**West Coast Trains Limited**

# Annual report and financial statements for the financial year ended 31 March 2016

Registered number 3007940

**West Coast Trains Limited**

## Contents

## Strategic report
## for the financial year ended 31 March 2016

### Introduction

The principal activity of the Company during the financial year was the operation of passenger rail services between London (Euston) and Birmingham, Wolverhampton, Holyhead, Chester, Liverpool, Manchester, Preston, Carlisle and Glasgow. The Company operated these services under the terms of the Interim Franchise Agreement, dated 5 December 2012, for the period from 9 December 2012 to 21 June 2014. The Interim Franchise Agreement operated as a management contract, with the majority of revenue and cost risk being borne by the Department for Transport ("DfT").

Following negotiations with the DfT, a new Franchise Agreement was signed on 18 June 2014. This superseded the Interim Franchise Agreement and was effective for the period from 22 June 2014 to 31 March 2017, with an option for the DfT to extend it by up to one year. This option was exercised on 21 December 2015 and the Franchise Agreement now runs to 31 March 2018. The Franchise Agreement has seen the Company taking on greater revenue and cost risk in return for the potential to earn a commercial profit margin. Over the franchise period, it will see the Company delivering improvements to the customer experience, local communities and the environment.

### Business review

The Company has seen continued passenger revenue and journey growth during the financial year.

The Company is focused on continually improving the customer experience and customer satisfaction levels. The selection, training, development and encouragement of staff continues to reflect this; while management is continually reviewing operations to provide the best value for money service to customers.

Customer satisfaction as measured by the independent National Passenger Survey is positive and the Company has maintained its position at the top of long distance train operators in terms of overall satisfaction scores.

Under the Franchise Agreement, the Company will build on its customer satisfaction levels by delivering a range of further enhancements to the customer experience. These include additional standard class seating capacity, high bandwidth Wi-Fi, station enhancements, a partnership with the Nectar loyalty scheme, more ticket vending machines, automatic ticket gates and an upgraded website.

As well as delivering customer satisfaction, the Company is focused on its corporate responsibility and meeting its commitments to the environment, to local communities and to the UK economy.

The Company continues to experience days of poor infrastructure performance which impact its overall Public Performance Measure ("PPM") being the percentage of trains that arrive at their destination within 10 minutes of their scheduled arrival time having called at all scheduled stations. The Company continues to press for improvements from Network Rail under its performance contract to ensure that the effects of poor performance delays are minimised. The Company is in an alliance with Network Rail which focuses on performance improvements and efficiency savings.

### Principal risks and uncertainties

Like most businesses, the Company faces a range of risks and uncertainties. Detailed below are those specific risks and uncertainties that the directors believe could have the most significant impact on the Company's performance. The risks and uncertainties described below are not intended to be an exhaustive list of all possible risks and uncertainties.

**Principal risks and uncertainties** *(continued)*

*Major incidents/ Terrorism*

As with any operator of public transportation, there is a risk that the Company is involved in a major incident which could result in injury to customers or staff. The potential impact on the Company includes damage to the Company's reputation and possible claims against the Company. The Company's focus on its safety environment is detailed in the Safety section below. In addition, the Company has procedures in place to respond to any major incident that may occur.

*Network Rail performance*

Reliable running of the Company's high frequency timetable depends on the ability of Network Rail to maintain a fully operational network. Failure to do so impacts the Company's operational performance. In order to manage the risk, there is close monitoring by management of performance targets.

*Economic conditions*

While revenue growth has been seen during the financial year, economic conditions affect demand for rail services with the subsequent impact on financial performance. Slower GDP growth and weakening consumer confidence may put pressure on discretionary spending and travel. In order to minimise this risk, there is a focus at all levels of the Company on cost control and efficient operation.

The Franchise Agreement includes a "GDP sharing" arrangement that is intended to ensure that the DfT bears most of the risk of variances in revenue resulting from UK GDP differing from that expected at the time of the June 2014 Franchise Agreement.

*West Coast Franchise Agreement*

The Franchise Agreement was negotiated using a range of assumptions with regard to revenue growth and cost base. It is imperative that the Company takes all actions outlined in its bid to ensure that its targets are met.

The Company is required to comply with certain conditions as part of its rail franchise agreement. If it fails to comply with these conditions, it may be liable to penalties or the potential termination of the franchise. Compliance with franchise conditions are closely managed and monitored and procedures are in place to minimise the risk of non-compliance.

*Cyber risk*

The Company, whilst maintaining adequate protection, is aware that the risks of cyber attacks are increasing. The Company, along with its suppliers, is constantly monitoring the risk to its operations.

*Failure of critical suppliers*

The Company has a number of key suppliers supporting various areas of the business, for example infrastructure, rolling stock and IT. Failure of one of these key suppliers would impact on financial and operational performance of the Company. The Company has made contingency plans for each key supplier if this eventuality occurs.

### Financial instruments

The Company's activities expose it to a variety of financial risks. It is the Company's policy to invest cash assets safely and profitably. To control credit risk, counterparty credit limits are set by reference to published credit ratings. In addition, the Company seeks to maximise finance income from short term deposits via the monitoring of cash balances and working capital requirements. The Company is exposed to commodity price risk and uses fuel derivatives to hedge against movements in the fuel price.

Liquidity risk is the risk that the Company may not be able to meet its financial obligations as they fall due. The Company ensures that there is sufficient liquidity to enable the Company to meet its financial commitments. The Company monitors its cash requirements on an ongoing basis.

### Financial key performance indicators

Financial KPIs focus on profitability and cash management. Financial results are closely monitored by management, shareholders and the DfT.

The Company has seen passenger revenue and journey growth year on year. Annual passenger journeys now stand at 35.7 million, a 3% increase from the previous financial year. The growth rate has been impacted by the closure of the Lamington viaduct as noted below.

### Other key performance indicators

Significant non-financial KPIs include safety, train punctuality, customer satisfaction and net advocacy scores. Safety is discussed further in the Safety section below.

The operations of the Company have been affected during the financial year by disruption on the West Coast Main Line, mainly at weekends and on bank holidays under normal industry possession arrangements. In addition in early January 2016 the Lamington viaduct, situated on the West Coast Main Line between Carlisle and Glasgow, was closed due to severe flood damage. The closure lasted for a seven week period during which the Company ran a reduced level of service to Glasgow.

Train punctuality is measured by PPM. The annual average was 86.0% for the financial year compared to 84.7% in the previous financial year. The current level continues to be below that expected by the directors and the Company is engaging with Network Rail to improve the service experienced by customers.

Our latest Customer Satisfaction survey results maintain the best in class position. This has been achieved by the Company's good value for money offerings and the dedication of staff. In the Autumn 2015 National Passenger Survey the Company achieved an overall satisfaction score of 91% (Autumn 2014: 90%).

### Safety

The Company remains committed, through annual continuous improvement, to maintaining a safe and secure environment for its passengers, workforce and the general public. The Company's ongoing safety strategic objectives are:

- to minimise the risk of death and injury to customers and staff;
- to eliminate main line Category A "Signals Passed At Danger";
- to support the national initiative to reduce trespass, vandalism and railway crime and disorder; and
- to encourage a rail industry partnership to raise safety standards through shared information, best practice and common safety values.

These are supported by specific focus on safety targets including passenger and staff accident levels, Signals Passed at Danger and safety related defects.

**Safety** *(continued)*

Both the Pendolino and Super Voyager train fleets have a range of safety features. These include (amongst others) enhanced crash protection, laminated windows, improved lighting, fire detection and fighting systems, power operated doors, CCTV and Train Management Systems.

The Company has made good progress against its shorter-term major initiatives which include:

- ongoing maintenance of a close safety partnership with Network Rail;
- ongoing use of driver training simulators supported by interactive computer based training assessment tools for improved safety, training and off-line experience; and
- promoting industry safety values throughout the Company and working with suppliers to do the same. Core safety values are included in training courses, job descriptions and Safety Responsibility Statements.

**Future developments**

The directors remain confident that, under the terms of the Franchise Agreement, the Company will remain profitable over its franchise term.

Based on the anticipated profitable position and forecast cash flows of the Company, the directors have a reasonable expectation that the Company has adequate resources to continue in operational existence for the current franchise term.

This report was approved by the board and signed on its behalf by:

**Philip Whittingham**
**Director**

Date: 23 June 2016

# Directors' report
## for the financial year ended 31 March 2016

The directors present their report and the financial statements for the financial year ended 31 March 2016.

### Results and dividends

The profit for the financial year, after taxation, amounted to £51,023,000 (2015: £39,125,000).

Dividends paid during the financial year totalled £55,000,000 (2015: £6,000,000).

### Directors

The directors who served during the financial year and up to the date of the Directors' report were:

| | |
|---|---|
| Graham Leech | |
| Philip Whittingham | |
| Phillip Bearpark | |
| Mark Whitehouse | (appointed 2 June 2016) |
| Patrick McGrath | (appointed 2 June 2016) |

### Political contributions

The Company made no political contributions during the financial year (2015: £Nil).

### Employees

The Company is a non-discriminatory employer operating an Equal Opportunities Policy that aims to eliminate unfair discrimination, harassment, victimisation and bullying. The Company is committed to ensuring that all individuals are treated fairly, with respect, and are valued irrespective of disability, race, gender, health, social class, sexual preference, marital status, nationality, religion, employment status, age or membership or non-membership of a trade union.

The Company uses the consultative procedures agreed with its staff and their elected representatives with a view to ensuring that its employees are aware of the financial and economic factors that affect the Company's performance and prospects.

The Company's policy, where possible, is to continue to employ those who may become disabled in service, together with some recruitment where circumstances permit. Training is adjusted to cater for an individual disability and the disabled share the same conditions of service as other staff in relation to career development and promotion.

### Disclosure of information to auditor

Each of the persons who are directors at that time when this Directors' report is approved has confirmed that:

- so far as that director is aware, there is no relevant audit information of which the Company's auditor is unaware,
- that director has taken all the steps that ought to have been taken as a director in order to be aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

## Directors' report
## for the financial year ended 31 March 2016

### Auditor

Pursuant to Section 487(2) of the Companies Act 2006, KPMG LLP will be deemed to be re-appointed and will therefore continue in office.

This report was approved by the board and signed on its behalf by:

**Philip Whittingham**
**Director**

Date: 23 June 2016

The Battleship Building
179 Harrow Road
London
W2 6NB

## Directors' responsibilities statement
## for the financial year ended 31 March 2016

The directors are responsible for preparing the Strategic report, the Directors' report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the financial statements in accordance with UK Accounting Standards and applicable law (UK Generally Accepted Accounting Practice), including FRS 101 'Reduced Disclosure Framework'.

Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company and the profit or loss of the Company for that period. In preparing these financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

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

## Independent auditor's report to the members of West Coast Trains Limited

We have audited the financial statements of West Coast Trains Limited for the year ended 31 March 2016, set out on pages 10 to 46. The financial reporting framework that has been applied in the preparation of the financial statements is applicable law and UK Accounting Standards (UK Generally Accepted Accounting Practice), including FRS 101 'Reduced Disclosure Framework'.

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

### Respective responsibilities of directors and auditor

As explained more fully in the Directors' responsibilities statement set out on page 7, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

### Scope of the audit of the financial statements

A description of the scope of an audit of financial statements is provided on the Financial Reporting Council's website at www.frc.org.uk/auditscopeukprivate.

### Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view of the state of the Company's affairs as at 31 March 2016 and of its profit for the financial year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

### Opinion on other matters prescribed by the Companies Act 2006

In our opinion the information given in the Strategic report and the Directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements.

## Independent auditor's report to the members of West Coast Trains Limited

### Matters on which we are required to report by exception

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

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

Darren Turner (Senior Statutory Auditor)

for and on behalf of
**KPMG LLP, Statutory Auditor**

One Snowhill
Snow Hill Queensway
Birmingham
B4 6GH

Date: 23 June 2016

## Profit and loss account and other comprehensive income for the financial year ended 31 March 2016

| | Note | 2016 £000 | 2015 £000 |
|---|---|---|---|
| **Revenue** | 3 | **1,068,668** | 1,018,704 |
| Other operating income | 4 | **57,391** | 40,036 |
| Train operating expenditure | 5 | **(631,173)** | (656,028) |
| Staff costs | 7 | **(180,141)** | (168,876) |
| Depreciation and amortisation | | **-** | (202) |
| Other operating charges | | **(249,039)** | (181,722) |
| **Operating profit** | | **65,706** | 51,912 |
| Finance income | 8 | **1,494** | 351 |
| Finance expense | 8 | **(39)** | (189) |
| **Profit on ordinary activities before tax** | 6 | **67,161** | 52,074 |
| Tax on ordinary activities before tax | 9 | **(16,138)** | (12,949) |
| **Profit for the financial year** | | **51,023** | 39,125 |
| | | | |
| **Other comprehensive income** | | | |
| *Items that will not be reclassified to profit or loss:* | | | |
| Remeasurements of defined benefit pension scheme | | **3,070** | 8,107 |
| | | | |
| *Items that are or may be reclassified to profit or loss:* | | | |
| Cash flow hedges: | | | |
| - Changes in fair value during the year | | **(3,715)** | (6,925) |
| - Reclassified and reported in profit for the year | | **4,417** | 1,311 |
| - Tax effect of cash flow hedges | | **(189)** | 1,123 |
| | | **513** | (4,491) |
| | | | |
| **Other comprehensive income for the financial year, net of tax** | | **3,583** | 3,616 |
| | | | |
| **Total comprehensive income for the financial year** | | **54,606** | 42,741 |

The accompanying notes form an integral part of this profit and loss account and other comprehensive income.

**West Coast Trains Limited**

**Balance sheet**
**as at 31 March 2016**

| | Note | £000 | 2016<br>£000 | £000 | 2015<br>£000 |
|---|---|---|---|---|---|
| **Fixed assets** | | | | | |
| Tangible assets | 10 | | - | | - |
| **Current assets** | | | | | |
| Stocks | 12 | 491 | | 694 | |
| Debtors: amounts falling due after more than one year | 13 | 21,277 | | 19,598 | |
| Debtors: amounts falling due within one year | 13 | 74,072 | | 62,270 | |
| Cash at bank and in hand | 14 | 96,720 | | 105,448 | |
| | | 192,560 | | 188,010 | |
| **Creditors:** amounts falling due within one year | 15 | (144,418) | | (137,003) | |
| **Net current assets** | | | 48,142 | | 51,007 |
| **Total assets less current liabilities** | | | 48,142 | | 51,007 |
| **Creditors:** amounts falling due after more than one year | 16 | | (7,041) | | (10,456) |
| **Provisions for liabilities** | 17 | | (3,532) | | (2,588) |
| **Net assets** | | | 37,569 | | 37,963 |
| **Capital and reserves** | | | | | |
| Called up share capital | 21 | | - | | - |
| Profit and loss account | 21 | | 41,547 | | 42,454 |
| Cash flow hedging reserve | 21 | | (3,978) | | (4,491) |
| **Shareholders' funds** | | | 37,569 | | 37,963 |

The accompanying notes form an integral part of this balance sheet.

The financial statements were approved and authorised by the board and were signed on its behalf by:

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**Philip Whittingham**
**Director**

Date: 23 June 2016

Registered number: 3007940

## West Coast Trains Limited

## Statement of changes in equity
## as at 31 March 2016

| | Share capital £000 | Profit and loss account £000 | Cash flow hedging reserve £000 | Total £000 |
|---|---|---|---|---|
| Balance at 1 April 2014 | - | 1,222 | - | 1,222 |
| Profit for the financial year | - | 39,125 | - | 39,125 |
| Other comprehensive income | - | 8,107 | (4,491) | 3,616 |
| **Total comprehensive income for the financial year** | - | **47,232** | **(4,491)** | **42,741** |
| Dividends paid on ordinary shares | - | (6,000) | - | (6,000) |
| **Balance at 31 March 2015** | - | **42,454** | **(4,491)** | **37,963** |
| Balance at 1 April 2015 | - | 42,454 | (4,491) | 37,963 |
| Profit for the financial year | - | 51,023 | - | 51,023 |
| Other comprehensive income | - | 3,070 | 513 | 3,583 |
| **Total comprehensive income for the financial year** | - | **54,093** | **513** | **54,606** |
| Dividends paid on ordinary shares | - | (55,000) | - | (55,000) |
| **Balance at 31 March 2016** | - | **41,547** | **(3,978)** | **37,569** |

The accompanying notes form an integral part of this statement of changes in equity.

## Notes to the financial statements
## for the financial year ended 31 March 2016

### 1 Accounting policies

West Coast Trains Limited ("the Company") is a company incorporated and domiciled in the UK.

The financial statements have been prepared in accordance with Financial Reporting Standard 101 'Reduced Disclosure Framework' ("FRS 101") and the Companies Act 2006.

In preparing these financial statements, the Company applies the recognition, measurement and disclosure requirements of International Financial Reporting Standards as adopted by the EU ("Adopted IFRSs"), but makes amendments where necessary in order to comply with the Companies Act 2006.

The principal accounting policies adopted in the preparation of these financial statements are set out below. These policies have been consistently applied to all years presented, unless otherwise stated.

Judgements made by the directors, in the application of these accounting policies that have a significant effect on the financial statements and estimates with a significant risk of material adjustment in the next year are discussed in note 2.

### 1.1 Transition to FRS 101

The Company has historically prepared its financial statements under UK Generally Accepted Accounting Practice ("UK GAAP"), this is the first year that the Company has prepared financial statements that comply with FRS 101. As such, the accounting policies and basis of preparation differ from those set out in the financial statements for the year ended 31 March 2015.

In the transition to FRS 101, the Company has applied IFRS 1 whilst ensuring that its assets and liabilities are measured in compliance with FRS 101. An explanation of how the transition to FRS 101 has affected the reported financial position and financial performance of the Company is provided in note 25.

IFRS 1 grants certain exemptions from the full requirements of Adopted IFRSs in the transition period. The following exemptions have been taken in these financial statements:

- Employee benefits – All cumulative gains and losses on remeasurement of defined benefit plans have been recognised in equity at 1 April 2014.

### 1.2 Basis of preparation

The financial statements have been prepared on the historical cost basis, except for certain financial instruments that are recorded at fair value.

In these financial statements, the Company has applied the exemptions under FRS 101 in respect of the following disclosures:

- Cash flow statement and related notes;
- Comparative period reconciliation for share capital;
- Related party disclosures in respect of wholly owned subsidiaries;
- Requirements of IFRS 7 'Financial Instruments: Disclosures';
- The effects of new but not yet effective IFRSs.

The Company proposes to continue to adopt the reduced disclosure framework of FRS 101 in its next financial statements.

## 1 Accounting policies *(continued)*

### 1.3 Going concern

The financial statements have been prepared on the going concern basis which assumes the Company will continue in operational existence for the foreseeable future. The directors have reviewed the cash flow forecasts of the Company for the foreseeable future. The forecasts demonstrate the Company expects to meet its liabilities as they fall due for the foreseeable future. The directors therefore believe it is appropriate for the financial statements to be prepared on the going concern basis.

### 1.4 Revenue

Revenue comprises amounts receivable by the Company in respect of goods and services supplied during the financial year, excluding VAT.

Passenger revenue principally represents amounts attributed to the Company by the Railway Settlement Plan (which administers the income allocation system within the UK rail industry) for each financial period. Income is attributed based on models of certain aspects of passenger behaviour and, to a lesser extent, from allocations agreed for specific revenue flows. The attributed share of season ticket income is deferred within creditors and released to the profit and loss account over the life of the relevant season ticket.

Other trading income consists principally of the provision of station facilities to other train operators, retail commissions receivable and car parking. Other trading income and catering income are recognised as the income is earned.

Revenue is recognised when all performance conditions associated with the revenue have been met.

### 1.5 Franchise expense/income

Revenue grants receivable and franchise premia payable in respect of the operation of rail franchises are recognised in the profit and loss account in the period in which the related revenue or expenditure is recognised in the profit and loss account or where they do not relate to any specific revenue or expenditure, in the period in respect of which the amount is receivable or payable.

### 1.6 Compensation for service disruption

Compensation receivable/payable for service disruption under the performance regime provisions of the track access agreement with Network Rail is recognised over the period of disruption and the net amount is shown within other operating income.

Network change compensation receivable in respect of lost revenue and incremental costs incurred due to Network Rail's alterations of the track and infrastructure is recognised over the period of disruption and is shown within other operating income.

### 1.7 Taxation

Tax on the profit or loss for the year 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, in which case it is recognised in equity.

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.

## 1 Accounting policies *(continued)*

### 1.7 Taxation *(continued)*

Deferred tax is provided on temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the temporary difference can be utilised. Deferred tax assets are reviewed at each balance sheet date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets and it is the intention to settle these on a net basis.

### 1.8 Tangible fixed assets

Tangible fixed assets are stated at cost less depreciation. Depreciation is provided to write off cost less estimated residual value, on a straight-line basis, over the shorter of the useful economic life of the assets or the remaining duration of the franchise and commences from the date on which the assets are ready to use.

### 1.9 Fixed asset investments

Fixed asset investments are shown at cost less provision for impairment.

### 1.10 Stocks

Stocks are stated at the lower of cost and net realisable value after making due allowance for obsolete and slow moving stocks.

### 1.11 Operating leases

Payments made under operating leases are recognised in the profit and loss account on a straight-line basis over the term of the lease. Lease incentives received are recognised in the profit and loss account as an integral part of the total lease expense.

### 1.12 Provisions

Provisions are recognised when the Company has a present legal or constructive obligation as a result of a past event and it is probable that the Company will be required to settle that obligation. The amounts recognised are the best estimate of the expenditure that will be required to meet the Company's obligation.

### 1.13 Financial instruments

Financial assets and financial liabilities are recognised when the Company becomes a party to the contractual provisions of the relevant instrument. In accordance with IAS 39, financial instruments are recorded initially at fair value. Subsequent measurement of those instruments at the balance sheet date reflects the designation of the financial instrument. The Company determines the classification at initial recognition and re-evaluates this designation at each balance sheet date except for those financial instruments measured at fair value through profit or loss.

## 1 Accounting policies *(continued)*

### 1.13 Financial instruments *(continued)*

*Derivative financial instruments and hedging*

The Company uses derivative financial instruments to manage its exposure to fuel price risk. Derivative financial instruments are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently re-measured at fair value. Derivatives are carried as assets when the fair value is positive and as liabilities when the fair value is negative.

For those derivatives designated as hedges and for which hedge accounting is desired, the hedging relationship is documented at its inception. This documentation identifies the hedging instrument, the hedged item or transaction, the nature of the risk being hedged and how effectiveness will be measured throughout its duration. Such hedges are expected at inception to be highly effective.

For the purposes of hedge accounting, hedges are classified as cash flow hedges when hedging exposure to variability in cash flows that is either attributable to a particular risk associated with a recognised asset or liability or a highly probable forecast transaction.

For cash flow hedges, the effective portion of the gain or loss on the hedging instrument is recognised in the statement of comprehensive income, while the ineffective portion is recognised in the profit and loss account. Amounts recorded in the statement of comprehensive income are transferred to the profit and loss account when the hedged transaction affects profit or loss, such as when a forecast sale or purchase occurs.

If the hedging instrument expires or is sold, terminated or exercised without replacement or rollover, or if its designation as a hedge is revoked, amounts previously recorded in the statement of comprehensive income remain in equity until the forecast transaction occurs and are then transferred to the profit and loss account. If a forecast transaction is no longer expected to occur, amounts previously recognised in the statement of comprehensive income are transferred to the profit and loss account immediately.

*Non-derivative financial assets*

Non-derivative financial assets are deemed to be assets which have no fixed or determinable payments that are not quoted in an active market and would therefore be classified as "loans and receivables". Such non-derivative financial assets are measured at amortised cost using the effective interest method, less any impairment and include trade and other receivables.

*Cash and cash equivalents*

For the purposes of the balance sheet and cash flow statement, cash and cash equivalents comprise cash on hand, deposits held at call with banks and other short-term highly liquid investments with maturities at the balance sheet date of twelve months or less.

*Impairment of non-derivative financial assets*

The Company assesses at each balance sheet date whether a non-derivative financial asset or group of financial assets is impaired. A financial asset is considered impaired if objective evidence indicates that one or more events that have occurred since the initial recognition of the asset have had a negative impact on the estimated future cash flows of that asset. An impairment loss in respect of a financial asset carried at amortised cost is calculated as the difference between its carrying value and the present value of the estimated future cash flows discounted at the asset's original effective interest rate.

## 1 Accounting policies *(continued)*

### 1.13 Financial instruments *(continued)*

*Non-derivative financial liabilities*

Non-derivative financial liabilities are initially recorded at fair value less directly attributable transaction costs, and subsequently at amortised cost, and include trade and other payables and provisions.

### 1.14 Retirement benefits

The Company participates in its own separate section of the Railways Pension Scheme ("RPS"), which provides benefits on a defined benefit basis.

Defined benefit obligations are measured at discounted present value whilst scheme assets are recorded at fair value. Any recognised net asset is limited to the present value of economic benefits available in the form of any future refunds from the scheme or reductions in future contributions to the scheme.

The service costs of defined benefit schemes are spread systematically over the working lives of employees and included within operating profit. Scheme administration expenses are also included within operating profit. Net interest expense or income is calculated by applying the discount rate and included within finance expense or finance income. Actuarial gains and losses are recognised immediately in the statement of comprehensive income. Mortality rates are considered when retirement benefit obligations are calculated. Past service costs are recognised immediately in income.

A full actuarial valuation of the scheme is undertaken triennially and updated annually using independent actuaries following the projected unit credit method. The present value of the scheme obligations is determined by discounting the estimated future cash flows using interest rates of high quality corporate bonds which have terms to maturity equivalent to the terms of the related obligations. Experience adjustments and changes in assumptions which affect actuarial gains and losses are reflected in the actuarial gain or loss for the year.

The Company has no rights or obligations in respect of the RPS following the expiry of the related franchise. The liability or asset recognised for the relevant section of the RPS represents only that part of the net deficit (or surplus) of the section that the employer expects to fund (or recover) over the life of the franchise to which the section relates. Where the award of a new rail franchise to the Company results in a pension accounting liability, a corresponding intangible asset is recognised, reflecting a cost in obtaining the right to operate the franchise. When a pension accounting surplus results, a corresponding deferred income balance is recognised. The intangible asset or deferred income balance is amortised to the profit and loss account on a straight-line basis over the expected life of the related franchise.

To reflect the fact that the Company has no rights or obligations in respect of the RPS following the expiry of the related franchise, it calculates an amount (the "franchise adjustment") representing the extent to which the Company does not expect to fund the existing deficit over the course of the franchise period, being the present value at the pensions discount rate of the difference between the agreed schedule of contributions and the expected service costs over that period. The franchise adjustment is treated in a similar way to a plan asset with an interest credit recognised in the profit and loss account and re-measurement recognised in other comprehensive income.
Overall, and subject to any experience adjustments, the cumulative profit and loss account amounts in respect of the RPS, together with the related intangible asset/deferred income balance amortisation, by the end of the franchise period, will be equal to the cumulative contributions and franchise adjustment re-measurements in other comprehensive income that offset cumulative re-measurements of the other plan assets.

### 1.15 Dividends

Dividends are recorded in the Company's financial statements in the period in which they are approved by the Company's shareholders.

## 2 Significant judgements, estimates and accounting policies

The preparation of the financial statements in conformity with FRS 101 requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

The following accounting policies are considered critical accounting policies as they require a significant amount of management judgement and the results are material to the financial statements.

*Pensions*

The determination of the Company's pension benefit obligation and expense for defined benefit schemes is dependent on the selection by the Directors of certain assumptions used by the actuaries in calculating such amounts. Those assumptions include the discount rate, the annual rate of increase in future salary levels and mortality levels. The Directors' assumptions are based on actual historical experience and external data. Significant differences in actual experience or significant changes in assumptions may materially affect the pension obligation and future expense.
In the calculation of the franchise adjustment, the Company has determined to apply the IAS 19R discount rate. This adopted policy is considered appropriate as it reflects best the underlying nature of the arrangement in that it focuses on the difference between the expected service costs and the agreed cash contributions over the franchise period.

*Rail contractual positions*

The UK Rail industry is subject to a complex matrix of contractual relationships. The Company is party to contractual relationships with, amongst others, the Department for Transport, Network Rail and rolling stock lessors. The nature of these contracts is such that there can be uncertainty over amounts receivable or payable by the Company in accordance with the contracts. The Company makes estimates of the amounts receivable or payable based on available, relevant information. Actual outcomes can differ from the estimates made by the Company.

*Taxation*

Provisions for tax contingencies require management to make judgements and estimates in relation to tax issues and exposures. Amounts provided are based on management's interpretation of tax law and the likelihood of settlement. Tax benefits are not recognised unless the tax positions will probably be sustained. In arriving at this position, management reviews each material tax benefit to assess whether a provision should be taken against full recognition of the benefit on the basis of potential settlement through negotiation and/or litigation. All such provisions are included in current tax liabilities.

## Notes to the financial statements
## for the financial year ended 31 March 2016

### 3 Revenue

| | 2016 £000 | 2015 £000 |
|---|---|---|
| Passenger revenue | **1,017,036** | 969,893 |
| Catering revenue | **12,628** | 12,495 |
| Other trading income | **39,004** | 36,316 |
| | **1,068,668** | 1,018,704 |

All revenue arose within the United Kingdom.

Other trading income consists primarily of the provision of station facilities to other train operators, retail commissions receivable and car parking.

### 4 Other operating income

| | 2016 £000 | 2015 £000 |
|---|---|---|
| Network change compensation and performance regime | **54,101** | 37,489 |
| Property income | **3,290** | 2,547 |
| | **57,391** | 40,036 |

Network change compensation is receivable in respect of lost revenue and incremental costs incurred due to Network Rail's alterations of the track and infrastructure during the financial year.

Net performance regime income/expense is in respect of service disruption under the performance regime provisions of the track access agreement with Network Rail.

During the financial year the level of performance regime income has been impacted by the closure, for seven weeks, of the Lamington viaduct, situated on the West Coast Main Line between Carlisle and Glasgow.

### 5 Train operating expense

| | 2016 £000 | 2015 £000 |
|---|---|---|
| Rolling stock costs | **313,066** | 323,181 |
| Track access costs | **155,479** | 167,957 |
| Station and depot access costs | **15,638** | 15,572 |
| Power costs | **60,645** | 62,314 |
| Other operating costs | **86,345** | 87,004 |
| | **631,173** | 656,028 |

Other operating costs consist primarily of retail commissions payable, catering supplies and British Transport Police charges.

## Notes to the financial statements
## for the financial year ended 31 March 2016

### 6 Expenses and auditor's remuneration

Included in profit/loss are the following:

| | 2016 | 2015 |
|---|---|---|
| | £000 | £000 |
| Depreciation of property, plant and equipment | - | 202 |
| Rentals under operating leases: | | |
| - Plant and machinery | 119,609 | 119,479 |
| - Other | 11,467 | 11,240 |
| Rental income received on properties | (3,290) | (2,547) |
| Franchise expense (see below) | 158,129 | 105,226 |

**Auditor's remuneration**

| | 2016 | 2015 |
|---|---|---|
| Remuneration of the auditor and its associates: | | |
| - Audit of these financial statements | 88 | 86 |

Amounts receivable by the Company's auditor and its associates in respect of services to the Company and its associates, other than the audit of the Company's financial statements, have not been disclosed as the information is required instead to be disclosed on a consolidated basis in the consolidated financial statements of Virgin Rail Group Holdings Limited, the parent undertaking of the smallest group of undertakings, including the Company, for which consolidated financial statements are drawn up.

**Franchise expense**

| | 2016 | 2015 |
|---|---|---|
| | £000 | £000 |
| Franchise Agreement payments | 140,832 | 58,629 |
| Profit share payment under Franchise Agreement | 17,297 | 12,712 |
| Interim Franchise Agreement payments | - | 33,885 |
| | 158,129 | 105,226 |

The Franchise Agreement, applicable from 22 June 2014, includes a profit share arrangement whereby a share of the profit above certain pre-determined thresholds is payable to the DfT.

The Interim Franchise Agreement, applicable up to 21 June 2014, allowed for the Company receiving a pre-tax profit margin equivalent to 1% of revenue.

## Notes to the financial statements
## for the financial year ended 31 March 2016

### 7 Staff costs

**Headcount and total remuneration**

The average number of persons employed by the Company, including the directors, during the financial year, analysed by category, was as follows:

| | 2016<br>No. | 2015<br>No. |
|---|---|---|
| Management | 499 | 461 |
| Other staff | 2,680 | 2,607 |
| | 3,179 | 3,068 |

The aggregate payroll costs of these persons were as follows:

| | 2016<br>£000 | 2015<br>£000 |
|---|---|---|
| Wages and salaries | 144,288 | 138,699 |
| Social security costs | 13,463 | 12,487 |
| Other pension costs | 22,390 | 17,690 |
| | 180,141 | 168,876 |

**Directors' remuneration**

| | 2016<br>£000 | 2015<br>£000 |
|---|---|---|
| **Total remuneration** | | |
| Remuneration | 848 | 876 |
| Amounts receivable under long term incentive schemes | 494 | 573 |
| Contributions to defined benefit pension schemes | 81 | 76 |
| **Highest paid director** | | |
| Remuneration | 354 | 295 |
| Amounts receivable under long term incentive schemes | 190 | 220 |
| Contributions to defined benefit pension schemes | 28 | 25 |

During the financial year retirement benefits were accruing to 3 directors (2015: 3) in respect of defined benefit pension schemes.

The directors are considered to be the key management personnel of the Company.

## Notes to the financial statements
## for the financial year ended 31 March 2016

### 8 Finance income and expense

| | 2016 | 2015 |
|---|---|---|
| | £000 | £000 |
| **Finance income** | | |
| Bank interest receivable | 702 | 350 |
| Other interest receivable | 2 | 1 |
| Interest income on defined benefit pension schemes | 790 | - |
| | 1,494 | 351 |
| **Finance expense** | | |
| Amounts payable to group undertakings | (2) | (25) |
| Other interest payable | (37) | (14) |
| Interest charge on defined benefit pension schemes | - | (150) |
| | (39) | (189) |

## 9 Taxation

| | 2016 | 2015 |
|---|---|---|
| | £000 | £000 |
| **Current tax** | | |
| Current tax on income for the year | **21,853** | 13,587 |
| Adjustments in respect of prior years | **1,681** | 229 |
| **Total current tax** | **23,534** | 13,816 |
| **Deferred tax** | | |
| Origination and reversal of temporary differences | **(6,309)** | (878) |
| Adjustments in respect of prior years | **(1,538)** | 11 |
| Change in tax rate | **451** | - |
| **Total deferred tax (see note 18)** | **(7,396)** | (867) |
| **Tax on profit on ordinary activities** | **16,138** | 12,949 |

### Factors affecting tax charge for the financial year

The actual tax charge for the financial year differs from that computed by applying the standard tax rate to the profit before tax as reconciled below:

| | 2016 | 2015 |
|---|---|---|
| | £000 | £000 |
| Profit on ordinary activities before tax | **67,161** | 52,074 |
| Tax at UK corporation tax rate of 20% (2015: 21%) | **13,432** | 10,936 |
| Effects of: | | |
| Non deductible expenses | **378** | 40 |
| Non deductible pension expenses | **1,734** | 1,733 |
| Adjustments in respect of prior years | **143** | 240 |
| Change in tax rate | **451** | - |
| **Tax on profit on ordinary activities** | **16,138** | 12,949 |

### Factors that may affect future tax charges

Reductions in the UK corporation tax rate from 23% to 21% (effective from 1 April 2014) and 20% (effective from 1 April 2014) were substantively enacted on 2 July 2013. Further reductions to 19% (effective from 1 April 2017) and to 18% (effective from 1 April 2020) were substantively enacted on 26 October 2015. As the Franchise Agreement runs to 31 March 2018, the deferred tax asset at 31 March 2016 has been calculated at 19% (2015: 20%). An additional reduction to 17% (effective from 1 April 2020) was announced in the Budget on 16 March 2016. This will reduce the Company's future current tax charge accordingly.

## 10 Tangible fixed assets

| | Fixtures & fittings £000 |
|---|---|
| **Cost** | |
| At 1 April 2014 and 31 March 2015 | 40,856 |
| **Depreciation** | |
| At 1 April 2014 | 40,654 |
| Depreciation for the year | 202 |
| **At 31 March 2015** | 40,856 |
| **Carrying amount** | |
| **At 31 March 2015** | - |
| **Cost** | |
| At 1 April 2015 and 31 March 2016 | **40,856** |
| **Depreciation** | |
| At 1 April 2015 and 31 March 2016 | **40,856** |
| **Carrying amount** | |
| **At 31 March 2016** | - |

## 11 Investments

At the beginning and end of the financial year, the Company owned one ordinary share of four pence in each of ATOC Limited, Rail Settlement Plan Limited and Rail Staff Travel Limited and one ordinary share of one pound in NRES Limited.

## Notes to the financial statements
## for the financial year ended 31 March 2016

### 12 Stocks

| | 2016<br>£000 | 2015<br>£000 |
|---|---|---|
| Raw materials and consumables | **491** | 694 |

### 13 Debtors

| | Note | 2016<br>£000 | 2015<br>£000 |
|---|---|---|---|
| **Due after more than one year** | | | |
| Deferred tax | **18** | **9,495** | 2,288 |
| Derivative financial instruments | **19** | **72** | - |
| Retirement benefit asset | **20** | **11,710** | 17,310 |
| | | **21,277** | 19,598 |
| **Due within one year** | | | |
| Trade debtors | | **62,207** | 45,841 |
| Provision for doubtful debtors | | **(1,381)** | - |
| Net trade debtors | | **60,826** | 45,841 |
| Amount owed by related undertakings | | **43** | 105 |
| Other debtors | | **10,878** | 10,551 |
| Prepayments and accrued income | | **2,325** | 5,773 |
| | | **74,072** | 62,270 |

### 14 Cash at bank and in hand

| | 2016<br>£000 | 2015<br>£000 |
|---|---|---|
| Cash at bank and in hand | **96,720** | 105,448 |

## Notes to the financial statements
## for the financial year ended 31 March 2016

### 15 Creditors: Amounts falling due within one year

| | Note | 2016 £000 | 2015 £000 |
|---|---|---|---|
| Trade creditors | | **81,001** | 74,533 |
| Amount owed to related undertakings | | **394** | 518 |
| Group relief | | **25** | 14 |
| Corporation tax | | **12,921** | 14,838 |
| Other taxation and social security | | **5,233** | 4,492 |
| Deferred income | | **2,769** | 4,952 |
| Deferred season ticket income | | **5,936** | 5,635 |
| Other creditors | | **30,057** | 28,079 |
| Accruals | | **657** | 780 |
| Derivative financial instruments | 19 | **5,425** | 3,162 |
| | | **144,418** | 137,003 |

### 16 Creditors: Amounts falling due after more than one year

| | Note | 2016 £000 | 2015 £000 |
|---|---|---|---|
| Trade creditors | | **1,691** | 1,368 |
| Deferred income | | **2,769** | 4,939 |
| Other creditors | | **2,581** | 1,443 |
| Derivative financial instruments | 19 | **-** | 2,706 |
| | | **7,041** | 10,456 |

### 17 Provisions

| | Dilapidations provision £000 |
|---|---|
| At 1 April 2014 | 835 |
| Amounts provided in the year | 1,777 |
| Amounts utilised in the year | (24) |
| At 31 March 2015 | 2,588 |
| As at 1 April 2015 | **2,588** |
| Amounts provided in the year | **1,042** |
| Amounts utilised in the year | **(98)** |
| At 31 March 2016 | **3,532** |

The dilapidations provision relates to costs required to be incurred at properties leased by the Company in accordance with lease obligations. These costs are expected to be incurred by the end of the franchise.

## Notes to the financial statements
## for the financial year ended 31 March 2016

### 18 Deferred tax

The net deferred tax movement in the balance sheet is as follows:

| | £000 |
|---|---|
| Balance as at 1 April 2014 | 298 |
| Recognised in profit and loss account | 878 |
| Adjustments in respect of prior years | (11) |
| Recognised in equity | 1,123 |
| Balance as at 31 March 2015 | **2,288** |
| Recognised in profit and loss account | **5,858** |
| Adjustments in respect of prior years | **1,538** |
| Recognised in equity | **(189)** |
| Balance as at 31 March 2016 | **9,495** |

Deferred tax is attributable to the following:

| | 2016 £000 | 2015 £000 |
|---|---|---|
| Excess of capital allowances over depreciation | **8,073** | 3,887 |
| Short term temporary differences | **1,422** | (1,599) |
| | **9,495** | 2,288 |

The amount of deferred tax recognised in the profit and loss account by type of temporary difference is as follows:

| | 2016 £000 | 2015 £000 |
|---|---|---|
| Excess of capital allowances over depreciation | **2,648** | 2,242 |
| Change on adoption of FRS 101 | **3,010** | (1,653) |
| Other short term temporary differences | **200** | 289 |
| | **5,858** | 878 |

The amount of deferred tax recognised in equity by type of temporary difference is as follows:

| | 2016 £000 | 2015 £000 |
|---|---|---|
| Cash flow hedges: fuel derivatives | **(189)** | 1,123 |

Based on the anticipated profitable position of the Company during the remaining franchise period, the deferred tax asset has been recognised.

## Notes to the financial statements
## for the financial year ended 31 March 2016

### 19 Financial instruments

### (a) Carrying values of financial instruments

| | 2016 £000 | 2015 £000 |
|---|---|---|
| **Financial assets** | | |
| Current assets | | |
| - Trade debtors | **60,826** | 45,841 |
| - Other debtors | **10,878** | 10,551 |
| - Cash and cash equivalents | **96,720** | 105,448 |
| | **168,424** | 161,840 |
| **Financial liabilities** | | |
| Creditors: amounts falling due after more than one year | | |
| - Trade creditors | **(1,691)** | (1,368) |
| - Other creditors | **(2,581)** | (1,443) |
| Creditors: amounts falling due within one year | | |
| - Trade creditors | **(81,001)** | (74,533) |
| - Other creditors | **(30,057)** | (28,079) |
| | **(115,330)** | (105,423) |
| **Net financial assets** | **53,094** | 56,417 |

The carrying values of financial assets and liabilities are deemed to approximate their fair values.

Derivatives that are designated as effective hedging instruments are not shown in the above table. Information on the carrying value of such derivatives is provided in note 19 (d).

**Fair value estimation**

The fair values of the Company's financial instruments are disclosed in fair value hierarchy levels based on the valuation technique used to determine fair values as follows:

- Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2: Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices); and
- Level 3: Inputs for the asset or liability that are not based on observable market data (that is, unobservable inputs).

The only instruments carried at fair value by the Company are the derivative financial instruments that consist of fuel derivatives. These are listed at level 2 on the fair value hierarchy. Discounted cash flow is the valuation technique used to arrive at fair value.

For all other financial instruments that are not measured at fair value on a recurring basis, the directors consider that the carrying amounts of financial assets and financial liabilities approximate their fair values.

**19 Financial instruments** *(continued)*

**(b) Nature and extent of risks arising from financial instruments**

The Company's use of financial instruments exposes it to a variety of financial risks, principally:

- Market risk - including currency risk, interest rate risk and price risk;
- Credit risk; and
- Liquidity risk.

The Company's overall risk management programme focuses on the unpredictability of financial markets and seeks to reduce the likelihood and/or magnitude of adverse effects on the financial performance and financial position of the Company. The Company uses derivative financial instruments from time to time to reduce exposure to commodity price risk. The Company does not hold derivative financial instruments for speculative purposes.

The Company's risk management policies are established to identify and analyse the risks faced by the Company, to set appropriate limits and controls and to monitor risks and adherence to limits. The Treasury function of the Company implements the financial risk management policies under governance approved by the Board. The Treasury function identifies, evaluates and hedges financial risks. The Board approves the written principles for overall risk management, as well as written policies covering specific areas, such as foreign exchange risk, interest rate risk, credit risk, the use of derivative financial instruments and investment of excess liquidity.

**(i) Market risk**

Market risk is the risk that changes in market prices, such as foreign exchange rates, interest rates and commodity prices will affect the Company's financial performance and/or financial position. The objective of the Company's management of market risk is to manage and control market risk exposures within acceptable parameters.

The Company enters into derivative financial instruments in the ordinary course of business, and also incurs financial liabilities, in order to manage market risk. Generally the Company seeks to apply hedge accounting in order to reduce volatility in the profit and loss account.

**Foreign currency translational risk**

Foreign currency transactional risk is the risk that future cash flows (such as from purchases of goods and services) will fluctuate because of changes in foreign exchange rates.

The Company is exposed to limited foreign currency transactional risk due to the low value of transactions entered into in currencies other than the functional currency.

The Company's exposure to commodity price risk includes a foreign currency element due to the impact of foreign exchange rate movements on the sterling cost of fuel for the Company's operations. The effect of foreign exchange rate movements on sterling-denominated fuel prices is managed through the use of fuel derivatives denominated in the functional currency in which the fuel is purchased. Further information on fuel hedging is given under the heading "Price risk" below.

**Interest rate risk**

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Company has limited exposure to this risk as it has no borrowings.

**19 Financial instruments** *(continued)*

**(i) Market risk** *(continued)*

**Price risk**

The Company is exposed to commodity price risk. The Company's operations as at 31 March 2016 consume approximately 27.5 million litres of diesel fuel per annum. As a result, the Company's profit is exposed to movements in the underlying price of fuel.

The Company's objective in managing commodity price risk is to reduce the risk that movements in fuel prices result in adverse movements in its profit and cash flow. The Company has a policy of managing volatility in its fuel costs by maintaining an ongoing fuel hedging programme whereby derivatives are used to fix or cap the variable unit cost of a percentage of projected future fuel costs, after taking account of derivatives in place, which varies due to movements in fuel prices.

The fuel derivatives hedge the underlying commodity price risk (denominated in US$) and they also hedge the currency risk due to the commodity being priced in US$ and the functional currency of the Company being pounds sterling.

At 31 March 2016 and 31 March 2015, the projected fuel costs (excluding premia payable on fuel derivatives, delivery margins, fuel taxes and fuel tax rebates) for the next twelve months were:

| | **2016**<br>**£000** | 2015<br>£000 |
|---|---|---|
| Costs subject to fuel swaps | **(10,014)** | (10,014) |
| Costs not subject to fuel swaps | **(1,181)** | (1,698) |

The figures in the above table are after taking account of derivatives and applying the fuel prices and foreign exchange rates at the balance sheet date.

If all of the relevant fuel prices were 10% higher at the balance sheet date, the amounts in the above table would change by the following:

| | **2016**<br>**£000** | 2015<br>£000 |
|---|---|---|
| Costs not subject to fuel swaps | **(118)** | (170) |
| Decrease in projected profit before taxation | **(118)** | (170) |

If all of the relevant fuel prices were 10% lower at the balance sheet date, the amounts in the above table would change by the following:

| | **2016**<br>**£000** | 2015<br>£000 |
|---|---|---|
| Costs not subject to fuel swaps | **118** | 170 |
| Increase in projected profit before taxation | **118** | 170 |

Demand for the Company's services can also be affected by movements in fuel prices due to the impact on the cost of competing transport service, including private cars.

The Company is also exposed to changes in electricity prices as electricity is consumed to power some of the trains operated. The Company has some protection to price changes via rail industry arrangements to fix the price on a proportion of anticipated electricity consumption.

## 19 Financial instruments *(continued)*

### (ii) Credit risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations.

Credit risk arises from cash and cash equivalents, derivative financial instruments and deposits with banks and financial institutions, as well as credit exposures to amounts due from outstanding receivables.

The Company's objective is to minimise credit risk to an acceptable level whilst not overly restricting the Company's ability to generate revenue and profit. It is the Company's policy to invest cash assets safely and profitably. To control credit risk, counterparty credit limits are set by reference to published credit limits.

The maximum exposure to credit risk is limited to the carrying value of each class of asset as summarised in the table at the beginning of this note. The Company's exposure to credit risk is influenced mainly by the individual characteristics of each customer or counterparty. The Company's largest credit exposures are to financial institutions with short-term credit ratings of A2 (or equivalent) or better, the Department for Transport and Rail Settlement Plan Limited, all of which the Company considers unlikely to default on their respective liabilities to the Company.

The movement in the provision for impairment for trade and other receivables is shown in note 13.

The ageing of financial assets past due, but not impaired is shown below:

| | **2016** | 2015 |
|---|---|---|
| | **£000** | £000 |
| 1-30 days | **-** | 326 |
| 31-60 days | **108** | - |
| Total | **108** | 326 |

The Company does not hold any collateral to mitigate this exposure.

### (iii) Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. The Company's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Company's reputation.

The Company monitors its cash requirements on an ongoing basis. Typically the Company ensures that it has sufficient cash on demand to meet expected operational expenses and impending capital calls and investment funding for a period of 24 months. This includes the servicing of financial obligations but excludes the potential impact of extreme circumstances that cannot be reasonably predicted, such as natural disasters.

**19 Financial instruments** *(continued)*

**(iii) Liquidity risk** *(continued)*

The maturity profile of financial liabilities based on undiscounted gross cash flows and contractual maturities is as follows:

| | | | | | **2016** |
|---|---|---|---|---|---|
| | **Carrying amount £000** | **Contractual cash flows £000** | **Within 1 year £000** | **1-2 years £000** | **2-5 years £000** |
| **Non-derivative financial liabilities** | | | | | |
| Trade and other payables | (115,330) | (115,330) | (111,058) | (4,272) | - |
| **Derivative financial liabilities** | | | | | |
| Derivatives used for hedging | (5,425) | (5,425) | (5,425) | - | - |

| | | | | | 2015 |
|---|---|---|---|---|---|
| | Carrying amount £000 | Contractual cash flows £000 | Within 1 year £000 | 1-2 years £000 | 2-5 years £000 |
| **Non-derivative financial liabilities** | | | | | |
| Trade and other payables | (105,423) | (105,423) | (102,612) | - | (2,811) |
| **Derivative financial liabilities** | | | | | |
| Derivatives used for hedging | (5,868) | (5,868) | (3,162) | (2,706) | - |

**(c) Capital management**

The Company regards its capital as comprising its equity and cash. The Company's objectives when managing capital are to safeguard the Company's ability to continue as a going concern in order to provide returns for shareholders and benefits for other stakeholders. The capital structure of the Company is kept under regular review.

**(d) Hedge accounting**

The Company's current hedging arrangements are summarised below:

| | |
|---|---|
| **Type of hedge** | Cash flow hedges |
| **Risks hedged by Company** | Commodity price risk |
| **Hedging instruments used** | Derivatives (commodity swaps) |

The Company's cash flow hedges run to the end of the franchise and are settled on a monthly basis.

## 19 Financial instruments *(continued)*

### (d) Hedge accounting *(continued)*

**Carrying value and fair value of derivative financial instruments**

Derivative financial instruments are classified on the balance sheet as follows:

| | 2016 £000 | 2015 £000 |
|---|---|---|
| **Non current assets** | | |
| Fuel derivatives | 72 | - |
| **Current liabilities** | | |
| Fuel derivatives | (5,425) | (3,162) |
| **Non current liabilities** | | |
| Fuel derivatives | - | (2,706) |
| Total fuel derivatives | (5,353) | (5,868) |

The fair value of derivative financial instruments is equal to their carrying value, as shown in the above table.

The fair value of fuel derivatives split by maturity is shown above.

The movements in the fair value of fuel derivatives in the financial year were as follows:

| | 2016 £000 | 2015 £000 |
|---|---|---|
| Fair value at start of year | (5,868) | - |
| Changes in fair value during year taken to cash flow hedging reserve | (3,715) | (6,925) |
| Cash paid during the year | 4,230 | 1,057 |
| Fair value at end of year | (5,353) | (5,868) |

The fair value of fuel derivatives is further analysed as follows:

| | Fair value £000 | Notional quantity of fuel covered by derivatives Thousands of litres |
|---|---|---|
| **As at 31 March 2016** | (5,353) | 45,870 |
| As at 31 March 2015 | (5,868) | 45,750 |

19 **Financial instruments** *(continued)*

(d) **Hedge accounting** *(continued)*

**Cash flow hedging reserve**

The movements in the cash flow hedging reserve were as follows:

| | Fuel derivatives £000 |
|---|---|
| At 1 April 2014 | - |
| Changes in fair value during the year taken to cash flow hedging reserve | (6,925) |
| Cash flow hedges reclassified and reported in profit for year | 1,311 |
| Tax effect of cash flow hedges | 1,123 |
| At 31 March 2015 | (4,491) |
| | |
| At 1 April 2015 | **(4,491)** |
| Changes in fair value during the year taken to cash flow hedging reserve | **(3,715)** |
| Cash flow hedges reclassified and reported in profit for year | **4,417** |
| Tax effect of cash flow hedges | **(189)** |
| At 31 March 2016 | **(3,978)** |
| | |
| Cash flow hedging reserve before tax | **(4,912)** |
| Tax to be credited to income statement in future periods | **934** |
| Cash flow hedging reserve after tax | **(3,978)** |

There have been no instances during the year ended 31 March 2016 (2015: None) where a forecast transaction for which hedge accounting had previously been used was no longer expected to occur.

## 20 Retirement benefits

### (a) Description of retirement benefit arrangements

The Company participates in its own separate shared cost section of the Railways Pension Scheme ("RPS"). The RPS is a funded scheme and provides benefits based on final pensionable pay. The assets of the RPS are held separately from those of the Company. The RPS is a shared costs scheme with costs being shared between the employer and the members on the basis of a 60:40 split.

The Company has no rights or obligations in respect of the RPS following expiry of the related franchise. Therefore, the liability (or asset) recognised for the relevant section of the RPS reflects only that part of the net deficit (or surplus) of the section that the employer is expected to fund (or expected to recover) over the life of the franchise to which the section relates.

The latest actuarial valuation of the Company's section of the RPS was undertaken at 31 December 2013 using the projected unit method. This valuation has been updated to 31 March 2016 by a qualified independent actuary, using revised assumptions that are consistent with the requirements of IAS 19.

### (b) Principal actuarial assumptions

The principal actuarial assumptions at the balance sheet date were as follows:

| | **2016** | 2015 |
|---|---|---|
| Discount rate | **3.8%** | 3.4% |
| RPI inflation assumption | **3.0%** | 3.0% |
| CPI inflation assumption | **1.7%** | 2.0% |
| Rate of increase in pensionable salaries | **2.5%** | 4.0% |
| Rate of increase of pensions in payment | **1.7%** | 2.0% |
| Post-retirement mortality (life expectancies in years) | | |
| - Current pensioners at 60 - male | **26.0** | 26.0 |
| - Current pensioners at 60 - female | **28.5** | 28.5 |
| - Future pensioners at 60 aged 40 now - male | **28.5** | 28.5 |
| - Future pensioners at 60 aged 40 now - female | **31.0** | 31.0 |

The assumptions relating to longevity underlying the pension liabilities at the balance sheet date are based on standard actuarial mortality tables and include an allowance for future improvements in longevity.

**20 Retirement benefits** *(continued)*

**(c) Pension amounts recognised in the balance sheet**

The amounts recognised in the balance sheet were as follows:

| | 2016 £000 | 2015 £000 |
|---|---|---|
| Growth Pooled Fund* | **434,128** | 406,378 |
| Private Equity | **63,174** | 59,417 |
| Infrastructure | **9,985** | 10,411 |
| Cash | **3,123** | 2,704 |
| Fair value of section assets | **510,410** | 478,910 |
| Present value of defined benefit obligations | **(656,740)** | (741,730) |
| Deficit in section | **(146,330)** | (262,820) |
| Members share of section | **58,530** | 105,130 |
| Franchise adjustment | **99,510** | 175,000 |
| Surplus recognised by Company | **11,710** | 17,310 |

*The Growth Pooled Fund is the principal investment vehicle for the Company's section of the RPS. This fund is a multi-asset fund, tactically adjusted by the RPS Investment team.

**(d) Movement in surplus recognised by Company**

| | 2016 £000 | 2015 £000 |
|---|---|---|
| At beginning of year | **17,310** | 3,120 |
| Employer contributions | **12,930** | 12,250 |
| Expense charged to profit and loss account | **(21,600)** | (17,840) |
| Recognised in the statement of comprehensive income | **3,070** | 8,107 |
| Surplus at start of new Franchise Agreement | **-** | 13,720 |
| Extinguish surplus from Interim Franchise Agreement | **-** | (2,047) |
| At end of year | **11,710** | 17,310 |

From 22 June 2014, the Interim Franchise Agreement was superseded by a new Franchise Agreement. The pension surplus remaining from the Interim Franchise Agreement at 22 June 2014 has been extinguished, with a corresponding debit to the profit and loss account within other operating charges, and superseded by the surplus in relation to the new Franchise Agreement.

**(e) Sensitivity analysis**

The following is an approximate sensitivity analysis of the impact of the change in the key actuarial assumptions. In isolation, the following adjustments would adjust the pension surplus as follows:

| | 2016 £000 |
|---|---|
| Discount rate - increase of 0.1% | **(620)** |
| Price inflation - increase of 0.1% | **610** |
| Rate of increase in pensionable salaries - increase of 0.1% | **300** |
| Rate of increase of pensions in payment - increase of 0.1% | **310** |
| Increase in life expectancy of pensioners or non-pensioners by 1 year | **610** |

## Notes to the financial statements
## for the financial year ended 31 March 2016

**20 Retirement benefits** *(continued)*

**(f) Pension amounts recognised in profit and loss account**

The amounts recognised in the profit and loss account were as follows:

| | 2016 £000 | 2015 £000 |
|---|---|---|
| Current service cost | (21,310) | (16,650) |
| Past service cost | (260) | (270) |
| Administration costs | (820) | (770) |
| Included in operating profit | (22,390) | (17,690) |
| Net interest (expense)/income | (5,160) | (4,780) |
| Unwinding of franchise adjustment | 5,950 | 4,630 |
| | (21,600) | (17,840) |

Service costs and administration costs are recognised in operating costs and net interest and unwinding of franchise adjustment are recognised in net finance costs.

**(g) Pension amounts recognised in statement of comprehensive income**

The amounts recognised in the statement of comprehensive income were as follows:

| | 2016 £000 | 2015 £000 |
|---|---|---|
| Actual return on scheme assets higher than discount rate | 15,460 | 57,150 |
| Changes in financial assumptions | 77,500 | (68,800) |
| Changes in demographic assumptions | - | (4,400) |
| Experience on benefit obligations | (8,450) | (27,900) |
| Change in franchise adjustment | (81,440) | 52,057 |
| | 3,070 | 8,107 |

**(h) Benefit obligations**

Changes in the present value of the defined benefit obligations are analysed as follows:

| | 2016 £000 | 2015 £000 |
|---|---|---|
| At beginning of year | 461,600 | 403,910 |
| Current service cost | 21,310 | 16,650 |
| Past service cost | 260 | 270 |
| Rail franchise change | - | (11,673) |
| Interest on benefit obligations | 14,990 | 15,820 |
| Unwinding of franchise adjustment | (5,950) | (4,630) |
| Benefits paid | (13,960) | (15,340) |
| Contributions by employees | 8,060 | 7,550 |
| *Actuarial losses/(gains) due to:* | | |
| - Changes in financial assumptions | (77,500) | 68,800 |
| - Changes in demographic assumptions | - | 4,400 |
| - Experience on benefit obligations | 8,450 | 27,900 |
| - Change in franchise adjustment | 81,440 | (52,057) |
| At end of year | 498,700 | 461,600 |

**20 Retirement benefits** *(continued)*

**(i) Scheme assets**

The movement in the fair value of scheme assets was as follows:

| | **2016** | 2015 |
|---|---|---|
| | **£000** | £000 |
| At beginning of year | **478,910** | 407,030 |
| Administration costs | **(820)** | (770) |
| Interest income | **9,830** | 11,040 |
| Employer contributions | **12,930** | 12,250 |
| Contributions by employees | **8,060** | 7,550 |
| Benefits paid | **(13,960)** | (15,340) |
| Remeasurement gain/(loss) | **15,460** | 57,150 |
| At end of year | **510,410** | 478,910 |

## Notes to the financial statements
## for the financial year ended 31 March 2016

### 21 Capital and reserves

#### (a) Share capital

| | 2016 | 2015 |
|---|---|---|
| | £ | £ |
| **Allotted, called up and fully paid** | | |
| 1 ordinary shares of £1 | 1 | 1 |

#### (b) Reserves

A reconciliation of the movements in each reserve is shown in the Statement of changes in equity.

The balance held in the profit and loss account reserve is the accumulated retained profits of the Company.

The cash flow hedging reserve records the portion of the gain or loss on a hedging instrument in a cash flow hedge that is determined to be an effective hedge. The cumulative gain or loss is recycled to the profit and loss account to match the recognition of the hedged item through the profit and loss account.

### 22 Commitments

#### (i) Commitments under operating leases

Non-cancellable operating lease rentals are payable as follows:

| | 2016 | | 2015 | |
|---|---|---|---|---|
| | Plant and machinery £000 | Other operating leases £000 | Plant and machinery £000 | Other operating leases £000 |
| Less than one year | 119,458 | 11,762 | 119,196 | 11,519 |
| Between one and five years | 119,458 | 11,997 | 116,609 | 11,749 |
| | 238,916 | 23,759 | 235,805 | 23,268 |

#### (ii) Other financial commitments

The Company has, in the normal course of business, entered into a number of long term supply contracts. The most significant of these relate to track and station access facilities, train maintenance arrangements and IT outsourcing.

Under the Franchise Agreement, there is a requirement for the Company to comply with certain performance and other obligations. If the Company fails to comply with these obligations, it may be liable to penalties or the potential termination of the franchise.

#### (iii) Capital commitments

The Company had no capital commitments at 31 March 2016 (2015: £Nil).

## 23 Related parties

At 31 March 2016 and 31 March 2015, the Company's ultimate parent undertaking was Virgin Group Holdings Limited, whose sole shareholder is Sir Richard Branson.

The shareholder of Virgin Group Holdings Limited has interests directly or indirectly in certain other companies which are considered to give rise to related party disclosures under International Accounting Standard 24: Related Party Disclosures.

During the financial year, the Company entered into the following transactions with related parties:

| | 2016 | 2015 |
|---|---|---|
| | £000 | £000 |
| **Companies related by virtue of common control or ownership** | | |
| Revenue | **220** | 179 |
| Purchases | **(2,764)** | (1,679) |
| Receivables outstanding | **36** | 16 |
| Payables outstanding | **-** | (105) |

Related party purchases are principally in respect of management services, royalty fees and commission.

## 24 Ultimate parent company and parent undertaking of larger group

The parent undertaking of the smallest group of undertakings, including the Company, for which consolidated financial statements are drawn up is Virgin Rail Group Holdings Limited. The parent undertaking of the largest group of undertakings, including the Company, for which consolidated financial statements are drawn up is Virgin UK Holdings Limited.

Copies of the Virgin Rail Group Holdings Limited and Virgin UK Holdings Limited consolidated financial statements are available to the public and may be obtained from the Registrar of Companies, Companies House, Crown Way, Cardiff, CF14 3UZ.

As at 31 March 2016 the ultimate parent company is Virgin Group Holdings Limited, a company registered in the British Virgin Islands.

**Notes to the financial statements**
**for the financial year ended 31 March 2016**

### 25 First time adoption of FRS 101

These financial statements, for the year ended 31 March 2016, are the first the Company has prepared in accordance with Financial Reporting Standard 101 'Reduced Disclosure Framework' ("FRS 101"). For periods up to and including the year ended 31 March 2015, the Company prepared its financial statements in accordance with UK GAAP.

Accordingly, the Company has prepared financial statements which comply with FRS 101 applicable for periods ending on or after 31 March 2016, together with the comparative period data as at and for the year ended 31 March 2015, as described in the accounting policies.

In preparing these financial statements, the Company's opening balance sheet was prepared as at 1 April 2014, the Company's date of transition to FRS 101.

This note explains the principal adjustments made by the Company in restating its UK GAAP balance sheet as at 31 March 2014 and its previously published UK GAAP financial statements as at and for the year ended 31 March 2015.

**Balance sheet**

**As at 31 March 2014**

| | As per UK GAAP £000 | (A) Reclass-ifications £000 | UK GAAP after re-classification £000 | (B) Remeas-urements £000 | As per FRS 101 £000 |
|---|---|---|---|---|---|
| Fixed assets | 522 | - | 522 | (320) | 202 |
| Current assets | 114,251 | 116 | 114,367 | 1,646 | 116,013 |
| Creditors: amounts falling due after more than one year | (90,326) | 1,051 | (89,275) | (2,832) | (92,107) |
| Creditors: amounts falling due within than one year | (21,000) | (1,051) | (22,051) | - | (22,051) |
| Provisions for liabilities | (835) | - | (835) | - | (835) |
| Pension liability, net of tax | (464) | (116) | (580) | 580 | - |
| Equity | 2,148 | - | 2,148 | (926) | 1,222 |

**As at 31 March 2015**

| | As per UK GAAP £000 | (A) Reclass-ifications £000 | UK GAAP after re-classification £000 | (B) Remeas-urements £000 | As per FRS 101 £000 |
|---|---|---|---|---|---|
| Fixed assets | 3,316 | - | 3,316 | (3,316) | - |
| Current assets | 172,588 | 58 | 172,646 | 15,364 | 188,010 |
| Creditors: amounts falling due after more than one year | (131,954) | 2,811 | (129,143) | (7,860) | (137,003) |
| Creditors: amounts falling due after more than one year | - | (2,811) | (2,811) | (7,645) | (10,456) |
| Provisions for liabilities | (2,588) | - | (2,588) | - | (2,588) |
| Pension liability, net of deferred tax | (232) | (58) | (290) | 290 | - |
| Equity | 41,130 | - | 41,130 | (3,167) | 37,963 |

## 25 First time adoption of FRS 101 *(continued)*

### Profit and loss account and other comprehensive income

| For the year ended 31 March 2015 | As per UK GAAP £000 | (B) Remeasurements £000 | As per FRS 101 £000 |
|---|---|---|---|
| **Revenue** | 1,018,704 | - | 1,018,704 |
| Other operating income | 40,036 | - | 40,036 |
| Train operating expenditure | (656,028) | - | (656,028) |
| Staff costs | (168,876) | - | (168,876) |
| Depreciation and amortisation | (1,604) | 1,402 | (202) |
| Other operating charges | (186,131) | 4,409 | (181,722) |
| **Operating profit** | 46,101 | 5,811 | 51,912 |
| Finance income | 6,331 | (5,980) | 351 |
| Finance expense | (39) | (150) | (189) |
| **Profit on ordinary activities before tax** | 52,393 | (319) | 52,074 |
| Tax on ordinary activities | (10,566) | (2,383) | (12,949) |
| **Profit for the financial year** | 41,827 | (2,702) | 39,125 |
| | | | |
| **Other comprehensive income** | | | |
| *Items that will not be reclassified to profit or loss:* | | | |
| Remeasurements of defined benefit pension scheme | 3,155 | 4,952 | 8,107 |
| | | | |
| *Items that are or may be reclassified to profit or loss:* | | | |
| Cash flow hedges: | | | |
| - Changes in fair value during the year | - | (6,925) | (6,925) |
| - Reclassified and reported in profit for the year | - | 1,311 | 1,311 |
| - Tax effect of cash flow hedges | - | 1,123 | 1,123 |
| | - | (4,491) | (4,491) |
| | | | |
| **Other comprehensive income for the financial year, net of tax** | 3,155 | 461 | 3,616 |
| | | | |
| **Total comprehensive income for the financial year** | 44,982 | (2,241) | 42,741 |

## 25 First time adoption of FRS 101 *(continued)*

### Reclassifications

| Balance sheet | Notes | 31 March 2015 £000 | 31 March 2014 £000 |
|---|---|---|---|
| Current assets | | | |
| Deferred tax | (i) | 58 | 116 |
| Creditors: amounts falling due within one year | | | |
| Trade and other payables | (ii) | 2,811 | 1,051 |
| Creditors: amounts falling due within one year | | | |
| Trade and other payables | (ii) | (2,811) | (1,051) |
| Pension liability, net of tax | | (58) | (116) |

**Notes**

**(i)** Deferred tax on the pension liability was previously netted against the pension liability balance. In accordance with FRS101 it is now presented within the deferred tax balance.

**(ii)** These reclassifications are to disaggregate certain trade and other payables between current and non current elements.

**Notes to the financial statements**
**for the financial year ended 31 March 2016**

## 25 First time adoption of FRS 101 *(continued)*

**Remeasurements**

| **Balance sheet** | **Notes** | **31 March 2015 £000** | **31 March 2014 £000** | **Cumulative total £000** |
|---|---|---|---|---|
| Fixed assets | | | | |
| Intangible assets | (i) | (3,316) | (320) | (3,636) |
| Current assets | | | | |
| Deferred tax | (ii) | (1,946) | (1,474) | (3,420) |
| Retirement benefit asset | (v) | 17,310 | 3,120 | 20,430 |
| | | 15,364 | 1,646 | 17,010 |
| Creditors: amounts falling due within one year | | | | |
| Trade and other payables | (i) | (4,698) | (2,832) | (7,530) |
| Derivative financial instruments | (iv) | (3,162) | - | (3,162) |
| | | (7,860) | (2,832) | (10,692) |
| Creditors: amounts falling due after more than one year | | | | |
| Trade and other payables | (i) | (4,939) | - | (4,939) |
| Derivative financial instruments | (iv) | (2,706) | - | (2,706) |
| | | (7,645) | - | (7,645) |
| Pension liability, net of tax | (v) | 290 | 580 | 870 |
| Net assets | | (3,167) | (926) | (4,093) |
| Equity | | | | |
| Retained earnings | | 1,324 | (926) | 398 |
| Cash flow hedging reserve | | (4,491) | - | (4,491) |
| | | (3,167) | (926) | (4,093) |

**25 First time adoption of FRS 101** *(continued)*

| **Statement of profit or loss and other comprehensive income** | **Note** | **Year ended 31 March 2015 £000** |
|---|---|---|
| Depreciation and amortisation | (i) | 1,402 |
| Other operating charges | (i) | 6,661 |
| Other operating charges | (v) | (2,252) |
| **Operating profit** | | 5,811 |
| Finance income | (v) | (5,980) |
| Finance costs | (v) | (150) |
| **Profit on ordinary activities before tax** | | (319) |
| Tax on ordinary activities | (ii) and (iii) | (2,383) |
| **Profit for the financial year** | | (2,702) |
| **Other comprehensive income** | | |
| *Items that will not be reclassified to profit and loss:* | | |
| Remeasurements of defined benefit pension scheme | | 4,952 |
| *Items that are or may be reclassified to profit and loss:* | | |
| Cash flow hedges: | | |
| - Changes in fair value during the year | (iv) | (6,925) |
| - Reclassified and reported in profit for the year | (iv) | 1,311 |
| - Tax effect of cash flow hedges | (ii) | 1,123 |
| | | (4,491) |
| **Other comprehensive income for the financial year, net of tax** | | 461 |
| **Total comprehensive income for the financial year** | | (2,241) |

**Notes**

(i) Under UK GAAP where a pension deficit was assumed at the start of the Franchise Agreement, a corresponding intangible asset was recognised, reflecting a cost in acquiring the right to operate the franchise. On transition the Company has changed the assumptions used in measuring the franchise adjustment. Calculating the franchise adjustment includes considering the expected return on plan assets in the relevant section over the life of the related franchise. The Company has determined to apply the IAS 19R discount rate rather than an expected real return on plan assets. This policy is considered more appropriate than computing the franchise adjustment on the basis (as formerly adopted) of an estimate of the franchise-end deficit for which the Company will not be responsible. That alternative would have resulted in the same cumulative total comprehensive income by the end of the franchise period but split between the statement of profit or loss and, in other comprehensive income, the re-measurements of plan assets other than the franchise adjustment.
This has resulted in an accounting surplus for the West Coast section of the Railways Pension Scheme and a corresponding deferred income balance has been recognised. The change to IFRS has therefore resulted in the release of the intangible asset and reversal of amortisation. The deferred income balance is amortised to the income statement on a straight-line basis over the expected life of the franchise.

(ii) This journal reflects the deferred tax effect of the adjustments arising from the first time adoption of FRS 101.

(iii) Under UK GAAP, deferred tax was provided on certain timing differences that had originated but not reversed at the balance sheet date. Under FRS 101, deferred tax is provided on temporary differences based upon future recovery or settlement of assets and liabilities recognised in the balance sheet.

**25 First time adoption of FRS 101** *(continued)*

(iv) Under UK GAAP the gain or loss on derivative financial instruments would not be recognised until the maturation of the contract. Under FRS 101 derivative financial instruments are initially recognised at fair value and subsequently re-measured at fair value. The derivative financial instruments have been designated as cash flow hedges with the effective portion of the gain or loss on the hedging instrument being recognised in the statement of comprehensive income, while the ineffective portion is recognised in the profit and loss account.

(v) The effect of applying IAS 19 'Employee Benefits' ("IAS19R") is that the Company's annual expense for defined benefit schemes now includes net interest expense or income calculated by applying the discount rate to the net defined benefit asset or liability. This net interest expense or income replaces the finance charge on scheme liabilities and the expected return on scheme assets and results in a higher annual expense.

The asset for the West Coast section of the Railways Pension Scheme reflects the difference between the expected service costs and the expected cash contributions over the life of the franchise to which the section relates.