Yorkshire Water Services Ltd

Interim Report and Financial Statements

For the six months ended 30 September 2017

Registered number: 2366682

Taking responsibility for the
water environment for good

Contents

Chairman's Statement

Yorkshire Water has continued to make good progress in the first half of the year and is forecast to meet most of its performance commitment targets. The Company has identified the areas where performance is not satisfactory and is taking action.

Although the Board maintains its focus on performance in the current period, it is also closely engaged in formulating the Company's response to the methodology for the next periodic review proposed by Ofwat. The draft methodology, published in July of this year, is a significant departure from previous approaches by the Regulator and the Board is considering the strategic implications for the Company.

As Yorkshire Water produces its business plan for the next five years the Board will play a key role as part of the assurance process, ensuring that our plans are robust and deliverable.

In the last six months there have been some notable changes to the Board. Charlie Haysom has stepped down as director of service delivery. Pamela Doherty re-joined the Board, taking over from Charlie in that role. We thank Charlie for his major role in leading service delivery. We also extend our thanks once again to Baroness Kath Pinnock for her significant contribution to the Company. Following Kath's retirement from the Board at the end of her term of office, we welcomed Andrew Wyllie, Chief Executive of the Costain Group plc, as an independent non-executive director. The Board also welcomed Scott Auty, Andrew Dench and Mike Osborne as non-executive directors. Scott, Andrew and Mike are existing directors of Kelda Holdings Limited and represent three of the Group's shareholders. Finally, I am pleased to advise that Ray O'Toole was appointed as our Senior Independent Director in July.

The Company looks forward to engaging with customers and stakeholders as it together its plans for the next five years.

Anthony Rabin
Chairman

Business Review

Chief Executive's Review

As we move into the second half of the five year investment period, I am pleased to report that we are continuing to deliver good progress against the current performance commitment targets. Most are on track and action is being taken to address shortfalls in a few areas such as our customer service or SIM scores.

We have taken steps to improve our position, in particular by looking to reduce the need for customers to contact us when it's not necessary for them to do so. As a result, the number of unwanted customer contacts is falling, whilst the number of customers switching to our digital channels, such as webchat and free call back facilities, is increasing. Customers are responding to these innovations in service and we believe we are one of the few utilities to offer guaranteed call backs within a ten minute slot.

Our strong focus on improving health and safety across the Company continues to make progress. Although much remains to be done, our lost time injury rate continues to fall and as a result of strong management attention, the reporting of incidents and near misses continues to show improvement. These are indicative of a growing health and safety culture in the organisation.

The last few months has seen the publication of Ofwat's proposed approach to the next price and investment review. This new methodology, to be confirmed in December, makes it clear that Yorkshire Water, along with the rest of the sector, faces some substantial challenges over both the last few years of this regulatory period and the full five years of the next.

The new methodology introduces comparative performance regulation in order to emulate the workings of a competitive market. As in a normal market, companies with exceptional performance and which show ambition and innovation in their business plans stand to receive significantly enhanced rewards. Those with poor performance and weak plans are likely to be penalised.

The other significant change is that companies hoping to achieve the most enhanced status – exceptional in Ofwat's terminology – will need to achieve high levels of performance from the beginning of the five year period rather than by the end. This in turn means that to achieve exceptional status, companies will in effect need to be demonstrating high levels of performance across the last two years of the current period, irrespective of their current performance commitments.

We have looked in detail at the opportunity which this new approach presents to Yorkshire Water and are currently considering how our operational plans for the next two years might need to be amended to reflect this and also what the implications might be for our business plan submission to Ofwat in 2018.

Our plans to implement new SAP based business processes across the Company are progressing well. These will give us a strong foundation to significantly enhance performance across the next investment period and into the future.

Business Review

Finally, I would like to thank all our colleagues in the business who have worked so hard to contribute to our current performance achievement and who have also shown considerable commitment to help us achieve our ambitions to enhance that performance further.

Richard Flint
Chief Executive

Business Review

Financial Performance

Yorkshire Water's performance in the six months to September 2017 is in line with plan and with prior year. Exceptional costs of £4.2m have been incurred relating to ongoing impacts of the 2015 flooding.

On 23 June 2016, the United Kingdom voted to leave the European Union ('Brexit'). This vote has resulted in uncertainty in economic and political spheres. Whilst much of the economic impact is still unknown for Yorkshire Water, to date we have seen minimal impact on the day-to-day operations and operating profit of the business.

In the 2016/17 financial year there was a significant movement of fair values held on the balance sheet for financial instruments, in particular the index linked swaps. This movement was as a result of the impact of interest rates which have fallen, increasing the negative fair values of the Company's portfolio of index linked swaps.

During the six months ended 30 September 2017, the Company restructured a portion of its portfolio of index-linked swaps, increasing the semi-annual interest receipt leg of the swaps in question by £9.7m (£19.3m per annum) for the next fifteen years. The first of these semi-annual receipts was received on 21 August 2017. Had this transaction to reduce cash interest costs not been implemented, the Company's gearing as stated in the table below would have been 4.0% lower at 30 September 2017.

This and other balance sheet strengthening measures undertaken in the six months ended 30 September 2017 resulted in Moody's moving the outlook on the Company's credit ratings from negative to stable on 4 July 2017.

Key financial performance indicators

The key performance indicators are set out below:

	Unaudited 6 months ended 30 September 2017	Unaudited 6 months ended 30 September 2016
Profit and loss indicators		
Turnover (£m)	**515.2**	506.5
Operating profit before exceptional item (£m)	**148.0**	147.8
EBITDA (£m)†	**295.1**	285.4
Exceptional (cost)/income (£m)	**(4.2)**	0.1
Capital expenditure (£m)	**182.0**	175.5
Regulatory indicators	**Unaudited as at 30 September 2017**	Audited as at 31 March 2017
Regulatory net debt (Note 7)	**4,751.6**	4,630.1
Regulatory Capital Value (RCV) (£m)	**6,324.2**	6,143.7
Regulatory gearing*	**75.1%**	75.4%

Business Review

Balance sheet indicators	**Unaudited as at 30 September 2017**	Audited as at 31 March 2017
Total adjusted net debt (£m) (Note 7)	**4,048.6**	3,773.6
Gearing	**64.0%**	61.4%

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

† EBITDA (Earnings before interest, tax, depreciation, amortisation and exceptional items) is a key performance measure for the Yorkshire Water Board. EBITDA is reconciled to Operating Profit in Note 3 to the financial statements.

Turnover increased by 1.7% to £515.2m (6 months ended 30 September 2016: £506.5m), due to the inflationary impact on prices.

Operating profit before exceptional items has increased in the period by 0.1% to £148.0m compared to the comparable period last year (6 months ended 30 September 2016: £147.8m). Operating costs have increased by 2.4% (from £358.7m to £367.2m). The primary reason for this is an increase in depreciation (£7.8m) due to the on-going capital programme.

EBITDA has increased, when compared to the comparable period last year, to £295.1m from £285.4m, a 3.4% increase. This is as a result of the movements in turnover and strong control over operating costs which are in line with prior year.

Exceptional costs relate to the flooding incident that occurred in December 2015. In this six month period the Company has incurred £4.2m operational costs associated with the assets damaged in this event.

During the six month period to 30 September 2017, net interest payable and similar charges before exceptional items was £116.5m, (30 September 2016: £96.0m). The increase is predominantly a result of additional debt raised in the second half of the 2016/17 financial year to finance the Company's operational and capital expenditure programme, together with the impact of inflation.

Capital expenditure in the six month period to 30 September 2017 was £182.0m (30 September 2016 £175.5m), a 3.7% increase. This is to be expected, as it is now the third year of the new investment period and a higher proportion of the capital programme has moved from feasibility and design into the construction phase of delivery.

At 30 September 2017, total net debt stands at £4,048.6m (31 March 2017: £3,773.6m) which is primarily as a result of additional debt raised to fund the index linked swap restructuring transaction detailed on page 4.

Net debt at 30 September 2017 includes £817.9m of amounts owed from other group companies (31 March 2017: £1,009.0m). Funds raised elsewhere within the Kelda Group were used to repay part of this loan.

Based on an RCV value of £6,324.1m, senior adjusted net debt to RCV at September 2017 is 64.0% (31 March 2017: 61.4%). The level of gearing is forecast to be maintained at similar levels throughout the financial year, in accordance with the Company's on-going strategy to improve its financial strength.

The fair value of the financial instruments is recognised on the balance sheet and the movement in the valuation is recognised in the profit and loss account. The significant movement in the six months ended 30 September 2017 is in relation to the fair value of the index linked swaps as set out in note 2.

Business Review

£44.8m of distributions have been made to the parent company during the period (6 months ended 30 September 2016: £94.7m), of which £31.6m (6 months ended 30 September 2016: £35.3m) 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 £13.2m (6 months ended 30 September 2016: £14.0m). No distributions have been made to the ultimate shareholders of Yorkshire Water.

Principal Risks and Uncertainties

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

Directors and executive management have performed a robust assessment of the principal risks which have been reviewed by the Audit Committee. The principal risks and uncertainties that the business faces over the remainder of this financial year are largely unchanged from those reported in our last Annual Report and Accounts listed below.

- Public and colleague safety
- Enough clean, safe drinking water
- Protect the environment
- Climate change resilience
- Customer trust
- Financial sustainability
- Security
- Talent, culture and succession
- Water sector reform
- Data protection
- Competition Act

As noted above, the Brexit vote of June 2016 has resulted in economic and political uncertainty and potential impacts are being considered across all of the relevant risks listed above.

Further detail on the risks and uncertainties is included in the Annual Report and Financial Statements for the year ended 31 March 2017 which can be found on the Yorkshire Water website at https://www.yorkshirewater.com/reports.

Condensed Profit and Loss Account

For the six months ended 30 September 2017

	Note	Unaudited six months ended 30 September 2017 £m	30 September 2016 £m
Turnover		**515.2**	506.5
Operating costs		**(367.2)**	(358.7)
Exceptional items		**(4.2)**	0.1
Operating profit		**143.8**	147.9
Interest receivable and similar income before exceptional items		**46.3**	50.6
Exceptional fair value income	*2*	**129.8**	79.8
Total interest receivable and similar income		**176.1**	130.4
Interest payable and similar charges before exceptional items		**(162.8)**	(146.6)
Exceptional fair value charges	*2*	**(37.9)**	(685.4)
Total interest payable and similar charges		**(200.7)**	(832.0)
Profit/(loss) on ordinary activities before tax		**119.2**	(553.7)
Tax on profit/(loss) on ordinary activities	*4*	**(59.1)**	129.2
Profit/(loss) for the period		**60.1**	(424.5)

Condensed Statement of comprehensive income and expense

For the six months ended 30 September 2017

		Unaudited six months ended 30 September 2017 £m	30 September 2016 £m
Profit/(loss) for the financial year		**60.1**	(424.5)
Other comprehensive income:			
Gains on cash flow hedges taken to equity		**1.9**	9.7
Deferred tax on cash flow hedges	*4*	**(0.3)**	(1.7)
Deferred tax due to fixed asset timing differences on revaluation	*4*	**-**	2.5
Total comprehensive income/(expense) for the year		**61.7**	(414.0)

All of the above results relate to continuing activities.

Condensed Balance Sheet

As at 30 September 2017

	Note	Unaudited 30 September 2017 £m	Audited 31 March 2017 £m
Fixed assets			
Intangible assets		**50.0**	51.3
Tangible assets		**7,298.8**	7,250.4
Investments		**0.1**	0.1
		7,348.9	7,301.8
Current assets			
Stocks		**2.5**	2.5
Debtors (including £1,168.3m after more than one year (31 March 2017: £1,398.4m))		**1,411.1**	1,601.3
Cash at bank and in hand		**68.8**	230.3
		1,482.4	1,834.1
Creditors: amounts falling due within one year		**(391.2)**	(384.3)
Net current assets		**1,091.2**	1,449.8
Total assets less current liabilities		**8,440.1**	8,751.6
Creditors: amounts falling due after more than one year	*6*	**(7,035.6)**	(7,423.1)
Provisions for liabilities			
Deferred tax liability		**(402.7)**	(343.3)
Other provisions		**(0.4)**	(0.7)
		(403.1)	(344.0)
Net assets		**1,001.4**	984.5
Capital and reserves			
Called up share capital		**10.0**	10.0
Revaluation reserve		**440.5**	440.5
Hedging reserve		**(3.6)**	(5.2)
Profit and loss account		**554.5**	539.2
Total shareholders’ funds		**1,001.4**	984.5

Condensed Statement of Changes in Equity

For the six months ended 30 September 2017

	Note	Called up Share capital £m	Revaluation reserve £m	Hedging reserve £m	Profit and loss account £m	Total Shareholders' funds £m
Balance at 1 April 2017		**10.0**	**440.5**	**(5.2)**	**539.2**	**984.5**
Total comprehensive income for the period						
Profit for the financial period		**-**	**-**	**-**	**60.1**	**60.1**
Other comprehensive income for the period		**-**	**-**	**1.6**	**-**	**1.6**
Total comprehensive income for the period		**-**	**-**	**1.6**	**60.1**	**61.7**
Transactions with owners recorded directly in equity						
Dividends	*5*	**-**	**-**	**-**	**(44.8)**	**(44.8)**
Balance at 30 September 2017		**10.0**	**440.5**	**(3.6)**	**554.5**	**1,001.4**
Balance at 1 April 2016		10.0	205.8	(8.1)	940.3	1,148.0
Total comprehensive income/(expense) for the period						
Loss for the financial period		-	-	-	(424.5)	(424.5)
Other comprehensive income for the period		-	-	8.0	2.5	10.5
Total comprehensive income/(expense) for the period		-	-	8.0	(422.0)	(414.0)
Other					(0.5)	(0.5)
Transactions with owners recorded directly in equity						
Dividends	*5*	-	-	-	(94.7)	(94.7)
Balance at 30 September 2016		10.0	205.8	(0.1)	423.1	638.8

Notes to the Condensed Interim Financial Statements

For the six months ended 30 September 2017

For the year ended 31 March 2017, the Company prepared its financial statements in compliance with Financial Reporting Standard 102, the Financial Reporting Standard applicable in the UK and Republic of Ireland ("FRS 102"). This interim report has been produced on the same basis.

The financial information for the six months ended 30 September 2017 and the equivalent period in 2016 has not been audited.

The interim financial information was approved for issue by the board of directors on 15 November 2017.

1. Basis of preparation and accounting policies

The financial information for the six month period ended 30 September 2017 has been prepared in accordance with FRS 104 'Interim Financial Reporting' and the Companies Act 2006. This report should be read in conjunction with the Company's annual financial statements for the year ended 31 March 2017, which have been prepared in accordance with Financial Reporting Standard 102, the Financial Reporting Standard applicable to the UK and Ireland (FRS 102).

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. As permitted by FRS 104 a statement of cash flows cumulatively for the current financial year-to-date, with a comparative statement for the comparable year-to-date has not been presented, as the Company does not present a statement of cash flows in its year end financial statements.

The financial information for the year ended 31 March 2017, presented in these notes, does not constitute the Company's statutory accounts for that period but has been extracted from the statutory accounts. The accounting policies, methods of computation and presentation are consistent with those published in the annual financial statements for the year ended 31 March 2017, as described in those annual financial statements. The half-yearly financial report should be read in conjunction with those annual financial statements.

No new standards, amendments or interpretations, which would have a material impact on the financial statements, have been adopted in the period. The principal risks and uncertainties as disclosed in the year end accounts are considered to be consistent with those that are still applicable now.

Notes to the Condensed Interim Financial Statements (continued)

For the six months ended 30 September 2017

2. Exceptional fair value income and charges

	Unaudited for the period ended 30 September 2017 £m	Unaudited for the period ended 30 September 2016 £m
Interest receivable and similar income		
Movement of fair value of combined cross currency interest rate swaps	**-**	38.5
Movement in fair value of cross currency debt	**24.7**	-
Movement of fair value of fixed to floating interest rate swaps	**-**	41.3
Movement in fair value of debt associated with fixed to floating interest rate swaps	**12.9**	-
Movement of fair value of finance lease interest rate swap	**1.6**	-
Movement of fair value of index linked swaps	**90.6**	-
	129.8	79.8
Interest payable and similar charges		
Movement of fair value of combined cross currency interest rate swaps	**(16.0)**	-
Movement in fair value of cross currency debt	**-**	(35.9)
Movement in fair value of fixed to floating interest rate swaps	**(11.8)**	-
Movement in fair value of debt associated with fixed to floating interest rate swaps	**-**	(30.4)
Movement of fair value of finance lease interest rate swap	**-**	(4.4)
Movement of fair value of index linked swaps	**(10.1)**	(614.7)
	(37.9)	(685.4)

The movement in the fair value of index linked swaps is a result of swaps, with a notional value of £1,289.0m, which were taken out by the Company during 2008/09 to hedge against movements in the retail price index (RPI). There are three cashflows associated with these index linked swaps:

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

The swaps have been valued at the reporting date at fair value, which at 30 September 2017, resulted in a £1,849.7m liability (31 March 2017: £2,156.5m liability). Of this, £1,702.5m (31 March 2017: £2,033.0m) is recognised within other financial liabilities (Note 8) and £147.2m (31 March 2017: £123.5m) is recognised within interest bearing loans and borrowings (Note 6).

During the six months ended 30 September 2017, Yorkshire Water completed a transaction to recoupon a proportion of the Company's index-linked swap portfolio. The swaps in question were amended so as to increase interest receivable on the receipt leg of the swaps by £19.3m per annum for the next 15 years, being £9.7m receivable semi-annually, with the first semi-annual amount of £9.7m being received in August 2017. As a result of the recouponing transaction, the fair value of the index-linked swap portfolio reduced by £239.9m on 22 June 2017, being the date of completion of the transaction

During the six months ended 30 September 2017, cash interest received on the LIBOR leg of the index linked swaps was £13.0m (2016 £4.7m) and cash interest paid on the RPI leg of the index linked swaps was £21.1m (2016 £20.4m). There were no associated RPI-linked accretion amounts paid.

Notes to the Condensed Interim Financial Statements (continued)

For the six months ended 30 September 2017

2. Exceptional fair value income and charges (continued)

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 in 2000. 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 2017, resulted in a £23.7m liability (31 March 2017: £25.3m). The decrease in the period in the liability of £1.6m has been recognised as exceptional finance income.

Exceptional finance costs include the fair value movement of various fixed to floating interest rate swaps and combined cross currency 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 2017. The net impact of the fair value movement of the fixed to floating interest rate swaps and their associated debt has resulted in a £1.1m credit to the profit and loss account, and the net impact of the fair value movement of the combined cross currency interest rate swaps and their associated debt has resulted in an £8.7m credit to the profit and loss account.

3. Operating Profit

Earnings before interest, tax, depreciation, amortisation and exceptional items (EBITDA) is calculated as follows:

	Unaudited for the period ended 30 September 2017	Unaudited for the period ended 31 March 2016
	£m	£m
Operating profit before exceptional items	**148.0**	147.8
Add back depreciation	**142.5**	134.6
Add back amortisation of intangible assets	**4.6**	3.0
EBITDA	**295.1**	285.4

4. Tax on profit on ordinary activities

	Unaudited for the period ended 30 September 2017	Unaudited for the period ended 31 March 2016
	£m	£m
Current tax	**-**	-
Deferred tax recognised in profit and loss account	**59.1**	(129.2)
Deferred tax recognised in other comprehensive income	**0.3**	(0.8)
Tax charge/(credit)	**59.4**	(130.0)

Notes to the Condensed Interim Financial Statements (continued)

For the six months ended 30 September 2017

4. Tax on profit on ordinary activities (continued)

Deferred tax relating to comprehensive income has been restated from the profit and loss account for 30 September 2016 to the statement of comprehensive income and expense.

5. Distributions paid

	Unaudited for the period ended 30 September 2017 £m	Unaudited for the period ended 30 September 2016 £m
Dividends paid during the period	**(44.8)**	(94.7)
Dividend paid	**(44.8)**	(94.7)
Dividends paid to holdings companies to fund payment of interest	**31.6**	35.3
Amounts retained to fund corporate costs	**13.2**	14.0
Available for distribution to ultimate shareholders	**-**	(45.4)

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

	Unaudited as at 30 September 2017 £m	Audited as at 31 March 2017 £m
Interest-bearing loans and borrowings (note 7)	**636.3**	636.5
Amounts owed to group undertakings	**4,228.4**	4,294.8
Other creditors	**3.4**	3.6
Other financial liabilities (note 9)	**1,733.2**	2,066.0
Deferred grants and contributions on depreciating fixed assets	**434.3**	422.2
	7,035.6	7,423.1

Notes to the Condensed Interim Financial Statements (continued)

For the six months ended 30 September 2017

7. Interest bearing loans and borrowings

	Bank loans and overdrafts 30 September 2017 £m	Other loans 30 September 2017 £m	Finance leases 30 September 2017 £m	Total 30 September 2017 £m
Short term borrowings:				
In one year or less or on demand	58.1	-	12.5	70.6
Long term borrowings:				
In more than one year, but not more than two years	35.7	-	14.0	49.7
In more than two years, but not more than five years	74.3	13.4	12.7	100.4
In more than five years	276.1	133.8	76.3	486.2
	386.1	147.2	103.0	636.3
Amounts owed to Group companies before fair value adjustment of bonds				4,113.5
Fair value adjustment of bonds owed to group companies				114.9
Total borrowings				**4,935.3**
Cash at bank and in hand				**(68.8)**
Amounts owed from group companies				**(817.9)**
Net debt at 30 September 2017				**4,048.6**

Notes to the Condensed Interim Financial Statements (continued)

For the six months ended 30 September 2017

7. Interest bearing loans and borrowings (continued)

	Bank loans and overdrafts 30 September 2016 £m	Other loans 30 September 2016 £m	Finance leases 30 September 2016 £m	Total 30 September 2016 £m
Short term borrowings:				
In one year or less or on demand	38.4	-	49.7	88.1
Long term borrowings:				
In more than one year, but not more than two years	44.9	-	12.4	57.3
In more than two years, but not more than five years	107.9	8.3	22.3	138.5
In more than five years	92.7	83.1	80.9	256.7
	245.5	91.4	115.6	452.5
Amounts owed to Group companies before fair value adjustment of bonds				4,067.5
Fair value adjustment of bonds owed to group companies				151.3
Total borrowings				**4,759.4**
Cash at bank and in hand				**(49.9)**
Amounts owed from group companies				**(1,009.0)**
Net debt at 30 September 2016				**3,700.5**

During the six months to 30 September 2017, amounts owed from group companies in relation to an upstream loan to Kelda Eurobond Co Limited was reduced by £191.1m to £817.9m (30 September 2016: £1,009.0m) using funds raised elsewhere within the Kelda Group.

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 £28.4m (31 March 2017: £28.2m), which accounted for the exchanged bonds at their fair value at the date of exchange.

Notes to the Condensed Interim Financial Statements (continued)

For the six months ended 30 September 2017

7. Interest bearing loans and borrowings (continued)

Net debt includes unamortised issue costs of £12.2m (31 March 2017: £13.7m).

Borrowings repayable in instalments after more than five years include £76.3m (31 March 2017: £77.0m) 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.

As at 30 September 2017 Yorkshire Water had access to undrawn committed bank facilities totalling £585.76m (31 March 2017: £784.76m), £319.76m of which expire in March 2018 and £266.0m expire in October 2018.

Of the total net debt, £540.1m (31 March 2017: £797.2m) relates to Class B debt.

The table below shows the reconciliation between Yorkshire Water Services Limited's reported net debt and the regulatory net debt as set out in Ofwat's guidelines.

	Unaudited for the period ended 30 September 2017	Audited for the period ended 31 March 2016
	£m	£m
Total adjusted net debt	**4,048.6**	3,773.6
Deduct fair value adjustment of bonds owed to group companies included in total adjusted net debt	**(114.9)**	(152.5)
Add back amounts owed from group companies included in total adjusted net debt	**817.9**	1,009.0
Regulatory net debt	**4,751.6**	4,630.1

Notes to the Condensed Interim Financial Statements (continued)

For the six months ended 30 September 2017

8. Reconciliation of movement in adjusted net debt

	Audited at 31 March 2017 £m	Cash movements £m	Non cash movements £m	**Unaudited at 30 September 2017 £m**	Unaudited at 30 September 2016 £m
Short term deposits	230.3	(161.5)	-	**68.8**	49.9
Cash and cash equivalents	230.3	(161.5)	-	**68.8**	49.9
Loans due within one year	(70.6)	30.2	(17.7)	**(58.1)**	(38.4)
Finance leases due within one year	(11.0)	8.3	(9.8)	**(12.5)**	(49.7)
Loans due after one year	(400.2)	-	14.1	**(386.1)**	(245.4)
Finance leases due after one year	(112.8)	-	9.8	**(103.0)**	(115.6)
Index linked swaps	(123.5)	-	(23.7)	**(147.2)**	(91.5)
External net debt	(718.1)	38.5	(27.3)	**(706.9)**	(540.6)
Amounts owed from parent companies	1,009.0	(191.1)	-	**817.9**	1,009.0
Amounts owed to subsidiary company	(4,294.8)	62.7	3.7	**(4,228.4)**	(4,218.8)
	(3,285.8)	(128.4)	3.7	**(3,410.5)**	(3,209.8)
Total adjusted net debt	(3,773.6)	(251.4)	(23.6)	**(4,048.6)**	(3,700.5)

The balance of £147.2m in relation to index linked swaps (31 March 2017: £123.5m) represents £232.5m (31 March 2017: £200.6m) of RPI accretion discounted by £85.3m (31 March 2017: £77.1m) to reflect the net present value of the future liability.

Notes to the Condensed Interim Financial Statements (continued)

For the six months ended 30 September 2017

9. Other financial assets and liabilities

	Unaudited as at 30 September 2017 £m	Audited as at 31 March 2017 £m
Derivative financial assets:		
Fixed to floating interest rate swaps	**49.7**	61.5
Combined cross currency interest rate swaps	**65.0**	79.8
	114.7	141.3
Financial liabilities:		
Finance lease interest swaps	**(23.7)**	(25.3)
Inflation linked swaps	**(1,702.5)**	(2,033.0)
Combined cross currency interest rate swaps	**(2.6)**	(1.4)
Energy swap	**(4.4)**	(6.3)
	(1,733.2)	(2,066.0)

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 £23.7m at 30 September 2017 (31 March 2017: £25.3m). 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 £49.7m at 30 September 2017 (31 March 2017: £61.5m). Hedge accounting has been applied.

Cross currency interest rate swaps

Yorkshire Water hedges the fair value of US dollar denominated private placement 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 £65.0m at 30 September 2017 (31 March 2017: £79.8m). Hedge accounting has been applied.

Yorkshire Water hedges the fair value of an Australian dollar denominated 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 £2.6m at 30 September 2017 (31 March 2017: £1.4m). 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 2017: £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.

Notes to the Condensed Interim Financial Statements (continued)

For the six months ended 30 September 2017

9. Other financial assets and liabilities (continued)

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.

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 £1,849.7m at 30 September 2017 (31 March 2017: £2,156.5m). Of this amount £147.2m has been recognised within long term borrowings, and represents the discounted value of the RPI bullet accrued to 30 September 2017 (31 March 2017: £123.5m). The remaining £1,702.5m is recognised within other financial liabilities (31 March 2017: £2,033.0m).

The valuation model used by Yorkshire Water to determine the fair value of the inflation linked swap portfolio as at 30 September 2017 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. The mark to market value of the index linked swaps, excluding these adjustments, is £2,282.7m (31 March 2017: £2,696.9m).

The RPI bullet accrued to 30 September 2017 was £232.5m (31 March 2017: £200.6m) which has been reduced by £85.3m (31 March 2017: £77.1m) when discounted to present values.

10. 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 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 any fines will not be known until further detail of the outcome of the investigation is received from the HSE.

Yorkshire Water has received a letter of 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 provided for no fee.

At this early 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.

Taking responsibility for the water environment for good