

# **BAE Systems Global Combat Systems Munitions Limited**

## **Annual Report and Financial Statements**

**31 December 2021**

Registered number: 01842252



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**BAE Systems Global Combat Systems Munitions Limited**  
**Annual Report and Financial Statements**  
**31 December 2021**

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**Strategic Report**  
for the year ended 31 December 2021

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**Review of business and principal activities**

BAE Systems Global Combat Systems Munitions Limited (the "Company") is a member of the BAE Systems plc Group ("BAE Systems Group or Group") of companies. Its principal activities are the design, development, manufacture and supply of munitions and associated components.

The Company is a wholly owned subsidiary of BAE Systems (Holdings) Limited. The main activity of the Company is the supply of small, medium and large calibre munitions to the UK Ministry of Defence ("MoD"). The MoD is the main customer however it isn't the only one. The Company has a strong order book and following the award of the 15 year Next Generation Munitions Solution ("NGMS") contract in November 2020, the Company has enacted plans to ensure an effective transition between the current munitions supply contract and NGMS. Transition plans are progressing well and the Company is on-track to meeting the jointly agreed timeframe for the transition into NGMS. In support of NGMS, the Company has commenced a £90m programme to update and expand its manufacturing equipment and infrastructure. This includes the development and migration of its existing enterprise resource planning system onto a new platform which is scheduled to complete in late 2023.

The Company continues to have contracts with other third parties and has a 50% investment in CTA International SAS, a business specialising in 40mm Cased Telescopic Armament Systems and associated munitions based in France.

The intercompany loan with Royal Ordnance B.V., a BAE Systems Group company, was settled during the period under review.

**Key performance indicators**

Key financial performance indicators are shown below:

	<b>2021</b>	<b>2020</b>
	<b>£000</b>	<b>£000</b>
Order intake	<b>170,927</b>	1,516,954
Revenue	<b>244,542</b>	244,412
Profit before tax	<b>25,148</b>	19,539
Return on sales	<b>10%</b>	8%

**Order intake** represents the value of funded orders received from customers in the year. It is a measure of in-year performance and supports future years' sales performance. The NGMS contract award in 2020 is the reason for the decrease in order intake.

**Revenue** represents the amounts derived from the provision of goods and services. Revenue has remained consistent and is in line with the direct costs traded under IFRS 15.

**Profit before tax** is used for internal performance analysis as a measure of operating profitability that is comparable over time. The increase has been driven by improved FX gains whereas the previous year had higher FX losses.

**Return on sales** this shows the percentage of profit as a function of sales. The increased margin has been driven by the improved FX movement in the year.

**Strategic Report (continued)**  
for the year ended 31 December 2021

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**Principal risks and uncertainties**

The Company's principal risks are identified below:

**The outbreak of contagious diseases may have a material adverse effect on the Company's business, financial condition and results of operations**

Many people have contracted COVID-19 across the world and many deaths have occurred as a result of the COVID-19 pandemic. Although there has been an effective roll-out of vaccination programmes in certain countries, it is still not clear how long this pandemic will last or how enduring its long-term impact will be, or the further measures that will be taken by governments and others to seek to control this pandemic and its impact. The uncertainties surrounding the development of this pandemic make it difficult to predict the extent to which the Company may be affected. Areas of the Company's business that could be impacted include a decrease in spending by the Company's major defence and commercial customers; an increase in taxation by governments; the failure to obtain awards for defence and commercial contracts; the failure of suppliers to deliver parts to the Company; the requirement for the Company or its suppliers to reduce site operational levels or close sites; the inability of the Company to meet contractual delivery requirements on time; the inability to adequately staff and manage the business; and an increase in the cost or lack of availability of funding. If the Company were unable to obtain appropriate funding either internally or externally it could be forced to make reductions in spending, seek to extend payment terms with suppliers and/or suspend or curtail planned programmes. Any of the above could have a material adverse effect on the Company's business, financial condition and results of operations.

Since the outbreak of the COVID-19 coronavirus pandemic, the Company has taken a number of responsive measures including reducing site operational levels and introducing new cleaning regimes, safe working distance measures and protective equipment for its employees. The Group continues to build on the experience gained to date in dealing with the pandemic. This includes the use of safe working practices and the effective use of home working.

By taking these measured actions to build in resilience for a prolonged period of disruption, the Company has continued to deliver critical work for its customer and, where operations were impacted, ensured that site-critical workers have now been able to safely return to work where possible.

Support for the defence industry from the government has been strong around prioritisation of capabilities, cash flows, recognising the need to maintain a strong supply chain and working collaboratively to maintain critical defence and security programmes.

**The Company's largest customers are governments. The Company is dependent on defence spending and terms of trade**

Defence spending by governments can fluctuate depending on change of government policy, other political considerations, budgetary constraints, specific threats and movements in the international oil price. There have been constraints on government expenditure in the UK. Defence spending by governments has also been impacted by the COVID-19 outbreak due to the reprioritisation of funds.

The Company has long-standing relationships and security arrangements with the government of the UK and its agencies. It is important that these relationships and arrangements are maintained.

In the defence and security industries, governments can typically modify contracts for their convenience or terminate them at short notice. Governments also from time to time review their terms of trade and underlying policies and seek to impose such new terms and policies when entering into new contracts

**Contract and delivery risk**

Whilst the undertaking of work within our core competencies and skills built on many years' experience in this market reduces the overall execution risks, the high technical requirements within our development contracts need careful management to minimise the inherent risks in that aspect of our work.

**Strategic Report (continued)**  
for the year ended 31 December 2021

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The Company is dependent upon the delivery of materials/components in a timely and satisfactory manner, on satisfactory commercial terms and in full compliance with applicable terms and conditions. The external supply chain environment is very dynamic at this time, with both lead-time and availability issues, but also pricing pressures, including from inflationary increases in labour, energy and other key materials.

**The Company may be impacted by environmental factors, including those relating to climate change**

The Company is subject to comprehensive environmental laws and regulations where it operates, including those relating to the impacts of climate change. Such laws and regulations impose standards with respect to air emissions, wastewater discharges, the use, handling and storage of hazardous wastes and materials, remediation of soil and groundwater contamination and the prevention of pollution. They can also include energy-related taxes and the increased costs of compliance with energy-related schemes. The Company may also be impacted by environmental factors, including physical risks arising from climate change, such as extreme weather events, for example, flooding and storms and scarcity of water and other resources. The Company may also be impacted by climate change transition risks resulting from the process of adjusting to a low carbon economy. Associated with this are potential risks around our ability to attract and retain future talent.

Environmental factors, including those relating to climate change, have the potential to materially impact the Company's business and operations. Increasing changes in environmental laws and regulations can expose the Company to increasing capital and operating costs associated with compliance, remediation and protection of the environment. Breaches of such laws and regulations can result in substantial costs, including fines, penalties or other sanctions, investigations and clean-up costs, and third-party claims for property damage or personal injury as well as the termination of permits. Extreme weather events can impact the Company's operational sites as well as those of its suppliers. The shift to a low carbon economy has the potential to increase the cost of business as the Company transitions to lower emissions technologies.

**Section 172(1) statement**

This statement contains an overview of how the directors have performed their duty to promote the success of the Company as set out in Section 172(1) of the UK's Companies Act 2006. That section requires a director of a company to act in the way he considers, in good faith, would most likely promote the success of the Company for the benefit of its shareholders. In doing this, the director must have regard, amongst other matters, to:

- a) the likely consequences of any decision in the long term,
- b) the interests of the Company's employees,
- c) the need to foster the Company's business relationships with suppliers, customers and others,
- d) the impact of the Company's operations on the community and the environment,
- e) the desirability of the Company maintaining a reputation for high standards of business conduct, and
- f) the need to act fairly as between members of the Company.

**Decision making**

The BAE Systems Group Operational Framework sets out the principles of good governance to which BAE Systems Group subsidiaries are required to adhere, together with BAE Systems Group's values, policies and processes. Decisions affecting a subsidiary are required to be taken in line with the Operational Framework, including in accordance with applicable delegations of authority.

Pursuant to the Operational Framework, BAE Systems' businesses each produce a strategic plan, a financial forecast for the current year and financial projections for the next five years. The directors of the Company contribute towards this process for the respective businesses of the Company for which they are responsible and are also responsible for identifying and managing principal and emerging risks in such businesses. In so doing the directors have regard to a variety of matters including the interests of various stakeholders, the consequences of their decisions in the long term and the long-term reputation of the Company and its businesses.

**Strategic Report (continued)**  
for the year ended 31 December 2021

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**Employees**

Employee engagement is a primary focus for the directors of the Company – connecting employees to the Company's and the BAE Systems Group's strategy and purpose, empowering them to contribute to improving business performance and creating an environment in which everyone can fulfil their potential. We keep the Company's employees informed about what is happening across the BAE Systems Group through the Group's intranet and email, podcasts, newsletters, and leadership blogs and briefings.

Keeping employees connected, informed and engaged has never been more important as the Company's employees continued to experience major impacts on their personal circumstances and ways of working through the pandemic. The Company used a range of channels to make sure its employees had access to the information and support they needed throughout the year, as well as keeping employees informed about the performance, developments and prospects of the business and the BAE Systems Group. This included engagement through the Group intranet, employee app, email, videos, podcasts, newsletters, leadership communications, virtual discussions and briefings, and through our line managers who played a key role in keeping their teams connected and engaged. This includes continuing to focus on two-way communications, ensuring there are channels through which employees can express their views, feedback and any concerns, helping the Company understand employee sentiment on an ongoing basis and respond appropriately.

These engagement activities form part of the Company's implementation of the BAE Systems Group-wide employee engagement processes and policies which are described on pages 11, 18, 23, 56-58 and 153 of BAE Systems plc's Annual Report 2021 (available at: [www.baesystems.com/investors](http://www.baesystems.com/investors)).

Pursuant to the Group's People Policy, Directors and employees are required to contribute to creating an engaged and inclusive work environment, where individuals are respected and where the value of a diverse workforce is recognised. Also, pursuant to the Policy, employees are to be provided with the means to give their views and feedback.

Through the implementation by the Company of these processes and policies, the Directors have regard to the interests of the Company's employees.

**Fostering business relationships with suppliers, customers and others**

The directors recognise that fostering business relationships with key stakeholders, such as customers and suppliers, is essential to the Company's success. The Company has close relationships with its customers, suppliers and industry partners which help us to create best-in-class, cost-effective equipment, goods, services and solutions.

Our largest customers are governments, and we also sell to large prime contractors and commercial businesses. Strong and collaborative relationships with our principal government and prime customers help us to identify our customers' requirements and to help position the Company as a trusted provider. The Directors are in regular contact with the principal government customers of the Company and in particular the UK Ministry of Defence.

The Company, together with its procurement and supply chain function, works with its suppliers and their supply chains to provide equipment, goods and services that meet its customers' requirements. The Company's supplier relationships are often long-term due to the length of the product life-cycles and the Directors meet with key suppliers and work with the BAE Systems Group's procurement function to develop deeper relationships with business in the supply chain and develop strategic relationships with key suppliers.

The value of long-term supplier partnerships was shown during 2021, with the Group's long-term global supply agreements, put in place prior to the pandemic, being of particular assistance in maintaining supply of critical components. A pro-active approach was taken to manage supplier relationships with the Group working closely with suppliers to anticipate issues and take action where possible to ensure continuity of supply.

**Strategic Report (continued)**  
for the year ended 31 December 2021

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**The community and the environment**

The directors recognise the importance of leading a company that not only generates value for shareholders but also contributes to wider society. Through the Operational Framework the Company implements the requirements of the BAE Systems Group's Community Investment Policy, which looks to ensure that we build and nurture mutually beneficial relationships between our business, our people and local stakeholders. Giving back to the communities in which we operate, and to charities that have meaning to our business, is vitally important to our Company and our employees, allowing us to make a positive difference and have an impact where it counts. In particular, the Company is a major employer in Glascoed and the directors recognise the significance of the Company in the local community.

As a manufacturer, we recognise that our operations have an impact on the environment – from the energy and resources we use, to the products we manufacture and the waste that we generate. As an organisation, the BAE Systems Group is committed to reducing the environmental impact of its operations and products, minimising its environmental footprint and, in turn, decreasing its operational costs.

Through the Operational Framework the Company implements the requirements of the BAE Systems Group's Environmental Policy, which details our commitment to high standards of environmental management. In particular, the Company is supporting the Group's target of achieving net zero greenhouse gas emissions across the Group's operations (scope 1 and 2) by 2030 and its target of working towards a net zero value chain by 2050.


All the above activities form part of the Company's implementation of the BAE Systems Group-wide community and environment processes and policies and the BAE Systems Group's impacts thereon which are described in the "Environment" and "Social" sections (pages 38-47 and pages 58-63 respectively) of BAE Systems plc's Annual Report 2021 (available at: [www.baesystems.com/investors](http://www.baesystems.com/investors)).

**Maintaining a reputation for high standards of business conduct**

The BAE Systems Group aims to be a recognised leader in business conduct which helps us to earn and maintain stakeholder trust and sustain business success. The directors consider it fundamental to maintain a culture focused on embedding responsible business behaviours. All employees of the Company are expected to act in accordance with the requirements of BAE Systems Group policies, including the Code of Conduct, at all times. As well as being the right thing to do, this reduces the risk of compliance failure and supports the Company in attracting and retaining high-calibre employees.

Detailed information on the BAE Systems Group-wide business conduct processes and policies are described in BAE Systems plc's Annual Report 2021 (available at: [www.baesystems.com/investors](http://www.baesystems.com/investors)) and in particular the "Governance and business conduct" section on pages 64-66.

**Approved by the Board and signed on its behalf by:**



**M A Clarke**  
Director

Date: 27 June 2022

## **Directors' Report**

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### **Company registration**

BAE Systems Global Combat Systems Munitions Limited is a private company, limited by shares and registered in England and Wales with the registered number 01842252.

### **Results and dividends**

The Company's profit for the financial year is £22,349k (2020: £23,286k profit). The directors propose a dividend of £20,000k (2020: £20,000k).

The dividend proposed per share is £0.10 (2020: £0.10).

### **Looking forward**

The Company's munitions supply continues under the Munitions Acquisition Supply Solution Partnering agreement which will be followed in 2023 by the recently agreed 15-year Next Generation Munitions Solution.

### **Going concern**

The financial statements have been prepared on the going concern basis, notwithstanding net current liabilities of £57,345k, which the directors believe to be appropriate for the following reasons. The Company is dependent for its working capital on funds provided to it by BAE Systems plc, the Company's ultimate parent. BAE Systems plc has indicated that, for at least 12 months from the date of approval of these financial statements, it will continue to make available funds as are needed by the Company to meet its liabilities as they fall due and in particular will not seek repayment of amounts currently made available.

### **Energy and carbon reporting exemption**

The Company has taken advantage of the exemption granted under The Companies (Directors' Report) and Limited Liability Partnerships (Energy and Carbon Report) Regulations 2018 as this information is disclosed on pages 38-47 in the 2021 consolidated accounts of its ultimate parent, BAE Systems plc (available at [www.baesystems.com/investors](http://www.baesystems.com/investors)).

### **Employees**

The Company is committed to giving full and fair consideration to applications for employment from disabled people who meet the requirements for roles, and making available training opportunities and appropriate accommodation to disabled people employed by the Company. In the event of members of staff becoming disabled every effort is made to ensure that their employment with the Company continues and that appropriate training is arranged.

Employee engagement enables our employees to contribute to improving business performance and helps us to gauge our performance in creating an environment in which everyone can fulfil their potential. Engagement with suppliers, customers and others has been considered within the Strategic Report on page 4.

The Company welcomes employees becoming shareholders in BAE Systems plc and offers employee share plans to support this.

### **Engagement with suppliers, customers and others**

Engagement with suppliers, customers and others has been considered within the Strategic Report on page 4.



## **Directors' Report (continued)**

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### **Research and development**

The Company is focused on technology innovation and engineering excellence and invests in next-generation research and technology programmes to improve the manufacturing and service of products, generating substantial intellectual property. Total research and development expenditure in the year was £2,720k (2020: £1,719k), of which £1,359k (2020: £812k) was funded by the Company.

### **Financial instruments**

The international nature of the Company's business means it is exposed to volatility in currency exchange rates. In order to protect itself against currency fluctuations, the Company's policy is to hedge all material firm transactional exposures.

### **Qualifying indemnity provisions**

The directors of BAE Systems Pension Funds Trustees Limited, BAE Systems 2000 Pension Plan Trustees Limited and Alvis Pension Scheme Trustees Limited benefit from indemnities in the governing documentation of the BAE Systems Pension Scheme, the BAE Systems 2000 Pension Plan and the Alvis Pension Scheme, respectively, given by the Company, which are qualifying indemnity provisions for the purpose of the Companies Act 2006. All such indemnity provisions are in force at the date of this Directors' Report.

### **Events after the reporting period**

Since the Balance Sheet date, several countries in which we operate have announced or are making plans to increase spending to counter the elevated and evolving threat environment on multiple fronts. This has been determined to be a non-adjusting post balance sheet event. It is not currently possible for the Company to estimate the potential future financial impact of such changes.

Since the Balance Sheet date, there has been an increase globally in supply chain and inflationary pressures for businesses. This has been determined to be a non-adjusting post balance sheet event. Owing to the uncertainty around supply chain and inflationary pressures, we have included this as a principal risk in this report. The Company is currently mitigating the major financial impacts of this issues and seeks to continue to do so.

### **Directors and their interests**

The directors who served throughout the year and up to the date of this Directors' Report, were as follows:

G E P Plant  
M A Clarke

The Board is not aware of any contract of significance in relation to the Company in which any director has, or has had, a material interest.

### **Disclosure of information to auditor**

The directors who held office at the date of approval of this Directors' Report confirm that, so far as they are each aware, there is no relevant audit information of which the Company's auditor is unaware; and each director has taken all the steps that they ought to have taken to make themselves aware of any relevant audit information and to establish that the Company's auditor is aware of that information. This confirmation is given and should be interpreted in accordance with the provisions of Section 418 of the Companies Act 2006.

**Directors' Report (continued)**

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**Auditors**

The auditor, Deloitte LLP, has indicated its willingness to continue in office and, in accordance with Section 487(2) of the Companies Act 2006, has been re-appointed.

**Approved by the Board and signed on its behalf by:**



**M A Clarke**  
Director

Date: 27 June 2022

Registered office:  
BAE Systems Global Combat Systems Munitions Limited  
Warwick House  
PO Box 87  
Farnborough Aerospace Centre  
Farnborough  
Hampshire  
GU14 6YU

## **Directors' Responsibilities Statement**

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

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law), including Financial Reporting Standard 101 ("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 accounting estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

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

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## **Independent Auditor's Report to the Members of BAE Systems Global Combat Systems Munitions Limited**

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### **Report on the audit of the financial statements**

#### **Opinion**

In our opinion the financial statements of BAE Systems Global Combat Systems Munitions Limited (the "Company"):

- give a true and fair view of the state of the Company's affairs as at 31 December 2021 and of its profit for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice, including Financial Reporting Standard 101 "Reduced Disclosure Framework"; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

We have audited the financial statements which comprise:

- the Income Statement;
- the Statement of Comprehensive Income;
- the Balance Sheet;
- the Statement of Changes in Equity;
- the Statement of accounting policies; and
- the related notes 1 to 27.

The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards, including Financial Reporting Standard 101 "Reduced Disclosure Framework" (United Kingdom Generally Accepted Accounting Practice).

#### **Basis for opinion**

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the auditor's responsibilities for the audit of the financial statements section of our report.

We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the Financial Reporting Council's (the "FRC's") Ethical Standard, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

#### **Conclusions relating to going concern**

In auditing the financial statements, we have concluded that the directors' use of the going concern basis of accounting in the preparation of the financial statements is appropriate.

Based on the work we have performed, we have not identified any material uncertainties relating to events or conditions that, individually or collectively, may cast significant doubt on the company's ability to continue as a going concern for a period of at least twelve months from when the financial statements are authorised for issue.

Our responsibilities and the responsibilities of the directors with respect to going concern are described in the relevant sections of this report.

#### **Other information**

The other information comprises the information included in the annual report, other than the financial statements and our auditor's report thereon. The directors are responsible for the other information contained within the annual report. Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our report, we do not express any form of assurance conclusion thereon.

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## **Independent Auditor's Report to the Members of BAE Systems Global Combat Systems Munitions Limited (continued)**

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Our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the course of the audit, or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether this gives rise to a material misstatement in the financial statements themselves. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact.

We have nothing to report in this regard.

### **Responsibilities of directors**

As explained more fully in the directors' responsibilities statement, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for 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 the directors 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 an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a 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 the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is located on the FRC's website at: [www.frc.org.uk/auditorsresponsibilities](http://www.frc.org.uk/auditorsresponsibilities). This description forms part of our auditor's report.

### **Extent to which the audit was considered capable of detecting irregularities, including fraud**

Irregularities, including fraud, are instances of non-compliance with laws and regulations. We design procedures in line with our responsibilities, outlined above, to detect material misstatements in respect of irregularities, including fraud. The extent to which our procedures are capable of detecting irregularities, including fraud is detailed below.

We considered the nature of the company's industry and its control environment, and reviewed the company's documentation of their policies and procedures relating to fraud and compliance with laws and regulations. We also enquired of management about their own identification and assessment of the risks of irregularities.

We obtained an understanding of the legal and regulatory framework that the company operates in, and identified the key laws and regulations that:

- had a direct effect on the determination of material amounts and disclosures in the financial statements. These included the UK Companies Act 2006 and the Corporation Tax Act 2010; and
- do not have a direct effect on the financial statements but compliance with which may be fundamental to the company's ability to operate or to avoid a material penalty.

We discussed among the audit engagement team regarding the opportunities and incentives that may exist within the organisation for fraud and how and where fraud might occur in the financial statements.

As a result of performing the above, we identified the greatest potential for fraud in the following areas, and our specific procedures performed to address it are described below:

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**Independent Auditor's Report to the Members of BAE Systems Global Combat Systems Munitions Limited (continued)**

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- Cumulative catch up adjustments recorded within the entity in the year may have been incorrectly calculated or calculated based on inappropriate judgments made over contingency creation and release. As a result, the margins recognised on contracts in year could be materially misstated. In response to the risk, our procedures included challenging the basis of changes made to contract estimates at completion and contingencies across various contracts, validating the mechanical accuracy of the cumulative catch up calculations, and assessing the design and implementation of relevant controls which govern the creation and release of contingencies on contracts.

In common with all audits under ISAs (UK), we are also required to perform specific procedures to respond to the risk of management override. In addressing the risk of fraud through management override of controls, we tested the appropriateness of journal entries and other adjustments; assessed whether the judgements made in making accounting estimates are indicative of a potential bias; and evaluated the business rationale of any significant transactions that are unusual or outside the normal course of business.

In addition to the above, our procedures to respond to the risks identified included the following:

- reviewing financial statement disclosures by testing to supporting documentation to assess compliance with provisions of relevant laws and regulations described as having a direct effect on the financial statements;
- performing analytical procedures to identify any unusual or unexpected relationships that may indicate risks of material misstatement due to fraud;
- enquiring of management and concerning actual and potential litigation and claims, and instances of non-compliance with laws and regulations; and
- reading minutes of meetings of those charged with governance.

**Report on other legal and regulatory requirements****Opinions on other matters prescribed by the Companies Act 2006**

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the Strategic Report and the Directors' Report have been prepared in accordance with applicable legal requirements.

In the light of the knowledge and understanding of the Company and its environment obtained in the course of the audit, we have not identified any material misstatements in the Strategic Report or the Directors' Report.

**Matters on which we are required to report by exception**

Under the Companies Act 2006 we are required to report in respect of the following matters 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 respect of these matters.

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**Independent Auditor's Report to the Members of BAE Systems Global Combat Systems Munitions Limited (continued)**

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**Use of our report**

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.



Douglas King (Senior Statutory Auditor)

for and on behalf of Deloitte LLP

The Hanover Building  
Corporation Street  
Manchester  
United Kingdom  
M4 4AH

27 June 2022

**BAE Systems Global Combat Systems Munitions Limited**  
**Annual Report and Financial Statements**  
**31 December 2021**

**Income Statement**  
for the year ended 31 December 2021

	Note	2021 £000	2020 £000
Revenue	3	244,542	244,412
Operating costs	4	(223,749)	(225,732)
Other income	5	2,631	3,398
<b>Operating profit</b>		<b>23,424</b>	<b>22,078</b>
Income from investments	6	2,332	2,692
Financial income	7	3,051	1,020
Financial expense	8	(3,659)	(6,251)
<b>Profit before tax</b>		<b>25,148</b>	<b>19,539</b>
Tax	11	(2,799)	3,747
<b>Profit for the financial year</b>		<b>22,349</b>	<b>23,286</b>



**Statement of Comprehensive Income**  
for the year ended 31 December 2021

	Note	2021 £000	2020 £000
Profit for the financial year		<b>22,349</b>	23,286
<b>Items that will not be reclassified to the Income statement:</b>			
Remeasurements on retirement benefit schemes	22	<b>55,700</b>	(2,200)
Tax on items that will not be reclassified to the Income Statement	11	<b>(17,821)</b>	(831)
<b>Items that may be reclassified to Income Statement:</b>			
Amounts (debited)/credited to hedging reserve	23	<b>(4,243)</b>	3,182
Tax on items that may be reclassified to the Income Statement	23	<b>936</b>	(583)
<b>Total comprehensive income for the year</b>		<b>56,921</b>	22,854

The notes on pages 19 to 61 form part of these financial statements.

The results for 2021 and 2020 arise from continuing activities.

**BAE Systems Global Combat Systems Munitions Limited**  
**Annual Report and Financial Statements**  
**31 December 2021**

**Balance Sheet**  
as at 31 December 2021


	Note	2021 £000	2020 £000
<b>Non-current assets</b>			
Property, plant and equipment	12	80,558	81,081
Intangible assets	13	829	-
Investments	14	15,149	15,149
Right-of-use assets	20	89,034	95,044
Other financial assets	19	1	686
Retirement benefit surpluses	22	150,200	124,000
		<u>335,771</u>	<u>315,960</u>
<b>Current assets</b>			
Inventories	16	33,736	33,440
Trade, other and contract receivables	17	198,802	227,609
Other financial assets	19	863	2,769
Current tax		294	-
		<u>233,695</u>	<u>263,818</u>
		<u>569,466</u>	<u>579,778</u>
<b>Total assets</b>			

**BAE Systems Global Combat Systems Munitions Limited**  
**Annual Report and Financial Statements**  
**31 December 2021**

**Balance Sheet (continued)**  
as at 31 December 2021

	Note	2021 £000	2020 £000
<b>Non-current liabilities</b>			
Lease liabilities	20	(90,297)	(94,520)
Other financial liabilities	19	(14)	(338)
Retirement benefit obligations	22	(25,400)	(56,200)
Provisions	21	(1,108)	(1,954)
Deferred tax liabilities	15	(34,623)	(14,947)
		<u>(151,442)</u>	<u>(167,959)</u>
<b>Current liabilities</b>			
Trade and other payables	18	(280,523)	(314,468)
Lease liabilities	20	(4,524)	(4,209)
Other financial liabilities	19	(3,002)	(1,026)
Provisions	21	(2,991)	(3,227)
		<u>(291,040)</u>	<u>(322,930)</u>
<b>Total liabilities</b>		<u>(442,482)</u>	<u>(490,889)</u>
<b>Net assets</b>		<u>126,984</u>	<u>88,889</u>
<b>Capital and reserves</b>			
Issued share capital	23	50,000	50,000
Other reserves	23	(1,937)	1,370
Retained earnings		78,921	37,519
<b>Total equity</b>		<u>126,984</u>	<u>88,889</u>

Approved by the Board on 27 June 2022 and signed on its behalf by:



**M A Clarke**  
Director

Registered number: 01842252

The notes on pages 19 to 61 form part of these financial statements.

**Statement of Changes in Equity**  
for the year ended 31 December 2021

	Issued share capital £000	Other reserves £000	Retained earnings £000	Total equity £000
At 1 January 2020	50,000	(1,229)	36,136	84,907
Profit for the year	-	-	23,286	23,286
Other comprehensive income/(loss)	-	3,182	(2,200)	982
Taxation in respect of items of other comprehensive (loss)	-	(583)	(831)	(1,414)
Dividends (note 24)	-	-	(20,000)	(20,000)
Share-based payments	-	-	1,128	1,128
At 31 December 2020	50,000	1,370	37,519	88,889
Profit for the year	-	-	22,349	22,349
Other comprehensive (loss)/income	-	(4,243)	55,700	51,457
Taxation in respect of items of other comprehensive income/(loss)	-	936	(17,821)	(16,885)
Dividends (note 24)	-	-	(20,000)	(20,000)
Share-based payments	-	-	1,174	1,174
At 31 December 2021	50,000	(1,937)	78,921	126,984

The notes on pages 19 to 61 form part of these financial statements.

## **Notes to the Financial Statements**

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### **1. General information**

BAE Systems Global Combat Systems Munitions Limited is a private company, limited by shares, and registered in England and Wales and incorporated in the United Kingdom. Its ultimate controlling party is disclosed in note 27. The address of the Company's registered office is shown on page 8.

The principal activity of the Company is set out in the Strategic Report on page 1. These financial statements, which have been prepared in accordance with the Companies Act 2006, are presented in pounds sterling and, unless otherwise stated, rounded to the nearest thousand.

### **2. Accounting policies**

#### **2.1 Basis of preparation**

These financial statements have been prepared in accordance with FRS 101. The Company applies the recognition, measurement and disclosure requirements of International Financial Reporting Standards ("IFRS") and International Accounting Standards ("IAS"), but makes amendments where necessary in order to comply with the Companies Act 2006, and has set out below where advantage of the FRS 101 disclosure exemptions has been taken:

- the requirements of paragraphs 45(b) and 46 to 52 of IFRS 2 Share-based Payment;
- the requirements of IFRS 7 Financial Instruments: Disclosures;
- the requirements of paragraphs 91-99 of IFRS 13 Fair Value Measurement;
- the requirements of the second sentence of paragraph 110 and paragraphs 113(a), 114, 115, 118, 119(a) to (c), 120 to 127 and 129 of IFRS 15 Revenue from Contracts with Customers;
- the requirement in paragraph 38 of IAS 1 Presentation of Financial Statements to present comparative information in respect of:
  - paragraph 79(a)(iv) of IAS 1 Presentation of Financial Statements;
  - paragraph 73(e) of IAS 16 Property, Plant and Equipment;
  - paragraphs 76 and 79(d) of IAS 40 Investment Property; and
- the requirements of paragraphs 10(d), 10(f), 16, 38A, 38B, 38C, 38D, 40A, 40B, 40C, 40D, 111 and 134 to 136 of IAS 1 Presentation of Financial Statements;
- the requirements of IAS 7 Statement of Cash Flows;
- the requirements of paragraphs 30 and 31 of IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors;
- the requirements of paragraph 17 and 18A of IAS 24 Related Party Disclosures;
- the requirements in IAS 24 Related Party Disclosures to disclose related party transactions entered into between two or more members of a group, provided that any subsidiary which is a party to the transaction is wholly owned by such a member; and
- the requirements of paragraphs 130(f)(ii), 130(f)(iii), 134(d)-134(f) and 135(c)-135(e) of IAS 36 Impairment of Assets.

## Notes to the Financial Statements

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### 2. Accounting policies (continued)

#### 2.1 Basis of preparation (continued)

The Company intends to continue to prepare its financial statements in accordance with FRS 101.

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, BAE Systems plc, a company registered in England and Wales. Accordingly, these financial statements present information about the Company as an individual undertaking and not as a group.

The financial statements have been prepared under the historical cost convention, as modified by the revaluation of relevant financial assets and financial liabilities (including derivative instruments).

These financial statements have been prepared using the going concern basis of accounting.

#### Critical accounting policies

Certain of the Company's significant accounting policies are considered by the directors to be critical because of the level of complexity, judgement or estimation involved in their application and their impact on the financial statements. The critical accounting policies are listed below:

Critical accounting policy	Description
Valuation of retirement benefit obligations	Defined benefit pension scheme accounting valuations are prepared by independent actuaries. The liabilities of the pension schemes are valued based on a number of actuarial assumptions. For each of the actuarial assumptions used there is a range of possible values and management estimates the point within that range that most appropriately reflects the Company's circumstances. Small changes in these assumptions can have a significant impact on the size of the deficit. See note 22.
Cumulative catch up adjustments	Cumulative catch up adjustments recorded within the entity in the year may have been incorrectly calculated or calculated based on inappropriate judgments made over contingency creation and release. As a result, the margins recognised on contracts in year could be materially misstated. In response to the risk, our procedures included challenging the basis of changes made to contract estimates at completion and contingencies across various contracts, validating the mechanical accuracy of the cumulative catch up calculations, and assessing the design and implementation of relevant controls which govern the creation and release of contingencies on contracts.

## Notes to the Financial Statements

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### 2. Accounting policies (continued)

#### 2.1 Basis of preparation (continued)

##### **Judgements made in applying accounting policies**

In the course of preparing the financial statements, no judgements have been made in the process of applying the Company's accounting policies, other than those involving estimates, that have had a significant effect on the amounts recognised in the financial statements.

##### **Sources of estimation uncertainty**

The application of the Company's accounting policies requires the use of estimates. In the event that these estimates prove to be incorrect, there may be an adjustment to the carrying amounts of assets and liabilities within the next financial year. Potential areas of the Company's financial statements which could be materially impacted may include, but are not limited to:

Post-employment benefit obligations - the Company's share of the net IAS 19 post-employment scheme surplus £124,800k (at 31 December 2021). See note 22 and critical accounting policies above.

##### **Changes in accounting policies**

The following standards, interpretations and amendments to existing standards became effective on 1 January 2021 and have not had a material impact on the Company:

- Amendments to IFRS 9, IAS 39, IFRS 4 and IFRS 16 Interest Rate Benchmark Reform (Phase 2); and
- Amendments to IFRS 4 Insurance Contracts: deferral of IFRS9.

The following amendments to existing standards have been issued and became effective in the year as a response to the COVID19 pandemic, but did not have a material impact on the Company:

- Amendment to IFRS 16 Leases: Covid-19-Related Rent Concessions beyond June 2021, effective from 1 April 2021 and adopted by the UK Secretary of State for Business, Energy and Industrial Strategy on 21 May 2021.

##### **Significant accounting policies**

The significant accounting policies applied in the preparation of these financial statements are set out below. These policies have been applied consistently to all the years presented, unless otherwise stated. The directors believe that the financial statements reflect appropriate judgements and estimates, and provide a true and fair view of the Company's financial performance and position.

#### 2.2 Revenue and profit recognition

Revenue represents income derived from contracts for the provision of goods and services, over time or at a point in time, by the Company to customers in exchange for consideration in the ordinary course of the Company's activities.

## Notes to the Financial Statements

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### 2. Accounting policies (continued)

#### 2.2 Revenue and profit recognition (continued)

##### *Performance obligations*

Upon approval by the parties to a contract, the contract is assessed to identify each promise to transfer either a distinct good or service or a series of distinct goods or services that are substantially the same and have the same pattern of transfer to the customer. Goods and services are distinct and accounted for as separate performance obligations in the contract if the customer can benefit from them either on their own or together with other resources that are readily available to the customer and they are separately identifiable in the contract. The Company provides warranties to its customers to give them assurance that its products and services will function in line with agreed-upon specifications. Warranties are not provided separately and, therefore, do not represent separate performance obligations.

##### *Transaction price*

At the start of the contract, the total transaction price is estimated as the amount of consideration to which the Company expects to be entitled in exchange for transferring the promised goods and services to the customer, excluding sales taxes. Variable consideration, such as price escalation, is included based on the expected value or most likely amount only to the extent that it is highly probable that there will not be a reversal in the amount of cumulative revenue recognised. The transaction price does not include estimates of consideration resulting from contract modifications, such as change orders, until they have been approved by the parties to the contract. The total transaction price is allocated to the performance obligations identified in the contract in proportion to their relative stand-alone selling prices. Given the bespoke nature of many of the Company's products and services, which are designed and/or manufactured under contract to the customer's individual specifications, there are typically no observable stand-alone selling prices. Instead, stand-alone selling prices are typically estimated based on expected costs plus contract margin consistent with the Company's pricing principles. Whilst payment terms vary from contract to contract, on many of the Company's contracts, an element of the transaction price is received in advance of delivery. The Company therefore has significant contract liabilities. The Company's contracts are not considered to include significant financing components on the basis that there is no difference between the consideration and the cash selling price either as a result of UK Ministry of Defence contracting rules which prohibit the inclusion of financing in the sales price or negotiations on competitive international export contracts which do not make allowance for the cash payment profile.

##### *Revenue and profit recognition*

Revenue is recognised as performance obligations are satisfied as control of the goods and services is transferred to the customer. For each performance obligation within a contract, the Company determines whether it is satisfied over time or at a point in time. Performance obligations are satisfied over time if one of the following criteria is satisfied:

- the customer simultaneously receives and consumes the benefits provided by the Company's performance as it performs;
- Company's performance creates or enhances an asset that the customer controls as the asset is created or enhanced; or
- the Company's performance does not create an asset with an alternative use to the Company and it has an enforceable right to payment for performance completed to date.

The Company has determined that most of its contracts satisfy the over-time criteria, either because the customer simultaneously receives and consumes the benefits provided by the Company's performance as it performs (typically services or support contracts) or the Company's performance does not create an asset with an alternative use to the Company and it has an enforceable right to payment for performance completed to date (typically development or production contracts).



## Notes to the Financial Statements

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### 2. Accounting policies (continued)

#### 2.2 Revenue and profit recognition (continued)

For each performance obligation to be recognised over time, the Company recognises revenue using an input method, based on costs incurred in the period. Revenue and attributable margin are calculated by reference to reliable estimates of transaction price and total expected costs, after making suitable allowances for technical and other risks. Revenue and associated margin are therefore recognised progressively as costs are incurred, and as risks have been mitigated or retired. The Company has determined that this method faithfully depicts the Company's performance in transferring control of the goods and services to the customer.

If the over-time criteria for revenue recognition are not met, revenue is recognised at the point in time that control is transferred to the customer, which is usually when legal title passes to the customer and the business has the right to payment, for example, on delivery.

When it is probable that total contract costs will exceed total contract revenue, the expected loss is recognised immediately as an expense.

##### *Outstanding commitments*

The Company regularly reviews outstanding commitment for purchases in its supply chain in order to inform revenue recognition under IFRS15 trading principles. Where the Company has received notification that the supplier has completed the manufacture of goods, but has not yet delivered and invoiced for them and the ultimate customer controls the asset, i.e. neither the subcontractor or the Company have an alternative use for the asset, the Company will accrue for these costs and recognise revenue in line with overtime trading principles under IFRS15.

##### *Contract modifications*

The Company's contracts are often amended for changes in customers' requirements and specifications. A contract modification exists when the parties to the contract approve a modification that either changes existing or creates new enforceable rights and obligations. The effect of a contract modification on the transaction price and the Company's measure of progress towards the satisfaction of the performance obligation to which it relates is recognised in one of the following ways:

1. prospectively, as an additional, separate contract; or
2. prospectively, as a termination of the existing contract and creation of a new contract; or
3. as part of the original contract using a cumulative catch-up.

The majority of the Company's contract modifications are treated under either 1 (for example, the requirement for additional distinct goods or services) or 3 (for example, a change in the specification of the distinct goods or services for a partially completed contract), although the facts and circumstances of any contract modification are considered individually as the types of modifications will vary contract-by-contract and may result in different accounting outcomes.

##### *Costs to obtain a contract*

The Company expenses pre-contract bidding costs which are incurred regardless of whether a contract is awarded unless legislation permits recovery, which can be the case for certain MOD single source contracts.

##### *Costs to fulfil a contract*

Contract fulfilment costs in respect of over-time contracts are expensed as incurred. Contract fulfilment costs in respect of point-in-time contracts are accounted for under IAS 2 Inventories.

## Notes to the Financial Statements

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### 2. Accounting policies (continued)

#### 2.3 Leases

##### *The Company as lessee*

All leases in which the Company is lessee (except as noted below) are recognised as a right-of-use asset and a corresponding lease liability at the date at which the leased asset is available for use by the Company. Each lease payment is allocated between repayment of the lease liability and finance cost. The finance cost is charged to the Income Statement over the lease term to produce a constant periodic rate of interest on the lease liability. The right-of-use asset is depreciated over the shorter of the asset's useful life and the lease term on a straight-line basis.

The lease liability is initially measured as the present value of future lease payments, discounted using the interest rate implicit in the lease. Where this rate is not determinable, the Company's incremental borrowing rate is used, which is the interest rate the Company would have to pay to borrow the amount necessary to obtain an asset of similar value, in a similar economic environment with similar terms and conditions.

The right-of-use asset is initially measured at cost, comprising the initial value of the lease liability, any lease payments made (net of any incentives received from the lessor) before the commencement of the lease, any initial direct costs and any restoration costs.

The carrying amounts of the Company's right-of-use assets are reviewed at each Balance Sheet date to determine whether there is any indication of impairment.

Payments in respect of short-term leases, low-value leases and leases of intangible assets are charged to the Income Statement on a straight-line basis over the lease term.

#### 2.4 Research and development

The Company undertakes research and development activities either on its own behalf or on behalf of customers.

Company-funded expenditure on research, and on development activities not meeting the conditions for capitalisation, is written off as incurred and charged to the Income Statement.

Where the research and development activity is performed on behalf of customers, the revenue arising is recognised in the Income Statement in accordance with the Company's revenue recognition policy.

Total research and development expenditure was £2,720k (2020: £1,719k), of which £1,359k (2020: £812k) was funded by the Company.

#### 2.5 Interest income and borrowing costs

Interest income and borrowing costs are recognised in the Income Statement in the period in which they are incurred.

## **Notes to the Financial Statements**

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### **2. Accounting policies (continued)**

#### **2.6 Retirement benefit obligations**

##### *Defined contribution pension schemes*

A defined contribution pension scheme is a post-employment benefit plan under which the Company pays fixed contributions into a separate entity and will have no legal or constructive obligation to pay further amounts.

Obligations for contributions are recognised as an expense in the Income Statement as incurred.

##### *Defined benefit pension schemes*

The cost of providing benefits is determined periodically by independent actuaries and charged to the Income Statement in the period in which those benefits are earned by the employees. Remeasurements, including actuarial gains and losses, are recognised in the Statement of Comprehensive Income in the period in which they occur. Past service costs resulting from a plan amendment or curtailment are recognised immediately in the Income Statement.

The retirement benefit surpluses and obligations recognised in the Company's Balance Sheet represents the fair value of scheme assets, less the present value of the defined benefit obligations calculated using a number of actuarial assumptions as set out on page 53. The bid values of scheme assets are not intended to be realised in the short term and may be subject to significant change before they are realised. The present values of scheme liabilities are derived from cash flow projections over long periods and are, therefore, inherently uncertain.

IAS 19 Employee Benefits, limits the measurement of a defined benefit surplus to the lower of the surplus in the defined benefit scheme and the asset ceiling. The asset ceiling is the present value of any economic benefits available in the form of refunds from the scheme or reductions in future contributions to the scheme. IFRIC 14 IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction, issued in 2007, provides an interpretation of the requirements of IAS 19, clarifying that a refund is available if the entity has an unconditional right to a refund in certain circumstances. The Company has applied IFRIC 14 and has determined that there is no limit on the recognition of the surpluses in its defined benefit pension schemes as at 31 December 2021.

The Company participates in a number of group and multi-employer schemes administered by its ultimate parent company, BAE Systems plc. A share of the IAS 19 Employee Benefits, pension deficit has been allocated to all participating employers. This allocation is based on the relative payroll contributions of active members which is consistent with prior years.

Whilst this methodology is intended to reflect a reasonable estimate of the share of the deficit, it may not accurately reflect the obligations of the participating employers. Gains and losses resulting from changes to the relative payroll contributions of active members year on year are included within the actual return on assets and actuarial gains and losses for the disclosures in respect of changes in the fair value of scheme assets and changes in the present value of defined benefit obligations, respectively.

In the event that an employer who participates in BAE Systems plc's pension schemes fails or cannot be compelled to fulfil its obligations as a participating employer, the remaining participating employers are obliged to collectively take on its obligations. The Company considers the likelihood of this event arising as remote.

## **Notes to the Financial Statements**

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### **2. Accounting policies (continued)**

#### **2.7 Share-based payments**

BAE Systems plc, the Company's ultimate parent company, issues equity-settled share options to employees of the Company. In accordance with the requirements of IFRS 2 Share-based Payment, the Company has recognised a charge for the equity-settled share options issued to its employees.

Equity-settled share options and long-term incentive plan arrangements are measured at fair value at the date of grant using an option pricing model.

The fair value is expensed on a straight-line basis over the vesting period, based on the Company's estimate of the number of shares that will actually vest.

#### **2.8 Related party transactions**

The Company has related party relationships with BAE Systems plc and its subsidiaries/joint-ventures. Transactions occur with related parties in the normal course of business, are priced on an arm's-length basis and settled on normal trade terms.

#### **2.9 Intangible assets**

Intangible assets are carried at cost or valuation, less accumulated amortisation and impairment losses.

##### *Software*

Software includes:

- Computer software licences acquired for use within the Company which are capitalised as an intangible asset on the basis of the costs incurred to acquire and bring to use the specific software; and
- Software development costs that are directly associated with the production of identifiable and unique software products controlled by the Company, and that will probably generate economic benefits exceeding costs beyond one year, which are recognised as intangible assets. Company-funded expenditure associated with enhancing or maintaining computer software programs for sale is recognised as an expense as incurred

##### *Amortisation*

Amortisation on intangible assets, is charged to the Income Statement on a straight-line basis over their estimated useful lives.

The estimated useful lives are as follows:

Software	- 2 to 10 years
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## Notes to the Financial Statements

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### 2. Accounting policies (continued)

#### 2.10 Tax

Tax expense comprises current and deferred tax. Current and deferred tax is recognised in the profit or loss except to the extent that it relates to a business combination or items recognised directly in equity or in other comprehensive income.

##### *Current tax*

Current tax is the expected tax payable or receivable on the taxable profit or loss for the year, using tax rates enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

##### *Deferred tax*

Deferred tax is recognised in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for tax purposes. Deferred tax is not recognised for temporary differences:

- on the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit or loss;
- related to investments in subsidiaries and equity accounted investments to the extent that it is probable that they will not reverse in the foreseeable future; and
- arising on the initial recognition of goodwill.

Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

A deferred tax asset is recognised for unused tax losses, tax credits and deductible temporary differences to the extent that it is probable that future taxable profits will be available against which they can be utilised. Deferred tax assets are reviewed at each reporting date and reduced to the extent that it is no longer probable that the related tax benefit will be realised.

Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets, and they relate to corporate income taxes levied by the same tax authority and they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realised simultaneously.

## Notes to the Financial Statements

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### 2. Accounting policies (continued)

#### 2.11 Property, plant and equipment

##### *Cost*

Items of property, plant and equipment are stated at cost less accumulated depreciation and impairment losses. The cost of self-constructed assets includes the cost of materials, direct labour and an appropriate proportion of production overheads. The cost of demonstration assets is written off as incurred.

Assets held for leasing out under operating leases are included in property, plant and equipment at cost less accumulated depreciation and impairment losses.

##### *Depreciation*

Depreciation is provided, normally on a straight-line basis, to write off the cost of property, plant and equipment over their estimated useful lives to any estimated residual value, using the following rates:

Buildings	- up to 50 years, or the lease term if shorter
Computer equipment and motor vehicles	- 4 to 5 years
Other equipment	- 10 to 20 years, or the project life if shorter

No depreciation is provided on freehold land and assets in the course of construction.

The assets' residual values, useful lives and depreciation methods are reviewed, and adjusted if appropriate, at each Balance Sheet date.

##### *Impairment*

The carrying amounts of the Company's property, plant and equipment are reviewed at each Balance Sheet date to determine whether there is any indication of impairment.

## **Notes to the Financial Statements**

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### **2. Accounting policies (continued)**

#### **2.12 Impairment**

The carrying amounts of the Company's intangible assets (excluding goodwill), property, plant and equipment, right-of-use assets, investment property and equity accounted investments are reviewed at each Balance Sheet date to determine whether there is any indication of impairment as required by IAS 36 Impairment of Assets. If any such indication exists, the asset's recoverable amount is estimated. For goodwill and intangible assets that are not yet available for use, impairment testing is performed annually.

An impairment loss is recognised whenever the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount.

The recoverable amount is the greater 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 using an appropriate pre-tax discount rate. For an asset that does not generate largely independent cash flows, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

Impairment losses are recognised in the Income Statement.

An impairment loss in respect of goodwill is not reversed. An impairment loss in respect of other intangible assets, property, plant and equipment, investment property and right-of-use assets is reversed if the subsequent increase in recoverable amount can be related objectively to an event occurring after the impairment loss was recognised or if there has been a change in the estimate used to determine the recoverable amount.

An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

#### **2.13 Investments**

Fixed asset investments in shares in subsidiary undertakings and in shares in participating interests are stated at cost less provision for impairment.

#### **2.14 Inventories**

Inventories are stated at the lower of cost, including all relevant overhead expenditure, and net realisable value. Inventory is provided for when it is either surplus to requirements or if it is awaiting disposal or scrappage.

#### **2.15 Trade, other and contract receivables**

The Company writes off a trade receivable when there is objective evidence that the debtor is in significant financial difficulty and there is no realistic prospect of recovery, for example, when a debtor enters bankruptcy or financial reorganisation.

Contract receivables represent amounts for which the Company has an unconditional right to consideration in respect of unbilled revenue recognised at the Balance Sheet date and comprise costs incurred plus attributable margin.

## Notes to the Financial Statements

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### 2. Accounting policies (continued)

#### 2.16 Trade and other payables

Trade and other payables are stated at amortised cost.

#### 2.17 Provisions

A provision is recognised in the Balance Sheet when the Company has a present legal or constructive obligation as a result of a past event, it is probable that an outflow of economic benefits will be required to settle the obligation and the amount has been reliably estimated. If the effect is material, provisions are determined by discounting the expected future cash flows at an appropriate pre-tax discount rate.

##### *Warranties and after-sales service*

Warranties and after-sales service are provided in the normal course of business with provisions for associated costs being made based on an assessment of future claims with reference to past experience. A provision for warranties is recognised when the underlying products and services are sold. The provision is based on historical warranty data and a weighting of possible outcomes against their associated probabilities.

##### *Contract loss*

The Company holds provisions for expected legal, contractual and environmental costs that it expects to incur over an extended period. Management exercises judgement to determine the amount of these provisions. Provision is made for known issues based on past experience of similar items and other known factors. Each provision is considered separately and the amount provided reflects the best estimate of the most likely amount, being the single most likely amount in a range of possible outcomes.

#### 2.18 Financial instruments

##### *Derivative financial instruments and hedging activities*

The international nature of the Company's business means it is exposed to volatility in currency exchange rates. In order to protect itself against currency fluctuations, the Company's policy is to hedge all material firm transactional exposures.

In accordance with its treasury policy, the Company does not hold derivative financial instruments for trading purposes.

Derivative financial instruments are recognised initially at fair value. Subsequent to initial recognition, such instruments are stated at fair value at the Balance Sheet date. The fair values are estimated by discounting expected future cash flows.

The Company has applied the IFRS 9 general hedge accounting requirements from the date of initial application on 1 January 2018.

##### *Cash flow hedges*

Where a derivative financial instrument is designated as a hedge of the exposure to variability in cash flows relating to a highly probable forecast transaction (income or expense) or recognised asset or liability, the effective portion of any change in the fair value of the instrument is recognised in other comprehensive income and presented in the hedging reserve in equity. Amounts recognised in equity are removed from the hedging reserve and included in the cost of the underlying transaction or reclassified to the Income Statement when the underlying transaction affects profit or loss. These amounts are presented within the same line item in the Income Statement as the underlying transaction, typically revenue or operating costs. The ineffective portion of any change in the fair value of the instrument is recognised in the Income Statement within finance costs immediately. The Company treats the foreign



## Notes to the Financial Statements

### 2. Accounting policies (continued)

#### 2.18 Financial instruments (continued)

currency basis element of the designated foreign exchange derivative hedging instruments as a cost of hedging and as such it is excluded from the hedge designation.

#### 2.19 Dividends

Dividends received and receivable are credited to the Company's Income Statement. Equity dividends paid on ordinary share capital are recognised as a liability in the period in which they are declared.

### 3. Revenue

Revenue by reporting segment

	2021 £000	2020 £000
External sales	221,666	226,016
Intercompany sales	22,876	18,396
	<u>244,542</u>	<u>244,412</u>

Revenue by customer location:

	2021 £000	2020 £000
United Kingdom	220,435	221,530
Rest of Europe	18,693	10,069
Rest of the world	5,414	12,813
	<u>244,542</u>	<u>244,412</u>

## Notes to the Financial Statements

### 4. Operating costs

	2021 £000	2020 £000
Raw materials, subcontracts and other bought-in items used	97,403	102,910
Staff costs (note 9)	54,295	54,481
Depreciation, amortisation and impairment	19,845	20,504
Other operating charges	52,206	47,837
	<u>223,749</u>	<u>225,732</u>

The remuneration of the auditor for the year ended 31 December 2021 for auditing of the financial statements was £150k (2020: £125k) and £nil (2020: £nil) in respect of non-audit work.

Total research and development expenditure was £2,720k (2020: £1,719k), of which £1,359k (2020: £812k) was funded by the Company.

### 5. Other income

	2021 £000	2020 £000
Royalty receivable	1,231	1,202
Other operating income	1,400	2,196
	<u>2,631</u>	<u>3,398</u>

### 6. Income from investments

	2021 £000	2020 £000
Dividends from investments	2,332	2,692
	<u>2,332</u>	<u>2,692</u>

## Notes to the Financial Statements

### 7. Financial income

	2021 £000	2020 £000
Net interest income on retirement benefit obligations (note 22)	900	1,000
Foreign exchange gains	2,151	20
	<u>3,051</u>	<u>1,020</u>

### 8. Financial expense

	2021 £000	2020 £000
Interest expense	809	1,049
Foreign exchange losses	63	2,293
Interest expense on lease liabilities (note 20)	2,787	2,909
	<u>3,659</u>	<u>6,251</u>

### 9. Employees

The monthly average number of Company employees was 1,007 (2020: 1,029). The aggregate staff costs of Company employees were as follows:

	2021 £000	2020 £000
Wages and salaries	42,291	42,630
Social security costs	4,158	4,060
Cost of defined benefit pension scheme (note 22)	5,400	5,500
Cost of defined contribution pension scheme (note 22)	1,272	1,163
Share-based payments	1,174	1,128
	<u>54,295</u>	<u>54,481</u>

## Notes to the Financial Statements

### 10. Directors' remuneration

The disclosures below represent an allocation of the emoluments received by the directors to reflect their qualifying services to the Company.

	<b>2021</b>	2020
	<b>£000</b>	£000
Directors' remuneration	<b>335</b>	388
Company contributions to money purchase pension schemes	<b>20</b>	11
Company contributions to defined benefit pension schemes	-	37
Compensation for loss of office	-	113
	<b>355</b>	549

Retirement benefits are accruing to the following number of directors under:

	<b>2021</b>	2020
	<b>Number of directors</b>	Number of directors
Money purchase schemes	<b>2</b>	2
Defined benefit schemes	-	2

	<b>2021</b>	2020
	<b>Number of directors</b>	Number of directors
Number of directors in respect of whose qualifying services shares were received or receivable under long-term incentive schemes	-	1

Amounts paid in respect of the highest paid director were as follows:

	<b>2021</b>	2020
	<b>£000</b>	£000
Remuneration and amounts receivable under long-term incentive schemes	<b>230</b>	158
Company contributions to money purchase pension schemes	<b>14</b>	10
	<b>244</b>	168

**Notes to the Financial Statements**

**11. Tax**

	2021 £000	2020 £000
<b>Current tax</b>		
UK:		
Current tax	(1,096)	(1,469)
Adjustments in respect of prior years	363	4,350
	<u>(733)</u>	<u>2,881</u>
<b>Deferred tax</b>		
Origination and reversal of temporary differences	(699)	542
Tax rate adjustment <sup>1</sup>	(1,293)	(582)
Adjustments in respect of prior years	(74)	906
	<u>(2,066)</u>	<u>866</u>
	<u>(2,799)</u>	<u>3,747</u>
<b>Tax (expense)/income</b>		

<sup>1</sup>The Government announced in 2021 that from 1 April 2023 the UK corporation tax rate would increase from 19% to 25%. The deferred tax liability at each Balance Sheet date has been calculated at the tax rates, enacted at that date, expected to apply to the temporary differences when they reverse. The resulting tax rate adjustment has been partly recorded in the Income Statement and partly in the Statement of Comprehensive Income.

## Notes to the Financial Statements

### 11. Tax (continued)

#### Reconciliation of tax expense

The following reconciles the expected tax expense, using the UK corporation tax rate, to the reported tax (expense)/income:

	2021 £000	2020 £000
<b>Profit before tax</b>	<b>25,148</b>	<b>19,539</b>
UK corporation tax rate	19.00%	19.00%
Expected tax expense on profit	(4,778)	(3,712)
Expenses not tax effected	(12)	(16)
Income not subject to tax	449	531
Property, plant and equipment	(202)	(478)
Provisions and accruals	-	(3)
Retirement benefit schemes	(78)	-
Share-based payments	(20)	16
Imputed interest expense/(income)	9	(17)
Losses received from fellow group companies	2,837	2,752
Adjustments in respect of prior years	289	5,256
Tax rate adjustment <sup>1</sup>	(1,293)	(582)
<b>Tax (income)/expense</b>	<b>(2,799)</b>	<b>3,747</b>

Notes to the Financial Statements

11. Tax (continued)

Tax recognised in other comprehensive income

	2021			2020		
	Before tax £000	Tax benefit/ (expense) £000	Net of tax £000	Before tax £000	Tax benefit/ (expense) £000	Net of tax £000
<b>Items that will not be reclassified to the Income Statement:</b>						
Remeasurements on retirement benefit schemes	55,700	(14,010)	41,690	(2,200)	207	(1,993)
Tax rate adjustment <sup>1</sup>	-	(3,811)	(3,811)	-	(1,038)	(1,038)
<b>Items that may be reclassified to the Income Statement:</b>						
Amounts credited/(charged) to hedging reserve	(4,243)	1,061	(3,182)	3,182	(605)	2,577
Tax rate adjustment <sup>1</sup>	-	(125)	(125)	-	22	22
	<b>51,457</b>	<b>(16,885)</b>	<b>34,572</b>	<b>982</b>	<b>(1,414)</b>	<b>(432)</b>

Notes to the Financial Statements

11. Tax (continued)

	2021			2020		
	Other reserves £000	Retained earnings £000	Total £000	Other reserves £000	Retained earnings £000	Total £000
<b>Current tax</b>						
Retirement benefit schemes	-	725	725	-	823	823
	-	725	725	-	823	823
<b>Deferred tax</b>						
Tax rate adjustment <sup>1</sup>	(125)	(3,811)	(3,936)	22	(1,038)	(1,016)
Financial instruments	1,061	-	1,061	(605)	-	(605)
Retirement benefit schemes	-	(14,735)	(14,735)	-	(616)	(616)
	936	(18,546)	(17,610)	(583)	(1,654)	(2,237)
<b>Tax on other comprehensive income</b>	936	(17,821)	(16,885)	(583)	(831)	(1,414)

<sup>1</sup>The Government announced in 2021 that from 1 April 2023 the UK corporation tax rate would increase from 19% to 25%. The deferred tax liability at each Balance Sheet date has been calculated at the tax rates, enacted at that date, expected to apply to the temporary differences when they reverse. The resulting tax rate adjustment has been partly recorded in the Income Statement and partly in the Statement of Comprehensive Income.



**Notes to the Financial Statements**

**12. Property, plant and equipment**

	Land and buildings £000	Plant and machinery £000	Total £000
<b>Cost or valuation</b>			
At 1 January 2021	38,947	171,252	210,199
Additions	2,685	11,075	13,760
Disposals	-	(560)	(560)
Transfers	-	(767)	(767)
<b>At 31 December 2021</b>	<b>41,632</b>	<b>181,000</b>	<b>222,632</b>
<b>Depreciation</b>			
At 1 January 2021	14,582	114,536	129,118
Depreciation charge for the year	1,749	11,703	13,452
Disposals	-	(496)	(496)
<b>At 31 December 2021</b>	<b>16,331</b>	<b>125,743</b>	<b>142,074</b>
<b>Net book value</b>			
<b>At 31 December 2021</b>	<b>25,301</b>	<b>55,257</b>	<b>80,558</b>
At 31 December 2020	24,365	56,716	81,081
<b>Non-depreciated assets:</b>			
Assets in course of construction			
<b>At 31 December 2021</b>	<b>2,565</b>	<b>16,492</b>	<b>19,057</b>
At 31 December 2020	171	13,095	13,266

**Capital commitments**

Capital expenditure contracted for but not provided for in full in the financial statements is £5,738k (2020: £1,710k).

## Notes to the Financial Statements

### 13. Intangible assets

	Computer software £000
<b>Cost</b>	
Additions - external	91
Transfers from assets in course of construction	767
At 31 December 2021	<u>858</u>
<b>Amortisation</b>	
Amortisation charge for the year	29
At 31 December 2021	<u>29</u>
<b>Net book value</b>	
At 31 December 2021	<u><u>829</u></u>

## Notes to the Financial Statements

### 14. Investments

	Investments £000
<b>Cost</b>	
At 1 January 2021	15,149
<b>At 31 December 2021</b>	<b>15,149</b>
<b>Net book value</b>	
<b>At 31 December 2021</b>	<b>15,149</b>
At 31 December 2020	15,149

#### Impairment testing

During the year, management conducted an impairment review of the investments held by the Company. As a result of this review, there were no impairment reversals required.

The recoverable amount of the investments held by the Company has been calculated with reference to their value in use. The value in use calculations use risk-adjusted future cash flow projections based on the five-year Integrated Business Plan (IBP) and include a terminal value based on the projections for the final year of that plan, with growth rate assumptions in the range 0% to 2% applied. The IBP process includes the use of historic experience, available government spending data and the BAE Systems plc group's order backlog. Pre-tax discount rates, derived from the group's post-tax weighted average cost of capital of 6% (2020 6.62%) (adjusted for risks specific to the market in which the cash-generating unit operates), have been used in discounting these projected risk-adjusted cash flows.

## Notes to the Financial Statements

### 14. Investments (continued)

#### Subsidiary undertakings and participating interests at 31 December 2021

In accordance with Section 409 of the Companies Act 2006, a full list of subsidiary undertakings and significant holdings as at 31 December 2021 is disclosed below. Unless otherwise stated, all subsidiary undertakings and significant holdings are owned directly by the Company and, unless otherwise stated, have a financial year end of 31 December.

Company name	Class of shares held	Proportion of class (%)
Royal Ordnance (Crown Service) Pension Scheme Trustees Limited <i>Warwick House, PO Box 87, Farnborough Aerospace Centre, Farnborough, Hampshire GU14 6YU, United Kingdom</i>	Ordinary shares of £1	100%
Royal Ordnance Senior Staff Pension Scheme Trustees Limited <i>Warwick House, PO Box 87, Farnborough Aerospace Centre, Farnborough, Hampshire GU14 6YU, United Kingdom</i>	Ordinary shares of £1	100%
International Military Sales Limited <i>Warwick House, PO Box 87, Farnborough Aerospace Centre, Farnborough, Hampshire GU14 6YU, United Kingdom</i>	Ordinary shares of £1	100%
CTA International SAS <i>13 Route De La Miniere, 78000 Versailles, France</i>	Ordinary shares of €15	50%

### 15. Deferred taxation

#### Deferred tax assets/(liabilities)

	Deferred tax assets		Deferred tax liabilities		Net balance at 31 December	
	2021	2020	2021	2020	2021	2020
	£000	£000	£000	£000	£000	£000
Property, plant and equipment	-	-	(5,846)	(4,094)	(5,846)	(4,094)
Provisions and accruals	264	253	-	-	264	253
Retirement benefit schemes:						
Surpluses	-	-	(31,200)	(12,882)	(31,200)	(12,882)
Additional contributions	1,621	2,174	-	-	1,621	2,174
Financial instruments	538	-	-	(398)	538	(398)
Deferred tax assets/(liabilities)	2,423	2,427	(37,046)	(17,374)	(34,623)	(14,947)

**Notes to the Financial Statements**

**15. Deferred taxation (continued)**

**Movement in temporary differences during the year**

	At 1 January 2021 £000	Recognised in income £000	Recognised in equity £000	At 31 December 2021 £000
Property, plant and equipment	(4,094)	(1,752)	-	(5,846)
Provisions and accruals	253	11	-	264
Retirement benefit schemes:				
Surpluses	(12,882)	(325)	(17,993)	(31,200)
Additional contributions	2,174	-	(553)	1,621
Financial instruments	(398)	-	936	538
	<u>(14,947)</u>	<u>(2,066)</u>	<u>(17,610)</u>	<u>(34,623)</u>

	At 1 January 2020 £000	Recognised in income £000	Recognised in equity £000	At 31 December 2020 £000
Property, plant and equipment	(5,037)	943	-	(4,094)
Provisions and accruals	95	158	-	253
Retirement benefit schemes:				
Surpluses	(8,819)	(235)	(3,828)	(12,882)
Additional contributions	-	-	2,174	2,174
Financial instruments	185	-	(583)	(398)
	<u>(13,576)</u>	<u>866</u>	<u>(2,237)</u>	<u>(14,947)</u>

The Government announced in 2021 that from 1 April 2023 the UK corporation tax rate would increase from 19% to 25%. The deferred tax liability at each Balance Sheet date has been calculated at the tax rates, enacted at that date, expected to apply to the temporary differences when they reverse. The resulting tax rate adjustment has been partly recorded in the Income Statement and partly in the Statement of Comprehensive Income.

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**Notes to the Financial Statements**

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**16. Inventories**

	<b>2021</b>	<b>2020</b>
	<b>£000</b>	<b>£000</b>
Work in progress (goods to be sold)	<b>33,736</b>	33,440
	<u><b>33,736</b></u>	<u>33,440</u>

**17. Trade, other and contract receivables**

	<b>2021</b>	<b>2020</b>
	<b>£000</b>	<b>£000</b>
<b>Current</b>		
Trade debtors	<b>10,244</b>	3,684
Amounts owed by BAE Systems plc and its subsidiaries	<b>126,387</b>	188,910
Other debtors	<b>2,140</b>	4,545
Prepayments	<b>2,622</b>	2,898
Contract receivables	<b>57,409</b>	27,572
	<u><b>198,802</b></u>	<u>227,609</u>

Amounts owed by BAE Systems plc and its subsidiaries are payable on demand and are expected to be settled in the Company's usual operating cycle of 12 months or less. No interest is applied to amounts owed.

**Notes to the Financial Statements**

**18. Trade and other payables**

	<b>2021</b>	<b>2020</b>
	<b>£000</b>	<b>£000</b>
<b>Current</b>		
Contract liabilities	<b>137,196</b>	123,200
Trade creditors	<b>9,101</b>	13,833
Amounts owed to BAE Systems plc and its subsidiaries	<b>82,545</b>	121,174
Other taxation and social security	<b>24,738</b>	28,317
Accruals	<b>26,943</b>	27,944
	<b>280,523</b>	314,468

Amounts owed to BAE Systems plc and its subsidiaries are payable on demand and are expected to be settled in the Company's usual operating cycle of 12 months or less. No interest is applied to amounts owed. During the period, as part of the BAE Systems Group intercompany simplification project, the Royal Ordnance BV intercompany loan was settled.

**19. Financial instruments**

	<b>2021</b>	<b>2020</b>
	<b>£000</b>	<b>£000</b>
<b>Financial assets</b>		
<b>Non-current</b>		
Cash flow hedges – foreign exchange contracts	<b>1</b>	686
<b>Current</b>		
Cash flow hedges – foreign exchange contracts	<b>863</b>	2,769
<b>Financial liabilities</b>		
<b>Non-current</b>		
Cash flow hedges – foreign exchange contracts	<b>(14)</b>	(338)
<b>Current</b>		
Cash flow hedges – foreign exchange contracts	<b>(3,002)</b>	(1,026)

## Notes to the Financial Statements

### 20. Leases

The Company leases land, buildings, vehicles and equipment under non-cancellable lease arrangements. There are no terms that represent unusual arrangements or create material onerous or beneficial rights or obligations.

	31 December 2021		
	Land and buildings £000	Plant and machinery £000	Total £000
Additions during the year	-	285	285
Depreciation expense for the year	6,124	240	6,364
Net book value	88,606	428	89,034
	31 December 2020		
	Land and buildings £000	Plant and machinery £000	Total £000
Additions during the year	-	185	185
Depreciation expense for the year	6,148	204	6,352
Net book value	94,748	296	95,044



**Notes to the Financial Statements**

**20. Leases (continued)**

**Lease liabilities**

A maturity analysis of the future undiscounted lease payments in respect of the Company's lease liabilities is presented in the table below.

	<b>2021</b>	<b>2020</b>
	<b>£000</b>	<b>£000</b>
Payments due:		
Within one year	<b>7,189</b>	6,992
Between one and five years	<b>29,960</b>	29,125
Later than five years	<b>79,740</b>	87,457
	<b>116,889</b>	123,574
Reconciliation to Balance Sheet:		
Undiscounted lease liability	<b>116,889</b>	123,574
Impact of discounting	<b>(22,068)</b>	(24,845)
Total discounted lease liability	<b>94,821</b>	98,729

The total cash outflow for leases recognised on the Balance Sheet in the year ended 31 December 2021, amounted to £7,050k (2020: 6,819k).

**Amounts recognised in the Income Statement**

	<b>2021</b>	<b>2020</b>
	<b>£000</b>	<b>£000</b>
<b>Included in operating costs:</b>		
Depreciation on right-of-use assets	<b>6,364</b>	6,352
	<b>6,364</b>	6,352
<b>Included in net finance costs:</b>		
Interest expense on lease liabilities	<b>2,787</b>	2,909
	<b>2,787</b>	2,909

## Notes to the Financial Statements

### 21. Provisions

	Warranties and after- sales service £000	Contract loss £000	Total £000
Non-current	1,954	-	1,954
Current	3,154	73	3,227
At 1 January 2021	5,108	73	5,181
Released	(1,368)	(1,853)	(3,221)
Created	447	5,403	5,850
Utilised in year	(1,214)	(2,497)	(3,711)
At 31 December 2021	<b>2,973</b>	<b>1,126</b>	<b>4,099</b>
<b>Represented by:</b>			
Non-current	978	130	1,108
Current	1,995	996	2,991
	<b>2,973</b>	<b>1,126</b>	<b>4,099</b>

#### Warranties and after-sales service

Warranty and after-sales service costs are generally incurred within three years post-delivery. Whilst actual events could result in potentially significant differences to the quantum, but not the timing, of the outflows in relation to the provisions, management has reflected current knowledge in assessing the provision levels.

#### Contract loss

Reflecting the inherent uncertainty within many legal proceedings, the amount of the outflows could differ significantly from the amount provided and the timing of the outflows cannot be reliably estimated.

## Notes to the Financial Statements

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### 22. Retirement benefit obligations

#### Background

BAE Systems plc operates pension schemes for qualifying employees in the UK, US and other countries. The principal schemes in the UK are funded defined benefit schemes and the assets are held in separate trustee-administered funds. The allocation of each Company's share of the pension deficit is based on the relative payroll contributions of active members, as outlined on page 25.

At 31 December 2021, the weighted average durations of the UK defined benefit pension obligations were 17 years (2020 18 years).

The Company participates in the following BAE Systems plc schemes: BAE Systems Pension Scheme (Main Scheme) and Royal Ordnance Pension Scheme.

The split of the defined benefit pension liability on a funding basis between active, deferred and pensioner members for the most significant schemes (based on the size of the closing net deficit/surplus) is set out below:

	Active %	Deferred %	Pensioner %
Main Scheme (merged) <sup>1</sup>	31	21	48
Royal Ordnance Pension Scheme <sup>2</sup>	13	19	68

1. Source: 31 October 2019 actuarial valuation reports.

2. Source: Royal Ordnance Pension Scheme actuarial valuation 31 March 2020.

#### Regulatory framework

The funded UK schemes are registered and subject to the statutory scheme-specific funding requirements outlined in UK legislation, including the payment of levies to the Pension Protection Fund as set out in the Pension Act 2004. These schemes were established under trust and the responsibility for their governance lies jointly with the trustees and BAE Systems plc.

#### Benefits

The UK defined benefit schemes provide benefits to members in the form of a set level of pension payable for life based on members' final salaries. The benefits attract inflation-related increases both in deferment and payment. All UK defined benefit schemes are closed to new entrants, with benefits for new employees being provided through a defined contribution scheme. The Normal Retirement Age for active members of the Main Scheme is 65. Specific benefits applicable to members differ between schemes. Further details on the benefits provided by each scheme are provided on the BAE Systems Pensions website: [www.baesystemspensions.com](http://www.baesystemspensions.com).

A UK High Court judgment was delivered on 26 October 2018 concerning gender equalisation for the effect of Guaranteed Minimum Pensions (GMPs) for occupational pension schemes. A further UK High Court judgment was delivered on 20 November 2020 which rules that past cash-equivalent transfer values needed to account for gender equalisation for the effect of GMPs. In 2018 and 2020, a non-recurring past service cost was included in the income statement to reflect the expectation that the impact of GMP equalisation would increase the pension deficit in the balance sheet. In 2021, an allowance was included within the pension deficit which is a consistent proportion of the UK liabilities as applied in prior years and reflects the updated UK IAS 19 valuations as at 31 December 2021.

## Notes to the Financial Statements

### 22. Retirement benefit obligations (continued)

#### Funding

##### Introduction

Disclosures in respect of pension funding provided below reflect the pension schemes as a whole. Disclosures in respect of pension accounting under IAS 19 are provided on pages 53 - 58.

The majority of the UK defined benefit pension schemes are funded by BAE Systems plc's subsidiaries and equity accounted investments. The individual pension schemes' funding requirements are based on actuarial measurement frameworks set out in their funding policies.

For funding valuation purposes, pension scheme assets are included at market value at the valuation date, whilst the liabilities are measured on an actuarial funding basis using the projected unit credit method and discounted to their present value based on prudent assumptions set by the trustees following consultation with scheme actuaries.

The funding valuations are performed by professional qualified independent actuaries and include assumptions which differ from the actuarial assumptions used for IAS 19 accounting purposes shown on page 53. The purpose of the funding valuations is to design funding plans which ensure that the schemes have sufficient funds available to meet future benefit payments.

##### Valuations

Funding valuations of the UK defined benefit schemes are performed every three years. Following the merger of several of the UK pension schemes in October 2019, BAE Systems plc and the trustees agreed to carry out an early triennial funding valuation for the Main Scheme as at 31 October 2019.

The results of the most recent triennial valuations are shown below. These valuations and, where necessary, deficit recovery plans were agreed with the trustees and certified by the scheme actuaries after consultation with The Pensions Regulator in the UK.

	Main Scheme as at 31 October 2019 £bn	Other schemes as at 31 March 2020 £bn
Market value of assets	20.6	2.1
Present value of liabilities	(22.5)	(2.0)
Funding (deficit)/surplus	(1.9)	0.1
Percentage of accrued benefits covered by the assets at the valuation date	92%	105%

The valuations in 2019 and 2020 were determined using the following mortality assumptions:

Life expectancy of a male currently aged 65 (years)	86 – 89
Life expectancy of a female currently aged 65 (years)	87 – 91
Life expectancy of a male currently aged 45 (years)	87 – 91
Life expectancy of a female currently aged 45 (years)	89 – 92

## **Notes to the Financial Statements**

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### **22. Retirement benefit obligations (continued)**

The discount rate assumptions used in the 2019 and 2020 valuations were directly based on prudent levels of expected returns for the assets held by the schemes, reflecting the planned investment strategies and maturity profiles of each scheme. The discount rates are curves which provide a different rate for each year into the future.

The inflation assumptions were derived using data from the Bank of England which is based on the difference between the yields on index-linked and fixed interest long-term government bonds. The inflation assumption is a curve which provides a different rate for each year into the future.

The funding valuations resulted in a significantly lower deficit than under IAS 19, largely due to lower liabilities reflecting the higher discount rate assumption. Under IAS 19, the discount rate for accounting purposes is based on third-party AA corporate bond yields whereas, for funding valuation purposes, the discount rate is based on a prudent level of expected returns from the broader and mixed types of investments reflected in the schemes' investment strategies, which are expected overall to yield higher returns than bonds.

The 2019 funding agreement is underpinned by a contingency plan, which includes a commitment by BAE Systems plc to a further £50m of deficit funding in each of 2021 and 2022 into the Main Scheme prior to the next triennial valuation in the event that the scheme funding level were to fall below pre-determined parameters. In addition, BAE Systems plc would be required to pay £187m in respect of the Main Scheme if the funding level were to fall significantly and were to remain at or below those levels for nine months.

There have been no changes to the contributions or benefits, as set out in the rules of the schemes, for pension scheme members as a result of the new funding valuations.

The results of future triennial valuations and associated funding requirements will be impacted by a number of factors, including the future performance of investment markets and anticipated members' longevity.

#### **Contributions**

Under the terms of the trust deeds of the UK schemes, BAE Systems plc is required to have a funding plan determined at the conclusion of the triennial funding valuations.

The total Company contributions made to the defined benefit schemes in the year ended 31 December 2021 were £7,100k (2020 £24,400k).

## Notes to the Financial Statements

### 22. Retirement benefit obligations (continued)

#### Risk management

The defined benefit pension schemes expose the Company to actuarial risks, including market(investment) risk, interest rate risk, inflation risk and longevity risk.

Risk	Mitigation
<b>Market (investment) risk</b> Asset returns may not move in line with the liabilities and may be subject to volatility.	<p>The investment portfolios are highly diversified, investing in a wide range of assets, in order to reduce the exposure of the total portfolio to a materially adverse impact from a single security or type of security. To reduce volatility, certain assets are held in a matching portfolio, which largely consists of index-linked bonds, gilts and swaps, designed to mirror movements in corresponding liabilities.</p> <p>Some 29% (2020 22%) of the UK pension scheme assets are held in equities and pooled investment vehicles due to the higher expected level of return over the long term.</p> <p>Some of the pension schemes use derivative financial instruments as part of their investment strategy to manage the level of market risk. The Main Scheme has an equity option strategy protecting £2.9bn of assets against a significant fall in equity markets, in line with the prior year. The strategy also caps the upside if equity markets increase more than an agreed percentage.</p>
<b>Interest rate risk</b> Liabilities are sensitive to movements in interest rates, with lower interest rates leading to an increase in the valuation of liabilities.	<p>In addition to investing in bonds as part of the matching portfolio, the UK schemes invest in interest rate swaps to reduce the exposure to movements in interest rates. The swaps are held with several banks to reduce counterparty risk. The current level of interest rate protection is expressed as a hedge ratio of 79.0% (2020 72.4%).</p> <p>The discount rate assumptions set as part of the UK funding valuations directly reflect the expected returns on assets held by the schemes and provide a natural hedge against interest rate risk. The planned investment strategy, which is reflected in the discount rate and liability calculation, is for the schemes to increase their investments in bonds or other assets which match the liabilities as the schemes mature. Under the UK funding valuations, the Company expects the schemes to be fully hedged against interest rate movements following a five-year transition period to the planned investment strategy.</p>
<b>Inflation risk</b> Liabilities are sensitive to movements in inflation, with higher inflation leading to an increase in the valuation of liabilities.	<p>In addition to investing in index-linked bonds as part of the matching portfolio, the principal UK schemes invest in long-term inflation swaps to reduce the exposure to movements in inflation. The swaps are held with several banks to reduce counterparty risk. The current level of inflation protection is expressed as a hedge ratio of 107.8% (2020 100.2%).</p> <p>The UK funding valuations provide a natural hedge against inflation movements within the discount rate. The Company is already fully hedged against inflation movements and, under the planned investment strategy, aims to maintain a fully hedged position.</p> <p>In 2014, the Main Scheme implemented a pension increase exchange to allow retired members to elect for a higher current pension in exchange for foregoing certain rights to future pension increases.</p>
<b>Longevity risk</b> Liabilities are sensitive to life expectancy, with increases in life expectancies leading to an increase in the valuation of liabilities.	<p>Longevity adjustment factors are used in the majority of the UK pension schemes in order to adjust the pension benefits payable so as to share the cost of people living longer with employees.</p> <p>In 2013, with the agreement of BAE Systems plc, the trustees of the 2000 Plan, Royal Ordnance Pension Scheme and Shipbuilding Industries Pension Scheme (SIPS) entered into arrangements with Legal &amp; General to insure against longevity risk for the current pensioner population, covering a total of £4.4bn of pension scheme liabilities. These arrangements reduce the funding volatility relating to increasing life expectancy. This longevity risk cover with Legal &amp; General remains in place following the merger of the 2000 Plan and SIPS into the Main Scheme.</p>

## Notes to the Financial Statements

### 22. Retirement benefit obligations (continued)

#### IAS 19 Accounting

The disclosures below relate to pension schemes in the UK which are accounted for as defined benefit schemes in accordance with IAS 19.

#### Principal actuarial assumptions

The assumptions used are estimates chosen from a range of possible actuarial assumptions which, due to the long-term nature of the obligation covered, may not necessarily occur in practice.

	2021	2020	2019
<b>Financial assumptions</b>			
Discount rate – past service (%)	1.9	1.4	2.1
Discount rate – future service (%)	1.9	1.6	2.2
Retail Prices Index (RPI) inflation (%)	3.1	2.7	2.8
Rate of increase in salaries (%)	3.1	2.7	2.8
Rate of increase in deferred pensions (%)	2.4/3.1	2.0/2.7	2.0/2.8
Rate of increase in pensions in payment (%)	1.7 – 3.7	1.6 – 3.6	1.5 – 3.6
<b>Demographic assumptions</b>			
Life expectancy of a male currently aged 65 (years)	86 – 89	86 – 88	87 – 88
Life expectancy of a female currently aged 65 (years)	88 – 90	88 – 90	88 – 90
Life expectancy of a male currently aged 45 (years)	86 – 90	87 – 89	88 – 89
Life expectancy of a female currently aged 45 (years)	89 – 91	89 – 91	89 – 91

#### Discount rate

The discount rate assumptions are derived through discounting the projected benefit payments of the principal schemes using a third-party AA corporate bond yield curve to produce a single equivalent discount rate. This inherently captures the maturity profile of the expected benefit payments. The discount rate used for future service differs from that used for past service as it only uses the cash flows relating to active members, which have a different duration. Further information on the duration of the schemes is detailed on page 49.

#### Retail Prices Index (RPI) and Consumer Prices Index (CPI) inflation

The inflation assumptions are derived by reference to the difference between the yields on index-linked and fixed-interest long-term government bonds, or advice from the local actuary depending on the available information. Index-linked government bonds contain a premium that investors are willing to pay to mitigate the risk that RPI inflation is higher than expected. To account for this, the RPI assumption includes an inflation risk premium deduction.

As a consequence of RPI reform announcements the Company has reviewed its approach to setting inflation assumptions. The inflation risk premium deduction has been set at 0.55% per annum (2020 0.5%) and the CPI assumption has been set at 0.7% per annum (2020 0.7%) lower than RPI. The resulting RPI assumption is 3.1% per annum and the CPI assumption is 2.4% per annum. The 0.7% per annum RPI-CPI differential is a weighted average of a 1% per annum differential pre-2030 and 0.1% per annum differential post-2030; this reflects the anticipated change to the RPI index from 2030.

#### Rate of increase in salaries

The rate of increase in salaries for the UK schemes is assumed to be RPI inflation of 3.1% (2020 2.7%), plus a promotional scale.

## Notes to the Financial Statements

### 22. Retirement benefit obligations (continued)

#### *Rate of increase in deferred pensions*

The rate of increase in deferred pensions for the UK schemes is based on CPI inflation of 2.4% (2020 CPI inflation of 2.0%), with the exception of the legacy 2000 Plan, which is based on RPI inflation of 3.1% (2020 RPI inflation of 2.7%). For all UK schemes, the rate of increase in deferred pensions is subject to inflation caps.

#### *Rate of increase in pensions in payment*

The rate of increase in pensions in payment differs between UK schemes. Different tranches of the schemes increase at rates based on either RPI or CPI inflation, and some are subject to an inflation cap. With the exception of two smaller schemes, the rate of increase in pensions in payment is based on RPI inflation.

#### *Life expectancy*

The Company has used the Self-Administered Pension Schemes S3 mortality tables based on year of birth (as published by the Institute of Actuaries) for both pensioner and non-pensioner members in conjunction with the results of an investigation into the actual mortality experience of scheme members and information on the demographic profile of the scheme's membership.

In addition, to allow for future improvements in longevity, the Continuous Mortality Investigation 2020 tables (published by the Institute of Actuaries) have been used (in 2020, the Continuous Mortality Investigation 2019 tables were used), with an assumed long-term rate of future annual mortality improvements of 1.0% per annum (2020 1.0%), an initial rate adjustment parameter ('A') of 0.25% (2020 0.25%) in conjunction with a smoothing parameter ('S<sub>k</sub>') of 7 for all members (2020 7). The Group has chosen to apply a weighting to the 2020 data in recognition of the abnormal excess deaths as a result of COVID-19. No further adjustments have been made to improvements expected in future years. The impacts of COVID-19 will continue to be monitored and assessed at future reporting dates.

The disclosures below are in respect of the Company's share of the IAS 19 deficit using the allocation methodology outlined on page 25.

#### **Summary of movements in retirement benefit obligations**

	£'000
Company's share of IAS 19 deficit at 1 January 2021	67,800
Actual return on assets excluding amounts included in interest expense/income	800
Decrease in liabilities due to changes in assumptions and experience	54,900
Contributions in excess of service cost	400
Past service cost – plan amendments	-
Net interest income	900
<b>Company's share of IAS 19 deficit at 31 December 2021</b>	<b>124,800</b>



Notes to the Financial Statements

22. Retirement benefit obligations (continued)

**Amounts recognised in the Balance Sheet**

	2021 £'000	2020 £'000
Present value of unfunded obligations	(1,044,500)	(1,128,600)
Fair value of scheme assets	1,169,300	1,196,400
<b>Company's share of IAS 19 deficit, net</b>	<b>124,800</b>	<b>67,800</b>
Represented by:		
Retirement benefit surpluses	150,200	124,000
Retirement benefit obligations	(25,400)	(56,200)
	<b>124,800</b>	<b>67,800</b>

**Changes in the fair value of scheme assets**

	£'000
Company's share of the value of scheme assets at 1 January 2020	1,118,900
Interest income	22,600
Actual return on assets excluding amounts included in interest income	79,300
Actual return on assets	101,900
Contributions by employer	23,000
Contributions by employer in respect of employee salary sacrifice arrangements	1,400
Total contributions by employer	24,400
Members' contributions	200
Administrative expenses	(900)
Benefits paid	(48,100)
Company's share of the value of scheme assets at 31 December 2020	1,196,400
Interest income	15,800
Actual return on assets excluding amounts included in interest income <sup>1</sup>	800
Actual return on assets	16,600
Contributions by employer	5,800
Contributions by employer in respect of employee salary sacrifice arrangements	1,300
Total contributions by employer	7,100
Members' contributions	100
Administrative expenses	(900)
Benefits paid	(50,000)
<b>Company's share of the value of scheme assets at 31 December 2021</b>	<b>1,169,300</b>

## Notes to the Financial Statements

### 22. Retirement benefit obligations (continued)

#### *Assets of defined benefit pension schemes*

	2021			2020		
	Quoted £'000	Unquoted £'000	Total £'000	Quoted £'000	Unquoted £'000	Total £'000
Equities:						
UK	15,000	-	15,000	14,000	-	14,000
Overseas	94,300	-	94,300	37,200	-	37,200
Pooled investment vehicles <sup>1</sup>	3,100	232,400	235,500	11,100	197,500	208,600
Fixed interest securities:						
UK gilts	288,100	-	288,100	370,400	-	370,400
UK corporates	218,700	38,900	257,600	278,500	41,800	320,300
Overseas government	800	-	800	700	-	700
Overseas corporates	90,900	600	91,500	98,500	-	98,500
Index-linked securities:						
UK gilts	406,100	-	406,100	382,800	6,000	388,800
UK corporates	-	15,100	15,100	-	13,600	13,600
Property <sup>2</sup>	-	24,200	24,200	-	27,200	27,200
Derivatives <sup>3</sup>	-	(328,100)	(328,100)	-	(326,500)	(326,500)
Cash:						
Sterling	13,900	46,200	60,100	13,600	17,100	30,700
Foreign currency	200	2,100	2,300	300	3,300	3,600
Other	400	6,400	6,800	-	9,300	9,300
<b>Company total</b>	<b>1,131,500</b>	<b>37,800</b>	<b>1,169,300</b>	<b>1,207,100</b>	<b>(10,700)</b>	<b>1,196,400</b>

1. Primarily invested in private markets and exchange traded funds. The amounts classified as unquoted primarily comprise investments in private markets, with the majority held in infrastructure, alternatives and direct funds, valued in accordance with International Private Equity and Venture Capital Valuation Guidelines.

2. Valued on the basis of open market value at the end of the year determined in accordance with the Royal Institution of Chartered Surveyors' Appraisal and Valuation Standards and the Practice Note contained therein.

3. Includes equity protection options, forward foreign exchange contracts, futures, and interest rate, inflation and longevity swaps. The valuations are based on valuation techniques using underlying market data and discounted cash flows.

#### **Longevity swap**

The Company holds longevity insurance contracts for some of its UK defined benefit pension schemes. These provide long-term protection and income to the underlying pension scheme in the event that insured members live longer than expected.

The value of the longevity insurance contracts held by the Company are calculated by an actuary. At a high level, they are measured by discounting the difference between the projected fixed and floating cash flows payable under the contracts, excluding the value of future projected fees. The significant assumptions used for this valuation are the discount rate and mortality assumptions; fair values for these assumptions are advised by an actuary based on external data and characteristics of the insured member population.

As at 31 December 2021, the longevity swap valuation leads to a negative adjustment to the assets which reflects that experience to date on the contracts has been higher than expected deaths.

## Notes to the Financial Statements

### 22. Retirement benefit obligations (continued)

#### *Changes in the present value of the defined benefit obligations*

	£'000
Company's share of the defined benefit obligations at 1 January 2020	(1,067,400)
Current service cost	(4,300)
Contributions by employer in respect of employee salary sacrifice arrangements	(1,400)
Total current service cost	(5,700)
Members' contributions	(200)
Past service cost – plan amendments	(300)
Actuarial loss due to changes in assumptions and experience	(81,500)
Interest expense	(21,600)
Benefits paid	48,100
Company's share of the defined benefit obligations at 31 December 2020	(1,128,600)
Current service cost	(4,500)
Contributions by employer in respect of employee salary sacrifice arrangements	(1,300)
Total current service cost	(5,800)
Members' contributions	(100)
Past service cost – plan amendments	-
Actuarial gain due to changes in assumptions and experience	54,900
Interest expense	(14,900)
Benefits paid	50,000
<b>Company's share of the defined benefit obligations at 31 December 2021</b>	<b>(1,044,500)</b>

#### *Amounts recognised in the Income Statement*

	2021 £'000	2020 £'000
<b>Included in operating costs:</b>		
Current service cost	(4,500)	(4,300)
Guaranteed Minimum Pension equalisation charge	-	(300)
Administrative expenses	(900)	(900)
	<b>(5,400)</b>	<b>(5,500)</b>
<b>Included in finance costs:</b>		
Net interest income on retirement benefit obligations	900	1,000

The Company incurred a charge of £1,272k (2020 £1,163k) in relation to defined contribution schemes for employees.

#### **Sensitivity analysis**

The sensitivity information has been derived using scenario analysis from the actuarial assumptions as at 31 December 2021 and keeping all other assumptions as set out on page 53.

The pension schemes hold a number of unquoted pooled investment vehicles, which are investments in private markets. These are valued based on latest available valuation reports, and as noted on page 20, these valuations are subject to estimation uncertainty as their valuation techniques incorporate a number of assumptions, including those associated with the COVID-19 pandemic and the impact of climate change.

## Notes to the Financial Statements

### 22. Retirement benefit obligations (continued)

#### *Financial assumptions*

The estimated impact of changes in the discount rate and inflation assumptions on the defined benefit pension obligation, together with the estimated impact on scheme assets after allocation to other participating employers, is shown in the table below. The estimated impact on scheme assets takes into account the risk management activities in respect of interest rate and inflation risk. The sensitivity analysis on the defined benefit obligation is measured on an IAS 19 accounting basis and, therefore, does not reflect the natural hedging in the discount rate used for funding valuation purposes.

	(Increase)/ decrease in pension obligation £'000	Increase/ (decrease) in scheme assets £'000
<b>Discount rate:</b>		
0.1 percentage point increase	15,000	(16,000)
0.1 percentage point decrease	(15,000)	16,000
0.5 percentage point increase	72,000	(80,000)
0.5 percentage point decrease	(81,000)	82,000
<b>Inflation:</b>		
0.1 percentage point increase	(15,000)	12,000
0.1 percentage point decrease	15,000	(12,000)
0.5 percentage point increase	(55,000)	62,000
0.5 percentage point decrease	52,000	(61,000)
1.0 percentage point increase	(112,000)	126,000
1.0 percentage point decrease	99,000	(120,000)

#### *Demographic assumptions*

Changes in the life expectancy assumption, including the benefit of longevity swap arrangements, would have the following effect on the net IAS 19 deficit:

	(Increase)/ decrease in net deficit £'000
<b>Life expectancy:</b>	
One-year increase	(32,000)
One-year decrease	32,000

## Notes to the Financial Statements

### 23. Share capital and other reserves

#### Share capital

	25p Ordinary shares	Nominal value £000
<b>Issued and fully paid</b>		
At 1 January 2020, 31 December 2020 and 31 December 2021	200,000,000	50,000

#### Other reserves

	Hedging reserve £000
<b>At 1 January 2020</b>	(1,229)
Amounts credited to hedging reserve	3,182
Tax on other comprehensive income	(583)
<b>At 31 December 2020</b>	1,370
Amounts debited to hedging reserve	(4,243)
Tax on other comprehensive loss	936
<b>At 31 December 2021</b>	(1,937)

#### *Hedging reserve*

The hedging reserve comprises the effective portion of the cumulative net change in the fair value of cash flow hedging instruments related to hedged transactions that have not yet occurred.

## Notes to the Financial Statements

### 24. Dividends

	2021 £000	2020 £000
Dividends paid in respect of prior year	20,000	20,000
	<u>20,000</u>	<u>20,000</u>

The directors are proposing a final dividend of £20,000k (2020: £20,000k), totalling £0.10 per share (2020: £0.10).

This dividend has not been accrued in the balance sheet.

### 25. Related party transactions

	2021 Sales £000	2021 Debtors £000	2020 Sales £000	2020 Debtors £000
CTAI	440	170	322	45
MBDA	6,158	125	5,224	5
Rheinmetall BAE Systems Land Limited	-	106	906	731
	<u>6,598</u>	<u>401</u>	<u>6,452</u>	<u>781</u>

### 26. Events after the reporting period

Since the Balance Sheet date, several countries in which we operate have announced or are making plans to increase spending to counter the elevated and evolving threat environment on multiple fronts. This has been determined to be a non-adjusting post balance sheet event. It is not currently possible for the Company to estimate the potential future financial impact of such changes.

Since the Balance Sheet date, there has been an increase globally in supply chain and inflationary pressures for businesses. This has been determined to be a non-adjusting post balance sheet event. Owing to the uncertainty around supply chain and inflationary pressures, we have included this as a principal risk in this report. The Company is currently mitigating the major financial impacts of this issues and seeks to continue to do so.

**Notes to the Financial Statements**

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**27. Controlling parties**

The immediate parent company is BAE Systems (Holdings) Limited and the ultimate parent company and controlling party is BAE Systems plc, which is both the smallest and largest parent company preparing group financial statements. Both companies are incorporated in the United Kingdom and registered in England and Wales.

The consolidated financial statements of BAE Systems plc are available to the public and may be obtained from its registered address:

6 Carlton Gardens  
London  
SW1Y 5AD  
Website: [www.baesystems.com](http://www.baesystems.com)