

Serco Limited

Annual Report and Financial Statements

for the Year Ended 31 December 2010



A company registered in England and Wales, number 00242246

Serco Limited
Contents

Company Information	1
Directors' Report	2 to 11
Directors' Responsibilities Statement	12
Independent Auditor's Report	13
Profit and Loss Account	14
Statement of Total Recognised Gains and Losses	15
Balance Sheet	16
Notes to the Financial Statements	17 to 43

Serco Limited
Company Information

Registered office Serco House
16 Bartley Wood Business Park
Bartley Way
Hook
Hampshire
RG27 9UY

Auditors Deloitte LLP
London
United Kingdom

Serco Limited

Directors' Report for the Year Ended 31 December 2010

The directors present their annual report and the audited financial statements for the year ended 31 December 2010. As set out in note 1 to the financial statements, the directors consider it appropriate to prepare the accounts on the going concern basis.

Principal activities

The Company operates to improve services mainly in the public sector by managing people, processes, technology and assets more effectively. Serco Limited supports governments, agencies and companies by offering operational, management and consulting expertise in the aerospace, defence, education, health, home affairs, local government, science, technology, transport and commercial sectors.

The Company's work for national and local governments involves us in the most important areas of public service, including transport, defence, science, employment, offender management, IT, BPO and education. Our private sector customers are industry-leading organisations in a wide variety of markets.

Business review

Turnover has increased by £59.7m or 3.4% in 2010 (2009 increase of £190.1m or 12.1%). Operating profit has increased by £39.5m (2009 decrease of £7.7m) to £87.4m and now represents 4.8% of turnover (2009 2.7%). Profit on disposal of investments amounted to £22.6m (2009 £nil). Net assets of the Company have increased by £63.6m to £523.5m (2009 decrease of £103.6m). A dividend of £30.0m (2009 £40.0m) was paid to the parent company during the year.

Restatement of segmental information

At the start of the financial year, the Company repositioned its business to maximise the focus on growth and opportunities and to ensure that it maintains a flexible and devolved organisation which is responsive to its customers' needs. From 1 January 2010, the Company reorganised its business into three new divisions focussed on the Company's principal markets: Civil Government, Local Government and Commercial, and Defence, Science and Nuclear. The key changes are as follows:

Civil Government, our Healthcare, Home Affairs and Welfare to Work business, is included in the new Civil Government market segment, and our Consulting, Education, Integrated Services, IT and BPO businesses are part of the new Local Government and Commercial market segment.

Defence has transferred to the new Defence, Science and Nuclear market segment.

Transport has been transferred to Civil Government.

Science has been transferred to Defence, Science and Nuclear.

As a consequence of these changes, previously published financial information on turnover by segment in note 2 has been restated. There is no impact on the Company's primary financial statements.

Serco Limited

Directors' Report for the Year Ended 31 December 2010

The Company manages its business on a market segment basis as reported in note 2

Civil Government

This market segment includes our UK and Middle Eastern operations in transport, home affairs (custodial, immigration and field services and border security and control), welfare to work and healthcare

The Company is a major provider of transport facilities, including operation of the Docklands Light Railway. On the Docklands Light Railway, customer satisfaction was 95.4% for overall service and 96.3% for safety and security in the fourth quarter of 2010. Passenger numbers grew in 2010, and were 9.3% higher than last year at 75.2 million journeys.

In August 2010, the Company launched Barclays Cycle Hire for Transport in London. By the end of the year, over 110,000 members had registered and the scheme is now also available to casual users. In total, over 2 million journeys have been made to date and in a survey, 91% of members said that they were happy with the service.

In home affairs, the Company signed a contract with the Ministry of Justice to provide and operate a new prison at Belmarsh West London. The contract has a value of approximately £415m over 26.5 years. The Company was also awarded a two year extension, valued at £38m, to our contract to run Colnbrook Immigration Removal Centre and a three year, £32m extension to our contract to manage Yarl's Wood Immigration Removal Centre. In addition, the Company secured an additional two years for our electronic monitoring contract for Scotland, valued at around £10m, and signed a one year extension to our electronic monitoring contract for England and Wales, valued at an additional £38m of revenue at current levels.

In border security and control, the Home Office has announced the termination of its e-Borders contract with Raytheon, the prime supplier of this advanced border control and security services programme to the UK Border Agency. As a subcontractor on the programme, the Company continues to fulfil its obligations to operate key parts of the existing service and remains fully committed to the e-Borders programme.

Within the welfare to work market, the Company has operated three Flexible New Deal contracts with the Department for Work and Pensions, helping people claiming Jobseekers Allowance who have been unemployed for more than 12 months to find sustainable work. These contracts, along with all other existing back to work schemes, will now end in June 2011 and be replaced by the Work Programme contracts, of which the Company has been named prime contractor in two areas - South Yorkshire and the West Midlands.

Defence Science and Nuclear

Defence, Science and Nuclear (DSN) represents the Company's operational support services in the UK defence markets, science-based businesses such as our energy market operations and nuclear safety and assurance businesses.

DSN's revenue reduced by 4.6% which reflected a slowdown both in decision making and in major contract awards in advance of the UK election and the Strategic Defence and Security Review during 2010. Key awards last year included a renewed and expanded multi-activity contract valued at £100m over ten years to provide services at RAF Halton which Serco has served since 1997, and RAF High Wycombe, the home of Headquarters Air Command. At RAF Brize Norton, the main gateway for British military personnel on overseas operations, the Ministry of Defence awarded the Company a contract for up to six years to deliver essential support services, worth approximately £35m.

Bridging the defence and energy markets, a new eight year contract with the MOD valued at around £20m to Serco, will help the UK tackle climate change through offshore wind energy. As prime contractor, the Company is working with Lockheed Martin to introduce radar technology that resists interference from wind farms, removing a significant obstacle to the roll out of offshore power across the UK.

In the civil energy market, Westinghouse has appointed the Company as their lead nuclear safety advisor in the UK. Serco's role is to lead a team of experts to help Westinghouse complete Step 4 of the Genenc Design Assessment for the AP1000, a critical stage in the reactor design approval process being conducted by the UK Nuclear Regulators which is due to complete in 2011.

In the expanding training market, the Company secured a 15 year contract worth more than £55m to manage and operate the Emergency Planning College on behalf of the Cabinet Office, including training delivery and support, sales and marketing, finance, estate management, ICT and security.

Serco Limited

Directors' Report for the Year Ended 31 December 2010

Local Government and Commercial

The Local Government and Commercial market segment comprises the Company's IT & BPO, integrated and environmental services, education, consulting and commercial businesses. Solutions for local government meet a wide range of local government's current and emerging needs, with services covering waste management, recycling, e-government, leisure, education and communications technology (ICT). Business in the private sector is dominated by multi-service facilities management contracts delivering a range of services from helpdesk operations to buildings maintenance, reception services, catering, cleaning, chauffeur services and stores management.

In the IT and BPO sector the Company won a new contract with Hertfordshire County Council to deliver a ground breaking strategic partnership. The contract, due to commence in April 2011, is valued at up to £200m over eight years and will achieve efficiency savings for the Council of at least £25m. The contract will provide front and back office operations, including ICT services, business processes such as finance, payroll and human resources, and support services such as facilities management, customer contact centres and occupational health.

In 2010 the Company successfully rebid for the contract to provide ICT services to the London Borough of Enfield. The new contract will deliver guaranteed cost savings of 20% for the Council, improve services for its employees and improve communication and interaction with residents. The initial five year contract is valued at £24m, with an option to extend for a further four years.

The replacement of the Regional Development Agencies with Local Enterprise Partnerships and related funding cuts will see the Company's regional Business Link services close by the end of 2011.

Within the integrated and environmental services business, the Company has been awarded a 25-year Waste Improvement Plan contract by Sandwell Metropolitan Borough Council, valued at around £650m to provide refuse and recycling collection, street cleansing services, and delivering waste processing and disposal, including the construction of a new waste transfer station. The Norfolk and Norwich University Hospital contract has also been extended for a further five years until 2016. The extension, under which we will continue to provide a full range of integrated non-clinical support services, is valued at £75m.

The Company also began a contract to provide facilities management services to the new Forth Valley Royal Hospital in Scotland, one of the most modern and well equipped hospitals in Europe. The contract is valued at £600m over 30 years.

Principal risks and uncertainties

The Company has significant receivable balances from long term contracts with third party customers. The directors do not consider that the Company is exposed to significant credit risk due to the nature and size of the contracts and there being no reliance on an individual customer.

The Company has no significant external borrowings and so the directors do not consider that the Company is exposed to interest risk or liquidity risk.

Serco Limited
Directors' Report for the Year Ended 31 December 2010

Financial risk management for the Serco Group is undertaken by Serco Group plc. The Group risk register is updated at least quarterly, reviewed six-monthly by the Risk Oversight Group and discussed at quarterly board meetings. Principal risks and uncertainties relating to the Company are as follows:

Risk - Significant change in Government policies

As a major proportion of Serco's customers are governments and governmental agencies, a substantial part of the business is dependent on government policies, budget priorities and regulatory or political constraints. As such, these businesses are susceptible to changes in government, government policy, budget allocations and the political environment, primarily in the UK. Any reduction in such government expenditure and funding could result in a suspension, cancellation, termination or non-renewal of contracts.

Impact

- Reduction in market opportunities
- Changes to terms of existing or new contracts
- Failure to meet growth or profit expectations

Mitigation

- Business strategy
- Diverse business across geographies and markets
- Business significantly focused on developed markets with strong and established legal systems providing protection to changes in contract terms

Risk - Failure to win a strategic or significant bid or rebid

Failure to win material bids or renew material contracts could restrict growth opportunities for the future or have an adverse impact on Serco's business, financial condition and results of operations.

Impact

- Failure to meet growth or profit expectations
- Significant financial loss or cost overrun,
- Damage to reputation resulting in loss of existing or new business,
- Impact on strategic objectives,

Mitigation

- Business Lifecycle Governance process embedded in SMS
- Governance structure managed through Investment Committee, Programme and Project Boards, Divisional and Contract Boards
- Business strategy and targets managed through internal boards
- Regular review and monitoring of risk register
- Gate review and formal sign off process

Risk - Any harm to the Company's reputation could adversely impact business

The Company is dependent on maintaining its reputation in each jurisdiction in which it operates in order to maintain and grow its business. It is exposed to the risk that litigation, misconduct, operational failures and negative publicity could harm its reputation.

Impact

Failure to meet growth or profit expectations

- Significant financial loss or cost overrun,
- Loss of contract revenue related to operations and service charges,
- Damage to reputation resulting in loss of existing or new business,
- Impact on strategic objectives,

Mitigation

- Robust bidding and contract review process including financial, technical and commercial reviews
- Governance structure managed through Investment Committee, Programme and Project Boards, Divisional and Contract Boards
- Business strategy and targets
- Regular review and monitoring of risk registers
- Gate review and formal sign off process
- Quality management systems

Serco Limited

Directors' Report for the Year Ended 31 December 2010

Risk - Failure of significant programmes, including operating within fixed costs

Serco has a number of complex programmes which it is contracted to deliver for the customer. These are often let on a fixed price basis irrespective of the actual costs incurred, and therefore if costs exceed the contract ceiling the Company may not be able to obtain full reimbursement. Further, some projects require delivery in accordance with specified milestones on agreed dates. Significant adverse financial consequences can be imposed where milestones are not met or a project is not delivered on time. The length and complexity of such projects mean that management estimates can be particularly difficult to make and could turn out to be inaccurate.

Impact

- Failure to meet growth or profit expectations
- Significant financial loss or cost overrun,
- Loss of contract revenue related to operations and service charges,
- Damage to reputation resulting in loss of existing or new business,
- Impact on strategic objectives,

Mitigation

- Robust bidding and contract review process including financial, technical and commercial reviews
- Governance structure managed through Investment Committee, Programme and Project Boards, Divisional and Contract Boards
- Business strategy and targets
- Regular review and monitoring of risk registers
- Gate review and formal sign off process

Risk - Major information security breach

Serco must comply with restrictions on the use of confidential and classified data and provide for secure transmission of such information. This is a heightened risk particularly with respect to government contracts due to the sensitive and confidential nature of government data. Despite controls to ensure the confidentiality of such information, Serco may breach restrictions or be subject to attack from computer programmes that attempt to penetrate its network security and misappropriate confidential information.

Impact

- Damage to reputation resulting in loss of existing or new business (disqualification from future tenders, contract termination, etc),
- Impact on strategic objectives,
- Costly to rectify and potential for dilution of shareholder returns,
- Criminal and civil action,
- Contract and business external accreditations withdrawn,
- Significant media attention and future scrutiny

Mitigation

- Information Systems policy, systems and embedded governance structure
- Think Privacy campaign to raise awareness and strengthen control processes
- User and data management including data encryption, information classification, data cleansing and password controls
- ISO27000 certification
- Internal and external audit

Serco Limited

Directors' Report for the Year Ended 31 December 2010

Risk- Major IT Failure or prolonged loss of critical IT systems

The IT Strategy is focussed on standardising common processes, establishing common business systems and enabling ways of working by providing and embedding tools that support what we do. Failings in the systems have the potential to seriously impact the management of the business.

Impact

- Damage to reputation resulting in loss of existing or new business,
- Impact on strategic objectives,
- Inability to meet contract requirements or perform core business processes,
- Costly to rectify and potential for dilution of shareholder returns,
- Significant media attention and future scrutiny

Mitigation

- Information policies and systems and governance structure
- Data recovery capability designed into systems and periodically tested
- Design out single points of failure
- Server and system performance monitoring and reporting
- Capacity management
- Data back up and business continuity plans in place

Risk - Major accident or incident

It is possible that a major catastrophic event, such as a major train derailment or air traffic accident, could occur at one of the projects in relation to which Serco has provided professional design, construction, engineering or support services. Such a catastrophic event could result in the personal injury or death of one or more employees of the Company, employees of other subcontractors working on the project or members of the public, significant, actionable environmental harm, and/or extensive damage to third party property.

Impact

- Deaths or serious injuries to employees or third parties
- Major environmental damage
- Severe financial impact (fine by regulators, suspension of operating licence, compensation, clean up etc)
- Loss of business (disqualification from future tenders, contract termination, etc),
- Contract and business external accreditations withdrawn,
- Significant media attention/future scrutiny,
- Criminal and civil action against company or individuals

Mitigation

- Robust management systems subject to external, regulatory and internal audit
- System certification and regulatory approval
- Formal oversight through Group Risk Management Committee, Health Safety and Environment Oversight Group, divisional and internal boards
- Crisis management and business continuity plans in place
- Insurance
- Strategy, objectives, targets and regular reporting
- Formal assurance structure operating within defined competencies
- Staff induction and training

Serco Limited

Directors' Report for the Year Ended 31 December 2010

Risk - Compliance with complex laws and regulations

Serco must comply with laws and regulations relating to the formation, administration and performance of government contracts that affect how it does business and may impose added costs. Further it is required to obtain environmental and safety permits from various government authorities which require periodic renewal or review of their conditions.

Impact

- Substantial monetary damages or criminal violations
- Damage to reputation resulting in loss of existing or new business
- Disbarment from tender lists
- Significant media attention and future scrutiny

Mitigation

- Policies and systems embedded in Serco Management System
- Code of Conduct
- Risk assessment
- Third Party Contracts
- System certification and regulatory approval
- Internal board and governance structure
- Staff induction and training

Risk - Failure to attract and retain senior management and other key employees

The success of the Company depends on the efforts, abilities, experience and expertise of the senior management teams and on recruiting, retaining, motivating, effectively communicating with and developing highly skilled and competent people at all levels of the organisation.

Impact

- Increased cost in recruitment activity and time taken to fill roles,
- Instability and loss of business continuity,
- Dilution of brand and values,
- Reduced employee engagement through loss of compelling leadership,
- Strengthen competitors (loss of leaders to them),
- Impact on business - risk of not achieving level of planned growth

Mitigation

- People policies and systems, strategy and targets supported by governance structure including remunerations committee
- Succession planning
- Leadership model
- Annual external (independent) remuneration review
- Job structure and grading system
- Talent database and leadership development programme
- Employment engagement strategy including annual staff survey

Serco Limited

Directors' Report for the Year Ended 31 December 2010

Risk - Failure to manage union/industrial relations

A significant number of Serco's employees are members of trade unions. These include operations where a failure to manage relationships may result in industrial action by Serco staff in high profile business operations i.e. where there will be significant reputational damage, client or media attention. Some sectors of the business are subject to union recognition agreements. The Company maintains a number of relationships with trade unions and staff through work councils and other bodies.

Impact

- Failure to deliver contractual requirements
- Instability and loss of business continuity,
- Dilution of brand and values,
- Reduced employee engagement
- Damage to reputation resulting in loss of existing or new business
- Significant media attention and future scrutiny

Mitigation

- Policies and systems embedded in Serco Management System
- Industrial Relations strategy
- Industrial Relations Working Group
- Stakeholder management of key relationships
- Annual external (independent) remuneration review
- Job structure and grading system
- Employment engagement strategy

Risk - Additional funding requirements for pension schemes

Serco operates defined benefit pension schemes for qualifying employees. The nature of a defined benefit scheme means that the funding levels of the schemes are subject to factors outside Serco's control which could create or impact a deficit in the scheme at future actuarial valuations. If the deficit in the scheme increases at future actuarial valuations, Serco may be required to make additional cash contributions to the schemes in the future, preventing the use of cash for other purposes, which could have a material impact on Serco's business, financial condition and results of operations over the long-term.

Impact

- Inability to meet profit expectations
- Increase in cash contributions to our pension schemes

Mitigation

- Actuarial assessment of scheme liabilities
- Appropriate Investment Management
- HR policy, systems and governance structure including Remunerations Committee and Board of Pension Trustees
- Annual external (independent) remuneration review
- Industrial Relations strategy
- Independent measurement of asset returns
- Internal audit

Serco Limited
Directors' Report for the Year Ended 31 December 2010

Directors of the company

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

G Leach

M Brown (resigned 31 August 2010)

N Brown

I Downie (resigned 1 April 2010)

G Hill (resigned 23 April 2010)

R McGuinness (resigned 1 April 2010)

T Riall

J Roberts (resigned 6 April 2010)

A White

D Gibson

A Crawshaw (appointed 23 April 2010)

Creditor payment policy

The Company requires its business units to negotiate and agree the terms and conditions for payment for the supply of capital and revenue items just as keenly as they negotiate prices and other commercial matters. Suppliers are made aware of the terms and the way in which disputes are to be settled. Payment is then made in accordance with those terms. The Company's average creditor payment terms in 2010 were 28 days (2009 35 days) based on the average daily amount invoiced by suppliers during the year.

Donations

During the year the Company made charitable donations of £200,000 to local and national charities. The Company did not make any political donations in the year.

Employment of disabled persons

Full and fair consideration is given to applications for employment made by disabled persons, having regard to their aptitude and ability. Appropriate training is arranged, including retraining of employees who have become disabled.

Employee involvement

Managers are tasked with developing employees' awareness of factors affecting the business and matters concerning them as employees and noting employees' views so that they can be taken into account when making decisions that may affect them or the business. Regular meetings are held with employee representatives where trade union or staff associations are recognised or where works councils are constituted.

Disclosure of information to the auditor

Each director has taken 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 auditor is aware of that information. The directors confirm that there is no relevant information that they know of and of which they know the auditor is unaware. This confirmation is given and should be interpreted in accordance with the provisions of s418 of the Companies Act 2006.

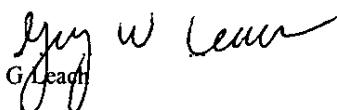
Serco Limited

Directors' Report for the Year Ended 31 December 2010

Auditor

Elective resolutions to dispense with holding annual general meetings, the laying of accounts before the Company in general meeting and the reappointment of auditors annually are currently in force. Deloitte LLP has expressed its willingness to continue in office and will therefore be deemed to have been reappointed.

Approved by the Board on 20 April 2011 and signed on its behalf by


G Leach

Serco Limited
Directors' Responsibilities Statement

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 the directors have elected to prepare the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law). 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 apply them consistently,
- make judgements and accounting estimates that are reasonable and prudent,
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements, and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

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

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

**Independent Auditor's Report to the Members of
Serco Limited**

We have audited the financial statements of Serco Limited for the year ended 31 December 2010, comprising the profit and loss account, the statement of total recognised gains and losses, the balance sheet and the related notes 1 to 31, set out on pages 14 to 43. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom 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 auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

As explained more fully in the Directors' Responsibilities Statement, 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

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 the 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 December 2010 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.

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.



Richard Knights (Senior Statutory Auditor)
For and on behalf of Deloitte LLP,
Chartered Accountants and Statutory Auditor
London, United Kingdom

Serco Limited
Profit and Loss Account for the Year Ended 31 December 2010

	Note	2010 £m	2009 £m
Turnover	2	1,819.5	1,759.8
Cost of sales		<u>(1,594.9)</u>	<u>(1,573.9)</u>
Gross profit		<u>224.6</u>	<u>185.9</u>
Other administrative expenses		(94.4)	(100.3)
Amortisation of intangible fixed assets	3	<u>(42.8)</u>	<u>(37.7)</u>
Administrative expenses		<u>(137.2)</u>	<u>(138.0)</u>
Operating profit	3	87.4	47.9
Profit on disposal of investments	4	22.6	-
Interest receivable and similar income	7	1.3	1.1
Interest payable and similar charges	8	<u>(10.9)</u>	<u>(10.4)</u>
Profit on ordinary activities before taxation		100.4	38.6
Tax on profit on ordinary activities	9	<u>(22.0)</u>	<u>(11.3)</u>
Profit for the financial year		<u><u>78.4</u></u>	<u><u>27.3</u></u>

Turnover and operating profit derive wholly from continuing operations

Serco Limited


Statement of Total Recognised Gains and Losses for the Year Ended 31 December 2010

	Note	2010 £m	2009 £m
Profit for the financial year		78.4	27.3
Credit in relation to share-based payment reserve	25	5.1	4.7
Amortisation of cash flow hedging reserve	25	0.3	0.2
Net fair value gain on cash flow hedges during the year	25	0.1	0.2
Tax charge on hedging and translation reserve	25	(0.1)	(0.1)
Net actuarial gain/(loss) on defined benefit pension schemes	25	12.4	(146.8)
Actuarial gains on reimbursable rights	25	1.7	13.4
Tax (charge)/credit on actuarial gain/(loss) on defined benefit pension schemes	25	(4.3)	37.5
Total recognised gains and losses relating to the year		<u>93.6</u>	<u>(63.6)</u>

Serco Limited
(Registration number: 00242246)
Balance Sheet at 31 December 2010

	Note	2010 £m	2009 £m
Fixed assets			
Goodwill	11	324 2	344 5
Other intangible assets	11	60 3	63 3
Tangible fixed assets	12	55 7	54 0
Investments	13	53 7	53 7
Derivative financial instruments	29	0 4	0 3
		<u>494 3</u>	<u>515 8</u>
Current assets			
Stocks	14	31 5	29 4
Debtors amounts falling due within one year	15	356 4	545 2
Debtors amounts falling due after more than one year	15	62 1	69 2
Derivative financial instruments	29	0 1	0 1
Cash at bank and in hand		<u>134 2</u>	<u>121 0</u>
		584 3	764 9
Creditors' amounts falling due within one year			
Creditors amounts falling due within one year	16	(465 0)	(523 0)
Derivative financial instruments	29	<u>(0 1)</u>	<u>(0 1)</u>
Net current assets		<u>119 2</u>	<u>241 8</u>
Total assets less current liabilities		613 5	757 6
Creditors: amounts falling due after more than one year			
Creditors amounts falling due after more than one year	17	(61 6)	(234 5)
Derivative financial instruments	29	<u>(0 4)</u>	<u>(0 1)</u>
Provisions for liabilities and charges	21	<u>(4 4)</u>	<u>(6 9)</u>
Net assets excluding pension liability		547 1	516 1
Defined benefit pension liability	27	<u>(23 6)</u>	<u>(56 2)</u>
Net assets		<u>523 5</u>	<u>459 9</u>
Capital and reserves			
Called up share capital	23	0 2	0 2
Share premium account	24	457 3	457 3
Hedging and translation reserve	25	0 2	(0 1)
Share based payment reserve	25	27 6	22 5
Profit and loss account	25	172 1	123 7
Retirement benefit obligation reserve	25	<u>(133 9)</u>	<u>(143 7)</u>
Shareholders' funds		<u>523 5</u>	<u>459 9</u>

Approved by the Board on 20 April 2011 and signed on its behalf by


G. Leach

Serco Limited
Notes to the Financial Statements for the Year Ended 31 December 2010

1 Accounting policies

The principal accounting policies are set out below and have been applied consistently throughout the current and preceding financial year

These financial statements have been prepared in accordance with UK GAAP and applicable UK law and accounting standards

The Company's business activities, together with the factors likely to affect its future development, performance and position are set out in the Directors' Report on pages 2 to 5

As described in note 2 the segmental information has been restated to reflect the reorganisation effective from 1 January 2010

Basis of preparation

The financial statements have been prepared under the historical cost convention

Exemption from preparing a cash flow statement

The company is exempt from preparing a cash flow statement as 90% or more of the voting rights are held within the group

Exemption from preparing group accounts

These financial statements present information about the Company as an individual undertaking and not about its group. Consolidated financial statements have not been prepared as the Company is a wholly owned subsidiary of a company incorporated in Great Britain and registered in England and Wales and so is therefore exempt, by virtue of s400 of the Companies Act 2006, from the requirement to prepare and deliver group accounts. The only group Company for which consolidated financial statements are prepared is Serco Group plc

Related parties

The Company is exempt under the terms of FRS 8 "Related Party Transactions" from disclosing related party transactions with entities that are 100% owned by Serco Group plc group

Going concern

The financial statements have been prepared on a going concern basis

The directors have acknowledged the latest guidance on going concern and financial reporting published by the Financial Reporting Council in October 2009. Whilst the current economic environment is uncertain, the broad base of the Company's contract portfolio and with 90% of the Company's customers being government bodies, the Company is well placed to manage its business risks successfully, including those arising from the failure of customers to meet contractual obligations.

The Company's revenues are largely derived from long-term contracts with governments which historically have been largely unaffected by changes in the general economy. The Company also has a large future order book and high visibility of future revenue streams. Based on detailed projections management believe that the Company has adequate resources to continue in operational existence for the foreseeable future, and as a result these accounts have been drawn up on the going concern basis.

Turnover

Turnover is measured at the fair value of the consideration received or receivable and represents amounts receivable for goods and services provided in the normal course of business, net of discounts, VAT and other sales-related taxes. Sales of goods are recognised when goods are delivered and title has passed. To the extent that the Company acts as an agent under the definitions of FRS 5 "Reporting the Substance of Transactions", Application Note G, amounts invoiced in respect of items procured on behalf of customers are not recognised within turnover.

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2010

..... continued

Goodwill

Goodwill arising on the acquisition of businesses is capitalised on the balance sheet in accordance with FRS 10 "Goodwill and Intangible Assets". Goodwill represents the excess of consideration paid over the fair value of assets acquired. Amortisation of goodwill is provided on a straight line basis over the useful economic life of the asset or a period of 20 years, whichever is shorter. Goodwill is reviewed for impairment at least annually. Any impairment is recognised immediately in the profit and loss account and is not subsequently reversed.

Intangible assets

Research expenditure is written off as incurred.

Development expenditure relating to software is capitalised as an intangible asset only if all of the following conditions are met:

- an asset is created that can be identified,
- it is probable that the asset created will generate future economic benefits, and
- the development cost of the asset can be measured reliably.

Development expenditure is amortised over the period over which the Company is expected to benefit. This period is between three and five years, or the length of the contract if longer. Provision is also made for any impairment. All other development expenditure is written off as incurred.

Pension related intangibles represent assets arising in relation to the Company's right to manage and operate contracts where there is a defined benefit pension scheme and it is not virtually certain that contributions will be recovered from the customer but where the Company's obligation to contribute to the scheme ends when the contract ends. The intangible assets represent the Company's share of scheme net liabilities on the date that the contracts commence and are amortised on a straight line basis over the contract life.

Tangible fixed assets

Tangible fixed assets are stated at cost or valuation, net of depreciation and any provision for impairment.

The gain or loss arising on the disposal or retirement of an asset is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in the profit and loss account.

Depreciation

Depreciation is provided on tangible fixed assets so as to write off the cost or valuation, less any estimated residual value, over their expected useful economic life as follows:

Asset class	Depreciation method and rate
Freehold buildings	2.5%
Short leasehold building improvements	The higher of 10% or rate produced by lease term
Machinery	15% - 20%
Motor vehicles	18% - 50%
Furniture	10%
Office equipment	20% - 33%
Leased equipment	The higher of the rate produced by either the lease term or useful life

Fixed asset investments

Fixed asset investments are stated at historical cost less provision for impairment.

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2010

... continued

Stocks, work in progress and long-term contracts

Stocks are stated at the lower of cost and net realisable value and comprise service spares and long-term project-based contract balances. Cost comprises direct materials and, where applicable, direct labour costs that have been incurred in bringing the stocks to their present location and condition.

Amounts recoverable on long-term contracts, which are included in debtors, represent costs incurred on specific contracts, net of amounts transferred to cost of sales in respect of work recorded as turnover by reference to the stage of completion of the work carried out to date and provision for anticipated future losses on contracts. No profit is recognised until the contract has advanced to a stage where the total profit can be assessed with reasonable certainty. Advance payments are included in creditors to the extent that they exceed the related work in progress.

Pre-contract costs

All bid costs are expensed through the profit and loss account up to the point where contract award (or full recovery of costs) is virtually certain, in accordance with Urgent Issues Task Force Abstract 34 "Pre-contract Costs". Bid costs incurred after this point are then capitalised within debtors. On contract award, these bid costs are amortised through the profit and loss account on a straight line basis over the contract period, unless separately reimbursed.

Provisions

Provisions are recognised when the Company has a present obligation as a result of a past event and it is probable that the Company will be required to settle that obligation. Provisions are measured at the directors' best estimate of the expenditure required to settle the obligation at the balance sheet date.

Current tax

Current tax, including UK corporation tax and foreign tax, is provided at amounts expected to be paid or recovered using the tax rates and laws that have been enacted or substantively enacted by the balance sheet date.

Deferred tax

Deferred tax is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date where transactions or events that result in an obligation to pay more tax in the future or a right to pay less tax in the future have occurred at the balance sheet date. Timing differences are differences between the Company's taxable profits and its results as stated in the financial statements.

A net deferred tax asset is regarded as recoverable and therefore recognised only to the extent that, on the basis of all available evidence, it can be regarded as more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted.

Basis of translation of foreign currencies

Transactions in currencies other than pounds sterling are recorded at the rates of exchange on the dates of the transactions. At each balance sheet date monetary assets and liabilities that are denominated in foreign currencies are retranslated at the rates prevailing on the balance sheet date. Gains and losses arising on retranslation are included in the profit and loss account for the period.

Hire purchase and leasing

Rentals payable under operating leases are charged on a straight line basis over the term of the relevant lease, even if the payments are not made on such a basis.

Assets held under finance leases are recognised as assets of the Company at fair value or, if lower, at the present value of the minimum lease payments determined at the inception of the lease. The corresponding liability to the lessor is included in the balance sheet as a finance lease obligation. Lease payments are apportioned between finance charges and reduction of the lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly against income unless they are directly attributable to a qualifying asset, in which case they are capitalised in accordance with the Company's general policy on borrowing costs.

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2010

... continued

Share-based payment

The Company has applied the requirements of FRS 20 "Share-based Payment" In accordance with the transitional provisions, FRS 20 has been applied to all grants of equity instruments after 7 November 2002 that were not fully vested as of 1 January 2007

The ultimate parent, Serco Group plc, issues equity settled share-based payments to certain employees and operates an HM Revenue & Customs approved Save As You Earn share option scheme open to eligible employees which allows the purchase of shares at a discount These are measured at fair value at the date of grant The fair value is expensed on a straight line basis over the vesting period, based on the Group's estimate of shares that will eventually vest

Fair value is measured by use of the Binomial or Monte Carlo simulation models, depending on the type of scheme Further details can be found in note 33 of the Serco Group plc financial statements The expected life used in the models has been adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions, and behavioural considerations When relevant, the value of the option has been adjusted to take account of market conditions applicable to the option

Financial instruments

Derivatives are accounted for initially and measured at fair value on the date that a derivative contract is entered into and subsequently measured at fair value The gain or loss on remeasurement is taken to the profit and loss account, except where the derivative is designated as a cash flow hedging instrument The accounting treatment of derivatives classified as "hedges" depends on their designation, which occurs on the date that a derivative contract is committed to The Company designates derivatives as

- a hedge of the fair value of an asset or liability ("fair value hedge")
- a hedge of the income/cost of a highly probable forecast transaction or commitment ("cash flow hedge")

Gains and losses on fair value hedges are recorded in the profit and loss account with the gain or loss on the hedged item attributable to the hedged risk

Gains or losses on cash flow hedges that are regarded as highly effective are recognised in equity Where the forecast transaction results in a financial asset or liability, only gains or losses previously recognised in equity are reclassified to profit or loss in the same period as the asset or liability affects profit or loss Where the forecast transaction or commitment results in a non-financial asset or liability, any gains or losses previously deferred in equity are included in the cost of the related asset or liability if the forecast transaction or commitment results in future income or expenditure Gains and losses deferred in equity are transferred to the profit and loss account in the same period as the underlying income or expenditure The ineffective portion of the gain or loss on the hedging instrument is recognised in the profit and loss account

For the ineffective portion of hedges or transactions that are not designated for hedge accounting under FRS 25 "Financial Instruments Disclosure and Presentation", any change in assets or liabilities is recognised immediately in the profit and loss account Where a hedge no longer meets the effectiveness criteria, any gains or losses deferred in equity are only transferred to the profit and loss account when the committed or forecast transaction is recognised in the profit and loss account However, where cash flow hedge accounting has been applied for a forecast or committed transaction that is no longer expected to occur, then the cumulative gain or loss that has been recorded in equity at that time remains in equity and is recognised when the forecast transaction is ultimately recognised in the profit and loss account

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2010

..... continued

Retirement benefit costs

Payments to defined contribution pension schemes are charged as an expense as they fall due

For defined benefit pension schemes, the cost of providing benefits is determined using the projected unit credit method, with actuarial valuations being carried out at each balance sheet date. Actuarial gains and losses are recognised in full in the period in which they occur. They are recognised outside the profit and loss account and are presented in the statement of total recognised gains and losses.

The current service cost represents the increase in the present value of the plan liabilities expected to arise from employee service in the current period.

Past service cost is recognised immediately to the extent that the benefits are already vested, and is amortised on a straight line basis over the average period until the benefit becomes vested. Gains and losses on curtailments or settlements are recognised in the period in which the curtailment or settlement occurs.

The retirement benefit obligation recognised on the balance sheet represents the present value of the defined benefit obligation, as adjusted for unrecognised past service costs, 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.

Defined benefit obligations arising from contractual obligations

Where the Company takes on a contract and assumes the obligation to contribute variable amounts to the defined benefit pension scheme throughout the period of the contract and it is not virtually certain that the contributions will be recovered from the customer, the Company's share of the defined benefit obligation less its share of the pension scheme assets that it will fund over the period of the contract is recognised as a liability at the start of the contract, with a corresponding amount being recognised as an intangible asset. The intangible asset, which reflects the Company's right to manage and operate the contract, is amortised over the contract period. The Company's share of the scheme assets and liabilities is calculated by reducing the scheme assets and liabilities by a franchise adjustment. The franchise adjustment represents the amount of scheme deficit that will be funded outside contract period. Subsequent actuarial gains and losses in relation to the Company's share of pension obligations are recognised outside the profit and loss account and are presented in the statement of total recognised gains and losses.

Multi-employer pension schemes

Multi-employer pension schemes are classified as either defined contribution pension schemes or defined benefit pension schemes, depending on the terms of the scheme. The Company accounts for these schemes as if they were defined contribution schemes.

Pension costs, defined contribution schemes

Contributions for the year in respect of defined contribution schemes are charged to the profit and loss account as they fall due. Differences between charges accruing during the year and cash payments are included as either accruals or prepayments in the balance sheet.

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2010

..... *continued*

2 Turnover

The Company manages its business on an operating segment basis and these segments are the basis on which the Company reports its segment information

Details of the different products and services provided by each operating segment are included in the Directors' Report. From 1 January 2010, the Company has reapportioned its business into three new divisions. The Company's reportable operating segments are

Civil Government - UK, Europe and Middle East civil government and transport,

Defence, Science and Nuclear - UK and Europe defence and science-based businesses, and

Local Government and Commercial - UK and Europe IT and BPO, integrated services, education and commercial businesses

Turnover by classes of business

	2010 £m	2009 £m Restated
Civil Government	719.8	678.2
Defence, Science and Nuclear	463.7	486.2
Local Government and Commercial	636.0	595.4
Total	1,819.5	1,759.8

An analysis of turnover by geographical location is given below

	2010 £m	2009 £m
United Kingdom	1,736.9	1,694.0
Overseas	82.6	65.8
Total	1,819.5	1,759.8

Turnover is shown by geographical origin. Turnover analysed by geographical destination is not materially different.

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2010

..... continued

3 Operating profit

Operating profit is stated after charging/(crediting)

	2010 £m	2009 £m
Amortisation of goodwill	22.1	22.1
Amortisation of other intangible assets	20.7	15.6
Net foreign exchange (gains)/losses	(0.1)	2.2
Research and development costs	9.8	6.0
Operating leases - land and buildings	24.4	15.9
Operating leases - plant and machinery	14.6	11.0
Depreciation of tangible fixed assets - owned	12.6	13.2
Depreciation of tangible fixed assets - held under finance leases	4.5	4.2
Fees paid to the Company's auditor for the audit of the Company's annual accounts	0.1	0.1
Other non-audit fees - tax services	0.1	0.1
Other non audit fees - other services	<u>0.1</u>	<u>0.1</u>

4 Profit on disposal of investments

	2010 £m	2009 £m
Profit on disposal of investments	<u>22.6</u>	<u>-</u>

During the year, as part of its ongoing exercise to rationalise its legal entity structure and liquidate entities which are no longer required, the Company liquidated its subsidiary, ITNET Limited and its two subsidiary companies, French Thornton Partnership and Serco Solutions Limited. The total gain on disposal was £22.6m.

5 Particulars of employees

The average number of employees employed by the company (including directors) during the year was 24,017 (2009 25,083).

The aggregate payroll costs were as follows

	2010 £m	2009 £m
Wages and salaries	691.8	686.3
Social security costs	64.8	63.0
Staff pensions	47.4	43.2
Share-based payment	<u>5.1</u>	<u>4.7</u>
	<u>809.1</u>	<u>797.2</u>

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2010

.. continued

6 Directors' remuneration

The directors' remuneration for the year was as follows

	2010 £m	2009 £m
Aggregate emoluments	<u>2.7</u>	<u>3.1</u>

During the year, nine directors (2009: three) received or were entitled to receive shares under long term incentive schemes. Ten directors (2009: ten) exercised shares options. Five directors (2009: six) were accruing benefits under defined benefit pension schemes. Two (2009: two) directors were members of a defined contribution scheme.

In respect of the highest paid director

	2010 £m	2009 £m
Remuneration	0.4	0.4
Company contributions to money purchase pension schemes	0.1	-
Defined benefit accrued pension entitlement at the end of the period	<u>-</u>	<u>0.0</u>

During the year the highest paid director exercised share options and also received or was entitled to receive shares under a long term incentive scheme.

7 Interest receivable and similar income

	2010 £m	2009 £m
Income from investments	0.2	-
Bank interest receivable	0.3	0.2
Interest receivable from group companies	0.6	0.7
Other interest receivable	<u>0.2</u>	<u>0.2</u>
	<u>1.3</u>	<u>1.1</u>

8 Interest payable and similar charges

	2010 £m	2009 £m
Bank loans and overdrafts	1.0	1.2
Other interest payable	1.5	0.2
Interest payable to group companies	6.1	4.5
Net interest payable on retirement benefit obligations	1.1	3.4
Amounts payable under finance leases	<u>1.2</u>	<u>1.1</u>
	<u>10.9</u>	<u>10.4</u>

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2010

..... *continued*

9 Taxation

Tax on profit on ordinary activities

	2010 £m	2009 £m
Current tax		
United Kingdom corporation tax charge at 28%	21.9	8.3
Group relief	0.8	0.2
Adjustments in respect of prior years	1.0	(3.1)
Double taxation relief	(0.1)	-
UK Corporation tax	<u>23.6</u>	<u>5.4</u>
Foreign tax	<u>0.1</u>	<u>-</u>
Total current tax	<u>23.7</u>	<u>5.4</u>
Deferred tax		
Origination and reversal of timing differences	1.6	4.6
Adjustment in respect of prior years	(3.3)	1.3
Total deferred tax	<u>(1.7)</u>	<u>5.9</u>
Total tax charge on profit on ordinary activities	<u>22.0</u>	<u>11.3</u>

Factors affecting current tax charge for the year

The current tax recognised on the profit on ordinary activities for the year is lower than (2009 - lower than) the standard rate of corporation tax in the United Kingdom of 28% (2009 - 28%)

The reason for this are set out below

	2010 £m	2009 £m
Profit on ordinary activities before taxation	<u>100.4</u>	<u>38.6</u>
Corporation tax charge (credit) at standard rate	28.1	10.8
Group relief with no consideration	(2.7)	(3.7)
Expenses not deductible for tax purposes	5.5	6.5
Capital allowances in excess of depreciation	(1.5)	(1.3)
Other short term timing differences	0.5	(3.3)
Tax incentives and tax exempt income	(7.2)	(0.5)
Adjustment in respect of prior periods	1.0	(3.1)
Current tax charge for the year	<u>23.7</u>	<u>5.4</u>

10 Dividends

	2010 £m	2009 £m
Dividends paid		
Equity dividend of £140.35 (2009 - £187.14) per ordinary share	<u>30.0</u>	<u>40.0</u>

Serco Limited
Notes to the Financial Statements for the Year Ended 31 December 2010

... .. *continued*

11 Goodwill and other intangible assets

	Goodwill £m	Licences, software and development expenditure £m	Pension related £m	Total £m
Cost				
At 1 January 2010	442.3	103.5	4.4	550.2
Additions	1.8	18.6	-	20.4
Disposals	-	(8.9)	-	(8.9)
Transfers to group companies	-	(0.7)	-	(0.7)
At 31 December 2010	<u>444.1</u>	<u>112.5</u>	<u>4.4</u>	<u>561.0</u>
Accumulated amortisation				
At 1 January 2010	97.8	42.4	2.2	142.4
Charge for the year	22.1	20.0	0.7	42.8
Eliminated on disposals	-	(8.7)	-	(8.7)
At 31 December 2010	<u>119.9</u>	<u>53.7</u>	<u>2.9</u>	<u>176.5</u>
Net book value				
At 31 December 2010	<u>324.2</u>	<u>58.8</u>	<u>1.5</u>	<u>384.5</u>
At 31 December 2009	<u>344.5</u>	<u>61.1</u>	<u>2.2</u>	<u>407.8</u>

On 30 November 2010, Serco Limited purchased the trade and assets of RB Solutions Limited, a fellow group company, for a consideration of £2.0m. The fair value of net assets acquired was £0.2m, and the resultant goodwill amounted to £1.8m.

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2010

.. continued

12 Tangible fixed assets

	Freehold land and buildings £m	Short leasehold building improvement £m	Machinery, motor vehicles, furniture and equipment £m	Total £
Cost				
At 1 January 2010	2 4	23 3	118 1	143 8
Additions	-	0 4	19 6	20 0
Foreign exchange	-	-	0 1	0 1
Disposals	-	-	(10 0)	(10 0)
At 31 December 2010	2 4	23 7	127 8	153 9
Accumulated depreciation				
At 1 January 2010	1 1	11 9	76 8	89 8
Charge for the year	0 1	2 7	14 3	17 1
Foreign exchange	-	-	0 1	0 1
Eliminated on disposals	-	-	(8 8)	(8 8)
At 31 December 2010	1 2	14 6	82 4	98 2
Net book value				
At 31 December 2010	1 2	9 1	45 4	55 7
At 31 December 2009	1 3	11 4	41 3	54 0

Finance lease assets

Included within the net book value of tangible fixed assets is £16 3m (2009 £18 3m) in respect of assets held under finance lease agreements. Depreciation for the year on these assets was £4 5m (2009 £4 2m)

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2010

.. .. continued

13 Investments held as fixed assets

Shares in group undertakings and participating interests

	Subsidiary undertakings £m	Joints ventures £m	Total £
Cost			
At 1 January 2010	48.2	5.5	53.7
At 31 December 2010	48.2	5.5	53.7

Details of undertakings

Most of the contracts are held in divisions within the Serco Limited company. However, the companies listed below are, in the opinion of the directors, the principal subsidiary and joint venture undertakings of Serco Limited. The percentage of equity capital held directly by Serco Limited is shown. The companies are incorporated and principally operate in the United Kingdom.

Full details of related undertakings will be attached to the Company's Annual Return to be filed with the Registrar of Companies.

Undertaking	Holding	Proportion of voting rights and shares held	Principal activity
Subsidiary undertakings			
Serco Geografix Limited	ordinary shares	100%	Manufacture and leasing of electronic tagging equipment
Joint ventures			
GSTS Pathology LLP		50%	Pathology services
Service Glasgow LLP		50%	Provision of facility management services

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2010

..... *continued*

14 Stocks

	2010 £m	2009 £m
Service spares	14 1	11 0
Parts awaiting installation	13 2	11 2
Long-term project-based contract balances	4 2	7 2
	<u>31 5</u>	<u>29 4</u>

There is no material difference between the value of stock and its replacement cost

15 Debtors

a) Amounts falling due within one year

	2010 £m	2009 £m
Trade debtors	208 4	222 6
Amounts recoverable on long term contracts	13 6	3 2
Amounts owed by group companies	56 8	238 9
Amounts owed by joint ventures	2 0	1 5
Corporation tax recoverable	0 1	3 4
Other debtors	25 9	26 4
Prepayments and accrued income	49 6	49 2
	<u>356 4</u>	<u>545 2</u>

Amounts owed by group companies are due within 30 days of the balance sheet date and do not bear interest

b) Amounts falling due after more than one year

	2010 £m	2009 £m
Amounts recoverable on contracts	30 7	47 8
Owed by group companies	0 1	-
Amounts owed by joint ventures	2 5	2 5
Deferred tax asset	16 7	15 1
Other debtors	1 4	3 3
Prepayments and accrued income	10 7	0 5
	<u>62 1</u>	<u>69 2</u>

Amounts owed by group companies have no fixed repayment date and bear interest based on LIBOR minus 0.2%

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2010

..... *continued*

Deferred tax

The movement in the deferred tax asset in the year is as follows

	2010 £m	2009 £m
At 1 January	15.1	18.5
Transferred in on transfer of trade	-	(0.6)
Deferred tax credited/(charged) to the profit and loss account	1.7	(2.7)
Items taken directly to equity	(0.1)	(0.1)
At 31 December	<u>16.7</u>	<u>15.1</u>

Analysis of deferred tax

	2010 £m	2009 £m
Difference between accumulated depreciation and amortisation and capital allowances	2.8	5.0
Other timing differences	<u>13.9</u>	<u>10.1</u>
	<u>16.7</u>	<u>15.1</u>

There are no unprovided deferred tax balances

16 Creditors: Amounts falling due within one year

	2010 £m	2009 £m
Other loans	15.5	24.1
Obligations under finance lease and hire purchase contracts	5.3	5.5
Trade creditors	72.9	91.0
Amounts owed to group companies	19.2	52.6
Amounts owed to joint ventures	-	0.2
Corporation tax	0.8	4.2
Other taxes and social security	48.8	52.3
Other creditors	51.0	33.6
Accruals and deferred income	<u>251.5</u>	<u>259.5</u>
	<u>465.0</u>	<u>523.0</u>

Amounts owed to group companies are due within 30 days of the balance sheet date and do not bear interest

Serco Limited
Notes to the Financial Statements for the Year Ended 31 December 2010

..... continued

17 Creditors: Amounts falling due after more than one year

	2010 £m	2009 £m
Obligations under finance lease and hire purchase contracts	9 0	9 8
Amounts owed to group companies	37 2	214 1
Other creditors	15 4	10 6
	<u>61 6</u>	<u>234 5</u>

Amounts due to group companies have no fixed repayment date and bear interest based on LIBOR plus 2%

Analysis of loan repayments:

	2010 £m	2009 £m
Within one year	<u>15 5</u>	<u>24 1</u>

Obligations under finance leases and HP contracts

Amounts repayable:

	2010 £m	2009 £m
On demand or within one year	5 3	5 5
Between two and five years	9 0	9 8
	<u>14 3</u>	<u>15 3</u>

Finance leases are secured by retention of title to the relevant assets

21 Provisions

	Other provisions £m	Total £m
At 1 January 2010	6 9	6 9
Utilised during the year	<u>(2 5)</u>	<u>(2 5)</u>
At 31 December 2010	<u>4 4</u>	<u>4 4</u>

Provisions include amounts relating to employee awards, property and contracts

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2010

.... continued

22 Contingent liabilities

The Company, together with its ultimate parent and certain other subsidiaries, is included within interest pooling arrangements involving cross guarantee structures. The maximum overdraft permitted by these arrangements is £12.0m (2009: £12.0m). The overdraft was undrawn on 31 December 2010.

The Company is aware of claims and potential claims which involve or may involve legal proceedings against the Company. The directors are of the opinion, having regard to legal advice received and the Company's insurance arrangements, that it is unlikely that these matters will, in aggregate, have a material effect on the Company's financial position.

23 Share capital

Allotted, called up and fully paid shares

	2010 £m	2009 £m
213,744 (2009: 213,744) ordinary shares of £1 each	<u>0.2</u>	<u>0.2</u>

24 Share premium account

	2010 £m	2009 £m
At 1 January and 31 December	<u>457.3</u>	<u>457.3</u>

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2010

..... *continued*

25 Reserves

	Hedging and translation reserve £m	Share-based payment reserve £m	Retirement benefit obligation reserve £m	Profit and loss account £m	Total £m
At 1 January 2010	(0 1)	22 5	(143 7)	123 7	2 4
Profit for the year	-	-	-	78 4	78 4
Equity dividend paid	-	-	-	(30 0)	(30 0)
Credit in relation to share-based payment	-	5 1	-	-	5 1
Amortisation of cash flow hedging reserve	0 3	-	-	-	0 3
Net fair value gain on cash flow hedges during the year	0 1	-	-	-	0 1
Tax charge on hedging and translation reserve	(0 1)	-	-	-	(0 1)
Net actuarial loss on defined benefit pension schemes	-	-	12 4	-	12 4
Actuarial gains on reimbursable rights	-	-	1 7	-	1 7
Tax credit on actuarial losses on defined benefit pension schemes	-	-	(4 3)	-	(4 3)
At 31 December 2010	<u>0 2</u>	<u>27 6</u>	<u>(133 9)</u>	<u>172 1</u>	<u>66 0</u>

Full details of the Group's share schemes, in which the Company participates, may be found in note 33 to the Serco Group plc consolidated financial statements

Serco Limited
Notes to the Financial Statements for the Year Ended 31 December 2010

.. *continued*

26 Reconciliation of movement in shareholders' funds

	2010 £m	2009 £m
Profit for the financial year attributable to the members of the Company	78.4	27.3
Equity dividends paid	(30.0)	(40.0)
Credit to share-based payment reserve	5.1	4.7
Amortisation of cash flow hedging reserve	0.3	0.2
Net fair value gain on cash flow hedges during the year	0.1	0.2
Tax charge on hedging and translation reserve	(0.1)	(0.1)
Net actuarial loss on post employment schemes net of tax	9.8	(95.9)
Net addition/(reduction) to shareholders' funds	63.6	(103.6)
Shareholders' funds at 1 January	459.9	563.5
Shareholders' funds at 31 December	523.5	459.9

27 Pension schemes

Defined contribution schemes

Pre-funded defined benefit schemes treated as defined contribution

The Company paid employer contributions of £32.3m (2009 £25.4m) into UK defined contribution schemes and foreign state pension schemes

Defined benefit schemes

The company operates defined benefit schemes for qualifying employees in the UK

The assets of the funded plans are held independently of the Company's assets in separate trustee administered funds. The Company's major plans are valued by independent actuaries annually using the projected unit credit method. This reflects service rendered by employees to the dates of valuation and incorporated actuarial assumptions primarily regarding discount rates used in determining the present value of benefits, projected rates of salary growth, and long term expected rates of return for plan assets. Discount rates are based on the market yields of high quality corporate bonds in the country concerned. Long term expected rates of return for plan assets are based on published brokers' forecasts for each category of scheme assets. Pension assets and liabilities in different defined benefit schemes are not offset unless the Company has a legally enforceable right to use the surplus in one plan to settle obligations in the other plan and intends to exercise this right.

The amounts recognised in the consolidated balance sheet are grouped together into two categories - contract specific and non-contract specific.

The normal contributions expected to be paid during the financial year ended 31 December 2011 are £29.0m (2010 £29.0m).

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2010

... .. continued

Principal actuarial assumptions

The principal actuarial assumptions at the balance sheet date are as follows

	2010 %	2009 %
Discount rate	5.4	5.8
Future salary increases	3.5	3.7
Future pension increases (RPI basis)	3.1	3.3
Future pension increases (CPI basis)	2.6	-
Inflation (RPI basis)	3.1	3.3
Inflation (CPI basis)	2.6	-
Expected return on scheme assets - equities	8.3	8.6
Expected return on scheme assets - bonds (except LDI)	5.4	5.8
Expected return on scheme assets - LDI	4.9	5.2
Expected return on scheme assets - gilts	4.2	4.5
Expected return on scheme assets - property	5.5	5.8
Expected return on scheme assets - cash and other	0.5	0.5
Expected return on scheme assets - annuity policies	5.4	5.8

Post retirement mortality assumptions

	2010 Years	2009 Years
Current pensioners at retirement age - male	20.8	20.3
Current pensioners at retirement age - female	23.3	23.2
Future pensioners at retirement age - male	22.4	21.6
Future pensioners at retirement age - female	24.5	24.4

The replacement of the retail prices index with the consumer prices index for retirement benefits

The UK government announced in its June 2010 budget that when they publish the statutory increase figure in the future they will use the CPI measure of inflation rather than the RPI. This was confirmed on 8 December 2010.

Certain of the Group's pension schemes reflect the lower liability where the benefits are explicitly based on statutory increases in the Rules in 31 December 2010 pension liability figures. If this change had not occurred, the liability of the pension schemes on the Company balance sheet would show a net liability for the pension schemes before deferred tax of £61.7m. There is no impact on the operating profit of the current year due to applying the change.

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2010

... continued

Contract specific

These are pre-funded defined benefit pension schemes. The Company has obligations to contribute variable amounts to the pension schemes over the terms of the related contracts. At rebid any deficit or surplus would transfer to the next contractor. The Company has recognised as a liability the defined benefit obligation less the fair value of scheme assets that it will fund over the period of the contracts with a corresponding amount recognised as an intangible asset at the start of the contract. Subsequent actuarial gains and losses in relation to the Company's share of the pension obligation are recognised in the statement of total recognised gains and losses. The intangible assets are amortised over the term of the contracts.

Reconciliation of scheme assets and liabilities to assets and liabilities recognised

The amounts recognised in the balance sheet are as follows

	2010 £m	2009 £m
Fair value of scheme assets	72.5	63.2
Present value of scheme liabilities	(92.9)	(81.6)
	(20.4)	(18.4)
Franchise adjustment	15.4	11.6
Deficit in the scheme	(5.0)	(6.8)
Related deferred tax asset	1.3	1.9
Net liability	(3.7)	(4.9)

	2010 £m	2009 £m
Related intangible assets (note 11)	1.5	2.2

Scheme assets

Changes in the fair value of scheme assets are as follows

	2010 £m	2009 £m
Fair value at start of year	63.2	49.9
Expected return on assets	4.7	3.5
Employer contributions	5.1	4.7
Contributions by scheme participants	0.5	0.5
Benefits paid	(2.0)	(1.1)
Actuarial gains and losses	1.0	5.7
Fair value at end of year	72.5	63.2

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2010

... .. continued

Analysis of assets

The major categories of scheme assets are as follows

	2010 £m	2009 £m
Equities	46.3	40.6
Bonds	11.3	10.8
Gilts	7.4	6.3
Property	1.3	-
Cash and other	5.2	2.6
Annuity policies	1.0	2.9
	<u>72.5</u>	<u>63.2</u>

Actual return on scheme assets

	2010 £m	2009 £m
Actual return on scheme assets	<u>5.7</u>	<u>9.2</u>

The pension scheme has not invested in any of the company's own financial instruments or in properties or other assets used by the company

Scheme liabilities

Changes in the present value of scheme liabilities are as follows

	2010 £m	2009 £m
Present value at start of year	81.6	55.7
Current service cost	3.7	2.9
Contributions by scheme participants	0.5	0.4
Interest cost	4.8	3.4
Benefits paid	(2.0)	(1.0)
Actuarial gains and losses	4.3	20.2
Present value at end of year	<u>92.9</u>	<u>81.6</u>

Amounts recognised in the profit and loss account

	2010 £m	2009 £m
Amounts recognised in operating profit		
Current service cost - employer	<u>3.7</u>	<u>2.9</u>
Recognised in arriving at operating profit	<u>3.7</u>	<u>2.9</u>
Amounts recognised in other finance cost		
Expected return on scheme assets	(4.7)	(3.5)
Interest on franchise adjustment	(0.7)	-
Interest cost	4.8	3.4
Recognised in other finance cost	<u>(0.6)</u>	<u>(0.1)</u>
Total recognised in the profit and loss account	<u>3.1</u>	<u>2.8</u>

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2010

..... continued

Amounts recognised in the statement of total recognised gains and losses

	2010 £m	2009 £m
Actual return less expected return on scheme assets	1 0	5 7
Other actuarial losses	(4 3)	(20 2)
Change in franchise adjustment	3 1	11 6
Total pension cost recognised in the statement of total recognised gains and losses	<u>(0 2)</u>	<u>(2 9)</u>

The cumulative amount of actuarial gains and losses recognised in the statement of total recognised gains and losses since 1 January 2004 is £6 3m loss (2009 £6 1m loss)

History of experience adjustments on scheme assets and liabilities

Amounts for the current and previous 4 periods are as follows

	2010 £m	2009 £m	2008 £m	2007 £m	2006 £m
Fair value of scheme assets	72 5	63 2	49 9	50 3	42 0
Present value of scheme liabilities	<u>(92 9)</u>	<u>(81 6)</u>	<u>(55 7)</u>	<u>(66 0)</u>	<u>(58 3)</u>
Deficit in scheme	<u>(20 4)</u>	<u>(18 4)</u>	<u>(5 8)</u>	<u>(15 7)</u>	<u>(16 3)</u>

Experience adjustments

	2010 £m	2009 £m	2008 £m	2007 £m	2006 £m
Experience adjustments arising on scheme assets	<u>1 0</u>	<u>5 7</u>	<u>(8 8)</u>	<u>3 1</u>	<u>2 1</u>
Experience adjustments arising on scheme liabilities	<u>(0 3)</u>	<u>(5 2)</u>	<u>(0 9)</u>	<u>(5 0)</u>	<u>(0 3)</u>

Non contract specific

This consists of a pre-funded defined benefit scheme that does not relate to any specific contract. The funding policy is to contribute such variable amounts, on the advice of the actuary, as will achieve 100% funding on a projected salary basis. Any liabilities arising are recognised in full.

Triennial funding valuation

Among our non-contract specific schemes, the largest is the Serco Pension and Life Assurance Scheme (SPLAS). The most recent full actuarial valuation of this scheme was undertaken as at 6 April 2009 and resulted in an actuarially assessed deficit of £141m. Following this review, the Group agreed with the Trustees to make cash contributions of 30% of members' pensionable salaries until 2019, plus lump sum payments of £20m, which was paid in December 2010 and £40m which was paid in January 2011. The level of benefits and contributions under the scheme is kept under continual review in light of the needs of the business and changes to pensions legislation.

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2010

..... continued

Reconciliation of scheme assets and liabilities to assets and liabilities recognised

The amounts recognised in the balance sheet are as follows

	2010 £m	2009 £m
Fair value of scheme assets	874 1	776 6
Present value of scheme liabilities	<u>(902 9)</u>	<u>(851 1)</u>
	(28 8)	(74 5)
Members' share of deficit	<u>1 5</u>	<u>3 3</u>
Deficit in the scheme	(27 3)	(71 2)
Related deferred tax asset	<u>7 4</u>	<u>19 9</u>
Net liability in the balance sheet	<u><u>(19 9)</u></u>	<u><u>(51 3)</u></u>

Scheme assets

Changes in the fair value of scheme assets are as follows

	2010 £m	2009 £m
Fair value at start of year	776 6	718 5
Expected return on assets - employer	45 9	35 2
Expected return on assets - employee	1 4	1 0
Employer contributions	45 9	26 9
Contributions by scheme participants	1 2	1 4
Benefits paid	(31 2)	(31 1)
Actuarial gains and losses	<u>34 3</u>	<u>24 7</u>
Fair value at end of year	<u><u>874 1</u></u>	<u><u>776 6</u></u>

Employer contributions for non-contract specific schemes in 2010 included a £20m special contribution paid in 2010

Analysis of assets

The major categories of scheme assets are as follows

	2010 £m	2009 £m
Equities	36 6	41 4
Bonds except LDI	16 6	15 2
Liability driven investments (LDI)	651 3	493 6
Gilts	1 1	0 9
Property	9 5	8 9
Cash and other	133 9	192 2
Annuity policies	<u>25 1</u>	<u>24 4</u>
	<u><u>874 1</u></u>	<u><u>776 6</u></u>

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2010

..... .. *continued*

Actual return on scheme assets

	2010 £m	2009 £m
Actual return on scheme assets	<u>81.6</u>	<u>60.9</u>

The pension scheme has not invested in any of the company's own financial instruments or in properties or other assets used by the company

Scheme liabilities

Changes in the present value of scheme liabilities are as follows

	2010 £m	2009 £m
Present value at start of year	851.1	669.3
Current service cost - employer	14.2	14.2
Current service cost - employee	0.5	0.6
Past service cost	0.3	0.7
Contributions by scheme participants	0.8	0.8
Interest cost - employer	47.6	38.7
Interest cost - employee	1.3	1.1
Benefits paid	(31.5)	(31.3)
Actuarial gains and losses	<u>18.6</u>	<u>157.0</u>
Present value at end of year	<u>902.9</u>	<u>851.1</u>

In some schemes, employee contributions vary over time to meet a specified proportion of the overall costs, including a proportion of any deficit. The liabilities recognised in the balance sheet for these schemes are net of the proportion attributed to employees. In addition, the amounts charged to the consolidated income statement for these schemes are net of the proportion attributed to employees. The amounts attributed to employees are shown separately in the reconciliation of changes in the fair value of scheme assets and liabilities.

Amounts recognised in the profit and loss account

	2010 £m	2009 £m
Amounts recognised in operating profit		
Current service cost - employer	14.2	14.2
Past service cost	<u>0.3</u>	<u>0.7</u>
Recognised in arriving at operating profit	<u>14.5</u>	<u>14.9</u>
Amounts recognised in other finance cost		
Expected return on scheme assets - employer	(45.9)	(35.2)
Interest cost on scheme liabilities - employer	<u>47.6</u>	<u>38.7</u>
Recognised in finance cost	<u>1.7</u>	<u>3.5</u>
Total recognised in the profit and loss account	<u>16.2</u>	<u>18.4</u>

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2010

.. *continued*

Amounts recognised in the statement of total recognised gains and losses

	2010 £m	2009 £m
Actual return less expected return on scheme assets	34 3	24 7
Other actuarial losses	(18 6)	(157 0)
Change in members' share	(1 4)	1 8
Total pension (cost)/income recognised in the statement of total recognised gains and losses	<u>14 3</u>	<u>(130 5)</u>

The cumulative amount of actuarial gains and losses recognised in the statement of total recognised gains and losses since 1 January 2004 is £38 5m loss (2009 £52 8m loss)

History of experience adjustments on scheme assets and liabilities

Amounts for the current and previous 4 periods are as follows

	2010 £m	2009 £m	2008 £m	2007 £m	2006 £m
Fair value of scheme assets	874 1	776 6	718 5	744 2	642 9
Present value of scheme liabilities	(902 9)	(851 1)	(669 3)	(774 0)	(765 5)
(Deficit)/surplus in scheme	<u>(28 8)</u>	<u>(74 5)</u>	<u>49 2</u>	<u>(29 8)</u>	<u>(122 6)</u>

Experience adjustments

	2010 £m	2009 £m	2008 £m	2007 £m	2006 £m
Experience adjustments arising on scheme assets	<u>34 3</u>	<u>24 7</u>	<u>(74 7)</u>	<u>2 6</u>	<u>14 5</u>
Experience adjustments arising on scheme liabilities	<u>(2 4)</u>	<u>(32 9)</u>	<u>(2 6)</u>	<u>1 3</u>	<u>(11 1)</u>

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2010

... .. continued

28 Commitments

Capital commitments

Amounts contracted for but not provided in the financial statements amounted to £1.6m (2009 £2.7m)

Operating lease commitments

As at 31 December 2010 the company had annual commitments under non-cancellable operating leases as follows

Operating leases which expire

	2010 £m	2009 £m
Land and buildings		
Within one year	1.8	1.2
Within two and five years	13.8	9.4
Over five years	1.8	2.8
	<u>17.4</u>	<u>13.4</u>
Other		
Within one year	2.4	0.9
Within two and five years	12.9	11.7
Over five years	0.3	-
	<u>15.6</u>	<u>12.6</u>

29 Derivative financial instruments

	2010 Assets £m	2010 Liabilities £m	2009 Assets £m	2009 Liabilities £m
Forward foreign exchange contracts	<u>0.5</u>	<u>(0.5)</u>	<u>0.4</u>	<u>(0.2)</u>

Analysed as

	2010 Assets £m	2010 Liabilities £m	2009 Assets £m	2009 Liabilities £m
Non-current	0.4	(0.4)	0.3	(0.1)
Current	<u>0.1</u>	<u>(0.1)</u>	<u>0.1</u>	<u>(0.1)</u>
	<u>0.5</u>	<u>(0.5)</u>	<u>0.4</u>	<u>(0.2)</u>

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2010

.... . *continued*

30 Post balance sheet events

As detailed in note 27, certain of the Group's pension schemes now reflect a lower pension liability due to the use of CPI as the statutory increase measure

Following this, in April 2011, the pension liability has further reduced by approximately £35m due to the Company applying the CPI measure of indexation for non-statutory pension increases where this change is permitted by the scheme rules

31 Control

The immediate parent company is Serco Holdings Limited. The ultimate parent company and controlling party of the Company is Serco Group plc, a company incorporated in Great Britain and registered in England and Wales. Serco Group plc is the parent undertaking of the smallest and largest group to consolidate these financial statements. The financial statements of Serco Group plc are available from the Company Secretary, Serco Group Plc, 16 Bartley Wood Business Park, Bartley Way, Hook, Hampshire RG27 9UY.