NATS (En Route) plc

Financial statements
for the year ended 31 March 2013

Company Number: 04129273

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Company Secretary

Richard Churchill-Coleman

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Registered in England and Wales
Company Number 04129273

Auditor

Deloitte LLP

Financial performance

(£m unless otherwise specified)	2013	2012	Change	%
Revenue	713.6	695.6	+18.0	+2.6
Operating profit	205.4	200.7	+4.7	+2.3
Profit before tax	151.4	154.8	-3.4	-2.2
Capital expenditure	126.8	127.3	-0.5	-0.4
Net debt[1]	605.5	647.6	-42.1	-6.5
Gearing[2] (%)	54.5%	57.8%	-3.3%	-5.7
Dividends	28.5	45.0	-16.5	-36.7

[1] Excludes derivative financial instruments

[2] Ratio of net debt to regulatory assets

Safety, operational and environmental performance

- We successfully managed the special aviation requirements for the London 2012 Olympic Games, co-ordinating extensively with key stakeholders to provide exceptional service performance during this period. This proved to be one of the transport infrastructure success stories of the Games.

- We handled just over 2.1 million flights in the year (2012: 2.2 million) and maintained our safety record, with no risk-bearing airprox attributable to NERL. Average delay per flight was 1.3 seconds compared with 7.0 seconds last year, reflecting the benefit of new controller tools and systems on which frontline operational staff received training last year.

- Mindful of the difficult economic environment facing airline customers the charges for UK en route services and London Approach were set £6m below the level allowed by the economic regulator.

- By providing our customers with more efficient flight profiles, in 2013 we enabled further savings of 6,926 tonnes of fuel worth approximately £4.5m. Cumulatively, since 2008, we have enabled fuel savings of 250,000 tonnes saving customers £160m. We are also meeting the economic regulator's target for environmental efficiency.

- NERL has developed a draft customer consultation Business Plan for Reference Period 2 (2015 to 2019) taking account of the EC's range of cost efficiency targets and is putting forward two price reduction offerings for customers to consider: a service-led plan at lower price and a price-led plan. The former is aimed at customers who want maximum price reduction with the same quality of service that we provide today together with airspace and system improvements in line with Future Airspace Strategy (FAS) and SESAR, and the latter delivers an even lower price in RP2 with good performance but with customers taking on more service risk.

It has been another excellent year characterised by outstanding safety and service performance, especially during the London Olympics whilst continuing to deliver solid financial performance. Ahead of this summer's consultations on the next regulatory control period we have expended considerable effort in developing an innovative proposal for our en route customers and in mitigating a potential increase in pension costs. It has also been a year which has brought us firmly into the public eye as part of the wider debates on transport infrastructure, leading to a better understanding of the role that we play in this respect and highlighting our potential as an exporter of expertise in air traffic management.

Our high safety standards were maintained and our attributable average ATFM delay[1] was 1.3 seconds per flight (2012: 7.0 seconds). This is less than 5% of the equivalent European average (2012: 13%) in a year when we faced the challenge of London hosting the 2012 Olympic Games. We met the en route service performance targets set by the Civil Aviation Authority (CAA), including the 3Di metric which tracks our performance in providing efficient flight profiles to help airlines reduce their fuel burn.

We delivered another solid set of financial results in 2012/13. Revenue improved by £18.0m to £713.6m (2012: £695.6m) reflecting an increase in UK en route revenue. Our pre-tax profits fell by £3.4m to £151.4m (2012: £154.8m) in part because of higher operating costs which included depreciation charges on controller tools and systems introduced last year and higher net finance charges. We invested £126.8m, largely in our economically regulated activities to sustain our operations and to develop future systems focused on future capability compatible with the European SESAR programme. We also secured funding through to 2016 by agreeing a new £275m bank facility. Finally, shareholders received dividends of £28.5m, a reduction of £16.5m on the previous year, as the Board took a measured response ahead of the outcome of the valuation of the defined benefit pension scheme.

Olympics success

We are delighted with the company's exceptional performance during the Olympic period and the part it played in managing a seamless service for our customers during this unique opportunity to showcase the United Kingdom.

The London 2012 Games presented a unique challenge: safely managing an influx of air traffic into some of the most

1 ATFM or air traffic flow management delay represents the delay between the last take-off time requested by an airline and the take-off slot which is allocated when an air navigation service provider (ANSP) applies a flow restriction. Delay which is directly attributable to an ANSP includes staffing, capacity and systems-related delay. Delay which is not directly attributable to an ANSP, includes weather at airports and en route, and delay attributed to airport infrastructure. NATS determines its delay based on those factors which are directly attributable to its activities (i.e. staffing, capacity and systems-related) and has compared its performance with the equivalent European value.

complex and congested airspace in the world, without disruption to our commercial airline customers and whilst accommodating HM Government's national security requirements.

Meeting this challenge required three years of planning, consultation and liaison with the Department for Transport, the military, the CAA, European ANSPs, EUROCONTROL, airlines, airports and the general and business aviation communities. Temporary airspace arrangements were necessary to manage the anticipated increase in air traffic volumes and national security arrangements. This required our engineers to update our systems and develop new controller workstations to reflect changes to airspace and our air traffic controllers to undertake intensive training to operate the new airspace and routings.

During the Olympics period we achieved an average delay per flight of just 1.5 seconds. This performance reinforces our internationally-recognised expertise in developing and safely managing complex airspace solutions. We are perfectly placed to provide advice and guidance to future hosts of the Games or other global events, particularly in regions that are experiencing a rapid growth in air traffic volume. Our experience and skill in managing our own congested airspace during the Games period means we can help solve these and similar issues.

Vision and strategy

NATS' vision is to be the acknowledged global leader in innovative air traffic solutions and airport performance.
Its strategy is based on three fundamental principles: to defend its existing market position; to grow its business by providing new and innovative products and services based on its core competencies; and to strengthen the capability of its business to enable us to realise its ambitions. At the very heart of this strategy is our intention to help our customers to deliver a better passenger experience.

NERL's business is founded on providing a safe, efficient and cost effective air traffic control service to its UK and North Atlantic en route customers. To defend its existing contracts it must continue to make its customer proposition attractive by focusing on service levels, our prices and the value which it offers. These principles are at the heart of our proposals for RP2, which we believe offers real choice to our en route customers for our Airspace activities. Achieving a satisfactory settlement for RP2 is a key priority for 2014, whilst taking the actions in CP3 necessary to ensure that cost efficiency targets can be met.

This year NATS reorganised its economically regulated and non-regulated businesses by service line. These reflect core competencies and routes to market and provide greater clarity to customers

of the capabilities offered under the NATS brand.

Safety

Our first priority remains the safety of aircraft and the travelling public. We have an international reputation for our approach to safety management, our well established safety culture and our excellent safety record.

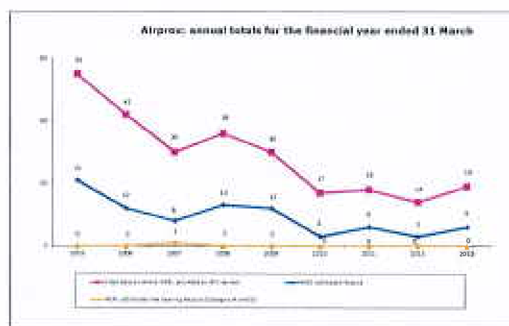
Our safety improvements focus on tackling the operational risks and subsequent sources of safety incidents, including working with others in our industry to do so. The most significant operational risks are: infringements of controlled airspace, level busts[2] and human performance.

During the year we have reduced the Weighted Safety Significant Event (SSE)[3] index by a further 33% when considering all events. For events that are attributable partly or wholly to NERL the reduction is 54%. This is an excellent achievement and is a further testament to the work we have done to reduce our contribution to safety risk in aviation. Over the first two years of this control period we have reduced the Weighted SSE Index by a cumulative 39% for all events and 64% for events attributable to NERL.

2 An aircraft deviation of 300 feet or more from its assigned level

3 The Weighted SSE Index is a single figure calculated by giving a weighted value to our 4 event scores (SSE 1-4). These values are combined in the index to provide the measure of safety performance used within the company to track our overall safety progress over time. It distinguishes between those events that are attributed wholly or partly to NERL, and those that are not (although both are addressed in our safety activities). The SSE scheme categorises safety events based upon severity (1-4) and separation distance (a-d), where 1a is the most severe and 4d the least severe.

For the fifth successive financial year we achieved our target of no category A or B Airprox[4] attributable to NERL and our strategic safety target to March 2015 is to maintain this record along with a further 10% reduction in our Weighted SSE index.



Note: Safety statistics for 2013 include NERL's assessment of the outcome of the UK Airprox Board reviews

The total number of Airprox events has increased since last year both in terms of the total number when NERL was providing a service (14 to 19) and the number of NERL attributed events (3 to 6). With such small numbers being reported we are focusing on further analysis of common causal factors for this increase, and the identification of associated lead indicators to ensure that this is reversed. It is also worth noting that the number of SSE events associated with Airprox remained the same at 6.

During the 2012 London Games, NERL safely implemented and controlled additional temporary airspace in conjunction with the military. No

4 An Airprox is a situation in which, in the opinion of a pilot or controller, the distance between aircraft as well as their relative positions and speeds have been such that the safety of the aircraft involved was or may have been compromised. The severity of these incidents is assessed periodically by the UK Airprox Board, an independent body, in the interests of enhancing flight safety.

overloads or incidents within the temporary controlled airspace were attributable to NERL.

Our safety improvement activities have been focused on addressing our most significant operational risks. The key activities on level busts have included a further roll-out of a broadcast of the Transition Level on the Automatic Terminal Information Service (which provides weather and essential airfield information to aircraft) at Luton and Heathrow to remind pilots of the level at which the altimeters need to be adjusted. This is to assist crews in avoiding a loss of separation. Also, the Barometric Pressure Setting Advisory Tool (BAT) continues to provide valuable mitigation in alerting controllers to incorrect pressure settings by flight crew.

With regards to infringements, NERL awarded the first Infringement Prevention Award to Stapleford Flight Centre for their success in reducing infringements by 50% from the previous year. This was achieved by working with NERL to improve pilot briefings and training. It is our intention to build on this with other airfields and flying clubs and we look forward to making this award on many more occasions in 2014.

To ensure we continue to develop our air traffic controllers, we have put in place a continuous professional development (CPD) programme. This is providing a foundation for improvements in safety and performance by ensuring that controllers are kept up to date with the demands of their continuously changing profession. CPD is now firmly embedded at Swanwick and is being implemented at Prestwick.

As the opportunities for tactical safety improvement continue to reduce, NERL is looking at how to address future risks to the ATM industry. To this end we have been developing our safety strategy through to 2025. This has included ensuring we are closely aligned to SESAR and developing long term strategies for automation and human performance. Taken together these strategies will enable the evolution of safety performance, reporting and monitoring within NERL over the next 10 years.

Regulatory developments

The overarching regulatory framework in which NERL's regulated activities operates is now determined by the European Commission's Single European Sky (SES) legislation. Under this framework, certain EU-wide performance targets are established and it is the role of member states and national regulators to develop Performance Plans consistent with these targets.

Last summer the European Commission (EC) approved the UK's National Performance Plan for Reference Period 1 (2012-2014), fulfilling the UK's obligations under the SES, which aims to modernise and optimise Europe's air traffic management network including the performance of air traffic service providers. NERL's plans for its

economically regulated activities formed the majority of this plan for the UK, which is consistent with the CAA's previous decision for the price control period 2011-2014. If it fulfils the assumptions made by the CAA for CP3, NERL will earn a cash-based regulatory return of c. 6.8% p.a. on its regulatory asset base.

The EC and CAA have already started preparations for the next regulatory period, Reference Period 2 (RP2), which runs from 2015 to 2019. The EC plans to finalise targets for RP2 in December 2013 covering four Key Performance Areas (KPAs): safety, capacity, environment and cost efficiency. Targets for RP1 were set for en route cost efficiency and capacity only.

Following consultation on potential changes to the regulations for RP2, the EC accepts that the impact of financial market conditions on defined benefit pension costs could be fully reflected in prices (subject to a stewardship test), that appropriate incentives should continue to exist to reward excellent service performance and penalise poor performance (subject to a cap) and that the one-off restructuring costs necessary to achieve its challenging cost efficiency targets could be included in prices and taken into account when assessing the contribution of ANSPs to cost efficiency targets.

EU member states will be required to submit draft Performance Plans by June 2014 to enable the EC to assess whether these plans make an adequate contribution towards the EU-wide targets and therefore whether they should be accepted. Unlike RP1, these Performance Plans will be established at Functional Airspace Block (FAB) level and therefore for the UK this means a combined UK-Irish submission.

Reflecting the requirements of airline customers, the EC's priority for RP2 is to secure significant en route price reductions, with the EC challenging ANSPs to reduce prices significantly at the same time as improving performance across all the other KPAs. The EC has stated that it expects a significant contribution from the major ANSPs to EU-wide cost efficiency for RP2. Although it accepted the UK's Performance Plan for RP1, the EC stated that it expects a more significant contribution to cost efficiency targets from the UK, especially as the UK currently has the highest unit rate in the EU.

It is worth noting though that when measured using the EC's own financial cost-effectiveness measure (cost per flight hour), NERL is the best of the largest five ANSPs (others being France, Germany, Italy and Spain) and it is on a par with Ireland.

The EC's advisers on economic regulation (the Performance Review Body) published in February 2013 initial proposals for RP2 cost efficiency targets ranging from real reductions in the unit rate of between 3.2% p.a. and 6.9% p.a. and revised this in May 2013 to between 3.9% p.a. and

5.8% p.a. (using STATFOR's base case forecast). By comparison, the EU-wide target for RP1 was for real reductions of 3.5% p.a.. NERL has developed a draft RP2 Business Plan taking account of the initial target range and is putting forward two price reduction offerings for customers to consider: a service-led plan at lower price and a price-led plan. The former is aimed at customers who want the lowest price for a similar quality of service that we provide today together with airspace and system improvements in line with Future Airspace Strategy (FAS) and SESAR (see below), and the latter delivers an even lower price in RP2 with good performance but with customers taking on more service risk. This Business Plan was published for customer consultation in May 2013. Following consultation in summer 2013 and publication by the EC of further information on its targets, NERL expects to submit a revised Business Plan to the CAA in October 2013. Following CAA scrutiny, this plan will form part of the UK-Ireland FAB Performance Plan.

The small airspace volume contained within the UK-Ireland FAB relative to other FABs in Europe makes it challenging to find direct cost saving opportunities. However, our 'design and build' approach has delivered significant operational benefits to our customers, including total cumulative savings which are estimated to arise between 2008 and 2020 of €337m through reducing fuel usage by 332,000 tonnes. Our RP2 Performance Plan will also include an extension of the High Level Sectors work by exploring the possibility of dynamic sectorisation both ways across our airspace boundary through operational trials in 2013 and 2014. Ensuring both operational and cost efficiency benefits to our customers will be key to its success.

Single European Sky (SES)

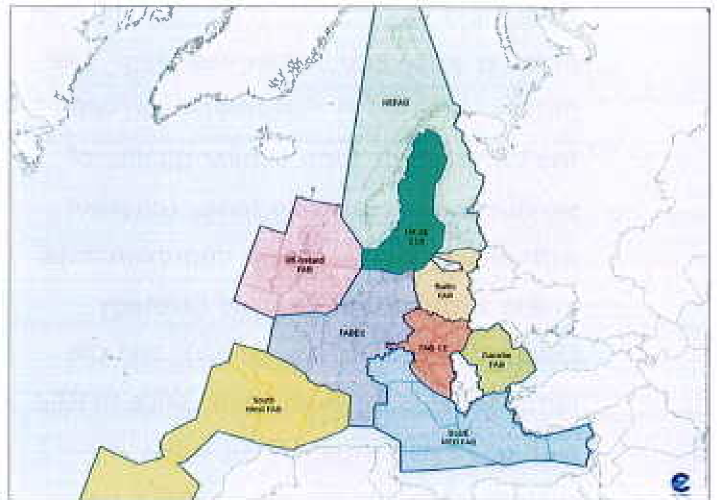
One of the challenges in Europe over the coming years will be deploying the technology and concepts that will help deliver the SES vision. The development of the new generation of technological systems is currently being managed by the SES ATM Research (SESAR) Joint Undertaking; a collaboration of the European Commission and the aviation industry, including NERL. Once this is completed in 2013, the deployment phase (2014 to 2020) will see the large-scale production and implementation of new air traffic management infrastructure that will be fully harmonised and interoperable across Europe. To manage this phase it is important that the deployment management role is clearly defined this year. Whilst there are a number of parties interested in the role, and a fully cooperative approach will be required in practice, as one of the biggest investors in the ATM system of the future it is vital that air navigation service providers (ANSPs) play a pivotal role in shaping deployment. NERL has been gathering support for an ANSP-led approach from the A6 Group, an alliance of the largest

European ANSPs set up to drive the modernisation of ATM systems in Europe which NATS chairs, and the Civil Air Navigation Services Organisation (CANSO), which represents the interests of ANSPs worldwide and on which we sit on the Executive Council. As a key step towards making the business case to airlines, NERL will continue to work within the A6 Group to ensure the next edition of the SESAR Master Plan (due in 2014) contains a robust assessment of deployment costs for all stakeholders and the net benefits it will enable, and press for the EC to accelerate setting up the deployment manager as an essential prerequisite to timely deployment.

Alliancing strategy

Given the strong EC regulatory focus on addressing Europe's current fragmented ATM system, achievement of future regulatory requirements through isolated national action by ANSP will be challenging. Therefore, there is growing pressure for operationally beneficial partnerships which build on, or compliment, the current frameworks (FABs and SESAR) to deliver the future SES ATM system.

Over the past few years NERL has entered into a number of alliances with a view to positioning itself as a European leader in ATM within the context of SES. The form and nature of these alliances varies, but fundamentally they have been focused on delivering operational benefit to our customers. For example, we are a member of the Borealis Alliance of 9 North European ANSPs which focuses on strategic business cooperation between ANSPs, seeking economies of scale and projects that can be achieved on a commercial basis, complementing the work of the northern



Source: EUROCONTROL

European Functional Airspace Blocks (FABs – see illustration) but without the need for regulatory or State involvement. This alliance also helps achieve Single European Sky ATM Research (SESAR) deployment, in service of Single European Sky (SES).

We will continue to develop alliances with European ANSPs and believe this wider cooperative model is likely to deliver greater integration benefits to customers in RP2 than the current FAB approach.

We are also influencing the industry in other ways. We are a member of the Aviation Platform, made up of representatives of the European aviation sector, set up to provide strategic advice to the EC on how to establish the basis for a sustainable future for air transport and

a competitive future for the European aviation industry.

UK Aviation strategy
The Department for Transport published its draft policy framework for aviation in July 2012. Its strategy focuses on more frequent flights to emerging markets, improved access to airports and a reduction of the impact of airports on local communities. The final policy framework is due for publication in July 2013.

Of particular relevance to NERL is support for the SES programme. To this end NERL is in the early stages of developing the airspace design which will deliver the Future Airspace Strategy published by the CAA in 2011, though any changes to airspace rely on clear environmental parameters being established by the aviation policy framework.

We are also contributing to the Airports Commission's review of options for ensuring appropriate hub capacity in the UK. It expects to publish an initial report later in the year that will include interim measures to address South-East airspace capacity pending development of a future hub strategy.

People
Our people are committed and professional at what they do. Our strategic objective is to have a motivated and competent workforce, proud of their contribution to the company's success in delivering an excellent performance for our customers: people valued and adding value.

The successful delivery of a safe and efficient air traffic service during the Olympic period is a testament to the professionalism of our front line operational staff and engineers and those supporting them. I would like to take this opportunity to congratulate and thank everyone involved in NATS and in our partners who contributed in the planning and execution of the Games service.

Our employees have faced other challenges this year too in the form of pension changes. Like many other UK defined benefit schemes, the fall in real gilt yields in recent years to record low levels has had the effect of significantly increasing the liabilities of NATS' defined benefit scheme but without a corresponding increase in scheme assets (two thirds of which are equities and similar return-seeking assets).

As a result, it was clear that NATS would be facing a material increase in pension contributions after the actuarial valuation at 31 December 2012 unless changes were made. Through Working Together with NATS' trades unions staff were balloted on, and agreed, to reduce the existing limit on the annual rate of increase in pensionable pay and to recommend to the scheme's Trustees that future service benefits should be indexed at CPI (rather than RPI). When these changes were reflected alongside the Trustees' assumptions for the 2012

valuation the NATS scheme's deficit was £382.6m (compared with £351.1m in 2009) and contributions were set at a more affordable level. NERL's share of the group deficit is c. 75% or £287m.

Staff agreed to a three-year pay award closely linked to CPI which provides certainty to them and the company alike. Also, from 2014 NATS is introducing a Company Performance Related Pay Scheme which directly links the NATS group's profit performance and the value of an employee's total rewards.

In order to achieve the cost efficiency targets we expect in RP2 we will have to reduce our headcount, and we announced a voluntary redundancy scheme to staff in May 2013. Crucially, to achieve the level of savings necessary, this will require staff reductions across all areas of the business including operational front line staff. This will be challenging and will require excellent engagement, careful resource planning, focused staff development and positive and constructive industrial relations through Working Together with trade unions.

Overview of financial performance

	2013 £m	2012 £m
Revenue	**713.6**	695.6
Operating profit	**205.4**	200.7
Profit before tax	**151.4**	154.8
Profit after tax	**118.4**	127.5
Dividends	**28.5**	45.0

It was a year of solid financial performance for the company. Revenues improved by £18.0m to £713.6m (2012 (£695.6m) due largely to net increases in en route revenues and better service performance. The factors impacting on revenue are described in more detail in the review of service line performance below.

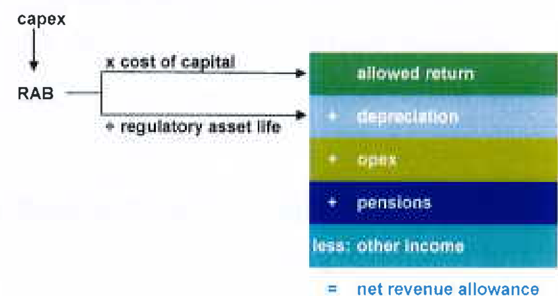
Profit before tax fell by £3.4m to £151.4m (2012: £154.8m). This reflected higher staff pension costs, a full year's depreciation charge for new controller tools (iFACTS and EFD) and higher net finance costs. The latter included the change in the market value of the index-linked swap contract and the unwinding of the discount applied to property re-instatement costs. The following table explains the reduction in profit before tax for the year.

	£m	Profit before tax £m
2012 profit before tax		154.8
Revenue changes		
NATS Airspace:		
Net increase in revenue (allowing for traffic volumes & inflation)	17.1	
Deferred recovery of revenue adjustments	(3.3)	
Pricing below the revenue cap	(1.0)	
Service performance incentive	1.4	
Revenue from other group companies	2.8	
Other net revenue changes (including foreign exchange)	1.7	
		18.7
Other NATS Service lines		(0.7)
Cost changes		
Staff costs		(3.6)
Non-staff costs		(1.5)
Depreciation & amortisation, net of deferred grants	(11.5)	
Asset impairment charges	2.3	
Loss on disposal of assets	1.0	
		(8.2)
Change in fair value of index-linked swap contract	(3.6)	
Other finance costs (net)	(4.5)	
		(8.1)
2013 profit before tax		151.4

Economic regulatory framework and price controls

NERL provides en route air traffic services under a licence granted by the Secretary of State under the Transport Act 2000. The Act gives the Civil Aviation Authority (CAA) the role of economic regulator. UK and North Atlantic en route, London Approach and North Sea helicopter advisory services are regulated by this licence.

Following consultations with airlines and other stakeholders, the CAA established revenue allowances for 2011 to 2014 (control period 3 or CP3) for the economically regulated services. These were set at levels designed to remunerate NERL's efficient investment (capex), operating costs (opex), pensions and an allowed return on the capital invested in the regulatory asset base (RAB) to recover the cost of capital. The RAB, which represents the value ascribed to the capital employed in our regulated businesses, was adjusted to reflect asset additions, disposal proceeds, regulatory depreciation and the rate of inflation. Certain other income generated outside of the economically regulated activities was deducted under a 'single till', leaving a net revenue allowance. The price condition for CP3 in NERL's licence has been set to allow NERL to recover this net revenue requirement based on forecast traffic for the control period. This regulatory model is illustrated below.



The price control for the 4 years of CP3 (the last 3 years of which coincide with Reference Period 1) was based on total revenues of £2.2bn (expressed by the CAA in 2008/09 prices) and provides a pre-tax real return on the RAB of 7.0% p.a.. This headline cost of capital was adjusted by the CAA to 6.8% to allow for the re-investment of surplus cash during each year. If the regulatory and other assumptions are borne out in practice, then a return of 6.8% p.a. would result.

The CP3 decision also provided three key risk mitigations: a risk sharing mechanism to protect against certain variations in traffic volumes from the level assumed; a true-up to charges in subsequent control periods where cash contributions to the defined benefit pension scheme differ

from the CP3 forecast; and a target and cap on the level of NERL's gearing set at 60% and 65% of net debt to RAB, respectively. Charges may be adjusted for service performance incentives, traffic volume risk sharing and for changes in inflation from the level forecast in the CP3 settlement.

As noted in the business review above, we have developed a customer consultation business plan for RP2. We expect the structure of the economic regulatory framework for UK en route services for RP2 will be largely consistent with CP3 and with similar risk mitigations.

Comparison between reported profit and regulatory return

The profits reported in these financial statements are prepared in accordance with International Financial Reporting Standards and policies described in note 2 to these accounts. As described above, the CAA applies an economic regulatory building block model. This is mainly cash-based. It can give rise to some significant differences between reported operating profit and regulatory return. The main reasons include:

- lower historical cost depreciation compared with regulatory depreciation which is indexed to enable the replacement of the capital investment base; and
- lower accounting pension costs using best estimate assumptions prescribed by accounting standards compared with the cash contributions agreed with Trustees which include a margin for prudence.

This difference in basis explains why, generally, reported profit is some £100m higher than regulatory return. This regulatory view is set out in NERL's audited published regulatory accounts.

Service line financial performance

From April 2012 we organised our activities according to service lines, each representing a core set of products and services that we offer to our customers. A brief description of each service line is provided below together with a summary of financial and operational performance. The principal financial targets for each service line are revenue and contribution. The latter takes account of the operating costs which service line managers are able to influence directly. For this reason depreciation charges, exceptional items, costs managed outside of service lines and variances to budgeted pension costs, for example, are not included in service line contribution. The volatility of market conditions between setting the budget for pension costs and the rate being known at the start of the financial year, combined with the size of the scheme, means these variances can be material. A reconciliation of service line contribution to the company's operating profit is provided in note 5 to the financial statements.

This year saw good financial performance across each of our service lines with each reporting an improvement in service line contribution.

NATS Airspace

	2013	2012
Financial performance:		
Revenue (£m)	710.8	692.1
Service line contribution (£m)	367.9	345.7
Capital expenditure (£m)	126.8	127.3
Operational performance:		
Flights handled ('000s)	2,126	2,167
Risk-bearing airprox (no.)	nil	nil
Average delay per flight (seconds)	1.3	7.0
Enabled fuel savings (tonnes)	6,926	25,000

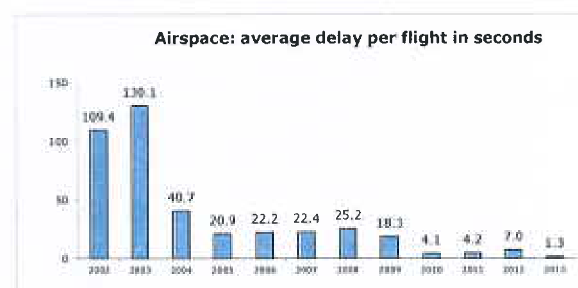
NATS Airspace includes all of NERL's economically regulated activities: UK en route services provided to aircraft operating in controlled airspace; en route services to traffic in that part of the North Atlantic where NERL provides a navigation service; approach services for aircraft arriving at and departing from the five main London airports; services to North Sea helicopter operators; and services and infrastructure provided to the military.

Revenue from NATS Airspace services increased to £710.8m (2012: £692.1m), principally due to an increase in UK en route revenues, after allowing for lower traffic volumes and higher inflation than assumed in the CP3 settlement, and due to better service performance. Offsetting this were a reduction arising from the deferred recovery of permitted revenue adjustments under EC charging rules and the impact of pricing below the level of permitted revenue allowances. The latter was a response to the difficult economic environment facing our en route and London Approach customers and saved them c. £1m this financial year and c. £5m in the 2014 financial year.

Service line contribution improved to £367.9m (2012: £345.7m). Attributed operating costs were lower mainly reflecting staff pension charges (at budgeted rates), capitalised staff costs and lower headcount which offset annual pay increases and indexation uplifts on property maintenance costs.

	2013 ('000s)	2012 ('000s)	Year on year change %
Chargeable Service Units	**9,395**	9,676	(2.9%)
Total UK traffic (flights):			
Domestic	385	395	(2.5%)
North Atlantic	310	322	(3.7%)
Other	1,431	1,450	(1.3%)
Total	**2,126**	2,167	(1.9%)
Oceanic traffic (flights)			
Chargeable flights	**393**	402	(2.2%)

The volume of flights handled in the year of 2.1m was 1.9% lower than the previous year, reflecting the weak UK and European economies and airlines increasing aircraft load factors.



The level of delay attributable to NATS Airspace represented an average delay per flight of 1.3 seconds, with 99.9% of flights not delayed (2012: 99.3%). This was achieved despite releasing operational staff for Olympics training in the first half of the year and reflects the benefit of iFACTS (interim Future Area Control Tools Support) which reduces controller workload in planning and maintaining safe separation, allowing more flights to be handled with improved

safety. Last year NATS Airspace achieved 7.0 seconds when frontline staff were being trained on iFACTS. The average delay per delayed flight was also lower at 15.6 minutes (2012: 16.6 minutes).

CP3 metrics: 2012 calendar year	Olympics period		Rest of period	
	Target adjusted for traffic	Actual	Target adjusted for traffic	Actual
T1: avg. delay per flight (secs)	13.6-27.6	1.5	7.7	1.5
T2: delay impact (score)	38.5-78.9	3.0	21.8	3.2
T3: delay variability (score)	299.3	-	1,137.5	1.0
T4: 3Di metric (score)	n/a	n/a	24.0	23.9

This service performance is within the CP3 par value targets (adjusted for lower traffic volumes than assumed in the CP3 settlement) for the Olympic period and for the rest of the 2012 calendar year, and earned a bonus of £6.8m (2012: £5.4m).

In addition to measures of delay, we are incentivised on the environmental performance of our network. The flight efficiency metric, the 3Di (three dimensional inefficiency score), was introduced for the 2012 calendar year. It compares the actual trajectory that an aircraft takes with an optimal profile that minimises fuel burn and CO_2 emissions. For the 2012 calendar year we achieved a 3Di score of 23.9 compared with the par value of 24.0.

The CAA estimates that achieving the 3Di target through CP3 will generate 600,000 tonnes of CO_2 savings compared to historic levels by the end of 2014, worth over £120m to airlines.

Our customers also set us service targets under our Operational Partnership Agreement (OPA) by which we work together to agree priorities and achieve short term operational improvements. We achieved the financial year targets for reducing early morning delays, avoiding the prolonged application of short-term air traffic flow restrictions and for generating fuel savings.

OPA performance targets for 2012/13	Target	Stretch	Actual
Early morning delays (flights delayed > 15 minutes)	2,200	1,600	199
Short term flow regulations (% <= 45 minutes duration)	94%	96%	96%
Enabled fuel savings (tonnes)	4,250	5,500	6,926

Our environmental strategy includes ensuring we consider the impact of how we control aircraft every day. This includes how we improve the efficiency of our airspace, route network and in the investment decisions we make regarding new technology. We also seek to deliver short term tactical benefits to our customers, and this year we enabled 6,926 tonnes (2012: 25,000 tonnes) of fuel savings from changes to procedures, equivalent to 22,025 tonnes (2012: 80,000 tonnes) of CO_2 emissions, and worth approximately £4.5m in savings to our customers (based on average fuel prices of £650 per tonne). For 2014, the OPA has set a target of 12,000 tonnes with a stretch of 18,000.

Achieving our CO_2 target beyond 2015 is heavily dependent upon investment and as such is subject to the outcome of RP2. A focus on achieving lower prices could materially affect those key programmes that enable flight efficiencies, impacting

our environmental performance during RP2.

A more detailed review of environmental performance and strategy is provided in the Corporate Responsibility section of the Annual Report and Accounts of NATS Holdings.

NATS Airspace invested £126.8m (2012: £127.3m) in support of its air traffic control infrastructure in the year. This included continuing to develop the next generation flight data processing system which will be compatible with European systems, though future expenditure on the necessary workstation and the timing and sequence of deploying this technology into air traffic control centres has been reviewed in light of lower traffic volumes. iFACTS, a significant investment made last year, is now in full operational service. It still features in our investment programme as we continue to upgrade our core systems.

The radar replacement programme is nearing successful completion with 26 of 27 radars having been replaced over the last ten years. Investment is now focusing on voice and data network modernisation and on implementing the EC's mandate for datalink services between pilots and air traffic controllers.

Additional investments are also being made in service of the UK's airspace strategy, discussed above. Of particular importance will be the development of airspace in the South-East, which will enable better safety, efficiency and environmental performance.

Other NATS Service lines

	2013	2012
Financial performance:		
Revenue (£m)	2.8	3.5
Service line contribution (£m)	2.2	2.1

Other NATS Service lines includes NATS Information and NATS Defence services provided to customers in the UK and overseas.

NATS Information provides data to enable improved efficiency and flight optimisation to customers. NERL already has a well-established relationship with the UK's Ministry of Defence (MoD) which we are seeking to extend: our joint and integrated civil and military air traffic control services contract is managed and reported by NATS Airspace.

Revenues at £2.8m (2012: £3.5m) are lower reflecting a number of one-off contracts undertaken in the prior year. Costs reduced by £0.8m to £0.6m (2012: £1.4m) mainly reflecting a reduction in costs associated with those one-off contracts. Overall the contribution increased by £0.1m to £2.2m (2012: £2.1m).

Review of operating costs

The company incurred operating costs of £508.2m (2012: £494.9m).

	2013 £m	2012 £m
Staff costs	**(279.5)**	(275.9)
Service and materials	**(46.8)**	(47.8)
Repairs and maintenance	**(28.7)**	(26.8)
External research and development	**(0.1)**	(0.2)
Other operating charges (net)	**(51.6)**	(50.9)
	(406.7)	(401.6)
Depreciation and amortisation	**(100.8)**	(89.5)
Asset impairment charges	**(1.1)**	(3.4)
Deferred grants	**0.4**	0.6
Loss on disposal of non-current assets	**-**	(1.0)
Operating costs (net)	**(508.2)**	(494.9)

Staff costs account for 55.0% (2012: 55.7%) of the company's operating costs. These increased by 1.3% on the previous year. Pension charges (before redundancy-related past service cost) were £6.9m higher at £71.1m (2012: £64.2m) mainly due to an increase in the accrual rate to 27.3% (2012: 24.1%) before salary sacrifice, for the defined benefit pension scheme reflecting the scheme's financial position at the start of the year and actuarial assumptions. This was partly offset by higher capitalisation of labour and lower overtime costs which were required last year for the delivery of controller tools (iFACTS and EFD). The average number of staff employed during the year was 3,404 (2012: 3,440) and those in post at 31 March 2013 decreased by 0.4% to 3,405 (2012: 3,420).

Non-staff costs at £127.2m (2012: £125.7m) increased by 1.2% and included higher property maintenance and utility costs.

Depreciation and amortisation charges increased to £100.8m (2012: £89.5m) as a full year's charge was incurred for technology introduced during the last financial year (such as iFACTS and Electronic Flight Data). This was partly offset by lower impairment charges of £1.1m (2012: £3.4m).

Net finance costs

Net finance costs increased by £8.1m to £54.0m (2012: £45.9m). This included an increase in the market value liability of the index-linked swap, reflecting market expectations of inflation and swap discount rates, and the effect of unwinding the discount on provisions for property re-instatement costs.

Taxation

The tax charge of £33.0m (2012: £27.3m) was at an effective rate of 21.8% (2012: 17.6%). This is lower than the 2012/13 headline rate of corporation tax of 24% due to the deferred tax impact of a reduction in the corporation tax rate to 23% from April 2013, as enacted by the 2013 Finance Bill.

A statement on the NATS group's tax strategy is set out in the Annual Report and Accounts of NATS Holdings.

Dividends

During the year the company paid dividends totalling £28.5m (2012: £45.0m).

In May 2013 the Board declared and paid an interim dividend for the year ending 31 March 2014 of £42.75m.

Balance sheet

The company balance sheet can be summarised as follows:

	2013 £m	2012 £m
Goodwill	**351.0**	351.0
Tangible and intangible fixed assets	**899.0**	874.1
Other non-current assets	**58.6**	47.3
Cash and short term deposits	**102.2**	102.2
Other net current assets	**30.1**	19.0
Derivatives (net)	**(145.6)**	(126.3)
Pension scheme surplus/(deficit)	**10.8**	(28.8)
Borrowings	**(707.7)**	(749.8)
Deferred tax	**(103.5)**	(95.5)
Other non-current liabilities	**(21.8)**	(12.5)
Net assets	**473.1**	380.7

Shareholders' funds increased by £92.4m to £473.1m during the year. This mainly reflects the retained earnings for the year less dividends of £28.5m.

Movements in pensions, cash and borrowings are explained below. Changes in fixed assets reflect the company's capital investment in the year of £126.8m, net of depreciation charges. Other significant changes in the financial position include the movement on derivative financial instruments and changes in the deferred tax liability mainly arising from the change in the pension financial position.

Defined benefit pensions

a. IFRS – accounting basis

At 31 March 2013, measured under international accounting standards and the associated best estimate assumptions, the company's share of the group's defined benefit scheme was in surplus with assets (of £2,943.7m) exceeding liabilities (of £2,932.9m) by £10.8m (2012: £28.8m deficit). The improved funding position was due to growth in the scheme's assets which offset the increase in liabilities, the latter being driven by a reduction in the discount rate from 5.05% to 4.45%. Under IFRS, the discount rate is based on the yield on AA corporate bonds.

The pension funding position under IFRS can be sensitive to certain changes in market conditions which impact on the value of pension scheme assets and/or liabilities (for example, a change in corporate bond yields).

b. Actuarial – Funding Basis

From January 2011, the company started to pay deficit recovery contributions to the defined benefit scheme under an 11-year recovery plan agreed with the Trustees following their 2009 actuarial valuation. This valuation, which is for funding purposes and uses assumptions including a margin for prudence, gives rise to a different valuation than that disclosed under international accounting standards. It determines the contributions that NATS is required to make to the defined benefit scheme.

The 2009 actuarial valuation reported a deficit of £351.1m (see table below), with NERL's share being c. 75% or £263m. During the year to 31 March 2013 the company paid its share of deficit recovery payments of £18.8m (2012: £18.3m). Before pension salary sacrifice payments of £11.7m and redundancy-related augmentation payments of £1.3m, the company's overall contributions to the defined benefit scheme were £93.9m (2012: £94.9m), equivalent to 45.9% of pensionable pay (2012: 45.5%).

Actuarial valuations at 31 December:

	2012 £m	2009 £m
Assets	3,527.5	2,793.9
Liabilities	(3,910.1)	(3,145.0)
Deficit	(382.6)	(351.1)

The scheme actuary's latest triennial valuation of the scheme was prepared as

at 31 December 2012. This reported a scheme deficit of £382.6m (NERL's share being c. £287m), an increase since the valuation as at 31 December 2009 despite the deficit recovery payments made since 2011 and the subsequent pension changes. This deficit has arisen mainly because the liabilities of the scheme increased significantly in the intervening period as a result of a reduction in real gilt yields, and because there was not a corresponding increase in the value of assets. The increase in liabilities would have been significantly worse had mitigating actions not been taken by the company to reduce the limit on increases in pensionable pay from RPI + 0.5% to CPI + 0.25%.

Following confirmation of the results of the 2012 actuarial valuation, the Trustees and the company have agreed a revised schedule of contributions and a deficit recovery plan for the period to 31 December 2023. This requires the company to contribute in line with the existing schedule of contributions until 1 January 2015. From 1 January 2015 future service contributions will reduce from 36.7% of pensionable pay (excluding salary sacrifice) to 29.4%, reflecting the revised cap on pensionable pay increases and the Trustees' decision to move to CPI-linked indexation of future service from 1 November 2013. Also, from 1 January 2015, annual deficit contributions will be revised and will start at £28.6m (NERL's share being c. £21.5m), increasing by 2.37% each year. This means that for the period of RP2 (2015 to 2019), contributions will average c. 41% of pensionable pay, compared with c. 46% currently. The lower cap on pensionable pay and change in future service indexation are estimated to avoid contribution increases amounting to c. £200m in RP2.

The company also continues to work with Trustees to ensure an appropriate investment strategy is in place, which includes de-risking the scheme as funding levels improve and thus mitigating future volatility in the funding position.

Funding and treasury management

In May 2012 the company refinanced its bank facilities with a £275m facility expiring in December 2016.

At 31 March 2013, borrowings were £707.7m (2012: £749.8m). Cash and investments remained constant at £102.2m (2012: £102.2m). Overall, net debt decreased by £42.1m to £605.5m (2012: £647.6m).

Movements in net debt

	Cash and short-term investments £m	Borrowings £m	Net debt £m
Balance at 31 March 2012	102.2	(749.8)	(647.6)
Cash flow	0.4	43.6	44.0
Short-term investments	(0.4)	-	(0.4)
Non-cash movements	-	(1.5)	(1.5)
Balance at 31 March 2013	**102.2**	**(707.7)**	**(605.5)**

Cash flow

Overall, the company's balance of cash and cash equivalents remained constant at £102.2m (2012: £102.2m).

Net cash flows from operating activities at £232.8m were £29.1m higher than last year (2012: £203.7m) reflecting higher income receipts and lower out flows from

operating costs. This enabled the company to finance its capital investment, service its debt obligations and pay dividends to shareholders. Bond repayments were £28.4m (2012: £14.2m) and £12.3m of bank loans were repaid (2012: £28.8m drawn).

	2013 £m	2012 £m
Cash generated from operations	**253.9**	218.9
Taxation	**(21.1)**	(15.2)
Net cash from operating activities	**232.8**	203.7
Interest received	**0.7**	0.9
Capital expenditure (net of costs of disposal)	**(127.6)**	(121.1)
Change in short-term investments	**0.4**	(14.1)
Net cash outflow from investing activities	**(126.5)**	(134.3)
Interest paid	**(35.1)**	(35.3)
Interest received on derivative financial instruments	**1.3**	1.6
Bank and other loans	**(12.3)**	28.8
Bank facility and arrangement fees	**(2.9)**	-
Loans repaid to fellow subsidiary	**-**	(0.9)
Repayment of bond principal	**(28.4)**	(14.2)
Dividends paid	**(28.5)**	(45.0)
Net cash outflow from financing activities	**(105.9)**	(65.0)
Increase in cash and equivalents	**0.4**	4.4

Principal risks and uncertainties

The operational complexities inherent in the business leave NERL exposed to a number of significant risks. The company has maintained a focus on mitigating those risks although many remain outside of our control – for example changes in governmental regulation, security threats, environmental factors and the impact of longevity and financial markets on pension funding.

The Board believes that the risks and uncertainties described below are the ones that may have the most significant impact on the long-term value of NERL. These risks are re-assessed regularly and reflect the Board's assessment as at the date of this report. The list is not intended to be exhaustive.

The company carries out detailed risk management reviews to ensure that the risks are mitigated where possible.

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

The risk of aircraft collision

A loss of separation attributable to NERL that results in a collision in the air would significantly impact on NERL's reputation as a provider of safe air traffic services. This could result in a loss of revenue in the short-term as investigations take place and the loss of future contracts. If notice was given by the Secretary of State requiring NERL to take action as a result of the collision and NERL was unable or failed to comply with the notice then ultimately this could result in revocation of NERL's air traffic services licence. To mitigate this risk NERL has developed a strategic plan for safety and maintains a safety risk management system.

Loss of service from an air traffic control centre

A loss of service from a centre would result in a loss of revenues as flow management procedures would be introduced to maintain safety standards. The extent of loss would depend on the time necessary to resume a safe service. To this end NERL has invested in developing contingency arrangements.

Operational systems resilience

Operational service provision is increasingly dependent on the performance and resilience of engineering systems and communications, surveillance and flight data infrastructure. To mitigate the risk of service disruption the resilience of operational systems is reviewed regularly.

Pension scheme funding

Adverse movements in pension asset and liability values arising from factors such as lower investment returns, lower real interest rates and improving life expectancy may increase the size of the pension deficit. Management regularly reviews the financial position of the defined benefit pension fund and is consulted by Trustees on the design of the risk reduction strategies that are in place. The scheme was closed to new entrants in 2009, pensionable pay rises have been capped for existing members and indexation of future service benefits will be CPI-linked from 1 November 2013. The next formal review of the funding of our defined benefit scheme will take place as part of the triennial valuation as at 31 December 2015.

Industry outlook

Poor market and economic conditions can reduce NERL's revenues to levels below those assumed by the economic regulator in making the CP3 price determinations. This in turn could impair shareholder returns. NERL monitors the key industry indicators on a monthly basis against CP3 forecasts and has taken action in the past to realign its cost base with lower revenues. As explained in the opening part of this financial review, NERL has traffic volume risk sharing arrangements that mitigate revenue reductions to a large extent.

Key programme and project risks

The complex and unique nature of some of NERL's technology projects create an inherent risk of project overruns, delayed benefits and damage to reputation with customers and other stakeholders. Changes in technology may also arise during the development period. NERL has mature project management processes and industry experts to mitigate this risk.

Electronic and other external threats

NERL has security processes, procedures and risk mitigation plans to address potential electronic and other external threats.

Employee relations

Industrial action could result in reduced air traffic service provision which adversely impacts on service performance. Every effort is made to maintain good employee relations at all times, including through our Working Together programme, to ensure the delivery of an efficient operational service and associated support.

Financial risks

The main financial risks of the company relate to the availability of funds to meet business needs (including meeting obligations to the pension scheme), the risk of default by counterparties 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 earnings. Transactional currency exposures that could significantly impact the income statement are hedged, typically using forward sales of foreign currencies. The company's most significant currency exposure arises because UK en route charges, which contribute 83% (2012: 83%) of total turnover, are set in sterling but are billed and collected in euros by applying a conversion rate determined monthly by EUROCONTROL, which administers the UK en route revenue collection. The resultant currency risk is materially eliminated by entering into forward foreign exchange contracts. At the year end, forward foreign currency transactions entered into to buy and sell sterling, designated as cash flow hedges, equivalent to £120.4m (net) were outstanding (2012: £106.6m (net)) as detailed in note 18.
- 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. NERL's strategy is to hedge a proportion of net debt in order to reduce its exposure to interest rate risk on its cash holdings. The regulatory charge control conditions that apply to the company's UK and North Atlantic en route services determines a revenue allowance for financing charges that is linked to inflation. To achieve an economic hedge of this income, in August 2003 coincident with the issue of its £600m bond, the company entered into an index-linked swap with a notional principal of £200m for the period up to March 2017 reducing semi-annually thereafter and expiring in March 2026. Under the terms of this swap, NERL receives fixed interest and pays interest at a rate adjusted for the movement in RPI. The swap does not qualify for hedge accounting under international accounting standards and is classified as held for trading. As such, movements in the fair value are taken to the income statement. As at 31 March 2013 (after derivatives), approximately 91.1% (2012: 89.4%) of NERL's net debt was either at fixed rates or at rates indexed to inflation.
- counterparty risk: as at 31 March 2013 the company had cash and deposits (shown as short-term investments) totalling £102.2m (2012: £102.2m). 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 £139.0m at 31 March 2013, the company had cash and short-term deposits totalling £102.2m. Included in cash of £102.2m is a liquidity reserve account balance held by NERL of £21.3m to provide liquidity in the event of certain pre-defined circumstances, particularly to ensure compliance with financial covenants. The short-term deposit of £30.1m represents a debt service reserve account held by NERL to fund bond principal, interest and fees scheduled for payment in the 6 months ending 30 September 2013. The company's policy is to hold free cash within NERL equivalent to between one and two months of projected UK en route services revenue (being between £49m and £98m for 2013) 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 (of which £42.6m had been repaid by 31 March 2013) issued by NERL with a final maturity date of 2026. At 31 March 2013 NERL had bank facilities totalling £275.0m that expire in December 2016.

Going concern

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

The company holds adequate levels of cash holdings and as at 31 March 2013 had access to £139.0m of undrawn committed bank facilities that are available until December 2016. The company's forecasts and projections reflect its expectations for CP3 and its initial assumptions for RP2 and taking account of reasonably possible changes in trading performance, show that the company should be able to operate within the level of its existing facilities for the foreseeable future. The UK en route business also benefits from some

protections against traffic volume risk afforded by its price control conditions. Other sources of income are generated mainly from long-term contracts. The company continues to actively make real reductions in the en route underlying operating cost base to meet cost efficiency targets expected to apply in RP2. As a result, the directors believe that the company is well placed to manage its business risks successfully despite the weak economic environment.

The directors have formed a judgement that taking into account the financial resources available to the company, it has adequate resources to continue to operate for the foreseeable future and have therefore adopted the going concern basis in the preparation of the financial statements for the year ended 31 March 2013.

Outlook

For now we remain firmly focused on understanding what our en route customers require from us in RP2. We understand that price reduction is now a key concern for them and for economic regulators. Therefore we are presenting them with choices which offer a trade-off between price and service performance, without compromising on safety.

A key unknown is the strength of the economy from now to the end of the next control period, and what this means for traffic volumes. Currently, in the near-term, the UK and European economies remain weak and airline operators are maintaining a cautious approach to network expansion. A slight improvement is expected for RP2, though the average annual flight growth of c. 2.4% pa is below pre-financial crisis levels. Flight volumes for the UK are now forecast to return to the previous peak level (achieved in 2007) by 2020. This is markedly later than Europe as a whole (2017), reflecting the severity of the impact of the financial crisis and slow recovery in the UK. This uncertainty is challenging for us and for our customers as we seek to agree investment plans and resource requirements for the RP2 period, which takes us to the end of the decade.

Many countries recognise that transport infrastructure and the air transport sector in particular, is an important driver of economic growth. To this end governments are assessing their strategy for aviation capacity to maintain or create transport hubs which provide national competitive advantage.

We have a clear role to play in supporting the development of the UK's infrastructure by contributing to the debate about hub capacity and bringing the industry together to optimise the efficiency of the network. We believe that this latter point will shape our strategy in future.

Martin Rolfe

Managing Director, NERL

Report of the directors

The directors present their report and the audited accounts for the year ended 31 March 2013.

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 the NATS group. 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.

A review of the company's activities and performance during the year, including principal risks and uncertainties, is contained in the Business and Financial Review on pages 2-24.

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.

Results and dividends

The results for the year are shown in the income statement on page 31.

The Board declared and paid an interim dividend of £2.85 per share (totalling £28.5m) in May 2012.

In May 2013 the Board declared an interim dividend for the year ending 31 March 2014 of £4.28 per share (totalling £42.75m) which was paid to its parent company in May 2013.

Charitable donations

The company made aggregate donations of £44,807 (2012: £67,680).

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 corporate performance and business plans. The NATS group CEO and the company's Managing Director maintain visibility with staff through visits to NATS sites where they talk to them about current business issues and take questions in an open and straightforward manner. Also, employees' views are represented through an open dialogue with Prospect and the Public and Commercial Services Union (PCS), the recognised unions on all matters affecting employees. This has been enhanced through the 'Working Together' programme aimed at working towards partnership principles as the basis for our relationship. Formal arrangements for consultation with staff exist through a local and company-wide framework agreed with the Trades Unions.

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

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

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

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

Policy and practice on payment of creditors

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

The average number of days taken to pay suppliers calculated in accordance with the requirements of the Companies Act 2006 is 33 days (2012: 43 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
Richard Deakin
Nigel Fotherby
Martin Rolfe

None of the directors had any interests in the share capital of the company. The interests of the directors in the ordinary shares of the company's ultimate parent undertaking, NATS Holdings are as follows:

Richard Deakin - 800
Nigel Fotherby – 2,777
Martin Rolfe – nil

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 financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union. Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period. In preparing these financial statements, International Accounting Standard 1 requires that directors:

- 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 IFRSs are 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
- make an assessment of the company's ability to continue as a going concern.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

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

The directors are responsible for the maintenance and integrity of the corporate and financial information included on the company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

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

Auditor

Deloitte LLP have expressed their willingness to continue in office as auditor and a resolution to re-appoint Deloitte will be proposed at the Annual General Meeting.

By order of the Board

Richard Churchill-Coleman
Secretary
27 June 2013

Registered office

4000 Parkway, Whiteley, Fareham,
Hampshire, PO15 7FL

Registered in England and Wales
Company Number: 04129273

Independent auditor's 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 2013 which comprise the income statement, the statement of comprehensive income, the balance sheet, the statement of changes in equity, the cash flow statement and the related notes 1 to 28. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

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

Respective responsibilities of directors and auditors

As explained more fully in the directors' responsibilities statement, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on the financial statements

In our opinion the financial statements:

- give a true and fair view of the state of the company's affairs as at 31 March 2013 and of its profit for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Separate opinion in relation to IFRSs as issued by the IASB

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

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

Opinion on other matters prescribed by the Companies Act 2006

In our opinion the information given in the Report of the directors' for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept; or
- the financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

John Clennett, Senior Statutory Auditor
For and on behalf of Deloitte LLP
Chartered Accountants and Statutory Auditor
Southampton, United Kingdom
27 June 2013

Income statement
for the year ended 31 March

	Notes	2013 £m	2012 £m
Revenue	4	713.6	695.6
Staff costs	7	(279.5)	(275.9)
Services and materials		(46.8)	(47.8)
Repairs and maintenance		(28.7)	(26.8)
External research and development		(0.1)	(0.2)
Depreciation, amortisation and impairment	6b	(101.9)	(92.9)
Loss on disposal of non-current assets		-	(1.0)
Other operating charges		(51.6)	(51.5)
Other operating income		-	0.6
Deferred grants released	6b	0.4	0.6
Net operating costs		(508.2)	(494.9)
Operating profit	6	205.4	200.7
Investment revenue	8	4.2	4.8
Finance costs	9	(58.2)	(50.7)
Profit before tax		151.4	154.8
Tax	10	(33.0)	(27.3)
Profit for the year attributable to equity shareholders		118.4	127.5

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

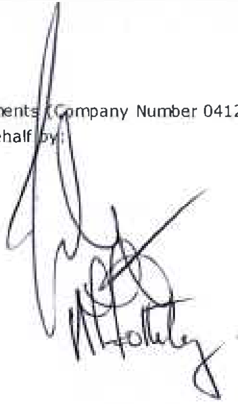
Statement of comprehensive income
for the year ended 31 March

	Notes	2013 £m	2012 £m
Profit for the year after tax		118.4	127.5
Other comprehensive income/(expense) for the year			
Actuarial gain/(loss) on defined benefit pension scheme	25	2.1	(109.4)
Change in fair value of hedging derivatives		1.2	3.7
Transfer to income statement on cash flow hedges		(0.2)	(3.4)
Deferred tax relating to components of other comprehensive income/(expense)	21	(0.6)	27.8
		2.5	(81.3)
Total comprehensive income for the year attributable to equity shareholders		120.9	46.2

Balance sheet
at 31 March

	Notes	2013 £m	2012 £m
Non-current assets			
Goodwill	12	351.0	351.0
Other intangible assets	13	283.4	258.3
Property, plant and equipment	14	615.6	615.8
Retirement benefit asset	25	10.8	-
Trade and other receivables	15	58.6	47.3
		1,319.4	1,272.4
Current assets			
Trade and other receivables	15	142.3	126.5
Short term investments	18	30.1	30.5
Cash and cash equivalents	18	72.1	71.7
Derivative financial instruments	17	1.6	0.2
		246.1	228.9
Total assets		1,565.5	1,501.3
Current liabilities			
Trade and other payables	19	(96.5)	(95.5)
Current tax liabilities		(14.9)	(10.4)
Borrowings	16	(27.2)	(176.7)
Provisions	20	(0.8)	(1.6)
Derivative financial instruments	17	(0.6)	(0.4)
		(140.0)	(284.6)
Net current assets/(liabilities)		106.1	(55.7)
Non-current liabilities			
Trade and other payables	19	(15.9)	(12.2)
Borrowings	16	(680.5)	(573.1)
Retirement benefit obligations	25	-	(28.8)
Deferred tax liability	21	(103.5)	(95.5)
Provisions	20	(5.9)	(0.3)
Derivative financial instruments	17	(146.6)	(126.1)
		(952.4)	(836.0)
Total liabilities		(1,092.4)	(1,120.6)
Net assets		473.1	380.7
Equity			
Called up share capital	22	10.0	10.0
Hedge reserve		0.6	(0.2)
Special reserves		33.7	33.7
Other reserves		17.1	18.2
Retained earnings		411.7	319.0
Total equity		473.1	380.7

The financial statements (Company Number 04129273) were approved by the Board of directors and authorised for issue on 27 June 2013 and signed on its behalf by:



Chairman John Devaney

Finance Director Nigel Fotherby

Statement of changes in equity

for the year ended 31 March

	Equity attributable to equity holders of the Company					
	Share capital £m	Special reserve £m	Hedge reserve £m	Other reserves £m	Retained earnings £m	Total £m
At 1 April 2011	10.0	33.7	(0.5)	20.1	316.2	379.5
Profit for the year	-	-	-	-	127.5	127.5
Other comprehensive income/(expense) for the year net of tax	-	-	0.3	(1.9)	(79.7)	(81.3)
Total comprehensive income/(expense)for the year	-	-	0.3	(1.9)	47.8	46.2
Dividends paid	-	-	-	-	(45.0)	(45.0)
At 31 March 2012	10.0	33.7	(0.2)	18.2	319.0	380.7
At 1 April 2012	10.0	33.7	(0.2)	18.2	319.0	380.7
Profit for the year	-	-	-	-	118.4	118.4
Other comprehensive income/(expense) for the year net of tax	-	-	0.8	(1.1)	2.8	2.5
Total comprehensive income/(expense) for the year	-	-	0.8	(1.1)	121.2	120.9
Dividends paid	-	-	-	-	(28.5)	(28.5)
At 31 March 2013	10.0	33.7	0.6	17.1	411.7	473.1

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

Cash flow statement
for the year ended 31 March

	Notes	2013 £m	2012 £m
Net cash inflow from operating activities	23	232.8	203.7
Cash flows from investing activities			
Interest received		0.7	0.9
Purchase of property, plant and equipment and other intangible assets		(127.6)	(120.9)
Cost of disposing of property, plant and equipment		-	(0.2)
Changes in short term investments		0.4	(14.1)
Net cash outflow from investing activities		(126.5)	(134.3)
Cash flows from financing activities			
Interest paid		(35.1)	(35.3)
Interest received on derivative financial instruments		1.3	1.6
Bank facility arrangement fees		(2.9)	-
Bank and other loans		(12.3)	28.8
Loans advanced by fellow subsidiary		-	(0.9)
Repayment of bond principal		(28.4)	(14.2)
Dividends paid		(28.5)	(45.0)
Net cash outflow from financing activities		(105.9)	(65.0)
Increase in cash and cash equivalents during the year		0.4	4.4
Cash and cash equivalents at 1 April		71.7	67.3
Cash and cash equivalents at 31 March		72.1	71.7
Net debt (representing borrowings net of cash and short term investments)		(605.5)	(647.6)

1. General information

NATS (En Route) plc (NERL) is a company incorporated in England and Wales and domiciled in the United Kingdom and acting under the Companies Act 2006. The address of the registered office is on page 28. The nature of the company's operations and its principal activities are set out in the Report of the Directors and in the business and financial review.

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

2. Accounting policies

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

Basis of preparation and accounting
The financial statements have been prepared on the going concern basis. For further detail please refer to page 23. 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 company financial statements comply with Article 4 of the EU IAS Regulation.

The following new and revised Standards and Interpretations have been adopted in the current year. Their adoption has not had any significant impact on the amounts reported in these financial statements.

Amendments to IFRS 7: *Financial Instruments: Disclosures*

The company has applied the amendments to IFRS 7 in the current year. The amendments increase the disclosure requirements for transactions involving the transfer of financial assets in order to provide greater transparency around risk exposures when financial assets are transferred but the transferor retains some level of continuing exposure to the asset.

There are no additional disclosures required as a result of applying this amendment.

The company has applied the amendments to IFRS 7 (amended) titled *Disclosures - Offsetting Financial Assets and Financial Liabilities*. The amendments to this standard require an entity to disclose additional information about the rights to offset financial asset and financial liability balances and any related arrangements for financial instruments.

The impact of the application of this amendment to this standard has resulted in no material disclosures in the financial statements.

Amendments to IAS 12: *Income Taxes*
The company has applied the amendments to IAS 12 (December 2010) titled *Deferred Tax: Recovery of Underlying Assets*. The amendments provide a practical approach for measuring deferred tax liabilities and deferred tax assets when investment property is measured using the fair value model in IAS 40: *Investment Property*. The amendments introduce a presumption that an investment property is recovered entirely through sale. This presumption is rebutted if the investment property is held within a business model whose objective is to consume substantially all of the economic benefits embodied in the investment property over time, rather than sale.

The company does not hold any investment property and as such this has not impacted the amounts reported in the financial statements in relation to deferred tax assets and liabilities.

Amendments to IAS 32: *Financial Instruments: Presentation* - the group has applied the amendments to IAS 32 (amended) titled *Offsetting Financial Assets and Financial Liabilities*. The amendments to IAS 32 clarifies that the legally

enforceable right to offset financial assets and financial liabilities must exist today and cannot be contingent on the occurrence of future events. There is also clarification as to the definition in IAS 32 of simultaneous realisation and settlement of financial assets and financial liabilities, essentially a settlement process would meet the requirements for offsetting if the financial asset and financial liability are to be settled simultaneously or net.

The impact of the application of these amendments to this standard has resulted in no material disclosures in the financial statements.

At the date of authorisation of these financial statements, the following Standards and Interpretations which have not been applied in these financial statements were in issue but not yet effective (and in some cases had not yet been adopted by the EU):

IFRS 1 (amended): *Government Loans*
Annual Improvements to IFRSs (2009 - 2011) Cycle
IFRS 9: *Financial Instruments*
IFRS 10: *Consolidated Financial Statements*
IFRS 10, IFRS 12 and IAS 27 (amended): Investment Entities
IFRS 11: *Joint Arrangements*
IFRS 12: *Disclosure of Interests in Other Entities*
IFRS 13: *Fair Value Measurement*
IAS 27 (revised): *Separate Financial Statements*
IAS 28 (revised): *Investments in Associates and Joint Ventures*
IFRIC 20: *Stripping Costs in the Production Phase of a Surface Mine*

The directors do not expect that the adoption of the Standards listed above will have a material impact on the financial statements of the company in future periods, except as follows:

IFRS 9: *Financial Instruments* - will impact the measurement and disclosures of financial instruments.

IFRS 12: *Disclosure of Interests in Other Entities* - will impact the disclosure of interests that the company has in other entities.

IFRS 13: *Fair Value Measurement* - will impact the fair value of certain assets and liabilities as well as the associated disclosures.

IAS 19: *Employee Benefits (2011)* - will impact the measurement of the various components representing movements in the defined benefit pension obligation and associated disclosures, but not the group's total obligation. It is likely that following the replacement of expected returns on plan assets with a net finance cost in the income statement, the profit for the period will be reduced and accordingly other comprehensive income increased.

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

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.

NERL also entered into an Inter-company Services Agreement on 25 July 2001 with NATS (Services) Limited (NATS Services). Under this agreement

this company provides NATS Services with the following services:

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

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

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

The company commenced trading from 26 July 2001.

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

Operating profit

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

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 NERL air traffic services licence (including volume risk sharing, service performance incentives and inflation adjustments) and other contracts. Amounts receivable include revenue allowed under the charge control conditions of the air traffic services licence and EC charging regulation.
- 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.

Operating segments

Operating segments are reported in a manner consistent with the internal reporting provided to the company's Executive team, who is considered to be the chief operating decision maker. An operating segment represents a service line that provides a core set of products or services to customers. Operating segments' operating results are reviewed regularly by the Executive team to make decisions about resources to be allocated to the segment and to assess its performance, and for which discrete financial information is available.

Inter-segment transfers or transactions are entered into under the normal commercial terms and conditions that would also be available to unrelated third parties.

Segment performance is assessed by service line revenue and contribution, where contribution represents revenue less costs directly attributed to individual service lines. Segment results that are reported to the Executive team include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Costs that are not attributed to service lines include the cost of central support functions, depreciation and amortisation (net of government grants), pensions accrual rate variances to budget, employee share

scheme costs, redundancy and relocation costs and any profit/(loss) on disposal of non-current assets.

Goodwill

Goodwill arising on consolidation in relation to NERL, 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 net realisable value and the value in use. In assessing value in use the estimated future cash flows are discounted to their present value using the pre-tax nominal regulated rate of return.

Leases

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

The company does not have any finance leases.

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

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

Property, plant and equipment

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

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

Freehold land and assets in the course of construction and installation are not depreciated. The gain or loss arising on the disposal or retirement of an asset is determined as the difference between the sale proceeds and the carrying amount of the asset and is recognised in income.

Borrowing costs

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

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

When funds are borrowed specifically for the purpose of acquiring or constructing a qualifying asset, the amount of borrowing costs eligible for capitalisation is the actual cost of borrowing incurred in the period. IAS 23 requires that where a qualifying asset is funded from a pool of general borrowings, the amount of borrowing costs eligible for capitalisation should be determined by applying

an appropriate capitalisation rate (based on the weighted average of borrowing costs applicable to the general outstanding borrowings during the period) to the expenditure during the period, to determine the borrowing costs eligible for capitalisation.

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

Deferred grants and other contributions to property, plant and equipment

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

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

Internally-generated intangible assets – research and development expenditure

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

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

- an asset is created that can be identified
- it is probable that the asset created will generate future economic benefits; and
- the development cost of the asset can be measured reliably.

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

Impairment of tangible and intangible assets, excluding goodwill

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

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

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

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

Emissions allowances

Consistent with the withdrawal of IFRIC 3, emissions allowances previously recognised at valuation are now recognised at cost. Emission allowances granted free of charge are recognised at nil 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 payment
The company has applied the requirements of IFRS 2: *Share-Based Payment*.

In 2001, the company's parent established an All-Employee Share Ownership Plan for the benefit of its employees to hold 5% of the share capital of NATS Holdings.

Shares awarded by the Plan are treated as cash-settled liabilities. A liability is recognised for shares awarded over the period from award to when the employee becomes unconditionally entitled to the shares and are measured initially at their fair value. At each balance sheet date until the liability is settled, as well as at the date of settlement, the fair value of the liability is re-measured based on independent share valuations with any changes in fair value recognised in profit or loss for the year.

In respect of the award schemes, the company provides finance to NESL (NATS Employee Sharetrust Limited) 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 is 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 substantively enacted by the balance sheet date.

Under the Finance Bill 2012 which was enacted on the 17 July 2012, the corporation tax rate was reduced to 23% with effect from 1 April 2013. It is the Government's intention that legislation will be introduced in the Finance Bill 2013 to reduce the main rate of corporation tax to 21% for the financial year commencing 1 April 2015. The future main tax rate reductions are expected to have a similar impact on the company's financial statements as outlined above, subject to the impact of other developments in the company's tax position which may reduce the beneficial effect of this in the company's tax rate. As the further reductions in UK corporate tax rates have not been substantively enacted at the balance sheet date, this is considered a non-adjusting event in accordance with IAS 10 and no adjustments have been made. The impact of any further reduction will be taken into account at subsequent reporting dates, once the change has been substantively enacted.

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

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

period when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted by the balance sheet date. Deferred tax in the income statement is charged or credited, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

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

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

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

Retirement benefit costs
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 comprehensive income.

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.

Since 2009, the NATS group and Trustees have introduced a number of pension reforms, as explained in note 25. These include: closing the defined benefit scheme to new entrants and establishing a defined contribution scheme for new employees from 1 April 2009, limiting the rate of increase in pensionable pay and changing the indexation reference rate for future service.

Contributions to the defined contribution pension scheme are expensed as incurred.

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

3. Critical judgements and key sources of estimation uncertainty

Impairment of goodwill, intangible and tangible assets
In carrying out impairment reviews of goodwill, intangible and tangible assets, (including assets in the course of construction), a number of significant assumptions have to be made when preparing cash flow projections and assessing net realisable values. These include air traffic growth, service performance, future cash flows, the value of the regulated asset base, market premiums for regulated businesses and the outcome of the

regulatory price control determinations. If the actual outcome should differ or changes in expectations arise, impairment charges may be required which would materially impact on operating results. A reduction in net realisable value of 1% (2012: value in use 3%) or a reduction in market premium by 2% (2012: 5%) would result in the recoverable amount being equal to the carrying amount of goodwill. Refer to notes 12, 13 and 14.

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

A number of key assumptions have been made in calculating the fair value of the company's defined benefit pension scheme which affect the balance sheet position and the company's reserves and income statement. Refer to note 25 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.

Recoverability of revenue allowances
The economic regulatory price control for UK en route services for Control Period 3 (2011 to 2014) established an annual revenue allowance that is recovered through a price based on the economic regulator's forecasts of traffic volumes and inflation made at the start of the price control period. Where traffic volumes or inflation differ from the regulator's forecasts, revenue actually recovered may be higher or lower than the revenue allowance. Where this is the case, the EU Charging Regulation allows an adjustment to be made to the price in subsequent years (from 2014 onwards, starting 2 years later) to reflect any over- or under-recovery. Also, following the CP3 price control review, the economic regulator deferred the recovery of adjustments for traffic volume risk sharing and service performance incentives arising in the previous control period (CP2: 2006 to 2010) and allowed these to be recovered through an adjustment to prices in the last three years of CP3. The weakness of the economy in the early part of CP3 has resulted in traffic volumes which are lower than the regulator assumed for CP3. Inflation has also been higher than assumed. When combined with the remaining balances deferred from CP2 of £39.3m and service performance incentives from CP3 of £8.2m, recoverable revenue allowances totalled £100.0m at 31 March 2013. The legal right to recover the revenue adjustments discussed above is provided by the EC Charging Regulation and NERL's air traffic services licence. The company expects to recover these amounts through adjustments to prices starting in 2014 and through into Reference Period 2 (RP2: 2015 to 2019).

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

4. Revenue

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

	2013 £m	2012 £m
NATS Airspace	710.8	692.1
Other NATS Service lines	2.8	3.5
	713.6	695.6
Other operating income	-	0.6
Investment revenue (see note 8)	4.2	4.8
	717.8	701.0

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

A portion of the company's revenue from the provision of services 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 a £0.2m gain (2012: £3.4m gain).

5. Business and geographical segments

Operating segments

The NATS Executive team is considered to be the chief operating decision maker as defined by IFRS 8. The segmental analysis is based on the information that the Executive team uses internally for the purposes of evaluating the performance of operating segments and determining resource allocation between segments. The business is organised into service lines, each service line provides a core set of products or services to our customers. Each service line is considered to be an operating segment as defined by IFRS 8. The performance of operating segments is assessed based on service line revenue and contribution.

Service line contribution represents the revenue and costs which are directly attributed to a service line. Costs which are not directly attributed to a service line include: costs managed outside of service lines, depreciation and amortisation (net of government grants), pension accrual rate variances to budget, employee share scheme costs, redundancy and relocation costs and any profit/(loss) on disposal of non-current assets. A reconciliation of service line contribution to operating profit is set out below.

For management reporting purposes, the company is organised into service lines: NATS Airspace and Other NATS Service lines. Other NATS Service lines include NATS Defence and NATS Information which are aggregated and reported to the chief operating decision maker as a single service line as they have similar economic characteristics and exhibit similar financial performance, the nature of the products and the services provided is in the support of air traffic solutions and services.

Principal activities

The following table describes the activities of each reporting segment:

NATS Airspace	This includes all of the company's economically regulated activities and encompasses en route, oceanic and terminal services provided from our Prestwick and Swanwick centres, together with all the supporting communications, navigation and surveillance infrastructure and facilities. This includes air traffic services for helicopters operating in the North Sea, approach services for London airports and the services to the Ministry of Defence.
Other NATS Service lines	Includes NATS Defence, providing a range of other defence services in the UK and internationally and NATS Information, providing data to enable future efficiency and flight optimisation.

The service line management reporting structure was introduced from 1 April 2012. As a result the comparatives for the year ended 31 March 2012 have been presented on a consistent basis.

Segment information about these activities is presented below.

Revenue

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

	2013 External revenue £m	2013 Inter-company revenue £m	2013 Revenue £m	2012 External revenue £m	2012 Inter-company revenue £m	2012 Revenue £m
NATS Airspace	692.4	18.4	710.8	676.5	15.6	692.1
Other NATS Service lines	2.8	-	2.8	3.5	-	3.5
	695.2	18.4	713.6	680.0	15.6	695.6

Inter-company revenue includes revenue for services to NATS (Services) Limited of £17.5m (2012: £14.7m) and to NATSNav Limited of £0.9m (2012: £0.9m).

5. Business and geographical segments (continued)

Operating profit

Service line contribution represents the revenue and costs which are directly attributed to a service line.

A reconciliation of service line contribution to operating profit is provided below:

	2013 £m	2012 £m
NATS Airspace	367.9	345.7
Other NATS Service lines	2.2	2.1
Service line contribution	370.1	347.8
Costs not directly attributed to service lines:		
Depreciation and amortisation (net of deferred grants released)	(101.5)	(92.3)
Profit/(loss) on disposal of non-current assets	-	(1.0)
Pension accrual rate variance to budget	(12.1)	1.1
Employee share scheme costs	(0.9)	(2.4)
Redundancy and relocation costs	(1.2)	(1.7)
Other costs not directly attributed to service lines	(49.0)	(50.8)
	205.4	200.7

Supplementary information

EC Regulations require air navigation service providers to present income and costs, prepared under international accounting standards, for each of their air navigation services. The following disclosure is provided in this respect:

	2013			2012		
	UK air traffic services	North Atlantic air traffic services	Total	UK air traffic services	North Atlantic air traffic services	Total
	£m	£m	£m	£m	£m	£m
Revenue	687.2	26.4	713.6	668.8	26.8	695.6
Operating costs	(487.3)	(20.9)	(508.2)	(474.8)	(20.1)	(494.9)
Operating profit	199.9	5.5	205.4	194.0	6.7	200.7

UK air traffic services provide en route air traffic services within UK air space, air traffic services for helicopters operating in the North Sea, approach services for London airports, services to the Ministry of Defence and miscellaneous activity connected to the en route business.

North Atlantic air traffic services provide en route air traffic services for the North Atlantic, including an altitude calibration service.

Geographical segments

The following table provides an analysis of the company's revenue by geographical area, based on the geographical location of its customers, and of the company's non-current assets (excluding goodwill, financial assets and the retirement benefit asset) by geographical location:

	Revenue		Non-current assets	
	2013 £m	2012 £m	2013 £m	2012 £m
UK	310.8	302.2	897.4	872.3
Rest of Europe	241.5	231.9	0.6	0.4
North America	115.6	117.0	1.0	1.4
Other	45.7	44.5	-	-
Total	713.6	695.6	899.0	874.1

Information about major customers

Included in revenues arising from NATS Airspace are revenues of £76.2m (2012: £69.1m) which arose from the company's largest customer.

6. Operating profit for the year

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

a Restructuring costs

Redundancy and relocation costs
In response to the economic downturn and changes in technology, voluntary redundancy was offered to staff in some areas of the business. Relocation costs were incurred in previous years following the closure of air traffic control centres, the training college at Hurn and the redeployment of staff to other sites. To the extent that staff could not be redeployed, termination terms were agreed.

	2013 £m	2012 £m
Voluntary redundancy costs (including pension augmentation costs, see note 7a)	1.3	3.1
Relocation of staff and offices to Swanwick area	-	0.2
Relocation of staff to the Prestwick area	-	(1.3)
Relocation of staff from Hurn to the Corporate & Technical Centre	(0.1)	(0.3)
	1.2	1.7

b Other items

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

	2013 £m	2012 £m
CAA regulatory charges	5.3	5.2
Depreciation of property, plant and equipment	76.2	71.6
Impairment of property, plant and equipment	0.4	1.6
Amortisation of intangible assets	24.6	17.9
Impairment of intangible assets	0.7	1.8
Deferred grants released	(0.4)	(0.6)
Research and development costs	9.2	6.9
Auditors remuneration for audit services (see below)	-	-

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

Research and development costs represent internal labour costs in support of research and development activities.

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

	2013 £m	2012 £m
Net charges for services provided by parent undertaking	12.1	11.1
Charges for services provided by other group companies	17.9	17.2

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

7. Staff costs

a. Staff costs

	2013 £m	2012 £m
Salaries and staff costs were as follows:		
Wages and salaries	221.0	220.1
Social security costs	23.6	23.1
Pension costs (note 7b)	72.4	66.4
	317.0	309.6
Less: amounts capitalised	(37.5)	(33.7)
	279.5	275.9

Wages and salaries includes redundancy costs of £nil (2012: £0.9m), share-based payment charges, other allowances and holiday pay. Pension costs include £1.3m (2012: £2.2m) for redundancy-related augmentation payments which staff elected to receive in lieu of severance payments.

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.

7. Staff costs (continued)

b. Pension costs

	2013 £m	2012 £m
Defined benefit pension scheme costs (note 25)	69.4	64.6
Defined contribution pension scheme costs	3.0	1.8
	72.4	66.4

The company operates a salary sacrifice arrangement for staff pension contributions. Wages and salaries and pension costs reflect this arrangement.

c. Staff numbers

The monthly average number of employees (including executive directors) was:

	2013 No.	2012 No.
Air traffic controllers	1,309	1,349
Air traffic service assistants	574	606
Engineers	835	816
Others	686	669
	3,404	3,440

8. Investment revenue

	2013 £m	2012 £m
Interest on bank deposits	0.5	0.7
Other loans and receivables	3.7	4.1
	4.2	4.8

Other investment revenue mainly includes the effect of unwinding the discount on amounts receivable after more than 1 year.

9. Finance costs

	2013 £m	2012 £m
Interest on bank overdrafts, loans and hedging instruments	1.8	1.0
Bond and related costs including financing expenses	31.6	32.1
Other finance costs	3.9	0.4
Interest payable on intercompany loans	0.4	0.3
	37.7	33.8
Loss on derivatives not qualifying for hedge accounting	20.5	16.9
	58.2	50.7

Other finance costs mainly includes the effect of unwinding the discount on provisions falling due after more than 1 year.

10. Tax

	2013 £m	2012 £m
Current tax (including a charge of £1.9m in respect of prior years, 2012: credit of £3.3m)	25.6	21.4
Deferred tax (see note 21)	7.4	5.9
	33.0	27.3

Corporation tax is calculated at 24% (2012: 26%) 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:

	2013 £m	2013 %	2012 £m	2012 %
Profit on ordinary activities before tax	151.4		154.8	
Tax on profit on ordinary activities at standard rate in the UK of 24% (2012: 26%)	36.3	24.0%	40.2	26.0%
Tax effect of change in corporation tax rate from 24% to 23% (2012: 26% to 24%)	(4.5)	(3.0%)	(8.0)	(5.2%)
Tax effect of prior year adjustments	1.9	1.3%	(3.3)	(2.2%)
Tax effect of research and development expenditure increased deductions	(1.3)	(0.9%)	(1.8)	(1.1%)
Tax effect of other permanent differences	0.6	0.4%	0.2	0.1%
Tax charge for year at an effective tax rate of 21.8% (2012: 17.6%)	33.0	21.8%	27.3	17.6%
Deferred tax (charge)/credit taken directly to equity (see note 21)	(0.6)		27.8	

11. Dividends

	2013 £m	2012 £m
Amounts recognised as distributions to equity holders in the year		
First interim dividend of £2.85 per share (2012: £3.72 per share)	28.5	37.2
Second interim dividend of £nil per share (2012: £0.78 per share)	-	7.8
	28.5	45.0

In May 2013, the Board declared an interim dividend for 2014 of £4.28 per share (totalling £42.75m), which was paid to the company's parent in May 2013.

12. Goodwill

	£m
At 31 March 2013 and 31 March 2012	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 UK air traffic services and North Atlantic air traffic services, representing the cash generating units, including market premiums for regulated businesses (assumed at 10%, 2012: 10%). The key assumptions for value in use calculations are the discount rate, future cash flows to the end of the current regulatory control period (31 December 2014 for UK air traffic services and 31 March 2015 for North Atlantic air traffic services) as assumed in the company's business plans, and a terminal value at that date, reflecting the regulatory asset bases of £1,214.7m (2012: £1,201.7m) and a market premium which is assessed annually by reference to recent market transactions within the utility sectors. The company's business plans reflect the outcome of the latest price control review which included forecasts of traffic volumes reflecting the current economic environment. The discount rate is a pre-tax nominal rate of 9.74% (2012: 9.99%). See note 3.

13. Other intangible assets

	Operational software £m	Non-operational software £m	Airspace and resectorisation £m	Assets in course of construction £m	Total £m
Cost					
At 1 April 2011	54.7	33.1	18.8	191.3	297.9
Additions internally generated	4.2	0.3	1.0	10.4	15.9
Additions externally acquired	2.4	6.5	0.1	27.1	36.1
Disposals during the year	-	(1.2)	-	(2.7)	(3.9)
Transfers during the year	77.2	2.1	1.1	(83.3)	(2.9)
At 1 April 2012	138.5	40.8	21.0	142.8	343.1
Additions internally generated	3.4	-	0.3	11.5	15.2
Additions externally acquired	2.0	1.9	0.1	29.1	33.1
Disposals during the year	-	(0.3)	(0.9)	(0.1)	(1.3)
Transfers during the year	21.4	3.2	0.7	(23.2)	2.1
At 31 March 2013	165.3	45.6	21.2	160.1	392.2
Accumulated amortisation					
At 1 April 2011	25.5	16.5	9.7	17.1	68.8
Charge for the year	11.4	4.9	1.6	-	17.9
Impairment provision recognised in income statement	-	-	-	1.8	1.8
Utilisation of impairment provision	-	-	-	(2.7)	(2.7)
Disposals during the year	-	(1.0)	-	-	(1.0)
At 1 April 2012	36.9	20.4	11.3	16.2	84.8
Charge for the year	17.5	5.4	1.7	-	24.6
Impairment provision recognised in income statement	-	0.3	-	0.4	0.7
Utilisation of impairment provision	-	(0.3)	-	(0.1)	(0.4)
Disposals during the year	-	-	(0.9)	-	(0.9)
At 31 March 2013	54.4	25.8	12.1	16.5	108.8
Carrying amount					
At 31 March 2013	110.9	19.8	9.1	143.6	283.4
At 31 March 2012	101.6	20.4	9.7	126.6	258.3

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

14. Property, plant and equipment

	Freehold land & buildings £m	Improvements to leasehold land & buildings £m	Air traffic control systems, plant and equipment £m	Vehicles, furniture & fittings £m	Assets in course of construction and installation £m	Total £m
Cost						
At 1 April 2011	224.0	38.2	1,094.4	15.5	161.4	1,533.5
Additions during the year	2.2	0.3	27.7	0.7	44.4	75.3
Disposals during the year	(0.4)	-	(117.7)	(1.5)	(3.0)	(122.6)
Other transfers during the year	4.6	1.0	119.2	2.0	(123.9)	2.9
At 1 April 2012	230.4	39.5	1,123.6	16.7	78.9	1,489.1
Additions during the year	3.6	2.7	25.4	0.4	46.4	78.5
Disposals during the year	(2.6)	-	(10.7)	(1.5)	-	(14.8)
Other transfers during the year	7.1	0.6	43.1	0.1	(53.0)	(2.1)
At 31 March 2013	238.5	42.8	1,181.4	15.7	72.3	1,550.7
Accumulated depreciation and impairment						
At 1 April 2011	90.9	24.5	794.0	9.7	3.0	922.1
Provided during the year	6.9	1.5	62.0	1.2	-	71.6
Provisions for impairment	-	-	1.5	-	0.1	1.6
Utilisation of impairment provision	-	-	(1.5)	-	(3.1)	(4.6)
Disposals during the year	(0.3)	-	(115.6)	(1.5)	-	(117.4)
At 1 April 2012	97.5	26.0	740.4	9.4	-	873.3
Provided during the year	7.3	1.5	65.9	1.5	-	76.2
Provisions for impairment	-	-	0.1	-	0.3	0.4
Utilisation of impairment provision	-	-	(0.1)	-	-	(0.1)
Disposals during the year	(2.6)	-	(10.6)	(1.5)	-	(14.7)
At 31 March 2013	102.2	27.5	795.7	9.4	0.3	935.1
Carrying amount						
At 31 March 2013	136.3	15.3	385.7	6.3	72.0	615.6
At 31 March 2012	132.9	13.5	383.2	7.3	78.9	615.8

The company conducts annual reviews of the carrying values of its property, plant, equipment and intangible assets. During the year, net impairment charges of £1.1m (2012: £3.4m) were made in respect of operational assets and assets in the course of construction reflecting a reassessment of certain projects and assets and the likelihood of benefits being realised in full.

During the year the company capitalised £1.5m (2012: £1.0m) of general borrowing costs at a capitalisation rate of 2.1% (2012: 1.3%), in accordance with IAS 23: *Borrowing costs*.

15. Financial and other assets

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

Trade and other receivables

	2013 £m	2012 £m
Non-current		
Prepayments	0.1	0.2
Accrued income	58.5	47.1
	58.6	47.3
Current		
Receivable from customers (gross)	51.7	50.8
Allowance for doubtful debts	(4.8)	(4.3)
	46.9	46.5
Other debtors	2.3	2.3
Prepayments	4.9	5.3
Amounts due from other group undertakings	0.5	-
Accrued income	87.7	72.4
	142.3	126.5

The average credit period taken on sales of services is 33 days (2012: 33 days). Interest is charged by Eurocontrol to UK en route customers at 11.57% (2012: 11.00%) 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 £4.8m (2012: £4.3m). Full provision is made for receivables from UK en route customers that are overdue. Debts that are neither impaired nor overdue are assessed for credit quality and reviewed periodically. Receivables in respect of other customers are provided for where there is an identified loss event, such as administration, receivership or liquidation which is evidence of a reduction in the recoverability of the cash flows.

15. Financial and other assets (continued)

Accrued income which is non-current represents revenues earned in the previous control period (CP2) and regulatory adjustments for the period January to March 2013 which will be recovered through 2015 charges. Accrued income which is current includes unbilled revenues for services provided in March 2013 and regulatory adjustments to revenue for service performance, traffic volume risk sharing and inflation to reflect differences between actual outcomes and the CAA's CP3 assumptions (see note 3).

Ageing of past due but not impaired trade receivables

	2013 £m	2012 £m
30-90 days	0.1	0.1
91 -365 days	-	0.1
More than 365 days overdue	0.1	-
	0.2	0.2

Movement in the allowance for doubtful debts

	2013 £m	2012 £m
Balance at the beginning of the year	4.3	5.2
Increase in allowance recognised in the income statement	1.0	0.6
Exchange movement in the year	-	(0.3)
Amounts written off as irrecoverable	(0.5)	(1.2)
Balance at end of year	4.8	4.3

In determining the recoverability of a trade receivable the company considers any change in credit quality of the trade receivable from the date credit was initially granted up to the reporting date. Credit risk is mitigated in part by regulatory price control conditions that include within UK en route annual revenue allowances £1m to cover bad debts. 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 £3.4m (2012: £3.7m) which are in administration, receivership or liquidation. The impairment recognised represents the carrying amount of these trade receivables. The company does not hold any collateral over these balances.

Ageing of impaired receivables

	2013 £m	2012 £m
30-90 days	0.5	0.1
90-365 days	0.9	1.4
More than 365 days overdue	3.4	2.8
	4.8	4.3

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

Cash and cash equivalents

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

Overall, the maximum credit risk for the items discussed above would be £298.1m (2012: £270.5m).

16. Borrowings

	2013 £m	2012 £m
Unsecured loans		
Intercompany loan	22.5	22.5
Secured loans		
£600m 5.25% Guaranteed Secured Amortising Bonds due 2026	555.7	583.9
Bank loans (revolving term loan and revolving credit facility expiring 2016)	136.0	-
Bank loans (revolving term loan and revolving credit facility expiring 2012-2013)	-	148.3
Gross borrowings	714.2	754.7
Unamortised bond issue costs	(4.2)	(4.9)
Unamortised bank loan issue costs	(2.3)	-
	707.7	749.8
Amounts due for settlement within 12 months	27.2	176.7
Amounts due for settlement after 12 months	680.5	573.1

The £600m 5.25% Guaranteed Secured Amortising Bond is secured by way of a debenture by which NERL grants its lenders a first legal mortgage over certain properties in England and Wales, a first fixed charge over all other real estate, plant and equipment and a floating charge over all other assets. Drawings of £136.0m made by NERL under its £275.0m committed bank facilities are similarly secured. Further security provisions are also provided by NATS Holdings Limited and NATS Limited. The carrying amount of the collateral provided as security for the £600m bond and bank borrowings is circa £1,419m (2012: £1,381m), including the carrying amount of balance sheet goodwill of £351.0m.

The average effective interest rate on the bank loans in the year was 1.8% (2012: 1.4%) and was determined based on LIBOR rates plus a margin and utilisation fee.

Costs associated with the issue of the £600m bond are being amortised over the life of the bond. Costs associated with the issue of the £275.0m bank facilities are also being amortised over the term of the facility.

16. Borrowings (continued)

Undrawn committed facilities

	2013 £m	2012 £m
Less than one year	-	22.7
Between one and two years	-	40.0
Expiring in more than two years	139.0	-
	139.0	62.7

NERL has, as at 31 March 2013, outstanding drawings of £136.0m on its committed bank facilities. These facilities expire on 21 December 2016.

17. Derivative financial instruments

Fair value of derivative financial instruments

	2013 £m	2012 £m
Current assets		
Derivative financial instruments in designated hedge accounting relationships		
Forward foreign exchange contracts (cash flow hedges)	1.6	0.2
Current liabilities		
Derivative financial instruments in designated hedge accounting relationships		
Forward foreign exchange contracts (cash flow hedges)	(0.6)	(0.4)
Non-current liabilities		
Derivative financial instruments classified as held for trading		
Index-linked swaps	(146.6)	(126.1)

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

The index-link swap has been classified as a non-current liability and the prior year comparative has been adjusted accordingly.

Fair value measurements recognised in the balance sheet

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

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

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

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

	2013				2012			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Financial assets								
Derivative financial instruments in designated hedge accounting relationships	-	1.6	-	1.6	-	0.2	-	0.2
Financial liabilities								
Derivative financial instruments in designated hedge accounting relationships	-	(0.6)	-	(0.6)	-	(0.4)	-	(0.4)
Derivative financial instruments classified as held for trading	-	(146.6)	-	(146.6)	-	(126.1)	-	(126.1)
	-	(147.2)	-	(147.2)	-	(126.5)	-	(126.5)

There were no transfers between individual levels in the year.

18. Financial instruments

Capital risk management

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

External capital requirements

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

As at 31 March 2013, the company had a credit rating of AA- (negative outlook) from Standard & Poor's and A2 (stable outlook) from Moody's (2012: AA- (negative outlook)/ A2 (stable outlook)).

Gearing ratio

Consistent with seeking to maintain an investment grade credit rating, the company sets a gearing target measured as the ratio of net debt to the regulatory asset base (RAB). Following the price control review for the four calendar years 2011 to 2014, the economic regulator (the CAA) has set NERL a gearing target of 60% and a cap of 65% of net debt to RAB with a requirement if this cap is exceeded for NERL to halt distributions and to remedy the position.

Significant accounting policies

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

Categories of financial instrument

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

	2013 £m	2012 £m
Financial assets		
Trade and other receivables, excluding prepayments and accrued income	49.7	48.8
Cash and cash equivalents and short term investments	102.2	102.2
Derivative financial instruments in designated hedge accounting relationships	1.6	0.2
	153.5	151.2
Financial liabilities		
Derivative financial instruments in designated hedge accounting relationships	(0.6)	(0.4)
Derivative financial instruments classified as held for trading	(146.6)	(126.1)
Other financial liabilities at amortised cost	(759.4)	(797.2)
	(906.6)	(923.7)

Other financial liabilities at amortised cost include balances for trade and other payables (excluding accruals and deferred income), the bond, bank borrowings and other loans.

The index-linked swap is categorised as held for trading. The loss on the movement in its market value of £20.5m has been recorded in the income statement in the year (2012: loss of £16.9m).

Financial risk management objectives

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

Market risk

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

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

Foreign currency risk management

The company's principal exposure to foreign currency transaction risk is in relation to UK en route services revenues, accounting for 83% of turnover (2012: 83%). 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 95% of the UK en route income that is forecast to arise by entering into forward foreign exchange contracts on a monthly or 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	
	2013 £m	2012 £m	2013 £m	2012 £m
Euro	90.9	91.1	(11.3)	(3.1)
Canadian Dollars	-	0.3	-	-
Danish Krone	0.1	0.1	-	-
	91.0	91.5	(11.3)	(3.1)

18. Financial instruments (continued)

Foreign currency sensitivity analysis

The company holds foreign currency cash balances of £10.2m (2012: £9.9m), which at 31 March 2013 were in Euro and Danish Krone.

The following table details the sensitivity to a 10% increase or decrease in the value of sterling against relevant foreign currencies. 10% is the sensitivity rate that represents 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	2013 Impact £m	2012 Impact £m
Euro	4.2	1.9
Canadian Dollars	(0.1)	(0.1)
Danish Krone	-	-
	4.1	1.8

The company's sensitivity to the Euro increased during the year reflecting a net reduction in Euro denominated monetary assets and a net increase in forward contracts taken out to hedge future receipts and purchase commitments. NERL believes that this sensitivity analysis accurately reflects its inherent foreign exchange risk as the exposure to foreign exchange risk was broadly constant throughout the reporting period.

Forward foreign exchange contracts

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

2013			Average exchange rate	2012			Average exchange rate
Euro sold	£m	€m		Euro sold	£m	€m	
0-3 months	125.8	147.5	0.8528	0-3 months	117.6	140.8	0.8354
Over 3 months	-	-	-	Over 3 months	-	-	-
	125.8	147.5	0.8528		117.6	140.8	0.8354
Euro bought	€m	£m		Euro bought	€m	£m	
0-3 months	3.4	2.9	0.8500	0-3 months	2.5	2.1	0.8449
Over 3 months	1.2	1.0	0.8293	Over 3 months	9.7	8.4	0.8622
	4.6	3.9	0.8447		12.2	10.5	0.8587
Canadian Dollar bought	C$m	£m		Canadian Dollar bought	C$m	£m	
0-3 months	0.4	0.2	1.5985	0-3 months	0.6	0.4	1.6002
Over 3 months	1.7	1.1	1.6057	Over 3 months	0.2	0.1	1.6330
	2.1	1.3	1.5967		0.8	0.5	1.6093
Danish Krone bought	DKK m	£m		Danish Krone bought	DKK m	£m	
0-3 months	1.3	0.1	9.2176	0-3 months	-	-	-
Over 3 months	0.7	0.1	9.2112	Over 3 months	-	-	-
	2.0	0.2	9.2154		-	-	-

At 31 March 2013, the aggregate amount of the unrealised gains under forward foreign exchange contracts deferred in the hedge reserve relating to the exposure on these future transactions was £0.6m (2012: £0.2m unrealised loss). The bulk of these contracts will mature within the first three months of the next financial year at which stage the amount deferred in equity will be realised in the income statement for hedges relating to revenue expenditure or capitalised and depreciated for those relating to capital expenditure.

In addition to the above, NERL has entered into average rate forward agreements with a contract date after 31 March 2013 to sell Euro anticipated to be received in July 2013 totalling £50.0m in respect of UK en route revenues. These contracts are also designated as cash flow hedges. They are not included in the table above.

Interest rate risk management

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

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

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

Exposure to interest rates on financial assets and financial liabilities are detailed below. The company held no interest rate swaps at 31 March 2013 (2012: none).

18. Financial instruments (continued)

Economic interest rate exposure

The company held cash and short term deposits as follows:

2013	Cash			Short term deposits			Total
Currency	Amount	Economic interest rate	Average maturity	Amount	Economic interest rate	Average maturity	
	£m	%	days	£m	%	days	£m
Sterling	61.9	0.4	5	30.1	0.4	186.0	92.0
Euro	10.1	-	5	-	-	-	10.1
Danish Krone	0.1	-	5	-	-	-	0.1
	72.1			30.1			102.2

2012	Cash			Short term deposits			Total
Currency	Amount	Economic interest rate	Average maturity	Amount	Economic interest rate	Average maturity	
	£m	%	days	£m	%	days	£m
Sterling	61.8	0.4	4	30.5	1.1	182.0	92.3
Euro	9.5	0.1	5	-	-	-	9.5
Canadian Dollar	0.3	-	1	-	-	-	0.3
Danish Krone	0.1	-	1	-	-	-	0.1
	71.7			30.5			102.2

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.

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 2013						
Sterling:						
5.25% guaranteed secured bonds	555.7	-	-	555.7	5.27%	7.0
Bank loans	136.0	136.0	-	-	1.49%	0.5
Inter-company loans	22.5	22.5	-	-	1.50%	0.5
Total	714.2	158.5	-	555.7		
At 31 March 2012						
Sterling:						
5.25% guaranteed secured bonds	583.9	-	-	583.9	5.27%	8.0
Bank loans	148.3	148.3	-	-	1.50%	0.4
Inter-company loans	22.5	22.5	-	-	1.62%	0.5
Total	754.7	170.8	-	583.9		

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 2013						
Sterling:						
5.25% guaranteed secured bonds	355.7	-	-	355.7	5.28%	7.0
5.25% guaranteed secured bonds	200.0	-	200.0	-	4.72%	0.5
Bank loans	136.0	136.0	-	-	1.49%	0.4
Inter-company loans	22.5	22.5	-	-	1.50%	0.5
Total	714.2	158.5	200.0	355.7		
At 31 March 2012						
Sterling:						
5.25% guaranteed secured bonds	383.9	-	-	383.9	5.28%	8.0
5.25% guaranteed secured bonds	200.0	-	200.0	-	4.51%	0.5
Bank loans	148.3	148.3	-	-	1.50%	0.4
Inter-company loans	22.5	22.5	-	-	1.62%	0.5
Total	754.7	170.8	200.0	383.9		

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

18. Financial instruments (continued)

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.

	2013 £m		2012 £m	
Net Debt	605.5		647.6	
	£m	%	£m	%
Fixed (net of bond discount and issue costs)	351.5	58.1	379.0	58.5
Index-linked	200.0	33.0	200.0	30.9
Floating (net of cash and short term investments and facility fees)	54.0	8.9	68.6	10.6
	605.5	100.0	647.6	100.0

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

Interest rate sensitivity analysis

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

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

	2013 Impact £m	2012 Impact £m
Cash on deposit (2013: £102.2m, 2012: £102.2m)	1.0	1.0
Borrowings (2013: £158.5m, 2012: £170.8m)	(1.6)	(1.7)
	(0.6)	(0.7)

Overall the company's sensitivity to interest rates has decreased marginally in the year, reflecting reduced borrowing levels.

Inflation rate risk

The regulatory charge control conditions that apply to the company's UK en route and North Atlantic services determines a revenue allowance for financing charges that is linked to inflation. To achieve an economic hedge of this income, in August 2003 coincident with the issue of its £600m 5.25% fixed rate bond, the company entered into an amortising index-linked swap with a notional principal of £200m for the period up to March 2017 reducing semi-annually thereafter and expiring in March 2026. Under the terms of this swap, NERL receives fixed interest at 5.25% and from December 2010 paid interest at a rate of 3.43% adjusted for the movement in RPI (prior to this date it paid interest at a rate of 2.98%). The index-linked swap cannot be designated as a cash flow hedge under IFRS, although it provides an economic hedge of certain of NERL's inflation-linked revenues.

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

Inflation rate sensitivity analysis

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

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

	2013 Impact £m	2012 Impact £m
Change in index-linked swap interest and mark to market value	(29.3)	(30.0)

The mark to market value of the index-linked swap is also sensitive to the discount rates that are used to determine the net present value of the cash flows under the swap agreement. The discount rate is determined by reference to market yields on interest rate swaps. The effect of a 1% increase in the discount rate would be to increase profit and equity by £14.1m (2012: £13.3m). There would be an equal and opposite impact on profit and equity if discount rates decreased by 1%.

18. Financial instruments (continued)

Credit risk management

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

The NATS group 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 and Poor's and Moody's; the Fitch rating is only used if one of these agencies does not provide a rating. Where there is a difference in the rating then the lowest of the ratings is applied.

Currently, the company's investments take the form of bank time deposits and money market fund investments. Investments in bank time deposits with maturities up to three months and between three and six months are only entered into with institutions holding a long-term minimum credit rating of A- and A+ respectively from Standard & Poor's or Fitch and A3 and A1 respectively from Moody's. However, dependent on market conditions, tighter restrictions on rating requirements and lower limits may be placed on the duration of deposits. Hence, since the 2008 financial crisis, the company has restricted deposits with banks rated below AA/Aa2 to a maximum of 1 week.

The tables below set out the group's investment limits that are applied to each institution based on its credit rating:

Rating (Standard and Poor's)	Limit per Institution £m
AAA	50.0
AA+	40.0
AA	30.0
AA-	20.0
A+	15.0
A	10.0
A-	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	2013 £m	By credit rating %	Limit utilised %	Number of institutions	2012 £m	By credit rating %	Limit utilised %
AAA	2	17.4	17.0	17.4%	-	-	-	-
AA-	1	20.0	19.6	100.0%	-	-	-	-
A+	5	41.6	40.7	55.5%	5	65.9	64.5	87.9%
A	3	23.2	22.7	77.3%	5	36.3	35.5	72.6%
		102.2	100.0			102.2	100.0	

Liquidity risk management

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

The policy is to:

a. maintain free cash equal to between 1 and 2 months of UK en route services revenues (see below). Free cash is defined as cash and cash equivalents and short term investments, excluding a debt service reserve account of £30.1m 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 110% of forecast requirements that are not otherwise covered by operating cash flows or other sources of finance through the period of the business plan. At 31 March 2013 NERL had access to bank facilities totalling £275m available until 21 December 2016. The new facilities comprise a £245m revolving term loan facility and a £30m revolving credit facility;

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 started to amortise in 2012 and has a final maturity date of 2026 and by having available shorter dated committed bank facilities (as referred to above).

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

	2013 £m	2012 £m
Average monthly UK en route services income receipts	49.3	47.9
Free cash at 31 March	50.8	50.4
Ratio of free cash to UK en route services income receipts	1.0	1.1

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

	2013 £m	2012 £m
Bank borrowings	136.0	148.3
Gross borrowings	714.2	754.7
Bank borrowings as a percentage of gross borrowings	19.0%	19.7%

18. Financial instruments (continued)

Maturity of borrowings

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

	2013				2012			
	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	0.3	60.2	45.2	105.7	0.4	210.6	42.5	253.5
Between one and two years	0.4	60.4	-	60.8	0.4	58.2	-	58.6
Due between two and five years	1.6	333.6	-	335.2	1.8	179.7	-	181.5
Due in more than five years	29.5	478.0	-	507.5	31.4	547.8	-	579.2
	31.8	932.2	45.2	1,009.2	34.0	996.3	42.5	1,072.8
Effect of interest, discount and unamortised bond issue and bank facility arrangement fees	(9.3)	(247.0)	-	(256.3)	(11.5)	(269.0)	-	(280.5)
	22.5	685.2	45.2	752.9	22.5	727.3	42.5	792.3

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

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

	Due within one year or less £m	Between one and two years £m	Due between two and five years £m	Due in more than five years £m	Total £m
2013					
Net settled:					
Index-linked swap receivable/(payable)	2.3	2.1	(8.4)	(144.1)	(148.1)
Gross settled:					
Foreign exchange forward contract receivables	131.4	-	-	-	131.4
Foreign exchange forward contract payables	(130.2)	-	-	-	(130.2)
	3.5	2.1	(8.4)	(144.1)	(146.9)
2012					
Net settled:					
Index-linked swap receivable/(payable)	2.5	2.3	1.2	(138.8)	(132.8)
Gross settled:					
Foreign exchange forward contract receivables	127.8	0.5	-	-	128.3
Foreign exchange forward contract payables	(127.6)	(0.5)	-	-	(128.1)
	2.7	2.3	1.2	(138.8)	(132.6)

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, forecast RPI inflation rates and is then discounted to its present value. The fair value of the £600m bond has been derived from its externally quoted price. The book values of other financial assets and liabilities approximate to their fair values because of their short maturities.

	Carrying amount		Fair value	
	2013 £m	2012 £m	2013 £m	2012 £m
Financial assets				
Trade and other receivables, excluding prepayments and accrued income	49.7	48.8	49.7	48.8
Cash and short term investments	102.2	102.2	102.2	102.2
Derivative financial instruments				
Forward foreign exchange contracts	1.6	0.2	1.6	0.2
	153.5	151.2	153.5	151.2
Financial liabilities				
Trade and other payables, excluding accruals and deferred income	(45.2)	(42.5)	(45.2)	(42.5)
£600m 5.25% Guaranteed Secured Amortising Bond	(555.7)	(583.9)	(661.0)	(666.5)
Bank loans	(136.0)	(148.3)	(136.0)	(148.3)
Intercompany loan	(22.5)	(22.5)	(22.5)	(22.5)
Derivative financial instruments				
Forward foreign exchange contracts	(0.6)	(0.4)	(0.6)	(0.4)
Index-linked swap	(146.6)	(126.1)	(146.6)	(126.1)
	(906.6)	(923.7)	(1,011.9)	(1,006.3)

19. Financial and other liabilities

Trade and other payables

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

	2013 £m	2012 £m
Current		
Trade payables	9.2	11.1
Amounts due to other group undertakings	36.0	31.1
Other payables	-	0.1
Accruals and deferred income		
- deferred grants	0.4	0.4
- other	50.9	52.8
	96.5	95.5
Non-current		
Amounts due to other group undertakings	-	0.1
Other payables	-	0.1
Accrual and deferred income		
- deferred grants	3.5	3.5
- other	12.4	8.5
	15.9	12.2
	112.4	107.7

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 (2012: 43 days). The directors consider that the carrying amount of the trade payables approximates to their fair value.

20. Provisions

	Relocation £m	Other £m	Total £m
At 1 April 2012	1.6	0.3	1.9
Additional provision in the year	0.2	5.9	6.1
Release of provision in the year	(0.3)	-	(0.3)
Utilisation of provision	(1.0)	-	(1.0)
At 31 March 2013	0.5	6.2	6.7

	Total £m
Amounts due for settlement within 12 months	0.8
Amounts due for settlement after 12 months	5.9
	6.7

The relocation provision represents the best estimate of the future cost of relocating staff when the site they work at closes and they are relocated to another site. The ageing of the provision reflects the expected timing of the employees' relocation date.

The other provisions represent the best estimate of other liabilities. These include the contractual obligation to re-instate leased properties to the same condition as at inception of the lease. The ageing of the provision reflects the best estimate of when these potential liabilities will fall due.

Redundancy costs are recharged by the company's parent through intercompany recharges and are included within amounts due to other group companies.

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/(liability) £m	Financial instruments £m	Other £m	Total £m
At 1 April 2011	125.7	9.4	(15.4)	(2.3)	117.4
(Credit)/charge to income	(6.7)	11.5	0.2	0.9	5.9
(Credit)/charge to equity	-	(27.9)	-	0.1	(27.8)
At 31 March 2012	119.0	(7.0)	(15.2)	(1.3)	95.5
At 1 April 2012	119.0	(7.0)	(15.2)	(1.3)	95.5
Charge/(credit) to income	0.3	9.1	(2.2)	0.2	7.4
Charge to equity	-	0.4	0.2	-	0.6
At 31 March 2013	119.3	2.5	(17.2)	(1.1)	103.5

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:

	2013 £m	2012 £m
Deferred tax liabilities	(121.8)	(119.0)
Deferred tax assets	18.3	23.5
	(103.5)	(95.5)

22. Share capital

	Authorised Number of shares	£m	Called up, allotted and fully paid Number of shares	£m
Ordinary shares of £1 each				
At 31 March 2012 and 31 March 2013	10,000,000	10.0	10,000,000	10.0

23. Notes to the cash flow statement

	2013 £m	2012 £m
Operating profit from continuing operations	205.4	200.7
Adjustments for:		
Depreciation of property, plant and equipment	76.2	71.6
Amortisation of intangible assets	24.6	17.9
Impairment loss	1.1	3.4
Deferred grants released	(0.4)	(0.6)
Loss on disposal of property, plant and equipment	-	1.0
Non-cash element of charge for pension costs	(37.5)	(44.4)
Operating cash flows before movements in working capital	269.4	249.6
Increase in trade and other receivables	(23.1)	(11.7)
Increase/(decrease) in trade and other payables and provisions	7.6	(19.0)
Cash generated from operations	253.9	218.9
Tax paid	(21.1)	(15.2)
Net cash inflow from operating activities	232.8	203.7

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.

24. Financial commitments

	2013 £m	2012 £m
Capital commitments contracted but not provided for in the accounts.	52.4	69.2
Minimum lease payments under operating leases recognised in the income statement for the year.	5.5	6.3

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:

	2013 £m	2012 £m
Within one year	6.4	6.4
In the second to fifth years inclusive	21.1	21.9
After five years	29.2	33.6
	56.7	61.9

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

Guarantees

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

25. Retirement benefit scheme

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

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

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

During the year the company consulted on further pension reforms to mitigate rising pension costs. These included a change to the limit on increases in pensionable pay to a maximum of the consumer price index (CPI) plus 0.25%. In addition, the Trustees consulted members of the Scheme on a change to the indexation of future service at CPI, rather than RPI.

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 the future.

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

The two valuations differ in a number of critical respects, including, for example, differences in timing and frequency as well as in valuation assumptions. The Trustees' latest funding assessment was prepared as at 31 December 2012, whereas the company's accounting valuation is prepared annually at 31 March. As a result, at each valuation date, the market conditions on which the assumptions are based will be different. Also, the assumptions adopted for the Trustees' funding assessment are set by the Trustees and include appropriate margins for prudence, whereas those adopted for the company's accounting valuation are prescribed by international accounting standards and reflect best estimates.

Trustees' funding assessment

The last Trustees' funding assessment of the NATS' section was carried out at 31 December 2012 and used the projected unit credit method. The assumptions which have the most significant effect on the result of the valuation are those relating to the rate of return on investments and the rates of increase in salaries and pensions. For the purpose of the Trustees' funding assessment, it was assumed that the annual investment returns before retirement will be 3.37% higher than the annual general increases in salaries (allowance is also made for further salary increases due to promotions) and the annual investment returns for pensions in payment will be 0.22% higher than the annual increases in pensions.

The market value of the NATS section's assets as at 31 December 2012 was £3,527.5m. For the purpose of the Trustees' funding assessment assets were taken at market value. The assets were sufficient to cover 90.2% of the benefits that had accrued to existing members.

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

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

Contributions to the pension scheme

During the year the company paid cash contributions to the scheme of £106.9m (2012: £109.0m). This amount included £11.7m (2012: £11.9m) of wages and salaries sacrificed by employees in return for pension contributions. Excluding the effect of salary sacrifice, employer cash contributions were paid at a rate of 45.9% (2012: 45.5%) of pensionable pay. The company increased contributions from May 2010 to 36.7% of pensionable pay, equivalent to the future service cost and in response to the 2009 triennial valuation, NATS has made further contributions of £2.0m per month from January 2011, NERL's share being c. £1.5m, increasing these by 3.5% each January thereafter, under a deficit recovery plan agreed with the Trustees. This plan will continue until 31 December 2014 before a revised schedule reflecting the 2012 valuation is implemented. NATS will contribute £2.4m per month from January 2015, NERL's share will be c. £1.8m per month.

25. Retirement benefit scheme (continued)

Company's accounting valuation under international accounting standards
The pension cost under IAS19: *Employee Benefits,* relating to the scheme is assessed in accordance with the advice of independent qualified actuaries.

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

A Trustees' funding assessment was carried out as at 31 December 2012 and updated to 31 March 2013 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:

	2013	2012	2011
RPI Inflation	3.35%	3.25%	3.45%
CPI Inflation	2.45%	n/a	n/a
Increase in:			
- salaries	2.70%	3.25%	3.95%
- deferred pensions	3.35%	3.25%	3.45%
- pensions in payment	3.35%	3.25%	3.45%
Expected return on:			
- equities	n/a	7.10%	7.35%
- property and other assets	n/a	6.60%	7.35%
- bonds	n/a	3.45%	4.70%
Discount rate for scheme liabilities	4.45%	5.05%	5.45%

The mortality assumptions have been drawn from actuarial tables 101% S1PMA light and 99% S1PFA light with future improvements in line with CMI 2011 projections for male/female members, subject to a long-term improvement of 1.5% p.a (2012: 82% S1PMA and 101% S1PFA with future improvements in line with 80%/60% long cohort projections for male/female members, subject to a minimum improvement of 1.25%). These tables assume that the life expectancy, from age 60, for a male pensioner is 29.3 years and a female pensioner is 30.8 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 31.1 years and for females to 32.6 years.

The assumptions for expected return on investments above are not applicable for 2013 following the introduction of IAS 19: *Employee benefits* (revised June 2011), which applies for the year ending 31 March 2014.

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

Assumption:	Change in assumption:	Impact on scheme liabilities:
Discount rate	Increase/decrease by 0.5%	Decrease by 11.6%/increase by 13.7%
Rate of inflation	Increase/decrease by 0.5%	Increase by 13.7%/decrease by 11.8%
Rate of salary growth	Increase/decrease by 0.5%	Increase by 4.2%/decrease by 3.9%
Rate of mortality	1 year increase in life expectancy	Increase by 2.3%

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

	2013 £m	2012 £m
Current service cost	(87.5)	(90.4)
Past service cost	(1.3)	(2.2)
Expected return on scheme assets	151.4	159.2
Interest cost on scheme liabilities	(132.0)	(131.2)
Total defined benefit charge recognised in arriving at operating profit	(69.4)	(64.6)

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

	2013 £m	2012 £m
Actual return less expected return on scheme assets	180.2	(60.9)
Experience losses and gains arising on scheme liabilities	118.8	(2.6)
Changes in assumptions underlying the present value of the scheme liabilities	(296.9)	(45.9)
	2.1	(109.4)

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

	2013 £m	2012 £m
Fair value of scheme assets	2,943.7	2,573.1
Present value of defined benefit obligations	(2,932.9)	(2,601.9)
Surplus/(deficit) in scheme	10.8	(28.8)

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

	2013 £m	2012 £m
At 1 April	2,573.1	2,433.8
Expected return on scheme assets	151.4	159.2
Actuarial gains and losses	180.2	(60.9)
Contributions from company	106.9	109.0
Benefits paid	(67.9)	(68.0)
At 31 March	2,943.7	2,573.1

25. Retirement benefit scheme (continued)

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

	2013 £m	2012 £m
At 1 April	(2,601.9)	(2,397.6)
Current service cost	(87.5)	(90.4)
Past service cost	(1.3)	(2.2)
Interest cost	(132.0)	(131.2)
Actuarial gains and losses	(178.1)	(48.5)
Benefits paid	67.9	68.0
At 31 March	(2,932.9)	(2,601.9)

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	
	2013 £m	2012 £m	2013 %	2012 %
Equity instruments	1,566.9	1,369.4	n/a	7.10
Property and other assets	392.8	362.4	n/a	6.60
Bonds	885.2	771.2	n/a	3.45
Cash and net current assets	98.8	70.1	n/a	3.45
	2,943.7	2,573.1	n/a	5.84

Where applicable, the overall expected return on assets represents a weighting based on the expected return for each asset class and the value of investments in each asset class.

The scheme assets do not include any investments in the equity of the company or debt instruments or any property occupied by, or other assets used by, the company.

The five year history of experience adjustments is as follows:

	2013 £m	2012 £m	2011 £m	2010 £m	2009 £m
Present value of defined benefit obligations	(2,932.9)	(2,601.9)	(2,397.6)	(2,120.1)	(1,692.8)
Fair value of scheme assets	2,943.7	2,573.1	2,433.8	2,179.8	1,641.0
Surplus/(deficit) in the scheme	10.8	(28.8)	36.2	59.7	(51.8)
Experience adjustments in scheme liabilities					
Amount (£m)	118.8	(2.6)	(20.9)	164	33.1
Percentage of scheme liabilities	(4.1%)	0.1%	0.9%	(7.7%)	(2.0%)
Experience adjustments in scheme assets					
Amount (£m)	180.2	(60.9)	79.8	421.4	(653.6)
Percentage of scheme assets	6.1%	(2.2%)	3.3%	19.3%	(39.8%)

The actual return on scheme assets for the year ended 31 March 2013 was £331.6m (2012: £98.3m).

The estimated contributions expected to be paid to the scheme during the financial year ending 31 March 2014 is £106m, including salary sacrifice contributions estimated at £12m.

26. Related party transactions

The NATS group has four shareholders - the Crown, The Airline Group Limited (AG), Heathrow Airport Holdings Limited and the NATS Employee Sharetrust Limited. 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).

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

Trading transactions

	Sales		Purchases		Amounts owed by related parties		Amounts owed to related parties	
	Year ended 31 March 2013	Year ended 31 March 2012	Year ended 31 March 2013	Year ended 31 March 2012	Year ended 31 March 2013	Year ended 31 March 2012	Year ended 31 March 2013	Year ended 31 March 2012
	£m	£m	£m	£m	£m	£m	£m	£m
Heathrow Airport Holdings Ltd	-	-	-	0.1	-	-	-	-
Ministry of Defence (MoD)	48.0	46.5	5.0	5.0	5.2	4.9	13.2	7.8
Department for Transport (DfT)	1.8	3.1	-	-	-	-	-	-
Meteorological Office	-	-	0.5	0.6	-	0.4	0.1	-

Sales are made to related parties at the company's usual rates and purchases at market prices. The amounts outstanding are unsecured and will be settled in cash. No guarantees have been received. No provisions (2012: £nil) have been made for doubtful debts in respect of amounts owed by related parties.

Directors' remuneration

Remuneration payable to the highest paid director of the company in the year was £720,000 (2012: £736,000).

27. Parent undertaking

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

The company's ultimate controlling party is The Airline Group Limited a 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, 4000 Parkway, Whiteley, Fareham, Hampshire, PO15 7FL.

28. Events after the reporting period

In May 2013, the Board declared an interim dividend for 2014 of £4.28 per share (totalling £42.75m), which was paid to the company's parent in May 2013.