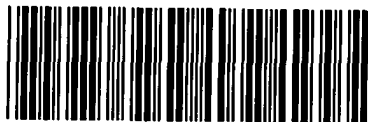


Serco Limited

Annual Report and Financial Statements

for the Year Ended 31 December 2022

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Serco Limited

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Serco Limited

Company Information

| | |
|--------------------------|--|
| Directors | A A Kirby N Girnary H Shaw |
| Company secretary | D Eveleigh |
| Registered number | 00242246 |
| Registered office | Serco House 16 Bartley Wood Business Park Bartley Way Hook Hampshire RG27 9UY |
| Auditor | KPMG LLP 15 Canada Square London United Kingdom E14 5GL |

Serco Limited

Strategic Report for the Year Ended 31 December 2022

The Directors present their Strategic Report for the year ended 31 December 2022.

Principal activity

The principal activity of Serco Limited (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, health, justice, immigration, and citizens services.

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 along with its subsidiaries is referred to in this document as the Group or Serco.

Business review

Overview

Turnover for the Company for the year was down 10.1% from £2,111.2m to £1,897.7m. The decline in turnover was mainly due to the loss of the Dubai Metro contract and the wind-down of Covid-19 related contracts.

The Company generated an operating profit, before net exceptional items, for the year of £13.3m (2021: £58.3m). The step down in operating profit, before exceptional net items, was caused by the reduction in revenue.

The Key Performance Indicators of Serco group PLC are outlined in its Annual Report and accounts on Page 2.

During the year the Company reported net exceptional costs of £9.9m (2021: £0.3m). The Company incurred £9.0m in exceptional costs (2021: £nil) for the provision of capital contributions to its subsidiaries, Serco Geografix Ltd and Serco Environmental Services Ltd. Additionally the Company incurred £0.9m of costs related to the acquisition of OXZ Holdings AG, on behalf of another company within the Group.

After exceptional items the operating profit of the Company for the financial year was £3.4m (2021: £58.0m).

The Company is focussed on its business development functions and bid pipeline, strengthening sector propositions, and consolidating differentiated capability to provide better outcomes and solutions to our customer. The Company continues to improve operational execution and drive further cost efficiencies in order to further improve underlying profitability.

As at 31 December 2022 the estimated actuarial deficit of the Company's primary defined benefit scheme was £27.0m (2021: surplus of £23.0m). During the year there was a high degree of volatility in the pensions market which has resulted in a significant reduction in pension scheme assets to £57.0m (2021: £149.5m).

**Strategic Report (continued)
for the Year Ended 31 December 2022**

Business Review (continued)

UK & Europe

The majority of Serco Group plc's UK & Europe division trades through the Company, and the operations support public service delivery and outcomes across all five of the Group's chosen sectors: our Justice & Immigration business provides a wide range of services to support safeguarding society and reducing re-offending, from secure accommodation management through to housing and welfare services for asylum seekers; in Defence, we are trusted to deliver critical support services and operate sensitive facilities; our Transport business provides a combination of passenger and commercial transport solutions through ferry services; our Health business provides primarily non-clinical support services to hospitals; and the Citizens Services business provides environmental and leisure services, as well as a wide range of other front, middle and back-office services to support public sector customers in the UK or European institutions.

Turnover for 2022 was £1,867.6m (2021: £2,004.8m), a decrease of 7% which makes up the majority of the revenue decrease for the Company.

Middle East

Revenue for the year was £30.1m (2021: £106.4m). The Company lost its contract to operate the Dubai Metro rail service in 2021 which is the primary reason for the fall in revenues within the region.

Principal risks and uncertainties

Risk management

The Company leverages the risk management processes of its ultimate parent company, Serco Group plc. The risk management policies of Serco Group plc are outlined in its Annual Report and Accounts dated 27 February 2022, are available on its website and are outlined below. As a listed company, the risk management policies of Serco Group plc are sufficient for this Company to rely upon.

The Company is exposed to a wide range of risks that, should they materialise, could have a detrimental impact on the Company's financial performance, reputation and operational resilience. The Company therefore takes risk management extremely seriously and invests significant effort into identifying and managing risks. The Board of Serco Group plc oversees the Company's risk management and internal control processes within an Enterprise Risk Management ("ERM") framework, discharging its oversight responsibilities through the Group Risk Committee ("GRC"), supported by the Corporate Responsibility Committee ("CRC") and Audit Committee.

The Company's ERM approach is not about eliminating risk but seeks to identify, understand, mitigate and manage risks that might disrupt the Company's ability to execute its strategy or deliver against the customer and contractual commitments. The key risks are agreed through an annual review with the Executive Committee and through quarterly challenge and review at either Serco Group plc's Group Risk Committee ("GRC"), Corporate Responsibility Committee, Audit Committee or Board supported by Divisional level quarterly reviews with the Executive Management teams. Each risk response reflects the nature of the activities being undertaken and the level of control considered necessary to protect the Company's interests and those of the stakeholders.

In addition to the operational focus on risk, consideration and assessment of risk is an integral part of the annual strategic review that helps inform the Company's approach to operating across geographies, jurisdictions and sectors. These discussions include consideration of several of the principal risks, most notably Failure to Grow. The Company has assessed its markets and possible growth over the next five years as part of the strategy review to ensure it is sustainable and provides sufficient growth opportunities to meet its ambition without the need for a material shift in the operating model and existing markets. Further detail on the market can be found on page 6 of Serco Group plc 2022 Annual Report and Accounts.

Strategic Report (continued)
for the Year Ended 31 December 2022

Risk management process

The risk policy is set at the Serco Group plc level with implementation and execution owned within each of its Divisions. Serco Group plc and its subsidiaries are collectively referred to as the Group or Serco, and the Board refers to the Board of Directors of the Group. The Serco risk management lifecycle process is mandated throughout the Company to seek a consistent approach to identification, analysis, monitoring and reporting of risks and to provide further assurance that the risk mitigation in place is sufficiently effective and appropriate.

We undertake a bottom-up review of risks quarterly, with our Business Units identifying the main threats to achievement of their objectives, documenting and analysing their potential impact, and defining clear actions to reduce the likelihood of those risks materialising and/or the financial impact if they should still occur. The Business Unit risks are consolidated and reported to Divisional leadership teams in a check and challenge capacity to ensure that risks on the Business Unit risk registers accurately reflect the concerns of local senior leadership. Once approved, the Divisional risks are reviewed by the Group ERM team and help inform the principal risk updates. The Board is updated after each GRC meeting.

Our principal risks, detailed on page 98 of Serco Group plc 2022 Annual Report and Accounts, are those risks that we determine to be the most material when considered against our strategic ambition (as outlined on page 25) and that can materially affect the performance, prospects or reputation of our business. These risks are identified and assessed as part of our strategic review and through additional discussions at a Divisional level, Executive Committee and the GRC where internal and external emerging risk trends are considered. Once identified, each risk's inherent, residual and target position is assessed against a standardised set of impact categories that include financial, reputational, operational and strategic considerations on a worst-case credible scenario basis. The likelihood of each risk occurring is then assessed, resulting in a residual risk position that enables us to score the risk from minor to severe and rank accordingly.

Each principal risk has a Subject Matter Expert (SME), who acts as the lead in overseeing risk updates and driving risk action, and a nominated Executive Committee sponsor, whose role is to advocate and oversee risk ownership, allocated to it, supporting its review and management. A robust assessment of our principal risks and their mitigations is carried out as part of the GRC reporting schedule, as well as reviews of topical deep dives that focus on pertinent risk themes. These deep dives may be focused on a region, led by the Divisional CEOs or risk leads, or on functional or business unit areas involving specialists from our business operations. This risk-focused approach facilitates flexibility that allows us to be responsive to changes in our risk profile throughout the year while still maintaining appropriate coverage of our principal risks and Divisional risk landscapes.

Each of our principal risks has an appetite statement to determine the nature and amount of risk that the Group is willing to accept as well as informing our decision-making. The statements include one of four appetite categories – averse, cautious, moderate and flexible – that reflect the Board's tolerance to each risk.

These statements are aligned to our Values, Code of Conduct and other ethical requirements to support and drive the right risk culture within the Group, are set through discussion with the principal risk Executive Committee Sponsor and SME and ratified annually by the GRC. The Board's risk appetite associated with each principal risk is shown on page 98 of Serco Group plc 2022 Annual Report and Accounts.

The majority of our principal risks operate under an averse risk appetite demonstrating we have a close to zero tolerance for incidents. We appreciate that, by the nature of our operations, we have inherent risk exposures but we strive to mitigate them. In the case of our Health, safety and wellbeing principal risk for example, despite our focus, we unfortunately do still experience incidents and near misses.

Strategic Report (continued)
for the Year Ended 31 December 2022

Risk management process (continued)

As part of our ERM approach we have dedicated Compliance Assurance teams which operate as a second line function focusing on validation and testing of key controls to augment annual control self-assessments and biannual compliance assurance attestation statements. Key controls mapped against our principal risks, significant local risks, our updated to Serco Management System ("SMS") and testing plans are reviewed annually to identify and respond to any significant amendments in the control environment. While many controls are tailored to meet Divisional requirements, there are consistent themes across our control environment to include clear oversight and reporting by Divisional management teams, robust bid governance processes, a focus on the health, safety and wellbeing of our colleagues and service users and the prioritisation of maintaining integrity and a strong ethics culture. In addition to the work of our in-house assurance teams, augmented by our internal audit external partners in certain specialist areas, we are also subject to significant third line assurance activities and audits delivered through our in-house internal audit team, external third parties appropriate to the regulatory environment, certification standards and customer requirements in our varied service lines and business units. These reviews include those that support the range of ISO certifications we manage across the business as well as independent performance and regulatory reports on Serco operations.

We review the effectiveness of the Risk Committee on an annual basis. Following an external Board Performance Evaluation Review in 2021 where no material changes to the Risk Committee were reported or deemed necessary, our approach this year is based on feedback obtained via a questionnaire sent to the Risk Committee members and those who regularly attend the Committee, including the Group CEO, Group COO and Group ERM Director. Focus areas for 2023 include further interaction between Board Committees who oversee individual principal risks and enhancements to our emerging risk approach.

Emerging risks

We have an annual process to identify and monitor emerging risks to ensure that adequate steps are being taken to understand and mitigate new risk themes before they materialise and to assess any impact on our principal risks. This robust assessment of emerging risks is completed through individual and group discussions with our Executive Committee members, via input from our Divisional risk teams and the Risk Committee and through the monitoring of internal and external macro risk trends.

Examples of some of the current emerging risks discussed and being monitored via our quarterly risk process include:

- political volatility and geo-political uncertainty, including the war in Ukraine, and the impact that could have directly and indirectly on Serco's operations;
- pandemic or other material black or grey swan events response and Serco's ability to respond/demonstrate business resilience;
- significant and prolonged IT infrastructure failure preparedness;
- macroeconomic implications and related cost-of-living challenges and inflation pressures that may be felt across the business and by our people; and
- technology risk and its potential implications on our ability to grow in line with our strategic ambitions.

Other risk areas

While no longer considered as emerging risks, more so as enduring bodies of work we are committed to, we also reviewed both ESG and climate change as part of the Emerging risk review.

ESG: We have a clear objective to address the ESG risks that are material to us and important to our stakeholders, recognising their deep strategic relevance. Managing these risks and taking them seriously is something we have been doing for many years as they are woven inseparably into our operational and commercial landscape, our strategy and governance and how we analyse our performance and prospects. Our refreshed ESG Framework consolidates our ESG priorities in one model aligned to our materiality assessment completed with internal and external stakeholders. We continue to treat ESG as an embedded consideration across several of our principal risks rather than a standalone item at the Group level. More information on our approach to ESG can be found on page 36 of Serco Group plc 2022 Annual Report and Accounts.

**Strategic Report (continued)
for the Year Ended 31 December 2022**

Other risk areas (continued)

Climate change: Our environmental footprint varies significantly between our contracts and business units and is dependent upon the boundary and scope of our environmental reporting. Across much of our business we work on our customers' premises and are not in direct control of environmental impacts. Regardless of where we operate, however, we recognise the need to drive consistent environmental behaviours and performance improvements throughout our operations. We have chosen not to consider climate risk as a standalone principal risk and instead consider it as a cross-cutting scenario under several of our principal risks, including Catastrophic incident, and have embedded this more clearly in the principal risk narrative. We will continue to monitor the profile of climate change matters as part of our ongoing quarterly risk reviews and it will remain a focus area for development throughout 2023.

Further detail on our approach to environmental reporting and TCFD can be found on page 74 and our commitment to climate change as part of our ESG agenda on page 52 of Serco Group plc 2022 Annual Report and Accounts.

Summary of principal risks and uncertainties

Principal risks, as described below, have been reviewed by the Executive Committee, GRC and the Board. The risks are described on the following pages, together with the relevant strategic business objectives, key risk drivers, the Group-wide material controls which have been put in place to mitigate principal risks and the mitigation priorities to improve the effectiveness of the controls. We have included the residual risk trend indicator for each risk and a brief commentary to contextualise these trends. Each of the principal risks is relevant to the achievement of our KPIs as outlined on page 28 of Serco Group plc 2022 Annual Report and Accounts with the strongest links highlighted as part of the commentary.

Principal risks are considered over the same three-year timeframe as the Viability Statement set out on page 109 of Serco Group plc 2022 Annual Report and Accounts, which takes account of the principal risks in its assessment.

In addition to the principal risks and uncertainties already identified, there may be other risks, either unknown, or currently believed to be immaterial, which could turn out to be material, the Covid-19 pandemic being a good example. These risks, whether they materialise individually or simultaneously, could significantly affect the Company's business and financial results.

Changes during the year

Our strategic objectives (outlined on page 25 of Serco Group plc 2022 Annual Report and Accounts) consider the risks and opportunities associated with our existing market and services and did not highlight a need for a material shift in approach. As outlined in the Chief Executive's Review on page 15 of Serco Group plc 2022 Annual Report and Accounts we are reporting strong financial performance and despite the macroeconomic volatility of the last 12 months we have not observed any material manifestation of risk that has caused significant operational or performance disruption. Our principal risks therefore remain valid with their definition and scope remaining largely unchanged. These risks continue to underpin our business model described on page 13 of Serco Group plc 2022 Annual Report and Accounts, and mitigation of the risks link directly to our four strategic priorities as described in our management philosophy on page 11 of Serco Group plc 2022 Annual Report and Accounts. Some changes are noted that reflect updated thinking and responses to operational influences. We have broadened the definition and scope of our Catastrophic incident risk such that it now includes consideration of our resilience to an external event such as extreme weather events, pandemic or infrastructure failure. Similarly, we have updated the definitions of our Failure to grow risk to incorporate a wide set of causal factors, including failure to continue to focus on and show progress in relation to ESG matters, digital ambition and to anticipate and respond appropriately to changing customer expectations, competitor activity and potential concentration risk. We also clarified that the Major information security breach risk includes data privacy and data governance elements appropriately.

Strategic Report (continued)
for the Year Ended 31 December 2022

Strategic risks

Failure to grow profitably

Integral to our Strategy Review process, this risk considers the potential impact of failure to win material bids or renew material contracts profitably, or a lack of opportunities in our chosen markets, restricting revenue growth which may in turn have an adverse impact on Serco's profitability. This risk has a broad and direct link to our ability to meet the financial KPIs described on page 28 of Serco Group plc 2022 Annual Report and Accounts. We have a cautious appetite for this risk recognising that we will take reasonable and considered risks to generate profitable growth. Our business is linked to changes in the economy, fiscal and monetary policy, political stability and leadership, budget priorities, and the perception and attitude of governments and the wider public to outsourcing, which could result in decisions not to outsource services or lead to delays in placing work. Our ability to succeed is also linked to the competitive landscape and our ability to efficiently deploy resources as part of our service offering as well as delivering our ESG commitments and digital strategy ambition. The Directors of the Group carried out a comprehensive strategy review that took the Divisional five-year strategies and rolled these up for a Group view. This work concluded that our markets remain robust with significant revenue opportunity in our chosen markets and chosen activities.

Key risk drivers:

- External factors reducing the pipeline of opportunities.
- Failure to be competitive.
- Inability to meet customer and solution requirements during design, implementation and delivery.
- Ineffective business development leading to lower than expected win rates.

Material controls:

- Serco Group and Divisional Strategy including periodic strategy reviews.
- Investment Committees, Divisional level Business Lifecycle Review Teams (BLRTs).
- Sector-specific Centres of Excellence and Value Propositions.
- Serco Institute developing thought leadership and innovation for our markets.
- Business Lifecycle Review Team Process.
- Pipeline and Business Development spend reviews
- Regular Growth Forum reviews.
- Divisional Performance Reporting process.

Mitigation priorities:

- Review portfolio for new attractive organic expansion areas.
- Keep focus on business development processes in UK to improve capture effectiveness.
- Strengthen our customer focus and interactions to better anticipate and shape markets and opportunities.
- Continue to improve leveraging of Serco best practice and innovation and refinement of bid development processes.
- Continue to adopt a robust bid qualification process.
- Retain focus on effective management for major bids.
- Develop efficient common platforms for service delivery to support our strategic pillars, in particular customer intimacy and market shaping.

Financial risks

Financial control failure

Serco operates complex financial systems and processes and there is an inherent risk that these may fail if appropriate oversight is not in place. Such failures 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, or an inability to forecast accurately; the failure to create a suitable capital structure; and an inability to execute critical financial transactions, leading to financial instability, potential business losses and negative reputational impact. This risk links directly to our ability to meet the financial KPIs outlined on page 28 of Serco Group plc 2022 Annual Report and Accounts. We have an averse appetite for financial control failures and require a robust framework of financial processes, systems and controls to enable timely and accurate financial reporting and forecasting.

Strategic Report (continued)
for the Year Ended 31 December 2022

Financial risks (continued)

The Group was able to demonstrate that its financial processes and systems were able to operate effectively despite the significant change to working conditions and reactive nature of the business operations brought about by the pandemic. The financial control framework is transitioning to the continuous improvement stage.

Over the last 12 months, the Group has continued to improve its financial control environment. While the UK Government's proposals outlined in the consultation document issued by the Department of Business, Energy and Industrial Strategy (BEIS) entitled Restoring Trust in Audit and Corporate Governance has not yet resulted in any formal changes to the expectations or reporting from businesses, the Group has continued to deliver its programme of work to improve the financial controls framework recognising that the objectives of this programme, if achieved, should support the objectives set out in the consultation document in respect of financial controls. The Group is conscious of the impact of this programme and has been mindful of additional costs and administration placed on its operations before the expectations from BEIS or the Financial Reporting Council are formalised.

Key risk drivers:

- Not setting the right tone from the top.
- Poor financial processes.
- Inadequate financial controls within the business.
- Loss of critical roles and/or systems.
- Poorly skilled and resourced finance teams to address complex finance standards.

Mitigation priorities:

- Group Governance and Finance strategy.
- Group Governance and Finance strategy.
- Standardised and mandated financial systems, processes (including forecasting and reporting) and data structures.
- Governance and review procedures associated with managing the quality of services delivered by third party partners.
- Skilled and adequately trained finance staff.
- Disaster recovery plans and testing.
- Monthly Divisional performance reviews.
- Dedicated Financial Assurance team.

Material controls:

- Agree future operations for financial processes operated by third party suppliers.
- Continue to develop the financial controls and assurance framework including work under our CFIP programme.
- Continue to deliver effective financial reporting.
- Continuously improve forecasting and reporting processes and data analysis.
- Deliver global finance process improvement and efficiency through automation and robotics.
- Continue to improve the Group-wide training curriculum.
- Effectiveness reviews of disaster recovery plans.
- Ensure talent is retained within the finance function.

Strategic Report (continued)
for the Year Ended 31 December 2022

Operational risks

Major information security breach (including cyber-attack and data protection)

An information security breach, resulting in the loss or compromise of information (including personal or customer data) or wilful damage resulting in the loss of service, causing significant reputational damage/financial penalties and loss of customer/data subject confidence is a key risk for us. We operate an averse risk appetite to any major information security breaches and cyber-attacks. We accept that due to the nature of the services we provide we face threats from both internal and external factors but will always endeavour to mitigate the impact of any breach and carry out prompt remedial actions.

We continue to make significant investments in cyber-security, particularly with respect to our servers, endpoints, network and application security devices (and nowadays including third-party Cloud infrastructure, platforms and software services provided by our partners). We run planned penetration tests as well as seeking to meet specific security standards in line with customer requirements as a provider of public services to government. We maintain a continuing programme of upgrading IT to ensure we operate on supported versions of the hardware and software and risk assess any essential exemptions, standardise services where possible and so this year are pleased to report that we continue to see a decreasing trend in the number of devices outside centralised management and monitoring.

Serco is committed to delivering secure services which protect our own and our customers' data and as such holds a variety of externally audited security-related certifications. In most of our jurisdictions this also includes accreditation or assessment against government standards. These include the Information Security Management System covering our UK corporate environment that is certified to ISO 27001, Cyber Essentials Plus in the UK and PCI-DSS globally where required. Our certifications are generally publicly available on the relevant accreditors' websites or can be requested from the Company directly.

Serco regularly reviews how we protect and secure information in our custody to ensure we maintain our defences. We have also approved for implementation in 2023 an additional investment in our cybersecurity tooling to assist in maintaining access to our cloud environment systems while simultaneously improving our ability to prevent, detect, investigate and respond to advanced threats against the background of the rising sophistication of modern attacks. As custodians that care for personal data held on behalf of our customers, suppliers, business partners, employees and data subjects we have adopted a risk-based approach to implement a data protection framework that is integrated into our management system and our customer requirements. It aims to strengthen our operating culture and to seek to ensure we operate and continuously improve our business in a compliant, ethical and responsible way.

We continue to invest in staff security training as a key mitigant to this risk. Security training is delivered via our Learning Management System as part of the broader Serco Essentials framework, and this has been recently refreshed with updated material launched from January 2023. Training comprises mandatory modules that cover a range of areas including responsibilities when dealing with personal data and how to identify and respond to issues. All Serco employees, including contractors, must complete Serco Essentials and pass a test at the end or, alternatively, in the case of subcontract staff, their employer must demonstrate that they provide equivalent security training. Training is further supplemented, where appropriate, to cover specific points relevant to any particular contract, together with regular campaigns and awareness tests such as protecting against phishing threats.

Strategic Report (continued)
for the Year Ended 31 December 2022

Operational risks (continued)

Major information security breach (including cyber-attack and data protection) (continued)

Key risk drivers:

- Non-compliant or obsolescent systems.
- Non-compliance or misconfiguration with policies and standards.
- Vulnerability of systems and information.
- Unauthorised use of systems.
- Inadequate incident monitoring and response.
- Increased regulatory scrutiny.
- Human factors leading to data breach.
- Failure to follow Data Protection laws and Customer requirements.
- Poor data mapping and retention.

Material controls:

- Enterprise Architecture Boards & Solution Review meetings.
- SMS including detailed guidance on minimum security controls.
- IT security infrastructure, processes and controls including isolated backups.
- Privileged Access Management and multi-factor authentication for our centralised managed systems.
- External assessments and scenario based cyber security testing and incident planning.
- Regular attestation statements on security controls compliance.
- Third-party supplier cyber assessment due diligence.
- Data Protection training and awareness campaigns.
- Data Protection Officer programme and Data Protection Champions network.
- Monitoring Data protection laws and Customer requirements.
- One Trust data inventory mapping and data retention programme.

Mitigation priorities:

- Perform market appraisals of technology when bidding new contracts and review existing technology at renewal points to ensure we maintain our defences as threats change and develop in sophistication.
- Ongoing continuous strategic improvement programmes to maintain our cyber defences (for example the investment in improved cyber tooling) as described in the section above.
- Continued routine vigilance and proactive vulnerability identification coordinated through our Security Operations Centres.
- Continued use of global key security risk indicators and regular third-party testing and best practice configuration reviews to support mitigation priorities.
- Leveraging Cloud adoption to ensure standardised control mechanisms.
- A focus on the behavioural aspects of our employees.
- Maintaining compliance with government security attestations.
- Data Protection training through Serco Essentials and communication through International Data Privacy Day week using 'back to basics' and other global campaigns reflected on [Serco.com/privacy](https://serco.com/privacy).
- Monitoring the Global changes in law including international transfer laws and customer requirements.
- Build a stronger consistent data protection framework of sharing information and knowledge through the Global Data Protection and Information Security Working Group.
- Gold IAPP Membership and data protection champions.

Strategic Report (continued)
for the Year Ended 31 December 2022

Operational risks (continued)

Contract non-compliance, non-performance or misreporting

With more than 20,000 employees directly or indirectly delivering services under circa 100 services contracts there is considerable scope for missed contract obligations or performance thresholds or inaccurately compiled performance reports. In the normal course of service provision, these failures are minor, fixable and often allowed for in the contracts we sign via defined tolerance levels and penalties. These are not the focus of this risk.

This risk is instead concerned with levels of failure that are unacceptable to Serco and its customers, especially deliberate misreporting of contractual performance or material contracts being taken away from Serco due to non-performance or non-compliance.

We have had no instances of such material failure levels throughout the past year, but have at times seen near misses, particularly where high levels of performance financial penalties have been incurred. In some instances this will lead to a rectification plan agreed with the relevant customer.

Our approach is to continue to strengthen the controls across each stage of the business cycle, including a near-term focus on: understanding and clarity of contract commitments at bid stages; communication and handover processes when transitioning to live operations; consistent processes for measuring the performance and maintaining clear and agreed contract documentation and increased focus on enhanced oversight, reporting and assurance.

Underpinning these initiatives, the review and relaunch of the SMS in 2023 will bring greater clarity to what is expected by each persona throughout the business cycle. The relaunch will bring greater visibility of the controls we do or do not have in place, allowing them to be challenged and strengthened throughout the year.

Key risk drivers:

- Not setting the right tone from the top.
- Unclear contract requirements/obligations.
- Human error (deliberate or unintentional).
- Operational delivery or reporting failures.

Material controls:

- Contract Management Application.
- Monthly performance reviews at Contract, Business Unit and Divisional level.
- Business Lifecycle Review team process.
- Communication of Our Values and Code of Conduct.
- Speak Up process (Ethicspoint).
- Extensive internal and external assurance reviews, including independent third-party reviews and customer oversight processes.

Mitigation priorities:

- Strengthen processes related to agreeing clear contracts, change management, bid to contract handover and KPI reporting, formalised through the enhanced application of SMS.
- Contract Management training (Global and Divisional).
- Greater visibility of performance through our contract performance dashboard "Gauge".
- Continued focus on consistent approach to risk assessment.
- Operational excellence improvement plans.
- Ongoing ethics, business conduct and compliance training.
- Improvements to assurance framework and activities.

Strategic Report (continued)
for the Year Ended 31 December 2022

Operational risks (continued)

Significant failure of the supply chain

As a result of a significant failure in Serco's end-to-end supply chain to perform to the required standard, Serco may be exposed to risks that mean Serco is unable to meet its customer obligations, perform critical business operations or win new business. Serco uses thousands of suppliers globally each year and we accept that it is not feasible to monitor and manage the performance of every supplier. This risk also includes risks to Serco from non-business critical suppliers and from the suppliers of our suppliers. Consequently, we take a proportionate approach to management of these third parties and have a moderate risk appetite for using them.

Over the last year, we have continued to see growing global supply chain risk, not just through increased reliance on suppliers through subcontracting and complex supplier services, but also volatility in the external environment through macroeconomic and geopolitical events as well as increasing environmental and social regulation.

To take account of these growing supply chain risks, our newly established Supplier Risk Management Framework, which was developed over the last year, encompasses the following risk exposures: information security and cyber; data protection; regulatory and legal; health and safety; environmental; business integrity and ethics, financial; performance and resilience. Each of these risk exposures has been considered in relation to stages of the supplier life cycle from supplier sourcing, contracting, onboarding, ongoing monitoring and exit, with gaps identified.

Where the performance of these third parties fall within our criteria of 'severe or major business critical' or where there are suppliers with material inherent risk against the range of risk exposures in our Supplier Management Framework, we seek to mitigate that uncertainty by endeavoring to put controls in place at each stage of the supplier life cycle.

Implementation of the Supplier Risk Management Framework is being progressed through a phased Divisional focus. A tiering approach to identifying the most material risk suppliers is being developed, which will enable better monitoring of the most material risk suppliers across the range of risk exposures, proportionate to the risks these represent for our business.

The risk remains elevated given macroeconomic circumstances, continued considerable inflationary pressures and consequent supply chain challenges for the foreseeable future. Although there is a risk of disruption in both Divisions, the highest perceived risk is in our UK&E Division where we continue to experience and manage localised challenges.

Key risk drivers:

- Inadequate procurement standards, operating procedures and controls.
- Failures or inadequate due diligence and onboarding when bringing new suppliers, partners and sub-contractors into the business including poor specification of requirements, inadequate sourcing and selection and inadequate contracting.
- Inadequate/lack of monitoring - and management of supplier performance and risks.
- High volume of suppliers or complexity of supply chain.

Material controls:

- SMS Procurement policy, Standards and Procedures including Supplier Code of Conduct.
- Supplier checks (pre-qualification or on-boarding).
- Serco standard contracts where possible including appropriate obligations, Key Performance Indicators and Service Level Agreements.
- Supplier Management Programme for most business-critical suppliers including performance, contract compliance and risk management.
- Annual procurement review process of business-critical suppliers.

Strategic Report (continued)
for the Year Ended 31 December 2022

Operational risks (continued)
Significant failure of the supply chain (continued)

Mitigation priorities:

- Phased and proportionate implementation of Supplier Risk Management Framework, including supplier triage and assessment.
- Enhance Procurement & Supply Chain Group Standard improving clarity and understanding of policy requirements, processes, controls and responsibilities.
- Risk assessment and mitigation plans incorporating actions to improve effective implementation of key risk controls for all material risk rated business-critical suppliers.
- Review of supplier management programme, aligning to Supplier Risk Management Framework, taking a tiered approach relative to risk. Review tools and guidance for contract-level supplier management aligned to needs of the business.

People risks

Failure to act with integrity

As a people-based business employing over 20,000 colleagues there is an inherent risk of rogue employees engaging in significant corrupt or dishonest acts including bribery, fraud, misreporting, cheating or lying. Such behaviour might arise through the actions of rogue employees or as a result of pressures individuals may feel they are being placed under to deliver financial or operational performance. Were we to fail to manage this risk it could lead to: the loss of existing business; restrictions on our ability to bid or win new business and a reduction in our ability to attract high-quality people or partners. It could also impact shareholder, investor and financial institutions' confidence in Serco and for these reasons we operate an averse risk appetite to this risk.

After significant work the Deferred Prosecution Order (DPA) was closed out successfully with no action being taken by the SFO. That means we have been released from all associated undertakings. Much of the work completed is about continuous improvement in programmes and processes to manage this risk and these activities will continue and remain a focus for management attention. While the DPA has ended the impact of something going wrong remains high and therefore we have not changed the risk rating to recognise that customer tolerance if found to have been misrepresenting and/or misreporting data at this critical time has the potential for serious reputational impact.

Other emerging factors that could impact this risk include fast changing sanction regulations following recent world events against which we need to remain vigilant. This places increased importance on due diligence of third parties and our new screening provider is strengthening our levels of review. We have seen increasing regulation, e.g. Whistleblowing directive and supplier due diligence including human rights and have also seen more active enforcement by regulatory authorities. Assurance of compliance controls is in place and remains key. Finally, there is the general economic pressure/cost of living which is hitting everyone and we recognise this may increase the risk of fraud.

This risk relies not just on clear policies and procedures but also behaviours. That is why our values and purpose sit at the top of our Management Philosophy described on page 11 of Serco Group plc 2022 Annual Report and Accounts, and integrity sits at the centre of and underpins our ESG framework. One achievement this year was the relaunch of our Code of Conduct (mycode.serco.com) which has been designed to be clear and engaging and a useful tool for all colleagues to understand what the right thing to do is. In addition, we have evolved our mandatory training for all colleagues and are updating our management modules for 2023, which continue to reinforce our strong tone at the top, and further developed our ESG framework as outlined on page 36 of Serco Group plc 2022 Annual Report and Accounts.

Strategic Report (continued)
for the Year Ended 31 December 2022

People risks (continued)
Failure to act with integrity (continued)

Key risk drivers:

- Not setting the right tone from the top.
- Weak values and culture.
- Increased pressure to deliver.
- Ineffective systems and processes.
- Weak diligence on where we work and who we work with.

Material controls:

- Strong, meaningful and understood Values and required behaviours which are defined in mycode, role modelled by leaders and included in bonus assessments for those that are eligible.
- Robust governance (Corporate Responsibility Committee; Executive Committee; Investment Committee; Divisional Executive Management etc.) exercising oversight of decisions within delegated authorities.
- Clear policy and procedures, including financial controls and processes defined within the SMS, which has been subject to a comprehensive review and refresh, supported by mycode.
- Independent Speak Up process supported by corporate investigations.
- Mandated Serco Essentials training.
- Group-wide Assurance programme.

Mitigation priorities:

- Continue to drive leadership ownership and accountability for a strong ethical culture.
- Roll out refreshed Ethics Compliance controls and procedures linked with the refresh of the SMS.
- Embed new due diligence processes for all third parties.
- Complete a review of Speak Up provision and related processes to improve efficiency and better manage risk of retaliation.
- Continue to strengthen Ethics Compliance resource and competency supported by robust data dashboards to inform management decisions.
- Continue to drive a programme of assurance including focusing on Ethics Compliance controls.

Failure to attract, engage and retain key talent

It is our ambition to be regarded as the best-managed company in the sector and, notwithstanding our framework of people processes, systems and controls, there is a risk that we are unable to attract, engage and retain an appropriately sized, qualified and competent workforce and management team. The impact of this risk materialising would restrict Serco's ability to deliver on its customer obligations, execute its strategy and achieve its business objectives while driving employee pride in the organisation. ESG is an implicit consideration in this risk and influences the achievement of our Employee Engagement KPI as outlined on page 30 of Serco Group plc 2022 Annual Report and Accounts. We have a cautious risk appetite and take a pragmatic approach to the attraction, retention and development of key talent. We ensure that robust contingency plans are in place for business-critical roles and regularly track turnover and vacancy rates but recognise that an element of churn is healthy for any business, meaning that we are not averse to change.

This risk includes consideration of key person reliance in our leadership and executive teams, including succession planning for our senior management team and other business-critical roles. It should be noted that, although difficulties in relation to labour markets continue, the overall downward trajectory of vacancies has continued with our recruitment teams making good progress. The positive trend has been seen across all Divisions with a number of our initiatives paying off, including our global employer brand refresh, increased utilisation of recruitment tools and processes and a refresh of our internal and external career websites.

The Board continues to ensure effective succession planning, both for Executive Committee and Group roles noting the successful Board and Executive Committee changes made this year as detailed in the Chairmans Statement on page 4 of Serco Group plc 2022 Annual Report and Accounts.

Strategic Report (continued)
for the Year Ended 31 December 2022

People risks (continued)

Failure to attract, engage and retain key talent (continued)

Key risk drivers:

- Lack of staff development.
- Poor talent management and succession planning.
- Low employee engagement.
- Unsatisfactory reward framework.
- Recruitment failings.
- Inability to attract appropriate new hires.

Material controls:

- Talent Management & Succession Processes.
- Leadership capability development.
- Targeted retention arrangements.
- Critical Resource Planning.
- Tracking of turnover and vacancy rates.
- Annual Performance Management process.
- Exit interview surveys.
- Annual Viewpoint survey.
- Focus on colleague health and wellbeing.

Mitigation priorities:

- Ensure up-to-date understanding of local employment markets.
- Continue to monitor channels to access external talent in chosen markets.
- Ongoing benchmarking activity to ensure market competitive reward packages to aid retention of existing staff and attraction of new.
- Continue with detailed review of succession plans and mitigation strategies as part of Talent Review process.
- Ensure ongoing use and analysis of exit interview survey results.
- Follow up and action on themes identified as a result of annual people survey.
- Further roll-out of ISO 45003 Psychological Health and Safety at Work across Divisions.

Health, safety and wellbeing

The diversity of services provided by Serco exposes our employees, customers and third parties to a wide range of health, safety and wellbeing risks inherent to our operations in both work and public environments. It also includes elements of risks related to environmental concerns recognising that extreme heat, flooding or other extreme weather events may impact the safety and wellbeing of our employees, the employees of our customers and suppliers and those we look after. These may be caused by a process or control failure or by the wrong behaviour and/or an inadequate safety culture. As responsible employers we recognise the complexity of wellbeing risk and aim to ensure that working for Serco does not impose any additional wellbeing challenges on our employees. This is a wide-reaching risk that directly supports the KPI target for Lost Time Incident Frequency Rate and Major Incident frequency rate as described on page 30 of Serco Group plc 2022 Annual Report and Accounts, and other HSE related metrics outlined in our ESG report on page 67. We have an averse risk appetite for actions/failures that would cause loss of life. We cannot eradicate this risk entirely while maintaining operational delivery so we prioritise prevention of major injuries and threats to wellbeing while accepting that minor injuries will occur on occasion but are minimised by training, risk assessment, safe systems of work, operating procedures, PPE, site supervision, audit and inspection, and a positive safety cultural approach.

Strategic Report (continued)
for the Year Ended 31 December 2022

People risks (continued)

Health, safety and wellbeing (continued)

Our vision is zero harm. We aim to ensure that no one comes to harm because of the work we do. Wherever we work, we are committed to the prevention of injury and promoting an equitable and positive safety culture in which we foster transparency, honesty and trust in order to identify root causes and prevent recurrence. Wherever we work, we are committed to the promotion of wellbeing and the prevention of ill health. We understand that healthier, happier employees go hand-in-hand with strong business performance, enhanced productivity, a positive culture and better outcomes for those we serve. In addition to personal injury concerns, a breach of health and safety regulations or failure to meet our contracted expectations could disrupt our business, have a negative impact on our reputation and lead to contractual, financial, regulatory and reputational costs.

While the impacts of the Covid-19 pandemic continue to challenge our people and services, these have largely merged into broader risk categories related to the wider public health, political and economic climates in which we are operating. The current cost-of-living challenges, for example, can trace their routes to the pandemic and are now being exacerbated by a number of global drivers, from the war in Ukraine to political decision-making. These broader risks can be labelled as crossover risks due to their potential for impact across several risk areas, from this risk, to Legal and Regulatory, Compliance, Attraction and Retention of Talent, and Catastrophic Incident risk. As with the pandemic, our Health, Safety and Wellbeing teams continue to support our organisational response across the business through key mitigations, including enhanced risk assessments, financial wellbeing support and updated training resources.

We continue to engage our people with this work and, through Viewpoint, the Safety Culture Survey and the Mind Workplace Wellbeing Index, can confidently comment that the controls and mitigations in place are more effective and well received. Notably the LTI reduction planning and the ISO 45003 accreditation are key markers of our continued focus on risk mitigation in these areas.

As the current societal challenges are predicted to increase we anticipate that these crossover risks will increase similarly, largely driven by financial pressures which will disproportionately impact our frontline workforce. Continuing to meet these developing people and compliance needs and mitigating their impact will be a key challenge for the organisation over the coming months.

Key risk drivers:

- Failure of the Serco Safety Management System.
- Insufficient communication of key issues, risks and changes.
- Lack of/out-of-date task specific competence.
- Human factors impact on behaviour.
- Occupational wellbeing risks including psychosocial risks.
- Public Health and wellbeing risks.
- Behavioural failures or human error resulting in injury or incident.
- Global economic challenges manifesting in colleague safety and wellbeing issues and incidents.
- Future impact of cross-cutting risks for example Catastrophic Incident, Legal and Regulatory etc.
- Extreme weather events such as fire and flooding.

Material controls:

- Serco Health, Safety, Environmental and Wellbeing ("HSEW") Strategies and Safety Management System (policies and procedures including Covid-19 Secure and specific guidance and policies) underpinned by the ESG framework.
- Safety and wellbeing training, communications and guidance (including Serco Essentials) and individual development plans and processes based on role and operational risk.
- Spontaneous and planned preventative, maintenance, inspection and repair programmes.
- Effective incident or near-miss observations reporting and investigations and effective use of ASSURE (independent reporting and compliance system).
- A programme of first, second and third line assurance.
- Risk assessments and supporting safe systems of work for activities.

Strategic Report (continued)
for the Year Ended 31 December 2022

People risks (continued)
Health, safety and wellbeing (continued)

Mitigation priorities:

- Continue to embed updated Health, Safety, Environment and Wellbeing strategies and a positive and equitable culture.
- Increase safety observation, Zero Harm Engagement and Safety Moment activity across the regions.
- Drive wellbeing agenda and ensure appropriate focus at a corporate level.
- Continuing first, second and third line assurance activities and ensuring understanding of appropriate levels of ownership, accountability, and responsibility.
- Further embed the Serco (Health, Safety, Environmental and Wellbeing) Strategies and Safety Management System (policies and procedures).
- Further development and maturity of our ESG agenda and programme of improvements to meet best practice and evolving stakeholder expectations.
- Continued review and sharing of lessons learnt throughout the global organisation.
- Continued CRC, Board and Executive Committee oversight and review.

Hazard risks

Catastrophic incident

Given the nature of the business the Company is exposed to the risk of an event (incident or accident) occurring as a result of Serco's actions or failure to effectively respond to or prepare for an event that results in multiple fatalities, and/or severe property/asset damage/loss and/or very serious environmental damage. Management of this risk influences the KPI target for Major Incident Frequency Rate as described on page 30 of Serco Group plc 2022 Annual Report and Accounts. The Company aims to provide safe services and places to work and has an averse risk appetite for this risk.

Throughout 2022 our five-step plan to ensure each Division continues to assess risks at a contract level to ensure that all relevant material risks have been identified, to assess and assure mitigations, including insurance cover, are appropriate and have been embedded. The physical risks linked to climate change-related events are now included more explicitly in our risk management framework as part of the work initiated for TCFD and outlined in more detail on page 77 of Serco Group plc 2022 Annual Report and Accounts. The former Health, Safety and Wellbeing elements of this risk have been moved to the Health, safety and wellbeing principal risk.

Given our average contract length, there tend not to be large fluctuations in this risk. That being said, we are working with some of our key insurance brokers to leverage climate change impact scenario analyses they have conducted, to see what potential risk quantification changes they project. This work will allow us to cross reference the insurance limits purchased and ensure they remain adequate, given insurance is one of the key mitigants for this risk.

Key risk drivers:

- Factors resulting in unsafe conditions.
- Ineffective or inadequate policies, standards and procedures.
- Lack of capability and experience.
- Lack of safety cultural alignment.
- Insufficient safety management oversight.
- Inadequate planning or response to a catastrophic event, including extreme weather or a climate change related event.
- Inadequate assurance and performance.
- Inadequate insurance cover.

Strategic Report (continued)
for the Year Ended 31 December 2022

Hazard risks (continued)
Catastrophic incident (continued)

Material controls:

- Regular reviews of high-risk contracts.
- HSEW Strategies and Safety Management System (policies and procedures) underpinned by our ESG framework.
- Safety training (including Serco Essentials) and individual development plans and processes based on role and operational risk.
- Effective incident or near-miss investigations and effective use of ASSURE (independent reporting and compliance system).
- Second and third line assurance reviews.
- Business continuity, crisis and incident emergency response plans and testing.
- Risk transfer via insurance where appropriate.

Mitigation priorities:

- Continue to embed updated HSEW strategies and a positive and equitable culture.
- Ongoing work within Divisions to identify and assess contract-specific risks and liabilities.
- Continued training in insurance and contractual risk management.
- Review and optimisation of the insurance programme and captive structure.
- Review levels and adequacy of compliance assurance.
- Continuing first, second and third line assurance activities and ensuring understanding of appropriate levels of ownership, accountability, and responsibility.
- Focus on maintenance and testing of robust business continuity, incident management and disaster recovery plans across each Division and function.

Legal and compliance risks

Material legal and regulatory compliance failure

Serco operates in complex legal and regulatory environments across multiple industries and geographies and there is a risk that we might not comply with all relevant laws and regulations. Failure to comply with laws and regulations could cause significant loss and damage to the Company and its people including exposure to regulatory prosecution and fines, reputational damage and the potential loss of licences and authorisations, all of which may prejudice the prospects for future bids. Defending legal proceedings may be costly and may also divert management attention away from running the business for a prolonged period. Uninsured losses or financial penalties resulting from any current or threatened legal actions may also have a material adverse effect on the Company. The Company is averse to risks which may result in legal and regulatory non-compliance and require processes that seek to minimise regulatory fines and legal action, as well as targeted and selected assurance activity.

We remain subject to a fast-moving and complex global legal and regulatory environment. In addition, various laws and regulations that apply across the business continue to be subject to increased focus and attention, including anti-bribery and corruption laws, Market Abuse Regulation, data and privacy laws, trade compliance, competition and antitrust, human rights and modern slavery.

The management of this risk is a key enabler of Serco's governance for ESG purposes.

Strategic Report (continued)
for the Year Ended 31 December 2022

Legal and compliance risks (continued)
Material legal and regulatory compliance failure (continued)

Key risk drivers:

- Lack of governance and oversight.
- Failure to comply with the SMS and contractual obligations.
- Failure to identify and respond to material changes in legal and regulatory requirements, including fast-moving new and changing laws.
- Lack of awareness by employees of the legal and regulatory requirements placed upon them and the business.
- Inadequate provision of systems and tools.
- Legal or regulatory compliance failure by a third party.
- Class action litigation and increasing regulatory fines.

Material controls:

- Externally appointed legal specialists and internal legal team monitoring and horizon scanning on legal and regulatory obligations and changes.
- Legal and contract subject matter experts aligned to functions and operations across the business supported by mandatory and bespoke training.
- Investment Committee and Business Life cycle Review Team ("BLRT") bid process and governance supported by Trading Principles.
- Third-party due diligence on customers and suppliers.
- Targeted compliance and assurance reviews.
- Speak Up process and systems and corporate investigation case management system.
- Group led ethics and compliance tools, frameworks and platforms, including anti-bribery and corruption.
- Trading principles refresh and enhanced BLRT and Investment Committee requirements.
- Ongoing targeted compliance and assurance reviews.
- SMS policies and procedures including data protection and fraud.
- Serco Essentials training.

Mitigation priorities:

- Maturing legislation tracking and horizon scanning on key new laws and regulations across global stakeholder map.
- Greater use of data and trend analysis.
- Embedding risk-based third-party due diligence including modern slavery risk assessment.
- Continuing development of Serco Essentials training programmes including Code of Conduct training.
- SMS refresh and implementation, including new governance policy.
- Supplier review and improvements to various key tools such as Speak Up and onboarding.

Strategic Report (continued)
for the Year Ended 31 December 2022

Corporate Governance Arrangements

As required under the Companies (Miscellaneous Reporting) Regulations 2018, this section of the Strategic Report describes the corporate governance arrangements of the Company during the year.

The Directors confirm that the Company has applied all of the Principles set out in the Wates Corporate Governance Principles for Large Private Companies 2018, a copy of which is available at www.frc.org.uk.

1. Purpose and Leadership

The Board of the Company is collectively responsible for promoting the success of the Company and ensuring that its values, strategy and culture align with its purpose. The purpose of the Company is set out on page 2 of these accounts, and the values, strategy and culture of the Company are aligned with those of the Company's ultimate parent company, Serco Group plc. Further information concerning the values, strategy and culture of the Group are provided in the 2022 Serco Group plc Annual Report and Accounts.

2. Board Composition

The Board of the Company's ultimate parent company, Serco Group plc, has delegated responsibility to the Executive Committee of Serco Group plc to ensure the effective direction and control of the business.

The Executive Committee has approved internal guidelines for the constitution of subsidiary boards which take into consideration the value and strategic importance of the contracts which operate through each subsidiary and the level of oversight required. This ensures that the Board of the Company is of an appropriate size and structure, and has an appropriate combination of skills, experience and knowledge to promote accountability and to provide constructive challenge to achieve effective decision making, and that the level of understanding is relevant to the Company's business needs and stakeholder interests.

The Board of Serco Group plc is committed to improving gender and ethnic diversity on the Serco Group plc Board and in the senior management population within the Group from which appointments to the Board of the Company are selected. Further details of how the Serco Group plc Board Diversity Policy is reviewed and assessed can be found on page 137 of the 2022 Serco Group plc Annual Report and Accounts. Details of how diversity and inclusion is promoted across the Group can be found in the People Report 2022, which is available on the Serco Group plc website, www.serco.com.

Details of how the members of the Board of the Company are supported in continued investment in personal and professional development are provided on page 47 of the 2022 Serco Group plc Annual Report and Accounts.

3. Director Responsibilities

The internal affairs of the Company are governed by the SMS. The SMS ensures clear levels of accountability and governance through policies, standards and procedures concerning:

- Business Conduct and Ethics
- Business Continuity and Crisis Management
- Business Development
- Environment and Climate Change
- Finance
- Governance
- Health and Safety
- Information Integrity
- Information Technology
- Operations
- People
- Procurement and Supply Chain
- Quality
- Risk Management
- Security

Strategic Report (continued)
for the Year Ended 31 December 2022

Corporate Governance Arrangements (continued)

3. Director Responsibilities (continued)

The policy statements can be found on the Serco Group plc website, www.serco.com.

4. Opportunity and Risk

The SMS includes policies, standards and procedures to identify future opportunities for innovation and entrepreneurship, and to ensure that business development is managed through organisational structures with clearly defined responsibilities and decision points. A specific procedure describes reserved powers and delegated powers of authority that apply within the Serco Group and its subsidiaries, including processes for approval of business opportunities of a certain value.

The Company leverages the risk management processes of its ultimate parent company, Serco Group plc, see pages 3 to 24 of the Annual Report for further details.

5. Remuneration

The Company is a subsidiary of Serco Group plc. The remuneration of its Directors, and the approach to remuneration for all colleagues within Serco Limited, follows the principles and philosophy of remuneration at Serco as set out in the Serco Group plc Directors' Remuneration Policy. The Remuneration Policy is set by the Remuneration Committee of Serco Group plc taking into consideration the pay and conditions of the wider workforce, and general practice in the external market. Full details of our approach to remuneration, and the framework applied throughout the Group, can be found in our 2020 Directors' Remuneration Report. The approach to remuneration is compliant with the provisions of the UK Corporate Governance Code.

6. Stakeholder Relationships and Engagement

The Company leverages the Environmental, Social and Governance ('ESG') agenda of its ultimate parent company, Serco Group plc, which is driven by the ESG Framework of the Group. Serco Group publishes an annual ESG report which details its commitment, strategy and performance which is available on the Serco Group plc website, www.serco.com.

The SMS includes workforce policies and procedures for reporting concerns regarding violations of Group values, policies or the Group Code of Conduct.

The Board of the Company is responsible for overseeing meaningful engagement with stakeholders, including the workforce, and must have regard to their views when taking decisions. The ways in which interests of stakeholders have been considered and the manner in which engagement is achieved is set out on pages 23 to 35 of the this Annual Report.

Section 172 (1) Statement

The Company is part of the Serco Group plc group of companies (the 'Group'), and the Board of Directors of its ultimate parent company, Serco Group plc, (the 'Serco Group plc Board') delegates day-to-day decision-making to the Executive Directors of Serco Group plc and, within defined levels of costs and impact, the Group Divisional leadership teams which includes the Directors of the Company, through a governance framework which, in addition to financial authorities, also covers areas such as risk, ethics, and new sector or country approaches.

The Group's governance framework is designed to drive high standards of business conduct across the Group and covers the values and behaviours expected of our employees, the standards to which they must adhere, how we engage with stakeholders and how the Board of Serco Group plc looks to ensure that we have a robust system of control and assurance processes.

Strategic Report (continued)
for the Year Ended 31 December 2022

Section 172 (1) Statement (continued)

The Directors of the Company consider that by adopting and adhering to the Group's governance framework they ensure that they give due care and consideration to discharging their duties under the Companies Act 2006, including their duty to act in the way they consider, in good faith, would most likely promote the success of the Company for the benefit of its members as a whole, taking into account the factors listed in section 172(1)(a) to (f) of the Companies Act 2006. This disclosure describes how the Board has had regard to those matters and forms the Directors' statement required under section 414CZA of the Companies Act 2006.

Further details of the Group's governance framework is provided in the Serco Group plc 2022 Annual Report on pages 119.

The Company's principal activity 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, health, justice, immigration, and citizens services on behalf of the Group, and therefore the Directors consider the needs of the Group in its decision-making as its direct stakeholders and looks to the activities undertaken by the Board of Directors of Serco Group plc (the 'Serco Group plc Board'), the Company's ultimate parent company, in engaging with the Group's wider stakeholders.


The Group's Environmental, Social and Governance ('ESG') Framework, of which the Company forms part, is structured around our key stakeholder and focus on our approach to and progress in delivering our ESG commitments has continued. The Group's progress and performance is summarised in the ESG section of the Serco Group plc 2022 Annual Report on pages 36 to 82.

Further information on how the Serco Group plc Board had regard to the matters set out in section 172 of the Companies Act 2006 can be found on pages 121 to 126 of the Serco Group plc 2022 Annual Report.

Streamlined Energy and Carbon Reporting (SECR)

Serco Limited is going to play its part to address climate change and further details on the goals set by the Directors along with emissions related information can be found in the Serco Group plc 2022 Annual Report and Accounts on pages 36 to 73.

Approved by the Board on 29 June 2023 and signed on its behalf by:


Nazim Girnary (Jun 29, 2023 14:48 GMT+1)
.....
N Girnary
Director

**Directors' Report
for the Year Ended 31 December 2022**

The Directors present their report and the financial statements for the year ended 31 December 2022.

Directors of the Company

The Directors, who held office throughout the year, and subsequently to the date of this report, unless otherwise stated, were as follows:

A A Kirby
N Girnary
M W Irwin (resigned on 1 January 2023)
H Shaw (appointed on 1 January 2023)

Going concern

The Company has net current assets of £450.7m as at 31 December 2022 (2021: £506.6m) including a £385.9m intercompany receivable which is repayable on demand although not intended to be recalled in the next year (2021: £348.4m) and a profit for the year then ended of £2.9m (2021: £193.1m). The Company's financial forecasts for the period of going concern indicate that the Company has sufficient financial resources to meet its financial obligations as they fall due during the period of assessment, considered to be twelve months from the signing date of these financial statements.

The Company is dependent on the availability of the intercompany financing facility that it uses to meet its day to day working capital requirements and therefore has obtained a letter of support from the Group's ultimate parent, Serco Group plc. Serco Group plc has indicated its intention to continue to make available such funds as are needed by the Company for the period of this assessment. The Directors of the Company have been made aware of the going concern assessment which has been performed in respect of the Group. The Directors believe they are able to place reliance on this letter of support, which is not legally binding, for the reasons discussed below.

At 31 December 2022, the Group's principal debt facilities comprised a £350.0m revolving credit facility (of which £nil was drawn) and £266.0m of US private placement notes, giving £616.0m of committed credit facilities and committed headroom of £402.0m. The principal financial covenant ratios are consistent across the private placement loan notes and revolving credit facility. As at 31 December 2022, the Group's primary restricting covenant, its leverage ratio, is below the covenant of 3.5x and is below the Group's target range of 1x-2x at 0.78x.

The Directors of the Group have undertaken a rigorous assessment of going concern and liquidity, taking into account financial forecasts, as well as the potential impact of key uncertainties and sensitivities on the Group's future performance. In making this assessment the Directors of the Group have considered the Group's existing debt levels, the committed funding and liquidity positions under its debt covenants, its ability to generate cash from trading activities, and its working capital requirements. The Directors of the Group have also identified a series of mitigating actions that could be used to preserve cash in the business should the need arise.

The basis of the assessment continues to be the budget approved by the Serco Group plc Board. The budget is prepared annually for the next two-year period and is based on a bottom-up approach to all of the Group's existing contracts, potential new contracts and administrative functions.

Directors' Report (continued)
for the Year Ended 31 December 2022

Going concern (continued)

Owing to the unprecedented levels of inflation driven by geopolitical factors, the Directors of the Group have considered the Group's resilience to rising costs. Due to the nature of the Group's operations, almost all of the revenue base has some form of inflationary protection, whether it be through contractual indexation mechanisms, cost plus billing, or being short term in nature. Though the timing of such protections becoming effective may, in the short term, differ from the impact of cost pressures, it is expected that the current inflation levels will not have a material impact on the Group's profitability.

The Directors of the Group believe that appropriate sensitivities in assessing the Group's ability to continue as a going concern are to model reductions in the Group's win rates for bids and extensions, and reductions in profit margins. Due to the diversity in the Group's operations, the Directors of the Group believe that a reverse stress test of these sensitivities to assess the headroom available under the Group's debt covenants and available liquidity provides meaningful analysis of the Group's ability to continue as a going concern. Based on the headroom available, the Directors are then able to assess whether the reductions required to breach the Group's financial covenants, or exhaust available liquidity, are plausible.

This reverse stress test assumes that the US private placement loan of £45m due to mature during the assessment period is repaid and no additional refinancing occurs. On this basis the Group can afford to be unsuccessful on 80% of its bids and extensions and suffer a reduction in profit margin of 80 basis points below the Group's forecast, whilst still retaining sufficient liquidity to meet all liabilities as they fall due and remain compliant with the Group's financial covenants.

In respect of win rates, rebids and extensions have a more significant impact on the Group's revenue than new business wins during the assessment period. The Group has won more than 85% of its rebids and available contract extensions by volume over the last two years, therefore a reduction of 80% or more to the budgeted bid and extensions rates is not considered plausible. The Group does not generally bid for contracts at margins below its target range.

In respect to margin reduction, due to the diversified nature of the Group's portfolio of long-term contracts and the fact that the Group has met or exceeded its full year guidance for the last five years, a reduction in margin of 80bps versus the Group's budget is not considered plausible within the assessment period combined with an 80% reduction in bid and extensions rates.

Consequently, the Directors of the Group are confident that the Group will have sufficient funds to continue to meet its liabilities as they fall due for at least 12 months from the date of approval of the financial statements and have provided a letter of support which enables the Directors to conclude that the Company will too. The financial statements have therefore been prepared on a going concern basis.

Research and Development

The Company is involved in research and development activities. The total charge relating to research and development activities included in profit or loss for the year ended 31 December 2022 was £0.5m (2021: credit of £0.1m).

Proposed dividend

The Directors do not recommend the payment of a dividend (2021: £nil).

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.

Directors' Report (continued)
for the Year Ended 31 December 2022

Political contributions

The Company made no political donations or incurred any political expenditure during the year (2021: £nil).

Corporate Governance Arrangements

Corporate Governance Arrangements are referred to in Strategic Report on page 20 to 21.

Branch offices

The Company operates through branches in France, Italy, Qatar and the United Arab Emirates.

Streamlined Energy and Carbon Reporting (SECR)

Streamlined Energy and Carbon Reporting is referred to in Strategic Report on page 22.

Employee Engagement

Employee Engagement is referred to in the Strategic Report on page 22.

Disclosure of information to auditor

The Directors have taken steps that they ought to have taken as Directors in order to make themselves aware of any relevant audit information and to establish that the Company's auditor is aware of that information. The Directors confirm that there is no relevant information that they know of and of which they know the auditor is unaware.

Risks and uncertainties

A review of risks is undertaken in the Strategic Report.

Reappointment of auditor

Pursuant to Section 487 of the Companies Act 2006, the auditor will be deemed to be reappointed and KPMG LLP will therefore continue in office.

Post balance sheet events

There were no post balance sheet events affecting the Company since the year end.

Approved by the Board on 29 June 2023 and signed on its behalf by:


Nazim Girnary (Jun 29, 2023 14:48 GMT+1)

N Girnary
Director

Statement of Directors' Responsibilities in respect of the Strategic Report, the Directors' Report and the Financial Statements

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

Company law requires the Directors to prepare financial statements for each financial year. Under that law they have elected to prepare the financial statements in accordance with UK accounting standards and applicable law (UK Generally Accepted Accounting Practice), 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 judgements and estimates that are reasonable and prudent;
- state whether applicable UK accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements;
- assess the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and
- use the going concern basis of accounting unless they either intend to liquidate the Company or to cease operations, or have no realistic alternative but to do so.

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 responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error, and have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Company and to prevent and detect fraud and other irregularities.

Independent Auditor's Report to the Members of Serco Limited

Opinion

We have audited the financial statements of Serco Limited (the "Company") for the year ended 31 December 2022 which comprise the Profit and Loss Account, the Statement of Comprehensive Income, the Balance Sheet, the Statement of Changes in Equity, and related notes, including the accounting policies in note 2.

In our opinion the financial statements:

- give a true and fair view of the state of the Company's affairs as at 31 December 2022 and of its profit for the year then ended;
- have been properly prepared in accordance with UK accounting standards, including FRS 101 *Reduced Disclosure Framework*; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities are described below. We have fulfilled our ethical responsibilities under, and are independent of the Company in accordance with, UK ethical requirements including the FRC Ethical Standard as applied to other entities of public interest. We believe that the audit evidence we have obtained is a sufficient and appropriate basis for our opinion.

During 2023, we identified that a KPMG member firm had provided foreign language translation services to the Company during 2022. The services, which have been terminated, were administrative in nature and did not involve any management decision-making or bookkeeping. The work had no direct or indirect effect on Serco Limited's financial statements.

In our professional judgment, we confirm that based on our assessment of the breaches, our integrity and objectivity as auditor has not been compromised and we believe that an objective, reasonable and informed third party would conclude that the provision of this service would not impair our integrity or objectivity. The Board of Directors concurred with this view.

Going concern

The Directors have prepared the financial statements on the going concern basis as they do not intend to liquidate the Company or to cease its operations, and as they have concluded that the Company's financial position means that this is realistic. They have also concluded that there are no material uncertainties that could have cast significant doubt over its ability to continue as a going concern for at least a year from the date of approval of the financial statements ("the going concern period").

In our evaluation of the Directors' conclusions, we considered the inherent risks to the Company's business model and analysed how those risks might affect the Company's financial resources or ability to continue operations over the going concern period.

Our conclusions based on this work:

- we consider that the Directors' use of the going concern basis of accounting in the preparation of the financial statements is appropriate;
- we have not identified, and concur with the Directors' assessment that there is not, a material uncertainty related to events or conditions that, individually or collectively, may cast significant doubt on the Company's ability to continue as a going concern for the going concern period.

However, as we cannot predict all future events or conditions and as subsequent events may result in outcomes that are inconsistent with judgements that were reasonable at the time they were made, the above conclusions are not a guarantee that the Company will continue in operation.

Independent Auditor's Report to the Members of Serco Limited (continued)

Fraud and breaches of laws and regulations - ability to detect

Identifying and responding to risks of material misstatement due to fraud

To identify risks of material misstatement due to fraud ("fraud risks") we assessed events or conditions that could indicate an incentive or pressure to commit fraud or provide an opportunity to commit fraud. Our risk assessment procedures included:

- Enquiring of Directors, internal audit, internal legal counsel, and inspection of policy documentation as to the Company's high-level policies and procedures to prevent and detect fraud, including the internal audit function, and the Company's channel for "whistleblowing", as well as whether they have knowledge of any actual, suspected or alleged fraud.
- Reading Board of Directors meeting minutes;
- Considering remuneration incentive schemes and performance targets for management, and directors.
- Using analytical procedures to identify any usual or unexpected relationships.

We communicated identified fraud risks throughout the audit team and remained alert to any indications of fraud throughout the audit.

As required by auditing standards, and taking into account our overall knowledge of the control environment, we perform procedures to address the risk of management override of controls and the risk of fraudulent revenue recognition, in particular:

- the risk that variable revenue is inappropriately recognised.
- the risk that management may be in a position to make inappropriate accounting entries; and
- the risk of bias in accounting estimates such as assessing whether long-term contracts are onerous determining provision for dispute and litigation are adequate and pension assumptions.

We did not identify any additional fraud risks.

We also performed procedures including:

- Identifying journal entries and other adjustments to test based on risk criteria and comparing the identified entries to supporting documentation. These included those posted by senior finance management/those posted to unusual accounts and those posted to seldom accounts.
- Assessing whether the judgements made in making accounting estimates are indicative of a potential bias.

Identifying and responding to risks of material misstatement related to compliance with laws and regulations

We identified areas of laws and regulations that could reasonably be expected to have a material effect on the financial statements from our general commercial and sector experience, and through discussion with the Directors and other management (as required by auditing standards), and from inspection of the Company's regulatory and legal correspondence and discussed with the Directors and other management the policies and procedures regarding compliance with laws and regulations.

We communicated identified laws and regulations throughout our team and remained alert to any indications of non-compliance throughout the audit.

The potential effect of these laws and regulations on the financial statements varies considerably.

Firstly, the Company is subject to laws and regulations that directly affect the financial statements including financial reporting legislation (including related companies legislation), distributable profits legislation, and taxation legislation and we assessed the extent of compliance with these laws and regulations as part of our procedures on the related financial statement items.

Secondly, the Company is subject to many other laws and regulations where the consequences of non-compliance could have a material effect on amounts or disclosures in the financial statements, for instance through the imposition of fines or litigation or the loss of the Company's license to operate. We identified the following areas as those most likely to have such an effect:

Independent Auditor's Report to the Members of Serco Limited (continued)

Fraud and breaches of laws and regulations - ability to detect (continued)

Identifying and responding to risks of material misstatement related to compliance with laws and regulations (continued)

- health and safety, given the front-line nature of many of the Company's operations;
- data protection laws, such as the General Data Protection Regulations in Europe due to the number of employees and the services performed for customers in Europe;
- anti-bribery and corruption, recognising the Governmental nature of many of the Company's customers;
- employment law, due to the significant number of employees the Company employs; and
- Single source procurement regulations in the UK, due to the contracting environment.

Auditing standards limit the required audit procedures to identify non-compliance with these laws and regulations to enquiry of the Directors and other management and inspection of regulatory and legal correspondence, if any. Therefore if a breach of operational regulations is not disclosed to us or evident from relevant correspondence, an audit will not detect that breach.

Context of the ability of the audit to detect fraud or breaches of law or regulation

Owing to the inherent limitations of an audit, there is an unavoidable risk that we may not have detected some material misstatements in the financial statements, even though we have properly planned and performed our audit in accordance with auditing standards. For example, the further removed non-compliance with laws and regulations is from the events and transactions reflected in the financial statements, the less likely the inherently limited procedures required by auditing standards would identify it.

In addition, as with any audit, there remained a higher risk of non-detection of fraud, as these may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal controls. Our audit procedures are designed to detect material misstatement. We are not responsible for preventing non-compliance or fraud and cannot be expected to detect non-compliance with all laws and regulations.

Strategic report and directors' report

The Directors are responsible for the strategic report and the directors' report. Our opinion on the financial statements does not cover those reports and we do not express an audit opinion thereon.

Our responsibility is to read the strategic report and the directors' report and, in doing so, consider whether, based on our financial statements audit work, the information therein is materially misstated or inconsistent with the financial statements or our audit knowledge. Based solely on that work:

- we have not identified material misstatements in the strategic report and the directors' report;
- in our opinion the information given in those reports for the financial year is consistent with the financial statements; and
- in our opinion those reports have been prepared in accordance with the Companies Act 2006.

Matters on which we are required to report by exception

Under the Companies Act 2006 we are required 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.

We have nothing to report in these respects.

Independent Auditor's Report to the Members of Serco Limited (continued)

Directors' responsibilities

As explained more fully in their statement set out on page 26, the Directors are responsible for: the preparation of the financial statements and for being satisfied that they give a true and fair view; such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and using the going concern basis of accounting unless they either intend to liquidate the Company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue our opinion in an auditor's report. Reasonable assurance is a high level of assurance, but does not guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

A fuller description of our responsibilities is provided on the FRC's website at www.frc.org.uk/auditorsresponsibilities.

The purpose of our audit work and to whom we owe our responsibilities

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.



John Luke (Senior Statutory Auditor)
for and on behalf of KPMG LLP, Statutory Auditor
Chartered Accountants
15 Canada Square
Canary Wharf
London
United Kingdom
E14 5GL

Date: 29 June 2023

Serco Limited

**Profit and Loss Account
for the Year Ended 31 December 2022**

| | Note | 2022 £m | 2021 £m |
|---|------|--------------|--------------|
| Turnover | 4 | 1,897.7 | 2,111.2 |
| Cost of sales | | (1,772.7) | (1,931.1) |
| Gross profit | | 125.0 | 180.1 |
| Administrative expenses | | (104.4) | (113.3) |
| Amortisation of intangible fixed assets | 13 | (7.3) | (8.5) |
| Exceptional operating items | 5 | (9.9) | (0.3) |
| Operating profit | 6 | 3.4 | 58.0 |
| Interest receivable and similar income | 9 | 6.4 | 1.3 |
| Interest payable and similar charges | 10 | (5.6) | (4.7) |
| Profit before tax | | 4.2 | 54.6 |
| Tax on profit | 11 | (1.3) | 138.5 |
| Profit for the financial year | | 2.9 | 193.1 |

The above results were derived from continuing operations.

The notes on pages 36 to 78 form an integral part of these financial statements.

Serco Limited

**Statement of Comprehensive Income
for the Year Ended 31 December 2022**

| | Note | 2022 £m | 2021 £m |
|---|------|---------------|--------------|
| Profit for the year | | 2.9 | 193.1 |
| Other comprehensive income for the year: | | | |
| Items that will not be reclassified subsequently to profit or loss | | | |
| Tax related to retirement benefit obligation reserve* | | 27.4 | (21.4) |
| Net actuarial (loss)/gain on defined benefit pension schemes* | 22 | (108.0) | 65.1 |
| Total | | (80.6) | 43.7 |
| Items that may be reclassified subsequently to profit or loss | | | |
| Net gain on cash flow hedges** | | - | 0.2 |
| Unrealised gain on derivatives | | 0.5 | - |
| Tax credit on net hedging reserve | | (0.1) | - |
| Total other comprehensive (expense)/income | | (80.2) | 43.9 |
| Total comprehensive income for the year | | (77.3) | 237.0 |

* Recorded in retained earnings in the Statement of Changes in Equity.

** Recorded in hedging and translation reserve in the Statement of Changes in Equity.

The notes on pages 36 to 78 form an integral part of these financial statements.

Serco Limited

**Balance Sheet
as at 31 December 2022
Registration number: 00242246**

| | Note | 2022 £m | 2021 £m |
|---|------|----------------|----------------|
| Fixed assets | | | |
| Goodwill | 13 | 6.7 | 6.7 |
| Intangible assets | 13 | 23.0 | 26.2 |
| Property, plant and equipment | 14 | 376.5 | 373.0 |
| | | <u>406.2</u> | <u>405.9</u> |
| Current assets | | | |
| Stocks and work in progress | | 11.7 | 8.8 |
| Debtors: amounts falling due within one year | 17 | 262.6 | 245.4 |
| Debtors: amounts falling due after more than one year | 17 | 385.9 | 348.7 |
| Deferred tax assets | 12 | 174.3 | 149.5 |
| Corporation tax asset | | 4.0 | 0.1 |
| Derivative financial instruments - receivable | 25 | 0.6 | - |
| Defined benefit pension asset | 22 | 57.0 | 166.2 |
| | | <u>896.1</u> | <u>918.7</u> |
| Total assets | | <u>1,302.3</u> | <u>1,324.6</u> |
| Current liabilities | | | |
| Creditors: amounts falling due within one year | 18 | (378.5) | (348.3) |
| Loans and overdrafts | 19 | (35.8) | (17.1) |
| Corporation tax liabilities | | (1.4) | (3.5) |
| Derivative financial instruments | 25 | - | (0.1) |
| Provisions | 21 | (29.7) | (43.1) |
| | | <u>(445.4)</u> | <u>(412.1)</u> |
| Net current assets | | <u>450.7</u> | <u>506.6</u> |
| Total assets less current liabilities | | <u>856.9</u> | <u>912.5</u> |
| Creditors: amounts falling due after more than one year | 20 | (457.5) | (437.2) |
| Provisions | 21 | (19.9) | (11.1) |
| | | <u>(477.4)</u> | <u>(448.3)</u> |
| Defined benefit pension liability | 22 | - | (16.7) |
| Net assets | | <u>379.5</u> | <u>447.5</u> |

Serco Limited

Balance Sheet (continued)
as at 31 December 2022

Capital and reserves

| | | | |
|----------------------------|----|--------------|--------------|
| Called up share capital | 23 | 0.8 | 0.8 |
| Share premium account | | 1,108.9 | 1,108.9 |
| Other reserves | | 0.4 | - |
| Profit And Loss Account | | (730.6) | (662.2) |
| Shareholder's funds | | <u>379.5</u> | <u>447.5</u> |

These financial statements were approved by the Board on 29 June 2023 and signed on its behalf by:


Nazim Girmay (Jun 29, 2023 14:48 GMT+1)

.....
N Girmay
Director

The notes on pages 36 to 78 form an integral part of these financial statements.

Serco Limited

**Statement of Changes in Equity
for the Year Ended 31 December 2022**

| | Called up share capital £m | Share premium reserve £m | Other reserves £m | Profit and loss account £m | Total £m |
|--|----------------------------------|-----------------------------------|-------------------------|----------------------------------|-------------|
| At 1 January 2021 | 0.8 | 1,108.9 | (0.2) | (900.3) | 209.2 |
| Profit for the year | - | - | - | 193.1 | 193.1 |
| Retirement benefit obligations | - | - | 0.2 | 43.7 | 43.9 |
| Total comprehensive income for the year | - | - | 0.2 | 236.8 | 237.0 |
| Credits in relation to share based payments | - | - | - | 1.3 | 1.3 |
| At 31 December 2021 | 0.8 | 1,108.9 | - | (662.2) | 447.5 |
| Profit for the year | - | - | - | 2.9 | 2.9 |
| Retirement benefit obligations | - | - | - | (80.6) | (80.6) |
| Hedging and translation | - | - | 0.4 | - | 0.4 |
| Total comprehensive income for the year | - | - | 0.4 | (77.7) | (77.3) |
| Credits in relation to share based payments | - | - | - | 9.3 | 9.3 |
| At 31 December 2022 | 0.8 | 1,108.9 | 0.4 | (730.6) | 379.5 |

The notes on pages 36 to 78 form an integral part of these financial statements.

**Notes to the Financial Statements
for the Year Ended 31 December 2022**

1. General information

The Company is a private company limited by share capital, incorporated and domiciled in the United Kingdom.

The address of its registered office is:
Serco House
16 Bartley Wood Business Park
Bartley Way
Hook
Hampshire
RG27 9UY

The registered company number is 00242246. The nature of the Company's operations and its principal activities are set out in the Strategic Report on page 2.

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

The level of rounding is to the nearest tenth of a million ('m) unless otherwise stated.

2. Accounting policies

2.1 Summary of significant accounting policies and key accounting estimates

The principal accounting policies applied in the preparation of these financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

2.2 Basis of preparation

These financial statements were prepared in accordance with Financial Reporting Standard 101 Reduced Disclosure Framework ("FRS 101").

In preparing these financial statements, the Company applies the recognition, measurement and disclosure requirements of UK-adopted international accounting standards in conformity with the requirements of the Companies Act 2006 ("UK-adopted IFRSs"), but makes amendments where necessary in order to comply with Companies Act 2006 and has set out below where advantage of the FRS 101 disclosure exemptions has been taken.

2.3 Summary of disclosure exemptions

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, fair value measurement, 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 26.

The financial statements have been prepared on the historical cost 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.

**Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022**

2. Accounting policies (continued)

2.4 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 & Wales.

2.5 New and amended standards and interpretations

There are no new or amended standards or interpretations for annual periods beginning on or after 1 January 2022 that have a material impact on the financial statements of the Company.

2.6 Changes in accounting policies

No modifications have occurred either during the year ended 31 December 2022 or 31 December 2021.

2.7 Going concern

The Company has net current assets of £450.7m as at 31 December 2022 (2021: £506.6m) including a £385.9m intercompany receivable which is repayable on demand although not intended to be recalled in the next year (2021: £348.4m) and a profit for the year then ended of £2.9m (2021: £193.1m). The Company's financial forecasts for the period of going concern indicate that the Company has sufficient financial resources to meet its financial obligations as they fall due during the period of assessment, considered to be twelve months from the signing date of these financial statements.

The Company is dependent on the availability of the intercompany financing facility that it uses to meet its day to day working capital requirements and therefore has obtained a letter of support from the Group's ultimate parent, Serco Group plc. Serco Group plc has indicated its intention to continue to make available such funds as are needed by the Company for the period of this assessment. The Directors of the Company have been made aware of the going concern assessment which has been performed in respect of the Group. The Directors believe they are able to place reliance on this letter of support, which is not legally binding, for the reasons discussed below.

At 31 December 2022, the Group's principal debt facilities comprised a £350.0m revolving credit facility (of which £nil was drawn) and £266.0m of US private placement notes, giving £616.0m of committed credit facilities and committed headroom of £402.0m. The principal financial covenant ratios are consistent across the private placement loan notes and revolving credit facility. As at 31 December 2022, the Group's primary restricting covenant, its leverage ratio, is below the covenant of 3.5x and is below the Group's target range of 1x-2x at 0.78x.

**Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022**

2. Accounting policies (continued)

2.7 Going concern (continued)

The Directors of the Group have undertaken a rigorous assessment of going concern and liquidity, taking into account financial forecasts, as well as the potential impact of key uncertainties and sensitivities on the Group's future performance. In making this assessment the Directors of the Group have considered the Group's existing debt levels, the committed funding and liquidity positions under its debt covenants, its ability to generate cash from trading activities, and its working capital requirements. The Directors have also identified a series of mitigating actions that could be used to preserve cash in the business should the need arise.

The basis of the assessment continues to be the budget approved by the Serco Group plc Board. The budget is prepared annually for the next two-year period and is based on a bottom-up approach to all of the Group's existing contracts, potential new contracts and administrative functions.

Owing to the unprecedented levels of inflation driven by geopolitical factors, the Directors of the Group have considered the Group's resilience to rising costs. Due to the nature of the Group's operations, almost all of the revenue base has some form of inflationary protection, whether it be through contractual indexation mechanisms, cost plus billing, or being short term in nature. Though the timing of such protections becoming effective may, in the short term, differ from the impact of cost pressures, it is expected that the current inflation levels will not have a material impact on the Group's profitability.

The Directors of the Group believe that appropriate sensitivities in assessing the Group's ability to continue as a going concern are to model reductions in the Group's win rates for bids and extensions, and reductions in profit margins. Due to the diversity in the Group's operations, the Directors believe that a reverse stress test of these sensitivities to assess the headroom available under the Group's debt covenants and available liquidity provides meaningful analysis of the Group's ability to continue as a going concern. Based on the headroom available, the Directors are then able to assess whether the reductions required to breach the Group's financial covenants, or exhaust available liquidity, are plausible.

This reverse stress test assumes that the US private placement loan of £45m due to mature during the assessment period is repaid and no additional refinancing occurs. On this basis the Group can afford to be unsuccessful on 80% of its bids and extensions and suffer a reduction in profit margin of 80 basis points below the Group's forecast, whilst still retaining sufficient liquidity to meet all liabilities as they fall due and remain compliant with the Group's financial covenants.

In respect of win rates, rebids and extensions have a more significant impact on the Group's revenue than new business wins during the assessment period. The Group has won more than 85% of its rebids and available contract extensions by volume over the last two years, therefore a reduction of 80% or more to the budgeted bid and extensions rates is not considered plausible. The Group does not generally bid for contracts at margins below its target range.

In respect to margin reduction, due to the diversified nature of the Group's portfolio of long-term contracts and the fact that the Group has met or exceeded its full year guidance for the last five years, a reduction in margin of 80bps versus the Group's budget is not considered plausible within the assessment period combined with an 80% reduction in bid and extensions rates.

Consequently, the Directors are confident that the Group will have sufficient funds to continue to meet its liabilities as they fall due for at least 12 months from the date of approval of the financial statements and have provided a letter of support which enables the Directors to conclude that the Company will too. The financial statements have therefore been prepared on a going concern basis.

**Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022**

2. Accounting policies (continued)

2.8 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 IFRS 16 Leases, or the calculation of net realisable value under IAS 2 Inventories or value in use under IAS 36 Impairment of Assets.

2.9 Revenue

The Company recognises revenue based on the principles set out in IFRS 15 Revenue from Contracts with Customers and is recognised in any period based on the delivery of performance obligations and an assessment of when control is transferred to the customer.

For all contracts, the Company determines whether each arrangement meets the definition of a contract under IFRS 15 and creates enforceable rights and obligations.

Contracts are combined if they are entered into at or near the same time and one or more of the following criteria are met:

- They are negotiated as a package with a single commercial objective.
- Consideration receivable in one contract depends on the other contract.
- Goods or services are a single performance obligation.

For contracts with multiple components, Management applies judgement to consider whether those promised goods and services are:

- a deliverable (i.e. a good or a service) that is distinct; or
- a series of distinct deliverables that are substantially the same and that have the same pattern of transfer to the customer (transferred over time using the same measure of progress).

At contract inception, the transaction price is the total amount of consideration to which the Company expects to be entitled to in exchange for transferring goods or services to a customer.

Once the total transaction price is determined, the Company allocates this to the identified performance obligations in proportion to their relative stand-alone selling prices and recognises revenue when (or as) those performance obligations are satisfied. Where there is only one performance obligation, no allocation is necessary as the full transaction price is allocated to the single performance obligation.

**Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022**

2. Accounting policies (continued)

2.9 Revenue (continued)

Where there is more than one performance obligation, the Company looks at each performance obligation separately to see if there is an observable price available, however due to the bespoke nature of the services provided by the Company there is normally no observable stand-alone selling price and the expected cost-plus margin approach is used. All bid models for new contracts are built up and negotiated with the customers on a cost-plus margin basis and therefore this approach most accurately reflects the commercial reality and the value of the benefits transferred to the customer.

The Company enters into contracts which contain extension periods where either the customer or both parties can choose to extend the contract or there is an automatic annual renewal and/or termination clauses that could impact the actual duration of the contract. Judgement is applied to assess the impact that these clauses have when determining the appropriate contract term. The term of the contract impacts both the period over which revenue from performance obligations may be recognised and the period over which contract fulfilment assets and capitalised bid and phase in costs are expensed.

Further details on revenue recognition for specific contract types are shown below.

Revenue recognition: Repeat service-based contracts

The majority of the Company's contracts are repeat service-based contracts where value is transferred to the customer over time as the core services are delivered. Therefore, in most cases revenue will be recognised on the output basis, based on direct measurements of the value to the customer of the services transferred to date relative to the remaining services under the contract. This is a faithful depiction of the transfer of services since the service delivered to the customer is unchanged. Where the output method is used, the Company often uses a method of time elapsed which requires minimal estimation. Certain repeat service-based contracts use output methods based upon user numbers; service activity levels; or fees collected. Where any price reductions within output-based contracts are contractual, but the level of service is not decreasing, revenue will be deferred from initial years to subsequent years in order for revenue to be recognised on a consistent basis.

There are certain contracts where a separate performance obligation has been identified for services where the pattern of delivery differs to the core services and which are capable of being distinct, such as asset construction or asset maintenance. In these instances, where the transfer of control is most closely aligned to our efforts in delivering the service, the input method is used to measure progress and revenue is recognised in direct proportion to costs incurred. In limited circumstances, other methods are used to measure progress under the input method, including resources consumed, time elapsed or labour hours expended. This is a faithful depiction of the transfer of services because costs (or other inputs) most accurately reflect the incremental benefits received by the customer from efforts to date.

**Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022**

2. Accounting policies (continued)

2.9 Revenue (continued)

Revenue recognition: Repeat service-based contracts (continued)

Where deemed appropriate, the Company will utilise the practical expedient within IFRS 15, allowing revenue to be recognised at the amount which the Company has the right to invoice, where that amount corresponds directly with the value to the customer of the Company's performance completed to date.

Under IFRS 15, unless upfront fees received from customers including transition payments can be clearly attributable to a distinct service the customer is obtaining, then such payments do not constitute a separate performance obligation and instead are deferred and spread over the life of the core services.

In general, the timing of satisfaction of performance obligations is consistent with when payment becomes due, other than in instances where up front win fees or transition payments are received, where in most instances these are deferred.

Any changes to the enforceable rights and obligations with customers and/or an update to the transaction price will not be recognised as revenue until there is evidence of customer agreement in line with the Company's policies.

Revenue recognition: Variable revenue

The Company has a number of contracts where at least an element of the revenue generated is variable in nature. Variability in revenue recognised can arise from a number of factors, including usage related volumes, graduated performance against contractual performance indicators, indexation linked pricing, profit sharing elements and customer decisions related to the provision of goods or services. Any variable amounts will only be recognised where it is highly probable that a significant reversal will not occur.

Revenue recognition: Long-term project-based contracts

The Company has a limited number of project-based long-term contracts. Revenue associated with these contracts is recognised at the point in time when control over the deliverable is passed to the customer.

Revenue recognition: Contract modifications

When a modification to an existing contract is approved, the Company first assesses whether it adds distinct goods or services to the existing contract that are priced commensurate with the stand-alone selling prices for those goods or services. If this is the case, then the modification is accounted for prospectively as a separate contract. If the pricing is not commensurate with the stand-alone selling prices for the goods or services and the new goods or services are not distinct from those in the original contract, then this is considered to form part of the original contract. Pricing is updated for the entirety of the revised contract and any historic adjustments recorded as a result are recognised as a cumulative adjustment to revenue in the period of the modification. If the pricing is not commensurate with the stand-alone selling prices for the goods or services and the new goods or services are distinct from those in the original contract, then this is considered to represent the termination of the original contract and the creation of a new contract which is accounted for prospectively from the date of modification.

Revenue recognition: Other

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

The Company has a limited number of pass through arrangements in respect of goods or services procured by the Company on behalf of customers where it assesses whether it is acting as a principal or as an agent.

Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022

2. Accounting policies (continued)

2.9 Revenue (continued)

Revenue recognition: Other (continued)

The Company is acting as principal if it is in control of a good or a service prior to transferring to the customer and gross revenue and costs are recognised.

More commonly, the Company is acting as agent where it is arranging for those goods or services to be provided to the customer without obtaining control, for example, where the Company is engaged to manage operations for a customer but procures goods or services on behalf and at the instructions of the customer in order to deliver the operation. When acting as an agent, only the fee or commission is recognised as revenue and the costs represent only the direct costs of facilitating the transaction.

Interest income is accrued for 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.

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

The Company has no material exposure to returns or refunds.

2.10 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 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, it affects neither the tax profit nor the accounting profit.

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries, 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.

**Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022**

2. Accounting policies (continued)

Tax (continued)

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.

2.11 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 statement of comprehensive income.

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. 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 reduced by the fair value of scheme assets. Any asset resulting from this calculation is limited to the present value of available refunds (which is only recognised to the extent that the Group 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.

2.12 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.

**Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022**

2. Accounting policies (continued)

2.13 Foreign currency transactions and balances

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 (SOI). Income and expense for overseas operations are translated at the average exchange rates for the period.

2.14 Goodwill

Goodwill is measured as the excess of the fair value of purchase consideration over the fair value of the net assets acquired and is recognised as an intangible asset when control is achieved. Negative goodwill is recognised immediately in the profit and loss account. Fair value measurements are based on provisional estimates and may be subject to amendment within one year of the acquisition, resulting in an adjustment to goodwill.

Goodwill itself does not generate independent cash flows and therefore, in order to perform required tests for impairment, it is allocated at inception to the specific cash generating units (CGUs) or groups of CGUs which are expected to benefit from the acquisition.

On the disposal of a business which includes all or part of a CGU, any attributable goodwill is included in the determination of the profit or loss on disposal.

The fair values associated with material business combinations are valued by external advisers and any amount of consideration which is contingent in nature is evaluated at the end of each reporting period, based on internal forecasts.

2.15 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.

Customer relationships can arise on the acquisition of subsidiaries and represent the incremental value expected to be gained as a result of existing contracts in the purchased business. These assets are amortised over a period that does not exceed the average length of the related contracts.

Licences comprise premiums paid for the acquisition of licences, while franchises represent costs incurred in obtaining franchise rights arising on the acquisition of franchises. These are amortised on a straight-line basis over the life of the respective licence or franchise.

Software and IT represent 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 average length of the related contracts.

**Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022**

2. Accounting policies (continued)

2.15 Other intangible assets (continued)

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

2.16 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.

Depreciation

Depreciation is charged so as to write off the cost of assets, other than land and properties under construction over their estimated useful lives, as follows:

| <i>Asset Class</i> | <i>Depreciation method and rate</i> |
|------------------------|--|
| 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% |
| Right-of-use assets | - Equally over the lease term from inception or equally over the remainder of the lease term from the date of a reassessment of the lease end date |

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.

Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022

2. Accounting policies (continued)

2.17 Leases

On entering into a lease, a lease liability is recorded equal to the value of future lease payments discounted at the appropriate incremental borrowing rate and, simultaneously, a right-of use-asset is created representing the right conferred to control the manner of use of the leased asset. The Company typically uses an appropriate incremental borrowing rate, based on the lease location and duration, as it typically does not have access to the interest rate implicit in the lease.

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 and corresponding assets are depreciated on a straight-line basis over the lease term.

The lease term is measured as the non-cancellable period of a lease, together with periods covered by an option to extend the lease if it is reasonably certain that the option will be exercised and periods covered by an option to terminate the lease if it is reasonably certain that the option will not be exercised. The lease term is reassessed if an event occurs which causes either the non-cancellable period to change, or another event occurs which changes the assessment of the likelihood of exercising an option included in the lease.

All changes to leases are accounted for on a prospective basis from the point at which the change is triggered.

Where, on inception, the term of a lease is less than twelve months or the value of the leased asset is less than £5,000, or both, rentals payable under the lease are charged to the profit and loss account on a straight-line basis over the term of the relevant lease.

2.18 Investments

Fixed asset investments

Investments held as fixed assets are stated at cost less provision for any impairment in value.

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.

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.

Where the Company enters into financial guarantee contracts to guarantee the indebtedness of other companies within its group, the Company considers these to be insurance arrangements and accounts for them as such. In this respect, the Company treats the guarantee contract as a contingent liability until such time as it becomes probable that the Company will be required to make a payment under the guarantee.

Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022

2. Accounting policies (continued)

2.19 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 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 Company 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.

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.

At each reporting date, the Company assesses whether there is an indication that a previously recognised impairment loss has reversed because of a change in the estimates used to determine the impairment loss. If there is such an indication, and the recoverable amount of the impaired asset, or CGU, subsequently increases, then the impairment loss is generally reversed.

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.

2.20 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 inventories to their present location and condition.

**Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022**

2. Accounting policies (continued)

2.21 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 where 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 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 be 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.

2.22 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.

2.23 Financial instruments

Where financial assets are not measured at fair value through profit and loss (FVTPL), there is a requirement to assess the carrying value of the assets by reference to the expected credit loss (ECL) associated with the asset. Under the ECL model, the Company calculates the allowance for credit losses by considering, on a discounted basis, the shortfall in cash receipts it would incur in various default scenarios and multiplying the shortfalls by the probability of each scenario occurring. The allowance is the sum of the probability weighted outcomes.

The primary financial assets carried by the Company which are not measured at FVTPL are trade receivables and intercompany receivables. Owing to the nature of counterparties in intercompany arrangements, and a detailed review of the ability of those counterparties to settle obligations as they fall due, there is no material ECL risk associated with intercompany balances. The Company's customer base is predominantly Government or Government-backed, and as a result, the Company's ECL at any given point in time across the entirety of the customer base is immaterial.

2.24 Trade payables

Trade payables are obligations to pay for goods or services that have been acquired in the ordinary course of business from suppliers. Accounts payable are classified as current liabilities if payment is due within one year or less (or in the normal operating cycle of the business if longer). If not, they are presented as non-current liabilities.

Trade payables are recognised initially at the transaction price and subsequently measured at amortised cost using the effective interest rate method.

**Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022**

2. Accounting policies (continued)

2.25 Loans

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

Loans are described as non-recourse loans and classified as such only if no Group company other than the relevant borrower has an obligation, under a guarantee or other arrangement, to repay the debt.

2.26 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.

2.27 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.

2.28 Share capital

Ordinary shares are classified as equity. Equity instruments are measured at the fair value of the cash or other resources received or receivable, net of the direct costs of issuing the equity instruments. If payment is deferred and the time value of money is material, the initial measurement is on a present value basis.

2.29 Defined benefit obligations arising from contractual obligations

Where the Company takes on a contract and assumes the obligation to contribute variable amounts to the defined benefit pension scheme throughout the period of the contract, the Company's share of the scheme assets and liabilities is calculated by reducing the scheme assets and liabilities with a franchise adjustment. The franchise adjustment represents the estimated amount of scheme deficit that will be funded outside the contract period. Subsequent actuarial gains and losses in relation to the Company's share of pension obligations are recognised in the statement of comprehensive income (SOCl).

**Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022**

2. Accounting policies (continued)

2.30 Share based payments

Where the fair value of share options requires the use of a valuation model, fair value is measured by use of Binomial Lattice, Black Scholes or Monte Carlo Simulation models depending on the type of scheme, as set out in note 34 of Serco Group plc Annual Report and Accounts. The expected life used in the models has been adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions, and behavioural considerations. Where relevant, the value of the option has also been adjusted to take account of market conditions applicable to the option.

2.31 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 26 of Serco Group plc Annual Report and Accounts.

Derivatives are initially recognised at fair value at the date a derivative contract is entered into and are subsequently re-measured 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 (fair value hedges), 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 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 statement of comprehensive income and described in note 26.

2.32 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.

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. The adjustment to the carrying amount of the hedged item arising from the hedged risk is amortised to profit or loss from that date.

Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022

2. Accounting policies (continued)

2.33 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 hedged 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.

2.34 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.

2.35 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

3. Critical accounting judgements 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 judgements 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.

Key sources of estimation uncertainty

Provisions for onerous contracts

Determining the carrying value of onerous contract provisions requires assumptions and complex judgements to be made about the future performance of the Company's contracts. 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. Due to the level of uncertainty and combination of variables associated with those estimates, there is a significant risk that there could be a material adjustment to the carrying amounts of onerous contract provisions within the next financial reporting period.

Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022

3. Judgements in applying accounting policies (continued)

Key sources of estimation uncertainty (continued)

Provisions for onerous contracts (continued)

Major sources of uncertainty which could result in a material adjustment within the next financial year are:

- The ability of the Company to maintain or improve operational performance to ensure costs or performance related penalties are in line with expected levels;
- Volume driven revenue and costs being within the expected ranges;
- The outcome of open claims made by or against a customer regarding contractual performance or contractual negotiations taking place where there is expected to be a positive outcome from the Group's perspective; and
- The ability of suppliers to deliver their contractual obligations on time and on budget.

In the current year, there has been an overall net charge of new and existing OCPs of £2.9m. 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.

The future range of possible outcomes in respect of those assumptions and significant judgements made to determine the carrying value of onerous contracts could result in either a material increase or decrease in the value of onerous contract provisions in the next financial year. The extent to which actual results differ from estimates made at the reporting date depends on the combined outcome and timing of a large number of variables associated with performance across multiple contracts.

The individual provisions are discounted where the impact is assessed to be significant. When used, discount rates are calculated based on the estimated risk-free rate of interest for the region in which the provision is located and matched against the ageing profile of the provision.

Onerous contract provisions totalling £3.4m are estimated for individual contracts, based on the specific characteristics of the contract including possible contract variations, estimates of transaction price such as variable revenues and forecast costs to fulfil those contracts. Management has considered the nature of the estimate for onerous contract provisions and concluded that it is reasonably possible that outcomes within the next financial year may be different from Management's assumptions and could, in aggregate, require a material adjustment to the onerous contract provision. However, due to the estimation uncertainty across numerous contracts each with different characteristics, it is not practical to provide a quantitative analysis of the aggregated judgements that are applied, and Management does not believe that disclosing a potential range of outcomes would provide meaningful information to a reader of the financial statements.

Whilst the focus of the judgement is to determine whether the Group is required to record an onerous contract provision, Management also inherently assess whether any assets dedicated to the contract are required to be impaired where contracts are forecast to make sustainable losses in the future. In accordance with IAS 37, the Group will impair assets dedicated to the contract before the recognition of an onerous contract provision.

Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022

3. Judgements in applying accounting policies (continued)

Key sources of estimation uncertainty (continued)

Retirement benefit obligations

Identifying whether the Company has a retirement benefit obligation as a result of contractual arrangements entered into requires a level of judgement, largely driven by the legal position held between the Company, the customer and the relevant pension scheme. The Group's retirement benefit obligations are covered in note 28 of the Serco Group plc financial statements.

The calculation of retirement benefit obligations is dependent on material key assumptions including discount rates, mortality rates, inflation rates and future contribution rates.

In accounting for the defined benefit schemes, the Company has applied the principle that the asset recognised for the Serco Pension and Life Assurance Scheme (SPLAS) and the shared cost section of the Railways Pension Scheme is equal to the full surplus that will ultimately be available to the Company as a future refund.

No pension assets are invested in the Company's own financial instruments or property.

Pension assets held by insurance companies including the annuity policies in SPLAS are valued at the equal and opposite of the defined benefit obligations that they insure.

The SPLAS pension scheme invests into private debt funds which do not have an observable market price and are remeasured to fair value at each reporting date. The valuation methodology relied upon the Net Asset Value provided by the fund administrator at 30 September adjusted for actual cash flows in the period to 31 December. The Group has undertaken a risk assessment to assess whether this industry standard valuation methodology remains the Group's best estimate at 31 December 2022 following the significant market volatility experienced in the third quarter of the year. The Group has concluded that although there is heightened estimation uncertainty, this methodology provides the most accurate valuation and estimate for Management.

Critical accounting judgements

Deferred tax

Deferred tax assets are recognised on tax deductible temporary differences to the extent that it is probable that taxable profit will be available against which they can be utilised. Significant Management judgement is required to determine the amount of the deferred tax asset that should be recognised, based upon the likely timing, geography and level of future taxable profits. Since a significant portion of the deductible temporary differences relate to historic tax losses, there has been historic evidence that future taxable profits may not be available.

A £174.3m tax asset is recognised on the Company's balance sheet at 31 December 2022 (2021 £149.5m) on the basis that structural changes in the underlying UK business indicate a sustained return to profitability which will enable future tax deductions within the UK to be utilised. The return to profitability is as a result of onerous contracts ending, being replaced by profitable long-term contracts as well as a significant reduction in exceptional restructuring spend following the strategy review in 2015, which also reduced the level of overhead spend within the UK business.

Further details on deferred taxes are disclosed in note 11.

Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022

4. Turnover

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

| | 2022 £m | 2021 £m |
|--|----------------|----------------|
| Turnover as disclosed in the profit and loss account | <u>1,897.7</u> | <u>2,111.2</u> |

The Company manages its business on an operating segment basis and these segments are the basis on which the Company reports its segment information. The Company's reportable operating segments are as follows:

- UK & Europe: Services for sectors including Citizen Services, Defence, Health, Justice & Immigration and Transport delivered to UK Government, UK devolved authorities and other public sector customers in the UK and Europe; and
- Middle East: Frontline services for sectors including Defence and Transport in the Middle East region.

The analysis of the Company's turnover for the year by operating segment is as follows:

| | 2022 £m | 2021 £m |
|-------------|----------------|----------------|
| UK & Europe | 1,867.6 | 2,004.8 |
| Middle East | 30.1 | 106.4 |
| | <u>1,897.7</u> | <u>2,111.2</u> |

The analysis of the Company's turnover for the year by geographical location is as follows:

| | 2022 £m | 2021 £m |
|----------------|----------------|----------------|
| United Kingdom | 1,849.8 | 1,977.1 |
| Other | 47.9 | 134.1 |
| | <u>1,897.7</u> | <u>2,111.2</u> |

Turnover is shown by geographical origin. Turnover analysed by geographical destination is not materially different. The majority of turnover in the Company is recognised over time.

Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022

4. Turnover (continued)

The following table shows the transaction price allocated to remaining performance obligations. This represents revenue expected to be recognised in subsequent periods arising on existing contractual arrangements.

| | 2022 £m | 2021 £m |
|---------------------|----------------|----------------|
| Less than 1 year | 1,417.5 | 1,469.1 |
| Between 1 - 5 years | 3,749.7 | 3,603.6 |
| More than 5 years | 3,246.5 | 3,307.5 |
| | <u>8,413.7</u> | <u>8,380.2</u> |

5. 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.

| | 2022 £m | 2021 £m |
|--|------------|------------|
| Costs associated with the UK Government review | - | (0.3) |
| Restructuring costs | - | (0.1) |
| Costs associated with successful acquisitions | 0.9 | - |
| Increase in onerous lease provision | - | 0.6 |
| Disposal of goodwill | - | 0.1 |
| Capital contributions to subsidiaries | 9.0 | - |
| Exceptional operating items | <u>9.9</u> | <u>0.3</u> |

Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022

5 Exceptional operating items (continued)

In 2019 the Company's ultimate parent, Serco Group plc, settled on behalf of the Company's subsidiary, Serco Geografix Limited, the fine it received from the Serious Fraud Office (SFO) in relation to issues with its Electronic Monitoring contract reported in 2013. The settlement was made by way of a loan between Serco Group plc and Serco Geografix Limited. In 2022, to facilitate the repayment of the outstanding loan, the Company made a non-refundable and non-repayable capital contribution to its Subsidiary. The capital contribution was not made by way of subscription for share capital since no new share were issued. As Serco Geografix Limited no longer has a trade, the investment was immediately impaired resulting in an exceptional charge of £7.3m.

During the period, the Company also made a £1.7m non-refundable and non-repayable capital contribution to its Subsidiary Serco Environmental Services Limited. The capital contribution was not made by way of subscription for share capital as no new shares were issued. The investment was to allow Serco Environmental Services Limited to settle a loan due to another Serco Group undertaking. As Serco Environmental Services Limited no longer has a trade, the investment was immediately impaired resulting in an exceptional charge of £1.7m.

Exceptional costs of £0.9m have been incurred on behalf the Company's parent, Serco Holdings Ltd. for the acquisition of OXZ Holdings AG.

The Company recognised the final costs associated with the Strategy Review during 2019 and, on review, final costs were charged to exceptional operating items resulting in a credit to exceptional items of £nil during 2022 (2021: £0.1m).

There were exceptional credits totalling £nil (2021: costs totalling £0.3m) associated with the UK Government reviews, and the associated programme of corporate renewal.

In the previous year 2021, Serco Limited has recorded an additional £0.6m property provision related to the onerous lease of a building to cover the expected loss until March 2025. The building was vacated following the strategy review completed in 2014 and therefore the associated cost is treated as exceptional.

**Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022**

6. Operating profit

Operating profit is stated after (crediting)/charging:

| | 2022 £m | 2021 £m |
|--|--------------|--------------|
| Research and development costs | 0.5 | (0.1) |
| Operating lease expense* - property | 0.4 | 0.3 |
| Operating lease expense* - plant and machinery | 0.2 | 0.2 |
| Staff costs (note 7) | 703.0 | 773.3 |
| Amortisation of other intangible assets (note 13) | 7.3 | 8.5 |
| Depreciation of tangible fixed assets - owned (note 14) | 9.0 | 8.6 |
| Depreciation of tangible fixed assets - leased (note 14) | 78.0 | 75.1 |
| Other exceptional operating items (note 5) | 9.9 | 0.3 |
| Lease asset impairment (note 14) | 2.4 | - |
| Owned asset impairment (note 14) | 2.3 | 0.3 |
| | <u>703.0</u> | <u>773.3</u> |

The Group's Audit Committee limits the non-audit work undertaken by the External Auditor and monitors the non-audit fees paid during the year. Amounts payable to KPMG LLP and their associates by the Company in respect of non-audit services are shown within the group financial statements. The audit fees were £480,000 (2021: £480,000).

*Operating lease expense relates to short term leases under IFRS 16.

7. Staff costs

The average number of persons employed by the Company (including Directors) during the year was 21,518 (2021: 23,418). The aggregate payroll costs (including Directors' remuneration) were as follows:

| | 2022 £m | 2021 £m |
|------------------------------|--------------|--------------|
| Wages and salaries | 593.9 | 677.9 |
| Social security costs | 65.0 | 58.7 |
| Staff pensions | 32.3 | 31.1 |
| Share-based payment expenses | 7.5 | 5.6 |
| | <u>698.7</u> | <u>773.3</u> |

Under the Long Term Incentive Plan (LTIP), eligible employees have been granted options or conditional share awards with an exercise price of two or zero pence. Awards vest after the performance period of two to three years and are subject to the achievement of certain performance measures, with the exception of non-performance awards. These non-performance awards are only subject to continued employment on vesting dates which vary from two to three years after the grant dates.

On the performance related awards, the performance measures are Earnings per Share (EPS), Total Shareholder Return (TSR) and Return on Invested Capital (ROIC).

**Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022**

8. Directors' remuneration

The Directors' remuneration for the year was as follows:

| | 2022 £m | 2021 £m |
|-----------------------------|------------|------------|
| Directors' remuneration | 2.4 | 2.3 |
| Long term incentive schemes | 1.6 | 1.0 |
| | <u>4.0</u> | <u>3.3</u> |

The number of Directors who exercised share options was:

| | | |
|-------------------------|----------|----------|
| Exercised share options | <u>3</u> | <u>1</u> |
|-------------------------|----------|----------|

The aggregate of remuneration and amounts receivable under long term incentive schemes of the highest paid Director was £1.1m (2021: £0.9m), and Company pension contributions of £nil (2021: £nil) were made to a money purchase scheme on their behalf.

During the year, the highest paid Director exercised share options and received shares under a long term incentive scheme.

9. Interest receivable and similar income

| | 2022 £m | 2021 £m |
|--|------------|------------|
| Interest receivable from group undertakings | 3.7 | 0.1 |
| Net interest receivable on retirement benefit assets | 2.7 | 1.2 |
| | <u>6.4</u> | <u>1.3</u> |

10. Interest payable and similar charges

| | 2022 £m | 2021 £m |
|--|------------|------------|
| Other interest payable | - | 0.1 |
| Interest payable to group undertakings | 2.1 | 1.1 |
| Interest payable under finance leases | 3.5 | 3.5 |
| | <u>5.6</u> | <u>4.7</u> |

Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022

11. Tax

Tax credited in the profit and loss account:

| | 2022 £m | 2021 £m |
|--|------------|----------------|
| Current taxation | | |
| UK corporation tax | 0.9 | 3.1 |
| Adjustments in respect of prior years | 2.0 | (0.1) |
| Consortium relief | (2.0) | - |
| | <u>0.9</u> | <u>3.0</u> |
| Deferred taxation | | |
| Arising from origination and reversal of temporary differences | 4.1 | (130.7) |
| Adjustments in respect of prior years | (2.9) | - |
| Impact of change in deferred tax rate | (0.8) | (10.8) |
| Total deferred taxation | <u>0.4</u> | <u>(141.5)</u> |
| | <u>1.3</u> | <u>(138.5)</u> |
| Tax charged/(credited) in the profit and loss account | <u>1.3</u> | <u>(138.5)</u> |

Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022

11. Tax (continued)**Factors affecting current tax charge for the year**

The tax on profit before tax for the year is higher than (2021: lower than) the standard rate of corporation tax in the UK of 19% (2021: 19%).

The differences are reconciled below:

| | 2022 £m | 2021 £m |
|---|------------|----------------|
| Profit before tax | 4.2 | 54.6 |
| Corporation tax at standard rate | 0.8 | 10.4 |
| Expenses not deductible for tax purposes | 1.2 | 7.1 |
| Group relief with no consideration | - | (0.1) |
| Unrelieved tax losses | 1.9 | 1.6 |
| Other non taxable income | (1.3) | (9.4) |
| Adjustment in respect of prior years | (0.9) | (0.1) |
| Overseas rate differences | 0.4 | 0.1 |
| Recognition of previously unrecognised tax losses | - | (137.3) |
| Impact of change in deferred tax rate | (0.8) | (10.8) |
| Total tax charge/(credit) | 1.3 | (138.5) |

12. Deferred tax

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

| | 2022 £m | 2021 £m |
|---|--------------|--------------|
| At 1 January | 149.5 | 29.6 |
| Deferred tax (charged)/ credited to profit and loss account | (1.0) | 141.5 |
| Items taken directly to equity - retirement benefit obligations reserve | 25.4 | (22.2) |
| Tax taken directly to reserves share based payments | 0.5 | 0.7 |
| Tax taken directly to reserves - hedge reserve | (0.1) | (0.1) |
| | 174.3 | 149.5 |

Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022

12. Deferred tax (continued)

| | 2022 £m | 2021 £m |
|--|--------------|--------------|
| Difference between accumulated depreciation and amortisation and capital allowance | 17.6 | 20.4 |
| Share based payments and employee benefits | 7.5 | 6.5 |
| Movement in retirement benefit obligations | (11.5) | (36.5) |
| Tax losses | 156.2 | 155.0 |
| Other temporary differences | 4.6 | 4.1 |
| Derivative financial instruments | (0.1) | - |
| | <u>174.3</u> | <u>149.5</u> |

Factors affecting future tax rate

The UK Budget 2021 announcements on 3 March 2021 included measures to support economic recovery as a result of the ongoing COVID-19 pandemic. These included an increase to the UK's main corporation tax rate to 25%, which is due to be effective from 1 April 2023. These changes were substantively enacted on 24 May 2021 and hence have been reflected in the measurement of deferred tax balances at 31 December 2022.

Unprovided deferred tax

| | 2022 £m | 2021 £m |
|---|------------|------------|
| Temporary differences on assets/liabilities | - | 0.3 |
| Share based payments and employee benefits | - | 0.1 |
| Other temporary differences | 0.6 | 2.2 |
| Capital losses | 1.2 | 1.2 |
| | <u>1.8</u> | <u>3.8</u> |

As noted above, the deferred tax asset provided at 31 December 2022 has been recognised at the tax rate applicable at the time the temporary differences are expected to reverse. Capital losses have not been provided as it is not expected that there will be future capital gains against which to offset them. The remaining unrecognised deferred tax asset at 31 December 2022 has arisen where the temporary differences are expected to reverse before 1 January 2024 and so the tax rate is expected to be less than 25% of the gross temporary difference.

Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022

13. Goodwill and other intangible assets

| | Goodwill £m | Software £m | Development expenditure £m | Customer relationships £m | Total £m |
|-----------------------|----------------|----------------|----------------------------------|---------------------------------|-------------|
| Cost | | | | | |
| At 1 January 2022 | 239.1 | 79.7 | 51.6 | 12.5 | 382.9 |
| Additions | - | 3.7 | 0.6 | - | 4.3 |
| Disposals | - | (1.4) | (0.2) | - | (1.6) |
| Foreign exchange | - | 0.2 | 0.4 | - | 0.6 |
| At 31 December 2022 | 239.1 | 82.2 | 52.4 | 12.5 | 386.2 |
| Amortisation | | | | | |
| At 1 January 2022 | 232.4 | 62.7 | 51.6 | 3.3 | 350.0 |
| Amortisation charge | - | 6.3 | 0.2 | 0.8 | 7.3 |
| Disposals | - | (1.3) | (0.2) | - | (1.5) |
| Impairment | - | 0.1 | - | - | 0.1 |
| Foreign exchange | - | 0.2 | 0.4 | - | 0.6 |
| At 31 December 2022 | 232.4 | 68.0 | 52.0 | 4.1 | 356.5 |
| Net book value | | | | | |
| At 31 December 2022 | 6.7 | 14.2 | 0.4 | 8.4 | 29.7 |
| At 31 December 2021 | 6.7 | 17.0 | - | 9.2 | 32.9 |

Serco Limited

Notes to the Financial Statements
for the Year Ended 31 December 2022

14. Property, plant and equipment

| | Land and Buildings Owned £m | Land and Buildings Leased £m | Furniture Fittings and Equipment owned £m | Furniture Fittings and Equipment Leased £m | Motor Vehicles Owned £m | Motor Vehicles Leased £m | Total £m |
|--|--------------------------------------|---------------------------------------|--|---|----------------------------------|-----------------------------------|-------------|
| Cost or valuation | | | | | | | |
| At 1 January 2022 | 4.0 | 431.8 | 45.6 | 6.3 | 29.1 | 70.9 | 587.7 |
| Additions | - | 95.0 | 3.9 | 0.2 | 1.5 | 6.7 | 107.3 |
| Cost of dilapidation provisions booked to right of use assets (note 20) | - | 0.8 | - | - | - | - | 0.8 |
| Disposals | - | (18.6) | (2.0) | (0.2) | (4.5) | (4.0) | (29.3) |
| Reclassifications | - | - | - | - | 1.1 | (1.1) | - |
| Foreign exchange movements | - | 0.1 | 0.2 | (0.1) | (0.1) | (0.1) | - |
| At 31 December 2022 | 4.0 | 509.1 | 47.7 | 6.2 | 27.1 | 72.4 | 666.5 |
| Depreciation | | | | | | | |
| At 1 January 2022 | 2.6 | 125.1 | 29.0 | 4.9 | 19.8 | 33.3 | 214.7 |
| Charge for the year | 0.2 | 68.6 | 6.2 | 0.5 | 2.6 | 8.9 | 87.0 |
| Eliminated on disposal | - | (6.4) | (1.9) | (0.2) | (4.5) | (3.3) | (16.3) |
| Reclassifications | - | - | - | - | 1.1 | (1.1) | - |
| Impairment charge | 0.2 | 2.4 | 2.0 | - | 0.1 | - | 4.7 |
| Foreign exchange movements | (0.2) | 0.1 | 0.2 | (0.1) | - | (0.1) | (0.1) |
| At 31 December 2022 | 2.8 | 189.8 | 35.5 | 5.1 | 19.1 | 37.7 | 290.0 |

Serco Limited

Notes to the Financial Statements
for the Year Ended 31 December 2022

14. Property, plant and equipment (continued)

Net book value

| | | | | | | | |
|---------------------|-----|-------|------|-----|-----|------|-------|
| At 31 December 2022 | 1.2 | 319.3 | 12.2 | 1.1 | 8.0 | 34.7 | 376.5 |
| | | | | | | | |
| At 31 December 2021 | 1.4 | 306.7 | 16.6 | 1.4 | 9.3 | 37.6 | 373.0 |
| | | | | | | | |

Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022

15. Investments**Details of undertakings**

The companies listed below are the subsidiaries 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 | Class of shares held | Proportion of voting rights and shares held | |
|--------------------------------------|--------------------------|----------------------|---|------|
| | | | 2022 | 2021 |
| Serco Geografix Limited | United Kingdom | Ordinary | 100% | 100% |
| Serco Environmental Services Limited | United Kingdom | Ordinary | 100% | 100% |

The address for Serco Geografix Limited is Serco House, 16 Bartley Wood Business Park, Bartley Way, Hook, Hampshire, RG27 9UY, United Kingdom. The activity for the Company was manufacture, sale and leasing of electronic tagging equipment (no activities pursued during the current year).

The address for Serco Environmental Services Limited is Serco House, 16 Bartley Wood Business Park, Bartley Way, Hook, Hampshire, RG27 9UY, United Kingdom. The activity for the Company was Provision of environmental cleaning services (no activities pursued during the current year).

The Company operates through branches in France, Italy, Qatar and the United Arab Emirates.

16. Stocks

| | 2022 £m | 2021 £m |
|--|-------------|------------|
| Service spares, supplies & consumables | 10.7 | 8.8 |
| Work in progress (goods to be sold) | 1.0 | - |
| | <u>11.7</u> | <u>8.8</u> |

Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022

17. Debtors

| | 2022 £m | 2021 £m |
|--|--------------|--------------|
| Amounts falling due within one year | | |
| Amounts owed by group companies | 53.3 | 27.7 |
| Trade debtors | 74.2 | 91.2 |
| Other debtors | 5.5 | 5.9 |
| Prepayments | 51.1 | 31.8 |
| Contract assets | 78.5 | 88.8 |
| | <u>262.6</u> | <u>245.4</u> |

Amounts owed by group companies have no fixed repayment date and are payable on demand. Interest is charged on the balance at LIBOR minus 0.2%. On 31 March 2023, the synthetic LIBOR rate was discontinued and was replaced by the Bank of England base rate in this calculation of interest.

Deferred bid and phase in costs are held within contract assets as due within one year. These assets represent up-front investment in contracts which are recoverable and expected to provide benefits over the life of those contracts. Bid costs are capitalised only when they relate directly to a contract and are incremental to securing the contract. Any costs which would have been incurred whether or not the contract is actually won are not considered to be capitalised bid costs.

The trade debtors balance is stated after an allowance for doubtful debts of £0.5m (2021: £0.6m). Movements on the Company's allowance for doubtful debts are as follows:

| | 2022 £m | 2021 £m |
|--------------|------------|------------|
| At 1 January | 0.6 | 3.6 |
| Utilised | (0.1) | (3.0) |
| | <u>0.5</u> | <u>0.6</u> |

Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022

17. Debtors (continued)

Contract assets

| | 2022 | 2021 |
|---|-------------|-------------|
| | £m | £m |
| Accrued income and unbilled receivables | 73.6 | 82.9 |
| Capitalised bid costs | 0.3 | 0.3 |
| Capitalised mobilisation and phase in costs | 4.6 | 5.6 |
| | <u>78.5</u> | <u>88.8</u> |

Deferred bid and phase in costs are held within contracts assets as they are realised as part of the normal operating cycle of the Company.

| | 2022 | 2021 |
|---|--------------|--------------|
| | £m | £m |
| Amounts falling due after more than one year | | |
| Amounts owed by group companies | 385.9 | 348.4 |
| Other debtors | 0.1 | 0.3 |
| | <u>386.0</u> | <u>348.7</u> |

18. Creditors: amounts falling due within one year

| | 2022 | 2021 |
|---------------------------------|--------------|--------------|
| | £m | £m |
| Trade creditors | 59.4 | 48.0 |
| Other taxes and social security | 44.6 | 53.6 |
| Other creditors | 4.4 | 5.3 |
| Accruals | 123.3 | 118.4 |
| Contract liabilities | 40.5 | 33.9 |
| Lease liabilities | 106.3 | 89.1 |
| | <u>378.5</u> | <u>348.3</u> |

19. Bank overdrafts

| | 2022 | 2021 |
|-----------------|-------------|-------------|
| | £m | £m |
| Bank overdrafts | <u>35.8</u> | <u>17.1</u> |

**Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022**

20. Creditors: amounts falling due after more than one year

| | 2022 £m | 2021 £m |
|---------------------------------|--------------|--------------|
| Amounts owed to group companies | 196.5 | 154.8 |
| Contract liabilities | 14.8 | 33.1 |
| Lease liabilities | 246.2 | 249.3 |
| | <u>457.5</u> | <u>437.2</u> |

Amounts owed to group companies have no fixed repayment date and are payable on demand. Interest is charged on the balance at LIBOR plus 2%. On 31 March 2023, the synthetic LIBOR rate was discontinued and was replaced by the Bank of England base rate in this calculation of interest

21. Provisions

| | Property £m | Contract £m | Employee benefits £m | Other provisions £m | Total £m |
|---|----------------|----------------|----------------------------|---------------------------|-------------|
| At 1 January 2022 | 12.1 | 1.2 | 9.4 | 31.5 | 54.2 |
| Charged to the profit and loss account | 2.3 | 3.0 | 2.3 | 3.3 | 10.9 |
| Released to the profit and loss account | (0.4) | (0.1) | (2.1) | (3.0) | (5.6) |
| Reclassification | (0.3) | - | - | 0.3 | - |
| Utilised | (0.7) | (0.6) | (2.7) | (8.1) | (12.1) |
| Transfer to payables | - | - | - | 0.7 | 0.7 |
| Cost of dilapidation provisions booked to right of use assets | 0.8 | - | - | - | 0.8 |
| Foreign exchange | - | (0.1) | 0.7 | 0.1 | 0.7 |
| At 31 December 2022 | <u>13.8</u> | <u>3.4</u> | <u>7.6</u> | <u>24.8</u> | <u>49.6</u> |
| Non-current liabilities | 4.9 | 1.5 | 7.3 | 16.0 | 29.7 |
| Current liabilities | <u>8.9</u> | <u>1.9</u> | <u>0.3</u> | <u>8.8</u> | <u>19.9</u> |

Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022

21. Provisions (continued)

Total provisions held by the Company at 31 December 2022 amount to £49.6m (2021: £54.2m).

Contract provisions relate to onerous contracts which will be utilised over the life of each individual contract. 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.

Discount rates used are calculated based on the estimated risk free rate of interest for the region in which the provision is located and matched against the ageing profile of the provision. In 2022, additional charges have been made in respect of future losses totalling £2.9m (2021: £1.0m) £2.5m of this related to a new OCP in year for an environmental services contract in Norfolk, with the remaining charges against existing OCPs.

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.

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, and it also includes dilapidations in occupied properties. 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.

Employee related provisions are for long-term service awards and terminal gratuity 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.

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. They will be utilised with reference to the specific facts and circumstances, with the majority expected to be settled by 30 September 2026.

**Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022**

22. Pension and other schemes

Defined benefit pension schemes

i) Characteristics and risks

The Company contributes to defined benefit schemes for qualifying employees in the UK. The normal contributions expected to be paid during the financial year ending 31 December 2023 are £4.9m (2022: £6.3m).

There are two non-contract specific schemes which are Serco Pension and Life Assurance Scheme (SPLAS) and a non-contract specific section of the Railways Pension Scheme (RPS). The funding policy for the UK pre-funded schemes is to contribute amounts which will achieve 100% funding on a projected salary basis based on regular actuarial valuations.

The Company also makes contributions under Admitted Body status for one section of the Local Government Pension Scheme for the period to the end of the relevant customer contract. The Group is required to pay regular contributions as decided by the respective scheme actuary and as detailed in each scheme's schedule of contributions. In addition, the Group may be required to pay some or all of any deficit (as determined by the respective scheme actuary) that is remaining at the end of the contract.

In respect of Local Government Pension Schemes, as there is a residual liability, the Group recognises a sufficient level of provision in these financial statements based on the IAS 19 Employee Benefits valuation at the reporting date and contractual obligations.

Scheme funding

The normal contributions expected to be paid during the financial year for all schemes ending 31 December 2023 are £4.9m (2021: £6.3m).

The assets of funded schemes are held independently of the Company's assets in separate trustee administered schemes. The trustees of each pension scheme are required by law to act in the interest of the scheme and of all relevant stakeholders in the scheme. The trustees of the pension schemes are responsible for the investment policy with regard to the assets of the scheme. The Group's schemes are valued by independent actuaries annually using the projected unit credit actuarial cost method for accounting purposes. This reflects service rendered by employees to the date of valuation and incorporates actuarial assumptions including discount rates to determine the present value of benefits, inflation assumptions, 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 the different defined benefit schemes are not offset.

The schemes typically expose the Company to risks that impact the financial performance and position of the Company and may affect the amount and timing of future cash flows. The key risks are set out below:

- **Investment risk.** The schemes hold assets with which to discharge the future liabilities of these schemes. Any decline in the value of these investments directly impacts on the ability of the schemes to meet its commitments and could require the Group to fund this shortfall in future years. SPLAS's investment strategy aims to reduce volatility risk by better matching assets to liabilities and is based on the actuarial funding basis. 48% of the scheme's assets are annuity policies, which result in an insurer funding the future benefit payments to the relevant members and therefore eliminate the risk of changes in the future value of the benefits to the scheme. The investment strategy outside of the annuity has a benchmark allocation of 45% Liability Driven Investments (LDIs), 40% Buy and Maintain Credit and 15% Private Debt. The main asset classes that make up the LDI investments are gilts and corporate bonds with inflation and interest swap overlays and are therefore linked to the key drivers of the scheme's liabilities.

Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022

22. Pension and other schemes (continued)

Defined benefit pension schemes (continued)

i) Characteristics and risks (continued)

Scheme funding (continued)

- Interest risk. The present values of the defined benefit schemes' liabilities are calculated using a discount rate determined by reference to high-quality corporate bond yields and therefore a decrease in the bond interest rate will increase the schemes' liabilities. This will be partially offset by an increase in the return of the schemes' debt investments.
- Longevity risk. The present values of the defined benefit schemes' liabilities are calculated by reference to the best estimate of the mortality of the schemes' participants, both during and after their employment. An increase in the life expectancy of the schemes' participants will increase the schemes' liabilities.
- Inflation risk. The present values of the defined benefit schemes' liabilities are calculated to include the effect of inflation on future purchasing power based on estimations around inflation rates. An increase in expected future inflation rates will increase the schemes' liabilities.
- Salary risk. The present values of the defined benefit schemes' liabilities are calculated by reference to the future salaries of the schemes' participants, as such, an increase in the salary of the schemes' participants will increase the schemes' liabilities.

Serco Pension and Life Assurance Scheme (SPLAS)

The largest non-contract specific schemes is SPLAS. The most recent full actuarial valuation of this scheme was undertaken as at 5 April 2021 and completed in May 2022. The actuarially assessed deficit for funding purposes was £70.0m. The increase to the actuarially assessed deficit for funding purposes was as a result of the RPI reform announced by the UK government to take effect from 2030.

Pension obligations are valued separately for accounting and funding purposes and there is often a material difference between these valuations. As at 31 December 2022, the estimated actuarial deficit on a funding basis for SPLAS was £27m (2021: £42m) whereas the accounting valuation resulted in an asset of £47.5m (2021: £166.2m). The primary reason a difference arises is that pension scheme accounting requires the valuation to be performed on the basis of a best estimate whereas the funding valuation used by the trustees makes more prudent assumptions.

The schedule of contributions for SPLAS was agreed during 2022, with 44.3% of pensionable salaries for active employees due to be paid in regular contributions from 1 June 2022. The schedule of contributions also determined that additional shortfall contributions were required and the Company has committed to make deficit recovery payments by 31 March of £6.6m per year from 2022 to 2030. An annual assessment of the shortfall is performed and if the scheme is determined to be in a surplus position the shortfall contributions due by 31 March are deferred to the following year. If the shortfall calculated in the annual assessment is less than the cumulative shortfall due to date the contribution is capped at the shortfall calculation and any excess is carried forward to the next year.

ii) Events in the year

During the year there has been a high degree of volatility in the pensions market. Discount rates and short-term inflation rates have been rising since 31 December 2021 which has resulted in the weighted average durations used for valuing pension schemes decreasing. Concerns over high global inflation, recession, disruption to supply chains due to the war in Ukraine and rising interest rates, compounded by the market volatility in September 2022 due to political events resulted in a sharp rise in bond yields and a subsequent reduction in the value of LDIs, which triggered collateral calls. The Company's ultimate parent on behalf of the Company made a short-term temporary loan of £60m to SPLAS on 28 September 2022 while the scheme liquidated assets to meet these collateral calls, in order to ensure that the LDI hedge was maintained; this loan was repaid on 3 October 2022.

Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022

22. Pension and other schemes (continued)

Defined benefit pension schemes (continued)

ii) Events in the year (continued)

The private debt investments are less volatile to the market conditions and therefore the allocation of investments was outside the scheme's benchmark at 31 December 2022, with 46% LDIs, 24% Buy and Maintain Credit and 30% Private Debt. The Trustees of SPLAS have been working closely with the Group and investment consultants to ensure the investment objectives of the scheme are maintained.

iii) Value recognised in total comprehensive income in the year

The amounts recognised in the financial statements for the year are analysed as follows:

| | 2022 £m | 2021 £m |
|--|------------|------------|
| Recognised in the profit and loss account | | |
| Current service cost - employer | 3.5 | 3.8 |
| Settlement gain recognised | (0.4) | - |
| Administrative expenses and taxes | 2.4 | 1.4 |
| | <hr/> | <hr/> |
| Recognised in arriving at operating profit | 5.5 | 5.2 |
| | | |
| Interest income on scheme assets - employer | (27.8) | (21.9) |
| Interest cost on scheme liabilities - employer | 25.1 | 20.7 |
| | <hr/> | <hr/> |
| Finance income | (2.7) | (1.2) |
| | <hr/> | <hr/> |
| Total recognised in profit and loss account | <u>2.8</u> | <u>4.0</u> |

Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022

22. Pension and other schemes (continued)

iii) Value recognised in total comprehensive income in the year (continued)

| | 2022 £m | 2021 £m |
|---|----------------|-------------|
| Included within the SOCI | | |
| Actual return on scheme assets | (539.6) | 40.4 |
| Less: interest income on scheme assets | (27.8) | (21.9) |
| Effect of changes in demographic assumptions | 20.9 | 19.9 |
| Effect of changes in financial assumptions | 515.0 | 23.3 |
| Effect of experience adjustments | (76.5) | 3.4 |
| Total recognised (loss)/gain in the SOCI | (108.0) | 65.1 |

iv) Balance sheet values

The SPLAS Trust Deed gives the Group an unconditional right to a refund of surplus assets, assuming the full settlement of plan liabilities in the event of a plan wind-up. Pension assets are deemed to be recoverable and there are no adjustments in respect of minimum funding requirements as economic benefits are available to the Group either in the form of future refunds or, for plans still open to benefit accrual, in the form of possible reductions in future contributions.

The high degree of volatility as noted above resulted in a reduction in pension scheme assets, particularly investments in bonds, LDIs and amounts held by insurance companies. There has been significant reduction in pensions scheme obligations as discount rates have risen but this has only partially offset the reduction in assets as the liabilities are hedged on an actuarial basis rather than an IAS 19 basis. The decrease in pension scheme obligations was partially offset by experience adjustments on SPLAS which were primarily due to the impact from inflation on the current year allowances for deferred valuations and pension increases.

Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022

22. Pension and other schemes (continued)

(iv) Balance sheet values (continued)

The schemes asset values at 31 December are:

| | 2022 £m | 2021 £m |
|---|------------|------------|
| Schemes assets fair value | | |
| Equities | 35.5 | 46.5 |
| Bonds except LDI | 290.6 | 368.1 |
| Pooled investment funds (Audax, Golub and Ares) | - | 107.6 |
| LDI | 217.7 | 390.0 |
| Property | 0.2 | 1.2 |
| Cash and other | 12.1 | 4.0 |
| Amounts held by insurance companies | 441.0 | 662.3 |
| | <hr/> | <hr/> |
| Fair value of scheme assets | 997.1 | 1,579.7 |
| Present value of scheme liabilities | (940.1) | (1,430.2) |
| | <hr/> | <hr/> |
| Net retirement benefit asset | 57.0 | 149.5 |

As required by IAS 19 Employee Benefits, the Group has considered the extent to which the pension plan assets should be classified in accordance with the fair value hierarchy of IFRS 13 Fair Value Measurement.

Equity and Bonds all virtually have quoted prices in active markets and are classified as level 1.

Pooled investment funds have no observable market price and the valuation is based on the Net Asset Value provided by the fund administrator at 30 September adjusted for actual cash flows in the period to 31 December. Therefore, these investments are classified as level 3.

LDIs are valued at fair value which is typically the Net Asset Value provided by the fund administrator and are classified as level 2.

LDIs are valued at fair value which is typically the Net Asset Value provided by the fund administrator. The LDIs are comprised of a mix of Level 1 and Level 2 instruments, including corporate/government bonds priced at their quoted bid price, derivatives made up of interest rate/inflation swaps and payables in respect of repurchase agreements.

Amounts held by insurance companies are valued at the equal and opposite of the defined benefit obligations that they insure and are classified as level 3.

Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022

22. Pension and other schemes (continued)

(iv) Balance sheet values (continued)

Changes in the fair value of scheme liabilities are analysed as follows:

| | 2022 £m | 2021 £m |
|--|--------------|----------------|
| At 1 January | 1,430.2 | 1,510.6 |
| Current service cost - employer | 3.5 | 3.8 |
| Scheme participants' contribution | 0.3 | 0.3 |
| Interest cost - employer | 25.1 | 20.7 |
| Benefits paid | (51.2) | (58.5) |
| Effect of changes in financial assumptions | (514.9) | (19.9) |
| Effect of changes in demographic assumptions | (20.9) | (3.4) |
| Effect of experience adjustments | 76.4 | (23.4) |
| Plan settlements | (8.4) | - |
| At 31 December | 940.1 | 1,430.2 |

Changes in fair value of scheme assets are analysed as follows:

| | 2022 £m | 2021 £m |
|--|--------------|----------------|
| At 1 January 2021 | 1,579.7 | 1,590.6 |
| Interest income on scheme assets - employer | 27.8 | 21.8 |
| Administrative expenses and taxes | (2.4) | (1.4) |
| Employer contributions | 18.1 | 8.4 |
| Contribution by employees | 0.3 | 0.3 |
| Benefits paid | (51.2) | (58.5) |
| Return on scheme assets less interest income | (567.3) | 18.5 |
| Plan settlement | (7.9) | - |
| | 997.1 | 1,579.7 |

Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022

22. Pension and other schemes (continued)

v) Actuarial assumptions: SPLAS

The assumptions set out below are for SPLAS, which reflects 93% of total liabilities and 93% of total assets of the defined benefit pension scheme in which the Company participates. The significant actuarial assumptions with regards to the determination of the defined benefit obligation are set out below.

The Company continued to set RPI inflation in line with the market break-even expectations less an inflation risk premium. The inflation risk premium has remained at 0.3% both at 31 December 2021 and at 31 December 2022.

The average duration of the benefit obligation at the end of the reporting period is 11.5 years (2021: 16.3 years).

| | 2022 % | 2021 % |
|--|-----------|-----------|
| Significant actuarial assumptions | | |
| Discount rate | 5.0 | 1.8 |
| Rate of salary increase | 2.9 | 3.0 |
| RPI Inflation | 3.2 | 3.4 |
| CPI Inflation | 2.4 | 2.5 |

| | 2022 Years | 2021 Years |
|-----------------------------------|---------------|---------------|
| Post retirement mortality | | |
| Current pensioners at 65 - male | 21.5 | 21.7 |
| Current pensioners at 65 - female | 24.1 | 24.3 |
| Future pensioners at 65 - male | 23.6 | 23.9 |
| Future pensioners at 65 - female | 26.2 | 26.4 |

Sensitivity analysis for SPLAS 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 2022 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. The defined benefit obligation as at 31 December 2022 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. Due to the increased volatility in the pension market the Group has updated its sensitivity disclosure to reflect a 1% change in the relevant assumption compared to a 0.5% change used in previous years. The prior year comparatives have been restated.

Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022

22. Pension and other schemes (continued)

v) Actuarial assumptions: SPLAS (continued)

| | 2022 £m | 2021 £m |
|---|------------|------------|
| Increase/(decrease) in defined benefit obligation of SPLAs | | |
| Discount rate - 1.0% increase | (93.4) | (205.9) |
| Discount rate - 1.0% decrease | 113.8 | 243.8 |
| Inflation - 1.0% increase | 68.0 | 145.7 |
| Inflation - 1.0% decrease | (68.1) | (157.0) |
| Rate of salary increase - 1.0% increase | 1.6 | 3.3 |
| Rate of salary increase - 1.0% decrease | (1.5) | (3.3) |
| Mortality - one year age rating | 25.4 | 49.7 |

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.

The increase or decrease in the defined benefit obligation in the sensitivity table above would be offset by the corresponding movement in the scheme's assets. A 1% change in the long-term gilt yields consistent with the discount rates would result in an approximate offsetting movement of £100m (2021: £180m) in the scheme's LDI investment and a 1% change in long term inflation expectation would result in an approximate offsetting movement of £70m (2021: £140m) in the scheme's LDI Investment.

Defined contribution pension scheme

The Company paid employer contributions of £27.3m (2021: £27.5m) into UK defined contribution schemes, foreign defined contribution schemes and foreign state pension schemes.

Serco participated in certain pre-funded defined benefit pension arrangements relating to contracts, including participations in public sector schemes, however, contractual protections are in place allowing actuarial and investment risk to be passed to the end customer via recoveries for contributions paid.

The nature of these arrangements varies from contract to contract but typically allow for the majority of contributions payable to the schemes in excess of an initial rate agreed at the inception to be recovered from the end customer, as well as exit payments payable to the schemes at the cessation of the contract, such that the Group's net exposure to actuarial and investment risk is immaterial. Cash contributions are recognised as pension costs and no asset or liability is shown on the balance sheet.

23. Share capital

Allotted, called up and fully paid shares

| | No. | 2022 £ | No. | 2021 £ |
|-----------------------------------|---------|-----------|---------|-----------|
| Ordinary share capital of £1 each | 800,766 | 800,766 | 800,766 | 800,766 |

Notes to the Financial Statements (continued)
for the Year Ended 31 December 2022

24. 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 £35.8m at 31 December 2022 (2021: £17.1m).

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 2022, the total facility amounts were £350m (2021: £250.0m) for the Revolving Credit Facility, £nil (2021: £120.0m) for a bank term loan facility and £266m (2021: £259.0m) for the US private placements.

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

25. Derivative financial instruments

| | Assets 2022 £m | Liabilities 2022 £m | Assets 2021 £m | Liabilities 2021 £m |
|------------------------------------|----------------------|---------------------------|----------------------|---------------------------|
| Forward foreign exchange contracts | 0.6 | - | - | (0.1) |
| | | | | |
| | Assets 2022 £m | Liabilities 2022 £m | Assets 2021 £m | Liabilities 2021 £m |
| Analysed as | | | | |
| Current | 0.6 | - | - | (0.1) |

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 £0.6 arising in the year (2021: loss of £0.1m) has been deferred in equity.

26. Parent and ultimate parent undertaking

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.

27. Post balance sheet events

There were no post balance sheet events affecting the Company since the year end.