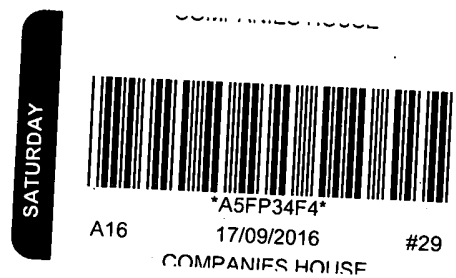


Serco Limited
Annual Report and Financial Statements
for the Year Ended 31 December 2015



Serco Limited

Contents

Company Information	3
Directors' Report	4 to 5
Strategic Report	6 to 21
Statement of Directors' Responsibilities	22
Independent Auditor's Report	23
Profit and Loss Account	24
Statement of Comprehensive Income	25
Statement of Changes in Equity	26
Balance Sheet	27
Notes to the Financial Statements	28 to 62

Serco Limited
Company Information

Registered office

Serco House
16 Bartley Wood Business Park
Bartley Way
Hook
Hampshire
RG27 9UY
United Kingdom

Auditor

Deloitte LLP
2 New Street Square
London
United Kingdom

Serco Limited

Directors' Report for the Year Ended 31 December 2015

The Directors present the annual report and financial statements for the Company for the year ended 31 December 2015.

Directors of the Company

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

G Leach

E Benison (appointed 28 August 2015)

K Craven (appointed 28 August 2015)

N Crossley (appointed 18 September 2015)

A Crawshaw (resigned 5 January 2015)

R Judge (resigned 24 November 2015)

T Lawlor (resigned 13 August 2015)

New shares allotted

In June 2015 new ordinary shares were allotted by Serco Limited for an aggregate consideration of £150.0m.

Going concern

In assessing the basis of preparation of the financial statements for the year ended 31 December 2016, the Directors have considered the principles of the Financial Reporting Council's 'Guidance on Risk Management, Internal Control and Related Financial and Business Reporting, 2014'; namely assessing the applicability of the going concern basis, the review period and disclosures.

The Directors have undertaken a rigorous assessment of going concern and liquidity, taking into account financial forecasts for the period to 31 December 2017. In order to satisfy ourselves that we have adequate resources for the future, the Directors have reviewed the strength of the Company's balance sheet, the recoverability of assets and availability of funding through the Group's existing facilities. The Company has received a letter of support from Serco Group plc that confirms it will make cash or equity funds available to the company to allow it to meet its financial obligations as and when they fall due over the period up to 12 months from the date of the accounts. Whilst the letter of support does not give rise to any legal obligation the Directors are satisfied that it provides sufficient assurance of the intent of the parent to continue to support the business.

The Directors have a reasonable expectation that the Company will be able to operate within the level of available facilities and cash for the foreseeable future and accordingly believe that it is appropriate to prepare the financial statements on a going concern basis.

Employment of disabled persons

Full and fair consideration is given to applications for employment made by the disabled, 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 business and matters concerning them as employees and noting employees' views so that they can be taken in to 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 steps that they ought to have taken as a Director in order to make themselves aware of any relevant audit information and to establish that the Company's auditors are aware of that information. The Directors confirm that there is no relevant information that they know of and of which they know the auditors are unaware.

Serco Limited
Directors' Report for the Year Ended 31 December 2015

Post balance sheet events

Subsequent to the year end the UK public voted to leave the European Union and whilst the Company's view of its principal risks and uncertainties remains substantially unchanged, the outcome of the UK vote has created uncertainties in our UK markets and the wider economy. Therefore, the impact of Britain leaving the EU remains a key consideration within the risk of failure to grow profitably. However, no adjustments were required to the Company's financial statements as a result of the political and economic changes brought about by the vote.

Since the year end certain contracts have been exited or renegotiated, resulting in releases of Onerous Contract Provisions (OCPs) of approximately £10m. These are non-adjusting post balance sheet events.

Auditor

In accordance with section 487 of the Companies Act 2006, Deloitte LLP has not been re-appointed as the Company's auditor. Following a competitive tender process, KPMG LLP have confirmed their willingness to be appointed as the Company's auditor for the year ending 31 December 2016.

Approved by the Board on 9 September 2016 and signed on its behalf by:



N Crossley
Director

Serco Limited

Strategic Report for the Year Ended 31 December 2015

The Directors present their Strategic Report for the year ended 31 December 2015.

Principal activity

The principal activity of the Company is to deliver essential services mainly in the public sector by effectively managing people, processes, technology and assets. Serco Limited supports governments, agencies and companies by offering operational, management and consulting expertise in the most important areas of public service, including transport, defence, science, employment, offender management, IT and Business Process Outsourcing (BPO).

The Strategy Review undertaken by the Group in 2014 determined Serco's future will be as an international Business to Government (B2G) business with core sectors of: Justice and Immigration, Defence, Transport, Citizen Services and Healthcare. As part of the Strategy Review, certain assets and liabilities have been designated as non-core and held for sale. As at 31 December 2015 this is limited to the remaining onshore private sector BPO business, which is expected to be sold within the next 12 months. Following the agreement to dispose of the offshore private sector BPO operations it was determined that the Environmental Services and Leisure businesses would no longer be disposed of, for both strategic and financial reasons. As a result, these operations were transferred out of held for sale at 15 December 2015, the point at which this decision was made and publically announced.

The Company's immediate parent is Serco Holdings Limited. The ultimate parent and controlling party is Serco Group plc, a company incorporated in the United Kingdom and registered in England and Wales.

Business review

Turnover for the Company for the year was down 12.0% from £1,749.5m to £1,538.7m driven principally by a reduction in new contract wins and a loss of existing contracts. The Company generated an operating loss, before net exceptional items, for the year of £21.3m (2014: loss of £452.0m). The operating loss was lower than in the prior year as a result of the impact of the Contract and Balance Sheet Review in 2014, contract attrition from low margin or loss making contracts and a reduction in costs associated with under-performing contracts. During the year net exceptional charges of £34.8m were incurred (2014: £392.5m), of which £24.4m is in respect of the impairment of assets transferred to held for sale. After exceptional items the operating loss of the Company for the financial year was £56.0m (2014: £844.5m loss).

Net assets of the Company have increased by 47% to £263.5m (2014: 179.7m). This includes the impact of a share issue of 364,382 ordinary shares with a nominal value of £0.4m which were allotted for an aggregate consideration of £150.0m, funded by an intercompany loan, giving rise to share premium of £149.6m.

Transformation continues through 2016 and 2017, and increasingly this will be focused on re-building the Company's business development functions and bid pipeline, strengthening our sector propositions, and consolidating our differentiated capability in order to win. We will also continue to improve operational execution and drive further cost efficiencies. Only when these transformational elements are all in place will we be able to harvest the financial benefit.

UK Central Government

Revenue for the year was £705.1m (2014: £870.9m), a decline of 19%. The principal drivers of the significant revenue reduction included the end of the contracts for the Docklands Light Railway (DLR) and the Colnbrook immigration removal centre. Other reductions included lower project or volume-related revenue, for example managing the Thameside prison expansion in 2014. There was limited growth elsewhere to offset these contract ends or reductions.

There was £45.3m of OCP utilisation in respect of the UK Central Government division, which was broadly in line with our original expectations. This includes those for COMPASS, PECS and FPMS, which as previously disclosed were amongst the largest provisions taken as part of the Contract and Balance Sheet Review.

Looking ahead, attrition is expected in 2016 as a result of known contract losses or other revenue reductions. The key drivers of this attrition are the transfer back of services that Serco Limited had previously been providing to the Defence Science and Technology Laboratory (Dstl) and the end of the current Defence Businesses Services arrangement, together with a number of smaller contracts ending or reducing in scope.

Additionally, of existing work where an extension or rebid will be required at some point during the next three years due to a scheduled contract end date before the end of 2018, there are approximately 8 contracts with annual revenue of over £5m each within the UK Central Government division. Our pipeline of major new bid opportunities due for decision within the next 24 months includes the Defence Fire & Risk Management Organisation and the operation of an immigration removal centre. Over the longer term, we continue to expect reform and improvement to the prison system, and for opportunities in Defence and other areas to emerge as the UK Government continues its efforts to save cost and improve public services.

Serco Limited

Strategic Report for the Year Ended 31 December 2015

UK Local and Regional Government

Revenue for the year was £731.0m (2014: £776.6m), a decline of 6%. There was modest revenue growth from the start of new contracts such as Lincolnshire County Council BPO services and Havering environmental services, together with additional volume-related revenues in health procurement services and a small number of other Citizen Services contracts. These areas of growth were offset by the end of the contracts such as Westminster City Council BPO support and Suffolk Community Healthcare, together with a number of other reductions in volume-related revenue predominantly in other Citizen Services operations.

Included in the Company's operating loss in respect of the UK Local and Regional Government division was a charge of £34.0m in relation to the Lincolnshire County Council contract due to the establishment of a new OCP together with related impairments and charges. There has been significant operational challenge in the first year, predominantly related to our responsibility to implement a new ERP system, which is now expected to result in losses for the remaining contractual period. £5.3m of the provision was utilised against the impairment of assets in the year. There was also £9.8m of OCP utilisation in relation to the Suffolk Community Healthcare contract operated by this division. Separately, there was a one-time profit of £9.0m relating to the Thurrock BPO services contract where settlement on early termination had been mutually agreed with the customer; the one-time profit represents a payment to Serco Limited in lieu of anticipated profit for future years, net of direct costs, impairments and other charges.

Signed contracts during the year included the successful rebids of Serco's support services to Wishaw General Hospital and Norfolk & Norwich University Hospital, an extension until the end of 2017 for the Child Maintenance Group (CMG) case management contract and a one-year extension to our operation of the Work Programme.

Looking ahead, significant attrition is expected in 2016 as a result of known contract losses or other revenue reductions. The key drivers of this attrition are the end of the Suffolk Community Healthcare and National Citizen Services contracts which were heavily loss-making and were not rebid, the early termination of the Thurrock BPO services contract, the ending of certain infrastructure services support to private sector customers, lower revenues on healthcare procurement operations, the reducing scale of CMG operations and a number of other smaller contracts ending or reducing in scope.

Our pipeline of major new bid opportunities due for decision within the next 24 months includes 5 tenders for various environmental services and hospital facilities management bids. We continue to evaluate developments in the other sectors of operation within the UK Local and Regional Government division, including other Citizen Services work and to expand our European business providing various operational support to government agencies.

Global Services

As part of Serco's previously announced strategy to exit non-core markets and to focus on the provision of public services, Serco is seeking to exit its private sector BPO operations. In July 2015 the Serco Group completed the sale of part of its UK onshore business, with the Company incurring £5.0m of costs in connection with the disposal. The remaining UK onshore operations will be exited either by further disposals, transfers, early termination or running-off the contracts over their remaining contractual period, which is reflected in the 18% decline of revenue in the year to £21.9m (2014: £26.8m).

Middle East

Revenue for the year was £80.7m (2014: £75.2m), an increase of 7%. There was higher procurement revenue on the Dubai Metro and Dubai Tram contracts, as well as additional revenue from the commencement of the Dubai Downtown Trolley contract.

Contract provisions

The total of current and non-current provisions, excluding provisions related to businesses held for sale, has decreased by £48.3m since 31 December 2014, the majority of which relates to a reduction in contract provisions as a result of the utilisation and release of provisions against losses on onerous contracts, offset by new or additional onerous contract provision charges made in the year. Movements in contract provisions are as follows:

	£ m
At 1 January 2015	256.6
Charged to the profit and loss account	51.5
Released to the profit and loss account – exceptional	(2.8)
Released to the profit and loss account	(30.3)
Utilised during the year	(69.7)
Transfer to assets held for sale	(0.9)
Unwinding of discount	1.7
At 31 December 2015	206.1

Serco Limited

Strategic Report for the Year Ended 31 December 2015

The following contracts account for the significant movements in the contract provision balance during the year:

Commercial and Operational Managers Procuring Asylum Support Services (COMPASS)

The COMPASS contract with the UK Home Office is for the provision of accommodation, transportation and subsistence payments for asylum seekers whilst their claims are being processed. Claim processing can take from a few months to several years. The contract commenced in 2012 and provides services in two of the six administrative regions of the contract in the UK; the North West, comprising fourteen Local Authority areas; and Scotland and Northern Ireland. The contract runs to December 2017, with a further extension of up to two years at the option of the customer. In 2015, the numbers of service users continued to be volatile, however for the year as a whole utilisation of the onerous contract provision was in line with the forecast expectation. The final outcome over the contract life will be heavily dependent on the future number of asylum seekers, the volatility of the numbers and our ability to find suitable accommodation.

Future Provision of Marine Services (FPMS)

The FPMS contract that commenced in 2007, which has a 15-year duration, provided marine support services to the UK Ministry of Defence (MOD) dockyard ports of Portsmouth, Plymouth and Faslane as well as support to military exercises and training to Raasay Ranges. In 2015 the contract has performed better than expected due largely to lower costs in respect of backfill vessel bookings and dockings, and the revenues from additional taskings from the customer. The forecasts for the contract have been reassessed with the result being a net release of £6.6m due to the favourable performance in the year, savings expected in future years from a voluntary redundancy programme run in 2015 and other changes to the estimated outcome; partially offset by lower RPI inflation on the contract than previously forecast and costs relating to the purchase of a new vessel.

Prisoner Escort and Custody Services (PECS)

The contract provides prisoner transportation services between courts and prisons and for the management of prisoner welfare when at court for the Ministry of Justice (MOJ). It was awarded in 2011 and runs for seven years. In 2015, utilisation of the OCP was slightly higher than originally expected. The contract is operated with a very challenging KPI regime and in order to meet these KPIs we require a larger workforce than previously envisaged, along with the associated recruitment, training and contract management costs; the forecast for the contract has been reassessed with the result being an increase in the OCP of £11.3m. In the case of this contract, we have judged that it is unlikely that the customer will wish to extend this contract beyond its minimum term in 2018 on the current basis. If this judgement proves to be incorrect, further OCP charges may be required.

HMP Ashfield

The HMP Ashfield PFI contract commenced in 1999 and runs through to 2024. In 2013 the operational role of Ashfield changed from a Young Offender Institution to an adult male sex offenders' prison, resulting in a changed cost base. Since the change of operational of the prison the MoJ has imposed a level of pricing that we dispute, and which would result in substantial losses over the remaining life of the contract. Discussions with the MoJ around re-pricing proposals are expected to conclude in 2016. In 2015 performance has been slightly better than expected due to the benefit of in year cost savings. The forecast for the contract has been reassessed with the result being a release of £8.7m due to the expected future ongoing benefits of the cost reductions and efficiencies delivered in 2015.

Lincolnshire County Council

The contract scope is to provide the following outsourced services: information management and technology services and support; back office services including finance, HR and payroll services; and customer services acting as the internal and external point of contact for Lincolnshire County Council and all Council services.

In 2015 the contract had difficulties implementing a new Enterprise Resource Planning (ERP) system and resolving these issues has been more complex and protracted than originally anticipated. While we are making good progress, the full implementation of the new system is not expected until later this year. The delay has impacted our ability to make the wider service transformation changes needed to make the contract more efficient and also led to operational service difficulties, triggering service credits. The issues have also resulted in the requirement to increase and maintain additional management and support resources on the contracts to remediate the problems faced. As a result of these factors a charge totalling £34.0m was taken in 2015, comprising a provision for future losses over the remaining term of the contract. In 2015 £5.3m of the provision was utilised against the impairment of assets. Included in operating loss is £5.2m in respect of the in-year losses on this contract.

National Citizen Services

This heavily loss making contract was successfully exited at a significantly lower cost than we initially expected, resulting in a release of the remaining provision.

Serco Limited

Strategic Report for the Year Ended 31 December 2015

Principal risks and uncertainties

The Company faces many risks and uncertainties which we mitigate and manage through risk management processes. The Group Risk Register sets out the principal risks facing the business as a whole, including those that are managed at the Serco Limited level, and is set by the Executive Committee after taking into consideration the various divisional risk registers. The Group Risk Register is reported to the Serco Group plc Board via the Corporate Responsibility and Risk Committee. In addition to the principal risks and uncertainties listed below there may be additional risks unknown to Serco Limited and other risks, currently believed to be immaterial, which could turn out to be material. These risks, whether they materialise individually or simultaneously, could significantly affect the Company's business and financial results.

The Company previously reported on the potential risk to its business should the UK public voted to leave the European Union and whilst the Company's view of its principal risks and uncertainties for the remaining four months of the financial year remains substantially unchanged, the outcome of the UK vote has created uncertainties in our UK markets and the wider economy. Therefore, the impact of Britain leaving the EU remains a key consideration within the risk of failure to grow profitably.

The Company has 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. 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.

Following the completion of the Strategic Review, a robust and systematic assessment of the principal risks facing the Group was carried out. These include the principal risks that would threaten the execution of Serco's strategy, business model, future performance, solvency and liquidity.

The resulting principal risks are each classified as strategic, reputational, financial, operational, legal or compliance. They are described on the following pages, together with the relevant strategic business objectives, key risk drivers and the Group-wide material controls which have been put in place to mitigate the principal risks. Further details can be found in the Serco Group plc financial statements.

The risks are considered within the timeframe of three years which is the same time period that has been used in the Viability Statement in the Serco Group plc financial statements.

Risk appetite

In 2016, the Executive Committee of Serco Group plc will undertake an exercise to assess the risk appetite for each of the principal risks. The risk appetite represents the nature and amount of risk that the Group is willing to accept and facilitates decision making as to the level of resource that should be expended to mitigate the principal risks.

Risk appetite statements are being developed which will be reviewed and endorsed by the Corporate Responsibility and Risk Committee. These statements will be used to define the risk tolerance levels throughout the business, and along with our values, Code of Conduct and mandatory ethics training will provide clarity on the risk culture of the Group.

Serco Limited

Strategic Report for the Year Ended 31 December 2015

Strategic and reputational risks

Risk	Key risk drivers	Mitigation
<p>Failure to attract and retain leaders fit for the future</p> <p><i>Impact on business objectives:</i></p> <ul style="list-style-type: none"> • Winning good business • Executing brilliantly • A place people are proud to work • Profitable and sustainable <p>People are at the core of our business at all levels of the organisation. Our success depends on the continued service and performance of highly qualified and experienced operational management and business development teams and their leaders.</p> <p>If our leaders are not able to meet the needs of the business, this could impact our integrity, brand and reputation, and could have a material adverse impact on our financial condition and results of operations affecting the prospects of the business.</p>	<p>Good leadership underpins our ability to develop and deliver the services we provide to customers. The ability to plan for management succession and to attract, train and retain good leaders and other employees is a key driver for our success.</p> <p>Failure to maintain a robust framework of people processes, systems and controls to enable attraction, selection, development and retention of the appropriate calibre of employees and leaders would compromise our ability to execute our strategy and achieve our business objectives. This would adversely affect employee pride in the organisation and prevent Serco Limited from becoming an employer of choice for talented people.</p> <p>Employee engagement is also critical to our success; engaged employees deliver better service to our customers, are more productive, and want to stay with us. Failure to attract, motivate and engage employees can create a decline in morale and an increase in staff turnover, which may adversely affect our ability to win new and retain existing contracts owing to a lack of appropriate skills and a reduction in customer satisfaction.</p>	<p><i>Material controls:</i></p> <ul style="list-style-type: none"> • Serco Management System • Serco Leadership Model • Centres of Excellence • Appropriately skilled / trained resources <p><i>Current mitigation actions:</i></p> <ul style="list-style-type: none"> • Implementation of Serco Leadership Model • Implementation of talent and succession processes • Implementation of a robust framework of people processes and procedures that supports the acquisition and retention of the right calibre of staff <p><i>Future actions:</i></p> <ul style="list-style-type: none"> • Continued improvements to our Leadership Model • Resourcing of the Centres of Excellence and functions with the intent to support the delivery of the Company strategy • Improvements to our talent pooling capability • Improvements to the 'on boarding' and induction processes and systems • Improvements to short- and long-term incentive arrangements • Establishment of our Leadership Academy

Serco Limited
Strategic Report for the Year Ended 31 December 2015

Strategic and reputational risks continued

Risk	Key risk drivers	Mitigation
<p>Failure to transform and deliver the Company strategy</p> <p><i>Impact on business objectives:</i></p> <ul style="list-style-type: none"> • Winning good business • Executing brilliantly • Profitable and sustainable <p>We have put in place transformation programmes to achieve lasting change in the way Serco Limited operates. Concurrent programmes are being delivered in Finance, IT, HR, Procurement, Contract Management and Business Development.</p> <p>Successful delivery of these in an integrated fashion will drive greater standardisation, achieve critical efficiencies and cost reductions, improve transparency and reinforce continuous improvement in our operational delivery.</p>	<p>Delivery of the Company strategy could be placed at risk because of too many competing programmes with complex interdependencies, poor programme and solution design, poor integration across activities (leading to operational inefficiency or incompatibility), or in the failure to achieve lasting cultural change (due to failure of buy-in or the setting of unrealistic or unclear expectations).</p> <p>Affordability may place a constraint on resources, which could jeopardise or delay the transformation of the Company.</p> <p>Note: The risk drivers and controls associated with achieving the objectives of the Company strategy are covered under other principal risk, for example the risk 'Failure to grow profitably' reflects the risk associated with failing to maintain a healthy pipeline of new contracts. The risk of failure to transform and deliver the Company strategy focuses on the delivery of the Company transformation programmes.</p>	<p><i>Material controls:</i></p> <ul style="list-style-type: none"> • Company strategy • Transformation programme design • Governance structure • Standardised Divisional Performance Reviews <p><i>Current mitigation actions:</i></p> <ul style="list-style-type: none"> • Establishment of a central Programme Management Office (PMO) to monitor and coordinate the programmes • Implementation of governance for transformation programmes. PMO reports delivery constraints to the Group Chief Operating Officer and the Executive Committee <p><i>Future actions:</i></p> <ul style="list-style-type: none"> • Coordination of a communication strategy to engage all individuals in the business so that they buy into the longer-term goals of the Company • Ongoing review of Company strategy and internal delivery structures to ensure Serco is set to excel in its chosen markets and sectors

Serco Limited

Strategic Report for the Year Ended 31 December 2015

Strategic and reputational risks continued

Risk	Key risk drivers	Mitigation
<p>Failure to build our reputation or act with integrity</p> <p><i>Impact on business objectives:</i></p> <ul style="list-style-type: none"> • Winning good business • Executing brilliantly • A place people are proud to work • Profitable and sustainable <p>Falling below our expected high standards with respect to operational performance and our behaviour will negatively impact our reputation with customers and other stakeholders. Operating effectively but without integrity will generate mistrust and scrutiny; conversely, acting with integrity but operating ineffectively will raise uncertainty in our ability to sustain and grow our business.</p> <p>Both these are key to our reputation, failing on either one could therefore significantly impact the economic value of our business, increase the risk of regulatory intervention, and impact on our ability to attract and retain talent.</p>	<p>Central to building our reputation are two key drivers – our operational performance and our behaviour.</p> <p>A number of factors can influence our ability to mitigate this risk effectively, including: how we effectively manage our operational, safety and financial risks; how we ensure compliance with contractual, legal and regulatory requirements; how we ensure that those who work for us behave with integrity and in an ethical manner; how we continually manage our reputation and stakeholder relationships; and how we ensure that we respond to incidents in a transparent and truthful manner.</p> <p>The critical area of risk for us is where operational weakness or failure and / or unethical behaviour intersects with a highly charged political environment resulting in a significant negative impact on the Company's reputation.</p>	<p><i>Material controls:</i></p> <ul style="list-style-type: none"> • Our Values and Code of Conduct • Assurance – three lines of defence • Serco Management System • Contract / legal review and documentation of Service Delivery Requirements • Standardised Divisional Performance Reviews • Appropriately skilled and trained resources • Business continuity, disaster recovery, crisis management and communication plans <p><i>Current mitigation actions:</i></p> <ul style="list-style-type: none"> • Enhancement of policies on business standards and ethics, including anti-bribery and corruption, protection of human rights, sanctions, adherence to competition law, avoidance of money-laundering, conflicts of interest, and employment of ex-government officials • Provision of mandatory ethics training to make it clear that Serco does not engage in and will not tolerate unethical behavior • Provision of guidance and tools on how our people can avoid this risk • Embedding of ethical and human rights reviews in our bidding process • Implementation of processes to monitor and react to emerging issues and developed divisional contingency communication plans • Implementation of tactical programmes centred on effective reactive responses to operational issues and proactive customer and stakeholder engagement programmes <p><i>Future actions:</i></p> <ul style="list-style-type: none"> • Continue to strengthen procedures on due diligence of third parties and ongoing monitoring of those relationships • Our Values have been refreshed and will be communicated in 2016

Serco Limited

Strategic Report for the Year Ended 31 December 2015

Financial risks

Risk	Key risk drivers	Mitigation
<p>Failure to grow profitably</p> <p><i>Impact on business objectives:</i></p> <ul style="list-style-type: none"> • Winning good business • Profitable and sustainable <p>We depend heavily on large contracts with a relatively limited number of major government customers and other public sector bodies and agencies for a substantial proportion of our revenue.</p> <p>If such customers decrease the amount of business they outsource to us for any reason, or if the relationship with such customers were to deteriorate, or we sustained damage to our reputation, or we were subject to negative publicity, then we could lose business across our customer base and face significant economic damage. Such damage could also include losing renewals and extensions of existing contracts.</p> <p>Serco previously reported on the potential risk to its business should the UK public voted to leave the European Union and whilst the Company's view of its principal risks and uncertainties for the remaining four months of the financial year remains substantially unchanged, the outcome of the UK vote has created uncertainties in our UK markets and the wider economy. Therefore, the impact of Britain leaving the EU remains a key consideration within the risk of failure to grow profitably.</p>	<p>The sustainability of our existing and future business with governments is dependent on a favourable policy of private sector provision of public services.</p> <p>Our government customers are affected by financial, regulatory and political constraints or policy changes. A substantial part of our business is, therefore, linked to changes in the global economy, fiscal and monetary policy, political stability, political leadership, budget priorities, and the perception and attitude of governments and the wider public to outsourcing. These could result in decisions not to outsource services or delays in placing work which might adversely impact our pipeline.</p> <p>Where a healthy pipeline of new business exists, Serco needs to effectively compete for business. Failure to have the critical skills and references, a value proposition that customers will find compelling and a risk appetite appropriate for the markets in which we compete will put Serco at a disadvantage, and put the sustainable growth necessary in our business at risk. In addition, failure to execute our bids in a professional manner by not understanding the strategic needs of a client, or by mispricing bids, developing unworkable solutions, misunderstanding risks and other bidding failures will also prevent us from achieving our growth ambitions.</p>	<p><i>Material controls:</i></p> <ul style="list-style-type: none"> • Company strategy market sectors and geographical regions • Centres of Excellence • Serco Management System • Business Lifecycle Gates Process • Appropriately skilled / trained resources • Standardised Divisional Performance Reviews • Contract / legal review and documentation of service delivery requirements <p><i>Current mitigation actions:</i></p> <ul style="list-style-type: none"> • Set up Centres of Excellence to critically review the markets and geographies we operate in globally and develop compelling value propositions in each market • Implemented improved bid management procedures • Strengthened the criteria, processes and level of scrutiny for management's review of all bids and rebids, and ensured stronger risk management earlier in the bid process to help identify potential onerous performance criteria or contract terms, and transition and operational risks, in advance • Continued to invest in appointing high calibre people for our key bids, and training our bidding teams to improve competency and performance <p><i>Future actions:</i></p> <ul style="list-style-type: none"> • Implement regular pipeline and market reviews • Embed Centres of Excellence and review sector drivers, market propositions and resource allocations • Review of Business Development processes, capability and resourcing • Review governance cycle to ensure lessons learned are embedded

Serco Limited

Strategic Report for the Year Ended 31 December 2015

Financial risks continued

Risk	Key risk drivers	Mitigation
<p>Financial control and finance IT systems failure</p> <p><i>Impact on business objectives:</i></p> <ul style="list-style-type: none"> • Executing brilliantly • Profitable and sustainable • A place where people are proud to work <p>Strong financial systems and controls are critical to the Company's success and underpin many key aspects of our business, from transaction processing to both internal and external reporting.</p> <p>Financial control failure or prolonged loss of financial IT systems may result in: an inability to accurately report timely financial results and meet contractual financial reporting obligations; a heightened risk of error and fraud; poor quality data leading to poor business decisions and an inability to forecast accurately; and an inability to make critical financial transactions that would lead to financial instability, potential business losses and negative reputational impact.</p>	<p>There are a number of critical elements driving the risk of financial control and finance IT systems failure. These include: a finance governance structure that sets the right tone from the top; adequate financial controls, including access controls to IT systems, which prevent instances of sabotage, fraud and error; the design and subsequent availability of critical financial IT systems; and the risk of information security breaches (see 'major information security breach' risk below).</p> <p>Serco Limited must communicate a clear Company Finance strategy supported by robust finance policies and standards that are embedded consistently throughout the Company.</p> <p>The risk of financial control and systems IT failure is largely driven by inadequate controls and processes. If these are poorly designed and complex, they may lead to potential inaccuracies, fraudulent behaviour and inefficient use of resources.</p> <p>The design of financial systems and access controls should ensure that key financial processes and systems are adequately protected from sabotage, fraud and error, and that instances of critical financial systems or locations not being available at critical times for prolonged periods is minimised.</p>	<p>Material controls:</p> <ul style="list-style-type: none"> • Standardised finance systems, processes and controls, and reporting • Company strategy – Finance Transformation Programme • Serco Management System • Business Lifecycle Gates Process • Appropriately skilled / trained resources • Standardised Divisional Performance Reviews • Contract / legal review and documentation of Service Delivery Requirements • Business continuity, disaster recovery, crisis management and communication plans • Assurance – three lines of defence • IT security infrastructure, processes and controls <p>Current mitigation actions:</p> <ul style="list-style-type: none"> • Embarked upon a major finance transformation programme to strengthen the financial control environment and to transform finance as a whole, with the goal of implementing standard processes and data hierarchies and common reporting language • Updated the Company's finance strategy and policies • Roll out of the Serco Finance Academy to articulate the future direction of finance and set expectations • Updated the delegated authorities matrix • Reshaped the design of financial systems and access controls • Strengthened the finance team and developed a new Finance Compliance Assurance programme <p>Future actions:</p> <ul style="list-style-type: none"> • Finance transformation programme will continue to address the Company's processes, targeting the improved effectiveness of its shared service operation • Review of contingency plans in place, including data recovery procedures and business continuity plans • Create a Corporate Shared Services Crisis Management Team and Business Continuity Plan • Ensure regular testing of back-up systems

Serco Limited
Strategic Report for the Year Ended 31 December 2015

Operational risks

Risk	Key risk drivers	Mitigation
<p>Major information security breach</p> <p><i>Impact on business objectives:</i></p> <ul style="list-style-type: none"> • Winning good business • Executing brilliantly • Profitable and sustainable <p>We and our appointed third party service providers and sub-contractors are vulnerable to a major information security breach resulting in the loss or compromise of sensitive information or wilful damage resulting in loss of service.</p> <p>A major information security breach could have a significant negative impact on our reputation and on the security of our customers. This impact could result in the loss of new or existing business by disqualification from future work, contract termination and heavy financial penalties causing a negative impact on our strategic objectives.</p> <p>Such breaches are costly to rectify and could dilute shareholder returns and result in criminal or civil action; contract and business external accreditations being withdrawn; and significant media scrutiny, all of which could materially adversely affect the business, financial condition, results of operations and prospects.</p>	<p>This is a heightened risk, particularly with respect to government contracts, due to the sensitive and confidential nature of government data that we handle.</p> <p>We collect and retain confidential information in computer systems regarding our business dealings and those of our customers, service end- users and suppliers. We provide high profile services, which adds to our attractiveness as a potential target.</p> <p>The threats facing sensitive information managed by the Company have increased with malicious and high profile attacks against major brands around the globe by well-known ‘hacktivist’ groups. Alongside this threat is the more insidious and low profile attack instigated by certain foreign bodies and their proxies to obtain information for defence or economic advantage.</p> <p>The secure processing, maintenance and transmission of information, and compliance with restrictions on the handling of sensitive information (including personal and customer information) is critical to our operations.</p>	<ul style="list-style-type: none"> • Serco Management System • Governance structure • IT security infrastructure, process and controls • Business Lifecycle Gates Process • Business continuity, disaster recovery, crisis management and communication plans • Appropriately skilled / trained resources <p><i>Current mitigation actions:</i></p> <ul style="list-style-type: none"> • Implemented information security policies and standards • Implementation of Cyber Defence Programme • Attainment of Cyber Essentials Plus (CES+) certification in the UK • Mandatory security awareness training and security awareness campaigns • Internal and external vulnerability scanning, risk and security impact assessments, and third-party due diligence assessment and penetration testing • Implemented Computer Security Incident Response teams <p><i>Future actions:</i></p> <p>Continued investment in Cyber Defence Programme to provide:</p> <ul style="list-style-type: none"> • Better visibility, monitoring and control of our security infrastructure • A Global Security Operations Centre equipped with security software and tools to monitor network and systems, and to prioritise, remediate and repel attacks and then report and manage response on a Group-wide basis • Feedback and monitoring of activities to drive user awareness and behavior • Enhanced awareness training to key personnel globally

Serco Limited

Strategic Report for the Year Ended 31 December 2015

Operational risks continued

Risk	Key risk drivers	Mitigation
<p>Catastrophic event</p> <p><i>Impact on business objectives:</i></p> <ul style="list-style-type: none"> • Winning good business • Executing brilliantly • A place people are proud to work <p>Due to the nature of the services that the Company provides, many of our operations, if not properly managed, entail the risk of significant harm to employees, third parties, members of the public or the environment.</p> <p>In the event that such a catastrophic event is found or perceived to be caused by the negligence of the Company, this could result in claims for personal injury, wrongful death or property damage by customers, subcontractors, governments, employees or members of the public, which could lead to the payment of extensive damages and result in significant adverse publicity and reputational harm.</p> <p>Certain events, including those arising as a result of third party acts such as acts of terrorism or war, are not within the Company's control, but may still result in losses and significant impact on customers and the public.</p> <p>Prolonged disruption to service delivery due to an ineffective response to catastrophic events will adversely impact the Company's reputation. Such adverse publicity and reputational harm could lead to loss of business.</p>	<p>Some of our operations are particularly high-risk; these include nuclear operations, aviation, rail, marine and custodial services. Although these are highly regulated, these carry inherent significant health, safety and environmental (HSE) risks, and the Company is exposed to the risk of material losses, liabilities and reputational damage from a catastrophic event, for example a major incident or accident.</p> <p>A number of factors may influence this risk, including: capability and experience in delivering services in high-risk sectors; an organisational culture that prioritises HSE management; robustness of safety management to support safety critical industries; ability to assess, prepare for and manage safety requirements; and the impact of external factors (for example regulatory change, war, terrorist act); and robustness of business continuity plans and crisis management.</p>	<p><i>Material controls:</i></p> <ul style="list-style-type: none"> • Company strategy • Safety management systems • Serco Management System (SMS) • Business Lifecycle Gates Process • Governance structure • Business continuity, disaster recovery, crisis management and communication plans • Appropriately skilled / trained resources • Contract / legal review and documentation of service delivery requirements • Assurance – three lines of defence • Our Values and Code of Conduct • Insurance <p><i>Current mitigation actions:</i></p> <ul style="list-style-type: none"> • Implementation of HSE strategy with clearly defined objectives and performance targets and safety oversight structures and governance • Policies, systems and procedures embedded in the SMS • Implementation of competency framework and mandatory training programmes • External and internal audits to confirm the effectiveness of these controls <p><i>Future actions:</i></p> <ul style="list-style-type: none"> • Regular review of processes and assurance of the controls to ensure continuous improvement • Review and update of crisis management plans

Serco Limited
Strategic Report for the Year Ended 31 December 2015

Operational risks continued

Risk	Key risk drivers	Mitigation
<p>Misreporting of performance</p> <p><i>Impact on business objectives:</i></p> <ul style="list-style-type: none"> • Winning good business • Executing brilliantly • A place people are proud to work <p>There may be incidents of employees not complying with the Company's policies, which might result, for example, in accounting irregularities or accounting misstatements, and failures in the accurate monitoring and reporting of contract performance. This may result in inaccurate performance and billing information being provided to Serco management, our customers and other stakeholders.</p> <p>If the misreporting is deliberate, it may constitute fraud, and the Company may be subject to litigation, inquiries or investigations that could divert management time and resources, and result in penalties, fines, sanctions, variation or revocation of permissions and authorisations, suspension or debarment from doing business with government customers.</p> <p>Accidental or deliberate misreporting of operational, regulatory and financial performance, both internally and externally, would result in reputational damage, loss of goodwill or contracts.</p>	<p>The reporting of operational performance and its accuracy is an inherent risk that is increased due to the large number of employees, geographical diversity and the diversity of the operations that we run.</p> <p>As a result, we are exposed to reputational and financial risks associated with employee errors, system errors, misunderstanding of requirements, inadequate quality of service provision and deliberate acts of misreporting of performance.</p>	<p><i>Material controls:</i></p> <ul style="list-style-type: none"> • Serco Management System • Our Values and Code of Conduct • Business Lifecycle Gates Process • Contract / legal review and documentation of service delivery requirements • Assurance – three lines of defence • Appropriately skilled / trained resources <p><i>Current mitigation actions:</i></p> <ul style="list-style-type: none"> • Following allegations in 2013, in relation to the prisoner escort and electronic monitoring contracts with the Ministry of Justice operated by the Company along with other Group companies, that Serco Group companies had overcharged the UK Government as a result of misreporting, the Group companies involved entered into a process of corporate renewal designed to mitigate the underlying risks of misreporting. Through the Corporate Renewal Programme, Group-wide controls that mitigate this risk are being implemented and are being embedded. These measures were introduced to reinforce the importance of data integrity and factual reporting down to the individual level, and diminish the risks in interpretation and understanding of our obligations. <p><i>Future actions:</i></p> <ul style="list-style-type: none"> • Contract management obligation mapping process to be implemented and used by all material contracts • Compliance assurance programme to include review of data integrity compliance • Review of annual performance review process to ensure incentives are aligned with our Values

Serco Limited
Strategic Report for the Year Ended 31 December 2015

Legal and compliance risks

Risk	Key risk drivers	Mitigation
<p>Contract non-compliance and contract non-performance</p> <p><i>Impact on business objectives:</i></p> <ul style="list-style-type: none"> • Winning good business • Executing brilliantly • Profitable and sustainable <p>Our success depends on our ability to win and successfully deliver contracts that balance risk and reward. If we fail to negotiate performance criteria and contract provisions that can be delivered at the right price, or we do not fully understand and mitigate the risks involved, or we do not put in place appropriate capabilities required to deliver against our contractual obligations, contracts that we win are more likely to suffer from poor performance and may result in compliance challenges.</p> <p>Not meeting our contractual obligations through either non-compliance with contractual requirements and / or failure to meet agreed service levels may result in significant financial or other penalties being levied, and in extreme circumstances, the termination of a contract with related compensation arrangements, which could extend to regulatory or other investigations. Apart from financial detriment, such failures could adversely affect our reputation and our ability to win new business.</p>	<p>There are a number of critical elements driving the risk of contractual non-compliance and non-performance, these include: failing to negotiate service levels and contract provisions that are appropriate for the level of reward; misunderstanding and / or not complying with contractual obligations, changes of scope, or incorrectly evaluating contractual assets; failure to properly manage contractual and operational risks; having insufficient transparency of performance and lack of capability (systems and people) to continually deliver against agreed service levels; and failure of sub-contractors and other suppliers in the performance of their obligations.</p> <p>Contracted services are delivered through direct delivery of services, through the use of sub-contractors, or through joint venture consortium partners. As a result, these drivers apply to us as well as our sub-contractors or consortium partners, where they do not have the right expertise, tools and resources to manage and monitor compliance with contract obligations and expectations adequately.</p> <p>These drivers span the full business lifecycle, including the bidding, transformation and operational phase through to contract close, and can result from insufficient discipline with respect to the development, implementation and adherence to corporate business processes, and inadequate programme governance.</p>	<p><i>Material controls:</i></p> <ul style="list-style-type: none"> • Serco Management System (SMS) • Our Values and Code of Conduct • Assurance – three lines of defence • Business Lifecycle Gates Process • Contract / legal review and documentation of Service Delivery Requirements • Appropriately skilled / trained resources • Standardised Divisional Performance Reviews (DPR) <p><i>Current mitigation actions:</i></p> <ul style="list-style-type: none"> • Revision of Company policies and governance for bidding, transition, contract management, risk management and compliance • Implementation of a new Compliance Assurance Programme to monitor compliance of contracts with respect to the SMS requirements • Roll-out of SMS self-assessment questionnaires to check compliance against SMS requirements • Business lifecycle gates process updated to include a requirement for make versus buy decisions (i.e. hire of staff versus use of sub-contractors) • Targeted investment in the recruitment and training of staff to improve the capability of bid and contract management staff. This training provides contract managers with awareness of contract management requirements and the SMS requirements • Trained key staff on the new risk management life cycle processes • Roll-out of standardised DPRs <p><i>Future actions:</i></p> <ul style="list-style-type: none"> • Currently implementing the contract management obligation mapping process across the Company. This will be used to document and track all material contractual obligations across all contracts globally

Serco Limited

Strategic Report for the Year Ended 31 December 2015

Legal and compliance risks continued

Risk	Key risk drivers	Mitigation
<p>Material legal and regulatory compliance failure</p> <p><i>Impact on business objectives:</i></p> <ul style="list-style-type: none"> • Winning good business • Executing brilliantly • A place people are proud to work • Profitable and sustainable <p>Operating across different sectors and geographies and working with national and local governments, public sector bodies and agencies, and government-regulated customers, the Company is required to comply with a complex and ever changing legal and regulatory environment. Failing to comply materially with these laws and regulations may cause significant loss to the Company.</p> <p>Legal proceedings (including class actions) may be costly and if they are not determined in the Company's favour, may divert management's attention away from the running of the business. Losses or financial penalties resulting from any current or threatened legal actions may have a material adverse effect on the Company's financial condition, results of operations and cash flows.</p>	<p>As a government contractor, the Company is subject to a greater risk of investigation, criminal prosecution, civil fraud, whistleblower lawsuits and other legal actions and liabilities than companies with exclusively commercial customers.</p> <p>As we have disclosed before, we are under investigation by the Serious Fraud Office. In November 2013, the UK's Serious Fraud Office announced that it had opened an investigation, which remains ongoing, into our Group's Electronic Monitoring Contract which is operated in part by Serco Limited. We are cooperating fully with the Serious Fraud Office's investigation but it is not possible to predict the outcome. However, in the event that the Serious Fraud Office decides to prosecute, the range of possible adverse outcomes is any one or a combination of the following:</p> <p>(i) that the Serious Fraud Office prosecutes the individuals and / or the Serco Group entities involved - which may result in the individuals or entities involved defending the action successfully; or the individuals and the entities involved being convicted, which may result in significant financial penalties, an impact on existing contracts with the UK Government and Serco being subject to a period of discretionary debarment from future contracts with UK Government entities; or</p> <p>(ii) that the Serious Fraud Office and the relevant Serco Group entities enter into a deferred prosecution agreement (DPA) – which may result in significant financial penalties and a period of discretionary debarment from future contracts with UK Government entities.</p>	<p><i>Material controls:</i></p> <ul style="list-style-type: none"> • Serco Management System • Assurance – three lines of defence • Business Lifecycle Gates Process • Contract / legal review and documentation of Service Delivery Requirements • Appropriately skilled / trained resources • Standardised DPRs <p><i>Current mitigation actions:</i></p> <ul style="list-style-type: none"> • Improvements to the capability of the organisation to interpret and implement these requirements correctly including accessible legal expertise, subject matter experts and knowledgeable staff and clear policies and procedures on how we manage our legal and regulatory requirements • Update to the business lifecycle gate process to include a requirement to identify the key material legal and regulatory requirements, and gain legal sign-off by contract and legal and contracts teams augmented by external legal counsel as appropriate • Identification of policy owners and subject matter experts responsible for the identification and tracking of new and existing requirements • Staff training on key material legal and regulatory requirements

Serco Limited

Strategic Report for the Year Ended 31 December 2015

Legal and compliance risks continued

Risk	Key risk drivers	Mitigation
Material legal and regulatory compliance failure	<p>Such debarment would be discretionary in the sense that a contracting authority may consider it not to be relevant to a given bid or rebid or that Serco has provided sufficient evidence that it has addressed any issues identified in a DPA, but would also in any event be limited in time under the terms of the Public Contract Regulations 2015.</p> <p>Upon any such conviction or DPA, the amount of additional work given to the Group by the UK Government may be reduced, and the Group may be subject to enhanced scrutiny with respect to its other contracts with the UK Government.</p> <p>It is possible that further actions beyond those being implemented under the Corporate Renewal Programme may need to be taken by us under the terms of any DPA.</p> <p>If the Group faces any criminal convictions, debarment consequences or enters into a DPA, any such outcome could result in significant fines and have a material adverse impact on the Group's ability to contract with the UK Government and its reputation which would, in turn, materially adversely affect its business, financial condition, results of operations and prospects.</p> <p>In addition, a criminal conviction of a Serco entity or of one or more of the Group's current or former employees would in certain circumstances allow the Ministry of Justice to re-open the £64.3m settlement agreed in respect of certain issues arising under the Electronic Monitoring Contract. In those limited circumstances, the UK Government may seek additional payments from Serco.</p> <p>We will continue to cooperate with the Serious Fraud Office's investigation</p>	<p><i>Future actions:</i></p> <p>A number of controls are currently being put in place to increase our ability to mitigate this risk these include:</p> <ul style="list-style-type: none"> • Review of mechanisms for the identification and management of key material legal and regulatory requirements • Development of policy and guidelines on management of key material legal and regulatory requirements • Implementation of Contract Management App (CMA) used to document and track all material contractual regulatory requirements and seek to ensure our requirements are met at all stages of the contract lifecycle including contract exit

Serco Limited
Strategic Report for the Year Ended 31 December 2015

Approved by the Board on 9 September 2016 and signed on its behalf by:

A handwritten signature in black ink, appearing to read 'N Crossley', written over a dotted line.

N Crossley
Director

Serco Limited

Statement of Directors' Responsibilities

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

Company law requires the Directors to prepare financial statements for each financial year. Under that law the Directors have elected to prepare the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law), including FRS 101 'Reduced Disclosure Framework'. Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company and 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 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.

Serco Limited

Independent Auditor's Report

We have audited the financial statements of Serco Limited for the year ended 31 December 2015, set out on pages 24 to 62 which comprise the Profit and Loss account, Statement of Comprehensive Income, Statement of Changes in Equity, Balance Sheet and related notes 1 to 29. 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), including Financial Reporting Standard 101 'Reduced Disclosure Framework'.

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

Respective responsibilities of Directors and Auditor

As explained more fully in the Statement of Directors' Responsibilities (set out on page 24), the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

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

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 2015 and of its loss 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 and the Strategic Report for the financial year for which the financial statements are prepared are 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.



John Charlton (Senior Statutory Auditor)
For and on behalf of Deloitte LLP, Statutory Auditor
London
United Kingdom

13 September 2016

Serco Limited
Profit and Loss Account for the Year Ended 31 December 2015

		Before exceptional items 2015 £ m	Exceptional items 2015 £ m	Total 2015 £ m	Before exceptional items 2014 £ m	Exceptional items 2014 £ m	Total 2014 £ m
Note							
Turnover	4	1,538.7	-	1,538.7	1,749.5	-	1,749.5
Cost of sales		(1,428.8)	-	(1,428.8)	(1,870.0)	-	(1,870.0)
Gross profit/(loss)		109.9	-	109.9	(120.5)	-	(120.5)
Administrative expenses		(100.5)	-	(100.5)	(284.0)	-	(284.0)
Amortisation of intangible fixed assets	15	(21.7)	-	(21.7)	(24.4)	-	(24.4)
Impairment of intangible fixed assets	15	(9.0)	-	(9.0)	(23.1)	-	(23.1)
Exceptional net (loss)/profit on disposal of operations	5	-	(4.3)	(4.3)	-	0.8	0.8
Other exceptional operating items	6	-	(30.4)	(30.4)	-	(393.3)	(393.3)
Operating loss	7	(21.3)	(34.7)	(56.0)	(452.0)	(392.5)	(844.5)
Interest receivable and similar income	10	21.1	-	21.1	5.3	-	5.3
Interest payable and similar charges	11	(19.9)	(0.1)	(20.0)	(24.0)	-	(24.0)
Loss before tax		(20.1)	(34.8)	(54.9)	(470.7)	(392.5)	(863.2)
Tax on loss on ordinary activities	12	(4.7)	-	(4.7)	(5.6)	(0.6)	(6.2)
Loss for the financial year		(24.8)	(34.8)	(59.6)	(476.3)	(393.1)	(869.4)

The above results were derived from continuing operations.

Serco Limited
Statement of Comprehensive Income for the Year Ended 31 December 2015

	Note	2015 £ m	2014 £ m
Loss for the year		(59.6)	(869.4)
Other comprehensive (expense)/income for the year:			
Items that will not be reclassified subsequently to profit or loss:			
Net actuarial (loss)/gain on defined benefit pension schemes ¹	23	(16.3)	59.1
Actuarial gain on reimbursable rights ¹	23	-	9.3
Tax relating to items not reclassified ¹	13	4.2	(13.2)
Items that may be reclassified subsequently to profit or loss:			
Net exchange loss on translation of foreign operations ²		-	(0.9)
Fair value loss on cash flow hedges ²		0.1	0.1
Total comprehensive expense for the year		(71.6)	(815.0)

¹ Recorded in retirement benefit obligation reserve in the Consolidated Statement of Changes in Equity

² Recorded in hedging and translation reserve in the Consolidated Statement of Changes in Equity

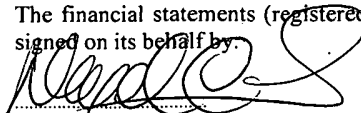
Serco Limited
Statement of Changes in Equity for the Year Ended 31 December 2015

	Called up share capital £ m	Share premium £ m	Hedging and translation reserve £ m	Share-based payments reserve £ m	Retirement benefit obligations reserve £ m	Profit and loss account £ m	Total £ m
At 1 January 2014	0.2	507.3	(0.1)	39.2	(119.8)	112.0	538.8
Total comprehensive (expense)/income for the financial year	-	-	0.1	-	55.2	(870.3)	(815.0)
New share capital subscribed	0.2	452.0	-	-	-	-	452.2
Credit in relation to share- based payments	-	-	-	3.1	-	-	3.1
Tax credit in relation to share-based payments	-	-	-	0.6	-	-	0.6
At 31 December 2014	0.4	959.3	-	42.9	(64.6)	(758.3)	179.7
Total comprehensive (expense)/income for the financial year	-	-	0.1	-	(12.1)	(59.6)	(71.6)
New share capital subscribed	0.4	149.6	-	-	-	-	150.0
Credit in relation to share- based payments	-	-	-	5.5	-	-	5.5
Tax credit in relation to share-based payments	-	-	-	-	-	-	-
Other	-	-	-	-	(0.1)	-	(0.1)
Transfer at contract end	-	-	-	-	(3.6)	3.6	-
At 31 December 2015	0.8	1,108.9	0.1	48.4	(80.4)	(814.3)	263.5

Serco Limited
Balance Sheet as at 31 December

		31 December 2015 £ m	31 December 2014 £ m
	Note		
Fixed assets			
Goodwill	15	-	-
Other intangible fixed assets	15	52.7	65.7
Property, plant and equipment	16	48.6	16.6
Investments	17	9.0	9.0
		<u>110.3</u>	<u>91.3</u>
Current assets			
Stocks	18	9.6	14.7
Debtors: amounts due within one year	19	969.7	456.3
Debtors: amounts falling due after more than one year	19	155.8	481.6
Deferred tax assets: amounts falling due after more than one year	13	10.5	10.5
Derivative financial instruments	27	0.2	0.2
Cash at bank and in hand		<u>123.1</u>	<u>191.8</u>
		<u>1,268.9</u>	<u>1,155.1</u>
Assets classified as held for sale	28	<u>9.7</u>	<u>61.0</u>
		<u>1,278.6</u>	<u>1,216.1</u>
Creditors: amounts falling due within one year			
Creditors: amounts falling due within one year	20	(408.3)	(432.0)
Corporation tax liability		(0.1)	(0.2)
Derivative financial instruments	27	(0.2)	(0.2)
Provisions	22	<u>(107.7)</u>	<u>(152.5)</u>
		<u>(516.3)</u>	<u>(584.9)</u>
Liabilities directly associated with assets classified as held for sale	28	<u>(24.5)</u>	<u>(62.6)</u>
		<u>(540.8)</u>	<u>(647.5)</u>
Net current assets		<u>737.8</u>	<u>568.6</u>
Creditors: amounts falling due after more than one year			
Creditors: amounts due after more than one year	21	(512.7)	(418.8)
Provisions	22	<u>(187.8)</u>	<u>(188.2)</u>
		<u>(700.5)</u>	<u>(607.0)</u>
Net assets excluding pension asset/(liability)		<u>147.6</u>	<u>52.9</u>
Defined benefit pension asset	23	127.1	143.9
Defined benefit pension liability	23	<u>(11.2)</u>	<u>(17.1)</u>
Net assets		<u>263.5</u>	<u>179.7</u>
Capital and reserves			
Called up share capital	24	0.8	0.4
Share premium		1,108.9	959.3
Hedging and translation reserve		0.1	-
Share-based payments reserve		48.4	42.9
Retirement benefit obligations reserve		(80.4)	(64.6)
Profit and loss account		<u>(814.3)</u>	<u>(758.3)</u>
Shareholder's funds		<u>263.5</u>	<u>179.7</u>

The financial statements (registered number 00242246) were approved by the Board of Directors on 9/9/16 and signed on its behalf by:


N Crossley
Director

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2015

1 General information

Serco Limited is a company incorporated in the United Kingdom under the Companies Act. The address of the registered office is given on page 3. The nature of the Company's operations and its principal activities are set out in the Strategic Report set out on pages 6 to 21.

These financial statements are presented in pounds Sterling because that is the currency of the primary economic environment in which the Company operates.

2 Accounting policies

The principal accounting policies adopted are set out below and have been applied consistently throughout the current and preceding year, unless otherwise stated.

Basis of accounting

The Company meets the definition of a qualifying entity under FRS 100 (Financial Reporting Standard 100) issued by the Financial Reporting Council. The financial statements have therefore been prepared in accordance with FRS 101 (Financial Reporting Standard 101) 'Reduced Disclosure Framework' as issued by the Financial Reporting Council.

As permitted by FRS 101, the Company has taken advantage of the disclosure exemptions available under that standard in relation to share-based payments, financial instruments, capital management, presentation of comparative information in respect of certain assets, presentation of a cash flow statement, standards not yet effective, impairment of assets and related party transactions. This is because the Company is included within the consolidated financial statements of Serco Group plc which are available from the address provided in note 29.

The financial statements have been prepared on the historical cost basis and on the going concern basis, except for the revaluation of certain financial instruments. Historical cost is generally based on the fair value of the consideration given in exchange for goods and services.

Adoption of new and revised standards

The following changes to IFRSs became effective in the current reporting period:

Title	Type	Background	Impact on Serco
Annual Improvements to IFRSs: 2011-2013 Cycle	Amendments	<p>Covers various matters:</p> <ul style="list-style-type: none"> IFRS 1 <i>First-time Adoption of International Financial Reporting Standards</i> IFRS 3 <i>Business Combinations</i> IFRS 13 <i>Fair Value Measurement</i> IAS 40 <i>Investment Property</i> <p>Effective for annual periods beginning on or after 1 January 2015, following EU Adoption.</p>	<p>IFRS 1 is not relevant as IFRSs have already been adopted.</p> <p>IFRS 3 changes relate to accounting within joint arrangements themselves and are therefore not relevant.</p> <p>IFRS 13 was amended to clarify the scope of the portfolio exception, which is not applied in the Group financial statements.</p> <p>IAS 40 is not relevant to Serco as no investment properties are held.</p>
IFRIC 21 Levies	New interpretation	<p>The interpretation was issued to clarify the timing of recognition of a levy payment, being a payment to a government for which no specific goods or services are received.</p>	<p>No material levy payments are made by the Group.</p>

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2015

Going concern

In assessing the basis of preparation of the financial statements for the year ended 31 December 2016, the Directors have considered the principles of the Financial Reporting Council's 'Guidance on Risk Management, Internal Control and Related Financial and Business Reporting, 2014'; namely assessing the applicability of the going concern basis, the review period and disclosures.

The Directors have undertaken a rigorous assessment of going concern and liquidity, taking into account financial forecasts for the period to 31 December 2017. In order to satisfy ourselves that we have adequate resources for the future, the Directors have reviewed the strength of the Company's balance sheet, the recoverability of assets and availability of funding through the Group's existing facilities. The Company has received a letter of support from Serco Group plc that confirms it will make cash or equity funds available to the company to allow it to meet its financial obligations as and when they fall due over the period up to 12 months from the date of the accounts. Whilst the letter of support does not give rise to any legal obligation the Directors are satisfied that it provides sufficient assurance of the intent of the parent to continue to support the business.

The Directors have a reasonable expectation that the Company will be able to operate within the level of available facilities and cash for the foreseeable future and accordingly believe that it is appropriate to prepare the financial statements on a going concern basis.

Exemption from preparing group accounts

The financial statements contain information about Serco Limited as an individual company and do not contain consolidated financial information as the parent of a group.

The Company is exempt under section 400 of the Companies Act 2006 from the requirement to prepare consolidated financial statements as it and its subsidiary undertakings are included by full consolidation in the consolidated financial statements of its ultimate parent, Serco Group plc, a company incorporated in the United Kingdom and registered in England and Wales.

Fair value

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, regardless of whether that price is directly observable or is estimated using another valuation technique. There are certain transactions in these financial statements which are similar to fair value, but are determined by the treatment set out in their respective standards. These are share based payment transactions that are within the scope of IFRS 2 *Share based Payment*, leasing transactions that are within the scope of IAS 17 *Leases*, or the calculation of net realisable value under IAS 2 *Inventories* or value in use under IAS 36 *Impairment of Assets*.

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2015

Turnover

Turnover is measured as the fair value of the consideration received or receivable and represents amounts due for goods and services provided in the normal course of business, net of discounts, VAT and other sales related taxes. Calculating the fair value of turnover typically does not require a significant level of judgement, the exceptions to this are the following areas (further detail of which is provided in note 3):

- Uncontracted variations or claims.
- Payment by results contracts.
- Long-term project based contracts.

Turnover is deferred when payment is received in advance of performing the related service of delivering the associated goods, and released when the relevant contractual commitment is fulfilled.

Turnover on repeat service-based contracts is recognised as services are provided. Where initial contract costs (phase in costs) are paid for by the customer, turnover is recognised when the related costs are incurred.

The Company has a number of long-term contracts for the provision of complex, project-based services. Where the outcome of such long-term project-based contracts can be measured reliably, income and costs are recognised by reference to the stage of completion of the contract activity at the balance sheet date in accordance with IAS 18 *Revenue* and IAS 11 *Construction Contracts*. This is normally measured by the proportion of contract costs incurred for work performed to date compared to the estimated total contract costs, but where a more accurate basis is available that alternative methodology is used. Contract costs include a rational allocation of overheads.

Where the outcome of a long-term project-based contract cannot be estimated reliably, contract turnover is recognised to the extent that it is probable that contract costs will be recovered. Contract costs are recognised as expenses in the period in which they are incurred.

When it is probable that the total contract costs will exceed total contract income, the expected loss is recognised as an expense immediately. Such amounts are not discounted.

Sales of goods are recognised when goods are delivered and title has passed.

Dividend income

Dividend income from investments is recognised when the right to receive payment has been established.

Interest income

Interest income is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount.

Tax

The tax expense represents the sum of current tax expense and deferred tax expense.

Current tax expense is based on taxable profit for the year. Taxable profit differs from net profit as reported in the profit and loss account because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Company's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is provided, using the liability method, on temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for accounting purposes.

Deferred tax liabilities are generally recognised for all taxable temporary differences. Deferred tax assets are generally recognised for all deductible temporary differences, carry forward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profits will be available against which these items can be utilised.

Deferred tax assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition of an asset and liability in a transaction other than a business combination and, at the time of the transaction, affects neither the taxable profit nor the accounting profit.

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2015

Tax continued

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

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be utilised.

Deferred tax is measured at the tax rates that are expected to apply in the period when the liability is settled or the asset is realised, based upon tax rates and legislation that have been enacted or substantively enacted at the balance sheet date. Deferred tax is charged or credited in the profit and loss account, except where it relates to items charged or credited directly to equity, in which case the deferred tax is also recognised in equity.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same tax authority where the Company intends to settle its current tax assets and liabilities on a net basis.

Foreign currencies

Transactions in currencies other than 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 net profit or loss for the period, except for exchange differences arising on non-monetary assets and liabilities where the changes in fair value are recognised directly in equity through the statement of comprehensive income (SOCI). Income and expense for overseas operations are translated at the average exchange rates for the period.

Goodwill

Goodwill arising on the acquisition of businesses is capitalised on the balance sheet in accordance with IAS 38 *Intangible Assets* and IFRS 3 *Business Combinations*. Goodwill represents the excess of consideration paid over the fair value of assets acquired. Goodwill is reviewed for impairment at least annually. Any impairment is recognised immediately in the profit and loss account and is not subsequently reversed. On disposal the attributable amount of goodwill is included in the determination of the profit or loss on disposal.

Property, plant and equipment

Assets held for use in the rendering of services, or for administrative purposes, are stated in the balance sheet at cost, net of accumulated depreciation and any provision for impairment. Assets are grouped into classes of similar nature and use and separately disclosed except where this is not material.

Depreciation is provided on a straight-line basis at rates designed to reduce the assets to their residual value over their estimated useful lives.

The principal annual rates used are:

Freehold buildings	2.5%
Short-leasehold assets	The higher of 10% or the rate produced by the lease term
Machinery	15% - 20%
Motor vehicles	10% - 50%
Furniture	10%
Office equipment	20% - 33%
Leased equipment	The higher of the rate produced by the lease term or useful life

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. Given that there is limited history of material gains or losses on disposal of fixed assets, the level of judgement involved in determining the depreciation rates is not considered to be significant.

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2015

Other intangible assets

Material intangible assets are grouped into classes of similar nature and use and separately disclosed. Other intangible assets are amortised from the date of completion.

Licences comprise premiums paid for the acquisition of licences. These are amortised on a straight-line basis over the life of the licence.

Software represents computer systems and processes used by the Company in order to generate future economic value through normal business operations. The underlying assets are amortised over the period from which the Company expects to benefit, which is typically between three and eight years.

Development expenditure is capitalised as an intangible asset only if all of certain conditions are met, with all research costs and other development expenditure being expensed when incurred. The period of expected benefit, and therefore period of amortisation, is typically between three and eight years. The capitalisation criteria are as follows:

- an asset is created that can be separately identified, and which the Company intends to use or sell;
- the finalisation of the asset is technically feasible and the Company has adequate resources to complete its development for use or sale;
- it is probable that the asset created will generate future economic benefits; and
- the development cost of the asset can be measured reliably.

Whilst licence assets will arise from specific transactions and can be clearly identified, both software and development type assets can include a significant level of internal costs in determining whether these are directly incremental to the creation of a specific asset requires a high level of judgement (further detail of which is provided in note 3).

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 received 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 the scheme net liabilities on the date that the contracts commence and are amortised on a straight line basis over the contract life.

Trademarks, licences and customer related intangible assets have a finite useful life and are carried at cost less accumulated amortisation and any accumulated impairment losses.

Asset impairment

The Company reviews the carrying amounts of its tangible and intangible assets (including goodwill) at each reporting period, together with any other assets under the scope of IAS 36 *Impairment of Assets*, in order to assess whether there is any indication that those assets have suffered an impairment loss. As the impairment of the assets has been identified as both a key source of estimation uncertainty and a critical accounting judgement, further details around the specific judgements and estimates can be seen in note 3.

If any indication of impairment exists, the recoverable amount of the asset is estimated in order to determine if there is any impairment loss. Goodwill is assessed for impairment annually, irrespective of whether there are any indicators of impairment. Where the asset does not generate cash flows that are independent from other assets, the Group estimates the recoverable amount of the CGU to which the asset belongs.

Recoverable amount is defined as the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value with reference to pre-tax discount rates that reflect the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

If the recoverable amount is estimated to be less than the carrying amount of the asset, the carrying amount is impaired to its recoverable amount. Impairment losses recognised in respect of CGUs are allocated first to reduce the carrying amount of any goodwill allocated to the CGU and then to reduce the carrying amount of the other assets in the CGU on a pro-rata basis.

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2015

Asset Impairment *continued*

An impairment loss in respect of goodwill is not reversed. In respect of other assets, impairment losses recognised in prior periods are assessed at each reporting date for indications that the loss has decreased or no longer exists. Where an impairment loss subsequently reverses, the carrying amount is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, had no impairment loss been recognised in prior years.

Impairment losses and reversals are recognised immediately within administrative expenses within the profit and loss account unless it is considered to be an exceptional item.

Investments in subsidiaries

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

Investments in joint ventures

A joint venture is an arrangement whereby the owning parties have joint control and rights over the net assets of the arrangement. The Company's investments in joint ventures are incorporated using the equity method of accounting.

Under the equity method, an investment in an associate or a joint venture is initially recognised in the consolidated balance sheet at cost and adjusted thereafter to recognise the Company's share of the profit or loss and other comprehensive income of the associate or joint venture. Any excess of the cost of acquisition over the Company's share of net fair value of the identifiable assets, liabilities and contingent liabilities of the joint venture recognised at the date of acquisition is recognised as goodwill. Goodwill is included within the carrying value amount of the investment and is assessed for impairment as part of that investment. Any excess of the Company's share of the net fair value of the identifiable assets, liabilities and contingent liabilities over the cost of acquisition, after reassessment, is recognised immediately in profit or loss. Where the Company transacts with a joint venture, profits and losses are eliminated to the extent of the Company's interest in that arrangement.

Determining whether joint control exists requires a level of judgement, based upon specific facts and circumstances which exist at the year end. Details of the unconsolidated joint ventures are provided in note 17.

Bid costs and phase in 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, being the point at which the Company has at least reached preferred bidder status. Bid costs incurred after this point are then capitalised within trade and other receivables. On contract award these bid costs are amortised through the profit and loss account over the contract period by reference to the stage of completion of the contract activity at the balance sheet date. Bid costs are only capitalised to the extent that it is expected that the related contract will generate sufficient future economic benefits to at least offset the amortisation charge.

Phase in costs that are incremental and directly related to the initial set-up of contracts are capitalised within trade and other receivables and are recognised on a straight line basis over the life of the contract, except where they are specifically reimbursed as part of the terms of the contract when they are recognised as turnover.

Determining whether bid and phase in costs are recoverable involves a high level of judgement as it requires a forecast to be prepared for the expected future profitability of the contract, taking into account the likely future costs and revenues associated with the services not yet performed.

Stocks

Stocks are stated at the lower of cost and net realisable value and comprise service spares, parts awaiting installation and work in progress for projects undertaken for customers where payment is received on completion. Cost comprises direct materials and, where applicable, direct labour costs that have been incurred in bringing the stocks to their present location and condition.

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2015

Trade receivables

Trade receivables are recognised initially at cost (being the same as fair value) and subsequently at amortised cost less any provision for impairment, to ensure that amounts recognised represent the recoverable amount.

A provision for impairment arises when there is evidence that the Company will not be able to collect amounts due, which is achieved by creating an allowance for doubtful debts recognised in the profit and loss account within administrative expenses. Determining whether a trade receivable is impaired requires judgement to be applied based on the information available at each reporting date. Key indicators of impairment include disputes with customers over commercial positions, or where debtors have significant financial difficulties such as historic default of payments or information that suggests bankruptcy or financial reorganisation are a reasonable possibility. The majority of contracts entered into by the Company are with government organisations or are blue chip private sector companies and therefore historic levels of default are relatively low and as a result the risks associated with this judgement are not considered to be significant.

When a trade receivable is expected to uncollectible, it is written off against the allowance for doubtful debts. Subsequent recoveries of amounts previously provided for or written off are credited against administrative expenses.

Cash and cash equivalents

Cash and cash equivalents comprise cash in hand and balances with banks and similar institutions, which are readily convertible to known amounts of cash and which are subject to insignificant changes in value and have a maturity of three months or less from the date of acquisition.

Provisions

Provisions are recognised when the Company has an obligation to make a cash outflow as a result of a past event. Provisions are measured at the best estimate of the expenditure required to settle the obligation at the balance sheet date when settlement is considered to be likely.

Onerous contract provisions (OCPs) arise when the unavoidable costs of meeting contractual obligations exceed the remuneration expected to be received. Unavoidable costs include total contract costs together with a rational allocation of shared costs that can be directly linked to fulfilling contractual obligations which have been systematically allocated to OCPs on the basis of key cost drivers except where this is impracticable, where contract revenue is used as a proxy to activity. The provision is calculated as the lower of termination costs payable for an early exit and the expected loss over the remaining contract period. Where a customer has an option to extend a contract and it is likely that such an extension will be made, any loss expected to be made during the extension period, is included within the calculation. However, where a profit can be reasonably expected in the extension period, no credit is taken on the basis that such profits are uncertain given the potential for the customer to either not extend or offer an extension under lower pricing terms. Further details of the judgements can be seen in note 3.

Leases

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

Assets held under finance leases are recognised as assets of the Company at fair value or, if lower, at the present value of 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 to the profit and loss account, 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.

Total rentals payable under operating leases are charged to the profit and loss account on a straight-line basis over the term of the relevant lease.

Serco Limited
Notes to the Financial Statements for the Year Ended 31 December 2015

Loans

Loans are stated at amortised cost using the effective interest-rate method. Accrued interest is recorded separately from the associated borrowings with current liabilities.

Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sale, are added to the cost of those assets, until such time as the assets are substantially ready for their intended use or sale.

All other borrowing costs are recognised as an expense in the period in which they are incurred.

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 actuarial cost 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 SOCI.

Both current and past service costs are the amounts recognised in the profit and loss account, reflecting the expense associated with the individuals. Current service cost represents the increase in the present value of the scheme 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. Gains and losses on curtailments or settlements are recognised in the profit and loss account in the period in which the curtailment or settlement occurs.

The retirement benefit obligation recognised in 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 (which is only recognised to the extent that the Company has an unconditional right to receive it) and reductions in future contributions to the scheme. To the extent that an economic benefit is available as a reduction in future contributions and there is a minimum funding requirement required of the Company, the economic benefit available as a reduction in contributions is calculated as the present value of the estimated future service cost in each year, less the estimated minimum funding contributions required in respect of the future accrual and benefits in that year.

Calculation of the amounts recognised in the financial statements in respect of defined benefit pension schemes requires a high level of judgement, as further explained in note 3.

Multi-employer pensions

Multi-employer pension schemes are classified as either a defined contribution pension scheme or a defined benefit pension scheme under the terms of the scheme. The Company accounts for these schemes as if they were defined contribution schemes in accordance with IAS 19 where the legal responsibility for settlement resides in another group entity and there is no contractual agreement for charging the net defined benefit cost associated with the Company.

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2015

Business combinations

Acquisitions of subsidiaries and businesses are accounted for using the acquisition method. The consideration for each acquisition is measured at the aggregate of the fair values, at the date of exchange, of assets given, liabilities incurred or assumed, and equity instruments issued by the Company in exchange for control of the acquiree. Acquisition related costs are recognised in profit or loss as incurred.

Where applicable, the consideration for the acquisition includes any asset or liability resulting from a contingent consideration arrangement, measured at its acquisition date fair value. Subsequent changes in fair values are adjusted against the cost of acquisition where they qualify as measurement period adjustments (which is subject to a maximum of one year). All other subsequent changes in the fair value of contingent consideration classified as an asset or liability are accounted for in accordance with the relevant accounting standards. Changes in the fair value of contingent consideration classified as equity are not recognised.

The acquiree's identifiable assets, liabilities and contingent liabilities that meet the conditions for recognition under IFRS 3 (2008) *Business Combinations* are recognised at their fair value at the acquisition date, except where a different treatment is mandated by another standard.

Assets classified as held for sale

Non-current assets and disposal groups are classified as held for sale if their carrying value will be recovered through a sale transaction rather than through continuing use. This condition is only met when the sale is highly probable, the asset or disposal group is available for immediate sale in its present condition and the Company expects the sale to be completed within one year. Amounts classified as held for sale are measured as the lower of the carrying amount and fair value less cost to sell.

Assessing whether the criteria are met requires judgement, in particular with regards to whether the subject of the assessment is in a suitable condition for sale. In addition, the calculation of the value of any goodwill to be allocated to the sale is dependent on an assessment of the likely sales proceeds and the likely structure of the transaction.

Derivative financial instruments and hedging activities

The Company enters into a variety of derivative financial instruments to manage the exposure to interest rate, foreign exchange risk and price risk, including currency swaps, foreign exchange forward contracts, interest rate swaps and commodity future contracts. Further details of derivative financial instruments are given in note 27.

Derivatives are initially recognised at fair value at the date a derivative contract is entered into and are subsequently remeasured to their fair value at each balance sheet date. The resulting gain or loss is recognised in profit or loss immediately unless the derivative is designated and effective as a hedging instrument, in which event the timing of the recognition in profit or loss depends on the nature of the hedge relationship. The Company designates certain derivatives as either hedges of the fair value of recognised assets or liabilities or firm commitments (fair value hedges) or hedges of highly probable forecast transactions or hedges of firm commitments (cash flow hedges).

At the inception of the hedge relationship, the Company documents the relationship between the hedging instrument and the hedged item, along with its risk management objectives and its strategy for undertaking the various hedge transactions. Both at the inception of the hedge and on a periodic basis, the Company assesses whether the hedging instrument that is used in a hedging relationship is highly effective in offsetting changes in fair values or cash flows of the hedged item.

A derivative is presented as a non-current asset or a non-current liability if the remaining maturity of the instrument is more than 12 months and it is not expected to be realised or settled within 12 months. Derivatives, which mature within 12 months, are presented as current assets or current liabilities.

Details of the fair values of the derivative instruments used for hedging purposes and movements in the hedging and translation reserve in equity are detailed in the SOCI and described in note 27.

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2015

Fair value hedges

Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in profit or loss immediately, together with any changes in the fair value of the hedged item that is attributable to the hedged risk. The change in the fair value of the hedging instrument and the change in the hedged item attributable to the hedged risk are recognised in the line of the profit and loss account relating to the hedged item.

Cash flow hedges

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges are deferred in equity. The gain or loss relating to the ineffective portion is recognised immediately in profit or loss. Amounts accumulated in equity are reclassified to profit or loss in the periods when the hedged item affects profit or loss, in the same line of the profit and loss account as the recognised hedge item.

Hedge accounting is discontinued when the Company de-designates the hedging relationship, the hedging instrument expires or is sold, terminated, exercised, or no longer qualifies for hedge accounting. Any cumulative gain or loss deferred in equity at that time remains in equity and is recognised when the forecast transaction is ultimately recognised in profit or loss. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was deferred in equity is recognised immediately in profit or loss.

Hedges of net investments in foreign operations

Hedges of net investments in foreign operations are accounted for similarly to cash flow hedges. Any gain or loss on the hedging instrument relating to the effective portion of the hedge is recognised in equity and accumulated in the hedging and translation reserve. The gain or loss relating to the ineffective portion is recognised immediately in profit or loss and is included in the 'net exchange gain/loss on translation of foreign operations' line item.

Gains and losses on the hedging instrument relating to the effective portion of the hedge accumulated in the foreign currency translation reserve are reclassified to profit or loss in the same way as exchange differences relating to the foreign operations.

Net investments in foreign operations

Exchange differences arising on monetary items that form part of the Company's net investment in foreign operations are initially recognised in equity and accumulated in the hedging and translation reserve and reclassified from equity to profit or loss on disposal of the net investment.

Dividends payable

Dividends are recorded in the Company's financial statements in the period in which they are declared, appropriately authorized and no longer at the discretion of the Company.

Share-based payments

The ultimate parent, Serco Group plc, makes equity-settled share-based payments to certain employees and operates an HMRC approved Save As You Earn (SAYE) 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 Company's estimate of shares that will eventually vest. SAYE options are treated as cancelled when employees cease to contribute to the scheme, resulting in an acceleration of the remainder of the related expense.

Where the fair value of share options requires the use of a valuation model, fair value is measured by use of the Binomial Lattice or Monte Carlo Simulation models depending on the type of scheme. Further details can be found in note 38 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 behavioral considerations. Where relevant, the value of the option has also been adjusted to take account of market conditions applicable to the option.

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2015

3 Critical accounting judgments and key sources of estimation uncertainty

In the process of applying the Company's accounting policies, which are described in note 2 above, management has made the following judgments that have the most significant effect on the amounts recognised in the financial statements. As described below, many of these areas of judgement also involve a high level of estimation uncertainty.

Provisions for Onerous Contracts

Determining whether provisions are required for loss making contracts requires significant judgements to be made regarding the ability of the company to maintain or improve operational performance. Judgements can also be made regarding the outcome of matters dependent on the behaviour of the customer in question or other parties involved in delivering the contract.

The level of uncertainty in the estimates made, either in determining whether a provision is required, or in the calculation of a provision booked, is linked to the complexity of the underlying contract and the form of service delivery.

In the current year material revisions have been made to historic provisions, which have led to a charge to contract provisions of £51.5m (excluding £5.5m in respect of businesses held for sale) and releases of £33.1m (excluding £0.5m in respect of businesses held for sale). All of these revisions have resulted from triggering events in the current year, either through changes in contractual positions or changes in circumstances which could not have been reasonably foreseen at the previous balance sheet date. To mitigate the level of uncertainty in making these estimates Management regularly compares actual performance of the contracts against previous forecasts and considers whether there have been any changes to significant judgements. A detailed bottom up review of the provisions is performed as part of the Company's formal annual budgeting process.

Impairment of Assets

Identifying whether there are indicators of impairment for assets involves a high level of judgement and a good understanding of the drivers of value behind the asset. At each reporting period an assessment is performed in order to determine whether there are any such indicators, which involves considering the performance of our business and any significant changes to the markets in which we operate. The total value of assets which are covered by this assessment process (after previous impairments) is £1,232.5m (2014: £1,025.0m), which is the maximum exposure related to this judgement. We mitigate the risk associated with this judgement by putting in place processes and guidance for the finance community and internal review procedures.

Determining whether assets with impairment indicators require an actual impairment involves an estimation of the expected value in use of the asset (or CGU to which the asset relates). The value in use calculation involves an estimation of future cash flows and also the selection of appropriate discount rates, both of which involve considerable judgement. The future cash flows are derived from approved forecasts, with the key assumptions being revenue growth, margins and cash conversion rates. Discount rates are calculated with reference to the specific risks associated with the assets and are based on advice provided by external experts. Our calculation of discount rates are performed based on a risk free rate of interest appropriate to the geographic location of the cash flows related to the asset being tested, which is subsequently adjusted to factor in local market risks and risks specific to the Company and the asset itself. Discount rates used for internal purposes are post tax rates, however for the purpose of impairment testing in accordance with IAS 36 Impairment of Assets we calculate a pre tax rate based on post tax targets.

Other than with respect to assets held for sale, there was no impairment of goodwill during the year (2014: £355.3m) nor of property, plant and equipment (2014: £27.5m). A charge of £9.0m (2014: £23.1m) was recognised in respect of certain intangible assets. Further details of these impairments can be seen in notes 15 and 16 to the financial statements. Assets held for sale are stated after an impairment charge of £6.5m (2014: £0.3m).

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2015

Valuation of assets held for sale

Held for sale assets are measured at the lower of their carrying amount and fair value less costs to sell and up to the point a sales price has been formally agreed a level of judgement is required in assessing the value of these assets. All assets included as held for sale are based on the latest offer received which is likely to be acceptable to us and the customer of the affected contract, but unforeseen events may lead to a change in this price prior to completion of the transaction. The total value of assets held for sale is a liability of £14.8m (2014: liability £1.6m) which is stated after an impairment charge for the year of £6.5m (2014: £0.3m).

Revenue Recognition

Calculating the fair value of the Company's revenue typically does not require a significant level of judgement, the exceptions to this are the following areas:

- **Uncontracted variations or claims.** Where work has been performed outside of the normal contracting framework at the request of the customer or a claim has been made for work performed but in dispute, judgement is required in order to determine whether there is sufficient certainty that the Company will be financially compensated. Revenue is only recognised to the extent that they have been orally agreed by the customer or are virtually certain of being received.
- **Payments by results contracts.** When returns are directly linked to performance through cost savings or other customer driven key performance indicators over a period of time an estimate is made of the likelihood of achieving the necessary level of performance when the period covers a financial year end. Revenue is only recognised when we can be reasonably certain of achieving the required level of performance.
- **Long-term contracts.** Revenue and profit is recognised for certain long-term project-based contracts based on the stage of completion of the contract activity. The assessment of the stage of completion requires the exercise of judgement and is measured by the proportion of costs incurred compared to estimated whole-life contract costs, except where whole life contract costs exceed the contract value, in which case the excess is expensed immediately.

Separation of Income Statement Items from Underlying Results

IAS 1 requires material items to be disclosed separately in a way that enables users to assess the quality of a company's profitability. In practice, these are commonly referred to as "exceptional" items, but this is not a concept defined by IFRS and therefore there is a level of judgment involved in determining what to include in underlying profit. We consider items which are material, non-recurring and outside of the normal operating practice of the Company to be suitable for separate presentation.

Retirement Benefit Obligations

The calculation of retirement benefit obligations is dependent on material key assumptions including discount rates, mortality rates, inflation rates and future contribution rates (see note 23). The value of net retirement benefit obligations at the balance sheet date is an asset of £115.9m (2014: £126.8m). Details of the impact of changes in assumptions relating to retirement benefit obligations are disclosed in note 23.

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2015

4 Turnover

The analysis of the Company's turnover for the year from continuing operations is as follows:

	2015 £ m	2014 £ m
Rendering of services	1,531.4	1,729.0
Turnover from long-term project-based contracts	7.3	20.5
Turnover as disclosed in the profit and loss account	1,538.7	1,749.5
Interest receivable and similar income (note 10)	21.1	5.3
Total income as defined in IAS 18	1,559.8	1,754.8

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 Strategic Report. The Company's reportable operating segments are as follows:

UK Central Government - Frontline services for sectors including Defence, Justice & Immigration and Transport delivered to UK Government and devolved authorities;

UK Local and Regional Government - Services for sectors including Health, Local Government Direct Services, Citizen Services and BPO services delivered to UK public sector customers;

Middle East - Frontline services for sectors including Defence, Transport and Health in the Middle East region;

Global Services - BPO services for private sector customers in the UK.

An analysis of turnover by class of business is given below:

	2015 £ m	2014 £ m
UK Central Government	705.1	870.9
UK Local and Regional Government	731.0	776.6
Middle East	80.7	75.2
Global Services	21.9	26.8
	1,538.7	1,749.5

An analysis of turnover by geographical location is given below:

	2015 £ m	2014 £ m
United Kingdom	1,429.0	1,658.4
Other	109.7	91.1
	1,538.7	1,749.5

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 2015

5 Exceptional net (loss)/profit on disposal of operations

During the year the Company generated the following net exceptional (loss)/profit on disposal of operations:

	2015 £ m	2014 £ m
Impairment of loan receivable in respect of prior year disposal	-	(4.6)
Prior period technical services disposal adjustment	-	5.4
Costs in connection with the disposal of part of the UK onshore business	(5.0)	-
Adjustment to prior period disposal of Occupational Health business	0.7	-
Net (loss)/profit on disposal of operations	(4.3)	0.8

In July 2015 the Company completed the sale of part of its UK onshore business, resulting in costs of £5.0m in connection with the write off of assets. The remaining UK onshore business is expected to be sold in 2016 and has therefore been treated as held for sale. This was partially offset by a gain of £0.7m recognised in the period in respect of an adjustment relating to the disposal of the Occupational Health business in the prior period.

6 Other exceptional operating items

Exceptional items are non-recurring items of financial performance that are outside of normal practice and material to the results of the Company either by virtue of size or nature. These items require separate disclosure on the face of the profit and loss account to assist in the understanding of the underlying performance of the Company.

	2015 £ m	2014 £ m
Costs associated with UK Government reviews	-	9.2
UK frontline clinical health contract provisions	(2.8)	16.1
Provision for settlement relating to pension deficit funding	-	(0.2)
Restructuring costs	8.8	12.9
Impairment of goodwill (note 15)	-	355.3
Impairment of assets transferred to held for sale	24.4	-
Exceptional operating items	30.4	393.3

In 2015 the exit of the UK Frontline Clinical Health contracts was completed with the Cornwall Out of Hours contract exited in May and the Suffolk Community Healthcare contract exited in September. On completion of the contract exits, onerous contract provisions of £2.8m, for which the charges were recorded as exceptional costs and that are no longer expected to be utilised, were released as credits through exceptional items.

In 2015, a charge of £8.8m (2014: £12.9m) arose in relation to the restructuring programme resulting from the Strategy Review. This included redundancy payments, provisions, external advisory fees and other incremental costs.

£24.4m of the charge recognised in the year relates to the impairment of assets in connection with the BPO operations transferred to held for sale.

Serco Limited
Notes to the Financial Statements for the Year Ended 31 December 2015

7 Operating loss

Operating loss is stated after charging/(crediting):

	2015	2014
	£ m	£ m
Research and development costs	4.3	2.5
Operating lease expense - property	21.8	23.3
Operating lease expense - plant and machinery	22.3	23.9
Staff costs (note 8)	699.6	786.4
Impairment of other goodwill (note 15)	-	355.3
Amortisation of other intangible assets (note 15)	21.9	24.4
Impairment of other intangible assets (note 15)	9.0	23.1
Depreciation of tangible fixed assets - owned (note 16)	3.8	12.2
Depreciation of tangible fixed assets - leased (note 16)	1.2	9.7
Impairment of tangible fixed assets (note 16)	-	27.5
Impairment of debtors	1.4	40.9
Write off of stocks	-	13.6
Net loss/(profit) on disposal of operations (note 5)	4.3	(0.8)
Other exceptional operating items excluding impairment of goodwill (note 6)	30.4	38.0
Foreign exchange losses	0.4	1.5

Amounts payable to Deloitte LLP and their associates by the Company in respect of audit and non-audit services are shown below.

	2015	2014
	£ m	£ m
Year ended 31 December		
Fees payable to the Company's Auditor for the audit of the Company's annual accounts	0.2	0.3
- Audit-related assurance services	0.2	0.2
- Other taxation advisory services	0.2	0.4
- Other services	-	0.2
Total non-audit fees	0.4	0.8

8 Staff costs

The average number of persons employed by the Company (including directors) during the year was 22,654 (2014: 23,899). The aggregate payroll costs (including directors' remuneration) were as follows:

	2015	2014
	£ m	£ m
Wages and salaries	601.8	668.6
Social security costs	51.4	61.9
Staff pensions	40.9	52.8
Share-based payment expenses	5.5	3.1
	699.6	786.4

The share-based payment expense for the year ended 31 December 2015 arose from equity-settled share-based payment charges related to the following plans in Serco Group plc share schemes: the Performance Share Plan (PSP), the Long Term Incentive Scheme (LTIS) and Long Term Incentive Plan (LTIP), the Sharesave 2012 and the Deferred Bonus Plan. The majority of the charge in the year related to the PSP and the only new awards granted in the year related to the PSP.

Under the PSP, eligible employees have been granted options with an exercise price of two pence. Awards vest after the performance period of three to five years and are subject to the achievement of four performance measures with the exception of new non-performance awards granted in 2014. These non-performance options are only subject to continued employment on vesting dates which vary from six months to three years after the grant dates.

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2015

8 Staff costs *continued*

On the performance related awards, the primary performance measure is TSR and the second performance measure is based on EPS growth. Two additional measures on new grants in 2014 were Absolute Share Price and Strategic Objectives. If the options remain unexercised after a period of ten years from the date of grant, the options expire.

The options outstanding at 31 December 2015 had a weighted average contractual life of 1.6 years (2014: 2.7 years). The exercise prices for options outstanding at 31 December 2015 ranged from £3.39 to £4.55 (2014: £3.39 to £4.55).

The weighted average share price at the date of exercise approximates to the weighted average share price during the year, which was £3.30 (2014: £3.45).

9 Directors' remuneration

The directors' remuneration for the year was as follows:

	2015 £ m	2014 £ m
Aggregate emoluments	1.4	1.5

Which include:

Aggregate emoluments of compensation to directors in respect of loss of office £nil (2014: £0.2m).

During the year the number of directors who were receiving benefits and share incentives was as follows:

	2015 No.	2014 No.
Received or were entitled to receive shares under long-term incentive schemes	6	4
Exercised share options	1	-
Accruing benefits under defined benefit pension scheme	-	-
Accruing benefits under defined contribution pension scheme	-	2

In respect of the highest paid director:

	2015 £ m	2014 £ m
Remuneration	0.5	0.5
Company contributions to money purchase pension schemes	-	0.1

During the year the highest paid director received shares under a long-term incentive scheme but no share options were exercised.

10 Interest receivable and similar income

	2015 £ m	2014 £ m
Bank interest receivable	0.1	0.1
Interest receivable from group undertakings	15.9	1.6
Net interest receivable on retirement benefit obligations	4.9	3.0
Other interest receivable	0.2	0.6
	21.1	5.3

11 Interest payable and similar charges

	2015 £ m	2014 £ m
Other interest payable	1.7	2.8
Interest payable to group undertakings	14.2	18.2
Borrowing costs	0.1	0.2
Interest payable under finance leases	2.2	2.8
Movement in discount on provisions	1.7	-
Exceptional finance charges	0.1	-
	20.0	24.0

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2015

12 Tax

Tax on loss on ordinary activities

	Before exceptional items 2015 £ m	Exceptional items 2015 £ m	Total 2015 £ m	2014 £ m
Current tax				
UK corporation tax	-	-	-	-
UK corporation tax adjustment to prior periods	-	-	-	(4.7)
	-	-	-	(4.7)
Foreign tax	0.2	-	0.2	0.4
Total current income tax	0.2	-	0.2	(4.3)
Deferred tax				
Current year	4.3	-	4.3	4.9
Adjustments in respect of prior years	0.2	-	0.2	5.6
Total deferred tax	4.5	-	4.5	10.5
Tax expense in the profit and loss account	4.7	-	4.7	6.2

Factors affecting current tax charge for the year

The tax on loss before tax for the year differs from the standard rate of corporation tax in the UK of 20.25% (2014: 21.5%). The differences are reconciled below:

	Before exceptional items 2015 £ m	Exceptional items 2015 £ m	Total 2015 £ m	2014 £ m
Loss on ordinary activities before tax	(20.1)	(34.8)	(54.9)	(863.2)
Corporation tax at 20.25% (2014: 21.5%)	(4.0)	(7.1)	(11.1)	(185.6)
Expenses not deductible for tax purposes	4.3	0.6	4.9	85.5
Unrelieved tax losses	0.4	6.4	6.8	100.9
Unprovided deferred tax	1.9	0.1	2.0	5.0
Statutory tax benefits	(0.6)	-	(0.6)	(0.5)
Impact of changes in statutory tax rates	2.4	-	2.4	(0.4)
RDEC credit written off	0.1	-	0.1	-
Irrecoverable overseas tax	-	-	-	0.4
Adjustment in respect of prior years	0.2	-	0.2	0.9
Total tax charge on loss on ordinary activities	4.7	-	4.7	6.2

Serco Limited
Notes to the Financial Statements for the Year Ended 31 December 2015

13 Deferred tax

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

	2015 £ m	2014 £ m
At 1 January	10.5	34.1
Arising on disposal of operations	-	-
Deferred tax credited/(charged) to profit and loss account	(4.2)	(10.5)
Items taken directly to equity - hedging and translation reserve	-	-
Items taken directly to equity - share-based payments reserve	-	0.5
Items taken directly to equity - retirement benefit obligations reserve	4.2	(13.6)
At 31 December	10.5	10.5

Of the £4.5m deferred tax charged to the profit and loss account, £0.2m has been credited to cost of sales and £0.1m has been credited to intangible fixed assets in respect of the Research & Development Expenditure Credit (RDEC), rather than deferred tax on the balance sheet.

	2015 £ m	2014 £ m
Difference between accumulated depreciation and amortisation and capital allowances	7.7	12.7
Share based payments and employee benefits	0.8	0.9
Movement in retirement benefit obligations	(20.4)	(24.5)
Other temporary differences	22.4	21.4
	10.5	10.5

Unprovided deferred tax

	2015 £ m	2014 £ m
Temporary differences on assets/liabilities	14.2	11.4
Share based payments and employee benefits	0.4	0.2
Other temporary differences	91.4	94.3
	106.0	105.9

14 Equity dividends

	2015 £ m	2014 £ m
Equity dividend of £nil (2014: £nil) per ordinary share	-	-

Serco Limited
Notes to the Financial Statements for the Year Ended 31 December 2015

15 Goodwill and other intangible assets

	Goodwill £ m	Licences, software and development expenditure £ m	Pension related intangibles £ m	Total £ m
Cost				
At 1 January 2015	434.3	197.4	6.2	637.9
Additions from internal development	-	19.4	-	19.4
Additions from external acquisition	-	3.5	-	3.5
Disposals	-	(96.0)	(6.2)	(102.2)
Reclassification to held for sale assets	-	(2.5)	-	(2.5)
Reclassification to property, plant and equipment	-	(0.3)	-	(0.3)
Foreign exchange movements	-	0.2	-	0.2
At 31 December 2015	434.3	121.7	-	556.0
Accumulated amortisation				
At 1 January 2015	434.3	131.7	6.2	572.2
Impairment	-	9.0	-	9.0
Amortisation charge - internal development	-	18.6	-	18.6
Amortisation charge - external	-	3.1	-	3.1
Disposals	-	(91.3)	(6.2)	(97.5)
Reclassification to held for sale assets	-	(2.0)	-	(2.0)
Reclassification to property, plant and equipment	-	(0.3)	-	(0.3)
Foreign exchange movements	-	0.2	-	0.2
At 31 December 2015	434.3	69.0	-	503.3
Net book value				
At 31 December 2015	-	52.7	-	52.7
At 31 December 2014	-	65.7	-	65.7

The total net book value of intangible fixed assets held by the Company at 31 December 2015 amounts to £52.7m (2014: £66.1m) and includes £52.7m (2014: £65.7m) shown above and £nil (2014: £0.4m) included within amounts held for sale on the balance sheet.

The net book value of intangible fixed assets has been reduced by £0.4m in respect of research & development expenditure credits (RDEC).

Included in licences, software and development expenditure is an amount of £11.8m (2014: £15.1m) in respect of leased intangibles.

The net book value of internally generated intangible assets at 31 December 2015 was approximately £19.3m (2014: £28.0m) in development expenditure and £26.6m (2014: £28.1m) for software.

Serco Limited
Notes to the Financial Statements for the Year Ended 31 December 2015

16 Property, plant and equipment

	Freehold buildings £ m	Short-leasehold assets £ m	Machinery, motor vehicles, furniture and equipment £ m	Total £ m
Cost				
At 1 January 2015	3.7	24.3	72.5	100.5
Additions	-	1.1	2.8	3.9
Disposals	(0.1)	(8.2)	(10.5)	(18.8)
Reclassifications to intangible fixed assets	-	0.4	(0.1)	0.3
Reclassification (to)/from held for sale assets	0.5	(3.1)	58.6	56.0
Foreign exchange movements	0.1	(0.1)	0.1	0.1
At 31 December 2015	4.2	14.4	123.4	142.0
Accumulated depreciation				
At 1 January 2015	2.1	19.0	62.8	83.9
Charge for the year	0.1	1.3	3.6	5.0
Impairment	-	-	-	-
Disposal	-	(7.8)	(9.0)	(16.8)
Reclassifications to intangible fixed assets	-	0.4	-	0.4
Reclassification (to)/from held for sale assets	0.2	(2.6)	23.4	21.0
Foreign exchange movements	(0.2)	-	0.1	(0.1)
At 31 December 2015	2.2	10.3	80.9	93.4
Net book value				
At 31 December 2015	2.0	4.1	42.5	48.6
At 31 December 2014	1.6	5.3	9.7	16.6

The carrying amount of the Company's Machinery, motor vehicles, furniture and equipment includes an amount of £32.1m (2014: £40.3m) in respect of assets held under finance leases, of which £nil (2014: £37.1m) is classified as held for sale.

The carrying amount of the Company's Short-leasehold assets includes an amount of £0.2m (2014: £0.2m) in respect of assets held under finance leases, of which £nil (2014: £0.2m) is classified as held for sale.

Serco Limited
Notes to the Financial Statements for the Year Ended 31 December 2015

17 Investments held as fixed assets

	Subsidiaries £ m	Joint ventures £ m	Total investments £ m
Cost			
At 1 January 2015 and at 31 December 2015	3.5	5.5	9.0

Details of undertakings

The companies listed below are the subsidiaries and joint venture undertakings of Serco Limited. The percentage of equity capital directly or indirectly held by the Company is shown below. The companies are incorporated and principally operate in the United Kingdom.

Undertaking	Country of incorporation	Proportion of voting rights and shares held	
		2015	2014
Subsidiary undertakings			
Serco Geografix Limited	United Kingdom	100%	100%
Serco Environmental Services Limited (incorporated June 2014)	United Kingdom	100%	0%
Joint ventures			
Viapath Group LLP	United Kingdom	33%	33%
Viapath Analytics LLP ¹	United Kingdom	33%	33%
Viapath Services LLP ¹	United Kingdom	33%	33%
Agbar Serco Technology Services Limited ²	United Kingdom	50%	50%
Service Glasgow LLP	United Kingdom	50%	50%

¹ Indirect subsidiaries of Serco Limited

² In liquidation as at 31 December 2015

18 Stocks

	2015 £ m	2014 £ m
Service spares	3.8	10.5
Parts awaiting installation	3.5	2.0
Work in progress	2.3	2.2
	9.6	14.7

Total stocks held by the Company at 31 December 2015 amount to £9.6m (2014: £15.6m) and include £9.6m (2014: £14.7m) shown above and £nil (2014: £0.9m) included within amounts held for sale on the balance sheet.

There is no material difference between the value of stocks and their replacement cost.

Serco Limited
Notes to the Financial Statements for the Year Ended 31 December 2015

19 Debtors

a) Amounts falling due within one year

	2015	2014
	£ m	£ m
Trade debtors	57.9	63.3
Amounts recoverable on long-term contracts	-	0.9
Amounts owed by group companies	752.7	228.0
Other debtors	20.0	25.5
Prepayments and accrued income	139.1	138.6
	<u>969.7</u>	<u>456.3</u>

Total debtors due within one year held by the Company at 31 December 2015 amount to £979.0m (2014: £476.4m) and include £969.7m (2014: £456.3m) shown above and £9.3m (2014: £20.1m) included within amounts held for sale on the balance sheet.

The trade debtors balance is stated after an allowance for doubtful debts of £9.6m (2014: £12.1m). Movements on the Company's allowance for doubtful debts are as follows:

	2015	2014
	£ m	£ m
At 1 January	12.1	0.3
(Released) / charged to the profit and loss account	(2.4)	11.6
Utilised	(0.7)	(0.1)
Exchange differences	0.5	0.4
Reclassified to held for sale	0.1	(0.1)
	<u>9.6</u>	<u>12.1</u>

The Company has a receivables financing facility of £30.0m (2014: £60m), of which £30.0m had been utilised at 31 December 2015 (31 December 2014: £32.8m utilised). This is a UK facility provided on a non-recourse basis with all relevant debtors requiring approval in advance by the facility provider.

The amounts recoverable on long-term contracts balance at 31 December 2015 included £74.6m (2014: £72.8m) of long term project-based contracts costs incurred plus recognised profits less recognised losses to date and there were £74.6m (2014: £71.9m) of progress payments. There were £nil (2014: £nil) of contract retentions held by customers.

Deferred bid and phase in costs are held within prepayments and accrued income as due within one year as they are realised as part of the normal operating cycle of the Company.

Amounts owed to group companies include a loan of £452.2m to Serco Holdings Limited, which is repayable on 29 April 2016 and bears interest based on LIBOR plus 2%. All other 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

	2015	2014
	£ m	£ m
Amounts owed by group companies	150.0	474.2
Amounts owed by joint ventures	-	2.5
Other debtors	5.8	4.9
	<u>155.8</u>	<u>481.6</u>

Amounts owed by group companies include a loan of £150.0m to Serco Holdings Limited, which has no fixed repayment date and bears interest based on LIBOR plus 2%. All other 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 2015

20 Creditors: Amounts falling due within one year

	2015 £ m	2014 £ m
Trade creditors	53.5	59.8
Obligations under finance lease and hire purchase contracts	14.2	8.5
Other loans	-	20.3
Amounts owed to group companies	100.7	37.1
Other taxes and social security	27.6	39.7
Other creditors	25.4	31.7
Accruals and deferred income	186.9	234.9
	<u>408.3</u>	<u>432.0</u>

Total creditors due within one year held by the Company at 31 December 2015 amount to £410.3m (2014: £464.5m) and include £408.3m (2014: £432.0m) shown above and £2.0m (2014: £32.5m) included within amounts held for sale on the balance sheet.

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

21 Creditors: Amounts falling due after more than one year

	2015 £ m	2014 £ m
Obligations under finance lease and hire purchase contracts	25.6	13.6
Amounts owed to group companies	482.1	388.1
Other creditors	5.0	17.1
	<u>512.7</u>	<u>418.8</u>

Total creditors due in more than one year held by the Company at 31 December 2015 amount to £512.7m (2014: £445.3m) and include £512.7m (2014: £418.8m) shown above and £nil (2014: £26.5m) included within amounts held for sale on the balance sheet.

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

Analysis of loan repayments

	2015 £ m	2014 £ m
Within one year	<u>-</u>	<u>20.3</u>

Serco Limited
Notes to the Financial Statements for the Year Ended 31 December 2015

21 Creditors: Amounts falling due after more than one year *continued*

Obligations under finance leases and hire purchase contracts

	Minimum lease payments £ m	Present value of minimum lease payments £ m
2015		
Within one year or on demand	15.9	14.7
Between two and five years	26.0	24.9
Over five years	0.6	0.7
Less: future finance charges	(2.2)	-
	40.3	40.3

	Minimum lease payments £ m	Present value of minimum lease payments £ m
2014		
Within one year or on demand	18.2	16.5
Between two and five years	39.8	37.5
Over five years	2.3	2.3
Less: future finance charges	(4.0)	-
	56.3	56.3

Balances for obligations under finance leases and hire purchase contracts include £0.5m (2014: £34.2m) of contracts shown within assets and liabilities held for sale.

Finance lease obligations are secured by the lessors' title to the leased assets.

The directors estimate that the fair value of the Company's lease obligations approximates to their carrying amount.

Serco Limited
Notes to the Financial Statements for the Year Ended 31 December 2015

22 Provisions

	Contract £ m	Employee related £ m	Property £ m	Other £ m	Total £ m
At 1 January 2015	256.6	12.8	12.3	59.0	340.7
Reclassified from trade and other payables	-	-	-	15.9	15.9
Charged to the profit and loss account - exceptional	-	2.5	-	-	2.5
Charged to the profit and loss account - other	51.5	8.4	0.7	10.6	71.2
Released to the profit and loss account - exceptional	(2.8)	(1.2)	-	(0.8)	(4.8)
Released to the profit and loss account - other	(30.3)	(0.6)	(0.2)	(9.1)	(40.2)
Utilised during the year	(69.7)	(4.8)	(2.1)	(14.3)	(90.9)
Transfer to assets held for sale	(0.9)	-	-	(0.1)	(1.0)
Unwinding of discount	1.7	-	-	-	1.7
Exchange differences	-	0.4	-	-	0.4
At 31 December 2015	206.1	17.5	10.7	61.2	295.5
Analysed as:					
Current	66.2	8.9	2.1	30.5	107.7
Non-current	139.9	8.6	8.6	30.7	187.8
	206.1	17.5	10.7	61.2	295.5

Total provisions held by the Company at 31 December 2015 amount to £318.0m (2014: £344.3m) and include £295.5m (2014: £340.7m) shown above and £22.5m (2014: £3.6m) included within amounts held for sale on the balance sheet.

Contract provisions relate to onerous contracts which will be utilised over the life of each individual contract, up to a maximum of 7 years from the balance sheet date. The present value of the estimated future cash outflows required to settle the contract obligations as they fall due over the respective contracts has been used in determining the provision. The individual provisions are discounted where the impact is assessed to be material.

A full analysis is performed at least annually of the future profitability of all contracts with marginal performances and of the balance sheet items directly linked to these contracts.

Due to the significant size of the balance and the inherent level of uncertainty over the amount and timing of the related cash flows upon which onerous contract provisions are based, if the expected operational performance varies from the best estimates made at the year end, a material change in estimate may be required. The key drivers behind operational performance is the level of activity to be serviced, which is often directed by the actions of the UK Government, and the efficiency of Company employees and resources.

Employee related provisions are for long-term service awards and terminal gratuities liabilities which have been accrued and are based on contractual entitlement, together with an estimate of the probabilities that employees will stay until retirement and receive all relevant amounts. There are also amounts included in relation to restructuring. The provisions will be utilised over various periods driven by local legal or regulatory requirements, the timing of which is not certain.

Property provisions relate to leased properties which are either underutilised or vacant and where the unavoidable costs associated with the lease exceed the economic benefits expected to be generated in the future. The provision has been calculated based on the discounted cash outflows required to settle the lease obligations as they fall due, with the longest running lease ending in November 2035.

Other provisions are held for legal and other costs that the Company expects to incur over an extended period. These costs are based on past experience of similar items and other known factors and represent management's best estimate of the likely outcome and will be utilised with reference to the specific facts and circumstances, with the majority expected to be settled by 30 September 2026.

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2015

23 Pension and other schemes

Defined contribution scheme

The Company operates a defined contribution scheme. The pension cost charge for the year represents contributions payable by the Company to the scheme which amounted to £29.6m (2014: £30.4m).

Contributions totalling £nil (2014: £nil) were payable to the scheme at the end of the year.

Pre-funded defined benefit schemes treated as defined contribution

Serco Limited accounts for certain pre-funded defined benefit schemes relating to contracts as defined contribution schemes because the contributions are fixed until the end of the current concession and at rebid any surplus or deficit would transfer to the next contractor. Cash contributions are recognised as pension costs and no asset or liability is shown on the balance sheet.

Defined benefit pension schemes

The Company operates defined benefit schemes for qualifying employees in the UK. The amounts in the balance sheet are grouped in to two categories: contract specific and non contract specific.

The assets of the funded schemes are held independently of the Company's assets in separate trustee administered funds. The trustees of the pension fund are required by law to act in the interest of the fund and of all relevant stakeholders in the scheme. The trustees of the pension fund are responsible for the investment policy with regard to the assets of the fund. The Company's major schemes are valued by independent actuaries annually using the projected unit credit actuarial cost method. This reflects service rendered by employees to the dates of valuation and incorporates actuarial assumptions primarily regarding discount rates used in determining the present value of benefits, projected rates of salary growth, and life expectancy of pension plan members. Discount rates are based on the market yields of high-quality corporate bonds in the country concerned. 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 scheme to settle obligations in the other scheme and intends to exercise this right.

In accounting for the defined benefit schemes, the Group has applied the following principles.

- Asset recognised for SPLAS is based on assumption that full surplus will ultimately be available to the Company as a future refund of surplus.
- No foreign exchange item is shown in the disclosures as the non-UK liabilities are not material.
- No pension assets are invested in the Company's own financial instruments or property.

The schemes in the UK typically expose the Company to actuarial risks such as: investment risk, interest rate risk, longevity risk and salary risk.

- Investment risk - the present value of the defined benefit schemes' liability is calculated using a discount rate determined by reference to high quality corporate bond yields; if the return on plan assets is below this rate, a deficit will be created.
- Interest risk - a decrease in the bond interest rate will increase the scheme liability but this will be partially offset by an increase in the return of the plan's debt investments.
- Longevity risk - the present value of the defined benefit plan liability is calculated by reference to the best estimate of the mortality of plan participants both during and after their employment. An increase in the life expectancy of the plan participants will increase the plan's liability.
- Salary risk - the present value of the defined benefit scheme liability is calculated by reference to the future salaries of plan participants, as such, an increase in the salary of the plan participants will increase the plan's liability.

The normal contributions expected to be paid during the financial year ending 31 December 2016 are £11.9m (31 December 2015: £13.5m).

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2015

Triennial funding valuation

The largest non contract specific scheme is the Serco Pension and Life Assurance Scheme (SPLAS). The estimated actuarial deficit of SPLAS as at 31 December 2015 was approximately £28.0m (2014: 5.0m). The most recent full actuarial valuation of this scheme was undertaken as at 5 April 2012 and resulted in an actuarially assessed deficit of £24m. Following this review, the Company agreed with the Trustees to make a small increase in contributions, bringing cash contributions of up to 33% of members' pensionable salaries until 2021. An actuarial valuation of the scheme as at 5 April 2015 is being undertaken and is due to be released in the autumn of 2016. 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 pension legislation.

A summary of the defined benefit pension schemes on the balance sheet is as follows:

	2015 £ m	2014 £ m
Contract specific	-	(4.0)
Non contract specific	115.9	130.8
Net retirement benefit asset	115.9	126.8
Analysed as:		
Retirement benefit assets	127.1	143.9
Retirement benefit obligations	(11.2)	(17.1)

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 comprehensive income. Intangible assets are amortised over the term of the contracts.

Contributions payable to the pension scheme at the end of the year are £nil (2014: £nil).

Reconciliation of scheme assets and liabilities to assets and liabilities recognised

The amounts recognised in the balance sheet are as follows:

	2015 £ m	2014 £ m
Fair value of scheme assets	-	29.8
Present value of scheme liabilities	-	(33.8)
Contract specific defined benefit pension scheme deficit	-	(4.0)

Serco Limited
Notes to the Financial Statements for the Year Ended 31 December 2015

Scheme assets Changes in the fair value of scheme assets are as follows:

	2015 £ m	2014 £ m
At 1 January	29.8	137.3
Interest income on scheme assets - employer	1.0	6.3
Return on scheme assets less interest income	0.5	12.0
Administrative expenses and taxes	-	(1.8)
Employer contributions	0.4	8.1
Contributions by employees	0.3	0.9
Benefits paid	(0.8)	(2.5)
Plan settlements	(31.2)	-
Eliminated on disposal of pension scheme	-	(130.5)
At 31 December	-	29.8

Analysis of assets The major categories of scheme assets are as follows:

	2015 £ m	2014 £ m
Equity instruments	-	19.4
Bonds	-	3.1
Gilts	-	1.8
Property	-	3.5
Cash and other	-	2.0
At 31 December	-	29.8

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. Virtually all equity and debt instruments have quoted prices in an active market.

Scheme liabilities Changes in the present value of scheme liabilities are as follows:

	2015 £ m	2014 £ m
At 1 January	33.8	159.3
Current service cost - employer	1.2	5.8
Effect of changes in financial assumptions	(0.7)	25.3
Effect of experience adjustments	(0.5)	(0.1)
Interest cost - employer	1.1	7.0
Benefits paid	(0.8)	(2.5)
Contributions by scheme participants	0.3	0.7
Plan settlements	(34.4)	-
Eliminated on disposal of pension scheme	-	(161.7)
At 31 December	-	33.8

Serco Limited
Notes to the Financial Statements for the Year Ended 31 December 2015

Amounts recognised in the profit and loss account

	2015 £ m	2014 £ m
Amounts recognised in operating loss		
Current service cost	1.2	5.8
Settlement gain	(3.3)	-
Administrative expenses and taxes	-	1.8
Recognised in arriving at operating loss	(2.1)	7.6
Amounts recognised in interest receivable and similar income		
Interest cost on scheme liabilities - employer	(1.0)	7.0
Interest cost on scheme assets - employer	1.1	(6.3)
Interest on franchise adjustment	-	(0.7)
Recognised in interest receivable and similar income	0.1	-
Total recognised in the profit and loss account	(2.0)	7.6

Amounts recognised in the statement of comprehensive income

	2015 £ m	2014 £ m
Remeasurements recognised in the statement of comprehensive income		
Return on scheme assets less interest income	0.5	12.0
Effect of changes in financial assumptions	0.7	(25.3)
Effect of changes in demographic assumptions	-	-
Effect of experience adjustments	0.4	0.1
	1.6	(13.2)
Actuarial (losses)/gains on reimbursable rights		
Change in franchise adjustment	-	13.2
	-	13.2
Total pension cost recognised in the statement of comprehensive income	1.6	-

In the prior year, the DLR contract and its associated defined benefit pension scheme ceased to be part of Serco Limited. As a result, Serco Limited ceased to be a participating employer in the DLR Pension scheme.

Non contract specific

This consists of two pre-funded defined benefit schemes that do 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.

Contributions payable to the pension scheme at the end of the year are £nil (2014: £nil).

Serco Limited
Notes to the Financial Statements for the Year Ended 31 December 2015

Reconciliation of scheme assets and liabilities to assets and liabilities recognised

The amounts recognised in the balance sheet are as follows:

	2015 £ m	2014 £ m
Fair value of scheme assets	1,304.3	1,361.8
Present value of scheme liabilities	(1,188.4)	(1,231.0)
	115.9	130.8
Members' share of deficit	-	-
Net non contract specific defined benefit pension scheme surplus	115.9	130.8
	2015 £ m	2014 £ m
Analysed as:		
Retirement benefit assets	127.1	143.9
Retirement benefit obligations	(11.2)	(13.1)
	115.9	130.8

Scheme assets Changes in the fair value of scheme assets are as follows:

	2015 £ m	2014 £ m
At 1 January	1,361.8	1,146.1
Interest income on scheme assets - employer	48.6	51.3
Interest income on scheme assets - employee	-	0.9
Administrative expenses and taxes	(4.5)	(3.5)
Employer contributions	11.4	15.4
Contributions by employees	0.6	0.5
Benefits paid	(46.4)	(39.1)
Return on scheme assets less interest income	(67.2)	190.2
At 31 December	1,304.3	1,361.8

Analysis of assets The major categories of scheme assets are as follows:

	2015 £ m	2014 £ m
Equity instruments	39.1	38.5
Liability Driven Investments (LDI)	1,144.4	1,252.8
Gilts	68.1	-
Bonds except LDI	-	15.6
Annuity policies	22.0	23.9
Cash and other	30.7	31.0
	1,304.3	1,361.8

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. Virtually all equity and debt instruments have quoted prices in an active market.

Serco Limited
Notes to the Financial Statements for the Year Ended 31 December 2015

Scheme liabilities Changes in the present value of scheme liabilities are as follows:

	2015 £ m	2014 £ m
At 1 January	1,231.0	1,091.1
Current service cost - employer	8.5	8.8
Current service cost - employee	-	0.2
Past service cost - employer	0.4	2.5
Plan participants' contributions	0.6	0.2
Interest cost - employer	43.6	48.3
Interest cost - employee	-	1.1
Benefits paid	(46.4)	(39.1)
Effect of changes in financial assumptions	(42.8)	116.8
Effect of changes in demographic assumptions	0.2	(3.2)
Effect of experience adjustments	(6.7)	4.3
At 31 December	1,188.4	1,231.0

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 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

	2015 £ m	2014 £ m
Amounts recognised in operating loss		
Current service cost - employer	8.5	8.8
Past service cost	0.4	2.5
Administrative expenses and taxes	4.5	3.5
Recognised in arriving at operating loss	13.4	14.8
Amounts recognised in interest receivable and similar income		
Interest income on scheme assets - employer	(48.6)	(51.3)
Interest cost on scheme liabilities - employer	43.6	48.3
Recognised in interest receivable and similar income	(5.0)	(3.0)
Total pension cost recognised in the profit and loss account	8.4	11.8

Serco Limited
Notes to the Financial Statements for the Year Ended 31 December 2015

Amounts recognised in the statement of comprehensive income

	2015 £ m	2014 £ m
Remeasurements recognised in the statement of comprehensive income		
Actual return on scheme assets less interest income	(67.2)	190.2
Effect of changes in financial assumptions	42.8	(116.8)
Effect of changes in demographic assumptions	(0.2)	3.2
Effect of experience adjustments	6.7	(4.3)
	<u>(17.9)</u>	<u>72.3</u>
Actuarial (losses)/gains on reimbursable rights		
Change in members' share	-	(3.9)
	<u>(17.9)</u>	<u>68.4</u>
Total pension cost recognised in the statement of comprehensive income		
	<u>(17.9)</u>	<u>68.4</u>

Principal actuarial assumptions

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

	2015 %	2014 %
Discount rate	3.8	3.6
Future salary increases	2.8	2.6
Future pension increases (CPI)	2.0	2.0
Future pension increases (RPI)	3.0	-
Inflation assumption (CPI)	2.1	2.1
Inflation assumption (RPI)	3.1	-

Post retirement mortality assumptions

	2015 Years	2014 Years
Current UK pensioners at retirement age - male	22.5	22.4
Current UK pensioners at retirement age - female	25.0	24.9
Future UK pensioners at retirement age - male	24.3	24.2
Future UK pensioners at retirement age - female	27.0	26.9

Management considers the significant actuarial assumptions with regards to the determination of the defined benefit obligation to be the discount rate, inflation, the rate of salary increases and mortality.

Sensitivity analysis is provided below, based on reasonably possible changes of the assumptions occurring at the end of the reporting period, assuming all other assumptions are held constant.

The sensitivities have been derived in the same manner as the defined benefit obligation as at 31 December 2015 where the defined benefit obligation is estimated using the Projected Unit Credit method. Under this method each participant's benefits are attributed to years of service, taking into consideration future salary increases and the scheme's benefit allocation formula. Thus, the estimated total pension to which each participant is expected to become entitled at retirement is broken down into units, each associated with a year of past or future credited service.

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2015

The defined benefit obligation as at 31 December 2015 is calculated on the actuarial assumptions agreed as at that date. The sensitivities are calculated by changing each assumption in turn following the methodology above with all other things held constant. The change in the defined benefit obligation from updating the single assumption represents the impact of that assumption on the calculation of the defined benefit obligation.

Assumption	Change in assumption	Change in present value of	Change in present value of
		scheme liabilities	scheme liabilities
	%	2015	2015
		%	%
Discount rate: 3.8%	0.5	(9)	(8)
	(0.5)	10	10
Inflation: 2.1% CPI	0.5	9	8
	(0.5)	(8)	(8)
Rate of salary increase: 2.6%	0.5	1	1
	(0.5)	(1)	(1)

If the mortality rate was increased by one year to the post retirement range of assumptions applied for male and female, current and future pensioners from 22.6 - 27.1, the change in present value of scheme liabilities would increase 2% (2014: 2%).

Management acknowledges that the method used of presuming that all other assumptions remaining constant has inherent limitation given that it is more likely for a combination of changes, but highlights the value of each individual risk and is therefore a suitable basis for providing this analysis.

24 Called up share capital

Allotted, called up and fully paid shares

	No. m	2015	No. m	2014
		£ m		£ m
Ordinary share capital of £1 each	0.8	0.8	0.4	0.4

New shares allotted

During the year 364,382 ordinary shares having a nominal value of £0.4m were allotted for an aggregate consideration of £150.0m; giving rise to share premium of £149.6m.

25 Contingent liabilities

The Company, together with its ultimate parent and certain other subsidiaries, is included within interest pooling arrangements involving cross guarantee structures. The overdraft balance was £11.1m at 31 December 2015 (undrawn at 31 December 2014).

Serco Limited is a cross-guarantor with other group companies on a joint and several basis in respect of the borrowing facilities of the Serco Group. These relate to bank debt facilities and US private placement bonds. As at 31 December 2015, the total facility amounts were £480m (2014: £730m) for the RCF and £375m (2014: £585m) for the US private placements.

The Company is aware of other 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.

As we have disclosed before, we are under investigation by the Serious Fraud Office. In November 2013, the UK's Serious Fraud Office announced that it had opened an investigation, which remains ongoing, into the Group's Electronic Monitoring Contract. We are cooperating fully with the Serious Fraud Office's investigation but it is not possible to predict the outcome. However, disclosed in the Principal Risks and Uncertainties in this Report is a description of the range of possible outcomes in the event that the Serious Fraud Office decides to prosecute the individuals and / or the Serco entities involved.

Serco Limited
Notes to the Financial Statements for the Year Ended 31 December 2015

26 Commitments

Capital commitments

The total amount contracted for but not provided in the financial statements was £12.9m (2014: £3.4m).

Operating leases

The total future value of minimum lease payments under non-cancellable operating leases is as follows:

	2015 £ m	2014 £ m
Within one year	20.1	27.4
In two to five years	38.2	67.0
In over five years	3.5	13.1
	61.8	107.5

27 Derivative financial instruments

	2015 Assets £ m	2015 Liabilities £ m	2014 Assets £ m	2014 Liabilities £ m
Forward foreign exchange contracts	0.2	(0.2)	0.2	(0.2)

	2015 Assets £ m	2015 Liabilities £ m	2014 Assets £ m	2014 Liabilities £ m
Analysed as:				
Non-current	-	-	-	-
Current	0.2	(0.2)	0.2	(0.2)
	0.2	(0.2)	0.2	(0.2)

The Company is exposed to foreign currency transaction risk on costs. Any material transactional exposure that does arise is hedged by the Group Treasury function using forward foreign currency contracts. Hedges on highly probable forecast transactions or commitments have been designed as cash flow hedges. All currency derivatives designated as cash flow hedges are highly effective and the fair value gain of £0.1m in the year (2014: £0.1m gain) has been deferred in equity.

Serco Limited

Notes to the Financial Statements for the Year Ended 31 December 2015

28 Assets held for sale

As part of the Strategy Review, certain assets and liabilities have been designated as non-core and held for sale. As at 31 December 2015 this is limited to the remaining onshore private sector BPO business, which is expected to be sold in 2016.

Following the agreement to dispose of the offshore private sector BPO operations it was determined that the Environmental Services and Leisure businesses would no longer be disposed of for both strategic and financial reasons. As a result, these operations were transferred out of held for sale at 15 December 2015, the point at which this decision was made and publically announced.

The balances included as held for sale as at 31 December are as follows:

	Note	2015 £ m	2014 £ m
Assets			
Other intangible assets	15	-	0.4
Property, plant and equipment	16	0.4	39.6
Stocks	18	-	0.9
Debtors: amounts due within one year	19	9.3	20.1
Assets classified as held for sale		<u>9.7</u>	<u>61.0</u>
Liabilities			
Creditors: amounts falling due within one year	20	(1.5)	(24.5)
Provisions	22	(22.5)	(3.6)
Obligations under finance leases	21	(0.5)	(34.2)
Creditors: amounts due after more than one year	21	-	(0.3)
Liabilities directly associated with assets classified as held for sale		<u>(24.5)</u>	<u>(62.6)</u>

29 Control

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