

Network Rail Infrastructure Finance PLC

Financial statements

Year ended 31 March 2011

Company registration no. 5090412

Contents

OFFICERS AND PROFESSIONAL ADVISORS	3
DIRECTORS' REPORT	4
STATEMENT OF DIRECTORS' RESPONSIBILITIES	7
INDEPENDENT AUDITORS' REPORT.	8
STATEMENT OF COMPREHENSIVE INCOME	10
STATEMENT OF CHANGES IN EQUITY	10
BALANCE SHEET	11
STATEMENT OF CASH FLOWS	12
NOTES TO THE FINANCIAL STATEMENTS	13

Officers and Professional Advisors

Directors

Andrew Ballsdon (appointed 26 May 2011)
Robert Berry
Jonathan Keighley
James Macdonald
Samantha Pitt
Trevor Winter (resigned 26 May 2011)

Secretary

Hazel Walker

Registered office

Kings Place
90 York Way
London
N1 9AG

Auditors

PricewaterhouseCoopers LLP
Chartered Accountants
London

Directors' report

The Directors present their annual report and audited financial statements for the year ended 31 March 2011.

Principal activities

The principal activity of the Company is to act as issuer for Network Rail's Debt Issuance Programme ("DIP").

Future activities

The Directors do not envisage any changes in the Company's principal activities in the foreseeable future.

Dividends

No dividend is paid or proposed in the current year (2010: £nil).

Business review

Network Rail Infrastructure Finance PLC ("NRIF") was incorporated on 31 March 2004 and entered into documentation to facilitate debt issuance on 29 October 2004.

The Company was incorporated for the sole purpose of acting as the issuer under Network Rail's DIP and is not a member of the Network Rail Group or related to or controlled by the Secretary of State for Transport.

The Company is not a member of the Network Rail Group. However, for accounting purposes the Company is treated as a subsidiary in the consolidated accounts of Network Rail Infrastructure Limited ("NRIL"). The DIP is guaranteed by a Financial Indemnity from the Secretary of State for Transport and as a result the Financial Indemnity is a direct sovereign obligation of the Crown and Network Rail's debt is zero per cent risk weighted.

The Financial Indemnity is an unconditional and irrevocable obligation of the UK Government to make payments directly to a Security Trustee to cover all debt service shortfalls, whatever the cause. The Financial Indemnity is also designed to ensure timely payment as well as ultimate recourse to the UK Government. The DIP continues to provide Network Rail access to the widest possible sources of funding at the lowest possible cost; it provides a stable base for funding a continuing programme of long-term investment in the national rail network.

Within the DIP, which is administered by NRIL, the owner and operator of the national rail network of Great Britain, is a £35bn multi currency note programme which has been assigned the following credit ratings: AAA by Standard and Poor's (negative outlook), Aaa by Moody's and AAA by Fitch.

Directors' report (continued)

In the financial year £1.8bn of bonds were issued. As at 31 March 2011, over 52.7% of gross debt was UK RPI index-linked. Cash balances reduced by £1.6bn. Individual bonds issued during the financial year were:

- \$1.5bn 1.5% nominal notes due Jan 2014 (sterling equivalent of £968m)
- £750m 2.5% nominal notes due Mar 2014
- \$100m 0.54% nominal notes due Mar 2012 (sterling equivalent of £62m)

Going concern

After making enquiries, the Directors have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future.

In reaching this conclusion the Directors considered: the Financial Indemnity as described on page 4; the collateral arrangements with banking counterparties as described in Note 12; that the Company has continued to raise debt as required by NRIL; and that the company has an inter-company agreement that recovers all net costs from NRIL.

Accordingly, they continue to adopt the going concern basis in preparing the annual report and accounts.

Treasury operations

The treasury operations of NRIL, who administers the programme on behalf of NRIF, are co-ordinated and managed in accordance with policies and procedures approved by its Board. Treasury operations are subject to regular internal audits and do not engage in trades of a speculative nature.

Company policy is to provide sufficient committed bank facilities, short-term investments and a £4bn Commercial Paper programme to cover the next 12 months' funding requirements.

The major financing risks that the Company faces are interest rate, foreign currency fluctuation risk and liquidity risk. Treasury operations seeks to provide sufficient liquidity to meet the Company's needs, while reducing financial risks and prudently maximising interest receivable on surplus cash (further details are supplied in Note 12).

Counterparty limits are set with reference to published credit ratings. These limits dictate how much and for how long management deals with each counterparty and are monitored on a regular basis (further details are supplied in Note 12).

Directors

The Directors who served throughout the year and subsequently are detailed on page 3.

None of the Directors had any interests in the shares of the Company or any other company within the Network Rail Group at any time in the year.

NRIF maintains, for its Directors and officers, liability insurance with a cover limit of £150 million for each claim or series of claims against them in that capacity. The Company also indemnifies its Directors and officers to the extent permitted by law.

Directors' report (continued)

Auditors

Pursuant under the Companies Act 2006 Section 418, each of the Directors confirms that, so far as he or she is aware, there is no relevant audit information of which the Company's auditors are unaware and that the Directors have taken all responsible steps in order to make themselves aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

Approved by the Board of Directors
and signed on behalf of the Board

Hazel Walker (Secretary)
13 June 2011

Statement of directors' responsibilities

The Directors are responsible for preparing the annual 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 International Financial Reporting Standards ("IFRSs") as adopted by the European Union. The financial statements are required by law to be properly prepared in accordance with IFRSs as adopted by the European Union and the Companies Act 2006.

International Accounting Standard 1 requires that financial statements present fairly for each financial year the company's financial position, financial performance and cash flows. This requires the faithful representation of the effects of transactions, other events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the International Accounting Standards Board's 'Framework for the Preparation and Presentation of Financial Statements'. In virtually all circumstances, a fair presentation will be achieved by compliance with all applicable International Financial Reporting Standards. However, directors are also required to:

- select appropriate accounting policies and apply them properly;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- provide additional disclosures when compliance with the specific requirements in IFRSs are insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance; and
- make an assessment of the company's ability to continue as a going concern.

The directors are responsible for keeping proper accounting records that 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 auditors' report

to the Members of Network Rail Infrastructure Finance PLC

We have audited the financial statements of Network Rail Infrastructure Finance PLC for the year ended 31 March 2011 which comprise the Balance sheet, the Statement of comprehensive income, the Statement of cash flows, the Statement of changes in equity and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

Respective responsibilities of directors and auditors

As explained more fully in the Statement of directors' responsibilities set out pages 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.

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.

Scope of the audit of the financial statements

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.

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 2011 and of its result and cash flows for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matter prescribed by the Companies Act 2006

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

Independent auditors' report (continued)

to the Members of Network Rail Infrastructure Finance PLC

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.

Jonathan Hook (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
London
13 June 2011

Statement of comprehensive income

	Notes	Year ended 31 March 2011 £m	Year ended 31 March 2010 £m
Profit from operations		-	-
Investment income	5	1,274	1,028
Finance costs	5	(1,274)	(1,028)
Other gains and losses	6	-	-
Profit before taxation		-	-
Tax	7	-	-
Profit for the year		-	-

All transactions in the current and prior years relate to continuing activities. All income and expense is recognised in the statement of comprehensive income

Statement of changes in equity

	Share capital £m	Retained Earnings £m	Total £m
At 31 March 2009	-	-	-
Net profit for the year	-	-	-
At 31 March 2010	-	-	-
Net profit for the year	-	-	-
At 31 March 2011	-	-	-

Balance sheet

	Notes	31 March 2011 £m	31 March 2010 £m
Non current assets			
Receivables: amounts falling due after more than one year	8	24,349	22,632
Derivative financial instruments	11	576	702
Total non current assets		24,925	23,334
Current assets			
Derivative financial instruments	11	313	417
Receivables: amounts falling due within one year	8	174	253
Cash and cash equivalents		645	2,237
Total current assets		1,132	2,907
Total assets		26,057	26,241
Current liabilities			
Loans	10	(2,309)	(2,220)
Derivative financial instruments	11	(348)	(209)
Other payables	9	(333)	(807)
Total current liabilities		(2,990)	(3,236)
Net current liabilities		(1,858)	(329)
Non current liabilities			
Loans	10	(22,998)	(22,998)
Derivative financial instruments	11	(69)	(7)
Total non current liabilities		(23,067)	(23,005)
Total liabilities		(26,057)	(26,241)
Net assets		-	-
Equity			
Share capital	13	-	-
Retained earnings	14	-	-
Total Equity		-	-

The financial statements were approved by the board of Directors and authorised for issue on 13 June 2011.

They were signed on its behalf by:

Samantha Pitt (Director)

Jonathan Keighley (Director)

Company registration number: 5090412

Statement of cash flows

	Note	31 March 2011 £m	31 March 2010 £m
Net cash outflow from operating activities	15	(1,040)	(1,303)
Financing activities			
Repayment of borrowings		(1,922)	(1,408)
New loans raised		1,780	4,053
Collateral repaid to counterparties		(395)	(508)
Loss on disposal of derivatives not hedge accounted		(15)	(192)
Net cash (outflow)/inflow from financing activities		(552)	1,945
Net (decrease)/increase in cash and cash equivalents		(1,592)	642
Cash and cash equivalents at beginning of the year		2,237	1,595
Cash and cash equivalents at end of the year		645	2,237

Notes to the Financial Statements

Year ended 31 March 2011

1. General information

Network Rail Infrastructure Finance PLC is a Company incorporated in Great Britain and registered in England and Wales under the Companies Act 2006.

The Company's registration number is 5090412.

The Company's registered office is situated at Kings Place, 90 York Way, London N1 9AG.

The Company's principal activities, details of the Company's business activities and key events and changes during the year are contained within the Directors' report on pages 4 to 6.

2. Significant Accounting Policies

The financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRSs") as adopted by the European Union.

The financial statements have been prepared under the historical cost basis, except for the revaluation of derivative financial instruments to fair value.

The principal accounting policies are set out below.

Adoption of new and revised standards

The following new and revised Standards and Interpretations have been adopted in these financial statements. Their adoption has not had any significant impact on the amounts reported in these financial statements but may affect the accounting for future transactions or arrangements.

IFRS 3 (revised)	<i>Business combinations</i>
Amendment to IFRS 1	<i>First time adoption of IFRS</i>
Revised IFRS 1	<i>First time adoption of IFRS</i>
Amendments to IFRS 2	<i>Share-based payments</i>
IAS 27 (revised)	<i>Consolidated and individual financial statements</i>
Amendment to IAS 32	<i>Classification of rights issues</i>
Amendment to IAS 39	<i>Financial Instruments: recognition and measurement (eligible hedged items)</i>
IFRIC 17	<i>Distribution of non-cash assets to owners</i>
IFRIC 18	<i>Transfers of assets from customers</i>
Improvements to IFRS 2009	

At the date of authorisation of these financial statements, the following Standards and Interpretations, which have not been applied in these financial statements, were in issue but not yet effective (and in some cases had not been adopted by the EU):

IFRS 9	<i>Financial instruments</i>
Revised IAS 24	<i>Related party transactions</i>
IFRIC 19	<i>Extinguishing financial liabilities with equity instruments</i>
Amendments to IFRIC 14	<i>Prepayments of a minimum funding requirement</i>

2. Significant Accounting Policies continued

Amendments to IFRS 1	<i>First time adoption of IFRS</i> (comparative IFRS 7 disclosures)
Amendments to IFRS 7	<i>Financial instruments: disclosures</i> (disclosures for transfers of financial assets)
Amendments to IAS 12	<i>Deferred tax</i>
Improvements to IFRS 2010	

The Directors anticipate that the adoption of these Standards and Interpretations in the future periods will have no material effect on the financial statements of the Group.

Going concern

The Company's business activities, together with the factors likely to affect its future development, performance and position, its financial position, its cash flows, liquidity position and borrowing facilities are described in the Director's report on pages 4 to 6. In addition, note 12 to the accounts includes the Company's objectives, policies and processes for managing its capital; its financial risk management objectives; details of its financial instruments and hedging activities; and its exposures to credit risk and liquidity risk.

After making enquiries, the Directors have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the annual report and accounts.

Operating segments

IFRS 8 *Operating Segments* requires operating segments to be identified on the basis of internal reports about components of the Company that are regularly reviewed by the Chief Executive to allocate resources to the segments and to assess their performance. The Company has adopted IFRS 8 for these financial statements. However, there has been no material change in presentation of these statements because the Company operates one class of business, that of acting as issuer for Network Rail's Debt Issuance Programme ("DIP") and undertakes that class of business in one geographical area, Great Britain.

Debt

Debt instruments are initially recorded at fair value, net of discount and direct issue costs. Finance charges, including premiums payable on settlement or redemption and direct issue costs are accounted for on an accruals basis (at amortised cost) in the income statement using the effective interest method and are added to the carrying value of the debt instrument to the extent that they are not settled in the period in which they arise.

2. Significant Accounting Policies (continued)

Derivative financial instruments and hedge accounting

The Company's activities expose it primarily to the financial risks of changes in interest rates and foreign currency exchange rates. The Company uses interest rate swaps and foreign exchange forward contracts to hedge these exposures.

Interest rate swaps and foreign exchange forward contracts are recorded at fair value at inception at each balance sheet date. Movements in fair value are recorded in other gains and losses in the Statement of comprehensive income.

Derivatives embedded in other financial instruments or other host contracts are treated as separate derivatives when their risks and characteristics are not closely related to those of host contracts and the host contracts are not carried at fair value. Unrealised gains or losses are reported in the income statement.

Investments

Investments are recognised on a trade date where a purchase or sale of an investment is under contract whose terms require delivery of the investment within the timeframe established by the market concerned, and are initially measured at cost, including transaction costs.

Investments are classified as available-for-sale and measured at subsequent reporting dates at fair value. For available-for-sale investments, gains or losses from changes in fair value are recognised directly in equity, until the security is disposed of or is determined to be impaired, at which time the cumulative gain or loss previously recognised in equity is included in the income statement for the period.

Foreign currencies

Monetary assets and liabilities expressed in foreign currencies are translated into sterling at rates of exchange prevailing at the end of the financial year. Individual transactions denominated in foreign currencies are translated into sterling at the exchange rates prevailing on the dates payment takes place. Gains or losses realised on any foreign exchange movements are recognised in 'Other gains and losses' in the Income statement.

Intra-group borrowings

The Company provides Network Rail with funding. It passes all transactions and balances through the intra-group borrowings to Network Rail Infrastructure Limited.

Tax

The tax expense represents the sum of the current tax payable and deferred tax. The Company's current tax liability is calculated using the tax rates that have been enacted or substantively enacted by the balance sheet date.

Current taxes are based on the taxable results of the Company and calculated in accordance with tax rules in the United Kingdom.

Deferred tax is the tax expected to be payable or recoverable on the temporary differences that arise when tax authorities recognise and measure assets and liabilities with rules that differ from those of the consolidated accounts. Deferred taxes are calculated under the balance sheet liability method at the rate of tax expected to prevail, subject to the rate being

2. Significant Accounting Policies (continued)

enacted or substantively enacted by that date, when the temporary differences reverse. Deferred tax is not discounted.

Deferred tax liabilities are recognised for all taxable temporary differences; and deferred tax assets are recognised on all deductible temporary differences to the extent that it is probable that there will be taxable profits available against which the temporary timing differences can be utilised.

Deferred tax assets/liabilities are not recognised if the temporary differences arise from the initial recognition of goodwill, non deductible goodwill or from initial recognition (other than business combination) of other assets and liabilities in a transaction that affects neither the taxable profit or loss nor the accounting profit or loss.

Deferred tax is charged or credited in the income statement, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

3. Staff costs

The Directors received no remuneration for their services in the current or prior year. Other than the Directors, there were no employees of the Company in the current or prior year. Administration services are provided by NRIL.

4. Auditors' remuneration

Fees payable to the Company auditors for the audit of the Company's annual accounts of £12,500 (2010: £12,500) have been borne by NRIL. No other fees were payable by the Company to the Company auditors in the current or prior year.

5. Investment income and finance costs

	Year ended 31 March 2011 £m	Year ended 31 March 2010 £m
Investment income - Interest receivable from Network Rail Infrastructure Limited	1,266	1,017
Interest receivable on investments	8	11
Total investment income	1,274	1,028
Finance costs - Interest payable on debt issued under the Debt Issuance Programme	(1,274)	(1,028)
Total finance costs	(1,274)	(1,028)

6. Other gains and losses

	Year ended 31 March 2011 £m	Year ended 31 March 2010 £m
Gains from retranslation of external debt	431	350
Net loss on fair value of external derivative financial instruments	(520)	(513)
Gain on fair value of embedded derivative	89	163
Realised losses arising from derivatives not hedge accounted	(15)	(192)
Received from Network Rail Infrastructure Limited	15	192
	-	-
Total gains and (losses)	-	-

7. Tax

There is a small tax charge of £31,000 (2010: £31,000) on the profit earned by the Company for providing NRIL with a loan facility. Neither is visible as the financial statements are presented in £m.

8. Receivables

	31 March 2011 £m	31 March 2010 £m
Non-current assets		
Loans to Network Rail Infrastructure Limited	24,349	22,632
	24,349	22,632
Current assets		
Interest on loans to Network Rail Infrastructure Limited	174	253
	174	253
Total receivables	24,523	22,885

The loan to NRIL mirrors the external debt in terms of repayment and interest accrued thereon (see note 10).

9. Other payables

	31 March 2011 £m	31 March 2010 £m
Current Liabilities		
Collateral obligation	159	554
Interest payable on bonds issued under the Debt Issuance Programme	168	245
Interest payable on European Investment Bank long term loans	6	8
Total payables	333	807

10. Loans

	31 March 2011 £m	31 March 2010 £m
Bonds issued under Debt Issuance Programme (less unamortised discount and fees)	24,405	24,234
European Investment Bank loans	902	984
	25,307	25,218
The borrowings are repayable as follows:		
On demand or due within one year	2,309	2,220
Due within one to two years	925	2,312
Due within two to five years	3,977	1,981
Due after five years	18,096	18,705
Total	25,307	25,218
Less: amounts repayable within one year (shown under current liabilities):		
Bonds issued under the Debt Issuance Programme	(2,309)	(2,120)
European Investment Bank loans	-	(100)
Amounts repayable within one year	(2,309)	(2,220)
Amounts repayable after more than one year	22,998	22,998

All borrowings are denominated in or swapped into sterling.

10. Loans (continued)

Bonds issued under the Debt Issuance Programme are analysed as follows:

	31 March 2011 £m	31 March 2010 £m
1.085% sterling index linked bond due 2052	111	106
0% sterling index linked bond due 2052	103	102
1.003% sterling index linked bond due 2051	21	20
0.53% sterling index linked bond due 2051	107	102
0.517% sterling index linked bond due 2051	106	101
0% sterling index linked bond due 2051	115	108
0.678% sterling index linked bond due 2048	107	101
1.125% sterling index linked bond due 2047	3,587	3,412
0% sterling index linked bond due 2047	65	67
1.1335% sterling index linked bond due 2045	44	41
1.5646% sterling index linked bond due 2044	238	227
1.1565% sterling index linked bond due 2043	49	46
1.1795% sterling index linked bond due 2041	60	57
1.2219% sterling index linked bond due 2040	236	225
1.2025% sterling index linked bond due 2039	65	62
4.6535% sterling bond due 2038	100	100
1.375% sterling index linked bond due 2037	4,085	3,876
4.75% sterling bond due 2035	1,224	1,223
1.6492% sterling index linked bond due 2035	359	343
4.375% sterling bond due 2030	870	869
1.75% sterling index linked bond due 2027	3,193	3,035
4.57% Norwegian krone bond due 2026	16	16
4.615% Norwegian krone bond due 2026	56	55
1.9618% sterling index linked bond due 2025	301	288
4.75% sterling bond due 2024	728	726
2.28% Japanese yen bond due 2021	75	70
2.315% Japanese yen bond due 2021	75	70
2.15% Japanese yen bond due 2021	75	70
2.76% Swiss franc bond due 2021	204	187
4.625% sterling bond due 2020	997	996
4.4% Canadian dollar bond due 2016	321	324
6% Australian dollar bond due 2016	322	302
4.875% sterling bond due 2015	994	993
1.5% US dollar bond due 2014	936	-
2.5% sterling bond due 2014	748	-
3.5% US dollar bond due 2013	778	821
1.75% US dollar bond due 2013	624	660
4.875% sterling bond due 2012	998	997
2% US dollar bond due 2012	624	658
0.54% US dollar bond due 2012	63	-
4.375% sterling bond due 2011	-	449
5.25% US dollar bond due 2011	625	658
3% US dollar bond due 2011	-	658
5.5% Australian dollar bond due 2010	-	513
5.125% sterling bond due 2010	-	500
	24,405	24,234

10. Loans (continued)

Other long term loans are analysed as follows:

	31 March 2011 £m	31 March 2010 £m
Index-linked European Investment Bank due 2037	402	384
5.57% European Investment Bank due 2013	200	200
5.77% European Investment Bank due 2012	300	300
6.42% European Investment Bank due 2011	-	100
	902	984

The Secretary of State for Transport has provided an unlimited financial indemnity in respect of the above borrowings and those borrowings under the Debt Issuance Programme which expires in 2052.

At 31 March 2010 the Company had the following undrawn committed facilities:

	2011 Drawn £m	2011 Undrawn £m	2011 Total £m	2010 Drawn £m	2010 Undrawn £m	2010 Total £m
Working capital facility	-	1,000	1,000	-	1,000	1,000

Undrawn committed facilities expire as follows:

	2011 Total £m	2010 Total £m
Within one year	1,000	1,000

11. Derivative financial instruments

	31 March 2011		31 March 2010	
	Fair value £m	Notional amounts £m	Fair value £m	Notional amounts £m
Derivative financial assets included in non-current assets	576	1,520	702	2,924
Derivative financial assets included in current assets	103	547	296	872
Embedded derivatives in the inter-company borrowing of Network Rail Infrastructure Limited (all within current assets)	210	6,169	121	6,616
	889	8,236	1,119	10,412
	Fair value £m	Notional amounts £m	Fair value £m	Notional amounts £m
Derivative financial liabilities included in non-current liabilities	(69)	1,636	(7)	693
Derivative financial liabilities included in current liabilities	(348)	2,466	(209)	2,127
	(417)	4,102	(216)	2,820

12. Funding and financial risk management

Introduction

The Company is not a member of the Network Rail Group. However, for accounting purposes the Company is treated as a subsidiary in the consolidated accounts of Network Rail Infrastructure Limited (NRIL). The Network Rail Group is largely debt funded. Debt is issued through Network Rail Infrastructure Finance PLC.

Significant accounting policies

Details of the significant accounting policies and methods adopted, including the criteria for recognition, the basis of measurement and the basis on which income and expenses are recognised, in respect of each class of financial asset, financial liability and equity instrument are disclosed in Note 2 to the financial statements.

12. Funding and financial risk management (continued)

Summary table of financial assets and liabilities

The following table presents the carrying amounts and the fair values of the Company's financial assets and liabilities at 31 March 2011 and 31 March 2010.

The fair values of financial assets and liabilities are recognised at the amount at which the instrument could be exchanged for in a current transaction between willing parties, other than in a forced or liquidation sale. With the exception of bank loans and bonds, all financial assets and liabilities are carried at amounts that approximate to their fair value. Those amounts are in accordance with the significant accounting policies set out in Note 2. Bank loans are valued based on market data at the balance sheet date and the net present value of discounted cash flows. Bonds issued under the DIP are valued based on market data at the balance sheet date. Where market data is not available valuations are obtained from dealing banks.

	31 March 2011		31 March 2010	
	Carrying value	Fair value	Carrying value	Fair value
	£m	£m	£m	£m
Financial assets				
Cash and cash equivalents	645	645	2,237	2,237
Loans and receivables - Loan to Network Rail Infrastructure Limited	24,349	24,349	22,632	22,632
Trade and other receivables	174	174	253	253
Derivative financial instruments	679	679	998	998
Embedded derivative	210	210	121	121
Total financial assets	26,057	26,057	26,241	26,241
Financial liabilities				
Financial liabilities held at amortised cost:				
European Investment Bank loans	(902)	(931)	(984)	(1,055)
Bonds issued under the DIP	(24,405)	(26,320)	(24,234)	(26,002)
	(25,307)	(27,251)	(25,218)	(27,057)
Trade and other payables	(174)	(174)	(253)	(253)
Collateral held	(159)	(159)	(554)	(554)
Derivative financial instruments	(417)	(417)	(216)	(216)
Total financial liabilities	(26,057)	(28,001)	(26,241)	(28,080)

12. Funding and financial risk management (continued)

Derivatives

The Company has contracted with NRIL to administer the DIP, the terms of which are set out in an administration agreement. NRIL has a comprehensive risk management process and its Board have approved and monitor the risk management processes, including documented treasury policies, counterparty limits, controlling and reporting structures.

Proceeds from the DIP are lent on to NRIL under the inter-company loan agreement which gives rise to an embedded derivative. In addition, the Company also uses other derivatives to reduce the foreign exchange risk and interest rate risk of Network Rail Infrastructure Limited. The Company does not use derivative financial instruments for speculative purposes. The use of derivative instruments can give rise to credit and market risk. Market risk is the possibility that future changes in foreign exchange rates and interest rates may make a derivative more or less valuable. Since the Company uses derivatives for risk management, market risk relating to derivative instruments will principally be offset by changes in the valuation of the underlying assets or liabilities.

Credit risk

The credit risk with regard to all classes of derivative financial instruments is limited because counterparties are banks with high credit ratings assigned by international credit-rating agencies. A Treasury sub-committee of the NRIL Board authorises the policy for setting counterparty limits based on credit-ratings. The Company spreads its exposure over a number of counterparties, and has strict policies on how much exposure can be assigned to each counterparty before cash collateralisation is sought.

The concentration of the Company's investments varies depending on the level of surplus liquidity. However, because of the strict criteria governing counterparties' suitability the risk is mitigated. A Treasury sub-committee of the NRIL Board also authorises the types of investment and borrowing instruments that can be used.

The credit risk on the inter-company loan with NRIL is considered limited as the Secretary of State for Transport has provided an unlimited financial indemnity in respect of borrowings under the Debt Issuance Programme which expires in 2052 meaning that obligations to debt holders could still be fulfilled without NRIL.

Particular attention is paid to the credit risk of swap counterparties. The credit risk with regard to all classes of derivative financial instruments is limited because Network Rail has arrangements in place which limits each bank to a threshold (based on credit ratings) which if exceeded requires the bank to post cash collateral. The thresholds were reviewed by the Treasury Committee in the year and the banking group are required to post collateral on positive mark to market swaps.

Foreign exchange risk

The Company is exposed to currency risks from its financing and, from time to time, investing activities. Foreign exchange risk for all currencies is managed by the use of currency swaps to limit the effects of movements in exchange rates on foreign currency denominated assets and liabilities.

It is estimated that a general increase of ten percentage points in the value of any currency against sterling would have no material effect on the Company's net profit before tax or equity. This is due to the workings of the inter-company loan agreement and the consequent embedded derivative.

12. Funding and financial risk management (continued)

Interest and inflation rate risk

The Company is exposed to interest rate risks from its financing and investing activities. Interest rate risk for all debt is managed by the use of interest rate swaps to limit the effects of movements in interest rates on floating rate liabilities.

Debt of £25,313m (2010: £23,689m) is arranged at or swapped into fixed rates. Fixing interest rates exposes the Company to fair value interest rate risk. Other borrowings were arranged at floating rates, thus exposing the Company to cash flow interest rate risk.

However, due to the workings of the inter-company loan agreement and the consequent embedded derivative, an increase or decrease in average interest rates during the year would have no impact upon the income statement, the net assets or the reserves of the Company.

The Company has £100m (2010: £325m) notional value of real rate swaps with an average real rate of inflation of -0.30% (2010: 0.28%) and £1,746m (2010: £2,127m) notional value of gilt locks with an average real rate of inflation of 1.64% (2010: 1.35%).

The Company has certain debt issuances which are index-linked and so is exposed to movements in inflation rates. The Company does not enter into any derivative arrangements to hedge these.

Due to the workings of the inter-company loan agreement and the consequent embedded derivative an increase or decrease in average inflation rates during the year would have no impact upon the income statement, the net assets or the reserves of the Company.

Embedded derivatives

The obligations and rights of the Company under the inter-company loan agreement with NRIL give rise to an embedded derivative in that agreement which reflects the external currency and interest rates risks to which the Company is exposed. The embedded derivative is treated as separate a derivative and accounted for in accordance with the accounting policy Note 2.

Liquidity risk management

Ultimate responsibility for liquidity risk management rests with the board of Directors. A Treasury sub-committee of the Board of NRIL, who acts as administrator for NRIF, has built an appropriate liquidity risk management framework for the management of the Company's short, medium and long-term funding and liquidity management requirements. Treasury is subject to regular internal audits.

Liquidity risk is managed by maintaining adequate banking facilities and reserve borrowing facilities by continuously monitoring forecast and actual cash flows and matching maturity profiles of financial assets and liabilities.

In addition, the Secretary of State for Transport has provided an unlimited financial indemnity in respect of borrowings under the Debt Issuance Programme which expires in 2052.

12. Funding and financial risk management (continued)

The following table details the Company's remaining contractual maturity for its financial liabilities. The table has been drawn up on the undiscounted cash flows of financial liabilities based on the earliest date on which the Company can be required to pay and, therefore, differs from both the carrying value and the fair value. The table includes both interest and principal cash flows.

	Within 1 year £m	1-2 years £m	2-5 years £m	5+ years £m	Total
31 March 2011					
Non derivative financial liabilities					
Bank loans and overdrafts	33	324	225	1,161	1,743
Bonds issued under the Debt Issuance Programme					
Sterling denominated DIP bonds	1,301	252	2,468	6,358	10,379
Sterling denominated index-linked DIP bonds	176	182	585	41,063	42,006
Foreign currency denominated DIP bonds	1,173	581	1,771	689	4,214
Derivative financial liabilities					
Net settled derivative contracts	109	-	(8)	66	167
Gross settled derivative contracts – receipts	(1,173)	(581)	(1,771)	(689)	(4,214)
Gross settled derivative contracts – payments	1,342	744	2,001	640	4,727
Collateral held	159	-	-	-	159
	3,120	1,502	5,271	49,288	59,181

12. Funding and financial risk management (continued)

	Within 1 year £m	1-2 years £m	2-5 years £m	5+ years £m	Total
31 March 2010					
Non derivative financial liabilities					
Bank loans and overdrafts	139	33	546	1,407	2,125
Bonds issued under the Debt Issuance Programme					
Sterling denominated DIP bonds	1,277	1,282	699	7,591	10,849
Sterling denominated index-linked DIP bonds	169	175	574	35,056	35,974
Foreign currency denominated DIP bonds	1,341	1,521	1,688	1,185	5,735
Derivative financial liabilities					
Net settled derivative contracts	88	-	(1)	(19)	68
Gross settled derivative contracts – receipts	(1,341)	(1,521)	(1,688)	(1,185)	(5,735)
Gross settled derivative contracts – payments	975	691	1,479	871	4,016
Collateral held	554	-	-	-	554
	3,202	2,181	3,297	44,906	53,586

Borrowings

Details of the Company's undrawn committed facilities and types of debt instruments used can be found in Note 10.

12. Funding and financial risk management (continued)

Derivative maturity

The derivatives have the following maturities:

	31 March 2011		31 March 2010	
	Fair value	Notional amount	Fair value	Notional amount
	£m	£m	£m	£m
Foreign currency swaps				
Within one year	74	1,267	463	1,419
One to five years	150	2,526	150	1,966
More than five years	354	529	366	779
	578	4,322	979	4,164
Interest rate derivatives				
Within one year	(319)	1,747	(209)	2,127
One to five years	-	-	12	325
More than five years	3	100	-	-
	(316)	1,847	(197)	2,452
Embedded derivatives				
Within one year	210	6,169	121	6,616
One to five years	-	-	-	-
More than five years	-	-	-	-
	210	6,169	121	6,616

Fair value measurements recognised in the Balance sheet

The following table provides an analysis of financial instruments that are measured subsequent to initial recognition at fair value, grouped into Levels 1 to 3 based on the degree to which the fair value is observable:

- Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities
- Level 2 fair value measurements are those derived from inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).

	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial Assets at fair value through profit and loss				
Derivative Financial Assets	-	889	-	889
Financial Liabilities at fair value through profit and loss				
Derivative Financial Liabilities	-	(417)	-	(417)
Total	-	472	-	472

There were no transfers between Level 1 and 2 during the year.

13. Share capital

	2011 £	2010 £
Authorised, called up, allotted and fully paid:		
50,000 ordinary shares of £1 partly paid to £0.25 each	12,500	12,500

14. Retained earnings

	Retained earnings £m
At 1 April 2009	-
Profit for the financial year	-
At 1 April 2010	-
Profit for the financial year	-
At 31 March 2011	-

15. Notes to the cash flow statement

	31 March 2011 £m	31 March 2010 £m
Profit from operations	-	-
Operating cash flow before movements in working capital		-
Increase in receivables	(1,040)	(1,303)
Increase in payables	-	-
Cash consumed by operations	(1,040)	(1,303)
Interest received	693	1,055
Interest paid	(693)	(1,055)
Net cash consumed by operating activities	(1,040)	(1,303)

16. Analysis of changes in net debt

	At 1 April 2010 £m	Cash flows £m	Non-cash movements £m	Capital accretion £m	Amortisation of discount £m	Foreign exchange differences £m	At 31 March 2011 £m
Cash *	1,683	(1,197)	-	-	-	-	486
Borrowings due within one year	(2,220)	1,858	(2,312)	-	(4)	369	(2,309)
Borrowings due after one year	(22,998)	(1,716)	2,312	(657)	(1)	62	(22,998)
Net Debt	(23,535)	(1,055)	-	(657)	(5)	431	(24,821)

* Excludes collateral held of £159m

	At 1 April 2009 £m	Cash flows £m	Non-cash movements £m	Capital accretion £m	Amortisation of discount £m	Foreign exchange differences £m	At 31 March 2010 £m
Cash *	533	1,150	-	-	-	-	1,683
Borrowings due within one year	(1,755)	1,223	(2,007)	-	-	319	(2,220)
Borrowings due after one year	(20,834)	(3,868)	2,007	(325)	(9)	31	(22,998)
Net Debt	(22,056)	(1,495)	-	(325)	(9)	350	(23,535)

* Excludes collateral held of £554m

17. Controlling party and related party transactions

49,999 shares of the Company are held by HSBC Trustee (C.I.) Limited. A nominee for the trustee, HSBC Private Banking Nominee 1 (Jersey) Limited holds 1 share. All shares in the Company are held for charitable purposes.

The Company is not a member of the Network Rail Group or related to or controlled by the Secretary of State for Transport.

For accounting purposes the Company is treated as a subsidiary in the consolidated accounts of Network Rail Infrastructure Limited.

Transactions with Network Rail Infrastructure Limited are clearly identified within the relevant notes to the accounts.