NATS (En Route) plc

Financial statements
for the year ended 31 March 2008

Company Number: 4129273

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Company No. 4129273

Auditors

Deloitte & Touche 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 2008.

Highlights

- NERL handled a record 2.5m flights during the year, an increase of 3.1% on the prior year.
- Average delay per flight was 26.8 seconds (2007: 22.6 seconds) in an environment of record traffic levels.
- In November the company successfully transferred the London Terminal Control operation from West Drayton to the London Area Control centre at Swanwick in Hampshire. The project was completed on time and within budget and was the culmination of four years work, involved major equipment rebuild and replacement and the relocation of 500 staff.
- A Lower Airspace Radar Service (LARS) was launched in September to enhance safety. This service has prevented 250 infringements of controlled airspace to date.
- In September, Standard & Poor's upgraded NERL's credit rating from A- to A. This enabled the company to redeem its £65m shareholder loans in December.
- NERL reported a profit before tax of £62.5m, lower than last year's £86.3m. This was expected and inevitable because of the cost of closing the air traffic control centre at West Drayton and the redemption fees associated with our plans to repay shareholder loans. Overall, exceptional operating costs amounted to £20.1m and exceptional finance costs were £15.8m. Exclude these factors and our results were once again very creditable.
- Revenue increased by £29.4m to £617.5m (2007: £588.1m). Operating costs, after exceptional costs and net of gains on asset disposals, increased by £33.5m to £492.1m (2007: £458.6m net). Operating profit was £125.4m (2007: £129.5m). Net finance costs after exceptional costs, amounted to £62.9m (2007: £43.2m).
- Net debt increased by £59.7m to £598.0m (2007: £538.3m) as the company drew down on its bank facilities to fund a dividend of £107.6m to its parent, NATS Limited. This was part of the group's strategy to repay more expensive shareholder loans held by NERL and NATS Limited.

Vision 2011

Earlier this year, NERL set out its strategic plan for the next three years, called Vision 2011. Underpinning this plan are the six brand values that are core to the NATS Group.

The NATS brand values define who we are and what we stand for as a business. Because they set the context for the work ahead - I have used them as the headings for the rest of my report – to be Proactive in Safety; Tuned In to Customers; Driving Efficiency; Great Partners to Work With; Acting Responsibly and Liberating and Inspiring People.

Proactive in Safety

NERL's first priority will always be safety - maintaining safe separation between aircraft both in the air and on the ground. In safety, NERL continues to maintain its performance against a background of rising traffic – up three per cent to nearly 2.5m flights for another record year. While the number of airproxes attributable to NERL rose from 8 to 11, there were no risk-bearing airprox in the financial year (2007: 1). The airprox summary for the NATS Group is included in the business and financial review section of the accounts of NATS Holdings Limited.

Our ten-year strategic safety plan, safety management system, governance processes for reviewing, monitoring and taking risk reduction actions enable appropriate monitoring of safety performance and help to mitigate safety risk. We believe that we continue to set new standards in this area in which we are regarded as world-leading.

We are already reaching beyond our direct responsibility to improve safety. In September we launched a Lower Airspace Radar Service (LARS) in the uncontrolled airspace underneath and around the controlled airspace used by commercial flights into and out of the London airports.

We had no regulatory obligation to do this – but we saw an opportunity to improve safety. NERL covered the start-up costs of £1m and will absorb the estimated cost of £0.5m.

LARS has already prevented more than 250 infringements of controlled airspace by light aircraft.

This project was complemented by the Controlled Airspace Infringement Tool, or CAIT, which highlights on the radar screen private aircraft mistakenly flying into controlled airspace around the London airports.

These two projects have resulted in a 40% reduction in infringements – and we expect further benefits.

Controllers at our Manchester centre benefited from the extension of the Mode-S radar aid, which continues to reduce the number of incidents where aircraft climb or descend to the wrong altitude, posing a possible safety risk.

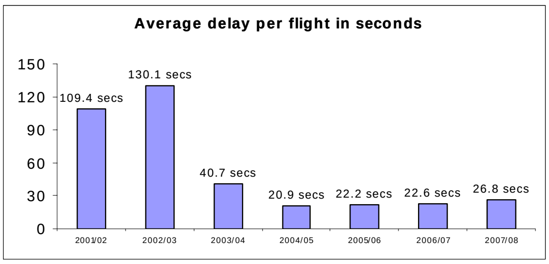
The Air Traffic Management (ATM) industry is key to ensuring our skies remain safe, no matter how many aircraft fly through them, no matter where they fly. And that, in my view, is why we in air traffic management are the natural leaders in shaping a new future of even safer aviation.

Tuned in to Customers & Driving Efficiency

NERL exists to serve its customers. That means listening to their requirements – meeting them cost effectively, and challenging them when we believe it is right to do so.

These two brand values are inextricably interlinked – because efficiency is at the heart of what our customers want. For NERL, driving efficiency is mainly about delivering benefits from our projects faster while retaining safety and service standards.

A slight rise in delay attributable to NERL of 26.8 seconds per flight compared to 22.6 seconds last year should be seen in the context of growing traffic and it should also be noted that this is well within our economic regulatory target of 45 seconds. The number of flights receiving no NATS-attributable delay was 97.5 per cent, compared to 97.7 per cent last year.



Our customers expect us to continue to provide capacity for growth and to minimise delay. To ensure that we are able to meet this expectation we are improving systems infrastructure and service resilience and have a programme that safeguards our facilities and provides contingency. We are also ensuring that we have sufficient numbers of trained air traffic controllers as we transfer between centres and develop new systems.

NERL's project capability rating, using an internal equivalent to the internationally recognised CMM standard which rates five the highest score, has been upgraded from 1.8 in 2004 to 3.7 in 2007. I applaud our people for making that happen. The development of our project management capability helps mitigate programme risk such as delays and cost over-runs.

iFACTS, the advanced controller tool which NERL has been developing for almost ten years, is nearing implementation. Previously planned for 2009, and now with an optimised schedule of Winter 2010, this is the most technically challenging project NATS has ever undertaken. The team working on it can be proud that they will deliver what will be the most significant innovation in ATM since radar, bringing with it marked safety and efficiency benefits.

Great Partners to Work With

Partnership can have different meanings and includes a wide range of different relationships. NERL is developing important partnerships within the industry to achieve a new vision for ATM across the world – and particularly in Europe. We are partners in the SESAR project to redraw the airways over Europe, creating a harmonised air traffic system to handle sustainably a forecast doubling in flight numbers by 2020, ever more safely, ever more efficiently.

I am pleased NERL has been accepted as part of the Joint Undertaking at the centre of the project. Our relationship with Europe is central to our future success and this year I made that clear to the business by creating a Directorate of European and Government Affairs. With our German and Spanish air traffic service partners, we are developing the next generation of air traffic management tools by investing to build the iTEC flight data processing system with the Spanish company, Indra.

NERL has continued discussions with the Irish Aviation Authority aimed at developing an agreement for a Functional Airspace Block (FAB) involving UK and Irish airspace. Our respective governments have just announced the FAB and I look forward to delivering operational benefits for our customers in the coming year.

It is not just in Europe where we are forging new relationships. In June, I was elected to the executive committee of CANSO – the Civil Air Navigation Services Organisation, which provides the global voice of ATM. I have personally committed to driving forward CANSO's environmental agenda and I intend to do all I can to support the chairman and director general in pursuing a collective vision of future innovation in ATM worldwide.

Partnerships much closer to home, be they with airports, airlines or our valuable close co-operation with our military colleagues have never been more important to our future success. Our fifteen-year, £750m contract to provide air traffic services for the military continues to lead to a more integrated approach, with nearly 200 service personnel now based at Swanwick.

Acting Responsibly

We are constantly challenging ourselves to strive for what seem to be demanding targets - none more so than our stance on climate change.

NERL has become the first air traffic service provider to set stretching environmental targets.

Our aim is to unite the industry in achieving a reduction, on average, of ten per cent per flight in ATM CO_2 by 2020, against a 2006 baseline, whilst also achieving a carbon-neutral estate by 2011.

In spite of rising traffic, our position as a business is to manage and, where possible, reduce the environmental impact of aviation down to air traffic control, however difficult that may be. This includes noise and emissions.

Many years ago, NERL pioneered Continuous Descent Approaches at British airports for quieter, smoother and more efficient landing profiles. Today, we are examining every aspect of our business to see where we can be "greener".

I have been telling our partners here and abroad that we can be a catalyst for action. In a speech to the Air Traffic Control Association in October, I challenged our air traffic colleagues worldwide to spark a radical overhaul to match the pace of change achieved by manufacturers, airlines and airports. Our partners across the industry expect nothing less.

We launched the world's biggest-ever consultation on proposed airspace change – Terminal Control North – for the skies serving the London airports. We have issued more than 3,000 consultation documents, and created a website with a postcode search and an explanatory video to help people living in the area understand our proposals for managing air traffic growth safely and efficiently in one of the most complex areas of airspace in the world.

This follows the consultation carried out last year for airspace over central and southern England – the Terminal Control South West proposal was approved by the Civil Aviation Authority earlier this year and implemented in April. Our experts have also contributed to the Government's consultation on proposals for expanding Heathrow's operations.

Liberating and Inspiring People

The single uniting factor across our business is our people. Everything we achieve is done so through the commitment and professionalism of an incredibly capable workforce. I would like to thank our employees for their outstanding contribution.

We continue to work closely with our union colleagues. This is a crucial partnership and one that we continue to develop across both our businesses and the different challenges they face. It is a robust relationship; we don't always agree but we always talk. That is entirely healthy and I am committed to ensure we continue to respect, and challenge, each other's views.

Working Together is important in maintaining good industrial relations and is especially important in the context of our challenging conversations about the future of the pension fund. Together, we commissioned an independent report this year and we are working with the unions to develop options to mitigate the potential future costs and risks of the pension scheme on our business.

Overview of Financial Performance

The company, which operates UK and North Atlantic en route air traffic control services (see below), generated a profit before tax for the year of £62.5m (2007: £86.3m). The results, summarised in the table below, were materially affected by two exceptional factors that were expected to arise in the financial year: the closure of the air traffic control centre at West Drayton, and the relocation of operations to Swanwick as part of the group's ongoing rationalisation of its air traffic control infrastructure from four centres to two, and the repayment of high interest shareholder loan notes financed by the company's strong operating cash flows. The repayment incurred an early redemption charge of £15.8m. The prior year's result also included the benefit of asset disposals.

	2008 £m	2007 £m
Turnover	**617.5**	588.1
Costs		
- Costs before exceptional items	(473.2)	(463.4)
- Exceptional items	(18.9)	4.8
	(492.1)	(458.6)
Operating profit		
- Operating profit before exceptional items	144.3	124.7
- Exceptional items	(18.9)	4.8
	125.4	129.5
Finance costs (net)		
- Net finance costs before exceptional items	(47.1)	(43.2)
- Exceptional finance costs	(15.8)	-
	(62.9)	(43.2)
Profit before taxation		
- Profit before tax and exceptional items	97.2	81.5
- Exceptional items	(34.7)	4.8
	62.5	86.3
Tax	**(15.4)**	(23.1)
Profit for the year	**47.1**	63.2

Profit before these items was better than the previous year. Revenues improved by £29.4m or 5.0%, from a combination of higher traffic volumes and some benefit from exchange gains from the stronger Euro. Operating costs before exceptional factors rose by £9.8m or 2.1%, due mainly to higher staff costs associated with inflation-linked increases in wages and salaries, provisions for holiday pay and employee share scheme costs and the buy-out of allowances. Net finance costs, before the redemption payment, were higher by £3.9m or 9.0% due mainly to marking to market fair value losses on derivatives.

Revenues

Revenues increased by £29.4m to £617.5m (2007: £588.1m) driven by an increase in revenue from the UK and North Atlantic en route businesses, explained in more detail below, and growth in MOD income.

	2008 £m	2007 £m
UK en route services	**522.2**	496.3
Support services to MoD	**43.2**	40.9
London approach services	**8.7**	8.6
North Sea helicopters	**6.3**	6.4
	580.4	552.2
Services to other group companies	**13.3**	13.4
UK air traffic services	**593.7**	565.6
North Atlantic air traffic services	**23.8**	22.5
	617.5	588.1

Operating costs

Included within operating costs are items we consider to be exceptional but are not defined as such in the financial statements.

Operating costs for the year are analysed as follows:

	2008 £m	2007 £m
Before exceptional items:		
Employee costs	**(252.0)**	(241.5)
Service and materials	**(53.9)**	(55.6)
Repairs and maintenance	**(23.2)**	(23.4)
External research and development	**(0.3)**	(0.5)
Other operating charges (net)	**(64.2)**	(59.4)
	(393.6)	(380.4)
Depreciation, amortisation and impairment	**(82.8)**	(87.5)
Deferred grants	**3.2**	4.5
Operating costs	**(473.2)**	(463.4)
Exceptional operating items (net)	**(18.9)**	4.8

Before exceptional items and asset related charges, operating costs were £393.6m or £13.2m (3.5%) higher than previously (2007: £380.4m).

Staff costs, before exceptional items, at £252.0m were £10.5m more than prior year (2007: £241.5m) reflecting inflationary increases in wages and salaries. Other factors included higher employee share scheme costs following an 84% increase in the price of employee shares during the year and higher charges for holiday pay and the buy-out of staff allowances. Staff costs also included a charge of £40.3m for pension costs (2007: £40.5m).

The company employed an average of 3,797 (2007: 3,895) staff through the year. Employees in post at 31 March 2008 fell by 164 to 3,742 (2007: 3,906).

Non-staff costs at £141.6m increased by a rate of 1.9%, less than inflation, or £2.7m (2007: £138.9m).

Depreciation, amortisation and impairment charges of £82.8m (2007: £87.5m) were incurred in the year. The current year included the effect of a full year's charge for the new Prestwick centre building. Impairment charges of £1.3m (2007: £12.5m) were £11.2m lower than last year and £3.2m (2007: £4.5m) of deferred grant income was recognised.

Exceptional operating items (net)	2008 £m	2007 £m
Redundancy and related costs	**(14.6)**	(2.3)
Relocation costs	**(5.5)**	(2.3)
	(20.1)	(4.6)
Profit on disposal of non-current assets	**1.2**	9.4
	(18.9)	4.8

NERL incurred £18.9m of net exceptional losses in the year (2007: £4.8m net gains). Charges of £20.1m were incurred for redundancy and staff relocation costs (2007: £4.6m) and mainly reflected the closure of West Drayton and the relocation of staff to the Swanwick area. Redundancy-related costs included a one-off charge of £3.0m to secure staff agreement to changes in redundancy terms necessary to comply with age discrimination legislation. The company also realised exceptional gains of £1.2m (2007: £9.4m gains) from property disposals.

The company reported underlying net finance costs of £47.1m (2007: £43.2m) in the year. This included lower net interest payable of £28.1m (2007: £32.8m), which reflected the benefits of lower gearing and the repayment of shareholder loan notes, offset by higher charges of £19m (2007: £10.4m) from marking to market its £200m index-linked swap. The value of the latter is dependent on market expectations of inflation and yields on long-dated gilts. The company also incurred an exceptional redemption payment of £15.8m associated with the repayment of the £65m perpetual 11.3575% shareholder loan notes. The early redemption payment was a condition of the loan agreement that ensured that investors (BAA and HM Government) received a defined required return on the total investment that they made in equity and loans when the company's debt was restructured in 2003.

The tax charge was £15.4m (2007: £23.1m) at an effective rate of 24.6% (2007: 26.8%). Factors affecting the tax charge for the year are set out in note 11 to the accounts.

Overall, NERL reported a profit before tax of £62.5m (2007: £86.3m).

UK air traffic services

	2008 £m	2007 £m
Turnover	**593.7**	565.6
Operating costs	**(376.1)**	(364.2)
Depreciation, amortisation, impairment and deferred grants	**(77.1)**	(81.2)
Exceptional items	**(18.9)**	5.0
Operating profit	**121.6**	125.2
Chargeable Distance (millions km)	**799.1**	772.0
Chargeable Service Units (000)	**10,850**	10,400

UK air traffic services are provided under the regulatory regime and comprise UK en route services, London approach services, services provided under the contract with the MoD and services to North Sea helicopter operators.

Revenues from these sources can be analysed as follows:

	2008 £m	2007 £m
UK en route services	**522.2**	496.3
Support services to MoD	**43.2**	40.9
London approach services	**8.7**	8.6
North Sea helicopters	**6.3**	6.4
	580.4	552.2
Services to other group companies	**13.3**	13.4
	593.7	565.6

Income from UK en route services, which are provided to traffic operating in those parts of UK airspace which constitute controlled airspace, increased by £25.9m in the year to £522.2m (2007: £496.3m). Over a third of this increase arose from the annual adjustment to prices under the RPI minus “X” price control formula.

	2007/08 ('000s)	2006/07 ('000s)	% change in year
Chargeable Service Units	**10,850**	10,400	4.3%
Chargeable Distance (km)	**799,071**	772,041	3.5%
Total UK traffic (flights):			
Domestic	**495**	502	(1.4%)
Transatlantic	**343**	325	5.6%
Other	**1,642**	1,579	4.0%
Total	**2,480**	2,406	3.1%
Oceanic traffic (flights)			
Total flights	**422**	396	6.5%

A further third arose from higher volumes (up 3.5% to 799.1m kilometres) whereby NERL benefits from 50% of the revenues above a regulatory baseline. The volume risk sharing mechanism also affords some protection against traffic downturns. The remainder of the revenue uplift arose from exchange gains from the strengthening Euro, including the re-translation of receivables. It is the group’s policy to hedge 90% of forecast UK en route services revenues.

London approach services, which are provided to aircraft arriving at or departing from Heathrow, Gatwick and Stansted airports, generated £8.7m (2007: £8.6m). Revenues from these services are combined with those from UK en route services and capped by the charge control conditions. The specific charge for London Approach is set after consultation with airlines and levied based on aircraft tonnage. Rates per tonne remained unchanged in the year at 20 pence up to 100 tonnes and 8 pence per tonne above this. Landed tonnage increased by 1.6% to 55.7m tonnes (2007: 54.8m tonnes).

NERL has a service contract, that became effective in July 2006, to provide services and support infrastructure to the MOD for military air traffic services. Revenues generated under the contract amounted to £43.2m (2007: £40.9m) with the increase arising from a combination of higher rates and additional services provided.

Charges for services to North Sea helicopter operators are levied on the basis of a charge per flight. Revenues decreased by £0.1m to £6.3m (2007: £6.4m) reflecting rate changes. Volumes remained flat at 38,495 (2007: 38,447).

Operating costs for UK air traffic services increased by 3.3% to £376.1m (2007: £364.2m) largely due to higher staff-related costs associated with pay awards, increased provisions for holiday pay, employee share scheme costs and the buy-out of London weighting allowances following staff relocation to the Swanwick area on closure of West Drayton.

Asset-related charges for depreciation, amortisation and impairment net of deferred grants fell by £4.1m to £77.1m (2007: £81.2m) as lower impairment charges were partly offset by higher underlying depreciation charges.

Exceptional losses of £18.9m, (2007: £5.0m net gains) mainly related to redundancy and relocation costs largely associated with the West Drayton centre closure and to a one-off payment to staff to compensate for the changes to redundancy terms that were required to comply with age discrimination legislation. The previous year's results included the benefit of gains on property sales of £8.5m.

UK air traffic services generated an operating profit of £121.6m for the year which was £3.6m lower than last year (2007: £125.2m) due to these exceptional costs.

North Atlantic air traffic services

	2008 £m	2007 £m
Turnover	**23.8**	22.5
Operating costs	**(17.5)**	(16.2)
Depreciation and amortisation	**(2.5)**	(1.8)
Exceptional items	**-**	(0.2)
Operating profit	**3.8**	4.3
Total flights (000)	**422**	396
Chargeable flights (000)	**420**	394

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 regulatory charge control conditions that allow for the annual adjustment of prices by the movement in the RPI less a specified percentage. Revenues at £23.8m (2007: £22.5m) were £1.3m higher than the prior year. Flight volumes increased by 6.6% to 420,267 and accounted for a £1.4m increase that was partly offset by a 0.6% reduction in the rate per flight from £56.01 to £55.68.

Operating costs at £17.5m were £1.3m higher than the previous year (2007: £16.2m) due to higher staff-related costs. Asset-related charges for depreciation, amortisation and impairment net of deferred grants also increased by £0.7m to £2.5m (2007: £1.8m) as the flight data processing system used to support North Atlantic operations at Prestwick went operational in the year.

Overall, North Atlantic air traffic services generated an operating profit of £3.8m, £0.5m lower than the previous year (2007: £4.3m) principally due to higher staff costs and depreciation charges.

Balance sheet

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

	2008 £m	2007 £m
Goodwill	**351.0**	351.0
Intangible fixed assets	**114.2**	92.7
Property, plant and equipment	**584.9**	557.0
Retirement benefit asset	**310.4**	179.1
Other non current assets	**3.9**	2.5
Cash and short term deposits	**93.2**	138.2
Other net current liabilities	**(85.7)**	(48.1)
Total assets less current liabilities	**1,371.9**	1,272.4
Borrowings	**(691.2)**	(676.5)
Provisions and other non-current liabilities	**(171.8)**	(134.1)
Net assets	**508.9**	461.8

Shareholders' funds increased £47.1m to £508.9m during the year (2007: £461.8m). This increase was primarily due to retained profit of £47.1m and the increase in the pension asset of £94.5m (net of deferred tax).

Other non current assets, of £3.9m (2007: £2.5m) include the deferred consideration on the sale of property. Other net current liabilities were £37.6m higher than the previous year principally due to an increase in the fair value liabilities of derivative financial instruments, as well as increases in holiday pay and employee share valuation costs.

Provisions and other non-current liabilities of £171.8m (2007: £134.1m) include deferred tax provisions which, at £164.3m, are £39.5m higher than prior year. The deferred tax effect of timing differences has been assessed at 28%, being the corporation tax rate applicable from 1 April 2008. This rate change reduced the provision required by £12.1m and partly offset increases arising mainly from the increase in the pension asset and accelerated capital allowances.

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

Capital expenditure

Additions to intangible and tangible assets are summarised by programme below:

	2008 £m	2007 £m
Airspace development	**3.9**	4.8
Business systems and relocation to CTC	**6.7**	14.0
Future centres programme	**22.3**	23.9
Communications, navigation and surveillance	**19.1**	11.4
Radar site services	**16.5**	16.7
Current software systems	**26.8**	20.5
Prestwick/Manchester programme	**23.6**	23.4
Swanwick/West Drayton programme	**9.8**	19.1
Other	**4.0**	2.7
Total	**132.7**	136.5

Capital expenditure for the year at £132.7m (2007: £136.5m) was £3.8m less than the prior year. The reduction in expenditure mainly reflects the successful transfer of the civil and military air traffic control operations from West Drayton to Swanwick, a reduction in spend on the Prestwick air traffic control centre which is nearing completion, and lower spend on non-operational information systems following the implementation of new systems at the start of the year.

Significant investment continued to be made on: the Future Centres programme to develop common platforms for centre systems, advanced controller tools and interoperability with other European air traffic service providers; data and voice networks, including the upgrades of tower systems for aircraft navigation; upgrades to the radar infrastructure; enhancing the capacity and resilience of software and display systems; and preparations for the move of the Manchester control centre to Prestwick and the new Prestwick building and systems.

Pensions

At 31 March 2008, under international accounting standards, the company's share of the NATS pension scheme had a surplus of assets over future liabilities of £310.4m (117%) compared with a surplus of £179.1m (109%) at 31 March 2007. The £131.3m increase in the surplus is due mainly to a decrease in the present value of the obligations arising from an increase in the prescribed discount rate from 5.2% to 6.2%. The company's share of the scheme's assets increased by just £10.4m or 0.5% to £2,136.3m in the year.

The company made cash contributions to the scheme of 12.2% (2007: 12.2%) of pensionable pay during the year giving a cash cost of £28.2m (2007: £24.6m). From 1 April 2008, cash contributions to the scheme will be paid at an annual effective rate of 20% of pensionable pay. This follows the outcome of the triennial valuation performed as of 31 December 2006, which reported a surplus of assets over liabilities of 112% and an increase in the future service cost to 37.3% of pensionable pay (from 26.8% at 31 December 2003).

The company is currently engaged in discussions with its Trades Unions on proposals to reduce the cost and risk of future pension provision.

Treasury management

Strong cash flows from operations financed the company's capital programme, serviced interest on debt, enabled the repayment of shareholder loan notes and part financed a dividend to the parent company. The latter was also financed by drawing on bank facilities. The dividend enabled the company's parent to reduce its own debt.

As detailed below, the net debt of the company increased by £59.7m to £598.0m (2007: £538.3m).

Movements in net debt

	Cash and short term investments £m	Borrowings £m	Net debt £m
Balance at 31 March 2007	138.2	(676.5)	(538.3)
Cash flow	(43.8)	(13.9)	(57.7)
Short term investments	(1.2)	-	(1.2)
Non-cash movements:	-	(0.8)	(0.8)
Balance at 31 March 2008	**93.2**	**(691.2)**	**(598.0)**

Risks and uncertainties

The principal operational risks and uncertainties of the company are described above. Specifically, these include risks associated with aircraft safety, provision of en route capacity, service resilience, project delivery and industrial action.

The main financial risks of the company relate to the availability of funds to meet business needs, 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 85% (2007: 84%) of total turnover, 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 resultant currency risk is materially eliminated by entering into forward foreign exchange contracts. At the year end, forward foreign currency transactions, designated as cash flow hedges, equivalent to £72.3m were outstanding (2007: £69.4m) as detailed in note 19.
- interest rate and inflation risk: the company'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. At the time of the PPP in 2001, in view of NERL's high gearing and the fact that cash holdings were forecast to be minimal, the company adopted a policy of hedging projected gross borrowings. As a result of NERL's improved financial performance, cash holdings have increased significantly since 2001. Hence in September 2006, NERL moved from a strategy of hedging gross debt to hedging 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 was a hedge under UK GAAP but is required to be categorised under IFRS as held for trading.

As at 31 March 2008 (after derivatives), approximately 98.8% of NERL's net debt (2007: 121.5%) was either at fixed rates or at rates indexed to inflation.

- counterparty risk: as at 31 March 2008 the company had cash and deposits (shown as short term investments) totalling £93.2m. 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 £138.7m, as at 31 March 2008 the company had cash and short term deposits totalling £93.2m. Included in cash of £76m 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 £17.2m represents a debt service reserve account to fund interest and fees scheduled for payment in the 6 months ending 30 September 2008. The company's policy is to hold free cash within NERL equivalent to between one and two months' of UK en route services revenue (of between £80m and £90m) 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 with a final maturity date of 2026. In addition, NERL has bank facilities totalling £216.2m of which £11m matures in 2010, £34.25m in 2011 and £170.95m in 2012.

Cash flow

Overall, the company's cash balances fell by £43.8m in the year to £76.0m (2007: £119.8m).

	2008 £m	2007 £m
Cash generated from operations	243.0	217.0
Taxation	(12.2)	(21.8)
Net cash from operating activities	230.8	195.2
Interest received	8.7	6.7
Capital expenditure	(138.6)	(146.6)
Sales of property, plant and equipment	0.1	6.8
Change in short-term investments	1.2	0.6
Net cash outflow from investing activities	(128.6)	(132.5)
Interest paid	(36.5)	(49.0)
Loan redemption payment	(15.8)	
Loan repayments	(65.0)	-
Bank drawings and other loans	78.9	
Loan from shareholder	-	(2.2)
Dividends paid	(107.6)	-
Net cash outflow from financing costs	(146.0)	(51.2)
Increase/(decrease) in cash and equivalents	(43.8)	11.5

Net cash from operating activities was £35.6m higher than 2007 at £230.8m

(2007: £195.2m). This included higher cash generated from operations at £243.0m (2007: £217.0m) and lower outflows for taxes paid of £12.2m (2007: £21.8m).

Net cash outflows from investing activities at £128.6m (2007: £132.5m), were £3.9m lower than 2007.

Net cash outflows of £146.0m from financing activities were £94.8m higher than the prior year (2007: £51.2m). The company paid interest of £36.5m, £12.5m lower than last year reflecting lower gearing and the benefit of repaying expensive shareholder loans from cash.

The credit rating upgrade of NERL by Standard & Poor's to A from A- in September 2007, provided NERL with the opportunity to redeem its £65m 11.3575% perpetual shareholder loan notes. Under the loan agreement, achieving an A rating was a condition for early repayment. The NERL loan notes, including a redemption payment of £15.8m, were redeemed in December 2007 using available cash. The company also paid a dividend to its parent company of £107.6m (2007: £nil) in March 2008, which enabled it to reduce its debt. This was funded from available cash in NERL of £30.1m and by way of a £77.5m drawing on NERL's committed bank facilities.

The company held short term deposits maturing after more than 3 months of £17.2m (2007: £18.4m) representing a debt service reserve account to fund finance payments due to be made in the six month period ending 30 September 2008.

Outlook

This has been a year of solid achievement and innovation to prepare for the risks and possibilities that lie ahead.

NERL will always strive to offer the best value for money in managing rising levels of air traffic safely and efficiently. Everything we do is tailored towards this outcome but we know there is always more to do.

NERL is already preparing the ground for the economic regulator's review of the charges that will apply for the five years from 1 January 2011. The regulator and our customers are demanding more from us, putting pressure on what we can charge for our service. We have created a small dedicated project team to help us ensure that we achieve an outcome for the next control period which meets customer requirements in a cost effective way with manageable risk and at a return satisfactory to our stakeholders.

We are at the heart of an industry that brings together the travelling public, the airlines, the airports and Government. We are very well placed to help integrate the interests of all stakeholders, and forging strong partnerships will mean we can help shape new aviation horizons and ensure we continue to be seen as a leader in our field.

Paul Barron
Chief Executive Officer

Report of the directors

The directors present their report and audited accounts for the year ended 31 March 2008.

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 above.

Results and dividends

The results for the period are shown in the income statement on page 23. An interim dividend of £107.6m was declared in the year (2007: £nil) and the Board recommends a final dividend of nil (2007:£nil).

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 Chief Executive Officer maintains high visibility with staff through an annual ‘roadshow’ to each NATS location where he briefs them on 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 in the last year 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, 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 group 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 1985 is 33 days (2007: 21 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
Danny Bernstein (resigned 31/12/2007)
Nigel Fotherby
Ian Hall
Lawrence Hoskins
Derek Stevens
Barry Humphreys
Ian Mills (appointed 28/02/2008)

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 ultimate parent undertaking NATS Holdings Limited: Paul Barron – 634; Nigel Fotherby - 1,777 and Ian Hall - 1,777.

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 1985.

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 s234ZA of the Companies Act 1985.

Auditors

Deloitte & Touche 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
26 June 2008

Registered office

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

Registered in England and Wales
Company Number: 4129273

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 2008 which comprise the income statement, the statement of recognised income and expense, the balance sheet, the cash flow statement and the related notes 1 to 29. These financial statements have been prepared under the accounting policies set out therein.

This report is made solely to the company's members, as a body, in accordance with section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the annual report and the financial statements in accordance with applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union are set out in the statement of directors' responsibilities.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view, in accordance with the relevant financial reporting framework, and are properly prepared in accordance with the Companies Act 1985. We also report to you whether in our opinion the information given in the directors' report is consistent with the financial statements.

In addition we report to you if, in our opinion, the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read other information contained in the directors' report and the other information contained in the annual report and consider whether it is consistent with the audited financial statements. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any further information outside the annual report.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the circumstances of the company, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion

In our opinion:

- the financial statements give a true and fair view, in accordance with IFRSs as adopted by the European Union, of the state of the company's affairs as at 31 March 2008 and of its profit for the year then ended;

- the financial statements have been properly prepared in accordance with the Companies Act 1985; and

- the information given in the directors' report is consistent with the financial statements.

Separate opinion in relation to IFRS

As explained in note 2 to the financial statements, the company in addition to complying with IFRSs as adopted by the European Union, has also complied with the IFRSs as issued by the International Accounting Standards Board.

In our opinion the financial statements give a true and fair view, in accordance with IFRSs, of the state of the company's affairs as at 31 March 2008 and of its profit for the year then ended.

Deloitte & Touche LLP

Chartered Accountants and Registered Auditors
Southampton, United Kingdom
26 June 2008

Income statement
for the year ended 31 March 2008

	Notes	Year ended 31 March 2008 £m	Year ended 31 March 2007 £m
Revenue	4	617.5	588.1
Staff costs	8	(266.6)	(243.4)
Services and materials		(53.9)	(55.6)
Repairs and maintenance		(23.2)	(23.4)
External research and development		(0.3)	(0.5)
Depreciation, amortisation and impairment	7	(82.8)	(87.5)
Profit on disposal of non-current assets		1.2	9.4
Other operating charges		(72.6)	(62.1)
Other operating income		2.9	-
Deferred grants released	7	3.2	4.5
Net operating costs		(492.1)	(458.6)
Operating profit	7	125.4	129.5
Investment revenue	9	9.2	6.7
Finance costs	10	(72.1)	(49.9)
Profit before tax		62.5	86.3
Tax	11	(15.4)	(23.1)
Profit for the year attributable to equity shareholders		47.1	63.2

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

Statement of recognised income and expense
for the year ended 31 March 2008

	Notes	Year ended 31 March 2008 £m	Year ended 31 March 2007 £m
Actuarial gain on defined benefit pension scheme net of deferred tax	21, 27	107.9	27.2
Change in fair value of hedging derivatives net of deferred tax	23	(2.8)	(0.1)
Net income recognised directly in equity		105.1	27.1
Transfer to income statement on cash flow hedges net of deferred tax	23	2.5	1.9
Profit for the year	23	47.1	63.2
Total recognised income and expense for the year		154.7	92.2

Balance sheet
at 31 March 2008

	Notes	2008 £m	2007 £m
Non-current assets			
Goodwill	13	351.0	351.0
Other intangible assets	14	114.2	92.7
Property, plant and equipment	15	584.9	557.0
Retirement benefit asset	27	310.4	179.1
Trade and other receivables	16	3.9	2.5
		1,364.4	1,182.3
Current assets			
Trade and other receivables	16	111.1	100.7
Short term investments	19	17.2	18.4
Cash and cash equivalents		76.0	119.8
		204.3	238.9
Total assets		1,568.7	1,421.2
Current liabilities			
Trade and other payables	20	(117.1)	(90.9)
Current tax liabilities		(5.6)	(6.6)
Derivative financial instruments	18	(74.1)	(51.3)
		(196.8)	(148.8)
Net current assets		7.5	90.1
Non-current liabilities			
Borrowings	17	(691.2)	(676.5)
Trade and other payables	20	(7.5)	(9.3)
Deferred tax liability	21	(164.3)	(124.8)
		(863.0)	(810.6)
Total liabilities		(1,059.8)	(959.4)
Net assets		508.9	461.8
Equity			
Called up share capital	22	10.0	10.0
Hedge reserve	23	(0.4)	(0.1)
Special reserves	23	33.4	33.1
Other reserves	23	37.4	44.9
Retained earnings	23	428.5	373.9
Total equity		508.9	461.8

The financial statements were approved by the Board of directors on 26 June 2008 and signed on its behalf by

Chairman John Devaney

Finance Director Nigel Fotherby

Cash flow statement

for the year ended 31 March 2008

	Notes	Year ended 31 March 2008 £m	Year ended 31 March 2007 £m
Net cash flow from operating activities	24	230.8	195.2
Cash flows from investing activites			
Interest received		8.7	6.7
Purchase of property, plant and equipment and other intangible assets		(138.6)	(146.6)
Sales of property, plant and equipment		0.1	6.8
Changes in short term investments		1.2	0.6
Net cash outflow from investing activities		(128.6)	(132.5)
Cash flows from financing activities			
Interest paid		(36.5)	(49.0)
Loans from shareholder		-	(2.2)
Secured loan notes repaid		(65.0)	-
Redemption payment		(15.8)	-
Bank and other loans		78.9	-
Dividends paid		(107.6)	-
Net cash outflow from financing activities		(146.0)	(51.2)
(Decrease) / increase in cash and cash equivalents during the year		(43.8)	11.5
Cash and cash equivalents at 1 April		119.8	108.3
Cash and cash equivalents at 31 March		76.0	119.8
Net debt (representing borrowings net of cash and short term investments)		(598.0)	(538.3)

1 General information

NATS (En Route) plc is a company incorporated under the Companies Act 1985 and domiciled in the United Kingdom. The address of the registered office is on page 20. The nature of the company's operations and its principal activities are set out in the Director's report 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 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.

In the current year, the company has adopted IFRS 7 Financial Instruments: Disclosures, and the related changes to IAS 1 Presentation of financial statements. The impact of the adoption of IFRS 7 and the changes to IAS 1 has been to expand the disclosures provided in these financial statements regarding the Group's financial instruments and management of capital (See note 19).

Five interpretations issued by the International Financial Reporting Interpretations Committee become effective for this period. These are: IFRIC 7: Applying the Restatement approach under IAS 29, Financial reporting in Hyperinflationary Economies; IFRIC 8: Scope of IFRS 2; IFRIC 9: Reassessment of Embedded Derivatives; IFRIC 10: Interim Financial Reporting and Impairment and IFRIC 11: Group and treasury Share Transaction. The adoption of these Interpretations has not led to any changes in the company's accounting policies.

In addition, the company has elected to adopt IFRS 8: Operating segments in advance of the effective date. The impact of adoption of IFRS 8 has been an additional disclosure. There have been no further changes to the basis of reporting as the company's business segments as reported to management are the same as the primary segments required to be reported under IAS 14, the previous standard. The following Interpretations have also been adopted in advance of their effective date and have had no effect on the accounting policies of the group: IFRIC 12: Service Concession Arrangements and IFRIC 13: Customer Loyalty Programmes.

IFRIC 14: The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction and IAS 23 (revised): Borrowing costs, which were in issue but not yet effective, have not been applied in these financial statements. The impact of IAS 23 is to remove the option, which the company adopts, that enable borrowing costs on qualifying capital assets to be expensed as incurred. The company does not expect the adoption of this standard to have a material impact on its results. The interpretation and standard are not effective until the year ending 31 March 2010.

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 (NSL). Under this agreement this company provides NSL with the following services:

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

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

- North Sea helicopter advisory service;
- air traffic services in certain sectors;
- services to London Approach service (engineering services, use of communications facilities);
- accommodation and support services to NERL units sited on NSL 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 and airports 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.

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: 10-30 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: 3-10 years.
- Furniture, fixtures and fittings: 10 years.
- Vehicles: 5 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.

Deferred grants and other contributions to tangible fixed assets
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 for free 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.

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 substantially 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 tax 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.

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 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
The company 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.

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 group 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 16 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 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 group 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 19 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 forecasted 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 future regulatory price control determinations. If actual results 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 7% would result in these being equal to the carrying amount of goodwill. Refer to notes 13, 14 and 15.

Retirement benefits

The company accounts for its share of the NATS defined benefit pension scheme such that the net pension scheme asset is reported on the balance sheet with actuarial gains and losses being recognised directly in equity through the statement of recognised income and expense. The pension asset assumes 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 asset and the company's reserves and income statement. Refer to note 27 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 and to rationalise the number of air traffic control centres. 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 2008 £m	Year ended 31 March 2007 £m
UK air traffic services	580.4	552.2
North Atlantic air traffic services	23.8	22.5
Inter-company income	13.3	13.4
	617.5	588.1

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 included in note 9.

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 £3.3m (2007: £0.1m)

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 2008	UK air traffic services £m	North Atlantic air traffic services £m	Total £m
Revenue			
Revenue from external customers	580.4	23.8	604.2
Revenue from internal customers	13.3	-	13.3
	593.7	23.8	617.5
Segmental operating profit	121.6	3.8	125.4
Investment revenue			9.2
Finance costs			(72.1)
Profit before tax			62.5
Tax			(15.4)
Profit for the period			47.1
Other information			
Capital expenditure	131.3	1.4	132.7
Depreciation and amortisation	79.0	2.5	81.5
Impairment losses recognised in income	1.3	-	1.3
Deferred grants released	(3.2)	-	(3.2)
Balance Sheet			
Segmental assets	1,523.6	45.1	1,568.7
Segmental liabilities	(1,029.4)	(30.4)	(1,059.8)

Year ended 31 March 2007	UK air traffic services £m	North Atlantic air traffic services £m	Total £m
Revenue			
Revenue from external customers	552.2	22.5	574.7
Revenue from internal customers	13.4	-	13.4
	565.6	22.5	588.1
Segmental operating profit	125.2	4.3	129.5
Investment revenue			6.7
Finance costs			(49.9)
Profit before tax			86.3
Tax			(23.1)
Profit for the period			63.2
Other Information			
Capital expenditure	134.4	2.1	136.5
Depreciation and amortisation	73.2	1.8	75.0
Impairment losses recognised in income	12.5	-	12.5
Deferred grants released	(4.5)	-	(4.5)
Balance Sheet			
Segmental assets	1,380.1	41.1	1,421.2
Segmental liabilities	(931.0)	(28.4)	(959.4)

5. Business and geographical segments (continued)

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 2008 £m	Year ended 31 March 2007 £m
UK	278.7	268.6
Rest of Europe	199.2	187.9
North America	103.8	98.8
Other	35.8	32.8
Total	617.5	588.1

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 £57.5m (2007: £62.8m) which arose from the company's largest customer.

6. Restructuring costs

During the year further restructuring costs were incurred following the closure of the air traffic control centre at West Drayton and the consequent relocation of staff to the Swanwick area. To the extent that staff could not be redeployed, termination terms were agreed. These costs are included in arriving at operating profit.

	Year ended 31 March 2008 £m	Year ended 31 March 2007 £m
Cost of relocation of staff and offices to Swanwick area	5.5	2.3
Voluntary redundancy costs	11.1	1.9
Other operating charges - intra group	0.5	0.4
Payment for changes in redundancy terms	3.0	-
	20.1	4.6

7. Operating profit

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

	Year ended 31 March 2008 £m	Year ended 31 March 2007 £m
CAA regulatory charges	3.8	4.2
Depreciation of property, plant and equipment	73.0	68.5
Impairment of property, plant and equipment	0.4	2.0
Amortisation of internally generated intangible assets	8.5	6.5
Impairment of internally generated intangible assets	0.9	10.5
Deferred grants released	(3.2)	(4.5)
(Profit)/loss on disposal of non-current assets:		
on company assets	(1.2)	(10.0)
inter company charges	-	0.6
Research and development costs	7.2	11.0
Auditors remuneration for audit services (see below)	-	-

Fees payable to Deloitte & Touche 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 2008 £m	Year ended 31 March 2007 £m
Net charges for services provided by parent undertaking	31.3	30.2
Charges for services provided by other group companies	13.9	10.3

In addition to the staff costs referred to in note 8a 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 NERL provides certain services to NSL. The MSA and Inter Company Services Agreement are explained in more detail in note 2.

8 Staff costs

a Staff costs

	Year ended 31 March 2008 £m	Year ended 31 March 2007 £m
Salaries and staff costs, including directors' remuneration, were as follows:		
Wages and salaries*	238.2	216.9
Social security costs	21.9	21.7
Pension costs (note 8b)	40.3	40.5
	300.4	279.1
Less: amounts capitalised	(33.8)	(35.7)
	266.6	243.4

* 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 2008 £m	Year ended 31 March 2007 £m
Pension scheme costs for year (note 27)	40.3	40.5

c Staff numbers

	Year ended 31 March 2008 No.	Year ended 31 March 2007 No.
The monthly average number of employees (including executive directors) was:		
Air traffic controllers	1,445	1,418
Air traffic service assistants	813	869
Engineers	1,002	1,036
Others	537	572
	3,797	3,895

9 Investment revenue

	Year ended 31 March 2008 £m	Year ended 31 March 2007 £m
Interest on bank deposits	8.9	6.7
Other loans and receivables	0.3	-
	9.2	6.7

10 Finance costs

	Year ended 31 March 2008 £m	Year ended 31 March 2007 £m
Interest payable		
Interest on bank overdrafts, loans and hedging instruments	0.6	1.1
Interest on shareholder loan notes	5.2	7.4
Bond and related costs including financing expenses	30.1	29.8
Interest payable on intercompany loans	1.4	1.2
	37.3	39.5
Loss on derivatives not qualifying for hedge accounting	19.0	10.5
Gains on derivatives not qualifying for hedge accounting	-	(2.7)
Fair value losses on interest rate swaps transferred from equity	-	2.6
	56.3	49.9
Payment on redemption of 11.3575% fixed rate secured shareholder loan notes	15.8	-
	72.1	49.9

11 Tax

	Year ended 31 March 2008 £m	Year ended 31 March 2007 £m
Current tax	(11.2)	(13.4)
Deferred tax (note 21)	(4.2)	(9.7)
	(15.4)	(23.1)

Corporation tax is calculated at 30% (2007: 30%) 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 2008 £m	%	Year ended 31 March 2007 £m	%
Profit on ordinary activities before tax	62.5		86.3	
Tax on profit on ordinary activities at standard rate in the UK of 30%	(18.7)	(30%)	(25.9)	(30%)
Tax effect of prior year adjustments	0.4	0%	0.1	0%
Tax effect of change in rate from 30% to 28% for deferred tax	4.3	7%	-	0%
Tax effect of other permanent differences	(1.4)	(2%)	2.7	3%
Tax charge for year at the effective tax rate of 24.6% (2007: 26.8%)	(15.4)	(25%)	(23.1)	(27%)
Deferred tax charge taken directly to equity (see note 21)	(35.3)		(12.4)	

Recent budget changes

If the 2008 Finance Bill is substantially enacted in its current draft, industrial buildings allowances will be abolished over the three years from 1 April 2008. The group would be obliged to recognise an additional deferred tax liability of £4.7m in the year ended 31 March 2009 although the accounting impact will be neutral in the long term as the liability will be released in the following years as the carrying values of assets reduce.

12. Dividends

	Year ended 31 March 2008 £m	Year ended 31 March 2007 £m
Amounts recognised as distributions to equity holders in the year		
Interim dividend for the year of £10.76 per ordinary share.	107.6	-

13 Goodwill

	£m
At 31 March 2008 and 31 March 2007	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. 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 discount rate is a pre-tax nominal rate of 9.51%. See note 3.

14 Other intangible assets

	Operational software £m	Non-operational software £m	Airspace and resectorisation £m	Assets in course of construction £m	Other intangibles £m	Total £m
Cost						
At 1 April 2006	20.7	8.0	6.8	58.6	0.6	94.7
Additions internally generated	0.5	0.2	1.0	14.2	-	15.9
Additions externally acquired	0.9	0.4	-	18.3	-	19.6
Disposals and transfers during the year	13.0	3.7	3.0	(24.8)	(0.6)	(5.7)
At 1 April 2007	35.1	12.3	10.8	66.3	-	124.5
Additions internally generated	-	1.9	-	16.7	-	18.6
Additions externally acquired	-	-	-	12.2	-	12.2
Disposals and transfers during the year	(0.1)	13.2	1.6	(15.4)	-	(0.7)
At 31 March 2008	35.0	27.4	12.4	79.8	-	154.6
Accumulated amortisation						
At 1 April 2006	3.6	3.6	2.1	6.6	-	15.9
Charge for the year	3.1	1.9	1.5	-	-	6.5
Impairment provision recognised in income statement	-	-	-	10.5	-	10.5
Disposals and transfers during the year	-	-	-	(1.1)	-	(1.1)
At 31 March 2007	6.7	5.5	3.6	16.0	-	31.8
Charge for the year	4.2	2.8	1.5	-	-	8.5
Impairment provision recognised in income statement	-	-	-	0.9	-	0.9
Disposals and transfers during the year	-	-	-	(0.8)	-	(0.8)
At 31 March 2008	10.9	8.3	5.1	16.1	-	40.4
Carrying amount						
At 31 March 2008	24.1	19.1	7.3	63.7	-	114.2
At 31 March 2007	28.4	6.8	7.2	50.3	-	92.7

15 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 2006	152.2	41.7	862.6	7.1	209.2	1,272.8
Additions during the year	6.7	0.3	25.3	2.6	66.1	101.0
Disposals and transfers during the year	54.0	3.8	63.1	3.6	(140.8)	(16.3)
At 1 April 2007	212.9	45.8	951.0	13.3	134.5	1,357.5
Additions during the year	0.1	0.2	32.2	-	69.4	101.9
Disposals and transfers during the year	0.9	0.1	44.4	(0.1)	(72.9)	(27.6)
At 31 March 2008	213.9	46.1	1,027.6	13.2	131.0	1,431.8
Accumulated depreciation and impairment						
At 1 April 2006	62.5	28.3	638.7	4.1	16.6	750.2
Provided during the year	4.2	1.8	61.3	1.2	-	68.5
Provisions for impairment	-	-	-	-	2.0	2.0
Utilisation of impairment provision	-	-	0.1	-	(0.1)	-
Disposals and transfers during the year	(2.6)	0.1	(3.0)	(0.2)	(14.5)	(20.2)
At 1 April 2007	64.1	30.2	697.1	5.1	4.0	800.5
Provided during the year	6.5	1.6	63.8	1.1	-	73.0
Provisions for impairment	-	-	-	-	0.4	0.4
Utilisation of impairment provision	-	0.2	0.1	-	(0.3)	-
Disposals and transfers during the year	-	-	(24.1)	(0.1)	(2.8)	(27.0)
At 31 March 2008	70.6	32.0	736.9	6.1	1.3	846.9
Carrying amount						
At 31 March 2008	143.3	14.1	290.7	7.1	129.7	584.9
At 31 March 2007	148.8	15.6	253.9	8.2	130.5	557.0

The company conducts annual reviews of the carrying values of its property, plant, equipment and intangible assets. During the year, impairment charges of £1.3m (2007: £12.5m) were made in respect of assets in the course of construction reflecting a reassessment of certain projects and the likelihood of benefits being realised in full.

16 Financial and other assets

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

Trade and other receivables

	2008 £m	2007 £m
Non-current		
Other debtors	3.9	2.5
Current		
Receivable from customers gross	44.1	42.7
Allowance for doubtful debts	(2.1)	(3.8)
	42.0	38.9
Other debtors	3.8	4.1
Prepayments	14.7	9.5
Accrued income	50.4	48.1
Accrued interest	0.2	0.1
	111.1	100.7

The average credit period taken on sales of services is 25 days. Interest is charged by Eurocontrol to UK en route customers at 9.24% 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 £2.1m (2007: £3.8m). Full provision is made for receivables from UK en route customers that are over due. 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.

Ageing of past due but not impaired trade receivables

	2008 £m	2007 £m
30-90 days	0.9	0.8

Movement in the allowance for doubtful debts

	2008 £m	2007 £m
Balance at the beginning of the year	3.8	3.7
Decrease in allowance recognised in the income statement	(0.1)	0.5
Amounts written off as irrecoverable	(1.6)	(0.4)
Balance at end of year	2.1	3.8

In determining the recoverability of a trade receivable the group 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 £1.2m (2007: £2.7m) which are in administration, receivership or liquidation. The impairment recognised represents the carrying amount of these trade receivables. The group does not hold any collateral over these balances.

Ageing of impaired receivables

	2008 £m	2007 £m
Current	-	0.1
30-90 days	0.5	0.5
90-365 days	0.3	0.8
more than 365 days overdue	1.3	2.4
	2.1	3.8

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.

17 Borrowings

	2008 £m	2007 £m
Unsecured loans		
Intercompany loan	22.5	22.5
Other loans (non interest bearing)	1.4	-
Total unsecured loans	23.9	22.5
Secured loans		
£600m 5.25% Guaranteed Secured Amortising Bonds due 2026	597.1	596.9
Fixed rate secured shareholder loan notes (11.3575%, no final maturity date)	-	65.0
Bank loans (variable rate revolving credit facility expiring 2010-2012)	77.5	-
Gross borrowings	698.5	684.4
Unamortised bond issue costs	(7.3)	(7.9)
	691.2	676.5

The £600m 5.25% Guaranteed Secured Amortising Bond is secured by way of a debenture by which NATS (En Route) plc 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 £77.5m made in March 2008 under its £216.2m committed bank facilities are similarly secured.

The average effective interest rate on the bank loan in the year was 5.94% and was determined based on 6 month LIBOR rates plus a margin.

The 11.3575% fixed rate secured shareholder loan notes of £65m together with accrued interest of £1.4m and a redemption payment of £15.8m were repaid in December 2007.

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

Undrawn committed facilities	2008 £m	2007 £m
Expiring in more than two years	138.7	216.2

Drawings of £77.5m were made on committed facilities of £216.2m in the year. The bank facilities expire as follows: £11.0m in November 2010; £34.25m in November 2011 and the balance of £170.95m in November 2012.

18 Derivative financial instruments

Fair value liability of derivative financial instruments

	2008 £m	2007 £m
Derivative financial instruments in designated hedge accounting relationships		
Forward foreign exchange contracts (cash flow hedges)	4.9	1.1
Derivative financial instruments classified as held for trading		
Index-linked swaps	69.2	50.2
	74.1	51.3

Further details on derivative financial instruments are provided in note 19. 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 (see note 19) and previously qualified as a hedge under UK generally accepted accounting principles prior to the group's conversion to international accounting standards.

19 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 the air traffic services licence and to provide returns to stakeholders. The capital structure of the company consists of debt, as disclosed in note 17, cash and cash equivalents, as explained in this note and equity attributable to shareholders as disclosed in notes 22 and 23.

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 2008, the company had a credit rating of A (stable outlook) from Standard & Poor's and A3 (positive outlook) from Moody's (2007: A- positive outlook/ A3 positive outlook).

Gearing ratio
Consistent with seeking to maintain an investment grade credit rating, the company sets a gearing ratio, 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.

19 Financial instruments continued

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

	2008 £m	2007 £m
Financial assets		
Loans and receivables (including cash and cash equivalents and short term investments)	142.9	183.7
Financial liabilities		
Derivative instruments in designated hedge accounting relationships	(4.9)	(1.1)
Derivative financial instruments classified as held for trading	(69.2)	(50.2)
Amortised cost	(757.9)	(727.1)
	(832.0)	(778.4)

The index-linked swap is categorised as held for trading. The movement in its market value of £19.0m has been recorded in the profit and loss account in the year (2007: £10.5m).

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 quarterly 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.

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 against 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 85% of turnover (2007:84%). 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	
	2008 £m	2007 £m	2008 £m	2007 £m
Euro	102.2	99.4	(12.6)	(6.7)
US Dollar	0.4	0.8	(0.1)	(0.1)
Canadian Dollars	0.9	1.3	-	-
	103.5	101.5	(12.7)	(6.8)

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

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	2008 Impact £m	2007 Impact £m
Euro	(1.7)	(2.3)
US Dollar	-	(0.1)
Canadian Dollars	(0.1)	(0.1)
	(1.8)	(2.5)

The company's sensitivity to foreign currency has reduced during the current reporting period mainly due to a decrease in net unhedged foreign currency assets. The company believes that this sensitivity analysis accurately reflects its inherent foreign exchange risk as the level of currency investments was broadly constant throughout the reporting period. Since 31 March 2008, the company has further reduced its exposure to foreign exchange risk by reducing the level of Euro currency deposits held.

19 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. These forward foreign exchange contracts have been designated as cash flow hedges. The following contracts were outstanding at year end:

	2008				2007		
Payment date	Euro sold €m	Sterling bought £m	Exchange rate €1 = £	Payment date	Euro sold €m	Sterling bought £m	Exchange rate €1 = £
23 April 2008	23.2	17.5	0.7492	25 April 2007	24.5	16.3	0.6664
23 April 2008	23.2	17.4	0.7493	25 April 2007	24.5	16.3	0.6663
21 May 2008	24.8	18.7	0.7538	23 May 2007	27.5	18.4	0.6707
21 May 2008	24.8	18.7	0.7539	23 May 2007	27.5	18.4	0.6707
Total/average	96.0	72.3	0.7526	Total/average	104.0	69.4	0.6680

In addition to the above, since the year end, agreements were entered into with a contract date after 31 March 2008 to sell Euro anticipated to be received in the period June through to August 2008 totalling €116.6m.

At 31 March 2008, 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 £0.4m (2007: unrealised losses of £0.1m). These contracts will mature within the first two months of the next financial year at which stage the amount deferred in equity will be realised in the income statement.

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 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 in the liquidity risk management section of this note.

Economic interest rate exposure
The company held cash and short term deposits as follows:

2008	Cash			Short term deposits			Total
Currency	Amount £m	Economic interest rate %	Average maturity days	Amount £m	Economic interest rate %	Average maturity days	£m
Sterling	59.6	5.5	12	17.2	5.7	184	76.8
EUR	15.1	4.1	3	-	-	-	15.1
USD	0.4	2.5	7	-	-	-	0.4
CAD	0.9	3.4	4	-	-	-	0.9
	76.0			17.2			93.2

2007	Cash			Short term deposits			Total
Currency	Amount £m	Economic interest rate %	Average maturity days	Amount £m	Economic interest rate %	Average maturity days	£m
Sterling	98.9	5.3	5	18.4	5.6	182	117.3
EUR	18.8	3.8	10	-	-	-	18.8
USD	0.8	5.2	13	-	-	-	0.8
CAD	1.3	4.1	12	-	-	-	1.3
	119.8			18.4			138.2

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.

19 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 2008						
Sterling:						
5.25% guaranteed secured bonds	597.1	-	-	597.1	5.28%	12.0
Bank loans	77.5	77.5	-	-	5.94%	0.5
Other loans	1.4	-	-	1.4	0.00%	0.9
Total	676.0	77.5	-	598.5		
At 31 March 2007						
Sterling:						
5.25% guaranteed secured bonds	596.9	-	-	596.9	5.28%	13.0
11.3575% secured shareholder loan notes	65.0	-	-	65.0	11.36%	N/A
Total	661.9	-	-	661.9		

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 2008						
Sterling:						
5.25% guaranteed secured bonds	397.1	-	-	397.1	5.29%	12.0
5.25% guaranteed secured bonds	200.0	-	200.0	-	3.50%	N/A
Bank loans	77.5	77.5	-	-	5.94%	0.5
Other loans	1.4	-	-	1.4	0.00%	0.9
Total	676.0	77.5	200.0	398.5		
At 31 March 2007						
Sterling:						
5.25% guaranteed secured bonds	396.9	-	-	396.9	5.29%	13.0
5.25% guaranteed secured bonds	200.0	-	200.0	-	3.37%	N/A
11.3575% secured shareholder loan notes	65.0	-	-	65.0	11.36%	N/A
Total	661.9	-	200.0	461.9		

The £65m perpetual fixed rate secured shareholder loan notes were issued by the company in March 2003 as part of the restructuring of the group's finances that took place following the events of September 11th, 2001. The coupon was set at 11.3575% to ensure that the new investor in the group (BAA) earned a satisfactory rate of return on its total investment. Achieving an A rating from Standard & Poor's enabled repayment of the 11.3575% perpetual shareholder loan notes in December 2007.

The interest rate payable under the RPI 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.

	2008 £m		2007 £m	
Net Debt	598.0		538.3	
	£m	%	£m	%
Fixed (net of bond discount and issue costs)	391.2	65.4	454.0	84.3
Index Linked	200.0	33.4	200.0	37.2
Floating (net of cash and short term investments)	6.8	1.2	(115.7)	(21.5)
	598.0	100.0	538.3	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.
In 2007 cash and short term investments significantly exceeded its floating rate borrowings with the result that the company was over hedged on a Net Debt basis.

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%.

	2008 Impact £m	2007 Impact £m
Cash On Deposit (2008: £93.2m, 2007: £138.2m)	0.9	1.4
Borrowings (2008: £77.5m, 2007: £nil)	(0.8)	-
	0.1	1.4

The sensitivity to interest rates has decreased during the year due to a closer matching of the balance of floating rate assets and liabilities, in accordance with hedging policy.

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.

The value of the notional principal of £200m of the index-linked swap is also linked to movements in RPI. The increase in the notional value is payable semi-annually commencing on 31 March 2017 and ending on 31 March 2026 (the expiry date of the swap).

19 Financial Instruments continued

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%.

	2008 Impact £m	2007 Impact £m
Change in index-linked swap interest and mark to market value	(29.7)	(23.0)

The mark to market value of the index-linked swap is also sensitive to the discount rate that is 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. NERL's index-linked swap is most sensitive to yields on swaps that mature within 10 to 15 years. The effect of a 1% increase in the discount rate on 15-year swaps would be to increase profit and equity by £19.4m (2007: £13.0m). 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 16.
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 and Moody's Investors Service.

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 and Moody's rating agencies. Where there is a difference in the rating then the lower of the two ratings is applied.

Currently, 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.

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	2008 £m	By credit rating %	Number of institutions	2007 £m	By credit rating %
AA	4	68.7	73.7	3	53.7	38.8
AA-	-	-	-	1	9.2	6.7
A+	1	15.0	16.1	2	20.3	14.7
A	1	9.5	10.2	6	55.0	39.8
		93.2	100.0		138.2	100.0

Liquidity risk management
The responsibility for liquidity management rests with the Board of NATS (Holdings) Limited with oversight provided by the Treasury Committee. Liquidity is managed 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 £17.2m 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. The company has access to bank facilities totalling £216.2m available until November 2010, and £170.95m until November 2012, thereby ensuring that committed funding is available at a competitive cost to meet its anticipated needs for the period covered by its business plan;
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 £11.0m expires in 2010, £34.25m in 2011 and £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:

	2008 £m	2007 £m
Average monthly UK en route services income	43.5	41.3
Free cash	53.9	99.5
Ratio of free cash to UK en route services income	1.2	2.4

During 2007, the company maintained a higher level of free cash than the policy in anticipation of repaying shareholder loan notes. During 2008, free cash of £82.2m was used to fund the redemption of the £65m 11.3575% shareholder loan notes together with accrued interest of £1.4m and an early redemption payment of £15.8m. In addition, £30.1m of free cash and a £77.5m drawing on bank facilities were used to finance a dividend paid to the company's parent NATS Limited.

19 Financial Instruments continued

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

	2008 £m	2007 £m
Bank borrowings	77.5	-
Gross borrowings	698.5	684.4
Bank borrowings as a percentage of gross borrowings	11.1%	0.0%

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 group can be required to repay. The table includes both interest and principal cash flows.

	2008				2007			
	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	36.8	59.4	97.5	1.3	40.0	42.7	84.0
Between one and two years	2.7	36.5	-	39.2	1.3	40.0	-	41.3
Due between two and five years	3.6	185.1	-	188.7	3.8	119.9	-	123.7
Due in more than five years	44.6	828.5	-	873.1	44.0	1,065.2	-	1,109.2
	52.2	1,086.9	59.4	1,198.5	50.4	1,265.1	42.7	1,358.2
Effect of interest and discount	(28.3)	(412.3)	-	(440.6)	(27.9)	(603.2)	-	(631.1)
	23.9	674.6	59.4	757.9	22.5	661.9	42.7	727.1

It should be noted that the 2007 analysis assumes that the loan notes are repaid on 31 March 2031. These were actually repaid in December 2007.

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 company also intends to re-finance existing bank borrowings through a bond issue as and when market conditions are favourable.

The following table sets out the maturity profile of the derivative financial liabilities. Cash flows under the RPI swap are not fixed and are subject to movements in inflation. Accordingly, the cash flows associated with the RPI 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
2008					
Gross settled:					
Index-linked swap receivable	10.5	10.5	31.5	92.9	145.4
Index-linked swap payable	(7.0)	(7.2)	(22.7)	(215.6)	(252.5)
Foreign exchange forward contract receivables	72.3	-	-	-	72.3
Foreign exchange forward contract payables	(77.2)	-	-	-	(77.2)
	(1.4)	3.3	8.8	(122.7)	(112.0)
2007					
Gross settled:					
Index-linked swap receivable	10.5	10.5	31.5	103.4	155.9
Index-linked swap payable	(6.8)	(6.9)	(22.0)	(222.7)	(258.4)
Foreign exchange forward contract receivables	69.4	-	-	-	69.4
Foreign exchange forward contract payables	(70.5)	-	-	-	(70.5)
	2.6	3.6	9.5	(119.3)	(103.6)

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 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, the break-even inflation rate which is calculated as the difference in yields on fixed interest and index-linked gilts of similar maturity to the swap contract and discounted to present value. The fair value of the £600m bond has been derived from its externally quoted price. The fair value of shareholder loan notes is stated at amortised cost. The book values of other financial assets and liabilities approximate to their fair values because of their short maturities.

	Carrying amount		Fair value	
	2008 £m	2007 £m	2008 £m	2007 £m
Financial assets				
Accounts receivable, cash and bank balances	142.9	183.7	142.9	183.7
Financial liabilities				
Trade and other payables (including current tax liabilities)	(59.4)	(42.7)	(59.4)	(42.7)
£600m 5.25% Guaranteed Secured Amortising Bond	(597.1)	(596.9)	(552.1)	(593.1)
11.3575% shareholder loan notes	-	(65.0)	-	(65.0)
Bank loans	(77.5)	-	(77.5)	-
Intercompany loan	(22.5)	(22.5)	(22.5)	(22.5)
Other loans	(1.4)	-	(1.4)	-
Derivative financial instruments				
Forward foreign exchange contracts	(4.9)	(1.1)	(4.9)	(1.1)
Index-linked swap	(69.2)	(50.2)	(69.2)	(50.2)
	(832.0)	(778.4)	(787.0)	(774.6)

20 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:

	2008 £m	2007 £m
Current		
Trade payables	9.8	7.3
Amounts due to other group undertakings	31.1	18.6
Other payables	12.9	10.2
Accruals and deferred income		
- deferred grants	2.2	3.6
- other	61.1	51.2
	117.1	90.9
Non-current		
Accrual and deferred income		
- deferred grants	7.5	9.3
	124.6	100.2

Trade creditors and accruals principally comprise amounts outstanding for trade purchases and ongoing costs. The average credit period taken for trade purchases is 33 days (2007: 21 days). The directors consider that the carrying amount of the trade payables approximates to their fair value.

21 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 £m	Retirement benefit asset £m	Financial Instruments £m	Other £m	Total £m
At 1 April 2007	66.5	46.8	(8.5)	(2.1)	102.7
Charge/(credit) to income	14.2	(4.6)	(0.8)	0.9	9.7
Charge to equity	-	11.6	0.8	-	12.4
At 31 March 2007	80.7	53.8	(8.5)	(1.2)	124.8
At 1 April 2007	80.7	53.8	(8.5)	(1.2)	124.8
Charge/(credit) to income	10.1	(2.4)	(3.1)	(0.4)	4.2
Charge/(credit) to equity	-	35.5	(0.2)	-	35.3
At 31 March 2008	90.8	86.9	(11.8)	(1.6)	164.3

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.

	2008 £m	2007 £m
Deferred tax liabilities	(177.7)	(134.5)
Deferred tax assets	13.4	9.7
	(164.3)	(124.8)

22 Share capital

	Authorised Number of shares	Authorised £m	Called up, allotted and fully paid Number of shares	Called up, allotted and fully paid £m
Ordinary shares of £1 each				
At 31 March 2007 and 31 March 2008	10,000,000	10.0	10,000,000	10.0

23 Reserves

	Hedge reserve £m	Special reserves £m	Other reserves £m	Retained earnings £m	Total £m
Balance at 1 April 2006	(1.9)	24.2	53.9	283.4	359.6
Movement in statement of recognised income and expense	1.8	-	-	27.2	29.0
Transfers between reserves	-	8.9	(9.0)	0.1	-
Net profit for the year	-	-	-	63.2	63.2
Balance at 31 March 2007	(0.1)	33.1	44.9	373.9	451.8
Movement in statement of recognised income and expense	(0.3)	-	-	107.9	107.6
Transfers between reserves	-	0.3	(7.5)	7.2	-
Net profit for the year	-	-	-	47.1	47.1
Dividends paid	-	-	-	(107.6)	(107.6)
Balance at 31 March 2008	(0.4)	33.4	37.4	428.5	498.9

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

24 Notes to the cash flow statement

	Year ended 31 March 2008 £m	Year ended 31 March 2007 £m
Operating profit from continuing operations	125.4	129.5
Adjustments for:		
Depreciation of property, plant and equipment	73.0	68.5
Amortisation of intangible assets	8.5	6.5
Impairment loss	1.3	12.5
Deferred grants released	(3.2)	(4.5)
Gain on disposal of property, plant and equipment	(1.2)	(9.4)
Non-cash element of charge for pension costs	12.1	15.9
Decrease in provisions	-	(0.2)
Operating cash flows before movements in working capital	215.9	218.8
Increase in trade and other receivables	(8.2)	(6.8)
Increase in trade and other payables	35.3	5.0
Cash generated from operations	243.0	217.0
Tax paid	(12.2)	(21.8)
Net cash from operating activities	230.8	195.2

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.

25 Financial commitments

	2008 £m	2007 £m
Capital commitments contracted but not provided for in the accounts.	120.8	84.5
Minimum lease payments under operating leases recognised in the income statement for the year.	7.7	7.7
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:		
Within one year	0.5	0.6
In the second to fifth years inclusive	3.0	5.5
After five years	40.1	40.8
	43.6	46.9

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. The prior year comparative for minimum lease payments has been re-stated to be consistent with the 2008 amount.

Guarantees

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

Breach of loan agreement

NERL is required by its loan documents to seek consent from its lenders to enter into certain capital and revenue contracts that are above a certain value or exceed a specified duration. In December 2007, NERL entered into a contract which met these criteria. However, consent was not sought until March 2008. Any breaches associated with this action were waived by lenders in April 2008.

26 Contingent liabilities

During the year, the company undertook a public consultation in respect of airspace changes in the Terminal Control South West region. The Civil Aviation Authority approved the proposals put forward by NERL and directed that the changes be implemented as of 10 April 2008. The CAA's decision is subject to a Judicial Review. NERL has been included in that process at its own request due to its status as an interested party. If the Judicial Review reverses the CAA's decision a new consultation may be necessary. The CAA may require the costs of a new consultation to be borne by NERL. In addition, NERL may incur significant legal costs through the Judicial Review process which may not be recoverable even if the decision is upheld.

27 Retirement benefit scheme

Background

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 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 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.

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' funding assessment was prepared as at 31 December 2006, 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.

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.

27 Retirement benefit scheme continued

Trustees' funding assessment

The last Trustees' funding assessment of the NATS' section was carried out at 31 December 2006 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 1.9% 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 1.5% higher than the annual increases in pensions.

The market value of the NATS' section's assets as at 31 December 2006 was £2,785.3m. For the purpose of the Trustees' funding assessment assets were taken at market value. The assets were sufficient to cover 112% of the benefits that had accrued to existing members.

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. The pension costs reported below represent the pension element of the fees the company pays to NATS Limited for the provision of services of the staff seconded to the company by NATS Limited - see note 8a above.

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 will continue to report under an immediate recognition approach in subsequent periods.

The Trustees' funding assessment carried out at 31 December 2006 was updated to 31 March 2008 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:

	2008	2007	2006
Inflation	3.60%	3.20%	2.95%
Increase in:			
- salaries	4.80%	4.40%	4.15%
- deferred pensions	3.60%	3.20%	2.95%
- pensions in payment	3.60%	3.20%	2.95%
Expected return on:			
- equities	7.60%	7.50%	7.30%
- property	7.60%	7.50%	7.30%
- bonds	4.95%	4.73%	4.63%
Discount rate for scheme liabilities	6.20%	5.20%	4.95%

The mortality assumptions have been drawn from actuarial tables PMA92 and PFA92 medium cohort (2007:PXA92 short cohort). These tables assume that the life expectancy, from age 60, for a male pensioner is 26.3 years and a female pensioner is 29.2 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 27.0 years and for females to 29.9 years.

Amounts recognised in income, in the staff costs line item, in respect of these defined benefit schemes are as follows:

	2008 £m	2007 £m
Current service cost	(81.5)	(83.6)
Past service cost	(3.4)	(1.3)
Expected return on scheme assets	147.0	137.6
Interest cost on scheme liabilities	(102.4)	(93.2)
Total defined benefit charge recognised in arriving at operating profit	(40.3)	(40.5)

Amounts taken to the statement of recognised income and expense are as follows:

	2008 £m	2007 £m
Actual return less expected return on scheme assets	(129.8)	(15.5)
Experience gains and losses arising on scheme liabilities	73.7	34.1
Changes in assumptions underlying the present value of the scheme liabilities	199.5	20.2
	143.4	38.8

27 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:

	2008 £m	2007 £m
Fair value of scheme assets	2,136.3	2,125.9
Present value of defined benefit obligations	(1,825.9)	(1,946.8)
Surplus in scheme	310.4	179.1

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

	2008 £m	2007 £m
At 1 April	2,125.9	2,014.0
Expected return on scheme assets	147.0	137.6
Actuarial gains and losses	(129.8)	(15.5)
Contributions from scheme members	11.7	11.6
Contributions from company	28.2	24.6
Benefits paid	(46.7)	(46.4)
At 31 March	2,136.3	2,125.9

Movements in the present value of the defined benefit obligations were as follows:

	2008 £m	2007 £m
At 1 April	(1,946.8)	(1,857.8)
Current service cost	(81.5)	(83.6)
Past service costs	(3.4)	(1.3)
Interest cost	(102.4)	(93.2)
Actuarial gains and losses	273.2	54.3
Contributions from scheme members	(11.7)	(11.6)
Benefits paid	46.7	46.4
At 31 March	(1,825.9)	(1,946.8)

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	
	2008 £m	2007 £m	2008	2007
Equity Instruments	1,288.6	1,350.0	7.60%	7.50%
Property	335.6	338.0	7.60%	7.50%
Bonds	490.4	431.5	4.95%	4.73%
Cash	21.7	6.4	4.95%	4.73%
	2,136.3	2,125.9	6.97%	6.86%

The four year history of experience adjustments is as follows:

	2008 £m	2007 £m	2006 £m	2005 £m
Present value of defined benefit obligations	(1,825.9)	(1,946.8)	(1,857.8)	(1,516.4)
Fair value of scheme assets	2,136.3	2,125.9	2,014.0	1,568.1
Surplus in the scheme	310.4	179.1	156.2	51.7
Experience adjustments in scheme liabilities				
Amount (£m)	73.7	34.1	22.0	54.9
Percentage of scheme liabilities	(4.0%)	(1.8%)	(1.2%)	(3.6%)
Experience adjustments in scheme assets				
Amount (£m)	(129.8)	(15.5)	322.2	71.5
Percentage of scheme assets	(6.1%)	(0.7%)	16.0%	4.6%

28 Related party transactions

Since 26 July 2001, the NATS group has had two major shareholders - the Crown and The Airline Group (AG). During the year transactions with the Crown have taken place with the Meteorological office, the Department for Transport (DfT) and the Ministry of Defence (MoD).

A loan of £2.2m was made by AG to NERL on 28 June 2005. The loan was repaid in full in the year to 31 March 2007 and the interest rate applicable to the loan was 200 basis points above the Interbank Rate. The interest was rolled up every six months into the loan value.

On 19 March 2003, the company issued £32.5m undated, secured, fixed rate loan notes to each of BAA plc and the Crown. These loans, which were repaid during the year, are described more fully in note 17.

Trading transactions

During the year, the company entered into the following transactions with related parties.

	Sales		Purchases		Amounts owed by related parties		Amounts owed to related parties	
	Year ended 31 March 2008 £m	Year ended 31 March 2007 £m	Year ended 31 March 2008 £m	Year ended 31 March 2007 £m	Year ended 31 March 2008 £m	Year ended 31 March 2007 £m	Year ended 31 March 2008 £m	Year ended 31 March 2007 £m
Ministry of Defence (MoD)	43.7	40.7	3.6	3.1	3.8	4.2	2.2	1.6
Department for Transport (DfT)	0.4	0.2	-	-	-	-	-	-
Meteorological Office	0.2	-	0.5	0.6	-	-	0.2	0.2

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 17 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.

29. 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.