Company No. 2081330

CAPITA

(SC199444)

ANNUAL REPORT 2017

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CONTENTS

STRATEGIC REPORT	03
Summary	01
Summary divisional performance	02
Chairman's introduction	04
Chief Executive Officer's review	06
Our strategy and business model	13
Key performance indicators	14
Chief Financial Officer's review	15
Our people and talent	23
Divisional performance	25
Internal control and risk management	36
Viability statement	44
Managing our business responsibly	45

CORPORATE GOVERNANCE	49
Chairman's report	50
Board members	52
Corporate governance statement	54
Committees	64
Directors' remuneration report	75

FINANCIAL STATEMENTS	90
Consolidated financial statements	91
Notes to the consolidated financial statements	96
Independent Auditor's report to the members of Capita plc	170
Company financial statements	185
Notes to the Company financial statements	187
Shareholder information	201
Alternative Performance Measures	202

IMAGE REMOVED

For more information visit
capita.com/year-in-review

we are
change
makers

In May 2017, we launched a new corporate marketing campaign called 'Change Makers' targeting a c-suite audience. The objectives of the campaign were to raise awareness of how we unlock value for our clients through talent and technology, as well as instilling pride within our employees. This is the first campaign of its kind that we have embarked upon. It was time to shine.

IMAGE REMOVED

How we use mountains of data to help a UK retailer reach new heights.

IMAGE REMOVED

Putting ŠKODA customers in the driving seat without leaving their armchairs.

IMAGE REMOVED

Making a difference to children, young people and schools in Staffordshire.

SUMMARY

We solve the complex challenges of our clients, increasing productivity, enhancing their use of technology and data, improving customer and public services and adding value to the UK and local economies. We do this by combining our talent, creativity, software, technology and innovation with sector knowledge and proven skills and expertise underpinned by our scaled operational platforms.

REPORTED SUMMARY[1]

REVENUE	LOSS BEFORE TAX	FREE CASH FLOW	EARNINGS PER SHARE
£4,234.6m	£(513.1)m	£37.7m	(80.1)p
2016: £4,368.6m	2016: £(89.8)m	2016: £367.3m	2016: (14.3)p

UNDERLYING SUMMARY[1]

REVENUE	PROFIT BEFORE TAX	FREE CASH FLOW	EARNINGS PER SHARE
£4,167.9m	£383.0m	£38.0m	45.6p
2016: £4,357.3m	2016: £268.5m	2016: £397.3m	2016: 31.7p

IMAGE REMOVED

IMAGE REMOVED

IMAGE REMOVED

IMAGE REMOVED

FOR MORE ABOUT KEY PERFORMANCE INDICATORS, SEE PAGE 14
FOR MORE ABOUT FINANCIAL HIGHLIGHTS, SEE PAGES 15–22

1 Continuing operations.
2 Refer to note 7 of the consolidated financial statements for order book definition.

SUMMARY DIVISIONAL PERFORMANCE

We currently report across five divisions with leading market positions, delivering innovative solutions for clients across the public and private sectors.

IMAGE REMOVED

PRIVATE SECTOR PARTNERSHIPS

Underlying revenue

£1,588.3m

2016: £1,544.4m

Underlying operating profit

£137.5m

2016: £71.4m

Customer management, Capita Europe, life, pensions, insura nce and employee solutions.

PUBLIC SERVICES PARTNERSHIPS

Underlying revenue

£1,087.2m

2016: £1,127.9m

Underlying operating profit

£73.0m

2016: £0.5m

Central and local public services and contracts, real estate property and infrastructure.

IMAGE REMOVED

PROFESSIONAL SERVICES

Underlying revenue

£532.8m

2016: £758.3m

Underlying operating profit

£104.9m

2016: £108.3m

HR, corporate and specialist services and commercialised public sector assets and joint ventures.

DIGITAL AND SOFTWARE SOLUTIONS

Underlying revenue

£410.9m

2016: £420.3m

Underlying operating profit

£113.9m

2016: £134.4m

Application software and solutions across public sector, utilities and financial services.

IMAGE REMOVED

IT SERVICES

Underlying revenue

£507.8m

2016: £481.5m

Underlying operating profit

£78.1m

2016: £47.1m

IT infrastructure, applications solutions and consulting services.

FOR MORE ABOUT DIVISIONAL PERFORMANCE, SEE PAGES 25–35

STRATEGIC REPORT

Summary	01	Chief Financial Officer's review	15
Summary divisional performance	02	Our people and talent	23
Chairman's introduction	04	Divisional performance	25
Chief Executive Officer's review	06	Internal control and risk management	36
Our strategy and business model	13	Viability statement	44
Key performance indicators	14	Managing our business responsibly	45

DRIVING VALUE

HOW WE USE MOUNTAINS OF DATA TO HELP A UK RETAILER REACH NEW HEIGHTS.

IMAGE REMOVED

we are change makers

FOR MORE ABOUT OUR CHANGE MAKERS, SEE CAPITA.COM/YEAR-IN-REVIEW

CHAIRMAN'S INTRODUCTION

IMAGE REMOVED

"2017 has been a difficult year of unprecedented change for Capita. Against a challenging backdrop in many of our markets, we began to address the underlying problems preventing Capita and its people from achieving their full potential. We have strengthened our leadership and governance, undertaken a strategic review and have launched a fully underwritten Rights Issue to position Capita well for the future."

SIR IAN POWELL, CHAIRMAN

It is apparent that Capita remains a systemically important business to the UK, with important services and strong market positions. Every day, our committed and talented people continue to fulfil our core mission – improving the efficiency and productivity of our clients. However, over the years, the business has become too complex, expanded beyond its core skills and failed to keep pace with a rapidly changing marketplace.

Shortly after I took up the Chair position on 1 January last year, it became apparent that there were three critical areas requiring immediate attention – Leadership, Strategy and Governance – each of which we as a Board have either addressed or are in the process of addressing.

LEADERSHIP

A critical first step was to steer the Company in a new direction under fresh leadership. We announced in early March 2017 that Andy Parker would stand down as Chief Executive Officer (CEO) later in the year, formally leaving Capita on 15 September 2017. At which time, Nick Greatorex, Chief Financial Officer (CFO), became Interim CEO until 30 November. Following a thorough executive search process, we welcomed Dr Jonathan (Jon) Lewis as our new CEO on 1 December 2017.

With his extensive technology background and strong track record in turnaround situations, Jon brings the skills, experience and energy required to lead Capita on its new course. He joined from Amec Foster Wheeler plc, where he served as CEO following an impressive career with Halliburton in the US. Jon has the credibility, knowledge, values and behaviours required to lead the transformation of this significant UK services business, accountable not just to our clients, investors and people but also to the wider community.

STRATEGY

Capita has lacked a clear strategy and operated with a short-term focus. This focus has resulted in short-term decisions to pursue near-term growth and in-year profitability at the expense of planning for long-term sustainability. Capita has taken on too many low-margin/high risk contracts and has amassed too much debt in support of acquisition-led growth. At the same time, it has under-invested in its infrastructure (especially in those functions that provide the oversight that a business of Capita's complexity requires) and as a result has made insufficient investments in financial and operational controls for a business of its scale. Crucially, a long-term strategy with aligned objectives were not in evidence when I became Chairman. Until new leadership was in place, it was inappropriate to undertake a full strategy review, however the preliminary work to facilitate such a review was put in place.

A strategic review of the business, its markets and purpose has been completed as part of the new strategy Jon is implementing. Capita's objective is to become a more focused and predictable, client-centric company, generating sustainable free cash flow. The Board believes that changes to its operating model under its new strategy will deliver enhanced performance through increased simplification, efficiency, standardisation and focus.

Given the breadth of Capita's activities and the complexity of our structure, this is necessarily an extensive exercise involving employees at all levels. The new strategy is detailed by Jon in his Chief Executive Officer's review on pages 6–12.

The changes necessary will require both cost savings and investment, a reappraisal of areas that were overlooked in the past and the implementation of a multi-year plan. To support this strategy, a fully underwritten Rights Issue has been launched to ensure Capita has the balance sheet to support its clients and operations. The proceeds of the Rights Issue will be used to support the delivery of Capita's new strategy; invest in the business and reduce indebtedness.

GOVERNANCE

We have worked to improve the Group's governance, rebalance the Board and bring it in line with current good practice. Prior to my joining the Board in September 2016, it comprised five Executive Directors and five Non-Executive Directors. Today, we have two Executive Directors – the CEO and CFO

– and six Non-Executive Directors. Whilst we will continue to review the constitution of the Board, we believe that this is a more appropriate Board structure to facilitate debate and challenge as the business undergoes its strategic transformation.

On behalf of the Board, I would like to thank Andy Parker who left on 15 September 2017 and Vic Gysin and Chris Sellers, who left in recent months – all of them having made meaningful contributions over many years of service. We also thank Paul Bowtell, who left Capita last May after seven years as a Non-Executive Director and Chair of the Audit and Risk Committee.

We are delighted to welcome Baroness Lucy Neville-Rolfe to the Board as a Non-Executive Director with effect from 6 December 2017. A backbencher in the House of Lords and former Government minister, Lucy brings extensive private and public sector experience from her time on the Boards of Tesco plc, ITV plc and Metro AG.

We are also delighted that Matthew Lester joined the Board in March 2017, taking over as Chair of the Audit and Risk Committee on 1 June. He was formerly CFO of Royal Mail plc and is a Non-Executive Director of Man Group plc and Barclays Bank plc. Finally, I would like to thank Nick Greatorex for his contribution during the year as Interim CEO.

In last year's Annual Report, I highlighted diversity as an area of both Board and wider leadership focus for the future. Ensuring that all of our people have the opportunity to fulfil their potential is an essential element of a successful organisation, both commercially and as a responsible and supportive employer. It is also the right thing to do. We have made some progress in this area in 2017 but not enough. Under our new leadership, we look forward to redoubling our diversity efforts at all levels, especially in senior leadership positions, as the transformation plan takes shape.

I am grateful to all Capita people, who have shown great resilience and commitment throughout an uncertain period. Jon, the Board and I are determined to give all our employees a sound basis for a stable and happy career within Capita, focused on delivering outstanding services to our clients and their customers.

PERFORMANCE

Market conditions remained challenging in 2017, new business wins were weak and we experienced some operational difficulties. Despite these challenging trading conditions, progress was made in a number of important areas, notably the disposal of the Capita Asset Services businesses valued at £888m to Link Group, early adoption of the new IFRS 15 revenue recognition standard, progress on a series of cost initiatives, the hiring of Jon Lewis as our new CEO and the commencement of the strategic review. We reported underlying profits before tax of £383.0m for 2017 and underlying profits before tax and before significant new contracts and restructuring costs of £400.9m, in line with our expectations for underlying trading.

Our reported operating loss for the year was £420.1m (2016: £16.1m), including a charge for specific items of £852.8m (2016: £353.5m). The significant increase in 2017 arises from the impairment of goodwill, intangible assets, and other non-current assets as at 31 December 2017. The impairment of goodwill and intangible assets amounted to £565.6m. The continued operational and external challenges faced by the Group, which became apparent following the conclusion of the 2018 business planning process, have led to a significant deterioration in new business opportunities from previous positions. In addition, the Group has experienced contract terminations and attrition as highlighted in the divisional performance reviews and the strategic review has identified areas that need to be addressed to rebuild and reposition Capita. These events and circumstances have led to the recognition of the impairment charge. Nick Greatorex will cover our detailed financial performance in his Chief Financial Officer's review on pages 15–22.

On 31 January 2018, we provided an update on the outlook for trading in 2018. In our update, we highlighted a number of headwinds, the need for investment and a transformation plan for the long-term benefit of the business, which is detailed in the Chief Executive Officer's review on pages 6–12.

BALANCE SHEET AND CAPITAL STRUCTURE

We have carried out an assessment of the appropriate financial leverage over the medium term, to provide a sustainable capital base to support our clients and operations, increase investment in the business and deliver its future strategy.

The Board has determined that the appropriate financial leverage for the Company is between 1.0x and 2.0x adjusted net debt to adjusted EBITDA prior to the adoption of IFRS 16, (compared to its existing leverage ratio of 2.27x adjusted net debt to adjusted EBITDA as at 31 December 2017), which the Board believes is the appropriate financial leverage for companies of similar size and with similar operations to Capita.

As announced on 31 January 2018, Capita intends, as a matter of good corporate responsibility, to reduce the remaining pension deficit in its defined benefit scheme. The current actuarial deficit is supported by an asset backed funding arrangement, the estimated value of which is £69m, and which is not included in the last disclosed IAS 19 deficit of £407m as at 31 December 2017. The triennial actuarial valuation of the scheme as at 31 March 2017 is due to be completed by 30 June 2018. In addition to Capita's current annual contributions, further contributions totalling £21.5m were paid in January 2018. Capita is fully committed to addressing the remainder of the deficit in the medium term.

In addition, we currently expect to achieve proceeds of approximately £300m from non-core disposals in 2018. We further intend to review the diversity of funding on our balance sheet over the next two years.

DIVIDEND

Given the short-term outlook and level of indebtedness, the Board did not recommend the payment of a final dividend in respect of 2017. However, the Board recognises the importance of regular dividend payments to investors in forming part of their total shareholder return, and will consider the payment of dividends once Capita is generating sufficient sustainable free cash flow.

THE WAY AHEAD

Capita is a key part of the UK corporate landscape, both in its own right and as the provider of essential services to businesses and public-sector institutions in every sector of the economy.

Scale has been critical to our offering. It has enabled us to achieve crucial efficiencies for our clients but it has also created its own operational difficulties that we must now address. From leadership and strategy to business mix and capital structure, we are assessing every aspect of the business.

Inevitably this is a difficult time for Capita's people, clients and shareholders. Our people are central to everything we do, and I want to thank them for their continued hard work, energy and commitment. The multi-year transformation process being led by Jon and his team will lead to a more sustainable, focused business operating with strong values to deliver great services to our clients. The Board and I are fully committed to the Rights Issue and the new strategy underpinned by the multi-year transformation plan to strengthen and simplify the business and deliver future success for the company, our employees, shareholders and clients.

CHIEF EXECUTIVE OFFICER'S REVIEW

IMAGE REMOVED

"We have the building blocks to create a great business; one that consistently delights its clients, has operational discipline and generates sustainable free cash flow. We are now executing the plan to deliver this."

JON LEWIS, CHIEF EXECUTIVE OFFICER

Introduction

I joined Capita on 1 December 2017 and have spent my first four months meeting many employees, clients, suppliers and shareholders to gain a full picture of the business and its strengths and weaknesses. There is a lot to be excited about: talented people, a blue-chip client base, great technology and the ability to deliver value-adding services but the more I have observed and learnt, the more I have realised that there is considerable work to be done to position Capita for future, sustainable success. Therefore, I have initiated a thorough review of the business, the results of which have shaped the design and implementation of our new strategy.

KEY FINDINGS OF THE STRATEGIC REVIEW

The initial focus of this review was to identify the strengths and weaknesses of the current Capita structure and operations. This has involved a systematic market-by-market review of the current attractiveness and future competitive landscape of each market, an assessment and benchmarking of Capita's capabilities and propositions, a review of internal processes and cost structure and a thorough assessment of current and potential synergies across Capita.

The key findings of this review included the following:

- Until recently, Capita's perspective was focused on short-term growth and, whilst this short-term perspective, coupled with an entrepreneurial culture, had assisted in the delivery of rapid growth in the past, it was also characterised by a lack of long-term business planning and investment in the infrastructure and resources required to support a large-scale organisation servicing increasingly complex client needs.
- This short-term sales-led approach also resulted in a failure to keep up with longer-term trends in a rapidly changing marketplace.
- Capita had become overly complex, spanning multiple markets and services, making it more challenging to maintain a competitive advantage in every business. In addition, some of Capita's offerings have featured a low level of operational, technological and commercial integration, which has led to higher costs and inefficiencies.

- This low level of current integration across divisions and their markets provides a significant opportunity to improve Capita's operating efficiency, reducing its cost base to support profit margins, and to improve operating cash flow which would be available to invest in the business.
- Investment is required across all of Capita's shared services, including its finance, IT, human resources, commercial, legal and related functions, which in some cases were inadequate and in other cases did not function effectively.
- In recent years, Capita developed a large amount of bespoke software for clients which was not scalable or reusable for other clients and would often become obsolete within a relatively short period of time. This has led to write-offs on Capita's income statement once the software had no further value to Capita. The review suggested that Capita should change its approach to software development in order to focus on reusable software tools and repeatable, scalable software.
- Effective, efficient investment in Capita's client propositions and its infrastructure is also required. A historic focus on short-term performance, and a resulting under-investment in certain key IT systems, has resulted in the current need for an increase in investment to upgrade Capita's enterprise-wide tools and software (including a more comprehensive customer relationship management (CRM) system).
- Whilst the majority of Capita's contracts have exhibited expected performance, Capita's record of successful operational delivery has been challenged recently by a number of execution issues on some of its major contracts. A common underlying issue arises from the separation, and lack of coordination, between the sales, implementation and operations teams which has led to a lack of clear accountability across contracts. Capita needs to simplify its processes and procedures to enhance the way it bids, implements and manages its contracts.
- Capita is also seeking to strengthen its balance sheet, and targeting a leverage ratio of between 1.0x and 2.0x adjusted net debt to adjusted EBITDA (prior to the adoption of IFRS 16), which can be achieved with the proceeds of the Rights Issue, the proceeds of certain non-core disposals expected later this year, and through further disposals over the next two to three years.
- Finally, it is important for Capita to develop new client offerings supporting data analytics, and to be at the forefront of business process automation in order to sharpen its competitive offering in current and future growth markets.

These initial findings have shaped and informed the design of our new strategy.

OUR NEW STRATEGY

Capita will simplify its business by focusing on key growth markets, realigning its organisational structure to mirror these markets and to significantly reduce costs at the same time as improving operational efficiency.

Capita will strengthen its businesses and capabilities by making selected investments in order to drive improvements to both Capita's expertise in digital, analytics and automation and its programme delivery and operational excellence. Capita will also ensure that it has the right leadership team and capital structure in place to support the delivery of the new strategy.

1. STRATEGY – SIMPLIFY

The markets in which Capita operates are changing quickly and new trends are emerging. The Board believes that Capita needs to be at the forefront of these changes rather than reacting to them. A key element of the new strategy is to 'do fewer things, better'. Central to this will be the simplification and reorganisation of the business portfolio to focus this on key growth markets where Capita has an established leading market presence. There will be a simplification of our operating model, reducing reinvention, being more selective on contract tendering, and dramatically reducing the cost base while at the same time strengthening our core client proposition, processes and tools.

Focus on key growth markets

Our key priorities will be to focus on the attractive, growing and profitable markets where we have an established leading market presence and offering. The Board continues to believe that Capita has a core of market-leading positions, with a portfolio of contracts with blue-chip clients that are performing well. We believe we can strengthen our client offering and grow our market positions further across the segments and markets it currently serves, including the following:

SOFTWARE

Capita is one of the UK's largest software companies and is a market leader in several specialist areas such as education, utilities, local government and police, justice, and emergency services with a 3% market share in 2017. The £15bn market is forecast to grow at an annual growth rate of 8% through 2021. Client preferences are evolving with sector specific needs, which we believe will give rise to new opportunities in specialist areas. For example, 'software as a service' providers have been gaining market share in recent years and Capita needs to adapt to this market trend. We expect to simplify our business by focusing on carefully selected specialist markets in the UK and internationally (including the market for 'software as a service'), developing reusable software tools, and building a market-aligned sales force and improved go-to-market capability. We also intend to strengthen our offering by investing in core products with distinctive offerings to defend position, and grow in existing and adjacent markets. We will create scaled, integrated shared service functions as well as a best-in-class development centre for production of standardised software. It will also invest in expanding selected products into the US market.

CHIEF EXECUTIVE OFFICER'S REVIEW CONTINUED

HR

Capita provides a full suite of HR offerings, supporting the employment life cycle from hiring to retiring for 6,500 clients across the private and public sectors. We focus on recruitment, learning and benefits, and pensions administration, supported by our proprietary digital platforms, Tesselo, Orbit and Hartlink. We also provide attraction screening, performance management and payroll services. We believe there is an opportunity to simplify this business by bringing together our current three HR offerings into one division across recruitment, learning and benefits. We will seek to create a sales culture which enables our clients to access multiple HR services within its portfolio. We have decided to merge these three existing businesses into a single division, with a new leadership team, and believe that by combining a broad capability across benefits, pensions, learning administration and recruitment outsourcing we can participate in a market valued at £5bn in 2017 (of which we have a 10% market share), and that is expected to grow at an annual growth rate of 5% through 2021. Capita is already a leading provider in most segments, such as benefits administration (where we have a 6% market share), learning process outsourcing (where we have a 21% market share) and recruitment process outsourcing (where we have a 12% market share). We will also endeavour to ensure that there are standard data extraction and management tools across all businesses. We intend to strengthen our offering by improving our core products and platforms, strengthening our analytics capability, and standardising existing solutions and technological partnerships with key ERP providers to ensure our solutions can integrate with existing client infrastructure.

CUSTOMER MANAGEMENT

Capita is a market leader in the UK with a 16% share of a £3.8bn market size as at 31 December 2017. Whilst the overall market is forecast to grow at an annual growth rate of 4% through 2021, close to double digit growth is expected in higher capability areas such as revenue support. We are using an increasingly digital and analytics-led approach that we believe will help to reinforce Capita's leadership position in transformational outsourcing and capture a greater share of those higher complexity transactions that are expected to grow fastest. Clients are increasingly seeing outsourcing as a partnership opportunity for value, rather than simply for transactional supply. As they look for new ways to improve their own customer management services, this provides new revenue opportunities for us. Capita has a leading track record in building such partnerships in the UK, and this year it is delivering the first such partnership in Germany. Capita is the second largest provider in the German and Swiss markets and expects these to offer a similar set of opportunities for transformational partnerships as the UK. We intend to exploit these opportunities by standardising best practices and service offerings for our clients, partnering with leading technology providers, and expanding our use of offshore resources in order to provide solutions cost effectively. We will also upgrade our infrastructure and tools, and continue to invest in our analytics capability to expand further into sectors such as transport and travel, financial services and automotive.

GOVERNMENT

Central government[1]: Although the opportunities for new large, long-term contracts have reduced over recent years, we believe that Capita will be able to utilise its strong market position (with 11% share of a £4bn market size)[2] and proven capabilities in particular in large-scale national operations, to focus on retenders and carefully targeted growth opportunities supported by high-performing and disciplined low-risk contract implementation. For complex deals, we intend to seek to build solutions which bring a best-in-class offering. However, unlike in the case of its software business where we provide our own proprietary software solutions, in the case of large and complex central government contracts, Capita is increasingly looking to partner with IT specialists in order to mitigate the development risks and costs of these new solutions and increase the likelihood of successful outcomes. We expect to simplify by focusing on our core capabilities (those where Capita has a distinct advantage), and will deprioritise and avoid smaller, fragmented activities. We will only pursue opportunities where commercial terms are acceptable. We intend to strengthen our business by investing in transformation capabilities, analytics and automation as well as investing in business development. In addition, following the UK's exit from the European Union there may be additional opportunities as the UK Government begins to develop new policies, require new services and establish new delivery requirements in a post-Brexit environment.

Local government: Capita is the largest provider of outsourced services across local authorities in the United Kingdom, (with 15% share of a £3bn market size[2]). We focus on the delivery of support services to local authorities, schools and health organisations, including IT and digital transformation, collecting payments from and making payments to citizens, and back-office processing. While the number of new, large deals for local authorities have been in decline in recent years, Capita believes that opportunities remain to shape the market by providing clients with a new commercial model focused on key services such as revenues and benefits, planning and regulatory affairs. Our strategic focus for local government includes developing new scalable and repeatable solutions, focusing on core capabilities while de-prioritising smaller, fragmented services, and exploiting Capita's growing capabilities in data analytics, robotics and automation. We will also focus on business development, focusing the sales team on incremental/organic growth rather than relying on larger deals with clients.

1 Central government includes health, defence and education.
2 Capita estimate based on Nelson Hall.

IT SERVICES

Capita is one of the top ten suppliers of IT services in the United Kingdom. Our IT Services business acts as a technology enabler across all of Capita's services both internally and externally. The UK IT services market is forecast to grow at an annual growth rate of 1% through 2020. Clients' needs are evolving as they seek value creation through digitisation and automation, more standardised offerings with modular add-ons and improved security. We believe that the breadth of Capita's portfolio enables it to maintain a competitive advantage across IT service provision, however it requires a simplified organisational structure, modernised offering and an optimised operating model to better serve selective external and internal clients. We need to first strengthen our capability to suit the requirements of existing clients as well as to make technology and infrastructure investments.

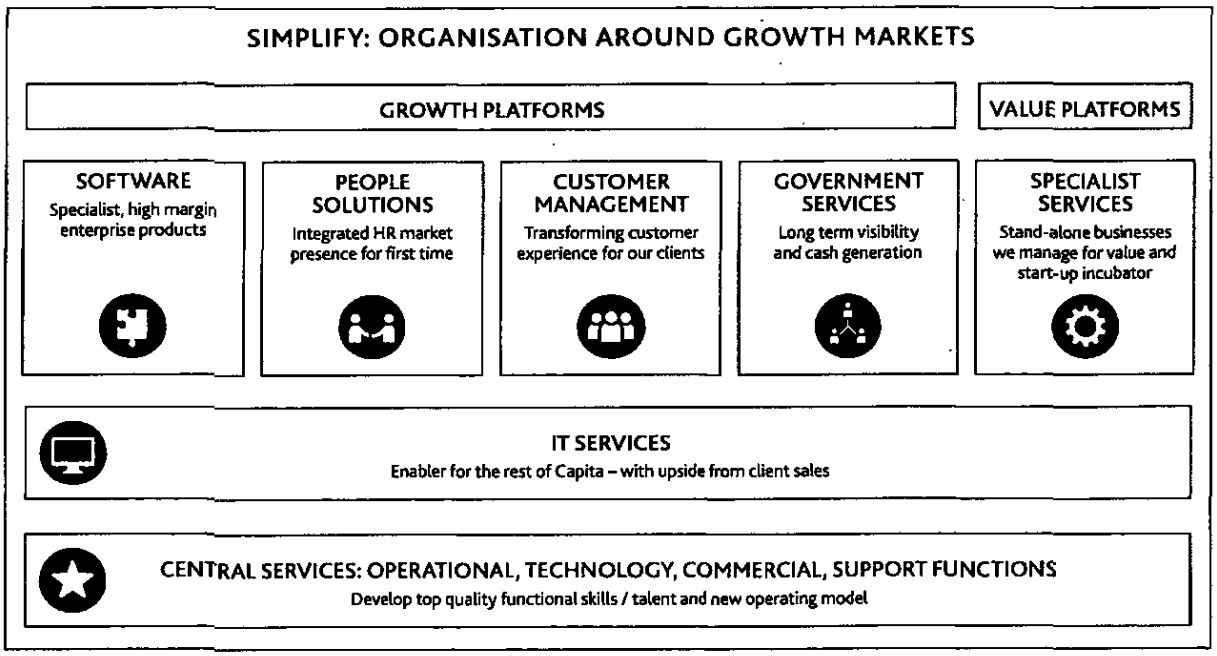
Realigned organisational structure

In line with our drive for simplification, we have reorganised our divisional structure in 2018 around five markets: Customer Management, HR, Software, Government Services and IT Services. This will increase Capita's focus upon customer management, previously included in Private Sector Partnerships, and brings together Capita's HR businesses, previously split between Private Sector Partnerships and Professional Services, under dedicated management as a single division called People Solutions for the first time.

Capita has also formed a sixth division, Specialist Services, which includes those businesses which either (a) are not within Capita's key growth markets and/or (b) have little commonality with the other divisions and/or (c) are at an early phase in their development but may be scaled up in the future. The businesses within Specialist Services are mostly stand-alone operations and will be managed on a portfolio basis in order to maximise value. We have chosen to separate these businesses to avoid detracting from management focus on the other five growth divisions. We also see real benefit in bringing these specialised businesses under dedicated management in one division.

The growth across the divisions will be supported by a common set of group capabilities including operations, sales and marketing, technology and support functions:

- Operational capabilities will be strengthened through improved contract take-on and execution processes, optimised use of offshore locations where possible and improved workforce optimisation.
- Technological capabilities will be strengthened through investing in better analytics, smarter use of data, improved, proven digitisation and automation, and better technology integration.
- Sales and marketing capabilities including consistent processes around planning, project budgeting, marketing, consultative selling, account management and proposition management.
- Common and stronger support functions including HR, Finance, IT, Commercial and Legal.



CHIEF EXECUTIVE OFFICER'S REVIEW CONTINUED

Cost reduction

We have identified a significant multi-year opportunity to reduce costs and improve operational efficiency. Historically, Capita has had no ongoing structural cost management programme and has been focused on in-year profit delivery rather than long-term efficiencies and scale. The opportunity includes reductions in general and administrative expenses, which are substantially higher than Capita's peers, centralising more procurement to leverage Capita's scale, standardising and investing in its processes and systems, increasing the use of offshoring, including scaling up its presence in India, and by increasing automation.

The Board's initial target is annualised initial cost savings of £175m from the above initiatives by the end of 2020. This includes £70m which is expected to be realised in the year ending 31 December 2018, and is reflected in our profit guidance. The balance is expected to be realised by the end of 2020.

These savings will come from a number of key areas:

- Operations: cost savings through offshoring, automation and improved consistency of processes;
- SG&A: cost savings through offshoring, the optimisation of shared services and the implementation of a new CRM system;
- IT: cost savings through consolidation of supply chain, helpdesks and networks;
- Procurement: cost savings through professionalisation and adoption of best practices across the Group, along with rationalising the supply chain and renegotiating with vendors; and
- Property: cost savings are anticipated through the consolidation of Capita's 360 site property portfolio, increased utilisation and adoption of flexible work patterns as well as offshoring to more cost-efficient locations and automation where appropriate.

The Board believes that the targeted efficiencies will not be detrimental to Capita's ability to serve its clients and its ability to win new contracts.

The cost to achieve these efficiencies is expected to be £40m for the year ending 31 December 2018 and £110m in total during the following two years.

Following the initial simplification of Capita's business and over the longer term, there could be potential to reduce costs further.

OVERVIEW OF NEW STRATEGY

SIMPLIFY

- Focus on strong positions with growth potential
- Align organisation around growth markets
- Use common, scalable capabilities
- Cost base

STRENGTHEN

- Leadership and governance
- Up to £500m investment in asset base, technology and people
- Win more of the right work
- Balance sheet

SUCCEED

- More predictable, lower risk
- At least £200m of sustainable free cash flow in 2020[1]

1 Before exceptional and restructuring charges and additional voluntary pension contributions.

2. STRATEGY – STRENGTHEN

A key aim of our new strategy is to strengthen our businesses and capabilities by making selected investments in order to drive improvements in both Capita's expertise in digital, analytics and automation and its programme delivery and operational excellence. We will also seek to ensure that we have the right leadership team and capital structure in place to support the delivery of its new strategy.

Strengthened leadership team, culture and incentives

We have formed a new Executive Committee which will meet at least once a month and often more regularly. Led by myself, this Committee brings together the six divisional leaders of the new divisional structure and a number of new functional roles, such as the Chief Transformation Officer, Chief People Officer, Chief Corporate Development Officer, Chief Sales and Marketing Officer, Chief Digital Officer and Chief Legal Officer. These new roles include six new hires to Capita, of which three are already in place. A new performance review process and a new incentive arrangement has been put in place for the Executive Committee, and clear priorities have been set for 2018.

The Executive Committee will focus on improving culture and engagement across Capita's approximately 70,000 employees, with the aim of harnessing the collective strength of our talented pool of people across all levels of the organisation. We will introduce a single set of behavioural values across all of our businesses and look at ways to better develop its employees' skills and longer-term careers, with incentives aligned to implementation of Capita's new strategy and retention of key talent. The Directors believe that Capita's newly refreshed senior management team and the Executive Committee, in particular, will help drive better behaviours and a new culture across the business, including better aligned behaviour around winning and execution of contracts.

This process will focus on four key areas:

- 'Capita values for the future' are being identified and a programme is being rolled out to adopt these values through a network of change agents.
- A tailored, multi-channel communication plan is being developed to communicate effectively deep into the organisation.
- A 'Managers and Leaders' programme is being developed to underscore the importance of leadership, to provide the right tools and technologies required to develop our talent, as well as to build a framework to reward positive behaviours.
- Finally, we believe that culture is inextricably linked to retention and, therefore, it is looking at improving retention. As part of this, we will define the right short-term and long-term incentivisation plans to retain and engage key talent. The aim is to ensures behaviours and culture are consistent with long-term shareholder value creation.

Diversity is an area of both Board and wider leadership focus for the future. Ensuring that all of our people have the opportunity to fulfil their potential is an essential element of a successful organisation, both commercially and as a responsible and supportive employer. It is also the right thing to do. We look forward to redoubling our diversity efforts at all levels, especially in senior leadership positions.

Focus on winning the work we can execute well

Capita has historically focused on short-term growth, with limited strategic business planning. It has sometimes taken on large contracts which, with hindsight, did not have the right level of planning ahead of commitment or proved to be too complex and were not executed well. In the future, we will be more focused on winning the work we are able to execute well and which has an acceptable risk and financial profile. We have established improved governance processes to support this approach.

A new pre-bid contract review committee has been formed which is led by myself and the CFO. The Committee reviews all contracts above set risk and financial thresholds and will evaluate these contracts to ensure a complete alignment with Capita's new strategy and financial goals, including an assessment of:

- Commercial terms;
- Capabilities;
- Intended operational plan;
- Life-time cash generation; and
- Potential risks and liabilities.

Post-bid, we have also put in place a process to ensure the work is done right, driving towards higher efficiency, lower risk and improved client satisfaction. This new post-win operational process will be used in the future for all major new contracts. The process provides a set of reusable services, capabilities, processes and tools. This process has been designed to deliver operational success for these new contracts, which in turn will allow Capita to have a better, more predictable and lower risk financial output.

Making targeted investments

As described above, in order for Capita to succeed in its key growth markets, selected targeted investments are required to address historic under-investment and to allow growth to follow. We plan to invest a total of up to £500m over the next three years in the following three areas:

- Maintenance infrastructure – These investments are partly business as usual in nature, but there is an element of investment to catch up underinvested areas of infrastructure. Investments will include upgrading our SAP system, improving our HR capability including payroll and talent management systems, using a single CRM system and data centre upgrades.
- Technology – Investments will include a group centre of excellence for analytics and system integration and automation across Capita covering over 1,000 FTEs and a dedicated software development group. We have created a new position, Chief Digital Officer, who will oversee technology investments across all divisions, including in robotics and data analytics.
- Organisation – Investments will include the Capita Academy to build skills across Capita, in improved programme management resources and methods and the design of a new target operating model.

Re-invigorating sales

We intend to make a number of changes in order to reduce complexity and improve the management of sales and the delivery of contracts. Focus on sales remains paramount and these improvements will require ongoing investment.

We have reallocated our centralised business development capability to the divisions, bringing it closer to each of the markets we serve and enabling the sales function to draw more fully on divisional expertise, resources and technology. This also ensures alignment of sales initiatives with innovations planned. Our divisions are now fully responsible for the bidding, implementation and management of contracts. This reduces complexity and risk and increases accountability for growth, client satisfaction and retention, as we seek to invest in sales as well as to improve sales performance. This initiative is not anticipated to incur any material additional costs.

We are increasing the emphasis on account management across our divisions, ensuring that our clients get access to the full range of Capita's capabilities and services, with the goal of increasing the number of clients for whom Capita provides multiple products or services. We plan to achieve this in two ways: through the introduction of a single client relationship management system and through improved senior relationship management of key clients.

CHIEF EXECUTIVE OFFICER'S REVIEW CONTINUED

We are also committed to driving better sales performance. Prospects, pipeline and order book tracking processes are being upgraded, initiatives are being put in place to drive cross-selling in key accounts and sales team incentivisation plans have been updated accordingly.

3. STRATEGY – SUCCEED

We will simplify our business by focusing on key growth markets, realigning our organisational structure to mirror these markets and to significantly reduce costs at the same time as improving operational efficiency.

We will strengthen our businesses and capabilities by making selected investments in order to drive improvements to both our expertise in digital, analytics and automation and our programme delivery and operational, commercial, and functional excellence. We will leverage off our investment in technology in order to win new clients and contracts. We will also ensure that we have the right leadership team and capital structure in place to support the delivery of our new strategy.

We have built a detailed, multi-year transformation plan in order to execute the strategy as outlined above, encompassing strategy implementation, cost competitiveness, capital structure, targeted investment, organisational alignment and re-igniting sales. This plan is already being executed and is being managed by a dedicated and highly experienced transformation team, headed by our newly appointed Chief Transformation Officer.

We believe that the near-term parts of this transformation are driven mostly by elements in our control and that there is a great amount of value to be extracted just from doing the basics better. The strategy has been designed to win the business which Capita can execute well, which will help make Capita's business more predictable and lower risk. The investments made into the business are expected to provide a stable and strong platform for growth which in turn can provide sustainable free cash flow in the medium term.

The financial impact of our strategy will be significant. We are initially targeting annualised initial cost savings of £175m by the end of 2020. This includes £70m which is expected to be realised in the year ending 31 December 2018 which is reflected in our profit guidance below. The cost to achieve these savings is expected to be £40m for the year ending 31 December 2018 and £110m in total in the following two years. We are also targeting double digit EBIT margins within three years.

We plan to increase investment in our business to upgrade key infrastructure and invest in differentiated capability in order to drive future growth and we plan to invest a total of up to £500m over the next three years. We are also committed to reducing the remaining pension deficit in our defined benefit scheme over the medium term as a matter of good corporate responsibility.

We expect to generate at least £200m of sustainable annual post-tax free cash flow by 2020, before exceptional and restructuring charges and additional voluntary pension contributions.

Our leverage will be reduced by the net proceeds of the Rights Issue and by non-core disposals, with the Company expecting to realise total proceeds of £300m in 2018. We have set a target range for leverage of between 1.0x and 2.0x adjusted net debt to adjusted EBITDA (prior to the adoption of IFRS 16).

Our transformation programme will be funded from a combination of existing resources, the net proceeds of the Rights Issue, the proceeds of any disposals and cash from operations.

Disposals

As part of our new strategy we intend to dispose of a number of non-core businesses, including ParkingEye and Constructionline for which a disposal programme has commenced. We expect to achieve proceeds of approximately £300m from non-core disposals in 2018. We intend to use the proceeds from these disposals to reduce indebtedness in the short term and to invest in the remaining core areas of the business over time.

Sales and business development review

Capita secured major contract wins, renewals and extensions with an aggregate total value of £676m in the year (2016: £1.34bn), comprising 41% new business and 59% renewals and extensions.

The Group's order book at 31 December 2017 stood at £8.2bn, including £8.1bn of long-term contracts and £0.1bn of contracts with a duration of less than two years. The order book represents the consideration to which Capita will be entitled to receive from clients when it satisfies the remaining performance obligations in its contracts. However, the total revenue that will be earned by Capita will also include volumetric revenue, new wins, scope changes and anticipated contract extensions. We believe the order book is a better indication of future revenues, and will be used as a key metric to replace the bid pipeline.

We chose not to rebid our Home Office escorting and detention services contract, worth slightly less than 1% of revenue, which is due to transfer to a new supplier in the first half of 2018. Our next material contract (defined as being in excess of 1% of revenue) renewal is the DWP Personal Independence Payments contract, which is due for renewal in 2019.

Outlook

In our January 2018 trading update, we highlighted that there is likely to be a significant negative impact upon profits from contract and volume attrition, the dropping out of one-off items including contract and supplier-related profits which were reported in 2017 and increases in some cost items, including depreciation and adoption of the General Data Protection Regulation. These headwinds are particularly expected to impact upon the financial performance of the Private Sector Partnerships, in both Insurance Services and Customer Management, Public Services Partnerships and IT Services divisions. We do not expect to offset these in-year challenges through the benefit of cost actions and new business wins. As a result, we expect that our underlying pre-tax profits, before significant new contracts restructuring costs, and implementation costs of the strategy in 2018 will be between £270m and £300m for the year ending 31 December 2018.

We have set a prudent plan for 2018, which includes investment in people, sales and our multi-year transformation plan for the long-term benefit of Capita.

"Looking further ahead, we have the building blocks to create a great business; one that consistently delights its clients, has operational discipline and generates sustainable free cash flow. We are now executing the plan to deliver this."

JON LEWIS, CHIEF EXECUTIVE OFFICER

OUR STRATEGY AND BUSINESS MODEL

WHAT WE DO

For more than 30 years Capita has been working across the public and private sectors, solving the complex challenges of our clients, increasing productivity, enhancing their use of technology and data, improving customer and public services and adding value to the UK and local economies. We do this by combining our talent, creativity, software, technology and innovation with sector knowledge and proven skills and expertise underpinned by our scaled operational platforms.

OUR NEW STRATEGY

Following the arrival of our new CEO in December 2017, a comprehensive strategy review was undertaken with the objective of becoming a more focused and predictable, client-centric company, generating strong sustainable free cash flow.

Recent history

Capita reported strong growth for much of the last two decades, supported by positive market conditions and its entrepreneurial culture. However, in recent years, Capita has experienced virtually no organic growth, with reported growth largely driven by acquisitions. Since 2016, Capita's operational and financial performance has weakened further due to cost overruns, delays and other issues in some of Capita's key contracts.

The business process management market was weaker than expected, which has resulted in a lower level of new business wins. Capita's weaker operational performance, expanding overhead costs and reduced cash generation also led to a significant increase in leverage. In addition, Capita was impacted by a variety of execution issues on a number of major contracts across its businesses. These included cost overruns on the PCSE contract, penalties and additional costs in relation to the TfL congestion charge contract and contract disputes in connection with certain services provided as part of the contract with The Co-operative Bank.

Further to the announcement on 31 January 2018, Capita expects there to be a significant negative impact on total and underlying profits for 2018 from contract and volume attrition, the non-recurrence of certain specific items that benefited Capita in 2017, and increases in some cost items. Capita also expects a free cash outflow in 2018, as a result of a number of known restructuring costs presented within underlying results, non-underlying payments and working capital items.

Despite the recent shortcomings identified and outlined above, the Board believes Capita has a strong underlying platform upon which to build for the future:

- Capita has a leading position in the United Kingdom in many of its markets, including customer management, HR and local government, and is also a leading strategic supplier to central government.
- In addition to the United Kingdom, Capita has a leading position in customer management across Germany and Switzerland.
- Capita has a balanced portfolio of public sector and private sector clients. Its blue-chip private sector clients view Capita as a partner who can create value as well as reduce costs, which supports profitable long-term relationships.
- Capita has a significant and differentiated technology offering in the customer management and HR markets, where it operates as a technology-enabled digital platform for its clients. The market for complex digital solutions, where the vast majority of Capita's activities lie, is expected to be a large, long-term, secular growth segment. In addition, Capita is a leading independent software provider in its chosen markets including education and local government.
- In 2017 Capita generated 70% of its revenue from long-term contracts, and has an order book of £8.2bn, which provides long-term revenue visibility.
- Capita has approximately 70,000 skilled employees who provide value-added services.

Capita recognises that the markets in which it currently operates and client demands are changing. Clients in the business process outsourcing market are offering fewer long-term 'mega deals' and more incremental sales on existing contracts, or smaller new contracts in which companies prove their value and grow over time. Clients are increasingly demanding flexible and as-a-service models, rather than one-time contracts. The services they are seeking place less reliance on generalist operational skills and more on the delivery of specialist digital platforms that deliver scale benefit and data insight. There is also an increasingly complex landscape of partners and collaborators across the value chain.

Capita needs to continue to evolve its vision to stay ahead of these changing market trends, from simply improving productivity by providing an outsourcing solution to driving value through improving client experience and insight, using innovative digital solutions and data analytics.

Underpinning all aspects of the new strategy are a number of fundamental themes, including a drive for increased simplification, efficiency, focus, standardisation and consistency of practices and culture. Capita intends to 'do fewer things, better' and use a 'build once, use many times' approach, which will enable Capita to take advantage of its scale in its markets and the breadth of its existing client relationships. The intended output of Capita's new strategy is to become a more focused and predictable business with improved returns, stronger client relationships and sustainable free cash flow.

Capita's new strategy has been designed in three elements and each of these is described in more detail below and in the Chief Executive Officer's review.

OUR BUSINESS MODEL

Our business and how we operate is changing. Our revised strategy has just been launched, detailed above and in the Chief Executive Officer's review. Our business model is being revised to reflect this new strategy and approach, along with a revised set of key performance measures for the business and its divisions.

OUR 2017 KEY PERFORMANCE INDICATORS

We consider that the following financial and non-financial key performance indicators (KPIs) are important in measuring the delivery of our strategic goals.

FINANCIAL KPIs

UNDERLYING[1] PROFIT BEFORE TAX
Aim: Achieve long-term growth in profits.
£383.0m
2016: £268.5m

UNDERLYING[1] OPERATING MARGIN
Aim: Maintain underlying operating margin.
10.7%
2016: 7.7%

UNDERLYING[1] EARNINGS PER SHARE (EPS)
Aim: Achieve long-term growth in EPS.
45.61p
2016: 31.68p

UNDERLYING[1,3] FREE CASH FLOW
Aim: Achieve sustainable, long-term free cash flow growth.
£38.0m
2016: £397.3m

REPORTED PROFIT BEFORE TAX
Aim: Achieve long-term growth in profits.
(£513.1m)
2016: (£89.8m)

RETURN ON CAPITAL EMPLOYED (ROCE)[1]
Aim: Deliver ROCE in excess of our cost of capital.
19.2%
2016: 12.8%

GEARING – ADJUSTED NET DEBT: ADJUSTED EBITDA
Aim: Keep ratio of adjusted net debt to adjusted EBITDA in the range of 2.0x to 2.5x over the long term[2].
2.27x
2016: 2.89x (as reported)

NON-FINANCIAL KPIs

PERCENTAGE OF MATERIAL SUPPLIERS[1] WHO COMPLY WITH OUR ETHICAL STANDARDS OF BUSINESS
Aim: Annually audit all material suppliers against Capita's ethical standards of business.
63%
2016: 40%

EMPLOYEE RETENTION %
Aim: Maintain high employee retention rate.
79%
2016: 78%

CARBON FOOTPRINT REDUCTION
Aim: We will aim to reduce our carbon footprint annually.
11%
2016: 2%

COMMUNITY INVESTMENT[2]
Aim: We will invest and engage with our local communities delivering community programmes to meet local needs.
£1.9m
2016: £2.1m

KPI This symbol is used to indicate our KPIs throughout the report.

Financial KPIs
1 Further details on our underlying performance are contained in our Consolidated income statement and in notes 4, 6 and 10 to the consolidated financial statements.
2 As announced on 31 January 2018, the Board's preliminary view is that the appropriate leverage for Capita over the medium term should be between 1.0 and 2.0 times adjusted net debt to adjusted EBITDA free adoption of IFRS 16.
3 Underlying free cash flow from continuing operations.
Note: The calculation of underlying figures and our KPIs are contained in our Alternative Performance Measures (APMs) on pages 202–204.

Non-Financial KPIs
1 Suppliers where our annual spend is £1m or greater.
2 Using the London Benchmarking Group methodology.
Note: With the launch of our new strategy and transformation plan, the current financial and non-financial key performance indicators used to measure performance will be reviewed and amended to reflect our new strategy.

CHIEF FINANCIAL OFFICER'S REVIEW

IMAGE REMOVED

"Reported profits in 2017 were impacted by significant non-underlying items and cash flow was weaker in the second half of the year."

NICK GREATOREX, CHIEF FINANCIAL OFFICER

Capita has early adopted IFRS 15, the new revenue recognition standard, and this report on our performance in 2017 against the comparative period in 2016 is under the new standard. The adoption of the standard has impacted our underlying results, introducing a number of one-off items, detailed below in the summary of financial performance. Following the adoption of IFRS 15, the Board has adopted a policy to separately disclose the operating profit/loss in-period from significant new contract wins and significant restructuring within underlying profits in order for users of the financial statements to obtain a proper understanding of the financial information and the performance of the business.

Effective from 1 January 2017, we restructured our organisational structure to simplify our business model, resulting in a reorganisation from 11 divisions into six market-facing divisions. Following the disposal of Capita Asset Services in the year, we are currently reporting under five divisions. In addition, we modified segmental reporting to align it with our management view of divisional performance. This includes allocating only direct overheads, such as payroll administration, pension and insurance costs, to the divisions, and showing central costs separately.

Underlying profits were in line with expectations, with improved profitability in the Private Sector Partnerships, Public Services Partnerships and IT Services divisions partially offset by lower profits in the Digital and Software Solutions division and higher central costs. However, reported profits were impacted by a number of significant non-underlying items, including goodwill and other asset impairments and the Asset Services settlement provision in relation to Connaught. There was a significant gain on the disposal of the Capita Asset Services businesses, which was treated as a discontinued operation.

CHIEF FINANCIAL OFFICER'S REVIEW CONTINUED

FINANCIAL HIGHLIGHTS

	Reported results – continuing operations			Underlying results – continuing operations		
	Reported 2017	Reported 2016	Reported YOY change	Underlying[1] 2017	Underlying[1] 2016	Underlying[1] YOY change
Revenue	£4,234.6m	£4,368.6m	(3)%	£4,167.9m	£4,357.3m	(4)%
Operating profit before significant new contracts and restructuring				£465.3m	£391.8m	+19%
Operating profit/(loss)	£(420.1)m	£(16.1)m	2,509%	£447.4m	£334.6m	+34%
Profit before tax before significant new contracts and restructuring				£400.9m	£325.7m	+23%
Profit/(loss) before tax	£(513.1)m	£(89.8)m	471%	£383.0m	£268.5m	+43%
Earnings/(loss) per share	(80.14)p	(14.27)p	462%	45.61p	31.68p	+44%
Total dividend per share	11.1p	31.7p	(65)%	11.1p	31.7p	(65)%
Free cash flow	£37.7m	£367.3m	(90)%	£38.0m	£397.3m	(90)%

1 Refer to Alternative Performance Measures on pages 202–204. Further details on our underlying performance are contained in our Consolidated income statement and in notes 3, 6 and 10 to the consolidated financial statements.

The Board has adopted a policy to separately disclose those items that it considers are outside the underlying operating results for the particular year under review and against which the Group's performance is assessed. Items within non-underlying include intangible amortisation, asset impairments, acquisition contingent consideration movements, the financial impact of business exits or businesses in the process of being exited, acquisition expenses, movements in the mark-to-market valuation of certain financial instruments, and specific non-recurring items in the income statement. In the Directors' judgement, these need to be disclosed separately by virtue of their nature and size and/or incidence, in order for users of the financial statements to obtain a proper understanding of the financial information and the underlying performance of the business. In 2017, specific non-recurring items include impairment of assets related to the life and pensions business, impairment of goodwill and impairment of other non-current assets following a comprehensive review of the recoverability of tangible and intangible assets, resulting from changes in client and Capita strategy in the second half of 2017.

The Alternative Performance Measures (APMs) disclosed on pages 202–204 provide more detail on the criteria that the Board believes give relevant information on the Group's financial performance, position and cash flows. These measures provide useful information which is not otherwise readily available from the financial statements. Further disclosure of the reporting of underlying and non-underlying presentation is included in note 2 to the financial statements – Summary of significant accounting policies (pages 96–108).

REPORTED OPERATING LOSS BRIDGE TO UNDERLYING OPERATING PROFIT

Reported operating loss	**£(420.1)m**
Impairment of goodwill	£551.6m
Impairment of other non-current assets	£63.5m
Impairment of life and pension assets	£61.2m
Claims and litigation provisions	£30.0m
Amortisation and impairment of acquired intangibles	£124.3m
Business exits	£14.7m
Other	£22.2m
Underlying operating profit	**£447.4m**

Whilst leverage (adjusted net debt to adjusted EBITDA[1]) at 31 December 2017 was 2.27 times, free cash flow was constrained by the partial normalisation of seasonal cash management and a reduction of deferred income in the second half of the year. As announced on 31 January 2018, following completion of the 2018 business planning process, the Group has set a plan, focusing on investment in people, sales capability and its transformation plan. We expect a free cash outflow in 2018, which will be impacted by a number of known non-underlying payments and working capital items. The Group holds cash and undrawn committed facilities to enable the Group to manage its liquidity risk. At 31 December 2017, the Group held cash and cash equivalents net of overdrafts of £478.4m, and has available to it a committed Revolving Credit Facility of £600m. Our plan shows that whilst the business can operate in compliance with the adjusted net debt to adjusted EBITDA covenants, downside scenarios indicate that the available headroom is not sufficient to operate within these covenant tests.

Given the Board's view of appropriate leverage for Capita discussed in the Chief Executive Officer's review, the short-term outlook, level of indebtedness and need to invest for the long-term benefit of the Group, the Board is not recommending the payment of a final dividend and has suspended dividends until the Company is generating sustainable free cash flow. In addition, the Board has announced its decision to dispose of a number of non-core businesses, and has announced the launch of a Rights Issue. Post the Rights Issue, and the disposal programme, Capita will be well positioned with a sustainable level of debt. This will enable us to provide confidence to all our stakeholders, including key clients.

In determining the appropriate basis of preparation of the financial statements for the year 31 December 2017, the Directors are required to consider whether the Group can continue in operational existence for the foreseeable future. The Board has concluded that it is appropriate to adopt the going concern basis, having undertaken a rigorous assessment of the financial forecasts and with consideration of the anticipated net proceeds from the announced Rights Issue which the Board is confident will be approved. The Board's assessment is set out in more detail on page 97.

As discussed, the Board has initiated a transformation plan to improve the performance of Capita over the medium- to long-term and to address a number of business imperatives. The costs of delivering this plan will entail costs such as restructuring and professional adviser fees, and will be disclosed separately within underlying profits. This is in line with the Board's policy to separately disclose the operating profit/loss in-period from significant new contract wins and restructuring in order for users of the financial statements to obtain a proper understanding of the financial information and the performance of the business.

The major items contributing to 2017 performance are detailed in the following summary of financial performance.

1 Refer to Accounting Policies in note 2 to the financial statements.

IMPACTS OF IFRS 15

KEY IMPACTS:

Revenue more evenly distributed over the life of contracts and active software licences – timing of profits re-profiled.

Potentially lower profits or losses in early years on contracts where there are significant upfront restructuring costs or higher operating costs prior to transformation – compensating increase in profits in later years.

Balance sheet includes
- New contract fulfilment assets created in the process of transforming services
- Deferred income in relation to contracts where payments have been received from clients to undertake transformation in advance of delivering planned outcomes.

NO IMPACT ON:

- Lifetime profitability of contracts
- Cash flow of contracts
- Majority of transactional businesses

IFRS 15

We have adopted IFRS 15 from 1 January 2017 using the full retrospective method, thereby restating the 2016 comparatives, to provide investors with clarity on the impact of the new accounting standard in a transitional period for Capita, in line with our strategy of simplifying the business and improving transparency. This was a significant project and I would like to thank all concerned for delivering it.

IFRS 15 gives rise to changes in the timing of revenue and cost recognition but will not impact upon the lifetime profitability of contracts, the cash flow of contracts or the majority of our transactional businesses. The main changes for Capita from the adoption of IFRS 15 are on its long-term contracts and software businesses, in particular:

- Revenue is more evenly phased over the life of contracts and active software licences in line with the delivery of outcomes to clients and, consequently, the timing of profits is re-profiled.
- We will potentially recognise lower profits or make losses in the early years of contracts where there are significant upfront restructuring costs or higher operating costs prior to transformation, with a compensating increase in profits in later years. The total net impact at Group level is a function of the balance of contracts in the early or late stage of their life cycle at transition to IFRS 15 and in subsequent years. As a result, contract profits, and in certain cases contract losses, are now reported in the prior periods.
- The Group's balance sheet includes new contract fulfilment assets created in the process of transforming services; and a significant increase in the level of deferred income in relation to contracts where payments have been received from clients to undertake work prior to the recognition of revenue and planned outcomes being delivered. For some contracts, in particular the Life and Pensions business, there are instances where this creates future profits in excess of future cash inflows. The majority of deferred income will unwind within the following 12 months and Capita aims to replace this with similar advanced payments subject to additions or changes to the Group's contract portfolio.
- The net impact of the recognition of the deferred income balances, contract fulfilment assets and other movements has resulted in the Group recording consolidated net liabilities, which were £929.8m as at 31 December 2017 (2016: net liability £552.9m).
- Contract terminations arising in the normal course of business may give rise to the disposal of a contract fulfilment asset and/or a true up of revenue recognised, which if material, may give rise to one-off gains or losses. Such amounts are included in underlying operating profit and separately disclosed if considered material.
- Due to the changes in the pattern and timing of revenue and cost recognition under IFRS 15, and the recognition of a deferred income liability and contract fulfilment assets on the balance sheet from 1 January 2016, the principles of IAS 12 give rise to a movement in deferred tax, primarily an increase in the deferred tax asset recognised.

The adoption of IFRS 15 will increase our focus upon efficiency and performance within the business, better aligning our financial results with the value delivered to its clients.

SUMMARY OF FINANCIAL PERFORMANCE IN 2017

Revenue

Reported revenue decreased by 3% to £4,234.6m (2016: £4,368.6m) and underlying revenue decreased by 4% to £4,167.9m (2016: £4,357.3m). Underlying revenue on a like-for-like basis, excluding results from businesses exited in both years, decreased by 0.6% including 1.5% organic decline and 0.9% growth from acquisitions.

Revenues increased in the Private Sector Partnerships division, which benefited from new contracts with Tesco Mobile and mobilcom-debitel and growth in TV Licensing and The Co-operative Bank. This was slightly outweighed by declines in the Public Services Partnerships division, due to weakness in real estate and central government services, and the Digital and Software Solutions division, due to licence attrition. Our revenue mix in 2017 was 70% long-term contractual, 16% short-term contractual and 14% transactional.

CHIEF FINANCIAL OFFICER'S REVIEW CONTINUED

Operating profit

Underlying operating profit

Following the adoption of IFRS 15, the Board has adopted a policy to separately disclose the operating profit/loss in-period from significant new contract wins and significant restructuring within underlying profits in order for users of the financial statements to obtain a proper understanding of the financial information and the performance of the business.

Underlying operating profit before significant new contracts and restructuring increased by 19% to £465.3m (2016: £391.8m). Profits increased as a result of improvements in the performance of a number of major contracts in the Private Sector Partnerships and Public Services Partnerships divisions, an improvement in the performance of our IT Services division, which included benefits from our actions to reduce costs and a one-off £9.2m settlement from a supplier, and a lower level of contract fulfilment asset write-offs in 2017 compared to 2016. This was partially offset by a decline in profits in the Digital and Software Solutions division, an increase in central costs and a decrease in property commercialisation, as set out in note 8 to our consolidated financial statements. We concluded discussions with the Ministry of Defence in relation to the Defence Infrastructure Organisation (DIO) contract and the results include a £22.0m benefit from the re-shaping of this contract, arising from the recognition of previously deferred income, which is not expected to recur in 2018.

UNDERLYING REVENUE

£4,167.9m

2016: £4,357.3m

UNDERLYING PROFIT BEFORE TAX

£383.0m

2016: £268.5

The DIO contract is expected to end in 2019. This re-shaping arises as a result of our new revenue recognition policy under IFRS 15. We now defer revenue over the expected life of a contract. Where a contract is terminated early, all deferred revenue is pulled forward and recognised in the year of termination. Similarly, any associated contract specific assets that were being amortised over the expected life of the contract are written off in the year of termination, unless there are alternative uses on other contracts. This will be a feature of our accounting going forward when terminations occur prior to the expected life of the contract. As noted above, IFRS 15 has introduced the recognition of contact fulfilment assets. Such assets are reviewed for impairment based on an assessment of the current and projected performance of the associated contract. During 2017, this resulted in the impairment of contract fulfilment assets with a charge of £14.1m (2016: £nil) recorded within underlying operating profit.

Underlying operating profit after significant new contracts and restructuring increased by 34% to £447.4m (2016: £334.6m). Significant new contracts and restructuring costs were £17.9m (2016: £57.2m), relating to professional adviser fees associated with the broadened transformation plan and, separately, the restructuring of a small number of businesses. There were no significant new contracts in the year.

Underlying operating profit is before charging a number of specific non-underlying items. This is consistent with prior years, to allow a better understanding of the business performance in-year.

Reported operating loss

Reported operating loss for the year was £420.1m (2016: loss £16.1m), including a charge for specific items of £852.8m (2016: £353.5m). The significant movement from 2017 arises from the impairment of goodwill, intangible assets, other non-current assets, and investment loans as at 31 December 2017. Further detail on the separately recorded items in 2017 is provided below:

- Impairment and amortisation of intangible assets (including goodwill): These amounted to £689.9m (2016: £229.2m) The Group carries on the balance sheet significant balances related to acquired intangible assets and goodwill. The amortisation of the acquired intangible assets, and any impairment charges, are reported separately due to the size of the annual charges and because the performance of the acquired businesses is assessed through the underlying operational results which, for internal purposes, excludes any amounts associated with the acquired intangible assets. During the year, impairment charges have been recorded in relation to businesses of £551.6m (2016: £66.6m). As reported in the Chief Executive Officer's review, significant actions are required to address recent operational and external challenges and a major transformation plan has been launched. Actions were taken in the prior year to implement a new simplified market-facing organisation structure, and at the time of the half year results Capita announced an improved win rate against the backdrop of a quiet market. Since that date, Capita has continued to experience a higher level of revenue attrition than expected, and continued to experience delays in client decision making and weakness in new sales. As announced in January 2018, Capita has shifted its strategy, and set a plan, which focuses on investing in people, sales capability and its transformation plan. The business plan for the divisions, produced between December 2017 and March 2018, indicates there is likely to be a significant negative impact upon profits from contract and volume attrition. In addition, this plan indicates a significant deterioration in new business opportunities from earlier positions. These events and circumstances have led to the recognition of the impairment charge as set out in note 16 to the consolidated financial statements.
- Impairment of life and pensions assets: The Group's life and pension business had developed a platform to support an existing life and pensions contract, but which could provide services to multiple clients in the future. The Group's strategic review has identified there is no longer a market for this platform and accordingly the carrying value of this and associated assets has been written off. The impact on the financial statements is a non-underlying charge of £61.2m representing the write-off of the non-current assets which have no further value to the Group and are redundant.

1 Refer to Alternative Performance Measures on pages 202–204.

- Other and disposals of non-current asset impairments: As part of its year-end close process, Capita has undertaken a comprehensive review of the recoverability of its tangible and intangible assets. Following the review, management has taken a decision to impair, at 31 December 2017, a number of assets relating to specific programmes resulting from changes in client and Capita strategy in the second half of 2017. Non-current assets amounting to £63.5m have been written off as a non-underlying charge consistent with prior year treatment, as the assets have no future use to the Group and accordingly are redundant.
- Impairment of loan and investment: the Group has fully impaired a historical loan and investment in the year totalling £9.0m (2016: £2.6m). The charge is reported separately due to its historical nature and to be consistent to the treatment applied for similar items in prior years.
- Fair value movements on financial instruments: including those that do not meet the criteria for hedge accounting £(2.1)m (2016: £7.7m): certain of the Group's financial instruments do not qualify for hedge accounting and accounting standards require these to be mark-to-market at each reporting date with any movements recorded in the income statement. Such charges or credits are dependent on external market factors and are not related to the underlying performance of the Group. For that reason, the amounts are reported as non-underlying items and therefore are not considered by the Board in assessing the performance of the Group.
- Other legal provisions: significant litigation costs relating to two claims were provided in the year (£30.0m). The claims were in respect of: a contract within the real estate and infrastructure business and was notified to the Group during 2017, and the related contract began in 2007; and a contract within the employee solutions business where more information on the progress of the claim has become apparent, and the related contract was delivered from 2009. The amount provided in respect of these two claims has been recognised in non-underlying specific items due to their age and significance.
- Acquisition-related costs: costs of £1.7m (2016: £9.0m) – IFRS requires certain costs incurred in connection with acquired businesses to be recorded within the Group income statement. These charges are not included in the internal assessment of business performance which, as above, is based on the underlying operational results. These charges are therefore separately disclosed as specific items.

The Board has considered FRC guidance on what should be excluded from GAAP numbers and concluded that it is appropriate to disclose the above items as specific non-underlying items.

We exited a number of businesses in 2017, including the majority of our specialist recruitment businesses, and were in an active process to sell a non-core property business at 31 December 2017. The loss from these business exits was £45.4m (2016: £3.4m gain). Business exits are also disclosed separately as non-underlying.

Discontinued operations

The disposal of the Capita Asset Services businesses has been treated as a discontinued operation as stipulated by IFRS 5. The profit on the disposal of these businesses was £445.4m. This profit is specific to the disposed businesses and is therefore excluded from both the underlying and reported results of the continuing operations.

The costs of £66.0m in relation to reaching a full and final settlement with the Financial Conduct Authority (FCA) regarding the Connaught Income Series 1 Fund, as detailed in note 27 to the consolidated financial statements, are separately identified as a non-underlying specific item attributable to the discontinued operation due to the significance and nature of the claims to which they relate.

Financing

The underlying interest charge in 2017, excluding the fair value movement on mark-to-market fixed rate swaps, was £64.4m (2016: £66.1m) and interest cover was 8.6 times for the year (2016: 8.8 times). Capita terminated its higher coupon fixed rate interest rate swaps in the first half of the year.

Cash flow

Free cash flow from continuing operations before non-underlying expenses was £38.0m (Restated 2016: £397.3m) and free cash flow after non-underlying expenses was £37.7m (Restated 2016: £367.3m).

Capita's free cash flow in 2017 was impacted by two changes in our working capital profile. Firstly, there was a partial normalisation of seasonal cash management, having historically optimised the working capital position at the end of reporting periods. Secondly, there was a reduction of deferred income in the second half of the year, which reflects the relatively low level of new business signed in 2016 and 2017, which meant that we received less cash payments from clients to undertake work than revenue recognised in the period. These items were largely responsible for a £311.8m working capital outflow from continuing operations.

Net capital expenditure on continuing operations was £114.1m in 2017 (2016: £139.7m), including an increase in discretionary spend in areas such as software and employee solutions and lower contract related and maintenance spend.

Net debt

Net debt at 31 December 2017 was £1,117.0m (2016: £1,778.8m), reflecting the receipt of the proceeds from the disposal of the Asset Services businesses which was partially offset by the aforementioned working capital items.

Consistent with prior years, the Group makes use of non-recourse trade receivable financing arrangements provided to it by a number of its relationship banks. £110.0m of receivables had been sold under these arrangements and had not been settled as at 31 December 2017 (2016: £133.6m). As these trade receivables have been sold without recourse, the Group does not consider them to be part of its core capital.

At 31 December 2017, our adjusted net debt to adjusted EBITDA[1] covenant ratio was 2.27 times. This ratio includes contingent obligations under bonds and guarantees and excludes our non-recourse receivables financing, which was a balance of £110.0m at 31 December 2017.

At each reporting date we assess the calculation of the Group's debt covenants, both for that period and subsequent ones. These covenants are calculated based on the underlying performance of the Group in that they exclude exceptional items. The Group has been consistent with previous years in its treatments of these items.

CHIEF FINANCIAL OFFICER'S REVIEW CONTINUED

Capital management and dividend

Following completion of the 2018 business planning process, the Group has set a plan, deciding to invest in people, sales capability and its transformation plan. We expect a free cash outflow in 2018, which will be impacted by a number of known restructuring costs presented within underlying results, non-underlying payments and working capital items. We expect around £300.0m spend in relation to known commitments, including £66.0m cash costs on the Connaught settlement, £51.0m in relation to the separation of Capita Asset Services (including a pension contribution), £40.0m costs in relation to realising cost savings and efficiencies from the transformation plan, £26.0m restructuring costs relating to Capita's previously announced cost reduction plan, contingent and deferred considerations, professional fees in order to create and implement the proposed transformation plan, litigation and other items. In addition, we expect a £130.0m cash outflow from the final normalisation of period end cash management activity, and a £130.0m cash outflow on continued reduction in deferred income, reflecting the ongoing low level of new business wins. Our plan shows that whilst the business can operate in compliance with the adjusted net debt to adjusted EBITDA covenants, downside scenarios indicate that the available headroom is not sufficient to operate within these covenant tests. The Group's policy is to hold cash and undrawn committed facilities at a level sufficient to fund the Group's operations and its medium-term plans. The Group holds cash and undrawn committed facilities to enable the Group to manage its liquidity risk. At 31 December 2017, the Group held cash and cash equivalents net of overdrafts of £478.4m, and has available to it a committed Revolving Credit Facility of £600m.

As discussed in the Chief Executive Officer's review the Board is reviewing the capital structure of the Group. The Board's view is that the appropriate leverage for Capita over the medium term should be between 1.0 and 2.0 times adjusted net debt to adjusted EBITDA (prior to the adoption of IFRS 16).

Given the short-term outlook, level of indebtedness and need to invest for the long-term benefit of the Group, the Board has decided upon a number of actions. Firstly, we are pursuing 'self-help' options, including the aforementioned cost actions and non-core disposals. Secondly, the Board is not recommending the payment of a final dividend making a total of 11.1p for the year (2016: 31.7p). However, the Board recognises the importance of regular dividend payments to investors in forming part of their total shareholder return, and will consider the payment of dividends once Capita is generating sufficient sustainable free cash flow. Finally, the Board has announced it is raising equity by way of a Rights Issue this year. The Company has entered into an underwriting agreement of £701m with Citigroup Global Markets Limited and Goldman Sachs International.

Capita has reached a comprehensive arrangement with the holders of its US Private Placement Notes in order to address certain issues which arose from the early adoption of IFRS 15. The arrangement provides increased headroom and flexibility under Capita's financial covenants, and thereby sets up a robust framework to support the new strategy. In return for this increased flexibility, Capita has agreed (i) to prepay £150m of principal of the US Private Placement Notes (plus an estimated make-whole payment of £7m) from the proceeds of the Rights Issue; (ii) to apply 50 per cent of the net proceeds from future disposals to the prepayment of principal of the US Private Placement Notes, with payment of make-whole, until such time as an estimated £315m of US Private Placement Notes have been pre-paid; and (iii) to pay a coupon uplift of 75 basis points, representing approximately £5m of incremental costs through 2018.

We set out in note 26 to the consolidated financial statements our future minimum rental payments under our lease arrangements that highlight gross commitments of £833.0m. In prior years we had presented these on a present value basis, but have changed the presentation to disclose the gross commitments as we believe this is more helpful in the context of assessing our future liability. The prior year comparative has been re-presented and the impact of this grossing up is £112.9m. Our lease arrangements have been reviewed extensively as part of the work we have initiated in preparing for the adoption of IFRS 16 Leases. This identified certain property leases that had been omitted in the prior year analysis, and we have corrected the comparative to include these gross commitments (£165.1m). The main adjustment related to our new head office property that we will occupy later in 2018, and which was under construction as at the end of the prior year.

Pension

As announced on 31 January 2018, Capita intends, as a matter of good corporate responsibility, to reduce the remaining pension deficit in its defined benefit scheme. The current deficit is supported by an asset backed funding arrangement of £69m at 31 March 2017, the value of which is not included in the last disclosed IAS 19 deficit of £407m as at 31 December 2017. The triennial actuarial valuation of the scheme as at 31 March 2017 is due to be completed by 30 June 2018. In addition to Capita's current annual contributions, further contributions totalling £21.5 million were paid in January 2018. Capita is fully committed to addressing the remainder of the deficit in the medium term.

1 Refer to Alternative Performance Measures on pages 202–204.

Taxation

Capita has an open and positive working relationship with HMRC, has a designated customer relationship manager, and is committed to prompt disclosure and transparency in all dealings with HMRC and overseas tax authorities. The Group does not have a complex tax structure, nor does it pursue any aggressive tax avoidance activities and in recognition of this and the aforementioned relationship it enjoys a low risk rating from HMRC. Due to client requirements and also due to the location of some of our businesses, the Group has operations in a number of countries outside of the UK. All Capita operations in non-UK jurisdictions are trading operations and pay the appropriate local taxes for these activities. Further detail, regarding the tax strategy, can be found on the Policies and Principles area of the Capita website.

In total, Capita contributed £204.8m (2016: £273.0m) in taxes across its UK operations in the year. This consisted of a net refund of £12.7m (2016: payment £48.6m) of UK corporation tax; £21.4m (2016: £23.9m) in irrecoverable VAT payments; £155.5m (2016: £163.7m) in employer NIC; and £40.6m (2016: £36.8m) in other levies including business rates, import duties, apprenticeship levy and environmental taxes. Additionally, the Group collected and remitted to the UK Government £409.9m (2016: £463.6m) of VAT and £367.7m (2016: £399.1m) of Capita employee PAYE and NIC. Capita entities in overseas jurisdictions paid £6.4m (2016: £15.1m) of tax on local profits.

STRATEGIC INITIATIVES

We continued to progress a number of short- and long-term initiatives to reduce our cost base, work more efficiently and enhance our financial reporting, which will now form part of Capita's broader transformation plan discussed in the Chief Executive Officer's review:

Restructuring

- Major restructuring activities, including reductions in overheads, headcount and related property costs. The net benefit from these cost initiatives was £38.0m in 2017.

Procurement

- Centralising more of our procurement. Capita's central procurement team has a wide ranging brief to find value, working with the divisions, through increasing the proportion of centrally controlled spend, consolidating our supplier base and leveraging our purchasing power.

Property

- Engaging our property expertise to rationalise and increase the utilisation of Capita's property estate, in metro centres and regionally. This includes a consolidation of our sites in London which is planned for 2018.

Finance transformation

- Improving Capita's financial reporting systems, processes and controls, through increasing standardisation, automation and the quality and availability of data. We are investing in an upgrade of our financial system and increasing the use of offshoring and shared services.

ACQUISITIONS

In 2017, Capita acquired a number of small businesses to build capability in existing markets, enter new markets and enhance our existing services and solutions. We spent £20.0m in acquiring five niche businesses in software, voice and data, IT, e-commerce and travel and events.

DISPOSALS

At the end of 2016, we announced our intention to dispose of the Capita Asset Services businesses and our standalone specialist recruitment businesses to increase the focus on technology-enabled business process management and reduce leverage. Both disposals were completed in the year, and contributed to the reduction in leverage at the year-end.

The disposal of the Capita Asset Services businesses has been treated as a discontinued operation and the comparatives have been restated, as detailed in note 5 of the consolidated financial statements on page 111.

FINANCE INITIATIVES

RESTRUCTURING

Major restructuring activities, including reductions in overheads, headcount and related property costs. The net benefit from these cost initiatives was £38m in 2017.

PROCUREMENT CENTRALISATION

Our central procurement team has a wide ranging brief to find value, working with the divisions, increasing the proportion of centrally controlled spend, consolidating the supplier base and leveraging our scale.

PROPERTY RATIONALISATION

Engaging our property expertise to rationalise and increase the utilisation of Capita's property estate, in metro centres and regionally. This includes a consolidation of our sites in London which is planned for 2018.

FINANCE TRANSFORMATION

Improving our financial reporting systems, processes and controls, through increasing standardisation, automation and the quality and availability of data. We are investing in an upgrade of our financial system and increasing the use of offshoring and shared services.

FINANCIAL RESULTS

The financial statements have been prepared under IFRS and the Group's accounting policies are set out on pages 96–108. Management also presents revenue, operating profit, profit before tax and earnings per share excluding non-underlying items to provide additional useful information on underlying trends to shareholders. More detail on the Alternative Performance Measures can be found on pages 202–204.

REPORTED RESULTS

Reported revenue

Reported revenue decreased by 3% to £4,234.6m (2016: £4,368.6m).

Reported profit before tax

KPI

Reported loss before tax in 2017 was £(513.1)m (2016: £(89.8)m), reflecting the impact of non-underlying charges as detailed in note 4 and note 6 of the consolidated financial statements on pages 110 and 112–113.

Reported earnings per share

Reported loss per share in 2017 was (80.14)p (2016: (14.27)p), reflecting the impact of non-underlying charges as detailed in note 4 and note 6 of the consolidated financial statements on pages 110 and 112–113.

UNDERLYING RESULTS

Underlying revenue

Underlying revenue[1] decreased by 4% to £4,167.9m (2016: £4,357.3m). Underlying revenue on a like-for-like basis[1], excluding results from businesses exited in both years, decreased by 0.6% including 1.5% organic decline and 0.9% growth from acquisitions.

Underlying operating profit and margin

KPI

Underlying operating profit[1] increased by 34% to £447.4m in 2017 (2016: £334.6m). Our underlying operating margin[1] was 10.7% (2016: 7.7%).

Underlying profit before tax

KPI

Underlying profit before tax[1] increased by 43% to £383.0m (2016: £268.5m) and underlying profit before tax[1] before significant new contracts and restructuring costs increased by 23% to £400.9m (2016: £325.7m).

Underlying earnings per share (EPS)

KPI APM

Underlying earnings per share[1] increased by 44% to 45.61p in 2017 (2016: 31.68p).

Dividends

The Board is not recommending the payment of a final dividend (2016: 20.60p), making a total of 11.10p for the year (2016: 31.70p). The Board will consider the payment of dividends once Capita is generating sufficient sustainable free cash flow.

Free cash flow

Free cash flow before non-underlying expenses[1] was £38.0m (2016: £397.3m) and free cash flow after non-underlying expenses was £37.7m (2016: £367.3m).

Capital expenditure

We aim to allocate capital efficiently, focusing upon opportunities that generate the best return for shareholders and avoiding tying up too much capital in long-term projects.

In 2017, net capital expenditure was £114.1m (2016: £139.7m), reflecting lower contract specific and maintenance spend. Investment will continue to be made on the basis of returns on the value of capital being deployed.

Gearing

APM

Net debt at end December 2017 was £1,117.0m (2016: £1,778.8m). As at 31 December 2017, we had £1,484m of private placement bond debt (net of currency swaps) of which £153m matures in 2018 and the remainder matures over the period up to 2027. In addition, we have £100m of bank debt which matures in 2019, and an undrawn £600m revolving credit facility of which £81m matures in August 2020 and £519m in August 2021.

In 2017, our adjusted net debt to adjusted EBITDA ratio[1] was 2.27 times and interest cover[1] was 8.6 times.

Debt maturity profile as at 31 December 2017 (£m)

Year	Bond debt[2]	Bank debt	Total
2018	153	–	**153**
2019	101	100	**201**
2020	294	–	**294**
2021	283	–	**283**
2022	309	–	**309**
2023	89	–	**89**
2024	–	–	**–**
2025	101	–	**101**
2026	46	–	**46**
2027	108	–	**108**
Total	1,484	100	**1,584**

Return on capital employed (ROCE)

KPI

ROCE reflects how productively we deploy capital and is incorporated into senior managements' long-term incentive schemes, which are 25% based upon performance against ROCE targets.

ROCE is calculated as underlying net operating profit after tax[1] (NOPAT) divided by average capital employed. Capital employed[1] (CE) is the total of equity shareholders' funds, net debt, pension deficit and cumulative equity impact from non-underlying items such as amortisation.

We have calculated our WACC by weighting the cost of our debt and equity financing in line with the amounts of debt and equity that we use to finance our activities, assuming a risk-free rate of 1.23%, a market risk premium of 13.89% and a beta of 0.57 times.

In 2017, our ROCE[1] was 19.2% (2016: 12.8%), which compares to our estimated post-tax WACC of 7.46%.

Nick Greatorex
Chief Financial Officer
23 April 2018

KPI This symbol is used to indicate our KPIs throughout the report.
APM This symbol is used to indicate our APMs throughout the report.

1 Refer to Alternative Performance Measures on pages 202–204.
2 Bond debt shown at face value after the effect of currency and interest rate swaps.

OUR PEOPLE AND TALENT

Our 70,000 talented, committed and engaged employees are essential to delivering business critical services and solutions across all our markets.

As referenced in the Chairman's Introduction, the Board is determined to give all employees the sound basis for a stable and happy career with Capita, focused on delivering outstanding services to our clients and their customers. Our approximately 70,000 talented, committed and engaged employees are essential to delivering business critical services and solutions across all our markets. Their skills, knowledge, attitude and creativity ensure we continue to deliver great service and positive outcomes for our clients.
2017 has been another challenging year for Capita and its employees. During the year, our divisions were restructured, impacting many of our businesses. We also disposed of The Capita Asset Services businesses and our specialist recruitment businesses, with 3,600 staff leaving the Company as a result. We initiated our multi-year transformation plan at the beginning of 2018, including looking at our cost base and how we we will deliver a renewed sales focus, a programme of significant change for the Company. A major part of the role of the new Chief People Officer, appointed in early 2018, will be to ensure the right resources are in place to deliver Capita back to a position of strength. During these periods of change, we work hard to ensure those affected are informed, involved and communicated to before and during the process.

SEE 'SUPPORTING PEOPLE THROUGH CHANGE' ON PAGE 24

EMPLOYEE ENGAGEMENT

Improving our culture and engagement with employees at all levels has been an important part of the change journey we have started, and there is work to be done.

In 2017, we conducted three pulse surveys to gauge our employees' motivation and engagement. Whilst participation and sentiment improved over the year, with a positive view in individual businesses of Capita as a good place to work, it also highlighted the need for greater career opportunities and personal development.

The McKinsey Organisational Health Index (OHI) culture and organisation health index undertaken in December 2017, an initiative under our new Chief Executive Officer, has given us deeper insight into our Company and employees' views and indicates that employee morale has been impacted by recent events. As we refresh the strategy and structure we will use the lessons from this deeper assessment as a foundation to help define the culture and leadership style we need to grow in the future.

CAREER DEVELOPMENT

Access to career opportunities is an important part of the benefit of working for Capita, with opportunities available to all employees, irrespective of how they joined Capita. The extensive range of roles, businesses, sectors and locations provides career possibilities most other businesses cannot offer.

In 2017, we made it easier for hiring managers to post their open roles internally and simplified the internal recruiting process therefore supporting greater internal mobility. We also launched a dedicated talent hub which profiles all the career opportunities across Capita to our employees. With most jobs now being made available to internal applicants, a new communication campaign has been launched, encouraging employees to 'look closer, go further' to find their next role with us.

Internal mobility rates have improved since we made these changes, with internal applicants now filling 22% of roles, up from 10% at the start of the year. And engagement data on career development has improved this year, with now over 60% saying that they are positive about their opportunities at Capita.

LEARNING AND DEVELOPMENT

Capita has continued to invest in ensuring our employees have the skills they need to do well. In the year we invested £14.0m in training (2016: £13.9m). With the introduction of the apprenticeship levy we also have a new focus on creating development opportunities for our employees who are starting their career journey. At the end of 2017 we had 234 apprentices working across our businesses, with 250 successfully completing their apprenticeships during the year.

2017 also saw a deeper focus on leadership capabilities, in particular the importance of visible leadership during periods of challenging under performance. A new standard for leaders has been introduced, making it clear that our best leaders are not only focusing on the financial and commercial performance of their business, but also show leadership in building partnerships of trust with clients, create motivated and high-performing teams, consistently demonstrate courageous judgement, and demonstrate visible leadership by standing up and leading for the future. These Leadership Hallmarks are being enshrined now in recruitment, assessment, development, and rewards for leaders.

LEADERSHIP HALLMARKS

P&L PERFORMANCE
Commercial and numbers-driven
Focused on costs and growth
Strong on execution

CLIENT PARTNERSHIP
Knows how to become a trusted partner
Great at selling additional services to existing clients
Consistently delivers best and right outcomes

TEAM COMMITMENT
Builds productive, effective, motivated, committed, progressive teams
Merits loyalty, trust and extra effort

COURAGEOUS JUDGEMENT
Independent thinker
Resilient, persistent
Curious, active, enquiring mind
Looks long term, does the best thing, not the expedient thing

VISIBLE LEADERSHIP
Communicates with compelling style
Talks about purpose, vision, future
Strong personal influence
Develops a positive reputation, stands for the right things

OUR PEOPLE AND TALENT CONTINUED

KPI

GENDER DIVERSITY

IMAGE REMOVED

IMAGE REMOVED

IMAGE REMOVED

ATTRACTION AND RETENTION

We recruit over 10,000 people into Capita every year, and our ability to attract the skilled workforce we need to serve our clients well is critical to our success. Particularly in the roles where we recruit many people into similar roles, such as customer management, we have been increasingly innovative in our approach to attracting great people. Equally important is our ability to recruit great talent at the most senior levels of the organisation, and in 2017 we have recruited executive talent from leading organisations from sectors as diverse as telecoms, oil and gas, software and financial services.

Despite the challenges Capita has faced, overall employee retention rates marginally improved to 79% (2016: 78%) as management teams across our businesses have increased their focus on employee engagement. Our sharpened focus on career development is also a factor, and multiple communications initiatives to ensure employees hear the information they need and feel part of a successful business. Retention will continue to be an area of risk for the Group as its embarks on its transformation plan, and this is a priority for our Head of Talent and for the new Chief People Officer, who joined in April 2018.

SEE INTERNAL CONTROL AND RISK MANAGEMENT PAGES 36–43

DIVERSITY

Having a diverse workforce brings fresh perspectives and helps us to create truly innovative solutions that benefit our clients and helps improve our own market competitiveness. We are committed to developing an inclusive culture that reflects the diversity of our clients, their customers and the communities in which we work.

ETHNICITY SPLIT[1]

18%

2016: 22%

Capita's employee group is diverse. Walk around any of our contact centres, or visit any of our offices across the UK and overseas, and you will appreciate just how diverse our employee base is. And we are proud of the fact that across Capita the gender mix is evenly balanced.

However, we recognise that with several recent senior leader departures and business disposals, we need to redouble our efforts to reflect our employee diversity at senior levels. Steps are now being taken to support female leaders rising through our organisation, and ensuring our culture supports our best leaders across the full spectrum of our diverse workforce. Our female leaders have come together to drive some sharper focus on diversity, including more emphasis on effective mentoring of female colleagues, encouraging formal and informal networking, improving recruitment practices, and ensuring our policies reflect the needs of a diverse workforce.

A greater push during the second half of 2017 to ensure that recruitment shortlists include diverse candidates is starting to show an outcome, with senior female hires up at 32%. There is work to be done here, but Capita is committed to ensuring that our leaders represent the diversity of our business and the people who work here.

GENDER BALANCE AND PAY

Alongside the progress made on improving the focus on diversity across Capita, the UK Government's gender pay reporting requirements are providing us with a good baseline and evidence from which we can develop our diversity strategy further.

The overall gender pay differential within Capita was:

Difference between men and women[2] (%)	
Mean pay differential	26.8%
Median pay differential	25.3%

This gap is higher than the UK average of 18%, and our work to understand this gap points to a number of factors: the imbalance of men and women in the organisational hierarchy; Capita has more men in senior positions across the business who are generally paid higher and there are more women than men in the roles attracting the lower salaries. Capita is dedicated to addressing the current gender pay gap and is committed to creating an inclusive and diverse culture which will enable our people and Company to thrive with creativity, innovation and success.

More detail is disclosed in our Gender Pay Gap Report on our website at www.capita.com/responsibility.

SUPPORTING PEOPLE THROUGH CHANGE

So, we can help our clients be more efficient and meet future business requirements, as well as addressing immediate performance and financial challenges, it is sometimes necessary to reduce the headcount on a particular contract or in a business or to move roles to our offshore centres. Where this is the case, Capita takes a proactive approach in seeking alternative employment options for those affected employees in order to redeploy them into other areas of our business.

Where suitable opportunities are not available we are open and honest about the situation. We go through a full redundancy consultation process involving individuals and their recognised trade union and employee representatives. Consultation with our trade unions is key to securing the most appropriate outcomes for affected employees.

Where we divest a business, or are unsuccessful in renewing a contract, we take a similar proactive approach helping our employees during these uncertain times. As Transfer of Undertakings (Protection of Employment) (TUPE) regulations apply to disposals of UK businesses and contract transfers we can provide assurance to affected employees that their roles will transfer to the new service provider or new owner. During the year, we transferred out 5,000 employees under TUPE, the majority as the result of the disposal of The Capita Asset Services businesses and our specialist recruitment businesses. Maintaining employee morale and service levels and protecting a business when it is identified for sale is critical to protecting jobs and the asset being sold. We run a communications programme as part of the mergers and acquisitions process, working with the senior leadership teams to protect employees and business interests. This ensures a smooth transfer out for employees and protects the value Capita has created. Capita's experience in this area is extensive.

KPI This symbol is used to indicate our KPIs throughout the report.

1 % employees from ethnic minorities, based on voluntary disclosure.
2 Data as at 5 April 2017.

DIVISIONAL PERFORMANCE

DIVISIONAL REPORTING AND PERFORMANCE

We are currently reporting our financial performance across five separate operating divisions, following the organisational restructuring at the beginning of 2017, and the disposal of our Capita Asset Services businesses in November 2017.

Following the recent strategic review and commencement of the transformation plan, we will be simplifying our structure further in 2018, focused on key growth markets. From this year we will be reporting under six operating divisions:

- **Software**
- **People Solutions**
- **Customer Management**
- **Government Services**
- **IT Services**
- **Specialist Services**

Further details can be found in the Chief Executive Officer's review on pages 6–12.

2017 DIVISIONAL STRUCTURE AND FINANCIAL PERFORMANCE

2017	Private Sector Partnerships	Public Services Partnerships	Professional Services	Digital and Software Solutions	IT Services
Underlying revenue (£m)	**1,588.3**	**1,087.2**	**532.8**	**410.9**	**507.8**
% of Group	39%	26%	13%	10%	12%
Underlying operating profit (£m)	**137.5**	**73.0**	**104.9**	**113.9**	**78.1**
% of Group	27%	14%	21%	23%	15%
Underlying operating margin (%)	**8.7%**	**6.7%**	**19.7%**	**27.7%**	**15.4%**
Employees	**44,500**	**12,500**	**4,000**	**3,700**	**4,300**
Services and contracts	Customer management UK and Europe Insurance services Retail banking and mortgage solutions Employee solutions (pensions and employee benefits)	Electronic monitoring DWP PIP DCC smart metering NHS PCSE DIO Central government services Local public services Real estate and infrastructure	HR solutions (resourcing and learning services) RPP army Recruiting AXELOS Fera Business travel Supplier assessment services Parking services	Education software Local government software Secure solutions and services Financial software AMT Sybex	Enterprise services Networking solutions Technology solutions Managed print solutions

The table above presents underlying revenue and trading results for the Group's business segments for the years 2017 and 2016. All operational divisions are continuing except for Capita Asset Services which was disposed of in the year and is disclosed as discontinued in both 2017 and 2016. The 2016 consolidated income statement has not been restated for the impact of business exits and other non-underlying items (except for Capita Asset Services). If the 2016 underlying consolidated income statement was restated for both businesses exited during 2016 and businesses that were held for sale in 2015 but were not exited in 2016, revenue would be increased by £173.9m and profit before tax would be reduced by £5.8m. See note 7 Segmental Information for detailed financial disclosure of our divisions. Changes to divisional underlying financial performance following early adoption of IFRS 15 is detailed within each division on the following pages. Reported profit is not included in our review of the divisions, as the items included within non-underlying are not within the results against which each division's performance is assessed by the Board, however we have highlighted non-current asset and goodwill impairments where relevant.

FOR FURTHER DETAILS SEE GROUP FINANCIAL OFFICER'S OVERVIEW, PAGES 15–22

DIVISIONAL PERFORMANCE CONTINUED

PRIVATE SECTOR PARTNERSHIPS

The Private Sector Partnerships division includes our UK customer management business (focused principally on retail, utilities, media and telecoms sectors), Capita Europe (customer management in Germany and Switzerland), Insurance Services (life and pensions, insurance services and retail banking) and employee solutions (employee benefits and corporate pensions administration).

FACT SHEET

Employees

44,500

Countries of operation

UK	India
South Africa	Poland

Key markets

Retail	Media
Telecoms	Life and Pensions
Utilities	Insurance

UNDERLYING REVENUE

£1,588.3m

IMAGE REMOVED

IMAGE REMOVED

OVERVIEW OF THE DIVISION

The Private Sector Partnerships division includes our UK customer management business (focused principally on retail, utilities, media and telecoms sectors), Capita Europe (customer management in Germany and Switzerland), Insurance Services (life and pensions, insurance services and retail banking) and employee solutions (employee benefits and corporate pensions administration).
We help clients to better service their end customers in a multi-channel world, become more efficient in their core processes and increase their workforce's engagement and productivity. Clients often partner with us to run their services under multi-year contracts, which can include transforming the end-to-end service supported by new technologies. Our differentiated approach is to deliver measurable business outcomes for clients including: guaranteed cost reduction, improvement in customer satisfaction and/or revenue generation.

Over 75% of the Private Sector Partnerships division's revenue is derived from long-term contracts (greater than two years).

FINANCIAL PERFORMANCE

	2017	2016
Underlying revenue	£1,588.3m	£1,544.4m
Underlying operating profit	£137.5m	£71.4m
Underlying operating margin	8.7%	4.6%
Order book	£4,002.0m	–

- Underlying revenue increased by 3%, driven by growth in Capita Europe, including the benefit of our new contract with mobilcom-debitel, an increase in TV Licensing and The Co-operative Bank. There was a modest decline in UK customer management, which reflected weakness in remediation services (mis-selling rectification).
- Underlying profits increased due to the renegotiation of The Co-operative Bank contract, a £26m swing from loss to profit on a major contract which reflected the dropping out of one-off modification costs incurred in 2016, cost initiatives and lower restructuring costs, partially offset by a lower contribution from Remediation Services and additional costs on the transformation of mobilcom-debitel in Germany.
- In January 2018, we announced that the administration of Prudential's life and pensions business, around 2% of Group revenue, will be transferring from Capita to a new supplier later in 2018. As previously disclosed, another of our life and pensions clients is conducting a strategic review, the outcome of which remains uncertain but is expected to result in the continuation of the contract with amended terms or the termination of the contract. Contract terminations arising in the normal course of business may give rise to the derecognition of a contract fulfilment asset and/or a true up of revenue recognised, which if material, may give rise to one-off gains or losses. Such amounts are included in underlying operating profit and separately disclosed if considered material.
- We expect divisional profits to decline in 2018 due to a combination of higher contract and volume attrition and increases in costs, including adoption of the General Data Protection Regulation, in Life, Pensions and Insurance and Customer Management businesses.
- Included within non-underlying charges in 2017 is £389.1m from the impairment of goodwill, £14.0m from the impairment of acquired intangibles, and £61.2m from the impairment of assets now considered redundant, and £20.6m from the impairment of other non-current assets, also considered redundant with no further benefit to the division (refer to note 6 to the consolidated financial statements).

OUR SERVICES AND PERFORMANCE

Customer management UK and Europe

Our customer management businesses account for nearly half of the division's revenues. We are the largest provider of customer management services in the UK, with 16%[1] market share. We operate across the breadth of the private sector with our core markets in retail, utilities, telecoms and media. We serve our UK clients from service centres in the UK, South Africa, India and Poland. We also service our clients in Germany and Switzerland from centres in those countries and from Poland.

The UK customer management market is estimated to be worth £3.8bn per annum and growing at around 4% CAGR[2] through 2021. The German and Swiss customer management markets are estimated to be valued at £3.7bn per annum and growing at 5% CAGR[2] through to 2021. In Capita's view, the markets in the UK, Germany and Switzerland are relatively under-penetrated with only 15-20% of customer management seats outsourced. Following the acquisition in 2015 of the German and Swiss customer management business avocis, the business has not performed as expected despite the favourable market conditions.

Outsourcing can provide a solution to solve multiple challenges: managing end customers in a multi-channel environment, addressing cost pressure, funding the investment challenge to refresh customer management platforms and resourcing 'peaks' to support the demands of multiple marketing campaigns often in an increasingly regulated environment.

In both the UK and Europe, Capita competes with a range of local and global players for transactional contracts, typically priced on a £/FTE hour basis, and in 2017 we experienced higher attrition in these lower value transactional contracts.

However, Capita is differentiated in its willingness to contract for outcomes, rather than on a £/FTE hour basis, for clients such as O2, Dixons Carphone, Marks & Spencer and npower. We offer an 'insight-led transformation' proposition, where we commit to reduce customer contact costs (both demand and unit costs) on a gain-share basis or a 'business-wide transformation' proposition, where we charge on a per customer basis, which normally declines over the contract term.

The growth of digital channels has resulted in an increase in customer contact as customer journeys become more complicated, for example 'Where Is My Order?' in retail.

In addition, the investment to support multiple channels exacerbates the cost challenge for clients, enabling us to position outsourcing as a route to create investment headroom for new channels and propositions.

Technology enables the reduction in customer contact costs. Our outcome-based propositions rely on Capita's capability to reduce demand, automate transactions and accelerate channel shift. This approach has been most successful for O2, our largest Group client, Dixons Carphone and Marks & Spencer. Capita works with a range of automation and robotic process automation (RPA) partners such as Eckoh, Jacada, Blue Prism and Fusion to underpin these propositions. We have the largest deployment of Blue Prism virtual robots in the UK and are a certified Blue Prism partner.

Increasingly, we are also using a combination of technology, data and insight to trigger proactive contact to end customers. Typically, this is driven by online behaviours; we use triggers to stimulate either SMS or voice contact to recover a broken customer journey or introduce a sales opportunity for clients such as EDF, Plusnet and Sky Mobile.

During the year, we maintained revenues and market share in our UK business, despite a more challenging economic environment and the loss of smaller contracts. Our largest contracts with O2 and npower continued to perform well, and we renewed relationships with Marks & Spencer, Volkswagen Group and the RSPCA. New sales wins in the year have been lower and this is an area which will get greater focus in 2018. In Germany, the core business faced higher costs as a result of minimum wage inflation, although this has now been stabilised and the focus in 2018 is on improving margins. We commenced the mobilcom-debitel contract in March 2017.

Life, pensions, insurance and retail banking

We are the market leader in 'closed book' BPO in the life insurance sector in the UK, administering 15 million life, pensions and savings policies. We also provide general and specialist insurance services and provide mortgage processing and remediation services to retail banks.

Accounting for a third of divisional revenues, this segment further declined in 2017 as the closed book life and pensions market in the UK is naturally declining as policies are surrendered and providers continue to consolidate. We deliver a dedicated service aligned to our clients' brands, whilst at the same time leveraging shared services to deliver scale, drive quality, and reduce cost and risk in a shrinking market. However, without a proprietary platform offering, our growth prospects in our Life & Pensions business are low as some clients require technology-led investment to reduce policy administration costs, and address their digital ambitions. In January 2018, we announced the loss of our largest life and pensions client, Prudential UK, who have made a strategic technology decision, switching to a new provider later in 2018, and ending our 10-year relationship early. Our other life clients continue to perform as expected, as we reduce our cost base commensurate with natural policy attrition. Our remediation services business, providing mis-selling rectification for UK retail banks, declined again in 2017 as the volume of new PPI claims continues to decrease. Our mortgage processing business, including The Co-operative Bank contract, performed well in the year, including a contract extension with Tesco Bank.

Employee solutions

The UK benefits administration market is valued at £3.4bn[1]. In corporate pensions administration, we are the market leader in the UK, managing over 1,500 pension schemes with over 5.2 million members on our proprietary platform, HartLink. Within the market, there is a shift from Defined Benefits to Defined Contribution administration, in line with a broader shift in corporate pensions. In addition, benefits are increasingly seen as part of the strategic HR agenda. Historically, outsourcing providers made money through broking on behalf of benefits providers. Following the FCA-led Retail Distribution Review (RDR), broking commissions are no longer permitted. Providers now offer benefits advice on a fee basis and position benefits as a route to drive employee engagement and improve retention.

We also have a proprietary benefits platform, Orbit, to support our proposition in the digital workplace. This platform delivers benefits to clients' workforces and is built to increase colleague engagement. For example, we offer educational functionality (e.g. financial wellbeing) to support the interactions with employees.

After reduced client engagement towards the end of 2016, the pensions administration business performed better in 2017, winning new contracts with the Cabinet Office (Royal Mail Statutory Pension Scheme administration), Diageo and Ferrero in addition to commencing services with recent new wins including Unilever, Marks & Spencer and British Coal.

1 Capita estimate based on BPS Market Forecast: 2017-2021, NelsonHall, 2017 generated February 2018.
2 BPS Market Forecast: 2017-2021, NelsonHall, generated February 2018.

DIVISIONAL PERFORMANCE CONTINUED

PUBLIC SERVICES PARTNERSHIPS

The Public Services Partnerships division provides business process management services across the UK public sector and local government, and real estate, property and infrastructure services into local government and the commercial property sector.

FACT SHEET

Employees

12,500

Countries of operation

UK | India

Key markets

Local government	Education
Central government	Health
Defence	Commercial property

UNDERLYING REVENUE

£1,087.2m

IMAGE REMOVED

IMAGE REMOVED

OVERVIEW OF THE DIVISION

The Public Services Partnerships division provides business process management services across the UK public sector and local government, and real estate, property and infrastructure services into local government and the commercial property sector. It contains our largest contracts by revenue and most complex central and local government contracts, working with our public sector partners to modernise and improve the efficiency, quality and accessibility of services whilst providing value to UK taxpayers.

Over 70% of 2017 revenue from long-term contracts (greater than two years) across our local government, central government, defence, education and health businesses.

FINANCIAL PERFORMANCE

	2017	2016
Underlying revenue	£1,087.2m	£1,127.9m
Underlying operating profit	£73.0m	£0.5m
Underlying operating margin	6.7%	–
Order book	£2,764.9m	–

- Underlying revenue fell by 4% due to weakness in real estate and central government services, which was partially offset by growth in our Department for Work and Pensions (DWP) PIP and DCC Smart Metering contracts.
- Underlying profits increased as a result of our Transport for London contract, on which we incurred £25.0m one-off costs in 2016, the re-shaping of our Defence Infrastructure Organisation (DIO) contract and the aforementioned performances from our DWP PIP and DCC Smart Metering contracts. The results include a £22.0m benefit from the re-shaping of the DIO contract arising from the recognition of previously deferred income, which is not expected to recur in 2018. The re-shaping arises as a result of our new revenue recognition policy under IFRS 15. We now defer revenue over the expected life of a contract. Where a contract is terminated early, all deferred revenue is pulled forward and recognised in the year of termination. Similarly, any associated contract specific assets that were being amortised over the expected life of the contract are written off in the year of termination, unless there are alternative uses on other contracts. The DIO contract is expected to end in 2019.
- Included within non-underlying charges in 2017 is £7.5m from the impairment of goodwill, and £14.0m from the impairment of other non-current assets considered redundant with no future benefit to the division (refer to note 6 to the consolidated financial statements).

OUR SERVICES AND PERFORMANCE

The division houses our largest central and local government contracts.

Key contracts	Description
DWP Personal Independence Payments (DWP PIP)	Administration of personal independence payments in two regions in England and Northern Ireland
Birmingham City Council	IT and digital services
Staffordshire County Council (Entrust)	Provisions of support services to schools
London Borough of Barnet	Customer services, finance, HR and property strategic partnership
NHS Primary Care Support England (NHS PCSE)	Support services for GPs, pharmacies, opticians and dental practices
Home Office Electronic Monitoring	Administration of tagging for offenders
Home Office Escorting and Detention Services[1]	Removal of overstayers
Defence Infrastructure Organisation (DIO)	Management of the Ministry of Defence's property estate
Transport for London	Administration of Congestion Charge and Low Emissions Zone
DCC Smart Metering	Management, implementation and development of the national smart metering infrastructure

Public sector contracting

The market for multi-year outsourced contracts in central government and the wider public sector remains subdued, with a weak sales pipeline in new larger opportunities, despite the pressure on Government to make cost savings, meet increasing service demands and improve service quality and access; although we are anticipating a number of rebid opportunities over the coming years – both for services currently run by Capita and a number where they currently reside with other suppliers. There is an increasing reluctance to outsource in the current economic and political environment, with Brexit continuing to create uncertainty and expected to continue until EU negotiations are complete. However, Capita believes that Brexit is likely to give rise to opportunities in the medium term as the UK Government starts to develop new policies, service needs and delivery requirements in a post-Brexit environment.

We have been successful this year in winning sole provider on a number of Cabinet Office frameworks but rebid terms have become less attractive and multi-year deals are being replaced with short-term flexible partnerships. We have increased our engagement with the Cabinet Office who remain supportive of appropriate outsourcing to the private sector, subject to performance, and Capita continues to be seen as a Strategic Supplier of services to Government.

Across our contract portfolio, the majority of our contracts are performing well. We continue to face challenges in our NHS Primary Care Support England (NHS PCSE) contract. NHS PCSE has improved operationally during the year and we continue to drive improvements across the service in conjunction with stakeholders and NHSE, but we have had to invest in the service in order to achieve this and the cash cost of recovering performance has been high.

Our Defence Infrastructure Organisation (DIO) partnership was modified in the second half of 2017, removing our gain share arrangement and changing our role to one where we essentially operate as a consultant, but with a significant ongoing commitment of specialist resource to support and guide operations and strategy. We will focus on supporting the DIO in achieving its goals until the contract ends.

Local public services

We are the largest provider of services across local government (with around 15%[2] forecast market share of a £3bn market size). Councils across England are under severe budgetary pressure, with budgets being cut significantly in the last five years. This has impacted the larger long-term opportunities we historically saw across the sector, however the need for innovation and digitisation to achieve long-term cost savings is driving engagement with providers.

Councils are reluctant to engage with providers on multi-year deals, however the need to focus on traditional revenue collection is paramount. The increasing role of regulation and planning and building controls are creating opportunities for our real estate and infrastructure practice, as authorities face skills and capacity shortages. In our core local public services practice we have brought together our wider service offering, providing opportunities for greater cost savings for clients. We have created a regional sales approach to focus on sourcing and converting smaller deal pipeline and created larger operational centres to offer more commodity solutions for new and existing clients.

Across our long-term strategic partnerships, we replaced Service Birmingham, our joint venture arrangement with Birmingham City Council, with a new and more flexible partnership. The next phase is implementing the Council's digital and IT transformation strategy.

Real estate and property infrastructure

We are a top-ten real estate and engineering consultancy in the UK. Our principal markets are housing, transport, local government, retail and health. We experienced ongoing challenges across these areas during 2017 and, as a result, lost some long-term contracts resulting in the overall business contracting in 2017.

Across the UK, owners and occupiers of real estate and infrastructure are keen to address both the increasing demands and opportunities that these assets present. For our asset management teams, increasing user expectations and commercialisation opportunities coupled with regulatory and sustainability demands presents future opportunities. With the increasing investment in infrastructure and the need for more housing (both for the public and private sectors) this should present opportunities for our development and project-related professionals.

As a relatively small provider in these competitive markets, we are re-shaping our proposition for our clients, reducing costs and changing our operating model to make our service offering more relevant to client needs and more focused on key segments of our markets.

1 Contract ends April 2018 after decision to not rebid.
2 Estimated BPS market shares UK & Ireland – State & Local: 2016 – NelsonHall, February 2018.

DIVISIONAL PERFORMANCE CONTINUED

PROFESSIONAL SERVICES

Our Professional Services division comprises a portfolio of businesses – our corporate and specialist services, including commercialised public sector assets and joint ventures.

FACT SHEET

Employees

4,000

Countries of operation

UK | Poland | India

Key markets

Financial services | Technology, Media & Telecoms | Central government | Utilities | Local government

UNDERLYING REVENUE

£532.8m

IMAGE REMOVED

IMAGE REMOVED

OVERVIEW OF THE DIVISION

Our Professional Services division comprises a portfolio of businesses – our corporate and specialist services, including commercialised public sector assets and joint ventures. The division provides a breadth of resourcing and HR managed services, employee engagement and branding, and learning services. It also contains our travel and events business, Constructionline, ParkingEye, our Army Recruiting Partnering Project (RPP) contract and AXELOS and Fera, our government commercial partnerships. Its strategy is focused on making clients' internal organisations more efficient and growing government assets.

Professional Services contains the smallest proportion of our long-term contracted revenue, which accounted for over 40% of the division's 2017 revenue. The main businesses are listed below in order of size of revenue.

FINANCIAL PERFORMANCE

	2017	2016
Underlying revenue	**£532.8m**	£758.3m
Underlying operating profit	**£104.9m**	£108.3m
Underlying operating margin	**19.7%**	14.3%
Order book	**£350.3m**	–

- Underlying revenue fell by 30% as a result of the disposal of our specialist recruitment businesses.
- Underlying revenue also fell on a like-for-like basis, excluding Specialist Recruitment from both years, due to the loss of part of our Civil Service Learning contract, a decline in Capita Resourcing and the dropping out of property commercialisation revenue which was recognised in the second half of 2016. This was partially offset by growth in the RPP contract and some of our trading businesses.
- Underlying profits decreased due to the dropping out of property commercialisation profits, which was partially offset by costs reducing on RPP and good growth in ParkingEye and Fera.
- Included within non-underlying charges in 2017 is £4.3m from the impairment of other non-current assets considered redundant with no future benefit to the division (refer to note 6 to the consolidated financial statements).

OUR SERVICES AND PERFORMANCE

HR solutions

Our HR businesses makes up the largest segment in this division by revenue. We are a leading provider of resourcing solutions across the public and private sector, providing full recruitment processing outsourcing (RPO) services for individual projects or as a full outsourced recruitment service and pre-employment vetting. Working alongside our employer branding, marketing and communications agency, we engage and attract top talent for some of the world's largest employers. We compete with some of the largest UK and global resourcing providers, with technology and the ability to provide an innovative online proposition an important differentiator. Learning services, our learning service businesses provide specialist training and development services and administers apprenticeship schemes for large corporates and for government departments. The UK employment market remains challenging, and wider public sector spend is still subdued, impacting our resourcing and learning services businesses. Despite this backdrop we secured a new contract to deliver apprenticeship services to the Civil Service, but we were unsuccessful in winning the replacement for our Contingent Labour One contract, which ends in June 2018.

Army Recruiting Partnering Project (RPP)

We have been managing the end-to-end recruitment of British Army regulars and reserves since 2014, under a 10-year contract. During the year, a new IT system went live in November which is being used to actively support recruiting.

Travel services

Capita travel and events is a mid-sized provider of travel, meetings and event management services to corporates and the public sector, providing managed business travel services to private and public sector clients in the UK. Using our proprietary booking and ticketing system we provide an end-to-end booking and ticketing service across rail, air and hotels, providing clients with a cost-effective service. The market is large and fast growing, as corporates seek to consolidate travel providers and reduce spend. The business performed better in the year, despite ongoing pressure on travel budgets by clients.

Axelos

AXELOS is a joint venture between Capita, with a 51% stake, and the Cabinet Office which was launched in January 2014 to promote and grow the Best Management Practice portfolio and to jointly realise wider commercial value for taxpayers from the Government's intellectual property. AXELOS, under Capita's management, is responsible for developing, enhancing and promoting a number of best-practice methodologies, such as Prince2, ITIL and Resilia, used globally by professionals working primarily in project, programme and portfolio management, IT service management and cyber resilience. The business continued to grow its revenues in the year through extending its portfolio of courses and increasing its membership.

Fera – Food and Environment Research Agency

Fera, a commercial partnership between Capita and DEFRA, formed in 2015, provides scientific services to government, academia and commercial clients, such as food retailers and manufacturers of crop protection products, in the UK and overseas. Capita holds a 75% stake in the venture. It specialises in translating scientific knowledge into practical applications, such as helping to ensure food safety and quality 'from farm to fork', food authenticity (e.g. Manuka honey), sustainable crop production, environmental management and conservation. It also plays a key role in the UK's ability to respond to, and recover from, emergency situations affecting the food chain and rural economy and has a global reputation for food science expertise.

In January 2018, as part of our strategic review, we announced the intention to sell our Constructionline and ParkingEye businesses.

DIVISIONAL PERFORMANCE CONTINUED

DIGITAL AND SOFTWARE SOLUTIONS

The Digital and Software Solutions product software division supplies application software and wider solutions across the public sector, utilities and financial services markets.

FACT SHEET

Employees

3,700

Countries of operation

UK	India

Key markets

Education	Emergency services
Local government	Justice
Police	Utilities

UNDERLYING REVENUE

£410.9m

IMAGE REMOVED

IMAGE REMOVED

OVERVIEW OF THE DIVISION

The Digital and Software Solutions product software division supplies application software and wider solutions across the public sector, utilities and financial services markets. As a software products provider, our industry and functional specific IP supports critical public services and business processes. We offer a broad range of services that include: local government and education software, digital transformation and development, secure software and technologies, mobile and big data solutions, geospatial solutions, business management software, travel management solutions, enterprise resource planning (ERP), workforce and resource management and business analytics.

We have a wide product portfolio of approximately 140 software products and modules, over 90% of our revenue is underpinned by long-term contracts (greater than two years), reflecting the business and service critical nature of some of the products we deploy and support for our clients.

FINANCIAL PERFORMANCE

	2017	2016
Underlying revenue	**£410.9m**	£420.3m
Underlying operating profit	**£113.9m**	£134.4m
Underlying operating margin	**27.7%**	32.0%
Order book	**£550.4m**	–

- With the introduction of IFRS 15, the majority of our software licence sales are recognised as 'active' licences, with revenue spread over the contract lifetime. Underlying revenue fell by 2%, reflecting a decline in Capita Software Services (local government, social housing and social care) and the end of a long-term active software licence with The Co-operative Bank. There was good growth in AMT Sybex (utilities) and Education Software Services was flat. The majority of division revenue is UK-based but we are putting partnerships in place with a view to increasing international sales.
- Underlying profits fell by 14%, reflecting the above decline in sales and increases in amortisation and staff costs. We continued to invest in product development and sales, including the next version of education software, and are progressing the offshoring of development work to enhance capability and efficiency.
- Included within non-underlying charges in 2017 is £125.1m from the impairment of goodwill, and £7.4m from the impairment of other non-current assets considered redundant with no future benefit to the division (refer to note 6 to the consolidated financial statements).

OUR SERVICES AND PERFORMANCE

Capita is a top five provider of enterprise software products in the UK[1], a market estimated to be worth £15bn in 2017, growing at 8% CAGR[1,2] through 2021. The majority of the division's products support the key public sector markets of education, local government, emergency services, health, and central government as well as the legal profession, utilities and financial services markets. We are increasing our focus on growing our international presence as we have identified good opportunities for growth outside our core UK market.

Whilst new sales wins have declined across our key sectors, a number of key wins in mortgage administration and the police and justice sectors has illustrated our continued product competitiveness and deep sector knowledge.

The increasing focus on application development offshoring has assisted in us building a strong development skill base in India at a lower cost base, with particular focus on key technologies such as cloud and digital transformation. This will enable us to fully support our multi-year product development cycles, critical to supporting our future sales pipeline.

During 2017, there has been an increasing focus on sales and standardising sales processes, resulting in a stronger qualified pipeline than the previous year.

Education

We are a leading provider of management information systems to primary and secondary schools and further education establishments in the UK, with a growing client base in English-speaking overseas markets. Capita's education software services provides software to over 22,000 schools and SIMS8, our cloud product, will go on general release in early 2018. During the year, we switched our focus to joining up our propositions to the sector and realigned our resources from client retention to growth. We delivered improved performance in the year.

Local government

We have software applications in over 95% of local authorities in England, supporting key finance functions including benefits claims administration, council tax and rates collection, housing management, parking and debt management for over 200 UK councils. The software services 'One' product family increased its penetration across the local government market with over 90% of all councils gaining value from some part of the product family. In addition, local councils are increasingly using our robotic process automation (RPA) services for faster, more efficient processing of revenue and benefits claims.

Policing, justice and emergency services

Our secure solutions and services business is the UK's leading provider of public contact and control room solutions to the emergency services, encompassing contact management, integrated communications and telephony and command and control, together with solutions that support custody, crime and intelligence operations as well as HR and back-office processes. Our control room and communication solutions currently support all 10 ambulance services, 36 fire services and 40 police forces. We are seeing increasing demand for our market leading ControlWorks and PoliceWorks solutions, most notably in the end-to-end implementation at Greater Manchester Police, and EvidenceWorks is delivering results in the area of evidence management. Our 999Eye streaming service for the emergency services continues to gain traction following positive media coverage of our collaboration with Gwent Police.

Utilities

In utilities our AMT Sybex business provides the main B2B platform for five of the 'Big 6' UK Energy retailers, supporting their field engineers. Our mobility solutions enable the inspection of 15,000km of UK rail track and 7,600km of UK high pressure gas pipeline.

Mortgage administration

We have a growing platform offering for mortgage administration. We are delivering the latest customer focused technologies such as digital consumer propositions and broker web portal, i. We now offer an end-to-end mortgage services solution, covering: origination, services, administration and recovery. In the year, we signed a new contract with HSBC and renewed our relationship with Tesco Bank.

1 UK Software and IT Services Rankings 2017, Techmarketview, June 2017.
2 Forecast: Enterprise Software Markets, Worldwide, 2014-2021, 4Q17 Update, Gartner, 15 December 2017.

DIVISIONAL PERFORMANCE CONTINUED

IT SERVICES

The IT Services division delivers a broad portfolio of IT infrastructure and applications solutions and consulting services to organisations across the private and public sectors and across Capita.

FACT SHEET

Employees

4,300

Countries of operation

UK | Poland | India

Key markets

Local government | Education | Central government | Health | Defence

UNDERLYING REVENUE

£507.8m

IMAGE REMOVED

IMAGE REMOVED

OVERVIEW OF THE DIVISION

The IT Services division delivers a broad portfolio of IT infrastructure and applications solutions and consulting services to organisations across the private and public sectors and across Capita. We operate across the UK and from our operations in India, supporting clients at a local and national level. We have strategic partnerships with leading global IT vendors and have invested in our own portfolio of hosted platforms and operate our own UK-wide network and datacentres.

Over 60% of the division's revenue is from long-term contracts (greater than two years).

FINANCIAL PERFORMANCE

	2017	2016
Underlying revenue	£507.8m	£481.5m
Underlying operating profit	£78.1m	£47.1m
Underlying operating margin	15.4%	9.8%
Order book	£514.3m	–

- Underlying revenue increased by 5%, including the full year benefit from the acquisition of Trustmarque. Good organic growth in networking solutions and managed print services was offset by declines in technology solutions, managed IT solutions and major clients within enterprise services.
- Underlying profits increased sharply, reflecting the benefits from our restructuring of the business in the second half of 2016 and a £9m one-off supplier settlement. Looking forward, we expect IT Services profits to decline in 2018, as a result of higher contract and volume attrition and the dropping out of the supplier settlement.
- Included within non-underlying charges in 2017 is £29.9m from the impairment of goodwill, and £13.0m from the impairment of other non-current assets considered redundant with no future benefit to the division (refer to note 6 to the consolidated financial statements).

OUR SERVICES AND PERFORMANCE

Capita is a top-ten supplier of IT services in the UK[1], a market estimated to be worth £27.9bn in 2017, growing at 1% CAGR[2] through 2020. IT Services operates across every industry in both the public and private sectors, with a strong market position in local government, education and health. Increased M&A activity has led to some new superplayers, however, long-standing market leaders are causing most change by repositioning from their traditional verticals. IT Services' breadth of portfolio is enabling us to maintain competitive advantage in our key markets.

Overall performance across the division has been variable during the year, as the division, under a new Executive Officer, continued to address the sales and trading issues which impacted its performance in 2016.

There has been significant focus on internal structure, with some non-core businesses being moved out of the division, including the IT recruitment business and the translation and interpreting businesses. The integration of previous acquisitions, most significantly the integration of part of Trustmarque with enterprise services was also addressed in the year.

Enterprise Services

Our enterprise services business, including Trustmarque and managed IT solutions, our largest segment by revenue, has significant scale and is able to provide enterprise level services to major clients with complex and demanding requirements. We have continued to make investments in our own Cloud and Hosted platforms and in infrastructure from hosted voice and collaboration platforms through to datacentre infrastructure, thus enabling us to offer a cloud/hybrid/on premise infrastructure proposition and match solutions to customer needs. Further investment in our datacentre estate will be required in 2018 following a review after the limited outtage in our main datacentre earlier in 2017.

Ongoing austerity within the public sector has led to clients looking for different funding models based on return on investment, profit or savings share. This is also driving the move to cloud technologies, helped by greater acceptance of the security of cloud across the public sector, which enables greater control and flexibility over spend. However, the challenging government outsourcing environment is still impacting sales growth.

During the year, we brought together our enterprise services and Trustmarque businesses together, combining our core, enterprise scale services with the agility of Trustmarque Services, drawing upon the Cloud capability and widening the end-to-end offering we can provide to our clients. Enterprise services have added further value across the business to our customer base and operations through our increased use of our offshore capability, consolidating teams to ensure consistency of experience. The business stabilised during the year after a challenging 2016, and we now have a good base to grow.

Managed IT solution's acquisition of Smartschools will further consolidate a good market position in the Education sector. We also secured a new contract with Ormiston Academy Trust, and extended existing contracts with key clients including ENNI and Viridian.

Network solutions

Our network solutions business, strengthened after our Updata acquisition in 2014, is growing market share and increasingly competing against the larger network providers. A good performance continued in network solutions, including winning the Transport for London networks and National Air Traffic Services contracts at the end of 2017. We were also one of the first operators to be confirmed as Stage 1 compliant on the new Health and Social Care Network (HSCN) which will replace N3, giving a significant competitive advantage in the health marketplace where ITS already has significant market share.

We were also awarded the Advanced Network Monitoring contract for HSCN. The voice business saw a number of net new wins within the public sector, whilst market share in the Scottish public sector continues to grow on the back of our SWAN contract. In the wireless LAN space, trading as Pervasive, we were again named Aruba HPE's biggest partner.

Technology solutions

Our hardware reselling business, technology solutions, is focused supply, selection, delivery and integration of IT hardware and infrastructure – from desktops and laptops through to printers, networks and telephony to clients in both public and private sectors. Its licensing division is one of the country's leading Microsoft partners, and through this team is able to deliver business intelligence, data management and analytics solutions. Technology solutions also offers security, governance and assurance services through its Professional Services division.

After challenging trading in the second half of 2016, and restructure in the early part of the year, there has been a renewed focus on the business in the second half, and the appointment of a new MD to head up a consolidated Trustmarque, Computerland and S3 business has yielded results. Performance in the business improved but there is still a sizeable opportunity for building consultancy services. Security remains a significant concern for our clients; security will move from a standalone product to an integral part of any IT strategy, with customer education forming a key opportunity.

1 UK Software and IT Services Rankings 2017, Techmarketview, June 2017.
2 UK Software and IT Services Market Trends & Forecasts, Techmarketview, June 2017.

INTERNAL CONTROL AND RISK MANAGEMENT

RISK MANAGEMENT IN CAPITA

Capita operates a business wide Risk Management Framework to allow management to identify and act on risks that are beyond tolerance.

Our announcement on 31 January 2018, which included an update on Capita's trading outlook, indicates there has been a weakness in the accurate forecasting and assessment of financial risks that developed during late 2017 through to January 2018 in that framework. Changes in the external environment – market, political and technological – had been recognised but the speed and impact of those during that period also did not translate adequately through the risk management framework. In addition, our new Chief Executive Officer, Jon Lewis, and the Board believed that a fundamental shift to longer-term strategic planning is required. As described in other parts of the Annual Report and Accounts, we will also invest in people, sales and our transformation plan for the long-term benefit of the Group. As a result of these factors, the update on the 2018 outlook following the completion of the budgeting process highlighted a lower expected Group's underlying pre-tax profits than initially predicted.

The Board will review the learnings from 2017 and early 2018 and act to make the required changes. The Board recognises that no system of risk management can guarantee the complete elimination of unforeseen matters arising due to external factors outside it's control. Work to improve the management of key risks had already commenced during the second half of 2017, and will continue in 2018 under the transformation plan. These include the upgrade of our financial systems, processes and controls, the introduction of improved Monthly Performance Reviews to better track a range of financial, operational and conduct metrics; development of clearer business and divisional financial KPIs; a new contract review process for new business and more robust delivery governance around critical and complex projects. The recent shift to a five-year planning range will enable more effective tracking of risks to strategy and is an important change and cultural shift across the Company.

It is accepted that whilst the existing Group-wide Risk Framework (the Framework) provides an appropriate basis for identifying *and managing key operational and compliance* risks, the main weakness was that not all risks (including strategic and financial) were equally measured (as described above). During 2018, to address the need for improvement, we will use the work being undertaken as part of the finance organisation change programme to design more robust financial management controls around the financial risk management process and seek to develop further our insight into this area.

In tandem, we will take further steps to develop more advanced methods to seek assurance from management on their control effectiveness. Whilst we operate second and third line control functions (see below), progressing the risk maturity of every business unit will support the continuance of a strong control environment. One further area the Audit and Risk Committee has challenged management with is the requirement to develop a more formal Risk Control Self-Assessment process which we will look to put in place in 2018. This will underline management's responsibility and provide greater line of sight for the Committee as to the state of key control frameworks.

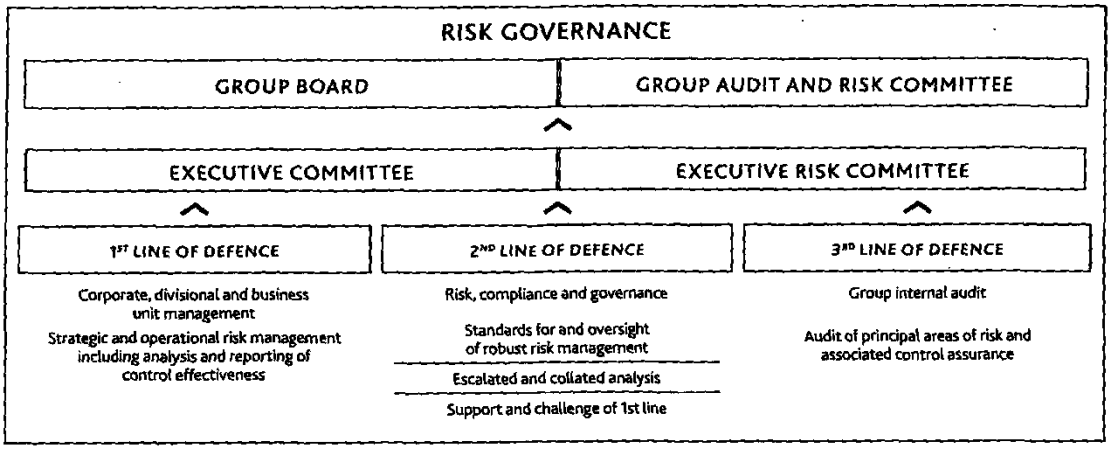
OUR CURRENT APPROACH

Capita seeks to embed effective risk management through the application of a '3 Lines of Defence' model to manage and mitigate risks and assure preventative controls. The Framework is maintained by the Group Risk & Compliance function. The Framework sets out Capita's risk management and internal control requirements, which are assured, implemented and operated by corporate, divisional and business unit management who have primary accountability for the strategic and operational risk management including analysis and reporting of control effectiveness.

1st line of defence

Each division operates its own Risk Committee to identify the inherent risks to its business or contracts, and the potential causes and impact, and then considers the related preventative controls to mitigate the risk to an acceptable residual level. The outputs from residual risks are reported by each division and aggregated for consideration by the Executive Risk Committee.

It is the responsibility of divisional management to monitor the contrast between the Board's risk appetite (the degree of risk the business is prepared to accept in the pursuit of its objectives) and the residual risks identified in any one business or contract. This in turn then acts as a catalyst for action, where required, to bring any 'uncomfortable' or 'critical' risk back into tolerance (see chart on next page).



2nd line of defence

The Group Risk & Compliance function has unrestricted access to all corporate, divisional and business unit management. It provides support as well as rigorous challenge to the 1st line of defence. In addition to maintaining standards for and providing oversight of robust risk management, this function also works to articulate the Board's risk appetite in its key mandatory policies and oversees the operational incident reporting and investigation process which both assists business to deal with operational incidents and ensures the learning from those is fed back into operational risk measurement and improvement. This function also undertakes major investigations, such as that requested by the Board following allegations in the press around the conduct of our TV Licence Field Visiting Officers early in 2017.

3rd line of defence

Further assurance is provided by the Group Internal Audit function, which independently reports to the Audit and Risk Committee on the controls in place in the business as well as the management's awareness and responsiveness to risk with more focus placed on principal areas of risk. The Group Internal Audit function also has complete access to all parts of Capita and the Head of Internal Audit has regular meetings with the Chair of the Audit and Risk Committee and members of the Board.

The Board is ultimately responsible for the management of the risks that face Capita. The Framework and associated appetite is reviewed annually by the Board but significant risks can be introduced or flexed into focus at any time. For example, during 2017 the operational IT issues which emerged during the year were incorporated into the framework and in 2018 we will now include the transformation plan risk which our recovery programmes will raise.

The Executive Risk Committee (which was formed in December 2017 after the sale of the Capita Asset Services businesses, by combining the separate Financial Services and Non-Financial Services Risk Committees) has the oversight of Capita's overall residual risks. This in turn reports the residual position with Executive narrative onto the Audit and Risk Committee to allow the Board full insight over the Corporate risk profile and material issues.

The whole risk management process is overseen by the Audit and Risk Committee. They approve both Group Internal Audit and Group Risk & Compliance's annual plans and in turn are provided with regular updates on progress throughout the year, with regular reports on findings, issues, risk incidents and themes for their attention.

INTERNAL CONTROL AND RISK MANAGEMENT CONTINUED

PRINCIPAL RISKS

Our Risk Framework is based around 22 risk categories against which our businesses measure their risk exposure and report on incidents and issues.

PRINCIPAL RISK CATEGORIES

Our Risk Framework is based around 22 risk categories against which our businesses measure their risk exposure and report on incidents and issues. The 'critical' risk exposures from this level are reported directly to the Audit and Risk Committee to provide direct line of sight, even if the risk exposures themselves are not 'material' at Group level. To provide more focused detail on the risks that may impact the strategic objectives of Capita, the Board has defined 13 corporate risks (into which are mapped each of the 22 wider risks) and these are reported on at every Executive Risk Committee and then on to the Audit and Risk Committee. These corporate risks represent the principal risks to the objectives of Capita plc. Of these, five Principal Risks are recognised as having the ability to cause significant damage to Capita's value in the event they crystallise in a severe, rapid and uncontrolled manner. These are:

- a significant failure in systems and controls;
- a lack of financial stability;
- a significant failure in information security controls;
- a major disruption to our operational IT; and
- significant legal/regulatory actions.

The remaining eight Principal Risks tend to cause issues over a longer term and hence may have an impact on profitability. These are:

- a failure to meet financial expectations;
- a failure to innovate;
- the impact of business complexity;
- the impact of political/client strategy risk;
- the impact of reputational risk;
- ineffective talent management;
- inadequate acquisition, contracting and delivery management; and
- a failure to deliver the planned transformation plan.

OUR PRINCIPAL RISK OUTLOOK

Capita is not risk averse, but it seeks to better oversee and manage those Principal Risk exposures which arise in the pursuit of its objectives.

CURRENT ASSESSMENT OF PRINCIPAL RISKS

IMAGE REMOVED

During 2017, we have seen emerging risks around the challenges in our diverse IT estate and greater regulatory and legal pressures with the introduction of General Data Protection Regulation (GDPR) and new Tax Evasion legislation. The finalisation of the FCA investigation into the historic operation of the Connaught Fund crystallised a long standing regulatory risk.

In addition, the Audit and Risk Committee has increased its focus on these key operational risks, seeking better information on the levels of risk exposure and, importantly, testing the robustness of management plans to mitigate exposures that are deemed out of tolerance. This includes more in-depth reviews of the level of IT resilience across Capita and the arrangements for managing disruptive events through Business Continuity/Disaster Recovery planning. Further focus was also taken on the arrangements to meet key regulatory changes such as the new EU Anti-Money Laundering Directive and GDPR.

Transformation risk is also identified as one of the principal risks and uncertainties which the Board will focus on in 2018. It is critical that the business successfully delivers the benefits of this plan put in place.

Notwithstanding these steps which we are taking, Capita will continue to have notable residual risk exposures in key risk areas. A number are linked to our recovery plans and will be monitored by the Board closely including:

- Financial stability – until the Rights Issue announced in 2018 is successfully completed, Capita will carry significant financial risk.
- Strategy – the failure to develop and agree on a clear and sustainable strategy could weaken the confidence of investors and threaten the future growth prospects of the Company.
- Transformation plan – the failure to deliver the planned transformation of the business would threaten future growth and success.
- Cost competitiveness – without matching our cost base to match industry peers, our ability to strengthen profitability will be impacted.

In addition to these recovery risks, there are further risks which the Board will continue to assess as to whether the risk/reward profile of the impacted businesses/services is acceptable and in our shareholders' interest. Where it feels that the residual risk is incompatible with our stated strategy and attractiveness of the returns available, the Board will take action to reduce or remove its exposure accordingly.

The risk areas of notable residual risk which Capita will carry are:

- Business complexity – Capita has grown rapidly through acquisitions and contract wins. Poor integration discipline has created undue complexity and cost as well as less than optimal delivery outcomes in some areas.
- Regulatory risk – the provision of services to and in the regulated Financial Services sector in the UK & Ireland.
- Information security risk – given we are a data-led organisation, we have stewardship over significant amounts of personal and commercial data.
- Operational IT risk – where the pace of change in technology across a diverse estate can lead to complexities, risk and adverse outcomes in any cases of major failure.
- Reputational risk – outsourcing is increasingly facing a more hostile reputational profile, particularly in the public sector.
- Political risk – the changing view of public sector outsourcing and complexities of balancing the transformation challenges in this sector with the contractual requirements being delivered out of government. Also the ongoing uncertainty over the final shape of the UK's trading relationship with the EU after Brexit.

EMERGING RISKS: CYBER ATTACKS

Ongoing cyber attacks on major institutions have continued throughout 2017 in various forms.

The 'Wannacry' attack, which particularly impacted NHS systems in the UK, was a good example of an attack whose primary purpose was not to steal personal data but to extract a ransom. Capita fully recognises the cyber threat and that the threats are various and increasing. The Board has taken focused interest in how our businesses and our systems are responding to these threats, including the operation of a dedicated oversight committee which reports to the Audit and Risk Committee. We operate a network of information security specialists across the Group which liaise with our businesses, clients and IT providers to maintain robust preventative and detective information security controls. Also, we work with partner organisations and HM Government agencies to help protect the key parts of the national information infrastructure with which we are entrusted.

EMERGING RISKS: GENERAL DATA PROTECTION REGULATION

As an organisation which has data in the heart of what we do, compliance with the EU General Data Protection Regulation (GDPR) is a significant risk issue for Capita.

There are several new requirements within this regulation which comes into force in May 2018. They include (for Data Controllers) the necessity to notify the UK Supervisory Authority (ICO) and, in some circumstances, individuals concerned, of personal data breaches. Up until now, most businesses would only have notified the ICO at their own discretion albeit that the ICO has encouraged the reporting of serious breaches. This exposes all businesses, including Capita, to the risk of reputational damage, fines and orders to pay compensation to the individuals concerned. Fines for instances of non-compliance have increased to between 2% and 4% of annual turnover depending upon the breach (or EUR10m or EUR20m whichever is the higher amount). To ensure our businesses meet the new requirements, we have a Capita-wide GDPR project underway with Executive Sponsorship. The project is led by the Data Privacy team which writes the key policies and procedures, defines the key objectives leaving the divisions to execute into their own businesses. Each division has its own project team to drive GDPR compliance providing regular reporting to our Group Steering Committee.

Work is progressing, focused upon key streams which include privacy notices, breach reporting, staff awareness, commercials and information asset registers.

INTERNAL CONTROL AND RISK MANAGEMENT CONTINUED

OPERATIONAL RISK

1 SIGNIFICANT FAILURES IN INTERNAL SYSTEMS OF CONTROL

Description	2017 developments and outlook
A material failure in the control frameworks around our business processes which results in operational incidents, causing unanticipated and significant financial loss or service detriment to our clients or end customers.	Capita operates control frameworks designed to minimise the risk of unanticipated operational failure, financial loss or damage to our reputation. Our overall assessment is that the risk has increased, due to the need to develop further our corporate risk framework (see above), strengthen the business' own attestation of controls and issues in the consistency of Business Continuity/Disaster Recovery controls identified during the year. During 2017, we have also experienced two unconnected frauds which, whilst not material in quantum to the Company, have identified control weaknesses in the businesses affected. These are both continuing to be investigated.

2 FAILURES IN INFORMATION SECURITY CONTROLS

Description	2017 developments and outlook
The appropriate protection of Capita's customer and corporate data is not only subject to greater legislative scrutiny, it is central to services we provide and any significant failures in this could lead to material costs, damage to our reputation and loss of trust from our clients. A significant breach of security could impact Capita's ability to operate and deliver against its business objectives.	Capita employs detailed and extensive controls to secure its information assets. These include, but are not limited to, physical and logical access controls, appropriate encryption of data and communications and raising and maintaining employee awareness of the threats. The 'cyber-threat' landscape is widening and Capita, like many businesses has been exposed to incidents during 2017 such as the APT10 and 'wannacry' ransomware attacks. Whilst neither caused significant impact, this enhanced inherent risk together with a need to continually develop our control framework means this remains an increasing corporate risk. Board oversight in this area operates through the Group Security Risk Committee which has considered our plans to improve staff training awareness, enhance our threat awareness capability, invest in new technology and manage our data retention effectively during 2017. We are actively preparing for the introduction of GDPR in May 2018 given this raises our inherent information security risk. Additional investment is planned through 2018 to strengthen our information security control framework in tandem with the GDPR work.

3 INCREASED BUSINESS COMPLEXITY

Description	2017 developments and outlook
The opportunity cost of a complex business structure and issues caused by a lack of strategic focus can weaken our ability to exploit market potential. This in turn threatens shareholder returns and value. In addition, any failure to manage multiple complex contract requirements effectively can mean contract benefits may not be fully realised, service delivery costs may increase, or activities do not perform in line with expectations.	Even with our divisional restructure at the start of 2017, Capita had exposure to an overly diverse set of markets and sectors. Jon Lewis has noted this led to the business being potentially too widely spread, making it more challenging to maintain a competitive advantage in every business and to deliver world class services to our clients every time. The CEO review details the plan to address this and bring strategic focus to our services and target markets. Until that is delivered, Capita will continue to have an uncomfortable exposure to a number of markets where we have not or cannot economically achieve scale. In respect to complex contracts, Capita is not averse to seeking major contracts with inherent complexity. But these come with inherent risk which must be managed and during 2017 the NHS PCSE transformation continued to prove challenging for Capita. In this case, actions have been taken to react to any shortfalls to client expectations, but the work required has been greater than expected at the outset. 2017 has seen the introduction of a new initiative to better assess the levels of complexity and how best to address the 'unknowns' in these complex transformation contracts, but the issues with the historic portfolio are receiving remedial action as required.

4 OPERATIONAL IT RISK

Description	2017 developments and outlook
Capita is a technology-driven services company in that the majority of our products and services are enabled by a resilient technical infrastructure. A disruptive failure in Capita's key systems infrastructure could lead to a failure of adequate service to our clients. In turn that means we may not meet contractual obligations, cause detriment for end customers and lead to consequent financial penalties and potential regulatory action.	During 2017, our systems have experienced isolated instances of short but significant impact on IT operational stability. These occurred in one of our legacy datacentres. The Board commissioned a review into this incident, which did disrupt some services to clients over a limited period. It concluded that historic investments to maintain service failed to fully address all of the technical risks this legacy infrastructure contains. This has required increased focus to address throughout 2017 and led this to assume a critical risk in our reporting, but which is now subject to remediation plans which we expect to see the residual risk to reduce through Q2 2018. The Board approved an immediate programme of remedial works and has sought to accelerate its consideration of a new IT strategy for its datacentre estate. Board and Audit and Risk Committee meetings have prioritised reports and reviews on this matter through the second half of 2017. The conclusion of the strategy work will set a blueprint for the investment Capita will make to deliver a more robust and secure IT infrastructure and data network during 2018, which will support our growth and more resiliently maintain service for existing clients.

Residual risk rating:
Increasing | Decreasing | Stable | V Viability statement

OPERATIONAL RISK CONTINUED

5 FAILURE TO EFFECTIVELY MANAGE TALENT AND HUMAN RESOURCES

Description	2017 developments and outlook
Failure to attract or retain the right people would limit Capita's ability to deliver its business plan commitments and continue to grow. KPI Employee retention SEE PAGES 23–24 FOR FURTHER INFORMATION ON OUR PEOPLE AND TALENT	Capita is a people business. The availability and competency of the right talent is critical to Capita's ability to meet the needs of its stakeholders and achieve its goals as a business. During 2017, Senior Talent attrition has been uncomfortable given the uncertainty which has arisen during this transitional phase. Organisation restructuring, cost efficiency and productivity initiatives and uncertainty over performance bonuses have impacted this group of employees. Therefore, supporting future talent development and retention continues to be a Board priority. The Board recruited a senior and experienced Talent Director in 2017 to recognise the investment we see as necessary in this field and they are further bolstering their resource in this area. This new focus offers us the opportunity to validate and endorse our existing initiatives such as our well regarded 'Lead the Way' Graduate scheme and introduce our new 'Talent Hub'. This aims to do a better job of recognising and promoting our talent from within, showcasing roles and opportunities across the business, thus promoting internal mobility and aiding retention. There has also been greater focus on the development of clearly defined Capita 'Leadership Principles' which will shape further initiatives during 2018 to strengthen our existing senior management team and offer guiding points for those who aspire to progress to that level. The new Chief Executive Officer has expressed a priority in providing career opportunities for talented people and plans significant work during 2018 to achieve this. A Chief People Officer has been appointed to lead this work joining Capita in April 2018. See pages 23–24 for further information on our people and talent.

6 WEAKNESSES IN ACQUISITION AND CONTRACTING LIFE CYCLE

Description	2017 developments and outlook
Capita acquisitions and client contracting fail to generate anticipated revenue growth, synergies and/or cost savings.	During the year, we have been able to reflect on the efficacy of our acquisition and integration processes. There have been a few isolated examples where incomplete integration has caused consequent risk around performance and systems and controls in these businesses. We recognise that the speed of integration and desire to derive the full financial benefit of any acquisition has, at times, led to certain steps not being prioritised. Some of these are unavoidable, such as trying to implement our UK-based mandatory policies in differing jurisdictions, others are not, such as moving acquired companies to our core financial platforms in a timely manner. As mentioned above (Internal business complexity), complex transformations that have come with some new contracts have also proved challenging in 2017. We have enhanced a number of key processes in this area during the year. First, we have revisited and refreshed our Bids & Acquisition policies to better focus our due diligence processes and will shortly be introducing a new Contract Review Committee. Second, we have created a new approach which sees transformation expertise embedded in the bidding teams earlier on in the process, reporting separately on the robustness of any plans and costs prior to contract signature. Third, we have introduced a new process to guide acquisitions through the first year of Capita ownership, to ensure the accountability and transparency that an effective integration process requires. However, we believe further work will need to be undertaken to embed these and consider other actions to manage this risk.

COMPLIANCE RISK

7 LEGAL/REGULATORY RISK

Description	2017 developments and outlook
Capita plc is subject to regulation primarily under UK legislation. The regimes which apply to its business include, but are not limited to: financial services, communication services, and energy market. Capita is also subject to generally applicable legislation including, but not limited to: anti-bribery, consumer protection, data protection and taxation. Failure to adhere to any of its legal and regulatory requirements could lead to legal and regulatory sanctions, redress costs, reputational risk and, ultimately, loss of licence or barring from contracts.	During 2017, Capita closed out a number of historical legal and regulatory issues. This included material litigation with The Co-operative Bank and litigation in our Corporate Services business in Capita Asset Services. In November, the Financial Conduct Authority (FCA) announced that it reached final settlement with Capita Financial Managers, a subsidiary of Capita Asset Services, in respect of historical issues arising from the operation of the Connaught Income Series 1 Fund during 2008-2009. The closure of these material cases and the disposal of the regulated businesses within Capita Asset Services has reduced the risk profile in this area. However, we recognise that our continued ability to operate and compete effectively can be impacted adversely by new legislation, policies or regulations. We work to identify and address our regulatory obligations and to respond to emerging requirements. We see that there continues to be a continued appetite by jurisdictions within which we operate to increase requirements on what we call 'Corporate Conduct'. These can be loosely defined as developing legal requirements and sanctions that are worded to bring the corporate into an increased risk of action for its conduct and at times open it to criminal proceedings. For 2017, significant work has been undertaken to position ourselves for the implementation of the GDPR, the Criminal Finances Act (introducing a criminal offence of facilitating tax evasion) and the Prevention of Modern Slavery Act. Working in highly-regulated sectors does mean a higher level of risk for Capita. The steps outlined above help manage that risk but, as noted in the introduction to this section, the Board will continually review the risks and rewards which each sector and jurisdiction brings to the overall business.

Residual risk rating:
Increasing | Decreasing | Stable | Viability statement

INTERNAL CONTROL AND RISK MANAGEMENT CONTINUED

FINANCIAL RISK

8 FAILURE TO MEET FINANCIAL EXPECTATIONS

Description	2017 developments and outlook
Adverse performance against our stated business plans undermines investor confidence and impacts the wider corporate position. Lower revenues and profits can also erode our corporate position in the market and weaken our ability to attract and retain the best talent. KPI Underlying profit before tax KPI Underlying operating margin KPI Underlying earnings per share SEE CHIEF FINANCIAL OFFICER'S REVIEW FOR MORE INFORMATION	The lower than predicted performance in 2016 indicated that the forecasting processes used within the businesses were in need of refresh and the management discipline in their execution required refocusing. There has been much work carried out during 2017 to improve transparency of key financial metrics across the businesses. However, the update on the trading outlook in January 2018 revealed that further improvements to the existing risk management framework and system are required. The faster than anticipated speed in the crystallisation of financial risks during late 2017 through to January 2018 highlighted that there has been a weakness in the accuracy of forecasting and translation of financial risks in the existing framework. Furthermore, the key strategic decisions made by the Board, particularly around investing in our people, sales and our transformation plan for the long-term benefit of the Group has also contributed to the lower expected Group's underlying pre-tax profits than initially predicted in December 2017. An immediate learning point was that not all key financial risks were tracked and measured in a disciplined manner, and more focus was given on strategic and operational risks. Nonetheless, work had already been underway to improve the robustness of the risk management framework and system, which include the upgrade of our financial systems, processes and controls, introduction of Monthly Performance Reviews, clearer financial KPIs at business and divisional levels, a new Contract Review process for new business, more robust delivery governance on critical and complex projects, and a shift to a five-year planning range. We will continue to work on these areas in 2018. In addition, we will ensure that all risks are equally measured and we will strengthen the financial management controls around the financial risk management process. We will also ensure that more onus is placed on the business unit owners by developing a more formal Risk Control Self-Assessment process and obtaining further assurance on their control effectiveness.

9 LACK OF CORPORATE FINANCIAL STABILITY

Description	2017 developments and outlook
The effective management of its financial exposures and access to finance is central to preserving Capita's profitability and investors' confidence; the absence of it would also impact our growth plans. KPI Gearing – Net debt: EBITDA	Following the deterioration in Capita's financial performance during 2016, we sold the Capita Asset Services businesses, focused on expenses and cash management so as to return the adjusted net debt: adjusted EBITDA ratio back into Capita's then medium-term target ratio of 2.0 times to 2.5 times. However, the new CEO, Jon Lewis, and the Board believe that a fundamental shift to longer-term strategic planning is required. As part of the new strategy launched, we have set a target range for leverage of 1.0x to 2.0x adjusted net debt to adjusted EBITDA ratio. The transformation plan, which encompasses strategy implementation, cost competitiveness, capital structure, targeted investment, organisational alignment and re-igniting sales, has been put in place to execute the new strategy. In the shorter term, our leverage will be reduced by the net proceeds of the Rights Issue and by non-core disposals.

STRATEGIC RISK

10 FAILURE TO INNOVATE

Description	2017 developments and outlook
The failure to identify emerging trends, developing consequent strategies and making the most of market opportunities would impact the long-term profitability of Capita. Major macroeconomic trends in key industries as well as technological developments like robotics and automation need to be fully understood and harnessed to deliver the growth to which we aspire.	Capita has always had technology at the heart of the solutions it offers its clients, but the rate of change in areas like robotics and automation requires greater investment and focus. We have set up an 'automation centre of excellence' and built out a central technological solutions team. We have recognised that we gain more through specialisation and therefore seek suitable external technology partners rather than try and develop in-house. However, our financial position has not allowed us to respond fast enough to shifting markets and technological change and to keep us at the forefront of our markets. There is still much to do to re-ignite our innovative edge as we are uncomfortable with our current position. We need to be consistently better at tracking the success of the initiatives outlined above and ensure where Capita businesses have demonstrated market leading innovation, we are better at sharing that best practice across the business and replicating success. In addition, we need to be more innovative in our contractual dealings with clients, both private and public, as expectations of business services providers change in our core markets.

Residual risk rating:
Increasing | Decreasing | Stable | V Viability statement

STRATEGIC RISK CONTINUED

11 ADVERSE CHANGES IN NATIONAL, INTERNATIONAL POLITICAL LANDSCAPE

Description	2017 developments and outlook
The political risks associated with operating across a broad number of jurisdictions and markets can affect Capita's ability to manage or retain interests in its business activities and could have a material adverse effect on the profitability, or, in extreme cases, viability of one or more of its services.	This is an increasing area of risk which the Board recognises requires careful analysis and action. The UK political landscape continues to be volatile, a situation which the 2017 General Election has clearly not remedied. This political environment will continue to impact our public-sector pipeline as well as our dealings with central government clients on existing contracts. We recognise that some in the political spectrum do not favour private involvement in the provision of public services. We believe that the best defence to this argument is the consistent delivery of cost and quality effective contracts to central and local government. Until the final deal emerges on Brexit, we believe this topic will lead to continued drag on our trading as clients themselves seek to delay potential longer-term investment and purchasing decisions. There will also be impacts on the limited number of Capita businesses using Financial Services passports and the make-up of the labour market we source our talent from. The impact of political risk is managed through maintaining a spread of operating sectors and markets, continuous monitoring of key UK and international policies, and dialogue with Government departments and trade associations. Changes in our strategy will likely cause a review of our activities in this area and lead to an increase in our participation in such fora. During 2018, Capita will continue to track the formation of the political and associated settlement of how the UK exits the EU. We are also considering how our remaining EU businesses (such as those in Ireland, Germany and Poland) can leverage the opportunity.

12 OPERATIONAL ISSUES LEADING TO REPUTATIONAL RISK

Description	2017 developments and outlook
Capita's reputation, and that of our clients, could be damaged by a significant adverse event leading to a loss of trust and confidence amongst our stakeholders. The diversity of our markets and clients can widen that risk and the increased use of social media alongside traditional media to highlight and promote grievances and issues is appreciated by Capita.	2017 has seen a number of significant issues such as press concerns about TV Licensing's officers' conduct, the efficacy of the NHS PCSE contract and ongoing criticism about elements of the DWP PIP contract delivery. These have been managed proactively together with the clients who we work in tandem with to address any legitimate concerns and present factual responses to any comment. This has been aided by the close links between business units and our Press Office, a willingness, where necessary, to undertake further investigation into legitimate issues and remedy where these are proven. Management, PR and Group Risk & Compliance work to identify and address issues as they are raised. The residual level of reputational risk has increased and it has moved to a point which is at the limit of our previously agreed tolerances. To address this in 2018, the Board expects that it will take more active steps to balance the degree to which there is acceptable reputational risk consistent with the financial returns on offer in new contracts.

13 TRANSFORMATION RISK

NEW

Description	2017 developments and outlook
The transformation plan announced by Jon Lewis, Chief Executive Officer, on 31 January 2018 will, as described earlier in the report, reshape the Company to address the known challenges. Given the importance of this and early stages of the work, we have marked this as 'uncomfortable' until we have greater visibility to its progress and execution.	The key elements of the transformation plan were identified in late 2017 with the appointment of a Chief Transformation Officer but the bulk of the detailed planning and execution will unfold during 2018.

Residual risk rating:
Increasing | Decreasing | Stable | Viability statement

VIABILITY STATEMENT

The Board has undertaken a rigorous assessment of the going concern assumption using the base-case financial forecasts and considering a wide range of downside scenarios.

The transformation plan is being finalised, and the key actions and forecast impacts incorporated into detailed business plans in support of the new strategy that has been reviewed and approved by the Board. These business plans cover a five-year outlook and encompass the full benefits that the Board is confident the transformation plan will deliver.

The base-case projections prepared for the going concern and viability assessment are derived from the business plans, but are necessarily more cautious as they do not include the impacts that are outside the control of the Company. Accordingly, they exclude future planned strategic disposals where external third parties will be involved and also exclude the disposal proceeds that will be available for re-investment. In addition, the base-case projections incorporate a cautious assessment of business prospects for 2019 and 2020 with only an initial view over cost efficiencies identified to date.

For the going concern assessment the Board have considered the base-case projections for the period to 31 December 2019. Provision C.2.2 of the 2014 revised Code requires the Directors to also consider the viability of the Group over a longer-term period and for this viability statement the Board has assessed the prospects for the Group using the base-case forecasts over an extended period to 31 December 2020. The Board considers this three-year period to be appropriate as there is sufficient clarity to consider the business prospects and the base case over this period provides a foundation to stress test against severe but plausible downside scenarios.

The Board acknowledges that the base case includes only an initial view of the cost efficiencies identified to date and by covering only the first three years is necessarily cautious with regard to the full benefits that will be delivered over the longer term and does not include the positive impacts the plan will have on the longer-term strategic positioning of the Group across the markets that it serves.

In assessing the going concern assumption, the Board has undertaken a rigorous assessment of the forecast outturns and assessed identified downside risks on a probability weighted basis and mitigating actions. The downside risks include a number of severe but plausible scenarios, also on a probability weighted basis, incorporating underperformance against the business plan, execution risk associated with the transformation plan, unexpected cash outflows and customer attrition and unwillingness to award the Group new contracts and extensions to existing arrangements. These financial downsides (SCENARIO 1) capture political, economic and reputation risks.

In considering the viability of the Group, the Board has extended the above financial downside scenarios to include stress testing and sensitivity analysis of the impact of various severe but plausible potential scenarios involving the threats posed by other principal risks. These have included (but not limited to) scenarios in respect of:

SCENARIO 2: an information security breach – an accidental significant loss of data or release of a significant amount of sensitive personal client data. The Board has considered among other items the potential impact to cash and profits arising from potential penalties and fines, compensation payments and negative impacts from such reputational damage in terms of an inability to win new business or retain existing contracts;

SCENARIO 3: legal and regulatory risks – failure of financial crime controls around AML assessment, due diligence and sanction assessment leading to a significant AML incident and investigation. The Board has considered among other items potential fines, and any actions taken that may prohibit or suspend the Group from operating within certain regimes;

SCENARIO 4: the efficacy of IT and infrastructure systems and controls – a significant IT incident causes failure to key systems for hosted services to major clients. The Board has considered among other items any contractual penalties that may arise, capital costs required to address any immediate infrastructure improvements, potential contract terminations and the negative impact on new contract wins; and

SCENARIO 5: a wider economic impact on Group financial stability – uncertainty of earnings as a result of a change in the UK Government to a party with a strong mandate for radical policy change. The Board has considered among other items new barriers to entry, changes to corporate taxation, and the termination of public sector contracts.

The Board has conducted stress tests against each individual scenario in order to test the resilience of the Group taking into account the efficacy of possible mitigating actions.

In addition to testing individual scenarios, the Board also considered the impact of a combination of the scenarios over the assessment period. This was in order to stress test an aggregation of severe but plausible risks occurring that would represent the greatest potential financial impact but in the short terms and longer-term viability period.

The Directors considered mitigating factors that could be employed when reviewing these scenarios and the effectiveness of the actions at their disposal, which were applied to the models. An example of the actions identified included adjusting the Group's investment in discretionary and maintenance capital projects, having due regard to the need to ensure the integrity of the Group's IT systems is not compromised nor the security of the data held therein; the reversal of the unwinding of the seasonal working capital assumed in 2018; and further reduction in discretionary operating expenditure.

Notwithstanding the actions available, the Directors concluded that the downside scenarios indicate that absent the anticipated net proceeds from the announced rights issue the available headroom is not sufficient to operate within the Company's key adjusted net debt to adjusted EBITDA covenant test. The Board has therefore considered the Rights Issue net proceeds in its assessment of viability.

As set out on page 98 the Rights Issue is subject to a shareholder vote, and the arrangement to the underwriting is subject to certain specific conditions, which are customary in nature but are outside the control of the Company. These events and conditions indicate a material uncertainty on the completion of the Rights Issue which may cast significant doubt about the Group's and parent company's ability to continue as a viable concern.

The Board is confident that the Rights Issue will be approved and subject to the inclusion of the anticipated net proceeds the Directors therefore have a reasonable expectation that the Group and parent company will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment.

On behalf of the Board:

Jon Lewis
Chief Executive Officer
Nick Greatorex
Chief Financial Officer
23 April 2018

MANAGING OUR BUSINESS RESPONSIBLY

During a difficult year for Capita, we remained focused on working in a way which is sustainable and ethical and has a positive social, environmental and economic impact on society.

CORPORATE RESPONSIBILITY

We do this by embedding responsible business practices at the heart of everything we do through our own community and environmental programmes and through the services and products we deliver. We touch the lives of millions of people and we understand that we can have a bigger impact by working collaboratively with partners to amplify what we do internally and working collaboratively with our clients to support their corporate responsibility agendas.

Our approach to corporate responsibility (CR) is determined by our stakeholders' view on the sustainable issues that they see as important for us as a business to be addressing and influencing, either through our own operations or by working collaboratively with clients. We address these issues through four priority areas:

- Delivering sustainable value for our clients ensures that as a business we put our clients and their customers first, developing services and products that meet their needs, improving their operational performance and are accessible to all people as well as working collaboratively with our clients to tackle their sustainable issues.
- Our people and culture addresses the issue that we must respect and nurture our workforce ensuring diversity, health, safety, wellbeing and training and development opportunities.
- Community investment ensures we address socio-economic issues by investing and engaging in our local communities.
- Responsible business practices helps us to address the issue of a diminishing public trust in business, ensuring we have robust governance in place and operate ethically with respect to the environment.

We have set commitments against each of these priority areas, using relevant metrics to measure and report our progress annually. For information on our commitments, please visit www.capita.com/responsibilty.

OUR FOUR PRIORITY FOCUS AREAS

1 DELIVERING SUSTAINABLE VALUE FOR OUR CLIENTS

Ensures that as a business we put our clients and their customers first, developing services and products that meet their needs

SEE PAGE 46

2 OUR PEOPLE AND CULTURE

Addresses the issue that we must respect and nurture our workforce

SEE PAGE 46

3 COMMUNITY INVESTMENT

Ensures we address socio-economic issues

SEE PAGE 46

4 RESPONSIBLE BUSINESS PRACTICES

Helps us to address the issue of a diminishing public trust in business

SEE PAGE 47

GOVERNANCE

Accountability for CR sits with our CR Steering Committee who report annually to the Board on progress against our strategy and commitments.

Our CR Steering Committee is chaired by Nick Greatorex, Chief Financial Officer, who has overall responsibility for our strategy. The Committee comprises functional heads from procurement, risk and compliance, human resources, health, safety and environment, company secretariat and corporate responsibility, who provide oversight and challenge of our strategy as well as being responsible for implementing our strategy, developing appropriate policies, providing guidance and sharing best practice with the business, as well as reporting progress to the Committee.

The Committee met twice in 2017 for a general update on progress and to cover current topics of focus, including our Ethical Code Statement, our corporate charity partnership with Alzheimer's Society, our continued efforts to reduce the risk of modern slavery in our supply chain and our approach to creating a more inclusive workforce.

In 2018, due to the appointment of our new CEO, Jon Lewis, we will align our approach to corporate responsibility to our new strategy demonstrating a purpose that serves society and the environment, respects the dignity of people and thereby delivers value for our clients and generates a fair return for our investors.

MANAGING OUR BUSINESS RESPONSIBLY CONTINUED

DELIVERING SUSTAINABLE VALUE FOR OUR CLIENTS

Our products and services touch the lives of millions of people and we understand that by working collaboratively with our clients to tackle socio-economic issues relevant to their organisation, we can deliver a wider social, environmental and economic impact.

Through our contract with the London Borough of Lambeth, we have delivered a potential wider social value of £2.5m-£3m, placing 102 Lambeth residents in apprenticeships, supporting 45 young offenders break the cycle of re-offending; delivering educational sessions to c.180 students on how to steer clear of crime and violence; supporting 43 young entrepreneurs to get their business ideas off the ground; and, raised the employability skills of 160 young people. In 2018, we will continue to share the skills of our people with young students, support young entrepreneurs and provide apprenticeship opportunities to address the priorities in the Lambeth community.

Within our 15-year partnership with North Tyneside Council we have been encouraging careers in science, technology, engineering and maths (STEM) to young people. We deliver a range of technical services to the Council including engineering, property, planning, building control and public protection and therefore our people have a wealth of knowledge when it comes to STEM subjects and career paths. We have supported the Engineering Education Scheme (EES) since 2013, a scheme which links companies with local schools giving students an insight into careers relating to STEM. We have invested £10,500 into the scheme. We also work with the Engineering Development Trust and the Institution of Civil Engineers delivering their respective Go 4 Set and Bridges to Schools projects. Over 140 students from the borough have been given hands-on civil engineering experience with some students choosing to study engineering or planning in further education.

We are at the forefront of the digital revolution unlocking value for our clients through digital transformation, data analytics, and automation. Alongside this, we understand that the rise of digital can make some products and services less accessible to people. That is why in many of our business units we support end customers to get online through volunteering. Through our West Sussex Partnership with West Sussex County Council, we delivered 'Digital Tea Parties' – afternoon workshops for the elderly teaching them how to use a computer. Previously, we have supported a scheme to help migrant women in Tower Hamlets learn how to use the internet. We ran computer skills workshops teaching attendees how to set up an email account, send emails and apply for jobs online. Volunteers from our London head office run monthly 1:1 mentoring sessions with the homeless.

As our world changes politically, environmentally and socially, we will continue to understand the socio-economic issues of importance to our clients and the communities in which we work, and develop our services ethically, responsibly and with respect for people and the environment.

OUR PEOPLE AND CULTURE

Our approximately 70,000 talented, committed and engaged employees are essential to delivering business critical services and solutions across all our markets. Their skills, knowledge, attitude and creativity ensure we continue to deliver great service and positive outcomes for our clients.

FOR MORE INFORMATION SEE OUR PEOPLE AND TALENT SECTION ON PAGES 23-24

Health, safety and employee wellbeing

We recognise that fostering a healthy, motivated workforce and safe working environment is not just the right thing to do, it's also good for business, reducing sickness absence and increasing retention rates. Our Capita-wide health and safety management system reduces the risks across our business ensuring that our people have a safe and comfortable working environment.

In 2017, our accident rate was 1.23 per 1,000 employees (2016: 1.41), showing a 13% reduction in reportable accidents.

We raise awareness of the importance of living a healthy work-life balance through campaigns like our 'Step-up Challenge' where we encourage our people to be active walking to and from work, walking to meetings or taking the stairs rather than the lift. We provide opportunities for flexible working (16% of our employees are part-time) and have introduced technology to enable employees to work remotely.

COMMUNITY INVESTMENT

As a major employer, we recognise that we have a duty to contribute to the wider economy, creating jobs, using local suppliers and supporting our clients in tackling local socio-economic issues. Alongside this, we also invest and engage directly in the communities where we work and, through our centrally created programmes, we encourage our employees to volunteer and fundraise, supporting causes they care about.

This Spring, following an employee consultation, we launched our new Capita-wide charity partnership with Alzheimer's Society – a national charity whose mission is to transform the landscape of dementia forever. Through our partnership we aim to:

- make 50% of our UK employee base Dementia Friends;
- become a dementia-friendly business;
- support innovation in dementia research and initiatives; and
- raise £500,000 for the charity.

Already, 900 of our employees are Dementia Friends and we have all helped raise over £100,000 through various events including 'Cupcake Day', Snowdon Challenge and celebrating our Charity Week in the UK.

Our community investment total for 2017 is £1.9m (2016: £2.1m). This includes community investment from c.44% of Capita reflecting that even in a year of change our employees and businesses continue to support charitable causes. This investment has supported c.150 charities, ranging from healthcare to improving education.

In 2018, we will continue to encourage our employees to volunteer and support charitable causes. With Alzheimer's Society, we look forward to raising our understanding of dementia and turning this understanding into action creating a more inclusive workforce and helping us to interact and better support our clients' more vulnerable end customers.

RESPONSIBLE BUSINESS PRACTICES

The 2017 Edelman Trust Barometer[1] reveals the largest-ever drop in public trust across the institutions of government, business, media and NGOs. Of the four institutions, business is viewed as the only one that can make a difference. In fact, three out of four respondents agree a company can take actions to both increase profits and improve economic and social conditions in the community where it operates.

It is therefore paramount for businesses to act responsibly and make a difference. We help build trust by committing to conduct our business in an open, honest and transparent manner embedding responsible business practices into the way we work with clients, suppliers and the way we run our business.

Working with our suppliers

Consisting of over 31,000 suppliers, we recognise that Capita's supply chain is critical to the Company's success; the agility, speed and value we need to be competitive are founded on equitable supplier relationships.

We actively encourage supplier diversity and currently 60% of our supply base are classed as small- and medium-sized enterprises (SMEs). We monitor our payment terms and, on average, we pay SMEs within 20 days of invoice receipt (target: 30 days). The equivalent figure for non-SMEs is 32 days (target: 40 days).

For larger suppliers who supply goods or services across the Capita group, a Preferred Supplier List is maintained to encourage the use of associated contractual terms where possible. Preferred Suppliers are also highlighted on Capita's purchasing platform and employees are made aware that no further tendering is required if a Preferred Supplier is selected. The Group Procurement team is responsible for maintaining awareness of Preferred Supplier relationships across the business.

Capita's Group Procurement team work with colleagues and suppliers to ensure that all necessary due diligence checks are undertaken, utilising a new procurement solution introduced during 2017. In the year we have audited 63% of our material suppliers (those with whom we spend over £1m) (57% of spend). These checks assess suppliers' approach to human rights, data protection, modern slavery and environmental issues and are not only necessary to comply with associated legislation but are also good practice for any responsible organisation. If risks are identified, we work with suppliers to address them. Once a supplier is approved, employees are free to make contact to discuss their needs.

Protecting our information and data

We regard the fair and lawful processing and correct treatment of personal information as crucial to the success of our operations, maintaining confidence between our business and those with whom we work, including our clients.

We fully endorse and adhere to the principles of data protection as set out in our Data Protection Policy and Information Security Policy which ensure that we treat personal information correctly in accordance with the law.

Data Protection standards are led by the Central Privacy team which considers the Data Protection legislation and, more broadly, controls on who has access to personal data, who we share it with, how we use it, what we collect and finally ensuring it is safeguarded and disposed of properly when we no longer have a business need to process it.

In order to drive compliance with the General Data Protection Regulations (GDPR), we have a comprehensive programme in place. We have an established network of trained privacy professionals across the divisions providing advice and guidance on their specific GDPR compliance programmes. Together with ensuring that Capita Data Controllers are compliant with the new requirements by May 2018, they are providing expert help and assistance where we are a Data Processor for our clients.

We have appointed a Data Protection Officer. Her central team together with the privacy leads across our divisions, will ensure that privacy is high on the agenda across the Company. We have raised awareness of privacy and data protection through various initiatives including mandatory data protection training to our Think Privacy; Think Security campaign in summer 2017.

1 www.edelman.com/trust2017/

MANAGING OUR BUSINESS RESPONSIBLY CONTINUED

Managing our environmental performance

We are committed to reducing our carbon footprint which we report in terms of tonnes CO_2 equivalent (tCO_2e) and tonnes CO_2 equivalent per person. We are proud to have reduced our emissions once again this year by 11% (7% reduction in tCO_2e/headcount) from 2016. We have achieved this predominantly through our energy reduction programme in the UK portfolio, which we commenced in 2015 and has already resulted in financial savings of £1.8m. The programme has seen improvements in the way we measure, manage and monitor our energy consumption (electricity and gas). We will continue to focus on driving down our emissions from energy in 2018, as well as look at improving the way we collect data on our resources use, for example waste and water.

Bribery and corruption

We have zero tolerance for bribery and corruption. Our Anti-Bribery and Corruption Policy applies to all Capita businesses and employees. The Central Risk & Compliance team monitor compliance against this policy ensuring all businesses are aware of their responsibilities in terms of donations, facilitated payments, gifts and hospitality. All employees must complete Financial Crime training annually.

Human Rights and Modern Slavery

We are committed to respecting the human rights of our employees and those within the communities in which we work. Our Human Rights Policy details our commitments to upholding the principles of human rights as set out in the United Nations' Universal Declaration of Human Rights (UDHR) and the International Labour Organisation (ILO) core conventions on Labour Rights. Within our Modern Slavery Statement, we set out our approach to stamping out modern slavery in our operations and supply chain.

Ethical Code and whistleblowing

Our Ethical Code Statement, refreshed in 2017, sets out how we conduct business responsibly, encouraging us to work together, support our clients, deliver long-term social and environmental value and be open, transparent and law-abiding. We expect our businesses and our employees to demonstrate these commitments in their decision-making and conduct.

We recognise that some situations can be more ethically challenging than others and therefore our Open Door Policy and Speak Up Policy enables employees to challenge and report ethical concerns. Our Open Door Policy helps us to encourage a culture of active listening by supporting employees to raise any concern openly at any time in confidence.

If employees raise concerns that there may be potential criminal matters that have or are taking place, or failures in applying key Capita policies, then our Speak Up Policy requirements must be followed.

Both our open door and speak up approach encourage employees to raise concerns to their line manager or supervisor in the first instance. Employees can also report matters dealt with under our Speak Up Policy through our dedicated 'whistleblowing' channel if it would be more appropriate to raise them in this way or if a speak up matter is not being dealt with. Our Speak Up Policy also sets out that employees may also raise 'protected disclosure' concerns to external bodies such as regulatory or professional bodies covering specific industries.

For further information on our corporate responsibility approach and programmes please visit www.capita.com/responsibilty.

NOTE:
The information required to be contained in the non-financial reporting statement under section 414CA Companies Act 2006 is set out on pages 23 to 24 and 45 to 48 of this strategic report. Other relevant information is detailed in the sections on Capita's business model, key performance indicators and approach to risk management.

The Strategic report was approved by the Board on 23 April 2018 and signed on behalf of the Board

Francesca Todd
Group Company Secretary
Capita plc

CORPORATE GOVERNANCE

Chairman's report	50	Committees	64
Board members	52	Directors' remuneration report	75
Corporate governance statement	54		

IN THE DRIVING SEAT

PUTTING ŠKODA CUSTOMERS IN THE DRIVING SEAT WITHOUT LEAVING THEIR ARMCHAIRS.

IMAGE REMOVED

we are change makers

FOR MORE ABOUT OUR CHANGE MAKERS SEE CAPITA.COM/YEAR-IN-REVIEW

CHAIRMAN'S REPORT

"2017 has been a difficult year for us. Against a challenging backdrop in many of our markets, we began to address the underlying problems preventing us from achieving our full potential."

SIR IAN POWELL, CHAIRMAN

IMAGE REMOVED

I am pleased to present this report on the work of the Capita Board during 2017, formed of this section (pages 50 to 58) and the section headed 'Other Statutory and Regulatory Information' (pages 58 to 63).

We have taken steps during the year to improve the governance and structure of the Board to bring it more in line with market practice. We intend to pursue the highest standards of corporate governance and business practice and I believe that there are a number of areas in which we can continue to improve, particularly in respect of Capita's diversity agenda. As an organisation of some 70,000 people and one of the UK's largest employers, Capita must recruit, retain, develop and reward its people well if it is to achieve its goals. Its values, culture and behaviours have to empower and encourage all of Capita's people to ensure everyone has the opportunity to fulfil their potential.

Governance has a key role to play in the culture of the organisation and I believe the Board changes we have introduced will drive improved governance and performance across the whole of the business.

RESULTS FOR 2017

In Jon Lewis' review on pages 6 to 12 we have detailed the results for the year. It has been a challenging year for Capita and the Board but we remain confident that the transformation plan we are pursuing will deliver the right outcomes.

BOARD ACTIVITIES IN 2017

The Board has a standing schedule to meet nine times a year and holds further meetings as required, operating with an open culture. A structured approach is taken when setting Board and Committee meetings – they are aligned with the Company's financial calendar. We set an agenda to cover the wide range of matters that are brought to our attention, ensuring each is given appropriate time and focus. Given the issues Capita faces, many additional meetings took place during the year and I would like to thank the Board members for their commitment throughout the year.

DIVISIONAL SENIOR MANAGEMENT

Following the disposal of the Capita Asset Services businesses in November 2017, Capita is currently comprised of five divisions. We continue to review the structure of our businesses and management and ensure that these are appropriate. There is further detail on this area on page 25.

BOARD EVALUATION IN 2017

Board evaluation is undertaken annually, with external evaluation every three years.

An internal evaluation was undertaken in November 2017. This was carried out by questionnaire requiring written responses from all Directors. To ensure independence and objectivity, the questionnaire was conceived, administered and reviewed by myself and the Group Company Secretary. The resultant report was presented in full to the Board.

There has been considerable change in the structure and constitution of the Board this year to address many of the issues raised in our Board evaluation. The actions from the evaluation will also be incorporated within the strategic review of the Group. The actions included:

i. Increased strategic discussion;

ii. Diversity of Non-Executive Directors; and

iii. Fuller engagement of Non-Executive Directors.

Progress has been made on the actions agreed last year as follows:

i. Review of board packs – a paperless board portal solution has been implemented to allow timely and secure distribution of board papers;

ii. Additional strategy sessions for the Non-Executive Directors – divisional strategy sessions were arranged in the autumn to allow fuller discussion and debate on key matters; and

iii. Action plan on Board Diversity – please refer to the Nomination Committee report on page 65 for further information.

In 2015, a full external evaluation of the Board was undertaken by Corinna Gillies from the independent consultancy Illuminating Leaders, neither of which has any other connection with the Company. A full external evaluation will be undertaken in 2018.

As part of our Board evaluation process, a meeting was held by the Non-Executives and the Senior Independent Director to discuss my performance. The views of the Executive Directors were taken into consideration by the Non-Executives as part of the evaluation and I was not present at either meeting. A meeting of the Non-Executive Directors without Executive Directors was also held.

I met with all members of the Board individually to receive feedback and discuss current and long-term opportunities.

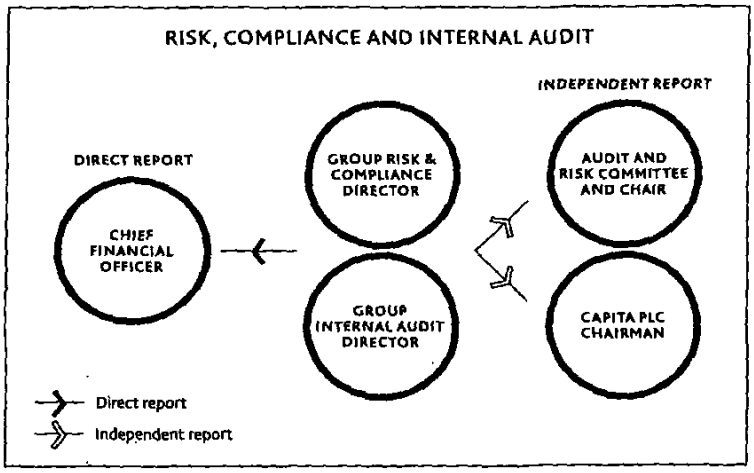
Consideration of Board balance is kept under review by myself and the Chief Executive Officer.

RISK & COMPLIANCE AND INTERNAL AUDIT

On pages 36 to 43 of the strategic report we have described fully the roles of Risk & Compliance and Group Internal Audit together with the risks and internal controls for Capita.

In order for the Board to ensure that the strategic direction of Capita is appropriate and has the appropriate risk oversight, numerous meetings are held throughout the year. These include individual meetings between the Group Risk & Compliance Director and the Group Internal Audit Director with the Chairman of the Audit and Risk Committee, as well as normal scheduled meetings. Risks are identified and categorised in a number of ways and are prioritised and delegated in accordance with the risk ratings provided to the risk owner.

Both the Group Risk & Compliance Director and the Group Internal Audit Director report to the Chief Financial Officer and independently to the Audit and Risk Committee. Both report respectively on the internal audit programme and risk and compliance management



activities and on the internal audit programme across Capita. They have access to all members of the Board and hold regular meetings with the Executive Directors and meet with the Audit and Risk Committee Chairman and myself at least quarterly. In October 2017, the risk sub-committees were restructured into a Group Executive Risk Committee and a *Technology & Security Risk Committee*, the latter having a particular focus on cyber security, information and IT risks.

DIRECTORS

The Directors of the Company currently in office are listed on pages 52 to 53.

All members of the Board will stand for re-election (Jon Lewis and Baroness Lucy Neville-Rolfe for election) at the forthcoming AGM. *All Board members have received a formal* performance evaluation, as described, which demonstrated that each Director continues to be effective and committed to the role.

The following pages in this section consist of our corporate governance and remuneration reports. I hope that you will find these and the entire Annual Report and Accounts informative. The Board will be happy to receive any feedback you may have.

Sir Ian Powell
Chairman
23 April 2018

BOARD MEMBERS

As at 31 December 2017, the Board comprised nine Directors, made up of the Chairman, Chief Executive Officer, two other Executive Directors and five independent Non-Executive Directors.

We have an experienced team in place to support our strategy and to meet the opportunities and challenges that the Group faces. As the Group develops, we will regularly review the Board composition to ensure it meets the needs of the business.

BOARD DIVERSITY

IMAGE REMOVED

Gender split as at date of publication 25%/75%

LENGTH OF TENURE AS BOARD DIRECTORS

IMAGE REMOVED

At 31 December 2017, we had two female Directors and seven male Directors. By the end of January 2018, we had two female and six male Directors and it is expected that diversity at both Board and senior leadership level will continue to be a focus of the Board.

CHAIRMAN

The role of the Chairman

The Chairman is responsible for leadership of the Board and ensuring its effectiveness on all aspects of its role. This includes setting the Board's agenda and ensuring that adequate time is available for discussion of all agenda items, in particular strategic issues. The Chairman should also promote a culture of openness and debate by facilitating the effective contribution of Non-Executive Directors in particular and ensuring constructive relations between Executive and Non-Executive Directors.
The Chairman is responsible for ensuring that the Directors receive accurate, timely and clear information and should ensure there is effective communication with shareholders.

IMAGE REMOVED

Sir Ian Powell N CC
Chairman

Appointed: September 2016

Independent at appointment: Yes

Key skills and experience: Sir Ian was appointed a Non-Executive Director on 1 September 2016 and as Chairman on 1 January 2017. Sir Ian is a chartered accountant and, prior to his retirement in June 2016, was Chairman and Senior Partner of PwC UK between 2008 and 2016, responsible for expertise management and board chairmanship of PwC UK. He joined PwC in 1977, serving in various roles of increasing responsibility, including Head of Advisory, prior to being elected Chairman and Senior Partner.

Other current appointments: Chairman – Police Now; Trustee – The Old Vic; Trustee – Wellbeing of Women; Member of the Development Committee – The National Gallery.

Committee memberships: Nomination (Chair).

EXECUTIVE DIRECTORS

The role of the Executive Directors

The Executive Directors are responsible for the day-to-day running of all aspects of the Group's business. This responsibility is different from the Chairman's role in running the Board. The role of Chief Executive Officer is separate from that of Chairman to ensure that no one individual has unfettered powers of decision.

IMAGE REMOVED

Jon Lewis
Chief Executive Officer

Joined Capita: 2017

Date appointed to Board: December 2017

Key skills and experience: Before joining Capita, Jon was Chief Executive Officer of Amec Foster Wheeler. Prior to that, Jon had a 20-year career at Halliburton Company Inc, where he held a number of senior roles, including Senior Vice President and member of the Halliburton Executive Committee.

Board responsibilities: Managing and developing Capita's business to achieve the Company's strategic objectives.

Other external appointments: None.

IMAGE REMOVED

Nick Greatorex
Chief Financial Officer

Joined Capita: 2006

Appointed: March 2015

Key skills and experience: Nick was appointed Chief Financial Officer on 1 March 2015 and served as Interim CEO from 15 September 2017 to 30 November 2017. Prior to his appointment as Chief Financial Officer, Nick was Executive Director for Life and Pensions and Insurance and Benefits Services and Commercial Director on major bids and contract implementations. He was previously Chief Financial Officer of Liberata plc (now owned by HCL) and held senior merger and acquisition roles at a number of organisations, including Centrica plc. He qualified as a chartered accountant in 1992 at Ernst & Young.

Board responsibilities: Overall control and responsibility for all financial aspects of the business's strategy.

Additional responsibilities: Property; Environment; Procurement; Commercial relationships; Supplier relationships; transformation plan.

Other external appointments: None.

NON-EXECUTIVE DIRECTORS

The role of the Non-Executive Directors

The Non-Executive Directors should constructively challenge and help develop proposals on strategy. They should scrutinise the performance of management in meeting agreed goals and objectives and monitor the reporting of performance. They should satisfy themselves on the integrity of financial information and that financial controls and systems of risk management are robust and defensible. They are responsible for determining appropriate levels of remuneration of Executive Directors and have a prime role in appointing and, where necessary, removing Executive Directors, and in succession planning.

IMAGE REMOVED

Gillian Sheldon (A) (N) (R)
Senior Independent Director

Date appointed to Board: September 2012 (appointed Senior Independent Director on 1 January 2013)

Independent: Yes

Key skills and experience: Gillian was appointed as Senior Independent Director on 1 January 2013 and was appointed to the Board on 1 September 2012. She is a senior adviser in Credit Suisse's investment banking division where she has gained substantial experience of advising boards across a wide range of complex situations and transactions. Prior to joining Credit Suisse, Gillian worked at NM Rothschild & Sons for seven years.

Other current appointments: Senior Banker at Credit Suisse, Trustee of BBC Children in Need; Member of Corporate Advisory Board of Royal Academy.

Committee memberships: Audit and Risk; Nomination; Remuneration.

IMAGE REMOVED

Matthew Lester (CC) (N) (R)
Non-Executive Director

Date appointed to Board: March 2017

Independent: Yes

Key skills and experience: Matthew was appointed Non-Executive Director on 1 March 2017. He is a Chartered Accountant with over 20 years of experience in senior finance roles. Most recently, Matthew was Group Chief Financial Officer of Royal Mail plc from November 2010 to July 2017. Matthew has also served as Group Chief Financial Officer for ICAP plc from May 2006 to November 2010. Prior to this he held senior roles at Diageo plc and Kleinwort Benson.

Other current appointments: Non-Executive Director of Man Group PLC and Barclays plc.

Committee memberships: Audit and Risk (Chair from 1 June 2017); Nomination; Remuneration.

IMAGE REMOVED

John Cresswell (A) (N) (CC)
Non-Executive Director

Date appointed to Board: 17 November 2015

Independent: Yes

Key skills and experience: John was appointed Non-Executive Director on 17 November 2015. John has substantial experience leading, growing and advising media and broadcast organisations at CEO and executive director levels and has worked in the Technology, Media and Telecommunications sector for 25 years. John is a Chartered Accountant, has a BSc in Economics and Politics, and attended the Advanced Management Programme at Harvard Business School. Most recently he served four-and-a-half years as CEO of Arqiva; previous to that he held a number of executive director roles on the board of ITV plc, and was formerly a director of Liverpool Football and Athletic Grounds plc and a director of Ambassador Theatre Group. John has recently been appointed CEO of Bibby Line Group Limited which he will join on 1 May 2018 – he will take over as CEO in summer 2018.

Other current appointments: None.

Committee memberships: Audit and Risk; Nomination; Remuneration (Chair).

IMAGE REMOVED

Andrew Williams (A) (N) (R)
Non-Executive Director

Date appointed to Board: January 2015

Independent: Yes

Key skills and experience: Andrew was appointed Non-Executive Director with effect from 1 January 2015. Andrew is Chief Executive of Halma plc, a leading specialist in safety, health and environmental technologies and a FTSE 100 company. He was appointed Chief Executive in February 2005. Andrew started his career at Halma in 1994 as Manufacturing Director of a subsidiary company and went on to hold a wide range of senior management positions across the Group. Andrew is a Chartered Engineer and a production engineering graduate of Birmingham University. He attended the Advanced Management Program at Wharton Business School, University of Pennsylvania in 2004.

Other current appointments: Chief Executive of Halma plc since 2005.

Committee memberships: Audit and Risk; Nomination; Remuneration.

IMAGE REMOVED

Baroness Lucy Neville-Rolfe, DBE CMG (A) (N) (R)
Non-Executive Director

Date appointed to Board: December 2017

Independent: Yes

Key skills and experience: Baroness Lucy Neville-Rolfe was appointed Non-Executive Director on 6 December 2017. Her key skills and experience are in international retail, governance, legal and regulatory issues and communications. She has been a member of the House of Lords since 2013 and served as a Government Minister from 2014-2017: Commercial Secretary to the Treasury, Minister of State and Minister of State for Energy and Intellectual Property; and Parliamentary Under Secretary in the departments for Business, Innovation & Skills and Digital, Culture, Media & Sport. She had a private sector career in Tesco from 1997-2013 and from 2006 was a member of the Board of Tesco plc as Executive Director, Corporate & Legal Affairs. Her Non-Executive Directorships included ITV plc and Metro AG and before Tesco she was a member of the Home Civil Service including time as Director of the Deregulation Unit and as a Member of the Prime Minister's Policy Unit, 10 Downing Street.

Other current appointments: Director of Assured Food Standards (Red Tractor) and Governor of London Business School.

Committee memberships: Audit and Risk; Nomination; Remuneration.

Key to committees

(A) Audit and Risk
(N) Nomination
(R) Remuneration
(CC) Committee chair

CORPORATE GOVERNANCE STATEMENT

Capita plc and its subsidiaries remain committed to maintaining high standards of corporate governance.

COMPLIANCE WITH THE FINANCIAL REPORTING COUNCIL'S UK CORPORATE GOVERNANCE CODE

Capita plc and its subsidiaries (the Group) remain committed to maintaining high standards of corporate governance.
The UK Corporate Governance Code 2016 (the Code) applies to accounting periods beginning on or after 17 June 2016. A copy of the Code is available from the Financial Reporting Council's website www.frc.org.uk. Throughout the accounting period to which this report relates, the Company complied with all relevant provisions set out in sections A to E of the Code.

Following the departures of Vic Gysin and Chris Sellers, there are now two Executive Directors on the Board, the Chief Executive Officer and Chief Financial Officer, which is more aligned with market practice in this area. The Board has six strong independent Non-Executive Directors, including the Chairman, to provide robust challenge and independent review.

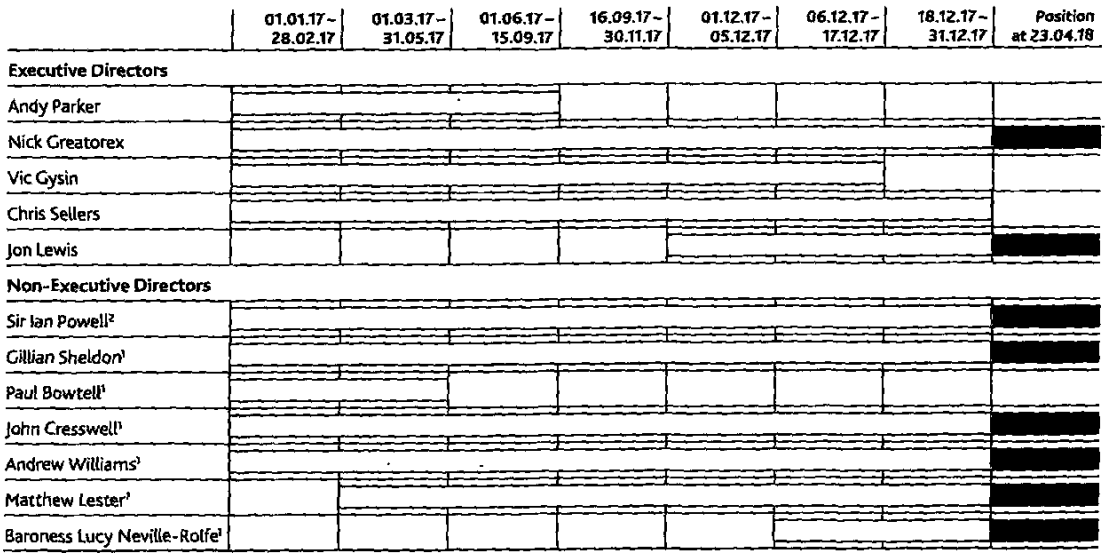
BOARD CHANGES IN THE YEAR

Name	Date	Position
Chris Sellers	1 January 2017	Appointed Group Business Development Director
Matthew Lester	1 March 2017	Appointed Non-Executive Director (Chair of Audit and Risk Committee from 1 June 2017)
Paul Bowtell	31 May 2017	Resigned as Non-Executive Director and Chair of Audit and Risk Committee
Andy Parker	15 September 2017	Resigned as Chief Executive Officer
Jon Lewis	1 December 2017	Appointed Chief Executive Officer
Baroness Lucy Neville-Rolfe	6 December 2017	Appointed Non-Executive Director
Vic Gysin	18 December 2017	Resigned as Group Operations & Performance Director

Nick Greatorex was appointed Interim Chief Executive Officer for the period from 16 September to 30 November 2017.

Further information on changes to the Board is set out in the Nomination Committee report on page 65.

BOARD COMPOSITION OVER THE YEAR



1 Independent in accordance with the Code.
2 Independent on appointment in accordance with the Code.

FREQUENCY OF MEETINGS AND ATTENDANCE

During 2017, the Board held nine scheduled meetings, excluding ad hoc meetings. Attendance of the Board Directors is recorded in the table below:

	Board meetings
Scheduled meetings	**9**
Sir Ian Powell	9
Jon Lewis[1]	1
Nick Greatorex	9
Gillian Sheldon	9
Matthew Lester[2]	7
John Cresswell	9
Andrew Williams	9
Baroness Lucy Neville-Rolfe[3]	1
Andy Parker[4]	6
Paul Bowtell[5]	4
Vic Gysin[6]	9
Chris Sellers[7]	9

1 *Jon Lewis was appointed to the Board on 1 December 2017.*
2 *Matthew Lester was appointed to the Board on 1 March 2017.*
3 *Baroness Lucy Neville-Rolfe was appointed to the Board on 6 December 2017.*
4 *Andy Parker resigned from the Board on 15 September 2017.*
5 *Paul Bowtell resigned from the Board on 31 May 2017.*
6 *Vic Gysin resigned from the Board on 18 December 2017.*
7 *Chris Sellers resigned from the Board on 23 January 2018.*

CORPORATE GOVERNANCE STATEMENT CONTINUED

Due to the nature of the challenges faced in 2017, a number of additional ad hoc Board and Committee meetings were held during the year. In total, there were 48 Board and Committee meetings (including both scheduled and ad hoc meetings) held during 2017. Meetings held outside of the normal schedule need to be flexible and are often held by telephone.

Any Director's absence from Board meetings was previously agreed with the Chairman of the Board or the Chief Executive Officer.

During 2017, the following formal Director meetings took place:

- The Chairman held one-to-one individual review sessions with each Executive Director and each Non-Executive Director.
- The Non-Executive Directors met without Executive Directors.
- The Non-Executive Directors met with just the Chief Executive Officer.
- The Non-Executive Directors met without the Chairman, led by the Senior Independent Director.

BOARD LEADERSHIP

Consistent with previous years, the Board continues to support the need to segregate the responsibility for operating the Board and managing the underlying business. This will continue in 2018 with the separation of Sir Ian Powell's role as Chairman and the role of Jon Lewis as Chief Executive Officer.

During the year, Sir Ian Powell as Chairman and Gillian Sheldon as Senior Independent Director also held meetings comprising solely the Non-Executive Directors. Both Sir Ian and Gillian are available to meet with shareholders when requested.

ROLE OF THE BOARD

The Companies Act 2006 requires Directors to act in a way they consider, in good faith, would be most likely to promote the success of the Company for the benefit of shareholders as a whole. In doing so, the Directors must have regard (amongst other matters) to:

- The likely consequences of any decision in the long term.
- The interests of the Company's employees.
- The need to foster business relationships with suppliers, clients and others.
- The impact of the Company's operations on the community and the environment.
- The desirability of the Company maintaining a reputation for high standards of business conduct.
- The need to act fairly towards all shareholders of the Company.

In addition to their statutory duties, the Directors must ensure that the Board focuses effectively on all its accountabilities.

The Board determines the strategic objectives and policies of the Group to best support the delivery of long-term value, providing overall strategic direction within an appropriate framework of rewards, incentives and controls. The Board is collectively responsible for the success of the Company: the Executive Directors are directly responsible for running the business operations and the Non-Executive Directors are responsible for bringing independent judgement and scrutiny to decisions taken by the Board. The Non-Executive Directors must satisfy themselves on the integrity of financial information and that financial controls and systems of risk management are robust. Following presentations by executive and divisional management and a disciplined process of review and challenge by the Board, clear decisions on policy or strategy are adopted, and the executive management are fully empowered to implement those decisions.

BOARD INDEPENDENCE

Non-Executive Directors are required to be independent in character and judgement. All relationships that may interfere materially with this judgement are disclosed as required under the conflicts of interest policy. The Board has determined that all the Non-Executive Directors who served during the year were independent and before and upon appointment as Chairman Sir Ian Powell met the criteria of independence as outlined in the Code.

The Board does not believe that a Non-Executive's tenure interferes materially with their ability to act in the best interests of the Group. The Board also believes that each of the Non-Executives has retained independence of character and judgement and has not formed associations with management or others that may compromise their ability to exercise independent judgement or act in the best interests of the Group.

The Board is satisfied that no conflict of interest exists for any Director. This matter is a standing agenda item.

A formal schedule of matters reserved by the Board has been adopted and these include, but are not limited to:

Strategy and management, including responsibility for the overall leadership of the Group, setting the Group's values and standards and overview of the Group's operational management.

Structure and capital including changes relating to the Group's capital structure and major changes to the Group's corporate structure including acquisitions and disposals and changes to the Group's management and control structure.

Financial reporting including the approval of the Annual Report and Accounts, half-yearly report, trading statements and preliminary announcement for the final results. Also the approval of dividend policy, the setting and approval of treasury policies and establishing and maintaining accounting policies.

Internal controls, ensuring that the Group manages risk effectively and approves all acquisitions, disposals of assets and share acquisitions.

Contracts, including approval of all major capital projects and major investments including the acquisition or disposal of interests of more than 3% in the voting shares of any company or the making of any takeover offer.

Ensuring satisfactory communication with shareholders.

Any changes to the structure, size and composition of the Board.

BOARD OF DIRECTORS' INDUCTIONS AND TRAINING

Following appointment to the Board, all new Directors receive an induction tailored to their individual requirements. They are encouraged to meet and be briefed on the roles of key people across the Group and have open access to all business areas and employees to build up an appropriate level of knowledge of the business that extends beyond formal papers and presentations to the Board. All Directors have received an appropriate induction for their roles within Capita. These have included familiarisation with:

- terms of reference for all committees and matters reserved for the Board;
- overviews of the business via Monthly Performance Review (MPR) reports; and
- the Group approach to risk management.

Following the announcement of their appointments to the Board, Jon Lewis and Baroness Lucy Neville-Rolfe received training and induction sessions with the Chairman, Executive Directors, Group Company Secretary, Group Risk & Compliance Director and Group Internal Audit Director. Jon Lewis held further induction meetings with the Divisional Executive Officers and other senior management.

Ongoing training and briefings are also given to all Directors, including external courses as required.

GROUP COMPANY SECRETARY

All Board members have access to independent advice on any matters relating to their responsibilities as Directors and as members of the various committees of the Board at the Group's expense.

Francesca Todd, as Group Company Secretary, is available to all Directors and is responsible for ensuring that all Board procedures are complied with.

The Group Company Secretary has direct access and responsibility to the Chairs of the standing committees and open access to all the Directors. The Group Company Secretary has been appointed as Secretary to the Audit and Risk, Remuneration and Nomination Committees to ensure that there are no conflicts of interest. The Group Company Secretary meets regularly with the Chairman, the Chair of the Audit and Risk Committee and the Chair of the Remuneration Committee, and briefs them on areas of governance and committee requirements.

MATTERS RESERVED FOR THE BOARD

A formal schedule of matters reserved by the Board has been adopted and these include, but are not limited to:

Strategy and management, including responsibility for the overall leadership of the Group, setting the Group's values and standards and overview of the Group's operational management.

Structure and capital including changes relating to the Group's capital structure and major changes to the Group's corporate structure including acquisitions and disposals and changes to the Group's management and control structure.

Financial reporting including the approval of the half-yearly report, interim management statements and preliminary announcement for the final results. Also the approval of the dividend policy, the setting and approval of treasury policies and establishing and maintaining accounting policies.

Internal controls, ensuring that the Group manages risk effectively and approves all acquisitions, disposals of assets and share acquisitions.

Contracts, including approval of all major capital projects and major investments including the acquisition or disposal of interest of more than 3% in the voting shares of any company or the making of any takeover offer.

Ensuring satisfactory communication with shareholders.

Any changes to the structure, size and composition of the Board.

DIALOGUE WITH THE COMPANY'S SHAREHOLDERS

The Board encourages proactive engagement with the Company's investors and seeks to build a mutual understanding of objectives between Capita and its investors. As part of this process the Executive Directors make regular presentations and meet with institutional investors to discuss the Group's business, performance and strategy, addressing any issues of concern, obtaining feedback and consider corporate governance issues. This is done through a combination of one-to-one meetings, participation in investor roadshows or attendance at investor conferences.

The Investor Relations team has effective day-to-day responsibility for managing investor communications and always acts in close consultation with the Board. All members of the Board, including the Non-Executive Directors, receive a report on any significant discussions with shareholders and feedback that follows the annual and half-yearly presentations to investment analysts and institutional investors. All analyst reports concerning Capita are circulated to the Directors and the Board is kept informed of changes in the share register.

During the year, the Head of Investor Relations, Chief Executive Officer and Chief Financial Officer maintained active, targeted communications with existing and potential shareholders and the wider investment community. The Investor Relations team continued to support the Chairman, Sir Ian Powell, in further building his relationships with key institutional shareholders. Following the appointment of Jon Lewis in December, meetings were organised with major institutional shareholders, ensuring all had the opportunity to meet with him and discuss their areas of concern prior to the end of the financial year.

CORPORATE GOVERNANCE STATEMENT CONTINUED

2017 calendar of investor events	
March	– 2016 year-end results released – UK investor roadshow
June	– Annual General Meeting and trading update
September	– IFRS 15 teach-in and restatement of 2016 full year results – 2017 half year results released – UK investor roadshow
November	– Numis Support Services Conference
December	– Pre-close trading update – Jon Lewis, CEO, introductory meetings with major shareholders

Shareholder meetings

All shareholders are encouraged to attend the Annual General Meeting (AGM) and information for shareholders is available on the Company's website www.capita.com. All the Non-Executive Directors are available to meet with shareholders to understand their views more fully. The Chairman is available to the significant shareholders of Capita. Directors, including Chairs of the various committees, are present at the AGM to answer any questions. The Board particularly encourages communication with and the participation of private investors at the AGM.

Shareholder communications

In addition to attendance at the AGM, shareholders can also access up-to-date information through the Group's website at www.capita.com. A telephone helpline, 0871 664 0300, provides a contact point directly to the Group's registrars, and private shareholders can also raise queries by email to enquiries@linkgroup.co.uk.

REMUNERATION COMMITTEE

Details of the Remuneration Committee and its activities are given in the Directors' remuneration report on pages 75 to 89.

RISK MANAGEMENT AND INTERNAL CONTROL

The Board monitors the Company's risk management and internal control systems and annually carries out a review of their effectiveness. This is reported within the Audit and Risk Committee report. The monitoring and review includes all material controls, including financial, operational and compliance controls. This process is regularly reviewed by the Board. The Group's key internal control procedures are fully documented within the strategic report on pages 36 to 43.

Furthermore, through the operation of the risk governance process, the Directors confirm (in accordance with provision C 2.1 of the Code) that they have carried out a robust assessment of the principal risks facing the Group, including those that would threaten its business model, future performance, solvency or liquidity. A description of those risks, together with how they are being managed or mitigated, is set out on pages 38 to 43.

OTHER STATUTORY AND REGULATORY INFORMATION

Strategic report

The Company is required to prepare a fair review of the business of the Group during the financial year ended 31 December 2017 and of the position of the Group at the end of the financial year and a description of the principal risks and uncertainties facing the Group (known as a 'strategic report'). The purpose of the strategic report is to enable shareholders to assess how the Directors have performed their duty under Section 172 of the Companies Act 2006 (duty to promote the success of the Company). The information that fulfils the requirements of the strategic report can be found on pages 03 to 48. Details of the Group's business goals, strategy and model are on page 13.

Corporate governance report

The corporate governance statement as required by Rule 7.2.1 of the Financial Conduct Authority's Disclosure and Transparency Rules is set out on pages 49 to 89.

Election to apply FRS101 – Reduced Disclosure Framework

The parent company continues to apply UK GAAP in the preparation of its individual financial statements in accordance with FRS 101 and these are contained on pages 185 to 200. FRS 101 applies IFRS as adopted by the European Union with certain disclosure exemptions. No objections were received from shareholders.

Management report

For the purposes of Rule 4.1.5R(2) and Rule 4.1.8R of the Financial Conduct Authority's Disclosure and Transparency Rules, this Directors' report and the strategic report on pages 03 to 48 comprise the management report.

EVENTS AFTER THE BALANCE SHEET DATE

Chris Sellers resigned from the Board on 23 January 2018.

As announced to the market on 31 January 2018, payment of a dividend has been suspended until the Company is generating sustainable free cash flow and a Rights Issue is scheduled for 2018.

APPOINTMENT, RE-APPOINTMENT AND REMOVAL OF DIRECTORS

Directors are appointed and may be removed in accordance with the Articles of Association of the Company and the provisions of the Companies Act 2006.

All Directors are subject to election at the first Annual General Meeting after their appointment and to re-election at intervals of no more than three years in accordance with the Code and the Company's Articles of Association. However, all Directors will retire and will offer themselves for re-election (Jon Lewis and Baroness Lucy Neville-Rolfe for election) at the Annual General Meeting in June 2018, in accordance with the UK Corporate Governance Code.

No person, other than a Director retiring at the meeting, shall be appointed or re-appointed a Director of the Company at any general meeting unless he/she is recommended by the Directors.

No person, other than a Director retiring at a general meeting as set out above, shall be appointed or re-appointed unless between 7 and 35 days' notice, executed by a member qualified to vote on the appointment or re-appointment, has been given to the Company of the intention to propose that person for appointment or re-appointment, together with notice executed by that person of his/her willingness to be appointed or re-appointed.

GROUP ACTIVITIES

Capita is the UK's leading provider of technology-enabled business process and customer management services and professional services. We generate the majority of our revenues from long-term contracts and partnerships across the private and public sectors. The Group's chosen markets are in the private sector – life, pensions and insurance, financial services, utilities and telecoms, retail, travel and transport, and other private sector, and in the public sector – central government, local government, education, health, justice and emergency services and defence.

Transforming business processes to drive down administration costs while also improving the end-user experience is the goal of the majority of what we do for our clients. We focus on delivering technology-enabled solutions,

providing excellent customer service and operational delivery. We will combine our expertise with technology to make processes smarter, organisations more efficient and customer experiences better.

A review of the development of the Group and its business activities during the year is contained in the strategic report on pages 03 to 48. The operational and financial performance of our divisions are detailed on pages 25 to 35.

RESULTS AND DIVIDENDS

The Group's reported loss before taxation amounted to £513.1m (2016 restated: £89.8m). As announced on 31 January 2018, the Directors do not recommend the payment of a final dividend (2016: 20.6p per share). The total dividend for the year was therefore 11.1p per share (2016: 31.7p per share).

The Employee Benefit Trust has waived its right to receive a dividend on the shares held within the Trust.

CONFLICTS POLICY

Under the Companies Act 2006, Directors are under an obligation to avoid situations in which their interests can or do conflict, or may possibly conflict, with those of the Company. In response to the conflicts of interest provisions, a comprehensive project was undertaken in 2008 to identify and disclose any conflicts of interest that have arisen or may arise across Capita. Procedures were implemented for evaluating and managing conflicts that have been identified in a way that ensures that decisions are not compromised by a conflicted Director. In addition, the Company's Articles of Association give the Board the power to authorise matters that give rise to actual or potential conflicts. The Board reports annually on the Company's procedures for ensuring that the Board's powers of authorisation of conflicts are operated effectively and that the procedures have been followed. A policy for ongoing identification and disclosure of conflicts is in place and is kept under regular review.

The Board has authorised the conflict of Nick Greatorex being a trustee of the Capita Pension and Life Assurance Scheme and gave specific guidance on this conflict going forward. Nick Greatorex did not participate in the discussion or vote on the guidance given. No other conflicts of interest declared were material to the Board. All conflicts of interest are reviewed on an annual basis by the Board and are revisited as part of the year-end process by the Directors. None of the Directors of the Company had a material interest in any contract with the Company or its subsidiary undertakings, other than their contracts of employment.

MAJOR SHAREHOLDERS

At 31 December 2017, the Company had received notifications that the following were interested in accordance with the Disclosure and Transparency Rules (DTRs):

Shareholder	Number of shares	% of voting rights as at 31 December 2017	Number of shares direct	Number of shares indirect
Veritas Asset Management LLP[1]	90,680,462	13.59	–	90,680,462
Invesco Asset Management	60,356,028	9.04	–	60,356,028
Woodford Investment Management LLP	51,567,196	7.73	51,567,196	–
BlackRock, Inc.	47,964,248	7.19	–	47,964,248
The Capital Group Companies, Inc.	45,382,384	6.80	–	45,382,384
Baillie Gifford & Co Limited	35,344,377	5.30	–	35,344,377
Capital Research Global Investors	29,488,695	4.42	–	29,488,695
Jupiter Asset Management	23,743,048	3.56	–	23,743,048
Schroder Investment Management	22,193,671	3.33	–	22,193,671
Veritas Funds PLC	22,127,050	3.32	–	22,127,050
Marathon Asset Management LLP	21,830,855	3.27	–	–
Vanguard Group	20,530,373	3.08	20,530,373	
T. Rowe Price	20,215,315	3.03	–	20,215,315

1 This includes the holding of Veritas Funds PLC.

As at 18 April 2018, the Company had received notifications that the following were interested in accordance with the DTRs:

Shareholder	Number of shares	% of voting rights as at 18 April 2018	Number of shares direct	Number of shares indirect
Veritas Asset Management LLP[1]	89,035,975	13.34	–	89,035,975
Woodford Investment Management LLP	66,758,754	10.00	66,758,754	–
Investec Asset Management Ltd	63,080,896	9.45	–	63,080,896
Invesco Ltd.	60,574,558	9.08	–	60,574,558
BlackRock, Inc.	44,104,108	6.61	–	44,104,108
Veritas Funds PLC	22,127,050	3.32	–	22,127,050
Marathon Asset Management LLP	21,694,771	3.25	–	21,694,771
Vanguard Group	20,654,592	3.09	20,654,592	–

1 This includes the holding of Veritas Funds PLC.

CORPORATE GOVERNANCE STATEMENT CONTINUED

DIRECTORS' INTERESTS

Details of Directors' interests in the share capital of the Company are listed on page 86.

SHARE CAPITAL

As at 23 April 2018, 670,241,242 ordinary shares of $2^1/_{15}$p each have been issued and are fully paid up and are quoted on the London Stock Exchange. There are 2,886,388 shares held in treasury and the total number of voting shares is 667,354,854. During the year ended 31 December 2017, no new ordinary shares were issued – options exercised pursuant to the Company's share option schemes were satisfied by the transfer of shares from treasury (213,854 shares) or from the Employee Benefit Trust (69,377 shares). No shares have been allotted under the Company's share option schemes since the end of the financial year to the date of this report. Of the total issued share capital, 1,644,664 shares are held within the Employee Benefit Trust used for satisfying employee share options.

The share price at 31 December 2017 was 400.9p. The highest share price in the year was 721p and the lowest was 390.6p.

The Company renewed its authority to re-purchase up to 10% of its own issued share capital at the Annual General Meeting in June 2017. During the year, the Company did not purchase any shares (2016: nil).

VIABILITY STATEMENT

This statement is detailed in full on page 44.

In accordance with provision C.2.2 of the Code, the Directors have assessed the viability of the Group over the three-year period to 31 December 2020 taking into account the Group's current position, the anticipated net proceeds from the announced Rights Issue and the potential impact of the principal risks set out in the strategic report. Based on this assessment, the Directors have a reasonable expectation that the Group is and will continue to be viable.

GOING CONCERN

The Group's business activities, together with the factors likely to affect its future development, performance and position are set out in the strategic report on pages 03 to 48. The financial position of the Group, its cash flows, liquidity position and borrowing facilities are described on pages 91 to 95. In addition, note 28 to the financial statements on pages 141–149 includes the Group's objectives, policies and processes for managing its capital, its financial risk management objectives, details of its financial instruments and hedging activities, and its exposures to credit risk and liquidity risk.

In determining the appropriate basis of preparation of the financial statements for the year 31 December 2017, the Directors are required to consider whether the Group can continue in operational existence for the foreseeable future. The Board has concluded that it is appropriate to adopt the going concern basis, having undertaken a rigorous assessment of the financial forecasts and with consideration of the anticipated net proceeds from the announced Rights Issue which the Board is confident will be approved.

On 31 January 2018, the Group announced a multi-year transformation plan, encompassing strategy, cost competitiveness, sales, IT and its capital structure, to improve the performance of Capita over the medium-to-long term. This transformation plan includes an assessment of the appropriate financial leverage for the Group over the medium term, to ensure that Capita has a sustainable capital base to support its customers and operations, increase investment in the business and deliver future strategy. The Board's view is that the appropriate leverage for Capita over the medium term should be between 1.0 and 2.0 times adjusted net debt to adjusted EBITDA (prior to the adoption of IFRS 16). Accordingly, the Board has decided to raise additional equity of £701m by way of a Rights Issue, which is fully underwritten by Citigroup Global Markets Limited and Goldman Sachs International.

The transformation plan is being finalised, and the key actions and forecast impacts incorporated into detailed business plans. These are in support of the new strategy that has been reviewed and approved by the Board. Details of the new strategy are outlined in the Chief Executive Officer's review on pages 6 to 12.

For the purpose of the going concern assessment the Directors have considered a 'base-case' set of projections that cover the first two years of the new strategic plan, to 31 December 2019. This base-case includes cost reduction identified to date but not the anticipated proceeds from the Rights Issue and planned strategic disposals, and therefore importantly does not include the investment these will enable the Group to make, and the benefits these will deliver over the longer term.

The Group's committed facilities and private placement notes are subject to compliance with covenant requirements including maximum ratios of adjusted net debt to adjusted EBITDA. This covenant threshold is tested semi-annually, and is set at 3.0 times to 3.5 times depending on the debt instrument in question. The Directors have applied judgement in terms of how the ratio is calculated by applying the same treatment that has been applied in preparing and presenting the financial statements.

Accordingly, items that are presented as non-underlying are excluded from the covenant definition of adjusted EBITDA (with the exception of acquisition costs), as are restructuring costs that are now presented within the underlying results as set out in note 3 to the consolidated financial statements. This basis of calculation is consistent with the approach adopted in prior years.

In assessing the going concern assumption, the Board has undertaken a rigorous assessment of the forecast outturns and assessed identified downside risks and mitigating actions, by reference to the relevant covenant tests. The downside risks include a number of severe but plausible scenarios, incorporating underperformance against the business plan, unexpected cash outflows and customer attrition and unwillingness to award the Group new contracts and extensions to existing arrangements. The Board has considered mitigating actions available to the Group in response to these sensitivities.

Whilst the 'base case' scenario shows the business can operate in compliance with its adjusted net debt to adjusted EBITDA covenants applying the reasonable downside scenarios indicate that, absent the anticipated net proceeds from the announced Rights Issue, and assuming no other mitigating actions are taken by the Group, the available headroom is not sufficient to operate within the 3.0 times adjusted net debt to adjusted EBITDA covenant test. The Board has therefore considered the Rights Issue net proceeds in its assessment of going concern and the Group's ability to realise their assets and discharge their liabilities in the normal course of business.

Rights Issue

The Company has today launched a Rights Issue to raise £701m.

The Rights Issue will be subject to shareholders' approval and the general meeting to approve the equity raise is scheduled for 9 May 2018.

The Rights Issue is fully underwritten for £701m, by Citigroup Global Markets Limited and Goldman Sachs International.

Material uncertainties

In assessing the going concern assumptions, the Board has reviewed the base case plans, identified downsides and anticipated receipt of proceeds from the Rights Issue. Following this assessment, the Board has a reasonable expectation that the Company and the Group will be able to operate as a going concern for the foreseeable future.

In undertaking the assessment, the Board has considered the fact that a shareholder vote is required in order to raise additional capital through the Rights Issue, and that the underwriting agreement is subject to certain specific conditions which, although customary in nature, are outside the control of the Company. These events and conditions indicate a material uncertainty on the completion of the Rights Issue which may cast significant doubt about the Group's and parent company's ability to continue as a going concern.

The Board is confident that the Rights Issue will be approved and the proceeds received and based on this expectation believes that, even in a reasonable downside scenario, the Group and parent company will continue to have adequate financial resources to realise their assets and discharge their liabilities as they fall due. Accordingly, the Directors have formed the judgement that it is appropriate to prepare the financial statements on the going concern basis. Therefore, the financial statements do not include any adjustments which would be required if the going concern basis of preparation is inappropriate.

The auditors' report on pages 170–184 refer to this material uncertainty, and their opinion is not qualified or modified in this regard.

AUDITOR REVIEW

The Auditor has reviewed the statements regarding going concern (see page 60) and longer-term viability (see page 44) and those parts of the statement of compliance with the Code relating to: (i) Directors' and auditor's responsibilities; (ii) the 'fair, balanced and understandable' statement; (iii) confirmation of robust risk assessment and monitor and review of effectiveness of risk management and internal control systems; and (iv) Audit and Risk Committee composition, role and responsibilities. Further details are in the Auditor's report which includes reference to a material uncertainty in relation to going concern. The Auditor's report is not modified in this respect (see page 171).

DISABLED PERSONS

It is the Group's policy to give full consideration to suitable applications for employment of disabled persons and to ensure that any reasonable adjustments are made to either the workplace or job content to accommodate a person's disabilities. Employees with a disability are eligible to participate in career development opportunities available to all employees and will be supported to do so. Opportunities also exist for employees of the Group who become disabled to continue in their employment with any reasonable adjustments being made or to be retrained for other positions in the Group.

EMPLOYEE DEVELOPMENT AND ENGAGEMENT

Capita has a real focus on supporting talent and development within the Company. Capita's approach to employee development ensures that individuals are offered continual challenges in their roles, supported through learning opportunities and personal development. The Company offers employees a comprehensive range of key business and management skills and personal development programmes through our internal training partners, as well as externally recognised universities and learning partners. At the same time our businesses provide business-specific training for all employees relevant to their role. In addition, Capita supports the achievement of professional qualifications including a range of National Vocational Qualifications and apprenticeships. This year also saw the launch of a dedicated talent hub which profiles all the career opportunities across the Company to our employees.

Employees receive corporate news through: frequent email notices; internal notice board statements; the employee intranet, Capita Connections, Yammer (internal social networking channel) and regular email updates on business performance from both Divisional Executive Officers and Executive Directors. Capita Connections enables employees to find out what is happening in the wider Group and to share information within and between business units and employees are encouraged to contribute news, views and feedback. Capita maintains a strong communications network and employees are encouraged, through its Open Door Policy, to discuss with management matters of interest to the employee and subjects affecting day-to-day operations of the Company. Employees are also encouraged to share their views through regular employee surveys and as outputs divisions develop action plans to address any improvements that are highlighted.

Capita has an established employee share purchase plan designed to promote employee share ownership and to give employees the opportunity to participate in the future success of the Company. In keeping with its belief that employees are the Company's most valuable asset, Capita operates employee recognition schemes both at Central and divisional level. The Capita Change Makers Awards, for example, celebrate the core values that embody the organisation and recognise employees for service excellence, teamwork, leadership, innovation and improvement, inter-divisional collaboration and charitable support and community engagement. We've also run an internal communications initiative that aligns with our external promotional campaign which encourages our people to see themselves as Change Makers, delivering positive, valuable change for our clients in many different forms across our businesses. We profile individuals from across the Company to showcase their success stories through our employee communications channels.

POLITICAL DONATIONS

The Group did not make any political donation or incur any political expenditure during the year (2016: £nil).

GREENHOUSE GAS EMISSIONS

A description of Capita's approach to greenhouse gas emissions is set out on page 48 of the strategic report but for the purpose of Section 7 of the Companies Act 2006 (Strategic Report and Directors' Report) Regulations 2013 the following metrics and methodology are disclosed below:

	2017	2016	2015
Scope 1	**21,217**	18,137	16,664
Scope 2	**54,262**	65,094	68,367
Scope 3	**29,264**	34,317	35,125
Total gross tonnes of CO_2e	**104,743**	117,489	120,157
Total gross tonnes of CO_2e/£1m revenue	**25.23**	26.97	25.71
Total gross tonnes of CO_2e/headcount	**1.5**	1.6	1.6

Notes:

Restated 2016 emissions data to improve the accuracy of reporting using actual data to replace estimations.

Scope 1: Emissions from Capita sources that are controlled by us, including the combustion of fuel, company owned vehicles and the operation of our facilities.

Scope 2: Emissions from the consumption of purchased electricity, heat or steam.

CORPORATE GOVERNANCE STATEMENT CONTINUED

Scope 3: Emissions from non-owned sources that are related to Capita's activities, including business travel.

Methodology

Our disclosures cover sources of our greenhouse gas emissions from our operations in UK, Ireland, Europe (Poland, Germany, Switzerland, Austria), India and South Africa. Capita converts the consumption data into a carbon footprint with consideration to the World Business Council for Sustainable Development and World Resources Institute's (WBCSD/WRI) Greenhouse Gas Protocol together with the latest emissions factors from the UK Department for Environment, Food and Rural Affairs (Defra) or, where available, the latest industry factors, e.g. hotel stays from Green Tourism Board Scheme.

FINANCIAL INSTRUMENTS

The Group's financial instruments primarily comprise bonds, bank loans, finance leases and overdrafts. The principal purpose of these is to raise funds for the Group's operations. In addition, various other financial instruments such as trade creditors and trade debtors arise directly from its operations. From time to time, the Group also enters into derivative transactions, primarily interest rate swaps, currency swaps and forward exchange contracts, the purpose of which is to manage interest risk and currency risk, arising from the Group's operations and its sources of finance.

The main financial risks, to which the Group has exposure, are interest rate risk, liquidity risk, credit risk and foreign currency risk.

The Group borrows in selected currencies at fixed and floating rates of interest and makes use of interest rate swaps and currency swaps to generate the desired interest profile and to manage its exposure to interest rate fluctuations.

In respect of liquidity risk, the Group aims to maintain a balance between continuity of funding and flexibility through the use of multiple sources of funding including bonds, bank loans, loan notes, finance leases and overdrafts, over a broad spread of maturities.

In respect of credit risk, the Group trades only with recognised, creditworthy third parties. It is the Group's policy that all clients who wish to trade on credit terms are subject to credit verification procedures. In addition, receivable balances are monitored on an ongoing basis with the result that the Group's exposure to bad debt is not significant.

With respect to credit risk arising from the other financial assets of the Group, such as cash, financial investments and derivative instruments, the Group's exposure to credit risk arises from default of the counterparty. The Group manages its operations to avoid any excessive concentration of counterparty risk and the Group takes all reasonable steps to seek assurance from the counterparties to ensure that they can fulfil their obligations.

The Group is not generally exposed to significant foreign currency risk, except in respect of its overseas operations in Europe, India and South Africa, which generates exposure to movements in the euro, Swiss franc, Indian rupee and South African rand exchange rates. The Group seeks to mitigate the effect of this exposure by entering forward currency instruments, including non-deliverable forward contracts, to fix the sterling cost of highly probable forecast transactions denominated in Indian rupee and South African rand. Exposures to the euro and Swiss franc are mitigated through the use of foreign exchange derivatives or borrowings in those currencies. Further details of the Group's financial instruments can be found in note 28 to the consolidated financial statements on pages 141 to 149.

QUALIFYING THIRD-PARTY INDEMNITY PROVISIONS FOR THE BENEFIT OF DIRECTORS

Under the Companies Act 2006, companies are under an obligation to disclose any indemnities which are in force in favour of their directors. The current Articles of Association of the Company contain a provision that enables the Company to indemnify the Directors of the Company in respect of certain liabilities and costs that they might incur in the execution of their duties as Directors. Such provisions have been in force during the year and are in force at the date this report is approved. Copies of the relevant extract from the Articles of Association are available for inspection at the registered office of the Company during normal business hours on any weekday and will be available at the venue of the 2018 Annual General Meeting from 15 minutes before the meeting until it ends.

All Directors have deeds of indemnity. These will be available for inspection at the Annual General Meeting with the service contracts.

POWERS OF DIRECTORS

The business of the Company shall be managed by the Directors who are subject to the provisions of the Companies Act 2006, the Articles of Association of the Company and to any directions given by special resolution, including the Company's power to repurchase its own shares.

The Company's Articles of Association may only be amended by a special resolution of the Company's shareholders.

CHANGE OF CONTROL

All the Company's share schemes contain provisions in relation to a change of control. Outstanding options and awards would normally vest and become exercisable on a change of control, subject to the satisfaction of any performance conditions at that time.

Capita has a number of borrowing facilities provided by various banks and other financial institutions. Capita's bank debt contains a change of control provision under which the banks may require immediate repayment in full on change of control. The bonds issued by Capita contain a change of control provision which requires the Group to offer to prepay the bonds in full if a change of control event occurs and Capita does not obtain an investment grade credit rating.

There are a number of significant client agreements which contain provisions relating to change of control, which in some cases could present a right of termination of the contract.

RIGHTS AND RESTRICTIONS ATTACHING TO SHARES

Under the Company's Articles of Association, holders of ordinary shares are entitled to participate in the receipt of dividends pro rata to their holding. The Board may propose and pay an interim dividend and recommend a final dividend in respect of any accounting period out of the profits available for distribution under English law. A final dividend may be declared by the shareholders in general meeting by ordinary resolution, but no dividend may be declared in excess of the amount recommended by the Board.

At any general meeting a resolution put to vote at the meeting shall be decided on a poll. On a poll, every member who is present in person or by proxy shall have one vote for every share of which they are the holder.

No person holds securities in the Company carrying special rights with regard to control of the Company. The Company is not aware of any agreements between holders of securities that may result in restrictions on the transfer of securities or on voting rights.

RESTRICTIONS ON TRANSFER OF SHARES

The Company's Articles of Association allow Directors to, in their absolute discretion, refuse to register the transfer of a share in certificated form unless the instrument of transfer is lodged, duly stamped, at the registered office of the Company, or at such other place as the Directors may appoint and (except in the case of a transfer by a recognised person where a certificate has not been issued in respect of the share) is accompanied by the certificate for the share to which it relates and such other evidence as the Directors may reasonably require to show the right of the transferor to make the transfer. They may also refuse to

register any such transfer where it is in favour of more than four transferees or in respect of more than one class of shares.

The Directors may refuse to register a transfer of a share in uncertificated form in any case where the Company is entitled to refuse (or is exempted from the requirement) under the Uncertificated Securities Regulations to register the transfer.

ANNUAL GENERAL MEETING

The 2018 Annual General Meeting (AGM) of the Company will be held at Linklakers LLP, One Silk Street, London EC2Y 8HQ on 26 June 2018. At the AGM a number of resolutions will be proposed. The resolutions are set out in the Notice of Meeting, which is sent to shareholders with the 2017 Annual Report and includes notes explaining the business to be transacted and is also available on the Company's website at www.capita.com.

In June 2017, shareholders granted authority for the Company to purchase up to 66,714,100 ordinary shares – this authority will expire at the conclusion of the 2018 AGM. No shares were purchased during 2017. A resolution to renew this authority will be put to shareholders at the 2018 Annual General Meeting.

The Directors consider that each of the resolutions are in the best interests of the Company and the shareholders as a whole and recommend that shareholders vote in favour of all of the resolutions.

For other general meetings the notice given would be 14 working (clear) days.

CROSS REFERENCES

For the purposes of LR 9.8.4R the following information is located as set out below:

Listing Rule	Subject	Page No.
9.8.4 (1)	Capitalisation of interest	103
9.8.4 (2) (4-11) and (14)	n/a	n/a
9.8.4 (12-13)	Shareholder waiver of dividends	59

STATEMENT OF DIRECTORS' RESPONSIBILITIES IN RESPECT OF THE ANNUAL REPORT AND THE FINANCIAL STATEMENTS

The Directors are responsible for preparing the Annual Report and the Group and parent company financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare Group and parent company financial statements for each financial year. Under that law they are required to prepare the Group financial statements in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU and applicable law and have elected to prepare the parent company financial statements in accordance with UK Accounting Standards and applicable law (UK Generally Accepted Accounting Practice) including FRS 101 Reduced Disclosure Framework.

Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and parent company and of their profit or loss for that period. In preparing each of the Group and parent company financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently.
- make judgements and estimates that are reasonable and prudent.
- for the Group financial statements, state whether they have been prepared in accordance with IFRSs as adopted by the EU.
- for the parent company financial statements, state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the parent company financial statements.
- assess the Group and parent company's ability to continue as a going concern disclosing, as applicable, matters related to going concern; and
- use the going concern basis of accounting unless they either intend to liquidate the Group or the parent company or to cease operations, or have no realistic alternative but to do so.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the parent company's transactions and disclose with reasonable accuracy at any time the financial position of the parent company and enable them to ensure that its financial statements comply with the Companies Act 2006.

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

Under applicable law and regulations, the Directors are also responsible for preparing a strategic report, Directors' report, Directors' remuneration report and corporate governance statement that comply with that law and those regulations.

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

Details of the principal risk categories can be found on pages 38–43.

APPROVAL OF THE ANNUAL ACCOUNTS

Responsibility statement of Directors in respect of the annual financial statements

We, the Directors of the Company, confirm that to the best of our knowledge:

- The financial statements prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and the undertakings included in the consolidation as a whole.
- The Directors' report, including content by reference, includes a fair review of the development and performance of the business and the position of the Issuer and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

Directors' statement on the Annual Report

The Directors consider the Annual Report, taken as whole, to be fair, balanced and understandable and that it provides the information necessary for the shareholders to assess the Company's position and performance, business model and strategy.

The Directors' report (pages 1 to 89) has been approved by the Board.

On behalf of the Board

Francesca Todd
Group Company Secretary
23 April 2018

Capita plc
Registered in England and Wales No. 2081330

COMMITTEES

COMMITTEES' TERMS OF REFERENCE

The terms of reference of the Nomination, Remuneration and Audit and Risk Committees (standing committees) were reviewed during the year. The terms of reference are summarised below and, along with the matters reserved for the Board, are displayed in full in the investor centre at www.capita.com/investors.

Terms of reference	Brief description of responsibilities
Nomination Committee	Reviews composition of the Board. Recommends appointment of new Directors. Considers succession plans for Chairman and Executive positions. Reviews and recommends Group diversity statement.
Audit and Risk Committee	Reviews accounting policies and contents of financial reports. Monitors internal control environment. Considers adequacy, effectiveness and scope of external and internal audit programme. Oversees relationship with our external Auditor. Monitors risk profile and obtains assurance that principal risks have been properly identified and appropriately managed.
Remuneration Committee	Sets policy for Executive Directors' and senior executives' remuneration. Approves individual remuneration awards. Agrees changes to senior executive incentive plans.
Disclosure Committee	A Disclosure Committee, comprising any two of the Chairman, Senior Independent Director and the Executive Directors , is responsible for the appropriate identification and management of inside information, including any decision to delay public disclosure.

MEMBERSHIP OF THE COMMITTEES

Membership of the Company's standing committees at the end of the year is shown below:

	Sir Ian Powell	Gillian Sheldon	John Cresswell	Matthew Lester	Andrew Williams	Baroness Lucy Neville-Rolfe
Nomination	(C)x	x	x	x	x	x
Audit and Risk		x	x	(C)x	x	x
Remuneration		x	(C)x	x	x	x

(C) Chair.

Matthew Lester was appointed Chair of the Audit and Risk Committee with effect from 1 June 2017.

FREQUENCY OF COMMITTEE MEETINGS AND ATTENDANCE

During 2017, the Nomination Committee met six times, the Remuneration Committee met 10 times and the Audit and Risk Committee met 13 times. The increase in Committee meetings during 2017 was due to significant changes in Board composition that took place during the year and the need to consider certain accounting matters such as adoption of IFRS 15. Attendance of the Board Directors at Committee meetings is shown in the following table:

	Audit and Risk Committee	Remuneration Committee	Nomination Committee
Number of meetings	13	10	6
Sir Ian Powell*	n/a	n/a	6
Gillian Sheldon	13	10	6
Matthew Lester**	10	5	2
Andrew Williams	12	8	5
John Cresswell	13	10	6
Baroness Lucy Neville-Rolfe***			

* Sir Ian Powell is not a member of the Audit and Risk Committee and Remuneration Committee, but has been invited and attended all meetings.
** Matthew Lester was appointed to the Board on 1 March 2017.
*** Baroness Lucy Neville-Rolfe was appointed to the Board on 6 December 2017.

Due to the nature of the acquisition and bid strategy, consideration of meeting times has to include flexibility to hold meetings outside of this timetable and meetings of this nature tend to be held by telephone.

Any Director's absence from meetings of the Audit and Risk, Remuneration or Nomination Committees was previously agreed with the Chairman of the Board, the Chief Executive Officer or the Chair of the relevant committee.

NOMINATION COMMITTEE

IMAGE REMOVED

"I am pleased to present the report on the activities of the Nomination Committee for the year to 31 December 2017. Set out below is a summary of the work carried out during the year."

SIR IAN POWELL, CHAIR, NOMINATION COMMITTEE

MEMBERS:

- Sir Ian Powell (Chair)
- Gillian Sheldon
- Matthew Lester
- Andrew Williams
- John Cresswell
- Baroness Lucy Neville-Rolfe

The Group Company Secretary acts as Secretary to the Committee and is available to assist the members of the Committee as required, ensuring that timely and accurate information is distributed accordingly.

The Committee met six times in 2017 and the attendance is shown on page 64.

The Committee reports and makes recommendations to the Board in relation to its activities and deliberations.

It is authorised under its terms of reference to obtain the advice of independent search consultants. The terms of reference for the Nomination Committee can be found on Capita's website at www.capita.com/investors. These were reviewed and updated during the year.

DIVERSITY

Capita's Equality & Diversity policy is based on the belief that success is a direct result of the experience and quality of its employees. Inherent within this approach is an acceptance and embracing of diversity in all its forms and an endorsement that the entire workforce, including the Board, be representative of the community in which Capita operates. Key aims of the policy are to ensure equality, diversity and inclusion in the workplace and to promote a culture where everyone is treated with respect and dignity.

Following the appointment of Jon Lewis as Chief Executive Officer, and in the light of recommendations contained in recent government-backed diversity reviews, the action plan on diversity among Non-Executive Directors is being blended with a wider review of the Group's culture and a new Board Diversity policy is being developed and is expected to be completed during 2018.

As at 31 December 2017, 15% of our senior management team and 22% of our Board were women. At the date of this report, 25% of the Board were women. Capita sees significant business benefit in having access to the diversity of thinking that comes from people with a wide range of backgrounds at all levels in the Company. Only by encouraging this diversity and by fostering talent throughout the business can the Company expect to achieve further diversity in senior management. Capita has a network of diversity champions across the businesses and the Company's training and mentoring initiatives actively support the fostering of talent at all levels in the business across the Company's diverse workforce. The Board and senior management teams across Capita are fully committed to working to provide an environment where everyone has the opportunity to fulfil their potential. The Company will continue to appoint and promote people on merit and in line with the skills and attributes identified for each post while striving to increase diversity at the Board level during 2018 in line with the policy that is being developed. Further information is shown on page 24 of the strategic report.

COMMITTEE ACTIVITIES DURING 2017

Key responsibilities	Activity in 2017
– to identify and nominate appropriate candidates for appointment to the Board, having due regard to the provisions of the Code and, in particular, the balance of skills, knowledge and experience on the Board and the diversity of its composition – to keep the structure and size of the Board and the leadership needs of the organisation under review and ensure that plans are in place for orderly succession and appointment to the Board – to review the time commitment required from Non-Executive Directors, the performance of Directors and all declarations of interest made by Board members – to consider Capita's diversity position.	Succession planning for the Board generally and for other senior positions below Board level; Recruitment and appointment of new Chief Executive Officer; Recruitment and appointment of new Audit and Risk Committee Chair; Consideration of the performance of all Directors, length of service, interests and potential conflicts to ensure that all Directors could stand for re-election or election at the AGM; Diversity of the Board; Conflicts of Interests considered for the independence of the Non-Executive Directors; For all the appointments to the Board the Committee considered the size and structure of the Board and the balance and range of the Directors' knowledge and experience; External search agencies were used for the Non-Executive and Chief Executive Officer appointments; Discussed and approved the resignation of Vic Gysin. The external search agencies used (Lygon Group for the Chief Executive Officer and Ridgeway Partners for Baroness Lucy Neville-Rolfe) do not have any other connection with the Company.

AUDIT AND RISK COMMITTEE

IMAGE REMOVED

"I am pleased to present my first report as Chairman of the Audit and Risk Committee (the Committee) covering the year to 31 December 2017, having taken up post on 1 June 2017."

MATTHEW LESTER, CHAIR, AUDIT AND RISK COMMITTEE

MEMBERS:

- Matthew Lester (Chair – from 1 June 2017)[1]
- Gillian Sheldon
- Andrew Williams
- John Cresswell
- Baroness Lucy Neville-Rolfe

1 Paul Bowtell resigned from the Board and as Chair of the Committee on 31 May 2017.

I have reviewed the operation and the role of the Committee to ensure that it provides the support to the Group Board that is the necessary part of its function.

I have assessed that the Committee fulfils its role of supporting the Board in its review of the integrity of the Group's financial reporting, monitoring the effectiveness of the Group's systems of risk management and internal controls, and overseeing the activities of the Group's internal audit function and its external Auditor. However, it is incumbent on me as chairman to review and improve with a view to ensuring continuous and effective support to the Board.

In this regard I have adjusted the standing agendas, the qualitative reporting into Committee meetings and the absolute responsibilities for those attendees at meetings both permanent or by invitation to provide a platform to discuss and challenge and therefore engender a robust forum to deliver the Committee's role and responsibilities.

COMMITTEE MEMBERSHIP AND ATTENDANCE AT MEETINGS

All members of the Committee are independent and I am considered to have recent and relevant financial experience for the purposes of the UK Corporate Governance Code (the Code). The composition of the Committee was reviewed and the blend of skills and experience across all members taken into account in order to form the view that, as a whole, the Committee has competence relevant to the sector in which the Group operates.

To encourage effective communication, in addition to the above members, the Board Chairman, Chief Executive Officer, Chief Financial Officer and Director of Group Finance are invited to attend Committee meetings along with certain members of the senior management team, the Head of Internal Audit, the Director of Group Risk & Compliance, and representatives from KPMG LLP, the Group's external Auditor. Opportunity exists at the end of each Committee meeting for the representatives of the Internal and External audit teams to meet with the Committee in the absence of management and both have access to the Committee should they wish to voice any concerns outside of the formal meetings.

The performance of the Committee is assessed as part of the Board performance evaluation undertaken annually. The Board is satisfied that the combined knowledge and experience of its members is such that the Committee discharges its responsibilities in an effective, informed and challenging manner and that, as a whole, the Committee has the competence relevant to the sector in which the Company operates.

The Group Company Secretary acts as Secretary to the Committee and is available to assist the members of the Committee as required, ensuring that timely and accurate information is distributed accordingly.

HOW THE COMMITTEE OPERATES

The Committee has established an annual forward agenda to cover the key events in the financial reporting cycle, specific risk matters identified by the Committee and standing items that the Committee is required to consider in accordance with its terms of reference. The annual agenda is supported by agenda setting meetings held in advance of each Committee meeting, led by me and attended by senior management. The purpose being to identify key issues impacting the business that may require consideration by the Committee.

Reports are received from the Group Risk & Compliance and Group Internal Audit departments and new sales wins and their contract terms are reviewed from a risk and accounting perspective as appropriate. At each Committee meeting the members may receive other reports and presentations covering key financial reporting, risk, compliance and audit matters which are delivered by key senior personnel who attend by invitation to enable any clarification or queries to be provided to the Committee. I report to the Board the key matters of discussion and make any significant recommendations as necessary.

ROLE AND RESPONSIBILITIES

The Audit and Risk Committee is responsible for carrying out the audit functions as required by DTR 7.1.3R and assists the Board in fulfilling its oversight responsibilities in respect of the Company and the Group. The Committee's key responsibilities are:

Financial Reporting	to review the reporting of financial and other information to the shareholders of the Company and monitor the integrity of the financial statements, including the application of key judgments in determining reported outcomes to ensure that they are fair, balanced and understandable
Risk management, internal controls and compliance	to review and assess the adequacy of the systems of internal control and risk management and monitor the risk profile of the business
Internal audit	to approve the annual internal audit plan, review the effectiveness of the internal audit function and review all significant recommendations and ensure they are correctly addressed in a timely manner
External audit	to review the effectiveness and objectivity of the external audit process, assess the independence of the Auditors and ensure appropriate policies and procedures are in place to protect such independence
Cyber security	to review and assess the cyber security risk and governance including the IT security for the Group and monitor the risks within this area
Effectiveness	to report to the Board on how it has discharged its responsibilities

The Audit Committee's terms of reference set out in full the role, responsibilities and authority of the Committee and can be found on the Company's website at www.capita.com/investors. These were reviewed and updated during the year.

HOW THE COMMITTEE DISCHARGED ITS ROLES AND RESPONSIBILITIES IN 2017

The Committee met 13 times during the year and attendance at each meeting is shown on page 64. Meetings are planned around the financial calendar for the Company.

In 2017, the Committee held a number of additional unscheduled meetings to discuss the impact, receive training, to consider the transitional arrangements and the effect on the financial statements of the early adoption of IFRS 15 – Revenue from Contracts with Customers (IFRS 15). This was a significant accounting policy change which required the review of every contract within the Group's portfolio to determine how revenue would be measured and recognised under this new standard.

IFRS 15 is effective for annual reporting periods beginning on or after 1 January 2018, with early adoption permitted. The Group has chosen to early adopt, with an adoption date of 1 January 2016 and presented its results under IFRS 15 for the first time in its interim results for June 2017, restating comparatives accordingly.

FINANCIAL REPORTING

Accounting judgements and significant accounting matters

As part of the process of monitoring the integrity of the financial information presented in the interim and these annual accounts the Committee reviewed the key accounting policies and judgements adopted by management to ensure that they were appropriate. The significant areas of judgement identified by the Committee, in conjunction with management and the external Auditor, together with a number of areas that the Committee deemed significant in the context of the financial statements are set out in the tables on pages 68 to 71.

Fair, balanced and understandable

At the Board's request, the Committee considered whether the Interim and Annual Reports were fair, balanced and understandable and whether the information provided was sufficient for a reader of the statements to understand the Group's position and performance, business model and strategy. The Committee reviewed both the narrative and financial sections of the report to ensure that they were consistent and gave a balanced view of the performance of the business in the year both positive and negative and that appropriate weight was given to each. It also assessed whether important communications for the year were presented clearly.

In light of the recent publication issued by the Financial Reporting Council (the FRC) which served as a reminder of Boards' reporting obligations, particularly for those in the construction and business support services sectors, the Committee has also considered whether the Annual Report and Accounts enable readers of the statements to understand the Company's financial position and prospects as well as assess its going concern status and longer-term viability.

It was the Committee's opinion, having conducted this review and viewed as a whole, that the Reports as presented did measure up to the fair, balanced and understandable benchmark and thus have made recommendations to the Board in this regard.

Communications with the FRC

In October 2017, the Company received a letter from the FRC following the announcement in December 2016 that it would conduct a thematic review of companies' reporting relating to significant judgements and sources of estimation uncertainty, with the objective of improving the quality of disclosures in this area. The Committee is pleased to report that, having been selected for this review, the FRC concluded that there were no substantive issues to raise with the Board or Committee albeit that certain presentational recommendations were made. Please note that the review carried out by the FRC only covered the specific disclosures relating to this thematic review and provided no assurance that the Annual Report and Accounts were correct in all material respects. The FRC's role is not to verify the information provided but to consider compliance with reporting requirements.

AUDIT AND RISK COMMITTEE CONTINUED

Significant issues in relation to the financial statements considered by the Audit and Risk Committee

GOING CONCERN

Matter considered	Action	Outcome
Consideration of the going concern assumption is the responsibility of the Board, and the Committee conducted an assessment as part of its support role given the inherent judgements required to be made in relation to the forecasts and definitions within the covenant calculations.	The going concern assertion has a significant impact on the basis of preparation of the financial statements. The Committee considered the 'base case' set of projections that cover the first two years of the new strategic plan to 31 December 2019. The Committee considered the assumptions behind the plausible but severe downside scenarios used for stress testing the Group's ability to meet its obligations as they fall due. It also considered and challenged the mitigating actions proposed by management. The Committee has challenged the key assumptions as set out on page 60. The Committee considered compliance with the key covenants included in the Group's committed facilities and private placement notes including maximum ratios of adjusted net debt to adjusted EBITDA. The Committee considered the judgements made by management in calculating the adjusted EBITDA. In particular, consideration was given to consistency of treatment with the prior year, including the exclusion of restructuring. Applying the downside scenarios the Committee concluded that absent the anticipated net proceeds from the Rights Issue, and assuming no mitigating actions are taken, the available headroom is not sufficient to operate within the 3.0 adjusted net debt to adjusted EBITDA. The Committee considered the going concern assumption disclosures. In particular, they considered the fact that a shareholder vote is required in order to raise additional capital through a Rights Issue, and that the standby underwriting agreement is subject to certain specific conditions which are outside the control of the Company, and the conclusion that these events and conditions indicate a material uncertainty on the success of the Rights Issue which may cast significant doubt about the Group's and parent company's ability to continue as a going concern. The Committee considered the requirements of the Code as it applies to the Group's viability statement including the three-year period of assessment which aligns with the Group's planning horizon and the processes supporting the viability statement. After significant discussion and having considered the various stress testing scenarios that were presented as part of the viability assessment alongside the liquidity and debt positions of the business, the Committee determined that the three-year measurement period continued to be appropriate and that the viability statement (as set out on page 44) should be recommended to the Board for approval.	The Committee is satisfied that pages 60 to 61 include detailed disclosures concerning the going concern assertion and key assumptions applied to inform the users of the assessment undertaken by the Board.

IFRS 15 AND BALANCE SHEET RESTATEMENT

Matter considered	Action	Outcome
The adoption of IFRS 15 has led to significant changes in the revenue recognition policies across the Group and significant restatement of prior period balance sheets and income statements. The project was complex and involved reviewing a significant number of contracts due to the bespoke nature of the Group activities.	The Committee received training on the major impacts of the adoption of the standard and considered the benefit of early adoption against a general review of the landscape of revenue recognition across the Group and the expected impact to the financial statements. Additionally, the Committee reviewed the transitional statement which detailed the effect on the prime statements and which was included in the half-year results issued on 21 September 2017. The Committee approved all accounting policies associated with the new revenue recognition standard.	On 7 September, the Group released the 2016 results restated for the adoption of IFRS 15 and hosted a presentation to investors and analysts. IAS 8 sets out the disclosure requirements for adopting a new IFRS. These are commonly dealt with in a 'transition note' which the Company published on 7 September. The 2017 half-year financial statements included this 'transition note' as an appendix detailing the impact of the adoption on the reported 2016 financial information. The Group's accounting policy for revenue has been completely rewritten to reflect the adoption of IFRS 15. This new policy is included in full in note 2 to the consolidated statements. The new policy also includes the treatment in respect of accounting for contract fulfilment assets, first year profits or losses and redundancy costs. The new policy also includes disclosure of significant judgements and estimates in relation to the application of these accounting policies.

REVENUE RECOGNITION

Matter considered	Action	Outcome
Following the adoption of IFRS 15 there is significant risk on long-term contracts related to revenue recognised from variations or scope changes, where significant judgement is required to be exercised by management. There is a risk that revenue may be recognised even though it is not probable that consideration will be collected, which could be due to uncertainties over contractual terms and ongoing negotiations with clients.	The Committee received regular updates on all major contracts during the transition to IFRS 15, throughout the year and specifically reviewed the material judgements as part of the year-end close process. The Committee has also considered the recognition of onerous provisions, where appropriate, and the lifetime profitability of contracts. The Committee received presentations from management that captured the key judgements applied under the new accounting policies adopted and for software sales, this included the adoption of policies to ensure appropriate recognition of revenue be that over time or point in time.	The new revenue recognition policy includes disclosure of the significant judgements and estimates in relation to its application and the Committee is satisfied that these have been properly disclosed. The Committee is satisfied that the disclosures given within the accounts are sufficient to gain a proper understanding of the methodology of accounting for revenue across the Group including the recognition of deferred income at the balance sheet date.

CONTRACT FULFILMENT ASSETS

Matter considered	Action	Outcome
The adoption of IFRS 15 has also led to the recognition of contract fulfilment assets (CFAs). Judgments are involved in assessing whether the costs incurred on a contract, or an anticipated contract meet the capitalisation criteria as set out under the standard. In addition, the amortisation of these assets involves estimation of the expected life of the contract.	As part of the adoption of IFRS 15, the Committee has considered and challenged the significant judgments and estimates involved in determining the carrying value of CFAs. As part of the review of all major contracts, the Committee has also considered the recoverability of CFAs.	The Committee is satisfied that appropriate judgments and estimates have been made in determining the carrying value of CFAs and the extent of impairment of CFAs recognised in these statements is appropriate. The Committee is satisfied that the accounting policy note provides sufficient clarity as to the new policy adopted.

AUDIT AND RISK COMMITTEE CONTINUED

IMPAIRMENT OF INTANGIBLE ASSETS, GOODWILL AND PARENT COMPANY'S INVESTMENT IN SUBSIDIARIES

Matter considered	Action	Outcome
The Group carries significant asset balances in respect of goodwill and intangible assets related to its acquisition activity. In addition, the parent company carries a material balance of investment in subsidiaries on its financial statements. The impairment assessment requires the application of judgement concerning future prospects and forecasts.	The Committee has reviewed the robustness of the impairment model and challenged the appropriateness of assumptions used to calculate and determine the existence of impairment. The Committee considered the events and circumstances that have led to the impairment charges since the publication of the interim results in September 2017. In particular, the Committee considered the continuing challenges both operationally and within the market served, the continued attrition in sales and the more significant contract terminations experienced in the later part of 2017 and early 2018. Following the update on the outlook for trading announced on 31 January 2018, the Committee has also re-reviewed the changes to the assumptions underpinning the impairment calculations. In particular, the Committee considered and challenged the appropriateness of the longer time horizon used in the revised model and the changes made to the growth and discount rates. The impairment of goodwill and intangible assets at Group level indicates that there may also be impairment of investment in subsidiaries on the parent company's financial statements. Accordingly, the Committee has reviewed the assumptions and calculation of impairment of these investments.	The Committee is satisfied that the impairment of goodwill and intangibles recognised in these statements is in line with expectations given the performance of certain areas of the Group's business in the year and the update on the trading outlook. The Committee is also satisfied that the assumptions, methodology and disclosure in note 16 are sufficient to give the reader an understanding of the action taken and the sensitivities within the goodwill and intangible assets balance to any further impairment risk. Of particular importance to the Committee was the inclusion of sufficient disclosures to set out the events and circumstances that have led to the impairment charges recorded in the year. The Committee also considered the impairment of investment in subsidiaries at the parent company level were appropriate and properly accounted for.

ITEMS DISCLOSED AS NON-UNDERLYING

Matter considered	Action	Outcome
As stated in its accounting policies, Capita separates its results between underlying and non-underlying to provide useful disclosure to aid the understanding of the performance of the Group: The Group separately presents intangible amortisation, certain asset impairments, acquisition contingent consideration movements, the financial impact of business exits or businesses in the process of being exited, acquisition expenses, movements in the mark-to-market valuation of certain financial instruments, and specific non-recurring items in the income statement which, in the Directors' judgement, need to be disclosed separately by virtue of their nature, size and incidence in order for users of the financial statements to obtain a proper understanding of the financial information and the underlying performance of the business.	The Committee has reviewed the individual items disclosed as non-underlying to understand the nature of each item and whether treatment as non-underlying is in line with the principal outcome of presenting a fair, balanced and understandable set of financial statements and commentary. The Committee has requested further information concerning the origination of the items disclosed where they felt it was necessary to enable a conclusion to be drawn as to whether the chosen presentation achieved the stated principal. The Committee has considered the accounting policy by reference to guidance issued by the FRC and the need to ensure any alternative performance measures are presented with equal prominence to reported figures and on a consistent basis year on year.	The Committee concurs with management's view that the presentation of items as non-underlying provides useful disclosure to aid the understanding of the performance of the Group and agree that the items disclosed in this category meet with the stated policy for recognition. Note 6 sets out the items that are separately presented, and the Committee is satisfied that this provides sufficient information to inform a reader on each category presented.

PROVISIONS AND CONTINGENT LIABILITIES

Matter considered	Action	Outcome
There is judgement applied in the level of provisioning across the Group. This involves making an assessment of the size, timing and probability of economic outflows due to the occurrence of a past event. It is therefore important to understand the judgement being made as well as the estimate of any accompanying outflow of funds.	The Committee has reviewed the disclosure in the financial statements and where necessary has sought further information from management to gain a fuller understanding of the items recorded. In particular, the Committee challenged the disclosure of the Connaught provisions in the interim financial statements and the classification of items as contingent liabilities, provisions or otherwise. The larger Capita Asset Services (CAS) provisions have been reviewed in light of the indemnity provided by Capita plc to the purchasers of the CAS business regarding certain existing matters.	The Committee is satisfied that the fact patterns underlying the provisions lead to the judgement that a provision is required, that it is properly estimated as to value and that the disclosure in the accounts is sufficient to gain an understanding of the nature of the provisions recognised (or any contingent liabilities recognised) and the impact they have on the financial statements.

PENSIONS		
Matter considered	**Action**	**Outcome**
The measurement of the defined benefit liability in respect of defined benefit pension schemes operated within the Group is a complex area, relying on assumptions on inflation, mortality, corporate bond yields, expectations of returns on assets and a number of other key inputs. There is a risk that any one of these could lead to misstatement of the Group's liability in respect of pension obligations and the pension charge or movement recognised in the income statement or statement of comprehensive income.	The Committee has reviewed the disclosure as presented in the accounts. The Committee also challenged the key assumptions and reviewed the sensitivity to changes in some of the key assumptions both on a standalone basis as well as in the context of defined benefit schemes across other external benchmarks.	The Committee is satisfied that the estimation of the Group's pension liabilities and the narrative that accompanies them gives the required level of information for a reader of the accounts to determine the impact on the Group of its pension obligations. The Committee also notes that in the year the Capita Life & Assurance Pension Scheme was closed to further accrual for a large body of members and the Committee reviewed the disclosure in respect of this within the accounts.

OTHER ISSUES IN RELATION TO THE FINANCIAL STATEMENTS CONSIDERED BY THE AUDIT AND RISK COMMITTEE

Materiality

Materiality is important in determining the risk attached to any judgement. The Committee considers the audit materiality set by the external Auditor to ensure that the Audit and Risk Committee is informed of individual items above a certain threshold that are most likely to have an impact on the financial statements. The Audit and Risk Committee reviews the external Auditor's report and the individual items that breach the materiality thresholds and assess their relative impact on the reported statements: income statement, balance sheet, statement of changes in equity and cash flow as well as the notes to the accounts.

The Committee requests further clarification from both the external Auditor, the Chief Financial Officer and Director of Group Finance as to the nature of these items and also their relative importance in the financial statements.

After having made such enquiries, the Audit and Risk Committee is satisfied that materiality has been applied correctly in the accounts and that material items brought to its attention remain unadjusted where its inclusion would not cause detriment to the overall reading of the financial statements.

Disclosure of information to Auditor

The Directors who held office at the date of the 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 steps that they ought to have taken as a Director to make themselves aware of any relevant audit information and to establish that the Company's Auditor is aware of that information.

Statutory Auditor

The Committee provides a forum for reporting by the Group's Auditor (KPMG), and it advises the Board on the appointment, independence and objectivity of the Auditor and on the remuneration for both statutory audit and non-audit work. It also discussed the nature, scope and timing of the statutory audit with the Auditor. The Audit and Risk Committee annually performs an independent assessment of the suitability and performance of the Auditor in making its recommendation to the Board for their re-appointment.

The external Auditor attends meetings of the Committee and reports to the Committee on the statutory reporting, non-audit fees and ongoing audit items.

Auditor independence

The Committee takes seriously its responsibility to put in place safeguards to Auditor objectivity and independence. The Company is committed to ensuring appropriate independence in its relationship with the Auditor and the key safeguards are:

- The Chief Financial Officer monitors the independence of the Auditor as part of the Group's assessment of Auditor effectiveness and reports to the Audit and Risk Committee.
- The Chief Financial Officer monitors the level and nature of non-audit fees accruing to the Auditor, and specific assignments are discussed in advance with the Auditor and flagged for the approval of the Audit and Risk Committee, as appropriate, and in accordance with the Company's policy on the provision of non-audit services by the Auditor. The Audit and Risk Committee reviews, in aggregate, non-audit fees of this nature on a six-monthly basis and considers implications for the objectivity and independence of the relationship with the Auditor.
- The Statutory Auditor provides bi-annual confirmations of its independence to the Audit and Risk Committee.

Ensuring conflicts of interest are avoided is a fundamental criterion in the selection of any third-party auditor for assignments with which the Group is involved. Such conflicts may arise across public or private sector clients and key supplier relationships, for example, and are a key determinant in the award process for external audit assignments.

Non-audit fees

The Committee has established a policy on the provision of services by the Group's Auditor. The policy describes the circumstances in which the Auditor may be permitted to undertake non-audit work for the Group. The Committee oversees compliance with the policy and considers and approves requests to use the Auditor for non-audit work. Any assignment where the expected fee is above £150,000 requires specific approval from the Committee or a member of the Committee. The Group Company Secretary deals with day-to-day administration of the policy, facilitating requests for approval by the Committee. All work with the external Auditor outside of the audit has to be pre-approved by the Chief Financial Officer, Nick Greatorex. The Auditor undertook various non-audit work such as assistance on acquisitions and bids across our business in 2017. Only the Audit and Risk Committee can authorise the scope and policy on non-audit fees.

Non-audit fees this year are at 16% (2016: 21%), as a percentage of all fees paid to the external Auditor. The Committee continued to receive updates throughout the year on the level of fees which have been approved where, as an individual instance, they were over the threshold stated above.

AUDIT AND RISK COMMITTEE CONTINUED

The policy is reviewed by the Committee annually. Details of audit and non-audit fees are given in note 8 of the consolidated financial statements and a summary of non-audit fees is shown in the table below.

	2017 £m	2016 £m
Non-audit services		
Taxation compliance services	0.1	0.1
Taxation advisory services	–	0.1
Services related to corporate finance transactions	0.1	0.1
Other assurance services	0.8	0.5
Other non-audit services	0.0	0.1
Total non-audit services	1.0	0.9

The FRC's 2016 Revised Ethical Standard introduced further restrictions on the provision of non-audit services. The new Standard applies to Capita with effect from 1 January 2017 and steps were taken with the external Auditor to ensure that ongoing services prohibited by the new Standard from 1 January 2017 had been completed by 31 December 2016.

External Auditor performance

The Committee discussed the performance of KPMG during the period and was satisfied that the level of communication and reporting was in line with requirements. This also included a review of effectiveness and quality of the audit process. The evaluation of KPMG also included the planning of the audit and a post-audit evaluation.

The evaluation focuses on understanding and challenging how the Auditor demonstrates the effectiveness of key professional judgement made throughout the audit and how this might be supported by evidence of the following critical auditor competencies:

- A mindset and culture that exhibits integrity and objectivity and is aligned with the expectations and interests of stakeholders of their reports.
- The skills and knowledge to develop a thorough understanding of the Company's business and industry, the environment in which it operates and of the applicable legal and regulatory framework, and the strength of character to provide effective challenge in performing the Audit.
- The ability to establish effective quality control by putting in place the processes necessary to deliver a consistently high quality audit.

The Audit and Risk Committee has ensured that the evaluation is integrated with other aspects of their role related to ensuring the quality of the financial statements – obtaining evidence of the quality of the Auditor's judgements made throughout the audit, in identifying audit risks, determining materiality and planning their work accordingly, as well as in assessing issues.

External Auditor re-appointment

The Company's audit services were last subject to a tender process in 2010, at which time KPMG Audit Plc, subsequently KPMG LLP, replaced Ernst & Young LLP as the Group's Auditor. The lead audit partner is rotated on a five-yearly basis. The current lead audit partner rotated on to the audit at the conclusion of the 2016 audit. There are no contractual obligations which restrict the Committee's choice of auditor.

Under the requirements of the Statutory Audit Services Order and the EU Audit Directive and Audit Regulation the provision of audit services should be re-tendered every 10 years. The complex nature and continued growth of the Group requires that a knowledge base is built up year on year by the incumbent to ensure that the external audit is conducted with a proper understanding of the Group's operations and the nature of the risks that it faces. This is an important factor in ensuring audit quality and therefore the Group have commenced planning for a tendering process to ensure that it is in a position to meet the 10-year requirement to re-tender the Group's audit. The Group has complied with the provisions of the Statutory Audit Services Order.

It is proposed that KPMG LLP be put forward as the Auditor of the Company at the forthcoming Annual General Meeting and will hold office from the conclusion of this meeting until the conclusion of the next general meeting at which accounts are laid before the Company, and that their remuneration be fixed by the Committee.

A resolution to re-appoint KPMG LLP as the Auditor of the Company will be put forward at the forthcoming Annual General Meeting.

Risk management and internal control

The Committee is responsible for reviewing the effectiveness of the Group's system of internal control and risk management. The system of internal control is designed to manage rather than eliminate the risk of failure to achieve business objectives and can only provide reasonable and not absolute assurance against material misstatement or loss. The Board has established a clear organisational structure with defined authority levels. The day-to-day running of the Group's business is delegated to the Executive Directors of the Company. The Executive Directors meet with both operational and finance management on a monthly basis through the Group's programme of monthly performance review meetings where key financial and operational measures are reported on a monthly basis and measured against both business plan (budget) and monthly re-forecasts.

The Committee receives regular reports from the Group Risk & Compliance Director and the Group Internal Audit Director utilising the Risk Framework the Group embedded through the organisation. This framework is a combination of corporate principal risks (top down) as utilised to assess going concern and the Longer Term Viability Statement as set out on page44 and business risks determined by each division. The bottom up business risks are mapped into the corporate risk. These risks are assessed regularly to determine whether the controls are operating within a tolerance level of the Group's appetite to risk or whether the level of risk is deemed as uncomfortable or critical. Whenever a risk is considered critical, a thorough review is conducted as to why this is and what immediate mitigating actions need to be taken. When a risk status moves adversely between meetings this risk is also thoroughly investigated.

On a monthly basis, through the reporting process, each business unit is required to prepare a risk assessment process on the key strategic, operational, financial and accounting risks to identify, evaluate and manage the significant risks to the Group's business. They include common definitions of risk and ensure, as far as practicable, that the policies and procedures established by the Board are appropriate to manage the perceived risks to the Group.

During the year, the Committee focused on key risk themes such as IT resilience, cyber risk, health and safety, anti-bribery and corruption, management of client money, property risk, regulatory risk, information security and data management. There was a particular focus by the Committee on IT resilience in the year, due mainly to a limited, but significant outage in our main datacentre in May.

The update on the trading outlook announced on 31 January 2018 highlighted that there has been a weakness in the accuracy of forecasting and translation of financial risks in the existing risk framework. The Board, with the advice of the Committee, will review the learnings from 2017 and early 2018 and act to make any changes as required. The Committee has also challenged management on the requirement to develop a more formal Risk Control Self-Assessment process.

In addition, we have also experienced two unconnected frauds during the year. The Committee is satisfied that additional controls have been put in place to limit the possibilities of similar frauds occurring in the future.

Despite the findings noted above, the Committee recognised that the risk management and internal control systems have been further enhanced through engagement with our Internal Audit co-sourcing partner PWC LLP in the year. This enhanced risk framework introduced a defined set of risk categories which form the basis of defining the Group's appetite to risk. In establishing this tolerance and critical limit/concern risk appetite, the Committee is able to maintain governance over the principal risks to the Group and ensure effective mitigation is in place.

Internal audit

There is a Group Internal Audit function headed by a Senior Manager, who has an administrative reporting line to the Chief Financial Officer and an independent reporting line to me as Chair of the Committee. The function has in place a co-sourcing arrangement with PWC LLP which adds expertise and breadth to the work of the internal audit team.

During the year, a programme of internal audits was completed. The scope of audit work generally focuses on assessing the adequacy and effectiveness of controls including management oversight and the degree of management risk awareness and responsiveness that operates within the businesses that are subject to audit. The scope of the audit programme is continually reviewed and challenged to ensure that the work Group Internal Audit undertakes is focused on the areas of higher risk to the Group.

Throughout the year, the Group Internal Audit function provides written reports to the Group Audit and Risk Committee on the work carried out to date and the in-flight work to be completed. A verbal update accompanies each report submitted to the Committee. An annual report is provided each year summarising the key matters arising. The representations given set out strengths and weaknesses identified during the work, together with any recommendations for remedial action or further review.

The reports are reviewed and discussed with Executive Directors to whom they pertain. During the year, the Group Internal Audit team reported significant weaknesses in the security and disaster recovery arrangements over the West Malling data centre. Management have responded and action is underway to address the weaknesses noted. A number of recommendations and observations from audits of the corporate finance landscape have been passed into the Group's current transformation of its finance systems and processes. Recommendations made during the year have strengthened the in-place controls and risk awareness.

The Committee reviews management's response to the matters raised and ensures that any action is commensurate with the level of risk identified, whether real or perceived.

Through the regular interaction between the Committee and Group Internal Audit Director, as well as the reports received from the function, the Committee is able to assess and satisfy itself that the Group's provision of internal audit is effective and that through the co-source arrangements there is access to expertise when required and that there is flexibility in the resources required to complete a full and targeted programme of internal audit work, within a group of Capita's size, and that these are in place.

Anti-bribery and whistleblowing (Speak Up)

Capita has a Group-wide anti-bribery and corruption policy, which is in compliance with the Bribery Act 2010. It periodically reviews its procedures to ensure continued effective compliance in its businesses around the world.

A 'Speak Up' Policy provides the framework to encourage and give employees confidence to 'blow the whistle' and report irregularities. Employees are encouraged to raise concerns with designated individuals and there is a dedicated email hotline to make such complaints easy to make. These are investigated on behalf of the Executive Directors or on my behalf as Chair of the Committee. All such reports will be investigated and reported (on an annual basis) to the Committee, together with details of corrective action taken.

Matthew Lester
Chair, Audit and Risk Committee
23 April 2018

GROUP EXECUTIVE RISK COMMITTEE

The former Group Financial Services Risk Committee and Group non-Financial Services Risk Committee (formed in 2012 and 2013 respectively) were combined into a single Group Executive Risk Committee in October 2017 and revised Terms of Reference were adopted. The disposal of the Capita Asset Services businesses resulted in fewer regulated businesses within the Group and the separation of financial services and non-financial services risk across two separate committees was no longer beneficial. The Group Executive Risk Committee continues to be chaired by Tim Brooke, an independent member of the Committee who previously chaired the Group Financial Services Risk Committee, and continues with a schedule of quarterly meetings to assess the risks across all Capita's businesses. Tim is independent of Capita and brings his expertise in the Financial Services sector to support the Committee. He is not an independent Non-Executive Director of Capita plc but he provides feedback to the Audit and Risk Committee when required. The Committee also comprises the Chief Financial Officer, each of the divisional Executive Officers, the Group Risk & Compliance Director and the Group Commercial Director.

During 2017, the Group Financial Services Committee met three times and the Group non-Financial Services Committee met twice (papers for a third meeting were circulated by email) prior to their amalgamation in October 2017 into the Group Executive Risk Committee which met once in December 2017. Attendance was as follows:

Group Financial Services Risk Committee (three meetings during 2017):

Name of member	Number of meetings attended
Tim Brooke (Chair)	3
Nick Greatorex	3
Vic Gysin[1]	3
Chris Terry[2]	3

Group non-Financial Services Risk Committee (two meetings during 2017):

Name of member	Number of meetings attended
Nick Greatorex (Chair)	2
Chris Terry[2]	1

1 Vic Gysin resigned from the Board and all committees on 18 December 2017.
2 Chris Terry – Group Risk & Compliance Director.

AUDIT AND RISK COMMITTEE CONTINUED

Group Executive Risk Committee (one meeting during 2017):

Name of member	Number of meetings attended
Tim Brooke (Chair)	1
Nick Greatorex	1
Chris Terry[1]	1
Rob Tolfts[2]	1
Mike Barnard[3]	1
Joe Hemming[4]	1
Stephen Sharp[5]	1
Peter Hepworth[6]	1
Chris Baker[7]	–
Vic Gysin[8]	–

1 Chris Terry – Group Risk & Compliance Director.
2 Rob Tolfts – Group Commercial Director.
3 Mike Barnard – Executive Officer, Private Sector Partnerships.
4 Joe Hemming – Executive Officer, IT Services.
5 Stephen Sharp – Executive Officer, Public Services Partnerships.
6 Peter Hepworth – Executive Officer, Professional Services.
7 Chris Baker – Executive Officer, Digital and Software Solutions.
8 Vic Gysin resigned from the Board and all committees on 18 December 2017.

The Chief Executive Officer and the Group Internal Audit Director have a standing invitation to attend all meetings of the Committee. All Non-Executive Directors have an open invitation to attend meetings of the Committee.

The Committee's role and duties can be summarised as oversight and challenge of the key risk and compliance activities and issues in Capita's businesses by:

- Reviewing the residual risk profile of Capita businesses, along with ensuring appropriate remedial actions are taken in line with Group objectives and risk appetites.
- Reviewing and commenting upon Group Control Function activity and oversight plans and monitoring progress of the same.
- Tracking key regulatory changes impacting on the Group's businesses.
- Tracking key business developments, including bids, acquisitions and offshoring developments.
- Receiving updates on regulatory capital issues (e.g. ICAAP).
- Receiving updates on Conduct risk issues.
- Reviewing and recommending for adoption policies applicable to the Group's businesses.
- Identifying items for the attention of the Board or Group Audit and Risk Committee.

The scope of the Committee includes all Capita business, including regulated activity in all jurisdictions in which the Group operates.

GROUP TECHNOLOGY & SECURITY RISK COMMITTEE

The scope and purpose of the former Security Risk Committee (which had been established at the beginning of 2015 to consider risks relating primarily to information security) was reviewed during the year. In October 2017, the Committee's remit was expanded to include risks relating to information technology as there is a close correlation between the two and it was felt that these risk areas should be considered together. The Committee was renamed the Group Technology & Security Risk Committee and new Terms of Reference, encompassing the extended remit, were adopted. The Committee continues to meet quarterly and is currently chaired by the Chief Financial Officer, Nick Greatorex. The former Security Risk Committee was chaired by the Group Risk & Compliance Director, Chris Terry, on an interim basis following the departure of Alex Cutler (former Chief Information Officer) in November 2016. Following the appointment of Jon Lewis as Chief Executive Officer in December 2017, a further review of the Committee's activities will take place in 2018.

During 2017, the Committee met three times as the Security Risk Committee and, following the extension of its remit in October 2017, once as the Group Technology & Security Risk Committee. Membership and attendance was as follows:

Name of member	Number of meetings attended
Nick Greatorex (Chair)	3
Chris Terry[1]	4
Mark Brown[2]	2
Vic Gysin[3]	3

1 Chris Terry, Group Risk & Compliance Director, chaired the former Security Risk Committee during 2017 on an interim basis prior to the establishment of the Technology & Security Risk Committee in October 2017.
2 Mark Brown, Chief Information Officer, was appointed to this role in March 2017.
3 Vic Gysin resigned from the Board and all committees on 18 December 2017.

Additional attendees are the Head of Group Security, the Group Data Privacy Officer and the Group Internal Audit Director.

The primary functions of the Committee are:

- Defining the cyber and information security and data privacy baseline policies to integrate such activities with business objectives.
- Monitor information security and data privacy legislative and regulatory compliance.
- Tracking key IT infrastructure and information security metrics.
- Identifying items for the attention of the Audit and Risk Committee.

DIRECTORS' REMUNERATION REPORT

IMAGE REMOVED

"It is important that the performance measures and targets for the 2018 LTIP awards be aligned with our strategy and be meaningful and robust."

JOHN CRESSWELL, CHAIR, REMUNERATION COMMITTEE

DEAR SHAREHOLDER

I am pleased to present my second report as Chair of the Remuneration Committee for the year ended 31 December 2017.

We received strong shareholder support at the 2017 AGM with positive votes for both our new Remuneration Policy (89.2%) and the Annual Report on Remuneration (90.3%).

MEMBERS:

- John Cresswell (Chair)
- Gillian Sheldon
- Matthew Lester
- Andrew Williams
- Baroness Lucy Neville-Rolfe

COMMITTEE MEMBERSHIP AND ATTENDANCE AT MEETINGS

All members of the Committee are Independent Non-Executive Directors.

None of the Committee members has day-to-day involvement with the business nor do they have any personal financial interest, except as shareholders, in the matters to be recommended. The number of formal meetings held and the attendance by each member is shown in the table on page 64. The Committee also held informal discussions as required.

To encourage effective communication, in addition to the above members, the Board Chairman, Chief Executive Officer, and senior human resources personnel are invited to attend all or part of Committee meetings along with representatives from Deloitte LLP, the Group's remuneration advisers.

The performance of the Committee is assessed as part of the Board performance evaluation undertaken annually.

The Group Company Secretary acts as Secretary to the Committee and is available to assist the members of the Committee as required, ensuring that timely and accurate information is distributed accordingly.

HOW THE COMMITTEE OPERATES

The Committee has an annual agenda to cover the key planning and decision events in the annual remuneration cycle.

Each meeting is supported by an agenda-setting discussion held in advance with the CEO, Group Company Secretary or Deloitte LLP to identify issues impacting remuneration that may require consideration by the Committee.

Regular reports including updates in corporate governance and regulatory developments are received from Deloitte LLP. At each Committee meeting the members may receive other reports and presentations covering the annual pay review, incentive scheme arrangements, gender pay reporting, salary proposals for members of the senior team and approval of remuneration packages for new members of the CEO's team.

The Remuneration Committee's terms of reference set out in full the role, responsibilities and authority of the Committee and can be found on the Company's website at www.capita.com/investors. These were reviewed and updated during the year.

HOW THE COMMITTEE DISCHARGED ITS ROLES AND RESPONSIBILITIES IN 2017

The Committee met 10 times during the year and attendance at each meeting is shown on page 64.

In 2017, the Committee held a number of additional unscheduled meetings to both consider and approve the termination arrangements of exiting Directors and consider and approve the remuneration package for the incoming CEO.

ACTIVITY IN 2017

As discussed in Sir Ian Powell's and Jon Lewis's reports, the Group is in a period of significant transition. The Board is focused on implementing the necessary strategic, financial and operational changes required to ensure the Group returns to expected levels of growth and as a Committee we are looking at performance metrics and setting targets which support the achievement of this ambition.

BOARD CHANGES

There has been significant change at Board level during 2017. Andy Parker stepped down from the Board and left the Group on 15 September 2017. Vic Gysin stepped down from the Board on 18 December 2017 and left the Group at the end of January 2018. Chris Sellers stepped down from the Board on 23 January 2018 and left Capita on 31 January 2018.

The termination arrangements are set out on page 88. The terms are in accordance with our Remuneration Policy and contractual obligations and were considered equitable in the circumstances.

Nick Greatorex served as Interim Chief Executive Officer for the period from 16 September 2017 to 30 November 2017 and was paid an allowance of £12,500 per month for his additional responsibilities up to 31 December including a one-month handover period to Jon Lewis.

As outlined in the Nomination Committee report, the Board conducted a thorough external search for our new Chief Executive Officer which resulted in Jon Lewis being appointed with effect from 1 December 2017. As disclosed in the Stock Exchange announcement of 10 October 2017, the Remuneration Committee agreed a remuneration package for Jon comprising an annual salary of £725,000 (which is fixed for three years) and a pension allowance of 5% of salary. Jon will also be eligible to participate in the Company's annual bonus plan and LTIP in line with our policy. No buy-out remuneration awards were granted in relation to Jon's appointment. As Sir Ian Powell noted in his introduction to the strategic report, Jon is a proven, successful business leader with the ideal blend of strategic vision and experience to lead the transformation of Capita. The Remuneration Committee believes this remuneration package was both appropriate and necessary to attract someone of Jon's experience and capabilities.

VARIABLE PAY OUTCOMES FOR 2017

Annual bonus

The maximum annual bonus for the Executive Directors that could be earned in relation to 2017 performance was 200% of salary (unchanged from 2016).

The annual bonus that could be paid to Executive Directors in respect of 2017 performance was determined by a range of

DIRECTORS' REMUNERATION REPORT CONTINUED

underlying profit before tax targets. 50% of the bonus was payable for achieving target performance with 100% payable for achieving the maximum target. No bonus would be paid for below target performance.

Although 2017 profit performance was within the target range, the Remuneration Committee has exercised its discretion following the trading update by the Company on 31 January 2018 and determined that no bonus will be paid to Executive Directors for the period to 31 December 2017.

This is the second consecutive year that no bonus has been payable to the Executive Directors.

LTIP and DAB matching awards

Vesting of LTIP and DAB Matching Awards granted in 2015 was determined by a combination of Earnings Per Share (EPS) and Return on Capita Employed (ROCE) performance and absolute share price, all assessed over the three-year period to 31 December 2017. As the share price performance target was not met, these awards will lapse in full during 2018.

These outcomes illustrate the alignment of our Remuneration Policy with shareholders' experience and the Committee's continued willingness to exercise discretion where appropriate.

PAY DECISIONS FOR 2018

Base salaries

Base salary for Jon Lewis is fixed at £725,000 as set out above. The base salary for Nick Greatorex is fixed at £410,000 and will be reviewed at the end of 2018.

Annual bonus

Earlier in this report, the Chief Executive Officer outlined a number of areas of significant change that are required for Capita's next stage of development and his transformation plan to achieve this change. In the past couple of months, the Remuneration Committee has reviewed the annual bonus plan to ensure it complements appropriately that transformation plan.

The previous annual bonus plan was based wholly on Group profit before tax (PBT)[1], however, the Remuneration Committee has concluded that in order to support the delivery of the transformation plan, the 2018 annual bonus plan needs to be based on a more rounded assessment of Group financial performance, incorporating Free Cash Flow and Cost Out measures alongside PBT, as well as relevant strategic and individual measures. The annual bonus plan for Executive Committee members will similarly be redesigned to incorporate a rounded assessment of financial, strategic and individual measures.

The maximum bonus opportunity will remain at 200% of salary. For Jon Lewis the split between Group financial metrics and personal and strategic measures will be 60:40 and for Nick Greatorex it will be 50:50. Any bonus pay-outs in respect of Group financial performance measures will be conditional upon Capita achieving a Group PBT[1] underpin target and will remain at the discretion of the Remuneration Committee.

Long Term Incentive Plan (LTIP)

It is important that the performance measures and targets for the 2018 LTIP awards be aligned with our strategy and be meaningful and robust. Accordingly, the Remuneration Committee will set the performance measures and targets for these awards after the full completion of the Chief Executive Officer's strategic review. Full details of the performance measures and targets will be subject to shareholder consultation and disclosed to shareholders both when they are determined and in next year's remuneration report.

Jon Lewis's LTIP award will be over shares worth 300% of salary which was agreed as part of his appointment and is consistent with LTIP awards granted to his predecessor. Nick Greatorex's award will be over a reduced salary multiple (200% of salary) relative to 2017.

Shareholding guidelines

Following the decision in 2017 to increase the minimum shareholding guideline for Executive Directors, the minimum requirement is 200% of salary for the Chief Financial Officer and 300% for the Chief Executive Officer. Directors are expected to retain at least half of vested share awards (post-tax) until they are compliant with the guideline.

Shareholder views

Details of voting on remuneration resolutions at the AGM in June 2017 are set out on page 82.

I hope you will find this report to be clear and helpful in understanding our remuneration practices and that you will be supportive of this year's advisory vote to approve the Annual Report on Remuneration at the AGM (set out on pages 82 to 89).

The Committee will continue to consult widely with shareholders to respond to shareholder expectations of Remuneration Policy and reporting and welcomes feedback.

John Cresswell
Chair, Remuneration Committee
23 April 2018

1 Underlying profit before tax before significant new contracts and restructuring

REMUNERATION POLICY

At the AGM in June 2017 shareholders approved, with a 89.2% majority, the Remuneration Policy which sets out the Company's policy on the remuneration of Executive and Non-Executive Directors. The Remuneration Policy became effective from the conclusion of the AGM and will apply until 31 December 2020 unless a revised policy is approved by shareholders and comes into force before that date.

For the benefit of shareholders we have included the Remuneration Policy on the following pages. Textual changes have been made, where appropriate, to ensure the report is relevant within the context of this Directors' remuneration report. The original Remuneration Policy, as approved by shareholders, can be found in the Directors' remuneration report of the 2016 Annual Report & Accounts (which can be found in the Investors section of our website).

The Committee is responsible, on behalf of the Board, for establishing appropriate remuneration arrangements for the Executive Directors and other senior management in the Group.

The information provided in this section of the remuneration report is not subject to audit.

Responsibilities and activities of the Remuneration Committee

The Committee is responsible for determining and agreeing with the Board the policy on Executive Directors' remuneration, including setting the over-arching principles, parameters and governance framework and determining the initial remuneration package of each Executive Director. In addition, the Committee monitors the structure and level of remuneration for the senior management team and is aware of pay and conditions in the workforce generally. The Committee also sets the Chairman's fee.

In setting the Remuneration Policy for the Executive Directors, the Committee ensures that the arrangements are in the best interest of both the Group and its shareholders, by taking into account the following general principles:

- To ensure total remuneration packages are simple and fair in design so that they are valued by participants.
- To ensure that total remuneration is highly performance orientated.
- To balance performance-related pay between the achievement of financial performance objectives and delivering sustainable performance; creating a clear connection between performance and reward and providing a focus on sustained improvements in profitability and returns.

- To provide a significant proportion of performance-linked pay in shares allowing senior management to build a significant shareholding in the business and, therefore, aligning management with shareholders' interests and the Group's performance, without encouraging excessive risk-taking.

Consideration of shareholder views

The Company is committed to maintaining good communications with investors. The Committee considers the AGM to be an opportunity to meet and communicate with investors, giving shareholders the opportunity to raise any issues or concerns they may have.

In addition, the Committee will seek to engage directly with major shareholders and their representative bodies should any material changes be proposed to the Policy.

REMUNERATION POLICY TABLE

The following table sets out the key aspects of the Policy.

BASE SALARIES

Purpose and link to strategy	Operation	Maximum opportunity	Performance framework
To attract and retain talent by ensuring base salaries are sufficiently competitive.	Normally reviewed annually in December with any changes usually effective in January. The Committee may award salary increases at other times of the year if it considers it to be appropriate. The review takes into account: – Salaries in similar companies and comparably-sized companies – Remuneration Policy – Economic climate – Market conditions – Group performance – The role and responsibility of the individual Director – Employee remuneration across the broader workforce.	There is no prescribed maximum monetary annual increase to base salaries. Any annual increase in salaries is at the discretion of the Committee taking into account the factors stated in this table and the following principles: – Salaries would typically be increased at a rate consistent with the average salary increase (in percentage of salary terms) for the broader workforce. – Larger increases may be considered appropriate in certain circumstances (including, but not limited to, a change in an individual's responsibilities or in the scale of their role or in the size and complexity of the Group). – *Larger increases may also be* considered appropriate if a Director has been initially appointed to the Board at a lower than typical salary.	Individual and business performance are considerations in setting base salaries.

ANNUAL BONUS AND DEFERRED ANNUAL BONUS (DAB) PLAN

Purpose and link to strategy	Operation	Maximum opportunity	Performance framework
Performance measures are selected to focus Executives on delivery of the Group business plan for the financial year.	The bonus scheme is reviewed annually to ensure that bonus opportunity and performance measures continue to support the business plan. Stretching targets are set at the start of each financial year. Performance against targets is reviewed following completion of the final accounts for the period under review. 50% of any bonus earned is normally delivered in shares deferred for three years under the DAB plan with the remainder delivered in cash or Deferred Shares at the Executive Director's discretion. An additional payment may be made at the time of vesting in respect of dividends that would have accrued on Deferred Shares during the deferral period. Malus and clawback provisions apply to all annual bonus and DAB awards for a period of up to three years after the determination of the annual bonus.	Maximum opportunity of 200% of salary.	Executive Directors' performance is measured over a one-year period relative to challenging targets for selected measures of Group financial, strategic or individual performance. The majority of the bonus will be determined by measure(s) of Group financial performance. A sliding scale is set for each Group financial measure. 50% of the bonus will be paid at target performance increasing to 100% for maximum performance. Any bonus payout is ultimately at the discretion of the Committee.

DIRECTORS' REMUNERATION REPORT CONTINUED

LONG TERM INCENTIVE PLAN (LTIP)

Purpose and link to strategy	Operation	Maximum opportunity	Performance framework
Designed to reward and retain Executives over the longer term while aligning their interests with those of shareholders. **To link reward to key longer-term business targets.** **To encourage share ownership.**	LTIP awards are usually granted in the form of nil cost options. Award levels for each award are set by the Committee at a level appropriate, in the Committee's opinion, with the individual's performance and experience. Performance targets applying to LTIP awards are relevant to business plan priorities and aligned with shareholder interests. Vesting is dependent on the achievement of performance conditions usually measured over a three-year period. An additional payment may be made at the time of vesting in respect of dividends that would have accrued on LTIP awards during the vesting period. Malus and clawback provisions apply to all LTIP awards for a period up to the fifth anniversary of grant.	The maximum annual award permitted under the LTIP is shares with a market value (as determined by the Committee) of 300% of salary.	Performance is measured relative to selected measures of Group financial or share price performance with the precise measures and weighting of the measures determined by the Committee ahead of each award. Performance targets are reviewed annually by the Committee and are set appropriate to the economic and political outlook and risk factors prevailing at the time, ensuring that such targets remain challenging in the circumstances, whilst remaining realistic enough to motivate and incentivise management. 25% of the awards vest at a threshold vesting point rising to 100% vesting at a maximum vesting point.

BENEFITS

Purpose and link to strategy	*Operation*	*Maximum opportunity*	*Performance framework*
Designed to be consistent with benefits available to employees in the Group.	Benefits include car allowance, private medical insurance, travel and property hire. Executive Directors can also participate in all-employee share plans. The Committee has discretion to add additional benefits which are not currently provided, for example, relocation expenses.	Benefit provision varies between different Executive Directors. Whilst there is no maximum level set by the Committee, benefits provision will be set at a level the Committee considers appropriate and be based on individual circumstances. Participation in the Company's HMRC-approved all-employee share plan will be limited by the maximum level prescribed by HMRC.	Not performance related.

PENSION

Purpose and link to strategy	Operation	Maximum opportunity	Performance framework
Designed to be consistent with benefits available to employees in the Group.	Pension contributions are paid into the Group's defined contribution scheme and/or as a cash allowance.	5% of salary.	Not performance related.

NON-EXECUTIVE DIRECTORS (NED) FEES

Purpose and link to strategy	Operation	Maximum opportunity	Performance framework
Market competitive fees are set so as to attract and retain Non-Executive Directors with required skills, experience and knowledge so that the Board can effectively carry out its responsibilities.	Reviewed periodically by the Board. Fee levels set by reference to market rates, taking into account the individual's experience, responsibilities, time commitment and pay decisions for the broader workforce. NED fees comprise payment of an annual basic fee and additional fees for further Board responsibilities such as: – Senior Independent Director. – Audit Committee Chairman. – Remuneration Committee Chairman. The Chairman of the Board receives an all-inclusive fee. No NED participates in the Group's incentive arrangements or pension plan or receives any other benefits other than where travel to the Company's registered office is recognised as a taxable benefit in which case a NED may receive grossed-up costs of travel as a benefit.	As for the Executive Directors there is no prescribed maximum monetary annual increase. An aggregate annual sum of £1m increased only to take account of the effect of inflation as measured by the Retail Price Index or such index as the Directors consider appropriate or such other amount as the Company may by ordinary resolution decide.	Not performance related.

Malus and clawback provisions apply to all incentive awards granted to Executive Directors. These provisions permit the Committee to recover bonus awards for up to three years after the determination of the annual bonus and up to the fifth anniversary of the grant of LTIP awards. The potential circumstances in which malus or clawback provisions can be applied include a material misstatement of the Group's financial results, if an individual deliberately misleads relevant parties regarding financial performance or if their actions cause reputational damage or amount to serious misconduct or conduct which causes significant financial loss.

The annual bonus performance measures are Group financial, strategic or individual measures which are selected annually so as to be consistent with key priorities for the Group.

The LTIP performance measures are chosen to provide alignment with our longer-term strategy of growing the business in a sustainable manner that will be in the best interests of shareholders and other key stakeholders in the Company.

Targets are set on sliding scales that take account of internal strategic planning and external market expectations for the Company. Only modest rewards are available for achieving threshold performance with maximum rewards requiring substantial outperformance of challenging strategic plans approved at the start of each year.

Share incentive plans incorporate the right to receive an amount (in cash or additional shares) equal to the value of dividends which would have been paid on the shares under an award that vests up to the time of vesting/release. This amount may be calculated assuming that the dividends have been re-invested in the Company's shares on a cumulative basis.

The Committee operates incentive arrangements for the Executive Directors in accordance with their respective rules, the Listing Rules and the HMRC rules where relevant.
The Committee, consistent with market practice and the scheme rules, retains discretion over a number of areas relating to the operation and administration of the plans. These include (but are not limited to) the following:

- Who participates
- The form in which the award is granted and settled (e.g. shares, nil cost options, cash)
- The timing of the grant of award and/or payment
- The size of an award (up to individual and plan limits) and/or a payment
- Discretion relating to the measurement of performance in the event of a 'good leaver' scenario or a change of control or reconstruction of the Company
- Determination of a good leaver (in addition to any specified categories) for incentive plan purposes
- Adjustments required in certain circumstances (e.g. share capital variation, rights issues, demerger, corporate restructuring, special dividends)
- The ability to vary or substitute any performance condition(s) if circumstances occur which cause it to determine that the original condition(s) have ceased to be appropriate, provided that any such variation or waiver is fair, reasonable and not materially less difficult to satisfy than the original condition (in its opinion). In the event that the Committee were to make an adjustment of this sort, a full explanation would be provided in the next remuneration report.

The Committee reserves the right to make any remuneration payments and/or payments for loss of office (including exercising any discretions available to it in connection with such payments) notwithstanding that they are not in line with the Policy set out above where the terms of the payment were agreed: (i) before the 2014 AGM (when the Company's first shareholder-approved Directors' Remuneration Policy came into effect); (ii) before the Policy set out above came into effect, provided that the terms of the payment were consistent with the shareholder-approved Directors' Remuneration Policy in force at the time they were agreed; or (iii) at a time when the relevant individual was not a Director of the Company and, in the opinion of the Committee, the payment was not in consideration for the individual becoming a Director of the Company. For these purposes 'payments' includes the Committee satisfying awards of variable remuneration and, in relation to an award over shares, the terms of the payment are 'agreed' at the time the award is granted.

The Committee may make minor amendments to the policy set out in this Policy Report (for regulatory, exchange control, tax or administrative purposes or to take account of a change in legislation) without obtaining shareholder approval for that amendment.

DIRECTORS' REMUNERATION REPORT CONTINUED

ILLUSTRATIONS OF THE APPLICATION OF OUR REMUNERATION POLICY

The value and composition of the Executive Directors' remuneration packages under the Policy for the year ending 31 December 2018 at a minimum, target and maximum performance level are set out in the charts below.

The charts are for illustrative purposes only and actual outcomes may differ from that shown.

Each chart is broken down to show how the total under each scenario is made up of fixed elements of remuneration, the annual bonus and the LTIP.

IMAGE REMOVED

IMAGE REMOVED

Basic includes the base salary, benefits and pension.

Notes

The scenarios in the above charts are defined as follows:

	Minimum	Performance in line with Expectations (Target)	Maximum
Fixed elements of remuneration	Base salary as at 1 January 2018 Estimated value of benefits provided under the Remuneration Policy 5% of salary pension provision		
Annual bonus – payout shown as a maximum opportunity	0%	50% of maximum	100% of maximum
LTIP – payout shown as a maximum opportunity	0%	50% of maximum	100% of maximum

As set out in the Policy table above, the maximum permitted annual bonus opportunity is 200% of salary and the maximum permitted LTIP award is 300% of salary. The charts above reflect the maximum bonus (200% of salary) and maximum LTIP award (200% – 300% of salary) that could be earned in 2018. The maximum that can be earned by the CFO in 2018 is lower than the maximum permitted under the Policy.

In these charts, LTIP awards have been shown at face value, with no share price growth or discount rate assumptions. All-employee share plans have been excluded.

The Committee considers pay and employment conditions of employees in the Group when determining Executive Directors' Remuneration Policy

When considering the Executive Directors' remuneration structure and levels, the Committee reviews base salaries and annual bonus arrangements for the management team, to ensure that there is a consistent approach across the Group. The annual bonus plan operates on a similar basis across the senior management team. LTIP awards are granted across the senior management population in order to encourage a high level of employee share ownership. Whilst vesting of regular LTIP awards to Executive Directors is always subject to performance conditions, awards to other senior management may, where appropriate (such as to assist in retention of key talent), be subject only to continued employment. Another key difference in the Policy for Executive Directors is that remuneration is more heavily weighted towards long-term variable pay than other employees. This ensures that there is a clear link between the value created for shareholders and the remuneration received by the Executive Directors.

The Committee did not formally consult with employees in respect of the design of the Policy, although the Committee will keep this under review.

Directors' recruitment and promotions

The Committee takes into account the need to attract, retain and motivate the best person for each position, while at the same time ensuring a close alignment between the interests of shareholders and management.

If a new Executive Director was appointed, the Committee would seek to align their remuneration package with other Executive Directors in line with the Policy table. However, flexibility would be retained to offer additional remuneration on appointment outside the Policy if the Committee believe it may be appropriate to make 'buy-out' awards or payments in respect of remuneration arrangements and contractual terms forfeited on leaving a previous employer. The Committee would look to replicate the arrangements being forfeited as closely as possible and in doing so, would take account of relevant factors including the nature of the remuneration and contractual terms, performance conditions and the time over which they would have vested or been paid.

The Committee would seek to structure awards on recruitment to be in line with the Company's remuneration framework so far as practical but, if necessary, the Committee may also grant such awards outside of that framework as permitted under Listing Rule 9.4.2. If appropriate, a new appointee's incentives in their year of joining may be subject to different targets to other Executive Directors. The Committee may also agree that the Company will meet certain relocation and incidental expenses as it considers appropriate.

The maximum level of variable remuneration which may be granted (excluding awards to compensate for remuneration arrangements and contractual terms forfeited on leaving the previous employer) to new Executive Directors in the year of recruitment shall be limited to 500% of salary (the maximum limit allowed within the Policy table).

The initial notice period for a service contract may be up to 24 months, which is longer than the policy of a 12-month notice period, provided it reduces to 12 months within a short space of time.

For an internal appointment or an appointment following the Company's acquisition of or merger with another company, any incentive amount awarded in respect of a prior role may be allowed to vest on its original terms, or adjusted as relevant to take into account the appointment. Any other ongoing remuneration obligations or terms and conditions existing prior to appointment may continue.

The Committee retains discretion to make appropriate remuneration decisions outside the standard Policy to meet the individual circumstances of recruitment when:

- an interim appointment is made to fill an Executive Director role on a short-term basis; or
- exceptional circumstances require that the Chairman or a Non-Executive Director takes on an executive function on a short-term basis.

In the event of the appointment of a new Non-Executive Director, remuneration arrangements will normally be in line with the structure set out in the Policy table for Non-Executive Directors. However, the Committee (or the Board as appropriate) may include any element listed in the Policy table or any other element which the Committee considers is appropriate given the particular circumstances excluding any variable elements, with due regard to the best interests of shareholders.

Directors' service agreements and payments for loss of office

The Committee regularly reviews the contractual terms of the service agreement to ensure these reflect best practice.

The service contracts for Executive Directors are for an indefinite period and provide for a 12-month notice period. They do not include provisions for predetermined compensation on termination that exceed 12-months' salary, pension and benefits. There are no arrangements in place between the Company and its Directors that provide for compensation for loss of office following a takeover bid. All Directors are appointed for an indefinite period but are subject to annual re-election at the Annual General Meeting.

In circumstances of termination on notice the Committee will determine an equitable compensation package, having regard to the particular circumstances of the case. The Committee reserves the right to make payments in connection with a Director's cessation of office or employment where the payments are made in good faith in discharge of an existing legal obligation (or by way of damages for breach of such an obligation) or by way of a compromise or settlement of any claim arising in connection with the cessation of a Director's office or employment. Any such payments may include but are not limited to paying any fees for outplacement assistance and/or the Director's legal and/or professional advice fees in connection with his cessation of office or employment. The Committee has discretion to require notice to be worked or to make payment in lieu of notice or to place the Director on garden leave for the notice period.

The annual bonus may be payable in respect of the period of the bonus plan year worked by the Director; there is no provision for an amount in lieu of bonus to be payable for any part of the notice period not worked. This will be at the discretion of the Remuneration Committee.

DAB Deferred Shares will vest on the date of leaving other than in circumstances of dismissal for gross misconduct.

For entitlement to unvested LTIP shares, the rules contain discretionary provisions setting out the treatment of awards where a participant leaves for designated reasons (i.e. participants who leave early on account of injury, disability or ill health, death, a sale of their employer or business in which they were employed, statutory redundancy or any other reason at the discretion of the Committee).

DIRECTORS' REMUNERATION REPORT CONTINUED

In these circumstances, a participant's awards will not be forfeited on cessation of employment and instead will continue to vest on the normal vesting date or earlier at the discretion of the Committee, subject to the performance conditions attached to the relevant awards. The awards will, other than in exceptional circumstances, be scaled back on a time pro-rated basis.

In the event of a change of control, all unvested LTIP awards would vest, to the extent that any performance conditions attached to the relevant awards have been achieved. LTIP awards will, other than if the Committee determines otherwise, be scaled back pro rata for the proportion of the performance period worked by the Director prior to the change of control. Unvested DAB Deferred Shares would vest in the event of a change of control.

Non-Executive Directors' terms of engagement

Non-Executive Directors are appointed by letter of appointment for an initial period of three years. Each appointment is terminable by three-months' notice on either side. At the end of the initial period, the appointment may be renewed by mutual consent, subject to annual re-election at the AGM.

The service agreements and Non-Executive Directors' letters of appointment are available for inspection during normal business hours at the Company's registered office, and available for inspection at the AGM.

Satisfaction of options

When satisfying awards made under its share plans, the Company uses newly issued, treasury or purchased shares as appropriate.

Dilution

All awards are made under plans that incorporate the overall dilution limit of 10% in 10 years. The estimated dilution from existing awards, including executive and all-employee share awards, is approximately 4.23% of the Company's share capital as at 31 December 2017.

ANNUAL REPORT ON REMUNERATION

This part of the remuneration report has been prepared in accordance with The Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013 and paragraphs 9.8.6R and 9.8.8 of the Listing Rules. The Annual Report on Remuneration will be put to an advisory shareholder vote at the 2018 AGM. The information on pages 84 to 88 has been audited as indicated.

External advice received

Deloitte LLP was, following a review, appointed by the Remuneration Committee during 2012 to provide advice on Executive remuneration matters. During the year, the Committee received independent and objective advice from Deloitte primarily on market practice, disclosure within the accounts and stakeholder liaison. Deloitte was paid £62,280 in fees during 2017 for these services (charged on a time plus expenses basis). Deloitte is a founding member of the Remuneration Consultants Group and, as such, operates voluntarily under the code of conduct in relation to Executive remuneration consulting in the UK. In addition, other practices of Deloitte, separate from the Executive remuneration practice, has provided services to the Group in respect of tax, property, advice to internal audit and other ad hoc advisory projects during the year.

The fees were considered as appropriate for the work undertaken and all fees were disclosed prior to the work being undertaken. Where appropriate, fees were tendered with other providers to ensure that the fees were in line with market practice and standards.

The Committee also consulted with Jon Lewis to provide further information to the Committee on the performance and proposed remuneration for the Chief Financial Officer and other senior management, but not in relation to his own remuneration.

Shareholder voting at AGM

The 2017 Directors' remuneration report will be presented to shareholders at the AGM in June 2018. At the AGM in 2017, the actual voting in respect of the ordinary resolution to approve the remuneration report for the year ended 31 December 2016 was as set out below. Details of the last shareholder vote on our Remuneration Policy are also set out below.

AGM 2017	Votes cast 'For'	Votes cast 'Against'	Abstentions[1]
Remuneration report for the year ended 31 December 2016	507m	54.4m	4.16m
	90.3%	9.7%	–
Remuneration Policy – voted on in June 2017	503.9m	60.8m	0.09m
	89.2%	10.8%	–

1 A vote abstained is not a vote in law and is not counted in the calculation of the proportion of votes 'for' and 'against' a resolution.

Statement of implementation of the Remuneration Policy for 2018

Base salary

Jon Lewis joined the Board as Chief Executive Officer on 1 December 2017 and his salary is fixed at £725,000 until 1 January 2021. Base salary for Nick Greatorex remains unchanged at £410,000.

Accordingly, base salaries for 2018 are:

	Base salary from 1 January 2018
Jon Lewis	£725,000
Nick Greatorex	£410,000

Fees for the Chairman and Non-Executive Directors

A summary of the fees for 2018 (unchanged from 2017) are as follows:

	Fee from 1 January 2018 or date of appointment
Sir Ian Powell – Chairman	£325,000
Gillian Sheldon – Senior Independent Director	£75,000
Matthew Lester – Audit and Risk Committee Chair	£64,500
John Cresswell – Remuneration Committee Chair	£64,500
Andrew Williams	£64,500
Baroness Lucy Neville-Rolfe	£64,500

Annual bonus for 2018

Consistent with prior practice and policy, the CEO and CFO's maximum bonus opportunity for 2018 will be 200% of base salary with 50% of any bonus normally deferred into shares for three years.

As explained in the Remuneration Committee Chairman's statement, the Executive Director bonus plan for 2018 has been redesigned to complement the new Chief Executive Officer's transformation plan. Accordingly, the bonus plan will incorporate a more rounded assessment of Group financial performance than in prior years as well as relevant strategic and individual measures consistent with the transformation plan. The following weightings and measures have been agreed by the Committee.

	Weighting of measures	
	Jon Lewis	Nick Greatorex
Group financial performance measures	60% (profit before tax, free cash flow, cost out)	50% (profit before tax, free cash flow, cost out)
Group strategic and individual performance measures	40%	50%

Any bonus payment would be at the discretion of the Remuneration Committee. There would be no bonuses paid in respect of the Group financial performance measures if Capita failed to achieve a PBT underpin target for 2018.

Details of the Group strategic and individual performance measures and the targets for the Group financial performance measures are considered commercially sensitive by the Board and so will be disclosed retrospectively in the 2018 remuneration report.

Any bonus payments will be subject to malus and clawback provisions as outlined in the Directors' Remuneration Policy.

Long-term incentive to be granted in 2018

Awards will be granted over shares worth 300% of salary to Jon Lewis and 200% of salary to Nick Greatorex. Performance measures and targets will be set for the 2018 LTIP award upon the completion of Jon Lewis' strategy review. The measures and targets will be set by the Remuneration Committee following consultation with major shareholders.

At the end of the LTIP performance period, the Remuneration Committee will assess the underlying financial and operational performance of Capita over the performance period and, if judged appropriate, can exercise its discretion to reduce the level of vesting.

DIRECTORS' REMUNERATION REPORT CONTINUED

Directors' remuneration earned in 2017 – single figure table (Audited)

The table below summarises Directors' remuneration received in 2017.

Single figure remuneration

		Base salary and fees	Benefits	Pension or pension allowance	Annual bonus	LTIP	DAB – Match	Total long-term incentives	Total remuneration
Sir Ian Powell	2017	325,000	216	–	–	–	–	–	325,216
	2016	21,500	–	–	–	–	–	–	21,500
Jon Lewis[1]	2017	60,417	41,216	3,021	–	–	–	–	104,654
	2016	–	–	–	–	–	–	–	–
Nick Greatorex[2]	2017	454,048	29,884	20,500	–	–	–	–	504,432
	2016	410,000	30,971	20,500	–	–	–	–	461,471
Chris Sellers[3]	2017	360,000	83,404	18,000	–	–	–	–	461,404
	2016	–	–	–	–	–	–	–	–
Gillian Sheldon	2017	75,000	216	–	–	–	–	–	75,216
	2016	75,000	–	–	–	–	–	–	75,000
Matthew Lester	2017	53,750	216	–	–	–	–	–	53,966
	2016	–	–	–	–	–	–	–	–
John Cresswell	2017	64,500	216	–	–	–	–	–	64,716
	2016	64,500	–	–	–	–	–	–	64,500
Andrew Williams	2017	64,500	–	–	–	–	–	–	64,500
	2016	64,500	–	–	–	–	–	–	64,500
Baroness Lucy Neville-Rolfe[4]	2017	4,607	–	–	–	–	–	–	4,607
	2016	–	–	–	–	–	–	–	–
Andy Parker[3]	2017	426,190	46,570	21,310	–	–	–	–	494,070
	2016	600,000	52,958	30,000	–	–	–	–	682,958
Vic Gysin[3]	2017	347,419	52,141	17,371	–	–	–	–	416,931
	2016	360,000	51,646	18,000	–	–	–	–	429,646
Paul Bowtell[5]	2017	26,875	216	–	–	–	–	–	27,091
	2016	64,500	–	–	–	–	–	–	64,500

1 Jon Lewis was appointed Chief Executive Officer on 1 December 2017.
2 Nick Greatorex was appointed interim CEO in respect of the period from 16 September 2017 to 30 November 2017 and was paid an allowance of £12,500 per month in respect of his additional responsibilities up to 31 December 2017 (including a one-month handover period to Jon Lewis). This is reflected in the 2017 figure for base salary.
3 Andy Parker, Vic Gysin and Chris Sellers resigned from the Board on 15 September 2017, 18 December 2017 and 23 January 2018 respectively. They received final payments in lieu of notice, further details of which are set out on page 88. Amounts shown in the table for Andy Parker and Vic Gysin relate to the period of time during which they served as Directors.
4 Baroness Lucy Neville-Rolfe was appointed as a Director on 6 December 2017.
5 Paul Bowtell resigned as a Director on 31 May 2017.

For 2016, in addition to the amounts noted above, total remuneration was also paid to the following Directors who left during 2016: Martin Bolland £200,000, Maggi Bell £393,456 and Dawn Marriott-Sims £367,799.

Base salary includes base salary plus fixed cash allowances which are a normal part of the fixed remuneration package and usual local practice. Benefits include all taxable benefits as defined by paragraph 11(1) of Schedule 8 to the Accounts regulations. This includes private medical insurance, company car allowance, work travel and accommodation. For Jon Lewis, this figure also includes one-off legal fees associated with the negotiation of his service contract. Staff entertainment has also been included under benefits and in some cases this cost will be for more than the individual director themselves.

No annual bonus was awarded for 2017 and the 2015 LTIP and DAB Matching Awards did not vest.

Performance targets for the 2015 LTIP awards were, for awards of more than 20,000 shares, EPS growth of 6% (18.75% vest) to 12% (75% vest), average ROCE 14% (6.25% vest) to 16% (25% vest) over the three-year period to 31 December 2017 and average share price at vesting must not be lower than at grant. For awards of 12,001 to 20,000 shares and awards up to 12,000 shares the targets were identical except that 50% and 75%, respectively, of the award would vest at 6% EPS.

No Director waived any fees or salary for 2017.

Annual bonus for 2017

The maximum annual bonus for the Executive Directors that could be earned in relation to 2017 performance was 200% of salary (unchanged from 2016).

The annual bonus that could be paid to Executive Directors in respect of 2017 performance was determined by a range of underlying profit before tax targets. 50% of the bonus was payable for achieving target performance with 100% payable for achieving the maximum target. No bonus would be paid for below target performance.

Although 2017 profit performance was within the target range, the Remuneration Committee has exercised its discretion following the trading update by the Company on 31 January 2018 and determined that no bonus will be paid to Executive Directors for the period to 31 December 2017.

	Below target performance	On-target performance	Maximum performance	Actual performance and bonus payout
Underlying profit before tax	<£390.5m	£390.5m	£403.75m	£400.9m
Bonus payout	0%	50% of maximum	100% of maximum	78.5% of maximum before discretion exercised to award nil bonus

These targets have been adjusted for IFRS 15.

SHARE PLAN AWARDS

Long Term Incentive Awards awarded in 2017 (Audited)

Name of Director	LTIP award	(£) Face value of LTIP award[1]	Percentage of salary[2]
Nick Greatorex	163,274	922,498	225%
Chris Sellers	159,292	900,000	250%
Vic Gysin	143,362	809,995	225%

1 The date of the grant was 2 March 2017. The closing price on the preceding day of £5.65 was used to determine the number of shares.
2 Percentage calculated using base salary as at date of award (Nick Greatorex – £410,000; Chris Sellers – £360,000; Vic Gysin – £360,000).

LTIP awards are granted as nil cost options and awarded as a percentage of salary. Awards will vest three years from the date of grant subject to EPS and ROCE performance over the three-year period to 31 December 2019. 25% of LTIP awards vest for achieving threshold performance. Performance targets for the 2017 award were set under GAAP before the Company had adopted IFRS 15 with effect from 1 January 2017. The targets will be reviewed to ensure that they do not become materially easier to achieve under the new standard and will be subject to consultation with major shareholders. Full details of the performance conditions relating to these awards are outlined on page 78.

DIRECTORS' REMUNERATION REPORT CONTINUED

Directors' interests and Shareholding Guidelines (Audited)

In line with the new Remuneration Policy approved in 2017, Executive Directors are expected to hold 200% (300% for the Chief Executive Officer) of salary in shares in the Company. This must be built up over a period of five years from appointment. The guidelines include shares held beneficially and also shares within the DAB that have been deferred over the three-year period. Any shares in the DAB used for this are calculated net of tax. Share awards that are subject to performance conditions are not included.

Director	Beneficially held interests at 31 December 2017[8]	Beneficially held interests at 31 December 2016	Interests in share incentive schemes, awarded without performance conditions at 31 December 2017	Interests in share incentive schemes, awarded without performance conditions at 31 December 2016	Interests in share incentive schemes, awarded subject to performance conditions at 31 December 2017	Interests in share incentive schemes, awarded subject to performance conditions at 31 December 2016	Interests in share option schemes where performance conditions have been met but not exercised at 31 December 2017	Interests in share option schemes where performance conditions have been met but not exercised at 31 December 2016	Percentage of shareholding target requirement at 31 December 2017 or date of retirement	Percentage of shareholding target requirement at 31 December 2017 – based on cost of investment
Sir Ian Powell	8,400	2,000	–	–	–	–	–	–	–	–
Jon Lewis[1]	–	–	–	–	–	–	–	–	–	–
Nick Greatorex	21,125	15,129	17,109	17,109	337,726	222,698	–	–	29%	62%
Chris Sellers[2]	21,337	15,514	–	8,635	259,943	166,167	–	–	24%	47%
Gillian Sheldon	3,000	1,000	–	–	–	–	–	–	–	–
Matthew Lester[3]	8,698	–	–	–	–	–	–	–	–	–
John Cresswell	3,000	3,000	–	–	–	–	–	–	–	–
Andrew Williams	10,000	–	–	–	–	–	–	–	–	–
Baroness Lucy Neville-Rolfe[4]	–	–	–	–	–	–	–	–	–	–
Andy Parker[5,9]	–	55,686	69,377	97,442	–	504,412	–	–	–	–
Vic Gysin[6,9]	17,817	–	32,267	66,045	305,523	304,078	–	–	–	–
Paul Bowtell[7,9]	1,129	1,073	–	–	–	–	–	–	–	–

1 Appointed 1 December 2017.
2 Appointed 1 January 2017.
3 Appointed 1 March 2017.
4 Appointed 6 December 2017.
5 Resigned 15 September 2017.
6 Resigned 18 December 2017.
7 Resigned 31 May 2017.
8 Beneficially held interests includes those held by connected persons.
9 2017 interests are shown as at date of resignation from the Board.

Between the end of the financial year and 18 April 2018, Jon Lewis and Nick Greatorex each acquired 369 and 370 shares under the Capita All-Employee Share Incentive Plan, increasing their beneficial interest in ordinary shares of the Company to 369 and 21,495 respectively.

Share plans (Audited)

Plan name: Deferred Annual Bonus (DAB) plan

Deferred award – this is the deferred element of an individual's bonus. Any deferral is made on a gross basis into Deferred Shares or as a net restricted share award. The Deferred Shares are held for a period of three years from the date of award. This part is not subject to performance conditions. No Director chose to take the award as restricted stock. As no bonus was awarded in 2017, there is no corresponding DAB deferred award.

Unvested DAB deferred/restricted awards at 31 December 2017

Name of Director	2015 award	2016 award	2017 award[1]	Total
Andy Parker[2]	42,337	27,040	N/A	69,377
Nick Greatorex	N/A	17,109	N/A	17,109
Chris Sellers[3]	N/A	N/A	N/A	N/A
Vic Gysin	15,258[4]	17,109	N/A	32,367

1 No bonus was awarded in 2017 (in respect of 2016 performance) therefore no deferred award was made.
2 Figures as at date of resignation from Board (15 September 2017).
3 Chris Sellers was not a Board Director at the time of the 2015 and 2016 awards.
4 2015 DAB was awarded as restricted stock.

Plan name: Long Term Incentive Plan (2017 LTIP)
At the Annual General Meeting in 2017, the Long Term Incentive Plan (LTIP) was approved by shareholders. Under the plan rules the Committee can award up to three times salary.

The vesting of awards will depend on performance measured over a three-year period.

Unvested LTIP awards at 31 December 2017

Name of Director	2015 award	2016 award	2017 award	Total
Nick Greatorex	73,666	100,786	163,274	**337,726**
Chris Sellers	46,571	54,080	159,292	**259,943**
Vic Gysin	73,666	88,495	143,362	**305,523**

Andy Parker's outstanding LTIP awards lapsed on 15 September 2017.

Capita adopted IFRS 15 *Revenue from Contracts with Customers* with effect from 1 January 2017, resulting in revenue and profits being recognised later across the life of many contracts, with potentially lower profits or losses in the early years of contracts and potentially higher profits in later years. In light of this change, the Committee considered what, if any, adjustments should be made to the EPS and ROCE targets applicable to outstanding LTIP awards granted in 2015, 2016 and 2017. The 2015 and 2016 LTIP awards are subject to a share price underpin (£11.81 and £10.17 respectively) and are therefore unlikely to vest. However, if the share price should draw significantly closer to the underpin target, the Committee may review the existing targets for these awards to take account of IFRS 15 accounting changes. The 2017 LTIP award is not subject to a share price underpin and, to reflect the impact of IFRS 15, the Committee will set amended EPS and ROCE targets that are not materially less difficult to satisfy than the original targets. Amended targets will be disclosed to shareholders when they have been determined by the Committee. Outstanding awards held by Andy Parker lapsed on 15 September 2017 in accordance with the LTIP rules.

Performance criteria

2015 and 2016

Performance measure	Performance condition
EPS – 75% of the Award is measured on EPS Growth	EPS growth: 6% – 12% per annum Vesting percentage: 18.75% – 75% of Award Straight-line vesting occurs between these points.
ROCE – 25% of the Award is measured on average ROCE	Average ROCE: 14% – 16% Vesting percentage: 6.25% – 25% of Award Straight-line vesting occurs between these points.
Share price underpin	Capita's average share price at the vesting date must not be below the share price at the date of grant.

2017

Performance measure	Performance condition[1]
EPS – 75% of the Award is measured on EPS Growth	EPS growth: 3% – 8% per annum Vesting percentage: 18.75% – 75% of Award Straight line vesting occurs between these points.
ROCE – 25% of the Award is measured on average ROCE	Average ROCE: 11% – 15% Vesting percentage: 6.25% – 25% of Award Straight-line vesting occurs between these points.

1 Subject to amendment by the Committee following adoption of IFRS 15.

Executive Directors' service agreements

Details of the service agreements are set out below:

Executive Directors	Date of contract	Notice period
Jon Lewis	1 December 2017	12 months
Nick Greatorex	1 January 2015	12 months

DIRECTORS' REMUNERATION REPORT CONTINUED

Non-Executive Directors' terms of engagement

In 2017, all Non-Executive Directors were considered to be independent of the Company.

Non-Executive Directors	Date of joining the Board	Expiry date of current three-year appointment
Ian Powell	1 September 2016	31 December 2019
Gillian Sheldon	1 September 2012	31 August 2018
Andrew Williams	1 January 2015	31 December 2017
John Cresswell	17 November 2015	16 November 2018
Matthew Lester	1 March 2017	28 February 2020
Baroness Lucy Neville-Rolfe	6 December 2017	5 December 2020

Payments to former Directors (Audited)

No payments (other than regular pension benefits and legacy share plan maturities which were commenced in previous years) were made during the year ended 31 December 2017 to any past Director of the Company.

Payments for loss of office (Audited)

Andy Parker stepped down from the Board and left Capita on 15 September 2017 following market announcements on 2 March 2017 and 11 September 2017. The agreed termination settlement comprises a payment in lieu of notice equal to 12 months' salary (£600,000), £45,000 as compensation for loss of benefits, £14,192 in respect of accrued holiday entitlement and £250 in consideration for enhanced post-employment undertakings. His DAB deferred awards vested (69,377 shares) and his outstanding LTIP awards lapsed on 15 September 2017. £7,500 (excluding VAT) was paid directly to third-party service providers in respect of legal services provided to Andy in connection with his settlement and he will continue to receive life assurance cover and private medical insurance cover consistent with current levels until 14 September 2018.

Vic Cysin stepped down from the Board on 18 December 2017 and left Capita on 31 January 2018 following a market announcement on 18 December 2017. The agreed termination settlement comprises a payment in lieu of notice of £393,000 in respect of salary and contractual benefits (including pension) for his 12-month notice period, £22,153 in respect of accrued holiday entitlement and £250 in consideration for enhanced post-employment undertakings. On 31 January 2018, Vic's DAB deferred award (17,109 shares) became exercisable for a period of three months and his 15,258 restricted shares were released. The Remuneration Committee having exercised its discretion, Vic's outstanding LTIP awards will remain capable of vesting in accordance with the rules of the scheme, subject to achievement of applicable performance measures and reduced pro-rata to reflect Vic's period of employment (including the notice period) as a proportion of each award's three-year vesting period. Up to £11,000 (excluding VAT) will be paid directly to third-party service providers in respect of: (i) legal services relating to Vic's settlement; and (ii) outplacement and training services and he will continue to receive life assurance cover and private medical insurance cover consistent with current levels until 31 January 2019.

Chris Sellers stepped down from the Board on 23 January 2018 and left Capita on 31 January 2018. The agreed termination settlement comprises a payment in lieu of notice of £360,000 in respect of salary for his 12-month notice period, £4,500 in respect of accrued holiday entitlement and £250 in consideration for enhanced post-employment undertakings. The Remuneration Committee having exercised its discretion, Chris' outstanding LTIP awards will remain capable of vesting in accordance with the rules of the scheme, subject to achievement of applicable performance measures and, where relevant, reduced pro-rata to reflect Chris' period of employment (including the notice period) as a proportion of each award's three-year vesting period. Up to £16,000 (excluding VAT) will be paid directly to third-party service providers in respect of: (i) legal services relating to Chris' settlement; and (ii) outplacement and training services and he will continue to receive life assurance cover (reduced to a level of two times base salary) and private medical insurance cover consistent with current levels until 31 January 2019.

Percentage change in remuneration levels

The table below shows change in base compensation, benefits and annual bonus for the CEO in the 2017 financial year, compared to the average for all employees:

	Chief Executive Officer		All employees
	At 31 December 2017 £	% change 2017 v 2016	% change 2017 v 2016
Base compensation	725,000	20.8%	3.00%
Benefits	59,544	12.4%	7.58%
Bonus	–	–%	(13.4)%

This all-employee information is based on UK employees only as it was felt that using overseas payroll data would distort the information.

The above figures for CEO pay in 2017 are annualised based on the salary and benefits, excluding one-off legal fees, payable to Jon Lewis as CEO from 1 December 2017.

Relative importance of the spend on pay

The table below shows the spend on employee costs in the 2017 financial year, compared to dividends:

	2017 £m	2016 £m	% change
Employee costs	2,218.9	2,216.9	1.0%
Dividends	211.0	214.8	(1.8)%

Performance graph and CEO pay

The following chart compares the value of an investment of £100 in the Company's shares with an investment of the same amount in the FTSE All-Share Index and the FTSE 350 Support Services Index assuming that all dividend income is re-invested.

CAPITA VS. FTSE ALL-SHARE INDEX AND FTSE 350 SUPPORT SERVICES INDEX VALUE OF INVESTMENT OF £100 ON 1 JANUARY 2009

IMAGE REMOVED

The Committee is of the opinion that this comparison provides a clear picture of the performance of the Group relative to both a wide range of companies in the UK and also a specific group of companies within the same sector. Over the nine-year period to 31 December 2017, £100 invested in Capita on 1 January 2009 would be worth £72 at 31 December 2017 compared to £263 for an investment in the FTSE All-Share Index and £348 for an investment in the FTSE 350 Support Services Index.

The total remuneration figures for the CEO during the 2017 financial year are shown in the table below. Consistent with the calculation methodology for the single figure for total remuneration, the total remuneration figure includes the total annual bonus award based on that year's performance and the LTIP award based on the three-year performance period ending in the relevant year. The annual bonus payout and LTIP award vesting level as a percentage of the maximum opportunity are also shown for this year.

Year	CEO – Single Figure of total remuneration	Annual bonus payout against maximum opportunity	Long-term incentive vesting rates against maximum opportunity
2017	£741,376	–%	–%
2016	£682,958	–%	–%
2015	£2,520,428	50%	71.365%
2014	£2,558,998	100%	67.2%
2013	£2,326,250	75%	54.5%
2012	£2,038,233	100%	47.75%
2011	£1,833,308	–%	56.02%
2010	£1,399,675	100%	88.567%
2009	£1,621,793	75%	100%

Note – the vesting rates for the long-term incentives are averaged between the LTIP and the DAB vesting rates for 2010-2013 and 2015. For 2014, this is the actual vesting for the LTIP as there is no DAB maturity in 2014.

Note – figures for 2010-2013 are based on remuneration for Paul Pindar. Figures for 2014-2016 are based on remuneration for Andy Parker. Figures for 2017 are based on remuneration paid to Andy Parker as CEO until 15 September 2017, to Nick Greatorex as interim CEO from 16 September 2017 to 30 November 2017 and to Jon Lewis as CEO from 1 December 2017.

Approval of the Directors' remuneration report

The Directors' remuneration report, including both the Remuneration Policy and the Annual Report on Remuneration, was approved by the Board on 23 April 2018.

John Cresswell
Chair, Remuneration Committee
23 April 2018

FINANCIAL STATEMENTS

Consolidated financial statements	91	Notes to the Company financial statements	187
Notes to the consolidated financial statements	96	Shareholder information	201
Independent Auditor's report	170	Alternative Performance Measures	202
Company financial statements	185		

MAKING A DIFFERENCE

TO CHILDREN, YOUNG PEOPLE AND SCHOOLS IN STAFFORDSHIRE.

IMAGE REMOVED

we are change makers

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CONSOLIDATED INCOME STATEMENT

FOR THE YEAR ENDED 31 DECEMBER 2017

		2017				Restated[1] 2016			
			Non-underlying				Non-underlying		
	Notes	Underlying (note 3) £m	Business exit (note 4) £m	Specific items (note 6) £m	Total £m	Underlying (note 3) £m	Business exit (note 4) £m	Specific items (note 6) £m	Total £m
Continuing operations:									
Revenue		4,167.9	66.7	–	4,234.6	4,357.3	11.3	–	4,368.6
Cost of sales		(3,121.8)	(54.7)	(5.5)	(3,182.0)	(3,418.5)	(6.7)	(42.3)	(3,467.5)
Gross profit		1,046.1	12.0	(5.5)	1,052.6	938.8	4.6	(42.3)	901.1
Administrative expenses	3,4,6	(598.7)	(26.7)	(847.3)	(1,472.7)	(604.2)	(1.8)	(311.2)	(917.2)
Operating profit/(loss)	3,6,8	447.4	(14.7)	(852.8)	(420.1)	334.6	2.8	(353.5)	(16.1)
Net finance costs	10	(64.4)	(0.1)	2.1	(62.4)	(66.1)	–	(7.7)	(73.8)
(Loss)/gain on business disposal	4	–	(30.6)	–	(30.6)	–	0.1	–	0.1
Profit/(loss) before tax		383.0	(45.4)	(850.7)	(513.1)	268.5	2.9	(361.2)	(89.8)
Income tax (expense)/credit	11	(68.0)	–	54.0	(14.0)	(46.4)	0.5	47.1	1.2
Profit/(loss) for the year from continuing operations		315.0	(45.4)	(796.7)	(527.1)	222.1	3.4	(314.1)	(88.6)
Discontinued operations:									
Profit/(loss) for the year	5,6	–	482.5	(66.1)	416.4	–	50.6	(13.7)	36.9
Total profit/(loss) for the year		315.0	437.1	(862.8)	(110.7)	222.1	54.0	(327.8)	(51.7)
Attributable to:									
Owners of the Company		303.6	437.1	(857.8)	(117.1)	210.6	54.0	(322.5)	(57.9)
Non-controlling interests		11.4	–	(5.0)	6.4	11.5	–	(5.3)	6.2
		315.0	437.1	(862.8)	(110.7)	222.1	54.0	(327.8)	(51.7)
Earnings/(loss) per share	12								
Continuing:									
– basic		45.61p	(6.82)p	(118.93)p	(80.14)p	31.68p	0.51p	(46.46)p	(14.27)p
– diluted		45.61p	(6.82)p	(118.93)p	(80.14)p	31.68p	0.51p	(46.46)p	(14.27)p
Total operations:									
– basic		45.61p	65.66p	(128.86)p	(17.58)p	31.68p	8.12p	(48.52)p	(8.72)p
– diluted		45.61p	65.66p	(128.86)p	(17.58)p	31.68p	8.12p	(48.52)p	(8.72)p

The accompanying notes are an integral part of the financial statements.

1 2016 restatement was due to the adoption of IFRS 15 during the year. Refer to note 38 for further details.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

FOR THE YEAR ENDED 31 DECEMBER 2017

	Notes	£m	2017 £m	£m	Restated[1] 2016 £m
Loss for the year			(110.7)		(51.7)
Other comprehensive income/(expense):					
Items that will not be reclassified subsequently to profit or loss					
Actuarial loss on defined benefit pension schemes	34	(51.4)		(157.7)	
Income tax effect	11	8.8		26.5	
			(42.6)		(131.2)
			(42.6)		(131.2)
Items that will or may be reclassified subsequently to profit or loss					
Exchange differences on translation of foreign operations			(4.6)		26.7
Net investment hedge of foreign operations		10.4		(11.7)	
Income tax effect	11	–		–	
			10.4		(11.7)
Gain on cash flow hedges	28	2.0		14.3	
Reclassification adjustments for losses included in the income statement	28	0.3		3.3	
Income tax effect	11	(0.4)		(5.6)	
			1.9		12.0
			7.7		27.0
Other comprehensive expense for the year net of tax			(34.9)		(104.2)
Total comprehensive expense for the year net of tax			(145.6)		(155.9)
Attributable to:					
Owners of the Company			(152.0)		(162.1)
Non-controlling interests			6.4		6.2
			(145.6)		(155.9)

The accompanying notes are an integral part of the financial statements.

1 2016 restatement was due to the adoption of IFRS 15 during the year. Refer to note 38 for further details.

CONSOLIDATED BALANCE SHEET
AS AT 31 DECEMBER 2017

	Notes	2017 £m	Restated[1] 2016 £m	Restated[1] As at 1 January 2016 £m
Non-current assets				
Property, plant and equipment	14	219.3	394.7	406.0
Intangible assets	15,16	1,812.1	2,754.2	2,810.0
Contract fulfilment assets	18	252.5	240.6	277.6
Financial assets	19	132.3	337.6	186.6
Deferred taxation	11	159.3	222.4	181.6
Trade and other receivables	20	28.0	48.8	44.4
		2,603.5	3,998.3	3,906.2
Current assets				
Financial assets	19	88.7	92.6	44.3
Disposal group assets held for sale	4	5.9	–	84.1
Funds assets	25	–	173.6	161.7
Trade and other receivables	20	775.8	842.7	768.2
Cash	21	921.7	1,098.3	534.0
Income tax receivable	11	25.6	–	–
		1,817.7	2,207.2	1,592.3
Total assets		4,421.2	6,205.5	5,498.5
Current liabilities				
Trade and other payables	22	755.2	977.0	873.0
Deferred income	23	1,201.2	1,374.9	1,157.3
Overdrafts	21	443.3	532.5	448.7
Financial liabilities	24	265.6	224.2	230.8
Disposal group liabilities held for sale	4	1.4	–	40.4
Funds liabilities	25	–	173.6	161.7
Provisions	27	164.1	112.5	69.4
Income tax payable	11	–	18.6	46.2
		2,830.8	3,413.3	3,027.5
Non-current liabilities				
Trade and other payables	22	17.0	21.0	13.8
Deferred income	23	314.0	216.7	228.5
Financial liabilities	24	1,721.7	2,694.4	2,163.4
Deferred taxation	11	12.2	19.6	17.0
Provisions	27	48.5	48.2	49.0
Employee benefits	34	406.8	345.2	188.3
		2,520.2	3,345.1	2,660.0
Total liabilities		5,351.0	6,758.4	5,687.5
Net liabilities		(929.8)	(552.9)	(189.0)
Capital and reserves				
Issued share capital	29	13.8	13.8	13.8
Share premium		501.3	501.3	500.7
Employee benefit trust and treasury shares	29	(0.2)	(0.2)	(0.3)
Capital redemption reserve		1.8	1.8	1.8
Foreign currency translation reserve		(0.4)	(6.2)	(21.2)
Cash flow hedging reserve		1.9	–	(12.0)
Retained deficit		(1,517.2)	(1,131.8)	(738.2)
Deficit attributable to owners of the Company		(999.0)	(621.3)	(255.4)
Non-controlling interests		69.2	68.4	66.4
Total deficit		(929.8)	(552.9)	(189.0)

The accompanying notes are an integral part of the financial statements.

1 2016 restatement was due to the adoption of IFRS 15 during the year. Refer to note 38 for further details.

The accounts were approved by the Board of Directors on 23 April 2018 and signed on its behalf by:

J Lewis
Chief Executive Officer

N Greatorex
Chief Financial Officer

Company registered number: 2081330

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

FOR THE YEAR ENDED 31 DECEMBER 2017

	Share capital £m	Share premium £m	Employee benefit trust and treasury shares £m	Capital redemption reserve £m	Retained earnings/ (deficit) £m	Foreign currency translation reserve £m	Cash flow hedging reserve £m	Total £m	Non-controlling interests £m	Total equity/ (deficit) £m
At 1 January 2016, as reported	13.8	500.7	(0.3)	1.8	196.5	(21.2)	(12.0)	679.3	74.0	753.3
Impact of change in accounting standards – IFRS 15	–	–	–	–	(934.7)	–	–	(934.7)	(7.6)	(942.3)
At 1 January 2016, restated[1]	13.8	500.7	(0.3)	1.8	(738.2)	(21.2)	(12.0)	(255.4)	66.4	(189.0)
Profit/(loss) for the year, restated[1]	–	–	–	–	(57.9)	–	–	(57.9)	6.2	(51.7)
Other comprehensive (expense)/income	–	–	–	–	(131.2)	15.0	12.0	(104.2)	–	(104.2)
Total comprehensive income/(expense)/for the year	–	–	–	–	(189.1)	15.0	12.0	(162.1)	6.2	(155.9)
Share based payment	–	–	–	–	(4.5)	–	–	(4.5)	–	(4.5)
Deferred income tax relating to share based payments	–	–	–	–	(12.6)	–	–	(12.6)	–	(12.6)
Income tax deduction on exercise of stock options	–	–	–	–	6.8	–	–	6.8	–	6.8
Shares issued	–	0.6	0.1	–	(0.1)	–	–	0.6	–	0.6
Equity dividends paid	–	–	–	–	(214.8)	–	–	(214.8)	(4.2)	(219.0)
Movement in put options held by non-controlling interests	–	–	–	–	20.7	–	–	20.7	–	20.7
At 1 January 2017, restated[1]	13.8	501.3	(0.2)	1.8	(1,131.8)	(6.2)	–	(621.3)	68.4	(552.9)
Profit/(loss) for the year	–	–	–	–	(117.1)	–	–	(117.1)	6.4	(110.7)
Other comprehensive (expense)/income	–	–	–	–	(42.6)	5.8	1.9	(34.9)	–	(34.9)
Total comprehensive (expense)/income for the year	–	–	–	–	(159.7)	5.8	1.9	(152.0)	6.4	(145.6)
Share based payment	–	–	–	–	2.9	–	–	2.9	–	2.9
Equity dividends paid	–	–	–	–	(211.0)	–	–	(211.0)	(5.6)	(216.6)
Investment in non-controlling interest	–	–	–	–	(11.1)	–	–	(11.1)	–	(11.1)
Movement in put options held by non-controlling interests	–	–	–	–	(6.5)	–	–	(6.5)	–	(6.5)
At 31 December 2017	13.8	501.3	(0.2)	1.8	(1,517.2)	(0.4)	1.9	(999.0)	69.2	(929.8)

Share capital – The balance classified as share capital is the nominal proceeds on issue of the Company's equity share capital, comprising 2½p ordinary shares.

Share premium – The amount paid to the Company by shareholders, in cash or other consideration, over and above the nominal value of shares issued to them.

Employee benefit trust and treasury shares – Shares that have been bought back by the Company which are available for retirement or resale; shares held in the employee benefit trust have no voting rights and do not have entitlement to a dividend.

Capital redemption reserve – The Company can redeem shares by repaying the market value to the shareholder, whereupon the shares are cancelled. Redemption must be from distributable profits. The Capital redemption reserve represents the nominal value of the shares redeemed.

Foreign currency translation reserve – Gains or losses resulting from the process of expressing amounts denominated or measured in one currency in terms of another currency by use of the exchange rate between the two currencies. This process is required to consolidate the financial statements of foreign affiliates into the total Group financial statements and to recognise the conversion of foreign currency or the settlement of a receivable or payable denominated in foreign currency at a rate different from that at which the item is recorded.

Cash flow hedging reserve – This reserve records the portion of the gain or loss on a hedging instrument in a cash flow hedge that is determined to be an effective hedge. Also recorded here are fair value changes on available-for-sale investments.

Retained earnings – Net profits kept to accumulate in the Group after dividends are paid and retained in the business as working capital.

Non-controlling interests (NCI) – This represents the equity in a subsidiary that is not attributable directly or indirectly to the parent company.

The accompanying notes are an integral part of the financial statements.

1 2016 restatement was due to the adoption of IFRS 15 during the year. Refer to note 38 for further details.

CONSOLIDATED CASH FLOW STATEMENT

FOR THE YEAR ENDED 31 DECEMBER 2017

	Notes	2017 Continuing	2017 Discontinued	2017 £m	Restated[1] 2016 Continuing	Restated[1] 2016 Discontinued	Restated[1] 2016 £m
Cash generated from operations before non-underlying cash items	31	196.8	20.1	216.9	650.3	89.2	739.5
Non-underlying net movement in payables and receivables	4	2.5	–	2.5	(12.3)	–	(12.3)
Asset Services settlement provision cash paid	27	–	(18.5)	(18.5)	–	(23.2)	(23.2)
Business exit provision cash paid	27	(2.8)	–	(2.8)	(14.4)	–	(14.4)
Insurance asset recovery		–	8.2	8.2	–	–	–
Pension settlement		–	–	–	(3.3)	–	(3.3)
Cash generated from operations		196.5	9.8	206.3	620.3	66.0	686.3
Income tax received/(paid)		9.5	(3.2)	6.3	(53.7)	(10.0)	(63.7)
Net interest received/(paid)		(54.2)	0.1	(54.1)	(59.6)	0.2	(59.4)
Net cash inflow from operating activities		151.8	6.7	158.5	507.0	56.2	563.2
Cash flows from investing activities							
Purchase of property, plant and equipment	14	(66.2)	(2.7)	(68.9)	(74.0)	(8.4)	(82.4)
Purchase of intangible assets	15	(71.0)	(1.9)	(72.9)	(66.3)	(5.9)	(72.2)
Proceeds from sale of property, plant and equipment/ intangible assets	8,14,15	23.1	–	23.1	0.6	–	0.6
Acquisition of subsidiary undertakings and businesses	6,17	(24.5)	–	(24.5)	(100.5)	–	(100.5)
Cash acquired with subsidiary undertakings	17	4.5	–	4.5	4.0	–	4.0
Proceeds on disposal of subsidiary undertakings	4,5	17.0	909.5	926.5	30.6	–	30.6
Cash disposed of with subsidiary undertakings	4,5	(0.1)	(45.8)	(45.9)	(4.2)	–	(4.2)
Deferred consideration received	19	11.8	–	11.8	3.0	–	3.0
Deferred consideration paid	*17,31*	*(5.8)*	*(5.0)*	*(10.8)*	*(10.7)*	–	*(10.7)*
Contingent consideration paid	17,28	(11.7)	–	(11.7)	(18.5)	–	(18.5)
Purchase of financial assets	8,19	(0.7)	–	(0.7)	–	(0.9)	(0.9)
Net cash inflow/(outflow) from investing activities		(123.6)	854.1	730.5	(236.0)	(15.2)	(251.2)
Cash flows from financing activities							
Issue of share capital	29	–	–	–	0.6	–	0.6
Intercompany dividends received/(paid)		46.6	(46.6)	–	–	–	–
External dividends paid	13	(216.6)	–	(216.6)	(219.0)	–	(219.0)
Capital element of finance lease rental payments	31	(2.1)	–	(2.1)	(5.5)	–	(5.5)
Proceeds on issue of bonds	31	–	–	–	170.8	–	170.8
Proceeds on issue of term debt	31	–	–	–	350.0	–	350.0
Proceeds on issue of loan note		–	–	–	0.3	–	0.3
Repayment of bonds	24,31	(124.1)	–	(124.1)	(141.0)	–	(141.0)
Repayment of term debt	31	(550.0)	–	(550.0)	–	–	–
Repayment of fixed rate swaps		(84.6)	–	(84.6)	–	–	–
Financing arrangement costs	24,31	(2.1)	–	(2.1)	(0.6)	–	(0.6)
Net cash inflow/(outflow) from financing activities		(932.9)	(46.6)	(979.5)	155.6	0.0	155.6
Increase in cash and cash equivalents		(904.7)	814.2	(90.5)	426.6	41.0	467.6
Cash and cash equivalents at the beginning of the period				565.8			85.3
Impact of movement in exchange rates	31			3.1			12.9
Cash and cash equivalents at 31 December				478.4			565.8
Cash and cash equivalents comprise:							
Cash at bank and in hand	21			921.7			1,098.3
Overdrafts	21			(443.3)			(532.5)
Total				478.4			565.8

1 2016 restatement was due to the adoption of IFRS 15 during the year. Refer to note 38 for further details.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1 CORPORATE INFORMATION

The consolidated financial statements of Capita plc for the year ended 31 December 2017 were authorised for issue in accordance with a resolution of the Directors on 23 April 2018. Capita plc is a public limited company incorporated in England and Wales whose shares are publicly traded.

The principal activities of the Group are given in the strategic report on pages 03 to 48.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Underlying profit

IAS 1 requires an entity to present additional information for specific items to enable users to better assess the entity's financial performance. In practice these items are commonly referred to as 'specific' or 'non-underlying' items although such terminology is not defined in IFRS and accordingly there is a level of judgement required in determining what items to separately identify. The Board has adopted a policy to separately disclose those items that it considers are outside the underlying operating results for the particular year under review and against which the Group's performance is assessed.

Those items which relate to the ordinary course of the Group's operating activities remain within underlying. Following the adoption of IFRS 15, the Board has adopted a policy to separately disclose in the notes to the financial statements the operating profit/loss from significant new contract wins in-period and significant restructuring. In order for users of the financial statements to obtain a proper understanding of the financial information and the performance of the business. A new contract is assessed as that which is significant and either entirely new to the Group, or a significant amendment to the scope and scale of an existing contract. The Group continually assesses the resourcing levels, both at a divisional level and also in relation to the management and delivery of individual contracts. This results in restructuring in the normal course of business and any such charges are recorded in 'Underlying before significant new contracts and restructuring' results. A significant restructuring is assessed as that above this normal level of restructuring. As discussed in the Chief Executive Officer's review, a major transformation plan has been launched and costs incurred in support of this, including external adviser costs, are also presented as restructuring charges. Contract terminations arising in the normal course of business and which result in the disposal of a contract fulfilment asset and/or a true-up of revenue recognised, will be included within 'Underlying before significant new contracts and restructuring', and separately disclosed if considered material (see note 3).

Items within non-underlying include intangible amortisation, non-current asset impairments, acquisition contingent consideration movements, the financial impact of business exits or businesses in the process of being exited, acquisition expenses, movements in the mark-to-market valuation of certain financial instruments, and specific non-recurring items in the income statement. In the Directors' judgement, these need to be disclosed separately (see notes 4, 5, 6, 10 and 11) by virtue of their nature, size and/or incidence, in order for users of the financial statements to obtain a proper understanding of the financial information and the underlying performance of the business.

This policy is kept under review by the Board and the Audit and Risk Committee, and is discussed in the Committee's report on pages 66–74.

Except for the disposal of our Capita Asset Services businesses, none of our 2017 business exits or businesses in the process of being exited meet the definition of 'discontinued operations' as stipulated by IFRS 5, which requires disclosure and the restatement of comparative information where the relative size of a disposal or business closure is significant. Accordingly, the separate presentation described above does not fall within the requirements of IFRS 5 concerning discontinued operations and comparatives have not been restated.

Assets held for sale

The Group classifies a non-current asset (or disposal group) as held for sale if its carrying amount will be recovered principally through a sale transaction rather than continued use.

For this to be the case, the asset (or disposal group) must be available for immediate sale in its present condition subject only to terms that are usual and customary for sales of such assets (or disposal groups) and its sale must be highly probable. For the sale to be highly probable, the appropriate level of management must be committed to a plan to sell the asset (or disposal group), and an active programme to locate a buyer and complete the plan must have been initiated. Further, the asset (or disposal group) must be actively marketed for sale at a price that is reasonable in relation to its current fair value. In addition, the sale should be expected to qualify for recognition as a completed sale within one year from the date of classification.

Significant accounting judgements, estimates and assumptions

The preparation of financial statements in conformity with generally accepted accounting principles requires the Directors to make judgements and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingencies at the date of the financial statements and the reported income and expense during the reported periods. Although these judgements and assumptions are based on the Directors' best knowledge of the amount, events or actions, actual results may differ.

The key sources of estimation uncertainty that have a significant risk of causing material adjustment to the carrying amounts of assets and liabilities within the next financial year are as follows:

- the measurement of revenue and resulting profit recognition – due to the size and complexity of some of the Group's contracts, there are significant judgements to be applied, including the measurement and timing of revenue recognition and the recognition of related balance sheet items (such as contract fulfilment assets, capitalisation of costs to obtain a contract, trade receivables, accrued income and deferred income) that result from the performance of the contract (see (e) and (s) below, and the Divisional Performance section of the strategic report). This is particularly in respect of contracts that are in the transformation stage and pre-inflection point, such as NHS PCSE and mobilcom-debitel. For the majority of contracts, clients assess Capita's performance on output measures (i.e what they deliver) rather than input (i.e. how they deliver) which drives the basis on which delivery of performance obligations are determined. This inherently leads to more judgement;
- the measurement of intangible assets other than goodwill in a business combination – on the acquisition of a business the identifiable intangible assets may include licences, customer lists and brands. The fair value of these assets is determined by discounting estimated future net cash flows generated by the asset where no active market for the assets exists. The use of different assumptions for the expectations of future cash flows and the discount rate would change the valuation of the intangible assets. The relative size of the Group's intangible assets, excluding goodwill, makes the judgements surrounding the estimated useful lives material to the Group's financial position and performance. Refer to (j) below and note 15;
- the measurement and impairment of goodwill – the amount of goodwill initially recognised as a result of a business combination is dependent on the allocation of the purchase price to the fair value of the identifiable assets acquired and the liabilities assumed. The determination of the fair value of the assets and liabilities is based, to a considerable extent, on management's judgement. Allocation of the purchase price affects the results of the Group as finite lived intangible assets are amortised. The Group determines whether goodwill is impaired on an annual basis or more frequently as required and this requires an estimation of the value in use of the cash-generating units to which the intangible assets are allocated utilising an estimation of future cash flows and choosing a suitable discount rate (see note 16);

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES CONTINUED

- the measurement of defined benefit obligations – the accounting cost of these benefits and the present value of pension liabilities involve judgements about uncertain events including such factors as the life expectancy of members, the salary progression of our current employees, price inflation and the discount rate used to calculate the net present value of the future pension payments. We use estimates for all of these factors in determining the pension costs and liabilities incorporated in our financial statements. The assumptions reflect historical experience and our judgement regarding future expectations (see note 34); and
- the measurement of provisions and contingent liabilities – measuring and recognising provisions and the exposures to contingent liabilities related to pending litigation or other outstanding claims subject to negotiated settlement, mediation and arbitration, as well as other contingent liabilities (see notes 27 and 33). Judgement is necessary in assessing the likelihood that a pending claim will succeed, or a liability will arise, and to quantify the possible range of the financial settlement. Because of the inherent uncertainty in this evaluation process, actual losses may be different from the originally estimated provision.

For further details on the sensitivity of carrying amounts to the methods, assumptions and estimates used, the reason for the sensitivity, the expected resolution of uncertainties, and the range of reasonable possible alternatives for each of the above, refer to the policies and notes referenced.

The Directors apply judgement when considering the presentation of underlying and non-underlying items. As discussed above, the Group separately presents specific non-recurring items in the income statement, which in the Directors judgement, need to be disclosed separately by virtue of their nature, size and/or incidence in order for users of the financial statements to obtain a proper understanding of the financial information and the underlying performance of the business (see note 6). This judgement has an impact on the calculation of covenants (refer to (b)).

(a) Statement of compliance

The consolidated financial statements of Capita plc and all of its subsidiaries (the Group) have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union and as applied in accordance with the provisions of the Companies Act 2006.

The parent company has applied FRS 101 – Reduced Disclosure Framework in the preparation of its individual financial statements and these are contained on pages 185 to 200. FRS 101 applies IFRS as adopted by the European Union with certain disclosure exemptions.

(b) Basis of preparation

The consolidated financial statements have been prepared under IFRS where certain financial instruments and the pension assets have been measured at fair value. The carrying value of recognised assets and liabilities that are hedged are adjusted to record changes in the fair values attributable to the risks that are being hedged. The consolidated financial statements are presented in pounds sterling and all values are rounded to the nearest tenth of a million (£m) except when otherwise indicated.

In determining the appropriate basis of preparation of the financial statements for the year ending 31 December 2017, the Directors are required to consider whether the Group can continue in operational existence for the foreseeable future. The Board has concluded that it is appropriate to adopt the going concern basis, having undertaken a rigorous assessment of the financial forecasts and with consideration of the anticipated net proceeds from the announced Rights Issue which the Board is confident will be approved.

The Group's committed revolving credit facility, bank term loan facilities and private placement notes are subject to compliance with covenant requirements including maximum ratios of adjusted net debt to adjusted EBITDA. The Group's covenanted maximum ratio is 3.0 times or to 3.5 times depending on the debt instrument in question. They are tested semi-annually.

The Group has net debt of £1,117.0m at 31 December 2017 (2016: £1,778.8m) and adjusted net debt of £1,219.4m at 31 December 2017 (2016: £1,809.3m). The components of net debt and adjusted net debt are shown in the table below. Net debt is reported in note 31 – additional cash flow information. Adjusted net debt is used to calculate the gearing ratio adjusted net debt to adjusted EBITDA (refer to Alternative Performance Measures on pages 202–204).

The Group's calculation of adjusted net debt to adjusted EBITDA at 31 December 2017 is 2.27 times and is compliant with the relevant ratios.

Net debt and adjusted net debt

	Notes	2017 £m	Restated 2016 £m
Cash, cash equivalents and overdrafts	21, 31	478.4	565.8
Other loan notes	31	(0.3)	(0.3)
Private placement loan notes	31	(1,664.0)	(1,961.7)
Interest and currency swaps in relation to USD denominated loan notes	31	176.8	357.9
Interest rate swaps in relation to GBP denominated loan notes	31	5.4	7.7
Term loan	31	(100.0)	(650.0)
Finance leases	31	(0.2)	(2.3)
Total net liabilities from financing activities		(1,582.3)	(2,248.7)
Underlying net debt		(1,103.9)	(1,682.9)
Fixed rate interest rate swaps	31	–	(85.1)
Deferred consideration	31	(13.1)	(10.8)
Net debt		(1,117.0)	(1,778.8)
Contingent obligations under bonds and guarantees	33	(88.4)	(30.5)
Money Market Funds		(14.0)	–
Adjusted net debt		(1,219.4)	(1,809.3)

On 31 January 2018, the Group announced a multi-year transformation plan, encompassing strategy, cost competitiveness, sales, IT and its capital structure, to improve the performance of Capita over the medium-to-long term. This transformation plan includes an assessment of the appropriate financial leverage for the Group over the medium term, to ensure that Capita has a sustainable capital base to support its customers and operations, increase investment in the business and deliver future strategy. The Board's view is that the appropriate leverage for Capita over the medium term should be between 1.0 and 2.0 times adjusted net debt to adjusted EBITDA (prior to the adoption of IFRS 16). Accordingly, the Board has decided to raise additional equity of £701m by way of a Rights Issue, which is fully underwritten by Citigroup Global Markets Limited and Goldman Sachs International.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES CONTINUED

The transformation plan is being finalised, and the key actions and forecast impacts incorporated into detailed business plans. These are in support of the new strategy that has been reviewed and approved by the Board. Details of the new strategy are outlined in the Chief Executive Officer's review on pages 6–12.

For the purpose of the going concern assessment the Directors have considered a 'base-case' set of projections that cover the first two years of the new strategic plan, to 31 December 2019. This base-case includes cost reduction identified to date but not the anticipated proceeds from the Rights Issue and planned strategic disposals, and therefore importantly does not include the investment these will enable the Group to make, and the benefits these will deliver over the longer term.

The Group's committed facilities and private placement notes are subject to compliance with covenant requirements including maximum ratios of adjusted net debt to adjusted EBITDA. This covenant threshold is tested semi-annually, and is set at 3.0 times to 3.5 times depending on the debt instrument in question. The Directors have applied judgement in terms of how the ratio is calculated by applying the same treatment that has been applied in preparing and presenting the financial statements. Accordingly, items that are presented as non-underlying are excluded from the covenant definition of adjusted EBITDA (with the exception of acquisition costs), as are restructuring costs that are now presented within the underlying results as set out in note 3 to the consolidated financial statements. This basis of calculation is consistent with the approach adopted in prior years.

In assessing the going concern assumptions, the Board has undertaken a rigorous assessment of the forecast outturns and assessed identified downside risks and mitigating actions, by reference to the relevant covenant tests. The downside risks include a number of severe but plausible scenarios, incorporating underperformance against the business plan, unexpected cash outflows and customer attrition and unwillingness to award the Group new contracts and extensions to existing arrangements. The Board has considered mitigating actions available to the Group in response to these sensitivities.

Whilst the 'base case' scenario shows the business can operate in compliance with its adjusted net debt to adjusted EBITDA covenants and applying the reasonable downside scenarios indicate that, absent the anticipated net proceeds from the announced Rights Issue, and assuming no other mitigating actions are taken by the Group, the available headroom is not sufficient to operate within the 3.0 times adjusted net debt to adjusted EBITDA covenant test. The Board has therefore considered the Rights Issue net proceeds in its assessment of going concern and the Group's ability to realise their assets and discharge their liabilities in the normal course of business.

Rights Issue

The Company has today launched a Rights Issue to raise £701m.

The Rights Issue will be subject to shareholders' approval and the general meeting to approve the equity raise is scheduled for 9 May 2018.

The Rights Issue is fully underwritten for £701m, by Citigroup Global Markets Limited and Goldman Sachs International.

Material uncertainties

In assessing the going concern assumptions, the Board has reviewed the base case plans, identified downsides and anticipated receipt of proceeds from the Rights Issue. Following this assessment, the Board has a reasonable expectation that the Company and the Group will be able to operate as a going concern for the foreseeable future.

In undertaking the assessment, the Board has considered the fact that a shareholder vote is required in order to raise additional capital through the Rights Issue, and that the underwriting agreement is subject to certain specific conditions which, although customary in nature, are outside the control of the Company. These events and conditions indicate a material uncertainty on the completion of the Rights Issue which may cast significant doubt about the Group's and parent company's ability to continue as a going concern.

The Board is confident that the Rights Issue will be approved and the proceeds received and based on this expectation believes that, even in a reasonable downside scenario, the Group and parent company will continue to have adequate financial resources to realise their assets and discharge their liabilities as they fall due. Accordingly, the Directors have formed the judgement that it is appropriate to prepare the financial statements on the going concern basis. Therefore, the financial statements do not include any adjustments which would be required if the going concern basis of preparation is inappropriate.

The Auditors' report on pages 170–184 refer to this material uncertainty, and their opinion is not qualified or modified in this regard.

(c) Basis of consolidation

The consolidated financial statements comprise the financial statements of Capita plc and its subsidiaries as at 31 December each year. The financial statements of the subsidiaries are prepared for the same reporting year as the parent company, using consistent accounting policies.

All intercompany balances and transactions, including unrealised profits arising from intra-group transactions, have been eliminated in full.

Subsidiaries are consolidated from the date on which control is transferred to the Group until control is transferred out of the Group. Where there is a loss of control of a subsidiary, the consolidated financial statements include the results for the part of the reporting year during which Capita plc has control and the profit or loss on disposal is calculated as the difference between the fair value of the consideration received and the carrying amount of the assets (including goodwill) disposed of. Losses applicable to the non-controlling interests in a subsidiary are attributed to the non-controlling interests even if that results in the non-controlling interests having a deficit balance.

(d) Changes in accounting policies

The accounting policies adopted are consistent with those of the previous financial year except for the early adoption of IFRS 15 Revenue from Contracts with Customers and Clarifications: Revenue from Contracts with Customers. In addition, the Group has adopted the following new amendments to IFRS: IAS 7 Amendments: Disclosure Initiative and IAS 12 Amendments: Recognition of Deferred Tax Assets for Unrealised Losses.

Initial adoption of IFRS 15 Revenue from Contracts with Customers

The standard has an effective date of 1 January 2018 but the Group has decided to early adopt this standard with a date of initial application to the Group of 1 January 2017 using the full retrospective method.

IFRS 15 replaces all existing revenue requirements in IFRS and applies to all revenue arising from contracts with customers unless the contracts are within the scope of other standards such as IAS 17 Leases.

The standard outlines the principles entities must apply to measure and recognise revenue with the core principle being that entities should recognise revenue at an amount that reflects the consideration to which the entity expects to be entitled in exchange for fulfilling its performance obligations to a customer.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES CONTINUED

The principles in IFRS 15 must be applied using the following 5 step model:

1 Identify the contract(s) with a customer

2 Identify the performance obligations in the contract

3 Determine the transaction price

4 Allocate the transaction price to the performance obligations in the contract

5 Recognise revenue when or as the entity satisfies its performance obligations

The standard requires entities to exercise considerable judgement taking into account all the relevant facts and circumstances when applying each step of this model to its contracts with customers. The standard also specifies how to account for the incremental costs of obtaining a contract and the costs directly related to fulfilling a contract, as well as requirements covering matters such as licences of intellectual property, warranties, principal versus agent assessment and options to acquire additional goods or services.

The Group has applied IFRS 15 fully retrospectively in accordance with paragraph C3 (a) of the standard, restating the prior period's comparatives and electing to use the following expedients:

- in respect of completed contracts, the Group will not restate contracts that: (i) begin and end within the same annual reporting period; or (ii) are completed contracts at the beginning of the earliest period presented (para. C5(a));
- in respect of completed contracts that have variable consideration, the Group will use the transaction price at the date the contract was completed rather than estimating variable consideration amounts in the comparative periods (para. C5(b)); and
- for all reporting periods presented before the date of initial application, the Group will not disclose the amount of the transaction price allocated to the remaining performance obligations or an explanation of when the Group expects to recognise that amount as revenue (para. C5(c)).

Details of the change in the Group's accounting policy in respect of revenue recognition, related matters consequent upon the early adoption of IFRS 15 and an explanation of the impact on the Group's prior period financial statements are set out in note 38.

IAS 7 Amendments: Disclosure Initiative

The amendments are part of the IASB's Disclosure Initiative and are designed to help users of financial statements better understand changes in an entity's debt. Entities are required to provide disclosures about changes in their liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes such as foreign exchange movements. This amendment had no impact on the Group as the Group's net debt disclosure was already compliant with the new requirements.

IAS 12 Amendments: Recognition of Deferred Tax Assets for Unrealised Losses

The amendments clarify the accounting for deferred tax assets for unrealised losses on debt instruments measured at fair value. They clarify that an entity needs to consider whether tax law restricts the sources of taxable profits against which it may make deductions on the reversal of that deductible temporary difference. These amendments have had no impact on the Group's financial statements.

(e) Revenue

The Group generates revenue largely in the UK and Europe.

The Group operates a number of diverse businesses and accordingly applies a variety of methods for revenue recognition, based on the principles set out in IFRS 15. Many of the contracts entered into are long term and complex in nature given the breadth of solutions the Group offers.

The revenue and profits recognised in any period are based on the delivery of performance obligations and an assessment of when control is transferred to the customer.

In determining the amount of revenue and profits to record, and related balance sheet items (such as contract fulfilment assets, capitalisation of costs to obtain a contract, trade receivables, accrued income and deferred income) to recognise in the period, management is required to form a number of key judgements and assumptions. This includes an assessment of the costs the Group incurs to deliver the contractual commitments and whether such costs should be expensed as incurred or capitalised. These judgements are inherently subjective and may cover future events such as the achievement of contractual milestones, performance KPIs and planned cost savings. In addition, for certain contracts, key assumptions are made concerning contract extensions and amendments, as well as opportunities to use the contract developed systems and technologies on other similar projects.

Revenue is recognised either when the performance obligation in the contract has been performed (so 'point in time' recognition) or 'over time' as control of the performance obligation is transferred to the customer.

For all contracts, the Group determines if the arrangement with a customer creates enforceable rights and obligations. This assessment results in certain Master Service Agreements (MSAs) not meeting the definition of a contract under IFRS 15 and as such the individual call-off agreements, linked to the MSA, are treated as individual contracts.

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

For contracts with multiple components to be delivered such as transformation, transitions and the delivery of outsourced services, management applies judgement to consider whether those promised goods and services are: (i) distinct – to be accounted for as separate performance obligations; (ii) not distinct – to be combined with other promised goods or services until a bundle is identified that is distinct; or (iii) part of a series of distinct goods and services that are substantially the same and have the same pattern of transfer to the customer.

At contract inception the total transaction price is estimated, being the amount to which the Group expects to be entitled and has rights to under the present contract. This includes an assessment of any variable consideration where the Group's performance may result in additional revenues based on the achievement of agreed KPIs. Such amounts are only included based on the expected value or the most likely outcome method, and only to the extent that it is highly probable that no revenue reversal will occur.

The transaction price does not include estimates of consideration resulting from change orders for additional goods and services unless these are agreed.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES CONTINUED

Once the total transaction price is determined, the Group allocates this to the identified performance obligations in proportion to their relative standalone selling prices and recognises revenue when (or as) those performance obligations are satisfied.

The Group infrequently sells standard products with observable standalone prices due to the specialised services required by clients and therefore the Group applies judgement to determine an appropriate standalone selling price. More frequently, the Group sells a customer bespoke solution, and in these cases the Group typically uses the expected cost plus margin or a contractually stated price approach to estimate the standalone selling price of each performance obligation.

The Group may offer price step downs during the life of a contract, but with no change to the underlying scope of services to be delivered. In general, any such variable consideration, price step down or discount is included in the total transaction price to be allocated across all performance obligations unless it relates to only one performance obligation in the contract.

For each performance obligation, the Group determines if revenue will be recognised over time or at a point in time. Where the Group recognises revenue over time for long-term contracts, this is in general due to the Group performing and the customer simultaneously receiving and consuming the benefits provided over the life of the contract.

For each performance obligation to be recognised over time, the Group applies a revenue recognition method that faithfully depicts the Group's performance in transferring control of the goods or services to the customer. This decision requires assessment of the real nature of the goods or services that the Group has promised to transfer to the customer. The Group applies the relevant output or input method consistently to similar performance obligations in other contracts.

When using the output method the Group recognises revenue on the basis of direct measurements of the value to the customer of the goods and services transferred to date relative to the remaining goods and services under the contract. Where the output method is used, in particular for long-term service contracts where the series guidance is applied (see below for further details), the Group often uses a method of time elapsed which requires minimal estimation. Certain long-term contracts use output methods based upon estimation of number of users, level of service activity or fees collected.

If performance obligations in a contract do not meet the over time criteria, the Group recognises revenue at a point in time (see below for further details).

The Group disaggregates revenue from contracts with customers by contract type, as management believe this best depicts how the nature, amount, timing and uncertainty of the Group's revenue and cash flows are affected by economic factors. Categories remain the same as presented at the 2017 half year: 'Long-term contractual – greater than 2 years' previously shown as 'Contract term longer than 2 years' and 'Short-term contractual – less than 2 years' as 'Over time service with contract length less than 2 years'. Years based from service commencement date.

Long-term contractual – greater than 2 years

The Group provides a range of services in the majority of its reportable segments under customer contracts with a duration of more than two years.

The nature of contracts or performance obligations categorised within this revenue type is diverse and includes: (i) long-term outsourced service arrangements in the public and private sectors; and (ii) active software licence arrangements (see definition below).

The Group considers that the services provided meet the definition of a series of distinct goods and services as they are: (i) substantially the same; and (ii) have the same pattern of transfer (as the series constitutes services provided in distinct time increments (e.g. daily, monthly, quarterly or annual services)) and therefore treats the series as one performance obligation. Even if the underlying activities performed by the Group to satisfy a promise vary significantly throughout the day and from day to day, that fact, by itself, does not mean the distinct goods or services are not substantially the same. For the majority of long-service contracts with customers in this category, the Group recognises revenue using the output method as it best reflects the nature in which the Group is transferring control of the goods or services to the customer.

Active software licences are those where the Group has a continuing involvement after the sale or transfer of control to the customer, which significantly affects the intellectual property to which the customer has rights. The Group is in a majority of cases responsible for any maintenance, continuing support, updates and upgrades and accordingly the sale of the initial software is not distinct. The Group's accounting policy for licences is discussed in more detail below.

Short-term contractual – less than 2 years

The nature of contracts or performance obligations categorised within this revenue type is diverse and includes: (i) short-term outsourced service arrangements in the public and private sectors; and (ii) software maintenance contracts.

The Group has assessed that maintenance and support (i.e. on-call support, remote support) for software licences is a performance obligation that can be considered capable of being distinct and separately identifiable in a contract if the customer has a passive licence. These recurring services are substantially the same as the nature of the promise is for the Group to 'stand ready' to perform maintenance and support when required by the customer. Each day of standing ready is then distinct from each following day and is transferred in the same pattern to the customer.

Transactional (point in time) contracts

The Group delivers a range of goods or services in all reportable segments that are transactional services for which revenue is recognised at the point in time when control of the goods or services has transferred to the customer. This may be at the point of physical delivery of goods and acceptance by a customer or when the customer obtains control of an asset or service in a contract with customer-specified acceptance criteria.

The nature of contracts or performance obligations categorised within this revenue type is diverse and includes: (i) provision of IT hardware goods; (ii) passive software licence agreements; (iii) commission received as agent from the sale of third-party software; and (iv) fees received in relation to delivery of professional services.

Passive software licences are licences which have significant standalone functionality and the contract does not require, and the customer does not reasonably expect, the Group to undertake activities that significantly affect the licence. Any ongoing maintenance or support services for passive licences are likely to be separate performance obligations. The Group's accounting policy for licences is discussed in more detail below.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES CONTINUED

Contract modifications

The Group's contracts are often amended for changes in contract specifications and requirements. Contract modifications exist when the amendment either creates new or changes the existing enforceable rights and obligations. The effect of a contract modification on the transaction price and the Group's measure of progress for the performance obligation to which it relates, is recognised as an adjustment to revenue in one of the following ways:

a. prospectively as an additional separate contract;

b. prospectively as a termination of the existing contract and creation of a new contract;

c. as part of the original contract using a cumulative catch up; or

d. as a combination of b) and c).

For contracts for which the Group has decided there is a series of distinct goods and services that are substantially the same and have the same pattern of transfer where revenue is recognised over time, the modification will always be treated under either a) or b). d) may arise when a contract has a part termination and a modification of the remaining performance obligations.

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.

Judgement is applied in relation to the accounting for such modifications where the final terms or legal contracts have not been agreed prior to the period end as management need to determine if a modification has been approved and if it either creates new or changes existing enforceable rights and obligations of the parties. Depending upon the outcome of such negotiations, the timing and amount of revenue recognised may be different in the relevant accounting periods. Modification and amendments to contracts are undertaken via an agreed formal process. For example, if a change in scope has been approved but the corresponding change in price is still being negotiated, management use their judgement to estimate the change to the total transaction price. Importantly any variable consideration is only recognised to the extent that it is highly probably that no revenue reversal will occur.

Principal versus agent

The Group has arrangements with some of its clients whereby it needs to determine if it acts as a principal or an agent as more than one party is involved in providing the goods and services to the customer. The Group acts as a principal if it controls a promised good or service before transferring that good or service to the customer. The Group is an agent if its role is to arrange for another entity to provide the goods or services. Factors considered in making this assessment are most notably the discretion the Group has in establishing the price for the specified good or service, whether the Group has inventory risk and whether the Group is primarily responsible for fulfilling the promise to deliver the service or good.

This assessment of control requires judgement in particular in relation to certain service contracts. An example is the provision of certain recruitment and learning services where the Group may be assessed to be agent or principal dependent upon the facts and circumstances of the arrangement and the nature of the services being delivered.

Where the Group is acting as a principal, revenue is recorded on a gross basis. Where the Group is acting as an agent, revenue is recorded at a net amount reflecting the margin earned.

Licences

Software licences delivered by the Group can either be right to access ('active') or right to use ('passive') licences. Active licences are licences which require continuous upgrade and updates for the software to remain useful, all other licences are treated as passive licences. The assessment of whether a licence is active or passive involves judgement. The key determinant of whether a licence is active is whether the Group is required to undertake activities that significantly affect the licensed intellectual property (or the customer has a reasonable expectation that it will do so) and the customer is, therefore, exposed to positive or negative impacts resulting from those changes.

When software upgrades are sold as part of the software licence agreement (i.e. software upgrades are promised to the customer), the Group applies judgement to assess whether the software upgrade is distinct from the licence (i.e. a separate performance obligation). If the upgrade is considered fundamental to the ongoing use of the software by the customer, the upgrades are not considered distinct and not accounted for as a separate performance obligation.

The Group considers for each contract that includes a separate licence performance obligation all the facts and circumstances in determining whether the licence revenue is recognised over time or at a point in time from the go live date of the licence.

Contract related assets and liabilities

As a result of the contracts which the Group enters into with its clients, a number of different assets and liabilities are recognised on the Group's balance sheet. These include but are not limited to:

- Property, plant and equipment[1]
- Intangible assets[1]
- Contract fulfilment assets[2]
- Contract assets derived from costs to obtain a contract[2]
- Trade receivables[1]
- Accrued income[2]
- Deferred income[2]

1 No change in the accounting policies for these assets as a result of the adoption of IFRS 15.
2 Refer below for the accounting policy applied following the adoption of IFRS 15.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES CONTINUED

Contract fulfilment assets

Contract fulfilment costs are divided into: (i) costs that give rise to an asset; and (ii) costs that are expensed as incurred.

When determining the appropriate accounting treatment for such costs, the Group firstly considers any other applicable standards. If those other standards preclude capitalisation of a particular cost, then an asset is not recognised under IFRS 15.

If other standards are not applicable to contract fulfilment costs, the Group applies the following criteria which, if met, result in capitalisation: (i) the costs directly relate to a contract or to a specifically identifiable anticipated contract; (ii) the costs generate or enhance resources of the entity that will be used in satisfying (or in continuing to satisfy) performance obligations in the future; and (iii) the costs are expected to be recovered. The assessment of this criteria requires the application of judgement, in particular when considering if costs generate or enhance resources to be used to satisfy future performance obligations and whether costs are expected to be recoverable.

The Group regularly incurs costs to deliver its outsourcing services in a more efficient way (often referred to as 'transformation' costs). These costs may include process mapping and design, system development, project management, hardware (generally in scope of the Group's accounting policy for property, plant and equipment), software licence costs (generally in scope of the Group's accounting policy for intangible assets), recruitment costs and training.

Group's accounting policy for property, plant and equipment), software licence costs (generally in scope of the Group's accounting policy for intangible assets), recruitment costs and training.

Capitalisation of costs to obtain a contract

The incremental costs of obtaining a contract with a customer are recognised as an asset if the Group expects to recover them. The Group incurs costs such as bid costs, legal fees to draft a contract and sales commissions when it enters into a new contract.

Judgement is applied by the Group when determining what costs qualify to be capitalised in particular when considering whether these costs are incremental and whether these are expected to be recoverable. For example, the Group considers which type of sales commissions are incremental to the cost of obtaining specific contracts and the point in time when the costs will be capitalised.

The Group has determined that the following costs may be capitalised as contract assets: (i) legal fees to draft a contract (once the Group has been selected as a preferred supplier for a bid); and (ii) sales commissions that are directly related to winning a specific contract.

Costs incurred prior to selection as preferred supplier are not capitalised but are expensed as incurred.

Utilisation, derecognition and impairment of contract fulfilment assets and capitalised costs to obtain a contract

The Group utilises contract fulfilment assets and capitalised costs to obtain a contract to cost of sales over the expected contract period using a systematic basis that mirrors the pattern in which the Group transfers control of the service to the customer. The utilisation charge is included within cost of sales. Judgement is applied to determine this period, for example whether this expected period would be the contract term or a longer period such as the estimated life of the customer relationship for a particular contract if, say, renewals are expected.

A contract fulfilment asset or capitalised costs to obtain a contract is derecognised either when it is disposed of or when no further economic benefits are expected to flow from its use or disposal.

Management is required to determine the recoverability of contract related assets within property, plant and equipment, intangible assets as well as contract fulfilment assets, capitalised costs to obtain a contract, accrued income and trade receivables. At each reporting date, the Group determines whether or not the contract fulfilment assets and capitalised costs to obtain a contract are impaired by comparing the carrying amount of the asset to the remaining amount of consideration that the Group expects to receive less the costs that relate to providing services under the relevant contract. In determining the estimated amount of consideration, the Group uses the same principles as it does to determine the contract transaction price, except that any constraints used to reduce the transaction price will be removed for the impairment test.

Where the relevant contracts or specific performance obligations are demonstrating marginal profitability or other indicators of impairment, judgement is required in ascertaining whether or not the future economic benefits from these contracts are sufficient to recover these assets. In performing this impairment assessment, management is required to make an assessment of the costs to complete the contract. The ability to accurately forecast such costs involves estimates around cost savings to be achieved over time, anticipated profitability of the contract, as well as future performance against any contract-specific KPIs that could trigger variable consideration, or service credits. Where a contract is anticipated to make a loss, these judgements are also relevant in determining whether or not an onerous contract provision is required and how this is to be measured.

Deferred and accrued income

The Group's customer contracts include a diverse range of payment schedules dependent upon the nature and type of goods and services being provided. The Group often agrees payment schedules at the inception of long-term contracts under which it receives payments throughout the term of the contracts. These payment schedules may include performance-based payments or progress payments as well as regular monthly or quarterly payments for ongoing service delivery. Payments for transactional goods and services may be at delivery date, in arrears or part payment in advance.

Where payments made are greater than the revenue recognised at the period end date, the Group recognises a deferred income contract liability for this difference. Where payments made are less than the revenue recognised at the period end date, the Group recognises an accrued income contract asset for this difference.

Onerous contracts

The Group reviews its long-term contracts to ensure that the expected economic benefits to be received are in excess of the unavoidable costs of meeting the obligations under the contract. The unavoidable costs are the lower of the net costs of termination or the costs of fulfilment of the contractual obligations. The Group recognises the excess of the unavoidable costs over economic benefits due to be received as an onerous contract provision.

Property commercialisation

Part of the Group's strategy is to create and deliver maximum value from assets that are either owned by its customers or are acquired by the Group as part of a wider transaction. By combining the Group's capabilities with the expertise and assets of any organisation, the Group can significantly increase the value that can be generated from often under-utilised assets. Our strategy often involves the commercialisation of property assets, where the Group will invest in real estate improvements to maximise the future capital value or commercial letting potential. Such an investment approach can generate substantial benefits that can be realised up-front or over time. Examples of up-front value creation include entering into transactions when current market values offer opportunities to generate immediate shareholder returns, with opportunities for continued investment in the underlying asset. For example, the Group will acquire property with a view to resale and subsequently complete a sale and lease back transaction resulting in revenue and profit recorded in the year. The Group applies judgement over the categorisation of such transactions as operating or finance leases.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES CONTINUED

(f) Foreign currency translation

The functional and presentation currency of Capita plc and its UK subsidiaries is the pound sterling (£). Transactions in foreign currencies are initially recorded at the functional currency rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the balance sheet date. All differences are taken to the consolidated income statement with the exception of differences on foreign currency borrowings that provide a hedge against a net investment in a foreign operation. These are taken directly to equity until the disposal of the net investment, at which time they are recognised in the consolidated income statement.

Tax charges and credits attributable to exchange differences on those borrowings are also dealt with in equity. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate as at the date of initial transaction. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

The functional currencies of overseas operations include the euro, Indian rupee, South African rand, and the US dollar. As at the reporting date, the assets and liabilities of the overseas operations are retranslated into the presentation currency of Capita plc at the rate of exchange ruling at the balance sheet date and their income statements are translated at the weighted average exchange rate for the year.

The exchange differences arising on the re-translation are taken directly to a separate component of equity. On disposal of a foreign operation, the deferred cumulative amount recognised in equity relating to that particular foreign operation shall be recognised in the income statement.

The Group has elected not to record cumulative translation differences arising prior to the transition date as permitted by IFRS 1 as at 31 December 2004. In utilising this exemption, all cumulative translation differences were deemed to be zero as at 1 January 2004 and all subsequent disposals shall exclude any translation differences arising prior to the date of transition.

(g) Property, plant and equipment

Property, plant and equipment is stated at cost less accumulated depreciation and any impairment in value. Depreciation is calculated on a straight-line basis over the estimated useful life of the asset as follows:

Freehold buildings and long leasehold property	– over 50 years
Leasehold improvements	– period of the lease
Plant and equipment	– 3 to 10 years

The carrying values of property, plant and equipment are reviewed for impairment when events or changes in circumstances indicate the carrying value may not be recoverable. If any such indication exists and where the carrying values exceed the estimated recoverable amount, the assets are written down to their recoverable amount. The recoverable amount of property, plant and equipment is the greater of net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs. Impairment losses are recognised in the income statement in the administrative expenses line item.

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset (retired). Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the item) is included in the income statement in the year in which the item is derecognised.

(h) Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of an asset that necessarily takes a substantial period of time to get ready for its intended use or sale are capitalised as part of the cost of the respective assets. All other borrowing costs are expensed in the period they occur. Borrowing costs consist of interest and other costs that an entity incurs in connection with the borrowing of funds.

The Group capitalises borrowing costs for all qualifying assets where construction commenced on or after 1 January 2009.

(i) Business combinations and goodwill

Business combinations are accounted for by applying the acquisition method as at the acquisition date, which is the date on which control is passed to the Group.

Acquisitions on or after 1 January 2010

For acquisitions on or after 1 January 2010, the acquisition is measured as the aggregate of the fair value of the consideration transferred plus the recognised amount of any non-controlling interests in the acquiree. For each business combination on a transaction-by-transaction basis, the Group measures the non-controlling interests at the fair value of the acquiree's identifiable net assets at the date of acquisition.

Costs related to the acquisition, other than those associated with the issue of debt or securities, are expensed as incurred and included within administrative expenses and included within the 'non-underlying' column.

Any contingent consideration payable is recognised at fair value at the acquisition date. If the contingent consideration is classified as equity, it is not re-measured and settlement is accounted for within equity. Otherwise, subsequent changes to the fair value of the contingent consideration are recognised in the income statement.

For acquisitions where material changes were made to the fair value of the acquired assets and liabilities within the measurement period, the relevant account balances in the prior year are restated to reflect these changes in accordance with IFRS 3 requirements. Details of these changes are shown in note 17.

In a business combination achieved in stages, the Group re-measures its previously held equity interest in the acquiree at its acquisition-date fair value and recognises the resulting gain or loss, if any, in the income statement.

Goodwill is initially measured at cost being the excess of the aggregate of the fair value of the consideration transferred and the recognised amount of any non-controlling interests (plus the fair value of any existing equity interest) over the net recognised amount of the identifiable assets acquired and liabilities assumed. When the excess is negative, a bargain purchase gain is recognised immediately in the income statement.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES CONTINUED

Acquisitions between 1 January 2004 (IFRS transition date) and 1 January 2010

For acquisitions between the Group's IFRS transition date of 1 January 2004 and 1 January 2010, goodwill represents the excess of the cost of the acquisition over the Group's interest in the recognised amount of the identifiable assets, liabilities and contingent liabilities of the acquiree. When the excess was negative, a bargain purchase gain was recognised immediately in the income statement.

Transaction costs, other than those associated with the issue of debt or equity securities, that the Group incurred in connection with business combinations were capitalised as part of the cost of the acquisition.

Contingent consideration was recognised only where the Group had a present obligation and the economic outflow was more likely than not and a reliable estimate was determinable. Any subsequent adjustment to the contingent consideration was recognised as part of goodwill.

Acquisitions prior to 1 January 2004 (IFRS transition date)

On transition to the adoption of IFRS, the Group took advantage of the exemption allowed in IFRS 1 not to restate business combinations which took place prior to the date of transition. Goodwill recognised under UK GAAP prior to the date of transition to IFRS is stated at net book value as at this date (deemed cost). This goodwill had been amortised on a straight-line basis over its useful economic life (ranging from 5 to 20 years).

Goodwill

Following initial recognition, goodwill is stated at cost less any accumulated impairment losses. Goodwill is reviewed for impairment annually or more frequently if events or changes in circumstances indicate that the carrying value may be impaired. Goodwill arising on acquisitions prior to 31 December 1997 remains set-off directly against reserves and does not get recycled through the income statement.

As at the acquisition date, any goodwill acquired is allocated to each of the cash-generating units which are expected to benefit from the combination's synergies. Impairment is determined by assessing the recoverable amount of the cash-generating unit to which the goodwill relates. Where the recoverable amount of the cash-generating unit is less than the carrying amount, an impairment loss is recognised. Where goodwill forms part of a cash-generating unit and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation.

Goodwill disposed of in these circumstances is measured on the basis of the relative values of the operation disposed of and the portion of the cash-generating unit retained.

Acquisitions and disposals of non-controlling interests

Acquisitions and disposals of non-controlling interests that do not result in a change of control are accounted for as transactions with owners in their capacity as owners and therefore no goodwill is recognised as a result of such transactions. The adjustments to non-controlling interests are based on a proportionate amount of the net assets of the subsidiary. Any difference between the price paid or received and the amount by which non-controlling interests are adjusted is recognised directly in equity and attributed to the owners of the parent company.

Prior to the adoption of IAS 27 (Amended), goodwill was recognised on the acquisition of non-controlling interests in a subsidiary, which represented the excess of the cost of the additional investment over the carrying amount of the interest in the net assets acquired at the date of the transaction.

(j) Intangible assets

Intangible assets acquired separately are capitalised at cost and those identified in a business acquisition are capitalised at fair value as at the date of acquisition. In the case of capitalised software development costs, research expenditure is written off to the income statement in the period in which it is incurred. Development expenditure is written off in the same way unless and until the Group is satisfied as to the technical, commercial and financial viability of individual projects. Where this condition is satisfied, the development expenditure is capitalised and amortised over the period during which the Group is expected to benefit.

Following initial recognition, the carrying amount of an intangible asset is its cost less any accumulated amortisation and any accumulated impairment losses. The useful lives of intangible assets are assessed to be either finite or indefinite. There were no indefinite-lived assets in 2017 or 2016. Amortisation is charged on assets with finite lives and this expense is taken to the income statement through the administrative expenses line item.

Intangible assets with finite lives are only tested for impairment, either individually or at the cash-generating unit level, where there is an indicator of impairment.

Gains or losses arising from derecognition of an intangible asset are measured as the difference between the net disposal proceeds and the carrying amount of the asset and are recognised in the income statement when the asset is derecognised.

Intangible assets identified and recognised since transition to IFRS are profiled, on a straight-line basis, as follows:

Intangible assets acquired in business combinations:

- brands are amortised over their useful economic lives of between 5 and 10 years
- I.P., software and licences are amortised over their useful economic lives of between 5 and 20 years
- contracts and committed sales are amortised over their useful economic lives of between 1.5 and 15 years
- client lists and relationships are amortised over their useful economic lives of between 4 and 10 years.

Intangible assets purchased or internally capitalised:

- capitalised software development costs are amortised over their useful economic lives of between 5 and 15 years
- software and licences are amortised over their useful economic lives of between 5 and 20 years
- other intangibles are amortised over their useful economic lives of 3 to 15 years.

(k) Recoverable amount of non-current assets

At each reporting date, the Group assesses whether there is any indication that a non-current asset may be impaired. Where an indicator of impairment exists, the Group makes a formal estimate of the asset's recoverable amount. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. The recoverable amount is the higher of an asset's or cash-generating unit's fair value less costs to sell and its value in use and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES CONTINUED

(l) Investments and other financial assets

All investments are initially recorded at their fair value. Subsequently they are reviewed for impairment if events or changes in circumstances indicate the carrying value may not be recoverable.

Investment loans are measured at amortised cost using the effective interest method.

Available-for-sale financial assets are measured at their fair value with unrealised gains or losses being recognised directly in equity. When the investment is disposed of, the cumulative gain or loss previously recorded in equity is recognised in the income statement.

Financial assets at fair value through the income statement (disclosed in investment income) include financial assets designated upon initial recognition as at fair value through the income statement.

Financial assets may be designated upon initial recognition as at fair value through profit or loss if the assets are part of a group of financial assets which are managed and their performance evaluated on a fair value basis, in accordance with a documented risk management strategy.

(m) Trade and other receivables

Trade receivables are recognised and carried at original invoice amount less an allowance for any uncollectible amounts. An estimate for doubtful debts is made when collection of the full amount is no longer probable. Bad debts are written off when identified.

(n) Cash and cash equivalents

Cash and short-term deposits in the balance sheet comprise cash at bank and in hand and short-term deposits with an original maturity of 3 months or less. For the purpose of the consolidated cash flow statement, cash and cash equivalents consist of cash and cash equivalents as defined above, net of outstanding bank overdrafts.

(o) Interest-bearing loans and borrowings

All loans and borrowings are initially recognised at their fair value less any directly attributable transaction costs.

After initial recognition, loans and borrowings are subsequently measured at amortised cost using the effective interest method, except for instruments designated in fair value hedge relationships. Amortised cost is calculated by taking into account any issue costs, and any discount or premium on settlement.

Gains and losses are recognised in the income statement when the liabilities are derecognised, as well as through the amortisation process.

(p) Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Where the Group expects some or all of a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognised as a separate asset but only when recovery is virtually certain. The expense relating to any provision is presented in the income statement net of any reimbursement. If the effect of the time value of money is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognised as a borrowing cost. The Group provides, on a discounted basis, for the future rent expense and related cost of leasehold property (net of estimated sub-lease income) where the space is vacant or currently not planned to be used for ongoing operations.

(q) Pension schemes

The Group maintains a number of defined contribution pension schemes and for these schemes the Group has no further payment obligations once the contributions have been paid. The contributions are recognised as an employee benefit expense in the income statement as the related service is provided.

In addition, the Group operates a defined benefit pension scheme and participates in a number of other defined benefit pension schemes, all of which require contributions to be made to separate trustee-administered funds. The costs of providing benefits under these schemes are determined separately for each scheme using the projected unit credit method, which attributes entitlement to benefits to the current period (to determine current service cost) and to the current and prior periods (to determine the present value of the defined benefit obligation) and is based on actuarial advice. Past service costs are recognised immediately in the income statement.

When a settlement (eliminating all obligations for benefits already accrued) or a curtailment (reducing future obligations as a result of a material reduction in the scheme membership or a reduction in future entitlement) occurs, the obligation and related plan assets are remeasured using current actuarial assumptions and the resultant gain or loss recognised in the income statement during the period in which the settlement or curtailment occurs.

Re-measurements of the net defined benefit asset/liability, which comprise actuarial gains and losses, the return on plan assets (excluding interest) and the effect of the asset ceiling (if any, excluding interest), are recognised immediately in other comprehensive income and reflected immediately in retained earnings and will not be reclassified to the income statement. The Group determines the net interest expense/income on the net defined benefit asset/liability for the period by applying the discount rate used to measure the defined benefit obligation at the beginning of the annual period to the then net defined benefit asset/liability, taking into account any changes in the net defined benefit asset/liability during the period as a result of contributions and benefit payments.

Current and past service costs are charged to operating profit whilst the net interest cost is included within net finance costs.

In respect of 3 of the defined benefit pension schemes in which the Group participates, the Group accounts for its legal and constructive obligation over the period of its participation which is for a fixed period only.

The liability on the balance sheet in respect of the defined benefit pension schemes comprises the total for each scheme, or group of schemes, of the present value of the defined benefit obligation (using a discount rate based on high quality corporate bonds), less the fair value of plan assets out of which the obligations are to be settled directly. Fair value is based on market price information and in the case of quoted securities is the published bid price. The value of a net pension benefit asset is restricted to the present value of any amount the Group expects to recover by way of refunds from the plan or reductions in the future contributions.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES CONTINUED

(r) Financial instruments

The Group uses derivative financial instruments such as interest rate swaps and foreign currency contracts to hedge risks associated with interest and exchange rate fluctuations. Such derivative financial instruments are stated at fair value. The fair values of interest rate swaps and foreign currency contracts are determined by reference to market rates for similar instruments.

For the purpose of hedge accounting, hedges are classified as: fair value hedges when they hedge the exposure to changes in the fair value of a recognised asset or liability; cash flow hedges where they hedge exposure to variability in cash flows that is attributable to a particular risk associated with either a recognised asset or liability or a forecast transaction; and hedges of a net investment in a foreign operation.

In relation to fair value hedges (e.g. fixed to floating interest rate swaps held as fair value hedges against fixed interest rate borrowings) which meet the conditions for hedge accounting, any gain or loss from re-measuring the hedging instrument at fair value is recognised immediately in the income statement. Any gain or loss on the hedged item attributable to the hedged risk is adjusted against the carrying amount of the hedged item and recognised in the income statement.

In relation to cash flow hedges, the effective portion of the gain or loss on the hedging instrument is recognised directly in equity, while any ineffective portion is recognised immediately in the income statement. Amounts taken to equity are transferred to the income statement when the hedged transaction affects the income statement, such as when the hedged financial income or financial expense is recognised or when a forecast transaction occurs. Where the hedged item is the cost of a non-financial asset or non-financial liability, the amounts taken to equity are transferred to the initial carrying amount of the non-financial asset or liability.

If the forecast transaction or firm commitment is no longer expected to occur, amounts previously recognised in equity are transferred to the income statement. If the hedging instrument expires or is sold, terminated or exercised without replacement or rollover, or if its designation as a hedge is revoked, amounts previously recognised in equity remain in equity until the forecast transaction or firm commitment occurs.

Hedges of a net investment in a foreign operation, including a hedge of a monetary item that is accounted for as part of the net investment, are accounted for in a way similar to cash flow hedges. Gains or losses on the hedging instrument relating to the effective portion of the hedge are recognised in equity while any gains or losses relating to any ineffective portion are recognised in the income statement. On disposal of the foreign operation, the cumulative value of any such gains or losses recorded in equity is transferred to the income statement.

The Group uses loans and foreign exchange derivatives as hedges of its exposures to foreign exchange risks on its investments in foreign subsidiaries.

For derivatives that do not qualify for hedge accounting, any gains or losses arising from changes in fair value are taken directly to the income statement and are presented as non-underlying.

Put options on the shares of subsidiaries held by non-controlling interest shareholders that oblige the Group to purchase those shares for cash or another financial asset are recognised as a financial liability for the present value of the option exercise price. When the financial liability is recognised initially, that amount is reclassified from equity, and subsequently measured at fair value. Changes in the carrying amount are recognised in equity.

On exercise of the put options, the Group will treat the transaction as the purchase of the non-controlling interest and will apply acquisition accounting as described in (i) Business Combinations and Goodwill – Acquisitions and disposals of non-controlling interests.

(s) Leasing

The determination of whether an arrangement is, or contains, a lease is based on the substance of the arrangement at inception date and is concerned with whether the fulfilment of the arrangement is dependent upon the use of a specific asset or assets and the arrangement conveys a right to use the asset.

In assessing whether a lease is an operating lease or a finance lease, judgement needs to be exercised in determining whether or not substantially all the risks and rewards of ownership of the leased asset are held by the Group. Given that finance leases are recognised as liabilities, and operating leases are not, this can have a significant effect on the reported financial position of the Group.

Group as a lessee: Finance leases, which transfer to the Group substantially all the risks and benefits incidental to ownership of the leased item, are capitalised at the inception of the lease at the fair value of the leased property or, if lower, at the present value of the minimum lease payments. Lease payments are apportioned between the finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly against income. Capitalised leased assets are depreciated over the shorter of the estimated life of the asset or the lease term.

Leases where the lessor retains substantially all the risks and benefits of ownership of the asset are classified as operating leases. Operating lease payments are recognised as an expense in the income statement on a straight-line basis over the lease term.

Where a lease is for an asset sold by the Group to the lessor, the two transactions are accounted for separately. If the sale-and-leaseback results in a finance lease, then any gain on the sale is deferred and recognised as income over the lease term. If the leaseback is classified as an operating lease, then any gain is recognised immediately if the sale-and-leaseback terms are at fair value. If the sale-and-leaseback are not deemed to be at fair value then the accounting is as follows:

- if the selling price is at or below fair value, then the gain or loss is recognised immediately. However, if a loss is compensated for by future rentals at below-market price, then the loss is deferred and amortised over the period in which the asset is expected to be used;
- if the selling price exceeds fair value, then that excess is deferred and amortised over the period for which the asset is expected to be used; and
- if the fair value of the asset is less than the carrying amount of the asset at the date of the transaction, then that difference is recognised immediately as a loss on the sale.

As noted above the assessment of whether the sale-and-leaseback transactions are at fair value may require significant judgement in addition to that applied to determine whether the lease is an operating or finance lease, and the resulting accounting can have a significant effect on the reported results of the Group.

Group as a lessor: Leases where the Group does not transfer substantially all the risks and benefits of ownership of the asset are classified as operating leases. Rental income arising from operating leases is recognised in the income statement on a straight-line basis over the lease term.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES CONTINUED

(t) Income tax

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

Deferred income tax liabilities are recognised for all taxable temporary differences:

- except where the deferred tax liability arises from the initial recognition of goodwill;
- except where the deferred income tax liability arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, except where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred income tax assets are recognised for all deductible temporary differences, carry-forward of unused tax assets and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences and the carry-forward of unused tax assets and unused tax losses can be utilised, except where the deferred income tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.

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

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the balance sheet date.

Income tax relating to items recognised directly in equity is recognised in equity and not in the income statement.

(u) Share based payments

The Group operates a number of executive and employee share schemes.

The cost of equity-settled transactions with employees is measured by reference to the fair value at the date at which they are granted and is recognised as an expense over the vesting period, which ends on the date on which the relevant employees become fully entitled to the award. Fair value is determined using an option pricing model. In valuing equity-settled transactions, no account is taken of any vesting conditions, other than conditions linked to the price of the shares of the Company (market conditions).

No expense is recognised for awards that do not ultimately vest, except for awards where vesting is conditional upon a market condition, which are treated as vesting irrespective of whether or not the market condition is satisfied, provided that all other performance conditions are satisfied.

At each balance sheet date before vesting, the cumulative expense is calculated, representing the extent to which the vesting period has expired and management's best estimate of the achievement or otherwise of non-market conditions, the number of equity instruments that will ultimately vest or, in the case of an instrument subject to a market condition, be treated as vesting as described above. The movement in cumulative expense since the previous balance sheet date is recognised in the income statement, with a corresponding entry in equity.

Where the terms of an equity-settled award are modified or a new award is designated as replacing a cancelled or settled award, the cost based on the original award terms continues to be recognised over the original vesting period. In addition, an expense is recognised over the remainder of the new vesting period for the incremental fair value of any modification, based on the difference between the fair value of the original award and the fair value of the modified award, both as measured on the date of the modification. No reduction is recognised if this difference is negative.

Where an equity-settled award is cancelled, it is treated as if it had vested on the date of cancellation, and any cost not yet recognised in the income statement for the award is expensed immediately. Any compensation paid up to the fair value of the award at the cancellation or settlement date is deducted from equity, with any excess over the fair value being treated as an expense in the income statement.

(v) New standards and interpretations not applied

The IASB have issued the following standards, amendments and interpretations with an effective date after the date of these financial statements. These are effective for annual periods beginning on or after the date indicated:

	Effective date
International Accounting Standards (IAS/IFRSs) and Interpretations (IFRICs)	
Endorsed by the EU:	
IFRS 9 Financial Instruments	1 January 2018
IFRS 16 Leases	1 January 2019
Annual Improvements to IFRS Standards 2014 – 2016 Cycle	1 January 2017/18
IFRS 2 Amendments: Classification and Measurement of Share-based Payment Transactions	1 January 2018
Not yet endorsed by the EU:	
IFRS 17 Insurance Contracts	1 January 2021
IFRIC 22 Foreign Currency Transactions and Advance Consideration	1 January 2018
IFRIC 23 Uncertainty over Income Tax Treatments	1 January 2019
IAS 40 Amendments: Transfers of Investment Property	1 January 2018
IAS 28 Amendments: Long-term Interests in Associates and Joint Ventures	1 January 2019
IFRS 9 Amendments: Prepayment Features with Negative Compensation	1 January 2019
IFRS 10 and IAS 28 Amendments: Sale or Contribution of Assets between an Investor and its Associate or Joint Venture	Deferred indefinitely
Annual Improvements to IFRS Standards 2015 – 2017 Cycle	1 January 2019
IAS 19 Amendments: Plan Amendment, Curtailment or Settlement	1 January 2019

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES CONTINUED

IFRS 9 Financial Instruments

IFRS 9 Financial Instruments (IFRS 9) replaces IAS 39 Financial Instruments: Recognition and Measurement (IAS 39) and is effective for annual periods beginning on 1 January 2018. The Group has performed an assessment to understand the requirements of IFRS 9 and how these differ from IAS 39, and considered the application of these requirements to the Group. Detailed models have yet to be prepared, however based on the work to date no significant impact is anticipated from the adoption of the new standard.

IFRS 16 Leases

IFRS 16 Leases (IFRS 16) was issued in January 2016, replacing IAS 17 Leases (IAS 17), and other relevant current guidance. IFRS 16 sets out the principles for the recognition, measurement, presentation and disclosure of leases. IFRS 16 will be effective for annual periods beginning on or after 1 January 2019 with early adoption permitted for entities that apply IFRS 15.

The main impact for the Group is that IFRS 16 introduces a single lessee accounting model and requires the recognition of assets and liabilities for all leases, unless the lease term is 12 months or less or the underlying asset is of low value.

The Group is in the advanced stages of the assessment of the new standard and expects its implementation to have a significant impact on the Group financial statements. As at 31 December 2017, the Group held a significant number of operating leases for which the future minimum lease payments amounted to £833.0m as disclosed in note 26.

The main impact on the Group financial statements will be:

- Financial liabilities and non-current assets will increase on implementation of the standard as obligations to make future payments under leases currently classified as operating leases will be recognised on the balance sheet, along with the related 'right-of-use' asset.
- On adoption, the 'right-of-use' asset will not exceed its recoverable amount. The Group will also annually review the 'right-of-use' assets for impairment.
- There will be a reduction in operating costs and an increase in net finance costs as operating lease costs are replaced with depreciation and lease interest expense. This will result in an increase to the Group's EBITDA, increase in EBIT as a result of higher interest costs, with an overall net increase to profit.
- The noted adjustments will be reflected in retained earnings on adoption date.

The total cash outflow for lease payments would not change but certain lease payments would be presented as cash flow from financing activities, as opposed to the current treatment as cash flow from operating activities, resulting in an improvement in cash outflow from operating activities and an increase in cash outflow for financing activities.

A number of leases in place at 31 December 2017 will end or not be renewed and new leases may be entered into. Further, our estimate requires several judgements, including determining the lease term, the lease payments (which may be variable) and the discount rate applicable to each lease. Determining the lease term can be complex where leases include rights of renewal or cancellation. The Group also has a number of lease arrangements where lease payments may not be fixed and may vary depending on an index or sales. These judgements will continue to be assessed until adoption. The Group is continuing to assess the precise impact of this new standard including considering the impact of applying relevant available transition expedients, and whether to early adopt.

3 UNDERLYING OPERATING PROFIT

	2017			Restated 2016		
	Underlying before significant new contracts and restructuring £m	Significant new contracts and restructuring £m	Total underlying £m	Underlying before significant new contracts and restructuring £m	Significant new contracts and restructuring £m	Total underlying £m
Continuing operations:						
Revenue	4,167.9	–	4,167.9	4,357.3	–	4,357.3
Cost of sales	(3,121.8)	–	(3,121.8)	(3,418.5)	–	(3,418.5)
Gross profit	1,046.1	–	1,046.1	938.8	–	938.8
Administrative expenses	(580.8)	(17.9)	(598.7)	(547.0)	(57.2)	(604.2)
Operating profit	465.3	(17.9)	447.4	391.8	(57.2)	334.6
Net finance costs	(64.4)	–	(64.4)	(66.1)	–	(66.1)
Profit before tax	400.9	(17.9)	383.0	325.7	(57.2)	268.5

Following the adoption of IFRS 15, the Board has adopted a policy to separately disclose the operating profit/loss from significant new contract wins in-period and restructuring, in order for users of the financial statements to obtain a proper understanding of the financial information and the performance of the business.

A new contract is assessed as that which is significant and either entirely new to the Group, or a significant amendment to the scope and scale of an existing contract. Neither of these have occurred in 2017 or 2016.

In 2016, the Board announced a major programme, with the restructuring of the Group into new reporting divisions under a Group-wide programme, the cost of which was £57.2m. In 2017, a further charge of £17.9m was recognised in relation to restructuring including costs incurred relating to professional fees associated with the broadened transformation plan initiated by the new Chief Executive Officer, which will benefit the Group over the long term.

Contract terminations arising in the normal course of business and which result in the disposal of a contract fulfilment asset and/or a true-up of revenue recognised, will be included within 'Underlying before significant new contracts and restructuring', and separately disclosed if considered material.

In 2017, we concluded discussions with the Ministry of Defence in relation to the the Defence Infrastructure Organisation (DIO) contract, which is expected to end in 2019. The 2017 results include a £22.0m benefit from the re-shaping of the DIO contract which will not recur in 2018.

In preparing these financial statements, the Group undertook a comprehensive review of its major contracts to identify indicators of impairment of contract fulfilment assets. Following this review, management has taken the decision to impair costs capitalised as contract fulfilment assets of £14.1m (2016: £nil) within underlying cost of sales. The review also resulted in the derecognition of £4.4m (2016: £17.0m) of contract fulfilment assets as no further economic benefits are expected to flow from the Group's use of the assets. These amounts are recognised in underlying before significant new contracts and restructuring. Refer to note 18 for further details of the review.

The IT Services division benefited from a one-off supplier settlement of £9.2m (2016: £nil).

Customer contracts sometimes contain provisions to compensate the Group for exit costs and future profits in the event of early termination. In-year customer contract terminations for customer convenience have led to associated exit fees paid to Capita of £6.4m (2016: £21.7m) being recorded as income. These are included in 'underlying before significant new contracts and restructuring' because these amounts are payable to the Group under the terms of the respective contracts being terminated.

4 BUSINESS EXIT

2017 business exit

Business exits are businesses that have been exited during the year or in the process of being disposed of.

Except for the disposal of Capita Asset Services (disclosed separately in note 5 'Discontinued Operations'), none of the Group's business exits meet the definition of 'discontinued operations' as stipulated by IFRS 5, which requires disclosure and comparatives to be restated where the relative size of a disposal or business closure is significant, which is normally understood to mean a reported segment. Accordingly, the separate presentation described below does not fall within the requirements of IFRS 5 concerning discontinued operations.

In the 2016 Annual Report, we disclosed that the Group intended to dispose of the majority of its specialist recruitment business which no longer fit the Group's business strategy. At 31 December 2016, this business did not meet the criteria to be treated as held for sale.

During the year, the disposal of the specialist recruitment business has completed along with the closure of a number of small businesses, and their results are all included within business exits for the period. As at 31 December 2017, the Group was in an active process to sell a non-core property business and has treated this as a disposal group held for sale at this date.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

4 BUSINESS EXIT CONTINUED

		Non-trading disposal			
Income statement impact	Trading £m	Cash £m	Non-cash £m	Total £m	Total £m
Revenue	66.7	–	–	–	66.7
Cost of sales	(54.7)	–	–	–	(54.7)
Gross profit	12.0	–	–	–	12.0
Administrative expenses	(13.0)	(4.7)	(9.0)	(13.7)	(26.7)
Operating loss	(1.0)	(4.7)	(9.0)	(13.7)	(14.7)
Net finance costs	(0.1)	–	–	–	(0.1)
Loss on business disposal	–	16.3	(46.9)	(30.6)	(30.6)
(Loss)/profit before tax	(1.1)	11.6	(55.9)	(44.3)	(45.4)
Taxation	–	–	–	–	–
(Loss)/profit after tax	(1.1)	11.6	(55.9)	(44.3)	(45.4)

Trading revenue and costs represent the current year trading performance of those businesses being exited or disposed.

Non-trading disposal and closure costs include the costs of exiting businesses and stranded costs such as property lease and redundancy payments.

The loss on disposal of £(30.6)m arises from the disposal of net assets of £47.0m for £17.0m cash consideration and costs of disposal of £(0.6)m.

Non-trading administrative expenses comprise £(4.7)m of disposal and closure costs and £(9.0)m of accelerated depreciation, amortisation and impairments.

Balance sheet – disposal group

As at 31 December 2017, the Group was in an active process to sell a non-core property business and has treated this as a disposal group held for sale at this date.

	2017 £m
Intangibles	1.5
Trade and other receivables	4.4
Assets held for sale	5.9
Trade and other payables	(1.4)
Liabilities held for sale	(1.4)

Non-underlying cash movements in payables and receivables

Businesses disposed of and held for sale during 2017 generated operating cash inflows, prior to disposal, of £2.5m.

2016 Business exit

In the prior year, the Group disposed of a specialist insurance and health business and exited certain small health businesses. The disposal process of a justice business ceased, and the business was moved out from being a disposal group held for sale back into underlying reported numbers.

		Non-trading disposal			
Income statement impact	Trading £m	Cash £m	Non-cash £m	Total £m	Total £m
Revenue	11.3	–	–	–	11.3
Cost of sales	(6.7)	–	–	–	(6.7)
Gross profit	4.6	–	–	–	4.6
Administrative expenses	(4.5)	2.9	(0.2)	2.7	(1.8)
Operating profit	0.1	2.9	(0.2)	2.7	2.8
Profit on business disposal	–	0.1	–	0.1	0.1
Profit before tax	0.1	3.0	(0.2)	2.8	2.9
Taxation	–	0.5	–	0.5	0.5
Profit after tax	0.1	3.5	(0.2)	3.3	3.4

Trading revenue and costs represent the current year trading performance of those businesses disposed.

Non-trading disposal and closure costs include the costs of exiting businesses and stranded costs such as property lease and redundancy payments.

During the year, the disposal process of the justice business ceased, and the business was moved out from being a disposal group held for sale back into underlying reported numbers. An onerous contract provision relating to that business, being £6.9m, was transferred into underlying and recognised within the administrative expenses relating to business exits, which will unwind over one to two years.

The gain on disposal of £0.1m arises from the disposal of net assets of £54.5m for £30.6m cash consideration, £20.0m of loan notes and £4.0m of residual non-controlling interest.

Non-underlying cash movements in payables and receivables

Businesses disposed of and held for sale during 2016 generated operating cash outflows, prior to disposal, of £(12.3)m.

5 DISCONTINUED OPERATIONS

In the 2016 Annual Report, we disclosed that the Group intended to dispose of the Capita Asset Services businesses. At 31 December 2016, this business did not meet the criteria to be treated as held for sale as the sale process had not progressed sufficiently to be reasonably certain at that time. The disposal completed in the year.

The disposal meets the definition of a discontinued operation as stipulated by IFRS 5. The comparatives have been restated. The following presentation, and that included in other notes, follows the requirements of IFRS 5.

	2017					2016				
Discontinued operations:	Trading £m	Non-trading £m	Total £m	Specific items £m	Total £m	Trading £m	Non-trading £m	Total £m	Specific items £m	Total £m
Revenue	261.9	–	261.9	–	261.9	316.3	–	316.3	–	316.3
Cost of sales	(94.0)	–	(94.0)	–	(94.0)	(111.8)	–	(111.8)	–	(111.8)
Gross profit	167.9	–	167.9	–	167.9	204.5	–	204.5	–	204.5
Administrative expenses	(120.3)	–	(120.3)	(66.2)	(186.5)	(144.5)	–	(144.5)	(17.7)	(162.2)
Operating (loss)/profit	47.6	–	47.6	(66.2)	(18.6)	60.0	–	60.0	(17.7)	42.3
Net finance costs	0.1	–	0.1	0.8	0.9	0.1	–	0.1	0.1	0.2
Profit on disposal	–	445.4	445.4	–	445.4	–	–	–	–	–
Profit before tax	47.7	445.4	493.1	(65.4)	427.7	60.1	–	60.1	(17.6)	42.5
Income tax expense	(10.6)	–	(10.6)	(0.7)	(11.3)	(9.5)	–	(9.5)	3.9	(5.6)
Profit for the period	37.1	445.4	482.5	(66.1)	416.4	50.6	–	50.6	(13.7)	36.9

Specific item administrative expenses are analysed in note 6. Specific item net finance costs includes fair value movements on available-for-sale assets.

The earnings per share impact from discontinued operations is 62.56p (2016: 5.55p) on basic earnings per share and 62.56p (2016: 5.55p) on diluted earnings per share.

Profit on business disposal	Cash £m	Non-cash £m	Total £m
Property, plant and equipment	–	73.0	73.0
Intangible assets	–	250.2	250.2
Trade and other receivables	–	74.6	74.6
Financial assets	–	3.3	3.3
Cash	45.8	–	45.8
Trade and other payables	–	(40.0)	(40.0)
Income tax payable	–	(2.7)	(2.7)
Financial liabilities	–	(0.2)	(0.2)
Deferred tax	–	(5.0)	(5.0)
Provisions	–	(3.2)	(3.2)
Total net assets disposed of	45.8	350.0	395.8
Cash consideration received	909.5	–	909.5
Recycled gains in foreign currency translation reserve	–	7.6	7.6
Recycled losses on hedges of a net investment in foreign operations	–	(17.0)	(17.0)
Costs of disposal	(58.9)	–	(58.9)
Proceeds, less costs, on disposal	850.6	(9.4)	841.2
Profit on business disposal	804.8	(359.4)	445.4

Costs of disposal include IT related separation costs, advisers fees and stranded costs such as property lease payments.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

6 SPECIFIC ITEMS

Included within the specific items column are:

		2017				Restated 2016			
	Notes	Cash in-year £m	Cash in future £m	Non-cash £m	Total £m	Cash in-year £m	Cash in future £m	Non-cash £m	Total £m
Cost of sales – continuing:									
Co-op contract dispute		–	–	–	–	–	–	42.3	42.3
Impairment of life and pension assets		–	–	5.5	5.5	–	–	–	–
Total cost of sales – continuing		–	–	5.5	5.5	–	–	42.3	42.3
Administrative expenses – continuing:									
Amortisation of acquired intangibles	15	–	–	124.3	124.3	–	–	147.9	147.9
Impairment of acquired intangibles	15	–	–	14.0	14.0	–	–	14.7	14.7
Impairment of loan and investment		–	–	9.0	9.0	–	–	2.6	2.6
Impairment of contract related assets	14/15	–	–	–	–	–	–	58.3	58.3
Impairment of other non-current assets	14/15	–	–	63.5	63.5	–	–	–	–
Impairment of goodwill	16	–	–	551.6	551.6	–	–	66.6	66.6
Co-op contract dispute		–	–	–	–	1.8	4.9	4.2	10.9
Impairment of life and pension assets	14/15	–	–	55.7	55.7	–	–	–	–
Claims and litigation provisions	27	–	30.0	–	30.0	–	–	–	–
Contingent consideration movements	28	–	–	(2.5)	(2.5)	–	–	1.2	1.2
Professional fees on acquisitions	17	1.0	0.5	–	1.5	6.4	2.0	–	8.4
Stamp duty paid on acquisitions	17	0.2	–	–	0.2	0.6	–	–	0.6
Total administrative expenses – continuing		1.2	30.5	815.6	847.3	8.8	6.9	295.5	311.2
Operating loss – continuing		1.2	30.5	821.1	852.8	8.8	6.9	337.8	353.5
Net finance costs – continuing					(2.1)				7.7
Income tax credit – continuing					(54.0)				(47.1)
Loss for the year – continuing					796.7				314.1
Administrative expenses – discontinued:									
Amortisation of acquired intangibles	15	–	–	0.6	0.6	–	–	4.3	4.3
Capita Asset Services indemnity and settlement provision	27	(0.7)	69.1	(2.8)	65.6	0.9	12.5	–	13.4
Total administrative expenses – discontinued		(0.7)	69.1	(2.2)	66.2	0.9	12.5	4.3	17.7
Operating loss – discontinued	5	(0.7)	69.1	(2.2)	66.2	0.9	12.5	4.3	17.7
Net finance costs – discontinued					(0.8)				(0.1)
Income tax expense/(credit) – discontinued					0.7				(3.9)
Loss for the year – discontinued					66.1				13.7
Total loss for the year					862.8				327.8

The above items are presented as specific non-underlying items as the Board have concluded that it is appropriate to do so. These amounts are (or have been) material, and require separate disclosure in order for the users of the financial statements to obtain a proper understanding of the financial information and the underlying performance of the business. The tax impact of the above items is a £53.3m credit. These items are discussed below:

6 SPECIFIC ITEMS CONTINUED

Continuing:

The Co-operative Bank contract dispute: the impact of the dispute with The Co-operative Bank on the prior year financial statements was a charge of £53.2m representing the write-off of contract fulfilment assets relating to the transformation plan of £42.3m to cost of sales; and software licence costs of £4.2m (included within other intangibles, see note 15), other costs of £5.8m and a provision for 2017 legal costs of £0.9m to administrative expenses. This was included within specific items because it was one-off in nature and was due to a contractual dispute rather than service credit penalties.

Impairment of life and pensions assets: The Group's life and pension business has developed a platform to support an existing life and pensions contract, but which could provide services to multiple clients in the future. The Group's transformation plan has identified there is no longer a market for this platform and accordingly the carrying value of this and associated assets has been written off. The impact on the financial statements is a non-underlying charge of £61.2m (£54.7m property, plant and equipment – see note 14; £1.0m capitalised software intangible assets – see note 15; £5.5m contract fulfilment asset – see note 18) representing the write-off of the non-current assets. The charge has been included within non-underlying as the assets have no further value to the Group.

Amortisation and impairment of acquired intangible assets: the Group carries on its balance sheet significant balances related to acquired intangible assets. The amortisation of these assets, and any impairment charges, are reported separately as they distort the in-year trading results, and performance of the acquired businesses is assessed through the underlying operational results.

Impairment of loan and investment: the Group has fully impaired a historic loan and investment in the year. The charge is reported separately due to its nature and to be consistent to prior years.

Impairment of contract related assets: as part of its year-end close process in 2016, Capita undertook a comprehensive review across its major contracts. Following this review management took the decision to impair, at 31 December 2016, a number of historical assets relating to a few specific contracts, which were being amortised over their contract life. Non-current assets amounting to £58.3m (£16.5m property, plant and equipment – see note 14; £41.8m capitalised software development intangible assets – see note 15) were written off as a non-underlying charge as the assets have no further value to the Group.

Impairment and disposals of other non-current assets: as part of its year-end close process in 2017, Capita has undertaken a comprehensive review of its tangible and intangible assets. Following the review, management has taken a decision to impair, at 31 December 2017, a number of assets relating to specific programmes resulting from changes in client and Capita strategy in the second half of 2017. These impairments will have no adverse impact on future cash or trading. Non-current assets amounting to £63.5m (£35.2m property, plant and equipment – see note 14; £28.3m capitalised software intangible assets – see note 15) have been written off as a non-underlying charge as the assets have no further value to the Group.

Impairment of goodwill: the Group carries on its balance sheet significant balances related to acquired goodwill. Goodwill is subject to annual impairment testing, and any impairment charges are reported separately as they distort the in-year trading results and IFRS does not permit the recognition of enhanced value of acquisitions, potentially leading to an unbalanced picture being shown over time. Refer to note 16 for further detail on the impairments.

Claims and litigation provisions: these significant litigation costs provided in the year, relate to two claims in respect of:

1. a contract within the Group's Real Estate and Infrastructure business and was notified to the Group during 2017. The related contract began in 2007; and
2. a contract within the Group's Employee Benefits business where more information on the progress of the claim has become apparent. The related contract was delivered from 2009.

The amount provided in respect of these two claims has been recognised in non-underlying specific items due to their age and significance.

Contingent consideration movements: in accordance with IFRS 3, movements in the fair value of contingent consideration on acquisitions go through the Group income statement. These are reported separately because performance of the acquired businesses is assessed through the underlying operational results and such a charge/credit movement would distort underlying results.

Acquisition-related costs and stamp duty: these costs incurred with acquisitions are not included in the assessment of business performance which is based on the underlying results. IFRS requires certain costs incurred in connection with acquired businesses to be recorded within the Group income statement. These charges are not included in the internal assessment of business performance which as above is based on the underlying operational results. These charges are therefore separately disclosed as specific items.

Discontinued:

Amortisation of intangible assets: the Group carries on its balance sheet significant balances related to acquired intangible assets. The amortisation of these assets, are reported separately as they distort the in-year trading results and performance of the acquired businesses is assessed through the underlying operational results. The discontinued element of the amortisation of intangible assets charge relates to the Capita Asset Services businesses disposed of in the year.

Capita Asset Services indemnity and settlement provision: these significant litigation costs are historical in nature, being tied to previous acquisitions, comprising mainly £69.1m of provisions for future costs (see note 27), and are included in specific items due to their size and nature. The discontinued element relates to the Capita Asset Services businesses disposed of in the year. The prior year charge was £13.4m.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

7 SEGMENTAL INFORMATION

The Group's operations are managed separately according to the nature of the services provided, with each segment representing a strategic business division offering a different package of client outcomes across the markets the Group serves. A description of the service provision for each segment can be found in the strategic report on pages 25 to 35.

As announced at the 2016 year-end, the Group from 1 January 2017 introduced a new structure after the disposal of the Capita Asset Services businesses. This is now reflected in the segment reporting and the comparatives have been restated on this same basis. No segments are aggregated to form the operating segments below, and the information presents the information as it is reported to the Group Board. In preparing these financial statements, the Board has considered how business performance is assessed internally and in addition to the announced new business divisions, Group trading and central functions will also be reported separately going forward. Comparative information has been restated accordingly. The Board believe the changes improve accountability and transparency across the Group. Specific items are not allocated to reportable segments in the below analysis which is in line with that reported to the Group Board.

Before eliminating sales between business units on consolidation, the Group accounts for sales between business units as if they were to a third party at market rates.

The tables below present revenue, trading result and certain asset and liability information for the Group's business segments for the years 2017 and 2016. All operational divisions are continuing except for the Capita Asset Services businesses which were disposed of in the year and is disclosed as discontinued in both 2017 and 2016. The 2016 consolidated income statement has not been restated for the impact of business exits and other non-underlying items (except for the Capita Asset Services businesses). If the 2016 underlying consolidated income statement was restated for businesses exited or held for sale in 2017, revenue would be decreased by £173.9m and profit before tax would be reduced by £5.8m.

Year ended 31 December 2017

	Private Sector Partnerships £m	Public Services Partnerships £m	Professional Services £m	Digital and Software Solutions £m	IT Services £m	Group trading and central functions £m	Total underlying £m	Business Exit £m	Specific Items £m	Total £m
Continuing operations										
Long-term contractual	1,214.0	774.1	225.1	370.9	323.3	22.6	2,930.0	–		2,930.0
Short-term contractual	306.3	165.4	90.7	32.6	63.6	9.1	667.7	10.8		678.5
Transactional (point in time)	68.0	147.7	217.0	7.4	120.9	9.2	570.2	55.9		626.1
Total segment revenue	1,588.3	1,087.2	532.8	410.9	507.8	40.9	4,167.9	66.7		4,234.6
Trading revenue	1,730.3	1,161.5	667.9	451.2	770.2	97.4	4,878.5			4,878.5
Inter-segment revenue	(142.0)	(74.3)	(135.1)	(40.3)	(262.4)	(56.5)	(710.6)			(710.6)
Total underlying segment revenue	1,588.3	1,087.2	532.8	410.9	507.8	40.9	4,167.9			4,167.9
Non-underlying revenue	1.5	10.1	55.1	–	–	–		66.7		66.7
Total segment revenue	1,589.8	1,097.3	587.9	410.9	507.8	40.9				4,234.6
Underlying operating profit before significant contracts and restructuring	131.4	79.0	105.7	116.1	79.5	(46.4)	465.3			465.3
Significant costs and restructuring	6.1	(6.0)	(0.8)	(2.2)	(1.4)	(13.6)	(17.9)			(17.9)
Underlying operating profit	137.5	73.0	104.9	113.9	78.1	(60.0)	447.4			447.4
Business exits	0.7	–	(1.7)	–	–	–		(1.0)		(1.0)
Total trading result	138.2	73.0	103.2	113.9	78.1	(60.0)				446.4
Non-trading items:										
Business exits – non-trading								(13.7)		(13.7)
Specific Items – see note 6									(852.8)	(852.8)
Operating profit/(loss)							447.4	(14.7)	(852.8)	(420.1)
Net finance costs							(64.4)	(0.1)	2.1	(62.4)
Loss on business disposal							–	(30.6)	–	(30.6)
Profit/(loss) before tax							383.0	(45.4)	(850.7)	(513.1)
Income tax (expense)/credit							(68.0)	–	54.0	(14.0)
Profit/(loss) for the year – continuing operations							315.0	(45.4)	(796.7)	(527.1)
Profit/(loss) for the year – discontinued operations							–	482.5	(66.1)	416.4
Profit/(loss) for the year – total							315.0	437.1	(862.8)	(110.7)

7 SEGMENTAL INFORMATION CONTINUED

Year ended 31 December 2016 – Restated

	Private Sector Partnerships £m	Public Services Partnerships £m	Professional Services £m	Digital and Software Solutions £m	IT Services £m	Group trading and central functions £m	Total underlying £m	Business Exit £m	Specific Items £m	Total £m
Continuing operations										
Long-term contractual	1,199.3	791.8	226.9	380.5	298.6	24.6	2,921.7	–		2,921.7
Short-term contractual	274.4	216.4	82.1	32.3	82.2	–	687.4	–		687.4
Transactional (point in time)	70.7	119.7	449.3	7.5	100.7	0.3	748.2	11.3		759.5
Total segment revenue	1,544.4	1,127.9	758.3	420.3	481.5	24.9	4,357.3	11.3	–	4,368.6
Trading revenue	1,656.5	1,192.8	895.8	451.8	792.1	68.8	5,057.8			5,057.8
Inter-segment revenue	(112.1)	(64.9)	(137.5)	(31.5)	(310.6)	(43.9)	(700.5)			(700.5)
Total underlying segment revenue	1,544.4	1,127.9	758.3	420.3	481.5	24.9	4,357.3			4,357.3
Non-underlying revenue	8.9	0.9	–	1.5	–	–		11.3		11.3
Total segment revenue	1,553.3	1,128.8	758.3	421.8	481.5	24.9				4,368.6
Underlying operating profit *before significant contracts* and restructuring	104.6	6.5	111.8	136.4	57.2	(24.7)	391.8			391.8
Significant costs and restructuring	(33.2)	(6.0)	(3.5)	(2.0)	(10.1)	(2.4)	(57.2)			(57.2)
Underlying operating profit	71.4	0.5	108.3	134.4	47.1	(27.1)	334.6			334.6
Business exits	–	–	0.1	–	–	–		0.1		0.1
Total trading result	71.4	0.5	108.4	134.4	47.1	(27.1)				334.7
Non-trading items:										
Business exits – non-trading								2.7		2.7
Specific items – see note 6									(353.5)	(353.5)
Operating profit/loss							334.6	2.8	(353.5)	(16.1)
Net finance costs							(66.1)	–	(7.7)	(73.8)
Gain on business disposal							–	0.1	–	0.1
Profit/(loss) before tax							268.5	2.9	(361.2)	(89.8)
Income tax (expense)/credit							(46.4)	0.5	47.1	1.2
Profit/(loss) for the year – continuing operations							222.1	3.4	(314.1)	(88.6)
Profit/(loss) for the year – discontinued operations							–	50.6	(13.7)	36.9
Profit/(loss) for the year – total							222.1	54.0	(327.8)	(51.7)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

7 SEGMENTAL INFORMATION CONTINUED

The tables below show the order book for each division, categorised into long-term contractual (contracts with length greater than 2 years) and short-term contractual (contracts with length less than 2 years). The length of the contract is calculated from the start of the service commencement date. The figures represent the aggregate amount of currently contracted transaction price allocated to the performance obligations that are unsatisfied or partially unsatisfied. Revenue expected to be recognised upon satisfaction of these performance obligations as of 31 December 2017 is as follows:

Order book	Private Sector Partnerships £m	Public Services Partnerships £m	Professional Services £m	Digital and Software Solutions £m	IT Services £m	Group trading and central functions £m	Total £m
Long-term contractual	4,002.0	2,670.2	328.2	550.4	494.3	6.4	8,051.5
Short-term contractual	–	94.7	22.1	–	20.0	2.7	139.5
Total	4,002.0	2,764.9	350.3	550.4	514.3	9.1	8,191.0

The table below shows the time bands of the expected timing of revenue to be recognised on long-term contractual as of 31 December 2017:

Time bands of long-term contractual in order book	Private Sector Partnerships £m	Public Services Partnerships £m	Professional Services £m	Digital and Software Solutions £m	IT Services £m	Group trading and central functions £m	Total £m
< 1 year	952.8	523.1	83.5	269.7	166.1	5.1	2,000.3
1-5 years	2,480.3	1,491.0	244.7	268.6	240.8	1.3	4,726.7
> 5 years	568.9	656.1	–	12.1	87.4	–	1,324.5
Total	4,002.0	2,670.2	328.2	550.4	494.3	6.4	8,051.5

The order book represents the consideration to which the Group will be entitled to receive from the customers when the Group satisfies the remaining performance obligations in the contracts. However, the total revenue that will be earned by the Group will also include volumetric revenue, new wins, scope changes and anticipated contract extensions. These elements have been excluded from the figures in the tables above as they are not contracted. In addition, revenue from contract extensions is also excluded in the order book unless they are pre-priced extensions whereby the Group has a legal binding obligation to deliver the performance obligations during the extension period. The total revenue related to pre-priced extensions that has been included in the tables above amounted to £502.0m. The amounts presented do not include orders for which neither party has performed and each party has the unilateral right to terminate a wholly unperformed contract without compensating the other party.

Of the £8.1bn revenue to be earned on long-term contractual, £4.9bn relates to material contracts to the Group. This amount excludes revenue that will be derived from frameworks (transactional (point in time) contracts) and non-contracted volumetric revenue from these material contracts, which together are expected to contribute an additional £1.8bn of revenue to the Group over the life of these contracts.

7 SEGMENTAL INFORMATION CONTINUED

Other segment information

31 December 2017	Private Sector Partnerships £m	Public Services Partnerships £m	Professional Services £m	Digital and Software Solution £m	IT Services £m	Group trading and central functions £m	Total £m
Property, plant and equipment	97.3	14.1	28.3	6.7	21.8	51.1	219.3
Intangible assets acquired in business combinations	286.4	218.8	389.2	337.6	410.9	2.3	1,645.2
Intangible assets capitalised/purchased	9.6	42.1	8.0	53.6	4.8	48.8	166.9
Contract fulfilment assets	118.7	35.8	5.6	72.8	19.6	–	252.5
Trade and other receivables	261.4	158.3	93.1	66.1	197.7	27.2	803.8
Financial assets						221.0	221.0
Deferred taxation						159.3	159.3
Disposal group assets held for sale						5.9	5.9
Cash						921.7	921.7
Income tax receivable						25.6	25.6
Total assets	773.4	469.1	524.2	536.8	654.8	1,462.9	4,421.2
Deferred income	677.7	355.5	96.2	250.4	129.5	5.9	1,515.2
Trade and other payables	83.4	68.6	36.0	18.2	39.9	526.1	772.2
Overdrafts						443.3	443.3
Financial liabilities						1,987.3	1,987.3
Deferred taxation						12.2	12.2
Disposal group liabilities held for sale						1.4	1.4
Provisions						212.6	212.6
Employee benefits						406.8	406.8
Total liabilities	761.1	424.1	132.2	268.6	169.4	3,595.6	5,351.0
Total net assets/(liabilities)	12.3	45.0	392.0	268.2	485.4	(2,132.7)	(929.8)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

7 SEGMENTAL INFORMATION CONTINUED

Other segment information

31 December 2016	Private Sector Partnerships £m	Public Services Partnerships £m	Professional Services £m	Digital and Software Solution £m	IT Services £m	Discontinued operations £m	Group trading and central functions £m	Total £m
Property, plant and equipment	163.3	28.1	29.9	8.0	39.8	76.3	49.3	394.7
Intangible assets acquired in business combinations	715.1	243.9	444.7	481.9	449.0	237.7	17.3	2,589.6
Intangible assets capitalised/purchased	17.4	81.1	11.6	44.6	9.3	–	0.6	164.6
Contract fulfilment assets	124.0	24.5	7.0	65.8	19.3	–	–	240.6
Trade and other receivables	238.7	152.5	125.2	31.4	167.3	119.4	57.0	891.5
Financial assets							430.2	430.2
Deferred taxation							222.4	222.4
Funds assets							173.6	173.6
Cash							1,098.3	1,098.3
Total assets	1,258.5	530.1	618.4	631.7	684.7	433.4	2,048.7	6,205.5
Deferred income	756.1	356.6	104.7	226.0	135.8	–	12.4	1,591.6
Trade and other payables	104.2	111.4	49.6	19.7	38.0	113.3	561.8	998.0
Overdrafts							532.5	532.5
Financial liabilities							2,918.6	2,918.6
Funds liabilities							173.6	173.6
Provisions							160.7	160.7
Deferred taxation							19.6	19.6
Income tax payable							18.6	18.6
Employee benefits							345.2	345.2
Total liabilities	860.3	468.0	154.3	245.7	173.8	113.3	4,743.0	6,758.4
Total net assets/(liabilities)	398.2	62.1	464.1	386.0	510.9	320.1	(2,694.3)	(552.9)

The table below presents revenue by geographical location, and carrying amount of non-current assets by location of those assets.

	2017			Restated 2016		
	United Kingdom £m	Non-United Kingdom £m	Total £m	United Kingdom £m	Non-United Kingdom £m	Total £m
Revenue	3,902.2	332.4	4,234.6	4,086.9	281.7	4,368.6
Non-current assets	2,547.5	56.0	2,603.5	3,903.4	94.9	3,998.3

8 OPERATING PROFIT

This is stated after charging/(crediting):

	Notes	2017 £m	Restated 2016 £m
Depreciation		63.5	72.1
Amortisation of capitalised/purchased intangible assets		19.9	15.4
(Profit)/loss on sale of property, plant and equipment and intangibles		0.5	0.8
Minimum lease payments recognised as an operating lease expense		121.1	127.8
Foreign exchange differences		(5.6)	(1.7)
Contract fulfilment asset utilisation, impairment and derecognition	18	89.3	113.5
TfL implementation costs and penalties		–	25.0
Property commercialisation		(2.7)	(28.0)
Contract termination (gains)/losses		(6.4)	(21.7)
Defence Infrastructure Organisation contract		(22.0)	–
Supplier settlement		(9.2)	–

The table above includes items only within underlying operating profit. Non-underlying items in operating profit are described in notes 3 and 6.

Underlying operating profit in 2017 includes the following items:

- **CFA utilisation, impairment and derecognition:** the Group undertook a comprehensive review of its major contracts to identify indicators of impairment of contract fulfilment assets. For further detail refer to note 18.
- **TfL implementation costs and penalties:** as announced during 2016, the Company encountered delays on the implementation of the new IT system on the Transport for London (TfL) congestion charge contract. As a result of the delays, costs of c.£25.0m, including penalties for delays, were incurred in 2016. These were recorded within underlying operating profit because these costs and penalties were remedies within the contract. There are no such costs in 2017;
- **Property commercialisation:** transactions, executed in the ordinary course of business, have delivered profits of £2.7m (2016: £28.0m). This profit is included within underlying operating profit because part of the Group's strategy is to create and deliver maximum value from assets that are either owned by its clients or are acquired by Capita as part of a wider transaction;
- **Contract termination (gains)/losses:** customer contracts usually contain provisions to compensate the Group for exit costs and future profits in the event of early termination. In-year customer contract terminations for customer convenience have led to associated exit fees paid to Capita of £6.4m (2016: £21.7m) being recorded as income in-year. These are included within underlying operating profit because these amounts are payable to the Group under the terms of the respective contracts being terminated;
- **Defence Infrastructure Organisation contract:** in 2017 we concluded discussions with the Ministry of Defence in relation to the Defence Infrastructure Organisation (DIO) contract, which is expected to end in 2019. The 2017 results include a £22.0m benefit from the re-shaping of the DIO contract which will not recur in 2018; and
- **Supplier settlement:** the IT Services division benefited from a one-off supplier settlement of £9.2m (2016: £nil).
- **Minimum lease payments:** see note 26 for further details.

Fees payable to the Company's auditor and its associates in respect of:	2017 £m	2016 £m
Audit and audit-related services		
The audit of the Company and Group financial statements[1]	3.8	2.2
The audit of the financial statements of subsidiaries of the Company	1.2	1.2
Total audit and audit-related services	5.0	3.4
Non-audit services		
Taxation compliance services	0.1	0.1
Taxation advisory services	–	0.1
Services related to corporate finance transactions	0.1	0.1
Other assurance services	0.8	0.5
Other non-audit services	–	0.1
Total non-audit services	1.0	0.9
Total audit and non-audit services	6.0	4.3

The amounts included in the above table relate to fees payable to KPMG LLP and its associates. Of this amount, £0.1m relates to the disposal of Capita Asset Services which is disclosed as a discontinued operation.

1 Fees for the audit of the Company and Group financial statements have increased year on year by £1.6m. Of this increase, £1.0m relates to the provision of IFRS 15 audit services.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

9 EMPLOYEE BENEFITS EXPENSE

	Notes	2017 £m	2016 £m
Wages and salaries		1,899.5	1,918.6
Social security costs		194.2	186.6
Pension costs	34	122.3	116.2
Share based payments	30	2.9	(4.5)
		2,218.9	2,216.9

The expenses above reflect total operations. Employee benefits expense for continuing operations is £2,098.6m (2016: £2,080.3m).

The aggregate amount of Directors' remuneration (salary, bonus and benefits) is shown on page 84 of the remuneration report;

- As shown on page 160 note 35 'related party transactions', the aggregate amount of gains made by Directors on exercise of share options was £0.7m (2016: £6.2m).
- The remuneration of the highest paid Director was £1,125,510 (2016: £914,894).
- Payments have been made to a defined contribution pension scheme on behalf of 5 Directors (2016: 5 Directors). For the highest paid Director, pension contributions of £21,310 (2016: £30,000) were made.

The average number of employees during the year was made up as follows:	2017 Number	Restated 2016 Number
Sales	1,825	1,883
Administration	8,148	8,831
Operations	59,486	60,872
	69,459	71,586

The average number of employees above reflects continuing operations and excludes employees relating to discontinued operations.

10 NET FINANCE COSTS

	Notes	2017 £m	Restated 2016 £m
Interest receivable		(0.7)	(0.5)
Private placement loan notes		37.7	35.6
Fixed rate interest rate swaps		2.6	12.6
Finance lease		–	0.2
Bank loans and overdrafts		15.6	11.6
Net interest cost on defined benefit pension schemes	34	9.2	6.6
Interest payable		65.1	66.6
Underlying net finance costs		64.4	66.1
Fixed rate interest rate swaps – mark-to-market	28	(0.5)	18.1
Discount unwind on public sector subsidiary partnership payment	28	1.8	2.3
Fair value movement in trade investments		0.6	(0.1)
Non-designated foreign exchange forward contracts – mark-to-market		(3.4)	(13.6)
Interest payable – business exit		0.1	–
Fair value hedge ineffectiveness[1]	28	(0.6)	1.0
Non-underlying net finance costs		(2.0)	7.7
Total net finance costs		62.4	73.8

1 This mark-to-market movement on hedge derivatives represents the extent to which the fair value of these instruments has been affected by the perceived change in the creditworthiness of the counterparties to those instruments and own credit risk. It also includes the ineffectiveness of the fair value hedge relationships arising from changes in the currency basis risk.

11 INCOME TAX

The major components of income tax expense for the years ended 31 December 2017 and 2016 are:

	2017 £m	Restated 2016 £m
Consolidated income statement		
Current income tax		
Current income tax (credit)/charge	(35.3)	57.7
Adjustment in respect of prior years	(10.7)	(17.4)
Deferred income tax		
Origination and reversal of temporary differences	58.1	(59.6)
Adjustment in respect of prior years	1.9	18.1
	14.0	(1.2)

	2017 £m	Restated 2016 £m
Consolidated statement of comprehensive income		
Deferred income tax on cash flow hedges	–	2.8
Income tax on cash flow hedges	0.4	2.8
Deferred income tax movement in relation to actuarial losses on defined benefit plans	(8.8)	(26.5)
	(8.4)	(20.9)

	2017 £m	Restated 2016 £m
Consolidated statement of changes in equity		
Deferred income tax movement in relation to share based payment	–	12.6
Income tax deduction on exercise of stock options	–	(6.8)
	–	5.8

The deferred income tax charge of £12.6m in relation to share based payments arose in the year ended 31 December 2016 due to share awards vesting in respect of which an income tax credit was recognised and the reduction in Capita plc's share price during the second half of the year ended 31 December 2016. There is no movement for year ended 31 December 2017 through the consolidated statement of changes in equity.

The reconciliation between tax expense/(credit) and the product of accounting profit multiplied by the UK corporation tax rate for the years ended 31 December 2017 and 2016 is as follows:

	2017 £m	Restated 2016 £m
Loss before tax	(513.1)	(89.8)
Notional (credit) at UK corporation tax rate of 19.25% (2016: 20.00%)	(98.8)	(18.0)
Adjustments in respect of current income tax of prior years	(10.7)	(17.4)
Adjustments in respect of deferred tax of prior years	1.9	18.1
Non-deductible expenses – underlying	4.2	3.7
Non-deductible expenses – business exit	2.9	–
Non-deductible expenses – specific items	5.6	–
Loss on disposal	6.0	–
Non-deductible goodwill impairment	102.0	12.8
Difference in rate recognition of temporary differences	(9.9)	1.6
Attributable to different rates in overseas jurisdictions	(3.9)	(0.6)
Movement in unrecognised deferred tax	14.7	(1.4)
At the effective tax rate of (2.7%) (2016: 1.3%)	14.0	(1.2)
Total tax expense/(credit) reported in the income statement	14.0	(1.2)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

11 INCOME TAX CONTINUED

The tax charge for the year ended 31 December 2017 was £14.0m (2016: credit of £1.2m). The tax charge/(credit) is equivalent to an effective tax rate of (2.7%) (2016: 1.3%). The effective tax rate on underlying profit is 17.7% (2016: 17.3%).

Adjustments in respect of current income tax of prior years for the year ended 31 December 2017 of £10.7m includes £5.5m relating to increased losses available for group relief surrenders arising from acquisitions and disposals in previous years but identified during the period, and £5.2m relating to adjustments which have a corresponding prior year deferred income tax impact and true ups of positions to filed tax returns.

Adjustments in respect of current income tax of prior years for the year ended 31 December 2016 of £17.4m includes a £5.8m net credit primarily relating to the successful resolution of issues with relevant tax authorities, £3.7m of adjustments which have a corresponding prior year deferred tax impact as noted below, £3.0m relating to the review of the tax treatment of various derivative related historic tax positions and £1.3m relating to successful prior year overseas tax incentive claims.

Adjustments in respect of deferred tax of prior years for the year ended 31 December 2017 of £1.9m reflects adjustments which have a corresponding prior year current income tax impact and true ups of temporary difference positions.

Adjustments in respect of deferred tax of prior years for the year ended 31 December 2016 of £18.1m includes £14.4m due to the write-off of deferred tax assets as a result of a review of the tax treatment of various derivative related historic tax positions, and £3.7m of adjustments which have a corresponding prior year current income tax impact.

Non-deductible expenses charged to underlying results are higher in 2017 due to expenses identified as not deductible relating to overseas companies that are being liquidated. Non-deductible expenses charged to business exits in 2017 relate to costs associated with disposal of businesses and reflect the change between periods. Non-deductible expenses charged to specific items in 2017 mainly relate to non-deductible specific costs detailed further in note 6.

Adjustments of £102.0m relating to non-deductible goodwill impairment reflect the impairment of goodwill on consolidation, detailed further in note 16.

Adjustments of £14.7m relate to the net movement in unrecognised deferred tax on losses, mainly relating to the non-recognition of deferred tax assets previously recognised in connection with deferred tax positions relating to the IFRS 15 accounting changes.

Deferred income tax

Deferred income tax at 31 December relates to the following:

	Consolidated balance sheet		Consolidated income statement	
	2017 £m	Restated 2016 £m	2017 £m	Restated 2016 £m
Deferred tax liabilities				
Contract fulfilment assets	(41.1)	(45.7)	(3.2)	(2.0)
Fair value adjustments on acquisition	(39.7)	(65.3)	(26.2)	(23.5)
	(80.8)	(111.0)	(29.4)	(25.5)
Deferred tax assets				
Accelerated capital allowances	34.9	11.9	(15.6)	9.8
Deferred income	63.1	238.3	165.4	(33.0)
Share based payments	0.4	0.3	(0.1)	–
Pension schemes' liability	55.8	46.5	(0.5)	–
Provisions	13.2	12.7	(2.2)	(3.1)
Losses available for offset against future taxable income	60.5	4.1	(57.6)	(4.1)
Mark-to-market movement on currency swaps	–	–	–	0.1
Cash flow forwards	–	–	–	1.7
Cash flow swaps	–	–	–	12.6
	227.9	313.8		
Net deferred tax asset	147.1	202.8		
Deferred income tax expense/(credit)			60.0	(41.5)

11 INCOME TAX CONTINUED

Impact of adoption of IFRS 15 on income tax balances

Due to the changes in assets, liabilities, income and expenses recognised as a result of the application of IFRS 15, there are consequent IAS 12 Income taxes differences that arise, and are reflected in the restated 31 December 2016 balances.

Due to the changes in the pattern and timing of revenue recognition under IFRS 15, a deferred income liability was recognised on the balance sheet from 1 January 2016, which will be recognised through the income statement in subsequent periods. The impact of these revenue recognition changes is only recognised for tax purposes via a one-off transitional tax adjustment in the year of adoption at entity level, so no tax deduction was available in 2016 for the reduction in historic revenue recognised.

Contract fulfilment assets were also recognised on the balance sheet from 1 January 2016, which will be charged to the income statement in subsequent periods. Under IAS 12, the tax base of an asset is the amount that will be deductible for tax purposes against any taxable economic benefits that will flow to an entity when it recovers the carrying amount of the asset. The tax base of the contract fulfilment asset recognised on the balance sheet prior to 1 January 2017 is therefore reduced by the amounts for which tax deductions have already been taken, creating a temporary difference.

Under the principles of IAS 12, the restated balance sheet for 31 December 2016 reflects a net movement of £192.9m, arising from an increase in deferred tax assets of £245.9m, and increase in deferred tax liability of £53.0m as a result of the transition to IFRS 15. As a result of the one-off transitional adjustment noted above in 2017, part of the deferred tax asset on deferred income liability as at 31 December 2016 converts into a deferred tax asset in connection with tax losses as at 31 December 2017. It is expected that the remaining deferred tax asset on deferred income liability as at 31 December 2017 will convert to a deferred tax asset in connection with tax losses during 2018.

Deferred tax

The UK corporation tax rate decreased from 20% to 19% on 1 April 2017 and will decrease further to 17% from 1 April 2020. The deferred tax balances have been adjusted to reflect this change.

The Group has unrecognised tax losses and other temporary differences of £382.6m (2016: £336.5m) that are available for offset against future taxable profits of the companies in which the losses or other temporary differences arose; of which £101.0m are related to losses incurred by companies acquired by the Group and therefore not as a result of the Group's trading performance. Deferred tax assets have not been recognised in respect of £382.6m (2016: £336.5m) of these losses or other temporary differences, as their recoverability is uncertain. Of the £382.6m, £348.1m relates to losses and £34.5m relates to other temporary differences. £344.1m of the £382.6m losses and temporary differences relate to the UK and have no time expiry. These losses will be subject to recently enacted UK tax loss relief legislation which could result in restricted utilisation in the future. £38.5m of the £382.6m losses and temporary differences relate to various overseas jurisdictions, some of which are being subject to specific loss restriction rules but have no time expiry.

Dividends received from subsidiaries on or after 1 July 2009 are largely exempt from UK tax but may be subject to dividend withholding taxes levied by the overseas tax jurisdictions in which the subsidiaries operate. The gross temporary differences of those subsidiaries affected by such potential taxes is £47.0m (2016: £38.9m). No deferred income tax liability is recognised on these temporary differences as the Group is able to control the timing of reversal and it is probable they will not reverse in the foreseeable future.

Tax litigation

The Group files income tax returns in many jurisdictions. Various tax authorities are currently examining the Group's income tax returns. Tax returns contain matters that could be subject to differing interpretations of applicable tax laws and regulations and the resolution of tax positions, through negotiations with relevant tax authorities or through litigation, can take several years to complete. Tax uncertainties are assessed throughout the year and specifically at the year-end with any associated provisions recognised considering the specific circumstances of each risk, including the merits of technical aspects, previous experience with tax authorities, recent tax law and if relevant, external specialist advice.

While it is difficult to predict the ultimate outcome in some cases, the Group does not currently anticipate that there will be any material impact on the Group's financial position or results of operations in the next financial year.

Tax developments

The Group continues to be directly and indirectly affected by new tax legislation and regulation and the interpretation of tax laws and regulation worldwide. Changes in such legislation, regulation or interpretation could increase our taxes and have an adverse effect on our operating results and financial position. This includes potential changes arising out of the implementation of the recommendations of the Base Erosion and Profit Shifting project initiated by the Organization for Economic Co-Operation and Development.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

12 EARNINGS/(LOSS) PER SHARE

Basic earnings/(loss) per share amounts are calculated by dividing net profit for the year attributable to ordinary equity holders of the parent company by the weighted average number of ordinary shares outstanding during the year.

Diluted earnings/(loss) per share amounts are calculated by dividing the net profit for the year attributable to ordinary equity holders of the parent company by the weighted average number of ordinary shares outstanding during the year plus the weighted average number of ordinary shares that would be issued on the conversion of all the dilutive potential ordinary shares into ordinary shares.

The following reflects the earnings and share data used in the basic and diluted earnings/(loss) per share computations:

	2017		Restated 2016	
	Continuing operations £m	Total operations £m	Continuing operations £m	Total operations £m
Underlying profit attributable to shareholders	303.6	303.6	210.6	210.6
Total loss attributable to shareholders	(533.5)	(117.1)	(94.8)	(57.9)

	2017 m	2016 m
Weighted average number of ordinary shares (excluding trust and treasury shares) for basic earnings per share	665.7	664.7
Dilutive potential ordinary shares:		
Employee share options	–	–
Weighted average number of ordinary shares (excluding trust and treasury shares) adjusted for the effect of dilution	665.7	664.7

At 31 December 2017, 3,395,030 options (2016: 30,754) were excluded from the diluted weighted average number of ordinary shares calculation because their effect would have been anti-dilutive. Under IAS 33-Earnings per Share, potential ordinary shares are treated as dilutive when, and only when, their conversion to ordinary shares would decrease earnings per share or increase loss per share from continuing operations. The Group made a loss in the current year from continuing operations hence the diluted profit/(loss) per share for each component of continuing and total operations needs to be the same amount as the basic profit/(loss) per share.

There have been no other transactions involving ordinary shares or potential ordinary shares between the reporting date and the date of completion of these financial statements.

The earnings per share figures are calculated based on underlying earnings attributable to ordinary equity holders of the parent company of £303.6m (2016 restated: £210.6m) and, after non-underlying costs, losses of £(117.1)m (2016 restated: losses of £(57.9)m). They are both included to provide a better understanding of the underlying trading performance of the Group.

		2017		Restated 2016	
		Continuing operations p	Total operations p	Continuing operations p	Total operations p
Basic earnings/(loss) per share	– reported underlying	45.61	45.61	31.68	31.68
	– reported	(80.14)	(17.58)	(14.27)	(8.72)
Diluted earnings/(loss) per share	– reported underlying	45.61	45.61	31.68	31.68
	– reported	(80.14)	(17.58)	(14.27)	(8.72)

13 DIVIDENDS PAID AND PROPOSED

	2017 £m	2016 £m
Declared and paid during the year		
Ordinary shares (equity):		
Final for 2016 paid: 20.6p per share (2015: 21.2p per share)	137.1	140.9
Interim for 2017 paid: 11.1p per share (2016: 11.1p per share)	73.9	73.9
Dividends paid to shareholders	211.0	214.8
Dividends paid to non-controlling interest	5.6	4.2
Total dividends paid	216.6	219.0
Proposed for approval at AGM (not recognised as a liability at 31 December)		
Ordinary shares (equity):		
Final for 2017: nil per share (2016: 20.6p per share)	–	137.0

14 PROPERTY, PLANT AND EQUIPMENT

	Leasehold improvements, land and buildings £m	Plant and machinery £m	Total £m
Cost:			
As at 1 January 2016	110.5	547.5	658.0
Subsidiaries acquired	–	2.7	2.7
Disposal of business	–	(0.5)	(0.5)
Transfer to held for sale assets	–	0.6	0.6
Additions	10.5	73.1	83.6
Disposals	(0.7)	(14.0)	(14.7)
Asset retirements	(18.2)	(198.8)	(217.0)
Re-class to intangible assets (net)	–	(2.6)	(2.6)
Exchange movement	2.9	12.3	15.2
As at 31 December 2016	105.0	420.3	525.3
Subsidiaries acquired	0.1	0.1	0.2
Disposal of business	(15.8)	(98.2)	(114.0)
Additions	5.8	63.1	68.9
Disposals – underlying	(3.6)	(10.7)	(14.3)
Disposals – specific items	(7.3)	(91.9)	(99.2)
Asset retirements	(7.6)	(75.2)	(82.8)
Re-class to intangible assets	–	(13.1)	(13.1)
Exchange movement	0.5	0.6	1.1
As at 31 December 2017	77.1	195.0	272.1
Depreciation and impairment:			
As at 1 January 2016	43.2	208.8	252.0
Depreciation charged during the year	12.3	69.6	81.9
Impairment – specific items	–	16.5	16.5
Disposal of business	–	(0.2)	(0.2)
Transfer to held for sale assets	–	0.5	0.5
Disposals	(0.3)	(13.0)	(13.3)
Asset retirements	(18.2)	(198.8)	(217.0)
Exchange movement	1.8	8.4	10.2
As at 31 December 2016	38.8	91.8	130.6
Depreciation charged during the year	11.1	58.9	70.0
Impairment – specific items	–	10.0	10.0
Disposal of business	(6.9)	(32.9)	(39.8)
Disposals – underlying	(1.4)	(7.0)	(8.4)
Disposals – specific items	(1.5)	(17.8)	(19.3)
Asset retirements	(7.6)	(75.2)	(82.8)
Re-class to intangible assets	–	(8.0)	(8.0)
Exchange movement	0.2	0.3	0.5
As at 31 December 2017	32.7	20.1	52.8
Net book value			
At 1 January 2016	67.3	338.7	406.0
At 31 December 2016	66.2	328.5	394.7
At 31 December 2017	44.4	174.9	219.3

The net book value of plant and machinery includes an amount of £0.2m (2016: £2.3m) in respect of assets held under finance leases.

Depreciation charged during the year includes £0.2m of accelerated depreciation in relation to businesses disposed of.

As part of its year-end close process in 2017, Capita has undertaken a comprehensive review of its tangible and intangible assets. Following the review, management has taken a decision to fully write down, at 31 December 2017, a number of assets relating to specific programmes resulting from changes in client and Capita strategy in the second half of 2017. Property, plant and equipment amounting to £89.9m has been fully written down as a non-underlying charge. The charge is shown above within impairment – specific items (£10.0m) and disposals – specific items (£79.9m, being cost £99.2m less accumulated depreciation £19.3m).

The above non-underlying write-downs relate to life and pensions assets (£54.7m) and other non-current assets (£35.2m). Refer to note 6 for further details.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

14 PROPERTY, PLANT AND EQUIPMENT CONTINUED

The table below reconciles the disposals and impairments of non-current assets between notes 6 and 15.

	Property, plant and equipment £m	Intangible assets £m	Notes	Total £m	Notes
Life and pension assets					
Disposals – cost	56.2	1.0		57.2	
Disposals – accumulated depreciation/amortisation	(1.5)	–		(1.5)	
	54.7	1.0		55.7	6
Other non-current assets					
Impairment	10.0	4.0		14.0	
Disposals – cost	43.0	39.3		82.3	
Disposals – accumulated depreciation/amortisation	(17.8)	(15.0)		(32.8)	
	35.2	28.3		63.5	6
Total					
Total impairment	10.0	4.0	15	14.0	
Total disposals – cost	99.2	40.3	15	139.5	
Total disposals – accumulated depreciation/amortisation	(19.3)	(15.0)	15	(34.3)	
	89.9	29.3		119.2	

In 2016, the Group experienced difficult market conditions, management conducted a review of contract related balances on major contracts across the Group. This review led to assets in the Insurance and Benefits Services division with a total net book value of £16.5m being fully written down.

15 INTANGIBLE ASSETS

	Intangible assets acquired in business combinations						Intangible assets capitalised/purchased			
	Brands £m	IP, software and licences £m	Contracts and committed sales £m	Client lists and relationships £m	Goodwill £m	Total acquired in business combinations £m	Capitalised software development £m	Other intangibles £m	Total capitalised/ purchased £m	Total £m
Cost										
At 1 January 2016	62.3	113.2	137.5	858.9	2,234.9	3,406.8	128.9	49.6	178.5	3,585.3
Subsidiaries acquired	27.1	–	–	23.3	67.9	118.3	–	0.3	0.3	118.6
Business disposal	(0.1)	–	–	(2.2)	(3.4)	(5.7)	–	(0.2)	(0.2)	(5.9)
Additions	–	–	–	–	–	–	68.1	7.4	75.5	75.5
Disposals	–	–	–	–	–	–	–	(0.3)	(0.3)	(0.3)
Transfer from assets held for sale	–	–	–	5.3	10.3	15.6	0.5	–	0.5	16.1
Re-class from property, plant and equipment	–	0.6	–	–	–	0.6	0.6	1.3	1.9	2.5
Asset retirement	(21.7)	(19.5)	(62.2)	(168.7)	–	(272.1)	(1.9)	(0.5)	(2.4)	(274.5)
Fair value adjustments in 2016 relating to 2015 acquisitions	–	–	–	–	1.7	1.7	–	–	–	1.7
Exchange movement	1.7	2.2	–	26.1	16.2	46.2	0.8	0.3	1.1	47.3
At 31 December 2016	69.3	96.5	75.3	742.7	2,327.6	3,311.4	197.0	57.9	254.9	3,566.3
Subsidiaries acquired	0.4	6.8	1.3	3.9	15.1	27.5	–	–	–	27.5
Business disposal	(3.0)	(0.4)	–	(50.3)	(266.9)	(320.6)	(17.2)	(0.7)	(17.9)	(338.5)
Additions	–	–	–	–	–	–	43.4	29.5	72.9	72.9
Disposals – underlying	–	–	–	–	–	–	(2.7)	(17.5)	(20.2)	(20.2)
Disposals – specific items	–	–	–	–	–	–	(31.0)	(9.3)	(40.3)	(40.3)
Transfer to held for sale	(0.2)	–	–	(3.7)	(7.1)	(11.0)	–	–	–	(11.0)
Re-class from property, plant and equipment	–	–	–	–	–	–	13.1	–	13.1	13.1
Asset retirement	(9.7)	(3.4)	(6.1)	(201.9)	–	(221.1)	(46.6)	(1.9)	(48.5)	(269.6)
Fair value adjustments in 2017 relating to 2016 acquisitions	–	–	–	–	1.2	1.2	–	–	–	1.2
Exchange movement	(0.3)	0.7	–	(2.6)	1.3	(0.9)	0.4	0.1	0.5	(0.4)
At 31 December 2017	56.5	100.2	70.5	488.1	2,071.2	2,786.5	156.4	58.1	214.5	3,001.0
Amortisation and impairment										
At 1 January 2016	37.2	42.3	89.4	492.7	85.4	747.0	21.3	7.0	28.3	775.3
Amortisation charged during the year	12.3	13.3	8.7	117.9	–	152.2	11.7	5.7	17.4	169.6
Impairment – specific items	0.6	–	–	14.1	66.6	81.3	41.8	4.2	46.0	127.3
Impairment – business exit	–	–	–	4.2	–	4.2	–	–	–	4.2
Business disposal	–	–	–	(0.7)	–	(0.7)	–	–	–	(0.7)
Disposals	–	–	–	–	–	–	–	(0.3)	(0.3)	(0.3)
Asset retirement	(21.7)	(19.5)	(62.2)	(168.7)	–	(272.1)	(1.9)	(0.5)	(2.4)	(274.5)
Transfers from assets held for sale	–	–	–	3.6	–	3.6	0.4	–	0.4	4.0
Exchange movement	0.2	0.6	–	5.5	–	6.3	0.6	0.3	0.9	7.2
At 31 December 2016	28.6	36.7	35.9	468.6	152.0	721.8	73.9	16.4	90.3	812.1
Amortisation charged during the year	11.4	12.8	9.0	92.0	–	125.2	16.6	6.6	23.2	148.4
Impairment – specific items	0.7	–	4.0	9.3	551.6	565.6	4.0	–	4.0	569.6
Impairment – business exit	–	–	–	–	7.1	7.1	–	–	–	7.1
Business disposal	(2.6)	(0.3)	–	(45.2)	(0.2)	(48.3)	(7.1)	(0.1)	(7.2)	(55.5)
Disposals – underlying	–	–	–	–	–	–	(0.8)	(6.7)	(7.5)	(7.5)
Disposals – specific items	–	–	–	–	–	–	(13.5)	(1.5)	(15.0)	(15.0)
Asset retirement	(9.7)	(3.4)	(6.1)	(201.9)	–	(221.1)	(46.6)	(1.9)	(48.5)	(269.6)
Transfer to assets held for sale	(0.1)	–	–	(2.3)	(7.1)	(9.5)	–	–	–	(9.5)
Re-class from property, plant and equipment	–	–	–	–	–	–	8.0		8.0	8.0
Exchange movement	(0.3)	0.1	–	0.8	(0.1)	0.5	0.1	0.2	0.3	0.8
At 31 December 2017	28.0	45.9	42.8	321.3	703.3	1,141.3	34.6	13.0	47.6	1,188.9
Net book value										
At 1 January 2016	25.1	70.9	48.1	366.2	2,149.5	2,659.8	107.6	42.6	150.2	2,810.0
At 31 December 2016	40.7	59.8	39.4	274.1	2,175.6	2,589.6	123.1	41.5	164.6	2,754.2
At 31 December 2017	28.5	54.3	27.7	166.8	1,367.9	1,645.2	121.8	45.1	166.9	1,812.1

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

15 INTANGIBLE ASSETS CONTINUED

Amortisation charged during the year includes £1.7m (£0.3m in acquired intangibles and £1.4m in capitalised/purchased intangibles) of accelerated amortisation in relation to businesses disposed or held for sale.

Goodwill impairments: During the year, the Group recognised an impairment charge relating to goodwill of £551.6m (2016: £66.6m). A full description of the impairment review process and assumptions made can be found in note 16.

Intangible assets acquired in business combination impairments: In 2017, £14.0m of intangible assets acquired in business combinations in relation to the Insurance, Life and Pensions businesses were identified as being impaired. During the prior year, intangible assets relating to the Capita Asset Services businesses were impaired by £14.7m and on the closure of a business in the period, acquired intangibles were impaired by £4.2m.

Intangible assets capitalised impairment and disposals: As part of its year-end close process in 2017, Capita has undertaken a comprehensive review of its tangible and intangible assets. Following the review, management has taken a decision to fully write down, at 31 December 2017, a number of assets relating to specific programmes resulting from changes in client and Capita strategy in the second half of 2017. Intangible assets amounting to £29.3m have been fully written down as a non-underlying charge. The charge is shown in the table within impairment – specific items (£4.0m) and disposals – specific items (£25.3m, being cost £40.3m less accumulated depreciation £15.0m). This impairment charge relates to life and pensions assets (£1.0m) and other non-current assets (£28.3m). Refer to note 6 for further details.

During the prior year, a similar review was undertaken which led to capitalised software development being written down by £41.8m. This 2016 impairment is reported within impairment of contract related assets of £58.3m in note 6.

The table in note 14 reconciles the disposals and impairments of non-current assets between notes 6, 14 and 15.

Other intangible asset impairments: During 2017, no other intangible asset impairments were identified. In the prior year, the impact of the dispute with The Co-operative Bank plc included a write down of software licence costs of £4.2m.

16 GOODWILL

Goodwill acquired through business combinations has been allocated to Cash-Generating Units (CGUs), which are expected to benefit from that business combination.

Following the simplification of the group structure in 2017 from 11 to 5 divisions, the Group has reviewed the historical assessment of CGUs and the allocation of goodwill. As part of this simplification within each division, business units were reorganised to be recognisable, identifiable businesses. It was therefore concluded that the Group's business units are the most appropriate lowest level at which cash flows can be identified and goodwill has been reallocated to these new CGUs. As at 31 December 2017, the Group has 45 CGUs. The opening goodwill balance has been restated for comparable purposes. The remaining disclosures have not been restated as they are not comparable, due to the change in CGU and goodwill allocation.

Carrying amount of goodwill allocated to groups of Cash-Generating Units

The following table shows the allocation of goodwill to groups of CGUs

	Private Sector Partnerships	Public Services Partnerships	Professional Services	Digital and Software Solutions	IT Services	Asset Services	Total
Total number of CGUs (No.)	9	10	12	8	6	–	45
	£m	£m	£m	£m	£m	£m	£m
31 December 2016	582.6	209.0	354.6	416.4	375.3	237.7	2,175.6
Additions	5.9	–	1.7	–	7.5	–	15.1
Fair value adjustment	–	–	–	–	1.2	–	1.2
Disposals	–	–	(29.0)	–	–	(237.7)	(266.7)
Held for sale	–	(7.1)	–	–	–	–	(7.1)
Exchange movement	1.4	–	–	–	–	–	1.4
Impairment	(389.1)	(7.5)	–	(125.1)	(29.9)	–	(551.6)
31 December 2017	**200.8**	**194.4**	**327.3**	**291.3**	**354.1**	**–**	**1,367.9**

16 GOODWILL CONTINUED

The table below sets out the split between significant and non-significant CGUs. A significant CGU is defined as a CGU exceeding 10% of opening goodwill, 10% of closing goodwill or a CGU that was impaired or disposed of during the year. The remaining 36 CGUs that have not been impaired, are included in the 'Other CGUs' column.

	Insurance, Life & Pensions £m	Asset Services £m	Secure Solutions & Services £m	Real Estate & Infrastructure £m	AMT £m	Specialist Recruitment £m	Capita Europe £m	Enterprise Services £m	Technology Solutions £m	Other £m	Total £m
31 December 2016	323.4	237.7	191.9	138.8	63.3	29.0	84.5	83.0	90.6	933.4	2,175.6
Additions	–	–	–	–	–	–	–	–	7.0	8.1	15.1
Fair value adjustments	–	–	–	–	–	–	–	–	1.2	–	1.2
Disposals	–	(237.7)	–	–	–	(29.0)	–	–	–	–	(266.7)
Held for sale	–	–	–	(7.1)	–	–	–	–	–	–	(7.1)
Exchange movements	0.8	–	–	–	–	–	–	–	–	0.6	1.4
Impairment	(324.2)	–	(113.2)	(7.5)	(11.9)	–	(64.9)	(26.5)	(3.4)	–	(551.6)
31 December 2017	–	–	78.7	124.2	51.4	–	19.6	56.5	95.4	942.1	1,367.9

The impairment test

The Group tests intangible assets, including goodwill, for impairment on an annual basis or more frequently if there are indications that any of these assets may be impaired.

The Group's impairment test compares the carrying value of each CGU with its recoverable amount. The recoverable amount of a CGU is determined by its value in use which is derived from discounted cash flow calculations. The key inputs to the calculations are described below, including changes in market conditions.

As reported in the Chief Executive Officer's review, significant actions are required to address recent operational and external challenges and a major transformational plan has been launched. Actions were taken in the prior year to implement a new simplified market facing organisation structure, and at the time of the interim results the Group announced an improved win rate against the backdrop of a quiet market. Since that date the Group has continued to experience a higher level of revenue attrition than expected, and continued to experience delays in customer decision making and weakness in new sales.

In January 2018, the Group announced that the administration of Prudential's life and pensions business, around 2% of Group revenue, will be transferring from Capita to a new supplier later in 2018. As previously disclosed, another of the Group's life and pensions clients is conducting a strategic review, the outcome of which remains uncertain but is expected to result in the continuation of the contract with amended terms, or the termination of the contract.

As announced in January 2018, Capita has shifted its strategy, and set a plan, focusing on investment in people, sales capability and its transformation plan. The business plan for the divisions indicate there is likely to be a significant negative impact upon profits from contract and volume attrition, the dropping out of one-off items including contract and supplier-related profits which were reported in 2017 and increases in some cost items.

The transformation plan encompasses strategy, cost competitiveness, sales, IT and the Company's capital structure, to improve the performance of Capita over the medium-to-long term. The Board is confident that the transformation plan will deliver significant benefits to Capita over the medium-to-long-term and the associated disposal programme will support the re-positioning of the Group.

In undertaking the annual impairment review, the Directors have considered both external and internal sources of information, and any observable indications that may suggest that the carrying value of goodwill may be impaired. The continued operational and external challenges faced by the Group have led to a significant deterioration in new sales opportunities from the positions in March and September 2017. In addition, the Group has experienced contract terminations and attrition as highlighted above, and the transformation plan has identified areas that need to be addressed to rebuild and reposition Capita. These events and circumstances have led to the recognition of the impairment charge as set out in this note.

Forecast cash flows

Previously, the Group prepared a one-year business plan. For 2018, the Group prepared a five-year strategic plan. The cash flow forecasts are derived from the most recent Board approved strategic plan for the years ended 31 December 2018 – 2022 and are based upon:

- past performance and known changes and expectations of current market conditions;
- the sales volume assumptions underlying the forecasts are based on the Directors' estimates of the route to new sales and renewals; and
- the efficiency of the cost base and whether it is at the correct level for the business currently and is supportive of future growth.

The markets in which the Group operate and the services which we provide are discussed in 'Divisional Performance 2017' starting on page 25.

Accounting standards require that cash flows after the forecast period, which for Capita is the period covered by the Board approved strategic plan, are extrapolated into the future over the useful life of the CGU, using a steady or declining growth rate that is consistent with that of the product, industry or country.

As the strategic plan covers a period of 5 years, no extrapolation is required and instead an appropriate terminal value has been applied to each year 5 CGU cash flow. The resulting cash flows are then discounted at a rate, which is discussed further below. The major assumptions in this extrapolation are:

- long-term growth rate; and
- the pre-tax discount rates to be used.

Long-term growth rates

The rates are based on long-term inflation rates specific to each CGU, adjusted for management's view of renewal rates on contracts. The growth rate assumptions do not exceed the average long-term growth rate forecast for UK GDP growth of 1.5%.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

16 GOODWILL CONTINUED

Discount rates

The resulting cash flows are discounted at a rate that recognised their CGU specific characteristics and is based on the overall Group Weighted Average Cost of Capital (WACC).

The Group's post-tax WACC is 7.46% (2016: 7.11%). The Group WACC is calculated by weighting the cost of our debt and equity financing in line with the amounts of debt and equity that we use to finance our activities. We have calculated our post-tax WACC assuming a risk-free rate of 1.23% (2016: 1.22%), a market risk premium of 13.89% (2016: 9.23%) and a Beta of 0.57 (2016: 0.79). These assumptions are based on publicly available sources.

For the discount rate used in the cash flows of each CGU, we have adjusted the rate, where appropriate, to reflect the risks specific to the market in which the CGU operates. The rate adjustment takes into account the relative risks in the business through adjustment to the risk premium and the weighting of the funding levels provided per CGU, whilst retaining a constant cost of debt.

The below table represents the range of pre-tax discount rates used and the range of implied compound annual growth rates for the years 2017 to 2022 for each CGU. The table also includes the divisions' compound annual growth rate for the same period.

	Pre-tax discount rate		Growth rate	
Division	Min	Max	Min	Max
Private Sector Partnerships	9.2%	14.1%	(13.9)%	9.5%
Public Services Partnerships	9.2%	14.1%	(5.7)%	25.4%
Professional Services	9.2%	9.2%	(2.9)%	14.1%
Digital and Software Solutions	9.2%	12.9%	1.1%	14.3%
IT Services	9.2%	9.2%	(11.9)%	6.7%

Sensitivity analysis

The impairment testing as described is reliant on the accuracy of management's forecasts and the assumptions that underlie them and also on the selection of the discount and growth rates to be applied. In order to gauge the sensitivity of the result to a change in any one, or combination of the assumptions that underlie the model, a number of scenarios have been run to identify the range of reasonably possible alternatives and measure which CGUs are the most susceptible to an impairment should the assumptions used be varied.

The table below shows how the impairment test would be impacted (with all other variables being equal) by an increase in discount rate of 1%, or if the business plan was missed by 10% for each of the 5 years or a decrease of 1% in the long-term growth rate for the Group in total and each of its divisions. We have also considered the impact of all of the scenarios together and disclosed the impact on impairment in the final column.

		Increase/(decrease) in NPV				
	No. of CGUs	1% increase in WACC	Miss targets by 10%	Long-term growth rate decrease by 1%	Combination sensitivity	(Increase)/Decrease in 2017 impairment using combination sensitivity scenario
Private Sector Partnerships	9	(92.6)	(111.8)	(65.7)	(241.9)	(19.6)
Public Services Partnerships	10	(52.6)	(74.6)	(34.2)	(148.2)	(34.2)
Professional Services	12	(146.7)	(138.3)	(111.0)	(349.2)	–
Digital and Software Solutions	8	(134.1)	(141.2)	(98.7)	(332.6)	(59.2)
IT Services	6	(78.8)	(76.5)	(59.2)	(189.2)	(64.4)
	45	(504.8)	(542.4)	(368.8)	(1,261.1)	(177.4)

Management continue to monitor closely the performance of all CGUs and consider the impact of any changes to the key assumptions. In conclusion, other than disclosed above with regard to those CGUs impaired in the year, management believe there is no reasonably possible change in the underlying assumptions that would result in a further significant impairment charge in the consolidated income statement.

17 BUSINESS COMBINATIONS

2017 acquisitions

The Group made a number of acquisitions in 2017 which are shown in aggregate. The fair values of the identifiable assets and liabilities acquired are disclosed in the table below:

	Fair value to Group recognised on acquisition £m
Property, plant and equipment	0.2
Intangible assets	12.4
Trade and other receivables due in less than 1 year	7.5
Corporation tax	(0.3)
Cash and cash equivalents	4.5
Trade and other payables (excluding accruals) due in less than 1 year	(2.9)
Accruals due in less than 1 year	(2.6)
Deferred tax	(2.2)
Net assets	16.6
Goodwill arising on acquisition	15.1
	31.7
Discharged by:	
Cash	23.3
Deferred consideration	2.0
Contingent consideration accrued	6.4
	31.7

In all cases, 100% of the ordinary share capital was acquired. The companies acquired have been mainly in the areas of IT Services, Travel and Events, Customer Management and Digital and Software Solutions which complement or extend the Group's existing skill sets and provide opportunities for growth into these markets. In addition, during the year the Group settled £10.8m of deferred consideration and £11.7m of contingent consideration payments with regard to previous acquisitions, all of which had been accrued.

Where this can be determined, the acquired subsidiaries contributed £1.8m to the profit before tax of the Group. If these acquisitions had occurred on 1 January 2017, Group's revenue would have been an estimated £4,237.7m and Group loss before tax would have been an estimated £512.8m. In determining these amounts, management has assumed that the fair value adjustments that arose on the date of acquisition would have been the same if the acquisition had occurred on 1 January 2017. During the year, some of the acquired businesses have been completely integrated into the existing business of the Group and therefore their post-acquisition performance cannot be determined.

Goodwill has arisen on the acquisitions because the fair value of the acquired assets was lower than the consideration paid; the goodwill represents the value to the Group that can be driven from these underlying assets over the life of the acquired businesses, particularly from synergies, and the capabilities of the acquired workforce. The total amount of goodwill recognised in the period that is expected to be deductible for tax purposes is £nil (2016: £nil).

The fair value exercise has been completed on a provisional basis for acquisitions made in 2017. The Group will complete this review in 2018 though any adjustment to the carrying value is likely to be insignificant to the individual acquisition. In total, the effect of revisions made to fair value adjustments in the current year that had been determined provisionally at the immediately preceding balance sheet date increases goodwill by £1.2m.

Contingent consideration

In respect of the acquisitions made in 2017, the Group has agreed to pay the vendors additional consideration dependent on the achievement of performance targets in the periods post acquisition. These performance periods are of up to 3 years in duration and will be settled in cash on their payment date on achieving the relevant targets. The range of the additional consideration payment is estimated to be between £nil and £24.7m. The Group has included £6.4m as contingent consideration related to the additional consideration, which represents its fair value at the acquisition date. Contingent consideration has been calculated based on the Group's expectation of what it will pay in relation to the post-acquisition performance of the acquired entities by weighting the probability of a range of payments to give an estimate of the final obligation.

Acquisition-related costs

The Group incurred acquisition-related costs of £1.7m related to professional fees paid for due diligence, general professional fees and legal related costs. These costs have been included in non-underlying administrative expenses in the Group's consolidated income statement consistent with prior years. Absent any material acquisitions, they will be included in underlying in future periods.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

17 BUSINESS COMBINATIONS CONTINUED

2016 acquisitions

The Group made a number of acquisitions in 2016 which are shown in aggregate. The fair values of the identifiable assets and liabilities acquired are disclosed in the table below:

	Fair value to Group recognised on acquisition £m
Property, plant and equipment	2.7
Intangible assets	50.7
Trade and other receivables due in less than 1 year	41.4
Corporation tax	(3.1)
Cash and cash equivalents	4.0
Trade and other payables (excluding accruals) due in less than 1 year	(21.2)
Accruals due in less than 1 year	(31.7)
Provisions	(1.0)
Deferred tax	(8.3)
Finance leases	(0.8)
Net assets	32.7
Goodwill arising on acquisition	69.6
	102.3
Discharged by:	
Cash	93.5
Contingent consideration accrued	8.8
	102.3

In all cases, 100% of the ordinary share capital was acquired. The companies acquired have been mainly in the areas of IT, and Digital and Software Solutions which complement or extend the Group's existing skill sets and provide opportunities for growth into these markets. In addition, during the year the Group settled £10.7m of deferred consideration and £18.5m of contingent consideration payments with regard to previous acquisitions, all of which had been accrued.

Where this can be determined, the acquired subsidiaries contributed £1.61m to the profit before tax of the Group. If these acquisitions had occurred on 1 January 2016 as reported in the prior year, Group revenue would have been an estimated £4,989.9m and Group profit before tax would have been an estimated £72.0m. In determining these amounts, management has assumed that the fair value adjustments that arose on the date of acquisition would have been the same if the acquisition had occurred on 1 January 2016. During the year, some of the acquired businesses have been completely integrated into the existing business of the Group and therefore their post-acquisition performance cannot be determined.

Goodwill has arisen on the acquisitions because the fair value of the acquired assets was lower than the consideration paid; the goodwill represents the value to the Group that can be driven from these underlying assets over the life of the acquired businesses, particularly from synergies, and the capabilities of the acquired workforce. The total amount of goodwill recognised in the period that is expected to be deductible for tax purposes is £nil (2015: £44.4m).

The fair value exercise was completed on a provisional basis for acquisitions made in 2016. The Group completed this review in 2017 with any adjustment to the carrying value insignificant to the individual acquisition. In total, the effect of revisions made to fair value adjustments in the current year that had been determined provisionally at the immediately preceding balance sheet date increases goodwill by £1.7m.

Contingent consideration

In respect of the acquisitions made in 2016, the Group has agreed to pay the vendors additional consideration dependent on the achievement of performance targets in the periods post acquisition. These performance periods are of up to 4 years in duration and will be settled in cash and loan notes on their payment date on achieving the relevant targets. The range of the additional consideration payment is estimated to be between £1.0m and £23.0m. The Group included £8.8m as contingent consideration related to the additional consideration, which represented its fair value at the acquisition date. Contingent consideration has been calculated based on the Group's expectation of what it will pay in relation to the post-acquisition performance of the acquired entities by weighting the probability of a range of payments to give an estimate of the final obligation.

Acquisition-related costs

The Group incurred acquisition-related costs of £9.0m related to professional fees paid for due diligence, general professional fees and legal related costs. These costs have been included in non-underlying administrative expenses in the Group's consolidated income statement.

18 CONTRACT FULFILMENT ASSETS

	£m
As at 1 January 2016	277.6
Additions	76.5
Derecognition	(59.3)
Utilised during the year – underlying	(54.2)
As at 31 December 2016	240.6
Additions	101.2
Impairment and derecognition	(24.0)
Utilised during the year – underlying	(65.3)
As at 31 December 2017	252.5

In preparing these financial statements, the Group undertook a comprehensive review of its major contracts to identify indicators of impairment of contract fulfilment assets. The Group determined whether or not the contract fulfilment assets were impaired by comparing the carrying amount of the asset to the remaining amount of consideration that the Group expects to receive less the costs that relate to providing services under the relevant contract. In determining the estimated amount of consideration, the Group used the same principles as it does to determine the contract transaction price, except that any constraints used to reduce the transaction price were removed for the impairment test.

In line with the Group's accounting policy, as set out in note 2, if a contract or specific performance obligation exhibited marginal profitability or other indicators of impairment, judgement was applied to ascertain whether or not the future economic benefits from these contracts were sufficient to recover these assets. In performing this impairment assessment, management is required to make an assessment of the costs to complete the contract. The ability to accurately forecast such costs involves estimates around cost savings to be achieved over time, anticipated profitability of the contract, as well as future performance against any contract-specific KPIs that could trigger variable consideration, or service credits.

Following this review, management has taken the decision to impair costs capitalised as contract fulfilment assets of £14.1m (2016: £nil) within underlying cost of sales.

The review also resulted in the derecognition of £9.9m (2016: £59.3m) of contract fulfilment assets as no further economic benefits are expected to flow from the Group's use of the assets.

Of these assets derecognised, £5.5m (2016: £42.3m) is included within non-underlying cost of sales. The Group's life and pensions business has developed a platform to support an existing life and pensions contract, but which could provide services to multiple clients in the future. The Group's transformation plan has identified there is no longer a market for this platform and accordingly the carrying value of this and associated assets has been written off. The impact on the financial statements is a non-underlying charge of £61.2m (£54.7m property, plant and equipment – see note 14; £1.0m capitalised software intangible assets – see note 15; and £5.5m contract fulfilment assets) representing the write-off of the non-current assets. The change has been included within non-underlying as the assets have no further value to the Group. In 2016, £42.3m of the charge relates to the impact of the dispute with The Co-operative Bank plc representing the write-off of contract fulfilment assets relating to the transformation plan. Refer to note 6 for full details of the non-underlying events.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

19 FINANCIAL ASSETS

Current financial assets	2017 £m	2016 £m
Deferred consideration[1]	3.0	6.0
Insurance asset recoverable[2]	5.0	15.5
Available-for-sale assets[3]	0.4	–
Cash flow hedges	4.0	0.7
Currency swaps in relation to USD denominated loan notes[4]	72.2	67.2
Non-designated foreign exchange forwards and swaps	4.1	3.2
	88.7	92.6

Non-current financial assets	2017 £m	2016 £m
Investment loan[5]	–	5.0
Investment[6]	–	4.0
Deferred consideration[1]	2.2	11.0
Available-for-sale assets[3]	4.2	5.6
Cash flow hedges	3.8	6.3
Currency swaps in relation to USD denominated loan notes[4]	113.1	293.8
Non-designated foreign exchange forwards and swaps	3.6	4.2
Interest rate swaps in relation to GBP denominated loan notes[4]	5.4	7.7
	132.3	337.6

1 The deferred consideration is related to the sale of the Health business held for sale in 2015, and which now has been disposed of. The amount has partly been recovered by a series of payments during 2017 with the remainder to be recovered in 2018 and 2019.

2 The insurance asset recoverable relates to amounts where the Group has virtual certainty of receiving a contribution in respect of a litigation or insurance claim.

3 Available-for-sale assets comprise investments in unlisted ordinary shares and fund assets. The unlisted ordinary shares, for which there is no immediately identifiable market and which have no fixed maturity date or coupon rate, are carried at cost less provision for any impairment. The fund assets, for which there are market values, are recorded at fair value as at 31 December 2017.

4 The currency swaps are used to hedge the exposure to interest rate and currency fluctuations on the Group's USD denominated loan notes. The change in the fair value of the underlying loan notes due to changes in interest and currency rates is offset by the fair value of the currency swaps recognised above. The interest rate swaps are used to hedge the fair value of the Group's GBP denominated loan notes and the change in the fair value of the underlying loan notes due to changes in interest rates is equivalent to the fair value of the interest rate swaps recognised above. Details of the interest rate swaps, currency swaps and cash flow hedges are contained in note 28.

5 The investment loan represented a funding arrangement which has subsequently been impaired.

6 The investment related to a non-current trade investment which has been impaired.

20 TRADE AND OTHER RECEIVABLES

Current	2017 £m	Restated 2016 £m
Trade receivables	379.5	443.9
Other receivables	26.9	50.7
Contract fulfilment assets	39.4	41.6
Accrued income	207.7	188.9
Prepayments	122.3	117.6
	775.8	842.7

Non-current	2017 £m	Restated 2016 £m
Other receivables	0.6	5.6
Prepayments	27.4	43.2
	28.0	48.8

Current contract fulfilment assets are costs directly related to a contract or to a specifically identifiable anticipated contract which will be used in satisfying performance obligations in the next 12 months from the balance sheet date.

Trade receivables are non-interest bearing and are generally on 30 days terms.

Consistent with prior years, the Group makes use of non-recourse trade receivable financing arrangements provided to it by a number of its relationship banks. There was a net balance of £110.0m sold on these arrangements as at 31 December 2017 (2016: £133.6m). As these trade receivables have been sold without recourse, the Group has derecognised them in the above table.

At 31 December 2017, trade receivables at a nominal value of £8.3m (2016: £11.5m) were impaired and fully provided for.

Movements in the provision for impairment of trade receivables were as follows:

	2017 £m	2016 £m
At 1 January	11.5	10.4
Utilised	(1.5)	(1.2)
Provided/(released in) year (net)	(1.4)	2.0
Business disposal/closure	(1.4)	–
Provisions acquired	1.1	0.3
At 31 December	8.3	11.5

As at 31 December, the analysis of trade receivables that were past due but not impaired is as follows:

			Past due but not impaired			
	Total £m	Neither past due nor impaired £m	0–3 months £m	4–6 months £m	7–12 months £m	More than 12 months £m
2017	379.5	252.1	121.5	5.9	–	–
2016	443.9	326.3	112.2	5.4	–	–

The Group monitors the level of trade receivables on a monthly basis, continually assessing the risk of default by any counterparty.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

21 CASH, CASH EQUIVALENTS AND OVERDRAFTS

	2017 £m	2016 £m
Cash at bank and in hand	921.7	1,098.3
Overdrafts	(443.3)	(532.5)
	478.4	565.8

Cash at bank earns interest at floating rates based on daily bank deposit rates. The fair value of cash is the same as the carrying amount above. Included in cash at bank and in hand is £14.0m held in a 45 day notice of withdrawal money market fund.

Included in Overdrafts are balances totalling £387.7m (2016: £530.2m) held in the Group's notional cash pools under which the bank has the right of offset against Cash at bank – see note 28.

22 TRADE AND OTHER PAYABLES

Current	2017 £m	2016 £m
Trade payables	274.9	366.5
Other payables	36.5	35.1
Other taxes and social security	150.8	202.6
Accruals	293.0	372.8
	755.2	977.0

Non-current	2017 £m	2016 £m
Other payables	0.1	6.8
Accruals	16.9	14.2
	17.0	21.0

Trade payables are non-interest bearing and are settled within terms agreed with suppliers.

23 DEFERRED INCOME

Current	2017 £m	Restated 2016 £m
Deferred income	1,201.2	1,374.9

Non-current	2017 £m	Restated 2016 £m
Deferred income	314.0	216.7

The Group's deferred income balances solely relate to revenue from contracts with customers. Movements in the deferred income balances were driven by transactions entered into by the Group within the normal course of business in the year, other than the accelerated revenue recognised of £22.0m relating to the benefit from the re-shaping of the DIO contract which is not expected to recur in 2018.

24 FINANCIAL LIABILITIES

Current	Notes	2017 £m	2016 £m
Contingent consideration		12.1	3.6
Deferred consideration		11.1	10.8
Public sector subsidiary partnership payment		9.4	9.4
Put option of non-controlling interests		6.8	–
Obligations under finance leases	26	0.2	2.2
Cash flow hedges		1.6	1.0
Non-designated foreign exchange forward contracts		0.3	3.3
Foreign exchange swaps held for foreign net investment		–	0.1
Private placement loan notes		224.1	192.0
Other loan notes		–	0.3
Fixed rate interest rate swaps		–	1.5
		265.6	224.2
Non-current			
Contingent consideration		12.5	19.4
Deferred consideration		2.0	–
Public sector subsidiary partnership payment		41.8	49.4
Put options of non-controlling interests		115.6	115.9
Obligations under finance leases	26	–	0.1
Private placement loan notes		1,439.9	1,769.7
Other loan notes		0.3	–
Term loan		100.0	650.0
Cash flow hedges		1.1	3.2
Currency swaps in relation to USD denominated loan notes		8.5	3.1
Fixed rate interest rate swaps		–	83.6
		1,721.7	2,694.4

Included in financial liabilities is an amount of £1,664.0m (2016: £1,961.7m) which represents the carrying value of the Group's private placement loan notes which should be considered in conjunction with the carrying value of currency and interest rate swaps of £190.7m included in financial assets and £8.5m included in financial liabilities (2016: £368.7m included in financial assets and £3.1m included in financial liabilities). This gives an effective liability of £1,481.8m (2016: £1,596.1m).

In 2017, the Group repaid at maturity USD179.0m of October 2007 Series B loan notes (GBP equivalent: £90.3m) and USD50.0m of June 2010 Series A loan notes (GBP equivalent: £33.8m).

The fees incurred on the amendment of the loan notes during the year amounted to £2.1m (new issue and amendment fees: 2016: £0.6m). Issue and amendment costs are spread over the term of the loan notes. The unamortised balance of issue and amendment costs at the year-end totalled £3.4m (2016: £2.5m).

The Group's bank term loan is a £100m 5-year term loan maturing in May 2019 which bears interest at floating rates linked to LIBOR.

During 2017, the Group repaid early a £200m term loan and £350m which was outstanding on a £600m term loan facility. Both were due to mature in September 2018.

The obligations under finance leases are secured on the assets being financed. The term loan and loan notes are unsecured.

The public sector subsidiary partnership payment liability is an estimate of the annual preferred payments to be made by AXELOS Limited (the partnership formed with the Cabinet Office) to the Cabinet Office in 2018 to 2023. This payment is funded by AXELOS Limited and is contingent on the profits of that business. Following these payments, the Company will pay profits to the partners according to their stake in the business.

The non-controlling shareholders of AXELOS Limited, Entrust Support Services Limited and Fera Science Limited have an option to sell their shareholding to a member of the Group. Accordingly, a liability of £122.4m (2016: £115.9m) has been recognised and a corresponding entry has been recorded against retained earnings. The options in each case are exercisable only after a period has elapsed, as a result, the liabilities have been split between current and non-current in the table above.

In 2017, the Group elected to terminate the Fixed rate interest rate swaps, recognising a gain of £0.5m in non-underlying finance costs. See note 28 for further details of these Fixed rate interest swaps.

The Group has available to it a committed Revolving Credit Facility of £600m of which £81m matures in August 2020 and £519m matures in August 2021. This facility is available for the Group's immediate use and £nil was drawn down at 31 December 2017 (2016: £nil).

The covenant terms in respect of the above liabilities are discussed in note 2.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

24 FINANCIAL LIABILITIES CONTINUED

As at 31 December 2017, the Group has issued unsecured private placement loan notes as follows:

Private placement loan notes	Interest rate %	Denomination	Face Value (m)	Maturity
Issued 2010				
Series C	4.78	GBP	50.0	30 June 2020
Issued 2011[1]				
Series A	4.85	GBP	50.0	22 July 2019
Series C	4.76	GBP	35.0	19 July 2021
Issued 2013				
Series A	3.73	GBP	75.0	30 September 2020
Issued 2015				
Series C	3.26	GBP	25.0	22 January 2022
Series F	3.54	GBP	10.0	22 January 2025
Series G	3.67	GBP	30.0	22 April 2025
Series I	3.58	GBP	32.0	22 January 2027
Issued 2016				
Series B	2.18	GBP	48.5	27 October 2021
Series D	2.52	GBP	37.0	27 October 2023
Series F	2.77	GBP	25.0	27 October 2026
Total of GBP denominated loan notes		GBP	417.5	
Issued 2008[2]				
Series B	6.51	USD	256.0	13 September 2018
Issued 2010[2]				
Series B	4.80	USD	250.0	30 June 2020
Issued 2011[2]				
Series B	4.65	USD	80.0	22 July 2019
Series A	3.72	USD	40.0	19 July 2018
Series B	4.50	USD	236.0	19 July 2021
Series A	4.75	USD	50.0	26 July 2021
Issued 2015[2]				
Series A	3.33	USD	40.0	22 January 2022
Series B	3.43	USD	65.0	22 April 2022
Series D	3.45	USD	53.0	22 January 2023
Series E	3.65	USD	98.5	22 January 2025
Series H	3.80	USD	37.0	22 January 2027
Issued 2016[2]				
Series A	3.03	USD	25.0	27 October 2021
Series C	3.37	USD	24.0	27 October 2023
Series E	3.59	USD	26.0	27 October 2026
Total of USD denominated loan notes		USD	1,280.5	
Issued 2015				
Series A	2.125	EUR	230.0	10 November 2022
Series B	2.875	EUR	60.0	10 November 2027
Series C	2.125	EUR	20.0	10 November 2022
Total of euro denominated loan notes		EUR	310.0	

1 The Group has entered into interest rate swaps to convert the interest cost to floating rates based on 6-month GBP LIBOR.

2 The Group has entered into currency swaps for the USD issues to achieve a floating rate of interest based on 6-month GBP LIBOR. Further disclosure on the Group's use of hedges is included in note 28.

All series are unsecured and rank pari passu in all respects.

25 FUNDS ASSETS AND LIABILITIES

	2017 £m	2016 £m
Funds receivables	–	171.4
Funds restricted cash	–	2.2
Funds assets	–	173.6
Funds liabilities	–	(173.6)

These balances relate to investors' purchase or redemption of units in Investment Funds of which Capita Financial Managers Limited, our unit trust administration business, is an Authorised Corporate Director. The balances are due to and from the investors and Investment Funds. The parties to the trade are permitted to take advantage of a 4-day settlement period between initiation and settlement of the trade. Capita Financial Managers Limited was disposed of during 2017 as part of the Capita Asset Services businesses sale.

26 OBLIGATIONS UNDER LEASES AND HIRE PURCHASE CONTRACTS

The Group uses finance leases and hire purchase contracts to acquire plant and machinery. These leases have terms of renewal and purchase options but no escalation clauses. Renewals are at the option of the lessee.

The value of future minimum lease payments is analysed as follows:

	2017 £m	2016 £m
Not later than 1 year	0.2	2.2
Later than 1 year but not more than 5 years	–	0.1
	0.2	2.3

The Group has entered into commercial leases on properties, motor vehicles and items of plant and machinery. These leases have an average duration of between 3 and 10 years.

Future minimum rentals payable under non-cancellable operating leases are as follows:

	2017 £m	Restated 2016 £m
Not later than 1 year	119.2	124.8
Later than 1 year but not later than 5 years	285.8	304.4
Later than 5 years	428.0	437.8
	833.0	867.0

The Group's project to prepare for adopting IFRS 16 Leases has initiated a comprehensive review of all lease arrangements across the Group and how these should be disclosed within our lease commitment note.

Management has amended the previously disclosed discounted future minimum lease payments to present undiscounted values, as this information is considered to be more relevant to users in the context of the future adoption of the new standard.

In addition, the IFRS 16 review has included a wide-ranging search of all leases across the Group and this has highlighted certain properties that were omitted from the disclosed commitments in the prior year. The comparatives have been restated accordingly. The key item relates to the Company's new Head Office which will be available during 2018, and which at the end of the prior year was under construction.

The effect of the restatement on the previously reported disclosures is as follows:

2016 reported lease commitments	£587.0m
Change in policy to present undiscounted commitments	£112.9m
Understatement of property lease commitments	£165.1m
2016 restated lease commitments	£867.0m

The review further highlighted that non-lease payments had incorrectly been included in the minimum lease payments expense disclosure in 2016. The comparatives have been restated accordingly. Refer to note 8 for the restated disclosure of £127.8m (previously £164.8m before restatement to £161.0m for discontinued operations).

This restatement of the 2016 disclosures has had no impact on the balance sheet, profit and loss or cash flows of the Group.

27 PROVISIONS

	Restructuring provision £m	Business exit provision £m	Asset services indemnity provision £m	Claim and litigation provision £m	Property provision £m	Other £m	Total £m
As at 1 January 2017	49.4	6.0	23.1	41.5	28.0	12.7	160.7
Provided/(released) in the year (net)	6.8	33.5	66.8	28.4	(3.7)	8.1	139.9
Utilisation	(45.5)	(2.8)	(18.5)	(5.6)	(1.5)	(10.7)	(84.6)
Disposal of subsidiaries	(0.1)	–	(2.3)	–	(0.1)	(0.7)	(3.2)
Reclassification between categories	–	0.3	–			(0.3)	–
Transfer to held for sale	–	–	–	–	(0.2)	–	(0.2)
As at 31 December 2017	10.6	37.0	69.1	64.3	22.5	9.1	212.6

The provisions made above have been shown as current or non-current on the balance sheet to indicate the Group's expected timing of the matters reaching conclusion.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

27 PROVISIONS CONTINUED

Judgement is required in measuring and recognising provisions related to pending litigation or other outstanding claims subject to negotiated settlement, mediation and arbitration, as well as other contingent liabilities. Judgement is necessary in assessing the likelihood that a pending claim will succeed, or a liability will arise, and to quantify the possible range of the financial settlement. Because of the inherent uncertainty in this evaluation process, actual losses may be different from the originally estimated provision. Where practicable the range of reasonably possible outcomes and sensitivities of the carrying amounts to the methodology, assumptions and estimates, the reason for the sensitivity, the expected resolution of uncertainties and the range of reasonable possible alternatives, are provided below. Where no reliable basis of estimation can be made no provision is recorded, however contingent liabilities disclosures are given when there is a greater than a remote probability of outflow of economic benefits.

Restructuring provision: The brought forward provision is in respect of the cost of the major restructuring activities undertaken by the Group commencing in the last quarter of 2016. It represents the cost of reducing role count where there is a constructive obligation created through communication to affected employees which has crystallised a valid expectation that roles are at risk. Additionally, it reflects the onerous nature of property lease provisions (net of any sub-letting opportunity) on a discounted basis, where due to the reduced requirement for space due to the redundancy programme there is additional surplus capacity. During the year, additional provision has been made for costs as further restructuring opportunities related to this major restructuring programme have been identified.

Business exit provision: The provision relates to the cost of exiting businesses through disposal or closure including professional fees related to business exits and the costs of separating the businesses being disposed. As described in notes 5 and 6, this includes a provision for costs of disposal for Capita Asset Services.

Capita Asset Services indemnity provision: The Group has agreed a full and final settlement with the Financial Conduct Authority (FCA) regarding the Connaught Income Series 1 Fund (The Fund). Capita Financial Managers Limited (CFM) was the Operator of the Fund until September 2009, when it was replaced by an unrelated company as Operator, following which CFM had no further involvement with the Fund. The Fund went into liquidation in 2012 and its liquidator brought a claim against both former Operators, which for its part, Capita settled in 2016 for a sum of £18.5m.

The FCA had been undertaking a formal review of the activities of both Operators and has announced that its conclusion is that CFM did not meet all of its regulatory requirements in the period April 2008 to September 2009. To ensure that investors receive appropriate redress and to bring this matter to a close enabling the smooth disposal of CFM, CFM and Capita have agreed a full and final settlement with the FCA. In reaching this settlement, the full cooperation which CFM has given to the FCA during the course of its investigation has been acknowledged.

CFM has agreed to a further £66.0m being made available for the benefit of the Fund's investors, with Capita agreeing to fund this amount. The FCA considers that this payment will be sufficient to return the amount originally invested, taking into account any interest, distributions and other payments that have already been received, with the intention of placing investors as closely as possible back into the position they would have been in if they had never invested in the Fund. Capita is expecting to make redress payments to the Fund's investors via the FCA and their agents during the first half of 2018.

This settlement allows for the available funds to be directed towards the Fund's Investors. Given the circumstances, the FCA do not consider that it would be appropriate to require CFM to pay a financial penalty.

As the FCA had previously indicated to Capita that it was minded to seek a financial penalty against CFM, Capita had made provision for the full potential amount of the financial penalty and associated legal costs of £37.0m as at 30 June 2017. Based on the information available at that time it was not however possible to determine what the ultimate outcome of the FCA investigation would be. That provision was released and £66.8m provided as at 31 December 2017 which is expected to unwind in less than 1 year.

Capita completed the disposal of its Capita Asset Services businesses, including CFM, to the Link Group on 3 November 2017. Capita plc, as part of the sale of the Capita Asset Services businesses, has provided an indemnity against certain legacy claims. The provisions held, namely the Asset Services settlement provision which includes provisions for Arch Cru, Connaught and other legacy claims, have therefore been retained within the Group. Giving due consideration to these claims, the Group has a provision of £69.1m (including the £66.8m above) at 31 December 2017 (31 December 2016: £23.1m).

Claims and litigation provision: In addition to the Capita Asset Services Indemnity provision, the Group is exposed to other claims and litigation. The Group makes a provision when a claim has been made where it is more probable than not that a loss might occur. These provisions are reassessed regularly to ensure that the level of provisioning is consistent with the claims that have been reported. The range of values attached to these claims, can be significant and, where obligations are probable and estimable, provisions are made representing the Group's best estimate of the expenditure to be incurred. The Group robustly defends its position on each claim and they are often settled for amounts significantly smaller than the initial claim and may result in no transfer of economic benefits. Therefore we do not disclose a range of possible outcomes for these claims.

In the period, the Group has settled a number of liabilities which it had provided for in previous years with the settlements being not materially different to the provisions held as at 31 December 2016. Additionally, it has made provision for new claims, which originate due to the nature of the Group's activities and revised existing provisions where more information on the progress of the claim has become apparent.

Included in the amounts provided in the year, £30.0m relates to two claims:

1. a contract within the Group's Real Estate & Infrastructure business that was notified to the Group during 2017. The related contract was delivered in 2007; and
2. a contract within the Group's Employee Benefits business where more information on the progress of the claim has become apparent. The related contract was delivered in 2009.

The amount provided in respect of these two claims have been recognised in non-underlying specific items due to their historical nature being tied to previous acquisitions.

The Group's exposure to claims is mitigated by having in place a number of large insurers providing cover for the Group's activities, albeit insurance recoveries are only recognised as an asset at the point the recovery is virtually certain. An asset has been recognised of £5.0m in respect of recoveries under an indemnity, no other recovery assets have been recognised.

Due to the nature of these claims, the Group cannot give an estimate of the period over which this provision will unwind.

Property provision: Includes a provision, on a discounted basis, for the difference between the market value of property leases acquired in 2011 with the Ventura and Vertex Private Sector acquisitions and the lease obligations committed to at the date the leases were signed by the previous owners. This is in accordance with IFRS 3 (revised) which requires the use of fair value measurement. The remaining property provision is made on a discounted basis for the future rent expense and related cost of leasehold property (net of estimated sub-lease income) where the space is vacant or currently not planned to be used for ongoing operations. The expectation is that this expenditure will be incurred over the remaining periods of the leases which range from 1 to 24 years.

Other provisions: Relates to provisions in respect of other potential exposures arising due to the nature of some of the operations that the Group provides. These are likely to unwind over a period of 1 to 10 years.

28 FINANCIAL INSTRUMENTS

Financial risk management objectives and policies

The Group's principal financial instruments are comprised of cash, bank loans, loan notes, finance leases and derivatives. The main purpose of these financial instruments is to raise finance for the Group's operations and to manage the Group's financial risks. The Group also has various other financial instruments such as trade receivables and trade payables which arise directly from its operations.

The Group enters into interest rate swaps, currency swaps, fixed rate interest rate swaps and forward currency contracts. The purpose of these transactions is to manage the interest rate and currency risks arising from the Group's operations and its sources of finance. It is, and has been throughout the period under review, the Group's policy that no speculative trading in financial instruments shall be undertaken.

The main risks arising from the Group's financial instruments are interest rate risk, foreign currency risk, credit risk and liquidity risk. The Board reviews and agrees policies for managing each of these risks and they are summarised below.

Carrying values and fair values of financial instruments

The following table analyses by classification and category the carrying value of the Group's financial instruments (excluding short-term debtors, creditors, fund payables/receivables and cash in hand) that are carried in the financial statements. The carrying values are a reasonable approximation of fair value other than 12 fixed rate loan notes totalling £604.4m, included below in the loan note value of £1,664.0m, with a carrying value of £604.4m and a fair value of £629.2m. The fair value of these loan notes has been calculated by discounting the expected future cash flows at prevailing interest rates and this fair value measurement would be categorised within level 2 of the fair value hierarchy.

At 31 December 2017	Available-for-sale £m	At fair value through the income statement £m	Loans and receivables £m	Derivatives used for hedging £m	Other financial liabilities £m	Total £m
Financial assets						
Available-for-sale assets	4.6	–	–	–	–	4.6
Deferred consideration	–	–	5.2	–	–	5.2
Insurance asset recoverable	–	–	5.0	–	–	5.0
Cash flow hedges	–	–	–	7.8	–	7.8
Non-designated foreign exchange forwards and swaps	–	7.7	–	–	–	7.7
Interest rate swaps in relation to GBP denominated loan notes	–	–	–	5.4	–	5.4
Currency swaps in relation to USD denominated loan notes	–	–	–	185.3	–	185.3
	4.6	7.7	10.2	198.5	–	221.0
Financial liabilities						
Overdraft	–	–	–	–	443.3	443.3
Private placement loan notes	–	–	–	–	1,664.0	1,664.0
Other loan notes					0.3	0.3
Term loan	–	–	–	–	100.0	100.0
Cash flow hedges	–	–	–	2.7	–	2.7
Non-designated foreign exchange forwards and swaps	–	0.3	–	–	–	0.3
Currency swaps in relation to USD denominated loan notes	–	–	–	8.5	–	8.5
Contingent consideration	–	–	–	–	24.6	24.6
Deferred consideration	–	–	–	–	13.1	13.1
Obligations under finance leases	–	–	–	–	0.2	0.2
Public sector subsidiary partnership payment	–	–	–	–	51.2	51.2
Put options of non-controlling interests	–	–	–	–	122.4	122.4
	–	0.3	–	11.2	2,419.1	2,430.6

The aggregate loan note value above of £1,664.0m includes the GBP value of the USD denominated loan notes at 31 December 2017. To remove the Group's exposure to currency fluctuations it has entered into currency swaps which effectively hedge the movement in the loan notes' fair value due to changes in prevailing foreign exchange and interest rates. The interest rate swap is being used to hedge the exposure to changes in the fair value of GBP denominated loan notes. The fair values of the currency and interest swaps are disclosed in note 19 – Financial assets and in note 24 – Financial liabilities.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

28 FINANCIAL INSTRUMENTS CONTINUED

At 31 December 2016	Available-for-sale £m	At fair value through the income statement £m	Loans and receivables £m	Derivatives used for hedging £m	Other financial liabilities £m	Total £m
Financial assets						
Available-for-sale assets	5.6	–	–	–	–	5.6
Investment loan	–	–	5.0	–	–	5.0
Investment	–	–	4.0	–	–	4.0
Deferred consideration	–	–	17.0	–	–	17.0
Insurance asset recoverable	–	–	15.5	–	–	15.5
Cash flow hedges	–	–	–	7.0	–	7.0
Non-designated foreign exchange forwards and swaps	–	7.4	–	–	–	7.4
Interest rate swaps in relation to GBP denominated loan notes	–	–	–	7.7	–	7.7
Currency swaps in relation to USD denominated loan notes	–	–	–	361.0	–	361.0
	5.6	7.4	41.5	375.7	–	430.2
Financial liabilities						
Overdraft	–	–	–	–	532.5	532.5
Private placement loan notes	–	–	–	–	1,961.7	1,961.7
Other loan notes	–	–	–	–	0.3	0.3
Term loan	–	–	–	–	650.0	650.0
Cash flow hedges	–	–	–	4.2	–	4.2
Non-designated foreign exchange forwards and swaps	–	3.3	–	–	–	3.3
Foreign exchange swaps held for foreign net investment	–	–	–	0.1	–	0.1
Currency swaps in relation to USD denominated loan notes	–	–	–	3.1	–	3.1
Contingent consideration	–	–	–	–	23.0	23.0
Deferred consideration	–	–	–	–	10.8	10.8
Obligations under finance leases	–	–	–	–	2.3	2.3
Public sector subsidiary partnership payment	–	–	–	–	58.8	58.8
Put options of non-controlling interests	–	–	–	–	115.9	115.9
Fixed rate interest rate swaps	–	85.1	–	–	–	85.1
	–	88.4	–	7.4	3,355.3	3,451.1

The fair value of financial instruments has been calculated by discounting the expected future cash flows at prevailing interest rates, except for available-for-sale assets (which are unlisted equity securities) and investment loans. The valuation models incorporate various inputs including foreign exchange spot and forward rates and interest rate curves. Unlisted equity securities and investment loans are held at amortised cost. The Group enters into derivative financial instruments with multiple counterparties, all of which are financial institutions with investment grade credit ratings.

Fair value hierarchy

The Group uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities

Level 2: other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly

Level 3: techniques which use inputs which have a significant effect on the recorded fair value that are not based on observable market data.

28 FINANCIAL INSTRUMENTS CONTINUED

As at 31 December 2017, the Group held the following financial instruments measured at fair value:

	2017 £m	2016 £m
Assets measured at fair value		
Disposal group assets held for sale	5.9	–
Non-designated foreign exchange forwards and swaps	7.7	7.4
Cash flow hedges	7.8	7.0
Interest rate swaps in relation to GBP denominated loan notes	5.4	7.7
Currency swaps in relation to USD denominated loan notes	185.3	361.0
Liabilities measured at fair value		
Disposal group liabilities held for sale	1.4	–
Private placement loan notes	1,059.6	1,368.6
Cash flow hedges	2.7	4.2
Non-designated foreign exchange forwards and swaps	0.3	3.3
Currency swaps in relation to USD denominated loan notes	8.5	3.1
Fixed rate interest rate swaps	–	85.1
Public sector subsidiary partnership payment	51.2	58.8
Put options of non-controlling interests	122.4	115.9
Contingent consideration	24.6	23.0

In 2016 and 2017, the Group only had Level 2 assets or liabilities measured at fair value apart from disposal group assets and liabilities held for sale, contingent consideration, the public sector subsidiary partnership payment and the put options of non-controlling interests which are Level 3 liabilities. It is the Group's policy to recognise transfers between levels of the fair value hierarchy at the end of the reporting period during which the transfer occurred. During the year ended 31 December 2017, there were no transfers between Level 1 and Level 2 fair value measurements and no transfers into or out of Level 3 fair value measurements.

Contingent consideration arises in business acquisitions where the Group has agreed to pay the vendors additional consideration dependent on the achievement of performance targets in the periods post acquisition. These performance periods are of up to 3 years in duration and will be settled in cash and loan notes on their payment date on achieving the relevant target. The Group makes provision for such contingent consideration for each acquisition based on an assessment of its fair value at the acquisition date. Contingent consideration has been calculated based on the Group's expectation of what it will pay in relation to the post-acquisition performance of the acquired entities by weighting the probability of a range of payments to give an estimate of the final obligation. A sensitivity analysis was performed on the expected contingent consideration of £24.6m. The sensitivity analysis performed adjusted the probability of payment of the contingent amounts. A 10% increase in the probability of contingent consideration being paid results in an increase in potential contingent consideration of £2.9m. A 10% decrease in the probability of the contingent consideration being paid results in a decrease in potential contingent consideration of £2.7m.

The public sector subsidiary partnership payment liability is an estimate of the aggregate of annual payments to be made by AXELOS Limited (the partnership formed with the Cabinet Office) to the Cabinet Office in the years 2018 to 2023. The amount is sensitive to movements in profitability, however there is a cap above which further movement does not impact value. In all reasonably plausible scenarios the cap is reached and therefore the sensitivity is nil. This payment is funded by AXELOS Limited and the carrying value of £51.2m has been derived by discounting the expected payment to arrive at its present value.

The put options of the non-controlling interests (see note 24) are measured at fair value based on the expected redemption value of the shares that will be paid in cash by the Group. This value is determined by reference to the expected date of exercise of the options, which is then discounted to arrive at a present value. The sensitivity of the valuation to movements in both the discount rate and the cash flows that have been used to calculate it, are as follows: a 10% increase/decrease in the earnings potential of the business results in a £12.0m increase/decrease in the valuation; a 1% increase/decrease in the discount rate applied to the valuation results in a £1.5m decrease/increase in the valuation.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

28 FINANCIAL INSTRUMENTS CONTINUED

The following table shows the reconciliation from the opening balances to the closing balances for Level 3 fair values.

	Contingent consideration £m	Subsidiary partnership payment £m	Put options of non-controlling interests £m	Disposal group held for sale – assets £m	Disposal group held for sale – liabilities £m
At 1 January 2017	23.0	58.8	115.9	–	–
Arising from business combinations in the period	6.4	–	–	–	–
Profit and loss movement – administrative expenses	(2.5)	–	–	–	–
Utilised	(2.3)	(9.4)	–	–	–
Movement of put options recognised in equity	–	–	6.5	–	–
Fair value of assets and liabilities transferred to disposal group	–	–	–	(5.9)	1.4
Discount unwind	–	1.8	–	–	–
At 31 December 2017	24.6	51.2	122.4	(5.9)	1.4

Interest rate risk

The Group's exposure to changes in market interest rates arises primarily from the Group's loan notes.

The Group's policy is to manage its interest cost using a mix of fixed and variable rate financial instruments to generate the desired interest rate profile and to manage its exposure to interest rate fluctuations.

The Group has issued fixed rate USD denominated loan notes, which have been swapped to floating rate GBP liabilities at the date of issuance using currency swaps. These currency swaps are designated as fair value hedges against changes in the fair value of the loan notes due to changes in prevailing foreign currency exchange and interest rates.

The Group executed a series of fixed rate interest rate swaps to convert from paying floating rate GBP interest to fixed rate GBP interest on certain of its swapped loan notes. These fixed rate interest rate swaps were not designated in any hedge relationship so their change in fair value was recognised in net finance costs in the income statement – see note 10 – Net finance costs.

Due to lower prevailing interest rates, these fixed rate interest rate swaps had a negative mark-to-market value of £85.1m at 31 December 2016. In February 2017, the Group elected to terminate these fixed rate swaps at a mark-to-market gain of £0.5m recognised in the year.

The Group has fixed rate loan notes of £604.4m in issue as at 31 December 2017 (underlying nominal value). The Group has a further £879.8m of swapped loan notes (underlying nominal value), £100.0m of term loans and a £600.0m undrawn committed revolving credit facility, all paying floating rate interest based on LIBOR. This gives the Group, as a whole, an acceptable interest rate risk profile.

The interest rate profile of the interest-bearing financial assets and liabilities of the Group as at 31 December is as follows:

At 31 December 2017	Within 1 year £m	Between 1–2 years £m	Between 2–3 years £m	Between 3–4 years £m	Between 4–5 years £m	More than 5 years £m	Total £m
Fixed rate							
Private placement loan notes	–	–	124.5	48.2	243.9	186.2	602.8
Obligations under finance leases	0.2	–	–	–	–	–	0.2
Floating rate							
Cash in hand	(921.7)	–	–	–	–	–	(921.7)
Overdraft	443.3	–	–	–	–	–	443.3
Deferred consideration	(3.0)	(2.2)	–	–	–	–	(5.2)
Private placement loan notes	224.1	112.7	194.7	275.7	78.1	175.9	1,061.2
Term loan	–	100.0	–	–	–	–	100.0
Cash flow hedges	(2.5)	(2.6)	–	–	–	–	(5.1)
Non-designated foreign exchange forwards and swaps	(3.8)	(1.8)	(1.8)	–	–	–	(7.4)
Interest rate swap in relation to GBP denominated loan notes	–	(2.4)	–	(3.0)	–	–	(5.4)
Currency swaps in relation to USD denominated loan notes	(72.2)	(10.1)	(26.3)	(37.8)	(12.5)	(17.9)	(176.8)

28 FINANCIAL INSTRUMENTS CONTINUED

At 31 December 2016	Within 1 year £m	Between 1–2 years £m	Between 2–3 years £m	Between 3–4 years £m	Between 4–5 years £m	More than 5 years £m	Total £m
Fixed rate							
Private placement loan notes	151.1	222.5	122.0	329.7	250.6	472.5	1,548.4
Obligations under finance leases	2.2	0.1	–	–	–	–	2.3
Interest rate swap in relation to GBP denominated loan notes	–	–	(3.8)	–	–	–	(3.8)
Currency swaps in relation to USD denominated loan notes	(60.4)	(94.7)	(17.7)	(43.6)	(54.6)	(13.1)	(284.1)
Fixed rate interest rate swaps	1.5	7.0	10.5	22.9	18.8	24.4	85.1
Floating rate							
Cash in hand	(1,098.3)	–	–	–	–	–	(1,098.3)
Overdraft	532.5	–	–	–	–	–	532.5
Investment loan	–	(0.5)	(0.3)	(0.3)	(0.4)	(3.5)	(5.0)
Deferred consideration	(6.0)	(6.0)	(5.0)	–	–	–	(17.0)
Private placement loan notes	40.9	33.1	–	9.8	101.7	227.8	413.3
Term loan	–	550.0	100.0	–	–	–	650.0
Cash flow hedges	0.3	(1.7)	(1.4)	–	–	–	(2.8)
Non-designated foreign exchange forwards and swaps	0.1	(2.5)	(0.9)	(0.8)	–	–	(4.1)
Foreign exchange swaps in respect of foreign net investment	0.1	–	–	–	–	–	0.1
Interest rate swap in relation to GBP denominated loan notes	–	–	–	–	(3.9)	–	(3.9)
Currency swaps in relation to USD denominated loan notes	(6.8)	(8.1)	–	(2.1)	(11.3)	(45.5)	(73.8)

The following table demonstrates the sensitivity to a reasonably possible change in interest rates, with all other variables held constant, of the Group's profit before tax (through the impact on floating rate borrowings). There is no impact on the Group's equity.

	Increase/(decrease) in basis points			Effect on profit before tax £m
2017	(30)	30	1.5	(1.5)
2016	(5)	5	0.2	(0.2)

Foreign currency risk

The Group has exposure to foreign currency risk where it has cash flows in overseas operations and foreign currency transactions in UK operations which are affected by foreign exchange movements. The Group is not generally exposed to significant foreign currency risk except in respect of its cash flows in overseas operations in Europe, India and South Africa which generate exposure to movements in the euro, Swiss franc, Indian rupee and South African rand exchange rates against sterling. The Group seeks to mitigate the effect of this exposure by entering forward currency contracts (including Non-deliverable Forward Contracts (NDFs)) to fix the GBP cost of highly probable forecast transactions denominated in Indian rupee and South African rand.

It is the Group's policy to negotiate the terms of the hedge derivatives to match the terms of the underlying cash flows in order to maximise hedge effectiveness.

At 31 December 2017, the Group held foreign exchange forwards against forecast monthly Indian rupee and South African rand costs expected in years up to and including 2022. These forecast costs have been determined on the basis of the underlying cash flows associated with the delivery of services under signed customer contracts.

The following table demonstrates the sensitivity to a reasonably possible change in the Indian rupee and South African rand exchange rates, with all other variables held constant, of the Group's profit before tax and the Group's equity due to changes in the fair value of the Group's forward exchange contracts.

	South African rand			Indian rupee		
	Increase/(decrease) in ZAR exchange rate	Effect on profit before tax £m	Effect on equity £m	Increase/(decrease) in INR exchange rate	Effect on profit before tax £m	Effect on equity £m
2017	14.15%	(2.8)	–	2.71%	–	(2.4)
2016	10.01%	(3.4)	–	3.09%	–	(4.4)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

28 FINANCIAL INSTRUMENTS CONTINUED

Hedges

Fair value hedges

The Group has in issue fixed rate dollar and sterling loan notes which it has hedged through a combination of interest rate and currency swaps.

The Group had interest rate swaps in place with a notional amount of £85.0m (2016: £85.0m) whereby it receives a weighted average fixed rate of interest of 4.81% (2016: fixed rate of interest 4.81%) and pays variable rates based on 6-month GBP LIBOR. The swaps are being used to hedge the exposure to changes in the fair value of £85.0m (2016: £85.0m) of the Group's loan notes.

The Group had in place currency swaps whereby it receives a fixed rate of interest and pays a variable rate based on 6-month GBP LIBOR. The currency swaps are being used to hedge the exposure to changes in the fair value of £794.8m (2016: £918.9m) of the Group's loan notes, which have coupon rates ranging from 3.03% to 6.51%.

The currency swaps are being used to hedge the exposure to changes in the fair value of its US dollar denominated loan notes. The loan notes, currency and interest rate swaps have the same critical terms including the amount and the date of maturity (see note 24).

The total loss in the year on the fair value hedges of £184.0m (2016: total gain £145.8m), excluding credit risk, was equal to the gain/loss on the hedged items resulting in no net gain or loss in the income statement apart from hedge ineffectiveness from credit risk and currency basis risk totalling £0.6m credit (2016: £1.0m debit) to the income statement – shown in net finance costs – note 10.

The Group may, at its option, upon notice of not less than 30 days and not more than 60 days, repay at any time all or part of the notes at no more than the present value of future payments.

Cash flow hedges

As noted above, the Group holds a series of forward exchange currency contracts in the form of NDFs designated as hedges of highly probable forecast transactions in INR of the Group's Indian operations.

	2017		2016	
Forward exchange contracts	Assets £m	Liabilities £m	Assets £m	Liabilities £m
Fair value	7.8	(2.7)	7.0	(4.2)

The terms of the forward currency contracts have been negotiated to match the terms of the commitments.

The cash flow hedges are in respect of highly probable forecast monthly costs, based on long-term contracts that the Group has in place, denominated in INR up to 2019. These were assessed to be highly effective as at 31 December 2017 and a net unrealised gain of £5.1m (2016: gain of £2.8m) less income tax credit of £3.2m (2016: credit of £2.8m) was recognised in equity. The net gain recognised on cash flow hedges during the year was £2.0m (2016: net gain £14.3m) whilst net losses of £0.3m (2016: losses of £3.3m) were reclassified to the income statement and included in administrative expenses. The tax effect of the net movement in cash flow hedges during the year was a debit to OCI of £0.4m (2016: debit of £5.6m).

In addition, the Group holds a series of forward exchange currency contracts against highly probable forecast transactions in ZAR of the Group's South African operations. The Group does not designate these hedges as cash flow hedges under IFRS. All gains or losses on these outstanding hedges are recognised in the income statement in net finance costs (see note 10).

Hedges of net investments in foreign operations

The Group has net investments in foreign operations, the re-translation of which on consolidation gives rise to exposure to the carrying values in equity. Until November 2017, the Group designated EUR97.0m of liability under its borrowings in EUR denominated loan notes as a hedge of a net investment in its EUR denominated foreign operations. In addition, the Group designated CHF110.0m of foreign exchange forwards and swaps as a hedge of net investment in its Swiss franc denominated foreign operations. Following the disposal of Capita Asset Services and the assessment of carrying values of intangible assets including goodwill, in November 2017 the Group decided to cease designation of net investment hedges for its foreign operations.

Credit risk

The Group trades only with recognised, creditworthy third parties. It is the Group's policy that all clients who wish to trade on credit terms are subject to credit verification procedures. In addition, receivable balances are monitored on an ongoing basis with the result that the Group's exposure to bad debts is not significant.

With respect to credit risk arising from the other financial assets of the Group, such as cash and cash equivalents, available-for-sale financial investments, investment loan and certain derivative instruments, the Group's exposure to credit risk arises from the risk of a default of the counterparty. The Group manages its operations to avoid any excessive concentration of counterparty risk and the Group takes all reasonable steps to seek assurance from the counterparties to ensure that they can fulfil their obligations.

The Group has a maximum exposure equal to the carrying amount of the above receivables and instruments.

The mark-to-market movement on derivatives includes the extent to which the fair value of these instruments has been affected by the perceived change in the creditworthiness of the counterparties to those instruments and that of the Group itself (own credit risk). The Group is comfortable that the risk attached to those counterparties is not significant and believes that the currency swaps continue to act as an effective hedge against the movements in the fair value of the Group's issued USD denominated loan notes.

Liquidity risk

The Group's policy is to hold cash and undrawn committed facilities at a level sufficient to fund the Group's operations and its medium-term plans. The Group holds cash and undrawn committed facilities and makes use of non-recourse trade receivable arrangements to enable the Group to manage its liquidity risk.

The Group monitors its risk to a shortage of funds using a daily cash management process. This process considers the maturity of both the Group's financial investments and financial assets (e.g. accounts receivable, other financial assets) and projected cash flows from operations.

The Group's objective is to maintain a balance between continuity of funding and flexibility through the use of multiple sources of funding including loan notes, bank loans, term loans, cash, overdrafts and finance leases over a broad spread of maturities to 2027.

28 FINANCIAL INSTRUMENTS CONTINUED

The table below summarises the maturity profile of the Group's financial liabilities at 31 December 2017 based on contractual undiscounted payments.

At 31 December 2017	Within 1 year £m	Between 1–2 years £m	Between 2–3 years £m	Between 3–4 years £m	Between 4–5 years £m	More than 5 years £m	Total £m
Overdraft	443.3	–	–	–	–	–	443.3
Private placement loan notes	219.0	109.2	310.0	313.6	324.9	363.8	1,640.5
Other loan notes	–	–	0.3	–	–	–	0.3
Interest on above loan notes	65.8	52.4	41.6	33.2	18.6	35.5	247.1
Term loan	–	100.0	–	–	–	–	100.0
Interest on above term loan	1.6	0.6	–	–	–	–	2.2
Contingent consideration	12.1	–	12.5	–	–	–	24.6
Public sector subsidiary partnership payment	9.4	9.4	9.4	9.4	9.4	9.4	56.4
Put options of non-controlling interests	6.8	108.8	–	10.5	–	–	126.1
Obligations under finance leases	0.2	–	–	–	–	–	0.2
Currency swaps	1.4	1.4	1.4	1.4	1.0	2.6	9.2
Non-designated foreign exchange forwards and swaps	0.2	–	–	–	–	–	0.2
Cash flow hedges	1.7	–	–	–	–	–	1.7
	761.5	381.8	375.2	368.1	353.9	411.3	2,651.8

At 31 December 2016	Within 1 year £m	Between 1–2 years £m	Between 2–3 years £m	Between 3–4 years £m	Between 4–5 years £m	More than 5 years £m	Total £m
Overdraft	532.5	–	–	–	–	–	532.5
Private placement loan notes	185.2	239.3	114.7	327.2	335.0	701.4	1,902.8
Other loan notes	0.3	–	–	–	–	–	0.3
Interest on above loan notes	79.1	69.7	55.0	43.5	34.7	55.7	337.7
Term loan	–	550.0	100.0	–	–	–	650.0
Interest on above term loan	9.7	7.4	0.5	–	–	–	17.6
Contingent consideration	3.6	16.7	2.7	–	–	–	23.0
Public sector subsidiary partnership payment	9.4	9.4	9.4	9.4	9.4	18.8	65.8
Put options of non-controlling interests	–	7.6	88.5	–	27.4	–	123.5
Obligations under finance leases	2.2	0.1	–	–	–	–	2.3
Currency swaps	1.4	1.4	1.4	1.4	21.5	44.2	71.3
Fixed rate interest rate swaps	17.9	23.5	21.7	14.8	10.2	12.6	100.7
Non-designated foreign exchange forwards and swaps	3.1	–	–	–	–	–	3.1
Cash flow hedges	0.7	0.6	0.4	–	–	–	1.7
	845.1	925.7	394.3	396.3	438.2	832.7	3,832.3

The above payments have been calculated based on the prevailing foreign exchange rates and interest rates at the end of the reporting period. For currency swaps, only payments are included, receipts are excluded.

Master netting or similar agreements

The Group has notional cash pools with its banks under which the bank may net cash balances with overdrafts held by other members of the Group. The effect of this is shown in the table below.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

28 FINANCIAL INSTRUMENTS CONTINUED

At 31 December 2017	Gross and net amounts of financial instruments in the balance sheet £m	Related financial instruments that are not offset £m	Net amount £m
Financial assets			
Cash at bank	921.7	(387.7)	534.0
Financial liabilities			
Overdrafts	(443.3)	387.7	(55.6)

At 31 December 2016	Gross and net amounts of financial instruments in the balance sheet £m	Related financial instruments that are not offset £m	Net amount £m
Financial assets			
Cash at bank	1,098.3	(529.3)	569.0
Financial liabilities			
Overdrafts	(532.5)	529.3	(3.2)

Capital management

The primary objective of the Group's capital management is to ensure that it maintains a strong credit rating and healthy capital ratios to support its business operations, its acquisition strategy and maximise shareholder value. The Group manages its capital structure, and makes adjustments to it, in the light of changes in economic conditions. To maintain or adjust the capital structure, the Group may adjust the dividend payment to shareholders, return capital to shareholders or issue new shares. Focus on capital management forms an important component of the monthly Board meetings with attention on various matters including: return on capital employed, ensuring a mix of funding sources to ensure continuity and flexibility, a balance between fixed and floating borrowings, a broad spread of maturities and adequate liquidity headroom.

The Group's capital management process ensures that it meets financial covenants in its borrowing arrangements. Breaches in meeting the financial covenants could permit the lenders to immediately accelerate repayment of loans and borrowings. The Group monitors, as part of its monthly Board review, that it will adhere to specified consolidated leverage ratios and consolidated net interest expense coverage ratios. There have been no breaches in the financial covenants of any loans and borrowings in the period.

The Group uses long dated debt, generally loan notes and long-term bank facilities, to enable it to manage refinancing risk and for the general purposes of the Group.

Capita plc supports the growth of its various financial services businesses. These financial firms are subject to various capital requirements imposed by financial services regulators. These requirements do not apply to Capita plc itself and the Group is not required to provide consolidated returns for regulatory purposes. The board of each regulated firm is responsible for ensuring it has embedded capital management frameworks that test there are adequate financial resources at all times. During the year, they complied with all externally imposed financial services regulatory capital requirements.

The Group seeks to maintain a conservative and efficient capital structure with an appropriate level of gearing. In 2017, Group policy was to target an adjusted net debt to adjusted EBITDA ratio in the range of 2.0x to 2.5x over the long term and maintain interest cover above 7.0 times (refer to Alternative Performance Measures on pages 202 to 204). At 31 December 2017, our annualised adjusted net debt to adjusted EBITDA ratio was 2.27x (2016 as reported: 2.89x) with annualised interest cover at 8.6 times (2016 restated: 8.8 times; 2016 as reported: 8.8 times). These ratios are monitored monthly by the Board. As the Group considers an adjusted net debt to adjusted EBITDA ratio the most appropriate measure for gearing, it does not maintain or monitor a targeted debt/equity ratio. Subsequently in January 2018, the Board reappraised the adjusted net debt to adjusted EBITDA target range. The Group's transformation plan includes an assessment of the appropriate financial leverage for the Group over the medium term, to ensure that it has a sustainable capital base to support its clients and operations, increase investment in the business and deliver its future strategy. Whilst the outcome of the transformation plan has yet to be finalised, the Board's preliminary view is that the appropriate financial leverage for Capita over the medium term should be an adjusted net debt to adjusted EBITDA ratio of between 1.0x and 2.0x (prior to the adoption of IFRS 16).

The Group's debt facilities include typical ongoing maintenance obligations, a covenant test connected with the indebtedness within the Group. The covenant test places restrictions on the level of liens and indebtedness permitted outside a group of guarantor companies as defined within the debt agreements. The Company agreed amendments with the debt holders, including a waiver over this covenant test in its private placement loan notes from 1 January 2018 to 12 May 2018. The Group has procedures in place to ensure ongoing compliance with the maintenance tests, including presentations to the Board confirming the work undertaken, and the key conclusions reached. The Group is satisfied that the procedures in place ensure ongoing full compliance with the covenants.

The Group raises debt in a number of markets including the bank loan market, bank overdraft, finance lease and private placement markets. The Group has available to it a committed Revolving Credit Facility of £600m of which £81m matures in August 2020 and £519m matures in August 2021. £nil was drawn down as at 31 December 2017 (2016: £nil). This facility is available for the Group's immediate use.

Consistent with prior years, the Group makes use of non-recourse trade receivable financing arrangements provided to it by a number of its relationship banks. £110.0m of receivables had been sold under these arrangements and had not been settled as at 31 December 2017 (2016: £133.6m). As these trade receivables have been sold without recourse the Group does not consider them to be part of its core capital.

During the year, the Group repaid loan notes at maturity totalling £124.1m and repaid £550.0m of bank term loans prior to their maturity (see note 24).

28 FINANCIAL INSTRUMENTS CONTINUED

The Group has a spread of loan note maturities from 2018 to 2027 (see note 24).

On 20 April 2018, Capita agreed the following with the noteholders under its US Private Placement Notes:

- the introduction of a permanent minimum basket size of £50m in relation to subsidiary indebtedness and permitted liens, replacing the above temporary waiver, in line with the corresponding baskets under Capita's other financing arrangements;
- the carve-out of up to £100m worth of bonds and guarantees from the definition of indebtedness;
- certain restructuring costs to be excluded from the calculation of the covenant test, and certain assets to be excluded from the restrictions on disposals; and
- the flexibility to increase the leverage covenant under the terms of the Private Placement Notes from 3.0x to 3.5x if Capita would otherwise breach the covenant as a result of first-year losses from significant new contract wins as a result of the adoption of IFRS 15.

In return for these amendments to the terms of the Private Placement Notes, the noteholders received the following:

- the prepayment of £150m of principal of the Private Placement Notes (plus a make-whole payment currently estimated to be £7m) from the proceeds of the Rights Issue;
- the application of 50% of the net proceeds from future disposals to the prepayment of principal of the Private Placement Notes, with payment of make-whole, until such time as an estimated £315m of Private Placement Notes have been pre-paid; and
- a coupon uplift of 75 basis points, representing approximately £5m of incremental costs through 2018.

The coupon uplift and restrictions on disposals will remain in place until Capita has repaid a total of £520m in principal (USD296m of which represents notes which are due to mature in July and September 2018) under the Private Placement Notes and satisfies a one time only test of leverage being less than 1.5x at the end of a testing period and for two further periods on a look-forward basis.

Given the short-term outlook, level of indebtedness and need to invest for the long-term benefit of the Group, the Board is not recommending the payment of a final dividend and is planning to raise equity by way of a Rights Issue during 2018. The Board does not intend to resume the payment of dividends until the Group is generating sufficient sustainable free cash flow. The precise quantum of the planned Rights Issue has yet to be determined and the Company has entered into a standby underwriting agreement for £701m with Citigroup Global Markets Limited and Goldman Sachs International. Any such fundraising will be supported by a strategic investment case to ensure a capital platform from which the Group can deliver sustainable profitability and cash flows in the future. In addition to the disposal of the majority of the Capita Asset Services businesses and our standalone specialist recruitment businesses which were completed during the year, the Group has identified a small number of businesses that are considered non-core and a disposal programme for these businesses has commenced. The proceeds from the disposals will be used to reduce indebtedness and to invest in the remaining core areas of the business.

The table below presents quantitative data for the componerits the Group manages as capital:

	2017 £m	Restated 2016 £m
Cash in hand	(921.7)	(1,098.3)
Overdraft	443.3	532.5
Other loan notes	0.3	0.3
Obligations under finance leases	0.2	2.3
Private placement loan notes	1,664.0	1,961.7
Term loan	100.0	650.0
Undrawn available Revolving Credit Facility	600.0	600.0
Currency and interest rate swaps	(182.2)	(365.6)
At 31 December	1,703.9	2,282.9

Following the adoption of IFRS 15 Revenue from Contracts with Customers, the Group no longer considers the balance sheet carrying value of shareholders' funds to represent the contribution to capital management from its equity holders and consequently has removed it from the above table.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

29 ISSUED SHARE CAPITAL

Allotted, called up and fully paid	2017 (m)	2016 (m)	2017 £m	2016 £m
Ordinary shares of 2 1/15p each				
At 1 January	670.1	670.0	13.8	13.8
Issued on exercise of share options	–	0.1	–	–
At 31 December	670.1	670.1	13.8	13.8

During the year, nil (2016: 131,037) ordinary 2 1/15p shares with an aggregate nominal value of £nil (2016: £2,708) were issued under share option schemes for a total consideration of £nil (2016: £0.6m).

Treasury shares	2017 (m)	2016 (m)	2017 £m	2016 £m
Ordinary shares of 2 1/15p				
At 1 January	3.2	5.8	(0.1)	(0.2)
Shares allotted in the year	(0.3)	(2.6)	–	0.1
At 31 December	2.9	3.2	(0.1)	(0.1)

In 2017, the Group made no purchases of shares into Treasury and allotted 0.3m (2016: 2.6m) shares with an aggregate nominal value of £4,420 (2016: £53,604). The total consideration received in respect of these shares was £nil (2016: £nil).

Employee benefit trust shares	2017 (m)	2016 (m)	2017 £m	2016 £m
Ordinary shares of 2 1/15p				
At 1 January	1.7	2.2	(0.1)	(0.1)
Shares allotted in the year	(0.1)	(0.5)	–	–
At 31 December	1.6	1.7	(0.1)	(0.1)

The Group will use shares held in the employee benefit trust (EBT) in order to satisfy future requirements for shares under the Group's share option and long term incentive plans. During the year, the EBT allotted 0.1m (2016: 0.5m) ordinary 2 1/15p shares with an aggregate nominal value of £1,434 (2016: £10,372) to satisfy exercises under the Group's share option and long term incentive plans. The total consideration received in respect of these shares was £nil (2016: £nil).

The Group has an unexpired authority to repurchase up to 10% of its issued share capital.

30 SHARE BASED PAYMENT PLANS

The Group operates several share based payment plans. The expense recognised for share based payments in respect of employee services received during the year to 31 December 2017 was £2.9m (2016: £(4.5)m credit), all of which arises from equity-settled share based payment transactions. Details of the schemes are as follows:

Deferred Annual Bonus Plan

This scheme is applicable to Executive Directors and Divisional Executive Directors. The award made in February 2015 in respect of 2014, is only applicable to Executive Directors. Under this scheme, awards are made annually consisting of only Deferred Shares, which are linked to the payout under the Annual Bonus Scheme (details of which are contained in the Directors' remuneration report on pages 75 to 89).

The value of Deferred Shares is determined by the payout under the Annual Bonus Scheme: half of the annual bonus is paid in cash and the remainder is compulsorily deferred into Deferred Shares. Directors have the option to defer up to 100% of their annual bonus into Deferred Shares. The Deferred Shares are held for a period of 3 years from the date of award, during which they are not forfeitable, except in the case of dismissal for gross misconduct.

For awards made in 2014 and earlier, participants were awarded conditional matching awards at the same time as the award of Deferred Shares, where participants received 2 Matching Shares for every Deferred Share. Following the award made in February 2014, it is not planned to award any further matching awards.

The vesting conditions for matching awards made in 2014 were such that 33% of the Matching Shares will vest if growth in the Company's earnings per share (EPS) is equal to growth in the UK Retail Price Index (RPI) plus 4% per annum, rising on a straight-line basis to 100% vesting if growth in the Company's EPS is equal to or greater than growth in the RPI plus 12% per annum.

Long Term Incentive Plan (2008 LTIP)

The 2008 LTIP was approved and adopted at the AGM on 6 May 2008. The vesting of awards will depend on share price growth and EPS growth targets measured over a 3-year period. An award will not vest if Capita's average share price at the date of vesting is below the average share price at the date of grant. This scheme is open to all senior employees and shares will vest according to performance criteria. The number of shares which will vest is dependent upon the Company's EPS growth exceeding RPI growth by 4% and on banding within the scheme. For awards granted in 2014 and 2015, the number of shares which will vest is dependent upon the Company's EPS growth exceeding RPI growth by 4%, the Company's Return on Capital Employed exceeding 14%, and on banding within the scheme.

1997 Executive Share Option Scheme

This scheme is open to senior employees other than Executive Directors and Divisional Executive Directors. The exercise price of the options is equal to the market price of the shares on the date of grant. Options granted under this scheme become exercisable if the growth in the Company's EPS exceeds the growth in RPI by 8% over the 3-year vesting period from the date of grant. The contractual life of each option granted is 7 years. There are no cash settlement alternatives.

30 SHARE BASED PAYMENT PLANS CONTINUED

Capita Sharesave Scheme

This is an employee Save As You Earn scheme open to all Capita employees. Under this scheme, employees are granted share options at the market price at the date of grant. The options become exercisable for a 6-month period following completion of a 3-year savings period. There are no performance conditions attached to these options.

The following table illustrates the number and weighted average exercise prices (WAEP) of, and movements in, share options during the year:

Share options (1997 Executive Share Option Scheme and Capita Sharesave Scheme)

	2017 (m)	2017 WAEP	2016 (m)	2016 WAEP
Outstanding as at 1 January	0.1	£6.83	0.2	£6.45
Granted during the year	–	–	–	–
Exercised	–	–	(0.1)	£6.30
Forfeited	(0.1)	£6.83	–	£4.39
Expired during the year	–	–	–	–
Outstanding as at 31 December	–	–	0.1	£6.83
Exercisable at 31 December	–	–	0.1	£6.83

The weighted average remaining contractual life of the above shares outstanding at 31 December 2017 was nil years (2016: 0.3 years).

2008 LTIP

	2017 (m)	2017 WAEP	2016 (m)	2016 WAEP
Outstanding as at 1 January	8.7	–	8.9	–
Awarded during the year	4.6	–	3.9	–
Exercised	–	–	(2.4)	–
Forfeited	(4.4)	–	(1.7)	–
Outstanding as at 31 December	8.9	–	8.7	–
Exercisable at 31 December	–	–	–	–

The weighted average remaining contractual life of the above shares outstanding at 31 December 2017 was 1.6 years (2016: 1.4 years). There are no exercise prices for any options issued under the 2008 LTIP scheme.

Deferred Annual Bonus Plan

The weighted average share price of options at the date of exercise in 2017 was £5.79. The options have been exercised primarily in the first half of the year and the weighted average share price during the year was £5.62 (2016: £9.20).

The total cash value of the Deferred Shares awarded during the year was £nil (2016: £1.0m). The Matching Shares allocation in respect of the 2016 awards under this plan charged in 2017 was £nil (2016: £nil).

All Schemes

The fair value of the options granted/awarded during the year was £4.37 (2016: £5.01). None of the existing option schemes have exercise prices.

The fair value of equity-settled share options granted pre 2017 is estimated as at the date of grant using a multiple simulation option pricing valuation model, taking into account the terms and conditions upon which the options were granted.

The following table lists the inputs to the model used for the years ended 31 December 2017 and 31 December 2016.

	2017	2016
Dividend yield (%)	–	2.49
Expected share price volatility (%)	–	20.78
Floor price for LTIP (applicable to LTIP 08)	–	£10.30
Risk-free interest rate (%)	–	0.41
Expected life of option (years)	–	3.00
Weighted average share price of options granted during the year	–	–

The fair value for the 2017 share scheme issues is effectively the market price of a Capita share at the date of grant. Accordingly, no assumptions have been disclosed in the table above.

The expected life of the options is based on historical data and is not necessarily indicative of exercise patterns that may occur. The expected volatility reflects the assumption that the historical volatility is indicative of future trends, which may also not necessarily be the actual outcome. In addition, within the 2008 LTIP is an average share price floor under which the share award will not vest. This floor is based on the Company's average share price at the date of vesting. No other features of options grant were incorporated into the measurement of fair value.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

31 ADDITIONAL CASH FLOW INFORMATION

Operating cash flow for the year ended 31 December 2017

		2017			Restated 2016		
	Note	Continuing operations £m	Discontinued operations £m	Total £m	Continuing operations £m	Discontinued operations £m	Total £m
Cash flows from operating activities							
Operating profit before interest and tax		(420.1)	(18.6)	(438.7)	(16.1)	42.3	26.2
Adjustment for underlying non-cash items:							
Depreciation	14	63.5	6.3	69.8	72.1	9.8	81.9
Amortisation of intangible assets (treated as depreciation)	15	19.9	1.9	21.8	15.4	2.0	17.4
Share based payment expense	30	2.9	–	2.9	(4.5)	–	(4.5)
Employee benefits	34	1.0	–	1.0	(4.1)	–	(4.1)
(Profit)/loss on sale of property, plant and equipment/ intangible assets	8	0.5	–	0.5	0.8	–	0.8
Adjustments for business exit non-cash items:							
Accelerated depreciation/amortisation on business exit	4	1.9	–	1.9	–	–	–
Other assets written-off on business exit	4	–	–	–	(1.3)	–	(1.3)
Business exit provision	27	33.5	–	33.5	(2.7)	–	(2.7)
Adjustment for specific item non-cash items:							
Capita Asset Services businesses settlement provision	27	3.4	63.4	66.8	9.5	13.4	22.9
Re-measurement of businesses held for disposal	4	8.6	–	8.6	–	–	–
Amortisation of intangible assets recognised on acquisition	6,17	124.3	0.6	124.9	148.3	3.9	152.2
Impairment of contract related assets and investment loan	6	128.2	–	128.2	60.9	–	60.9
Impairment of goodwill	6	551.6	–	551.6	66.6	–	66.6
Impairment of intangibles acquired in business combinations	15	14.0	–	14.0	14.7	–	14.7
Contingent consideration	6	(2.5)	–	(2.5)	1.2	–	1.2
Co-op dispute costs	6	–	–	–	18.4	–	18.4
Professional fees on acquisitions	6	0.5	–	0.5	–	–	–
Movement in underlying provisions (net)	27	(22.6)	(1.1)	(23.7)	51.1	–	51.1
Movements in working capital:							
Trade and other receivables		(116.6)	45.0	(71.6)	(63.2)	1.0	(62.2)
Trade and other payables		(116.5)	(80.8)	(197.3)	46.2	19.1	65.3
Deferred income and contract fulfilment assets		(78.7)	3.4	(75.3)	237.0	(2.3)	234.7
Cash generated from operations before non-underlying cash items (see cash flow statement)		196.8	20.1	216.9	650.3	89.2	739.5
Income tax paid		9.5	(3.2)	6.3	(53.7)	(10.0)	(63.7)
Net interest paid		(54.2)	0.1	(54.1)	(59.6)	0.2	(59.4)
Purchase of property, plant and equipment	14	(66.2)	(2.7)	(68.9)	(74.0)	(8.4)	(82.4)
Purchase of intangible assets	15	(71.0)	(1.9)	(72.9)	(66.3)	(5.9)	(72.2)
Proceeds from sale of property, plant and equipment/ intangible assets		23.1		23.1	0.6	–	0.6
Underlying free cash flow		38.0	12.4	50.4	397.3	65.1	462.4

31 ADDITIONAL CASH FLOW INFORMATION CONTINUED

Reconciliation of net cash flow to movement in net funds/(debt)

	Net debt at 1 January 2017 £m	Cash flow movements £m	Non-cash flow movements: Acquisitions in 2016 £m	Foreign exchange movements £m	Fair value changes £m	Other[2] £m	Net debt at 31 December 2017 £m
Cash, cash equivalents and overdrafts	565.8	(90.5)	–	3.1	–	–	478.4
Other loan notes	(0.3)	–	–	–	–	–	(0.3)
Private placement loan notes[1]	(1,961.7)	126.2	–	(10.7)	184.0	(1.8)	(1,664.0)
Interest and currency swaps in relation to USD denominated private placement loan notes[1]	357.9	–	–	–	(181.1)	–	176.8
Interest rate swaps in relation to GBP denominated private placement loan notes[1]	7.7	–	–	–	(2.3)	–	5.4
Term loan	(650.0)	550.0	–	–	–	–	(100.0)
Finance leases	(2.3)	2.1	–	–	–	–	(0.2)
Total net liabilities from financing activities	(2,248.7)	678.3	–	(10.7)	0.6	(1.8)	(1,582.3)
Underlying net debt	(1,682.9)	587.8	–	(7.6)	0.6	(1.8)	(1,103.9)
Fixed rate interest rate swaps	(85.1)	84.6	–	–	0.5	–	–
Deferred consideration	(10.8)	10.8	(2.0)	–	–	(11.1)	(13.1)
Net debt	(1,778.8)	683.2	(2.0)	(7.6)	1.1	(12.9)	(1,117.0)

1 The sum of these items held at fair value equates to the underlying value of the Group's private placement loan note's debt of £1,481.8m (2016: £1,596.1m). Cash flow movement in private placement loan notes includes both repayment of private placement loan notes of £(124.1)m and financing arrangement costs of £(2.1)m.

2 Other comprises the amortisation of loan note issue costs, the amortisation of the discount on the euro debt issue, and deferred consideration in relation to the acquisition of the remaining shares in Capita Birmingham Limited.

The aggregate private placement loan note's fair value above of £1,664.0m (2016: £1,961.7m) (disclosed in note 24 – Financial liabilities) includes the GBP value of the USD denominated loan notes at 31 December 2017. To remove the Group's exposure to currency fluctuations it has entered into currency swaps which effectively hedge the movement in the underlying loan notes' fair value. The interest rate swap is being used to hedge the exposure to changes in the fair value of GBP denominated private placement loan notes.

The combined fair value of the interest and currency swaps, of £182.2m (2016: £365.6m), is disclosed in note 19 – Financial assets, and in note 24 – Financial liabilities.

	Net debt at 1 January 2016 £m	Cash flow movements £m	Non-cash flow movements: Acquisitions in 2015 £m	Foreign exchange movements £m	Fair value changes £m	Amortisation of bond issue costs £m	Net debt at 31 December 2016 £m
Cash, cash equivalents and overdrafts	85.3	467.6	–	12.9	–	–	565.8
Other loan notes	–	(0.3)	–	–	–	–	(0.3)
Private placement loan notes[1]	(1,749.4)	(29.2)	–	(36.0)	(145.8)	(1.3)	(1,961.7)
Interest and currency swaps in relation to USD denominated private placement loan notes[1]	213.9	–	–	–	144.0	–	357.9
Interest rate swaps in relation to GBP denominated private placement loan notes[1]	6.9	–	–	–	0.8	–	7.7
Long-term debt	–	–	–	–	–	–	–
Term loan	(300.0)	(350.0)	–	–	–	–	(650.0)
Finance leases	(7.0)	5.5	(0.8)	–	–	–	(2.3)
Total net liabilities from financing activities	(1,835.6)	(374.0)	(0.8)	(36.0)	(1.0)	(1.3)	(2,248.7)
Underlying net debt	(1,750.3)	93.6	(0.8)	(23.1)	(1.0)	(1.3)	(1,682.9)
Fixed rate interest rate swaps	(67.0)	–	–	–	(18.1)	–	(85.1)
Deferred consideration	(21.5)	10.7	–	–	–	–	(10.8)
	(1,838.8)	104.3	(0.8)	(23.1)	(19.1)	(1.3)	(1,778.8)

1 The sum of these items held at fair value equates to the underlying value of the Group's private placement loan notes debt of £1,596.1m (2015: £1,528.6m). Cash flow movement in private placement loan notes includes issue of private placement loan notes of £170.8m repayment of private placement loan notes of £141.0m and financing arrangement costs of £0.6m.

32 CAPITAL COMMITMENTS

At 31 December 2017, amounts contracted for but not provided in the financial statements for the acquisition of property, plant and equipment amounted to £8.8m, relating to building improvement on a leased property (2016: £10.0m).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

33 CONTINGENT LIABILITIES

Contingent liabilities represent potential future cash outflows which are either not probable or cannot be measured reliably.

The Group has provided, through the normal course of its business, performance bonds and bank guarantees of £88.4m (2016: £91.7m).

One of the Group's major life and pensions clients is conducting a strategic review, the outcome of which is uncertain but could result in the continuation of the contract with amended terms or the termination of the contract. If the operation is terminated, the Group may incur associated costs. As the outcome of the client's review is uncertain, the Group has not made any provision for a future outflow of funds that might result from the eventual outcome.

Capita completed the disposal of its Capita Asset Services businesses, including CFM, to the Link Group on 3 November 2017. Capita plc, as part of the sale of the Capita Asset Services businesses, has provided an indemnity against certain legacy claims.

The Capita Group entities are parties to legal actions and claims which arise in the normal course of business. The Group throughout the year needs to apply judgement in determining the merit of litigation against it and the chances of a claim successfully being made. It needs to determine the likelihood of an outflow of economic benefits occurring and whether there is a need to disclose a contingent liability or whether a provision might be required due to the probability assessment. At any time there are a number of claims or notifications that need to be assessed across the Group.

As set out in note 27, provisions have been recorded in the year for two historical claims that came to light during the year. At any time there are a number of claims or notifications that need to be assessed across the Group. The disparate nature of the group entities heightens the risk that not all potential claims are known at any point in time. Under the new transformation plan, the support functions including commercial and legal will be strengthened and a Chief General Counsel will be appointed. This will enhance the current processes in place to assess the likelihood of historic claims arising.

34 EMPLOYEE BENEFITS

The Group operates both defined benefit and defined contribution pension schemes.

The pension charge for the defined contribution pension schemes for continuing operations for the year is £86.2m (2016: £88.2m).

As at 31 December 2017, retirement obligations are disclosed in relation to 11 defined benefit pension schemes. The Group is the sole employing sponsor of the Capita Pension and Life Assurance Scheme. Grouped together under 'Other schemes' are 10 smaller arrangements:

- three further schemes where the Group is the sole employing sponsor (two of which are based in Switzerland and one is based in Ireland);
- an allocated section of a Local Government Pension Scheme where the Group is the employing sponsor;
- a segregated section of a multi-employer scheme in which the Group is a participating employer;
- three segregated sections in industry wide schemes; and
- two schemes to which the Group makes contributions under Admitted Body status to the Group's clients' defined benefit pension schemes in respect of certain TUPE employees. For the Admitted Body schemes, the Group will only participate in the schemes for a finite period up to the end of the contract with the client.

There are a further 55 defined benefits pension arrangements in which various Capita businesses have participated during 2017. These have been included in the defined contribution pension charge on materiality grounds either due to contractual protections or the size of the scheme. One of these relates to participation in the Social Housing Pension Scheme which is a non-segregated multi-employer defined benefit pension scheme where it is not possible to identify the Group's share of the scheme under IAS 19. For this reason it has been included in the defined contribution pension charge. At the last valuation in 2014, a total deficit of £1,323.0m was disclosed. Total deficit contributions from all employers as a result of the 2014 valuation were £133.6m per annum, of which the Group's share was £0.25m per annum. The Group's expected employer contributions for this scheme in 2018 is £0.28m.

The Capita Pension and Life Assurance Scheme (Scheme)

The Scheme is an HMRC registered pension scheme and is subject to standard UK pensions and tax law. Details of the benefits provided are set out in the Scheme's documentation.

Responsibility for the governance of the Scheme lies with the trustees and the nature of the relationship between the Group and the trustees is governed by regulations. The appointment of the trustees is determined by the trust documentation.

The assets of the Scheme are held in a separate fund (administered by the trustees of the Scheme) to meet long-term pension liabilities to beneficiaries. The trustees of the Scheme invest the assets in line with their Statement of Investment Principles.

The Statement of Investment Principles has been established after taking into consideration the liabilities of the Scheme and the investment risk that the trustees are willing to accept. The Group was consulted before the Statement of Investment Principles was formally adopted.

The most recent funding assessment of the Scheme which was carried out as at 31 March 2014, showed a funding level of 99.8%. As a result, the Group entered into an agreement to make additional contributions to the Capita scheme over a period of time.

The next scheme funding assessment is being carried out with an effective date of 31 March 2017 and is expected to be finalised by 30 June 2018. It is estimated that the funding position of the Scheme has deteriorated since the 2014 assessment, mainly due to the significant fall in gilt yields experienced over this time. The Group has identified reducing deficits in its defined benefit pension schemes as a priority and is working with the Trustees to agree an appropriate recovery plan, recognising that this may result in a significant increase in the level of deficit reduction contributions. At each scheme funding assessment, the present value of the contributions detailed in the current recovery plan is compared with any shortfall revealed. Where the contributions under the current recovery plan are no longer expected (by the end of periods specified in the recovery plans) to be sufficient to remove the shortfall, a new recovery plan will need to be agreed between the trustees and the Group. Options include increasing contributions due from the Group, extending the recovery periods with additional contributions paid after the expiry of current recovery periods or some combination of the two. The affordability to the Group of any increase in contributions is a primary consideration in the agreement of any new recovery plan.

Where the contributions are more than sufficient to remove the shortfall by the end of the recovery period, options include reducing contributions due, keeping the recovery period the same, or shortening the recovery period.

The Group expects to contribute £34.0m to the Scheme over 2018.

As part of the sale of Capita Asset Services businesses to Link Administration Holdings, it was agreed with the trustees that a cash contribution of £17.0m (included in the £34.0m mentioned above) would be made to the Scheme. This was paid in January 2018 and so is not reflected in the below disclosures.

34 EMPLOYEE BENEFITS CONTINUED

The Scheme was closed to future accrual for the majority of members on 30 November 2017, with these members joining the Group's main defined contribution scheme. As a result of the Scheme closing to future accrual, there was a past service curtailment gain of £2.3m reflecting the affected members moving from active members to deferred members. In addition, a number of employers ceased to employ contributing members of the Scheme. As a consequence of this the Group paid £4.5m into the Scheme during January 2018 and guarantees have been provided by four of these employers in favour of the Scheme.

Further to a funding plan agreed with the Scheme's trustees in 2012, the Group established the Capita Scotland (Pension) Limited Partnership (the Partnership) with the Scheme. Under this arrangement, intellectual property rights (IPR) in specific Group software was transferred to the partnership and the rights to use, develop and exploit this IPR was licensed back to the Group in return for an annual fee. The Scheme's interest in the Partnership entitles it to an annual distribution of £8.0m for 15 years.

The Group's interest in the Partnership is fully consolidated into these Group financial statements. The Group has taken advantage of the exemption conferred by Regulation 7 of the Partnerships (Accounts) Regulations 2008 and has, therefore, not appended the accounts of this qualifying partnership to these financial statements. Separate accounts for the Partnership are not required to be, and have not been, filed at Companies House.

Under IAS 19 (Revised) the interest in the Partnership does not represent a plan asset for Group reporting purposes and therefore the Scheme's deficit position presented in these accounts does not reflect the Scheme's interest in the Partnership. Accordingly, distributions from the Partnership to the Scheme are reflected in these Group accounts as pension contributions to the Scheme on a cash basis as paid.

Other schemes

Admitted body arrangements

For those schemes to which the Group makes contributions under Admitted Body status (which are all part of the Local Government Pension Scheme) responsibility for the governance of the schemes lies with boards which operate under a framework of corporate governance and are responsible for following the relevant statutory regulations. For the local government pension schemes there is a similar funding regime which is set out in the Local Government Pension Scheme (Administration) Regulations 2008.

For the Admitted Body schemes, the Group will only participate in the schemes for a finite period up to the end of the contracts. The Group is required to pay regular contributions as decided by the respective Scheme Actuary and as detailed in each scheme's Schedule of Contributions. In addition, the Group will be required to pay some or all of any deficit (as determined by the respective Scheme Actuary) that is remaining at the end of the contract. In respect of this, the Group is carrying a sufficient level of provision in these financial statements.

The Lancashire contract ended on 30 June 2016 and was not renewed. A final payment of £1.6m was paid by the Group in 2017 in final and full settlement of any obligations to the scheme in relation to this contract.

Other UK schemes

For the non-public sector schemes, the scheme funding regime introduced by the Pensions Act 2004 required trustees to carry out regular funding assessments of the schemes and establish schedules of contributions and recovery plans when there is a shortfall in the schemes. The recovery plans detail the amount and timing of the contributions required to eliminate the shortfall in the schemes. Funding assessments are carried out at least every 3 years. Approximate funding updates are produced at each scheme anniversary, when a full scheme funding assessment is not being undertaken.

For these schemes, the latest formal valuations for each scheme were carried out between 31 December 2015 and 31 March 2016. The valuations for the other schemes are updated by qualified actuaries at each balance sheet date. Scheme assets are stated at their market valuations at each respective balance sheet date.

For the local government pension scheme there is a similar funding regime which is set out in the Local Government Pension Scheme (Administration) Regulations 2008.

Overseas schemes

The Irish scheme is classed as a cross border scheme for which the beneficiaries of the scheme have their liabilities, and the trustees hold assets, denominated in euros. The Scheme is governed under the UK regulations and subject to the further requirements applying to cross border schemes.

The Swiss schemes are administered and governed through collective foundations which are separate legal entities. At the start of 2017 there were 3 Swiss schemes. During 2017, two of these merged together.

The total employer contributions to the 'Other' schemes for 2018 are estimated to be £3.0m.

Risks associated with the Group's pension schemes

These defined benefit pension schemes expose the Group to actuarial risks, such as longevity risk, interest rate risk, salary risk, market (investment) risk and currency risk.

The trustees of the Capita Pension and Life Assurance Scheme have entered into two bulk annuity contracts with an insurer in respect of a small number of high individual liability pensioner members (one in 2015 and the second in late 2017) with total value included in the assets at 31 December 2017 below of £76.7m.

The trustees have also entered into a Liability Driven Investment programme. The level of risk that is managed by this is set by various market related and funding trigger points. The current level of hedging (interest rate and inflation – including the two buy-ins) under this programme is around 30% of the liabilities measured on the trustees long-term funding basis.

IFRIC 14

The Group has considered the impact of IFRIC 14 on the various schemes and has concluded that the effect of any such adjustment, as they may arise, is not material and accordingly has not made any adjustments at the balance sheet date.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

34 EMPLOYEE BENEFITS CONTINUED

The assets and liabilities of the defined benefit pension schemes (excluding additional voluntary contributions) as at 31 December are:

	Capita scheme		Other schemes		Group total	
	2017 £m	2016 £m	2017 £m	2016 £m	2017 £m	2016 £m
Scheme assets at fair value:						
Equities:						
– UK	40.6	49.0	4.9	8.1	45.5	57.1
– Overseas	305.9	294.4	10.4	19.9	316.3	314.3
– Private[1]	–	–	1.5	0.6	1.5	0.6
	346.5	343.4	16.8	28.6	363.3	372.0
Debt securities:						
– UK Government	249.9	231.1	13.8	3.4	263.7	234.5
– UK Corporate	45.0	45.1	0.4	2.8	45.4	47.9
– Overseas Government	34.1	24.6	2.6	1.8	36.7	26.4
– Overseas Corporate	137.2	138.9	0.4	0.6	137.6	139.5
– Emerging Markets	29.5	28.1	0.3	0.2	29.8	28.3
– Private Debt[1]	34.6	24.7	–	–	34.6	24.7
– Secured Loans	–	–	1.6	1.5	1.6	1.5
	530.3	492.5	19.1	10.3	549.4	502.8
Property	78.3	70.4	4.8	3.6	83.1	74.0
Infrastructure	–	–	–	0.4	–	0.4
Credit Funds	–	–	8.2	3.2	8.2	3.2
Asset Backed Securities	–	–	0.7	0.7	0.7	0.7
Hedge Funds	214.4	166.0	0.6	1.5	215.0	167.5
Absolute return funds	–	11.0	–	–	–	11.0
Diversified growth funds	–	–	5.0	0.1	5.0	0.1
Insurance Contracts[1]	76.7	51.2	16.4	15.7	93.1	66.9
Cash	(144.9)	(96.5)	1.2	4.6	(143.7)	(91.9)
Other	–	–	3.7	3.0	3.7	3.0
	224.5	202.1	40.6	32.8	265.1	234.9
Total	1,101.3	1,038.0	76.5	71.7	1,177.8	1,109.7
Present value of scheme liabilities	1,493.4	1,366.4	91.2	88.5	1,584.6	1,454.9
Net liability	(392.1)	(328.4)	(14.7)	(16.8)	(406.8)	(345.2)

1 The assets of the schemes are all quoted with the exception of the private equity, private debt holdings and insurance contracts.

The Trustees of the Capita Scheme transacted the second bulk annuity contract at the end of 2017. Under the terms of the transaction the premium fell due for payment in early January 2018. This transaction is reflected in the accounts as a negative balance of £28.6m in the cash holding representing the premium paid in the subsequent accounting period.

These amounts do not include any directly owned financial instruments issued by the Group.

There are two assets which have been classified as insurance contracts for the purposes of these accounts:

- The two bulk annuity contracts entered into by the trustees of the Capita scheme late in 2015 and 2017. These contracts have been valued as an asset equal to the corresponding liability under the end of year IAS 19 assumptions.
- The investment of the assets in respect of the Swiss schemes occurs by the collective foundations in the context of reinsurance contracts.

34 EMPLOYEE BENEFITS CONTINUED

The following table shows a reconciliation from the opening balances to the closing balances for the net defined benefit liability and its components:

	Defined benefit obligation		Fair value of plan assets		Group total Net defined liability	
	2017 £m	2016 £m	2017 £m	2016 £m	2017 £m	2016 £m
Balance at 1 January	1,454.9	1,143.5	(1,109.7)	(955.2)	345.2	188.3
Included in the income statement:						
Current service cost	30.0	25.9	–	–	30.0	25.9
Administration costs	2.3	2.2	–	–	2.3	2.2
Past service cost including curtailments	(1.3)	(0.1)	–	–	(1.3)	(0.1)
Settlements	(1.8)	(33.8)	1.6	33.8	(0.2)	–
Interest cost/(income)	39.8	43.4	(30.6)	(36.8)	9.2	6.6
Sub-total in income statement	69.0	37.6	(29.0)	(3.0)	40.0	34.6
Included in other comprehensive income:						
Re-measurements loss/(gain)	–	–	–	–	–	–
Actuarial loss/(gain) arising from:						
– demographic assumptions	(0.5)	(10.5)	–	–	(0.5)	(10.5)
– financial assumptions	83.9	316.8	–	(3.8)	83.9	313.0
– experience adjustments	14.1	0.3		–	14.1	0.3
– changes in asset ceiling/minimum liability	–	–	–	–	–	–
Return on plan assets excluding interest	–	–	(45.8)	(145.1)	(45.8)	(145.1)
Foreign currency translation	(0.9)	–	0.6	–	(0.3)	–
Sub-total in other comprehensive income	96.6	306.6	(45.2)	(148.9)	51.4	157.7
Employer contributions	–	–	(29.8)	(35.4)	(29.8)	(35.4)
Contributions by employees	1.6	1.6	(1.6)	(1.6)	–	–
Benefits paid	(37.3)	(34.4)	37.3	34.4	–	–
Contract bulk transfers/business combinations	(0.2)	–	0.2	–	–	–
Balance at 31 December	1,584.6	1,454.9	(1,177.8)	(1,109.7)	406.8	345.2

The defined benefit obligation comprises £1,584.6m (2016: £1,454.9m) arising from schemes that are wholly or partly funded.

Of the total pension cost of £40.0m (2016: £34.6m), £28.6m (2016: £25.8m) was included in cost of sales, £2.3m (2016: £2.2m) was included in administrative expenses, and £9.1m in finance costs (2016: £6.6m).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

34 EMPLOYEE BENEFITS CONTINUED

	Capita scheme					
	Defined benefit obligation		Fair value of plan assets		Net defined liability	
	2017 £m	2016 £m	2017 £m	2016 £m	2017 £m	2016 £m
Balance at 1 January	1,366.4	1,017.7	(1,038.0)	(849.4)	328.4	168.3
Included in the income statement:						
Current service cost	27.9	23.8	–	–	27.9	23.8
Administration cost	2.0	1.9	–	–	2.0	1.9
Past service cost including curtailments	(1.5)	0.1	–	–	(1.5)	0.1
Settlements	–	–	–	–	–	–
Interest cost/(income)	37.8	39.3	(29.0)	(33.2)	8.8	6.1
Sub-total in income statement	66.2	65.1	(29.0)	(33.2)	37.2	31.9
Included in other comprehensive income:						
Re-measurements loss/(gain)	–	–	–	–	–	–
Actuarial loss/(gain) arising from:						
– demographic assumptions	(0.5)	(9.0)	–	–	(0.5)	(9.0)
– financial assumptions	81.2	298.9	–	–	81.2	298.9
– experience adjustments	13.8	5.7	–	–	13.8	5.7
Return on plan assets excluding interest	–	–	(42.5)	(142.4)	(42.5)	(142.4)
Sub-total in other comprehensive income	94.5	295.6	(42.5)	(142.4)	52.0	153.2
Employer contributions	–	–	(25.5)	(27.4)	(25.5)	(27.4)
Contributions by employees	0.1	0.2	(0.1)	(0.2)	–	–
Benefits paid	(33.6)	(29.3)	33.6	29.3	–	–
Contract bulk transfers/business combinations	(0.2)	17.1	0.2	(14.7)	–	2.4
Balance at 31 December	1,493.4	1,366.4	(1,101.3)	(1,038.0)	392.1	328.4

	Other schemes					
	Defined benefit obligation		Fair value of plan assets		Net defined liability	
	2017 £m	2016 £m	2017 £m	2016 £m	2017 £m	2016 £m
Balance at 1 January	88.5	125.8	(71.7)	(105.8)	16.8	20.0
Included in the income statement:						
Current service cost	2.1	2.1	–	–	2.1	2.1
Administration cost	0.3	0.3	–	–	0.3	0.3
Past service cost including curtailment	0.2	(0.2)	–	–	0.2	(0.2)
Settlements	(1.8)	(33.8)	1.6	33.8	(0.2)	–
Interest cost/(income)	2.0	4.1	(1.6)	(3.6)	0.4	0.5
Sub-total in income statement	2.8	(27.5)	0.0	30.2	2.8	2.7
Included in other comprehensive income:						
Re-measurements loss/(gain)	–	–	–	–	–	–
Actuarial loss/(gain) arising from:						
– demographic assumptions	–	(1.5)	–	–	–	(1.5)
– financial assumptions	2.7	17.9	–	(3.8)	2.7	14.1
– experience adjustments	0.3	(5.4)	–	–	0.3	(5.4)
– changes in asset ceiling/minimum liability	–	–	–	–	–	–
Return on plan assets excluding interest	–	–	(3.3)	(2.7)	(3.3)	(2.7)
Foreign currency translation	(0.9)	–	0.6	–	(0.3)	–
Sub-total in other comprehensive income	2.1	11.0	(2.7)	(6.5)	(0.6)	4.5
Employer contributions	–	–	(4.3)	(8.0)	(4.3)	(8.0)
Contributions by employees	1.5	1.4	(1.5)	(1.4)	–	–
Benefits paid	(3.7)	(5.1)	3.7	5.1	–	–
Contract bulk transfers/business combinations	–	(17.1)	–	14.7	–	(2.4)
Balance at 31 December	91.2	88.5	(76.5)	(71.7)	14.7	16.8

34 EMPLOYEE BENEFITS CONTINUED

Information about the defined benefit obligation for the Capita scheme:

	Proportion of overall liability %	Duration (years)
Active members	8	24.8
Deferred members	64	24.4
Pensioners	28	13.8
Total	100	21.5

	Capita scheme		Other schemes[3]	
Main assumptions:	2017 %	2016 %	2017 %	2016 %
Rate of price inflation – RPI/CPI	3.20/2.20	3.25/2.25	3.20/2.20	3.25/2.25
Rate of salary increase	3.20	3.25	3.20	3.25
Rate of increase of pensions in payment[1]:				
– RPI inflation capped at 5% per annum	3.10	3.15	3.10	3.15
– RPI inflation capped at 2.5% per annum	2.20	2.20	2.20	2.20
– CPI inflation capped at 5% per annum	2.25	2.25	2.25	2.25
– CPI inflation capped at 2.5% per annum	1.80	1.80	1.80	1.80
Discount rate	2.50	2.80	2.50	2.80
CARE active revaluation (inflation capped at 3.5% per annum)	2.75	2.75	2.75	2.75
Expected take up maximum available tax free cash	85.0	85.0	85.0	85.0

The average future life expectancy from age 65 (in years) for mortality tables used to determine scheme liabilities for the various different schemes at 31 December 2017 and 31 December 2016 are as follows:

	Member currently aged 65 (current life expectancy)				Member currently aged 45 (life expectancy at 65)			
	Male		Female		Male		Female	
	2017	2016	2017	2016	2017	2016	2017	2016
Capita scheme	22.7	22.5	24.4	24.3	23.1	22.9	25.4	25.3
Other schemes[3]	22.7 to 24.2	22.5 to 24.1	24.4	24.3	23.1 to 25.9	22.9 to 25.8	25.4 to 26.2	25.3 to 26.1

1 There are other levels of pension increase which apply to particular periods of membership.

2 Only the discount rate is relevant to the Admitted Body schemes. Different assumptions apply to non-UK schemes: the discount rate for the Irish Scheme is 2.0% per annum and for the two Swiss schemes, 0.6% in 2017.

3 This does not apply to the Admitted Body schemes or the Swiss schemes.

The assumptions used for the Capita scheme are tailored for each member. The assumptions adopted make allowance for an increase in the longevity in the future. The rate for members currently aged 65 is derived from the pensioner membership and the rate for members reaching age 65 in 20 years' time is derived from non-pensioner membership.

Sensitivity Analysis

Given the nature and number of assumptions, which are not in the control of the Group, there are a range of reasonably possible outcomes. The table below shows how the value of the defined benefit obligations would increase if the assumptions were changed as shown (assuming all other assumptions remain constant):

Change in assumptions compared with 31 December 2017 actuarial assumptions	Capita scheme £m	Other schemes £m
0.1% decrease in discount rate	32.2	1.5
0.1% change in salary increases	1.1	0.1
0.1% change in inflation (and related assumption, e.g. salary and pension increases)	17.3	1.1
1 year increase in life expectancy	59.7	2.9

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

35 RELATED PARTY TRANSACTIONS

Compensation of key management personnel

	2017 £m	2016 £m
Short-term employment benefits	11.3	11.1
Pension	0.2	0.3
Share based payments	0.1	0.8
	11.6	12.2

Gains on share options exercised in the year by Capita plc Executive Directors were £0.7m (2016: £6.2m) and by key management personnel £0.2m (2016: £4.5m), totalling £0.9m (2016: £10.7m).

During the year, the Group rendered administrative services to Smart DCC Ltd, a wholly-owned subsidiary which is not consolidated (refer to note 36). The Group received £55.5m (2016: £40.3m) of revenue for these services. The services are procured by Smart DCC on an arm's length basis under the DCC licence. The services are subject to review by Ofgem to ensure that all costs are economically and efficiently incurred by Smart DCC.

Capita Pension and Life Assurance Scheme is a related party of the Group. Transactions with the Scheme are disclosed in note 34 – Employee benefits on pages 154 to 159.

The following companies are substantial shareholders in the Company and therefore a related party of the Company (in each case, for the purposes of the Listing Rules of the UK Listing Authority). The number of shares held on 18 April 2018 was as below:

Shareholder	No. of shares	% of voting rights
Veritas Asset Management LLP[1]	89,035,975	13.34
Woodford Investment Management LLP	66,758,754	10.00
Investec Asset Management Ltd.	63,080,896	9.45
Invesco Ltd.	60,574,558	9.08
BlackRock, Inc.	44,104,108	6.61
Marathon Asset Management LLP	21,694,771	3.25
Vanguard Group	20,654,592	3.09

1 This includes the holding of Veritas Funds PLC.

36 GROUP COMPOSITION AND NON-CONTROLLING INTERESTS

The Group's subsidiaries are listed in note 8 and note 18 of the parent company financial statements on pages 192 and 196 to 200. This includes AXELOS Limited and Entrust Limited which both have 49% non-controlling interests, and Fera which has a 25% non-controlling interest, none of whose contribution was material to the Group's financial performance, financial position or cash flow in both 2017 and 2016.

The Group holds a majority of the voting rights in all of these subsidiaries and the Directors have determined that, other than the entity commented on below, in each case the Group exercises de facto control.

On 23 September 2014, the Secretary of State for the Department for Energy and Climate Change granted Smart DCC Ltd (DCC), a wholly-owned subsidiary of the Group, a licence to establish and manage the smart metering communications infrastructure, governed by the Smart Energy Code. Each year the Group reassess whether it has control over DCC as required under IFRS 10. The Group's ability to control the relevant activities of DCC is restricted by DCC's operating licence. The power that the Group has over DCC's relevant activities by virtue of owning it is limited (given the restrictions in the licence). That power is held by the board of DCC where the Group has minority representation in compliance with the licence. The Group has therefore not consolidated DCC within its Group accounts. The disclosure of related party transactions with DCC is included in note 35 to these financial statements.

37 POST BALANCE SHEET EVENT

There are no post balance sheet events that have an adjusting effect on the financial statements. In January 2018, we announced that the administration of Prudential's life and pensions business, around 2% of Group revenue and £0.3bn of the order book disclosed in note 7, will be transferring from Capita to a new supplier later in 2018. This has no adjusting effect on the financial statements for 2017.

38 FINANCIAL STATEMENTS RESTATEMENT UNDER IFRS 15

The Group early adopted IFRS 15 Revenue from Contracts with Customers (IFRS 15) on 1 January 2017 using the full retrospective method. This note details the Group's new accounting policy for revenue and shows the impact of the adoption of IFRS 15 on the Group's primary financial statements.

The cumulative effect of the adoption of IFRS 15 has resulted in a decrease in net assets of £942.3m as at 1 January 2016 (31 December 2016: £1,036.3m). This reflects an important change in accounting policy as the Group moves from one based predominantly on percentage of completion revenue recognition to a methodology that is focused on aligning revenue recognition to the delivery of solutions and value to its clients.

Consolidated income statement restatement under IFRS 15

		As reported, year ended 31 December 2016				Discontinued operations		Impact of IFRS 15		Restated, year ended 31 December 2016			
	Adjustment	Underlying £m	Business exit £m	Specific items £m	Total £m	Underlying/ reclassification to business exit £m	Specific items £m	Underlying £m	Specific items £m	Underlying £m	Business exit £m	Specific items £m	Total £m
Revenue	A,B,C	4,897.9	11.3	–	4,909.2	(316.3)	–	(224.3)	–	4,357.3	11.3	–	4,368.6
Cost of sales	A,D	(3,627.7)	(6.7)	(7.5)	(3,641.9)	111.8	–	97.4	(34.8)	(3,418.5)	(6.7)	(42.3)	(3,467.5)
Gross profit		1,270.2	4.6	(7.5)	1,267.3	(204.5)	–	(126.9)	(34.8)	938.8	4.6	(42.3)	901.1
Administrative expenses	H	(728.9)	(1.8)	(388.3)	(1,119.0)	144.5	17.7	(19.8)	59.4	(604.2)	(1.8)	(311.2)	(917.2)
Operating profit		541.3	2.8	(395.8)	148.3	(60.0)	17.7	(146.7)	24.6	334.6	2.8	(353.5)	(16.1)
Net finance costs		(66.0)	–	(7.6)	(73.6)	(0.1)	(0.1)	–	–	(66.1)	–	(7.7)	(73.8)
Gain on disposal		–	0.1	–	0.1	–	–	–	–	–	0.1	–	0.1
Profit before tax		475.3	2.9	(403.4)	74.8	(60.1)	17.6	(146.7)	24.6	268.5	2.9	(361.2)	(89.8)
Income tax (expense)/credit	E	(87.9)	0.5	54.9	(32.5)	9.5	(3.9)	32.0	(3.9)	(46.4)	0.5	47.1	1.2
Profit/(loss) for the period from continuing operations		387.4	3.4	(348.5)	42.3	(50.6)	13.7	(114.7)	20.7	222.1	3.4	(314.1)	(88.6)
Profit/(loss) for the period from discontinued operations		–	–	–	–	50.6	(13.7)	–	–	–	50.6	(13.7)	36.9
Total profit/(loss) for the period		387.4	3.4	(348.5)	42.3	–	–	(114.7)	20.7	222.1	54.0	(327.8)	(51.7)
Attributable to:													
Owners of the Company		376.7	3.4	(343.2)	36.9			(115.5)	20.7	210.6	54.0	(322.5)	(57.9)
Non-controlling interests		10.7	–	(5.3)	5.4			0.8	–	11.5	–	(5.3)	6.2
		387.4	3.4	(348.5)	42.3			(114.7)	20.7	222.1	54.0	(327.8)	(51.7)
Earnings/(loss) per share													
Continuing operations:													
– basic		56.67p	0.51p	(51.63)p	5.55p	(7.61)p	0.50p	(17.38)p	3.11p	31.68p	0.51p	(48.02)p	(15.83)p
– diluted		56.67p	0.51p	(51.63)p	5.55p	(7.61)p	0.50p	(17.38)p	3.11p	31.68p	0.51p	(48.02)p	(15.83)p
Total operations:													
– basic		56.67p	0.51p	(51.63)p	5.55p	–p	–p	(17.38)p	3.11p	31.68p	8.12p	(48.52)p	(8.72)p
– diluted		56.67p	0.51p	(51.63)p	5.55p	–p	–p	(17.38)p	3.11p	31.68p	8.12p	(48.52)p	(8.72)p

Total adjustment to Total profit for the period due to the adoption of IFRS 15 is £(114.7)m to underlying and £20.7m to specific items, being £94.0m.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

38 FINANCIAL STATEMENTS RESTATEMENT UNDER IFRS 15 CONTINUED

Consolidated balance sheet restatement under IFRS 15

	Adjustment	As reported 1 January 2016 £m	Impact of IFRS 15 £m	Restated 1 January 2016 £m	As reported 31 December 2016 £m	Impact of IFRS 15 £m	Restated 31 December 2016 £m
Non-current assets							
Property, plant and equipment		406.0	–	406.0	394.7	–	394.7
Intangible assets		2,810.0	–	2,810.0	2,754.2	–	2,754.2
Contract fulfilment assets	D	–	277.6	277.6	–	240.6	240.6
Financial assets		186.6	–	186.6	337.6	–	337.6
Deferred taxation	E	18.8	162.8	181.6	32.0	190.4	222.4
Trade and other receivables	F	86.1	(41.7)	44.4	128.4	(79.6)	48.8
		3,507.5	398.7	3,906.2	3,646.9	351.4	3,998.3
Current assets							
Financial assets		44.3	–	44.3	92.6	–	92.6
Disposal group assets held for sale		84.1	–	84.1	–	–	–
Funds assets		161.7	–	161.7	173.6	–	173.6
Trade and other receivables	D,F	1,011.9	(243.7)	768.2	976.0	(133.3)	842.7
Cash		534.0	–	534.0	1,098.3	–	1,098.3
		1,836.0	(243.7)	1,592.3	2,340.5	(133.3)	2,207.2
Total assets		5,343.5	155.0	5,498.5	5,987.4	218.1	6,205.5
Current liabilities							
Trade and other payables	G	1,144.0	(271.0)	873.0	1,297.6	(320.6)	977.0
Deferred income	B,C,G	–	1,157.3	1,157.3	–	1,374.9	1,374.9
Overdrafts		448.7	–	448.7	532.5	–	532.5
Financial liabilities		230.8	–	230.8	224.2	–	224.2
Disposal group liabilities held for sale		40.4	–	40.4	–	–	–
Funds liabilities		161.7	–	161.7	173.6	–	173.6
Provisions		69.4	–	69.4	112.5	–	112.5
Income tax payable	E	46.2	–	46.2	18.6	–	18.6
		2,141.2	886.3	3,027.5	2,359.0	1,054.3	3,413.3
Non-current liabilities							
Trade and other payables	G	29.3	(15.5)	13.8	35.1	(14.1)	21.0
Deferred income	B,C,G	–	228.5	228.5	–	216.7	216.7
Financial liabilities		2,163.4	–	2,163.4	2,694.4	–	2,694.4
Deferred taxation	E	19.0	(2.0)	17.0	22.1	(2.5)	19.6
Provisions		49.0	–	49.0	48.2	–	48.2
Employee benefits		188.3	–	188.3	345.2	–	345.2
		2,449.0	211.0	2,660.0	3,145.0	200.1	3,345.1
Total liabilities		4,590.2	1,097.3	5,687.5	5,504.0	1,254.4	6,758.4
Net assets		753.3	(942.3)	(189.0)	483.4	(1,036.3)	(552.9)
Capital and reserves							
Issued share capital		13.8	–	13.8	13.8	–	13.8
Share premium		500.7	–	500.7	501.3	–	501.3
Employee benefit trust and treasury shares		(0.3)	–	(0.3)	(0.2)	–	(0.2)
Capital redemption reserve		1.8	–	1.8	1.8	–	1.8
Foreign currency translation reserve		(21.2)	–	(21.2)	(6.2)	–	(6.2)
Cash flow hedging reserve		(12.0)	–	(12.0)	–	–	–
Retained earnings		196.5	(934.7)	(738.2)	(102.3)	(1,029.5)	(1,131.8)
Equity attributable to owners of the Company		679.3	(934.7)	(255.4)	408.2	(1,029.5)	(621.3)
Non-controlling interests		74.0	(7.6)	66.4	75.2	(6.8)	68.4
Total equity		753.3	(942.3)	(189.0)	483.4	(1,036.3)	(552.9)

38 FINANCIAL STATEMENTS RESTATEMENT UNDER IFRS 15 CONTINUED

Consolidated cash flow statement restatement under IFRS 15

As a result of the adoption of IFRS 15, certain reclassifications are required in relation to the following cash flow movements between relevant balance sheet accounts. There has been no change in the net cash generated from operations as a result of these reclassifications or restatement of these balance sheet accounts:

- As identified in adjustment H (below), in 2016, the Group recognised a write down of accrued income in underlying profit and specific items in relation to certain long-term service contracts. Under IFRS 15, this accrued income would not have been originally recognised and hence has been reversed out of the income statement on adoption of IFRS 15. Movements in the operating cash flow note reflect the reversal of this non-cash movement;
- As identified in adjustment D (below), the Group has recognised new contract fulfilment assets on adoption of IFRS 15 from 1 January 2016 with amortisation and impairment expenses recorded through the income statement in the year ended 31 December 2016. Movements in the operating cash flow note reflect these non-cash movements recorded in the income statement; and
- As identified in adjustments D, B and C, on transition to IFRS 15 as at 1 January 2016, the Group has recognised contract fulfilment assets and restated the accrued income and deferred revenue accounts recorded in the balance sheet. Movements in the operating cash flow note reflect the relevant cash and non-cash movements in reclassified line items.

Consolidated statement of changes in equity restatement under IFRS 15

No reconciliation of the restated consolidated statement of changes in equity is presented as the only changes to this primary statement for the relevant period presented are as follows:

- **Consolidated statement of changes in equity as at 1 January 2016:** recognition of the restated retained earnings figure as presented in the restated consolidated balance sheet as at this date.
- **Consolidated statement of changes in equity as at 31 December 2016:** recognition of the restated profit for the year ended 31 December 2016 as presented in the restated consolidated income statement for this year.

Notes to the financial statements restatement under IFRS 15

Management has undertaken an extensive exercise to consider the Group's major contractual arrangements as part of the implementation of IFRS 15. A number of significant areas have been identified for adjustment which include:

- Recognition of revenue by the Group as agent or principal (Adjustment A);
- Accounting for software licences (Adjustment B);
- Recognition of profit from service contracts over time in line with the output method (Adjustment C);
- Recognition, utilisation and derecognition of contract fulfilment assets (Adjustment D);
- Impact on tax balances as a result of adoption of IFRS 15 (Adjustment E);
- Decrease in trade and other receivables (Adjustment F);
- Reclassification of trade and other payables (Adjustment G);
- Reversal of prior period accrued income impairment within specific items (Adjustment H); and
- Reclassification of significant restructuring costs to underlying (Adjustment I).

These adjustments are discussed in the relevant sections below.

Under IFRS 15, the pattern and timing of revenue recognition has changed resulting in an overall decrease of £224.3m in revenue for the year ended 31 December 2016, increase in deferred income of £1,099.3m at the 1 January 2016 opening balance sheet date (31 December 2016: £1,256.9m) and decrease in accrued income of £325.8m at the 1 January 2016 opening balance sheet date (31 December 2016: £254.5m).

Table 1 on the following page reconciles the movements in relation to IFRS 15 for the income statement for the year ended 31 December 2016 and the balance sheet as at 1 January 2016 and as at 31 December 2016.

Table 2 provides further detail on the reconciling movements for the income statement for the year ended 31 December 2016.

Following the tables are explanatory notes for each of the adjustments referred to above.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

38 FINANCIAL STATEMENTS RESTATEMENT UNDER IFRS 15 CONTINUED

The table below reconciles movements in relation to IFRS 15 for the income statement for the year ended 31 December 2016 and the balance sheet as at 1 January 2016 and as at 31 December 2016. Refer to below the tables for explanatory notes on each of the adjustments.

Table 1:

		Consolidated income statement for the year ended 31 December 2016							
		Underlying				Specific items			
Adjustment	Adjustment to net assets at 1 January 2016 £m	Revenue £m	Cost of sales £m	Admin expenses £m	Tax £m	Cost of sales £m	Admin expenses £m	Tax £m	Profit/(loss) for the period £m
A – Agent vs. principal	–	(90.9)	90.9	–	–	–	–	–	–
B – Software licences	(163.2)	(15.3)	–	–	–	–	–	–	(15.3)
C – Recognition in line with output	(1,214.8)	(118.1)	–	–	–	–	–	–	(118.1)
D – Recognition of non-current contract fulfilment assets	214.7	–	(0.6)	–	–	(42.3)	–	–	(42.9)
D – Recognition of software contract fulfilment assets	62.9	–	5.9	–	–	–	–	–	5.9
D – Recognition of current contract fulfilment assets	40.4	–	1.2	–	–	–	–	–	1.2
E – Tax	164.8	–	–	–	32.0	–	–	(3.9)	28.1
G – Reclassification of trade and other payables	–	–	–	–	–	–	–	–	–
H – Reversal of accrued income impairment	(47.1)	–	–	39.6	–	7.5	–	–	47.1
I – Reclassification of significant restructuring	–	–	–	(59.4)	–	–	59.4	–	–
Total	(942.3)	(224.3)	97.4	(19.8)	32.0	(34.8)	59.4	(3.9)	(94.0)

	Consolidated balance sheet for the year ended 31 December 2016										
	Trade and other receivables		Deferred income		Trade and other payables		Contract fulfilment asset	Contract costs capitalised	Deferred tax		
Adjustment	Non-current £m	Current £m	Current £m	Non-current £m	Current £m	Non-current £m	Non-current £m	Current £m	Asset £m	Liability £m	Adjustment to net liabilities at 31 December 2016 £m
A – Agent vs. principal	–	–	–	–	–	–	–	–	–	–	–
B – Software licences	–	–	(104.8)	(73.7)	–	–	–	–	–	–	(178.5)
C – Recognition in line with output	(79.6)	(174.9)	(949.5)	(128.9)	–	–	–	–	–	–	(1,332.9)
D – Recognition of non-current contract fulfilment assets	–	–	–	–	–	–	171.8	–	–	–	171.8
D – Recognition of software contract fulfilment assets	–	–	–	–	–	–	68.8	–	–	–	68.8
D – Recognition of current contract fulfilment assets	–	–	–	–	–	–	–	41.6	–	–	41.6
E – Tax	–	–	–	–	–	–	–	–	190.4	2.5	192.9
G – Reclassification of trade and other payables	–	–	(320.6)	(14.1)	320.6	14.1	–	–	–	–	–
H – Reversal of accrued income impairment	–	–	–	–	–	–	–	–	–	–	–
I – Reclassification of significant restructuring	–	–	–	–	–	–	–	–	–	–	–
Total	(79.6)	(174.9)	(1,374.9)	(216.7)	320.6	14.1	240.6	41.6	190.4	2.5	(1,036.3)

38 FINANCIAL STATEMENTS RESTATEMENT UNDER IFRS 15 CONTINUED

The table below provides further detail on the reconciling movements for the income statement for the year ended 31 December 2016. Refer to below the table for explanatory notes in respect of each adjustment.

Table 2:

		Consolidated income statement for the year ended 31 December 2016						
Adjustment		As reported £m	Discontinued operations £m	*As reported – continuing operations £m*	Adjustments: from pre 1 January 2016 and recognised in 2016 £m	Adjustments: previously recognised in 2016 now spread forward £m	Reclassifications £m	Restated £m
Agent vs. principal	A	–	–	–	–	–	(90.9)	
Software revenue from pre 1 January 2016 and recognised in 2016	B	–	–	–	100.0	–	–	
Software revenue previously recognised in 2016 now spread forward	B	–	–	–	–	(115.3)	–	
Recognition in line with output from pre 1 January 2016 and recognised in 2016	C	–	–	–	1,096.6	–	–	
Recognition in line with output previously recognised in 2016 now spread forward	C	–	–	–	–	(1,214.7)	–	
Underlying Revenue		4,897.9	(316.3)	4,581.6	1,196.6	(1,330.0)	(90.9)	4,357.3
Agent vs. principal	A	–	–	–	–	–	90.9	
Non-current contract fulfilment asset utilisation in 2016	D	–	–	–	(47.1)	–	–	
Non-current contract fulfilment asset disposals in 2016	D	–	–	–	(17.0)	–	–	
Non-current contract fulfilment asset additions in 2016	D	–	–	–	–	63.5	–	
Software contract fulfilment asset utilisation in 2016	D	–	–	–	(7.1)	–	–	
Software contract fulfilment asset additions in 2016	D	–	–	–	–	13.0	–	
Completion of point in time performance obligations	D	–	–	–	(40.4)	–	–	
Costs deferred to future point in time performance obligations	D	–	–	–	–	41.6	–	
Underlying cost of sales		(3,627.7)	111.8	(3,515.9)	(111.6)	118.1	90.9	(3,418.5)
Reversal of accrued income impairment	H	–	–	–	39.6	–	–	
Reclassification of 2016 group restructuring to underlying from specific items	I	–	–	–	–	–	(59.4)	
Underlying admin expenses		(728.9)	144.5	(584.4)	39.6	–	(59.4)	(604.2)
Underlying operating profit		541.3	(60.0)	481.3	1,124.6	(1,211.9)	(59.4)	334.6
Underlying profit before tax		475.3	(60.1)	415.2	1,124.6	(1,211.9)	(59.4)	268.5
Specific items – contract fulfilment asset derecognised	D	–	–	–	(42.3)	–		
Specific items – reversal of accrued income impairment	H	–	–	–	7.5	–	–	
Specific items cost of sales		(7.5)	–	(7.5)	(34.8)	–	–	(42.3)
Reclassification of 2016 group restructuring to underlying from specific items	I	–	–	–	–	–	59.4	
Specific items admin expenses		(388.3)	4.3	(384.0)	–	–	59.4	(324.6)
Specific items profit/(loss) before tax		(403.4)	4.2	(399.2)	(34.8)	–	59.4	(374.6)
Profit/(loss) before tax		74.8	(55.9)	18.9	1,089.8	(1,211.9)	–	(103.2)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

38 FINANCIAL STATEMENTS RESTATEMENT UNDER IFRS 15 CONTINUED

Adjustment A – Accounting for agent vs. principal

The previous agent vs. principal guidance contained in IAS 18 has been revisited by the Group in light of the revised guidance under IFRS 15 in assessing whether it acts as an agent or as a principal in its major contractual arrangements.

As a result of this assessment, the Group concluded that for certain contracts it is appropriate to move from principal to agency accounting or vice versa. In respect to moving from principal to agency, this related to certain software sales arrangements as the Group has concluded that the Group does not control the goods or service being provided to the customer. As a result, there is a net adjustment of £90.9m to reduce revenue and cost of sales for the year ended 31 December 2016.

Adjustment B – Accounting for software licences

Under previous accounting, revenue in relation to certain software licences was recognised at a point in time. Under IFRS 15, the Group has determined that a number of these arrangements result in the customer having the right to access the licence (an 'active' licence) rather than having the right to use the licence (a 'passive' licence). Under an active licence the ongoing support and upgrades are fundamental to the ongoing use of the licences by the customer.

Hence total revenue for the licence and upgrades are combined with these revenues now recognised over the term of the customer contract rather than at a point in time resulting in a net decrease in accrued/deferred income at 1 January 2016 of £163.2m, 31 December 2016: £178.5m; and a net decrease in revenue in the year ended 31 December 2016 of £15.3m.

For the year ended 31 December 2016, the net decrease in revenue comprises the recognition of £100.0m of revenue from pre 1 January 2016 and the deferral of £115.3m of revenue previously recognised in 2016.

Adjustment C – Revenue recognition in line with output

Under the previous accounting, revenue for certain contracts was recognised under the percentage of completion method based upon costs incurred to date as a proportion of the estimated full cost of completing the contract, and applying the percentage to the total revenue expected to be earned. Such percentage of completion accounting would typically result in higher levels of revenue recognised in the earlier stages of a contract in line with the profile of costs incurred.

Under IFRS 15, all elements of the contract, including transformation activity, are combined. Due to the application of the series guidance and output methodology within IFRS 15, these contracts now have revenue recognised in line with their output measured on a contract specific basis.

As such, revenue is now spread over the expected life of the contract rather than in line with the costs profile, which has resulted in a reduction in revenue recognised in periods prior to 1 January 2016 and a net increase in deferred/accrued income as at 1 January 2016 of £1,214.8m, as at 31 December 2016: £1,332.9m; and a decrease in opening retained earnings as at 1 January 2016 of £1,214.8m, and a decrease in revenue in the year ended 31 December 2016 of £118.1m.

For the year ended 31 December 2016, the net decrease in revenue comprises the recognition of £1,096.6m of revenue from pre 1 January 2016 and the deferral of £1,214.7m of revenue previously recognised in 2016.

Adjustment D – Recognition, utilisation and derecognition of contract fulfilment assets

IFRS 15 specifies that certain costs to fulfil a contract are to be capitalised as non-current contract fulfilment assets (if utilisation is expected to occur beyond 12 months from balance sheet date) and current contract fulfilment assets (if utilisation is expected to occur within 12 months from balance sheet date) if relevant criteria are met.

The Group incurred costs that were previously expensed and which related to resources to allow it to deliver services under its contracts and active software licence arrangements. In certain situations, costs associated with the installation of certain IT equipment in contracts have also been capitalised as non-current and current contract fulfilment assets, where relevant.

The adjustments to recognise non-current and current contract fulfilment assets on the balance sheet as at 1 January 2016 of £277.6m and £40.4m respectively recognise the net book value of the identified contract fulfilment assets at the opening balance sheet date.

These adjustments also include the recognition of certain costs of obtaining a contract. IFRS 15 specifies that the incremental costs of obtaining a contract with a customer are capitalised if the entity expects to recover them.

The cost of utilising these assets is recognised within cost of sales on a consistent basis over the life of the relevant customer contract.

The adjustment of £6.5m for the year ended 31 December 2016 is to recognise a net decrease in cost of sales due to the derecognition of contract costs now capitalised as contract fulfilment assets net of the utilisation charge recorded for the year in relation to these assets and the derecognition of certain contract fulfilment assets.

For the year ended 31 December 2016, the above net adjustment of £6.5m comprises: non-current contract fulfilment additions of £63.5m, utilisation of £47.1m, and derecognition of £17.0m; software contract fulfilment additions of £13.0m, and utilisation of £7.1m; and current contract fulfilment asset additons of £41.6m, and utilisation of £40.4m.

Specific item

As disclosed in the 31 December 2016 financial statements, Capita ceased to work on the IT system transformation in respect of its contract with The Co-operative Bank plc. Under IFRS 15, this modification has led to an impairment of a contract fulfilment asset in respect of this contract as these costs were no longer considered recoverable.

The adjustment of £42.3m in the year ended 31 December 2016 recognises the charge incurred on derecognising this contract fulfilment asset. This item has been included within the other non-underlying column because it is one-off in nature and is due to a contractual dispute rather than arising as a result of service credit penalties.

Adjustment E – Tax

Due to the changes in assets, liabilities, income and expenses recognised as a result of the application of IFRS 15, there are consequent IAS 12 Income taxes differences that arise as discussed below.

38 FINANCIAL STATEMENTS RESTATEMENT UNDER IFRS 15 CONTINUED

Deferred tax

Due to the changes in the pattern and timing of revenue recognition under IFRS 15, a deferred income liability is recognised on the balance sheet from 1 January 2016, which will be recognised through the income statement in later periods. The impact of these revenue recognition changes is only recognised for tax purposes via a one-off transitional tax adjustment on 1 January 2017, so no tax deduction is available in 2016 for the reduction in historic revenue recognised.

Contract fulfilment assets have also been recognised on the balance sheet from 1 January 2016, which will be charged to the income statement in later periods. Under IAS 12, the tax base of an asset is the amount that will be deductible for tax purposes against any taxable economic benefits that will flow to an entity when it recovers the carrying amount of the asset. The tax base of the contract fulfilment asset recognised on the balance sheet prior to 1 January 2017 is therefore reduced by the amounts for which tax deductions have already been taken, creating a temporary difference.

Under the principles of IAS 12, a movement of £164.8m in deferred tax therefore arises, recognised as an increase in the deferred tax asset of £162.8m and a reduction in the deferred tax liability of £2.0m as at 1 January 2016 (31 December 2016: £192.9m movement, increase in deferred tax asset of £190.4m, and reduction in deferred tax liability of £2.5m) as a result of the transition to IFRS 15.

Income statement deferred tax credit

The deferred tax asset balance increase of £190.4m and the deferred tax liability decrease of £2.5m as at 31 December 2016, give rise to an income statement deferred tax credit of £28.1m for the year ended 31 December 2016.

Income statement current tax expense

There is no income statement current tax expense impact for the year ended 31 December 2016.

Adjustment F – decrease in trade and other receivables

The decrease in trade and other receivables relates to the restatement of accrued revenues as detailed in Adjustments B and C above. The decrease in non-current accrued income is £41.7m as at 1 January 2016, and £79.6m at 31 December 2016, and the decrease in current accrued income is £284.1m and £174.9m at 31 December 2016.

Adjustment G – Reclassification of trade and other payables

In order to provide users with relevant financial information in the primary financial statements, the Group has decided to reclassify deferred income into its own primary statement line item reflecting the materiality and nature of this balance in the context of the Group's business.

The decrease in trade and other payables relates to the reclassification and restatement of deferred income as discussed above. Prior to adoption of IFRS 15, deferred income was classified within 'Trade and other payables' although this was not accounted for as a financial liability.

Adjustment H – Reversal of accrued income impairments

In 2016, the Group recognised an impairment of £47.1m historic accrued income, of which £39.6m was recognised in underlying profit, and £7.5m within the specific items column in relation to the dispute with The Co-operative Bank plc. Under IFRS 15, this accrued income would not have been originally recognised as the timing of revenue recognition has changed in comparison to the previous accounting policy as discussed in Adjustment C above, hence the adjustment of £47.1m for the year ended 31 December 2016 recognises the reversal of these previous impairments.

Adjustment I – Reclassification of significant restructuring

Following the adoption of IFRS 15, the Board has adopted a policy to separately disclose the in-year operating profit/loss from significant new contract wins and related, or significant, restructuring ('Significant new contract wins and restructuring') within underlying results, in order for users of the financial statements to obtain a proper understanding of the financial information and the performance of the business.

The Group continually assesses the resourcing levels, both at a divisional level and also in relation to the management and delivery of individual contracts. This results in restructuring in the normal course of business and any such charges are recorded in 'underlying before significant new contract wins and restructuring' results. A significant restructuring is assessed as that above this normal level of restructuring.

In the year ended 31 December 2016, the Board announced a major programme, with the restructuring of the Group into 6 new reporting divisions under a Group-wide programme. The cost of this Group-wide programme, £59.4m (£57.2m: continuing operations), was charged to specific items, being the element above the normal level of restructuring undertaken by the Group. Following the adoption of the above policy, the 2016 income statement has been restated to reclassify the cost of this programme to 'Significant new contract wins and restructuring' within underlying.

STATEMENT OF DIRECTORS' RESPONSIBILITY

The Directors confirm that, to the best of their knowledge:

a. the consolidated financial statements in this report, which have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union, IFRIC interpretations and those parts of the Companies Act 2006 applicable to companies reporting under IFRS, give a true and fair view of the assets, liabilities, financial position and profit of the Group taken as a whole;

b. the parent company financial statements in this report, which have been prepared in accordance with United Kingdom Accounting Standards (UK GAAP) and applicable law, give a true and fair view of the assets, liabilities, financial position and profit of the Company; and

c. the management report contained in this report includes a fair review of the development and performance of the business and position of the Company and the Group taken as a whole, together with a description of the principal risks and uncertainties that they face.

By order of the Board.

J Lewis
Chief Executive Officer

N Greatorex
Chief Financial Officer

23 April 2018

STATEMENT OF DIRECTORS' RESPONSIBILITIES IN RESPECT OF THE ANNUAL REPORT AND THE FINANCIAL STATEMENTS

The Directors are responsible for preparing the Annual Report and the Group and parent company financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare Group and parent company financial statements for each financial year. Under that law they are required to prepare the Group financial statements in accordance with International Financial Reporting Standards as adopted by the European Union (IFRSs as adopted by the EU) and applicable law and have elected to prepare the parent company financial statements in accordance with UK accounting standards, including FRS 101 Reduced Disclosure Framework.

Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and parent company and of their profit or loss for that period. In preparing each of the Group and parent company financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable, relevant, reliable and prudent;
- for the Group financial statements, state whether they have been prepared in accordance with IFRSs as adopted by the EU;
- for the parent company financial statements, state whether applicable UK accounting standards have been followed, subject to any material departures disclosed and explained in the parent company financial statements;
- assess the Group and parent company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and
- use the going concern basis of accounting unless they either intend to liquidate the Group or the parent company or to cease operations, or have no realistic alternative but to do so.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the parent company's transactions and disclose with reasonable accuracy at any time the financial position of the parent company and enable them to ensure that its financial statements comply with the Companies Act 2006. They are responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error, and have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

Under applicable law and regulations, the Directors are also responsible for preparing a strategic report, Directors' report, Directors' remuneration report and Corporate governance statement that complies with that law and those regulations.

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

Responsibility statement of the Directors in respect of the annual report

We confirm that to the best of our knowledge:

- the financial statements, prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and the undertakings included in the consolidation taken as a whole; and
- the strategic report includes a fair review of the development and performance of the business and the position of the issuer and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

Directors' statement on the annual report

The Directors consider the annual report, taken as whole, to be fair, balanced and understandable and that it provides the information necessary for the shareholders to assess the Company's position and performance, business model and strategy.

The Directors' report and the strategic report (pages 3–48) have been approved by the Board.

J Lewis
Chief Executive Officer

N Greatorex
Chief Financial Officer

23 April 2018

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF CAPITA PLC

Independent auditor's report

to the members of Capita plc

1. Our opinion is unmodified

We have audited the financial statements of Capita plc ("the Company") for the year ended 31 December 2017 which comprise the consolidated income statement, consolidated statement of comprehensive income, consolidated balance sheet, consolidated statement of changes in equity, consolidated cash flow statement, company balance sheet, company statement of changes in equity, and the related notes, including the accounting policies in note 2 to the Group financial statements and note 1 to the Parent Company financial statements.

In our opinion:

- the financial statements give a true and fair view of the state of the Group's and of the Parent Company's affairs as at 31 December 2017 and of the Group's loss for the year then ended;
- the Group financial statements have been properly prepared in accordance with International Financial Reporting Standards as adopted by the European Union;
- the Parent Company financial statements have been properly prepared in accordance with UK accounting standards, including FRS 101 Reduced Disclosure Framework; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities are described below. We believe that the audit evidence we have obtained is a sufficient and appropriate basis for our opinion. Our audit opinion is consistent with our report to the audit committee.

We were appointed as auditor by the Directors on 18 August 2010. The period of total uninterrupted engagement is for the 8 financial years ended 31 December 2017. We have fulfilled our ethical responsibilities under, and we remain independent of the Group in accordance with UK ethical requirements including the FRC Ethical Standard as applied to listed public interest entities. No non-audit services prohibited by that standard were provided.

Overview	
Materiality: Group financial statements as a whole	£12m (2016:£12m) 4.8% (2016: 4.0%*) of normalised Group profit before tax
Coverage	82% (2016:82%*) of total Group revenue 85% (2016: 83%*) of total profits and losses before tax 78% (2016: 93%*) of total Group assets

** The 2016 coverage percentages have been calculated based on the financial statements before the restatement for the adoption of IFRS 15.*

Risks of material misstatement		vs 2016
Recurring risk for the Group and the Parent Company	Going concern	▲
New risk for the Group- non-recurring	IFRS opening balance restatement	
Recurring risks for the Group	Revenue and profit recognition	▲
	Impairment of intangible assets and goodwill	▲
	Items disclosed as 'non-underlying'	◄►
	Provisions and contingent liabilities	◄►
	Pensions obligations	◄►
New risk for the Group-recurring	Capitalisation and recoverability of contract assets	
Recurring risks for the Parent Company	Recoverability of Parent Company's investment in subsidiaries	◄►

2. Material uncertainty related to going concern

	The risk	Our response
Going Concern We draw your attention to note 2(b) on pages 97-98 which indicates that there is a material uncertainty relating to the Group and Parent Company's ability to continue as a going concern. The Board's going concern assessment and conclusion includes the anticipated receipts from the rights issue, which is dependent, inter alia, on shareholder approval and the underwriting agreement. The fact that a shareholder vote is required in order to raise additional capital through a rights issue, and that the underwriting agreement is subject to certain specific conditions which, although customary in nature, are outside the control of the Company. These events and conditions give rise to a material uncertainty that may cast significant doubt about the Group's and Parent's ability to continue as a going concern. We describe opposite how the scope of our audit has responded to this risk. Our opinion is not modified in respect of these matters.	**Accounting basis** The financial statements explain how the Board has formed a judgment that it is appropriate to adopt the going concern assumption as the basis of preparation for the Group and Parent Company. The assessment is based on future projections of both profit and cash, together with calculations of the headroom available when applying the key financial covenants over the period ending 31 December 2019. This assessment involves a consideration of future events and there is a risk that such judgments are inappropriate and do not include an appropriate allowance for the execution risk associated with such future plans. In addition there is judgement over what adjustments should be made to calculate the adjusted EBITDA figure used in the key financial covenant calculations and a risk that items excluded should not be. **Disclosure quality** Clear and full disclosure of the assessment undertaken by the Board and the rationale for using the going concern assumption, including the identification of any material uncertainties, represents a key financial statement disclosure requirement. There is a risk that insufficient details are disclosed to allow a full understanding of the assessment undertaken by the Board. Auditing standards require such matters to be reported as a key audit matter.	**Our procedures included:** – We tested the integrity of the cash flow projections and considered the appropriateness of key assumptions used in preparing those projections, with a specific focus on the cost reduction assumptions. We evaluated these via enquiries with each of the divisional Finance Directors and with the external advisors who assisted with the initial cost reduction review performed for the purpose of the base case projections. We also assessed the projections and assumptions by reference to our knowledge of the business and general market conditions and assessed the potential risk of management bias. – We re-performed calculations, for 30 June 2018, 31 December 2018, 30 June 2019 and 31 December 2019, prepared to test expected compliance with the key financial covenant tests to test mathematical accuracy. – We considered the adjustments made in the adjusted EBITDA for the covenant calculations, considering the appropriateness compared to the loan agreements and historical accepted practice with the current lenders. In addition, we inspected the correspondence between the Company and the private placement lenders that set out the proposed items to be excluded in the adjusted EBITDA definition and compared these against the items included in the covenant calculations. – We inspected also correspondence with the lenders concerning the key financial covenants, and any terms attaching (including the periods covered), and checked all were captured appropriately within the model to test continuing compliance for the period considered. – We challenged the level of sensitivities applied (including downside scenarios) for reasonableness based on our knowledge of the business and markets served, and we evaluated whether the Directors' plans to alleviate the downside risk evident from these scenarios were feasible in the circumstances.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF CAPITA PLC CONTINUED

The risk	Our response
See risk described on page 171.	– We inspected the terms of the proposed rights issue, including the underwriting agreements, to assess the impact on the forecast models and to check completeness of disclosures concerning the material uncertainties. – We considered the terms of all the Group's financing arrangements, including both committed and uncommitted facilities, and assessed any impacts arising from the proposed rights issue and how these had been factored into the forecast models. – We assessed the accuracy of the matters covered in the going concern disclosures by reference to: the internal company strategic plans; the Board considerations with regard to the transformation programme and initiatives as disclosed in the RNS dated 31 January 2018; communications and discussions with the sponsoring Banks; and enquiries with the Board concerning completion and timing of the proposed rights issue. – We also assessed the going concern disclosures for clarity, including that sufficient details were provided concerning the material uncertainties. **Our findings** We found the disclosures included in note 2(b) made by the Directors, including the material uncertainty description to be acceptable.

We are required to report to you if the Directors' going concern statement under the Listing Rules set out on pages 60-61 is materially inconsistent with our audit knowledge. We have nothing to report in this respect.

KPMG

3. Other key audit matters: our assessment of risks of material misstatement

Key audit matters are those matters that, in our professional judgment, were of most significance in the audit of the financial statements and include the most significant assessed risks of material misstatement (whether or not due to fraud) identified by us, including those which had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team.

Going concern is a significant key audit matter and is described in section 2 above. We summarise below the other key audit matters, in decreasing order of audit significance, in arriving at our audit opinion above, together with our key audit procedures to address those matters and, as required for public interest entities, our results from those procedures. All of these key audit matters were addressed, and our results are based on procedures undertaken, in the context of, and solely for the purpose of, our audit of the financial statements as a whole, and in forming our opinion thereon, and consequently are incidental to that opinion, and we do not provide a separate opinion on these matters.

	The risk	Our response
IFRS15 Opening Balance Restatement The adoption of IFRS15 has led to significant changes in the revenue recognition accounting policies adopted across the Group, and the recognition of contract fulfilment assets. The new accounting standard has been early adopted and applied retrospectively and has led to a number of adjustments being required to restate the opening balance sheet financial position and the comparative consolidated income statement (refer note 38).	**Accounting application** The new accounting policies require the exercise of judgment across a number of areas (see below for the recurring risks associated with revenue recognition and contract assets) and this gives rise to a significant audit risk. **Data capture** There is a risk that the adjustments made are not appropriate or do not capture all of the adjustments required under their retrospective option applied on transition. This requires application of the new standard on all the Group's contracts at the start of the earliest *period presented.* **Disclosure quality** There is a risk that the disclosures presented are not sufficient to explain the significant changes to the accounting policies following adoption of IFRS15, the impacts arising and the key judgments applied.	**Our procedures included:** – **Assessing principles**: we conducted a detailed assessment of the accounting policy papers prepared by the Group Finance team that detailed the new policies to be applied. These papers set out the Directors' interpretation of the requirements. We considered any alternative interpretations and assessed the appropriateness of the new policies using our audit knowledge of Capita. – **Control design**: we considered the models and questionnaires that were prepared by the Capita Finance team and the Company's external advisor, to capture the necessary adjustments and checked whether these were structured appropriately to obtain all of the information necessary to allow consideration of the impact of the new accounting policies. – **Assessing application**: we made enquiries over the scope of the project, including discussions with the Audit and Risk Committee, to assess the coverage across all of the Group's contracts and whether this appropriately covered all information back to the start of the earliest period being adjusted. – **Tests of detail**: we substantively tested the restatements of the opening consolidated balance sheet as at 1 January 2016 and the consolidated income statement for the year ended 31 December 2016, which included testing the individual models for each of the major contracts and then on a sample of other contracts, and such testing included: • checking whether the underlying accounting policies have been appropriately applied and quantified; • agreement of the key assumptions back to our previous audit work, and / or underlying contracts to check facts and circumstances; and • agreement of the IFRS15 adjustments back to the underlying accounting trackers that collated all differences to be posted at a Group level. – **Tests of detail**: where no adjustments had been identified as part of the transition to IFRS15, we corroborated the divisional Finance Directors' assessment by assessing the questionnaires completed by the business units utilising our knowledge of the business gained from our audits.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF CAPITA PLC CONTINUED

The risk	Our response
See risk described on page 173.	– **Assessing principles**: we assessed the Group's accounting policy and detailed guidance issued in terms of the criteria for capitalising costs by reference to the requirements and principles set out in IFRS15. – The Directors made assessments of the costs at contract inception that would have been capitalised had IFRS15 been in place at that time. We considered the processes adopted to apply the necessary hindsight adjustments. This included analysing the revenues allocated to the transformation stages, against which contract costs were incurred, and from this data deriving an estimate of the appropriate level of costs to capitalise. – We discussed with the Audit and Risk Committee the judgments being applied and the specific representations sought as part of the audit from the divisional Finance Directors regarding the appropriateness of the hindsight process applied and key judgments made. – **Tests of detail**: we obtained a breakdown of contract fulfilment assets and other assets capitalised at 1 January 2016 and 31 December 2016 and selected a sample of these assets based on both quantitative and qualitative criteria. – Where hindsight was applied we considered the adjustments on a sample basis by reference to our prior years' audit work and where appropriate checked the facts and circumstances back to the original contract terms. We recalculated the adjustments made and considered any cost inefficiencies via discussion with the individual project managers, Finance Directors and divisional Finance Directors. – **Assessing transparency**: we considered the disclosures in the financial statements to check that these were comprehensive and provided sufficient detail of the impacts of applying the new standard, and of the key judgments applied under the new policies adopted. **Our findings**: We found the adjustments made to restate the opening balance sheet financial position and the comparative consolidated income statement for the adoption of IFRS15 to be acceptable.

	The risk	Our response
Revenue and profit recognition Reported Group revenue of £4,234.6 million (2016: £4,368.6 million). Refer note 2(e), and Audit and Risk Committee report (pages 66-74). Group revenue is derived from long term contracts and sales of software with ongoing upgrade agreements.	**Accounting treatment** Professional standards require us to make a rebuttable presumption that the fraud risk from revenue is a significant risk. The incentive/pressures on management to achieve bonus targets and/or market consensus increase the risk of fraudulent revenue recognition. **Subjective estimate** Following the adoption of IFRS15 the significant risk on long-term contracts relates to revenue recognised from variations or scope changes, where significant judgment is required to be exercised by the Board. There is a risk that revenue may be recognised even though it is not probable (i.e., not more likely than not) that consideration will be collected, which could be due to uncertainties over contractual terms and ongoing negotiations with customers. For long term contracts, the contractual arrangements can be complex with regard to variable consideration and service performance measures. This can involve significant judgments that may impact the recognition of revenue and contract profits including, among others, those over: – the interpretation of contract terms concerning future obligations; – the allocation of revenue to performance obligations; – the combining of performance obligations where the services are inter related; and – the consideration of onerous contract conditions and associated loss provisions. **Disclosure quality** There is a risk that the disclosures presented are not sufficient to explain revenue recognition accounting policies and the key judgments applied.	Our audit procedures vary between revenue from long-term contracts, and revenue from sales of software. **Tests of detail – both contract types:** – The key judgment associated with the new revenue recognition policy relates to future contract price variations or scope changes and to address this we obtained and inspected a sample of the contractual agreements to understand the contract terms and conditions that underpin the revenue and the profit recognition assumptions and to identify conditions under which variable revenue can arise. – Where contract negotiations are ongoing in relation to variable consideration we discussed the current status with those involved in the negotiations. – We considered the assumptions within the business plans and lifetime assessments, checking that onerous contracts had been recognised appropriately, particularly on contracts that have had a poor performance in the current year. – In determining whether onerous contract provisions should be recorded, we assessed contract profitability forecasts by analysing historic performance relative to contractual commitments over its full term. This included critically assessing the assumptions over future costs including projected savings and the actions required to achieve these by comparison to historical cost savings achieved on similar projects. **Tests of detail:** for revenue from long-term contracts: – where significant variable consideration had been recognised, we obtained and inspected the contractual agreements to understand the contract terms and conditions that underpin the revenue recognition assumptions; – where relevant we also inspected correspondence with customers or other supporting documentation in relation to the variations or scope; and – we challenged whether the judgments made by the Board are appropriate based on the underlying contractual terms and evidence obtained.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF CAPITA PLC CONTINUED

The risk	Our response
See risk described on page 175.	**Tests of detail:** for revenue from sales of software: – we obtained and inspected the contractual agreements for a sample of sales made in the period, along with supporting documentation in relation to services delivered; – in particular we assessed on a sample basis revenue recognition recognised immediately prior to the year end to check whether it was appropriately recognised and/or carried forward where the software licence sale 'met the criteria for bundling with the ongoing upgrade and maintenance contract(s); and – we assessed whether the revenue recognised in year is appropriate based on the contractual terms and the requirements of IFRS15 to defer revenue where future obligations exist. – **Assessing transparency**: we considered the disclosures in the financial statements to check that these were comprehensive and provided sufficient detail of the revenue recognition policies and of the key judgments applied. **Our findings**: We found the amounts of revenue recognised to be acceptable.

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	The risk	Our response
Impairment of Intangible Assets and Goodwill The Group records goodwill of £1,367.9 million (2016 £2,175.6 million) and other intangible assets £444.2 million (2016: £578.6 million) – see notes 15 & 16. Refer the Audit and Risk Committee report on pages 66-74.	**Forecast based valuation** We consider the carrying value of intangible assets and goodwill and the risk over potential impairment to be a significant audit risk because of the inherent uncertainty involved in forecasting and discounting future cash flows, which are the basis of the assessment of recoverability. **Disclosure quality** There is a risk that the disclosures presented are not sufficient to explain the key assumptions that drive the value in use calculations, and the key sensitivities that the Board has considered. In addition there is a risk that the disclosures do not adequately explain the events and circumstances that led to the impairment charge recorded in 2017.	**Our procedures included:** – **Comparing valuations**: we compared the total amount of discounted cash flows as per the calculations to the Group's market capitalisation and assessed the rationale for the difference at the year end with the support of our own internal valuation specialists. – **Control operation**: we tested the principles and integrity of the Group's discounted cash flow model. – **Tests of detail**: we compared the cash flows used in the impairment model to the output of the Group's budgeting process and against the understanding we obtained about the business areas through our audit, and assessed if these cash flows were reasonable. – **Historical comparison**: we assessed the historical accuracy of the forecasts used in the Group's impairment model by considering actual performance against prior year budgets, and considering any relevant Group internal audit reports over this process. – **Benchmarking assumptions**: we used external data and our own internal valuation specialists to evaluate the key inputs and assumptions for growth and discount rates. – **Sensitivity analysis**: we performed sensitivity and break-even analyses for the key inputs and assumptions, and identified those cash-generating units we consider most sensitive to impairment. – **Assessing transparency**: we evaluated the adequacy of the disclosures related to the estimation uncertainty, judgments made and assumptions over the recoverability of intangible assets and goodwill, in particular checking that the sensitivity disclosures provided sufficient detail. We also assessed whether the disclosures adequately explained the events and circumstances that led to the impairment charge in 2017. **Our findings**: We found the amounts of intangible assets and goodwill recognised as at 31 December 2017 to be acceptable.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF CAPITA PLC CONTINUED

	The risk	Our response
Presentation of items as 'underlying' and 'non-underlying' Refer note 6 that details items reported as 'non-underlying' and the Audit and Risk Committee report on pages 66-74.	**Presentation appropriateness** The Group separately presents certain income and expenditure as 'non-underlying' on the face of the consolidated income statement. Its financial highlights and commentary refers to 'underlying' measures as well as those derived on an adopted IFRS basis. The reasoning behind this presentation is set out in notes to the financial statements. 'Non-underlying' items are not defined by IFRSs and therefore judgment is required by the Directors to identify such items as 'non-underlying' and to maintain the comparability of results with previous years and in accordance with the Group's accounting policy. As such there is a risk of management bias. Failure to disclose clearly the nature and impact of material non-underlying earnings may distort the reader's view of the financial result in the year.	**Our procedures included:** **Assessing principles:** – We communicated our consideration on the classification of underlying and non-underlying to the Audit and Risk Committee to inform the debate on the Board's assessment of the policy decision to present items as 'non-underlying items'. – We examined the presentation of underlying measures in the front half of the annual report and consider this against applicable guidelines (including the FRC publications on the presentation of alternative performance measures). **Assessing balance:** – We considered whether there are any items included in the underlying results that would be more appropriately classified as 'non-underlying' and vice versa. – We also assessed whether there was sufficient balance between credit and debit items that are so separately presented. – As part of this consideration, we assessed the consistency of application of the Group's accounting policy for the classification of 'non-underlying' items year-on-year and that the policy. **Assessing transparency:** – We assessed whether the basis of the 'underlying' financial information is clearly and accurately described and consistently applied and that all 'alternative performance measures', together with reconciliations to the adopted IFRS position, are shown with sufficient prominence in the annual report. **Our findings:** We found the amounts presented for underlying' and 'non-underlying' to be acceptable.

	The risk	Our response
Provisions and Contingent Liabilities See note 27 for details of the provisions totalling £212.6 million as at 31 December 2017 (2016: £160.7 million) and note 33 for a discussion on the contingent liabilities identified. Also refer the Audit and Risk Committee report on pages 66-74.	**Subjective estimates** Significant judgment is required to assess whether actual or potential claims, litigation or fines arising from regulatory oversight, or from contractual arrangements with customers and suppliers, should be recognised as provisions within the financial statements or warrant disclosing as contingent liabilities. The determination and estimation of amounts for these provisions is inherently judgmental by their nature and there is a risk that the estimate is incorrect and any provision is materially misstated. ***Disclosure quality*** Where the impact of possible and present obligations is not probable or not reliably measurable, and thus no provision is recorded, failure to adequately disclose the nature of these circumstances within the financial statements may distort the reader's view as to the potential risks faced by the Group.	**Our procedures included:** – **Personnel interviews:** We enquired of the Directors and inspected board minutes for actual and potential claims arising in the year based on any external communications with the Group as noted in any Board discussions, and assessed whether provisions are required for these claims. Our enquiries are included as standard questions in all our meetings with those responsible for preparing the financial statements including the divisional Finance Directors, heads of functions at Group and corporate level, and the Executive Directors. **Tests of detail:** – we obtained an understanding and status of existing claims and litigations via enquiries and examining any relevant correspondence. This included enquiries of the Directors' assessment regarding the likelihood of the existence of obligations, and the basis used to measure any provisions; – We compared the Directors' estimate of the risk and impact of these claims and litigations to third party evidence, where available; – In respect of open matters of claims and litigations, where appropriate, we had discussions with the Group's external legal advisors in respect of the reasonableness of the estimated liability. – **Assessing transparency:** we evaluated the adequacy of the Group's provisions and contingent liability disclosures in the financial statements in accordance with accounting standards, and in particular the disclosure of the estimation uncertainty and the quantification of that uncertainty where appropriate. **Our findings:** We found the amounts included for provisions to be acceptable. We found the disclosures included for provisions and contingent liability to be acceptable.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF CAPITA PLC CONTINUED

	The risk	Our response
Pensions obligations See note 34 for details of the Group pension schemes and their obligations as at 31 December 2017. Also refer to the Audit and Risk Committee report on pages 66-74.	**Subjective estimation** Significant estimates are made in estimating the Group's defined benefit pension obligations and small changes in assumptions and estimates used would have a significant effect on this amount. There is a risk that the assumptions applied are not appropriate in the context of the pension scheme arrangements. **Disclosure quality** There is a risk that the disclosures presented are not sufficient to explain the key assumptions that the Board has adopted for the purpose of valuing the pension obligations.	**Our procedures included:** – **Assessing valuer's credentials:** we evaluated the competence and independence of the external actuaries who are engaged by the Group to estimate the pension scheme obligations for the purpose of the financial statements. – **Methodology choice:** we used our internal actuary specialists to consider and critically assess the methodologies applied including benchmarking the key assumptions applied in determining the Group's defined benefit obligations, being the discount rate, inflation rate and mortality/life expectancy. This included a comparison of these key assumptions against externally derived data. – **Assessing transparency:** we evaluated the adequacy of the disclosures in respect of the sensitivity of the obligations to these assumptions. **Our findings:** We found the amounts included for pension schemes obligations to be acceptable.
Capitalisation and recoverability of contract assets The adoption of IFRS15 has led to the recognition of contract fulfilment assets (see note 18) in addition to other contract assets including intangible assets and prepayments. Refer notes 2(e) & 18, and Audit and Risk Committee report (pages 66-74).	**Accounting application** IFRS15 requires that costs incurred on a contract, or an anticipated contract that generate or enhance the resources of an entity to deliver the contract should be capitalised and amortised over the expected life of the contract. **Subjective estimate** Judgment is required in applying the accounting policy that Capita has introduced to assess whether the costs incurred will enhance the future economic benefits to the Company. Where a contract is not performing as expected the costs capitalised may not be recoverable and an impairment of the asset may need to be recorded. Contract fulfilment assets are required to be amortised over the expected life of the contract and this requires an estimate of any likely contract extensions. **Disclosure quality** There is a risk that the disclosures presented are not sufficient to explain the capitalisation criteria that are used to assess whether items of expense should be recorded as a contract asset.	**Our procedures included:** **Tests of detail:** – We tested on a sample basis the costs capitalised in 2017 as contract fulfilment assets by reference to the criteria set out in the Group's accounting policy. For each of the assets sampled we obtained third party support, or for internally generated time, we obtained the relevant costing rates and records, to support the basis of capitalisation. – We also selected a sample of prepayments at 31 December 2017 and obtain third party support. – **Sensitivity analysis:** where a contract has performed below budget, we assessed whether there was uncertainty in regard to the recoverability of the contract fulfilment asset through future contract profitability. – **Tests of detail:** we considered on a sample basis the useful economic lives applied to the contract fulfilment assets and assessed the expected contract life by reference to the contract terms or where appropriate any agreed extensions to the original contract. – **Assessing transparency:** we considered the disclosures in the financial statements to check that these provided sufficient detail of the criteria used to assess whether expense items should be recorded as a contract asset. **Our findings:** We found the amounts of contract assets recognised to be acceptable.

	The risk	Our response
Recoverability of the Parent Company's investment in, and amounts due from, its subsidiaries Investment carrying value £220.2 million (2016: £311.0 million), and amounts due from subsidiaries £992.7m (2016: £1,001.8m). Refer to note 1 (accounting policies) and notes 8-9 (financial disclosures) and Parent Company Balance Sheet.	**Low risk, high value** The carrying amount of the Parent Company's investment in, and amounts due from, its subsidiaries represents 11.2% and 50.7% (2016: 14.2% and 45.8%) of its total assets respectively. The recoverability is not at a high risk of significant misstatement or subject to significant judgment. However, due to its materiality in the context of the Parent Company financial statements, this is considered to be the area that had the greatest effect on our overall Parent Company audit.	**Our procedures included:** – **Tests of detail**: we compared the carrying amount of the investment, and the amounts due from subsidiaries, with the relevant subsidiary's draft statutory balance sheet to identify whether its net assets, being an approximation of its minimum recoverable amount, was in excess of its carrying amount and assessed whether the subsidiary has historically been profit-making. **Our findings**: we found the Parent Company's assessment of the recoverability of the investment in subsidiaries to be acceptable.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF CAPITA PLC CONTINUED

4. Our application of materiality and an overview of the scope of our audit

The materiality for the Group financial statements as a whole was set at £12.0 million, determined with reference to a benchmark of normalised Group profit before tax of £251.5 million, of which it represents 4.8%.

In order to set this benchmark we consider the nature of items included within non-underlying earnings. Group reported loss before tax from continuing operations is £513.1 million. We add back certain non-underlying items including the non-trading business exit disposal expense – £13.7 million (note 4); losses on business disposals – £30.6 million (note 4); impairments of other non-current assets – £63.5 million (note 6); impairments of life and pension assets – £61.2 million (note 6); impairment charges against goodwill and acquired intangibles – £565.6 million (note 6); claims and litigation provisions expense – £30.0 million (note 6). Total adjustments to reported profit before tax amount to £764.6 million resulting in a normalised Group profit before tax for materiality purposes of £251.5 million.

Materiality for the prior year was set at £12.0 million determined with reference to a benchmark of normalised Group profit before tax of £302.8 million (as was originally reported in that year), of which it represented 4.0%.

In order to set that benchmark we considered the nature of items included within non-underlying earnings. Group originally reported profit before tax was £74.8 million. We added back costs or excluded income arising from certain non-underlying items including the non-trading business exit disposal income – £2.7 million (note 4); profits on business disposals – £0.1 million (note 4); impairments of contract related assets – £58.3 million (note 6); impairment charges against goodwill and acquired intangibles – £81.3 million (note 6); restructuring costs of £59.4 million; the asset services settlement provision – £13.4 million (note 6); income arising from The Co-operative Bank contract dispute as originally reported– £18.4 million (note 6). Total adjustments to originally reported profit before tax amounted to £228.0 million resulting in an originally reported normalised Group profit before tax for materiality purposes of £302.8 million).

The Parent Company materiality is set at £7.8 million (2016: £12.0 million), as communicated by the Group audit team. This is lower than the materiality we would otherwise have determined by reference to total assets, and represents 0.7% of the Company's total assets (2016: 0.5%).

We report to the Audit and Risk Committee any corrected or uncorrected identified misstatements with a profit impact in excess of £0.6 million (2016: £0.6 million), in addition to other identified misstatements that warranted reporting on qualitative grounds.

Audits for Group reporting purposes were performed by component auditors at 29 (2016: 36) key reporting components in the United Kingdom, Switzerland, Germany, and by the Group audit team over 2 key components in the United Kingdom (2016: in the United Kingdom, Switzerland, Germany, Ireland and Guernsey and by the Group audit team over 2 key components in the United Kingdom).

The Group audit team, with the assistance of the component auditors where appropriate, performed procedures on the items excluded from normalised Group profit before tax. These procedures covered approximately 81.5% of total Group revenue (2016: 81.7% as originally reported); 85.0% of the total profits and losses that made up Group profit before tax (2016: 82.5% as originally reported); and 78.3% of total Group assets (2016: 92.6% as originally reported). For the remaining components, we performed analysis at an aggregated Group level to re-examine our assessment that there were no significant risks of material misstatement within these.

The Group operates a shared service centre in London, the outputs of which are included in the financial information of the components it services. The service centre is subject to risk-focused audit procedures, predominantly the testing of transaction processing and review controls. Additional procedures are performed at certain reporting components to address the audit risks not covered by the work performed over the shared service centre.

The Group audit team approved the component materiality levels, which ranged from £0.1 million to £7.8 million (2016: £0.2 million to £12 million), having regard to the mix of size and risk profile of the Group across the components.

Detailed audit instructions were sent to the component auditors. These instructions covered the significant audit areas that should be covered by these audits (which included the relevant risks of material misstatement detailed above) and set out the information required to be reported back to the Group audit team. Telephone conference meetings were held with component auditors throughout the audit. At these meetings, the findings reported to the Group team were discussed in more detail, and any further work required by the Group team was then performed by the component auditor.

5. We have nothing to report on the other information in the Annual Report

The Directors are responsible for the other information presented in the Annual Report together with the financial statements. Our opinion on the financial statements does not cover the other information and, accordingly, we do not express an audit opinion or, except as explicitly stated below, any form of assurance conclusion thereon.

Our responsibility is to read the other information and, in doing so, consider whether, based on our financial statements audit work, the information therein is materially misstated or inconsistent with the financial statements or our audit knowledge. *Based solely on that work we have not identified material misstatements in the other information.*

Strategic report and Directors' report

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

Directors' remuneration report

In our opinion the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006.

Disclosures of principal risks and longer-term viability

Based on the knowledge we acquired during our financial statements audit, we have nothing material to add or draw attention to in relation to:
- the Directors' confirmation within the viability statement (page 60) that they have carried out a robust assessment of the principal risks facing the Group, including those that would threaten its business model, future performance, solvency and liquidity;
- the Principal Risks disclosures describing these risks and explaining how they are being managed and mitigated; and
- the Directors' explanation in the viability statement of how they have assessed the prospects of the Group, over what period they have done so and why they considered that period to be appropriate, and their statement as to whether they have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.

Under the Listing Rules we are required to review the viability statement. We have nothing to report in this respect.

Corporate governance disclosures

We are required to report to you if:
- we have identified material inconsistencies between the knowledge we acquired during our financial statements audit and the Directors' statement that they consider that the annual report and financial statements taken as a whole is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group's position and performance, business model and strategy; or
- the section of the annual report describing the work of the Audit Committee does not appropriately address matters communicated by us to the Audit Committee.

We are required to report to you if the Corporate Governance Statement does not properly disclose a departure from the eleven provisions of the UK Corporate Governance Code specified by the Listing Rules for our review.

We have nothing to report in these respects.

6. We have nothing to report on the other matters on which we are required to report by exception

Under the Companies Act 2006, we are required to report to you if, in our opinion:
- adequate accounting records have not been kept by the Parent Company, or returns adequate for our audit have not been received from branches not visited by us; or
- the Parent Company financial statements and the part of the Directors' Remuneration Report to be audited are not in agreement with the accounting records and returns; or
- certain disclosures of Directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

We have nothing to report in these respects.

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INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF CAPITA PLC CONTINUED

7. Respective responsibilities

Directors' responsibilities

As explained more fully in their statement set out on page 169, the Directors are responsible for: the preparation of the financial statements including being satisfied that they give a true and fair view; such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; assessing the Group and Parent Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and using the going concern basis of accounting unless they either intend to liquidate the Group or the Parent Company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities

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

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

Irregularities – ability to detect

Our audit aimed to detect non-compliance with relevant laws and regulations (irregularities) that could have a material effect on the financial statements. In planning and performing our audit, we considered the impact of laws and regulations in the specific areas of anti-bribery and corruption, data protection, employment law, health and safety, regulatory capital and liquidity, pension regulation and certain aspects of company legislation. This recognises the broad range of business process outsourcing services offered by the Group that include financial and regulated activities in the Private Sector Partnerships and Professional Services divisions, and the Governmental nature of many of the group's customers in the Public Sector division. We identified these areas through discussion with the Directors and other management (as required by auditing standards) and from our sector experience. In addition we had regard to laws and regulations in other areas including financial reporting, and company and taxation legislation.

We considered the extent of compliance with those laws and regulations that directly affect the financial statements, being anti-bribery and corruption, data protection, employment law, health and safety, regulatory capital and liquidity, pension regulation and certain aspects of company legislation, as part of our procedures on the related financial statement items. For the remaining laws and regulations, we made enquiries of Directors and other management (as required by auditing standards).

We communicated identified laws and regulations throughout our team and remained alert to any indications of non-compliance throughout the audit. This included communication from the Group to component audit teams of relevant laws and regulations identified at Group level, with a request to report on any indications of potential existence of irregularities in these areas, or other areas directly identified by the component team.

As with any audit, there remained a higher risk of non-detection of irregularities, as these may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal controls.

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

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

Robert J Brent (Senior Statutory Auditor)
for and on behalf of KPMG LLP, Statutory Auditor
Chartered Accountants
15 Canada Square, London, E14 5GL
23rd April 2018

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COMPANY BALANCE SHEET
AS AT 31 DECEMBER 2017

	Notes	2017 £m	2016 £m
Fixed assets			
Intangible assets	5	29.7	16.1
Tangible assets	6	18.6	16.3
Investments	8	220.2	311.0
		268.5	343.4
Current assets			
Financial assets	7	8.1	3.9
Debtors due within 1 year	9	1,099.5	1,063.5
Debtors due after more than 1 year	9	129.5	317.0
Cash		452.5	461.1
		1,689.6	1,845.5
Creditors: amounts falling due within one year	10	276.5	430.2
Provisions	10	130.4	5.8
Net current assets		1,282.7	1,409.5
Total assets less current liabilities		1,551.2	1,752.9
Creditors: amounts falling due after more than 1 year	10	281.4	715.5
		1,269.8	1,037.4
Capital and reserves			
Called up share capital	12	13.8	13.8
Employee benefit trust and treasury shares	12	(0.2)	(0.2)
Share premium account		501.3	501.3
Capital redemption reserve		1.8	1.8
Merger reserve		44.6	44.6
Profit and loss account		708.5	476.1
		1,269.8	1,037.4

The Accounts were approved by the Board of Directors on 23 April 2018 and signed on its behalf by:

J Lewis
Chief Executive Officer

N Greatorex
Chief Financial Officer

Company registered number: 2081330

COMPANY STATEMENT OF CHANGES IN EQUITY

FOR THE YEAR ENDED 31 DECEMBER 2017

	Share capital £m	Employee benefit trust and treasury shares £m	Share premium £m	Capital redemption reserve £m	Merger reserve £m	Profit and loss account £m	Total £m
At 1 January 2016	13.8	(0.3)	500.7	1.8	44.6	364.5	925.1
Profit for the year	–	–	–	–	–	330.9	330.9
Other comprehensive expense	–	–	–	–	–	–	–
Total comprehensive income for the year	–	–	–	–	–	330.9	330.9
Share based payment	–	–	–	–	–	(4.5)	(4.5)
Shares issued	–	0.1	0.6	–	–	–	0.7
Equity dividends paid	–	–	–	–	–	(214.8)	(214.8)
At 1 January 2017	13.8	(0.2)	501.3	1.8	44.6	476.1	1,037.4
Profit for the year	–	–	–			440.5	440.5
Other comprehensive expense	–	–	–	–	–	–	–
Total comprehensive income for the year	–	–	–	–	–	440.5	440.5
Share based payment	–	–	–	–	–	2.9	2.9
Equity dividends paid	–	–	–	–	–	(211.0)	(211.0)
At 31 December 2017	13.8	(0.2)	501.3	1.8	44.6	708.5	1,269.8

NOTES TO THE COMPANY FINANCIAL STATEMENTS

1 ACCOUNTING POLICIES

(a) Basis of preparation

The accounts are prepared under the historical cost convention and in accordance with applicable accounting standards.

In determining the appropriate basis of preparation of the financial statements for the year 31 December 2017, the Directors are required to consider whether the Company can continue in operational existence for the foreseeable future. The Board has concluded that it is appropriate to adopt the going concern basis, having undertaken a rigorous assessment of the financial forecasts and with consideration of the anticipated net proceeds from the announced Rights Issue which the Board is confident will be approved.

The Group's committed revolving credit facility, bank term loan facilities and private placement notes are subject to compliance with covenant requirements including maximum ratios of adjusted net debt to adjusted EBITDA. The Group's covenanted maximum ratio is 3.0 times or to 3.5 times depending on the debt instrument in question. They are tested semi-annually.

The Group has net debt of £1,117.0m at 31 December 2017 (2016: £1,778.8m) and adjusted net debt of £1,219.4m at 31 December 2017. (2016: £1,809.3m). The components of net debt and adjusted net debt are shown in the table below. Net debt is reported in note 31 – additional cash flow information. Adjusted net debt is used to calculate the gearing ratio adjusted net debt to adjusted EBITDA (refer to Alternative Performance Measures on pages 202 to 204).

The Group's calculation of adjusted net debt to adjusted EBITDA at 31 December 2017 is 2.27 times and is compliant with the relevant ratios.

Net debt and adjusted net debt	Notes	2017 £m	Restated 2016 £m
Cash, cash equivalents and overdrafts	21, 31	478.4	565.8
Other loan notes	31	(0.3)	(0.3)
Private placement loan notes	31	(1,664.0)	(1,961.7)
Interest and currency swaps in relation to USD denominated loan notes	31	176.8	357.9
Interest rate swaps in relation to GBP denominated loan notes	31	5.4	7.7
Term loan	31	(100.0)	(650.0)
Finance leases	31	(0.2)	(2.3)
Total net liabilities from financing activities		(1,582.3)	(2,248.7)
Underlying net debt		(1,103.9)	(1,682.9)
Fixed rate interest rate swaps	31	–	(85.1)
Deferred consideration	31	(13.1)	(10.8)
Net debt		(1,117.0)	(1,778.8)
Contingent obligations under bonds and guarantees	33	(88.4)	(30.5)
Money Market Funds		(14.0)	–
Adjusted net debt		(1,219.4)	(1,809.3)

On 31 January 2018, the Group announced a multi-year transformation plan, encompassing strategy, cost competitiveness, sales, IT and its capital structure, to improve the performance of Capita over the medium-to-long term. This transformation plan includes an assessment of the appropriate financial leverage for the Group over the medium term, to ensure that Capita has a sustainable capital base to support its customers and operations, increase investment in the business and deliver future strategy. The Board's view is that the appropriate leverage for Capita over the medium term should be between 1.0 and 2.0 times adjusted net debt to adjusted EBITDA. Accordingly, the Board has decided to raise additional equity of £701m by way of a Rights Issue, which is fully underwritten by Citigroup Global Markets Limited and Goldman Sachs International.

The transformation plan is being finalised, and the key actions and forecast impacts incorporated into detailed business plans. These are in support of the new strategy that has been reviewed and approved by the Board. Details of the new strategy are outlined in the Chief Executive Officer's Review on pages 6 to 12.

For the purpose of the going concern assessment the Directors have considered a base case set of projections that cover the first two years of the new strategic plan, to 31 December 2019. This base case includes cost reduction identified to date but not the anticipated proceeds from the Rights Issue and planned strategic disposals, and therefore importantly does not include the investment these will enable the Group to make, and the benefits these will deliver over the longer term.

The Group's committed facilities and private placement notes are subject to compliance with covenant requirements including maximum ratios of adjusted net debt to adjusted EBITDA. This covenant threshold is tested semi-annually, and is set at 3.0 times to 3.5 times depending on the debt instrument in question. The Directors have applied judgement in terms of how the ratio is calculated by applying the same treatment that has been applied in preparing and presenting the financial statements. Accordingly, items that are presented as non-underlying are excluded from the covenant definition of adjusted EBITDA (with the exception of acquisition costs), as are restructuring costs that are not presented within the underlying results as set out in note 3 to the consolidated financial statements. This basis of calculation is consistent with the approach adopted in prior years.

In assessing the going concern assumption, the Board has undertaken a rigorous assessment of the forecast outturns and assessed identified downside risks and mitigating actions, by reference to the relevant covenant tests. The downside risks include a number of severe but plausible scenarios, incorporating underperformance against the business plan, unexpected cash outflows and customer attrition and unwillingness to award the Group new contracts and extensions to existing arrangements. The Board has considered mitigating actions available to the Group in response to these sensitivities

Whilst the 'base case' scenario shows the business can operate in compliance with its adjusted net debt to adjusted EBITDA covenants applying the reasonable downside scenarios indicate that, absent the anticipated net proceeds from the announced Rights Issue, and assuming no other mitigating actions are taken by the Group, the available headroom is not sufficient to operate within the 3.0 times adjusted net debt to adjusted EBITDA covenant test. The Board has therefore considered the Rights Issue net proceeds in its assessment of going concern and the Group's ability to realise their assets and discharge their liabilities in the normal course of business.

NOTES TO THE COMPANY FINANCIAL STATEMENTS CONTINUED

1 ACCOUNTING POLICIES CONTINUED

Rights Issue

The Company has today launched a Rights Issue to raise £701m.

The Rights Issue will be subject to shareholders' approval and the general meeting to approve the equity raise scheduled for 9 May 2018.

The Rights Issue is fully underwritten for £701m, by Citigroup Global Markets Limited and Goldman Sachs International.

Material uncertainties

In assessing the going concern assumptions, the Board has reviewed the base case plans, identified downsides and anticipated receipt of proceeds from the Rights Issue. Following this assessment, the Board has a reasonable expectation that the Company and the Group will be able to operate as a going concern for the foreseeable future.

In undertaking the assessment, the Board has considered the fact that a shareholder vote is required in order to raise additional capital through the Rights Issue, and that the underwriting agreement is subject to certain specific conditions which, although customary in nature, are outside the control of the Company. These events and conditions indicate a material uncertainty on the completion of the Rights Issue which may cast significant doubt about the Group's and parent company's ability to continue as a going concern.

The Board is confident that the Rights Issue will be approved and the proceeds received and based on this expectation believes that, even in a reasonable downside scenario, the Group and parent company will continue to have adequate financial resources to realise their assets and discharge their liabilities as they fall due. Accordingly, the Directors have formed the judgement that it is appropriate to prepare the financial statements on the going concern basis. Therefore, the financial statements do not include any adjustments which would be required if the going concern basis of preparation is inappropriate.

The auditors' report on pages 170 to 184 refer to this material uncertainty, and their opinion is not qualified or modified in this regard.

A separate profit and loss account dealing with the results of the parent company undertaking only has not been presented as provided by Section 408 of the Companies Act 2006.

(b) Compliance with accounting standards

These financial statements have been prepared in accordance with Financial Reporting Standard 101 – Reduced Disclosure Framework (FRS 101).

In preparing these financial statements, the Company applies the recognition, measurement and disclosure requirements of International Financial Reporting Standards as adopted by the EU (Adopted IFRSs), but makes amendments where necessary in order to comply with Companies Act 2006 and has set out below where advantage of FRS 101 disclosure exemptions have been taken.

The consolidated financial statements are prepared in accordance with International Financial Reporting Standards as adopted by the EU (EU-IFRS) and are on pages 91 to 167 of this report. In these Company financial statements, the following disclosure exemptions available under FRS 101 have been applied:

- A cash flow statement and related notes;
- Comparative period reconciliations for share capital, tangible fixed assets, and intangible assets;
- Disclosures in respect of transactions with wholly-owned subsidiaries;
- The effects of new but not yet effective IFRSs;
- An additional balance sheet for the beginning of the earliest comparative period following the retrospective change in accounting policy; and
- Disclosures in respect of the compensation of key management personnel.

As the consolidated financial statements include equivalent disclosures, the Company has also taken the disclosure exemptions under FRS 101 available in respect of the following disclosures:

- Certain disclosures required by IFRS 2 Share Based Payments in respect of Group settled share based payments;
- Certain disclosures required by IAS 36 Impairments of assets in respect of the impairment of goodwill and indefinite life intangible assets;
- Certain disclosures required by IFRS 3 Business Combinations in respect of business combinations undertaken by the Company in the prior periods; and
- Disclosures required by IFRS 7 Financial Instrument Disclosures.

(c) Tangible fixed assets

Depreciation is provided on all tangible fixed assets at rates calculated to write-off the cost on a straight-line basis over the expected useful lives of the assets concerned, as follows:

Computer equipment	3 to 10 years
Furniture, fixtures and equipment	4 to 5 years
Leasehold improvements	over the period of the lease

(d) Intangible assets

Intangible assets are valued at cost less any accumulated amortisation and any impairment losses. Amortisation is calculated to write-off the cost in equal annual instalments over their estimated useful life of 3 to 15 years. In the case of capitalised software development costs, research expenditure is written off to the statement of profit and loss in the period in which it is incurred. Development expenditure is written off in the same way unless and until the Company is satisfied as to the technical, commercial and financial viability of individual projects. Where this condition is satisfied, the development expenditure is capitalised and amortised over the period during which the Group is expected to benefit.

(e) Investments

Fixed asset investments are shown at cost, less provisions for impairment.

Investments held as current assets are stated at the lower of cost and net realisable value.

The carrying values of fixed asset investments are reviewed for impairment if events or changes in circumstances indicate the carrying values may not be recoverable.

1 ACCOUNTING POLICIES CONTINUED

(f) Pension schemes

The Company maintains a number of defined contribution schemes and contributions are charged to the profit and loss account in the year in which they are due. These schemes are funded and the payment of contributions is made to separately administered trust funds. The assets of these schemes are held separately from the Company. The Company remits monthly pension contributions to Capita Business Services Limited, a subsidiary undertaking, which pays the Group liability centrally. Any unpaid contributions at the year-end have been accrued in the accounts of that company.

The Company also has employees who are members of defined benefit schemes operated by the Group. As there is no contractual arrangement or stated group policy for charging the net defined benefit cost of the plan to participating entities, the net defined benefit cost of the pension plan is recognised fully by the sponsoring employer. The Company then recognises a cost equal to its contribution payable for the period.

The contributions payable by the participating entities are determined on the following basis:

The Capita Pension & Life Assurance Scheme (the Capita DB Scheme) provides benefits on a defined benefit basis funded from assets held in a separate trustee-administered fund.

The Capita DB Scheme is a non-segregated scheme but there are around 200 different sections in the Scheme where each section provides benefits on a particular basis (some based on final salary, some based on career average earnings) to particular groups of employees. Of these sections, around 50 include members currently accruing benefits.

At each funding assessment of the Capita DB Scheme (carried out triennially), the contribution rates for those sections containing active members are calculated. These are then rationalised such that sections with similar employer contribution rates (when expressed as a percentage of pensionable pay) are grouped together and an average employer contribution rate for each of the rationalised groups calculated.

The Company's contribution is consequently calculated by applying the appropriate average employer contribution rates to the pensionable pay of its employees participating in the scheme.

Following the most recent funding assessment of the Capita DB Scheme which was carried out as at 31 March 2014, the Group entered into an agreement to make additional contributions to the Capita DB Scheme over a period of time until 2027. The next scheme funding assessment is being carried out with an effective date of 31 March 2017 and is expected to be finalised by 30 June 2018.

(g) Leasing commitments

Assets obtained under finance leases are capitalised in the balance sheet and depreciated over the shorter of the lease term and their useful economic lives.

The finance charges under finance leases and hire purchase contracts are allocated to accounting periods over the period of the lease and represent a constant proportion of the balance of capital repayments outstanding. Rentals due under operating leases are charged on a straight-line basis over the lease term.

(h) Deferred taxation

Deferred income tax is provided, using the liability method, on all temporary differences at the balance sheet date between the tax bases and liabilities and their carrying amounts for financial reporting purposes.

Deferred income tax liabilities are recognised for all taxable temporary differences:

- except where the deferred tax liability arises from the initial recognition of goodwill;
- except where the deferred income tax liability arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of taxable temporary differences associated with investments in subsidiaries, except where the timing of the reversal of the temporary timing differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred income tax assets are recognised for all deductible temporary differences, carry-forward of unused tax assets and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible differences and the carry-forward of unused tax assets and unused tax losses can be utilised, except where the deferred income tax asset relating to the deductible temporary differences arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction affects neither the accounting profit nor taxable profit or loss.

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

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the balance sheet date.

(i) Foreign currencies

Transactions in foreign currencies are recorded at the rate ruling at the date of the transaction or at the contracted rate if the transaction is covered by a forward exchange contract. Monetary assets and liabilities denominated in foreign currencies are translated at the rate of exchange ruling at the balance sheet date or if appropriate at the forward contract rate. All differences are taken to the profit and loss account with the exception of differences on foreign currency borrowings, to the extent that they are used to finance or provide a hedge against foreign equity investments, which are taken directly to reserves together with the exchange difference on the carrying amount of the related investments.

(j) National Insurance on share option gains

National Insurance on outstanding share options at the year-end has been grossed up and shown as a provision and a receivable on the balance sheet.

(k) Financial instruments: disclosure and presentation

A separate note dealing with the disclosures of IFRS 7 has been included in the consolidated financial statements on pages 141 to 149.

NOTES TO THE COMPANY FINANCIAL STATEMENTS CONTINUED

1 ACCOUNTING POLICIES CONTINUED

(l) Derivative financial instruments

The Company uses derivative financial instruments such as interest rate swaps and foreign currency contracts to hedge risks associated with interest and exchange rate fluctuations. Such derivative financial instruments are stated at fair value. The fair values of interest rate swaps and foreign currency contracts are determined by reference to market rates for similar instruments.

For the purpose of hedge accounting, hedges are classified as either: fair value hedges when they hedge the exposure to changes in the fair value of a recognised asset or liability; or cash flow hedges where they hedge exposure to variability in cash flows that is attributable to either a particular risk associated with a recognised asset or liability or a forecast transaction.

In relation to fair value hedges (e.g. fixed to floating interest rate swaps held as fair value hedges against fixed interest rate borrowings) which meet the conditions for hedge accounting, any gain or loss from re-measuring the hedging instrument at fair value is recognised immediately in the profit and loss account. Any gain or loss on the hedged item attributable to the hedged risk is adjusted against the carrying amount of the hedged item and recognised in the profit and loss account.

In relation to cash flow hedges the effective portion of the gain or loss on the hedging instrument is recognised directly in equity, while any ineffective portion is recognised immediately in the profit and loss account. Amounts taken to equity are transferred to the profit and loss account when the hedged transaction affects the profit and loss account, such as when the hedged financial income or financial expense is recognised or when a forecast transaction occurs. Where the hedged item is the cost of a non-financial asset or non-financial liability, the amounts taken to equity are transferred to the initial carrying amount of the non-financial asset or liability.

If the forecast transaction or firm commitment is no longer expected to occur, amounts previously recognised in equity are transferred to the profit and loss account. If the hedging instrument expires or is sold, terminated or exercised without replacement or rollover, or if its designation as a hedge is revoked, amounts previously recognised in equity remain in equity until the forecast transaction or firm commitment occurs.

For derivatives that do not qualify for hedge accounting, any gains or losses arising from changes in fair value are taken directly to the profit and loss account.

(m) Share based payments

The Company operates a number of executive and employee share schemes.

The cost of equity-settled transactions with employees is measured by reference to the fair value at the date at which they are granted and is recognised as an expense over the vesting period, which ends on the date on which the relevant employees become fully entitled to the award. Fair value is determined using an option pricing model. In valuing equity-settled transactions, no account is taken of any vesting conditions, other than conditions linked to the price of the shares of the Company (market conditions).

No expense is recognised for awards that do not ultimately vest, except for awards where vesting is conditional upon a market condition, which are treated as vesting irrespective of whether or not the market condition is satisfied, provided that all other performance conditions are satisfied.

At each balance sheet date before vesting, the cumulative expense is calculated, representing the extent to which the vesting period has expired and management's best estimate of the achievement or otherwise of non-market conditions, the number of equity instruments that will ultimately vest or in the case of an instrument subject to a market condition, be treated as vesting as described above. The movement in cumulative expense since the previous balance sheet date is recognised in the profit and loss account, with a corresponding entry in equity.

Subsidiary undertakings of the Company reimburse the Company through the intercompany account for charges attributable to their employees participating in the Company's share schemes.

2 DEFERRED TAXATION

	2017 £m	2016 £m
The deferred taxation included in the balance sheet is as follows:		
Accelerated capital allowances	(2.2)	(0.4)
Provisions	4.1	3.5
Included in debtors (note 9)	1.9	3.1

3 PROFIT ATTRIBUTABLE TO MEMBERS OF THE PARENT COMPANY UNDERTAKING

The profit after taxation dealt with in the accounts of the parent company undertaking was £440.5m (2016: £330.9m).

4 DIVIDENDS

	2017 £m	2016 £m
Declared and paid during the year		
Ordinary shares (equity):		
Final for 2016 paid: 20.6p per share (2015: 21.2p per share)	137.1	140.9
Interim for 2017 paid: 11.1p per share (2016: 11.1p per share)	73.9	73.9
	211.0	214.8
Proposed for approval at AGM (not recognised as a liability at 31 December)		
Ordinary shares (equity):		
Final for 2017: nil per share (2016: 20.6p per share)	–	137.0

5 INTANGIBLE ASSETS

	Capitalised software development £m	Other intangibles £m	Total £m
Cost			
1 January 2017	1.4	15.8	17.2
Additions	0.6	28.7	29.3
Intra Group Transfer	(1.2)	–	(1.2)
Disposal	(0.1)	(14.3)	(14.4)
Retirement	(0.1)	(0.1)	(0.2)
31 December 2017	0.6	30.1	30.7
Amortisation			
1 January 2017	0.1	1.0	1.1
Charge for year	0.1	1.9	2.0
Disposal	(0.1)	(1.8)	(1.9)
Retirement	(0.1)	(0.1)	(0.2)
31 December 2017	–	1.0	1.0
Net book value at:			
1 January 2017	1.3	14.8	16.1
31 December 2017	0.6	29.1	29.7

Other intangibles relates to software purchased from third parties.

6 TANGIBLE FIXED ASSETS

	Computer equipment £m	Short-term leasehold improvements £m	Total £m
Cost			
1 January 2017	32.1	1.2	33.3
Additions	11.3	–	11.3
Disposals	(14.5)	–	(14.5)
Asset retirements	(3.4)	(0.9)	(4.3)
31 December 2017	25.5	0.3	25.8
Depreciation			
1 January 2017	16.0	1.0	17.0
Charge for year	3.8	0.1	3.9
Disposals	(9.5)	–	(9.5)
Asset retirements	(3.4)	(0.8)	(4.2)
31 December 2017	6.9	0.3	7.2
Net book value at:			
1 January 2017	16.1	0.2	16.3
31 December 2017	18.6	–	18.6

7 FINANCIAL ASSETS

Current	2017 £m	2016 £m
Cash flow hedges	4.0	0.7
Non-designated foreign exchange forwards and swaps	4.1	3.2
	8.1	3.9

NOTES TO THE COMPANY FINANCIAL STATEMENTS CONTINUED

8 INVESTMENTS

Fixed asset investments

	Shares in subsidiary undertakings £m
Cost	
1 January 2017	311.0
Additions	26.1
Disposals	(99.4)
Impairment	(17.5)
31 December 2017	220.2

As reported in the Chief Executive Officer's review, significant actions are required to address recent operational and external challenges and a major transformational plan has been launched. Actions were taken in the prior year to implement a new simplified market facing organisation structure, and at the time of the interim results the Group announced an improved win rate against the backdrop of a quiet market. Since that date, the Group has continued to experience a higher level of revenue attrition than expected, and continued to experience delays in customer decision making and weakness in new sales.

In January 2018, the Company announced that the administration of Prudential's life and pensions business, around 2% of Group revenue, will be transferring from Capita to a new supplier later in 2018. As previously disclosed, another of the Group's life and pensions clients is conducting a strategic review, the outcome of which remains uncertain but is expected to result in the continuation of the contract with amended terms, or the termination of the contract.

As announced in January 2018, the Company has shifted its strategy, and set a plan, focusing on investment in people, sales capability and its transformation plan. The business plan for the divisions indicate there is likely to be a significant negative impact upon profits from contract and volume attrition, the dropping out of one-off items including contract and supplier-related profits which were reported in 2017 and increases in some cost items.

The transformation plan encompasses strategy, cost competitiveness, sales, IT and the Company's capital structure, to improve the performance of Capita over the medium-to-long term. The Board is confident that the transformation plan will deliver significant benefits to Capita over the medium-to-long-term and the associated disposal programme will support the re-positioning of the Group.

In undertaking the annual impairment review, the Directors have considered both external and internal sources of information, and any observable indications that may suggest that the carrying value of shares in subsidiary undertakings may be impaired. The continued operational and external challenges faced by the Group have led to a significant deterioration in new sales opportunities from the positions in March and September 2017. In addition, the Group has experienced contract terminations and attrition as highlighted above, and the transformation plan has identified areas that need to be addressed to rebuild and reposition Capita. These events and circumstances have led to the recognition of an impairment of shares in subsidiary undertakings as at 31 December 2017.

Direct investments	Country of registration and operation	Proportion of nominal value of issued shares held by the Company
Brokers Educational Supply Teachers Underwriting Agency Limited[2]	England	100%
Capita Legal Services Limited[2]	England	100%
Capita Financial Services Holdings Limited[1]	England	100%
Capita Group Insurance PCC Limited[2]	Guernsey	100%
Capita Gwent Consultancy Limited[2]	England	51%
Capita Holdings Limited[1]	England	100%
Capita International Limited[2]	England	100%
Capita Life & Pensions Regulated Services Limited[2]	England	100%
SIMS Holdings Limited[2]	England	0.001%
Capita Life & Pensions Services Limited[2]	England	100%

1 Investing holding company.
2 Outsourcing services company.

Certain subsidiaries of the Group have opted to take advantage of a statutory exemption from having an audit in respect of their individual statutory accounts. Strict criteria must be met for this exemption to be taken and has been agreed to by the Directors of those subsidiary entities. Listed in note 18 to the Company financial statements are subsidiaries controlled and consolidated by the Group, where the Directors have taken advantage of the exemption from having an audit of the entities' individual financial statements for the year ended 31 December 2017 in accordance with Section 479A of The Companies Act 2006.

In order to facilitate the adoption of this exemption, Capita plc, the parent company of the subsidiaries concerned, undertakes to provide a guarantee under Section 479C of the Companies Act 2006 in respect of those subsidiaries.

Details of all indirect subsidiaries, as required under Section 409 of the Companies Act 2006, are reported in note 18 to the Company financial statements.

During the year, the following direct investments of Capita plc were disposed of as part of the group disposal of the Capita Asset Services businesses:

- Capita International Financial Services Holdings Limited;
- Capita IRG Trustees Limited;
- Capita International Financial Services (Ireland) Limited;
- Capita Financial Investments Limited;
- Capita Fiduciary Group Limited;
- Capita (LLRP) Trustee Limited;
- Capita Alternative Fund Services (Guernsey) Limited; and
- Capita Financial Administrators (Guernsey) Limited.

9 DEBTORS

Debtors due within 1 year	2017 £m	2016 £m
Amounts owed by subsidiary undertakings	992.7	1,001.8
Taxation recoverable	15.3	25.6
Other debtors	4.9	1.9
Other taxes and social security	4.3	–
Other debt securities held – current	5.0	–
Currency swap – USD private placement loan notes	72.2	27.9
Prepayments and accrued income	5.1	6.3
	1,099.5	1,063.5

Debtors due beyond 1 year	2017 £m	2016 £m
Prepayments and accrued income	1.7	1.9
Deferred taxation	1.9	3.1
Currency swaps	113.1	293.8
Interest rate swaps	5.4	7.7
Cash flow hedges	7.4	10.5
	129.5	317.0

10 CREDITORS

Amounts falling due within 1 year	2017 £m	2016 £m
Amounts owed to subsidiary undertakings	72.8	95.7
Bank overdraft	161.8	309.9
Trade creditors	9.2	2.5
Other creditors	0.3	0.1
Accruals and deferred income	30.5	15.3
Fixed rate interest rate swaps	–	1.5
Cash flow hedge	1.9	4.5
Other taxes and social security	–	0.7
	276.5	430.2

Provisions	2017 £m
As at 31 December 2016	5.8
Reclassified from amounts falling due after more than 1 year	15.0
Provided/(released) in the year (net)	107.2
Utilisation	(2.6)
Intra group transfer	5.0
As at 31 December 2017	130.4

The majority of the provisions relate to the Capita Asset Services indemnity provision (£69.1m) and Business exit provision (£30.1m). Further detail on these provisions can be found in note 27 to the consolidated financial statements.

Amounts falling due after more than 1 year	2017 £m	2016 £m
Private placement loan notes	271.8	260.6
Term Loans	–	350.0
Currency swap	8.5	3.1
Cash flow hedges	1.1	3.2
Fixed rate interest rate swaps	–	83.6
Provisions	–	15.0
	281.4	715.5

The private placement loan notes are unsecured. The bank overdraft is guaranteed by cash held by other members of the Group.

NOTES TO THE COMPANY FINANCIAL STATEMENTS CONTINUED

11 DEFERRED TAXATION

	£m
At 1 January 2017	3.1
Utilisation of provisions in the year	(1.2)
At 31 December 2017 – included in debtors (note 9)	1.9

12 SHARE CAPITAL

	2017 (m)	2016 (m)	2017 £m	2016 £m
Allotted, called up and fully paid				
Ordinary shares of 2¹/₁₅p each				
At 1 January	670.1	670.0	13.8	13.8
Issued on exercise of share options	–	0.1	–	–
At 31 December	670.1	670.1	13.8	13.8

During the year, nil (2016: 131,037) ordinary 2¹/₁₅p shares with an aggregate nominal value of £nil (2016: £2,708) were issued under share option schemes for a total consideration of £nil (2016: £0.6m).

Treasury shares

	2017 (m)	2016 (m)	2017 £m	2016 £m
Ordinary shares of 2¹/₁₅p each				
At 1 January	3.2	5.8	(0.1)	(0.2)
Shares allotted in the year	(0.3)	(2.6)	–	0.1
At 31 December	2.9	3.2	(0.1)	(0.1)

In 2017, the Group made no purchases of shares into Treasury and allotted 0.3m (2016: 2.6m) shares with an aggregate nominal value of £4,420 (2016: £53,604). The total consideration received in respect of these shares was £nil (2016: £nil).

Employee benefit trust shares

	2017 (m)	2016 (m)	2017 £m	2016 £m
Ordinary shares of 2¹/₁₅p each				
At 1 January	1.7	2.2	(0.1)	(0.1)
Shares allotted in the year	(0.1)	(0.5)	–	–
At 31 December	1.6	1.7	(0.1)	(0.1)

The Group will use shares held in the employee benefit trust (EBT) in order to satisfy future requirements for shares under the Group's share option and long term incentive plans. During the year, the EBT allotted 0.1m (2016: 0.5m) ordinary 2¹/₁₅p shares with an aggregate nominal value of £1,434 (2016: £10,372) to satisfy exercises under the Group's share option and long-term incentive plans. The total consideration received in respect of these shares was £nil (2016: £nil).

The Group has an unexpired authority to repurchase up to 10% of its issued share capital.

13 COMMITMENTS AND CONTINGENT LIABILITIES

(a) At 31 December 2017, the Company was committed to making the following payments under non-cancellable operating leases and other agreements:

	2017 £m	2016 £m
Not later than 1 year	0.1	0.6
Later than 1 year but not more than 5 years	0.1	0.3
Over 5 years from the balance sheet date	–	–
	0.2	0.9

(b) The Company has a committed Revolving Credit Facility amounting to £600.0m (2016: £600.0m), of which £nil had been drawn down at 31 December 2017 (2016: £nil drawn down).

(c) The Group has provided, through the normal course of its business, performance bonds and bank guarantees of £88.4m (2016: £91.7m).

14 BORROWINGS

	2017 £m	2016 £m
Private placement loan notes	271.8	260.6
Term loans	–	350.0
	271.8	610.6
Repayments fall due as follows:		
Within 1 year	–	–
After more than 1 year:		
In more than 1 year but not more than 2 years	–	–
In more than 2 years but not more than 5 years	219.1	350.0
In more than 5 years	52.7	260.6
Total borrowings	271.8	610.6

The Company has issued guaranteed unsecured private placement loan notes as follows:

	Interest rate (%)	Denomination	EUR (m)	Maturity
Issued 2015				
Series A	2.125	EUR	230.0	10 November 2022
Series B	2.875	EUR	60.0	10 November 2027
Series C	2.125	EUR	20.0	10 November 2022
Total of euro denominated private placement loan notes			310.0	

All series are unsecured.

In 2017, the Company repaid £350.0m of December 2016 bridging facility debt. The Company has a committed Revolving Credit Facility amounting to £600.0m (2016: £600.0m), of which £nil had been drawn down at 31 December 2017 (2016: £nil drawn down).

15 RELATED PARTY TRANSACTIONS

In the following, figures for purchases and sales are for transactions invoiced during the year inclusive of Value Added Tax where applicable. All transactions are undertaken at normal market prices.

During the year, the Company sold goods/services in the normal course of business to Urban Vision Partnership Limited for £0.1m (2016: £0.1m). The Company purchased goods/services in the normal course of business for £nil (2016: £nil). At the balance sheet date, the net amount receivable from Urban Vision Partnership Limited was £nil (2016: £nil).

During the year, the Company sold goods/services in the normal course of business to Service Birmingham Limited for £0.4m (2016: £1.0m). The Company purchased goods/services in the normal course of business for £0.1m (2016: £0.1m). At the balance sheet date, the net amount receivable from Service Birmingham Limited was £nil (2016: £nil).

During the year, the Company sold goods/services in the normal course of business to Entrust Support Services Limited for £0.3m (2016: £0.5m). The Company purchased goods/services in the normal course of business for £nil (2016: £nil). At the balance sheet date, the net amount receivable from Entrust Support Services Limited was £nil (2016: £nil).

During the year, the Company sold goods/services in the normal course of business to AXELOS Limited for £0.2m (2016: £0.2m). The Company purchased goods/services in the normal course of business for £nil (2016: £0.8m). At the balance sheet date, the net amount receivable from AXELOS Limited was £nil (2016: £2.8m).

During the year, the Company sold goods/services in the normal course of business to Capita Glamorgan Consultancy Limited for £0.1m (2016: £nil). The Company purchased goods/services in the normal course of business for £nil (2016: £nil). At the balance sheet date, the net amount receivable from Capita Glamorgan Consultancy Limited was £0.1m (2016: £nil).

During the year, the Company sold goods/services in the normal course of business to Fera Science Limited for £1.8m (2016: £0.9m). The Company purchased goods/services in the normal course of business for £nil (2016: £nil). At the balance sheet date, the net amount receivable from Fera Science Limited was £1.5m (2016: £0.1m).

16 PENSION COSTS

The Company operates a defined contribution scheme.

The pension charge for the defined contribution scheme for the year was £4.7m (2016: £3.6m).

17 SHARE BASED PAYMENT

The Company operates several share based payment plans and details of the schemes are disclosed in note 30 of the Group's consolidated financial statements on pages 150 to 151.

The Group recognised an expense for share based payments in respect of employee services received during the year to 31 December 2017 of £2.9m (2016: £(4.5)m credit), all of which arises from equity-settled share based payment transactions. The total Company expense, after recharging subsidiary undertakings, charged to the profit and loss account in respect of share based payments was £1.2m (2016: £(2.1)m credit).

NOTES TO THE COMPANY FINANCIAL STATEMENTS CONTINUED

18 INDIRECT INVESTMENTS

Unless otherwise indicated, all shareholdings comprise ordinary shares, are owned indirectly by the Company and represent 100% of the issued share capital of the subsidiary. Dormant companies are marked (D). Companies sold or dissolved since 31 December 2017 are marked *. Companies are listed under their registered office address as at 31 December 2017.

Company Name	% ownership	Directly held by Capita plc	Share class
1004 Bin Harmoodah Building, Khalifa St., PO Box 113 740, Abu Dhabi			
Capita Property and Infrastructure Consultants LLC	49%		
12 Castle Street, St. Helier, JE2 3RT			
Capita Symonds (CI) Limited			
Symonds Group (Jersey) Limited (D)			(£0.10 Ordinary-a, £0.10 Ordinary-b, £0.10 Ordinary-c)
1603 C.C Wu Building, 302-308 Hennessy Road, Wan Chai, Hong Kong			
Capita IB Solutions (HK) Limited			
17 Rochester Row, London, SW1P 1QT			
ABS Network Solutions Ltd (D)			
Acutest Limited			
Aghoco 1005 Limited (D)			
Aghoco 1018 Limited (D)			
Amity Communications Limited			
AMT-Sybex (Engineering) Limited (D)			
AMT-Sybex Limited			
Aspire Business Solutions Ltd			
Atlas Master Trust Trustee Limited			
AXELOS Limited	51%		(£0.01 Ordinary B)
BCS Design Ltd			
Behavioural Health Limited (D)			
Beovax Computer Services Limited			
Booking Services International Limited			
Brentside Communications Limited (D)			
Brokers Educational Supply Teachers Underwriting Agency Limited (D)	100%	•	
BSI 360 Limited (D)			
BSI Group Limited (D)			
BSI Holdings Limited (D)			
Call Centre Technology Limited (D)			
Capita (06243477) Limited (D)			
Capita (06413358) Limited (D)			
Capita (3498350) Limited (D)			
Capita (Banstead 2011) Limited (D)			
Capita (D1) Limited (D)			
Capita 03075476 Limited (D)			
Capita Building Standards Limited			
Capita Commercial Insurance Services Limited			
Capita Consulting Limited (D)			
Capita Corporate Director Limited (D)			
Capita Customer Management Limited			
Capita Customer Solutions (UK) Limited			
Capita Dubai Limited			
Capita Employee Benefits (Consulting) Limited			
Capita Employee Benefits Holdings Limited			
Capita Employee Benefits Limited			
Capita Employee Benefits Services Limited (D)			
Capita Energy Services Limited			
Capita Financial Services Holdings Limited	100%	•	
Capita Financial Software Limited (D)			
Capita Glamorgan Consultancy Limited			
Capita GMPS Trustees Limited (D)			
Capita Grosvenor Limited (D)			
Capita Group Secretary Limited (D)			
Capita Hartshead Benefit Consultants Limited (D)			
Capita Hartshead Consultancy Services Limited (D)			
Capita Hartshead Pensions Limited (D)			
Capita Hartshead Solutions Limited (D)			
Capita Hartshead Trading Solutions Limited (D)			
Capita Health and Wellbeing Limited			
Capita Health Holdings Limited			
Capita Holdings Limited	100%	•	
Capita IB Solutions (UK) Limited (D)			
Capita Information Limited (D)			
Capita Insurance Services Holdings Limited			
Capita Intelligent Building Infrastructure Services Limited			
Capita International Retirement Benefit Scheme Trustees Limited (D)			
Capita IT Services (BSF) Holdings Limited (D)			
Capita IT Services Holdings Limited			
Capita Justice & Secure Services Holdings *Limited*			
Capita Legal Services Limited	100%	•	
Capita Managing Agency Limited			
Capita Membership Management Online Limited (D)			
Capita Mortgage Administration Limited			
Capita Mortgage Software Solutions Limited			
Capita Property and Infrastructure Holdings Limited			
Capita Property and Infrastructure International Holdings Limited (D)			
Capita Property and Infrastructure International Limited (D)			
Capita Property and Planning Limited (D)			
Capita Secure Information Solutions Limited			
Capita Secure Resource Solutions Limited (D)			
Capita SIP Services Limited (D)			
Capita Southampton Limited	80%		
Capita Symonds (Asia) Limited (D)			
Capita Symonds (Health & Safety) Limited (D)			
Capita Translation and Interpreting Limited			
Capita Travel & Events Holdings Limited			
Capita Travel and Events Limited			
Capita Treasury Services Limited (D)			
Capita Wealth and Distribution Services Limited (D)			
Capita Workforce Management Solutions Limited (D)			
Car Parking Partnership Limited (D)			
Cardiff Research Consortium (HOG) Limited (D)			
Chaya Ltd (D) *			
Clinical Solutions Acquisition Limited (D)			
Clinical Solutions Holdings Limited (D)			
Clinical Solutions IP Limited			
CMGL Group Limited (D)			
Complete Imaging Limited			
Complete Imaging Trustee Company Limited (D)			
Computerland UK Limited			
Contact Associates Limited			

18 INDIRECT INVESTMENTS CONTINUED

Company Name	% ownership	Directly held by Capita plc	Share class
CPLAS Trustees Limited (D)			
Data Mail Systems Limited			
Design & Manage Europe Limited (D)	50%		
E.B. Consultants Limited (D)			
Eastgate Insurance Market Solutions Limited (D)			
Eclipse (Hardware) Limited			
Electra-Net (UK) Limited			
Electra-Net Group Limited			
Electra-Net Holdings Limited			
Elsworth Sykes Northern Limited (D)			
Elsworth Sykes Partnership Limited (D)			
Elsworth Sykes Trustee Limited (D)			
Emergency Services Academy Limited (D)			
Entrust Education Services Limited (D)			
Equinox Employee Benefit Trust Limited (D)			
Equitable Holdings Limited (D)			
ESA Design Limited (D)			
ESPM Project Management Limited (D)			
Expotel Hotel Reservations Limited (D)			
Fera Science Limited	75%		(£1.00 Ordinary B)
Fire Service College Limited			
First Retail Finance Limited (D)			
FirstAssist Services Limited			
Fortek Computers Limited (D)			
FPS Group of Companies Limited (D)			
G L Hearn Limited			
G L Hearn Management Limited			
Gissings Trustees Limited (D)			
Grosvenor Career Services Limited (D)			
I2Q Limited (D)			
IBS Opensystems (UK) Limited (D)			
Inter-City Paging Limited (D)			
International Reservations Limited (D)			
International Travel Group Limited (D)			
Inventures Limited (D)			
ITR International Translation Resources Limited			
John Crilley Limited (D)			
Latemeetings.com Limited (D)			
Leadcall Limited			
Liberty Communication Services Ltd.			
Liberty Printers (Ar And Rf Reddin) Limited			
Lovejoy Partnership Limited (D)			
Madagans Limited (D)			
Magnos (Holdings) Limited			
Medicals Direct Assets Limited (D) *			
Medicals Direct Clinics Limited (D) *			
Medicals Direct Group Limited (D) *			
Medicals Direct Healthcare Limited (D) *			
Medicals Direct Holdings Limited (D) *			
Medicals Direct Medico-legal Limited (D) *			
Medicals Direct Screenings Limited *			
Metacharge Limited			
Micro Librarian Systems Holdings Limited (D)			
Micro Librarian Systems Limited			
Multi-Tech Contracts Limited (D)			
Myshares Limited (D)			
NB Finance Limited (D)			
NB Real Estate Group Limited (D)			

Company Name	% ownership	Directly held by Capita plc	Share class
NB Real Estate Holdings Limited			
Network Technology Solutions (UK) Limited			
NIS Europe Limited (D)			
Nova Bidco Limited (D)			
Nova Midco Limited (D)			
Nurse Direct Limited (D) *			
NYS Corporate Ltd.			
NYS Holdings Limited			
Optilead Limited			
Orange Bus Limited (D)			
Orbit Benefits Limited (D)			
Pay360 Limited			
PIFC Consulting Limited (D)			
Projen Limited *			
Property Research Limited (D)			
Ramesys (UK) Limited (D)			
Ramesys EBT Limited (D)			
RE (Regional Enterprise) Limited	51%		(£1.00 Ordinary A)
Re Ltd (D)			
Red Procurement and Business Systems Ltd (D)			
Repair Management Services Holdings Limited (D)			
Repair Management Services Limited (D)			
Resource Management Limited (D)			
Retain International (Holdings) Limited (D)			
Retain International Limited (D)			
Right Document Solutions Holdings Limited (D)			
Right Document Solutions Limited			
RIPA International Limited (D)			
S.G. Ingram : Actuary Limited (D)			
S3dc Limited			
Sbj Benefit Consultants Limited (D)			
Sbj Professional Trustees Limited (D)			
Sector Holdings Limited (D)			
Security Watchdog Limited (D)			
Settlement Integrated Solutions Limited (D)			
SIMS Holdings Limited (D)	100%	•	
SIMS Limited (D)			
Smart DCC Limited			
Smart Public Limited (D)			
Smiths Consulting Limited (D)			
Solid State Solutions Limited			
STL Technologies Limited (D)			
Synaptic Software Limited			
Synetrix (Holdings) Limited (D)			
Synetrix Limited (D)			
Tascor E & D Services Limited			
Tascor Limited (D)			
Tascor Services Limited			
Tempus Finance Limited (D)			
The Royal Borough Of Kensington And Chelsea Assured Homes Limited (D)			
Trustmarque Solutions Limited			
Two-Ten Communications Limited (D)			
Underwriting Direct Limited (D) *			
Updata Infrastructure (North) Limited (D)			
Updata Infrastructure (UK) Limited			
Updata Infrastructure 2012 Limited (D)			
Ventura (UK) India Limited (D)			

NOTES TO THE COMPANY FINANCIAL STATEMENTS CONTINUED

18 INDIRECT INVESTMENTS CONTINUED

Company Name	% ownership	Directly held by Capita plc	Share class
Venues Event Management Limited (D)			
Vision 2 Learn Limited			
Western Mortgage Services Limited			
Westhill Consulting Limited (D)			
Westpoint Limited			
2 Grand Canal Square, Grand Canal Harbour, Dublin 2, Ireland			
AMT Group Limited			
AMT-Sybex (I) Limited (D)			
AMT-Sybex (Managed Services) Limited (D)			
AMT-Sybex (Research) Limited			
AMT-Sybex (Software) Limited			
AMT-Sybex Group Limited			
Capita Business Support Services Ireland Limited			
Capita IB Solutions (Ireland) Limited			
Dupree Holdings Limited			
Marrakech (Ireland) Limited (D)			
Marrakech Limited			
Rathcush Limited			
Vilanova Management Limited (D)			
Wabowden Limited (D)			
21/9, Warszawska Street, 40-009, Katowice, Poland			
ESA spółka z ograniczoną odpowiedzialnością w likwidacji – in liquidation (D)			
24 Blythswood Square, Glasgow, G2 4BG			
Sp Collect Ltd			
Stirling Park LLP			
3 Ponton Street, Edinburgh, EH3 9QQ			
Capita Scotland (Pension) Limited Partnership			
33-37 Athol Street, Douglas, IM1 1LB, Isle Of Man			
Capita (Isle of Man) Limited (D)			
33/34 Winckley Square, Preston, Lancashire, PR1 3EL			
Akinika Debt Recovery Limited			
Akinika Limited			
Akinika UK Limited			
Legal & Trade Collections Limited (D)			
40 Eaton Avenue, Buckshaw Village, Chorley, Lancashire, PR7 7NA			
Parkingeye Limited			
42/44 Henry Street, Northampton, Northamptonshire, NN1 4BZ			
Equita Limited			
4th Floor, Park Gate 161-163, Preston Road, East Sussex, Brighton, BN1 6AF			
Premier Medical Holdings Limited (D)	19.90%		(£1 Ordinary A)
50, Raffles Place, #32-01 Singapore Land Tower, Singapore, 048623			
Capita Insurance Services Asia Pte. Ltd.			
5th Floor, Fort Dunlop, Fort Parkway, Birmingham, B24 9FD			
Service Birmingham Limited (renamed Capita Birmingham Limited on 22 January 2018)			
6th Floor, One America Square, 17 Crosswall, London, EC3N 2LB			
Brokers Educational Supply Teachers Claims Limited			
71 Victoria Street, London, SW1H 0XA			
Capita Aurora Leasing Limited (D)			
Capita Aurora Limited			
Capita Business Services Ltd			

Company Name	% ownership	Directly held by Capita plc	Share class
Capita Insurance Services Group Limited (D)			
Capita Insurance Services Limited			
Capita Inverita Limited (D)			
Capita Land Limited (D)			
Capita Life & Pensions Regulated Services Limited	100%	•	
Capita Life & Pensions Services Limited	100%	•	
Capita Property and Infrastructure (Structures) Limited			
Capita Property and Infrastructure Limited			
Capita Resourcing Limited			
Capita Retail Financial Services Limited			
Capita Specialist Insurance Solutions Limited			
Evolvi Rail Systems Limited			
Market Mortgage Limited	50%		£0.001 Ordinary Capita Shares
Woolf Limited			
803, Manning House, 38 Queen's Road Central, Hong Kong			
ThirtyThree APAC Limited			
850 New Burton Road, Suite 201, Dover DE 19904, USA			
Capita (USA) Holdings Inc.			
Capita Business Services (USA) LLC			
Capita CTI (USA) LLC			
G2G3 (USA) LLC			
Optilead Inc.			
ThirtyThree USA Inc.			
8th Floor, Union Castle Building, 55 St Georges Mall, Cape Town, 8001, South Africa			
Capita (South Africa) (Pty) Limited			
Full Circle Contact Centre Services (Proprietary) Limited			
9 Bonhill Street, London, EC2A 4DJ			
Cobalt Insurance Holdings Limited	24.6%		
9, Allee Scheffer, L-2520, Luxembourg			
CAPITA (Luxembourg) s.a r.l			
Alameda dos Guaramomis, no 930 , 1st Floor, Suite 01, Bairro, Moema, CEP 04076-011, Brazil			
Eureka Asessoria Empresarial Ltda (D)	49.90%		
Centrum Biurowe Lubicz I,ul. Lubicz 23, 31-503, Krakow, Poland			
Capita (Polska) Spolka z ograniczona odpowiedzialnoscia			
Civic Centre, Chorley Road, Swinton, M27 5AS			
Urban Vision Partnership Limited	50.10%		(£1.00 Ordinary-b)
Clinch's House, Lord Street, Douglas, IM99 1RZ			
Capita Life and Pensions Services (Isle of Man) Limited			
Capita Services (Isle of Man) Limited			
Corporation Service Company 2711, Centerville Road, Suite 400, Wilmington, County of Newcastle DE 19808, USA			
CAS Services US Inc			
Clinical Solutions Group (International) LLC (D)			
Corporation Trust Centre, 1209 Orange Street, Wilmington, New Castle DE 19801, USA			
Capita Translation and Interpreting LLC			
Daisy House Suite 1, Lindred Road Business Park, Nelson, Lancashire, BB9 5SR			
Daisy Updata Communications Limited	50%		(£1.00 Ordinary B)

18 INDIRECT INVESTMENTS CONTINUED

Company Name	% ownership	Directly held by Capita plc	Share class
Deloitte Place, Mriehel ByPass, Mriehel, BKR 3000, Malta			
Capita Symonds (Malta) Limited (D)			
Exchange House, 1 Radian Court, Knowlhill, Milton Keynes, MK5 8PJ			
NB Real Estate Limited (In Liquidation) (D)			
Floor 2, Ibex House, 42-47 Minories, London, EC3N 1DY			
Cost Advocates Limited			
Hardturmstrasse 101, Zürich, 8005, Switzerland			
TELAG AG			
Hepworth House, Claypit Lane, Leeds, LS2 8AE			
Optima Legal Services Limited			
Hillview House, 61 Church Road, Newtownabbey, Co Antrim, BT36 7LQ			
AMT-Sybex (NI) Limited (D)			
AMT-Sybex Holdings Limited			
Capita Managed IT Solutions Limited			
Learnserve Limited (D)			
Käfertaler Str. 190, Mannheim, 68167, Germany			
adato GmbH			
Kalzstraße 21, Saalfeld, 07318, Germany			
3C DIALOG Saalfeld GmbH			
Kommandatenstrasse 22, Berlin, 10969, Germany			
Capita Customer Services (Germany) GmbH			
Kommandatenstrasse 22, Berlin, 10970, Germany			
Capita rentable GmbH			
Kommandatenstrasse 22, Berlin, 10971, Germany			
Capita Süd GmbH			
Kommandatenstrasse 22, Berlin, 10972, Germany			
Capita West GmbH			
Konstanzerstrasse 17, Tägerwilen, 8274, Switzerland			
Capita Customer Services AG			
Landmark Virtual Offices, Africa Re Building - Plot 1679, Karimu Kotun Street, Lagos, Victoria Island, Nigeria			
Capita Norman + Dawbarn Limited (D)	97.30%		
Level No. 3, Gate Village 7, Dubai International Finance Centre, Dubai, PO BOX 49983			
Capita (Dubai FZ) Limited			
Maison Trinity, Trinity Square, St. Peter Port, Guernsey, GY1 4AT			
Capita Group Insurance PCC Limited	100%	•	(£1 CG1, £1 CIC2, £1 Ordinary)
Montague House, Adelaide Road, Dublin 2, Ireland			
Capita Life and Pensions Services (Ireland) Limited	0.001% (99.999% held by a subsidiary)	•	
Mr S Fisher, The Grange, Bishops Cleeve, Cheltenham, Gloucestershire, GL52 8YQ			
Cobex Corporate Member No. 1 Limited	50.10%		
Nassauer Ring 39-41, Krefeld, 47803, Germany			
Capita Energie Services GmbH	74.90%		
Pavilion Building, Ellismuir Way, Tannochside Park, Uddingston, Glasgow, G71 5PW			
Barrachd Limited			
Capita IT Services Limited			
Capita Scotland General Partner (Pension) Limited			
Capita Secure Mobile Solutions Limited (D)			
G2G3 Propulsion Ltd. (D)			
Opin Systems Limited			
Plant 6, Gate No.2, Godrej & Boyce Complex, Pirojshahnagar, L.B.S Marg, Vikhroli (West), Maharashtra, Mumbai, 400079, India			
Capita India Private Limited			
Capita IT and Consulting India Private Limited			
Capita Offshore Services Private Limited	0.01% (99.99% held by a subsidiary)	•	
Capita SIMS (India) Private Limited			
Capita Symonds India Private Limited			
CS Clinical Solutions India Private Limited			
Riyadh			
Capita Symonds Property and Infrastructure Consultants (KSA) (D)	50%		
Room 615 Zhucheng Building, No Jia 6 Zhongguancun South Street, Beijing 100086, Haidian District, China			
Symonds Project Management Consultancy (Beijing) Ltd (D)			
St David's House, Pascal Close, St Mellons, Cardiff, CF3 0LW			
Capita Gwent Consultancy Limited	51%	•	(£0.01 Preference)
Suite 13.03, 13th Floor, Menara Tan & Tan, 207 Jalan Tun Razak, 50400 Kuala Lumpur, Malaysia			
Symonds Travers Morgan (Malaysia) SDN. BHD			
Suite 4301-5, Tower One Times Square, 1 Matheson Street, Causeway Bay, Hong Kong			
Symonds Travers Morgan (Hong Kong) Limited (D)			
The Beacon, 176 St Vincent Street, Glasgow, G2 5SG			
Capita Mclarens Limited			
The Riverway Centre, Riverway, Stafford, ST16 3TH			
Entrust Support Services Limited (D)	51%		(£1.00 Ordinary-X)
Themistokli Dervi, 3, Julia House, P.C. 1066, Nicosia, Cyprus			
Capita Cyprus Holdings Limited			
Capita Cyprus Limited (D)			
Unit 8, Wessex Park, Bancombe Road Trading Estate, Somerton, Somerset, TA11 6SB			
Ross & Roberts Limited			
Unit B, West Cork Technology Park, Clonakilty, Cork, Ireland			
Capita Customer Solutions Limited			
Wing 'C', Marisoft Annex, Vadgaon sheri, Kalyani Nagat, Maharashtra, Pune, 411014, India			
Ventura (India) Private Limited			

NOTES TO THE COMPANY FINANCIAL STATEMENTS CONTINUED

18 INDIRECT INVESTMENTS CONTINUED

Listed below are subsidiaries controlled and consolidated by the Group, where the Directors have taken the exemption from having an audit of its financial statements for the year ended 31 December 2017. This exemption is taken in accordance with Companies Act Section 479A.

Company Name	%	Registered Office	Company registration	Location	Held directly by Capita plc	Share Class
Barrachd Intelligence Solutions Limited	100%	Pavilion Building, Ellismuir Way, Tannochside Park, Uddingston, Glasgow, G71 5PW	SC430881	UK		
Brightwave Enterprises Limited	100%	17 Rochester Row, London, SW1P 1QT	7066783	UK		
Brightwave Holdings Limited	100%	17 Rochester Row, London, SW1P 1QT	7462788	UK		
Brightwave Limited	100%	17 Rochester Row, London, SW1P 1QT	4092349	UK		
Capita (6588350) Limited (previously Projen Holdings Limited)	100%	17 Rochester Row, London, SW1P 1QT	6588350	UK		
Capita Gas Registration and Ancillary Services Limited	100%	17 Rochester Row, London, SW1P 1QT	05078781	UK		
Capita HCH Limited	100%	17 Rochester Row, London, SW1P 1QT	02384029	UK		
Capita HELM Corporation Limited	100%	Beacon House, 27 Clarendon Road, Belfast, BT1 3PR	NI025165	UK		
Capita International Limited	100%	17 Rochester Row, London, SW1P 1QT	02683437	UK		
Capita IT Services (BSF) Limited	100%	17 Rochester Row, London, SW1P 1QT	01855936	UK		
Cardiff Research Consortium Limited	100%	17 Rochester Row, London, SW1P 1QT	03962364	UK		
CCSD Services Limited	100%	17 Rochester Row, London, SW1P 1QT	05399460	UK		
CHKS Limited	100%	17 Rochester Row, London, SW1P 1QT	02442956	UK		
Clinical Solutions Finance Limited	100%	17 Rochester Row, London, SW1P 1QT	5337592	UK		
Clinical Solutions International Limited	100%	17 Rochester Row, London, SW1P 1QT	04394761	UK		
CMGL Holdings Limited	100%	17 Rochester Row, London, SW1P 1QT	05509018	UK		
Creating Careers Limited	100%	17 Rochester Row, London, SW1P 1QT	03885966	UK		
Cymbio Limited	100%	17 Rochester Row, London, SW1P 1QT	06462086	UK		
Data Equipment Limited	100%	17 Rochester Row, London, SW1P 1QT	1738098	UK		
Debt Solutions (Holdings) Limited	100%	33-34 Winckley Square, Preston, Lancashire, PR1 3EL	03673307	UK		
Euristix (Holdings) Limited	100%	17 Rochester Row, London, SW1P 1QT	05564856	UK		
Euristix Limited	100%	17 Rochester Row, London, SW1P 1QT	05420948	UK		
Fish Financial Solutions Limited	100%	17 Rochester Row, London, SW1P 1QT	07467833	UK		
G2G3 Digital Limited	100%	17 Rochester Row, London, SW1P 1QT	03063669	UK		
Hallco 1626 Limited	100%	17 Rochester Row, London, SW1P 1QT	6603462	UK		
Health Analytics Ltd	100%	17 Rochester Row, London, SW1P 1QT	6947862	UK		
Knowledgepool Group Limited	100%	17 Rochester Row, London, SW1P 1QT	04968329	UK		
Marrakech (U.K.) Limited	100%	17 Rochester Row, London, SW1P 1QT	3785263	UK		
Medicals Direct International Limited	100%	17 Rochester Row, London, SW1P 1QT	07168308	UK		
PageOne Communications Limited	100%	17 Rochester Row, London, SW1P 1QT	4560277	UK		
Pervasive Limited	100%	17 Rochester Row, London, SW1P 1QT	5679204	UK		
Pervasive Networks Limited	100%	17 Rochester Row, London, SW1P 1QT	3429318	UK		
SDP Regeneration Services 2 Limited	100%	17 Rochester Row, London, SW1P 1QT	04626963	UK		
Sigma Seven Limited	100%	Pavilion Building, Ellismuir Way, Tannochside Park, Uddingston, Glasgow, G71 5PW	SC212846	UK		
Smartpoint Limited	100%	17 Rochester Row, London, SW1P 1QT	2831803	UK		
Tempus Finance Limited	100%	17 Rochester Row, London, SW1P 1QT	6943069	UK		
The G2G3 Group Ltd.	100%	Pavilion Building, Ellismuir Way, Tannochside Park, Uddingston, Glasgow, G71 5PW	SC199414	UK		
The Write Research Company Limited	100%	17 Rochester Row, London, SW1P 1QT	04272836	UK		
Thirty Three Group Limited	100%	17 Rochester Row, London, SW1P 1QT	3626724	UK		
Thirty Three LLP	100%	17 Rochester Row, London, SW1P 1QT	OC372712	UK		
Voice Marketing Limited	100%	17 Rochester Row, London, SW1P 1QT	5820091	UK		

SHAREHOLDER INFORMATION

In this section we have provided you with some key information to manage your shareholding in Capita plc.

USEFUL WEBSITES

Capita (www.capita.com/investors)

Our corporate site is our main external communication channel where we showcase our services, solutions and innovations from across the wider Company. It also contains an investor section, where institutional and private shareholders can access the latest announcements, financial and statutory information and reports.

Shareholder portal (www.capitashares.co.uk)

Capita's register of shareholders is maintained by Link Asset Services. Our shareholder portal is a secure online site where you can manage your shareholding quickly and easily. You can manage many aspects such as view your holding, update contact details, manage dividend payments, request to receive shareholder communications by email and register. To register you will need your investor code, which can be found on your share certificate or dividend confirmation.

E-COMMUNICATIONS

Help us communicate with you in a greener, more efficient and cost-effective way by switching from postal to email communications which means that we will notify you by email each time new shareholder communications have been placed on the Capita website.

Registering for e-communications is very straightforward. Go to our shareholder portal www.capitashares.co.uk. Further information about our shareholder portal is below.

MANAGING YOUR SHAREHOLDING

We aim to communicate effectively with our shareholders, via our website www.capita.com/investors. Shareholders who have questions relating to the Group's business or wish to receive further hard copies of annual reports should contact Capita's investor relations team on 020 7799 1525 or email: IRTeam@capita.co.uk.

If you have any queries about your shareholding or dividend payments please contact the Company's registrar, Link Asset Services:

Link Asset Services
The Registry
34 Beckenham Road
Beckenham
Kent BR3 4TU

Email: enquiries@linkgroup.co.uk
Tel (UK): 0871 664 0300 (Calls cost 12p per minute plus your phone company's access charge)
(Overseas): +44 371 664 0300[1]

Lines are open between 9.00am – 5.30pm, Monday to Friday excluding public holidays in England and Wales.

Share dealing

A quick and easy share dealing service is available for existing Capita shareholders to either sell or buy Capita plc shares online or by telephone.

For further information go to: www.linksharedeal.com or telephone +44 (0) 371 664 0445[1]. Lines are open between 8.00am – 4.30pm, Monday to Friday excluding public holidays in England and Wales.

If you have only a small number of shares which are uneconomical to sell, you may wish to donate them to charity free of charge through ShareGift (Registered Charity 1052686). Find out more at www.sharegift.org.uk or by telephoning 020 7930 3737.

COMPANY CONTACT DETAILS

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Registered in England and Wales number with registration number: 2081330

Investor Relations

IRTeam@capita.co.uk
Head of Investor Relations – Andrew Ripper

Company Secretariat

secretariat@capita.co.uk
Company Secretary – Francesca Todd

COMPANY ADVISERS

Independent auditor

KPMG LLP

Corporate brokers

Citi
Goldman Sachs

Bankers

Barclays Bank plc
HSBC Bank plc
The Royal Bank of Scotland Plc

Registrars

Link Asset Services

The Directors present the Annual Report for the year-ended 31 December 2017 which includes the strategic report, governance and audited accounts for this year. Pages 1 to 89 of this Annual Report comprise a report of the Directors that has been drawn up and presented in accordance with English company law and the liabilities of the Directors in connection with that report shall be subject to the limitations and restrictions provided by such law. Where we refer in this report to other reports or material, such as a website address, this has been done to direct the reader to other sources of Capita plc information which may be of interest to the reader. Such additional materials do not form part of this report.

* Calls to 0871 numbers cost 12p per minute plus your phone company's access charge. Calls to 0371 numbers are charged at the standard geographic rate and will vary by provider. Calls outside the United Kingdom will be charged at the applicable international rate.

ALTERNATIVE PERFORMANCE MEASURES

The Group presents various APMs as the Directors believe that these are useful for users of the financial statements in helping to provide a balanced view of, and relevant information on, the Group's financial performance, position and cash flows.

The Group presents various APMs as the Directors believe that these are useful for users of the financial statements in helping to provide a balanced view of, and relevant information on, the Group's financial performance, position and cash flows. These APMs are mainly measures which disclose the 'underlying' performance of the Group excluding specific items which are regarded as non-underlying. The Group separately presents intangible amortisation, asset impairments, acquisition contingent consideration movements, acquisition expenses, the financial impact of business exits or businesses in the process of being exited, movements in the mark-to-market valuation of certain financial instruments and other specific items in the income statement which, in the Directors' judgement, need to be disclosed separately (see notes 4, 5 and 6) by virtue of their nature, size and incidence in order for users of the financial statements to obtain a proper understanding of the financial information and the underlying performance of the business.

In addition, the Group presents other APMs including Key Performance Indicators (KPIs) such as return on capital employed and interest cover by which we monitor our performance and others such as organic and acquisition revenue growth which provide useful information to users which is not otherwise readily available from the financial statements.

APMs presented	2017	Restated 2016	% change	Source
REVENUE – CONTINUING OPERATIONS				
Total revenue as reported	£4,234.6m	£4,368.6m	(3.1)%	Line item in income statement
Deduct: Business exit	(£66.7m)	(£11.3m)		Non-underlying item in income statement
1. Underlying revenue	£4,167.9m	£4,357.3m	(4.3)%	
Deduct: business exits		(£165.1m)		Revenue from businesses exited in 2017 (excluding discontinued operations)
2. Underlying revenue on a like-for-like basis	£4,167.9m	£4,192.2m	(0.6)%	Underlying revenue excluding results from businesses exited in both years
Deduct: 2016 acquisitions	(£29.7m)			Additional contribution in 2017 of acquisitions acquired in 2016
Deduct: 2017 acquisitions	(£7.0m)			Contribution in 2017 of acquisitions acquired in 2017
3. Underlying organic revenue	£4,131.2m	£4,192.2m	(1.5)%	Underlying revenue excluding businesses exited and acquired
Prior year underlying revenue on a like-for-like basis	£4,192.2m			From Line 2 above
Total acquisitions	£36.7m			2016 acquisitions plus 2017 acquisitions
4. Growth from acquisitions	0.9%			Total acquisitions divided by prior year underlying revenue on a like-for-like basis
PROFIT – CONTINUING OPERATIONS				
Operating loss as reported	(£420.1m)	(£16.1m)		Line item in income statement
Add back: Business exit	£14.7m	(£2.8m)		Non-underlying item in income statement
Add back: Specific items	£852.8m	£353.5m		Non-underlying item in income statement
5. Underlying operating profit	£447.4m	£334.6m	33.7%	
6. Underlying operating margin KPI	10.7%	7.7%		Underlying operating profit/underlying revenue
Add back: Significant new contracts and restructuring	£17.9m	£57.2m		Line item in note 3 – Underlying operating profit
7. Underlying operating profit before significant new contracts and restructuring	£465.3m	£391.8m	18.8%	
Loss before tax as reported KPI	(£513.1m)	(£89.8m)		Line item in income statement
Add back: Business exit	£45.4m	(£2.9m)		Non-underlying item in income statement
Add back: Specific items	£850.7m	£361.2m		Non-underlying item in income statement
8. Underlying profit before tax KPI	£383.0m	£268.5m	42.6%	
9. Underlying earnings per share KPI	45.61p	31.68p	44.0%	Line item in income statement and note 12 – earnings per share

APMs presented (continued)		2017	Restated 2016	% change	Source
CASH FLOW – CONTINUING OPERATIONS					
10. Underlying free cash flow KPI		**£38.0m**	£397.3m	(90.4)%	Line item in note 31 – additional cash flow information
Non-underlying payments		*(£0.3m)*	*(£30.0m)*		*Non-underlying payments in 2017 include movement in payables and receivables and Business exit provision paid*
11. Free cash flow after non-underlying items		**£37.7m**	£367.3m	(89.7)%	

		2017	As reported 2016	Source
GEARING				
Underlying EBIT		**£447.4m**	£541.3m	Underlying operating profit
Deduct: non-controlling interest		*(£14.1m)*	*(£13.4m)*	*Underlying EBIT attributable to non-controlling interests*
Deduct: acquisition costs		**(£1.7m)**	(£9.0m)	Line items in note 6 – specific items
Add back: Significant new contracts and restructuring		**£17.9m**	–	Line items in note 3 – underlying operating profit
Add back: (profit)/loss on disposal of non-current assets		**£0.5m**	–	Line item in note 31 – additional cash flow information
Add back: share based payment charge		**£2.9m**	–	Line item in note 31 – additional cash flow information (note: charge only)
Add back: non-current service pension charge		**£0.8m**	*£2.4m*	*Line items in note 34 – employee benefits*
Add back: amortisation on purchased intangibles		**£19.9m**	–	Line item in note 31 – additional cash flow information
Adjusted EBIT	a	**£473.6m**	£521.3m	
Add back: pre-acquisition underlying profit		**£0.3m**	£5.6m	Disclosure in note 17 – business combinations
Add back: depreciation		**£63.5m**	£99.3m	Line item in note 31 – additional cash flow information
Adjusted EBITDA	b	**£537.4m**	£626.2m	
12. Underlying interest charge		**(£64.4m)**	(£66.0m)	Line item in income statement
Interest cost attributable to pensions		**£9.2m**	£6.6m	Line item in note 34 – employee benefits
Borrowing costs	c	**(£55.2m)**	(£59.4m)	Underlying interest charge excluding pension interest
13. Interest cover	a/c	**8.6x**	8.8x	Adjusted EBITA/Borrowing costs
Equity attributable to shareholders	d	**(£999.0m)**	£408.2m	Line item on balance sheet
15% of equity attributable to shareholders	e = d x 15%	**(£149.9m)**	£61.2m	
Contingent obligations under bonds and guarantees	f	**£88.4m**	£91.7m	Disclosure in note 33 – contingent liabilities
	g	**£88.4m**	£30.5m	If f > e, the difference is treated as debt
Money Market Funds	h	**£14.0m**	–	
Net debt	i	**£1,117.0m**	£1,778.8m	Line information in note 31 – additional cash flow information
Adjusted net debt	j = g+h+i	**£1,219.4m**	£1,809.3m	
14. Adjusted net debt to Adjusted EBITDA ratio KPI	j/b	**2.27x**	2.89x	Adjusted net debt/Adjusted EBITDA

ALTERNATIVE PERFORMANCE MEASURES CONTINUED

APMs presented (continued)		2017	Restated 2016	Source
RETURN ON CAPITAL EMPLOYED (ROCE)				
Underlying operating profit	A	465.3	391.8	Operating profit excluding non-underlying items and restructuring cost (note 3)
Tax rate	B	17.7%	17.3%	Line item note 11
Tax	C = A x B	82.4	67.8	Underlying profit multiplied by tax rate
Underlying operating profit after tax	D = A - C	382.9	324.0	Underlying profit less tax
Current year net liabilities	E	(929.8)	(552.9)	Line in balance sheet
Current year underlying net debt	F	1,103.9	1,682.9	Line item in note 31 – additional cash flow information
Adjustments to capital employed	G	1,359.7	1,280.3	Includes post-tax impact of accumulated acquired intangible amortisation, fixed rate swaps, put options and pensions
	M[1] = E+F+G		2,410.3	Used in 2017 average capital employed
Less acquisition spend in-year	H	(18.8)	(89.5)	Consideration paid – cash acquired + debt acquired, per note 17
Current year capital employed	I = E+F+G+H	1,515.0	2,320.8	
Prior year net liabilities	J		(189.0)	
Prior year underlying net debt	K		1,750.3	
Comparative prior year adjustments	L		1,046.2	Includes post-tax impact of accumulated acquired intangible amortisation, fixed rate swaps, put options and pensions
Prior year capital employed	M[2] = J+K+L		2,607.5	Used in 2016 average capital employed
Average capital employed pre-acquisitions	N = (I+M)/2	1,962.7	2,464.2	
Weighted average acquisition spend in-year	O	35.8	59.7	Pro rata number of months post-acquisition (including contingent and deferred consideration payments)
Average capital employed	P = N+O	1,998.5	2,523.9	
15. ROCE KPI	Q = D/P	19.2%	12.8%	

Designed and produced by Radley Yeldar
Printed by Capita
This report is printed on Inspira Paper and Board which is a PEFC certified paper containing material sourced from responsibly managed forest.
Inspira Paper & Board is manufactured under a strict environmental management system, by an ISO 9001 certified paper mill.

LOGO REMOVED

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