

**NORTHLINK FERRIES LIMITED
DIRECTORS' REPORT & FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 MARCH 2011**

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Directors' Report

The Directors present their Directors' Report and financial statements for the year ended 31 March 2011.

Principal activity and business review

The Company holds the contract for the provision of the Northern Isles ferry services for the 6-year period ending June 2012.

The principal activity of the Company is the provision of lifeline ferry services under this contract with the Scottish Government. Under the terms of the contract, the Company receives grant support from the Scottish Government.

The Company made a profit for the year before tax of £1.4m. A dividend of £1.0m was paid to the Company's sole shareholder during the year.

The operating performance of the ferry services is monitored by the Scottish Government under the terms of the contract for the provision of the lifeline services against measures for reliability and punctuality (allowing for weather and safety related disruptions), the availability of onboard services at the port terminals and for the welfare of livestock carried.

During the year to 31 March 2011, the Company achieved reliability and punctuality levels of 99.8% and 99.3% respectively; 100% record was achieved on the other targets.

Revenue from fares and other sources at £25.1m was higher than anticipated and operating costs were in line with expectations.

MV Helliar was deployed on the NorthLink freight operation on a time charter basis from January 2011, replacing MV Clare whose time charter had expired.

The Board were delighted that the Company won the Scottish Government backed "Healthy Living Award".

It is anticipated that an Invitation to Tender for the next 6-year contract to operate the services to the Northern Isles will be issued by the Scottish Government later this year. The Company intends to submit a bid to operate the services to the Northern Isles for the 6-year period commencing July 2012.

The Board examines, on an ongoing basis, existing practices with a view to identifying more efficient and cost effective ways of delivering and improving standards of service. In the opinion of the Directors, the state of affairs of the Company is satisfactory.

Political and charitable donations

The Company made no political or charitable donations during the year. However, the Company supports a range of local organisations through travel related sponsorship. During the year the value of travel related sponsorship was £79,000 (2010: £87,000).

Directors and their interests

The Directors who held office during the year and up to the date of this report were as follows:

P K Timms	
C A Robertson	- appointed 21 July 2010
W S M Davidson	- appointed 1 April 2011
I Gillies	
A M Lynch	
L B MacLeod	- resigned 27 May 2011
D C McGibbon	
N L Quirk	
P Stark	- resigned 27 May 2011
G A Taylor	
R Sinclair	- resigned 31 December 2010
W L Sinclair	- retired 30 June 2010

Dr Robert Sinclair resigned from office to pursue other interests; Mr MacLeod and Ms Stark resigned as part of a corporate restructuring programme.

None of the Directors had any beneficial interest in the share capital of the Company at any time during the year.

The Company's sole Shareholder is David MacBrayne Ltd, which is wholly owned by the Scottish Ministers.

Employees

The Company is a non-discriminatory employer operating an Equal Opportunities Policy and is committed to ensuring that all individuals are treated fairly, with respect and are valued.

Policy of employment of people with disabilities

It is the Company's policy to consider applications for employment from people with disabilities on the same basis as other potential employees subject to the nature and extent of disability and the degree of physical fitness demanded of the position. Ability and aptitude are the determining factors in the selection, training, career development and promotion of all employees with disabilities. If any employee becomes disabled during the period of employment, the Company will, if possible, retain the employee for duties commensurate with the employee's abilities following the disablement.

Adoption of going concern basis

On the basis of the information available to them, the Directors have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future. For this reason, the Directors consider it appropriate to adopt the going concern basis in preparing the financial statements.

Disclosure of information to Auditors

The Directors who held office at the date of approval of this Directors' Report confirm that, so far as they are each aware, there is no relevant audit information of which the Company's auditors are unaware and each Director has taken all the steps that he/she ought to have taken as a Director to make himself/herself aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

Auditors

A resolution to re-appoint KPMG LLP as auditors of all companies within the David MacBrayne Group will be put to the members at the David MacBrayne Ltd Annual General Meeting.

On behalf of the Board



W S M Davidson
Director
22 June 2011

Statement of Directors' responsibilities in respect of the Directors' Report and the financial statements

The Directors are responsible for preparing the Directors' Report and the financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare financial statements for each financial year. Under that law they have elected to prepare the financial statements in accordance with UK Accounting Standards and applicable law (UK Generally Accepted Accounting Practice).

Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period.

In preparing these financial statements, the Directors are required to:

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

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the financial statements comply with the Companies Act 2006. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Company and to prevent and detect fraud and other irregularities.

The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Independent Auditors' Report to the members of NorthLink Ferries Limited

We have audited the financial statements of NorthLink Ferries Limited for the year ended 31 March 2011 set out on pages 5 to 12. The financial reporting framework that has been applied in their preparation is applicable law and UK Accounting Standards (UK Generally Accepted Accounting Practice).

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

Respective responsibilities of Directors and auditors

As explained more fully in the Directors' Responsibilities Statement set out on page 3, 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 (APB's) Ethical Standards for Auditors.

Scope of the audit of the financial statements

A description of the scope of an audit of financial statements is provided on the APB's web-site at www.frc.org.uk/apb/scope/private.cfm.

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 profit for the year then ended;
- have been properly prepared in accordance with UK Generally Accepted Accounting Practice; 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.

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.



**G Macrae (Senior Statutory Auditor)
for and on behalf of KPMG LLP**

Chartered Accountants
191 West George Street
Glasgow
G2 2LJ

22 June 2011

**Profit and Loss Account
for the year ended 31 March 2011**

	Note	2011 £000	2010 £000
Turnover	2	61,115	58,275
Cost of sales		(58,086)	(54,025)
Gross profit		3,029	4,250
Administrative expenses		(1,612)	(1,883)
Operating profit		1,417	2,367
Interest receivable and similar income	6	10	6
Interest payable and similar charges	7	-	(35)
Profit on ordinary activities before taxation	3-4	1,427	2,338
Tax on profit on ordinary activities	8	(5)	(5)
Profit for the financial year	18	1,422	2,333

All results are derived from continuing operations.

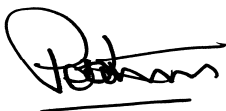
There were no recognised gains or losses other than the results for the financial years reported above.

The accompanying notes are an integral part of these financial statements

**Balance Sheet
as at 31 March 2011**

	Note	2011 £000	2010 £000
Fixed assets			
Tangible assets	9	3,333	4,311
Investments	11	-	-
		<hr/>	<hr/>
		3,333	4,311
		<hr/>	<hr/>
Current assets			
Stocks	12	987	673
Debtors	13	5,298	6,580
Cash at bank and in hand		4,458	2,166
		<hr/>	<hr/>
		10,743	9,419
		<hr/>	<hr/>
Creditors			
Amounts falling due within one year	14	(6,964)	(5,808)
		<hr/>	<hr/>
Net current assets		3,779	3,611
		<hr/>	<hr/>
Total assets less current liabilities		7,112	7,922
		<hr/>	<hr/>
Provision for liabilities	15	-	(400)
		<hr/>	<hr/>
Accruals and deferred income	16	(3,185)	(4,017)
		<hr/>	<hr/>
Net assets		3,927	3,505
		<hr/>	<hr/>
Capital and reserves			
Called up share capital	17	74	74
Profit and loss account	18	3,853	3,431
		<hr/>	<hr/>
Shareholder's funds	19	3,927	3,505
		<hr/>	<hr/>

These financial statements were approved by the Board of Directors and signed on 22 June 2011 on its behalf by:



P K Timms, Chairman



A M Lynch, Director

The accompanying notes are an integral part of these financial statements

Notes on the financial statements

1. Accounting policies

(a) Basis of preparation

These financial statements have been prepared under the historical cost accounting convention and in accordance with applicable accounting standards. A summary of the more important policies, which have been applied consistently, is set out below.

The Company is exempt by virtue of s400 of the Companies Act 2006 from the requirement to prepare group financial statements. These financial statements present information about the Company as an individual undertaking and not about its Group.

(b) Tangible assets

Gross book values of all tangible assets are stated at cost. No depreciation is charged until the asset comes into use.

(c) Investments

Fixed asset investments are carried at cost.

(d) Depreciation

Depreciation is provided on tangible assets by equal instalments calculated to write off the cost (taking account of anticipated residual values) over their estimated useful economic lives as follows:

Buildings	-	20 years
Plant and equipment	-	3 - 6 years
Computer equipment	-	3 years

(e) Capital Grants

Capital grants are deferred and taken to the profit and loss account over the anticipated lives of the assets to which they relate.

(f) Operating Leases

Operating lease rentals are charged to the profit and loss account on a straight line basis over the period of the lease.

(g) Stock

Stock is valued at the lower of average invoiced cost and net realisable value.

(h) Maintenance and repair costs

Routine maintenance and repair costs, as well as vessel overhaul costs, are charged to the profit and loss account in the financial year in which the work is performed.

(i) Taxation

The Company has elected into the Tonnage Tax regime available to shipping organisations. Tonnage tax is levied wholly on the net tonnage of the vessels operated by the Company. Accordingly, the amount of Tonnage Tax payable is not affected by the amount of accounting profits or losses.

(j) Post retirement benefits

The Company operates a defined contribution pension scheme. The assets of the scheme are held separately from those of the Company in independently administered funds. The amount charged to the profit and loss account represents the contributions payable by the Company to the scheme in respect of the accounting year.

(k) Derivatives and financial instruments

The Group has adopted FRS 13: Derivatives and other financial instruments. The Company's financial instruments comprise cash, other liquid resources and various items such as trade debtors and creditors which arise directly from operations. The Company's policy is not to trade or speculate in financial instruments but to utilise them to finance operations. However, the Group enters into fuel hedging arrangements as and when this is considered appropriate.

(l) Receipts in advance

Receipts for advanced bookings are recognised with reference to time of travel. The deferred element of this income is shown under creditors.

(m) Foreign currencies

Transactions in foreign currencies are recorded using the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated using the contracted rate or the rate of exchange ruling at the balance sheet date and the gains or losses on translation are included in the profit and loss account.

(n) Dividend to Shareholder

A dividend is payable annually to the holding company, David MacBrayne Limited. The quantum of the dividend is dependent on the estimated profit which is expected to be achieved for the financial year and the Company's cash position.

Notes on the financial statements continued

2. Turnover

Turnover represents the amount (excluding value added tax) derived from the operation of ferry services and also includes grant income received from the Scottish Government. Transportation income is recognised at point of departure and all other income is recognised at point of sale of the goods or services.

Analysis of turnover:

	2011 £000	2010 £000
Fares and other income	25,051	23,832
Grant receivable from the Scottish Government	36,064	34,443
	<hr/> 61,115	<hr/> 58,275

3. Profit on ordinary activities before tax

Profit on ordinary activities before taxation is stated after charging/(crediting):

	2011 £000	Restated 2010 £000
Auditors' remuneration - audit of these financial statements	25	30
- other services relating to taxation	7	2
Amortisation of intangible assets	-	248
Depreciation written off tangible fixed assets	978	1,329
Gain on disposal of fixed assets	-	(358)
Amortisation of capital grants	(832)	(1,187)
Agency staff costs	11,131	11,411
Operating lease rentals - property	707	637
- vessels/other	14,984	12,551
	<hr/> 14,984	<hr/> 12,551

4. Staff numbers and costs

The average number of people employed by the Company, including Directors, during the year was 71 (2010: 69).

The aggregate payroll costs of these people were as follows:

	2011 £000	2010 £000
Wages and salaries	1,337	1,205
Social security costs	133	121
Pension costs (note 21)	57	56
	<hr/> 1,527	<hr/> 1,382

Notes on the financial statements continued

5. Directors' remuneration

None of the Directors received remuneration for services to the Company during the year.

6. Interest receivable and similar income

	2011 £000	2010 £000
Bank interest receivable	10	6
	<hr/>	<hr/>

7. Interest payable and similar charges

	2011 £000	2010 £000
Amounts payable to group undertakings	-	35
	<hr/>	<hr/>

8. Taxation

Analysis of charge for year

	2011 £000	2010 £000
UK corporation tax		
Current tax on income for the year being total current tax	5	5
	<hr/>	<hr/>
Total current tax being tax on profit on ordinary activities	5	5
	<hr/>	<hr/>

Factors affecting the tax charge for the current year

The current tax charge for the year is lower than (2010: lower than) the standard rate of corporation tax in the UK, 28% (2010: 28%). The differences are explained below:

	2011 £000	2010 £000
Current tax reconciliation		
Profit on ordinary activities before tax	1,427	2,338
	<hr/>	<hr/>
Current tax at 28% (2010: 28%)	400	655
Effects of:		
Tonnage tax	(395)	(650)
	<hr/>	<hr/>
Total current tax charge	5	5
	<hr/>	<hr/>

Factors affecting future tax charges

The Company has elected into the Tonnage Tax regime available to shipping organisations and has been under that regime throughout this financial year. The Company will continue to be under the Tonnage Tax regime for the foreseeable future and there are no other taxation charges for the current year. Tonnage tax is levied wholly on the net tonnage of the vessels operated by the Company. Accordingly, the amount of tonnage tax payable is not affected by the amount of accounting profits or losses.

Notes on the financial statements continued

9. Tangible fixed assets

	Buildings £000	Plant and equipment £000	Computer equipment £000	Total £000
Cost				
As at 1 April 2010	2,531	3,601	729	6,861
As at 31 March 2011	2,531	3,601	729	6,861
Depreciation				
As at 1 April 2010	162	1,869	519	2,550
Transfers	-	-	-	-
Depreciation charge	127	722	129	978
As at 31 March 2011	289	2,591	648	3,528
Net book value				
As at 31 March 2011	2,242	1,010	81	3,333
As at 1 April 2010	2,369	1,732	210	4,311

10. Cash flow statement

Under FRS1, the Company is exempt from the requirement to prepare a cash flow statement on the grounds that it is a wholly owned subsidiary and the parent undertaking includes the Company in its published consolidated financial statements.

11. Investments

£000

At beginning and end of year

-

The Company owns the whole of the issued ordinary share capital of NorthLink Crewing Guernsey Ltd, which is registered in Guernsey, and administers the offshore crewing arrangements.

12. Stocks

	2011 £000	2010 £000
On board fuel stocks	811	505
Finished goods and goods for resale	176	168
	987	673

13. Debtors

	2011 £000	2010 £000
Trade debtors	1,229	1,220
Amounts owed by Group undertakings	355	122
Other debtors and prepayments	3,714	5,238
	5,298	6,580

Included within other debtors and prepayments is £279,000 (2010: £1,984,000) owed from the Scottish Government.

14. Creditors: amounts falling due within one year

	2011 £000	2010 £000
Trade creditors	2,943	2,168
Other creditors and accruals	2,001	1,734
Deferred income	1,898	1,636
Corporation tax	5	5
Amounts owed to Group undertakings	117	265
	<hr/>	<hr/>
	6,964	5,808
	<hr/>	<hr/>

15. Provisions for liabilities

	2011 £000	2010 £000
Provision for liabilities	-	400
	<hr/>	<hr/>

The above provision is wholly in respect of employment related legal claims and was reversed in 2011.

16. Accruals and deferred income

	Capital based grants £000
At beginning of year	4,017
New grants in year	-
Disposals	-
Amortisation	(832)
	<hr/>
At end of year	3,185
	<hr/>

17. Called up share capital

	2011 £000	2010 £000
Authorised, allotted, called up and fully paid		
74,496 ordinary shares of £1 each (classified in Shareholders' funds)	74	74
	<hr/>	<hr/>

18. Profit and loss account

	2011 £000	2010 £000
At beginning of year	3,431	2,598
Profit for the year	1,422	2,333
Dividend paid during the year	(1,000)	(1,500)
	<hr/>	<hr/>
At end of year	3,853	3,431
	<hr/>	<hr/>

19. Reconciliation of movements in Shareholders' funds

	2011 £000	2010 £000
Opening Shareholders' funds	3,505	2,672
Profit for the financial year	1,422	2,333
Dividend paid during the year	(1,000)	(1,500)
	<hr/>	<hr/>
Closing Shareholders' funds	3,927	3,505
	<hr/>	<hr/>

Notes on the financial statements continued

20. Commitments

Annual commitments under non-cancellable operating leases are as follows:

	2011	2011	2010	Restated
	Land and	Other	Land and	2010
	Buildings	£000	Buildings	Other
	£000	£000	£000	£000
Operating leases which expire:				
2 - 5 years	676	15,385	628	14,741
	<hr/>	<hr/>	<hr/>	<hr/>

21. Pension scheme

The Company operates a defined contribution pension scheme. The pension charge for the year represents contributions payable by the Company to the scheme and amounted to £57,000 (2010: £56,000).

The Company also paid £254,000 to the Merchant Navy Officers' Pension Fund in respect of active member employer deficit contributions (2010: £300,000).

22. Related party disclosures

The Company is wholly owned by David MacBrayne Limited, its immediate parent company, which is in turn wholly-owned by the Scottish Ministers. The Company has taken advantage of the exemption contained in FRS 8 and has not disclosed transactions or balances with entities which form part of the Group which is consolidated (note 23).

Details of transactions with the Scottish Ministers during the year and the amounts due as at 31 March 2011 are as follows:

	2011	2010
	£000	£000
Transactions during the year – receivable:		
Grant income	36,064	34,657
	<hr/>	<hr/>
Amounts due at end of year - receivable:	279	1,699
	<hr/>	<hr/>

23. Ultimate parent company

The Company is a subsidiary undertaking of David MacBrayne Limited which is in turn wholly-owned by the Scottish Ministers.

The largest Group in which the results of the Company are consolidated is that headed by David MacBrayne Limited. The consolidated accounts of this Company are available to the public and may be obtained from Ferry Terminal, Gourock, PA19 1QP. No other group accounts include the results of the Company.

Corporate information

Registered office	The Ferry Terminal Gourock PA19 1QP
Auditors	KPMG LLP
Solicitors	Shepherd and Wedderburn LLP
Bankers	The Royal Bank of Scotland plc
Principal insurers	The North of England Protecting & Indemnity Association
Website	www.northlinkferries.co.uk

NorthLink Ferries Limited

The UK authorities require NorthLink Ferries Ltd to produce separate audited Profit and Loss accounts for Public Service activities and for Commercial activities.

The separate Profit and Loss accounts are provided below:

Profit and Loss Accounts for the year ended 31 March 2011

	Public Service Contract £m	Commercial Activity £m	Total £m
Turnover	48.9	12.2	61.1
Cost of Sales	46.3	11.8	58.1
Gross Profit	<u>2.6</u>	<u>0.4</u>	<u>3.0</u>
Administrative expenditure	1.5	0.1	1.6
Operating profit/(loss)	<u><u>1.1</u></u>	<u><u>0.3</u></u>	<u><u>1.4</u></u>