

KCH (HOLDINGS) LIMITED

Annual Report and Financial Statements

for the year ended 31 March 2017



KCH (HOLDINGS) LIMITED

ANNUAL REPORT AND FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2017

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KCH (HOLDINGS) LIMITED

OFFICERS AND PROFESSIONAL ADVISERS

DIRECTORS

P Simpson (resigned 10 October 2016)
W Halbert

COMPANY SECRETARY

K Smith

REGISTERED OFFICE

37 Carr Lane
Hull
HU1 3RE

BANKERS

Royal Bank of Scotland
3rd Floor,
2 Whitehall Quay
Leeds
LS1 4HR

INDEPENDENT AUDITORS

PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
Embankment Place
London
WC2N 6RH

KCH (HOLDINGS) LIMITED

STRATEGIC REPORT FOR THE YEAR ENDED 31 MARCH 2017

The director presents the strategic report and the audited financial statements of the company for the year ended 31 March 2017. These financial statements are prepared under United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice), including Financial Reporting Standard 101 Reduced Disclosure Framework (FRS 101).

PRINCIPAL ACTIVITIES AND REVIEW OF THE BUSINESS

The principal activities of the company are the administration of the Group's payroll function and pension schemes, as well as being an intermediate holding company. The results for the year include the Group's staff costs and reserves associated with the sale of related services to another Group company. Also included are dividends received from subsidiary undertakings and interest on the Group's external borrowings. The company is incorporated in England and Wales and domiciled in England.

RESULTS

The profit for the financial year attributable to shareholders amounts to £62,134,000 (2016: loss of £10,716,000).

REVIEW OF THE BUSINESS

On 31 March 2016, the Group brought together its four brands into one business under the common brand name, KCOM.

As part of this process, the Group completed the next stage of the simplification of its statutory entity structure, resulting in certain assets and liabilities of the company being transferred to KCOM Holdings Limited, a fellow group company incorporated in the United Kingdom. The function of KCH (Holdings) Limited being changed to administer the Group payroll and pension schemes and hold external borrowings.

As a result, the company incurred employee costs relating to all employees of the Group, excluding 138 employed by KCOM Contact Centres Limited. The services provided by these employees have been sold to other Group entities resulting in revenues of £85,084,000.

In the current year the company received dividend income of £65,017,000 from subsidiary companies (2016: £Nil). These combined factors have resulted in an EBITDA before exceptionals of £66,701,000 (2016: loss of £6,891,000).

Exceptional costs of £3,414,000 (2016: £301,000) have been recognised in the year relating to restructuring costs associated with redundancies as a result of organisational changes.

KEY PERFORMANCE INDICATORS

	Year ended 31 March 2017 £'000	Year ended 31 March 2016 £'000
Revenue	85,084	28,408
EBITDA before exceptional items	66,701	(6,891)
Profit/(loss) before taxation and exceptional items (%)	76%	(45%)

YEAR END POSITION

As at 31 March 2017, the company remains in a strong net asset position.

At the year end, the company has external borrowings of £50.0 million (2016: £Nil). In September 2016, the Group agreed a new five year £180.0 million revolving credit facility on the same terms as the previous arrangement (see note 18 for further details).

STRATEGIC OBJECTIVES

The company's strategic objectives are to support the KCOM Group in achieving its strategic objectives, which can be found in KCOM Group PLC's annual report and financial statements on pages 20 and 21.

KCH (HOLDINGS) LIMITED
STRATEGIC REPORT FOR THE YEAR ENDED 31 MARCH 2017

PRINCIPAL RISKS AND UNCERTAINTIES

The principal risks associated with the company are considered to be resilience of our IT systems, and health and safety. Further details of the risks can be found on pages 26 to 29 of the Strategic Report in the annual report and financial statements of the KCOM Group PLC.

Approved by the board, and signed on its behalf



W Halbert
Director,
12 October 2017

KCH (HOLDINGS) LIMITED

DIRECTOR'S REPORT FOR THE YEAR ENDED 31 MARCH 2017

The director present the annual report and the audited financial statements of the company for the year ended 31 March 2017. These financial statements are prepared under United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice), including Financial Reporting Standard 101 Reduced Disclosure Framework (FRS 101).

FUTURE DEVELOPMENTS

The Director is focused on maintaining the company as a holding company. For further details of future developments of the group, see pages 20 to 21 in the KCOM Group PLC annual report and financial statements.

DIVIDENDS

The director has paid ordinary dividends of £32,464,000 (2016: £36,155,000) during the year. The director recommend a final dividend of £Nil per share, amounting to £Nil.

FINANCIAL RISK MANAGEMENT

In the normal course of business, the company is exposed to certain financial risks, principally interest rate risk, liquidity risk and credit risk. These risks are managed by the central treasury function of KCOM Group PLC, in conjunction with the company, in accordance with risk management policies that are designed to minimise the potential adverse effects of these risks on financial performance. The policies are reviewed and approved by the Board of KCOM Group PLC.

Further details of the financial risk management policies can be found on page 42 of the Directors' Report in the annual report and financial statements of the KCOM Group PLC.

EMPLOYEES

The company encourages its employees to be aware of the financial and economic factors affecting the performance of the company. A consultative committee has been established which meets regularly.

Employment policies are designed to provide equal opportunities irrespective of colour, ethnic or national origin, nationality, sex, religion, material or disabled status. Full consideration is given to the employment, training and career development of disabled persons.

Health and safety is an integral part of good business management, and well established systems of safety management are in place throughout the company. The company's employment policy is in accordance with that of the Group, further details of which can be found on page 32 of the Strategic Report in the annual report and financial statements of KCOM Group PLC.

DIRECTORS

The directors who served during the year and up to the date of signing the financial statements are listed on page 1.

STATEMENT OF DIRECTORS' RESPONSIBILITIES

The director is responsible for preparing the Strategic Report, Director's Report and the financial statements in accordance with applicable law and regulations.

Company law requires the director to prepare financial statements for each financial year. Under that law the director has prepared the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards, comprising FRS 101 "Reduced Disclosure Framework", and applicable law). Under company law the director must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period. In preparing the financial statements, the director is required to:

- select suitable accounting policies and then apply them consistently;
- state whether applicable United Kingdom Accounting Standards, comprising FRS 101, have been followed, subject to any material departures disclosed and explained in the financial statements;
- make judgements and accounting estimates that are reasonable and prudent; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The director is 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.

KCH (HOLDINGS) LIMITED
DIRECTOR'S REPORT FOR THE YEAR ENDED 31 MARCH 2017

STATEMENT OF DIRECTOR'S RESPONSIBILITIES (CONTINUED)

The director is 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.

In the case of each director in office at the date the Director's Report is approved:

- so far as the director is aware, there is no relevant audit information of which the company's auditors are unaware; and
- they have taken all the steps that they ought to have taken as a director in order to make themselves aware of any relevant audit information and to establish that the company's auditors are aware of that information.

INDEPENDENT AUDITORS

A resolution has been passed to maintain PricewaterhouseCoopers LLP as auditors until such time as the Board decides otherwise.

Approved by the board and signed on its behalf



W Halbert
Director

12 October 2017

KCH (HOLDINGS) LIMITED

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF KCH (HOLDINGS) LIMITED

Report on the financial statements

Our opinion

In our opinion, KCH (Holdings) Limited's financial statements (the "financial statements"):

- give a true and fair view of the state of the company's affairs as at 31 March 2017 and of its profit for the 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.

What we have audited

The financial statements, included within the Annual Report and Financial Statements (the "Annual Report"), comprise:

- the Statement of Financial Position as at 31 March 2017;
- the Income Statement and Statement of Comprehensive Income for the year then ended;
- the Statement of Changes in Equity for the year then ended; and
- the notes to the financial statements, which include a summary of significant accounting policies and other explanatory information.

The financial reporting framework that has been applied in the preparation of the financial statements is United Kingdom Accounting Standards, comprising FRS 101 "Reduced Disclosure Framework", and applicable law (United Kingdom Generally Accepted Accounting Practice).

In applying the financial reporting framework, the director has made a number of subjective judgements, for example in respect of significant accounting estimates. In making such estimates, they have made assumptions and considered future events.

Opinions on other matters prescribed by the Companies Act 2006

In our opinion, based on the work undertaken in the course of the audit:

- 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; and
- the Strategic Report and the Directors' Report have been prepared in accordance with applicable legal requirements.

In addition, in light of the knowledge and understanding of the company and its environment obtained in the course of the audit, we are required to report if we have identified any material misstatements in the Strategic Report and the Directors' Report. We have nothing to report in this respect.

OTHER MATTERS ON WHICH WE ARE REQUIRED TO REPORT BY EXCEPTION

Adequacy of accounting records and information and explanations received

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- we have not received all the information and explanations we require for our audit; or
- 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.

We have no exceptions to report arising from this responsibility.

KCH (HOLDINGS) LIMITED
INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF KCH (HOLDINGS) LIMITED

Directors' remuneration

Under the Companies Act 2006 we are required to report to you if, in our opinion, certain disclosures of directors' remuneration specified by law are not made. We have no exceptions to report arising from this responsibility.

RESPONSIBILITIES FOR THE FINANCIAL STATEMENTS AND THE AUDIT

Our responsibilities and those of the directors

As explained more fully in the Directors' Responsibilities Statement set out on page 4 & 5, 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) ("ISAs (UK & Ireland)"). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

What an audit of financial statements involves

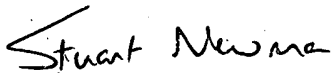
We conducted our audit in accordance with ISAs (UK & Ireland). An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of:

- whether the accounting policies are appropriate to the company's circumstances and have been consistently applied and adequately disclosed;
- the reasonableness of significant accounting estimates made by the directors; and
- the overall presentation of the financial statements.

We primarily focus our work in these areas by assessing the directors' judgements against available evidence, forming our own judgements, and evaluating the disclosures in the financial statements.

We test and examine information, using sampling and other auditing techniques, to the extent we consider necessary to provide a reasonable basis for us to draw conclusions. We obtain audit evidence through testing the effectiveness of controls, substantive procedures or a combination of both.

In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report. With respect to the Strategic Report and Directors' Report, we consider whether those reports include the disclosures required by applicable legal requirements.



Stuart Newman (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
London

12 October 2017

KCH (HOLDINGS) LIMITED
INCOME STATEMENT
For the year ended 31 March 2017

		2017	2016
	Note	£'000	£'000
Revenue	2	85,084	28,408
Other operating income	3	65,203	—
Operating expenses		(87,000)	(40,102)
Operating profit/(loss)	3	63,287	(11,694)
Analysed as:			
EBITDA before exceptional items		66,701	(6,891)
Exceptional items	4	(3,414)	(301)
Depreciation of property, plant and equipment		—	(689)
Amortisation of intangible assets		—	(3,813)
Finance income	6	1,483	3,908
Finance costs	7	(3,240)	(5,303)
Profit/(Loss) before taxation		61,530	(13,089)
Tax on profit/(loss)	8	604	2,373
Profit/(Loss) for the financial year		62,134	(10,716)

The notes on pages 11 to 27 are an integral part of these financial statements.

STATEMENT OF COMPREHENSIVE INCOME
For the year ended 31 March 2017

	2017	2016
	£'000	£'000
Profit/(Loss) for the financial year	62,134	(10,716)
Remeasurements on retirement benefit obligation	(12,035)	12,130
Tax on items that will not be reclassified	1,738	(2,426)
Other comprehensive (expense)/income: items that will not be reclassified to the income statement	(10,297)	9,704
Fair value movements of financial derivative instruments	—	(442)
Deferred tax relating to financial derivative instruments	—	(569)
Other comprehensive expense: items that may be reclassified to income statement	—	(1,011)
Total comprehensive income/(expense) for the financial year	51,837	(2,023)

KCH (Holdings) Limited

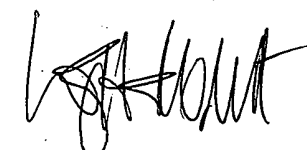
Company Registration No. 6072997

KCH (HOLDINGS) LIMITED
STATEMENT OF FINANCIAL POSITION
As at 31 March 2017

	Note	2017 £'000	2016 £'000
Non-current assets			
Investments	11	126,422	126,422
Deferred tax assets	16	3,578	3,349
		130,000	129,771
Current assets			
Trade and other receivables: amounts falling due within one year	12	4,769	3,887
Trade and other receivables: amounts falling due after more than one year	13	20,643	21,887
Cash and cash equivalents	18	305	11,254
		25,717	37,028
Creditors: amounts falling due within one year	14	(40,227)	(126,057)
Net current liabilities		(14,510)	(89,029)
Total assets less current liabilities		115,490	40,742
Bank loans	15	(48,587)	—
Retirement benefit obligation	19	(19,691)	(14,350)
Deferred tax liabilities	16	(3,896)	(4,048)
Net assets		43,316	22,344
Equity			
Called up share capital	17	2,000	2,000
Retained earnings		41,316	20,344
Total shareholders' funds		43,316	22,344

The notes on pages 11 to 27 are an integral part of these financial statements.

The financial statements on pages 8 to 27 were approved by the Board of Directors and authorised for issue on 12 October 2017. They were signed on its behalf by:



W Halbert
Director

KCH (Holdings) Limited

Company Registration No. 6072997

KCH (HOLDINGS) LIMITED
STATEMENT OF CHANGES IN EQUITY
For the year ended 31 March 2017

	Note	Called up share capital £'000	Hedging reserve £'000	Retained earnings £'000	Total shareholders' funds £'000
At 1 April 2015		2,000	442	56,868	59,310
Loss for the financial year		—	—	(10,716)	(10,716)
Other comprehensive income/(expense)		—	(442)	9,135	8,693
Total comprehensive expense for the year		—	(442)	(1,581)	(2,023)
Current tax credit relating to share schemes	8	—	—	125	125
Deferred tax credit relating to share schemes		—	—	90	90
Employee share schemes		—	—	997	997
Dividends	9	—	—	(36,155)	(36,155)
At 31 March 2016		2,000	—	20,344	22,344
Profit for the financial year		—	—	62,134	62,134
Other comprehensive expense		—	—	(10,297)	(10,297)
Total comprehensive income for the year		—	—	51,837	51,837
Deferred tax charge relating to share schemes	8	—	—	(122)	(122)
Employee share schemes		—	—	1,721	1,721
Dividends	9	—	—	(32,464)	(32,464)
At 31 March 2017		2,000	—	41,316	43,316

The notes on pages 11 to 27 are an integral part of these financial statements.

KCH (HOLDINGS) LIMITED
NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 March 2017

1. ACCOUNTING POLICIES

The principal accounting policies are summarised below. They have all been applied consistently throughout the year.

Basis of accounting

These financial statements have been prepared in accordance with United Kingdom Accounting Standards, in particular, Financial reporting Standard 101 Reduced Disclosure Framework (FRS 101) and the Companies Act 2006 (the Act) as appropriate to companies using FRS101. FRS 101 sets out a reduced disclosure framework for a 'qualifying entity' as defined in the standard which addresses the financial reporting requirements and disclosure exemptions in the individual financial statements of qualifying entities that otherwise apply the recognition, measurement and disclosure requirements of EU-adopted IFRS.

The company is a qualifying entity for the purposes of FRS 101. Note 20 gives details of the company's ultimate parent and from where its consolidated financial statements prepared in accordance with IFRS may be obtained.

FRS 101 sets out amendments to EU-adopted IFRS that are necessary to achieve compliance with the Act and related Regulations. The disclosure exemptions adopted by the company in accordance with FRS 101 are as follows:

- a) Statement of cash flows
- b) Capital risk management
- c) Related party transactions
- d) Share based payments
- e) Accounting policies issued but not yet effective
- f) Certain exemptions allowable under IAS1

The financial statements have been prepared under the historical cost convention modified by the valuation of derivative financial statements. A summary of the accounting policies is set out below.

Critical accounting estimates

Exceptional items

Exceptional items are disclosed separately in the financial statements where it is necessary to do so to provide better understanding of the financial performance of the company. They are material items of income or expense that are shown separately due to the significance of their nature or amount.

The Director is required to make judgements regarding whether items are material to the users of the accounts and whether separate disclosure will aid the understanding of the financial performance.

Post-employment benefits

The company operates two defined benefit schemes. All post-employment benefits associated with these schemes have been accounted for in accordance with IAS 19 'Employee benefits (revised)'. As detailed within the accounting policies note, in accordance with IAS 19, all actuarial gains and losses have been recognised immediately through the Statement of comprehensive income.

For all defined benefit schemes, pension valuations have been performed using specialist advice obtained from independent qualified actuaries. In performing those valuations, judgements, assumptions and estimates have been made. These assumptions are disclosed within Note 19.

New and amended standards adopted by the company

There are no IFRSs or IFRIC interpretations that are effective for the first time for the financial year beginning on 1 April 2015 that have had a material impact on the company.

Consolidation

The company has taken advantage of the exemption from preparing consolidated financial statements afforded by Section 400 of the Companies Act 2006 because its immediate parent undertaking is incorporated within the European Union and it is included and consolidated within the group the financial statements of KCOM Group PLC, which are publically available.

KCH (HOLDINGS) LIMITED
NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 March 2017

1. ACCOUNTING POLICIES (CONTINUED)

Going concern

The company meets its day-to-day working capital requirements through its bank facilities. The company's forecasts and projections, taking account of reasonably possible changes in trading performance, show that the company should be able to operate within the level of its current facilities. After making enquires, the directors have a reasonable expectation that the company has adequate resources to continue in operational existence for the foreseeable future. The company therefore continues to adopt the going concern basis in preparing its financial statements.

Investments

Investments in subsidiaries are held at cost less accumulated impairment losses. They are reviewed at each reporting date for possible reversal of the impairment.

Trade receivables

Trade receivables are recognised initially at fair value and measured subsequently at amortised cost, using the effective interest method, less any impairment. A provision for impairment of trade receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of the receivables. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganisation, and default or delinquency in payments are considered indicators that the trade receivable is impaired.

The amount of provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account, and the amount of the loss is recognised in the income statement within operating expenses. When a trade receivable is uncollectible, it is written off against the allowance account for trade receivables. Subsequent recoveries of amounts written off are credited against operating expenses in the income statement.

Cash and cash equivalents

Cash and cash equivalents includes cash in hand, short-term deposits and other short-term highly liquid investments with original maturities of three months or less and bank overdrafts. Bank overdrafts are shown within borrowings in current liabilities on the balance sheet, unless a right of offset exists.

Payables

Payables are recognised initially at fair value and measured subsequently at amortised cost using the effective interest method.

Share capital

Ordinary shares are classified as equity.

Leases

Rentals payable under operating leases are charged in the income statement on a straight-line basis over the lease term.

Revenue recognition

Revenue excludes value added tax and comprises the value of services provided. Revenue is recognised in respect of the right to consideration for each individual component where a reliable fair value can be attributed to these components.

Interest income is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable.

KCH (HOLDINGS) LIMITED
NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 March 2017

1. ACCOUNTING POLICIES (CONTINUED)

Exceptional items

Exceptional items are disclosed separately in the financial statements where it is necessary to do so to provide better understanding of the financial performance of the company. They are material items of income or expense that have been shown separately due to the significance of their nature or amount. In particular costs associated with organisational restructuring, costs and provisions associated with onerous contracts, profits or losses on the sale of an operation and one-off pension costs and credits are treated as exceptional items.

Taxation

The tax expense represents the sum of the tax currently payable and deferred tax. The tax payable is currently based on taxable profit for the year. Taxable profit differs from profit before tax as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other years and/or items that are never taxable or deductible. The company's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.

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

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced or increased to the extent that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries and associates, and interests in joint ventures, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realised. Deferred tax is charged or credited in the income statement, except when it relates to items recognised in other comprehensive income or directly to equity. In this case the deferred tax is also recognised in other comprehensive income or directly in equity respectively.

Financial instruments and hedge accounting

Financial assets and liabilities are recognised in the company's balance sheet when the company becomes a party to the contractual provisions of the instrument. The company uses derivative financial instruments to hedge its exposure to foreign exchange and interest rate risks arising from operational, financing and investment activities. In accordance with its Treasury Policy, the company does not hold or issue derivative financial instruments for trading purposes.

Derivative financial instruments are initially and subsequently recognised at fair value. Any gain or loss on remeasurement to fair value is recognised immediately in the income statement. However, where derivatives qualify for hedge accounting, recognition of the resultant gain or loss depends on the nature of the item being hedged.

The fair value of the interest rate swaps is the estimated amount that the company would receive or pay to terminate the swap at the balance sheet date, taking into account current interest rates and the current creditworthiness of the swap counterparties. The fair value of forward exchange contracts is their quoted market price at the balance sheet date, being the present value of the quoted forward price.

KCH (HOLDINGS) LIMITED
NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 March 2017

1. ACCOUNTING POLICIES (CONTINUED)

Financial instruments and hedge accounting (continued)

Changes in the fair value of derivative financial instruments that are designated and effective as hedges of future cash flows are recognised directly in other comprehensive income and the ineffective portion is recognised immediately in the income statement. If the cash flow hedge of a firm commitment or forecasted transaction results in the recognition of an asset or liability, then, at the time the asset or liability is recognised, the associated gains or losses on the derivative that had previously been recognised in other comprehensive income are included in the initial measurement of the asset or liability. For hedges that do not result in recognition of an asset or a liability, amounts deferred in equity are recognised in the income statement in the same period in which the hedged item affects net profit or loss.

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

Foreign currency translation

These financial statements are presented in Pounds Sterling which is the currency of the primary economic environment in which the company operates. Transactions in foreign currencies are recorded at the rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the rate of exchange ruling at the balance sheet date.

Pensions

Prior to 12 January 1998, all new employees were eligible to join the defined benefit pension funds operated by the ultimate parent company. At 12 January 1998, that scheme was closed to new members, and all employees commencing employment after that date are eligible to join the defined contribution Group Personal Pension Scheme. In addition, the Group decided to close the defined benefit funds to future accrual in September 2010. As at 31 March 2011, the pension schemes were transferred from KCOM Group PLC to KCH (Holdings) Limited. KCH (Holdings) Limited is the principal sponsoring entity for the pension schemes.

The company provides pension arrangements to a number of full time employees through these two defined benefit schemes, which are operated by KCH (Holdings) Limited. For defined benefit retirement schemes, the cost of providing benefits is determined using a building block approach, with actuarial valuations being carried out at each balance sheet date. Remeasurements are recognised in full in the period in which they occur and are recognised in equity and presented in the statement of comprehensive income.

The current and past service costs of the scheme (the increase in the present value of employees' future benefits attributable to the current or prior periods) are charged to the income statement in the period. The cost or benefit of committed settlements and curtailments is recognised immediately in the income statement. The interest cost of the scheme is recognised in the income statement in the period to which it relates.

The retirement benefit obligation recognised in the balance sheet represents the present value of the defined benefit obligation as adjusted for unrecognised past service cost and as reduced by the fair value of scheme assets. Any asset resulting from this calculation is limited to past service cost, plus the present value of available refunds and reductions in future contributions to the plan.

Share-based payments

The company has applied the requirements of IFRS 2 Share-based payments.

The ultimate parent undertaking, KCOM Group PLC, issues equity-settled share-based payments to certain employees. Other equity-settled share-based payments arise where payment for goods and services is settled in shares or other equity instruments.

Equity-settled employee schemes, including employee share options, discretionary long term incentive schemes and save as you earn schemes, provide employees the option to acquire shares of KCOM Group PLC. Employee share options and long term incentive schemes are generally subject to performance or service conditions.

KCH (HOLDINGS) LIMITED
NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 March 2017

1. ACCOUNTING POLICIES (CONTINUED)

Share-based payments (continued)

The fair value of equity-settled share-based payments relating to KCH (Holdings) Limited employees is measured at the date of grant and charged to the profit and loss account over the period during which performance or service conditions are required to be met, or immediately where no performance or service criteria exist. The fair value of equity-settled share-based payments granted is measured using either the Black-Scholes or Monte Carlo model, depending on the terms under which the options were granted. The amount recognised as an expense is adjusted to reflect the actual number of employee share options that vest, except where forfeiture is only due to market based performance criteria not being met.

At the end of each reporting period, the Group revises its estimates of the number of options that are expected to vest based on the non-market vesting conditions. It recognises the impact of the revision to original estimates, if any, in the income statement, with a corresponding adjustment to equity.

The ultimate parent undertaking, KCOM Group PLC, also operates a Share Incentive Plan (SIP) under which employees have the option to purchase shares in KCOM Group PLC each month and offers employees free matching and partnership shares on a sliding scale of between 1:3 to 2:1. The free shares relating to employees of KCH (Holdings) Limited are recognised as an expense in KCOM Holdings Limited over the period of any applicable service condition, or immediately when no service condition exists.

Dividends

Dividends to the company's shareholders are recognised as a liability in the financial statements in the period in which the dividends are approved by the company's shareholders.

Dividend income is recognised when the right to receive payment is established.

2. REVENUE

Revenue is generated wholly within the UK. All revenue is generated by one class of business, being principally the provision of services to other group companies. In the current year revenue has related to the provision of payroll related services, whereas in the prior year revenue related to the provision of other services including: technical and engineering support; IT; finance; estates; legal; and HR services.

3. OPERATING PROFIT/(LOSS)

Operating profit is stated after charging / (crediting):

	Notes	2017 £'000	2016 £'000
Wages and salaries		70,364	26,756
Social security costs		7,226	2,706
Other pension costs		3,526	1,208
Share based payments	10	1,721	1,117
Restructuring costs relating to employees	4	3,368	3,337
Non-employee-related pension costs		655	656
Operating lease rentals		—	4,212
Auditors' remuneration for the audit of the financial statements		40	78
Other non-audit services		—	150
Audit related assurance services		—	10
Depreciation of property, plant and equipment		—	689
Amortisation of intangible assets		—	3,813
Profit on disposal of property, plant and equipment		—	(51)
Bank charges		46	144
Restructuring costs	4	46	—
Onerous lease	4	—	(191)
Regulatory matters	4	—	(2,845)
Dividends received from subsidiary companies		(65,017)	—
Distribution received from another group company		(186)	—

KCH (HOLDINGS) LIMITED
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4. EXCEPTIONAL ITEMS

	2017	2016
	£'000	£'000
Restructuring costs	3,414	3,337
Onerous lease	—	(191)
Regulatory matters	—	(2,845)
	3,414	301

Restructuring costs relate to redundancies arising as a result of organisational changes.

In the prior year, there was an onerous lease credit recognised of £191,000 due to an unused provision previously classified as an exceptional item.

The regulatory matters item in 2016 related to an Ofcom determined settlement of claims relating to an industry-wide regulatory ruling; treated as an exceptional in accordance with our accounting policy.

5. EMPLOYEES AND DIRECTORS

The average monthly number of employees (including executive directors) was 1,574 (2016: 638).

At 31 March 2017, Mr W Halbert was a director of KCOM Group PLC, and other fellow subsidiary companies. Mr W Halbert received total emoluments of £862,000 (2016: £578,000) from KCOM Group PLC but it is not practicable to ascertain the proportion of his emoluments that specifically relate to the company. Mr W Halbert has elected not to be a member of any company pension scheme. Instead he received cash payments in the year totalling £66,000 (2016: £66,000).

Previous director, Mr P Simpson, who resigned on 11 October 2016 received total emoluments of £414,000 (2016: £395,000) from KCOM Group PLC but it is not practicable to ascertain the proportion of his emoluments that specifically relate to the company. In addition, Mr P Simpson is a member of the Kingston Group Personal Pension Plan, a defined contribution scheme. During the financial year, KCOM Group PLC made contributions of £25,000 on behalf of Mr P Simpson (2016: £50,000).

6. FINANCE INCOME

	2017	2016
	£'000	£'000
Other finance income	1,483	3,908
	1,483	3,908

7. FINANCE COSTS

	2017	2016
	£'000	£'000
On bank loans, overdrafts and other loans	1,195	2,353
Interest payable to group undertakings	1,087	1,564
Amortisation of loan arrangement fees	583	432
Net interest on retirement benefit obligation (note 19)	375	954
	3,240	5,303

KCH (HOLDINGS) LIMITED
NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 March 2017

8. TAX ON PROFIT/(LOSS)

The tax credit for the year comprises:

	2017 £'000	2016 £'000
UK corporation tax:		
– current tax on profits for the year	(1,839)	(3,168)
– adjustment in respect of prior years	—	(155)
Total current tax	(1,839)	(3,323)
UK deferred tax:		
Origination and reversal of temporary differences in respect of:		
– profit for the year	127	(17)
– rate difference	591	—
– adjustment in respect of prior years	—	516
– deferred tax relating to retirement benefit obligation (note 19)	517	451
Total deferred tax	1,235	950
Total taxation credit for the year	(604)	(2,373)

Factors affecting tax credit for the year:

	2017 £'000	2016 £'000
Profit/(Loss) before taxation	61,530	(13,089)
Profit/(Loss) before taxation at the standard rate of corporation tax in the UK of 20% (2016: 20%)	12,306	(2,618)
Effects of:		
– income not subject to tax	(13,501)	—
– permanent differences	—	50
– adjustments relating to prior year current and deferred tax	—	296
– rate difference	591	—
– non-taxable impairment of long term intercompany balances	—	(101)
Total taxation credit for the year	(604)	(2,373)

The tax credit includes a charge relating to the vesting of the share schemes of £122,000 (2016: credit of £125,000) which is a reclassification from the reserves on the unwinding of the deferred tax asset.

Factors affecting the current and future tax charges

Changes to the UK corporation tax rates were substantively enacted as part of Finance Bill 2015 (on 26 October 2015) and Finance Bill 2016 (on 7 September 2016). These include reductions to the main rate to reduce the rate to 19% from April 2017 and to 17% from April 2020. Deferred taxes at the balance sheet date have been measured using these enacted tax rates and reflected in these financial statements.

9. DIVIDENDS

	2017 £'000	2016 £'000
Amounts recognised as distributions to equity holders in the year:		
Final dividend for the year ended 31 March 2015 of £9.25 per share	—	18,494
Interim dividend for the year ended 31 March 2016 of £8.83 per share	—	17,661
Final dividend for the year ended 31 March 2017 of £16.23 per share	32,464	—
	32,464	36,155

KCH (HOLDINGS) LIMITED
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Year ended 31 March 2017

10. SHARE-BASED PAYMENTS

The company participated in two share-based payment schemes during the year ended 31 March 2017 (2016: two), the Long-Term Incentive Plan (LTIP) and the Share Incentive Plan (SIP) which is operated by the company's ultimate parent undertaking, KCOM Group PLC. The company recognised a total charge of £1,721,000 (2016: £1,117,000) in the year relating to share-based payment transactions issued after 7 November 2002. Details of the scheme is provided below:

Long-Term Incentive Plan (LTIP)

The LTIP is an equity settled share-based payment scheme open to the Executive Directors and selected senior employees at the discretion of the Remuneration Committee. The Awards were granted at nil cost on 19 July 2012, 17 July 2013 and on 19 July 2014 and vest dependent on TSR performance over a three-year performance period relative to the TSR performance of each company within a comparator group. For further information on the grants and the performance conditions see the Remuneration report in the KCOM Group PLC financial statements on page 50.

In the year ended 31 March 2017, a charge of £1,085,000 (2016: £926,000) was recognised by the company.

	Number	Weighted average exercise price (pence)
Outstanding at the beginning of the year	5,225,401	Nil
Granted	1,590,389	Nil
Vested	(1,074,176)	Nil
Lapsed	(1,098,265)	Nil
	4,643,349	Nil

None of these awards were exercisable at the year end. The awards have been valued using a Monte Carlo simulation model. The weighted average assumptions used during the year are as follows:

Share price at valuation date (pence)	108.0
Exercise price (pence)	Nil
Expected volatility (%)	21.8
Risk free rate (%)	0.1

Share Incentive Plan (SIP)

The SIP is open to all employees and offers partnership, matching and free shares (the basis depends on the individual's contribution into the scheme) in the ultimate parent undertaking, KCOM Group PLC. No performance criteria are attached to these matching shares other than an employee must remain in employment for five years from the date of grant to be able to have their free and matching shares. In 2016/17, 1,209,754 matching shares were granted during the year to employees of KCH (Holdings) Limited employees and a charge of £636,000 (2016: £191,000) was recognised within the company.

	Number	Weighted average exercise price (pence)
Outstanding at the beginning of the year	—	Nil
Transferred from another Group company	6,427,916	Nil
Granted during the year	1,209,754	Nil
Vested during the year	(1,839,382)	Nil
Lapsed during the year	(103,220)	Nil
	5,695,068	Nil

KCH (HOLDINGS) LIMITED
NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 March 2017

11. INVESTMENTS

	Total £'000
Cost	
At 1 April 2016 and 31 March 2017	270,872
Historical impairments	
At 1 April 2016 and 31 March 2017	144,450
Net book value	
At 31 March 2017	126,422
At 31 March 2016	126,422

Details of the principal subsidiary undertakings of the company are as follows:

Name of company	Place of registration	Holding	Proportion held	Nature of business
Network Holdco 3 BV	Holland ¹	Ordinary shares	100%	Dormant
Smart 421 Technology Group Limited	England and Wales ²	Ordinary shares	100%	Intermediate holding company
Kingston Network Holdings Limited	England and Wales ²	Ordinary shares	100%	Dormant holding company
Kingston Service Holdings Limited	England and Wales ²	Ordinary shares	100%	Dormant holding company
Kingston Communications International Limited	England and Wales ²	Ordinary shares	100%	Dormant
KCOM (General Partner) Limited	Scotland ³	Ordinary shares	100%	Intermediate holding company
KCOM Central Asset Reserve Limited Partnership	Scotland ³	Ordinary shares	100%	Partnership
KCOM Contact Centres Limited	England and Wales ²	Ordinary shares	100%	Provision of call centre facilities
Kingston Communications (Data) Trustees Limited	England and Wales ²	Ordinary shares	100%	Dormant
Kingston Communications (Hull) Trustees Limited	England and Wales ²	Ordinary shares	100%	Dormant
Affiniti Integrated Solutions Limited*	England and Wales ²	Ordinary shares	100%	Dormant
Kingston Information Services Limited*	England and Wales ²	Ordinary shares	100%	Publication of telephone directories
KCOM Holdings Limited	England and Wales ²	Ordinary shares	100%	Design and delivery of communication and integration services
Eclipse Networking Limited	England and Wales ²	Ordinary shares	100%	Dormant
Eclipse Internet Limited*	England and Wales ²	Ordinary shares	100%	Dormant
Kingston Communications (Hull) Limited*	England and Wales ²	Ordinary shares	100%	Dormant
Omnetica Investment Limited*	England and Wales ²	Ordinary shares	100%	Dormant Holding Company
Omnetica Inc*	USA ⁴	Ordinary shares	100%	Dormant
Smart421 Limited*	England and Wales ²	Ordinary shares	100%	Dormant
Smart421 Solutions Inc*	USA ⁵	Ordinary shares	100%	Dormant
SmartIntegrator Technology Limited	England and Wales ²	Ordinary shares	50%	Software development

*Indicates indirect shareholding

KCH (HOLDINGS) LIMITED
NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 March 2017

11. INVESTMENTS (CONTINUED)

- | | |
|--|---|
| 1. Prins Bernhardplein 200, 1097 JB Amsterdam, The Netherlands | 4. 200 Knickerbocker Avenue, Bohemia, New York, 11716, USA. |
| 2. 37 Carr Lane, Hull, HU1 3RE | 5. 9 East Loockerman Street, Dover, Delaware, 19901, USA. |
| 3. 50 Lothian Road, Festival Square, Edinburgh, EH3 9WJ | |

Following the group wide restructuring of statutory entities, the directors have undertaken an impairment review of investments and believe the values of the investments are supported by the underlying net assets of the subsidiaries.

12. TRADE AND OTHER RECEIVABLES: AMOUNTS FALLING DUE WITHIN ONE YEAR

	2017 £'000	2016 £'000
Amounts owed by group undertakings	47	—
Prepayments and accrued income	2,726	2,711
Other receivables	157	1,176
Group relief debtor	1,839	—
	4,769	3,887

Amounts owed by group undertakings within one year are unsecured, have no fixed date of repayment, bear no interest and are repayable on demand.

13. TRADE AND OTHER RECEIVABLES: AMOUNTS FALLING DUE AFTER MORE THAN ONE YEAR

	2017 £'000	2016 £'000
Amounts owed by group undertakings	450	450
Prepayments and accrued income	20,193	21,437
	20,643	21,887

Amounts owed by group undertakings are unsecured. There are no formal arrangements for the repayment of amounts owed by group undertakings greater than one year. However, they have been confirmed as not due for repayment within one year. Interest at market rates is charged on amounts owed by group undertakings due after more than one year, except for amounts owed by dormant entities where nil interest is charged.

14. CREDITORS: AMOUNTS FALLING DUE WITHIN ONE YEAR

	2017 £'000	2016 £'000
Trade payables	110	—
Amounts owed to group undertakings	39,870	125,755
Other payables	207	302
Accruals	40	—
	40,227	126,057

KCH (HOLDINGS) LIMITED
NOTES TO THE FINANCIAL STATEMENTS
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15. BANK LOANS

	2017 £'000	2016 £'000
Bank borrowings		
Amount falling due:		
- between two and five years	50,000	—
	50,000	—
Loan issue costs	(1,413)	—
	48,587	—

The group loan facilities are secured by guarantees given by all material subsidiaries of KCOM Group PLC, including KCH (Holdings) Limited, in favour of the banks.

The bank borrowings are fully repayable in December 2021 and attract an interest rate of LIBOR plus a margin dependent on specific covenants. Further information on interest rate swaps, see Note 18. The above bank facilities were refinanced in September 2016. See Note 18 for further detail.

In 2016 the Group repaid all outstanding loan borrowings and as a consequence associated outstanding loan issue costs (£1.2m) were reclassified to other receivables. During 2017 the Group has drawn down on its loan facility and therefore loan issue costs have been classified against bank borrowings.

16. DEFERRED TAX

	Asset £'000	Liability £'000
At 1 April 2016	3,349	(4,048)
Charged to income statement (note 8)	(1,235)	—
Charged to reserves	1,464	152
At 31 March 2017	3,578	(3,896)

Deferred tax comprises:

	Asset 2017 £'000	Asset 2016 £'000	Liability 2017 £'000	Liability 2016 £'000
Other timing differences	231	478	—	—
Retirement benefit obligation	3,347	2,871	—	—
Asset backed partnership	—	—	(3,896)	(4,048)
	3,578	3,349	(3,896)	(4,048)

Deferred tax assets have been recognised where there is sufficient available evidence that suitable taxable profits will arise against which these assets are expected to reverse. There are no unrecognised deferred tax assets in either year.

17. CALLED UP SHARE CAPITAL

	2017 £'000	2016 £'000
Allotted and fully paid		
2,000,000 (2016: 2,000,000) ordinary shares of £1 each	2,000	2,000

KCH (HOLDINGS) LIMITED
NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 March 2017

18. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

The company's principal financial instruments during the year comprised bank loans, cash on short term deposit and forward foreign exchange contracts. The main purpose of these financial instruments is to finance KCOM Group PLC's operations and to minimise the impact of fluctuations in exchange rates on future cash flows. The company has various other financial instruments such as short term receivables and payables which arise directly from its operations.

The company regularly reviews its exposure to interest, liquidity and foreign currency risk. Where appropriate the company will take action, in accordance with a Board approved Treasury Policy, to minimise the impact on the business of movements in interest rates and currency rates.

The company only enters into derivative instruments with members of the banking group to ensure appropriate counterparty credit quality.

Liquidity Risk

KCOM Group PLC keeps its short, medium and long-term funding requirements under constant review. Its policy is to have sufficient committed funds available to meet medium-term requirements, with flexibility and headroom to make minor acquisitions for cash if the opportunity should arise.

In September 2016, the Group re-negotiated its multi-currency revolving credit facility. The £180.0m facility provided by a group of five core relationship banks matures in December 2021. The Group considers that this facility will provide sufficient funding to support the Group's growth. In addition, short-term flexibility of funding is available under the £10.0 million overdraft facility provided by the Group's clearing banks.

The table below analyses the company's financial liabilities which will be settled on a net basis into relevant maturity groupings based on the remaining period at the balance sheet date to the contractual maturity date.

Notional interest is included for the period from the year end up to the contractual maturity date of the debt, calculated on the amount of debt drawn down at the year end.

	Less than one year £'000	One to three years £'000	Over three years £'000
At 31 March 2016			
Trade payables	—	—	—
Borrowings	—	—	—
Total	—	—	—
At 31 March 2017			
Trade payables	—	—	—
Borrowings	1,255	2,450	52,144
Total	1,255	2,450	52,144

Foreign currency risk

The KCOM Group's only major foreign currency risk arises due to the purchase of equipment invoiced in US dollars. Whenever possible the Group resells this equipment in US dollars. The remaining exposure is managed by the company principally through the use of forward foreign exchange contracts in order to minimise the impact of fluctuations in exchange rates on future cash flows and gross margin. The KCOM Group also has some euro cash flows but these are not material on a net basis and are not hedged.

KCH (HOLDINGS) LIMITED
NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 March 2017

18. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (CONTINUED)

Credit risk

Credit risk arises from cash and cash equivalents and derivative financial instruments, as well as credit exposures to business and retail customers.

Credit ratings of institutions which hold the Group's financial assets are regularly monitored to ensure they meet the minimum credit criteria set by the Board through the Group Treasury Policy. At the year end all the institutions holding the Group's financial assets were rated A-/A- or higher by Standard and Poor's.

The credit quality of customers is assessed by taking into account their financial position, past experience and other factors. Individual risk limits are set and the utilisation of credit limits monitored regularly.

Financial assets

The company had financial assets of £305,000 at the year-end (2016: £11,254,000), comprising cash on overnight money market deposits and cash at bank. This attracts floating rates of interest.

The currency profile of the company's financial liabilities and assets at 31 March 2017 and 31 March 2016 was:

	2017 £'000	2016 £'000
Currency		
Sterling	305	7,181
US Dollar	—	3,925
Euro	—	148
	305	11,254

Foreign currency cash balances are held on a short term basis to fund cash flow requirements in these currencies.

Financial liabilities

The currency and interest rate risk profile of the company's financial borrowings at 31 March 2017 and 31 March 2016 was:

	2017			2016		
	Floating £'000	Fixed £'000	Total £'000	Floating £'000	Fixed £'000	Total £'000
Sterling	50,000	—	50,000	—	—	—

Undrawn committed borrowing facilities at the year-end were £130,000,000 (2016: £200,000,000). Interest on amounts drawn under the committed borrowing facility is based on the relevant LIBOR plus margin.

Fair values of financial assets and financial liabilities

IFRS 7 requires disclosure of fair value measurements by level of the following fair value measurement hierarchy:

- quoted prices (unadjusted) in active markets for identical assets or liabilities (level 1);
- 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) (level 2); and
- inputs for the asset or liability that are not based on observable market data (that is, unobservable inputs (level 3).

All of the company's financial instruments fall into hierarchy level 2.

Capital risk management

Under the terms of the Group's £180.0 million revolving credit facility the Group is required to comply annually with certain financial and non-financial covenants. The Group is required to maintain a minimum interest cover ratio and maximum net debt to EBITDA ratio. Both financial covenants were tested and complied within throughout the year and at year end. The Board monitors both covenant compliance and net debt performance on a regular basis.

KCH (HOLDINGS) LIMITED
NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 March 2017

19. RETIREMENT BENEFIT OBLIGATION

Defined contribution schemes

The company operates defined contribution schemes, which are open to all eligible employees. Contributions charged to the income statement in respect of the defined contribution schemes amounted to £3.5m.

Defined benefit schemes

The principal defined benefit scheme at 31 March 2017 was the Kingston Communications Pension Scheme, which is a funded scheme and provides defined benefits based on final pensionable salary. The assets of the scheme are held separately from the assets of the Group in trustee administered funds. The company operates also a second funded defined benefit scheme, the Kingston Communications (Data) Pension Scheme. Both schemes are closed to both new members and future accrual.

The defined benefit schemes are operated in the UK under the same regulatory frameworks. Both of the schemes are final salary pension schemes, which provide benefits to members in the form of a guaranteed level of pension payable for life. The level of benefits provided depends on members' length of service and their salary in the final years leading up to retirement. In the schemes, pensions in payment are generally updated in line with the retail price index. With the exception of this inflationary risk, the schemes face the same risks, as described below.

All of the benefit payments are from trustee administered funds. Plan assets held in trusts are governed by local regulations and practice in each country, as is the nature of the relationship between the Group and the trustees (or equivalent) and their composition. Responsibility for governance of the plans – including investment decisions and contribution schedules – lies jointly with the Group and the Trustees. The Trustees must be composed of representatives of the Group and scheme participants in accordance with the scheme's regulations.

Most recent valuations

The most recent formal valuation for the Kingston Communications Pension Scheme was at 31 March 2016. The main long-term financial assumptions used in that valuation were:

	Per annum %
Rate of return on scheme assets	2.90
Rate of future CPI inflation	2.20

The most recent formal valuation for the Kingston Communications (Data) Pension Scheme was at 31 March 2016. The main long-term financial assumptions used in that valuation were:

	Per annum %
Rate of return on scheme assets	3.10
Rate of future CPI inflation	2.20

Funding

Asset backed partnership

On 31 March 2013, the Group reached an agreement with the Trustees to provide the Group with an efficient mechanism of funding the schemes' current deficit position.

The Group established a general partner, KCOM (General Partner) Limited, and a partnership, KCOM Central Asset Reserve Limited Partnership ("the Partnership"), which are both consolidated within these financial statements. The Group takes advantage of the exception conferred by Regulation 7 of the Partnership (Accounts) Regulations 2008 and has therefore not appended the financial statements of the Partnership to these financial statements. Separate financial statements for the Partnership are not required to be filed at Companies House. The Group provided sufficient capital to the Partnership to enable it to procure freehold property assets with a market value of £12.6 million owned by fellow Group subsidiaries. These properties were immediately leased back and continue to be operated by those Group companies and not by the Partnership. The Group retains control over these properties including the flexibility of substituting the freehold property assets with other assets. As partners in the Partnership, the pension schemes are entitled to an annual income distribution.

KCH (HOLDINGS) LIMITED
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Year ended 31 March 2017

19. RETIREMENT BENEFIT OBLIGATION (CONTINUED)

Funding (continued)

Asset backed partnership (continued)

On 24 March 2014, the Group reached an agreement with the Trustees to provide further funding of the Schemes' current deficit position through the asset backed Partnership ("the Partnership") that had been previously established during the year ended 31 March 2013.

As part of this agreement, a loan note of £20,000,000 was secured over the Hull and East Yorkshire network asset. The security does not offer the Trustees any "normal" rights of enforcement over the assets. Instead it provides first priority payment of any value that would be realised from the Hull and East Yorkshire Network on an insolvency event.

As partner in the Partnership, the pension schemes are entitled to an annual income distribution of £1,600,000, rising in line with the Consumer Price Index (CPI) (capped at 5%) over a potential period of 15 years. The total value of this income distribution to the Schemes is £16,000,000 which provided an immediate improvement to the funding deficit.

Under IAS 19, the investment held by the pension schemes in the Partnership does not represent a plan asset for the purpose of the Group's consolidated financial statements. The distribution of the Partnership's profits to the pension schemes are reflected as pension contributions in these Group financial statements on a cash basis.

Employer contributions

Contributions into the two defined benefit schemes during the year were as follows:

	2017 £'000	2016 £'000
Payments to the schemes	7,724	6,565

Main financial assumptions

The main financial assumptions for the schemes made by the actuaries for the purpose of IAS 19 were:

	2017 per annum %	2016 per annum %
RPI inflation	3.15	2.95
CPI inflation	2.15	1.95
Rate of increase to pensions in payment	2.20	2.00
Discount rate	2.50	3.45

The mortality assumptions are based on standard mortality tables, which allow for future improvements in life expectancy. The effect of these tables are that:

- a future pensioner aged 65 at retirement will live on average to age 88.8 (2016: 89.1) if they are male and on average to age 90.7 (2016: 91.3) if they are female; and
- a current pensioner aged 65 will live on average to age 87.4 (2016: 87.4) if they are male and on average to age 89.1 (2016: 89.3) if they are female.

The key assumptions used for IAS 19 are discount rate, inflation and mortality. The sensitivity of the retirement benefit obligation deficit to changes in the assumptions is as follows:

	Impact on the net retirement benefit obligation		
	Sensitivity	Of increase	Of decrease
RPI inflation	0.1%	20.8%	(18.8%)
Discount rate for scheme liabilities	0.1%	(23.9%)	24.4%
Mortality	1 year	42.2%	(42.7%)

KCH (HOLDINGS) LIMITED
NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 March 2017

19. RETIREMENT BENEFIT OBLIGATION (CONTINUED)

The above sensitivity analyses are based on a change in an assumption while holding all other assumptions constant. In practice, this is unlikely to occur, and changes in some of the assumptions may be correlated. When calculating the sensitivity of the retirement benefit obligation deficit to significant actuarial assumptions the same method (present value of the defined benefit liability calculated with the projected unit credit method at the end of the reporting year) has been applied as when calculating the retirement benefit obligation deficit recognised in the Group balance sheet.

Fair value of assets

	2017 £'000	2016 £'000
Equities	52,707	34,308
Property	1,827	995
Hedge funds	56,751	48,352
Index linked gilts	—	455
Corporate bonds	42,608	42,656
Other	97,645	86,422
	251,538	213,188

Reconciliation of funded status to balance sheet

	2017 £'000	2016 £'000
Fair value of assets	251,538	213,188
Present value of funded retirement benefit obligations	(271,229)	(227,538)
Liability recognised on the balance sheet	(19,691)	(14,350)

Analysis of income and expenditure charge:

– administration expenses	655	656
– finance costs	375	954
Charge recognised in income statement	1,030	1,610

Reconciliation of present value of scheme liabilities

	2017 £'000	2016 £'000
Opening retirement benefit obligation	227,538	240,217
Finance costs	7,685	7,663
Remeasurements arising from changes in financial assumptions	49,075	(8,677)
Remeasurements arising from changes in demographic assumptions	(3,368)	(2,732)
Net benefits paid out	(9,701)	(8,933)
Closing retirement benefit obligation	271,229	227,538

Reconciliation of fair value of scheme assets

	2017 £'000	2016 £'000
Opening fair value of assets	213,188	208,782
Finance income	7,310	6,709
Administration expenses	(655)	(656)
Remeasurements	33,672	721
Contributions by the employer	2,711	2,702
Deficit repair payments	5,013	3,863
Net benefits paid out	(9,701)	(8,933)
Closing fair value of assets	251,538	213,188

KCH (HOLDINGS) LIMITED
NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 March 2017

19. RETIREMENT BENEFIT OBLIGATION (CONTINUED)

Reconciliation of deferred tax relating to the retirement benefit obligation

	2017	2016
	£'000	£'000
Opening deferred tax asset	2,870	6,287
Charged to income statement	(1,108)	(451)
Credited/(charged) to reserves	1,585	(2,966)
Closing deferred tax asset	3,347	2,870

20. PARENT UNDERTAKING AND CONTROLLING PARTY

The company's immediate parent undertaking is KCOM Group PLC. Copies of KCOM Group PLC's annual report and financial statements can be obtained from 37 Carr Lane, Hull, HU1 3RE.

The parent undertaking of the smallest and largest group of undertakings for which group financial statements are drawn up and of which the company is a member is KCOM Group PLC, registered in England and Wales. KCOM Group PLC is also the company's ultimate controlling party. Copies of KCOM Group PLC's annual report and financial statements can be obtained from 37 Carr Lane, Hull, HU1 3RE.

KCH (HOLDINGS) LIMITED

GLOSSARY

ALTERNATIVE PERFORMANCE MEASURES

In response to the Guidelines on Alternative Performance Measures (APMs) issued by the European Securities and Markets Authority (ESMA), we have provided additional information on the APMs used by the Company. The Director's use of the APMs listed below as they are critical to understanding the financial performance of the Company. As they are not defined by IFRS, they may not be directly comparable with other companies who use similar measures

APM	Definition	Reconciliation to equivalent IFRS measure of performance
EBITDA before exceptional items	Operating profit before finance costs, taxation, depreciation, amortisation and exceptional items	Profit before tax of £62.3, less finance income of £1.5m, plus finance costs of £2.2m and exceptionals of £3.4m