. The sensitivity analysis includes foreign currency cash balances, trade receivables, trade payables and forward foreign exchange contracts and adjusts their translation at the period end for a 10% change in foreign currency rates.

The table below shows the effect of a 10% strengthening of sterling against the relevant currency. A positive number below indicates an increase in profit and equity and a negative number a reduction in profit and equity. There would be an equal and opposite impact on profit and equity if sterling devalues by 10% against the relevant currency.

Currency	2010 Impact £m	2009 Impact £m
Euro	(2.6)	(2.2)
US Dollar	-	-
Canadian Dollars	-	-
Danish Krone	-	(0.2)
	(2.6)	(2.4)

NERL believes that this sensitivity analysis accurately reflects its inherent foreign exchange risk as the exposure to foreign exchange risk was broadly constant throughout the reporting period.

18 Financial Instruments (continued)

Forward foreign exchange contracts

Forward foreign exchange contracts were entered into during the year to sell Euro forecast to be received from Eurocontrol in respect of UK en route revenues. In addition, NERL has entered into other forward foreign exchange contracts to fund purchases of equipment. These forward exchange contracts have been designated as cash flow hedges. The following contracts were outstanding at year end:

2010

Euro sold	£m	€m	Average exchange rate
0-3 months	103.3	116.5	0.8867
Over 3 months	1.4	1.5	0.9075
	104.7	118.0	0.8869
Euro bought	€m	£m	
0-3 months	6.3	5.6	0.8870
Over 3 months	17.2	15.2	0.8847
	23.5	20.8	0.8857
Canadian Dollar bought	C$m	£m	
Over 3 months	0.1	0.1	1.792
Danish Krone bought	DKK m	£m	
0-3 months	5.2	0.6	8.3870
Over 3 months	1.5	0.2	8.4070
	6.7	0.8	8.3914
Danish Krone sold	£m	DKK m	
Over 3 months	-	-	N/A

2009

Euro sold	£m	€m	Average exchange rate
0-3 months	69.3	77.0	0.9002
Over 3 months	-	-	-
	69.3	77.0	0.9002
Euro bought	€m	£m	
0-3 months	1.0	0.9	0.8925
Over 3 months	0.4	0.3	0.8796
	1.4	1.2	0.8890
Canadian Dollar bought	C$m	£m	
Over 3 months	-	-	-
Danish Krone bought	DKK m	£m	
0-3 months	1.4	0.2	8.1395
Over 3 months	10.3	1.2	8.4241
	11.7	1.4	8.3892
Danish Krone sold	£m	DKK m	
Over 3 months	0.2	1.6	8.1933

At 31 March 2010, the aggregate amount of the unrealised losses under forward foreign exchange contracts deferred in the hedging reserve relating to the exposure on these future transactions was £0.5m (2009: unrealised gains of £0.2m). The bulk of these contracts will mature within the first three months of the next financial year at which stage the amount deferred in equity will be realised in the income statement for hedges relating to revenue expenditure or capitalised and depreciated for those relating to capital expenditure.

In addition to the above, NERL has entered into average rate forward agreements with a contract date after 31 March 2010 to sell Euro anticipated to be received in July and August 2010 totalling €91.2m in respect of UK en route revenues. These contracts are also designated as cash flow hedges. They are not included in the table above.

Interest rate risk management

NERL is exposed to interest rate risk to the extent that it holds borrowings at fixed, floating and index-linked interest rates. Its interest rate risk management policies are kept under continuous review.

The company seeks to limit exposure to movements in interest rates by ensuring that it holds an appropriate balance of fixed, floating and index-linked debt as a percentage of its net debt by the use of interest rate swap contracts and index-linked swap contracts. The appropriate mix of fixed, floating and index-linked borrowing varies over time and reflects the certainty of future borrowing requirements and the prevailing interest rates. Recognising that long term borrowing forecasts are inherently more uncertain than short term forecasts, the policy is to reduce the proportion of debt that is fixed for borrowings of longer maturity as follows:

Debt maturity	Fixed Rate %	Index linked %	Floating %
Within one year	40-70	30-50	0-30
Between one and two years	40-60	30-50	0-30
Between two and five years	30-50	30-50	10-40
After five years	20-40	30-70	10-50

Exposure to interest rates on financial assets and financial liabilities are detailed below. The company held no interest rate swaps at 31 March 2010 (2009: none).

Economic interest rate exposure

The company held cash and short term deposits as follows:

2010

	Cash			Short term deposits			Total
Currency	Amount £m	Economic interest rate %	Average maturity days	Amount £m	Economic interest rate %	Average maturity days	£m
Sterling	61.6	0.6	3	15.5	0.8	183	77.1
Euro	2.0	0.2	6	-	-	-	2.0
Candian Dollar	0.1	-	1	-	-	-	0.1
Danish Krone	0.4	0.3	6	-	-	-	0.4
	64.1			15.5			79.6

2009

	Cash			Short term deposits			Total
Currency	Amount £m	Economic interest rate %	Average maturity days	Amount £m	Economic interest rate %	Average maturity days	£m
Sterling	62.6	0.5	1	15.6	1.8	183	78.2
Euro	4.5	0.2	1	-	-	-	4.5
Danish Krone	0.5	-	1	-	-	-	0.5
US Dollar	0.2	-	1	-	-	-	0.2
	67.8			15.6			83.4

The economic interest rate reflects the true underlying cash rate that the company was paying on its borrowings or receiving on its deposits at 31 March.

18 Financial Instruments (continued)

The economic interest rate exposure of the loans is presented below with and without the effect of derivatives, as follows:

Excluding derivatives

	Total £m	Variable rate £m	Inflation rate £m	Fixed rate £m	Economic interest rate %	Weighted average time for which rate is fixed years
At 31 March 2010						
Sterling:						
5.25% guaranteed secured bonds	597.6	-	-	597.6	5.27%	10.0
Bank loans	89.3	89.3	-	-	1.13%	0.5
Inter-company loans	23.0	23.0	-	-	1.16%	0.5
Total	709.9	112.3	-	597.6		
At 31 March 2009						
Sterling:						
5.25% guaranteed secured bonds	597.4	-	-	597.4	5.27%	11.0
Bank loans	77.5	77.5	-	-	2.15%	0.5
Inter-company loans	25.9	25.9	-	-	2.31%	0.5
Other loans	1.2	-	-	1.2	0.00%	N/A
Total	702.0	103.4	-	598.6		

Including derivatives

	Total £m	Variable rate £m	Inflation rate £m	Fixed rate £m	Economic interest rate %	Weighted average time for which rate is fixed years
At 31 March 2010						
Sterling:						
5.25% guaranteed secured bonds	397.6	-	-	397.6	5.28%	10.0
5.25% guaranteed secured bonds	200.0	-	200.0	-	3.64%	0.5
Bank loans	89.3	89.3	-	-	1.13%	0.5
Inter-company loans	23.0	23.0	-	-	1.16%	0.5
Total	709.9	112.3	200.0	397.6		
At 31 March 2009						
Sterling:						
5.25% guaranteed secured bonds	397.4	-	-	397.4	5.28%	11.0
5.25% guaranteed secured bonds	200.0	-	200.0	-	3.51%	0.5
Bank loans	77.5	77.5	-	-	2.15%	0.5
Inter-company loans	25.9	25.9	-	-	2.31%	0.5
Other loans	1.2	-	-	1.2	0.00%	N/A
Total	702.0	103.4	200.0	398.6		

The interest rate payable under the index-linked swap is adjusted semi-annually in line with the movement in the UK RPI.

The following table shows the percentage of fixed, index-linked and floating rate debt as a percentage of net debt. Net debt is defined for this purpose as borrowings net of cash and short term investments as distinct from the definition used for financial covenants purposes explained above.

	2010 £m		2009 £m	
Net Debt	624.2		611.9	
	£m	%	£m	%
Fixed (net of bond discount and issue costs)	391.5	62.7	391.9	64.0
Index-linked	200.0	32.0	200.0	32.7
Floating (net of cash and short term investments)	32.7	5.3	20.0	3.3
	624.2	100.0	611.9	100.0

In 2007, in order to reduce its exposure to interest rate risk on its cash balances, the company adopted a strategy of hedging net debt rather than gross debt. This is an economic hedge whereby exposure to floating rate debt is offset by interest on cash balances.

Interest rate sensitivity analysis
The sensitivity analysis below has been determined based on the exposure to interest rates on floating rate assets and liabilities. The analysis is prepared assuming the amount of assets or liabilities at the balance sheet date was in place for the whole year. A 1% increase or decrease is considered to represent management's assessment of the reasonably possible change in interest rates.

The following table shows the effect of a 1% increase in interest rates on cash and floating rate bank loans on profit for the year and on equity. A positive number represents an increase in profit and equity and a negative number a decrease in profit and equity. There would be an equal and opposite impact on profit and equity if interest rates fell by 1%.

	2010 Impact £m	2009 Impact £m
Cash On Deposit (2010: £79.6m, 2009: £83.4m)	0.8	0.8
Borrowings (2010: £112.3m, 2009: £103.4m)	(1.1)	(1.0)
	(0.3)	(0.2)

The sensitivity to interest rates has increased during the year primarily due to a reduction in the amount of cash on deposit and higher borrowings.

18 Financial Instruments (continued)

Inflation rate risk

The regulatory charge control conditions that apply to the company's en route and North Atlantic services determines a revenue allowance by reference to inflation on an "RPI-X" basis. To achieve an economic hedge of this income, in August 2003 coincident with the issue of its £600m 5.25% fixed rate bond, the company entered into an amortising index-linked swap with a notional principal of £200m for the period up to March 2017 reducing semi-annually thereafter and expiring in March 2026. Under the terms of this swap, NERL receives fixed interest at 5.25% and pays interest at a rate of 2.98% adjusted for the movement in RPI. The index-linked swap cannot be designated as a cash flow hedge under IFRS, although it provides an economic hedge of NERL's RPI-linked revenues.

The value of the notional principal of £200m of the index-linked swap is also linked to movements in RPI. Commencing in 31 March 2017, semi-annual payments will be made relating to the inflation uplift on the amortisation of the notional principal.

Inflation rate sensitivity analysis

The sensitivity analysis below has been determined based on the exposure to breakeven inflation arising from the index-linked swap. The difference between fixed rate and index-linked gilts reflects the market's expectations of future RPI and is a proxy for the breakeven inflation rate. The analysis is prepared assuming that the index-linked swap at the balance sheet date was in place for the whole year. A 1% increase or decrease in breakeven inflation is considered to represent management's assessment of the reasonably possible change in inflation. An increase in the rate of RPI will increase the future index-linked payments that the company is required to make under the swap contract and so impacts its mark to market value.

The following table shows the effect of a 1% increase in breakeven inflation on the amount of interest payable in respect of this swap and the impact on its value when marked to market. A positive number indicates an increase in profit and equity and a negative number a reduction in profit and equity. There would be an equal and opposite impact on profit and equity if breakeven inflation falls by 1%.

	2010 Impact £m	2009 Impact £m
Change in index-linked swap interest and mark to market value	(31.8)	(34.5)

The mark to market value of the index-linked swap is also sensitive to the discount rates that are used to determine the net present value of the cash flows under the swap agreement. The discount rate is determined by reference to market yields on interest rate swaps. The effect of a 1% increase in the discount rate would be to increase profit and equity by £11.2m (2009: £12.3m). There would be an equal and opposite impact on profit and equity if discount rates decreased by 1%.

Credit risk management

Credit risk refers to the risk that a counterparty will default on its contractual obligations resulting in financial loss. The exposure to credit risk arises from the risk of default by customers on settlement of trade receivables and from the risk of a failure of a financial institution in which funds are invested for return or held for trading purposes or with whom derivative contracts are entered into. The risk of loss from default by customers and the mitigations against this risk are explained in note 15. With regard to funds or contracts held with financial institutions, the group's policy is to transact with counterparties that hold a minimum credit rating as supplied by independent rating agencies, Standard & Poor's, Moody's Investors Service and Fitch Ratings.

The group's policy is to allocate limits to the value of investments, foreign exchange transactions and interest rate hedging transactions that may be entered into with a bank or financial institution and to allocate an aggregate credit risk limit. The limits are based upon the institution's credit rating with Standard & Poor's, Moody's and Fitch rating agencies. Where there is a difference in the rating then the lowest of the ratings is applied.

Currently, the company's investments take the form of bank time deposits. Investments in bank time deposits with maturities up to 3 months and between 3 and 6 months are only entered into with institutions holding a long term minimum credit rating of A- and A+ respectively from Standard & Poor's and A3 and A1 respectively from Moody's. During 2008 the group tightened its investment criteria and currently only places deposits that have a maturity in excess of seven days with banks rated AA- or better.

The tables below set out the limits that are applied to each institution based on its credit rating and the balances held at 31 March with those institutions:

Rating (Standard and Poor's/Moody's)	Limit per Institution £m
AAA/Aaa	50.0
AA+/Aa1	40.0
AA/Aa2	30.0
AA-/Aa3	20.0
A+/A1	15.0
A/A2	10.0
A-/A3	7.5

The following table shows the distribution of the company's deposits at 31 March by credit rating (Standard & Poor's):

Rating (Standard & Poor's)	Number of institutions	2010 £m	By credit rating %	Number of institutions	2009 £m	By credit rating %
AA-	1	16.0	20.1	2	37.4	44.8
A+	3	31.2	39.2	2	20.9	25.1
A	2	18.4	23.1	3	25.1	30.1
A-	2	14.0	17.6	-	-	-
		79.6	100.0		83.4	100.0

18 Financial Instruments (continued)

Liquidity risk management

The responsibility for liquidity risk management, the risk that the company will have insufficient funds to meet its obligations as they fall due, rests with the Board of NATS (Holdings) Limited with oversight provided by the Treasury Committee. The company manages liquidity by maintaining adequate reserves and borrowing facilities by monitoring actual and forecast cash flows and ensuring funding is diversified by source and maturity and available at competitive cost.

The policy is to:

a. maintain free cash equal to between 1 and 2 months of UK en route services revenues (see below). Free cash is defined as cash and cash equivalents and short term investments, excluding a debt service reserve account of £15.5m used to fund interest and fees scheduled for payment in the next six months and a liquidity reserve account of £21.3m held to provide liquidity in the event of certain pre-defined circumstances, particularly to ensure compliance with financial covenants;

b. ensure access to bank facilities sufficient to meet 120% of forecast requirements that are not otherwise covered by operating cash flows or other sources of finance through the period of the business plan. NERL has access to bank facilities totalling c.£216.2m available until November 2010, c.£205.2m available until November 2011 and c.£170.95m until November 2012. To ensure that committed funding is avaliable at a competitive cost to meet its anticipated needs for the period covered by its CP3 business plan, the company anticipates that it will replace these facilities with a new five year facility during the financial year ending 31 March 2012;

c. ensure access to long term funding to finance its long term assets. This is achieved in the form of a £600m amortising sterling bond with a final maturity date of 2026;

d. ensure that the ratio of bank funding to total gross borrowings does not exceed 75%; and

e. maintain a portfolio of debt diversified by source and maturity. This is achieved through the issuance of a £600m sterling bond that starts to amortise in 2012 and has a final maturity date of 2026 and by having available committed bank facilities totalling c.£216.2m of which £11m expires in 2010, £34.25m in 2011 and c.£170.95m in November 2012.

The following table shows the ratio of free cash to average monthly UK en route service income during the year:

	2010 £m	2009 £m
Average monthly UK en route services income	41.6	42.6
Free cash	42.8	45.2
Ratio of free cash to UK en route services income	1.0	1.1

The following table shows the ratio of the company's bank borrowings to its gross borrowings at 31 March:

	2010 £m	2009 £m
Bank borrowings	89.3	77.5
Gross borrowings	709.9	702.0
Bank borrowings as a percentage of gross borrowings	12.6%	11.0%

Maturity of borrowings

The following table sets out the remaining contractual maturity of non-derivative financial liabilities. The tables have been drawn up based on the undiscounted cash flows of financial liabilities based on the earliest date on which the company can be required to repay. The table includes both interest and principal cash flows.

	2010				2009			
	Unsecured loans £m	Secured loans £m	Other liabilities £m	Total £m	Unsecured loans £m	Secured loans £m	Other liabilities £m	Total £m
Due within one year or less	1.3	35.2	52.8	89.3	2.0	35.3	59.9	97.2
Between one and two years	0.9	49.7	-	50.6	0.8	35.5	-	36.3
Due between two and five years	3.7	268.1	-	271.8	6.7	245.5	-	252.2
Due in more than five years	37.4	669.3	-	706.7	45.5	750.4	-	795.9
	43.3	1,022.3	52.8	1,118.4	55.0	1,066.7	59.9	1,181.6
Effect of interest, discount and unamortised bond issue costs	(20.3)	(341.5)	-	(361.8)	(27.9)	(398.5)	-	(426.4)
	23.0	680.8	52.8	756.6	27.1	668.2	59.9	755.2

In order to manage the liquidity risk arising on the contractual maturity of its borrowings, it is the company's intention to replace bank facilities and bonds with facilities of a similar nature at least 12 months in advance of contractual maturity.

The following table sets out the maturity profile of the derivative financial liabilities. Cash flows under the index-linked swap are not fixed and are subject to movements in inflation. Accordingly, the cash flows associated with the index-linked swap have been derived from the company's long term forecasts of inflation as used for business planning purposes. The table shows undiscounted net cash inflows/(outflows) on these derivatives.

	Due within one year or less £m	Between one and two years £m	Due between two and five years £m	Due in more than five years £m	Total £m
2010					
Net settled:					
Index-linked swap receivable/(payable)	3.3	3.2	8.1	(112.0)	(97.4)
Gross settled:					
Foreign exchange forward contract receivables	121.7	4.8	-	-	126.5
Foreign exchange forward contract payables	(122.2)	(4.7)	-	-	(126.9)
	2.8	3.3	8.1	(112.0)	(97.8)
2009					
Net settled:					
Index-linked swap receivable/(payable)	3.5	3.5	9.1	(109.1)	(93.0)
Gross settled:					
Foreign exchange forward contract receivables	69.5	-	-	-	69.5
Foreign exchange forward contract payables	(73.9)	-	-	-	(73.9)
	(0.9)	3.5	9.1	(109.1)	(97.4)

18 Financial Instruments (continued)

Fair value of financial instruments
The fair value of forward exchange contracts represents the unrealised gain or loss on revaluation of the contracts to year end exchange rates and in the majority of cases is expected to be realised within one year. The fair value of the index-linked swap is determined independently by reference to contractual cash flows, forecast RPI inflation rates and is then discounted to its present value. The fair value of the £600m bond has been derived from its externally quoted price. The book values of other financial assets and liabilities approximate to their fair values because of their short maturities.

	Carrying amount		Fair value	
	2010	2009	2010	2009
	£m	£m	£m	£m
Financial assets				
Trade and other receivables, excluding prepayments and accrued income	38.2	41.4	38.2	41.4
Cash and short term investments	79.6	83.4	79.6	83.4
Derivative financial instruments				
Forward foreign exchange contracts	0.8	-	0.8	-
	118.6	124.8	118.6	124.8
Financial liabilities				
Trade and other payables	(52.8)	(59.9)	(52.8)	(59.9)
£600m 5.25% Guaranteed Secured Amortising Bond	(597.6)	(597.4)	(608.6)	(543.9)
Bank loans	(89.3)	(77.5)	(89.3)	(77.5)
Intercompany loan	(23.0)	(25.9)	(23.0)	(25.9)
Other loans	-	(1.2)	-	(1.2)
Derivative financial instruments				
Forward foreign exchange contracts	(1.1)	(1.8)	(1.1)	(1.8)
Index-linked swap	(87.0)	(80.7)	(87.0)	(80.8)
	(850.8)	(844.4)	(861.8)	(791.0)

19 Financial and other liabilities

Trade and other payables
The company had balances in respect of other non-interest bearing financial and other liabilities as follows:

	2010	2009
	£m	£m
Current		
Trade payables	13.5	11.6
Amounts due to other group undertakings	39.1	47.1
Other payables	0.2	1.2
Accruals and deferred income		
- deferred grants	1.4	1.7
- other	58.9	60.3
	113.1	121.9
Non-current		
Accrual and deferred income		
- deferred grants	4.5	5.9
- other	1.6	5.2
	6.1	11.1
	119.2	133.0

Trade creditors and accruals principally comprise amounts outstanding for trade purchases and ongoing costs. The average credit period taken for trade purchases is 44 days (2009: 38 days). The directors consider that the carrying amount of the trade payables approximates to their fair value.

20 Deferred tax

The following are the major deferred tax assets and liabilities recognised by the company, and movements thereon during the current and prior reporting periods.

	Accelerated tax depreciation	Retirement benefit asset	Financial Instruments	Other	Total
	£m	£m	£m	£m	£m
At 1 April 2008	90.8	86.9	(11.8)	(1.6)	164.3
Charge/(credit) to income	20.0	2.2	(0.4)	(1.4)	20.4
(Credit)/charge to equity	-	(103.6)	0.2	-	(103.4)
At 31 March 2009	110.8	(14.5)	(12.0)	(3.0)	81.3
At 1 April 2009	110.8	(14.5)	(12.0)	(3.0)	81.3
Charge/(credit) to income	20.4	(2.4)	(1.6)	(0.2)	16.2
Charge to equity	-	33.6	0.1	-	33.7
At 31 March 2010	131.2	16.7	(13.5)	(3.2)	131.2

Certain deferred tax assets and liabilities have been offset. The following is the analysis of the deferred tax balances (after offset) for financial reporting purposes.

	2010	2009
	£m	£m
Deferred tax liabilities	(147.9)	(110.8)
Deferred tax assets	16.7	29.5
	(131.2)	(81.3)

21 Share capital

	Authorised		Called up, allotted and fully paid	
	Number of shares	£m	Number of shares	£m
Ordinary shares of £1 each				
At 31 March 2009 and 31 March 2010	10,000,000	10.0	10,000,000	10.0

22 Notes to the cash flow statement

	Year ended 31 March 2010	Year ended 31 March 2009
	£m	£m
Operating profit from continuing operations	92.3	111.4
Adjustments for:		
Depreciation of property, plant and equipment	73.8	68.8
Amortisation of intangible assets	9.9	8.2
Impairment loss	2.4	2.7
Deferred grants released	(1.7)	(2.1)
Gain on disposal of property, plant and equipment	-	(0.8)
Non-cash element of charge for pension costs	8.3	(7.9)
Operating cash flows before movements in working capital	185.0	180.3
Increase in trade and other receivables	(13.9)	(7.2)
(Decrease)/increase in trade and other payables	(13.1)	8.5
Cash generated from operations	158.0	181.6
Tax paid	(0.1)	(14.4)
Net cash from operating activities	157.9	167.2

Cash and cash equivalents, which are presented as a single class of asset on the face of the balance sheet, comprise cash at bank and short term highly liquid investments with a maturity of three months or less.

23 Financial commitments

	2010 £m	2009 £m
Capital commitments contracted but not provided for in the accounts.	96.6	90.2
Minimum lease payments under operating leases recognised in the income statement for the year.	6.2	6.9

At the balance sheet date the company had outstanding commitments to future minimum lease payments under non-cancellable operating leases, which fall due as follows:

	2010 £m	2009 £m
Within one year	0.8	0.7
In the second to fifth years inclusive	1.4	1.7
After five years	33.2	36.1
	35.4	38.5

Operating lease payments represent rentals payable by the company for certain of its properties, equipment used for air navigation and vehicles. Leases are negotiated on varying terms depending on the type of asset leased.

Guarantees

NATS Holdings Limited has given guarantees to the Ministry of Defence in relation to NERL's performance under its contract with the MoD.

Technical breach of loan agreement

NERL's finance documents require that NERL complies with the terms of its air traffic services licence. In March 2009, NERL failed to comply with Condition 5.8 of its air traffic services Licence in not providing the Civil Aviation Authority (CAA) a certificate prior to declaring and subsequently paying a dividend to its parent company, NATS Limited. Following issuance in May 2010 of a notice under section 22 (11) of the Transport Act 2000 confirming that the CAA intended to take no action as a result of the Licence breach, NERL's lenders agreed to waive any breach of loan documents associated with this action.

24 Retirement benefit scheme

NATS Limited, the company's immediate parent undertaking, has entered into a deed of adherence with the CAA and the Trustees of the Civil Aviation Authority Pension Scheme whereby the company was admitted to participate in the Civil Aviation Authority Pension Scheme from 1 April 1996. At 31 March 2001, the business of NATS was separated from the CAA. As a consequence, NATS has become a "non associated employer" which requires the assets relating to the liabilities of NATS active employees at 31 March 2001 to be separately identified within the Pension Scheme. The Pension Scheme has been divided into two sections to accommodate this and a series of common investment funds established in which both sections will participate for investment purposes.

The Civil Aviation Authority Pension Scheme is a fully funded benefit scheme providing benefits based on final pensionable pay. The assets of the scheme are held in a separate trustee administered fund. Upon transfer of NATS Limited (formerly National Air Traffic Services Limited) to the Secretary of State, two separate sections of the scheme were established, namely the CAA section and the NATS section. The assets and membership of the scheme prior to transfer were allocated between these sections in accordance with Statutory Instrument 2001 Number 853, Transport Act 2000 (Civil Aviation Authority Pension Scheme) Order 2001.

During 2009 the parent company introduced a number of reforms to manage the cost and risk of pensions. The defined benefit pension scheme was closed to new joiners with effect from 31 March 2009. In addition, from 1 January 2009, annual increases in pensionable pay were limited to a maximum increase in the retail price index (RPI) plus 0.5%. A defined contribution scheme was also introduced for new joiners. NATS has agreed to match employee contributions to this scheme at a ratio of 2:1, up to a total employer cost of 18%. Finally, pension salary sacrifice arrangements were introduced with effect from 1 April 2009.

A Trustees' funding assessment of the NATS section is prepared at least every three years by the pension scheme actuary at the request of the Trustees in order to establish the financial position of the NATS section and to determine the level of contributions to be paid by NATS in future.

For the purpose of accounting for the scheme in these financial statements, the company obtains an updated valuation from a qualified independent actuary that is prepared in accordance with international accounting standards.

The two valuations differ in a number of critical respects, including, for example, differences in timing and frequency as well as in valuation assumptions. The Trustees' latest funding assessment was prepared as at 31 December 2009, whereas the company's accounting valuation is prepared annually at 31 March. As a result, at each valuation date, the market conditions on which the assumptions are based will be different. Also, the assumptions adopted for the Trustees' funding assessment are set by the Trustees and include appropriate margins for prudence, whereas those adopted for the company's accounting valuation are prescribed by international accounting standards and reflect best estimates.

Trustees' funding assessment
The last Trustees' funding assessment of the NATS' section was carried out at 31 December 2009 and used the projected unit credit method. The assumptions which have the most significant effect on the result of the valuation are those relating to the rate of return on investments and the rates of increase in salaries and pensions. For the purpose of the Trustees' funding assessment, it was assumed that the annual investment returns before retirement will be 3.0% higher than the annual general increases in salaries (allowance is also made for further salary increases due to promotions) and the annual investment returns for pensions in payment will be 0.75% higher than the annual increases in pensions.

The market value of the NATS' section's assets as at 31 December 2009 was £2,793.9m. For the purpose of the Trustees' funding assessment assets were taken at market value. The assets were sufficient to cover 89% of the benefits that had accrued to existing members.

NATS Limited, the immediate parent of the company, is the employer of, and seconds to the company, all personnel who undertake the company's business. In that capacity, NATS Limited participates in Civil Aviation Authority Pension Scheme and bears the employment (including pension) costs of those personnel.

The company pays fees to NATS Limited for the provision of services, including those of the staff. An element of those fees represents the employment costs (including pension contributions) of staff provided by NATS Limited to NERL. In that way, the existence of a pension deficit or surplus may have an indirect impact upon the company through variations in pension contributions and so the level of those fees.

Contributions to the pension scheme
During the year the company paid cash contributions to the scheme of £79.5m (2009: £52.0m). This amount included £12.0m (2009: nil) of wages and salaries sacrificed by employees in return for pension contributions. Excluding the effect of salary sacrifice, employer cash contributions were paid at a rate of 27.5% (2009: 22.0%) of pensionable pay. The group is increasing these cash contributions from May 2010 to 36.7% of pensionable pay, equivalent to the future service cost. In response to the triennial valuation, NATS has also agreed a deficit recovery plan with Trustees and from January 2011 it will make further contributions of £2.0m per month for calendar year 2011 (NERL's share being c.£1.5m), increasing these by 3.5% each January thereafter.

24 Retirement benefit scheme (continued)

Company's accounting valuation under international accounting standards
The pension cost under International Accounting Standard 19, Employee benefits, relating to the scheme is assessed in accordance with the advice of independent qualified actuaries.

On transition to IFRS, NATS elected to adopt a 'clean start' approach which recognised all actuarial gains and losses at 1 April 2004, and NATS has reported under an immediate recognition approach in subsequent periods.

A Trustees' funding assessment was carried out as at 31 December 2009 and updated to 31 March 2010 for the company's accounting valuation under IAS 19 by a qualified actuary. The major assumptions used by the actuary for the purposes of the IAS 19 figures at the relevant year ends are set out in the table and narrative below:

	2010	2009	2008
Inflation	3.65%	3.40%	3.60%
Increase in:			
- salaries	4.15%	3.90%	4.80%
- deferred pensions	3.65%	3.40%	3.60%
- pensions in payment	3.65%	3.40%	3.60%
Expected return on:			
- equities	7.55%	7.05%	7.60%
- property and other assets	7.55%	7.05%	7.60%
- bonds	4.90%	4.40%	4.95%
Discount rate for scheme liabilities	5.65%	6.40%	6.20%

The company moderated the salary growth assumption in the first half of the 2009 financial year in line with a general lowering of expectations and its business plan assumptions.

The mortality assumptions have been drawn from actuarial tables 82% S1NMA and 101% S1NFA medium cohort with a 1% underpin (2009: PMA92 and PFA92 medium cohort). These tables assume that the life expectancy, from age 60, for a male pensioner is 27.6 years and a female pensioner is 28.7 years. Allowance is made for future improvements in longevity, such that based on the average age of the current membership, when these members reach retirement, life expectancy from age 60 will have increased for males to 29.3 years and for females to 30.2 years.

The sensitivities regarding the principal assumptions used to measure the scheme liabilities are set out below:

Assumption:	Change in assumption:	Impact on scheme liabilities
Discount rate	Increase/decrease by 0.5%	Decrease by 11.1%/Increase by 13.0%
Rate of inflation	Increase/decrease by 0.5%	Increase by 13.2%/Decrease by 11.3%
Rate of salary growth	Increase/decrease by 0.5%	Increase by 4.4%/Decrease by 4.2%
Rate of mortality	Increase by 1 year	Increase by 1.9%

Amounts recognised in income in respect of the defined benefit scheme are as follows:

	2010 £m	2009 £m
Current service cost	(73.2)	(74.1)
Past service cost	(8.7)	(5.0)
Expected return on scheme assets	102.7	149.2
Interest cost on scheme liabilities	(108.6)	(114.2)
Total defined benefit charge recognised in arriving at operating profit	(87.8)	(44.1)

Amounts taken to the statement of other comprehensive income are as follows:

	2010 £m	2009 £m
Actual return less expected return on scheme assets	421.4	(653.6)
Experience gains and losses arising on scheme liabilities	164.0	33.1
Changes in assumptions underlying the present value of the scheme liabilities	(465.6)	250.4
	119.8	(370.1)

24 Retirement benefit scheme (continued)

The amount included in the balance sheet arising from the group's obligations in respect of its defined benefit retirement benefit schemes is as follows:

	2010	2009
	£m	£m
Fair value of scheme assets	2,179.8	1,641.0
Present value of defined benefit obligations	(2,120.1)	(1,692.8)
Surplus/(deficit) in scheme	59.7	(51.8)

Movements in the fair value of scheme assets during the year were as follows:

	2010	2009
	£m	£m
At 1 April	1,641.0	2,136.3
Expected return on scheme assets	102.7	149.2
Actuarial gains and losses	421.4	(653.6)
Contributions from scheme members	0.2	12.2
Contributions from company	79.5	52.0
Benefits paid	(65.0)	(55.1)
At 31 March	2,179.8	1,641.0

Movements in the present value of the defined benefit obligations were as follows:	2010	2009
	£m	£m
At 1 April	(1,692.8)	(1,825.9)
Current service cost	(73.2)	(74.1)
Past service costs	(8.7)	(5.0)
Interest cost	(108.6)	(114.2)
Actuarial gains and losses	(301.6)	283.5
Contributions from scheme members	(0.2)	(12.2)
Benefits paid	65.0	55.1
At 31 March	(2,120.1)	(1,692.8)

The analysis of the scheme assets and the expected rate of return at the balance sheet date was as follows:

	Fair value of assets		Expected return	
	2010	2009	2010	2009
	£m	£m	%	%
Equity Instruments	1,144.7	863.5	7.55	7.05
Property and other assets	283.0	267.8	7.55	7.05
Bonds	721.3	483.9	4.90	4.40
Cash	30.8	25.8	4.90	4.40
	2,179.8	1,641.0	6.64	6.23

24 Retirement benefit scheme (continued)

The five year history of experience adjustments is as follows:

	2010 £m	2009 £m	2008 £m	2007 £m	2006 £m
Present value of defined benefit obligations	(2,120.1)	(1,692.8)	(1,825.9)	(1,946.8)	(1,857.8)
Fair value of scheme assets	2,179.8	1,641.0	2,136.3	2,125.9	2,014.0
Surplus/(deficit) in the scheme	59.7	(51.8)	310.4	179.1	156.2
Experience adjustments in scheme liabilities					
Amount (£m)	164.0	33.1	73.7	34.1	22.0
Percentage of scheme liabilities	(7.7%)	(2.0%)	(4.0%)	(1.8%)	(1.2%)
Experience adjustments in scheme assets					
Amount (£m)	421.4	(653.6)	(129.8)	(15.5)	322.2
Percentage of scheme assets	19.3%	(39.8%)	(6.1%)	(0.7%)	16.0%

25 Related party transactions

The NATS group has four major shareholders - the Crown, The Airline Group (AG), BAA Limited and the NATS Employee Share Trust Limited.

AG is a consortium of seven airlines: British Airways, bmi, easyJet, Monarch, Thomas Cook Airlines, Thomson Airways and Virgin Atlantic.
AG has a 42% stake in NATS Holdings Limited which it purchased through the PPP transaction in July 2001. The directors of NATS Holdings Limited are satisfied that the seven members of the AG have not exercised undue influence on the group either acting individually or in concert and therefore the individual transactions with each member of AG have not been disclosed in this set of accounts.

Trading transactions

	Sales		Purchases		Amounts owed by related parties		Amounts owed to related parties	
	Year ended 31 March 2010	Year ended 31 March 2009	Year ended 31 March 2010	Year ended 31 March 2009	Year ended 31 March 2010	Year ended 31 March 2009	Year ended 31 March 2010	Year ended 31 March 2009
	£m	£m	£m	£m	£m	£m	£m	£m
BAA Ltd	-	-	0.4	-	-	-	-	-
Ministry of Defence (MoD)	44.3	45.1	4.2	3.6	-	-	5.3	4.5
Department for Transport (DfT)	0.6	1.3	-	-	0.1	0.1	-	-
Meteorological Office	-	0.1	-	0.7	-	-	-	0.1

Sales are made to related parties at the company's usual rates and purchases at market prices. The amounts outstanding are unsecured and will be settled in cash. No guarantees have been received. No provisions have been made for doubtful debts in respect of amounts owed by related parties.

Directors' remuneration

The Report of the Directors on page 20 includes details of the directors of the company. None of these directors received any fees in the year for their services as directors of this company. The consolidated accounts of NATS Holdings Limited include details of the remuneration received by the directors of the group.

Directors' transactions

Paul Barron has disclosed a related party transaction in that his wife Dawn Barron of Human Alchemy had been engaged by the business during the financial year 2009/10 at a cost of £105,555 (2009: £129,673). This work was at the request of Philip James, NATS HR Director and Ian Mills, NERL Managing Director who have utilised her skills and understanding in specific leadership tools and techniques being introduced across the company. There was £7,000 outstanding at 31 March 2010 (2009: £nil).

26 Parent undertaking

The company's ultimate parent undertaking and controlling party is NATS Holdings Limited a private company incorporated in Great Britain and registered in England and Wales.

The largest and smallest group in which the results of the company are consolidated is that of which NATS Holdings Limited is the parent company. The consolidated accounts of NATS Holdings Limited can be obtained from the company's secretary, at its registered office, 5th Floor, Brettenham House South, Lancaster Place, London WC2E 7EN.

27 Events after the reporting period

Airspace use restrictions were imposed by the UK and European aviation authorities in response to the risks to aircraft safety from a volcanic ash cloud that drifted across UK and European airspace following the eruption of an Icelandic volcano. This resulted in severely reduced air traffic volumes for a period of 6 days from 15 April 2010 and intermittent disruption through May 2010. The financial effects of this were a cash shortfall from lower billings to customers of c. £10m and a reduction in revenues for the financial year ending 31 March 2011 of c. £5m, reflecting volume protections provided to NERL in the economic regulatory formula. No adjustment has been made to the result for the year ended 31 March 2010 or the financial position at that date.

NATS and others have received correspondence from Ryanair in relation to the volcanic ash contamination of UK airspace in April and May 2010. This correspondence may lead to a legal claim for damages for economic losses allegedly incurred as a result of flight restrictions. At this time it is not possible to quantify the amount of any such claim. The Directors believe, based on advice from NATS' solicitors and Leading Counsel, that a claim for damages arising from Ryanair's correspondence would be unlikely to succeed.

In May 2010 the board approved and paid an interim dividend for the year ended 31 March 2011 of £1.50 per share (totalling £15m) to its parent company NATS Limited.