Kelda Finance (No.1) Limited

Condensed Consolidated Interim Financial Statements

For the 6 month period ended 30 September 2018

Contents

Information to accompany the Condensed Consolidated Interim Financial Statements

The consolidated results for Kelda Finance (No.1) Limited for the six month period ended 30 September 2018 are presented in this report.

These interim statements have been prepared in accordance with International Financial Reporting Standards (IFRS).

Kelda Finance (No.1) Limited is the holding company of a group including Kelda Finance (No.2) Limited, Kelda Finance (No.3) PLC, Yorkshire Water Services Holdings Limited and its subsidiary companies.

Group Condensed Consolidated Statement of Profit and Loss

For the 6 month period ended 30 September 2018

	Note	**Unaudited 6 month period ended 30 Sep 2018 £m**	Unaudited 6 month period ended 30 Sep 2017 £m
Group revenue		**529.4**	513.0
Operating costs before exceptional items		**(382.6)**	(362.5)
Exceptional items	*2*	**(18.9)**	(4.2)
Group operating profit from continuing operations		**127.9**	146.3
Finance income		**62.0**	49.1
Exceptional finance income	*2*	**30.5**	129.7
Finance costs		**(164.5)**	(174.2)
Exceptional finance costs	*2*	**(43.7)**	(37.9)
Profit from continuing operations before taxation		**12.2**	113.0
Tax charge on continuing operations	*3*	**(2.9)**	(15.8)
Profit for the period from continuing operations		**9.3**	97.2
Profit from discontinued operations net of tax	*4*	**0.1**	-
Profit for the period		**9.4**	97.2

Group Condensed Consolidated Statement of Other Comprehensive Income

For the 6 month period ended 30 September 2018

	Unaudited 6 month period ended 30 Sep 2018 £m	Unaudited 6 month period ended 30 Sep 2017 £m
Profit for the period	**9.4**	97.2
Other comprehensive income for the period	**-**	-
Total comprehensive income for the period	**9.4**	97.2

Group Condensed Consolidated Statement of Financial Position

As at 30 September 2018

	Note	**Unaudited at 30 Sep 2018 £m**	Audited at 31 Mar 2018 £m
Non-current assets			
Intangible assets		**72.4**	68.5
Property, plant and equipment		**7,697.0**	7,603.9
Financial assets	8	**107.2**	88.2
Trade and other receivables		**1,187.5**	1,191.6
		9,064.1	8,952.2
Current assets			
Inventories		**3.0**	3.0
Trade and other receivables		**197.3**	168.0
Cash and cash equivalents	6	**47.4**	41.2
Assets held for sale	7	**62.8**	58.5
		310.5	270.7
Total Assets		**9,374.6**	9,222.9
Current liabilities			
Trade and other payables		**(344.8)**	(336.9)
Deferred grants and contributions on depreciated assets		**(10.4)**	(10.0)
Short term borrowings	6	**(224.9)**	(279.9)
Liabilities associated with assets held for sale	7	**(10.0)**	(6.4)
		(590.1)	(633.2)
Non-current liabilities			
Long term borrowings	6	**(5,261.0)**	(5,055.1)
Long term payables		**(6.3)**	(5.6)
Financial liabilities	8	**(1,791.3)**	(1,779.6)
Deferred grants and contributions on depreciated assets		**(438.0)**	(433.5)
Provisions		**(0.4)**	(0.4)
Deferred tax liabilities		**(420.4)**	(424.2)
		(7,917.4)	(7,698.4)
Total liabilities		**(8,507.5)**	(8,331.6)
Net assets		**867.1**	891.3
Equity			
Share capital	11	**-**	-
Revaluation reserve		**605.8**	605.8
Retained earnings		**261.3**	285.5
Total equity		**867.1**	891.3

Group Condensed Consolidated Statement of Cash Flows

For the 6 month period ended 30 September 2018

	Note	**Unaudited 6 month period ended 30 Sep 2018 £m**	Unaudited 6 month period ended 30 Sep 2017 £m	Audited year ended 31 Mar 2018 £m
Cash flows from operating activities	9	**271.7**	317.6	557.7
Income taxes (paid)/received		**(11.5)**	-	0.1
Interest paid	10	**(134.8)**	(140.2)	(239.0)
Net cash generated from operating activities		**125.4**	177.4	318.8
Cash flows from investing activities				
Interest received	10	**57.1**	45.4	109.4
Proceeds on disposals of property, plant and equipment		**2.5**	2.7	3.0
Purchases of property, plant and equipment		**(255.6)**	(204.1)	(439.0)
Capital grants and contributions		**9.6**	13.5	26.9
Net cash used in investing activities		**(186.4)**	(142.5)	(299.7)
Cash flows from financing activities				
Dividends paid	5	**(27.6)**	(36.6)	(74.4)
Borrowings raised (net of fees)		**183.2**	530.7	390.0
Repayment of borrowings		**(82.7)**	(431.2)	(322.3)
Repayments of obligations under finance leases and hire purchase agreements		**(9.8)**	(8.4)	(11.0)
Repayment of loan from parent company		**4.1**	-	57.2
Amount payable upon restructure of index-linked swaps		**-**	(250.0)	(250.0)
Net cash from/(used in) financing activities		**67.2**	(195.5)	(210.5)
Net increase/(decrease) in cash and cash equivalents		**6.2**	(160.6)	(191.4)
Cash and cash equivalents at the start of the period		**41.2**	232.6	232.6
Cash and cash equivalents at the end of the period	6	**47.4**	72.0	41.2

Group Condensed Consolidated Statement of Changes in Equity

For the 6 month period ended 30 September 2018

	Ordinary shares	Hedging reserve	Revaluation reserve	Retained earnings	Total equity
	£m	£m	£m	£m	£m
At 31 March 2018, as reported	**-**	**-**	**605.8**	**285.5**	**891.3**
Adjustment from adoption of IFRS 9	**-**	**-**	**-**	**(6.0)**	**(6.0)**
Restated at 31 March 2018	**-**	**-**	**605.8**	**279.5**	**885.3**
Profit for the period	-	-	**-**	9.4	9.4
Dividends paid	-	-	**-**	(27.6)	(27.6)
At 30 September 2018	-	-	605.8	261.3	867.1

	Ordinary shares	Hedging reserve	Revaluation reserve	Retained earnings	Total equity
	£m	£m	£m	£m	£m
At 31 March 2017, as reported	-	(13.2)	440.6	297.6	725.0
Profit for the period	-	-	-	97.2	97.2
Dividends paid	-	-	-	(36.6)	(36.6)
At 30 September 2017	-	(13.2)	440.6	358.2	785.6

Notes to the Condensed Consolidated Interim Financial Statements

For the six month period ended 30 September 2018

1. Basis of preparation and accounting

The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS).

The accounting policies, methods of computation and presentation are consistent with those used for the audited financial statements of Kelda Finance (No.1) Limited for the year ended 31 March 2018 except for the adoption of new standards effective as of 1 January 2018. The group has not early-adopted any other standard, interpretation or amendment that has been issued but is not yet effective.

These interim financial statements consolidate the results of Kelda Finance (No.1) Limited, Kelda Finance (No.2) Limited, Kelda Finance (No.3) PLC, Yorkshire Water Services Holdings Limited and its subsidiary companies for the six months ended 30 September 2018.

New standards and interpretations

The group applies, for the first time, IFRS 15 'Revenue from Contracts with Customers' and IFRS 9 'Financial Instruments'. The transition disclosures can be found in note 13. The changes to the accounting policies are set out below:

IFRS 15 – Revenue from contracts with customers

IFRS 15 establishes a comprehensive framework for determining whether, how much and when revenue is recognised, and replaces IAS 18 – revenue, and IFRIC 18 – transfers of assets from customers.

The principles of IFRS 15 have been applied using the five step model:

1. Identify the contract with a customer
2. Identify the performance obligations in the contract
3. Determine the transaction price
4. Allocate the transaction price to the performance obligations in the contract
5. Recognise revenue when or as the entity satisfies its performance obligations.

Revenue is recognised either when the performance obligation in the contract has been performed ("point in time") or "over time" as control of the performance obligation is transferred to the customer.

Notes to the Condensed Consolidated Interim Financial Statements

1. Basis of preparation and accounting

The details of the new significant accounting policies and the nature of the changes to previous accounting policies in relation to the group's material revenue streams are set out below:

Type of service	IFRS 15 treatment	Nature of change in accounting policy and impacts
Provision of water and waste water services	For the group's main revenue stream the performance obligations are clear, that being the supply of clean water and the collection of waste water. Revenue from these core activities is recognised at a point in time, consistent with previous treatment.	Revenue for which recoverability is not probable has been derecognised under IFRS 15. The nature of this adjustment is set out in note 13.
New connections	Revenue from new connections is recognised over the useful economic life of the asset, consistent with previous treatment.	None
Infrastructure charges	Infrastructure charges are intrinsically linked with new connection charges. The infrastructure charge facilitates the provision of water and waste water services, as well as the connection activities, and the ongoing maintenance of the connection. The infrastructure charge on its own is without material value to the customer without the provision of water and waste water services. Revenue from new connections is recognised over the useful economic life of the asset, consistent with previous treatment.	None
Diversions	In some instances, Yorkshire Water are requested to make diversions to the network. Income is received from the requestors. Revenue from diversions activity is recognised over the time taken to complete the diversion.	Revenue was previously recognised within fixed assets, under IFRIC 18. The transition has resulted in the reclassification of the revenue and associated costs from fixed assets, to the profit and loss account, with an element of deferred income on the balance sheet. The nature of this adjustment is set out in note 13.

Notes to the Condensed Consolidated Interim Financial Statements

1. Basis of preparation and accounting (continued)

IFRS 9 – Financial Instruments

IFRS 9 Financial Instruments replaces IAS 39 Financial Instruments: Recognition and Measurement for periods beginning on or after 1 January 2018, bringing together all three aspects of accounting for financial instruments: classification and measurement; impairment; and hedge accounting.

On transition to IFRS 9, the key change in the group's accounting policy for financial instruments is to recognise the gain or loss on a non-substantial modification of debt through the profit and loss account, amortised over the life of the financial liability through the effective interest rate. The nature of this adjustment is set out in note 13.

In relation to the impairment of financial assets, IFRS 9 requires an expected credit loss model as opposed to an incurred credit loss model under IAS 39. The expected credit loss model requires the group to account for expected credit losses and changes in those expected credit losses at each reporting date to reflect changes in credit risk since initial recognition of the financial assets. In other words, it is no longer necessary for a credit event to have occurred before credit losses are recognised.

As at 1 April 2018, the directors of the company reviewed and assessed the group's existing trade receivables for impairment using reasonable and supportable information that is available without undue cost or effort in accordance with the requirements of IFRS 9 to determine the credit risk of the respective items at the date they were initially recognised. There is no material change to the amount of the provision after undertaking of this exercise.

Estimates and Judgements

The estimates and judgements applied in preparing these financial statements are largely consistent with those applied in the annual report and financial statements for the year ending 31 March 2018. The calculation of the bad debt provision is no longer included as an area of critical estimation uncertainty, as only a significant alteration to the estimate would result in a material change to the provision. There has also been an additional judgement made, on initial application of IFRS 15 being:

The Group provide water connections to new build residential properties. Currently the accounting treatment is to defer the income on the balance sheet over the 50 year life of the associated asset. The Group consider the payment to be a contribution to the future costs of maintaining the asset, and therefore deferral of the income over the asset life appears appropriate.

Infrastructure charges relate to amounts paid by developers at the time that a connection of a domestic property to the water/wastewater network is made for the first time. These amounts represent a contribution to future reinforcement of the wider network, recognising that increased demand is placed on the network as more properties are connected, and therefore reinforcement works will be required in the future in order to ensure that the network is fit for purpose and can continue to deliver the required level of service provision across the total customer base. Due to the clear link to the network assets, deferral of the associated revenue appears to be the most appropriate treatment.

Notes to the Condensed Consolidated Interim Financial Statements

1. Basis of preparation and accounting (continued)

Impact of standards issued but not yet applied by the entity

The group anticipates that IFRS 16 – ‘leases’, effective from 1 April 2019, will not have a material impact on the financial statements. The key effect of this standard will be to require the group to create a long term depreciating ‘right of use’ asset and corresponding lease liability for leases currently classified as operating leases and charged over the lease term in accordance with the current standard IAS 17 – ‘Leases’. Short-term and small value leases are excluded from the revised standard. This will result in increases to non-current assets and liabilities on the statement of financial position, and increases in depreciation and finance expense and a decrease in operating expenses in the income statement.

Notes to the Condensed Consolidated Interim Financial Statements

2. Exceptional finance income and costs

	Unaudited 6 month period ended 30 Sept 2018 £m	Unaudited 6 month period ended 30 Sept 2017 £m
Included in operating profit		
Operating costs	**(18.9)**	(4.2)
Interest receivable and similar income		
Movement in fair value of combined cross currency interest rate swaps	**18.2**	-
Movement in fair value of cross currency debt	**-**	24.7
Movement in fair value of debt associated with fixed to floating interest rate swaps	**10.9**	12.9
Movement in fair value of finance lease interest rate swap	**1.4**	1.5
Movement in fair value of inflation linked swaps	**-**	90.6
	30.5	129.7
Interest payable and similar charges		
Movement in fair value of combined cross currency interest rate swaps	**-**	(16.0)
Movement in fair value of cross currency debt	**(21.1)**	-
Movement in fair value of fixed to floating interest rate swaps	**(9.6)**	(11.8)
Movement in fair value of inflation linked swaps	**(13.0)**	(10.1)
	(43.7)	(37.9)

Exceptional operating costs

In the six month period the company has incurred £3.9m operational costs associated with the assets damaged in the flooding incident that occurred in December 2015. (£4.2m in the six month period ended 30 September 2017). In addition, £15.0m of operational costs associated with the severe weather conditions, (a period of unusually low temperatures and heavy snowfall followed by the prolonged dry summer) have been incurred to date.

Notes to the Condensed Consolidated Interim Financial Statements

2. Exceptional finance income and costs (continued)

Movement in the fair value of cross currency swaps and associated debt

The group holds a number of combined cross currency interest rate swaps which have been designated in fair value hedge relationships and have been valued at the reporting date at fair value. In line with IFRS 9, the financial instruments to which the swaps relate have also been measured at fair value at 30 September 2018. The fair value movement of the combined cross currency interest rate swaps has resulted in £18.2m income (six month period ended 30 September 2017: £16.0m expense) to the profit and loss account. This is offset by the fair value movement in the associated debt of £21.1m expense (six month period ended 30 September 2017: £24.7m income). The net impact to the profit and loss account is £2.9m of cost (six month period ended 30 September 2017: £8.7m income).

Movement in the fair value of fixed to floating interest rate swaps

The group holds a number of fixed to floating interest rate swaps which are designated as fair value hedge relationships and have been valued at the reporting date at fair value. In line with IFRS 9, the financial instruments to which these fixed to floating interest rate swaps relate to have also been measured at fair value at 30 September 2018. The fair value movement of fixed to floating interest rate swaps has resulted in £9.6m expense (six month period ended 30 September 2017: £11.8m) to the profit and loss account. This is offset by £10.9m income (six month period ended 30 September 2017: £12.9m). This is a net impact to the profit and loss account of £1.3m of income (six month period ended 30 September 2017: £1.1m).

Movement in the fair value of finance lease swaps

The group has two floating to fixed interest rate swaps that have been taken out by the company to hedge against movements in the 12 month London Interbank Offered Rate (LIBOR) interest rates on floating rate finance leases. The finance lease 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 2018 resulted in a £19.9m liability (31 March 2018: £21.3m). The decrease of the liability in the six month period to 30 September 2018 of £1.4m (six month period ended 30 September 2017: £1.5m) has been recognised as exceptional fair value income. 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.

Movement in the fair value of inflation linked swaps

Inflation linked swaps have been valued at the reporting date at fair value, which at 30 September 2018 resulted in a £1,955.2m liability (31 March 2018; £1,926.2m liability). Of this, £1,767.1m (31 March 2018: £1,754.1m) is recognised within other financial liabilities (note 8) and £188.1m (31 March 2018: £172.1m) is recognised within long-term borrowings (note 6).

This six month period has seen the liability on the inflation linked swaps increase by £29.0m (six month period ended 30 September 2017: £306.8m decrease), with £13.0m cost disclosed in note 2 as an exceptional item, (six month period ended 30 September 2017: £80.5m net income). Of this amount, £31.0m relates to the six month period increase in the fair value amount, offset by £18m that relates to an inflation linked swap restructuring transaction that occurred during July 2018.

Notes to the Condensed Consolidated Interim Financial Statements

3. Tax charge

		Unaudited 6 month period ended 30 Sep 2018 £m	Unaudited 6 month period ended 30 Sep 2017 £m
Tax relating to continuing operations:	Current tax charge	**(6.8)**	-
	Adjustments in respect of prior periods	**0.2**	-
	Total current tax charge	**(6.6)**	-
	Deferred tax credit/(charge)	**3.7**	(15.8)
	Total tax charge	**(2.9)**	(15.8)

The current tax charge comprises corporation tax calculated at the estimated effective tax rates for the year.

Notes to the Condensed Consolidated Interim Financial Statements

4. Discontinued operations

At 31 March 2018, the group classified the non-household retail element of Yorkshire Water Services as held for sale (see note 7).

Results from discontinued operation

	Unaudited 6 month period ended 30 Sep 2018 £m	Unaudited 6 month period ended 30 Sep 2017 £m
Revenue	**5.0**	-
Expenses	**(4.9)**	-
Profit before tax	**0.1**	-
Income tax expense	**-**	-
Profit after tax	**0.1**	-

The profit after tax from the discontinued operation of £0.1m (6 month period ended 30 September 2017: £:nil) is attributable entirely to the owners of the group.

5. Dividends paid

	Unaudited 6 month period ended 30 Sep 2018 £m	Unaudited 6 month period ended 30 Sep 2017 £m
Cash dividends	**27.6**	36.6
Total dividends	**27.6**	36.6

Notes to the Condensed Consolidated Interim Financial Statements

6. Analysis of net debt

	Unaudited at 30 Sep 2018 £m	Audited at 31 Mar 2018 £m
Cash and cash equivalents:		
Cash at bank and in hand	**25.1**	7.1
Short term deposits	**22.3**	34.1
	47.4	41.2
Short term borrowings:		
Bank loans	**(55.8)**	(47.3)
Finance leases	**(14.1)**	(12.6)
Other borrowings	**(155.0)**	(220.0)
	(224.9)	(279.9)
Long term borrowings:		
Bank loans	**(528.9)**	(371.0)
Fixed rate guaranteed bonds due in less than 5 years	**(955.2)**	(755.4)
Fixed rate guaranteed bonds due in more than 5 years	**(1,806.2)**	(2,004.9)
Index linked guaranteed bonds due in more than 5 years	**(1,324.7)**	(1,303.7)
Fixed rate US Dollar bonds due in less than 5 years	**(205.6)**	(192.5)
Fixed rate US Dollar bonds due in more than 5 years	**(133.4)**	(125.7)
Fixed rate AUS Dollar bonds due in more than 5 years	**(30.0)**	(29.6)
Index linked swaps	**(188.1)**	(172.1)
Finance leases	**(88.9)**	(100.2)
	(5,261.0)	(5,055.1)
Amounts owed by parent entities	**768.8**	768.8
Total net debt	**(4,669.7)**	(4,525.0)

The long term bank loans stated above include £255.5m (£260.0m loan less £4.5m unamortised issue costs) held at Kelda Finance (No.2) Limited. Fixed rate guaranteed bonds due in less than 5 years includes £199.0m (£200.0m bond less unamortised issue costs of £1.0m) held at Kelda Finance (No.3) PLC. All other long term borrowings are held within the Yorkshire Water Services Holdings Limited group of companies.

Notes to the Condensed Consolidated Interim Financial Statements

6. Analysis of net debt (continued)

Net debt at 30 September 2018 includes £768.8m of amounts due from group companies (31 March 2018: £768.8m).

Index linked swaps of £188.1m (31 March 2018: £172.1m), represent £289.1m (31 March 2018: £268.2m) of RPI accretion discounted by £101.0m (31 March 2018: £96.1m) to reflect the net present value of the future liability.

Included in net debt above are £5.5m (31 March 2018: £6.2m) of unamortised loan issue costs.

7. Assets held for sale

Assets and liabilities of the disposal group

At 30 September 2018 the disposal group is stated at its book value at the date it met the recognition of a disposal group held for sale. Management have assessed the fair value of the disposal group using expected selling price based on actual bids received. The fair value of the disposal group is higher than the book value and therefore the carrying amount of the disposal group in the financial statements has been presented as the book value. The disposal group comprises the following assets and liabilities:

	Unaudited at 30 Sep 2018	Audited at 31 March 2018
	£m	£m
Trade and other receivables	**62.8**	58.5
Assets held for sale	**62.8**	58.5
Trade and other payables	**(10.0)**	(6.4)
Liabilities held for sale	**(10.0)**	(6.4)

Notes to the Condensed Consolidated Interim Financial Statements

8. Other financial assets and liabilities

	Unaudited at 30 Sep 2018	Audited at 31 March 2018
	£m	£m
Financial assets:		
Fixed to floating interest rate swaps	**35.7**	45.3
Combined cross currency interest rate swaps	**53.2**	34.9
Derivative financial instruments on energy contracts	**18.3**	8.0
	107.2	88.2
Financial liabilities:		
Finance lease interest swaps	**(19.9)**	(21.3)
Inflation linked swaps	**(1,767.1)**	(1,754.1)
Combined cross currency interest rate swaps	**(4.3)**	(4.2)
	(1,791.3)	(1,779.6)

Fixed to floating Interest rate swaps

The group holds three fixed to floating interest rate swaps, which mature in 2029 and 2033. The movement in the fair value of the swaps from £45.3m asset to £35.7m asset resulted in a charge of £9.6m recognised in the income statement (six month period ended 30 September 2017: £11.8m charge). This is offset by the change in fair value of the associated bonds of £10.9m income (six month period ended 30 September 2017: £12.9m income). The income relating to the fair value of the individual associated bonds is as follows.

£5.6m of income (six month period ended 30 September 2017: £7.5m) of change in fair value of associated bonds relates to the 3.625% 2029 guaranteed bonds with a fair value of £270.7m at 30 September 2018 (31 March 2018: £276.3m). £3.4m (six month period ended 30 September 2017: £2.9m) change in fair value of associated bonds relates to the 4.965% 2033 Class B guaranteed bonds with a fair value of £100.6m at 30 September 2018 (31 March 2018: £104.0m). The remaining £1.9m (six month period ended 30 September 2017: £2.5m) change in fair value of associated bonds relates to the 3.54% 2029 guaranteed bond issued during the year with a fair value of £99.2m at 30 September 2018 (31 March 2018: £101.1m).

Notes to the Condensed Consolidated Interim Financial Statements

8. Other financial assets and liabilities (continued)

Cross currency interest rate swaps

The group entered into several multi-currency interest rate swap transactions involving fifteen Fixed US Dollar bonds and one AUS Dollar bond, referred to as Cross Currency swaps.

As detailed in note 2, the net impact of the fair value movement on the swaps resulted in a net loss of £2.9m (six month period ended 30 September 2017: £8.7m income) to the profit and loss account. This impact is split out as follows.

The fair value movement in combined cross currency swap assets from £34.9m to £53.2m of £18.3m income, plus the fair value movement in the combined cross currency swap liabilities from £4.2m to £4.3m of £0.1m expense resulted in a combined income of £18.2m being recognised in the income statement (six month period ended 30 September 2017: £16.0m loss).This is offset by the change in fair value of the associated bonds resulting in a loss of £21.1m (six month period ended 30 September 2017: £24.7m income). Of the change in fair value of the associated bonds, £20.7m loss (six month period ended 30 September 2017: £23.1m income) relates to Fixed US Dollar bonds and £0.4m loss (six month period ended 30 September 2017: £1.6m income) relates to the AUS Dollar bonds.

Energy derivative

The group holds energy price swaps, which hedge the company's exposure to energy price risk by exchanging the day ahead index price of energy for a fixed price. The movement in the derivative asset from £8.0m to £18.3m of £10.3m has been recognised in the profit and loss account within operating profit.

Finance lease interest swaps

The group holds two floating to fixed interest rate swaps in relation to floating rate finance leases. These have a total nominal value of £45m. The movements in the fair value of floating to fixed rate swaps in respect of finance leases from a liability of £21.3m to a liability of £19.9m resulted in an income of £1.4m recognised in the income statement as an exceptional item (six month period ended 30 September 2017: £1.5m).

Notes to the Condensed Consolidated Interim Financial Statements

8. Other financial assets and liabilities (continued)

Inflation linked swaps

The company holds a number of inflation linked swaps, with a notional value of £1,289.0m. There are three cashflows associated with these inflation linked 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.

In addition, a proportion of the inflation linked swaps also receives six monthly interest amounts based on a fixed rate.

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 paydowns of the inflation linked swaps. This is accrued in the profit and loss account and recognised within long-term borrowings.

Given current six month LIBOR and applicable discount rates, the group's portfolio of inflation linked swaps gave rise to a fair value liability of £1,955.2m (31 March 2018: £1,926.2m). Of this amount £188.1m (31 March 2018: £172.1m) has been recognised within long-term borrowings, and represents the discounted value of the RPI bullet accrued to 30 September 2018. The remaining £1,767.1m (31 March 2018: £1,754.1m) is recognised within other financial liabilities.

The valuation model used by the group to determine the fair value of the inflation linked swap portfolio as at 30 September 2018 includes a funding valuation adjustment, credit valuation adjustment and debit valuation adjustment to reflect the long term credit risk of Yorkshire Water's inflation linked swap portfolio, which includes instruments with super-senior status as well as non-senior status derivatives. The funding valuation adjustments, credit valuation adjustments and debit value adjustments to the valuation represent unobservable inputs that have the potential to materially affect the resultant fair valuation, and therefore require estimation techniques to be adopted by management. Management uses a third party expert to advise on the appropriateness of these assumptions, and prepared sensitivity analysis in order to evaluate the impact of a reasonably possible range of assumptions on the resultant valuation. The total adjustment made to the valuation as a result of the assumptions adopted in respect of these key inputs was £479.6m (31 March 2018: £442.6m).

The mark to market value of the inflation linked swaps excluding these adjustments as at 30 September 2018 is £2,481.4m (31 March 2018: £2,398.8m).

The RPI bullet accrued to 30 September 2018 was £289.1m (31 March 2018: £268.2m) which has been reduced by £101.0m (31 March 2018: £96.1m) when discounted to present values

Notes to the Condensed Consolidated Interim Financial Statements

9. Reconciliation of profit from continuing operations to cash generated by continuing operations

	Unaudited 6 month period ended 30 Sep 2018 £m	Unaudited 6 month period ended 30 Sep 2017 £m	Audited year ended 31 Mar 2018 £m
Total profit for the period	**9.4**	97.2	74.9
Tax charge	**2.9**	15.8	19.8
Profit from continuing operations before taxation	**12.3**	113.0	94.7
Finance income	**(62.0)**	(49.1)	(104.4)
Finance costs	**164.5**	174.2	339.3
Net exceptional finance costs/(income)	**13.2**	(91.8)	(41.4)
Movements of fair value of derivative financial instrument (energy contracts)	**(10.3)**	(1.9)	(14.4)
Depreciation and amortisation of capital grants	**151.2**	137.3	285.1
Profit on disposal of property, plant and equipment	**(2.4)**	(1.9)	(1.9)
Amortisation of intangibles	**6.1**	4.1	8.9
Impairment of property, plant and equipment	**-**	-	1.0
Decrease/(increase) in inventories	**0.1**	0.1	(0.5)
Increase in trade and other receivables	**(27.5)**	(8.0)	(25.7)
Increase in trade and other payables	**31.4**	41.0	27.0
Movement in provisions	**-**	-	(0.6)
Amortisation of capital grants	**(5.1)**	-	(10.0)
Other movements	**0.2**	0.6	0.6
Cash generated from continuing operations	**271.7**	317.6	557.7

Notes to the Condensed Consolidated Interim Financial Statements

10. Cash interest

	Unaudited 6 month period ended 30 Sep 2018 £m	Unaudited 6 month period ended 30 Sep 2017 £m
Cash interest paid:		
External interest on Kelda Finance facility	**7.2**	6.9
External interest paid by Yorkshire Water financing group	**127.6**	133.3
	134.8	140.2
Cash interest received:		
External interest received by Yorkshire Water financing group	**28.1**	15.9
Interest received from parent entities	**29.0**	29.5
	57.1	45.4

11. Share capital

		Ordinary shares
	Number	**£**
Closing balance at 30 September 2018 and 31 March 2018	100	100

12. Contingent liabilities

In September 2016 Yorkshire Water received a claim on behalf of personal search companies (PSC) relating to a claim for historical fees that they have paid to Yorkshire Water for water and drainages reports obtained when buying a house. The PSCs state that the historical fees should not have been paid to Yorkshire Water as the information should have been provided for no fee.

At this stage it is not known if Yorkshire Water would be liable for these claims, the total value to which they could amount, or the timing of any cash outflow.

Notes to the Condensed Consolidated Interim Financial Statements

13. Adoption of new accounting standards

In the six months ended 30 September 2018, the Group applies, for the first time, IFRS 15 Revenue from Contracts with Customers and IFRS 9 Financial Instruments.

The changes in accounting policies as a result are detailed out in note 1.

The transition to the new standards is complete; however, the group will monitor emerging developments and interpretations of the new standard. The cumulative effect method of transition has been adopted, with the effect of initially applying the standard recognised at the date of initial application (1 April 2018). Accordingly, the comparative information presented has not been restated.

(a) On transition to IFRS 15, the key change in the Group's accounting policy for revenue from contracts with customers has been a reduction in recognition of revenue largely offset by a reduction in the bad debt charge relating to those customers from whom it is not probable that the entity will collect the consideration entitled. IFRS 15 stipulates that if it is not probable that the entity will collect the consideration entitled, the contract does not fall under the scope of the standard. The group are not legally permitted to cease water supply to a property, as a result of this there are a number of customers from which consideration is not expected. In the six month period, revenue in relation to these customers has not been recognised. This adjustment is offset by the adjustment to the bad debt provision.

(b) Diversions income was previously accounted for in fixed assets, under IFRIC 18. Revenue from diversions is now recognised in revenue under IFRS 15, over the time it takes to complete the diversion. The adjustment reflects the diversions income in the six-month period. The practical expedient has been applied with regard to accounting for completed contracts, whereby they will not be restated under IFRS 15, and therefore no cumulative catch up adjustment has been made.

(c) On transition to IFRS 9, the group has recognised the loss on a non-substantial modification of debt through the profit and loss account, amortised over the life of the financial liability through the effective interest rate. The exchange accounting took place in 2009. The adjustment to retained earnings reflects the cumulative effect from modification to transition.

The cash flows of the group are not impacted by any of the adjustments above.

Notes to the Condensed Consolidated Interim Financial Statements

13. Adoption of new accounting standards (continued)

Profit and loss account

	Notes	As reported (IFRS 15 & IFRS 9) £m	Adjustments £m	Unaudited 6 months to 30 September 2018 Amounts without adoption of IFRS 15 & IFRS 9 £m	Unaudited 6 months to 30 September 2017 Amounts without adoption of IFRS 15 & IFRS 9 £m
Group revenue	(a), (b)	**529.4**	6.7	536.1	513.0
Operating costs before exceptional items	(a)	**(382.6)**	(8.1)	(390.7)	(362.5)
Exceptional items		**(18.9)**	-	(18.9)	(4.2)
Group operating profit from continuing operations		**127.9**	(1.4)	126.5	146.3
Finance income		**62.0**	-	62.0	49.1
Exceptional finance income		**30.5**	-	30.5	129.7
Finance costs	(c)	**(164.5)**	0.8	(163.7)	(174.2)
Exceptional finance costs		**(43.7)**	-	(43.7)	(37.9)
Profit from continuing operations before taxation		**12.2**	(0.6)	11.6	113.0
Tax (charge)/credit on continuing operations	(b)	**(2.9)**	0.2	(2.7)	(15.8)
Profit for the period from continuing operations		**9.3**	(0.4)	8.9	97.2
Profit from discontinued operations net of tax		**0.1**	-	0.1	-
Profit for the period		**9.4**	(0.4)	9.0	97.2

Notes to the Condensed Consolidated Interim Financial Statements

13. Adoption of new accounting standards (continued)

Balance sheet

	Notes	As reported (IFRS 15 & IFRS 9)	Adjustments	Unaudited At 30 September 2018 Amounts without adoption of IFRS 15 & IFRS 9	Unaudited At 31 March 2018 Amounts without adoption of IFRS 15 & IFRS 9
		£m	£m	£m	£m
Intangible assets		**72.4**	-	72.4	68.5
Property, plant and equipment	(b)	**7,697.0**	(1.4)	7,695.6	7,603.9
Financial assets		**107.2**	-	107.2	88.2
Trade and other receivables		**1,187.5**	-	1,187.5	1,191.6
		9,064.1	(1.4)	9,062.7	8,952.2
Inventories		**3.0**	-	3.0	3.0
Trade and other receivables		**197.3**	-	197.3	168.0
Cash and cash equivalents		**47.4**	-	47.4	41.2
Assets held for sale		**62.8**	-	62.8	58.5
		310.5	-	310.5	270.7
Total Assets		**9,374.6**	(1.4)	9,373.2	9,222.9
Current liabilities					
Trade and other payables		**(344.8)**	-	(344.8)	(336.9)
Deferred grants and contributions on depreciated assets		**(10.4)**	-	(10.4)	(10.0)
Short term borrowings		**(224.9)**	-	(224.9)	(279.9)
Liabilities associated with assets held for sale		**(10.0)**	-	(10.0)	(6.4)
		(590.1)	-	(590.1)	(633.2)
Non-current liabilities					
Long term borrowings	(c)	**(5,261.0)**	6.8	(5,254.2)	(5,055.1)
Long term payables		**(6.3)**	-	(6.3)	(5.6)
Financial liabilities		**(1,791.3)**	-	(1,791.3)	(1,779.6)
Deferred grants and contributions on depreciated assets		**(438.0)**	-	(438.0)	(433.5)
Provisions		**(0.4)**	-	(0.4)	(0.4)
Deferred tax liabilities	(b)	**(420.4)**	0.2	(420.2)	(424.2)
		(7,917.4)	7.0	(7,910.4)	(7,698.4)
Total liabilities		**(8,507.5)**	7.0	(8,500.5)	(8,331.6)
Net assets		**867.1**	5.6	872.7	891.3
Equity					
Share capital		**-**	-	-	-
Revaluation reserve		**605.8**	-	605.8	605.8
Retained earnings	(b), (c)	**261.3**	5.6	266.9	285.5
Total equity		**867.1**	5.6	872.7	891.3

Taking responsibility for the
water environment for good