Yorkshire Water Services Ltd

Interim Report and Financial Statements

For the six months ended 30 September 2015

Registered number: 2366682

Taking responsibility for the water environment for good

Contents

Chairman's Statement

It is with great sadness and regret that I have to report the death of our colleague, Mick Jennings, a mechanical fitter in our Engineering Reliability team, who passed away on 22 July, following an accident at Tadcaster waste water treatment works. Mick's death has been a considerable shock to the Company and our colleagues. On behalf of the Company I would like to record our sincere condolences to Mick's family and his close colleagues.

During my first 6 months as Chairman I have spent a great deal of time visiting many of Yorkshire Water's sites and meeting many colleagues. I have been consistently impressed by the quality and commitment of our executive, colleagues and partners. Throughout the Company there is a strong culture of customer service and commitment to improving Yorkshire's environment.

We have a challenging business plan for the period 2015 to 2020 which will deliver improved services to customers and improvements to Yorkshire's environment whilst keeping bills one of the lowest in the industry.

Richard Parry-Jones
Chairman

Business Review

Chief Executive's Review

Yorkshire Water has made good progress towards the delivery of its 26 customer performance commitments during the first six months of the year, while being able to report a strong financial performance.

The Company is currently on track to meet the overwhelming majority of its operational, environmental and service commitments, with strong delivery plans in place. A major change programme is currently being reviewed which will drive further business improvements over the 5 year regulatory period and beyond.

Key highlights for the half year include:

- Water quality compliance remains high, with the number of interruptions to supply and customer contacts ahead of target;
- The number of pollution incidents in the region remains ahead of plan;
- Serviceability remains stable across all four of Ofwat's key indicators;
- Whilst overall customer satisfaction remains high, we were disappointed with the results of Ofwat's Service Incentive Mechanism (SIM survey), covering the first half year. Billing enquiries and water services results were very strong but waste water scores were disappointing. The recent awarding of a major new waste water delivery contract and announcement of investment in our Saltend Waste Water Treatment Works are planned to drive significant improvements in our future response times and resolution of sewerage issues;
- We remain on course to achieve our leakage reduction target;
- A satisfaction survey conducted at Yorkshire Water's recreation sites showed that an overwhelming 98% of visitors enjoy the outdoor experiences we provide; and
- Yorkshire Water recently also became the first major company in the region to pledge financial and in-kind support to Hull 2017 – the organisation set up to co-ordinate Hull's UK City of Culture celebrations.

As a result of the recent PR14 price review settlement, in 2015/16 customers have benefitted from a 3% reduction in the average household bill which fell from £373 to £360. This means that by 2020, our customers will be paying £15 less for their water and sewerage services than the national average bill.

During the first six months of 2015/16 we have delivered £98.5m of capital investment to protect and enhance the services we provide to our customers and improve the water environments in which we operate. We are on course to deliver our investment outputs for the year. Preparations for the expansion of the retail business market in April 2017 are also progressing well.

Earlier this year Yorkshire Water's parent company, the Kelda Group, announced the creation of a new business which will compete to provide retail services to businesses across the UK.

In the meantime, major organisational, operational and cultural changes are being made to Yorkshire Water's wholesale operations to ensure the business is ready to service the needs of multiple retail operators once the Shadow Market opens in October 2016.

We also continue to work positively with Ofwat on their Water 2020 programme which looks to consider the need for long term reform of the sector.

Business Review

This interim report is the first published accounts for Yorkshire Water under the new reporting framework (Financial Reporting Standard 102). The most significant change is in the net asset position where we are now required to bring financial instruments on to the balance sheet at fair value and significantly change the manner in which we account for deferred taxation. Further detail is set out in the financial review.

As noted by the Chairman in his statement I would also like to express my sadness and condolences to Mick Jennings' family and close colleagues. We continue to support in any way we can Mick's family and colleagues who have been impacted by his death.

The Police and Health and Safety Executive investigations are on-going and we continue to provide them with full support. We have also set up our own, internal investigation into the accident which continues and is expected to conclude in the second half of the year.

Richard Flint
Chief Executive

Business Review

Financial Performance

For the year ended 31 March 2015, the Company prepared its financial statements under United Kingdom Generally Accepted Accounting Practice ("UK GAAP"). The Company has elected to prepare its financial statements for the year ended 31 March 2016 in compliance with Financial Reporting Standard 102, the Financial Reporting Standard applicable in the UK and Republic of Ireland ("FRS 102") and therefore these results are presented in line with the new reporting framework required within the UK. The key impacts of the change are set out in this business review and are detailed in note 11.

Key financial performance indicators (presented under FRS 102)

The results for the 6 month period are reported in line with FRS 102 and the comparatives have been restated.
The key performance indicators, on the new basis, are set out below:

	6 months ended 30 September 2015 FRS 102	6 months ended 30 September 2014 FRS 102
Profit and loss indicators		
Turnover (£m)	**493.5**	509.8
Operating profit (£m)	**156.9**	199.7
EBITDA (£m)	**285.2**	319.1
Capital Expenditure (£m)	**98.5**	113.7
Balance sheet indicators	**30 September 2015**	31 March 2015
Net debt (£m)	**3,523.7**	3,547.4
Gearing: Adjusted net debt to Regulatory Capital Value (RCV)*	**79.4%**	76.8%

*Ofwat's Key performance indicators for the water industry, definitions available at: http://www.ofwat.gov.uk/regulating/compliance/reportingperformance/kpi

Turnover decreased by 3.2% to £493.5m (6 months ended 30 September 2014: £509.8m) in line with expectation and is as a result of the recent PR14 price review settlement. In 2015/16 customers have benefitted from a 3% reduction in the average household bill which fell from £373 to £360 impacting directly on reported turnover.

Operating profit has reduced in the period by 21.4% to £156.9m compared to the comparable period last year (6 months ended 30 September 2014: £199.7m). This is as a result of the 3.2% decrease in turnover and an 8.5% increase in operating costs (from £310.1m to £336.6m). The primary movements are an increase in depreciation of £11m, as a result of capital investment during 2014/15, additional contributions to the pension scheme of £4m and the inflationary increases to manpower costs and business rates.

EBITDA has also decreased in the period to £285.2m from £319.1m, a 10.6% decrease. This is as a result of the movements in turnover and additional operating costs set out above, excluding depreciation.

Business Review

Capital expenditure in the 6 month period to September 2015 is £98.5m (30 September 2014 £113.7m), a 13.4% decrease. This is as expected within the first year of a new investment period and is due to a combination of factors including changes to the National Environment Programme (NEP) and ongoing work with our capital partners to ensure that the 5 year programme is fully optimised.

During the six month period to 30 September 2015, total net debt has reduced to £3,523.7m (31 March 2015: £3,547.4) which reflects the repayment of external debt offset by the utilisation of the capital facility to finance the capital programme. Net debt at 30 September 2015 includes £1,009.0m of amounts due from group companies (31 March 2015: £1,009.0m). Based on an RCV value of £5,720.9m, senior adjusted net debt to RCV at September 2015 is 79.4% (31 March 2015: 76.8%). The apparent increase in gearing is due to the anticipated reduction to the RCV on 1 April 2015 resulting from capital outperformance in the previous regulatory period. The level of gearing is forecast to reduce below its current level by the end of the financial year due to the on-going strategy to improve the Company's financial strength.

As required by FRS 102 the fair value of the financial instruments are now recognised on the balance sheet and the movement in the valuation is recognised in the profit and loss account. The only significant movement in the six months ended 30 September 2015 is in relation to the fair value of the index linked swaps as set out in note 2.

£43.4m of distributions have been made to the parent company during the period (6 months ended 30 September 2014: £47.5m), of which £34.7m (6 months ended 30 September 2014: £34.8m) was distributed to Kelda Eurobond Co Ltd in order to allow Kelda Eurobond Co Ltd to make an interest payment and loan repayment on their loan from Yorkshire Water. Net distributions made to fund group costs were £8.7m (6 months ended 30 September 2014: £12.7m). No distributions have been made to the ultimate shareholders of the Kelda group.

Business Review

Transition to FRS 102

The adoption of the new accounting framework has impacted the financial accounts as reported for the 6 month period ended 30 September 2015. In order that the performance of the Company is understood a comparison has been set out below of the key elements of the financial statements under both FRS 102 and UK GAAP so that the main impacts are visible. Further detail can be found in note 11.

Non-statutory disclosure	**FRS 102 as at 30 September 2015 £m**	UK GAAP as at 30 September 2015 £m
Turnover	**493.5**	496.4
EBITDA	**285.2**	290.5
Net interest payable including exceptional fair value movements	**(4.1)**	(91.3)
Net debt	**3,523.7**	3,482.5
Net assets	**1,107.1**	2,972.2

There is minimal impact on the level of turnover, EBITDA and net debt from the change in the reporting standards so the performance trends as stated above will apply under both reporting standards. However, more significant change can be seen in the level of net interest payable and net assets. These changes are principally as a result of the recognition of financial instruments on the balance sheet at their fair value and the movement in the fair values being taken through the interest line in the profit and loss account, as required by FRS 102.

The financial instruments have existed for a number of years but have not previously been carried on the balance sheet as required by UK GAAP.

By bringing the financial instruments on to the balance sheet the net asset position of the Company has been reduced by £1,115.2m. Net assets have also been affected by other changes, the most significant of which are the change in tax treatment and the change to the accounting policies in relation to fixed assets.

Under FRS 102 deferred tax can no longer be discounted and must also now be provided in relation to the revaluation of fixed assets. The deferred tax liability has increased by £606.5m as at 30 September 2015 due to these changes.

There have also been a number of changes to the accounting of fixed assets, the most significant of which is in relation to contributions from customers towards capital works. The change in treatment has reduced the net asset position by £176.7m.

More detail of the changes can be found in note 11.

Business Review

Principal Risks and Uncertainties

The Company's risk management process aims to be comprehensive, systematic and continuous and based on constant monitoring of business risk. The Board is also responsible for the Company's internal control and for reviewing its effectiveness.

The Company's principal risks and uncertainties include changes to the regulatory environment, changes in legislation, climatic changes, social influences and supplier markets.

Further detail on the risks and uncertainties is included in the Annual Report and Financial Statements for the year ended 31 March 2015.

Profit and Loss Account

For the Six Months Ended 30 September 2015

	Note	*Unaudited six months ended* **30 September 2015** £m	*30 September 2014* £m
Turnover		**493.5**	509.8
Operating costs		**(336.6)**	(310.1)
Operating profit		**156.9**	199.7
Interest receivable and similar income before exceptional items		**46.9**	45.0
Exceptional fair value income	2	**106.1**	30.0
Total interest receivable and similar income		**153.0**	75.0
Interest payable and similar charges before exceptional items		**(137.0)**	(140.8)
Exceptional fair value charges	2	**(20.1)**	(126.6)
Total interest payable and similar charges		**(157.1)**	(267.4)
Profit on ordinary activities before tax		**152.8**	7.3
Tax on profit on ordinary activities	3	**(7.0)**	31.1
Profit for the period		**145.8**	38.4

All of the above results relate to continuing activities. There is no material difference between the profit before tax and the profit for the period stated above and their historical cost equivalents. The results for the six months ended 30 September 2014 have been restated and are presented in accordance with FRS 102.

Balance Sheet

As at 30 September 2015

	Note	**30 September 2015 £m**	31 March 2015 (restated) £m
Fixed assets			
Intangible assets		**27.4**	24.8
Tangible assets		**6,895.0**	6,917.9
Investments		**0.1**	0.1
		6,922.5	6,942.8
Current assets			
Stocks		**1.9**	1.3
Debtors (including £1,311,755,000 due after more than one year (31 March 2015: £1,324,728,000))		**1,521.4**	1,519.3
Cash at bank and in hand		**41.7**	35.2
		1,565.0	1,555.8
Creditors: amounts falling due within one year		**(354.3)**	(389.9)
Net current assets		**1,210.7**	1,165.9
Total assets less current liabilities		**8,133.2**	8,108.7
Creditors: amounts falling due after more than one year	*5*	**(6,588.1)**	(6,672.3)
Provisions for liabilities			
Deferred tax liability		**(437.4)**	(430.4)
Other provisions		**(0.6)**	(0.6)
		(438.0)	(431.0)
Net assets		**1,107.1**	1,005.4
Capital and reserves			
Called up share capital		**10.0**	10.0
Revaluation reserve		**201.0**	201.0
Cash flow hedge reserve		**(0.7)**	-
Profit and loss account		**896.8**	794.4
Shareholders' funds		**1,107.1**	1,005.4

The results for the year ended 31 March 2015 have been restated and are presented in accordance with FRS 102.

Statement of Changes in Equity

For the six months ended 30 September 2015

	Note	Called up Share capital £m	Revaluation reserve £m	Cash Flow Hedge reserve £m	Profit and loss account £m	Total equity £m
Balance at 1 April 2014 (restated)		10.0	13.8	-	978.2	**1,002.0**
Total comprehensive income/(expense) for the year						
Loss for the financial year		-	-	-	(90.3)	**(90.3)**
Revaluation of fixed assets before taxation		-	234.6	-	-	**234.6**
Income tax on revaluation of fixed assets		-	(46.8)	-	-	**(46.8)**
Other comprehensive income/(expense) for the year		-	-	-	(0.5)	**(0.5)**
Total comprehensive income/(expense) for the year		**-**	**187.8**	**-**	**(90.8)**	**97.0**
Transfer		-	(0.6)	-	0.6	**-**
Transactions with owners recorded directly in equity						
Dividends		-	-	-	(93.6)	**(93.6)**
Balance at 31 March 2015 (restated)		**10.0**	**201.0**	**-**	**794.4**	**1,005.4**
Total comprehensive income/(expense) for the period						
Profit for the financial period		-	-	-	145.8	**145.8**
Other comprehensive income/(expense) for the period		-	-	(0.7)	-	**(0.7)**
Total comprehensive income/(expense) for the period		-	-	(0.7)	145.8	**145.1**
Transactions with owners recorded directly in equity						
Dividends	4	-	-	-	(43.4)	(43.4)
Balance at 30 September 2015		**10.0**	**201.0**	**(0.7)**	**896.8**	**1,107.1**

The results for the year ended 31 March 2015 have been restated and are presented in accordance with FRS 102.

Notes to the Financial Statements

For the six months ended 30 September 2015

For the year ended 31 March 2015, the Company prepared its financial statements under United Kingdom Generally Accepted Accounting Practice ("UK GAAP"). The Company has elected to prepare its financial statements for the year ended 31 March 2016 in compliance with Financial Reporting Standard 102, the Financial Reporting Standard applicable in the UK and Republic of Ireland ("FRS 102"). Therefore the financial statements for the year ended 31 March 2015 were the last financial statements prepared by the Company under old UK GAAP.

The Company's financial statements for the year ended 31 March 2016 that will be prepared in compliance with the requirements of FRS 102 will include comparative information for the year ended 31 March 2015. Those financial statements will be the first financial statements prepared by the Company in accordance with FRS 102 therefore this is the first interim report prepared by the Company in accordance with FRS 102.

The financial information for the six months ended 30 September 2015 and the equivalent period in 2014 has not been audited.

The interim financial information was approved for issue by the board of directors on 25 November 2015.

1. Basis of preparation and accounting policies

The financial information for the six month period ended 30 September 2015 has been prepared in accordance with FRS 102 and in accordance with pronouncements on interim reporting issued by the Accounting Standards Board and the comparative information for the six month period ended 30 September 2014, and as at 31 March 2015 has been restated.

The following section explains how, in preparing this financial information, the Directors of the Company have applied the first-time adoption provisions set out in FRS 102 and the assumptions they have made about the requirements and interpretations expected to be effective and the accounting policies expected to be adopted in the 31 March 2016 FRS 102 financial statements.

The Company is exempt by virtue of s400 of the Companies Act 2006 from the requirement to prepare group financial statements. This financial information presents information about the Company as an individual undertaking and not about its group.

This financial information was prepared in accordance with FRS 102, except as described below, and the Companies Act 2006. The presentation currency of this financial information is sterling.

In the transition to FRS 102 from old UK GAAP, the Company has made measurement and recognition adjustments. An explanation of how the transition to FRS 102 has affected the financial position and financial performance of the Company is provided in note 11.

FRS 102 grants certain first-time adoption exemptions from the full requirements of FRS 102 in the transition period. The following exemptions have been taken in this financial information:

- Revaluation as deemed cost - The previous GAAP revaluation at transition date has been used as deemed cost for infrastructure assets.
- Separate financial instruments - the carrying amount of the Company's cost of investment in subsidiaries is its deemed cost at 1 April 2014.
- Lease arrangements - in order to determine whether an arrangement contains a lease, the Company has analysed facts and circumstances existing at 1 April 2014 rather than the commencement date of the relevant arrangement.
- Business combinations - Business combinations that took place prior to 1 April 2014 have not been restated.
- Kelda Eurobond Co Limited includes the Company in its consolidated financial statements. The consolidated financial statements of Kelda Eurobond Co Limited are prepared in accordance with International Financial Reporting Standards

Notes to the Financial Statements

For the six months ended 30 September 2015

as adopted by the EU and are available to the public and may be obtained from Western House, Halifax Road, Bradford, West Yorkshire, BD6 2SZ. The Company is considered to be a qualifying entity (for the purposes of this FRS) and has applied the exemptions available under FRS 102 in respect of the following disclosures, which it anticipates applying in its financial statements prepared under FRS 102:

- Cash Flow Statement and related notes;
- Key Management Personnel compensation; and
- Transactions between wholly-owned subsidiaries, or with their parent.

As the consolidated financial statements of Kelda Eurobond Co Limited include the equivalent disclosures, the Company has also taken certain exemptions under FRS 102 available in respect of the disclosures required by FRS 102.11 Basic Financial Instruments and FRS 102.12 Other Financial Instrument Issues.

On first time adoption of FRS 102, the Company has not retrospectively changed its accounting under old UK GAAP for derecognition of financial assets and liabilities before the date of transition, hedge accounting for any hedging relationships that no longer existed at the date of transition, accounting estimates or discontinued operations.

Judgements made by the directors, in the application of these accounting policies that have significant effect on the financial information and estimates with a significant risk of material adjustment in the next year are discussed in note 10.

Measurement convention

The financial information is prepared on the historical cost basis except that the following assets and liabilities are stated at their fair value: derivative financial instruments, financial instruments classified at fair value through the profit or loss and certain categories of tangible fixed assets measured in accordance with the revaluation model.

Foreign currency

Transactions in foreign currencies are translated to the Company's functional currency at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are retranslated to the functional currency at the foreign exchange rate ruling at that date. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are retranslated to the functional currency at foreign exchange rates ruling at the dates the fair value was determined. Foreign exchange differences arising on translation are recognised in the profit and loss account.

Basic financial instruments

Trade and other debtors

Trade and other debtors are recognised initially at transaction price less attributable transaction costs. Subsequent to initial recognition they are measured at amortised cost using the effective interest method, less any impairment losses. If the arrangement constitutes a financing transaction, for example if payment is deferred beyond normal business terms, then it is measured at the present value of future payments discounted at a market rate of instrument for a similar debt instrument.

Trade and other creditors

Trade and other creditors are recognised initially at transaction price plus attributable transaction costs. Subsequent to initial recognition they are measured at amortised cost using the effective interest method. If the arrangement constitutes a financing transaction, for example if payment is deferred beyond normal business terms, then it is measured at the present value of future payments discounted at a market rate of instrument for a similar debt instrument.

Interest-bearing borrowings classified as basic financial instruments

Notes to the Financial Statements

For the six months ended 30 September 2015

Interest-bearing borrowings are recognised initially at fair value less attributable transaction costs. Subsequent to initial recognition, interest-bearing borrowings are stated at amortised cost using the effective interest method, less any impairment losses.

Investments in subsidiaries

Investments in subsidiaries are carried at cost less impairment.

Cash and cash equivalents

Cash and cash equivalents comprise cash balances and call deposits.

Other financial instruments

Financial instruments not considered to be basic financial instruments (Other financial instruments)

Other financial instruments not meeting the definition of basic financial instruments are recognised initially at fair value. Subsequent to initial recognition other financial instruments are measured at fair value with changes recognised in profit or loss except as follows:

- investments in equity instruments that are not publicly traded and whose fair value cannot otherwise be measured reliably shall be measured at cost less impairment; and
- hedging instruments in a designated hedging relationship shall be recognised as set out below.

Derivative financial instruments and hedging

Derivative financial instruments are recognised at fair value. Where hedge accounting is not applied, the gain or loss on remeasurement to fair value is recognised immediately in profit or loss, however, where derivatives qualify for hedge accounting, recognition of any resultant gain or loss depends on the nature of the item being hedged (see below).

Fair value hedges

Where a derivative financial instrument is designated as a hedge of the variability in fair value of a recognised asset or liability or an unrecognised firm commitment, all changes in the fair value of the derivative are recognised immediately in the profit and loss account. The carrying value of the hedged item is adjusted by the change in fair value that is attributable to the risk being hedged (even if it is normally carried at cost or amortised cost) and any gains or losses on remeasurement are recognised immediately in the profit and loss account (even if those gains would normally be recognised directly in reserves).

If hedge accounting is discontinued and the hedged financial asset or liability has not been derecognised, any adjustments to the carrying amount of the hedged item are amortised into the profit and loss account using the effective interest method over the remaining life of the hedged item.

The Company applies fair value hedge accounting to its cross currency interest rate swaps and associated bonds and its fixed to floating interest rate swaps and associated bonds.

Notes to the Financial Statements

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Cash flow hedges

Where a derivative financial instrument is designated as a hedge of the variability in cash flows of a recognised asset or liability, or a highly probable forecast transaction, the effective part of any gain or loss on the derivative financial instrument is recognised directly in other comprehensive income. Any ineffective portion of the hedge is recognised immediately in profit or loss.

For cash flow hedges, where the forecast transactions resulted in the recognition of a non-financial asset or non-financial liability, the hedging gain or loss recognised in other comprehensive income is included in the initial cost or other carrying amount of the asset or liability. Alternatively when the hedged item is recognised in the profit and loss account the hedging gain or loss is reclassified to the profit and loss account.

When a hedging instrument expires or is sold, terminated or exercised, or the entity discontinues designation of the hedge relationship but the hedged forecast transaction is still expected to occur, the cumulative gain or loss at that point remains in equity and is recognised in accordance with the above policy when the transaction occurs. If the hedged transaction is no longer expected to take place, the cumulative unrealised gain or loss recognised in equity is recognised in the profit and loss account immediately.

Fixed rate swaps in respect of finance leases were historically designated as cash flow hedges. However cash flow hedging is no longer applied as these hedges are now ineffective.

Tangible fixed assets

Infrastructure assets that had been revalued to fair value prior to the date of transition to FRS 102, are measured on the basis of deemed cost, being the revalued amount on the date of that revaluation. Post transition, the Company continues to adopt a policy of revaluation. Residential properties, non-specialised properties and rural estates held within land and buildings are held at valuation. Other tangible fixed assets are stated at cost less accumulated depreciation and accumulated impairment losses.

Where parts of an item of tangible fixed assets have different useful lives, they are accounted for as separate items of tangible fixed assets. Leases in which the Company assumes substantially all the risks and rewards of ownership of the leased asset are classified as finance leases. All other leases are classified as operating leases. Leased assets acquired by way of finance lease are stated on initial recognition at an amount equal to the lower of their fair value and the present value of the minimum lease payments at inception of the lease, including any incremental costs directly attributable to negotiating and arranging the lease. At initial recognition a finance lease liability is recognised equal to the fair value of the leased asset or, if lower, the present value of the minimum lease payments. The present value of the minimum lease payments is calculated using the interest rate implicit in the lease. Lease payments are accounted for as described on page 18.

The Company assesses at each reporting date whether tangible fixed assets are impaired.

Depreciation is charged to the profit and loss account on a straight-line basis over the estimated useful lives of each part of an item of tangible fixed assets. Leased assets are depreciated over the shorter of the lease term and their useful lives. Land is not depreciated. Assets in the course of construction are not depreciated until commissioned. The estimated useful lives are as follows:

Notes to the Financial Statements

For the six months ended 30 September 2015

Land and Buildings	
Buildings	25 - 100 years
Residential properties, non-specialised properties (revalued)	60 years
Rural estates (land) (revalued)	Not depreciated
Plant and equipment	
Fixed plant	5 - 40 years
Vehicles, mobile plant and computers	3 -10 years
Infrastructure assets	
Infrastructure assets - water mains and sewers	30 - 125 years
Infrastructure assets - earth banked dams and reservoirs	200 years

Depreciation methods, useful lives and residual values are reviewed if there is an indication of a significant change since last annual reporting date in the pattern by which the Company expects to consume an asset's future economic benefits.

Revaluation

Infrastructure assets, residential properties, non-specialised properties and rural estates are stated at fair value less any subsequent accumulated depreciation and impairment losses. Any increase in the carrying value of fixed assets arising as a result of a revaluation is recognised by first reversing any accumulated depreciation relating to the associated assets. Any remaining increase in carrying value after depreciation has been reversed is recognised as an increase in the cost of the associated assets.

FRS 102 requires assets to be valued by independent valuers on a periodic basis, which is adopted by the Company. An interim valuation is booked in the intervening years if there has been a material change. The last valuation of infrastructure assets was carried out on 31 March 2015. The last valuation of residential properties, non-specialised properties and rural estates held within land and buildings was carried out on 31 March 2014. The valuation of land and buildings carried out at 31 March 2014 was considered at 31 March 2015 by the directors, who concluded that current book values were not materially different to current market values.

The fair value of infrastructure assets was measured using a two step approach. Firstly the Company measured the value in use, using a discounted cash flow model. The discounted cash flow incorporates the future growth rates and an assumed discount rate. The business value in use less relevant working capital balances was then allocated to individual classes of fixed assets. This value in use method is considered the most reliable method to determine the current value for the tangible fixed assets.

The fair value of certain categories of land and buildings was measured on the basis of existing use.
Gains on revaluation are recognised in other comprehensive income and accumulated in the revaluation reserve. However, the increase is recognised in the profit and loss account to the extent that it reverses a revaluation decrease previously recognised in the profit and loss account.
Losses arising on revaluation are recognised in other comprehensive income to the extent of any previously recognised revaluation increase accumulated in equity, in respect of that asset. Any excess is recognised in the profit and loss account.

Contributions

Capital contributions - The Company is permitted by the regulator, Ofwat, to recover costs in relation to mains and sewer diversions, where requested by other counterparties. This is presented net within fixed assets, thus decreasing the cost of new components.

Notes to the Financial Statements

For the six months ended 30 September 2015

Intangible assets and goodwill

Goodwill is stated at cost less any accumulated amortisation and accumulated impairment losses. Goodwill is allocated to cash-generating units or groups of cash-generating units that are expected to benefit from the synergies of the business combination from which it arose.

Other intangible assets

Other intangible assets that are acquired by the Company are stated at cost less accumulated amortisation and less accumulated impairment losses.

Amortisation

Software is amortised on a straight line basis over its useful life. The useful life of software is estimated to be 5 years.
Goodwill is amortised on a straight line basis over its useful life. Goodwill has no residual value. The finite useful life of goodwill is estimated to be 19 years.

The Company reviews the amortisation period and method when events and circumstances indicate that the useful life may have changed since the last reporting date.

Goodwill is tested for impairment in accordance with FRS 102 Section 27 Impairment of assets when there is an indication that goodwill may be impaired.

Government grants

Government grants are included within accruals and deferred income in the balance sheet and credited to the profit and loss account over the expected useful lives of the assets to which they relate or in periods in which the related costs are incurred.

Stocks

Stocks are stated at the lower of cost and estimated selling price less costs to complete and sell. Cost includes expenditure incurred in acquiring the stocks, production or conversion costs and other costs in bringing them to their existing location and condition.

Impairment excluding stocks and deferred tax assets

Financial assets (including trade and other debtors)

A financial asset not carried at fair value through profit or loss is assessed at each reporting date to determine whether there is objective evidence that it is impaired. A financial asset is impaired if objective evidence indicates that a loss event has occurred after the initial recognition of the asset, and that the loss event had a negative effect on the estimated future cash flows of that asset that can be estimated reliably.

An impairment loss in respect of a financial asset measured at amortised cost is calculated as the difference between its carrying amount and the present value of the estimated future cash flows discounted at the asset's original effective interest rate. For financial instruments measured at cost less impairment, an impairment is calculated as the difference between its carrying amount and the best estimate of the amount that the Company would receive for the asset if it were to be sold at the reporting date. Interest on the impaired asset continues to be recognised through the unwinding of the discount. Impairment losses are recognised in profit or loss. When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through profit or loss.

Notes to the Financial Statements

For the six months ended 30 September 2015

Non-financial assets

The carrying amounts of the Company's non-financial assets, other than stocks and deferred tax assets are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For the purpose of impairment testing, assets that cannot be tested individually are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets (the "cash-generating unit"). The goodwill acquired in a business combination, for the purpose of impairment testing is allocated to cash-generating units, or ("CGU") that are expected to benefit from the synergies of the combination. For the purpose of goodwill impairment testing, if goodwill cannot be allocated to individual CGUs or groups of CGUs, the Company tests the impairment of goodwill by determining the recoverable amount of the entity in its entirety, including the integrated acquired operations.

An impairment loss is recognised if the carrying amount of an asset or its CGU exceeds its estimated recoverable amount. Impairment losses are recognised in profit or loss. Impairment losses recognised in respect of CGUs are allocated first to reduce the carrying amount of any goodwill allocated to the units, and then to reduce the carrying amounts of the other assets in the unit (group of units) on a pro rata basis.

An impairment loss is reversed if and only if the reasons for the impairment have ceased to apply.
Impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

Employee benefits

Defined contribution plans and other long term employee benefits

A defined contribution plan is a post-employment benefit plan under which the Company pays fixed contributions into a separate entity and will have no legal or constructive obligation to pay further amounts. Obligations for contributions to defined contribution pension plans are recognised as an expense in the profit and loss account in the periods during which services are rendered by employees.

Group plans

The Company's employees are members of a group wide defined benefit pension plan. As there is no contractual agreement or stated group policy for charging the net defined benefit cost of the plan to participating entities, the net defined benefit cost of the pension plan is recognised fully by the sponsoring employer of the plan, which is Kelda Group Limited. The Company recognises a cost equal to its contribution payable for the period as an expense.

Termination benefits

Termination benefits are recognised as an expense when the Company is demonstrably committed, without realistic possibility of withdrawal, to a formal detailed plan to either terminate employment before the normal retirement date, or to provide termination benefits as a result of an offer made to encourage voluntary redundancy. Termination benefits for voluntary redundancies are recognised as an expense if the Company has made an offer of voluntary redundancy, it is probable that the offer will be accepted, and the number of acceptances can be estimated reliably. If benefits are payable more than 12 months after the reporting date, then they are discounted to their present value.

Notes to the Financial Statements

For the six months ended 30 September 2015

Provisions

A provision is recognised in the balance sheet when the Company has a present legal or constructive obligation as a result of a past event, that can be reliably measured and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are recognised at the best estimate of the amount required to settle the obligation at the reporting date.
Where the Company enters into financial guarantee contracts to guarantee the indebtedness of other companies within its group, the Company considers these to be insurance arrangements and accounts for them as such. In this respect, the Company treats the guarantee contract as a contingent liability until such time as it becomes probable that the Company will be required to make a payment under the guarantee.

Turnover

Turnover comprises charges to customers for water, waste water and other services excluding value added tax and arises only in the United Kingdom.

Turnover is not recognised until the service has been provided to the customer. Turnover relates to charges due in the year, excluding any amounts paid in advance. Turnover for measured water charges includes amounts billed plus an estimation of the amounts unbilled at the year end. The accrual is estimated using a defined methodology based upon daily average water consumption, which is calculated based upon historical billing information.

No turnover is recognised for unoccupied properties and no bills are raised. If a bill has been issued, and the Company subsequently becomes aware that the property is unoccupied, the bill and relevant turnover is cancelled. Generally a property is classed as void if it is unoccupied and unfurnished.

Expenses

Operating lease

Payments (excluding costs for services and insurance) made under operating leases are recognised in the profit and loss account on a straight-line basis over the term of the lease unless the payments to the lessor are structured to increase in line with expected general inflation; in which case the payments related to the structured increases are recognised as incurred. Lease incentives received are recognised in profit and loss over the term of the lease as an integral part of the total lease expense.

Finance lease

Minimum lease payments are apportioned between the finance charge and the reduction of the outstanding liability using the rate implicit in the lease. The finance charge is allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability. Contingent rents are charged as expenses in the periods in which they are incurred.

Interest receivable and Interest payable

Interest payable and similar charges includes interest payable, movements in the fair value of financial instruments excluding those meeting hedging criteria, finance leases recognised in profit or loss using the effective interest method, and net foreign exchange losses that are recognised in the profit and loss account (see foreign currency accounting policy). Borrowing costs that are directly attributable to the acquisition, construction or production of an asset that takes a substantial time to be prepared for use, are capitalised as part of the cost of that asset.

Other interest receivable and similar income includes interest receivable on funds invested, movements in the fair value of financial instruments excluding those meeting hedging criteria and net foreign exchange gains.
Interest income and interest payable are recognised in profit or loss as they accrue, using the effective interest method. Dividend income is recognised in the profit and loss account on the date the Company's right to receive payments is established. Foreign currency gains and losses are reported on a net basis.

Notes to the Financial Statements

For the six months ended 30 September 2015

Dividends payable

Final dividends payable are recognised on approval of the dividend. Interim dividends are recognised on payment of the dividend.

Exceptional items

Exceptional items are items which derive from events or transactions that fall within the ordinary activities of the reporting entity and which individually or, if of a similar type, in aggregate need to be disclosed by virtue of their size or incidence if the financial information is to give a true and fair view.

Taxation

Tax on the profit or loss for the period comprises current and deferred tax. Tax is recognised in the profit and loss account except to the extent that it relates to items recognised directly in equity or other comprehensive income, in which case it is recognised directly in equity or other comprehensive income.

Current tax is the expected tax payable or receivable on the taxable income or loss for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided on timing differences which arise from the inclusion of income and expenses in tax assessments in periods different from those in which they are recognised in the financial information. The following timing differences are not provided for: differences between accumulated depreciation and tax allowances for the cost of a fixed asset if and when all conditions for retaining the tax allowances have been met. Deferred tax is not recognised on permanent differences arising because certain types of income or expense are non-taxable or are disallowable for tax or because certain tax charges or allowances are greater or smaller than the corresponding income or expense.

Deferred tax is measured at the tax rate that is expected to apply to the reversal of the related difference, using tax rates enacted or substantively enacted at the balance sheet date. For non-depreciable assets that are measured using the revaluation model, deferred tax is provided at the rates and allowances applicable to the sale of the asset/property, except when the asset has a limited useful life and the objective of the Company's business model is to consume substantially all of the value through use. In the latter case the tax rate that is expected to apply to the reversal of the related difference is used.
Unrelieved tax losses and other deferred tax assets are recognised only to the extent that is it probable that they will be recovered against the reversal of deferred tax liabilities or other future taxable profits.

Notes to the Financial Statements

For the six months ended 30 September 2015

2. Exceptional items

	30 September 2015 £m	30 September 2014 £m
Interest receivable and similar income		
Movement of fair value of combined cross currency interest rate swaps	**-**	13.0
Movement in fair value of cross currency debt	**6.7**	-
Movement of fair value of fixed to floating interest rate swaps	**-**	17.0
Movement in fair value of associated bonds	**17.5**	-
Movement of fair value of finance lease interest rate swap	**2.1**	-
Movement of fair value of index linked swaps	**79.8**	-
	106.1	30.0
Interest payable and similar charges		
Movement of fair value of index linked swaps	**-**	(94.7)
Movement of fair value of finance lease interest rate swap	**-**	(2.4)
Movement in fair value of fixed to floating interest rate swaps	**(10.4)**	-
Movement in fair value of associated bonds	**-**	(17.4)
Movement of fair value of combined cross currency interest rate swaps	**(9.7)**	-
Movement in fair value of cross currency debt	**-**	(12.1)
	(20.1)	(126.6)

The movement in the fair value of index linked swaps is a result of swaps which were taken out by the Company during 2007/08. These swaps hedge against movements in the retail price index (RPI) by receiving interest based on LIBOR and accruing interest payable based on RPI. The swaps have been valued at the reporting date at fair value, which at 30 September 2015 resulted in a £1,771.5m liability (31 March 2015: £1,858.3m liability). Of this, £1,628.8m (31 March 2015: £1,708.6m) is recognised within other financial liabilities (Note 8) and £142.7m (31 March 2015: £149.7m) is recognised within long term borrowings (Note 6).

Of the movement for the period of £86.8m income, a charge of £9.7m relating to RPI accretion has been recognised within finance costs, a credit of £79.8m has been recognised as an exceptional finance income and the net remaining movement of £16.7m was cash paid. Non cash changes in fair value of this instrument have been included in the profit and loss account as the specific circumstances which would allow it to be held in reserves have not been met and therefore hedge accounting has not been applied.

The movement in the fair value of finance lease swaps is a result of floating to fixed interest rate swaps taken out by the Company to hedge against movements in 12 month LIBOR interest rates on floating rate finance leases. The swaps hedge the movement in interest rates by receiving interest based on 12 month LIBOR and accruing interest payable at a fixed rate. The swaps have been valued at the reporting date at fair value, which at 30 September 2015 resulted in a £22.1m liability (31 March 2015: £24.2m). The decrease in the period in the liability of £2.1m has been recognised as an exceptional finance cost. This has been included in the profit and loss account as the specific circumstances which would allow it to be held in reserves were no longer met.

Exceptional finance payable includes the fair value movement of various combined cross currency interest rate swaps which were designated in fair value hedge relationships. The combined cross currency interest rate swaps have been valued at the reporting date at fair value. In line with FRS 102, the financial instruments to which the swaps relate have also been measured at fair value at 30 September 2015. The net impact of the fair value movement of the cross currency swaps and the associated bonds has resulted in a £3.0m charge to the profit and loss account.

Notes to the Financial Statements

For the six months ended 30 September 2015

Exceptional finance income includes the fair value movement of various fixed to floating interest rate swaps which were designated in fair value hedge relationships. These fair value interest rate swaps have been valued at the reporting date at fair value. In line with FRS102, the financial instruments to which the swaps relate have also been measured at fair value at 30 September 2015. The net impact of the fair value movement of the fixed to floating interest rate swaps and the associated bonds has resulted in a £7.1m credit to the profit and loss account.

3. Tax on profit on ordinary activities

	Unaudited six months ended	
	30 September 2015 £m	30 September 2014 £m
Current tax – current period	**0.1**	0.2
Current tax – prior year adjustment	**-**	(8.4)
Deferred tax – current period	**6.9**	(19.9)
Deferred tax – prior year adjustment	**-**	(3.0)
Tax charge/(credit)	**7.0**	(31.1)

4. Distributions paid

	30 September 2015 £m	30 September 2014 £m
Dividends paid during the period	**43.4**	47.5
Gross dividend paid	**43.4**	47.5
Dividends paid to holdings companies to fund payment of interest	**(34.7)**	(34.8)
Amounts retained to fund corporate costs	**(8.7)**	(12.7)
Available for distribution to ultimate shareholders	**-**	-

5. Creditors: amounts falling due after more than one year

	30 September 2015 £m	31 March 2015 £m
Interest-bearing loans and borrowings (note 6)	**570.3**	626.6
Amounts owed to group undertakings	**3,928.8**	3,889.9
Other creditors	**34.5**	32.8
Other financial liabilities (note 8)	**1,661.2**	1,739.4
Deferred grants and contributions on depreciating fixed assets	**393.3**	383.6
	6,588.1	6,672.3

Notes to the Financial Statements

For the six months ended 30 September 2015

6. Interest bearing loans and borrowings

	Bank loans and overdrafts 30 September 2015 £m	Other loans 30 September 2015 £m	Finance leases 30 September 2015 £m	Total 30 September 2015 £m
Short term borrowings:				
In one year or less or on demand	38.2	-	37.1	75.3
Long term borrowings:				
In more than one year, but not more than two years	37.2	-	49.6	86.8
In more than two years, but not more than five years	112.1	13.0	31.1	156.2
In more than five years	113.1	129.7	84.5	327.3
	262.4	142.7	165.2	570.3
Amounts owed to Group companies before fair value adjustment of bonds				3,887.6
Fair value adjustment of bonds owed to group companies				41.2
Total borrowings				**4,574.4**
Cash at bank and in hand				**(41.7)**
Amounts owed from group companies				**(1,009.0)**
Net debt at 30 Sep 2015				**3,523.7**

Net amounts owed to group companies include £1,009.0m receivable in relation to loans to parent companies. This is presented within debtor's receivable after more than one year.

Amounts owed to group companies includes loans from other members of the Yorkshire Water financing group relating to bonds originally held by Yorkshire Water Services Finance Limited, subsequently exchanged for bonds held by Yorkshire Water Services Odsal Finance Ltd.

Yorkshire Water raises debt as part of the Yorkshire Water financing group. This group of companies includes Yorkshire Water and its subsidiary companies. Debt covenants covering the financing group include the consolidated external debt of this group of companies. When calculating the consolidated debt position it should be noted that the book value recorded in these accounts on the internal loan relating to the exchanged bonds is higher than the book value recorded in Yorkshire Water Services Odsal Finance accounts by £32.7m (31 March 2015: £34.6m), which accounted for the exchanged bonds at their fair value at the date of exchange.

Net debt includes unamortised issue costs of £2.0m (31 March 2015: £2.4m).

Borrowings repayable in instalments after more than five years include £84.5m (31 March 2015: £85.5m) in respect of finance leases which have expiry dates ranging from 2032 to 2043 and carry interest rates based on 12 month LIBOR and 6 month LIBOR. The finance lease creditors are secured on the underlying assets.

Notes to the Financial Statements

For the six months ended 30 September 2015

As at 30 September 2015 Yorkshire Water had access to undrawn committed bank facilities totalling £745.4m (31 March 2015: £782.3m), £305.4m of which expire in April 2016 (31 March 2015: £305.4m) and £440.0m expire in October 2018 (31 March 2015: £490.0m). The cash at bank includes £8.9m of ring fenced cash relating to a swap collateral account (31 March 2015: £12.0m).

Of the total net debt, £587.2m (2014: £587.2m) relates to Class B debt.

7. Reconciliation of movement in adjusted net debt

	Audited At 31 March 2015 £m	Cash movements £m	Non cash movements £m	**Unaudited At 30 September 2015 £m**	Unaudited At 30 September 2014 £m
Short term deposits	35.2	6.5	-	**41.7**	38.5
Cash and cash equivalents	35.2	6.5	-	**41.7**	38.5
Loans due within one year	(41.0)	2.8	-	**(38.2)**	(28.8)
Finance leases due within one year	(34.1)	31.7	(34.7)	**(37.1)**	(33.5)
Loans due after one year	(277.0)	14.6	-	**(262.4)**	(291.6)
Finance leases due after one year	(199.9)	-	34.7	**(165.2)**	(202.8)
Index linked swaps	(149.7)	16.7	(9.7)	**(142.7)**	(129.4)
External net debt	(701.7)	65.8	(9.7)	**(645.6)**	(686.1)
Amounts owed from parent companies	1,009.0	-	-	**1,009.0**	1,009.0
Amounts owed to subsidiary company	(3,889.9)	(48.3)	9.4	**(3,928.8)**	(3,873.4)
	(2,880.9)	(48.3)	9.4	**(2,919.8)**	(2,864.4)
Total adjusted net debt	(3,547.4)	24.0	(0.3)	**(3,523.7)**	(3,512.0)

Index linked swaps of £142.7m (31 March 2015: £149.7m) represents £226.7m (31 March 2015: £234.8m) of RPI accretion discounted by £84.0m (31 March 2015: £85.1m) to reflect the net present value of the future liability.

Under the terms of the Common Terms Agreement (CTA), Compliance Certificates are completed for the YW Financing Group. The debt used to calculate net debt to RCV within the Compliance Certificates benefits from cash held by other members of the YW Financing Group that are removed on consolidation, excludes the discount of the RPI accretion on index linked swaps and excludes unamortised debt issue costs.

Notes to the Financial Statements

For the six months ended 30 September 2015

8. Other financial liabilities

	30 September 2015 £m	31 March 2015 £m
Derivative financial assets:		
Fixed to floating interest rate swaps	**28.6**	39.0
Combined cross currency interest rate swaps	**22.2**	28.8
	50.8	67.8
Financial liabilities:		
Finance lease interest swaps	**(22.1)**	(24.2)
Inflation linked swaps	**(1,628.8)**	(1,708.6)
Combined cross currency interest rate swaps	**(9.6)**	(6.6)
Energy swap	**(0.7)**	-
	(1,661.2)	(1,739.4)

Interest rate swaps

Yorkshire Water holds £45.0m notional value of floating to fixed rate interest swaps. These swaps are recognised at a fair value liability of £22.1m at 30 September 2015 (31 March 2015: £24.2m). Hedge accounting has not been applied.

Yorkshire Water holds £430.0m notional value of fixed to floating rate interest swaps. These swaps are recognised at a fair value asset of £28.6m at 30 September 2015 (31 March 2015: £39.0m). Hedge accounting has been applied.

Cross currency interest rate swaps

Yorkshire Water hedges the fair value of the US dollar notes using a series of combined interest rate and foreign currency swaps that in combination form cross currency interest rate swaps, swapping dollar principal repayments into sterling and fixed rate dollar interest payments into floating rate sterling interest payments. These swaps are recognised at a fair value asset of £22.2m at 30 September 2015 (31 March 2015: £28.8m). Hedge accounting has been applied.

Yorkshire Water hedges the fair value of the Australian dollar bond using a combined interest rate and foreign currency swap, swapping Australian dollar principal repayments into sterling and fixed rate Australian dollar interest payments into floating rate sterling interest payments. These swaps are recognised at a fair value liability of £9.6m at 30 September 2015 (31 March 2015: £6.6m). Hedge accounting has been applied.

Index linked swaps

The Company holds a number of index linked swaps, with a notional value of £1,289.0m (31 March 2015: £1,289.0m).
There are three cash flows associated with the swaps:

- six monthly interest receivable linked to LIBOR;
- six monthly interest payable linked to RPI; and
- an RPI-linked bullet that is payable on maturity of the instruments or at certain predetermined dates over the duration of the swaps.

Interest payments and receipts are accrued in the profit and loss account. The RPI bullet accumulated at the balance sheet date has been discounted using an appropriate rate applied to the specific life of the future accretion pay downs of the index linked swaps. This is accrued in the profit and loss account and recognised within long term borrowings.

Notes to the Financial Statements

For the six months ended 30 September 2015

With six month LIBOR and applicable discount rates at historically low levels in the short term, these swaps gave rise to a fair value liability of £1,771.5m at 30 September 2015 (31 March 2015: £1,858.3m). Of this, £142.7m has been recognised within long term borrowings, and represents the discounted value of the RPI bullet accrued to 30 September 2015 (31 March 2015: £149.7m). The remaining £1,628.8m is recognised within other financial liabilities (31 March 2015: £1,708.6m). The RPI bullet accrued to 30 September 2015 was £142.7m (31 March 2015: £149.7m) which has been reduced by £84.0m (31 March 2015: £85.1m) when discounted to present values.

Under the index linked swaps, Yorkshire Water has contracted to pay a fixed rate on an inflation accreting notional and in return receives 6 month GBP LIBOR on a semi-annual basis. The contractual obligations of approximately two thirds of Yorkshire Water's portfolio of index linked swaps require Yorkshire Water to pay the inflation accretion of the notional amount at maturity as a single "bullet" payment. The remaining (i.e. one third) require Yorkshire Water to make periodic payments of the inflation accretion on the notional amount throughout the life of each swap.

This payment profile at maturity increases the potential credit exposure for the counterparties involved. In order to mitigate this credit exposure, a number of these swaps are subject to mandatory termination clauses ("MTC"). Under the MTC the inflation linked swaps will automatically be terminated for a cash settlement amount at each MTC date unless both Yorkshire Water and the respective counterparty agree to extend the MTC date or restructure the existing transactions.

As at 31 March 2015 Yorkshire Water's portfolio of index linked swaps had a total fixed notional value of £1,289m and a total fair value liability of £1,858.3m. Of this amount approximately 35% of the total notional value was subject to MTCs. As at 30 September 2015 Yorkshire Water's portfolio of index linked swaps had a total fixed notional of £1,289m and a total fair value liability of £1,771.5m. Of this amount approximately 23% of the total notional of the portfolio was subject to MTCs (with the mandatory breaks occurring in February 2020, February 2023 and February 2025).

During the reporting period Yorkshire Water executed a number of transactions with various counterparties to restructure a portion of Yorkshire Water's index linked swap portfolio with a total fixed notional value of £160 million which removed the MTCs effective in February 2018.

The transactions removed the MTCs in return for an increase in the fixed real rate and this gave rise to an increase in the net mark to market at execution of £50m which is to be recognised in the income statement over the remaining life of the inflation linked swaps.

The valuation model used by Yorkshire Water to determine the fair value of the inflation linked swap portfolio as at 30 September 2015 includes a funding valuation adjustment, credit valuation adjustment and debit valuation adjustment to reflect the long term credit risk of Yorkshire Water's index linked swap portfolio. Reflecting this model and the inputs involved, some of the inflation linked swaps are now considered a level 3 valuation under IFRS13 and are disclosed accordingly.

9. Contingent liabilities

On 20 July 2015 an employee of the Company suffered a fatal accident while carrying out their duties. This is currently subject to a Police and Health and Safety Executive investigation. The duration, timing and outcome of this investigation are currently unknown.

Should the Company be found liable as a result of these investigations (which has not been indicated by any authority) it is possible it will be subject to fines, the size and timing of which are unknown due to the early stages of the investigation.

Notes to the Financial Statements

For the six months ended 30 September 2015

10. Accounting estimates and judgements

Key sources of estimation uncertainty

The directors consider the principal areas of judgement in this financial information to be:

- Fair value of financial instruments

The Company's accounting policy for financial instruments is detailed in note 1. In accordance with FRS 102 financial instruments are recognised in this financial information at fair value. The fair value of financial instruments that are not traded on an active market is determined using a discounted cash flow valuation technique. Management uses its judgement to make assumptions relating to future cash flows, mainly based on forward interest rates from observable yield curves at the end of the reporting period, counter-party funding adjustments and contract interest rates, discounted at a rate that reflects own or counter-party credit risk. The fair value of financial instruments would be £31.4m (31 March 2015: £15.0m) higher or lower were the counter-party funding assumption to change by 10 basis points. The fair value of financial instruments would be £47.9m (31 March 2015: £12.1m) higher or lower were the credit curve assumption to change by 10 basis points.

- Property, plant and equipment

The Company's accounting policy for property, plant and equipment (PPE) is detailed in note 1 of these financial statements. Estimated useful economic lives of PPE are based on management's judgement and experience. When management identifies that actual useful lives differ materially from the estimates used to calculate depreciation, that charge is adjusted prospectively. Due to the significance of capital investment to the Company, variations between actual and estimated useful lives could impact operating results both positively and negatively. Historically, only minor changes to estimated useful lives have been required. Certain categories of PPE are held at valuation based on value in use. Value in use is determined using a discounted cash flow model which requires management to make subjective judgements concerning the cash flows, growth rates and discount rates of the cash generating units under review.

The Company is required to evaluate the carrying value of PPE for impairment whenever circumstances indicate, in management's judgement, that the carrying value of such assets may not be recoverable.

- Provision for doubtful debts

At each balance sheet date, the Company evaluates the collectability of trade receivables and records provisions for impairment of receivables based on experience including, for example, comparisons of the relative age of accounts and consideration of actual write-off history. The actual level of debt collected may differ for the estimated levels of recovery, which could impact operating results positively or negatively. As at 30 September 2015 current trade receivables were £124.7m (31 March 2015: £120.0m), before provision for impairments.

- Taxation

Amounts recognised in respect of corporation tax reflects management's estimation of the amount of tax payable for fiscal years with open tax computations where liabilities remain to be agreed by HM's Revenue and Customs.

Notes to the Financial Statements

For the six months ended 30 September 2015

11. Explanation of transition to FRS 102 from Adopted UK GAAP

As stated in note 1, this financial information has been prepared on the basis expected to be applicable in the first set of financial statements prepared in accordance with FRS 102 for the year ended 31 March 2016. The accounting policies set out in note 1 have been applied in preparing the financial information for the year ended 31 March 2015 and the six month results ended 30 September 2014. The date of transition was 1 April 2014.

In preparing its FRS 102 balance sheet, the Company has adjusted amounts reported previously in financial statements prepared in accordance with its old basis of accounting (UK GAAP). An explanation of how the transition from UK GAAP to FRS 102 has affected the Company's reported financial performance and financial position is set out in the following tables.

Reconciliation of September 2015 interim income statement from old UK GAAP to FRS 102

	Note	*30 September 2015 UK GAAP* £m	*Adjustments to convert to FRS 102* £m	***30 September 2015 FRS 102*** **£m**
Turnover	(h), (i)	496.4	(2.9)	**493.5**
Operating costs	(f)-(i), (n)	(346.0)	9.4	**(336.6)**
Operating profit		150.4	6.5	**156.9**
Interest receivable and similar income		46.9	-	**46.9**
Exceptional fair value income	(a)-(e)	-	89.0	**89.0**
Interest payable and similar charges	(b), (f)	(138.2)	1.2	**(137.0)**
Exceptional fair value charges	(a)-(e)	-	(3.0)	**(3.0)**
Profit on ordinary activities before tax		59.1	93.7	**152.8**
Tax on profit on ordinary activities	(a)-(q)	2.9	(9.9)	**(7.0)**
Profit for the period		62.0	83.8	**145.8**

Notes to the Financial Statements

For the six months ended 30 September 2015

Reconciliation of September 2015 net assets from old UK GAAP to FRS 102

	Note	***30 September 2015*** **£m**
Net Assets old UK GAAP		2,972.2
Recognition of financial instruments	(a)-(e)	(1,115.2)
Capitalised borrowing costs	(f)	44.1
Accounting for infrastructure assets	(g)-(i)	(176.7)
Change in recognition of deferred taxation	(j)-(l)	(606.5)
Other	(n)	(0.9)
Taxation		(9.9)
Net Assets under FRS 102		**1,107.1**

Notes to the Financial Statements

For the six months ended 30 September 2015

Reconciliation of September 2014 interim profit/(loss) and equity from old UK GAAP to FRS 102

	Note	**Profit or loss for the period ended 30 September 2014 £m**	**Equity as at 31 March 2015 £m**	**Equity as at 1 April 2014 £m**
Amount under old UK GAAP		**90.1**	**2,953.5**	**2,561.5**
Recognise financial instrument re finance lease swap net of deferred tax	(a)	(1.9)	(19.4)	(12.6)
Recognise financial instrument re index linked swap net of deferred tax	(b)	(81.4)	(1,173.8)	(868.2)
Recognise financial instrument re cross currency interest rate swaps and fair value movement in associated bonds net of deferred tax	(c)	0.7	(1.2)	(4.6)
Recognise financial instrument re interest rate swaps and fair value movements in associated bonds net of deferred tax	(d)	(0.4)	(2.0)	(5.8)
Recognise financial instrument re energy derivative net of deferred tax	(e)	-	-	(5.1)
Capitalise borrowing costs net of deferred tax	(f)	12.1	39.5	50.0
Remove impact of infrastructure renewals accounting and apply FRS 102 compliant accounting net of deferred tax	(g)	23.8	(2.9)	10.4
Recognise assets transferred from customers - adopted sewers and mains	(h)	-	(148.9)	(119.1)
Recognise assets transferred from customers - requisitioned service charges	(i)	0.1	(28.5)	(14.2)
Recognise deferred tax on revaluation of infrastructure asset at 31 March 2012 (deemed cost of the infrastructure assets)	(j)	2.3	(305.2)	(305.2)
Removal of discounting on deferred tax disallowed under FRS 102	(k)	4.5	(254.4)	(280.2)
Recognise deferred tax on land and buildings revaluation	(l)	-	(3.4)	(3.4)
Infrastructure charge receipts net of deferred tax	(m)	-	0.1	(0.2)
Operating leases – spread over life of lease net of deferred tax	(n)	-	(1.1)	(1.2)
Recognise deferred tax on rolled over gains	(o)	-	(0.1)	(0.1)
Recognise deferred tax on revaluation of infrastructure assets at 31 March 2015	(p)	-	(46.8)	-
Depreciation on revaluation on infrastructure assets at 31 March 2012	(q)	(11.5)	-	-
Amount under FRS 102		**38.4**	**1,005.4**	**1,002.0**

There are no movements in Other Comprehensive Income for the 6 month period ended 30 September 2014.

Notes to the Financial Statements

For the six months ended 30 September 2015

Notes to the reconciliation of profit/(loss)

a) FRS 102 requires derivative financial instruments to be recognised at fair value. The Company holds floating to fixed rate interest rate swaps in respect of finance leases. Previously under UK GAAP the Company did not recognise these instruments in the financial statements. Upon transition, a liability has been recognised at fair value.

b) FRS 102 requires derivative financial instruments to be recognised at fair value. The Company holds inflation linked swaps. Previously under UK GAAP the Company did not recognise these instruments in the financial statements at fair value but rather at amortised cost, that being the fair value of the swaps when they were transferred to the Company from a fellow subsidiary of the Kelda Holdings Limited group in August 2008. Upon transition, a liability has been recognised at the fair value of the swaps on the transition date, with any subsequent changes in the fair value of the swaps recognised in the income statement as an exceptional interest item. Hedge accounting is not applied or available under FRS102 for these swaps.

c) FRS 102 requires derivative financial instruments to be recognised at fair value. The Company hedges the fair value of the US dollar bonds using a series of combined rate and foreign currency swaps that in combination form cross currency interest rate swaps, swapping dollar principal repayments into sterling, and fixed rate dollar interest payments into floating rate sterling interest payments. The Company also hedges the fair value of the Australian dollar bond using a combined interest rate and foreign currency swap, swapping Australian dollar principal repayments into sterling, and fixed rate Australian dollar interest payments into floating rate sterling interest payments. Previously under UK GAAP the Company did not recognise these instruments in the financial statements, nor any adjustment in the fair value of the bonds. Upon transition, a liability has been recognised at fair value. As both during the year, and since inception, the hedge was at least 95% effective in hedging the fair value exposure to interest rate movements and foreign currency exposure, the carrying amount of the bonds was also adjusted for fair value movements.

d) FRS 102 requires derivative financial instruments to be recognised at fair value. The Company holds fixed to floating rate interest rate swaps. These are designated as fair value hedges of fixed rate bonds of the same value. Previously under UK GAAP the Company did not recognise these instruments in the financial statements, nor any adjustment in the fair value of the bonds. Upon transition a liability has been recognised at fair value. As both during the year, and since inception, the hedge was at least 95% effective in hedging the fair value exposure to interest rate movements, the carrying amount of the bonds was also adjusted for fair value movements.

e) FRS 102 requires derivative financial instruments to be recognised at fair value. The Company held an energy derivative. Previously under UK GAAP the Company did not recognise these instruments in the financial statements. Upon transition a liability has been recognised at fair value.

f) FRS 102 permits the capitalisation of borrowing costs. Previously under UK GAAP the Company did not capitalise borrowing costs. Upon transition, these have been capitalised and depreciated at the same rate as the underlying asset.

g) FRS 102 does not permit renewals accounting for infrastructure assets. Previously under UK GAAP renewals accounting has been applied. Upon transition, the previous valuation at 31 March 2012 has been applied as deemed cost and post revaluation movements are accounted for in accordance with FRS 102.17. Thus, infrastructure assets have been depreciated and renewals accounting is disallowed. As a result, expenditure incurred in maintaining the infrastructure network are only capitalised if they meet the definition of an asset under FRS 102.17 and depreciated over an appropriate useful economic life. Any expenditure incurred which does not meet the definition of an asset is recognised in the profit and loss as incurred.

Notes to the Financial Statements

For the six months ended 30 September 2015

h) FRS 102 does not give specific guidance on contributions from customers. In its absence, management has applied the requirement and guidance of FRS 102 on similar and related issues and considered treatment under EU-IFRS. Previously, under UK GAAP, assets transferred from customers in relation to adopted sewers and mains have been recognised at £nil cost. Upon transition, the Company has recognised the adopted sewers and mains at fair value with a corresponding amount of deferred income. The assets are depreciated over their expected useful economic life and the associated deferred income is released to the profit and loss at the same rate.

i) FRS 102 does not give specific guidance on contributions from customers. In its absence, management has applied the requirement and guidance of FRS 102 on similar and related issues and considered treatment under EU-IFRS. Previously under UK GAAP, assets transferred from customers in relation to requisitioned service charges have been recognised as income at the same time as the connection costs are incurred, resulting in assets effectively recognised at £nil cost. This is where the Company installs a new service pipe and meter, which are connected by the Company to the water main. The developer or customer is charged a service connection charge. A contribution is received from the developer for the cost of connection. Upon transition, the Company has recognised the requisitioned service charges at fair value with a corresponding amount of deferred income.

j) Revaluation of infrastructure assets - under previous UK GAAP a company was only required to recognise a deferred tax liability (where an asset stood to produce a gain on its disposal) or deferred tax asset (where an asset stood to produce a loss on its disposal) if the company had entered into a binding sale agreement in relation to the relevant asset. Under FRS 102, there is no such requirement and deferred tax must be provided in relation to the potential tax that would arise on disposal of the Company's assets. As such, deferred tax has been recognised on the revaluation of infrastructure assets as at 31 March 2012 (being the deemed cost of the asset on transition).

k) Under previous UK GAAP discounting of deferred tax balances was permitted. Deferred tax balances have been restated without any discounting as, under FRS 102, discounting of deferred tax is prohibited.

l) Revaluation of land and buildings - under previous UK GAAP a company was only required to recognise a deferred tax liability (where an asset stood to produce a gain on its disposal) or deferred tax asset (where an asset stood to produce a loss on its disposal) if the company had entered into a binding sale agreement in relation to the relevant asset. Under FRS 102, there is no such requirement and deferred tax must be provided in relation to the potential tax that would arise on disposal of the Company's assets. As such, deferred tax has been recognised on the revaluation of land and buildings as at 31 March 2014.

m) The Company charges infrastructure charges for new connections to the network. Previously under UK GAAP, these have been included in the cost of infrastructure as a reduction to the cost of the asset. Under FRS 102, these receipts have been deferred over the period during which a customer is consuming the benefit from these infrastructure charge receipts. These are recognised as revenue over the life of the network or capital program cycle.

n) Under previous UK GAAP operating lease incentives, including rent free periods are recognised on a straight-line basis as a reduction of the rental expense, over the shorter of the lease term and the period to the first rent review. It is common practice under previous UK GAAP to recognise guaranteed increases in rentals as incurred. Under FRS 102, guaranteed increases in rentals and lease incentives are generally recognised over the entire lease term and a transition adjustment has been made to recognise this difference.

o) Chargeable gains have been rolled over into certain fixed assets held by the Company. Whilst there was an exemption from recognising the deferred tax liability that will arise on a future disposal of such assets under UK GAAP as a binding sale agreement in relation to the relevant asset is necessary, there is no such exemption under FRS 102. As such deferred tax is recognised in relation to the relevant rolled over gains.

Notes to the Financial Statements

For the six months ended 30 September 2015

p) Revaluation of infrastructure assets - under previous UK GAAP a company was only required to recognise a deferred tax liability (where an asset stood to produce a gain on its disposal) or deferred tax asset (where an asset stood to produce a loss on its disposal) if the company had entered into a binding sale agreement in relation to the relevant asset. Under FRS 102, there is no such requirement and deferred tax must be provided in relation to the potential tax that would arise on disposal of the Company's assets. As such, deferred tax has been recognised on the revaluation of infrastructure assets as at 31 March 2015.

q) Depreciation of revaluation of infrastructure assets as at 31 March 2012.

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