



# Annual Report 2015



**Through their technical expertise, domain know-how and rigorous independent thinking, our engineers and scientists are uniquely placed to help customers meet challenges that define the modern world.**

**Our prized possession is trust. We inspire confidence by working in partnership with our customers to ensure that they meet their goals, first time, every time.**

## **We work across four key markets:**

Defence, security and aerospace are our key markets but we have a growing position in select commercial markets. Our customers are predominantly government organisations, including defence departments, as well as international customers in other targeted sectors.



Find out more about our key markets on page 6.

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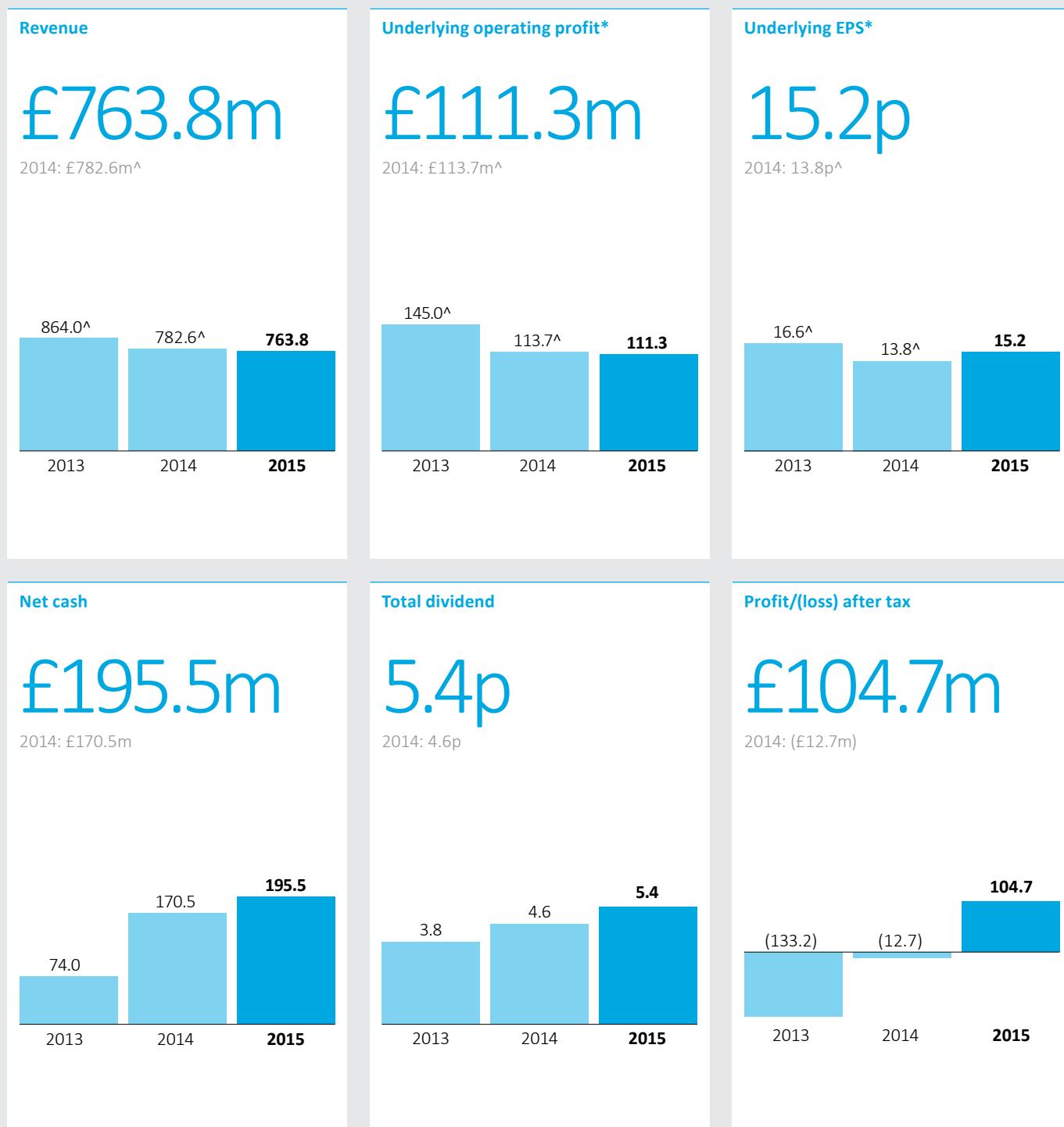
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Read more online: [www.QinetiQ.com](http://www.QinetiQ.com)

You can view this Annual Report and Accounts, all other results materials and additional case studies at [www.QinetiQ.com](http://www.QinetiQ.com). In addition, the QinetiQ Investor Relations iPad App gives you the latest investor and financial media information. The App allows you to get the latest share price information and corporate news, as well as view financial reports.

# Strong financial performance

## Financial



Note: year end references (2015, 2014 and 2013) relate to the years ending 31 March.

\* Definitions of underlying measures of performance can be found in the glossary on page 141.

<sup>^</sup> Restated to reflect continuing/discontinued operations (see note 1 to the financial statements on page 97).

# Meeting changing customer needs

## Operational



**Organic-Plus strategy delivered increased earnings**

→ **P12** Our Organic-Plus strategy



**Strong performance in EMEA Services with core Air, Weapons and Maritime businesses all delivering good results**

→ **P38** EMEA Services



**New President appointed to lead repositioning of US Global Products**

→ **P42** Global Products



**5% Club membership reaches over 70 companies that are committed to creating opportunities for young people**

→ **P24** Responsible business

# Understanding what QinetiQ does

**The technical expertise and domain know-how of our people differentiate our customer offerings from our peers.**

**QinetiQ is trusted, impartial and independent – we are not a manufacturer. We rarely compete directly with aerospace and defence companies, but instead work in partnership with them.**

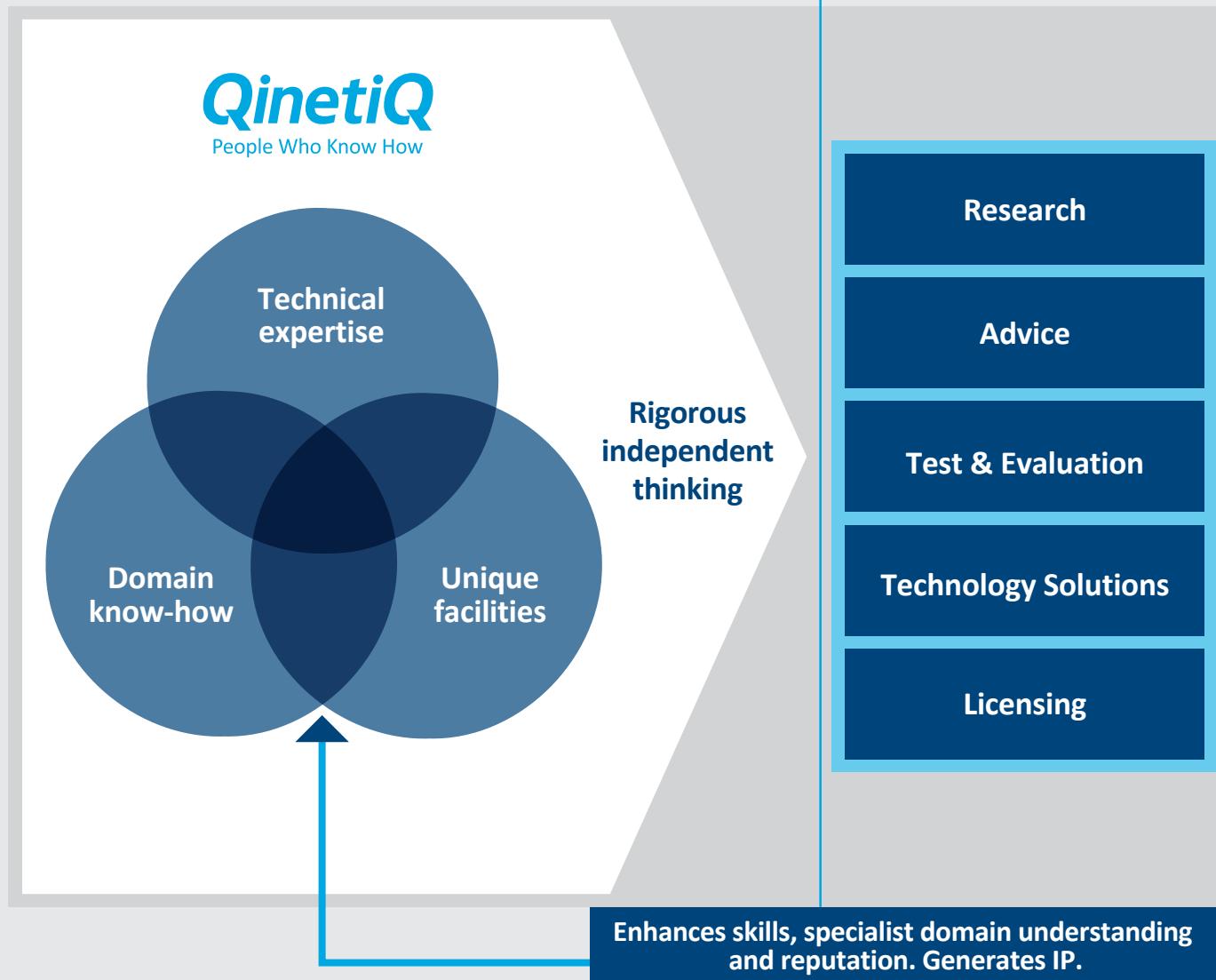
We also work in partnership with customers, leveraging our assets, facilities and capabilities to deliver rigorous independent thinking that ensures they meet their goals.

QinetiQ's level of customer intimacy has been developed over many years. Our specialist know-how about customer domains is nurtured by working in partnership to understand their problems, shape their needs and deliver solutions that help meet their challenges now and for the future.

Our principal revenue streams are research, technology, advice, test and evaluation, technology solutions and the royalties from licensing.

## What makes QinetiQ different

## How we generate value



Our business model is robust and sustainable because our knowledge base is constantly refreshed. As well as enhancing the domain know-how and reputation of our people, our work provides a dynamic source of new intellectual property and future technology-based offerings.

As a business whose reputation and achievements are centred around our people, QinetiQ has low capital and resource requirements. Our future success is primarily dependent on our ability to recruit, develop and retain exceptional employees, subject matter experts and world renowned specialists.

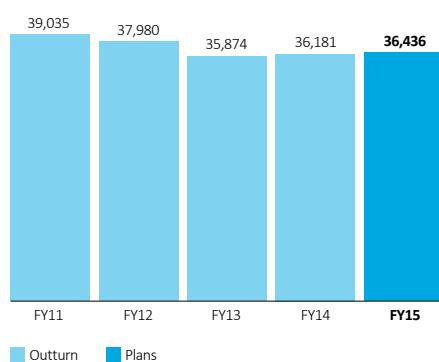
How we deliver		Principal markets			
Divisions	Business units	Defence	Security	Aerospace	Commercial
EMEA Services	Air	✓		✓	
	Weapons	✓			
	Maritime	✓			
	Australia	✓			
	Procurement Advisory Services	✓		✓	
	Training	✓			✓
	C4ISR	✓		✓	
	Cyber Security			✓	
	Cyveillance®			✓	✓
	EMEA products	✓	✓		
	US products	✓			✓
	OptaSense®			✓	✓
Global Products	Space Products			✓	

Working in partnership to shape needs and deliver solutions

# Understanding our markets

## Market drivers

### UK Ministry of Defence budget (£m)



Source: HM Treasury – Public expenditure statistical analysis

**The world is an increasingly uncertain and less secure place. Technology proliferation has lowered the bar for terrorism, organised crime and conflict, meaning that threats to security are increasing in number and diversity.**

**At the same time, technology proliferation enables governments to 'spin-in' technologies from the commercial sector with the help of organisations like QinetiQ which are independent from the supply chain and experts in the application of technology.**

QinetiQ's ability to innovate and apply technology to mitigate security threats, enables us to 'work smarter' and to leverage available resources to help customers deliver when budgets are under pressure.

The UK Government continues to face a significant budget deficit, and a further period of fiscal austerity looks likely following the 2015 election result. Defence expenditure is not protected by Government ring-fencing, unlike spending on healthcare, schools and international aid, but the UK Ministry of Defence (MOD) has made significant progress over the last five years in balancing its budget.

In the US, the Federal Government continues to pursue technological superiority in response to the deteriorating security situation and as its principal source of military advantage. President Obama recently requested an 8% increase to the US defence budget for 2016, forcing the Republican majority to weigh up competing concerns about defence and tackling the ongoing fiscal deficit.

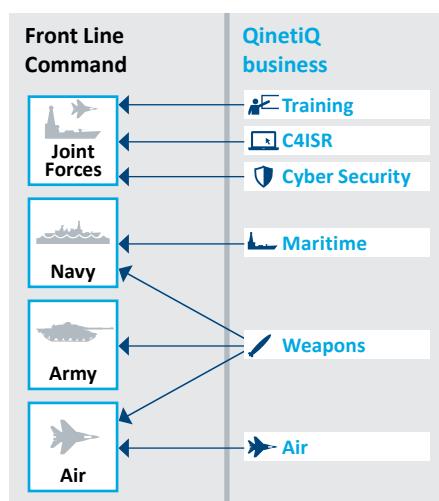
Elsewhere, governments and commercial organisations continue to build capability and balance budgetary constraints with security concerns.

These fiscal pressures, both in the UK and worldwide, are no longer new. Despite reduction in the UK defence budget over the last parliamentary term, QinetiQ was able to improve its financial performance.

### → P4 Our business model

## UK defence market

### QinetiQ business units are aligned closely to the Front Line Commands



To date, the UK Government has aimed to spend 2% of GDP on defence and 1.2% of the budget on science and technology, although these commitments are likely to be considered as part of the Strategic Defence and Security Review (SDSR) expected in 2015. As in 2010, we expect the SDSR to include consultation with industry to help the Government meet the challenges facing UK defence, and look forward to contributing to topics including test and evaluation, and research and technology. QinetiQ has maintained the capability to carry out work not required to be undertaken within Government and the rationalisation of defence budgets and structures could provide further opportunities in this area.

Defence transformation has been a priority since 2010, incorporating a number of significant programmes. For example, the MOD's procurement agency Defence Equipment and Support (DE&S) is transforming its operating model and has been given access to private sector expertise to help improve its performance.

**The Front Line Commands (Navy, Army, Air and Joint Forces) are exercising their newly delegated powers to shape future capabilities and our business units are aligned closely to these Commands and are well placed to help them with their growing procurement responsibilities.**

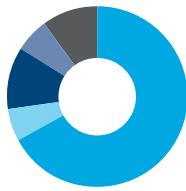
Joint Forces Command has been created to bring 'improved focus to technological enablers' and 'give intellectual energy' to how warfare should be conducted 'in the information age'. With its own procurement arm and multi-billion pound budget, Joint Forces Command provides a more focused channel for our Cyber Security, C4ISR, and Training businesses which were aligned during the year.

Revised single source regulations and pricing terms for single source contracts are now in place under the new 'Orange Book'. They cover new contracts worth £5m or more, requiring additional reporting and tightening definitions of allowable costs. Our combination of capabilities is unique in the UK and, consequently, 33% of EMEA Services revenue is derived from single source contracts, excluding the non-tasking element of the Long Term Partnering Agreement (LTPA). Greater transparency and an independent regulator – the Single Source Regulations Office (SSRO) – will help demonstrate the value for money the Government derives from single source contracts. The SSRO has confirmed the Government profit formula for 2016 is broadly consistent with 2015 but has stated it will be reviewing the methodology for this formula for future periods.

### → P38 EMEA Services

## Global markets

### Breakdown of revenue by customer



2015	%
UK MOD	67
US Department of Defence (DoD)	6
Government agencies	11
Commercial defence	6
Commercial	10

In May 2014, we completed the sale of the US Services division and are no longer active in the US federal services market. Our Global Products division has a significant US footprint, providing a route to the world's largest defence market.

The US Government is continuing to drawdown the number of troops deployed on Overseas Contingency Operations (OCO) and reduce the accompanying OCO procurement budget. Although there are 'reset' opportunities, this continues to depress demand for conflict-related products.

US military customers are assessing their post-war requirements and formulating new Programs of Record which will determine the 'peacetime' demand for products, such as unmanned systems. Our US products business is responding to these opportunities with a greater focus on these Programs of Record, contract-funded research and development, and non-defence markets. The disposal of US Services has helped to facilitate this renewed focus by removing any customer concerns about Organisational Conflict of Interest.

**Although our traditional markets are the UK and US, many of our unique capabilities are transferable to other geographies. For example, as the Canadian and Australian Governments pursue similar defence transformation programmes to the UK, they value our independent advice, test and evaluation in support of better procurement.**

Governments in Europe, the Middle East and Asia are building their defence capabilities in response to the increasing volume and diversity of the threats to security, increasing the demand for C4ISR, cyber and training expertise.

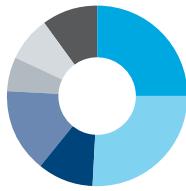
Amongst the prime contractors, competition is becoming fiercer. They are liaising with the supply chain to find new sources of competitive advantage.

Much of QinetiQ's innovation is created from solving a specific set of customer problems, and at the same time generating technology and expertise with the potential to be transferred into new sectors offering higher growth potential.

→ **P42 Global Products**

## Impact on our business

### Breakdown of revenues by key domains



2015	%
Air	25
Weapons	26
Maritime	10
Cyber, C4ISR and Training	15
Other EMEA Services	6
Global Products – US	8
Global Products – EMEA	10

**We rarely compete directly with aerospace and defence companies but instead provide client-side support through the domain know-how and technical expertise of our people. In general, we are not significantly impacted by changes in individual procurement projects. Instead we provide research, technical advice, and test and evaluation across all military domains and the majority of equipment programmes through the LTPA and other key contracts.**

Our position, independent from the supply chain, means we bring unique, impartial skills that help our customers meet the dual challenges of declining budgets and increasing security threats. Although the MOD transformation programme, the election of a new Government and SDSR may slow decision-making this year and create some short-term uncertainty in the UK, they also provide opportunities for us to build on our strong record of a smarter way of working and efficient and effective outcomes. This track record underpins our ability to increase the scope of existing contracts, win new outsourcing opportunities and take our capabilities to new international markets.

## 2016 Outlook

Defence transformation, and the forthcoming Comprehensive Spending Review and SDSR are expected to have an impact on the UK defence market this year. This will provide future opportunities for EMEA Services to build on its strong record of delivering 'more for less', whilst recognising that in FY16 there will be uncertainty and the potential for interruptions to order flow. The portion of revenue under contract at the start of FY16 was similar to a year ago and the balance is supported by a pipeline of opportunities but order flow and contract cover will be watched closely over the coming months. Overall, given the opening backlog position, expectations for the performance of EMEA Services in the current financial year are unchanged.

In Global Products, newer products are recording notable milestones and the amount of revenue under contract at the start of FY16 is up slightly on a year ago, but the drawdown of American overseas military forces is continuing to depress demand for conflict-related products. As the division has a lumpy revenue profile which is dependent on the timing and shipment of key orders, there is a range of possible outcomes for the performance of Global Products in the current year.

In balancing the market uncertainties with the strength of the Group's operations, the Board is maintaining its expectations for Group performance in the current financial year.

→ **P20 Key performance indicators**

# Another year of progress

## Mark Elliott

Non-executive Chairman



## Key highlights

- **Strong demand for QinetiQ's highly differentiated capabilities**
- **Steve Wadey appointed as CEO – an outstanding leader with a track record of driving growth**
- **£150m share buyback well advanced**
- **17% increase in full year dividend reflecting upgrade at the half year and the Group's progressive dividend policy**
- **Maintaining expectations for Group performance in the current financial year**

### Results

In today's world, where threats to our security are many and varied, demand for QinetiQ's highly differentiated capabilities is strong and we are pleased to be able to report another year of progress.

In the year to 31 March 2015, Group revenue was £763.8m (2014: 782.6m<sup>1</sup>), and underlying operating profit\* was £111.3m (2014: £113.7m<sup>1</sup>). Full year underlying earnings per share\* were 15.2p (2014: 13.8p<sup>1</sup>). Total Group profit after tax was £104.7m (2014: loss of £12.7m). Underlying operating cash conversion remained strong at 103% (2014: 93%<sup>1</sup>) with net cash increasing to £195.5m (31 March 2014: £170.5m).

The Board is maintaining its expectations for Group performance in the year to 31 March 2016.

### Employees, customers and shareholders

The expertise and domain know-how of our people is our key competitive advantage. We prioritise the safety and development of highly skilled employees because they underpin the relationships with our customers that build mutual trust and deliver unique benefits. We are pleased to report further progress with employee engagement and customer satisfaction scores this year and that we remain committed to customer service excellence.

At QinetiQ, our most prized possession is trust. Our leaders are responsible for ensuring that ethical and responsible business practices are embedded in our culture. We would like to thank the leadership team for continuing to drive a more open and empowered culture across the Group.

QinetiQ has many sites distributed across the UK. We recognise and support the important role our employees play in local communities and their environmental stewardship of those sites.

Along with customers and employees, shareholders are key stakeholders as the owners of the company. QinetiQ operates across many platforms and contracts, so we set ourselves the target of providing information to shareholders that is timely, clear and concise. We would like to thank our shareholders for their continued support and the time that they commit to a constructive dialogue with our Board and executive team.

### Strategy

We are encouraged that the Group's strategy has delivered further progress this year, with increased demand for the capabilities provided by our core businesses and further development of our pipeline of new opportunities, all underpinned by continued financial discipline.

The sale of US Services, completed in May, was a key step in transforming QinetiQ into a Group that is differentiated by the expertise of its people and by its innovation, which provides a dynamic source of potential future revenue streams. We now have a new leadership team and Proxy Board in North America which is starting to reshape our US products business.

The Group is cash generative and disciplined about capital allocation. This supports ongoing investment in growth opportunities, a progressive dividend policy and the maintenance of the balance sheet strength necessary in an uncertain trading environment.

## Dividend and shareholder returns

The Board proposes a final dividend of 3.6p per share for the year ended 31 March 2015 (2014: 3.2p), making the full year dividend 5.4p (2014: 4.6p). Subject to approval at the Annual General Meeting, the final dividend will be paid on 4 September 2015 to shareholders on the register at 7 August 2015. The full year dividend represents an increase of 17%, reflecting the Group's progressive dividend policy and upgrade at the half year.

In May 2014, we were pleased to be able to initiate a £150m capital return to shareholders by way of a share buyback. We believe the scale of the return reflects the strong cash generative characteristics of the Group, as well as its confidence in its strategy, while taking into account the continuing uncertainty in QinetiQ's end markets, its pension obligations and the strength of its working capital position. By 15 May 2015, the Group had bought back 63 million shares at a cost of £128m. The Board remains committed to maintaining an efficient balance sheet.

## The Board

The priorities that I have set for the Board are strategic growth balanced with capital discipline, succession planning and to ensure the effective stewardship of QinetiQ through appropriate governance processes and systems of control. Good governance is pivotal in the relationship of trust between QinetiQ, its customers, its employees and other key stakeholders.

In June 2014, we announced the appointment of Ian Mason as Non-executive Director and the retirement of Noreen Doyle after nearly nine years on the Board.

On 15 October 2014, Leo Quinn tendered his resignation as CEO of QinetiQ to take up a new role as CEO of Balfour Beatty. Leo arrived at QinetiQ in 2009 at a difficult point in the Company's history with a downturn in defence spending on the horizon. Under his leadership, QinetiQ has been transformed into the strong, competitive company it is today, and on behalf of the Board, we wish him every success in his new role.

Following Leo's departure, Chief Financial Officer David Mellors took over as interim CEO in addition to his existing responsibilities. We would also like to place on record the Board's appreciation for David's outstanding leadership during this period.

In January 2015, we were pleased to announce the appointment of Steve Wadey as our new CEO, with effect from 27 April 2015. We were looking for an outstanding leader with a track record of driving growth, a deep understanding of the defence industry and the technological know-how to lead QinetiQ in the next stage of our Organic-Plus strategy. Steve fits all these criteria and is respected across the MOD and European defence sector; we look forward to working with him on the next stage of our strategic journey.

## Mark Elliott

Non-executive Chairman  
21 May 2015

## Current Board Committee members

### Audit Committee

**Paul Murray, Committee Chairman**  
Admiral Sir James Burnell-Nugent  
Michael Harper  
Ian Mason  
Susan Searle

### Nominations Committee

**Mark Elliott, Committee Chairman**  
Admiral Sir James Burnell-Nugent  
Michael Harper  
Ian Mason  
Paul Murray  
Susan Searle  
Steve Wadey

### Remuneration Committee

**Michael Harper, Committee Chairman**  
Admiral Sir James Burnell-Nugent  
Mark Elliott  
Ian Mason  
Paul Murray  
Susan Searle

### Risk & CSR Committee

**Admiral Sir James Burnell-Nugent, Committee Chairman**  
Mark Elliott  
Michael Harper  
Ian Mason  
David Mellors  
Paul Murray  
Susan Searle  
Steve Wadey

### Security Committee

**Admiral Sir James Burnell-Nugent, Committee Chairman**  
Michael Harper  
Ian Mason  
David Mellors  
Paul Murray  
Susan Searle  
Steve Wadey

## Key governance highlights

- Continuity in governance structures put in place at the end of 2013, with the Operating Committee overseeing operational management and the Governance Committee overseeing risk management
- Continued focus on succession planning, with changes at Executive and Non-executive Director level during the year
- Good working relationship established with the new Proxy Board in the USA following the US restructuring in 2014
- Continued focus on strategy and greater measurement of progress against targets

\* Definitions of underlying measures of performance can be found in the glossary on page 141.

<sup>†</sup> Restated to reflect continuing/discontinued operations (see note 1 to the financial statements on page 97).

# Customer-focused

**Steve Wadey**  
Chief Executive Officer



## Future priorities

- Operational excellence and capital discipline
- Innovation and investment in organic capabilities
- Customer focus

### **QinetiQ is a company that is focused firmly on its customers.**

I am delighted to be leading QinetiQ – a company that is built on the expertise of its people focused on providing effective solutions for our customers.

There's no denying that global markets are challenging, but they also present opportunities. Throughout the world, the proliferation and pace of technology means that threats to our security are increasing in number and diversity. The ability to harness information, knowledge and technology is critical to meeting these global challenges.

In the UK, Government customers need to deliver more with less and so are seeking greater value. They are looking for suppliers that not only have a track record of delivering efficiencies but can also help them meet new challenges through innovation.

In the US, the Federal Government continues to pursue technological superiority as its principal source of military advantage and has posed the question – 'what next?' Disruptive innovation will be at the heart of any answer, and this will have an impact on military customers and markets worldwide.

Amongst prime contractors, competition is becoming more fierce. They are engaging with the supply chain to find new sources of competitive advantage.

Although changes in market dynamics can cause uncertainty, they also create chances to do things differently, particularly for companies like QinetiQ with the right foundations and inherent capabilities.

Competitive and financially robust, QinetiQ is a company that is ready for a new phase of its journey. Our people already have a sense of where we are going in the future but the changes in global markets demand that we are more externally facing.

Success will be built on operational excellence – doing what we say we are going to do, and underpinned by continued capital discipline.

It will be driven by investing in our organic capabilities and responding proactively to the changes in our global markets through agility and innovation that deliver effective solutions for our customers.

I look forward to leading QinetiQ during the next phase in its journey and to the exciting future that we have ahead of us, focused firmly on continuing to meet our customers' needs.

### **Steve Wadey**

Chief Executive Officer  
21 May 2015



## 2015 Year in review – David Mellors, CFO

- Strong performance in EMEA Services with increased orders, revenue and operating profit
- Core Air, Weapons and Maritime businesses all performed well
- New President appointed to lead repositioning of US Global Products in response to a challenging market
- Continued high cash conversion
- £150m share buyback well advanced; £128m complete at 15 May 2015
- 17% increase in full year dividend reflecting upgrade at the half year and progressive dividend policy
- 77% revenue under contract at start of 2016 consistent with prior year; balance supported by pipeline of opportunities
- Maintaining expectations for Group performance in the current financial year

Orders grew 3% to £613.6m (2014: £596.9m<sup>^</sup>), and Group Book-to-Bill ratio was 1.1x. At the beginning of the new financial year, 77% of the Group's FY16 revenue was already under contract, a similar level to a year ago.

Revenue was £763.8m (2014: £782.6m<sup>^</sup>). EMEA Services delivered a strong performance, with a 3% increase in revenue and the core Air, Weapons and Maritime businesses all delivering improved results. The performance of Global Products continued to be impacted by the ongoing reduction of US military forces deployed to Afghanistan, which depressed demand for conflict-related products.

Underlying operating profit\* was £111.3m (2014: £113.7m<sup>^</sup>) with growth in EMEA Services offset by Global Products, which was impacted by the reduction in revenue and by approximately \$5m of additional one-off costs associated with separating from US Services infrastructure.

Underlying profit before tax\* increased 7% to £107.8m (2014: £101.2m<sup>^</sup>) with underlying net finance costs\* falling to £3.5m (2014: £12.5m<sup>^</sup>) as a result of the early repayment of the private placement debt in June 2014.

Underlying earnings per share\* for the continuing Group were up 10% at 15.2p (2014: 13.8p<sup>^</sup>), benefiting from the higher underlying profit before tax\* and reduced number of shares following the repurchase of £107m of the £150m share buyback programme as at 31 March 2015. Basic earnings per share for the total Group (including US Services) were 16.6p (2014: 1.9p loss per share).

Underlying operating cash conversion\* remained strong at 103% (2014: 93%<sup>^</sup>), delivering an underlying cash flow from continuing operations\* of £114.9m (2014: £106.2m<sup>^</sup>). At 31 March 2015, the Group had £195.5m net cash, compared to £170.5m net cash at 31 March 2014 and £205.7m at 30 September 2014.

## QinetiQ investment case

### 1. Unique and resilient competitive position

- Unique technical expertise and domain know-how
- Trusted advisor – independent position in supply chain
- Excellent customer relationships
- Underpinned by a portfolio of large long-term contracts
- Sustainable core businesses well positioned to win market share
- Opportunity to expand existing capabilities into new international markets

### 2. Delivering earnings growth and shareholder returns

- Strategy for growing sustainable earnings through effective management of the Group's portfolio
- Competitive cost base
- High cash generation
- Strong balance sheet
- Disciplined investment management for core and 'Explore' portfolios, with 'Test for Value' largely customer funded
- Progressive shareholder returns

### 3. Significant option value

- Potential for profitable growth from emerging 'Explore' businesses with demonstrable markets
- Development of new options from customer-funded R&D in rigorously managed 'Test for Value' portfolio

\* Definitions of underlying measures of performance can be found in the glossary on page 141.

<sup>^</sup> Restated to reflect continuing/discontinued operations (see note 1 to the financial statements on page 97).

# Our value pipeline

## Organic-Plus strategy

- The objective of our Organic-Plus strategy is to deliver growing sustainable earnings by optimising our portfolio.
- We aim to win market share in core markets and nurture 'Explore' opportunities to deliver growth particularly beyond defence, all underpinned by continued financial discipline.
- The Group is sufficiently cash generative and disciplined about capital allocation to support ongoing investment in growth opportunities, a progressive dividend policy and the maintenance of a strong balance sheet.

## Value pipeline

- Our Organic-Plus strategy prioritises active portfolio management. All of our business operations are graded within a value pipeline which gives us full visibility and direction over our assets and capabilities.
- Whether they are well-established business models or new capabilities with as yet unclear commercial potential, we manage and invest in them according to three criteria:
  - Maturity: how ready is our offering and is there an attractive market?
  - Potential scale: can it one day earn significant profits?
  - Investment: how much will it cost to achieve success?

The Group's principal role is to optimise business returns by allocating resources appropriately.

## Core

### Increased market share

85%  
Revenue

**Sustainable and defensible businesses, focused on growing market share. This is the 'engine' on which our reputation and customer relationships are built, the driver for continual renewal of our expertise and technology, and the source of the majority of our profit and cash flow.**

Our core businesses are focused on relatively resilient sectors in which the technical expertise and domain know-how of our people is used to provide trusted independent advice and solutions for our customers' critical operations.

These are our sustainable and defensible core capabilities, mostly comprising EMEA Services, and operating largely in the defence, security and aerospace markets.

Much of the revenue is derived from longer-term contracts, with known dates for renewal and re-tender. These contracts exhibit relatively low risk characteristics with low capital requirements and strong, predictable cash flows that can be invested for future growth. Our core businesses also provide a dynamic source of new intellectual property that is initially collected and categorised in 'Test for Value' and managed through the value pipeline.

Representing around 85% of our revenue, the performance of the core is the main driver of the future value of the Group and the majority of capital investment is focused on these businesses. We are investing selectively in key capabilities to win market share in existing markets and to deploy these capabilities in new sectors and international territories.



Strategic

Employees

Customers

## Operated under strict rigour

**Explore****Growth in new markets**

**10%**  
Revenue

**Our 'Explore' businesses are high potential, emerging businesses, typically with a proven competitive offering in growth markets, often beyond defence. They represent the best opportunities for future growth, to at least \$100 million revenue a year, from both our services and products divisions.**

These are established, commercially viable businesses that have proven technology and customers. In many cases, they have been separated out as 'Explore' business units in their own right, with appropriate support from the corporate team.

The challenge they face is to evolve a business model that can achieve significant scale in order to become the sustainable, value-accretive core businesses of the future. By meeting this challenge we will deliver a broader base of significant businesses, thereby increasing the diversification of the Group.

We are selectively investing in these businesses to determine their ability to deliver growth both in the UK and overseas. Investments can include new leadership and skills, accelerated business development, strategic acquisitions, alliances and partnership as appropriate to build momentum.

**Test for Value****Commercial traction**

**5%**  
Revenue

'Test for Value' offerings are early-stage options that are typically based around innovative technology or know-how.

These technologies are often developed under customer-funded programmes, so the portfolio can be likened to a drug pipeline for a pharmaceutical company, except that development takes place in partnership with customers who provide the majority of early-stage funding.

Investment is required to achieve full commercialisation and so we rigorously assess the viability of these options and their markets to determine how best to realise their potential. Technologies are often licensed out to reduce implementation and sales risks, or taken to market with partners. They can also be integrated to 'Explore' and receive investment, divested or closed.



IP as an additional benefit

**Priorities****Growth Orientation**

Strategic Priorities		Employees
To deliver		Capability through our People Who Know How
<b>What we are striving for</b> <p><b>Key:</b>  <span style="color: #005a99; font-weight: bold;">15</span> 2015 progress  <span style="color: #005a99; font-weight: bold;">16</span> 2016 priorities</p>		Empowered, engaged and highly skilled employees who are passionate about customer service excellence, innovation and responsible business practice.
<b>How we are getting there</b> <p><b>Key:</b>  <span style="color: #005a99; font-weight: bold;">15</span> 2015 progress  <span style="color: #005a99; font-weight: bold;">16</span> 2016 priorities</p> 		<p><b>Creating the right environment</b>  <i>Building a collaborative, empowered culture that recognises the contribution of all employees</i></p> <p><span style="color: #005a99; font-weight: bold;">15</span> Enhanced engagement with the EEG, our independent consultative forum</p> <p><span style="color: #005a99; font-weight: bold;">15</span> EST community established for our Engineers, Scientists and Technicians</p> <p><span style="color: #005a99; font-weight: bold;">16</span> Facilitate greater collaboration by building understanding of cross-functional working</p> <p><span style="color: #005a99; font-weight: bold;">16</span> Develop training, guidance and support networks to ensure inclusivity of all employees</p> <p><b>Attracting talent</b>  <i>Sourcing People Who Know How today and developing the pipeline for tomorrow</i></p> <p><span style="color: #005a99; font-weight: bold;">15</span> Focused Centre of Excellence created for Early Careers</p> <p><span style="color: #005a99; font-weight: bold;">15</span> 5% Club target achieved</p> <p><b>Developing our people's potential</b>  <i>Investing in our people to enhance their knowledge and skills</i></p> <p><span style="color: #005a99; font-weight: bold;">15</span> Learning and development Centre of Excellence established</p> <p><span style="color: #005a99; font-weight: bold;">15</span> Launched eLearning tools for technical skills, management and leadership</p> <p><span style="color: #005a99; font-weight: bold;">16</span> Launch QinetiQ Academy to develop our people to their full potential</p> <p><span style="color: #005a99; font-weight: bold;">16</span> Develop structured Early Careers Programmes to improve the development of young employees</p> <p><b>Retaining talent</b>  <i>Creating opportunities for our people to flourish and grow</i></p> <p><span style="color: #005a99; font-weight: bold;">16</span> Build transparency of the employee proposition by developing Total Reward Statements</p>
<b>KPIs</b> <p>The KPIs used as a measure of executive performance are marked in bold.</p>		<ul style="list-style-type: none"> <li>• Health and safety</li> <li>• Voluntary employee turnover</li> <li>• <b>Employee engagement</b></li> <li>• % Apprentices and graduates</li> </ul>
<b>Risks</b>		<ul style="list-style-type: none"> <li>• Recruitment and retention</li> </ul>
The way we work		
<b>Risk sensitive</b> <ul style="list-style-type: none"> <li>• Emerging and reputational risk</li> <li>• Significant breach of relevant laws, regulations, IT and security</li> <li>• Defined benefit pension obligations and tax legislation</li> </ul>		<b>Measuring progress</b> <ul style="list-style-type: none"> <li>• <b>Underlying operating profit</b></li> <li>• Total Group profit after tax</li> <li>• <b>Underlying EPS</b></li> <li>• <b>Underlying operating cash flow</b></li> </ul>
 <b>P30</b> Risk management		 <b>P20</b> Key performance indicators

## Customers

## Growth Orientation

### Increased market share

Customer relationships which build mutual trust so we can help our customers shape and achieve their current and future challenges.

#### Helping shape the requirement

*Listening to and helping to shape the needs of our customers*

- 15 Structure aligned with MOD Front Line Commands
- 15 Board-to-Board meetings established with key customers
- 16 Develop new propositions for the MOD
- 16 Extend customer base

#### Delivering solutions

*Working in partnership with them to understand and solve their problems*

- 15 Working with the MOD to support its transformation
- 16 Invest in Long Term Partnering Agreement
- 16 Support Front Line Commands with their new accountabilities

#### Excellence in delivery

*Doing what we say we are going to do and ensuring good contract governance*

- 15 'Safe for Life' programme supported by 70 safety champions
- 15 Launched an academy for development of over 400 project managers
- 15 Customer feedback gathered every year by independent third party
- 16 Launch accredited training for commercial managers

#### 'Working smarter'

*Fully leveraging available resources*

- 15 Hackathons held regularly, offering innovation for customers

### UK and international growth

Growth both in and beyond the UK, using our domain know-how and the reputation of our people, plus a pipeline of future technology-based offerings to remain ahead of global technology proliferation.

#### Developing our existing business

*Actively managing our portfolio*

- 15 US Services sale completed
- 15 'Explore' opportunities established as independent business units
- 16 Increase frequency of engagement with senior customers

#### Looking for new opportunities

*Developing new partnerships and alliances and rigorously evaluating opportunities for risk.*

- 15 International Business Development Director appointed
- 15 Canadian market potential developing with the opening of our Ottawa office
- 16 Develop international strategy, model and propositions
- 16 Target countries and regions through independent market research

#### Developing new ideas

*Generating new intellectual property*

- 15 Chief Technology Officer appointed focused on innovation
- 16 Reposition My Contribution programme to focus on innovation and growth

### • Customer satisfaction

- Orders
- Organic revenue growth

### • Defence and security spending

- Trading in a global market

## High performance culture

- Protecting and enhancing our reputation by being a responsible and sustainable business
- Working smarter through operational excellence and continuously improving our productivity
- Environmental stewardship and community investment

## Defence

# Transportable ranges protect vessels and save money



## Employees

### An expert stealth team

Neil Allan, QinetiQ project manager – “We minimise a ship’s signature both magnetically and acoustically, making an 8,500-tonne Type 45 Destroyer virtually unrecognisable by a mine.”

Rob Wild, MOD Operational Signature Services – “The service includes managing all the associated and wide ranging logistics in getting equipment into theatre, managing subcontractors such as divers and providing the specialist, knowledgeable and highly experienced QinetiQ staff.”



## Customers

### Making an 8,500 tonne destroyer look like a much smaller vessel

Often delivered in difficult conditions and under severe time pressures, our Maritime Stealth Information and Range Services team provides the UK Royal Navy with world-class stealth management capabilities, helping to make vessels combat ready. Rather than sailing mine-hunters out and back for six-month tours in the Middle East, our in-theatre expertise saves the customer more than 85,000 nautical miles, allowing four vessels to be based in the region for years. We place magnetic and acoustic sensors in the water, sail a vessel over

them, and then calibrate onboard systems to avoid detection by aggressors.

Mechanical Engineering Officer, HMS Shoreham – “Ranging highlighted issues we were unaware of... identifying defects that may otherwise be missed.”

Weapons Engineering Officer, HMS Shoreham – “I consider the level of support received from QinetiQ during the magnetic ranging to be of the highest level; very proactive.”

## Growth Orientation

### World-class capabilities to protect vessels

Independent of manufacturers and proven in the field – we are already the ‘go to’ solutions provider for a leading navy – these services are available to other navies, subject to MOD approval. Potential customers recognise our ranges are among the world’s most sensitive and, coupled with our high performance modelling software, far superior to other offerings.

## Security



# Protecting the public in 'soft target' mass transit locations

## Employees

### Innovative technology from expert engineers

We've been developing passive millimetre wave technology for many years, initially to see through dense foggy environments, and earlier versions of SPO™ were used in operational trials, informing the next generation. Colin Cameron, QinetiQ Technical Lead: "Through constant contact with the customer and exploring how the product can be used successfully, we've directly helped the TSA plug a real capability gap."

## Customers

### Detecting threats for the US Transportation Security Administration (TSA)

The TSA has awarded QinetiQ a \$3m two-year contract for an innovative threat detection system that uses our passive millimetre wave technology: SPO-NX™. With the TSA concerned about terrorist threats to targets like railway stations, ferry and bus terminals, it wanted leading-edge technology to help secure these venues. Working at a range of up to 15 metres, our SPO™ technology scans a crowd and detects if a person is hiding something under clothing – perhaps an explosive device –

without people needing to stop. Travellers are not inconvenienced, the system doesn't emit harmful radiation, and no privacy laws are contravened.

With earlier versions deployed in locations including New Jersey, Washington and Los Angeles, QinetiQ also provides maintenance, support and end user training. Crucially, the TSA itself is actively involved in developing the system.

## Growth Orientation

### Addressing terrorist threats in new ways and more locations

We aligned our experience, know-how and innovation with this customer's active participation and investment to develop next-generation threat detection. With SPO-NX™ intended for a mass market, we plan to expand its reach and deliver larger quantities to customers in the US and organisations in Europe and the Middle East that face security challenges.

Strategic report

Governance

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Additional information

QinetiQ Group plc Annual Report and Accounts 2015

## Defence

# Innovation in aerial targets: delivering accuracy worldwide



## Employees

### Delivering customer-focused target solutions

In this heavily regulated environment, our experience in aviation, engineering and operations management means we can organise the complex logistics required for the most accurate aerial target engagements for our customers worldwide while continuously improving safety and compliance. Mark Sydenham, QinetiQ Target Services Manager: "Our 40-strong team works around the world, is highly mobile and deploys fast, often at short notice."

## Customers

### Combined Aerial Target Service (CATS) builds on unparalleled weapons know-how

Under a 20-year contract, we provide aerial targets worldwide for the UK Army, Royal Navy, RAF and project teams working on new weapons. Previously, the MOD had several contracts with different providers, including ageing and soon-to-be obsolete systems. With reduced military spending and increased emphasis on affordability, it decided to bring all aerial target needs under a single contract with one provider: QinetiQ. We have also completed successful aerial target projects

for the US Air Force, Swiss MOD, Danish Navy and BAE Systems.

Steve Attrill, MOD – "The CATS contract has been a success for the MOD, and QinetiQ is delivering a high level of service. QinetiQ makes available an extremely flexible and responsive service, often reacting at short notice to Armed Forces requirements". During this contract, both customer satisfaction and reliability have consistently increased.

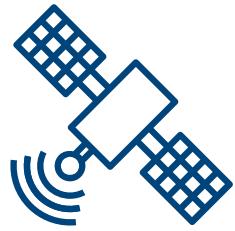
## Growth Orientation

### Continuing innovation in the air

Demand for our services is rising: a recent contract for Sweden involved working with a US target manufacturer to deliver launchers and operators, and we are now exploring opportunities to bring other suppliers' targets into CATS to offer even better performance and value for money to customers.



## Aerospace



# Leading-edge satellite technology breaks new ground in space

## Employees

### Pushing the boundaries of the possible

Frank Preud'homme, QinetiQ Space – “We've established an enviable track record through our work on previous missions such as Proba-2, which captured the famous image of March's solar eclipse. ESA chose QinetiQ because Proba-3 requires a small and agile platform at an affordable price, and we can deliver cutting-edge technology in shorter time scales and at lower cost.”

## Customers

### Compact, highly complex avionics power a remarkable spaceflight

The European Space Agency awarded QinetiQ Space a €16m three-year contract to develop the computer and avionics for its Proba-3 mission: two satellites making a virtually 'fixed' structure in space by precise formation flying only 150 metres apart. Proba-3 will study the Sun's corona using an eclipsing mechanism, with a camera fixed on one satellite and an occulting disk on the other – and flying at the optimal distance apart to shield the camera from the Sun and create conditions usually only observable during a solar eclipse.

Our Belgium-based team is creating highly compact avionics able to process millions of instructions per second while also operating effectively in the punishing high-radiation environment of space. Affordability was a critical element in this technically challenging project.

## Growth Orientation

### A future in space

This mission will demonstrate the importance of formation flying for scientific research, with QinetiQ expertise contributing to the success of future missions. Our Space business is currently running four additional ESA satellite studies, expected to feed into future missions, with each project won competitively.

# Measuring our progress

## Key performance indicators (KPIs)

The objective of our Organic-Plus strategy is to deliver growing sustainable earnings by optimising our portfolio. Progress is measured through a range of financial and non-financial key performance indicators. Measurements of health and safety, customer satisfaction and employee engagement underpin sustainability. Measures such as order intake, organic revenue growth, profitability and cash flow track financial performance.

Similar indicators are used to review performance in each of the Group's businesses.

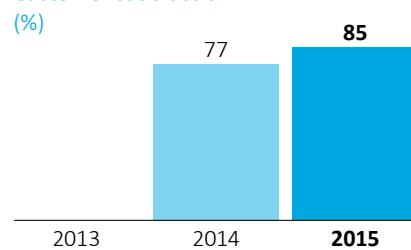
 **P24** Responsible business

## Continuing operations

All KPIs have been restated to reflect the continuing operations only.

## Non-financial KPIs

### Customer satisfaction



### 2015 performance

**85%**

Of our customers recognise us as a top three supplier

### Description

QinetiQ's customer satisfaction survey was introduced in 2014, following suspension of the MOD survey, to ask all UK customers with contracts over £200,000 about QinetiQ's delivery, engagement and relationship. In the US, customer satisfaction metrics are reviewed on a contract-by-contract basis.

### Rationale

Using an independent third party we annually survey around 100 of our largest projects to help us understand our performance and what we need to be doing to continuously improve. We also gather qualitative feedback through structured interviews.

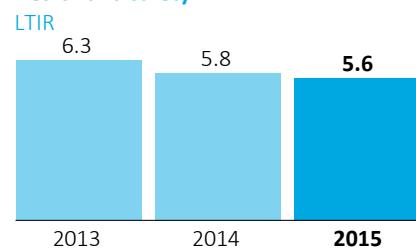
### Performance this year

Of those surveyed, 85% told us that QinetiQ is performing as a 'top three' supplier, up from 77% last year. We are moving in the right direction.

### Link to strategy

Developing relationships with our customers that are built on mutual trust is a key strategic priority.

### Health and safety



### 2015 performance

**5.6**

Calculated on the lost time incident rate (LTIR)

### Description

The LTIR is calculated using the total number of accidents resulting in at least one day taken off work, multiplied by 1,000 divided by the average number of employees in that year.

### Rationale

Health and safety performance is monitored to drive continual improvement in minimising risks to employees and reducing harm.

### Performance this year

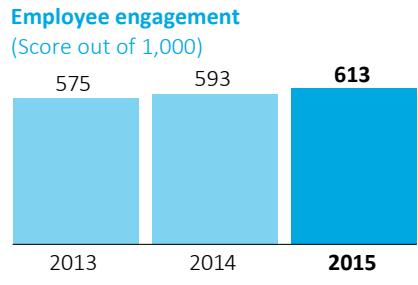
The LTIR has decreased slightly from previous year. The absolute number of lost time incidents, resulting in at least one day off work, is broadly similar to last year.

### Link to strategy

The safety, health and wellbeing of our people are intrinsically linked to our strategic success.

 **P72** Directors' remuneration report

 **P24** Responsible business

**2015 performance****613**

Scale of 0–1,000 based on Best Companies Employee Survey

**Description**

A measure of employee engagement (in the UK) on a scale of 0–1,000, based on the Best Companies Employee Survey. Through this survey, employees share their views about working at QinetiQ under the headings of management, leadership, company, personal growth, my team, giving something back, fair deal and wellbeing.

**Rationale**

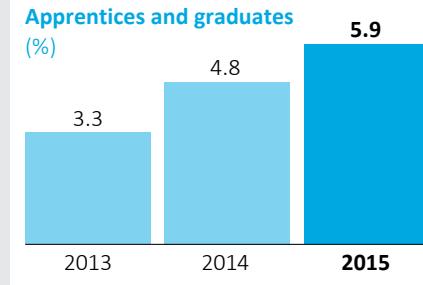
The annual survey enables comparison between QinetiQ and other UK companies.

**Performance this year**

We have again seen an improvement in our overall engagement score, taking us into the Best Companies 'ones to watch' category.

**Link to strategy**

QinetiQ seeks to develop, engage and empower highly skilled employees who are passionate about customer service excellence, innovation and responsible business practice.

**2015 performance****5.9%**

Total percentage of our UK workforce

**Description**

The number shown is the total number of apprentices and graduates as a percentage of our UK workforce.

**Rationale**

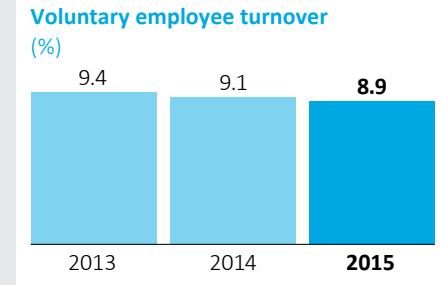
Provides a measure of QinetiQ's ability to attract and develop new employees. It is also a measure of our commitment to The 5% Club, an industry-led initiative to grow the number of young people on apprenticeships and graduate programmes.

**Performance this year**

We have increased the percentage of our UK workforce who are on apprenticeships or graduate programmes to 5.9%, meeting the target we set last year.

**Link to strategy**

To deliver outstanding value for our stakeholders we need to source People Who Know How today and develop the pipeline for tomorrow. QinetiQ is seeking to inspire a new generation of engineers and scientists.

**2015 performance****8.9%**

Employees leaving not at QinetiQ's instigation

**Description**

This is a measure of the number of employees leaving the Company not at QinetiQ's instigation.

**Rationale**

Provides a measure of the Group's ability to retain employees.

**Performance this year**

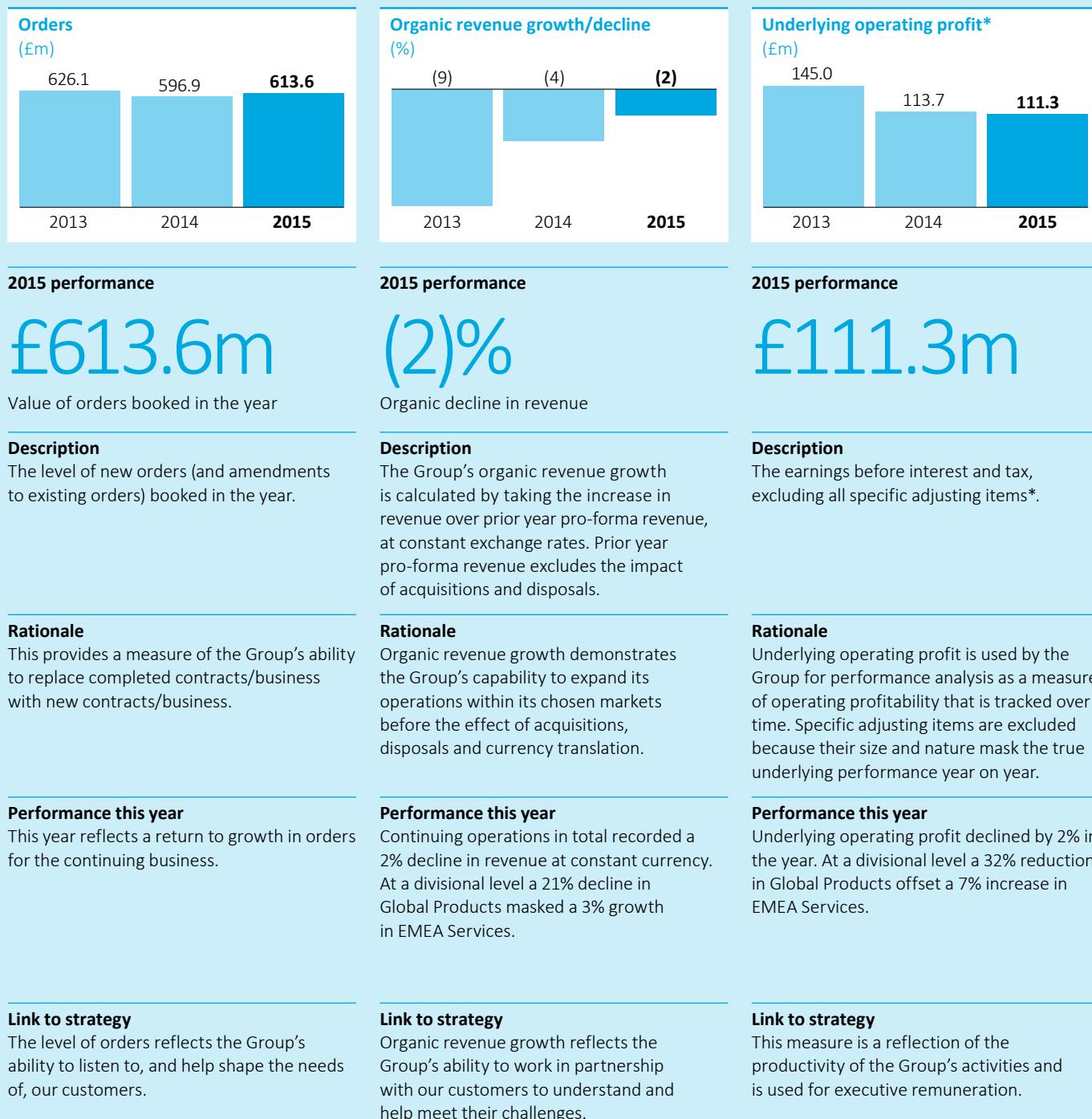
The trend of a reduction in voluntary employee turnover has continued this year, falling to 8.9%.

**Link to strategy**

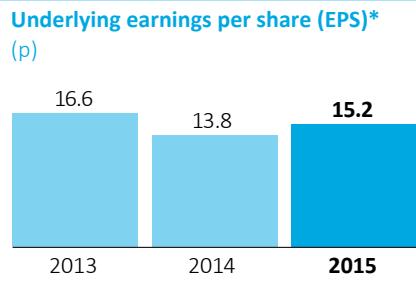
Our employees are our principal source of competitive advantage, directly impacting our ability to win and retain business. As such, QinetiQ's future success lies in its ability to create opportunities for our people to flourish and grow.

**P72** Directors' remuneration report**P24** Responsible business

## Financial KPIs – continuing operations unless stated



\* Definitions of underlying measures of performance and specific adjusting items can be found in the glossary on page 141.



#### 2015 performance

**15.2p**

Per share

#### Description

The underlying earnings, net of interest and tax, expressed in pence per share.

#### Rationale

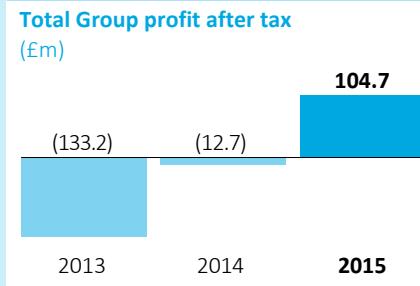
Underlying EPS provides a measure of the earnings generated by the Group after deducting tax and interest. Specific adjusting items are excluded because their size and nature mask the true underlying performance year on year.

#### Performance this year

Underlying EPS grew by 10%. A marginal decline in underlying operating profit was more than offset by a reduction in net finance expense (following repayment of private placement debt), a marginal reduction in the tax rate and a lower number of shares in issue.

#### Link to strategy

This is used for executive remuneration, determining the level of pay-out for certain of the Group's long-term incentive plans.



#### 2015 performance

**£104.7m**

#### Description

This is the total Group profit/(loss), net of interest and tax, including all specific adjusting items and including discontinued items\*.

#### Rationale

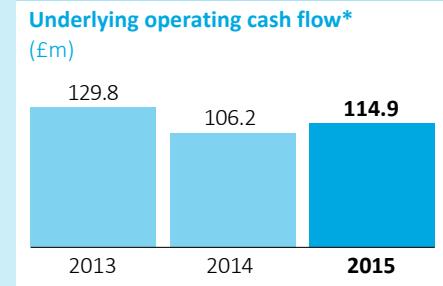
This shows the overall financial performance of the Group reflecting both underlying and specific adjusting items of income and expenditure. A key financial measure used to reflect overall financial performance for the year.

#### Performance this year

The significant step up in the total Group profit after tax primarily results from the absence of impairment charges in the year as the prior years both contained significant impairments of goodwill.

#### Link to strategy

This is a key financial measure of overall financial performance for the year.



#### 2015 performance

**£114.9m**

#### Description

This represents net cash flow from operations before cash flows of specific adjusting items, less net cash outflows on the purchase/sale of intangible assets and property, plant and equipment.

#### Rationale

This provides a measure of the Group's ability to generate cash from its operations and gives an indication of its ability to service its debt, make discretionary investments and pay dividends to shareholders.

#### Performance this year

Underlying operating cash flow increased from the prior year and represents a cash conversion of more than 100%.

#### Link to strategy

This is a measure of the cash-generative characteristics of the Group and is a measure used for executive remuneration.

\* Definitions of underlying measures of performance and specific adjusting items can be found in the glossary on page 141.

# Making a positive impact

## Key highlights

- CBI Award for The 5% Club
- Green Apple Award for Energy Matters programme
- Successful pilot of the Safe for Life programme
- Improved Employee Engagement Survey score

### QinetiQ's corporate responsibility priorities

Our priorities can be summarised across four themes, which we believe ensures that we meet our stakeholders' expectations and contribute to our future success.

### Business ethics

To be a responsible and sustainable business

 P25



### Responsibility to our people

To attract, engage and develop the best people

 P26



### Community investment

To make a positive contribution to the community

 P28



### Environmental stewardship

To be an excellent environmental steward

 P29



### Engaging with our stakeholders

Our Corporate Responsibility strategy reflects the material issues for our business – defined by our overall business strategy and taking into account stakeholder priorities. We ensure that we understand these priorities through regular dialogue such as investor meetings, involvement in the MOD-Industry Sustainable Procurement Working Group and our employee engagement programmes. We have introduced a corporate responsibility network with representatives from across the business to raise awareness of programmes and plans. We are actively engaged with industry through the Defence Growth Partnership and trade body working groups on topics such as skills, environment and ethics.

### Managing our approach to responsible business

#### Governance

Successful delivery of responsible business practice is driven by strong leadership and governance and we have Board and executive level commitment to corporate responsibility through the Group Risk & CSR Committee.

### P70 – Report of the Risk & CSR Committee

The Committee receives reports and briefings on all material corporate responsibility issues including business ethics, health and safety, environment, reputational risk and human rights for its regular meetings. In QNA the Proxy Board oversees these activities, obtaining independent assurance on the adequacy of its compliance programmes on an ongoing basis. QinetiQ's commercial success is influenced by our ability to conduct business in overseas territories, transacting with foreign governments and commercial organisations in a legally compliant manner, controlling the international movement of certain strategic items. Employees are provided with annual training on export controls.

#### Certification

The Group's policies and management systems underpin our corporate responsibility programmes. In the UK, the business assurance tool provides internal assurance and we have the external certification ISO 14001 for our environmental management system, ISO 9001 for our quality management system and OHSAS 18001 for our health and safety management system.

#### Supplier management

While QinetiQ prides itself on having 'The People Who Know How', we also draw upon the goods and services provided by our approved suppliers. Our suppliers range from other industry primes to Small and Medium sized Enterprises (SMEs), meaning that QinetiQ contracts and collaborates with a wide variety of industry partners, and ensuring that our customers receive the best available solutions in the marketplace. Our robust procurement and supplier risk management processes ensure that we work openly and ethically, in the best interest of our customers.



## Business ethics

In December 2014 we updated the QinetiQ Group Code of Conduct, including a new section on ethical decision-making. The Code lays out our ethical standards, providing employees with clear direction and guidance on how we do business across the Group. Employees are encouraged to talk to a manager if they have a concern and are provided with contact details for our ethics email advice services and our independently run, 24/7 confidential reporting line. Employees are supported in understanding and using the Code of Conduct through our annual business ethics training, which is a mandatory requirement for all employees. It is also undertaken by our Board and is available for our contractors and customers as well. In addition to explaining the Code of Conduct, the training provides a number of challenging scenarios to help employees know what to do if they were to come across issues such as bribery, fraud, discrimination and conflict of interest. We have also communicated with managers to remind them of the need to act if employees come

to them with issues. We have provided help and advice in response to all queries received via our ethics email advice services and all communication through the whistleblowing line is appropriately investigated.

### Anti-bribery and corruption

We have a zero-tolerance approach to bribery and corruption and have put in place a range of governance measures. Anti-bribery risk management is embedded in our business processes; we have a process for undertaking due diligence, monitoring and auditing of our use of commercial intermediaries, and we use expert third-party providers of due diligence where appropriate. We provide more in-depth anti-bribery training for those in higher risk roles, for example those who carry out overseas business. Our anti-bribery programmes are overseen by our Chief Ethics Officers, who are senior executives.

### Human rights

QinetiQ recognises that the UN Guiding Principles on Business and Human Rights

set a standard of conduct expected of companies. We seek to anticipate, prevent and mitigate potential negative human rights impacts through our policy and process, and through our Code of Conduct and business ethics training for employees, all of which underpin our commitment to responsible business conduct. QinetiQ has policies in place, among others, to support adherence to export controls, health and safety, non-discrimination, anti-bribery and environmental laws and guidance. This is further supported by our procedures on product safety, sustainable procurement, due diligence and risk management. We monitor the application of these policies and procedures through our business assurance processes. We believe that this embedded approach is effective. We have recently implemented a more structured approach to understanding human rights risk within our international business risk management process. We have also been working to improve our approach to human rights risk in the supply chain.

## Corporate responsibility in action

### STEM Outreach: Inspiring the next generation

Our Malvern site welcomed more than 90 children from four schools to a special STEM (Science, Technology, Engineering and Maths) event. With competitive activities such as creating autonomous Lego robots, programming airlocks, behavioural modelling and building Android apps alongside live

demonstrations of QinetiQ technology, our objective is to continue inspiring the next generation of scientists and engineers.

The event organiser, QinetiQ systems engineer and STEM ambassador Tara Francis, has been an outstanding volunteer in outreach initiatives, and was nominated in 2014 for a national STEMNET "Most Dedicated STEM Ambassador" Award.



### The 5% Club: Investing in a generation

In September 2014, The 5% Club won the CBI Special Award for 'Outstanding Business Led Campaign'. The award was presented to The 5% Club Campaign Director, QinetiQ's Dr Sam Healy, who said:

"Aiming to tackle the dual issues of youth unemployment and skills shortages, the campaign encourages members to provide great 'earn and learn' opportunities for young people with the aim of having 5% of their workforce on apprenticeships or graduate programmes. It's been a rewarding experience to work on this campaign. I'm delighted by the response from industry – we now have over 70 members and I'm looking forward to working with even more organisations in the future."



## Responsibility to our people

### 2015 Highlights

- The 5% Club received the CBI Award for Outstanding Business Led Campaign
- Increased employee engagement
- Successful pilot of Safe for Life

### 2016 Priorities

- Introduce a UK Safety Culture Climate Survey score
- Continuing reduction in Lost Time Incident Rate
- Increase employee engagement
- Continued commitment to The 5% Club

#### Safety, health and wellbeing

QinetiQ puts the safety, health and wellbeing of its people at the heart of operations and safety, health and wellbeing underpin our strategic goals. We continue to focus on reducing accidents and work-related ill health as part of our continuous improvement activity. Last year we decided to move away from a focus on the UK RIDDOR (Reporting of Injuries, Diseases and Dangerous Occurrences Regulations 2013) to overall Lost Time Incident (LTI) Rate, which provides a more internationally relevant lagging indicator for the Group. LTI Rate is highly dependent on the number of employees (calculated as the number of lost time incidents, where the employee is away from work for one or more days, times 1,000 divided by the total number of employees). The headcount in the North American business reduced significantly with the divestment of US Services. Therefore the LTI Rate of prior years has been restated to exclude the US Services business. On this restated basis the LTI Rate has reduced slightly from 5.8 to 5.6.

Lost Time Incident Rate	2015	2014	2013
QinetiQ Group (Excluding US Global Products)	5.0	5.0	5.3
US Global Products	17.8	17.8	17.6
<b>Total</b>	<b>5.6</b>	<b>5.8</b>	<b>6.3</b>

Adjusted in prior years to exclude US Services business.

Last year we recognised a weakness in lagging indicators and, coupled with the desire to improve safety, we introduced 'Safe for Life' into our UK Weapons business. 'Safe for Life' focuses on behavioural safety including safety leadership, human factors, error management and everyday behaviours of our people. The programme is underpinned by a Safety Culture Climate Survey and is supported by local champions. The pilot programme will complete with another Safety Culture Climate Survey in the first half of 2016. Whilst it is too early to identify changes in the safety climate, safety theory would suggest that where safety culture is working well there will be ongoing reduction in significant incidents accompanied by an increase in the reporting of safety related behaviours and hazards. Encouragingly the significant incident rate has halved from 2.7 to 1.3 (per 1,000 employees) and the reporting of safety related behaviours and hazards has significantly increased.

There were no prosecutions, prohibition notices or improvement notices issued by regulators in the UK in 2015.

We continue to develop our health and wellbeing programmes. The UK Wellbeing programme and QinetiQ Benefits+ scheme in the UK are offering more services, with increasing uptake by employees. Free flu jabs and health assessments (measuring BMI, blood pressure and cholesterol) continue to be popular. A new area of focus in the coming year will be improving the inclusion of employees who have underlying health conditions by providing an expert support network.

#### Safety of products

Our most prized possession is trust; delivering products and services safely is essential to our commitment to customers. We have created distinct lines of responsibility for both ensuring and assuring product safety and compliance, with competent individuals holding formally delegated responsibilities. In the UK, technical assurance and independent design review have been fully integrated into our product and engineering lifecycles. We continue to invest in attracting and developing engineers and scientists with

specialist safety expertise and competence. Improvements continue to be driven by our Engineering, Science and Technical leadership team, supported by independent review and audit. We actively support collaborative working with the MOD and other industry organisations, including professional institutions, in order to develop and implement best practice safety standards.

#### Employee engagement

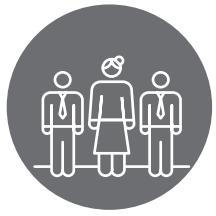
We regularly communicate with employees to ensure they understand QinetiQ strategy and business priorities. Company performance is shared to ensure our employees are aware of what the results mean to our business, how we have made progress against our strategic direction and the market challenges we face. We do this through a wide range of communications channels, e.g. the intranet, roadshows and townhalls.

Our UK Employee Engagement Group (EEG) is an independent consultative forum which covers almost 85% of the Group workforce. Representatives, elected by employees, share views with leadership teams at local, divisional and executive level; so everyone gets to have their say. The EEG listens, gathers feedback and represents employees through times of change; whether it's a local or Company-wide issue. The representatives are the employee voice to constructively challenge policy decisions and actions that have an effect on employees' working lives or wellbeing.

The annual independent Employee Engagement Survey is one of the key tools used to gain feedback from our employees. Following the divestment of US Services, the survey now covers over 90% of employees (it excludes US Global Products). The response rate in 2015 was 73%, which is high in comparison to industry norms, and we scored 613, up from 593, which places us in Best Companies 'Ones to watch' category. The leadership teams develop specific action plans to address areas identified for improvement, e.g. collaboration between teams.

#### Learning and development

Our people are critical to the delivery of excellent service to our customers and we have a highly qualified, experienced



and stable workforce. We have a continued focus on attracting, developing, supporting and retaining our people, which creates the foundation for our future growth. We have established an Engineering, Science and Technical community to create a supportive and collaborative environment for our technical people and we have appointed six new Fellows, who are recognised by QinetiQ customers and peers for their expertise and excellence in their field.

In 2016 we will be launching the QinetiQ Academy, which will underpin our continued focus on delivering excellent training and development. It will support our people in the competencies they need to deliver their roles today, but also ensure they have the skills and succession opportunities for the future. By developing leadership programmes to enhance the skills and knowledge of our current senior team, and growing our next leaders through our talent pool, QinetiQ is well placed to respond to change and look to new horizons.

#### **The 5% Club – Investing in a Generation**

The 5% Club, spearheaded by QinetiQ, has gone from strength to strength, with membership at 72 (at 31 March 2015) and including large and small companies from a range of sectors and recently the MOD. The 5% Club involves formalising what an organisation does in terms of apprentice and graduate programmes and making the public commitment that these will comprise 5% of the UK workforce within the next five years. By encouraging employers to offer great 'earn and learn' opportunities for young people, we see this as a key step in developing the future skills, knowledge and experience needed across the UK.

The 5% Club	2015	2014
Number of apprentices	208	121
Number on graduate programmes	102	106
Number of sponsored students	8	17
Percentage of UK workforce	5.9%	4.8%

Given QinetiQ's commitment to the development of the next generation, we have reviewed our UK Graduate Scheme and will be improving the overall experience. Graduates will be given opportunities outside their main specialism, with the ability to grow their career with us across a much wider career remit. We are refreshing 'Cortex', which provides a practical and friendly support network for those at the start of their careers. Recognising the difference in the attraction and support needed to continue to achieve our objectives with The 5% Club, we have separated out the Early Careers Team into a specialist Centre of Excellence within HR. This team continues to look at new and innovative ways to engage with schools, colleges, universities and other establishments to attract talented people.

A team of QinetiQ apprentices reached the final of the Brathay Apprentice Challenge 2014, a six-month competition that saw them come in second place and raise £2,300 for charity. Supported by the National Apprenticeship Service, the Challenge tests non-technical work skills and the personal attributes of competing apprentices. The eight finalist teams were selected from over 110 teams and 1,000 apprentices who entered the competition.

#### **Diversity and inclusion**

Inclusion of all employees is a key objective. The US Global Products business has a number of alliance partners that assist in all aspects of inclusion. In the UK, we are working with the Employers Network for Equality and Inclusion and, using tools they have developed, we have undertaken a gap analysis to evaluate areas for improvement in our approach to diversity and inclusion. This will form the baseline to measure improvement. With the Global Working Centre of Excellence being set up to look at issues related to the increased activity across the global market, they will also give consideration to diversity and inclusion issues across the territories and regions in which we work.

The breakdown of the number of employees by gender at the end of March 2015 is shown in the table below.

Level	Female	Male
Board Directors	1	8
Senior managers	33	279
All employees	1,236	5,014

The QinetiQ Brathay challenge team, 2014.





## Community investment

### 2015 Highlights

- Several successful flagship STEM outreach events including Schools Powerboat Challenge
- Second year of awarding the Volunteer of the Year award
- Employee Engagement Survey score 'giving something back' increased

### 2016 Priorities

- Continue to increase employee volunteering participation and reaching more girls as part of the Your Life campaign pledge

QinetiQ is committed to being a good neighbour in the communities in which we operate. We believe it's the right thing to do and it is valued by our employees. The 'giving something back' section in our employee survey allows employees to express their opinions on our community programmes.

One way in which employees contribute to being a good neighbour is by volunteering their time and professional skills. Our UK Employee Volunteering Scheme has been running since 2011 and provides employees with time and access to a bursary. A similar

programme has been launched this year in Australia, called 'Operation Give Back', where employees volunteer as individuals or in teams for one day a year.

Our flagship initiative is our STEM (Science, Technology, Engineering & Maths) outreach programme with the aim of inspiring the next generation of scientists and engineers. We value our relationships with organisations such as STEMNET, the Arkwright Scholarship Trust and the SmallPeice Trust in the UK and various robotics education programmes in the US. Our UK STEM Ambassadors have organised STEM outreach events for school children such as the annual Powerboat Challenge and have hosted the UK Cyber Security Challenge. QinetiQ Australia has provided its Paramarine Ship and Submersible Design Software to students of Australian schools participating in the Future Submarine Technology Challenge (SUBS in Schools) in association with the Re-Engineering Australia Foundation Ltd. QinetiQ's Space business in Belgium participates in STEM outreach programmes such as Technoteens.

QinetiQ is a signatory of the 'Your Life' campaign, and our priorities are to encourage employees to take part in STEM outreach programmes, and ensure that we are reaching more girls. Our non-STEM employees also use their

professional skills in the communities where we operate through programmes such as Young Enterprise and they offer mentoring through the Social Mobility Foundation.

Last year we created a new Volunteer of the Year award, which recognised the achievement of an employee who has made an outstanding contribution by volunteering in the community. Last year's award was won by Dr Ruth Tunnell for her mentoring through the Social Mobility Foundation.

QinetiQ in the UK continues to support three corporate charities voted for by employees (Cancer Research UK, Help for Heroes and RNLI) by providing matched funding for any employee fundraising activities. A sponsorship and donations committee reviews charity requests and a small number of additional donations to local charities are made on a case by case basis where there is an alignment to our strategy. Employees can also choose to give to their chosen charity pre-tax through payroll giving. In the US, employees focus on supporting wounded military and their families by contributions to a range of specialist organisations. In Belgium they continue to support a community investment project at a school in Baladharshan, India.

QinetiQ employees climbed Helvellyn mountain via Striding Edge for Cancer Research UK. Together they raised over £3,000.





## Environmental stewardship

### 2015 Highlights

- Green Apple Award for Energy Matters programme
- Good progress against energy reduction target

### 2016 Priorities

- Improve asset re-use and waste recycling
- Reduce greenhouse gas emissions due to UK energy use by 17% by 2020 from the 2013 baseline

#### Environmental stewardship

QinetiQ's environmental management system (EMS) is geared to the unique challenges of delivering a compliant, sustainable and ever improving workplace against the background of MOD and technology based trials, often within environmentally sensitive areas. Our UK EMS, certified to ISO 14001, is supported through the collaboration of the business, site and functional teams, with specialist support from our regional Environmental Advisors. The use of sustainability appraisals, in trial and project planning, enables early identification of potential hazards/impacts and determination of suitable and sufficient mitigation measures. In addition, our monitoring processes have been further strengthened, during 2015, via structured Evaluation of Compliance formats and processes, feeding a site status EMS matrix.

Director of facilities management and Energy manager, receiving the Green Apple Award for the Energy Matters Initiative.



#### UK waste management

Total waste levels in FY15 were lower than in the previous year with 5,001 tonnes (including 313 tonnes of hazardous waste) compared to 5,514 tonnes (including 112 tonnes of hazardous waste) in FY14. However we missed our challenging objective to have less than 10% waste go to landfill. We achieved 13%, principally due to the need to review and re-balance segregation and collection arrangements following footprint and waste service changes. There was, however, a slight increase in recycling, reaching 76% (up from 74% in FY14). Enhanced re-use of assets and segregation/recycling of waste will continue to be our focus during FY16.

#### Greenhouse gas emissions and energy management

We are making good progress on UK energy reduction via our Energy Matters programme. Energy Matters brings together a focused campaign element, promoting involvement and the contribution that can be made at all levels within the organisation, with a structured network of Energy Champions and Energy Engineers to identify and manage significant consumption reduction projects and maintenance. During 2015, we received a Green Apple Award for the Energy Matters initiative. Our UK electricity usage was 7% lower than last year and oil use reduced by 5%, however there was a 2% increase in our use of gas.

We continue to submit voluntarily to the CDP Climate Change Programme and are registered for the Carbon Reduction Commitment (CRC) scheme. During 2016, we will be seeking accreditation to the ISO 50001 Energy Management standard, as part of our ongoing commitment to driving and demonstrating improvement across the footprint and to meet the requirements of ESOS (the Energy Savings Opportunity Scheme). We continue to capture and report our greenhouse gas (GHG) emissions across the Group to reflect the requirements of the Companies Act 2006 (Strategic report and Directors' report) Regulations 2013.

The GHG emissions statement below provides a summary of the Group's emissions from 1 April 2014 to 31 March 2015, giving a summary of Scope 1 (fuel combustion and operation of facilities) and Scope 2 (purchased electricity) emissions and an intensity ratio (per £m of revenue). We have adopted a financial control approach and have used the UK Government's Conversion Factors for Company Reporting 2014 and Defra reporting guidance (October 2013).

The figures below reflect a number of changes in our business, including the divestment of US Services, some acquisitions, and some improvements in data capture.

Group GHG emissions	Year ended 31 March 2015	Year ended 31 March 2014
Total Scope 1 emissions (tCO <sub>2</sub> e)	26,534	27,590
Total Scope 2 emissions (tCO <sub>2</sub> e)	39,668	38,371
Total Scope 1 and 2 emissions (tCO <sub>2</sub> e)	66,202	65,960
Intensity ratio (tCO <sub>2</sub> e per £m of revenue)	87	55

#### Conservation

Our partnership with Marwell Wildlife, for the management of the Eelmoor Marsh Site of Special Scientific Interest (SSSI), at our Head Office in Farnborough, goes from strength to strength, ensuring ongoing 'favourable condition' status. During FY15, we enhanced communications to our employees and introduced some guided tours of the area, with significant positive feedback; an initiative we are keen to repeat during FY16. Many of our sites and those we manage on behalf of the MOD contain designated conservation areas and our sustainability appraisal process plays an important part in addressing any potential issues as we deliver our test, evaluation and training support services.

# Understanding and managing our risks

## Admiral Sir James Burnell-Nugent

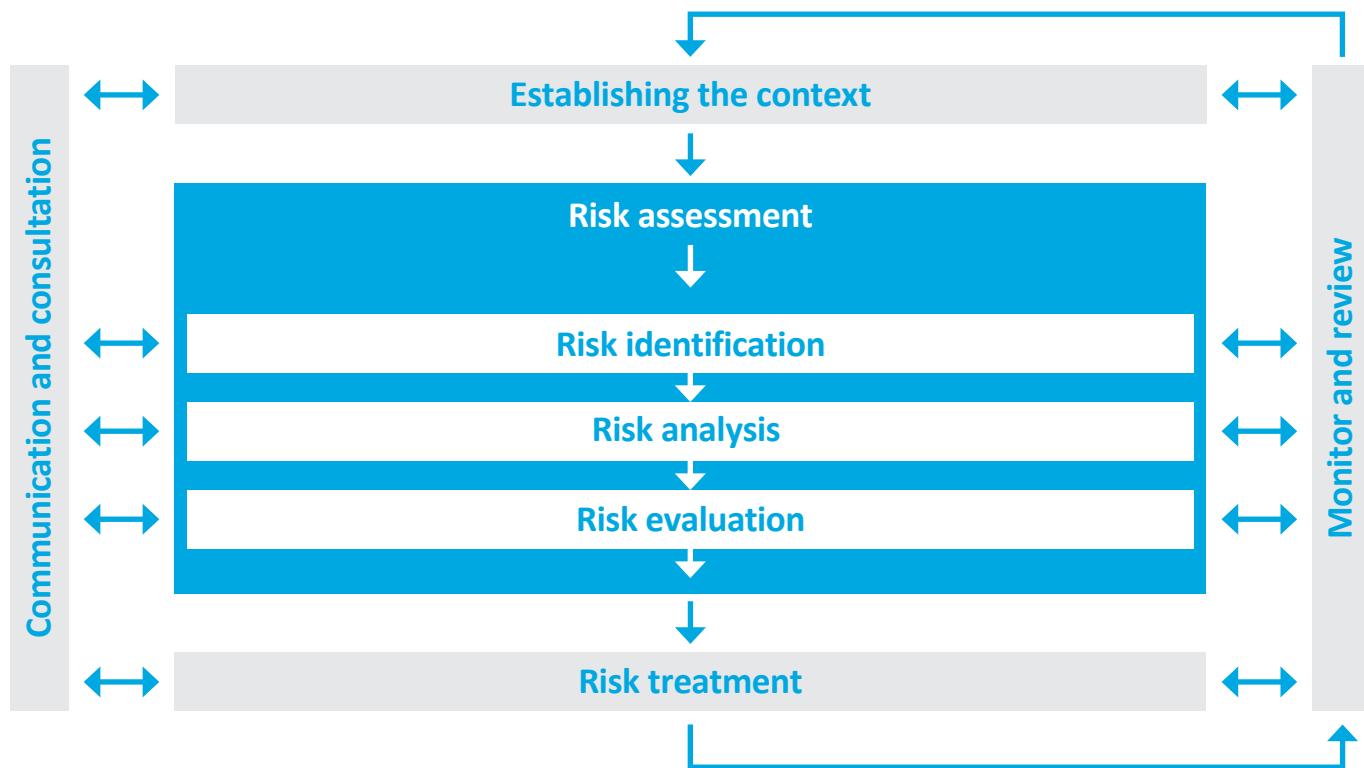
## Risk & CSR Committee Chairman



The Board recognises that QinetiQ operates in varied business environments and that risk management must reflect both the need to take risk and to avoid harm. Board level oversight is discharged through two committees, the Audit Committee, which focuses on risks where the primary impact is financial, and the Risk & CSR Committee, which focuses on risks where the primary impact is non-financial; both committees retain visibility of both the financial and non-financial risks.

The Board agrees and reviews its tolerance of risk through establishing a clear risk appetite and setting appropriate delegations of authority to the executive and senior leaders. The Board's risk appetite is set to provide boundaries and guidance to support executives and senior leaders in their decision-making and allow operational flexibility. Local decision-making is supported within defined delegation of authority and the Board requires all employees to abide by relevant legal requirements as a minimum.

## Managing risk



## Our areas of risk



Risk appetite within QinetiQ focuses on those critical risk areas necessary to achieve our strategic goals. Three categories of appetite are defined as follows:

- **Hungry:** Willing to consider all delivery options and eager to be innovative and to choose options offering potentially higher business rewards, with a mature understanding of inherent risk
- **Balanced:** Preference for delivery options that have a low or moderate degree of residual risk and where successful delivery also provides an acceptable level of reward and value for money
- **Cautious:** Avoidance of risk and uncertainty is the key objective, a greater level of control and mitigation may be required. Significantly greater returns expected for commercial opportunities to offset risk

Within the context of the core, 'Explore' and 'Test for Value' strategy, the Board's commercial appetite is:

- **Hungry** for opportunities relating to increased market share where we have proven delivery, existing and potential new customers
- **Balanced** for opportunities that translate proven delivery into new markets or new capability/delivery into existing customers or that commit QinetiQ to unlimited or excessive liabilities
- **Cautious** for opportunities that involve new capability or delivery into new markets and any opportunity into a new country outside the US and UK

The Board agrees and reviews its tolerance of risk through appropriate delegations of authority to the executive and senior leaders.

The management of risk is key to ensuring QinetiQ is successful in delivering its objectives, whilst protecting the interests of its stakeholders. QinetiQ's risk management methods and processes provide a framework which allows:

- **Risk identification:** identification of risks and opportunities relevant to the Group's objectives
- **Risk analysis:** assessment of risks in terms of likelihood and impact
- **Risk evaluation:** determine and prioritise which risks need treatment
- **Risk treatment:** appropriate management strategies put in place
- **Monitor and review:** monitoring and oversight of risk management

The Group Risk Register consists of material risks relating to effective delivery of our strategy. These risks may emerge as standalone risks or be present through the aggregation or interlinking of risks. Our reputation is a highly valuable asset and reputational impact is considered as a factor in assessing overall risk impact. The Group Risk Register is reviewed by the executive and the Board. In addition, the risk owners present an update of current status and mitigating actions by rotation throughout the year.

# Understanding and managing our risks

Key risk	Associated strategic priority	Description and impact	Likelihood/Impact
<b>Defence and security spending</b>	<b>Customers</b>	<ul style="list-style-type: none"> <li>The Group's revenue is predominantly derived from government customers in the defence and security sector. 70% of the Group's revenue comes directly from contracts with the UK Government and 7% comes directly from contracts with the US Government.</li> <li>Any reduction in government defence and security spending in either the UK or the US could have an adverse impact on the Group's financial performance.</li> <li>The financial burden on both UK and US Government budgets from the current economic downturn may lead to reduced spending in the markets in which the Group operates.</li> <li>This could be exacerbated by the Comprehensive Spending Review (CSR) as well as the next Strategic Defence and Security Review (SDSR) expected to follow the 2015 General Election. The SDSR is expected to take place in the next 12 months. The total amount, and subdivision of, UK defence spending post SDSR may be different to the current budget. The Group's main contracts are exposed to spend on Test &amp; Evaluation and Research &amp; Technology, both of which are expected to be studied in the SDSR.</li> <li>The Group's US products business (approximately £60m annual revenue) has been largely funded through overseas contingency budgets which are expected to decline as the US withdraws from Afghanistan.</li> </ul>	Medium/High
<b>Complex market characteristics and contract profile</b>	<b>Customers</b>	<ul style="list-style-type: none"> <li>The aerospace, defence and security markets are highly competitive. The Group's performance may be adversely affected should it not be able to compete in the markets in which it aims to operate.</li> <li>Following the Currie Review, the Defence Reform Act and the Single Source Regulations are now in place. The Single Source Regulations Office (SSRO) is established with a Chairman and Board appointed. The 'Yellow Book', a legally binding framework, has been replaced by the 'Orange Book' for how single sourced work must be contracted to ensure that a fair and reasonable price is paid for goods and services procured in the absence of competition.</li> <li>This could have an adverse impact on the Group's financial performance. The 'Baseline Profit Rate' for single sourced work has been set at 10.6% for 2016 (2015: 10.7%) This percentage is reviewed annually. The new regulations apply to new single source contracts over £5m in value from April 2015. Approximately 33% of EMEA Services revenue is derived from single sourced work, excluding the non-tasking element of the LTPA contract.</li> <li>The ongoing 'transformation' of the UK MOD's Defence Equipment and Support (DE&amp;S) organisation has now adopted a model of 'bespoke trading entity' rather than Government-Owned Contractor-Operated, which was the intended model. DE&amp;S has hired 'Managed Service Providers' (MSPs), companies to help drive the transformation programme to improve programme delivery and implement new systems and processes as it looks to reduce costs.</li> <li>Some of the Group's revenue is derived from contracts that have a fixed price. There is a risk that the costs required for the delivery of a contract could be higher than those agreed in the contract as a result of the performance of new or developed products, operational over-runs or external factors. Any significant increase in costs which cannot be passed on to a customer may reduce the profitability of a contract or even result in a contract becoming loss making.</li> <li>Many of the Group's contracts have terms, not unusual in defence, that provide for unlimited liabilities for the Group, or termination rights for the customer, often without cause.</li> <li>The timing of orders receipts could have a material impact on the Group's performance in a given reporting period as the amounts payable under some government contracts can be significant.</li> </ul>	Medium/High

Mitigation	Associated KPIs	Responsibility	Risk appetite
<ul style="list-style-type: none"> <li>The Group services the UK defence domains of Air, Land, Maritime and Joint Forces as well as adjacent sectors. This provides a degree of portfolio diversification. The Group will continue to monitor expenditure changes in its traditional markets and will adjust business activities where appropriate.</li> <li>The MOD has made considerable progress in balancing its equipment budget. In defence research, where QinetiQ is the private sector market leader, spending was stabilising at about £400m p.a. due to the 1.2% floor on R&amp;T spend (pre SDSR).</li> <li>QinetiQ monitors and responds to potential opportunities arising from the MOD's actions to deliver improved value for money by making proactive proposals that deliver the desired outcome.</li> <li>QinetiQ expects that the SDSR process will enable consultation between Government and industry to ensure UK defence priorities are properly considered.</li> <li>Further investment in the pursuit of international opportunities assists in the diversification away from the dependency on UK and US Government spending.</li> <li>US products (such as unmanned systems) are targeted to be funded through Programs of Record (i.e. in the US Base budget) in approx 2017.</li> </ul>	• Customer satisfaction	<ul style="list-style-type: none"> <li>Business Development Director</li> <li>Strategic Business Director – Defence</li> </ul>	Hungry
<ul style="list-style-type: none"> <li>QinetiQ seeks to focus on areas within these markets in which its deep customer understanding, domain knowledge, technical expertise and platform independence provide a strong proposition and a significant advantage in competitive bidding.</li> <li>QinetiQ and defence industry partners have been fully engaged with the MOD in the development of the new 'Orange Book' framework and its practical application. QinetiQ and defence industry partners have been consulted by the SSRO on the draft Statutory Guidance, due to be published early in 2015.</li> <li>The contracts and orders pipeline is regularly reviewed by senior operational management.</li> <li>The nature of many of the services provided under fixed-price arrangements is often for a defined amount of effort or resource rather than firm deliverables and, as a result, mitigates the risk of costs escalating. The Group ensures that its fixed-price bids and projects are reviewed for early detection and management of issues which may result in cost over-run or excessive delivery risk.</li> </ul>	• Customer satisfaction	<ul style="list-style-type: none"> <li>Business Development Director</li> <li>Strategic Business Director – Defence</li> </ul>	Balanced

Key risk	Associated strategic priority	Description and impact	Likelihood/Impact
<b>Complex market characteristics and contract profile</b> (continued)	Customers	<ul style="list-style-type: none"> <li>Organisational Conflicts of Interest (OCI) may occur where the Group provides services to both a defence end-user customer as well as those within the defence supply chain.</li> </ul>	Medium/High
	Customers	<ul style="list-style-type: none"> <li>The Group is reliant on a limited number of major customers. A material element of the Group's revenue is derived from one contract. The Long Term Partnering Agreement (LTPA) is a 25-year contract to provide test, evaluation, and training services to the MOD. The original contract was signed in 2003. The LTPA operates under five-year periods with specific programmes, targets and performance measures set for each period.</li> <li>In 2015 the LTPA directly contributed 26% of the Group's revenue and supported a further 17% through tasking services using LTPA managed facilities.</li> </ul>	Medium/High
<b>Recruitment and retention</b>	Employees	<ul style="list-style-type: none"> <li>The Group operates in many specialised engineering, technical and scientific domains.</li> <li>The lack of graduates in the science, technology, engineering and mathematics (STEM) domains leads to future skills shortage.</li> <li>Key capabilities and competencies may be lost through failure to recruit and retain employees due to internal factors, as well as macro factors across the sector affecting the desirability, intake and training of engineers, scientists and technicians.</li> </ul>	Low/High
<b>Breaches of security and IT systems failure</b>	The way we work	<ul style="list-style-type: none"> <li>The Group operates in a highly regulated IT environment.</li> <li>The data held by QinetiQ is confidential and needs to be secure, against a background of increasing cyber threat.</li> <li>A breach of data security or IT systems failure could have an adverse impact on our customers' operations, resulting in significant reputational damage, as well as the possibility of exclusion from some types of government contracts.</li> <li>The Group's financial systems are required to be adequate to support US and UK Government contracting regulations.</li> </ul>	High/High
<b>Trading in a global market</b>	Growth Orientation	<ul style="list-style-type: none"> <li>QinetiQ operates internationally. Risks include: regulation and administration changes, taxation policy, political instability, civil unrest, and differences in culture.</li> <li>Negative events could disrupt some of the Group's operations and have a material impact on its future financial performance.</li> </ul>	Low/Medium

Mitigation	Associated KPIs	Responsibility	Risk appetite
<ul style="list-style-type: none"> <li>QinetiQ takes proactive steps to manage any potential OCI and maintain its ability to provide independent advice. QinetiQ operates under the MOD's generic formal compliance regime and applies a rigorous compliance process.</li> <li>Where QinetiQ wishes to operate on both the advice and supply chain side of an opportunity we do so only after receiving approval from the MOD.</li> </ul>	<ul style="list-style-type: none"> <li>Customer satisfaction</li> </ul>	<ul style="list-style-type: none"> <li>Strategic Business Director – Defence</li> </ul>	Balanced
<ul style="list-style-type: none"> <li>In February 2013 the Group signed the LTPA for a third five-year period with the MOD. The next scheduled 're-pricing' break point is in 2018.</li> <li>The Group continues to achieve strong customer performance and satisfaction levels, and significantly exceeded the agreed minimum performance rating of 80% in 2014.</li> <li>The Group has achieved significant cost savings for the MOD on delivered services, and is on track to exceed the £700m of savings originally projected to be delivered over the life of the contract.</li> <li>The Group expects to engage with the MOD regarding the study of future plans for test and evaluation services within the SDSR.</li> </ul>	<ul style="list-style-type: none"> <li>Customer satisfaction</li> </ul>	<ul style="list-style-type: none"> <li>LTPA Director</li> </ul>	Hungry
<ul style="list-style-type: none"> <li>The Group conducts regular activities to identify key roles and personnel. Succession plans are in place looking internally at candidates ready now or in need of development to fill particular roles and externally to identify people QinetiQ may wish to attract.</li> <li>QinetiQ has made improvements in employee engagement and conducts an annual satisfaction survey.</li> <li>STEM outreach from primary school age through to work experience and graduate opportunities.</li> <li>QinetiQ is leading industry in The 5% Club, a campaign to increase the recruitment of graduates and apprentices.</li> </ul>	<ul style="list-style-type: none"> <li>Health and Safety</li> <li>Voluntary employee turnover</li> <li>Employee satisfaction</li> <li>% of graduates and apprentices</li> </ul>	<ul style="list-style-type: none"> <li>Business Unit Managing Directors</li> </ul>	Balanced
<ul style="list-style-type: none"> <li>Data security is assured through a multi-layered approach that provides a hardened environment, including robust physical security arrangements and data resilience strategies.</li> <li>Comprehensive internal and external testing of potential vulnerabilities is conducted along with 24/7 monitoring.</li> <li>The Group engages with US and UK Government contracting audit agencies, to enable them to test relevant financial systems and data, and implements any recommended improvement plans.</li> <li>Information systems are designed with consideration to single points of failure and the removal of risk of minor and major system failures.</li> <li>The Group maintains business continuity plans that cover geographical assets as well as the technical capability of employees. These plans cover a range of scenarios (including loss of access to IT) and are regularly tested.</li> </ul>	<ul style="list-style-type: none"> <li>Underlying operating profit</li> <li>Profit after tax</li> <li>Underlying EPS</li> <li>Underlying operating cash flow</li> </ul>	<ul style="list-style-type: none"> <li>Business Unit Managing Directors</li> <li>Functional Directors</li> </ul>	Cautious
<ul style="list-style-type: none"> <li>While the Group has a growing geographical footprint, its traditional activities are confined to the UK and the US.</li> <li>Relationships or contracts in new markets are assessed for their inherent risks, using our International Business Risk Assessment process, before being formally agreed. This allows opportunities to be reviewed at different levels of management according to their inherent risk.</li> </ul>	<ul style="list-style-type: none"> <li>Orders</li> <li>Organic revenue growth</li> </ul>	<ul style="list-style-type: none"> <li>Business Unit Managing Directors</li> <li>International Business Development Director</li> </ul>	Cautious

Key risk	Associated strategic priority	Description and impact	Likelihood/Impact	
<b>Significant breach of relevant laws and regulations</b>	The way we work	<ul style="list-style-type: none"> <li>The Group operates in highly regulated environments and recognises that its operations have the potential to have an impact on a variety of stakeholders.</li> <li>Failure to comply with particular regulations could result in a combination of fines, penalties, civil or criminal action.</li> <li>In addition, failure may also lead to suspension or debarment from government contracts, as well as reputational damage to the QinetiQ brand.</li> <li>Key areas of focus for the Group include the following: <ul style="list-style-type: none"> <li>Safety liability of products, services and advice.</li> <li>Workplace and occupational health, safety and environmental matters.</li> <li>Bribery and ethics.</li> <li>International trade controls.</li> </ul> </li> </ul>	Low/High	
<b>Defined benefit pension obligations</b>	The way we work	<ul style="list-style-type: none"> <li>The Group operates a defined benefit (DB) pension scheme which is closed to future accrual.</li> <li>At the year end the DB pension scheme was a liability of £39.4m under an IAS 19 basis.</li> <li>The size of the deficit may be materially affected by a number of factors, including inflation, investment returns, changes in interest rates and improvements in life expectancy of members.</li> <li>Any change to the deficit may require the Group to increase the cash contributions to the scheme, which would reduce the Group's cash available for other purposes.</li> </ul>	Medium/High	
<b>Tax legislation</b>	The way we work	<ul style="list-style-type: none"> <li>QinetiQ is liable to pay tax in the countries in which it operates, principally the UK and the US.</li> <li>Changes in tax legislation in these countries could have an adverse impact on the level of tax paid on profits generated by the Group.</li> <li>In the UK, R&amp;D Expenditure Credits (RDEC) were introduced from 1 April 2013 and will be mandatory from 1 April 2016, replacing the R&amp;D super deduction. Until that date, QinetiQ expects to claim the super deduction while the treatment of RDEC for MOD single source contracts remains under discussion between industry and the Government.</li> </ul>	High/High	

Mitigation	Associated KPIs	Responsibility	Risk appetite
<ul style="list-style-type: none"> <li>The Group has robust policy, procedures and training in place to ensure that it meets all current regulations; for example role-specific safety training and business ethics training which is mandatory for Board members and all employees across the Group.</li> <li>The QinetiQ Code of Conduct defines clear expectation for the Group and its employees; for example it states that the Group does not tolerate bribery and corruption and will comply with relevant international trade regulations.</li> <li>The Group manages the effective identification, measurement and control of regulatory risk.</li> <li>Local management continuously monitor local laws. Professional advice is sought when engaging in new territories to ensure that the Group complies with local and international regulations.</li> <li>Accreditation to external standards; for example safety and environmental systems continue to be accredited to international standards; external authorisation for regulated design and maintenance services in the aviation sector.</li> </ul>	<ul style="list-style-type: none"> <li>Underlying operating profit</li> <li>Profit after tax</li> <li>Underlying EPS</li> <li>Underlying operating cash flow</li> <li>Health and Safety</li> </ul>	<ul style="list-style-type: none"> <li>Business Unit Managing Directors</li> <li>Functional Directors</li> </ul>	Cautious
<ul style="list-style-type: none"> <li>Scheme performance is reviewed regularly by Group management in conjunction with the scheme's independent Trustee.</li> <li>External actuarial and investment advice is regularly taken to ensure the best interests of both the Group and the scheme members.</li> <li>The Group works in collaboration with the Trustees to agree an investment strategy that progressively de-risks the scheme as the funding level improves.</li> <li>The Company continues to pay the deficit recovery payments outstanding from the 2011 valuation. Company contributions to the scheme are expected to continue at £13m per annum until 2018.</li> <li>The scheme was closed to future accrual on 31 October 2013.</li> <li>At the year end 45% of the inflation risk is hedged and 20% of interest rate risk hedged, measured on a gilts basis. A 5% inflation cap protects £264m of pensioner liabilities for ten years to 2025.</li> </ul>	<ul style="list-style-type: none"> <li>Profit after tax</li> <li>Underlying EPS</li> <li>Underlying operating cash flow</li> </ul>	<ul style="list-style-type: none"> <li>Group Treasurer</li> </ul>	Balanced
<ul style="list-style-type: none"> <li>External advice and consultation are sought on potential changes in tax legislation in the UK, the US and elsewhere as necessary enabling the Group to plan for and manage potential changes.</li> <li>The Group is currently actively engaging with industry, MOD and industry bodies regarding the treatment of RDEC.</li> <li>The Group has £291.6m of UK tax losses carried forward as at 31 March 2015 (2014: £213.9m).</li> </ul>	<ul style="list-style-type: none"> <li>Profit after tax</li> <li>Underlying EPS</li> </ul>	<ul style="list-style-type: none"> <li>Group Tax Manager</li> </ul>	Balanced

# EMEA Services

EMEA Services combines world-leading expertise with unique facilities to provide technical assurance, test and evaluation and training services, underpinned by long-term contracts. The most significant of these contracts is the Long Term Partnering Agreement (LTPA) for test, evaluation and training services which has delivered an improved service and significant savings for the MOD over the last 12 years. Capital expenditure is likely to increase in the future as we continue to invest in the LTPA contract. EMEA Services is also a market leader in research and advice in specialist areas such as C4ISR, procurement advisory services and cyber security.

## Financial performance

EMEA Services delivered a strong performance in 2015. Each of the core Air, Weapons and Maritime businesses performed well despite the uncertainty in the UK defence market resulting from the MOD transformation programme and forthcoming Strategic Defence and Security Review.

Orders, excluding the £998m third term of the LTPA contract, grew 3% to £461.6m (2014: £447.8m) demonstrating the unique strengths of the division and its highly differentiated position in its markets.

Revenue grew 3% on an organic basis at constant currency, building on the 3% increase last year. At the beginning of the new financial year, 80% of the division's FY16 revenue was already under contract, a similar level to a year ago.

Underlying operating profit\* increased 7% to £93.0m (2014: £86.7m) assisted by an insurance recovery and the completion of a final milestone on an international project.

 **P93** Financial statements

## Markets and outlook

- The Front Line Commands (Navy, Army, Air and Joint Forces) are exercising their newly delegated powers to shape future capabilities. QinetiQ's business units are aligned closely to these Commands and so are well placed to help them with their growing procurement responsibilities.
- During the year our Cyber, C4ISR and Training businesses were aligned to meet the requirements of the recently created Joint Forces Command, such as the need for information superiority, as well as demand from other government and commercial customers.

Defence transformation, the forthcoming comprehensive spending review and SDSR are expected to have an impact on the UK defence market this year. This will provide future opportunities for EMEA Services to build on its strong record of delivering 'more for less', whilst recognising that in FY16 there will be uncertainty and the potential for interruptions to order flow. The portion of revenue under contract at the start of FY16 was similar to a year ago and the balance is supported by a pipeline of opportunities but order flow and contract cover will be watched closely over the coming months. Overall, given the opening backlog position, expectations for the performance of EMEA Services in the current financial year are unchanged.

 **P6** Market overview

	2015 £m	2014 £m
Orders <sup>(1)</sup>	<b>461.6</b>	447.8
Revenue	<b>625.6</b>	607.0
Underlying operating profit*	<b>93.0</b>	86.7
Underlying operating margin*	<b>14.9%</b>	14.3%
Book to bill ratio <sup>(1)</sup>	<b>1.1x</b>	1.1x
Funded backlog <sup>(1)</sup>	<b>678.6</b>	661.0

(1) Excludes the £998m third term of the LTPA contract. B2B ratio is orders won divided by revenue recognised, excluding the LTPA contract.

\* Definitions of underlying measures of performance can be found in the glossary on page 141.

## Our value pipeline

Our Organic-Plus strategy prioritises active portfolio management. All of our business operations are graded within a value pipeline which gives us full visibility and direction over our assets and capabilities.

Core	←	Explore	←	Test for value
Air		Training		International procurement advice
Weapons		Cyber Security		Smart metering assurance
Maritime		Cyveillance®		Directed Energy
C4ISR		Procurement Advisory Services		Weapons
Australia		International ranges		Secured navigation systems
		UAS Services		

 **P12** Our Organic-Plus strategy

# Year in review

## Core

QinetiQ's **Air** business de-risks complex aviation programmes. It works with supply chain partners and signed new long-term agreements with key suppliers to deliver additional flexibility for customers. During the year it secured a £16m extension to its largest MOD test and evaluation contract, and a four-year £5m contract for research into aircrew performance. The business also continued to grow its engineering services offering and now provides maintenance, repair and overhaul services for fixed and rotary wing aircraft across three main contracts, with opportunities to take this capability into new international markets.

QinetiQ's **Weapons** business supplies independent research, evaluation and training services for integrated weapons systems. The business delivers the MOD's conventional weapons research programme through the Weapons Science and Technology Centre, which secured £17m of orders during the year. In response to the growing complexity of weapons systems trials work, major infrastructure improvements took place at a number of the ranges that the business runs under the LTPA contract including new communications infrastructure in the Hebrides and a new range control centre at Aberporth in Wales. QinetiQ's expertise continues to attract international customers with work undertaken for the South Korean government as well as European customers. The Weapons business has a long track record of delivering complex managed services in high risk environments and is pursuing a number of outsourcing opportunities.

The **Maritime** business delivers operational advantage to naval clients worldwide through the provision of independent technical advice and support, particularly in the areas of platform performance, stealth, command information systems and systems integration. The business won a £5m contract from a competitor to deliver the MOD's mobile underwater targets service at the BUTEC range it operates off North West Scotland, which also benefited from over £20m of investment to modernise its acoustic measurement system, enhancing QinetiQ's ability to deliver stealth-related services. During the year the business supported the integration of a new radar on Type 23 frigates and a new Command System for the helicopter carrier HMS Ocean. This expertise underpins a new mission systems integration service to meet demand from international customers, particularly in the Asia Pacific region. The business was also awarded a contract to deliver technical support for ship procurement for the Canadian government. QinetiQ's Portsdown site was selected to host the Defence Growth Partnership's Centre for Maritime Intelligent Systems which will help UK industry meet customer interest in emerging technologies such as autonomous systems.

QinetiQ **Australia** provides impartial advice and services predominantly to government customers. The business is underpinned by two long-term contracts with the Commonwealth Government of Australia's Department of Defence – the Defence Science and Technology Organisation (DSTO) contract which is focused on provision of engineering services workshops and the Aircraft Structural Integrity contract which supports the airworthiness of military aircraft. QinetiQ Australia delivered a steady performance against a background of fiscal pressures and defence reform, securing a two-year extension to the services it delivers at DSTO Fishermans bend in Melbourne. Greg Barsby, a former KBR executive, took up the role of Managing Director in December 2014. His remit is to target long-term contracts through improved commercial and business development capabilities as well as to reinforce partnerships with government and industry.

QinetiQ's **C4ISR** business provides research, advice and bespoke solutions for secure communications, command and control, surveillance sensors and information management. It is the MOD's leading supplier of C4ISR research, which underpins the advice capability of the business as well as future opportunities to support customers' transformation and innovation needs. In the UK, recent funding rounds and announcements have protected or enhanced budgets for C4ISR. The UK's Joint Forces Command provides a focus for multi-billion pound procurements of 'enabling' capabilities that have not existed before and C4ISR is now aligned with the Cyber and Training businesses to meet these requirements. In addition, ongoing instability in the Middle East is increasing opportunities from governments in the region.

## Explore

In the 'Explore' category, QinetiQ's **Training** business uses Commercial-Off-The-Shelf (COTS) technology to connect people and assets for mission rehearsal and tactic development. The business secured its largest ever contract for the continued provision in the UK of Distributed Synthetic Air Land Training valued at £33m over five years. It also beat a number of competitors to win the next stage of a core research programme worth £3m over four years. As a result, the business is well positioned for future opportunities as the MOD moves towards its vision of a network of simulators across the UK to augment live training. Having established an office in Orlando, Florida, the heart of the US training and simulation market, the business has secured a position on three IDIQ contracts working in partnership with established prime contractors such as Alion and developing a promising pipeline of opportunities in the US.

**Cyber Security** is an 'Explore' business with opportunities in critical national infrastructure, as well as defence and security. It won a new £3m contract to deliver secure monitoring and hosting services for a major financial institution. In recognition that compliant systems alone do not necessarily reduce business risk, the business is integrating QinetiQ's human science expertise into its consultancy offering and is investing in its cyber intelligence capabilities. Closer alignment with the Training business will ensure that QinetiQ is better able to meet the demand for cyber training. QinetiQ's cyber intelligence business, Cyveillance®, launched a cloud-based cyber threat centre that monitors the internet, provides alerts and delivers data on domain names, IP addresses, phishing and malware attacks. This provides direct access for customers to its monitoring and investigative tools and complements its existing consultancy-based services. QinetiQ's suite of cyber security offerings is completed by its wholly-owned subsidiary Boldon James, which provides data classification and secure messaging solutions and is reported as part of the Global Products division.

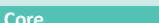
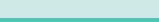
**Procurement Advisory Services** was established as a stand-alone 'Explore' business in 2014. It provides tender assessment, cost and analytical services principally to support complex procurement programmes in highly regulated markets. During the year, the business provided horizon scanning for the UK Cabinet Office, cost forecasting services to the MOD, and won a £2m MOD contract for business case support to help address frontline challenges such as the supply of water, fuel and power. Procurement Advisory Services is spear-heading QinetiQ's presence in Canada, where an office was opened during the year.

Within the Air business, QinetiQ delivers turnkey services for customers using **Unmanned Aerial Systems (UAS)** to meet growing demand particularly from international organisations such as the United Nations. The business has developed commercial relationships with the three largest manufacturers of unmanned aircraft outside the US and in September opened the UK's first airfield capable of operating large UAS at Llanbedr in Wales. During the year, it was awarded a competitively-won contract to provide manpower for a short duration service for an international institution.

## Test for value

EMEA Services is 'testing for value' a number of early stage offerings. These include the provision of technical services in support of Directed Energy Weapons (DEW) and the delivery of secured navigation systems such as the secure signal processing already being provided for the Galileo constellation of satellites – the European Union version of GPS.

## Understanding our business

	What we do	Approximate annual revenue	Approximate total employees	Key sites (UK unless stated)	Key contracts
 <b>Air</b>	De-risk complex aviation programmes by testing military aircraft and equipment, evaluating the risks and assuring safety.	c.£190m	c.1,600	• Boscombe Down • Farnborough	• Long Term Partnering Agreement (LTPA)
 <b>Core</b>					
 <b>Weapons</b>	Supplies independent research, evaluation and training services for integrated weapons systems.	c.£200m	c.1,200	• Shoeburyness • Fort Halstead • Farnborough • Hebrides • Aberporth • Pendine • West Freugh	• LTPA • Combined Aerial Targets Service (CATS) • Weapons, Science and Technology Centre
 <b>Core</b>					
 <b>Maritime</b>	Delivering operational advantage to naval clients worldwide through the provision of independent technical advice and support.	c.£75m	c.700	• Portsdown Technology Park (PTP) • Haslar	• LTPA • Maritime Strategic Capabilities Agreement (MSCA) • Naval Combat System Integration Support Services (NCSISS)
 <b>Core</b>					
 <b>Australia</b>	Delivers impartial advice and services predominantly to government customers.	under £25m	c.200	• Melbourne, Australia • Canberra, Australia • New South Wales, Australia	• DSTO – munitions • ASI – airworthiness
 <b>Core</b>					
 <b>C4ISR</b>	A leading supplier of research and advice on sensors, communications and intelligence.		c.450	• Malvern • Farnborough	• DSTL research
 <b>Core</b>					
 <b>Training</b>	Uses technology to reduce the cost of training, drawing on training capability from across QinetiQ.		c.100	• Farnborough • Malvern	• Distributed Synthetic Air Land Training 2
 <b>Explore</b>					
 <b>Cyber Security</b>	Protects critical national infrastructure through the provision of consultancy, managed security services, secure information exchange, and threat and risk assessments.		c.100	• Malvern • Farnborough	
 <b>Explore</b>					
 <b>Procurement Advisory Services</b>	Provides decision support, cost, analytical and tender assessment services.	under £25m	c.150	• Bristol, • Farnborough • Boscombe Down • Malvern	• Operational Support Programme Customer Friend
 <b>Explore</b>					
 <b>Cyveillance®</b>	Provides open source threat intelligence and remediation to customers across the world including many of the Fortune 500.	under £25m	c.100	• Reston, Virginia US	
 <b>Explore</b>					



# More flexible and realistic training drives mission success

## Employees

### World-leading simulation and synthetic training from domain experts

Fraser Bruce, DSALT Programme Technical Manager – “With UK Armed Forces no longer in Afghanistan, requirements shifted from specific predeployment training to training for ‘contingent operations’. We adapted and configured systems and services, listening to the customer and using virtualisation technologies to address obsolescence and deliver savings.” Dawn Harrison, QinetiQ Training, sums it up – “This is testament to our ability to seamlessly pull together subject matter experts and sub-contractors: the customer comes to QinetiQ because they trust our team. We deliver.”



## Customers

### Meeting and exceeding customer needs

Under a five-year contract that runs from 2014, QinetiQ is delivering the Distributed Synthetic Air Land Training 2 capability for UK MOD, building on successful delivery of a previous five-year contract. Operating from the Air Battlespace Training Centre in Lincoln, the £33m DSALT2 training programme provides the UK Army and Royal Air Force with extremely realistic and flexible representations of operating environments. Our bid was supported by a pan-QinetiQ team and includes sub-contractors Boeing and Plexsys.

Russ Cole, Flight Simulation and Synthetic Trainers Team Leader at MOD’s Defence Equipment and Support – “Simulation and synthetic training is an extremely important part of training...the ability to practise and train in highly realistic but safe environments is a vital, life-saving capability essential to effective mission preparation.”

## Growth Orientation

### A flexible resource for tomorrow’s needs

Adaptability is fundamental to DSALT: reconfiguration means training can evolve to meet changing operational needs. The move into ‘contingent operations’ required an even more proactive approach, working with the customer to deploy training to best effect while future proofing the capability for later programmes. This capability is also fully transferable to address a range of commercial requirements.

# Global Products

Global Products combines cutting-edge technologies with an intimate understanding of customer problems and strong productisation skills to deliver innovative solutions to meet customer requirements. The division also undertakes contract-funded research and development, developing intellectual property in partnership with key customers, with potential for new revenue streams. To reduce the volatility of its revenue profile over time, QinetiQ is seeking to increase its portfolio of products and to find new markets and applications for its existing offerings.

## Financial performance

The performance of Global Products continued to be impacted by the ongoing reduction of US military forces deployed to Afghanistan and reduced funding for US military operations which depressed demand for conflict-related products.

Revenue was £138.2m (2014: £175.6m) primarily due to reduced sales of conflict-related products.

Orders grew by 2% to £152.0m (2014: £149.1m) as demand for EMEA products offset the slow order intake in the US products business. The Global Products division had more than half of its FY16 revenue already under contract at the beginning of the new financial year, slightly better than at the same time last year.

Underlying operating profit\* was £18.3m (2014: £27.0m), impacted by the reduction in revenue and by approximately \$5m of additional one-off costs associated with separating from US Services infrastructure.

## Markets and outlook

- In January 2015, Jeff Yorsz took up his appointment as President of QinetiQ's US products business, joining from Northrop Grumman. Jeff is leading the realignment of the business in response to structural changes in its core markets. This will result in a greater focus on contract-funded research and development and US DoD Programs of Record, as well as on commercial and international markets.

In Global Products, newer products are recording notable milestones and the amount of revenue under contract at the start of FY16 is up slightly on a year ago, but the drawdown of American overseas military forces is continuing to depress demand for conflict-related products. As the division has a lumpy revenue profile which is dependent on the timing and shipment of key orders, there is a range of possible outcomes for the performance of Global Products in the current year.

 **P6** Market overview

## Understanding our business

	What we do	Approximate annual revenues	Approximate total employees	Key sites (UK unless stated)
	<b>US products</b> <b>Core</b> Contract-funded research and development and innovative products that protect people and assets, such as military robots.	£60m	c.250	• Waltham, Massachusetts, US
	<b>OptaSense®</b> <b>Explore</b> A bespoke fibre sensing business that delivers Decision Ready Data to multiple vertical markets.	under £25m	c.150	• Farnborough, Winstone and Portishead, UK • Houston, US • Calgary, Canada • Dubai, UAE
	<b>Space Products</b> <b>Explore</b> Provides satellites, payload instruments, sub-systems and ground station services.	under £25m	c.150	• Antwerp, Belgium • Farnborough
	<b>EMEA products</b> <b>Test for value</b> Provides research services and bespoke solutions developed from IP spun out from the core.	£40m	N/A	• N/A

Despite the continued prevalence of Lowest-Price-Technically-Acceptable acquisitions in the US, careful cost control and a reduction of headcount provided some protection to profitability, with the division delivering an underlying operating profit margin\* of 13.2% (2014: 15.4%).

	2015 £m	2014 £m
Orders	152.0	149.1
Revenue	138.2	175.6
Underlying operating profit*	18.3	27.0
Underlying operating margin*	13.2%	15.4%
Book to bill ratio	1.1x	0.8x
Funded backlog	116.7	97.1

\* Definitions of underlying measures of performance can be found in the glossary on page 141.

 **P93** Financial statements

## Our value pipeline

Our Organic-Plus strategy prioritises active portfolio management. All of our business operations are graded within a value pipeline which gives us full visibility and direction over our assets and capabilities.

Core	←	Explore	←	Test for value
TALON® robots		OptaSense®		ASX™
Survivability products		Space Products		SPO™
Contract-funded R&D		Robotic appliqué kits – DriveRobotics™		MEWS™
		Commerce Decisions – AWARD®		Linewatch™
				High density generator

 **P12** Our Organic-Plus strategy

# Year in review

## Core

US Global Products continues to meet the US Department for Defence (DoD) requirements for maintenance, repair and overhaul for military robots, demonstrating the customer's commitment to keeping **unmanned systems** as a principal part of Explosive Ordnance Disposal missions. The business won \$24m of orders to reset TALON® robots, modernising them for future operations. These 'reset' awards position the business well for future US DoD Programs of Record, although to date these have been slow to emerge. The fifth generation of TALON® was launched during the year, incorporating the ability to use third-party commercial components to capitalise on the continued convergence of military and civil robotic technologies. In addition, \$14m of orders for unmanned systems were won from international customers. In response to the growing use of robotics in the construction and demolition industries, the US products business launched DriveRobotics™, an appliqué kit that transforms existing and new Bobcat vehicles into unmanned vehicles. Demand for survivability products continues to be impacted by the drawdown of US military operations, although new orders were received for armour for the C-130 aircraft.

The sale of QinetiQ's US Services division, completed in May 2014, removed organisational conflict of interest (OCI) barriers that prohibited the US Global Products business from pursuing strategically important DoD **research and development** contracts. The business is now building on its base of contract-funded R&D projects both as an alternative revenue stream and as a source of future intellectual property; it saw a modest increase in these activities during the year. For example, it was one of two suppliers to receive a contract from the Defense Advanced Research Projects Agency (DARPA) for the first phase development of the Hydra programme to develop a distributed undersea network of modular unmanned platforms and payloads. This positions the business well for follow-on phases of the programme and other projects with the US Office of Naval Research.

## Explore

**OptaSense®** is a Distributed Acoustic Sensing (DAS) business which is organised around market-facing business development units and a single technical Centre of Excellence now incorporating the laser manufacturer Redfern Integrated Optics (RIO) acquired this year. The business made progress implementing its strategy of developing partnerships with leading industry players to exploit its key markets. In rail, OptaSense® continues to work with German rail operator Deutsche Bahn and also won a \$5m initial award from the Saudi Rail Organisation to provide security monitoring for over 1,000km of rail line. In oil and gas, the product development agreement with Shell continues to deliver significant technical progress. This year, the fall in the oil price, and consequent capex reductions by Oil Majors, slowed the adoption of DAS for well completion but improved the economics of its use for flow monitoring and seismic profiling. Immediately after year end the business entered into a non-exclusive strategic alliance with Weatherford to deliver solutions to optimise well planning, construction and production. In infrastructure security, the delivery of some key projects was interrupted by a worsening security situation particularly in the Middle East, however the increased threat to

national infrastructure also increased demand. At the end of the year, OptaSense® signed a framework supply agreement to protect critical national infrastructure including pipelines, airports and other facilities for a customer in the Middle East. When complete, the two-year project could involve 200 units and encompass up to 8,000km of assets.

QinetiQ's **Space Products** business provides satellites, payload instruments, sub-systems and ground station services. At the end of the year, it was awarded a contract worth €16m over three years to develop the computer and avionics for the European Space Agency's (ESA's) Proba-3 satellites that will fly in formation and use an eclipsing mechanism to study the Sun. The business is also playing a vital role in ESA's IXV mission launched in February 2015, as its technology will be responsible for guiding the 'space taxi', a smaller version of the US space shuttle, safely back to Earth.

**Subsidiaries** Boldon James and Commerce Decisions are reported in Global Products. Commerce Decisions delivered record revenue and profit in 2015, securing an enterprise-wide contract for the third year from the MOD for its AWARD® procurement software, as well as delivering growth in the UK health and transport markets. The business also secured its first order in Canada shortly after year end.

## Test for value

In the 'Test for Value' category, field evaluations are underway for the Linewatch™ power line sensor system, which precisely measures voltage and currents on power grids. The product is designed to meet emerging Smart Grid requirements for the detection of faults and power theft, condition-based maintenance, and distributed power generation. In addition, the US products business is developing a High Power Density Generator which can provide the modular 'roll-on/roll-off' power required for emerging defence and civil applications.

QinetiQ's UK business has world-leading capabilities in electronic signals intelligence and during the year it launched ASX™, a small sensor that delivers airborne surveillance capability. The MOD selected QinetiQ's Modular Electronic Warfare System (MEWS™) ahead of more established products to form the basis of its Medium Weight Electronic Surveillance Capability for expeditionary operations. Further milestone orders won during the year included a \$3m contract with the US Transportation Security Administration to develop the next generation of QinetiQ's SPO™ stand-off Millimetre Wave threat detection system.

**“Another strong year of operational cash flow and the completion of the US Services disposal has enabled us to clear debt and return £150m to shareholders, whilst retaining a strong balance sheet”**

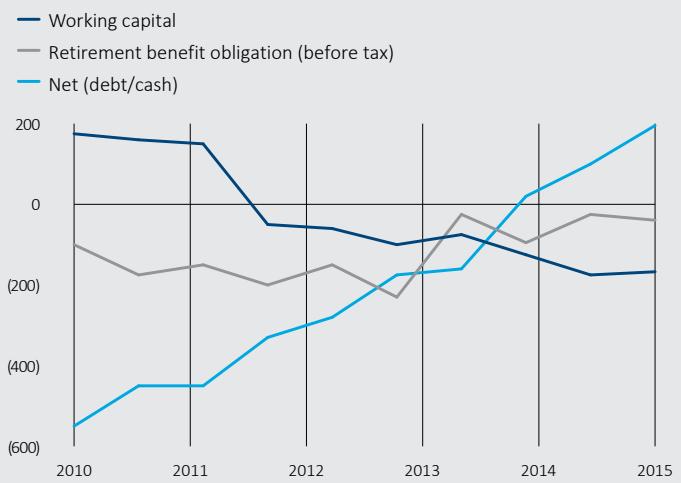
**David Mellors**  
Chief Financial Officer



### Financial highlights

- Strong performance from EMEA Services with 3% growth in both orders and revenue
- Further strengthening of the balance sheet with net cash of £195.5m at 31 March 2015 (2014: £170.5m)
- Re-basing of the dividend, with full year dividend of 5.4p, 17% growth on prior year
- Completed sale of the US Services division for net cash inflow in the year of £78.6m. This was associated with pay-down of private placement debt and a £6m contribution to the pension scheme
- Revolving credit facility refinanced during the year, with a new five-year, multi-currency facility of £166m and \$100m
- Completed £107m of the planned £150m share buyback programme

### Strengthening of the balance sheet (£m)



## Group summary – continuing operations

	2015	2014 <sup>a</sup>
Revenue (£m)	763.8	782.6
Organic change at constant currency (%)	(2%)	(4%)
Underlying operating profit* (£m)	111.3	113.7
Underlying operating margin* (%)	14.6%	14.5%
Total operating profit (£m)	109.5	97.1
Underlying profit before tax* (£m)	107.8	101.2
Total profit before tax (£m)	105.4	84.0
Underlying net finance expense* (£m)	(3.5)	(12.5)
Underlying effective tax rate* (%)	10.9%	11.3%
Underlying earnings per share* (pence)	15.2p	13.8p
Basic earnings per share (pence)	18.6p	10.4p
Dividend per share (pence)	5.4p	4.6p
Underlying net cash from operations (post-capex)* (£m)	114.9	106.2
Underlying operating cash conversion (%)	103%	93%
Net cash (£m)	195.5	170.5

### Headline results

Group revenue was £763.8m (2014: £782.6m), down 2% on an organic basis at constant currency, excluding a £3.7m decrease due to foreign exchange movements (primarily a weakening of the Australian dollar and the Euro). EMEA Services performed well during the year returning 3% growth in both orders and revenue. Revenue was £625.6m (2014: £607.0m). Global Products revenue was £138.2m (2014: £175.6m), a 21% decrease at constant currency. Performance was again impacted by the reduction in demand for US conflict-related products.

### Specific adjusting items

Specific adjusting items, shown in the ‘middle column’, include a profit of £15.9m recognised on the disposal of US Services, a one-off accelerated interest cost of £28.8m associated with the early repayment of the private placement debt and £25.2m in respect of the capitalisation of a proportion of the Group’s unused tax losses. The prior year statutory operating profit included a one-off net benefit of £27.1m following the closure of the Group’s defined benefit pension scheme to future accrual. Details of all specific adjusting items and a reconciliation of underlying profit to total profit is shown in the table below.

## Specific adjusting items

The performance of the Group after allowing for specific adjusting items is shown below:

	2015 £m	2014 £m
Underlying profit for the year attributable to equity shareholders – continuing operations	96.0	89.8
– discontinued operations	0.7	14.2
Underlying profit for the year attributable to equity shareholders – total	96.7	104.0
Impairment of goodwill	–	(125.9)
US Services transaction costs	–	(6.0)
Amortisation of intangible assets arising from acquisitions	(3.6)	(11.0)
Release/(charge) in respect of the 2013 US restructuring	1.0	(0.3)
Reduction in pension liabilities on closure to future accrual	–	31.1
Pension closure mitigation costs	–	(4.0)
Pension net finance expense	(0.6)	(1.7)
Impairment reversal in respect of property	–	1.4
(Loss)/gain on business divestments and disposals of investments	(12.9)	1.1
Tax impact of items above	(1.1)	(1.4)
Recognition of deferred tax asset in respect of UK trade losses	25.2	–
<b>Profit/(loss) for the year attributable to equity shareholders of the parent company</b>	<b>104.7</b>	<b>(12.7)</b>

\* Definitions of specific adjusting items and underlying measures of performance can be found in the glossary on page 141.

<sup>a</sup> Restated for the reclassification of US Services (excluding Cyveillance®) as a discontinued operation.

### Finance costs

Net finance costs were £4.1m (2014: £14.2m<sup>^</sup>). The underlying net finance costs\* were £3.5m (2014: £12.5m<sup>^</sup>), with an additional £0.6m (2014: £1.7m) in respect of the pension net finance expense reported within specific adjusting items. The reduction in underlying net finance costs\* reflects pay down of the private placement debt during 2015.

### Taxation

The effective tax rate for the continuing Group was 10.9% (2014: 11.3%^).

The effective tax rate continues to be below the statutory rate in the UK, primarily as a result of the benefit of research and development relief. The effective tax rate is expected to remain below the UK statutory rate in the medium term, subject to the impact of any tax legislation changes, the geographic mix of profits and the assumption that the benefit of R&D relief continues to be reported in the tax line. The 2013 Finance Act allows the continued super-deduction approach for R&D expenditure until April 2016, when mandatory R&D Expenditure Credit (RDEC) treatment is introduced.

At 31 March 2015 the Group had unused tax losses of £291.6m (31 March 2014: £213.9m) available to offset against future profits. These comprise UK and overseas trade and non-trade losses. A deferred tax asset of £25.2m in respect of an element of these losses was capitalised on the balance sheet in the year due to the probability of them being used in the foreseeable future. The income statement credit associated with this capitalisation went through the 'middle column' rather than underlying earnings. No deferred tax asset has been recognised in respect of other tax losses due to uncertainty over timing and extent of their utilisation.

### Earnings per share

Underlying basic earnings per share\* for the continuing Group were 15.2p (2014: 13.8p<sup>^</sup>) benefiting from the higher profit before tax and the reduced number of shares in issue following £107m of the £150m share buyback programme as at 31 March 2015. Basic earnings per share for the total Group (including US Services) were 16.6p (2014: 1.9p loss per share). The average number of shares in issue during the year, as used in the basic earnings per share calculations, was 630.9m (2014: 651.7m), and there were 608.6m shares in issue at the year end.

\* Definitions of specific adjusting items and underlying measures of performance can be found in the glossary on page 141.

<sup>^</sup> Restated for the reclassification of US Services (excluding Cyveillance®) as a discontinued operation.

### Dividend

The Board proposes a final dividend of 3.6p per share for the year ended 31 March 2015 (2014: 3.2p). Subject to approval at the AGM, the final dividend will be paid on 4 September 2015 to shareholders on the register at 7 August 2015.

### Cash flow

The Group's cash flow from operations before cash flows in respect of specific adjusting items but after capital expenditure was £114.9m (2014: £106.2m<sup>^</sup>). Underlying operating cash conversion\* remained strong at 103% (2014: 93%^).

The net cash outflow in the year on restructuring was £0.6m (2014: £10.3m).

At 31 March 2015 net cash was £195.5m (2014: £170.5m), reflecting continued strong operating cash performance.

Total committed facilities available to the Group at year end amounted to £233.3m (2014: £416.8m). This is made up of a revolving credit facility of £233.3m (2014: £267.9m), which is currently undrawn. 2014 included private placement debt of £148.9m.

### Treasury policy

The Group treasury department works within a framework of policies and procedures approved by the Audit Committee. As part of these policies and procedures, there is strict control on the use of financial instruments. Speculative trading in financial instruments is not permitted. The policies are established to manage and control risk in the treasury environment and to align the treasury goals, objectives and philosophy of the Group.

### Pensions

The net pension deficit under IAS 19 (revised), before deducting deferred tax, was £39.4m (2014: £22.2m). The increase in net pension deficit is primarily driven by macro-economic factors. An actuarial loss arises from the resultant changes to financial assumptions which is partially offset by re-measurement gains on scheme assets.

The key assumptions used in the IAS 19 valuation of the scheme were:

Assumption	2015	2014
Discount rate	3.2%	4.2%
Inflation – CPI	2.1%	2.6%
Life expectancy – male (currently aged 40)	91	90
Life expectancy – female (currently aged 40)	93	92

Each assumption is selected by the Group in consultation with the Company actuary and takes account of industry practice amongst comparator listed companies. The sensitivity of each of the key assumptions is shown in the table below. The market value of the assets at 31 March 2015 was £1,454.6m (2014: £1,304.6m) and the present value of scheme liabilities was £1,494.0m (2014: £1,326.8m).

Assumption	Change in assumption	Indicative effect on scheme liabilities (before deferred tax)
Discount rate	Increase/decrease by 0.1%	Decrease/increase by £28m
Inflation	Increase/decrease by 0.1%	Increase/decrease by £28m
Life expectancy	Increase by 1 year	Increase by £37m

The latest triennial valuation of the scheme is being completed as at 30 June 2014. It is expected that the recovery plan will require £13m contributions per annum until 31 March 2018, the same annual funding level as previously.

#### Foreign exchange risk management

The principal exchange rates affecting the Group were the sterling to US dollar exchange rate and the sterling to Australian dollar exchange rate.

Assumption	2015	2014
£/US\$ – opening rate	<b>1.67</b>	1.52
£/US\$ – average rate	<b>1.63</b>	1.59
£/US\$ – closing rate	<b>1.49</b>	1.67
£/A\$ – opening rate	<b>1.80</b>	1.46
£/A\$ – average rate	<b>1.85</b>	1.69
£/A\$ – closing rate	<b>1.95</b>	1.80

The Group's income and expenditure is largely settled in the functional currency of the relevant Group entity, mainly sterling or US dollar. The Group has a policy in place to hedge all material transaction exposure at the point of commitment to the underlying transaction.

Uncommitted future transactions are not routinely hedged. The Group continues its practice of not hedging income statement translation exposure.

#### Tax risk management

QinetiQ's tax strategy is to ensure compliance with all relevant tax legislation, wherever we do business, whilst managing our effective and cash tax rates. Tax is managed in alignment with our corporate responsibility strategy in that we strive to be responsible in all our business dealings. These principles are applied in a consistent and transparent manner in pursuing the Group's tax strategy and in all dealings with tax authorities around the world.

#### Accounting standards

As a UK-listed company, the Group is required to adopt EU endorsed IFRSs and comply with the Companies Act 2006. The effect of changes to financial reporting standards in the year is disclosed in note 1 to the financial statements.

#### Critical accounting estimates and judgments

A description and consideration of the critical accounting estimates and judgments made in preparing these financial statements is set out in note 1 to the financial statements.

#### David Mellors

Chief Financial Officer  
21 May 2015

# Focus on governance

## Mark Elliott

Non-executive Chairman



### In this section:

• <b>Compliance</b>	49	Good governance is pivotal to the relationship of trust between the Company, its customers, its employees and other key stakeholders. Effective stewardship and risk management are key to the markets in which QinetiQ operates and provide the stability necessary to enable the Group to grow its business and create future success.
• <b>Relations with shareholders</b>	52	Succession planning continued to be a key priority for the Board. Following the departure of Colin Balmer and the appointment of Susan Searle during the 2014 financial year, further changes took place with the appointment of Ian Mason as an additional Non-executive Director in June 2014 and the retirement of Noreen Doyle as a Non-executive Director in July 2014, having completed nearly nine years on the Board. Leo Quinn resigned as Chief Executive Officer with effect from December 2014 and Steve Wadey was appointed as the new Chief Executive Officer with effect from April 2015. This process of change and renewal is critical as the Group moves from the period of transformation under Leo Quinn to a greater focus on growth. I am delighted to be working with Steve Wadey as we begin this new phase in QinetiQ's development.
• <b>Leadership</b>	54	At the executive level, the Operating Committee continued to be responsible for the day to day management of the Group's activities (other than for the part of the US business that is subject to a Proxy agreement) and the Governance Committee continued to be responsible for overseeing risk management. Both committees report to the Board via the Chief Executive Officer. At the annual Board strategy meeting in October, members of the Board had an opportunity to meet with and challenge business leaders on their business plans and strategy.
– Roles and responsibilities	54	
– Board objectives	54	
– Composition of the Board	55	
– Board meetings and attendance	55	
– Committees	55	
• <b>Directors' biographies</b>	58	
• <b>Effectiveness</b>	60	Following completion of the sale of the US Services business in May 2014 and the appointment of the new Proxy Board to manage that element of the retained US business that is required to be insulated from foreign ownership, control or influence (as detailed on page 65), work began in evaluating the retained US business. An excellent working relationship has been established with the new Proxy Board and the Proxy Board Chairman, Len Moodispaw, has joined the UK Board on occasion. The internal audit function continues to work closely with US management to gain assurance that an effective control environment is in place.
– Director training and development	60	
– Independence of Non-executive Directors	60	
– Performance of the Board	60	
• <b>Report of the Nominations Committee</b>	62	
• <b>Accountability</b>	63	
– Identification and review of risks	63	
– Internal control	64	
– Management and control of US subsidiaries	65	
• <b>Report of the Audit Committee</b>	66	During the year ended 31 March 2015 the Board oversaw significant change within the Group, both in terms of personnel and in terms of its structure. The governance arrangements ensured 'business as usual' throughout this period and continue to provide a stable environment for the new Chief Executive Officer.
• <b>Report of the Risk &amp; CSR Committee</b>	70	
• <b>Report of the Security Committee</b>	71	
• <b>Directors' remuneration report</b>	72	
– Report of the Remuneration Committee	72	
– Remuneration Policy Summary	76	
– Annual Report on Remuneration	78	
• <b>Directors' report</b>	86	
• <b>Directors' responsibility statement</b>	89	
• <b>Independent auditor's report</b>	90	

## Mark Elliott

Non-executive Chairman  
21 May 2015

### Compliance statement

QinetiQ is subject to the Financial Reporting Council's UK Corporate Governance Code (the Code) as currently in effect. The Code and associated guidance are publicly available on the Corporate Governance page of the Financial Reporting Council's website, [www.frc.org.uk](http://www.frc.org.uk).

With the exception of the external evaluation of the Board, as detailed below, the Board considers that QinetiQ has complied with all relevant Provisions of the Code throughout the last financial year. This statement provides details of the way in which the Main Principles of the Code have been applied during that year.

### External evaluation of the Board – Code Provision B.6.2.

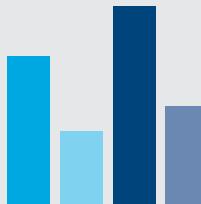
Code Provision B.6.2. states that evaluation of the board of FTSE 350 companies should be externally facilitated at least every three years. An external evaluation of the Board would have taken place during the year under review, however, pending the appointment of the new Chief Executive Officer, the Board decided to defer the external evaluation process by one year, and to proceed with an externally provided online questionnaire-based review tool in 2015, to allow time for the new Chief Executive Officer to take up his role. Further details of the review can be found in the 'Effectiveness' section on page 60.

An overview of the Group's corporate governance arrangements can be found on the QinetiQ website at: [www.QinetiQ.com/about-us/corporate-governance](http://www.QinetiQ.com/about-us/corporate-governance).

### Effective governance

An effective Board sets the tone, influencing culture and behaviours through its decisions and leadership. To be effective, a Board should comprise experienced individuals with a range of background and experience, who are independent in character and judgment.

#### Board skills



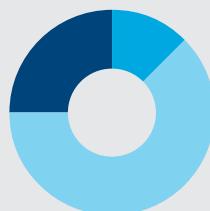
2015	Number of Directors
Defence	6
Engineering	3
Financial	8
Science	4

#### Board independence



2015	%
Non-independent	37.5
Independent	62.5

#### Board composition



2015	%
Non-executive Chairman	12.5
Non-executive Directors	62.5
Executive Directors	25

# Overview of the application of the Main Principles of the Code

## A. Leadership (pages 54 to 59)

### A1 The Role of the Board

The Board met seven times during the year. There is a schedule of matters reserved to the Board and the Board has a set of objectives and responsibilities. Details of the Board membership and their attendance at Board and Committee meetings are included in this Annual Report on page 55.

### A2 Division of Responsibilities

The roles of Chairman and Chief Executive are not exercised by the same individual and their separate responsibilities are established.

### A3 The Chairman

The Chairman, working with the Company Secretary, sets the agenda for Board meetings and encourages an open and constructive debate.

### A4 Non-executive Directors

The Non-executive Directors provide constructive challenge to management. The Board has appointed a Senior Independent Non-executive Director. Regular meetings are held with the Chairman and Non-executive Directors without the executives present.

## B. Effectiveness (pages 60 to 63)

### B1 The Composition of the Board

At least half the Board (excluding the Chairman) comprises independent Non-executive Directors. The Board considers the overall size and composition to be appropriate, having regard to the experience and skills the Directors bring to their duties.

### B2 Appointments to the Board

The Nominations Committee oversees appointments to the Board, its balance of skills and experience and the succession planning process. The report of the Nominations Committee can be found on page 62.

### B3 Time Commitment

The anticipated time commitment required in respect of the non-executive role is communicated in the appointment process. The Board is notified of changes to other significant commitments and the Chairman consulted where appropriate.

### B4 Director Training and Development

All Directors receive a tailored induction on joining the Board. Site visits and training are made available to enable Directors to develop and update their knowledge and capabilities.

### B5 Information and Support for Directors

The Chairman, working in conjunction with the Company Secretary, ensures that the Board receives accurate, timely and clear information.

### B6 Performance evaluation

An evaluation of the performance of the Board, its Committees and individual Directors is carried out annually.

### B7 Re-election of Directors

The Company requires each serving member of the Board to be put forward for election or re-election on an annual basis at each Annual General Meeting.

## C. Accountability (pages 63 to 71)

### C1 Financial and Business Reporting

The Board presents its results at the full year and the half year and provides quarterly updates to the market. The Annual Report and Accounts contains a Strategic report which provides an explanation of the business model and the strategy for delivering the objectives of the Company. A going concern statement is included on page 88, responsibility statements can be found on pages 88 to 89, and details of the process for ensuring that the Annual Report is fair, balanced and understandable can be found on page 89. There is also a statement in the auditor's report on page 92 about their reporting responsibilities.

### C2 Risk Management and Internal Control

The risk management process and the system of internal control necessary to manage risks are overseen by the Audit Committee (financial risks) and the Risk & CSR Committee (non-financial risks). A report on specific risk review activity undertaken during the year by those committees, together with the current risk registers, was presented by the CEO to the Board at its March meeting. The Strategic report contains on pages 30 to 37 details of risk management and the Company's principal risks and uncertainties, their impact and how they are managed. Details of risk management and internal control processes can be found on pages 63 to 65.

### C3 Audit Committee and Auditors

The Board has established an Audit Committee comprising at least three independent Non-executive Directors, with formal terms of reference. It oversees the financial risk management and internal controls process, the effectiveness of internal audit activities, the external auditor's independence and objectivity and makes recommendations to the Board in respect of the reappointment of the external auditor and their remuneration. The report of the Audit Committee can be found on pages 66 to 69.

## D. Remuneration (pages 72 to 85)

### D1 Level and Components of Remuneration

The Board has established a Remuneration Committee with formal terms of reference. It is responsible for ensuring that levels of remuneration are sufficient to attract, retain and motivate Directors of sufficient quality and that any performance related elements are relevant, stretching and designed to promote the long-term success of the Company.

### D2 Developing Remuneration Policy and Packages

The report of the Remuneration Committee can be found on pages 72 to 74 and provides details of, or links to, the procedure for setting policy on Executive Director remuneration. The Committee also recommends and monitors the level and structure of remuneration for senior management.

## E. Relations with shareholders (pages 52 to 53)

### E1 Dialogue with Shareholders

The Chairman ensures that all Directors are made aware of major shareholder issues and concerns, by way of reports from the Executive Directors at Board meetings, attendance at key financial calendar events and by making themselves available to meet shareholders as required.

### E2 Constructive Use of the Annual General Meeting

All shareholders are invited to attend the Annual General Meeting and to ask questions. The Chairs of the Audit, Nominations, Remuneration, Risk & CSR and Security Committees attend the meeting and are available to answer any questions on the work of the committees.

## Relations with shareholders

The Company attaches significant importance to the effectiveness of its communications with shareholders and sets itself the target of providing information that is timely, clear and concise. Responsibility for maintaining regular communications with shareholders rests with the Chief Executive Officer (CEO) and the Chief Financial Officer (CFO), assisted by the Investor Relations Director.

An investor perception audit was conducted during the financial year by an independent third party comprising interviews with a dozen leading institutional shareholders in July and August 2014 controlling some 45% of the issued equity. The results of this audit were considered by the Board as part of its review of Group strategy in October, and when setting the criteria for the new CEO recruitment process.

According to the audit, the QinetiQ investor relations team had met with over 100 institutional contacts in the preceding 12 months, accounting for more than three-quarters of QinetiQ's institutional shareholding base. More than 70 of these meetings were hosted by the Executive Directors, who met with eight out of ten top shareholders and 21 out of the top 30.

The Chairman proactively offers to attend meetings with key shareholders, and their corporate governance teams, on a regular basis. The Chairman, the Senior Independent Director and Non-executive Directors routinely attend key financial calendar events such as presentations of interim and preliminary results and make themselves available to meet shareholders as required.

Following the announcement of the resignation of the Chief Executive Officer, the Chairman and Investor Relations Director engaged with top shareholders, subsequently meeting with a number of them face-to-face. All top shareholders were also proactively contacted following the announcement of the appointment of Steve Wadey as the Group's new CEO.

The Board as a whole is informed on a regular basis about the views of key shareholders, including their concerns. The Investor Relations Director reports to the CEO, and provides regular updates to the Chairman and Non-executive Directors by way of face-to-face briefings, email updates and a section in the Executive Directors' report which is included in the Board papers as a standing item. The following information is included in these reports:

- financial calendar and draft material;
- share price performance;
- the composition of the shareholder register;
- feedback from investor meetings, including key questions;
- covering sell-side analysts, their recommendations and expectations; and
- peer group news.

Other investor activity during the last financial year included:

- telephone briefings for analysts and investors, at least six times per year in conjunction with key financial announcements and financial period ends;
- face-to-face presentations of full year and half-year results, in May and November respectively, where the Chairman and Directors were available for discussions with investors;
- live and post-event webcasts of key presentations such as the full year and half-year results;
- investor 'road shows' held in London, Edinburgh, and the east and west coasts of the United States in May, June, November and December;
- visits, sales team briefings, group lunches, conference presentations and ad hoc meetings on request;
- web-based investor centre optimised for mobile devices and iPad app updated regularly and incorporating best practice; and
- the Annual General Meeting held on 22 July 2014.

### Annual General Meeting

The Code notes that the Board should use the Annual General Meeting (AGM) to communicate with investors and encourage their participation. The Board invites holders of ordinary shares to attend the Company's AGM each year and to ask questions. The Chairs of the Audit, Remuneration, Nominations, Risk & CSR and Security Committees are available at that meeting to answer any questions on the work of the Committees.

The 2014 AGM was held at Pennyhill Park Hotel, Bagshot, Surrey on 22 July 2014 and, with the exception of Noreen Doyle, who had a prior engagement, each member of the Board attended the meeting and was available to take questions.

The 2015 AGM is scheduled to be held at the same venue, Pennyhill Park Hotel, Bagshot, Surrey, on 22 July 2015. The Company confirms that it will send the Notice of Meeting and relevant documentation to all shareholders at least 20 working days before the date of the AGM. For those shareholders who have elected to receive communications electronically, notice is given of the availability of documents in the 'Investors' section of the Group's website. All shareholders will be entitled to vote on the resolutions put to the AGM and, to ensure that all votes are counted, a poll will be taken on all of the resolutions in the Notice of Meeting. The results of the votes on the resolutions will be published on the Company's website, [www.QinetiQ.com](http://www.QinetiQ.com), in the 'Investors' section.

### Website information

All shareholders and potential shareholders can gain access to the Annual Report, presentations to investors, AGM documentation, key financial information, regulatory news, financial calendar, share and dividend data and other significant information about QinetiQ in the 'Investors' section of the Company's website, [www.QinetiQ.com](http://www.QinetiQ.com). The site also provides contact details for any investor-related queries, by telephone and by email.

The Company continues to look at ways of improving the quality of its engagement with shareholders and to explore with investors any additional practical means by which it can give effect to the requirements of the Financial Reporting Council's UK Stewardship Code for institutional investors, and of the Code.

Details of the Company's share capital, which are required to be disclosed in accordance with rule 7.2.6 of the Financial Conduct Authority's Disclosure Rules and Transparency Rules, and the Directors' powers in relation to issuing and buying back shares can be found on pages 88 and 86 respectively in the Directors' report section of this Annual Report.

## Leadership

### Roles and responsibilities

The Board of Directors:

- is responsible for overseeing the Executive Directors' management of operations and, in this capacity, determines the Group's strategic and investment policies;
- monitors the performance of the Group's senior management team and organises its business to have regular interaction with key members of senior management; and
- is responsible for overseeing the management of the business of the Group. Its powers are subject to the Articles of Association and any applicable legislation and regulation.

### Board objectives

The overarching remit of the Board is to demonstrate the highest standards of corporate governance in accordance with the Code:

- to ensure the continuing evolution and implementation of the Group's strategy to deliver value to all stakeholders: customers, employees and shareholders;
- to develop challenging objectives for the business and monitor management performance against those goals;
- to provide a framework of effective controls to assess and manage risks, with clear expectations of conduct to the highest standards of ethics;
- to provide support and constructive challenges to the CEO to promote the Group's success;
- to demonstrate leadership in management systems around health, safety and environment; and
- to manage succession planning for the Board and the Group's executive management.

### The Board

The Board represents the interests of both QinetiQ and its shareholders. It comprises a range of experience and expertise required to meet the challenges facing the Group. The Non-executive Directors bring independent judgment on key issues affecting the Group and its business operations, including strategy, performance, resources (including key appointments) and standards of conduct. Directors receive ongoing training about the Company and their duties.

### Operation

The Board operates through a comprehensive set of processes, which define the schedule of matters to be considered by the Board and its Committees during the annual business cycle.

This includes the level of delegated authorities (both financial and non-financial) available to Executive Directors and other layers of management in the business, QinetiQ's business ethics, risk management, and health, safety and environmental processes.

The Board devotes one entire meeting each year to consider strategy and planning issues that have an impact on the Group, from which the corporate plan is generated. It is also regularly kept up to date on strategic issues throughout the year.



**P55** See Operation of the Board for more information

### Matters reserved to the Board

The Board has a clearly articulated set of matters which are specifically reserved to it for consideration.

These include:

- reviewing and approving the annual budgets;
- raising indebtedness;
- granting security over Group assets;
- approving Group strategy and the corporate plan;
- approving the Annual and Interim Report and Accounts;
- approving significant investment, bid, acquisition and divestment transactions;
- approving HR policies (including pension arrangements);
- reviewing material litigation; and
- monitoring the overall system of internal control, including risk management.

### Composition of the Board

At the date of this report, the Board has eight members: the Non-executive Chairman; five other Non-executive Directors; and two Executive Directors – the CEO and the CFO. Their names and biographical details can be found on pages 58 to 59.

The following changes in Board membership took place during the year:

- Ian Mason was appointed as a Non-executive Director on 3 June 2014.
- Noreen Doyle retired as a Non-executive Director on 22 July 2014, having served on the Board for more than eight years.
- Leo Quinn resigned as an Executive Director and Chief Executive Officer on 31 December 2014.
- David Mellors was appointed as interim Chief Executive Officer from 1 January 2015 until 26 April 2015.

The following change took place after the year end:

- Steve Wadey was appointed as an Executive Director and Chief Executive Officer on 27 April 2015.

### Attendance at meetings of the Board and its Committees

– 1 April 2014 to 31 March 2015

Members	Committee				
	Board	Audit	Nominations	Remuneration	Risk & CSR
Mark Elliott	7/7	–	4/4	6/6	4/4
Admiral					
Sir James					
Burnell-Nugent	7/7	5/5	4/4	6/6	4/4
Noreen Doyle <sup>~</sup>	1/2	2/2	1/1	1/2	1/2
Michael Harper	7/7	5/5	4/4	6/6	4/4
Ian Mason	6/6	3/3	3/3	5/5	3/3
David Mellors <sup>&lt;</sup>	7/7	–	2/2	–	4/4
Paul Murray	7/7	5/5	4/4	6/6	4/4
Leo Quinn	5/5	–	1/2	–	2/3
Susan Searle	7/7	5/5	4/4	6/6	4/4

Steve Wadey has not been included in the above table as he did not serve as a Director during the year under review.

<sup>~</sup> Noreen Doyle was unable to attend the July meetings due to a prior engagement.

<sup><</sup> David Mellors was interim CEO during the period from 1 January 2015 to 26 April 2015 and attended meetings in that capacity where appropriate.

### Operation of the Board

For each meeting, the Board receives a written report from the CEO and CFO, together with a separate report on investor relations which is prepared in consultation with QinetiQ's brokers, and a report produced by the Company Secretary on key legal and regulatory issues that affect the Group. The CEO's and CFO's report addresses the key strategic initiatives which have had an impact on the Group since the previous Board meeting, with particular focus on the progress of each of the businesses. Other key areas of focus include health, safety and environmental matters; employee and organisational issues; corporate responsibility; the status of key account management/customer relationship initiatives; the pipeline of potential bids, acquisitions, disposals and investments; and the post-acquisition performance of recently acquired businesses.

The Board also receives updates from key functional areas on an 'as needed' basis, on issues such as human resources, treasury, corporate responsibility, real estate, security, trade controls and pensions.

Key issues considered by the Board in the past year include:

- the impact of the disposal of the US Services division;
- the strategy for the Group as a whole; and
- succession planning.

Further details are set out on the next page.

### Committees

QinetiQ operates by way of two key Executive Committees and five principal Board Committees. Details can be found on page 57.

**Key issues covered by the Board during the past year include:**

**a) Disposal of the US Services business**

The US Services business disposal was completed in May 2014. The retained US business was split into those areas where no Proxy arrangement was necessary, and the US Global Products business where a new Proxy arrangement was required (as detailed on page 65). Since then the Board has received updates, via the regular Executive Directors' Report to the Board and by presentations from the US Global Products executive team,

of progress with the new Proxy arrangement, an evaluation of the business and its strategy, and measurement against its objectives. During the year, a new president was appointed to drive forward the development of the business, which will remain an important subject of the Board's focus.

**b) Group strategy**

During the year, the Board received updates on progress against strategy by way of regular presentations from the Group Strategy Director. The presentations included a measurement of progress against milestones/objectives and a linkage between strategy and daily activity. In October, the Board held its annual two-day strategy meeting at an off-site location where the strategy for the Group as a whole was reviewed. In advance of the meeting, the Board had given guidance to the Group Strategy Director on subject areas it would like to see covered at the strategy meeting. As in the previous year, the Managing Directors from each business and the leaders of key corporate functions attended the two-day meeting and gave presentations on the strategy for their respective business areas.

The Board was able to meet both formally and informally with business leaders, to understand the key drivers and risks (including their mitigation) for their business areas. Following the meeting, the strategic business plans were updated and form the basis for regular progress reports to the Board by the Group Strategy Director.

Alongside the process for the setting and review of Group strategy, the Board also commissioned an external report to identify shareholder perspectives and observations on the Company's stated strategy and investment proposition. The report was tabled at a Board meeting and it was noted that, amongst other things, shareholders' general observations were that the Company had been transformed into a more focused and manageable business with net cash on its balance sheet, there was strong support for management and a well understood strategy. The output from the report in terms of growth has been used to inform the Company's strategic thinking in respect of value creation and growth.

**c) Succession planning**

Succession planning, both at Executive and Non-executive level, remains a key focus for the Board. In July 2014 the Board highlighted succession planning as one of its top priorities for the year. The Board stated its objective of reviewing comprehensive succession plans for the top 12 to 15 executive positions with a focus on improving the talent pipeline and diversity. In addition, the Board stated that it will continue to focus on the succession plans for the Non-executive Directors, including both training and refreshment, to ensure they align Board skills with the needs of the strategy.

Membership of the Board was refreshed during the year, with the appointment of Ian Mason as a Non-executive Director in June 2014 and the search and appointment of a new Chief Executive Officer which was completed with the appointment of Steve Wadey, who joined the Board in April 2015. Further details can be found in the report of the Nominations Committee on pages 62 to 63.

As regards talent management within the wider Group, at the September Board meeting, the Director of Capability updated the Board on the activities being taken in respect of equality, diversity and inclusion. The Board approved the policy and noted the means of measuring progress by way of a scorecard approach. At the October strategy meeting, the Director of Capability gave a presentation on enhancing human capability within the Group, including to protect and secure suitably qualified and experienced personnel, in particular to support the business strategy and to continue to develop the Company's culture, with improved diversity, an emphasis on unlocking the potential of the workforce and the encouragement of innovation.

Further details on diversity can be found in the Responsible business section on pages 24 to 29.

## The Board and its Committees

### Board

The Board of Directors is responsible for the governance of the Company and for agreeing its strategy and monitoring its progress. Details of the Directors at the date of this report can be found on page 55.

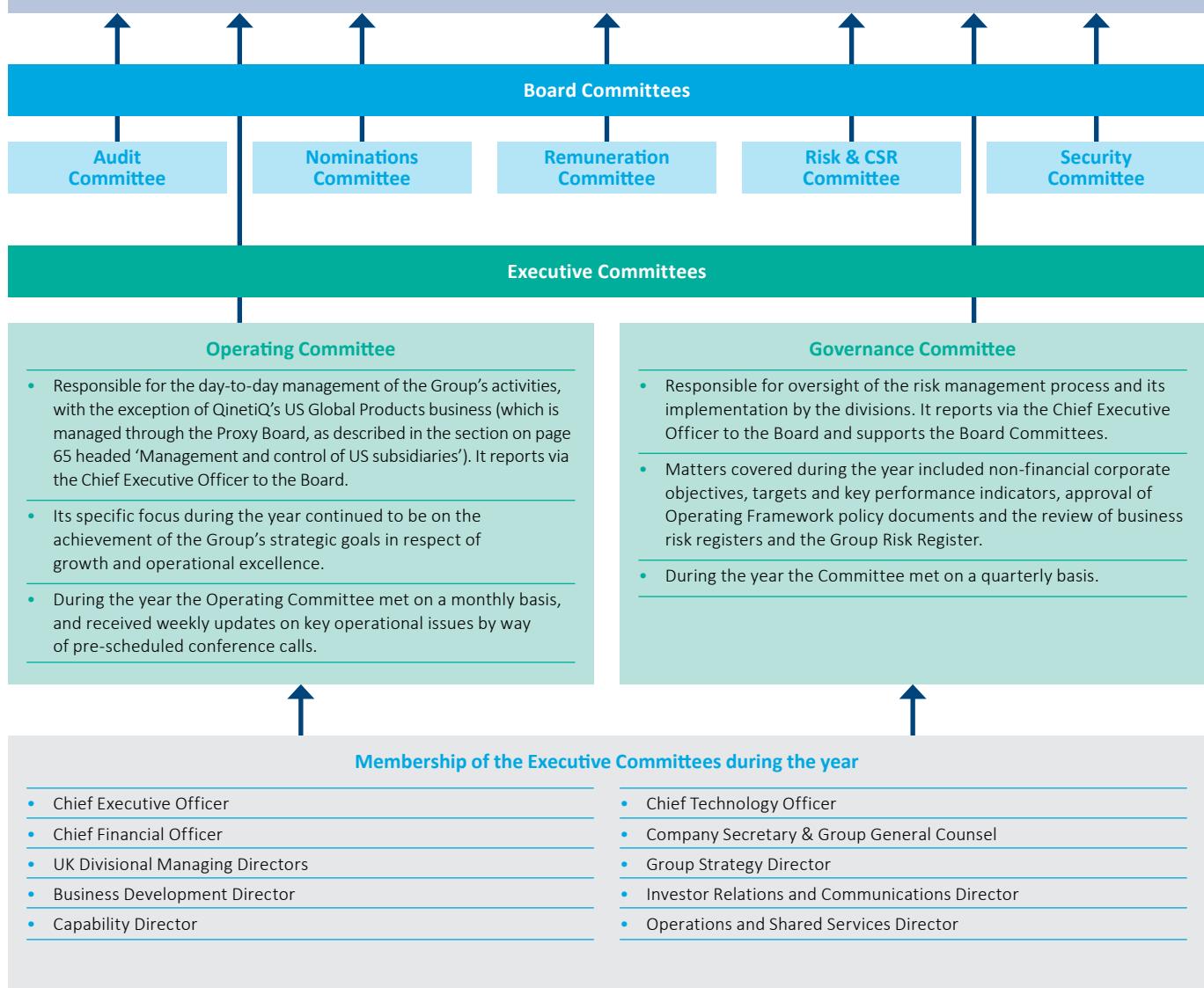
The Board has established five principal Committees: the Audit Committee, the Nominations Committee, the Remuneration Committee, the Risk & CSR Committee and the Security Committee. Each operates within written terms of reference approved by the Board. The full terms of reference can be found in the Governance section of the QinetiQ website at [www.QinetiQ.com/about-us/corporate-governance](http://www.QinetiQ.com/about-us/corporate-governance).

Given the size of the Board, and in the interests of full Board participation and transparency, the Board maintains a policy of all-Director membership of Committees, other than where prohibited by the Code, statutory or Security Committee requirements.

Where a Committee is not attended by the full Board, details of the key issues discussed, and decisions taken, are circulated to all members of the Board after the relevant Committee meeting.

A report in respect of each of these Committees is contained on pages 62 to 74. The details of each Committee member's attendance at Committee meetings are set out in the table contained within each Committee report.

Details of the Group's reward and remuneration policies and payments, together with the report of the Remuneration Committee, can be found in the Directors' remuneration report on pages 72 to 85 which is incorporated into this corporate governance statement by reference.



<b>Mark Elliott</b> Non-executive Chairman	<b>Steve Wadey</b> Chief Executive Officer	<b>David Mellors</b> Chief Financial Officer	<b>Michael Harper</b> Deputy Chairman and Senior Independent Non-executive Director
			
<b>Appointment to the Board</b>	Appointed Non-executive Chairman in March 2010; Non-executive Director between June 2009 and February 2010.	Appointed Chief Executive Officer in April 2015.	Appointed Chief Financial Officer in August 2008. Interim Chief Executive Officer from 1 January 2015 until 26 April 2015.
<b>Independent</b>	Independent on appointment	Not applicable	Not applicable
<b>Skills and experience</b>	<ul style="list-style-type: none"> <li>Extensive experience in the technology services sector having worked for IBM for over 30 years in a number of senior management positions.</li> <li>Experience of a variety of industry sectors from membership of the boards of FTSE listed companies.</li> <li>The Board considers that Mark's extensive experience, including listed company governance experience, is a valuable asset to the Group in terms of leadership and of addressing the strategic issues that affect the Group.</li> </ul>	<ul style="list-style-type: none"> <li>In-depth experience of the defence industry and technology.</li> <li>Extensive operational and corporate experience and stewardship.</li> <li>Fellow of the Royal Academy of Engineering.</li> <li>Fellow of the Institution of Engineering and Technology.</li> <li>Fellow of the Royal Aeronautical Society.</li> </ul>	<ul style="list-style-type: none"> <li>Extensive experience of working in a listed company environment.</li> <li>Knowledge of the defence, technology and services sectors.</li> <li>A member of the Institute of Chartered Accountants in England and Wales.</li> </ul> <p>• A depth of operational and corporate experience and stewardship, including in the engineering sector.</p> <p>• The Board considers that Michael's wealth of operational and corporate experience, including listed company governance experience, enables him to make a significant contribution to the Board.</p>
<b>External appointments</b>	<ul style="list-style-type: none"> <li>Non-executive Director of G4S plc, where he is the Senior Independent Director and Chairman of the Remuneration Committee.</li> <li>Chairman of Kodak Alaris Holdings Limited (appointed during the year under review).</li> </ul>	<ul style="list-style-type: none"> <li>Co-chair of the Defence Growth Partnership.</li> <li>Non-executive director of the MOD Research and Development Board.</li> </ul>	<ul style="list-style-type: none"> <li>None</li> </ul>
<b>Past roles</b>	<ul style="list-style-type: none"> <li>Non-executive Director of Reed Elsevier Group plc (and also Chairman of its Remuneration Committee) and Reed Elsevier NV from April 2003 until April 2013.</li> <li>Worked for IBM for over 30 years where he occupied a number of senior management positions, including General Manager of IBM Europe, Middle East and Africa.</li> <li>Member of IBM's worldwide Management Council.</li> </ul>	<ul style="list-style-type: none"> <li>Various roles with MBDA from 2001 to 2014, most recently as Managing Director, MBDA UK and Technical Director for the MBDA Group.</li> <li>Matra BAe Dynamics – various roles in engineering held from 1996 to 2001.</li> <li>Various roles with British Aerospace held from 1989 to 1996.</li> <li>Co-Chair of the National Defence Industries Research &amp; Development Group.</li> </ul>	<ul style="list-style-type: none"> <li>Deputy Chief Financial Officer of Logica plc. He was also Chief Financial Officer of Logica's international division, covering operations in North America, Australia, the Middle East and Asia and, before that, was the Group Financial Controller.</li> <li>Various roles with CMG plc, Rio Tinto plc and Price Waterhouse.</li> </ul> <p>• Chairman of Ricardo plc from November 2009 until November 2014, having joined that Board in 2003.</p> <p>• Chairman of BBA Aviation plc from June 2007 until May 2014, having joined that Board in 2005.</p> <p>• Chairman of Vitec Group plc from 2004 to 2012.</p> <p>• Director of Williams plc where, at the time of the demerger in 2000, he became CEO of Kidde plc.</p>
<b>Committee membership</b>	Nominations Committee (Chairman) Remuneration Committee Risk & CSR Committee	Nominations Committee Risk & CSR Committee Security Committee	Risk & CSR Committee Security Committee
			Audit Committee Nominations Committee Remuneration Committee (Chairman) Risk & CSR Committee Security Committee

<b>Ian Mason</b> Non-executive Director	<b>Admiral Sir James Burnell-Nugent</b> Non-executive Director	<b>Paul Murray</b> Non-executive Director	<b>Susan Searle</b> Non-executive Director	<b>Jon Messent</b> Company Secretary and Group General Counsel
				

Appointed Non-executive Director in June 2014.	Appointed Non-executive Director in April 2010.	Appointed Non-executive Director in October 2010.	Appointed Non-executive Director in March 2014.	Appointed Company Secretary and Group General Counsel in January 2011.
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Yes	Yes	Yes	Yes	Not applicable
<ul style="list-style-type: none"> <li>Considerable experience in strategy, business transformation, eCommerce and international development.</li> <li>The Board considers that Ian's experience in strategy, business transformation and international development is of significant benefit to the Board.</li> </ul>	<ul style="list-style-type: none"> <li>Significant experience of the defence industry, contracting with government and management.</li> <li>The Board considers that Sir James' expertise in the Government contracting domain, particularly with the UK MOD and HM Treasury, is highly beneficial in the context of QinetiQ's government-sourced operations.</li> </ul>	<ul style="list-style-type: none"> <li>A broad range of experience in finance and corporate governance from a range of industries.</li> <li>The Board considers that Paul's experience in finance and corporate governance from a cross-section of industries, all of which leverage technology, and including listed company governance experience, is of significant benefit to the Board.</li> </ul>	<ul style="list-style-type: none"> <li>Extensive experience of the new technologies sector.</li> <li>A founder of Imperial Innovations Group plc.</li> <li>The Board considers Susan's strong experience of commercialising new technologies and intellectual property of particular relevance to QinetiQ as it pursues its Organic-Plus strategy.</li> </ul>	<ul style="list-style-type: none"> <li>Extensive experience as a General Counsel and Company Secretary in other FTSE250 companies.</li> <li>Background in legal private practice.</li> </ul>

• None	• High Sheriff of Devon.	• Non-executive Director and Chair of the Audit & Risk Committee at Royal Mail Group plc.	• Benchmark Holdings plc. <sup>(a)</sup>	• None
• Group Chief Executive of Electrocomponents plc from 2001 until 31 March 2015, having joined that company in 1995.	• 37-year career in the Royal Navy that culminated in his appointment as Commander-in-Chief Fleet.	• Director of Knowledge Peers plc.	• Horizon Discovery Group plc. <sup>(a)</sup>	• Joined QinetiQ from Chloride Group plc.

• Non-executive Director of the Sage Group plc from 2007 to 2013.	• Commanded the aircraft carrier HMS Invincible and three other ships and submarines.	• Senior Independent Director of Taylor Nelson Sofres plc.	• Chair of Woodford Patient Capital Trust plc.	• General counsel and company secretarial experience in other FTSE250 companies.
• Between operational duties, several positions at the MOD and gained cross-Whitehall experience while on secondment to HM Treasury.	• Non-executive Director of Thomson SA.	• Non-executive Director of Tangent Communications plc.	• Mericia Technologies plc. <sup>(b)</sup>	

Audit Committee Nominations Committee Remuneration Committee Risk & CSR Committee Security Committee	Audit Committee Nominations Committee Remuneration Committee Risk & CSR Committee (Chairman) Security Committee (Chairman)	Audit Committee (Chairman) Nominations Committee Remuneration Committee Risk & CSR Committee Security Committee	Audit Committee Remuneration Committee Risk & CSR Committee Nominations Committee Security Committee
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## Effectiveness

The Board considers that the skills and experience of its individual members, particularly in the areas of UK defence and security, the commercialisation of innovative technologies, corporate finance and governance, mergers and acquisitions, and risk management, have been fundamental in the pursuit of QinetiQ's strategic initiatives (as described on pages 10 to 19 of this report) in the past year. In addition, the quoted company experience of members of the Board in a variety of industry sectors and international markets has also been invaluable to the Group as it seeks to consolidate its position in its core markets and geographic territories.

### Director training and development

On appointment, Directors receive a tailored induction programme, comprising site visits, meetings with management and training where required. On an ongoing basis, Directors receive appropriate training about the Company and their duties. The Company Secretariat organises site visits and training to suit individual requirements. Recent training has included regulatory updates presented at Board meetings by the Company's legal advisors and by the auditor.

### Independence of Non-executive Directors

Of the current Directors of the Company, the Board considers all the Non-executive Directors to be independent of QinetiQ's executive management and free from any business or other relationships that could materially interfere with the exercise of their independent judgment. The Board considers that more than half its members were independent Non-executive Directors throughout the last financial year.

The Non-executive Directors bring independent judgment on key issues affecting the Group and its business operations including strategy, performance, resources (including key appointments) and standards of conduct. Their independence of character and integrity, together with the experience and skills that they bring to their duties, prevent any individual or small group from dominating the decision making of the Board as a whole.

### Performance of the Board

QinetiQ continues each year to evaluate the performance of the Board and its Committees. The most recent external evaluation of the Board's effectiveness was carried out by Independent Audit Limited in 2012 and reported in that year's Annual Report and Accounts. In 2013 and 2014, the Board's effectiveness was assessed internally by way of a questionnaire completed by Board members and individual performance reviews carried out by the Chairman and the Senior Independent Director.

For the year ended 31 March 2015, the Company was due to carry out an external evaluation of the performance of the Board, however, owing to the change of Chief Executive Officer during the year, it was considered appropriate to defer the external review by one year, to allow time for the incoming Chief Executive Officer to take up his new role. Accordingly, to ensure an external and independent perspective on the self-assessment, the Company used an online questionnaire tool provided by Independent Audit Limited which was completed by Board members, coupled with individual performance reviews carried out by the Chairman. Independent Audit Limited had no other connection with the Company during the period, other than the provision of advice to the Audit Committee on the continued independence of the external auditor in connection with contractual arrangements.

In terms of the fulfilment of its governance responsibilities, the overall conclusion of the 2014 review had been that the Board was satisfied that it continued to be effective in executing its duties and that progress had been made in a number of areas since the last review.

Following on from the 2014 review, the Board had undertaken during 2015 a programme of continuous improvement, as follows:

- strategy and succession remained key priorities for the Board. With regard to strategy, the Board required improved reporting of daily activity implementing the strategy, with the preparation of a note of achievement against strategy by the use of milestones and the preparation of key objectives against which plans are measured. These details have since been included in the regular updates on progress against strategic targets provided to the Board by the Group Strategy Director;
- alignment of Board risk appetite as it related to the Company's growth strategy;
- the Company Secretariat facilitates site visits for the Non-executive Directors at their request and there were visits to five sites by Non-executive Directors during the year;
- Board training – continuation of the focus on individual training requirements. Recent training included a group training session on cyber risk management and a formal presentation to the Board by the external auditor on the changes to the UK Corporate Governance Code;

- continue the practice of making key senior management available to the Board during site visits and other Company events, and the focus on inviting some of them to attend the Board to report on progress on key Company programmes – during the year under review, Board meetings were held at the Company's Aberporth and Farnborough sites;
- continued efficiencies in the provision of Board materials, by the use of a standardised layout for Board and Committee papers, including an executive summary and clear indication of the action required or purpose of the materials; and
- identification by the Board of a consolidated set of key objectives and responsibilities for the Board – each Director had been asked to provide to the Chairman their view on three main objectives for the Board. The Chairman had collated these and worked with the CEO and CFO to finalise a consolidated set of objectives which included:
  - Shareholder perspectives – to commission an external report to capture shareholders' views as to the Company's strategy and investment proposition and their attitudes on growth, risk and resource allocation. The report was commissioned and details of the results of this review considered at the Board's October strategy meeting;
  - Strategy development – to review progress and future development of the Company's strategy in the context of the new portfolio of assets, focusing on means to accelerate value creation including through growth, balanced with shareholders' and the Board's appetite for risk;
  - Board operations – to continue to focus on improving Board operations, including disciplined use of time and making papers 'fit for purpose', recognising that papers for issue resolution or decisions might differ from those intended to update or inform the Board; and
  - Succession planning – to continue to improve on succession planning with the review of comprehensive succession plans for the Company's top 12 to 15 executive positions with a focus on improving the talent pipeline and diversity. In addition, to continue to focus on the succession plans for the NEDs to ensure the alignment of Board skills with the needs of the Company's strategy.

To build upon the continuous improvement programme which had begun during the year, the 2015 effectiveness review had covered the following main areas:

- The role of the Board and the skills mix;
- The effectiveness of decision-making processes and the quality of supporting documentation;
- The level of risk appetite and oversight; and
- Engagement with stakeholders.

The general outcome was that the Board was operating effectively and carrying out its duties appropriately. There had been improved reporting in the papers for the Board, allowing for a greater understanding and support. Following the recent changes in the Board membership, and with the arrival of the new CEO, it was agreed that steps would be taken to integrate all members of the Board and also to facilitate further attendance at Board meetings by members of the Operating Committee and senior management to enhance the Board–business relationship.

# Report of the Nominations Committee

## Mark Elliott

Nominations Committee Chairman



I am pleased to report that the Nominations Committee addressed succession planning as a priority during the year, with the appointment of Ian Mason as a Non-executive Director and the search for a new Chief Executive Officer and subsequent appointment of Steve Wadey being completed during the year. Going forwards, we have identified succession planning as one of the Board's primary objectives and we will continue to focus on this. Diversity is a fundamental element of the succession planning process and remains an area of focus.

### Membership and attendance during the year

Member	Attendance
Mark Elliott (Committee Chair)	4/4
Admiral Sir James Burnell-Nugent	4/4
Noreen Doyle <sup>~</sup>	1/1
Michael Harper	4/4
Ian Mason <sup>#</sup>	3/3
David Mellors <sup>&lt;</sup>	2/2
Paul Murray	4/4
Susan Searle	4/4
Leo Quinn <sup>&gt;</sup>	1/2
Steve Wadey*	N/A

<sup>~</sup> Noreen Doyle retired as a Director on 22 July 2014.

<sup>#</sup> Ian Mason was appointed as a Director on 3 June 2014.

<sup><</sup> David Mellors was interim CEO during the period from 1 January 2015 to 26 April 2015 and attended meetings in that capacity.

<sup>></sup> Leo Quinn ceased to be a Director on 31 December 2014.

\* Steve Wadey became a member of the Committee in April 2015 and will attend future meetings.

### Main responsibilities

The role of the Committee is to ensure that the composition of the Board and Committees has the optimum balance of skills, knowledge and experience, and to oversee succession planning for the Board and senior management. It considers diversity, including skills mix, international industry experience and gender, when seeking to appoint a new Director to the Board. The Committee meets as necessary and when called by its Chair. During the financial year ended 31 March 2015, the Committee met on four occasions.

### Overview

Key areas of focus during the year were:

- a) Succession planning at Non-executive Director level.
- b) Succession planning at Executive Director level including the review and preparation of a memorandum setting out the role and capabilities required for a new CEO to lead the organisation through the next phase in its development.
- c) Succession planning at senior management level.

### a) Appointment of Non-executive Directors

In 2014, to ensure the alignment of Board skills with the needs of the Group's strategy, the Committee had agreed to focus on the search in the UK for potential Non-executive Director candidates, which was being undertaken by the Zygos Partnership. The firm is a signatory to the Voluntary Code of Conduct for Executive Search Firms, which requires them to ensure that at least 30% of the candidates are women, and it has no other connections with the Company. This led to the appointment of Susan Searle in March 2014. A further Non-executive Director was sought, again with assistance from the Zygos Partnership, and we were delighted to appoint Ian Mason as an additional Non-executive Director in June 2014. Details of the background and experience for both Susan and Ian can be found on page 59. Susan brings wide experience of the new technologies sector and Ian brings experience of business transformation, eCommerce and international development.

### b) Appointment of CEO

In October 2015, we announced the resignation of Leo Quinn as CEO and began the search for a new CEO. As part of this process, the Chairman and the Investor Relations Director engaged with and met top shareholders. JCA Group was appointed to carry out the recruitment. The firm is a signatory to the Voluntary Code of Conduct for Executive Search Firms and it has no other connection with the Company. The Chairman worked with investors, the Board, senior management and JCA Group to identify the qualities which would be required in a new CEO to take the Company forwards. The general theme that emerged was that the Company required an accomplished leader with the character, drive and skills to lead the business through its growth agenda in challenging market conditions. The search resulted in the appointment of Steve Wadey, which was announced in January 2015, and he joined the Company as CEO on 27 April 2015.

### c) Senior management succession planning

The Committee continues to maintain oversight of the processes for ensuring that succession plans are in place for the top layer of management, with a focus on improving the talent pipeline and diversity. This process includes ensuring that the Board as a whole meets with senior management, that remuneration policy and long-term incentives for senior management are reviewed by the Remuneration Committee and that the Chairman works with the CEO to review succession planning and to ensure the right mix of skills and experience at OpCo level. At the executive level, the Capability Director works with the Governance Committee to ensure that succession plans for the top layer of management are in place and this is reported to the Risk & CSR Committee by the CEO.

#### Board Diversity Policy

During 2013 the Board approved a Board Diversity Policy. The key statement and objectives of that policy (the full text of which is available on the Group's website [www.QinetiQ.com/about-us/corporate-governance](http://www.QinetiQ.com/about-us/corporate-governance)) are as follows:

##### Statement:

The QinetiQ Board recognises the benefits of diversity. Diversity of skills, background, knowledge, international and industry experience, and gender, amongst many other factors, will be taken into consideration when seeking to appoint a new Director to the Board. Notwithstanding the foregoing, all Board appointments will always be made on merit.

##### Objectives:

The Board should ensure an appropriate mix of skills and experience to ensure an optimum Board and efficient stewardship.

The Board should ensure that it comprises Directors who are sufficiently experienced and independent in character and judgment.

The Board aims to increase the proportion of women on the Board to 25% by the end of 2015. Thereafter, subject always to ensuring that all Board appointments are made on merit, the Board aspires to maintain a minimum Board composition of 25% women, such percentage to be reviewed annually.

##### Progress against the policy:

The appointment of Susan Searle in March 2014 brought the proportion of women on the Board to 25%, which was in line with our objective. In July 2014, Noreen Doyle retired from the Board after over eight years in office, reducing the proportion of women Directors to 12.5%. We will aim to ensure that gender diversity will be taken into consideration for any future appointments, with the proviso that appointments will always be made on merit and will continue to take into account diversity, not only in terms of gender, but also in terms of the appropriate mix of background skills and experience.

We have issued a Company-wide diversity policy and details can be found in the Responsible business section on pages 24 to 29.

## Accountability

### Board review of the effectiveness of risk management and internal control processes

The Board confirms that it has conducted a review of the effectiveness of the Company's risk management and internal control systems in operation during the year, as required by the Code. The details of the review and its findings can be found on page 64.

### Directors' responsibilities

Statements explaining the Directors' responsibilities for preparing the Group's Annual Report and financial statements and the auditor's responsibilities for reporting on those statements are on pages 88 and 89.

### Going concern

A statement regarding the business as a going concern can be found on page 88.

### Board responsibility for risk management and internal control

The Board is ultimately responsible for the Group's system of internal control and for reviewing its effectiveness in safeguarding shareholders' interests and the Company's assets. The system is designed to manage and mitigate, rather than eliminate, the risk of failure to achieve business objectives, and, like any appropriate or proportionate system of corporate internal control, cannot provide absolute assurance against material misstatement or loss.

### Identification and review of risks

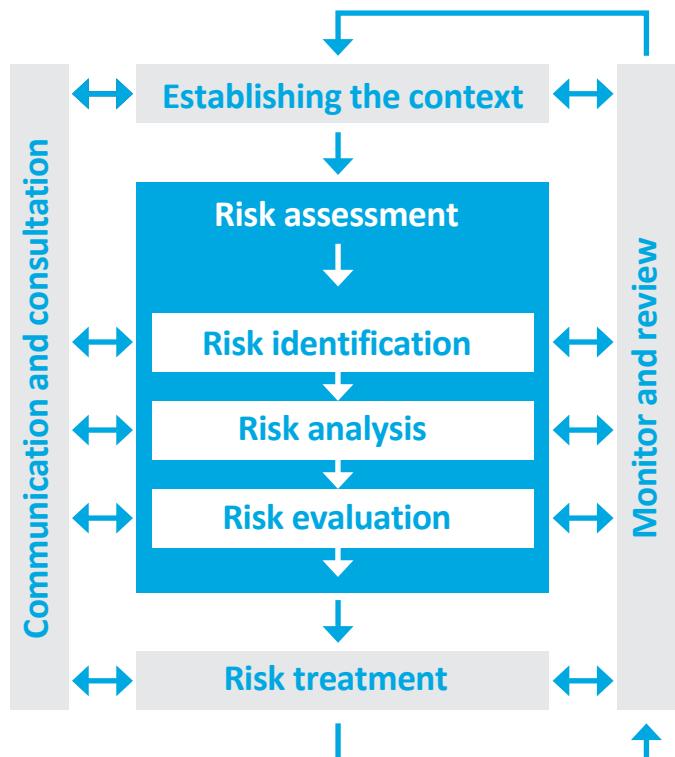
QinetiQ managers are responsible for the identification and evaluation of significant risks, both financial and non-financial, applicable to their areas of business, together with the design and operation of suitable internal controls to ensure effective mitigation. These risks, which are related to the achievement of business objectives, are assessed on a continual basis and may be associated with a variety of internal and external events, including control breakdowns, competition, disruption, regulatory requirements, and natural and other catastrophes. The Board, the Audit Committee and the Risk & CSR Committee regularly review significant risks to the business.

QinetiQ's risk management processes are defined in the Group's Operating Framework and mirror the Institute of Risk Management's guidance as detailed in the figure on page 64.

Risk reporting is embedded in the management of the business through the Operating Committee and Quarterly Business Reviews and feeds into Group strategy at the executive and Board level.

Risk assurance activity conforms to the three lines of defence model detailed on the following page and is performed by the businesses, oversight functions and Internal Audit, reporting to the Governance Committee and the Board's Audit Committee in respect of financial risks, and Risk & CSR Committee in respect of non-financial risks.

Details of key risks can be found in the Principal risks and uncertainties section of this Annual Report on pages 32 to 37.



Risk assurance activity during 2015 covered the following areas:

- Quarterly updates in respect of general risk governance from the Safety and Assurance Director.
- Quarterly reviews of divisional risk registers and moderation to form the Group Risk Register.
- Quarterly reports from the Internal Audit function in respect of the effective management of Group risks and the risk management process.
- Challenge to risk identification by business divisions and functions.
- Use of the Business Assurance Tool to manage effective internal control against regulatory and operational risks.
- Regularly requiring risk owners to report their activity to the Risk & CSR Committee (see page 70).

#### Self-certification process

An annual process of hierarchical self-certification, which provides a documented and auditable trail of accountability for the operation of the system of internal control, is in operation. This self-certification process is informed by a rigorous and structured self-assessment that addresses compliance with Group policy. It provides for successive assurances to be given at increasingly higher levels of management and, finally, to the Board.

#### Internal control

Our businesses are responsible for ensuring that a robust risk and control environment is in place as part of their day-to-day operations. Business assurance managers oversee this process and a clear set of delegated authorities is in place, covering financial and non-financial activities, and is consistent with effective operational control and risk management and the Board's risk appetite. The business is guided by two key documents which are managed by our Safety and Operational Assurance team:

- 'The Way We Work' is applicable to all staff and covers three key pillars of the way we operate: Organisation, Risk Management and Assurance, and Key Business Processes. It is underpinned by key business policies, the Operating Framework (referred to below) and our culture, values and brand; and
- The Operating Framework (Business Management System), which contains the policies, procedures and codes of practice which are expected to be complied with across the business.

The internal audit function, which is independent of the business and has a direct reporting line to the Audit Committee, provides assurance to the Board and its Committees over the effectiveness of the internal control environment. The programme of work undertaken by the internal audit function is approved in advance by the Audit Committee. It is prioritised according to risks identified by the Group through its risk management processes. Additionally, regular discussions are held between the internal audit function and the external auditor regarding internal audit reports, risks, internal audit plans and the wider control environment.

The risk management process and the system of internal control necessary to manage risks are managed by the Audit Committee (financial risks) and the Risk & CSR Committee (non-financial risks). The full Board attends these Committee meetings, either as a Committee member or a guest so as to receive at first-hand the findings of the Committee. Details of the Committee memberships are set out on page 55. The internal audit function independently reviews the risk identification and control processes implemented by management and reports to the respective Committee.

The Audit Committee and the Risk & CSR Committee also review the assurance process, ensuring that an appropriate mix of techniques is used to obtain the level of assurance required by the Board.

At its meeting in March 2015, the Board reviewed the effectiveness of the system of internal control that was in operation during the financial year ended 31 March 2015. Details of specific risk review activity undertaken during the year by the Audit and Risk & CSR Committees, together with the current risk registers, were presented by the CEO. The Board confirmed its approval that the risk review activities undertaken during the year under review, as presented by the CEO, amounted to an effective system being in place to ensure that all aspects of risk management and internal control had been considered for the year under review.

The Board also routinely challenges management to ensure that the systems of internal control are constantly improving to maintain their effectiveness. The internal control and risk management systems described above, as well as finance policy and codes of practice, apply to the Company's process of financial reporting and the preparation of consolidated accounts. A structured approach to the review and challenge of financial information is also an essential element of the process.

#### Anti-bribery and the prevention of corruption

QinetiQ has internal procedures in place that are designed to ensure compliance with the UK Bribery Act 2010, and other international regulations and best practice relating to the prevention of corruption, which are applicable to its business.

#### Whistleblowing

The Company has in place a whistleblowing process which is detailed on the Company's intranet. If an individual does not feel that they can resolve any concerns with the Company directly, either through discussions with their line manager, or directly with the Company Secretary or Group Internal Audit Manager, they can use the whistleblowing hotline – an externally provided confidential internet and telephone reporting system. All concerns are passed by the external third party to the Group Internal Audit Manager who will ensure that they are held in strict confidence and are properly investigated. Reports on whistleblowing activity and the outcome of investigations are regularly reported to the Audit Committee. The Audit Committee reviewed the effectiveness of the Group's whistleblowing process during the year.

#### Ethics

The Company provides employees with guidance to assist them in making informed ethical decisions on a day-to-day basis, including the Company's Code of Conduct, annual ethics training for all employees and links to the country risk table and review panel processes for doing business in high risk countries.

Further details regarding activity in respect of corporate responsibility, including in respect of business ethics and anti-bribery risk management, can be found in the Responsible business section on pages 24 to 29.

#### Management and control of US subsidiaries

Following the sale of the US Services division in May 2014, the US operations retained by QinetiQ (comprising 9% of the turnover of the QinetiQ Group as a whole) have been split, with the US Global Products business, trading as QinetiQ North America and comprising approximately 84% of the total US turnover at 31 March 2015, placed under a new Proxy arrangement, as detailed below, and with the remainder of the US business operating outside the Proxy regime and therefore following the same reporting lines and processes as the Group's other, non-regulated businesses.

#### US Global Products business and the Proxy arrangement

The US Global Products business, trading as QinetiQ North America, is managed via Foster-Miller, Inc. (FMI), a wholly-owned subsidiary of QinetiQ in the US. It has been placed under a Proxy arrangement as it is required by the US National Industrial Security Program to maintain facility security clearances and to be insulated from foreign ownership, control or influence. Under the new Proxy arrangement, FMI and the US Department of Defense (DoD) are parties to a Proxy agreement that regulates the management and operation of FMI. Pursuant to this Proxy agreement, QinetiQ has appointed three US citizens who hold the requisite US security clearances (Len Moodispaw, David Carey and John Currier) as Proxy holders to exercise the voting rights in FMI. The Proxy holders are also directors of FMI and, in addition to their powers as directors, have power under the Proxy arrangements to exercise all prerogatives of share ownership of FMI. The Proxy holders have a fiduciary duty, and agree, to perform their role in the best interests of QinetiQ as shareholder (including the legitimate economic interest), and in a manner consistent with the national security interests of the US. QinetiQ Group plc does not have any representation on the Board of FMI. QinetiQ Group plc may not remove the Proxy holders other than for acts of gross negligence or wilful misconduct or for breach of the Proxy agreement (and always only with the consent of the US Defense Security Service).

In terms of the power to govern, the Proxy agreement vests certain powers solely with the Proxy holders and certain powers solely with QinetiQ. For example, the Proxy holders cannot carry out any of the below without QinetiQ's express approval:

- sell or dispose of, in any manner, capital assets or the business of FMI;
- pledge, mortgage or encumber assets of FMI for purposes other than obtaining working capital or funds for capital improvements;
- merge, consolidate, reorganise or dissolve FMI; and
- file or make any petition under the federal bankruptcy laws or similar law or statute of any state or any foreign country.

Unlike minority interest holders with protective veto rights, QinetiQ can unilaterally require the above to be carried out and these are, therefore, considered to be significant participative features. In addition, QinetiQ can require the payment of dividends, and the pay-down of parent company loans, from FMI.

The Company maintains its involvement in FMI's activities through normal business activity and liaison with the Chair of the Proxy Board. FMI commercial and governance activity is included in the business update provided in the regular executive report to the Board. This activity is subject always to the confines of the Proxy regime to ensure that it meets the requirement that FMI must conduct its business affairs without external control or influence, and the requirements necessary to protect the US national security interest.

# Report of the Audit Committee

## Paul Murray

Audit Committee Chairman



The Committee focuses specifically on the effectiveness of the management of financial risks and the integrity of financial reporting. This report describes the work of the Committee in discharging its responsibilities, including:

- the significant issues considered by the Committee in relation to the preparation and reporting of the full and half-year financial statements, and how these issues were addressed;
- assessing external audit effectiveness and the approach taken for the reappointment of the external auditor;
- the review of the provision of non-audit services and safeguarding auditor independence; and
- overseeing the work of the Internal Auditor.

In last year's report, I stated that I aimed to encourage an open but challenging dialogue between the Committee, management, and internal and external auditors. This way of working continues, with reports from the executive and internal and external auditors being scrutinised and challenged where appropriate, and I intend to continue with this robust approach.

With the disposal of the US Services business, the US Group has been re-shaped and a new Proxy Board appointed to oversee the US Global Products business. We have been working with the Proxy Board and with US colleagues to achieve, where possible, consistency between the US and the UK in respect of the assessment and reporting of internal controls, risks and governance arrangements generally.

## Membership and attendance during the year

Member	Attendance
Paul Murray (Committee Chair)	5/5
Admiral Sir James Burnell-Nugent	5/5
Noreen Doyle*	2/2
Michael Harper	5/5
Ian Mason*	3/3
Susan Searle	5/5

# Noreen Doyle retired as a Director on 22 July 2014.

\* Ian Mason was appointed as a Director on 3 June 2014.

The Audit Committee is chaired by Paul Murray. The Board considers him to have recent and relevant financial experience. He was formerly Group Finance Director of Carlton Communications plc and LASMO plc, and he is currently Audit & Risk Committee Chairman at Royal Mail Group plc. The Board considers the members of the Committee to be independent. They bring extensive experience of corporate management in senior executive positions to the Company. Details of their background and experience can be found on pages 58 and 59. The CEO, CFO, Group Financial Controller, Group Internal Audit Manager and representatives of the external auditor normally attend Audit Committee meetings.

## Main responsibilities

The Audit Committee monitors the Group's integrity in financial reporting and reviews the effectiveness of the financial risk management framework. The Committee has an annual calendar of activities, in addition to which it identifies particular areas of focus during the year. The Audit Committee meets as necessary and at least four times a year. During the financial year ended 31 March 2015, the Committee met on five occasions. The external auditor has the right to request that a meeting of the Audit Committee be convened. During the past financial year, and in accordance with its terms of reference, the Committee met with each of QinetiQ's external auditor and the Group Internal Audit Manager on two separate occasions, without Executive Directors present, to discuss the audit process and assure itself regarding resourcing, auditor independence and objectivity.

## Overview

Key areas of focus during the year were:

- a) the review of the audit process for the full year and half-year results, a review of the accounting policies and an assessment of the estimates and judgments made by management;
- b) a review of the "fair, balanced and understandable" assessment of the Annual Report;
- c) a regular review of the effectiveness of internal controls including working arrangements with the US Proxy regime;
- d) a review of Group Tax policies and issues;
- e) the effectiveness of external audit, non-audit services, contractual arrangements with the external auditor and the re-tender of the external audit; and
- f) the effectiveness of governance arrangements.

Further details are set out below.

**a) Financial statements:**

The Committee reviews whether suitable accounting policies have been adopted, whether management has made appropriate estimates and judgments, and also seeks support from the external auditors to assess them. The Committee reviewed the following main issues for the periods ended 30 September 2014 and 31 March 2015:

- IFRS 10 criteria in respect of the consolidation of the US Global Products business (operating under a Proxy Board) into the Group's results;
- the basis for, and judgments made by management in determining, the liabilities recorded for litigation, onerous contracts, potential claims and other disputes;
- the provisions for income tax and deferred tax, specifically the recognition of a deferred tax asset of £25.2m in respect of UK tax losses;
- the carrying values of the Group's cash generating units (CGUs), specifically the £67.2m of goodwill associated with the US Global Products CGU. The major assumptions impacting on the NPV of future expected cash flows were also discussed. Certain discount rate assumptions and market growth forecasts are advised by external consultants;
- assumptions used to value the net pension liability of £39.4m (as advised by the Company's external actuaries); and
- the disclosures in the Preliminary Announcement and Annual Report and Accounts, in particular those relating to risk, goodwill and discontinued operations.

The review was carried out by way of papers presented by the CFO, the external auditor and the internal auditor, and through discussions with management. Based upon the business assurance process and discussions with management and the external auditors, the Committee was satisfied that the disclosures and assumptions were reasonable and appropriate for a business of the Group's size and complexity, that the auditors had fulfilled their responsibilities in scrutinising the financial statements for any material misstatements and that the disclosures were satisfactory.

**b) Assessment of the fair, balanced and understandable requirement:**

Regarding the provision of advice to the Board to meet with the requirements of the Code on whether the Annual Report and Accounts, taken as a whole, provide a fair, balanced and understandable assessment of the Company's financial position and future prospects and provide all information necessary to a shareholder to assess the Group's performance, business model and strategy, the CEO and members of management presented to the Committee details of the processes followed by management in preparing the accounts, and in particular the Committee noted:

- The Group has a clear strategy, which is presented to the Board for review each year by business leaders, with interim updates during the year.

- Quarterly business reviews are undertaken by senior management which include monitoring business progress against budget.
- Business performance is monitored by the Board as detailed on page 55.
- Key individuals from appropriate business divisions and functions contribute to, or are involved in the verification of, the content of the Annual Report.
- The Company has an Annual Report working group, comprising individuals from the Finance, Investor Relations, Assurance, HR, Group Strategy, Company Secretariat and Communications functions, which adheres to a timetable of actions for the production and review of the Annual Report.
- The Annual Report working group is aware of the fair, balanced and understandable requirements and is tasked with ensuring that the Annual Report takes account of those requirements.
- A checklist of considerations to ensure the requirements were met was completed by the working group and presented to the Committee in order to provide assurance to the Committee (and to the Board).

**c) Review of internal controls:**

The Committee monitors the effectiveness of the systems of internal control to gain assurance that an effective control framework is maintained. Reports on the effective operation of the control framework are received from management and reviewed by the Committee along with key policies and processes.

At four meetings during the year, reports on the operation of internal controls and risk management processes are also received from the internal audit function, including whistleblowing arrangements as detailed on page 65.

Particular attention is given to the timely and effective implementation of remedial actions, either identified by the business directly, or by Internal Audit. The Internal Audit risk based strategic and annual plan is presented to, and scrutinised twice a year by, the Committee to provide assurance that resources are adequate and directed towards key risk areas. The annual plan is structured to ensure that all significant financial and non-financial risks are reviewed within a rolling two-year strategic plan. In the last 12 months, the results of 20 completed internal audits were reported to the Committee, detailing all significant findings and management action taken to address the issues identified. The audits included the review of financial systems, programmes and projects, as well as the management of specific risks identified through the Group's risk management processes. Internal audit activity in the year continued to indicate that overall an effective control environment was in place with an open culture of continuous improvement being demonstrated by regular management requests for internal audits to be undertaken.

The Committee also regularly reviews the effectiveness of the financial risk management framework, including reviewing key financial risks and assessing the effectiveness of management's remedial action plans. The financial risk register is presented by management to the Committee at four meetings each year, noting (i) risks being actively managed through internal mitigation activity, including the timeframe for current mitigation to improve the risk position, (ii) risks managed at post-mitigation levels but heavily influenced by external factors and/or that require ongoing monitoring, and (iii) retired risks.

The process in respect of the US Global Products business is adjusted to take into account the Proxy arrangements referred to on page 65. The executive management function have regular contact with the Chair of the Proxy Board and with US executive management, and the Group's internal controls have been applied as far as possible within the requirements of the Proxy regime. The internal audit function continues to work closely with US management to gain assurance that an effective control environment is in place. A full external audit in respect of the US Global Products business was undertaken during the year.

The Committee confirms its view that it has received sufficient, reliable and timely information from management in the last financial year to enable it to fulfil its responsibilities.

**d) Review of Group Tax priorities and issues:**

The CEO presented a paper to update the Committee on the Group's tax priorities and issues. The Committee considered these in the light of regulatory requirements and the Group's profit mix. Among more general matters, procurement rules, R&D tax relief, the use of tax losses and the effective tax rate were discussed.

**e) External audit: Its effectiveness, the provision of non-audit services, QinetiQ provision of services to the external auditor, auditor re-appointment and the re-tender of the external audit:**

The Committee's September meeting had considered the approach for monitoring the effectiveness and independence of the external audit process in the light of the requirements of the Code and FRC guidance. At this meeting, it was agreed that an effectiveness review would be undertaken by way of questionnaire and would include collecting the views of management and employees involved in supporting the external audit work, feedback from the CFO and Group Financial Controller and an open Committee discussion without external auditors being present.

The review covered a range of topics, including:

- the audit partner and the audit team;
- the audit approach – planning and execution;
- communication with the Audit Committee;
- supporting the work of the Audit Committee;
- insights and adding value;
- independence and objectivity; and
- formal reporting.

The outcome of the review was considered at the May 2015 Committee meeting and the following were noted and reported to the Board:

- the independence and objectivity of the external auditor were strongly reaffirmed;
- the external audit process was considered to be effective and robust;
- communication with the Audit Committee was effective; and
- more regular technical and other relevant training would be provided to the Board and its Committees.

**External auditor independence: non-audit services**

At its September meeting the Committee reviewed the Company's Code of Practice relating to the principles for regulating the award of non-audit work to the external auditor and for the employment of the external auditor's staff, and considered that it remained appropriate. Details of non-audit fees are tabled at three Committee meetings each year.

In the last financial year, there have been non-audit services conducted by KPMG that exceeded £50,000 in value. These fees related predominantly to the investor perception audit referred to on pages 52 and 56 carried out by KPMG Makinson Cowell and also to the disposal of the US Services business. The Committee concluded, prior to engaging KPMG for the provision of these services, that there had not been any conflict of interest that might compromise the independence of KPMG's audit work.

The Company views it as essential that the external auditor is both independent of any conflict of interest and perceived to be so. To safeguard auditor independence and objectivity, the Company has embedded the Code of Practice which sets out the principles for regulating the award of non-audit work to the external auditor within its Operating Framework. The policy clearly articulates the non-audit services which are prohibited, the non-audit services which can be purchased and the key approval requirements for non-audit work.

In line with this policy, the Committee ensures that any other advisory and/or consulting services provided by the external auditor do not conflict with its statutory audit responsibilities and are conducted through entirely separate working teams; such advisory and/or consulting services generally only cover regulatory reporting, tax, and mergers and acquisitions work. The cost and nature of non-audit work undertaken by the auditor is regularly reviewed by the Committee during the financial year and is included at regular intervals in its annual schedule as a standing item. This process enables the Committee to take corrective action if it believes that there is a risk of the auditor's independence being undermined through the award of such work.

It is also QinetiQ's policy that no KPMG employee may be appointed to a senior position within the QinetiQ Group without the prior approval of the CFO. Any non-audit services conducted by the auditor require the consent of the CFO or the Chairman of the Audit Committee before being initiated; any services exceeding £50,000 in value require the consent of the Audit Committee as a whole.

### **Auditor re-appointment**

At its May meeting, the Committee reviewed the effectiveness and the independence of the external auditor during the year, as detailed on the previous page. The members of the Committee have declared themselves satisfied with the performance of KPMG as the Company's auditor in the last financial year and therefore the Committee has recommended to the Board that KPMG be reappointed for the financial year ending 31 March 2016.

At its meeting in March, the Committee considered the timings for the tender of the external audit.

The Company notes the provision in the UK Corporate Governance Code that FTSE 350 companies should put the external audit out to tender at least every ten years. KPMG has been the auditor of the QinetiQ Group since its formation in 2001 as the result of a competitive tender, and the Company's auditor since its incorporation in 2002. During that time, there have been periodic changes in audit partners in accordance with professional and regulatory standards to protect independence and objectivity.

A rotation of KPMG's lead audit partner was last undertaken during 2012, at which time the second audit partner was appointed since the Company's flotation in 2006.

The Company stated in the 2014 Annual Report and Accounts that it was its intention to align the process for putting the external audit contract out to tender with the conclusion in 2017 of the five-year tenure of the audit partner.

Following the approval of the EU audit regulation which takes effect in member states from June 2016, the Committee will continue to monitor developments in the implementation of this regulation in the UK and will adjust the timings for the external audit tender process where necessary.

The Committee will continue, however, with the annual review of the performance of the external auditor and act accordingly.

### **f) Governance reviews:**

The Committee's September meeting had considered the processes to be followed for the various governance reviews.

The process for the external audit review is detailed on the previous page. As regards the UK internal audit function, the Committee had agreed that there would be a self-assessment on progress being made against the internal audit continuous improvement programme which had been updated to take account of the recommendations of the Chartered Institute of Internal Auditors, following their effectiveness review of Internal Audit during 2014, together with feedback from the Company's management on their experience of internal audit.

At the Committee's March meeting, it was noted that progress had been made through the year in implementing the suggested actions, most notably the alignment of internal audit plans to strategy-related and other risks. In addition, it was agreed that consideration would be given to the secondment of talented individuals into the internal audit function as part of their career development.

The Committee also noted that the feedback from customer satisfaction questionnaires (which were issued on completion of each audit to the auditee) indicated that the service was well received within the business.

As reported on page 60, due to the change of CEO during the year, it was decided that it would not be appropriate to undertake an external review of the effectiveness of the Board and its Committees (including therefore the Audit Committee), but that an evaluation would be carried out by way of an externally provided online questionnaire tool which was circulated to Board and Committee members for completion. The Committee Chairman had evaluated the results and reported on them at the Committee's March 2015 meeting.

The questionnaire had asked the Directors to give their views on progress against the actions from the previous year's effectiveness review, the Committee's prior year performance, Committee training, an assessment of key challenges for the year ahead and the identification of future 'deep dives'.

It was noted that, following completion of the US restructuring, oversight of the US governance arrangements had been re-established with the Proxy Chair, and direct access gained into the US for the internal audit function.

The following key actions were noted from the review:

- the Committee members would seek to undertake routine, externally-sourced training to keep up to date with changes in regulation and guidance;
- the Committee would review the annual calendar of activities to ensure the most efficient and effective way to complete its oversight activities; and
- the Committee would continue to support the Remuneration Committee in assessing 'quality of earnings' decisions that drove long-term incentive and bonus outcomes.

# Report of the Risk & CSR Committee

## Admiral Sir James Burnell-Nugent

Risk & CSR Committee Chairman



I am pleased to report that, during the year, the Committee continued to carry out its core functions with the support of the executive Governance Committee in respect of risk management and oversight. The annual calendar of activity, together with the in-depth review of red risks and 'deep dives' into key risk areas, has continued to provide a firm basis on which the Committee is able to oversee the operation of the non-financial risk management processes within the Group. Regular updates from management responsible for specific areas such as sustainability or international trade, coupled with presentations from external specialists, serve to further the Committee's understanding of risks and how they are mitigated.

### Main responsibilities

The Committee has three primary functions:

- to oversee the sound operation of the Company's risk management systems;
- to monitor non-financial risk exposures, including security, trade controls, ethics, corporate social responsibility and health, safety and environment; and
- to monitor adherence to the generic compliance system.

The Committee has an annual calendar of activities and meets as necessary, although normally not less than four times a year. During the financial year ended 31 March 2015, the Committee met on four occasions.

The Governance Committee continued to report to the Risk & CSR Committee and covered areas such as the status of non-financial risks identified on the Group risk register, assurance around regulatory compliance and emerging risks.

### Membership and attendance during the year

Member	Attendance
Admiral Sir James Burnell-Nugent (Committee Chair)	4/4
Noreen Doyle <sup>#</sup>	1/2
Mark Elliott	4/4
Michael Harper	4/4
Ian Mason*	3/3
David Mellors	4/4
Paul Murray	4/4
Leo Quinn <sup>&gt;</sup>	2/3
Susan Searle	4/4
Steve Wadey <sup>~</sup>	N/A

# Noreen Doyle retired as a Director on 22 July 2014. She was unable to attend the July meeting due to a prior engagement.

\* Ian Mason was appointed as a Director on 3 June 2014.

> Leo Quinn ceased to be a Director on 31 December 2014 and was unable to attend one meeting due to a prior engagement.

~ Steve Wadey became a member of the Committee in April 2015 and will attend future meetings.

### Overview

During the year, the Committee continued to carry out its core functions by way of regular reporting in accordance with its annual calendar. The Committee continued to oversee health, safety and environment, trade controls, corporate responsibility, ethics and security through quarterly reports from the heads of those functions in the business. A summary of the key focus and activities of the health, safety and environment and ethics functions is set out in the Responsible business section on pages 24 to 29.

Key areas of focus during the year were:

- a) a review of the Group's risk management processes including working arrangements with the US Proxy regime;
- b) the operation of the generic MOD compliance system;
- c) a review of the Group Risk Register in accordance with FRC recommendations; and
- d) the effectiveness of the Committee's performance during the year.

Further details are set out below. Details of the principal risks and uncertainties can be found on pages 32 to 37 of the Strategic report.

#### a) A review of the Group's risk management processes:

The Committee receives a report at each meeting from the Safety and Assurance Director with regard to key areas of risk management activity, such as health and safety, international trade controls and Proxy regime compliance. Typically a report includes a high level summary of changes to non-financial risks, an overview of assurance and audit activity, and any other items to bring to the Committee's attention. Following the disposal of the US Services business, work has progressed to establish, where possible, a consistency of approach by the US Global Products business, as far as it is able to do so having regard to the US Proxy regime, in respect of areas such as risk appetite, the risk register and internal control, and the internal audit function is able to visit and undertake work at the business, both in respect of financial and non-financial risks.

In addition to the report from the Safety and Assurance Director, a series of 'deep dives' are scheduled for the course of each year, to facilitate an in-depth review and discussion of key risks. The following are examples of deep dive reviews carried out during the year:

- The review of emerging reputational related risks considered how these are detected and managed within the Company. The review included a presentation from the senior manager responsible, on latest thinking around reputational risk, impact on other organisations and how emerging reputational risks are currently detected and monitored.
- Continuing the focus on cyber risk, an external specialist on how boards should address cyber issues gave a presentation to the Committee on current threats and set out some of the questions which boards are facing. As a result of the presentation, a series of actions were agreed, including testing of the Company's I.T. resistance to cyber attack, metrics to measure improvement actions and a segmentation of security risks for review by the Governance Committee prior to agreeing a risk appetite for each segment.

**b) Generic compliance system:**

The Committee continues to monitor the generic compliance system, which is designed to give the MOD customer confidence that QinetiQ is able to provide impartial advice during any competitive evaluation of a procurement where the Group wishes to operate on both the 'buy' and the 'supply' sides. The aim is to achieve a balance between meeting the needs of the procurement customers in the MOD (principally Defence Equipment & Support) and the need to allow QinetiQ the flexibility to exploit research into the supply chain and pursue its planned commercial activities, without compromising the defence or security interests of the UK. The Board nominates two senior executives to act as Compliance Implementation Director and Compliance Audit Director. Oversight of the operation of the system is provided by the Committee. The Committee receives a bi-annual report on the compliance areas that it monitors from the internal audit function. A typical report includes a summary of the scope and an executive summary of the findings with an audit opinion. The report includes specific findings with agreed associated time-bound action plans.

Recent activity included the adjustment of the financial reporting system to ensure that the sales lead is required to make a specific notification of the ultimate customer and the setting up and closing down of firewalls in response to changes in bid activity.

The Committee addresses any issues that would arise if QinetiQ were to fail to comply with the requirements of the generic compliance system. No breaches were noted during the year.

**c) A review of the risk register in accordance with FRC recommendations:**

The review of the Risk Register is a standing item on the Committee's agenda, with amendments being made to reflect changes in the Group's business and strategy. Further details can be found in the Risk management section on pages 30 to 31 of the Strategic report. 'Red' risks are made the subject of a report to the Committee or become the subject of a 'deep dive' review as part of the Company's risk management processes.

**d) Effectiveness review:**

As reported on page 60, due to the change of CEO during the year, it was decided that it would not be appropriate to undertake an external review of the effectiveness of the Committee itself, but that an evaluation would be carried out by way of an externally provided online questionnaire tool which was circulated to Committee members and key executives for completion. The Committee Chairman had reviewed the responses and reported on them at the Committee's May 2015 meeting.

The review noted that there was generally a good level of satisfaction with the work and processes of the Committee. Areas noted for improvement were:

- improved clarity and brevity in reporting to allow the Committee to focus on key issues;
- increased liaison with the US business; and
- considering risk appetite in relation to risk areas, such as cyber risk.

**Admiral Sir James Burnell-Nugent**  
Security Committee Chairman



## Report of the Security Committee

### Membership and attendance during the year

The Security Committee is chaired by Admiral Sir James Burnell-Nugent and the other Committee members during the year were Michael Harper, Ian Mason (from 3 June 2014), David Mellors, Paul Murray, Leo Quinn (until 31 December 2014) and Susan Searle. Steve Wadey became a member of the Committee on 27 April 2015.

There was no requirement for the Committee to meet during the year.

### Main responsibilities

The Committee was established in June 2009 to enable UK nationals on the Board to consider matters of a UK national security dimension that have an impact on QinetiQ's UK business.

# Report of the Remuneration Committee

## Michael Harper

Remuneration Committee Chairman



On behalf of the Board, I am pleased to present the Annual Report on Remuneration for the year ended 31 March 2015 for which we will be seeking approval at the AGM on 22 July 2015.

### Remuneration Committee membership and attendance during the year ended 31 March 2015

Michael Harper became Chair of the Committee on 22 July 2014 following the retirement of Noreen Doyle.

Member	Attendance
Michael Harper (Committee Chair)	6/6
Noreen Doyle (retired 22 July 2014)	1/2
Mark Elliott (Group Chairman)	6/6
Admiral Sir James Burnell-Nugent	6/6
Paul Murray	6/6
Susan Searle	6/6
Ian Mason (appointed 3 June 2014)	5/5

### Dear shareholder,

On the following pages you will find information on:

- the key activities and main decisions made by the Remuneration Committee (the Committee) during the year;
- the link between the Company strategy and the Remuneration Policy; and
- a summary of the Remuneration Policy.

The Annual Report on Remuneration is subject to an advisory shareholder vote at the AGM of the Company on 22 July 2015.

### Remuneration policy

Last year the Committee conducted an extensive review of the Directors' Remuneration Policy which was approved at the 2014 AGM (22 July 2014). The full Policy may be found in the Corporate Governance section on the Company's website.

As a Committee we work to ensure that the remuneration structure supports the Company strategy and aligns with the interests of shareholders so that we are able to attract, retain and motivate high calibre executives by rewarding the creation of long-term sustainable value. We are proposing no changes to the Policy at this year's AGM and so the Policy will normally next be subject to shareholder approval at the 2017 AGM.

## Activities

The Committee sets remuneration and incentives for Executive Directors and approves and monitors remuneration and incentives for senior executives of the Group. No Executive Director or employee of QinetiQ is permitted to be present or participate in the Committee's discussions about their own remuneration.

The Committee engages with investors as appropriate to ensure a meaningful dialogue and is grateful for all the support it has received from investors and their representative bodies over the course of the year.

The Committee meets as necessary. During the financial year ended 31 March 2015, it met on six occasions.

Month	Main agenda Items
May	<ul style="list-style-type: none"> <li>Annual Cash Bonus Plan results (y/e 31 March 2014)</li> <li>Operating Committee Reward structure</li> <li>Directors' Remuneration Report</li> <li>Share plan allocations and nominations</li> <li>Share plan performance and vesting</li> </ul>
July	<ul style="list-style-type: none"> <li>Bonus Banking Plan rules prior to shareholder approval</li> <li>Executive Directors' salary review</li> <li>Directors' Remuneration Report</li> <li>Committee programme for the year</li> </ul>
October	Executive Director remuneration
November	<ul style="list-style-type: none"> <li>Trends in Remuneration Policies</li> <li>Review of Executive shareholding</li> <li>Reward and retention – all employees</li> </ul>
January	Executive incentive arrangements
March	<ul style="list-style-type: none"> <li>Projected share plan vesting</li> <li>Target setting for Annual Bonus (y/e 31 March 2016)</li> <li>Directors' Remuneration Report</li> <li>Chairman's fee</li> <li>New CEO remuneration</li> <li>Review of Committee effectiveness</li> </ul>

## Link to Company strategy

Our objective is to grow the business through the Organic-Plus Strategy. Progress is measured through a range of financial and non-financial KPIs to monitor Group and divisional performance. Financial KPIs include measures such as order intake, organic sales growth, profitability and cash conversion performance; while non-financial KPIs include health and safety, productivity, customer satisfaction and employee engagement. More details are provided in the Strategic report on pages 2 to 47.

## Key decisions made during the year

Summarised below are the key decisions the Committee made during the year.

### Adjustment to Performance Conditions

Following the sale of the US Services business and resulting share buyback, the Committee worked with the Audit Committee to review the EPS performance conditions for the Performance Share Plan (PSP) and Deferred Annual Bonus (DAB) to assess their continued appropriateness.

In respect of these two events the Remuneration Committee decided to exercise its discretion to amend the EPS performance conditions as follows:

- in accordance with best practice guidance the number of shares bought under the share buyback has been added back in calculating the current year's EPS for the incentive plans, which reduced the current year's as reported EPS from 15.2p to 14.7p;
- to use only earnings reflecting continuing operations, which reduced 2012 EPS from 13.6p to 10.5p;
- to treat the accelerated interest charge for the Private Placement loan redemptions in 2012 consistently with the similar charge in 2015 which increased 2012 EPS by 2.5p from 10.5p to 13.0p;
- as a result of these adjustments the impact for the Executive Director was that, of the shares subject to the EPS performance condition due to vest in 2015, 36.97% under the PSP will vest compared with 32.84% before the adjustments, and that in either case no Deferred Annual Bonus Matching Shares would vest.

### CEO Remuneration

On Leo Quinn's resignation all his unvested performance based share awards lapsed, and David Mellors was appointed Interim CEO. We decided to increase Mr Mellors' salary to reflect his new duties. Furthermore, to ensure that Mr Mellors' remuneration was aligned to the priorities of his new role, as agreed by the Board, his annual bonus targets were amended.

### Interim CEO

The details of the Interim CEO package for David Mellors is as follows:

Element	Value	Rationale
Salary	£633,800	The salary was positioned to reflect David Mellors' wide range of responsibilities as both Interim CEO and CFO.
Annual Bonus	225% salary	No change to maximum quantum. However, the performance targets were changed so that 50% of the maximum bonus opportunity was based on role specific targets with a proportionate reduction to the financial performance conditions.
Benefits	Policy	No change from CFO package.
Pension	20% salary	No change from CFO package.
PSP	150% salary	No additional award on becoming Interim CEO.

**New CEO**

On recruitment, the agreed policy on remuneration of new Executive Directors is to pay competitively to attract the appropriate high calibre candidate to the role, following the same principles as for the current Executive Directors. The key elements of the package for Steve Wadey are set out in the following table:

Element	Value	Rationale
Salary	£560,000	The base salary will be set taking into account the responsibilities of the individual and the salaries paid to similar roles in comparable companies as per our base salary Policy. The CEO will be eligible to receive benefits in line with the Policy.
Annual Bonus	225% salary	The CEO will be eligible to participate in the Bonus Banking Plan to the declared maximum potential as set out in the Policy.
PSP	150% salary	The CEO will be eligible to participate in the PSP to the declared maximum potential (200% of salary) as set out in the Policy.
Pension	20% salary	The CEO will be eligible to receive pension benefits as set out in the Policy (maximum 25% of salary).

**Effectiveness review**

The Committee reviewed its terms of reference and evaluated the effectiveness of its performance during the year by way of an effectiveness questionnaire which was completed by Committee members. The questionnaire covered areas including culture and behaviour, oversight and key contributors.

It was noted that the Committee continued to be effective in carrying out its duties and that good progress had been made against the objectives arising from the prior year review. Key areas from the 2015 review where improvements could be made were noted as follows:

- the Committee would anticipate and consider more broadly the issues likely to impact remuneration judgments. This would involve the Committee, both its internal and external advisors, and the Executives increasing their level of engagement;
- remuneration arrangements would be refined to ensure the most advantageous use of reward as a means to drive the Company's Organic-Plus growth strategy; and
- the Committee would continue to work closely with the Audit Committee on 'quality of earnings' evaluations when deciding upon the outcomes of incentive plans.

**Conclusion**

We have provided an 'At a glance' summary immediately after this letter which summarises the Policy, how it was implemented in the year and how it is proposed to operate it for the year ending 31 March 2016.

I hope that we can rely on your vote in favour of the Annual Report on Remuneration at the AGM on 22 July 2015.

**Michael Harper**

Remuneration Committee Chairman

21 May 2015

# At a glance

## How have we performed against our corporate performance objectives?

In this section we highlight the performance and remuneration outcomes for the year ended 31 March 2015. More detail can be found in the Annual Report on Remuneration.

Bonus Banking Plan	Target performance	Stretch performance	Actual performance	% of maximum reward achieved
Underlying profit after tax <sup>(a)</sup>	£86.9m	£104.3m	£96.0m	71.38%
Underlying operating profit <sup>(a)</sup>	£105.0m	£126.0m	£111.3m	58.00%
Underlying operating cash flow <sup>(a)(b)</sup>	£72.40m	£86.9m	£134.0m	100.00%
Interim CEO Personal Objectives:				
• underlying operating profit in line with the Board's expectations;	Meet Expectations	Exceed Expectations	Exceeded Expectations	
• 'Best Companies' Employee Engagement Survey outcome;	600	610	613.5	100.00%
• Customer Satisfaction Survey – Top 3 ranking; and	80%	85%	85%	
• overall stability maintained within the Group during the period up to the new CEO's commencement date.	Meet Expectations	Exceed Expectations	Exceeded Expectations	

<sup>(a)</sup> Definition of underlying measures and performance can be found in the glossary on page 141.

<sup>(b)</sup> Adjusted to exclude LTPA and MSCA capital expenditure. An explanation of the underlying cash flow performance is given under Bonus Banking Plan on page 79.

Long-Term Incentives	Threshold performance	Stretch performance <sup>(a)</sup>	Actual performance	% of maximum reward achieved
2012 Performance Share Plan (EPS) <sup>(b)</sup>	14.2p	17.3p	14.7p	36.97%
2012 Performance Share Plan (TSR)	Median	Upper Quartile	Below Median	0.00%
2012 Deferred Annual Bonus Matching (EPS) <sup>(b)</sup>	15.9p	19.8p	14.7p	0.00%

<sup>(a)</sup> Performance Share Plan and Deferred Annual Bonus Matching use different Compound Annual Growth Rates (CAGR). Details provided on page 80.

<sup>(b)</sup> Adjusted EPS. Details provided on page 73.

## How have we performed against our corporate performance objectives?

The following tables set out:

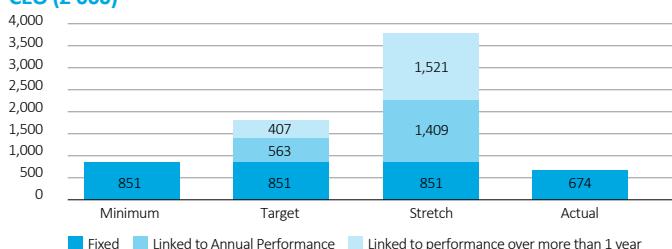
- the single figure for 2015 calculated in accordance with the regulations showing how much the Executive Directors earned in respect of 2015; and
- the single figure for 2015 compared to the Policy remuneration scenarios for 2014.

## What did our executives earn during the year?

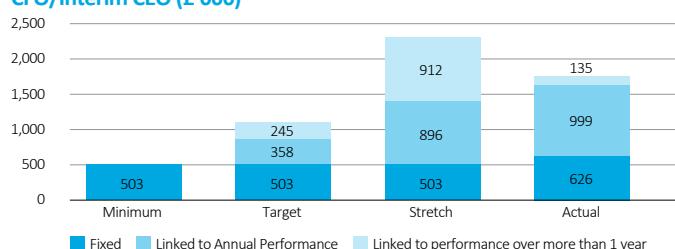
All figures in £	2015 Salary/Fee	2015 Benefits	2015 Bonus Banking Plan	2015 Long-Term Incentive	2015 Pension	2015 Total	2014 Total
CEO(a)	469,776	87,290	0	0	116,913	673,979	£2,177,742
CFO(b)	501,227	27,447	998,603	134,881	97,522	1,759,680	£1,236,601

<sup>(a)</sup> Resigned 31 December 2014. <sup>(b)</sup> Appointed Interim CEO 20 October 2014.

### CEO (£'000)

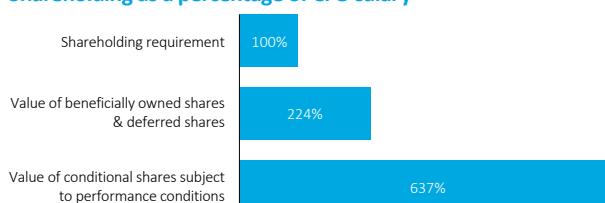


### CFO/Interim CEO (£'000)



The following chart shows the shareholding for the CFO:

### Shareholding as a percentage of CFO salary



# Policy summary

Element	Y/E 31 March 2015
<b>Salary</b> We aim to pay base salaries in line with the market median against defined comparator groups. Typically, the base salaries of Executive Directors in post at the start of the policy period and who remain in the same role throughout the policy period will be increased by a similar percentage to the average annual percentage increase in salaries of all other employees in the Group.  The exceptions to this rule may be where: <ul style="list-style-type: none"> <li>• an individual is below market level and a decision is taken to increase base pay to reflect proven competence in role; or</li> <li>• there is a material increase in scope or responsibility in the Executive Director's role.</li> </ul>	Leo Quinn (CEO) £615,325 per annum to 31 August 2014; £633,800 per annum thereafter until leaving date 31 December 2014.  David Mellors (CFO) £391,400 per annum to 31 August 2014; £403,150 per annum to 20 October 2014.  David Mellors (Interim CEO) £633,800 per annum from 20 October 2014.
<b>Benefits</b> Benefits include car allowance, health insurance, life assurance, income protection and membership of the Group's Employee Share Incentive Plan which is open to all UK employees.	Policy benefits provided during financial year.
<b>Pension</b> The Group's policy is to offer all UK employees participation in the QinetiQ Defined Contribution Group Personal Pension (GPP).  Executives whose benefits are likely to exceed the Lifetime Allowance may opt out of the GPP. In such cases, or if the Annual Allowance would be exceeded, the individual will be paid an allowance in lieu of pension contributions. This supplement will be a non-consolidated allowance and will not impact any incentive calculations.	Payment in lieu of pensions.  Leo Quinn (CEO) 25% of salary.  David Mellors (CFO & Interim CEO) 20% of salary.
<b>Bonus Banking Plan</b> As well as determining the performance conditions, targets and relative weighting, the Committee will also determine, within the approved range of 90%-135% of salary, the level of target bonus at the beginning of the plan year.  Upon assessment of performance by the Committee, a contribution will be made by the Company into the participant's plan account and 50% of the cumulative balance will be paid in cash or shares. Any remaining balance will be converted into shares.  100% of the balance in year 4 will be paid in shares to the participant. During the four-year plan period, 50% of the retained balance is at risk of forfeiture based on a minimum level of performance determined annually by the Committee.  The Committee has discretion to adjust targets in exceptional circumstances. However, where such targets are altered, the Committee will adjust the performance targets so that the revised target is not materially less challenging than the target as originally set.	Maximum Annual Opportunity 225% of salary.  Target = 90% of salary.  Threshold = 0% of salary.  Details of the performance conditions and their level of satisfaction are set out on page 79.
<b>Performance Share Plan</b> Awards are earned based on an equal weighting of absolute underlying EPS growth and relative TSR performance. The performance period runs for three years from the start of the financial year in which the award is granted.  The Committee has discretion to vary the weighting of performance metrics over the life of this Remuneration Policy to ensure alignment with business strategy. If events occur which cause the Committee to consider that the performance targets are no longer an appropriate measure of Group performance, the Committee may alter the terms of performance targets as it considers appropriate, but so that the revised target is not materially less challenging than the target as originally set.	Normal grant level = 150% of salary. Maximum grant level = 200% of salary.  The percentages of the award which vest at threshold performance are 25% for EPS growth and 30% for relative TSR rising on a linear basis to 100% vesting at stretch performance.  See page 80 of the Annual Report on Remuneration for the grants made in the year reported on.
<b>NED Fees</b> Non-executive Director fee policy aims to pay at median level, when considering the same comparator group used for Executive Directors, and increases will generally be in line with those of employees.	See page 81 of the Annual Report on Remuneration for the fees and allowances paid in the year reported on.

Y/E 31 March 2016	Notes
<p>Stephen Wadey (New CEO) £560,000 per annum appointed on 27 April 2015.</p> <p>David Mellors (Interim CEO) to 30 April 2015 £633,800 per annum.</p> <p>David Mellors (CFO) from 1 May 2015 £440,000 per annum.</p>	<p>Leo Quinn, the CEO at the beginning of the financial year, resigned on 31 December 2014. David Mellors was Interim CEO from 1 January 2015 until 26 April 2015. However, to reflect the increasing assumption of responsibilities up until his formal appointment as Interim CEO on 1 January 2015, his salary was increased from 20 October 2014.</p> <p>On 27 April 2015 a new CEO, Steve Wadey, was appointed.</p> <p>David Mellors returned to an enlarged role as CFO on 1 May 2015, taking on the operational management of Group procurement and an increased remit for Group strategy.</p>
No change.	
<p>Stephen Wadey (CEO) 20% of salary.</p> <p>David Mellors (CFO) 20% of salary.</p>	No change for year ending 31 March 2016.
<p>Maximum Annual Opportunity 225% of salary.</p> <p>Target = 112.5% of salary.</p> <p>Threshold = 0% of salary.</p> <p>Performance conditions (weighting):</p> <ul style="list-style-type: none"> <li>• Group underlying operating profit (30%).</li> <li>• Group underlying operating cash flow (30%).</li> <li>• Group underlying profit after tax (20%).</li> <li>• Qualitative measures based on Company KPIs (20%).</li> </ul>	<p>Details of specific performance targets have not been provided as they are deemed commercially sensitive.</p> <p>They will be disclosed retrospectively in next year's Annual Report on Remuneration.</p> <p>In line with best practice malus and clawback provisions are applicable.</p>
<p>CEO 150% of salary.</p> <p>CFO 150% of salary.</p> <p>Performance conditions:</p> <p>50% of the PSP award is based on EPS growth:</p> <ul style="list-style-type: none"> <li>• EPS growth of 3% p.a. 25% vesting.</li> <li>• EPS growth of 10% p.a. 100% vesting.</li> </ul> <p>50% of the PSP award is based on relative TSR compared to the FTSE 250:</p> <ul style="list-style-type: none"> <li>• 30% vesting for median.</li> <li>• 100% vesting for upper quartile.</li> </ul> <p>Straight line vesting between points.</p>	No change in operation of the PSP for year ending 31 March 2016.
<p>Basic Non-executive Director fee From 1 July 2015 £46,000.</p>	Last reviewed in 2013, increase is equivalent to 3% per annum in line with increases to employees generally.

# Annual Report on Remuneration

## Introduction

The following section of this report details how the Remuneration Policy has been implemented for the year ended 31 March 2015.

## Performance measures and targets

The performance targets are determined annually. The Committee selected the performance conditions, as detailed on the next page, for the Bonus Banking Plan because these are central to the Group's overall strategy and are the key metrics used by the Executive Directors to oversee the operation of the business.

The Committee is of the opinion that the specific performance targets for the Bonus Banking Plan are commercially sensitive in respect of the Company and that it would be detrimental to the interests of the Company to disclose them. The targets will be disclosed after the end of the relevant financial year in that year's Remuneration Report.

The Performance Share Plan performance conditions, as defined on page 80, complement the performance conditions described in the Bonus Banking Plan, supporting sustainable performance.

## Executive Director single figure remuneration

The auditors are required to report on the information in this table. Executive Director remuneration is shown as a single figure to provide an annual comparison between the actual remuneration for the performance year ended 31 March 2015 and the preceding year. The CFO figure for 2015 includes the period as Interim CEO.

Executive Director	Salary/fees <sup>(a)</sup>		Benefits <sup>(b)</sup>		Bonus Banking Plan <sup>(c)</sup>		Long-Term Incentive <sup>(d)</sup>		Pension <sup>(e)</sup>		Single figure	
	2015	2014	2015	2014	2015	2014	2015	2014	2015	2014	2015	2014
CEO <sup>(a)</sup>	£469,776	£610,844	£87,290	£59,524	£0	£710,393	£0	£644,270	£116,913	£152,711	£673,979	£2,177,742
CFO <sup>(b)</sup>	£501,227	£388,550	£27,447	£23,188	£998,603	£451,871	£134,881	£295,282	£97,522	£77,710	£1,759,680	£1,236,601

<sup>(a)</sup> Base salary is presented prior to adjustments for salary sacrifice pensions. For further details please refer to Additional supporting information for each Executive Director below.

<sup>(b)</sup> Benefits comprise car allowance, private medical insurance, life assurance and income protection. For 2015 the CEO figure includes a payment of £36,565 in lieu of untaken holiday.

<sup>(c)</sup> The Bonus Banking Plan was introduced in 2015 replacing the previous Annual Bonus scheme and Deferred Bonus arrangements. The figure provided comprises the value of both cash and deferred award. Performance measures are Group Underlying Profit After Tax, Group Underlying Operating Profit, Group Underlying Cash Flow and Personal Objectives for year ended 31 March 2015. For the year ended 31 March 2014 the Annual Bonus scheme performance measures were Group Underlying Operating Profit, Group Underlying Cash Flow, and Underlying EPS. For the performance year ended 31 March 2015 all measures exceeded target performance resulting in a payout of 88.55% of maximum bonus opportunity. Additional supporting information for each Executive Director below provides a detailed breakdown of calculations. For the performance year ended 31 March 2014 all performance measures exceeded target resulting in a payout of 76.97%.

<sup>(d)</sup> Long-Term Incentive figures for the year ending 31 March 2015 comprise the 2012 PSP and the 2012 DAB Matching Plan. For the 2012 PSP the EPS exceeded threshold performance and the TSR did not meet threshold performance resulting in a payout equivalent to 18.49% of maximum. For the 2012 DAB Matching Plan the EPS failed to meet threshold performance resulting in nil payout. Long-Term Incentives for the year ending 31 March 2014 comprise the 2011 Value Sharing Plan and the 2011 DAB Matching Plan. For the 2011 VSP only TSR exceeded target performance resulting in an overall payout equivalent to 13.80% of maximum. The EPS performance measure in the 2011 DAB Matching Plan exceeded threshold resulting in a payout equivalent to 26.47% of maximum. Additional supporting information for each Executive Director below provides a breakdown of calculations. Long-Term Incentive figures include dividend equivalent payments for both 2015 and 2014.

<sup>(e)</sup> CEO pension figure represents cash in lieu of pension equating to 25% of base salary for both performance years. For the year ending 31 March 2015 the CFO pension figure represents cash in lieu of pension equating to 20% of base salary. For year ending 31 March 2014 the CFO pension figure represents £38,344 paid into GPP and £39,366 cash in lieu of pension equating to 20% of base salary.

## Additional supporting information for each Executive Director

To support the single figure, this section documents each element of remuneration and how the figure was calculated for the performance year ended 31 March 2015.

### Base salary

Executive Director	From 20 October 2014 <sup>(a)</sup>	From 1 September 2014 <sup>(b)</sup>	From 1 July 2013	Pro-rated single figure <sup>(c)</sup>
CEO	—	633,800	615,325	469,776
CFO/Interim CEO	633,800	403,150	391,400	501,227

<sup>(a)</sup> The CEO's and CFO's salaries increased by 3% (£18,475 per annum and £11,750 per annum respectively) effective from 1 September 2014, in line with salary increases generally awarded to UK employees at that date.

<sup>(b)</sup> The CFO's salary was increased on 20 October 2014 on becoming Interim CEO.

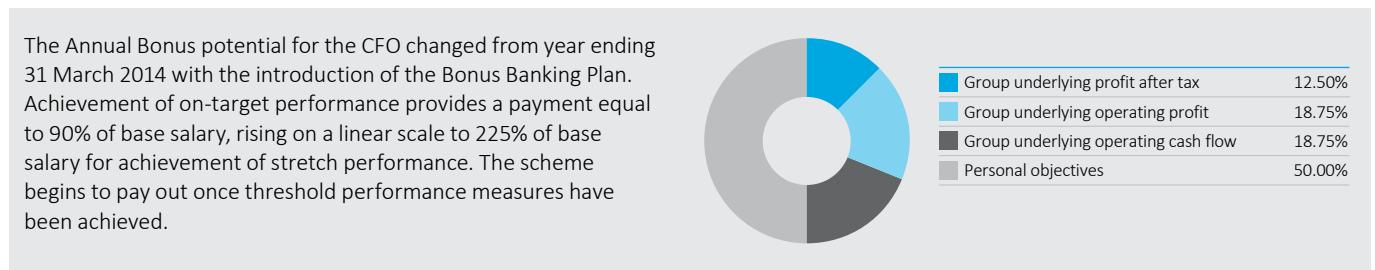
<sup>(c)</sup> 2015 pro-rata calculated on a daily basis. 2014 pro-rata calculated on a monthly basis.

### Total pension entitlements

No Directors participate in the QinetiQ Pension Scheme.

## Bonus Banking Plan

The CFO/Interim CEO was measured against the targets as shown below:



The following table details how the Remuneration Policy has been implemented and collates the Bonus Banking Plan results for the year ended 31 March 2015.

Performance measure	Threshold	Target	Stretch	Actual	% of maximum reward achieved	CFO/Interim CEO payment
Underlying profit after tax <sup>(a)</sup>	£78.2m	£86.9m	£104.3m	£96.0m	71.38%	£100,624
Underlying operating profit <sup>(a)</sup>	£94.5m	£105.0m	£126.0m	£111.3m	58.00%	£122,644
Underlying operating cash flow <sup>(a)(b)</sup>	£65.2m	£72.40m	£86.9m	£134.0m	100.00%	£211,455
Interim CEO Personal Objectives:						
• underlying operating profit in line with the Board's expectations;	N/A	Meet Expectations	Exceed Expectations	Exceeded Expectations		
• 'Best Companies' Employee Engagement Survey outcome;	593.5	600	610	613.5		
• Customer Satisfaction Survey – Top 3 ranking; and	77%	80%	85%	85%	100.00%	£563,880
• overall stability maintained within the Group during the period up to the new CEO's commencement date.	N/A	Meet Expectations	Exceed Expectations	Exceeded Expectations		
Overall Results					88.55%	£998,603
50% paid in cash					44.28%	£499,302
50% banked <sup>(c)</sup>					44.28%	£499,301

<sup>(a)</sup> Definition of underlying measurements of performance can be found in the glossary on page 141.

<sup>(b)</sup> Adjusted to exclude LTPA and MSCA capital expenditure. Operating cash flow was significantly higher than budgeted. This was partially a result of the higher operating profit but was largely due to the predicted unwind of working capital not materialising as originally expected. The latter results from favourable contract milestones and customers paying within terms ahead of the year end cut-off.

<sup>(c)</sup> Banked portion of Bonus Banking Plan held in share units.

For the year ended 31 March 2015, no discretion was applied to the calculated results; therefore, £998,603 has been reported in the single figure calculation. For the year ended 31 March 2014, financial targets were exceeded providing a payment of 76.97% of base salary for both the CEO and CFO as detailed in the single figure table (50% of which was deferred into shares, which will vest, subject to the rules, in June 2017). No discretion was applied to these payments.

## Deferred Annual Bonus

As reported in the 2012 Annual Report, the CEO and CFO deferred 50% (£362,000) and 40% (£185,000) respectively of their annual cash bonus into the DAB Plan, allocating 229,596 and 117,173 shares respectively. These shares were held in trust prior to transfer to the outgoing CEO on 5 January 2015, and will be released to the CFO on 29 June 2015. These figures are not reported in the single figure as they have been previously reported under the regulations.

### Long-Term Incentive summary

The following table details how the Remuneration Policy has been implemented and collates the Long-Term Incentive Plan results for the performance period ended 31 March 2015. Plan details are provided in the paragraphs immediately following this table. As a result of his resignation the CEO forfeited all outstanding awards, totalling 2,140,929 shares.

Plan	Conditional shares maturing	Shares vesting	Percentage shares vesting	Share value <sup>(a)</sup>	Accrued dividends <sup>(b)</sup>	Reported single figure value
CFO	2012 Performance Share Plan <sup>(c)</sup>	356,250	65,860	18.49%	126,846	8,035
	2012 Deferred Annual Bonus Matching	117,173	0	0.00%	0	0
	Total	473,423	65,860	13.91%	126,846	8,035

<sup>(a)</sup> Share price used in calculation equals £1.926. Three-month average 1 January 2015 – 31 March 2015.

<sup>(b)</sup> Cash equivalent dividends are earned during the performance period and any period when shares are held in trust.

<sup>(c)</sup> 50% of PSP shares granted are subject to the EPS performance measure, 50% are subject to the TSR performance measure.

Following the sale of the US Services business and the £150m share buyback programme the Committee reviewed the EPS performance conditions to assess their continued appropriateness. In respect of these two events the Remuneration Committee decided to exercise its discretion to amend the EPS performance conditions as follows:

- in accordance with best practice guidance the number of shares bought under the share buyback have been added back in calculating the current year's EPS for the incentive plans, which reduced the current year's as reported EPS from 15.2p to 14.7p;
- to use only earnings reflecting continuing operations, which reduced 2012 EPS from 13.6p to 10.5p; and
- to treat the accelerated interest charge for the Private Placement loan redemptions in 2012 consistently with the similar charge in 2015 which increased 2012 EPS by 2.5p from 10.5p to 13.0p.

As a result, 65,860 conditional shares will vest with a value of £126,846 using a share price of £1.926 (three-month average to 31 March 2015).

### Long-Term Incentive Plan Results

Performance measure and level	Performance Share Plan	DAB Matching
EPS Growth:		
Threshold Performance	3% (CAGR)	7% (CAGR)
Vesting at Threshold	25%	25%
Maximum Performance	10% (CAGR)	15% (CAGR)
Vesting at Maximum	100%	100%
EPS at Start of Performance Period (Adjusted)	13.0p	13.0p
EPS at Threshold Performance	14.2p	15.9p
EPS at Maximum Performance	17.3p	19.8p
Actual Performance (Adjusted)	14.7p	14.7p
Actual Vesting	36.97%	0.00%
TSR Performance:		
Threshold Performance	Median	
Vesting at Threshold	30%	
Maximum Performance	Upper Quartile	
Vesting at Maximum	100%	
Actual Performance	Below Median	
Actual Vesting	0.00%	
<b>Total PSP Vesting</b>	<b>18.49%</b>	

### Value Sharing Plan

As reported in the 2014 Annual Report, the CEO and CFO single figure value relating to the VSP was £502,682 and £251,341 respectively. The CEO forfeited all shares outstanding under this plan. For the CFO, as per scheme rules, 50% of the vested shares were deferred until 26 May 2015. These figures are not reported in the 2015 single figure as they were included in the single figure for 2014 in accordance with the regulations.

### Scheme interests awarded during the financial year ended 31 March 2015

The auditors are required to report on the information in this table. The following awards were made to Executive Directors.

Plan name	Performance measure	Grant date	Award as percentage of salary	Face value of award	Share price at date of grant	No. of shares granted	Performance period from – to	Percentage of award vesting at threshold
CFO	PSP 2014	EPS	28 May 14	75.0%	£293,550	200p	146,775	1 Apr 14 to 31 Mar 17
CFO	PSP 2014	TSR	28 May 14	75.0%	£293,550	200p	146,775	1 Apr 14 to 31 Mar 17
CFO	DAB Matching 2014 <sup>(a)</sup>	EPS	1 July 14	57.7%	£225,936	207.7p	108,779	1 Apr 14 to 31 Mar 17

<sup>(a)</sup> DAB Matching 2014 is 50% of the deferred annual bonus earned in respect of year ended 31 March 2014.

### Payments to past Directors

No payments were made to past Directors.

### Payments for loss of office

No payments were made for loss of office. Leo Quinn on his resignation from the Company was paid until his date of cessation on 31 December 2014. He received no bonus for the year ended 31 March 2015 and no payment in lieu of notice of salary or benefits other than £36,565 in lieu of untaken holiday. All matching deferred shares and performance share awards lapsed in their entirety on his cessation of employment.

### Single figure remuneration for each Non-executive Director

Non-executive Director remuneration is shown as a single figure to provide an annual comparison between the actual remuneration awarded during the performance year ended 31 March 2015 and the preceding year.

Non-executive Director	Salary/fees		Benefits		Committee Chair fees		US attendance fee		Single figure	
	2015	2014	2015	2014	2015	2014	2015	2014	2015	2014
Mark Elliott	£236,250	£228,750	£75,000	£75,000	–	–	–	–	£311,250	£303,750
Michael Harper	£43,000	£43,000	–	–	£16,549	£10,000	£2,500	£5,000	£62,049	£58,000
Paul Murray	£43,000	£43,000	–	–	£9,000	£9,000	£2,500	£5,000	£54,500	£57,000
Admiral Sir James Burnell-Nugent	£43,000	£43,000	–	–	£9,000	£1,500	–	£5,000	£52,000	£49,500
Susan Searle	£44,985	–	–	–	–	–	£2,500	–	£47,485	–
Ian Mason	£35,392	–	–	–	–	–	–	–	£35,392	–
Noreen Doyle	£13,320	£43,000	–	–	£2,880	£9,000	–	£5,000	£16,200	£57,000
Colin Balmer	–	£35,833	–	–	–	£7,500	–	£2,500	–	£45,833

Mark Elliott receives an accommodation allowance of £75,000 as he is US resident.

Susan Searle received an additional fee in April 2014 – payment for service provided in the previous financial year.

Ian Mason appointed 4 June 2014.

Noreen Doyle retired 22 July 2014. Colin Balmer retired 31 January 2014.

### Statement of Directors' shareholding and share interests

Set out below are the Directors' shareholdings as at 31 March 2015. As stated in the Remuneration Policy, the Company requires Executive Directors to hold shares equivalent to 100% of base salary.

The CFO exceeds the minimum shareholding requirement with a current holding equivalent to 224% of base salary using a share price of £1.926 (three-month average to 31 March 2015).

	Shares beneficially owned <sup>(a)</sup>	Shares subject to performance conditions <sup>(b)</sup>	Shares not subject to performance conditions <sup>(c)</sup>	Total shares held at 21 May 2015
David Mellors	33,035	1,332,948	435,996	1,801,979
Mark Elliott	125,000	–	–	125,000
Michael Harper	30,000	–	–	30,000
Paul Murray	56,077	–	–	56,077
Admiral Sir James Burnell–Nugent	11,419	–	–	11,419
Susan Searle	10,000	–	–	10,000
Ian Mason	10,000	–	–	10,000

<sup>(a)</sup> Shares beneficially owned comprise shares held under the Share Incentive Plan (including matched shares) and shares owned by the Executive Director and any connected persons.

<sup>(b)</sup> Shares subject to performance conditions comprise awards made under the DAB (matching) for 2014, 2013 and 2012, and PSP for 2014, 2013 and 2012.

<sup>(c)</sup> Shares not subject to performance conditions comprise deferred shares under the DAB plan for 2014, 2013 and 2012, and VSP 2011.

**Total scheme interests summary**

The auditors are required to report on the information in this table. Total scheme interests, including those awarded during the financial year ended 31 March 2015, are as follows.

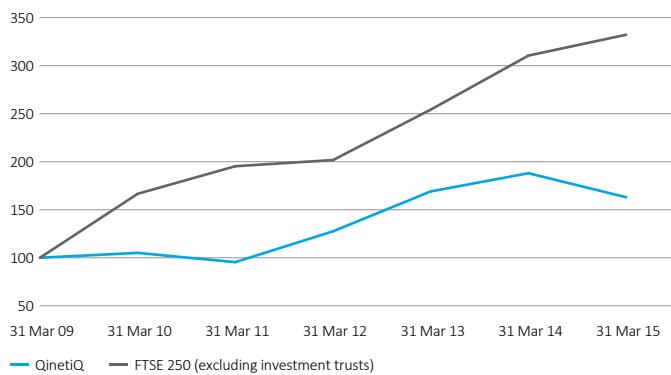
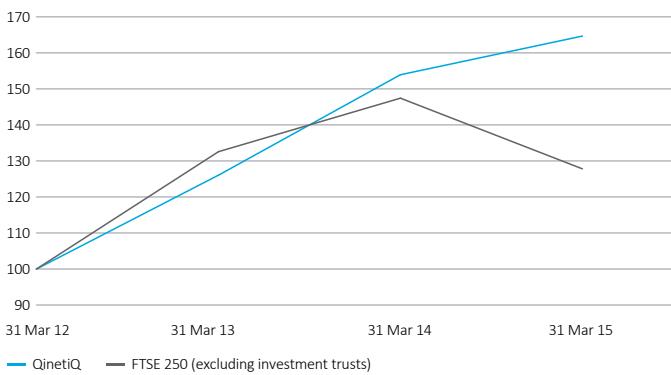
**David Mellors**

Plan name	Date of grant	Number at 1 April 2014	Granted in year (maximum potential of awards)	Exercised/ vested in year	Lapsed in year	Number at 31 March 2015	Market price on date of grant	Earliest vest date	Latest vest date
VSP 2010	29 Jul 10	154,551	–	154,551	–	–	124.9	29 Jul 13	29 Jul 13
VSP 2011	26 May 11	765,900	–	52,847	660,206	52,847	112.3	26 May 14	26 May 14
DAB Match 2011	01 Jul 11	70,379	–	18,627	51,752	–	129.1	01 Jul 14	01 Jul 14
DAB Match 2012	29 Jun 12	117,173	–	–	–	117,173	157.1	29 Jun 15	29 Jun 15
PSP 2012	09 Aug 12	356,250	–	–	–	356,250	166.0	09 Aug 15	09 Aug 15
PSP 2013	28 Jun 13	300,000	–	–	–	300,000	180.4	28 Jun 16	28 Jun 16
DAB Match 2013	28 Jun 13	157,196	–	–	–	157,196	180.4	28 Jun 16	28 Jun 16
PSP 2014	28 May 14	–	293,550	–	–	293,550	200.0	28 May 17	28 May 17
DAB Match 2014	1 Jul 14	–	108,779	–	–	108,779	207.7	28 May 17	28 May 17
		<b>1,921,449</b>	<b>402,329</b>	<b>226,025</b>	<b>711,958</b>	<b>1,385,795</b>			

The awards in the table above are subject to the performance conditions described on pages 76 to 77. The price of a QinetiQ share at 31 March 2015 was 190.9p. The highest and lowest prices of a QinetiQ share during the year ended 31 March 2015 were 229.4p and 182.1p. There have been no changes to the interests shown above between 31 March 2015 and 21 May 2015.

**Performance review**

The graph shows the Company's TSR over the period from 31 March 2009 to 31 March 2015 and 31 March 2012 to 31 March 2015 compared with the FTSE 250 (excluding investment trusts) over the same period based on spot values. The Committee has chosen to demonstrate the Company's performance against this index as it is an appropriate sector comparison within the index in which the Company is listed. This comparator group is also used to measure TSR performance in the PSP.

**Six-year Comparator Chart****Three-year Comparator Chart**

## Incentive plans

### Performance table

The table below shows the CEO's remuneration over the same performance period (1 April 2010 to 31 March 2015):

Year ended 31 March	Salary/fees	Single figure	Annual Bonus (% of maximum)	Long-Term Incentives (% of maximum vesting)
2015 <sup>(a)</sup>	469,776	673,979	0.00%	0.00%
2015 <sup>(b)</sup>	501,227	1,725,960	88.55%	13.91%
2014	610,844	2,177,742	76.97%	15.43%
2013	593,050	3,992,001	100.00%	40.27%
2012	580,000	1,495,284	100.00%	0.00%
2011	580,000	1,327,156	100.00%	0.00%
2010 <sup>(c)</sup>	217,872	886,564	0.00%	0.00%
2010 <sup>(d)</sup>	266,667	1,246,320	0.00%	0.00%

<sup>(a)</sup> Leo Quinn left the Company on 31 December 2014.

<sup>(b)</sup> David Mellors was Interim CEO from 20 October 2014.

<sup>(c)</sup> Leo Quinn joined the Company on 16 November 2009. He was awarded £600,000 in lieu of compensation for monies earned from a third party.

<sup>(d)</sup> Graham Love left the Company on 30 November 2009. His single figure comprises earnings up to and including his leaving date and incorporates compensation for loss of office and accelerated share vestings.

### Percentage change in CEO remuneration

The following table compares change in CEO remuneration with an employee comparator group (averaged per capita). For comparison purposes, Leo Quinn's figures to 31 December 2014 and David Mellor's figures for three months to 31 March 2015 have been used.

	2015	2014	% change	Comparison group <sup>(a)</sup>		
				2015	2014	% change
Base salary	627,792	610,344	2.9	38,073	36,684	3.8
Benefits	57,587	59,524	-3.3	1,193	1,036	15.2
Annual bonus	998,603	710,393	40.6	870	838	3.8

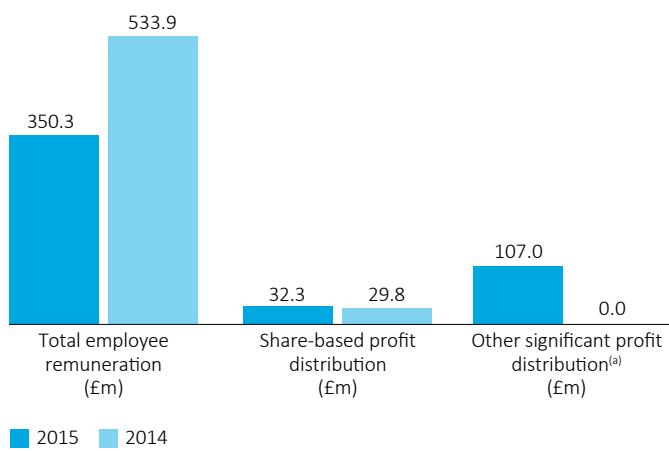
<sup>(a)</sup> The comparison group (4,000 employees) represents the UK principal businesses in service between 1 April 2014 and 31 March 2015.

### Remuneration Policy for all employees

All employees of QinetiQ are entitled to base salary, benefits and pension. UK and Australia based employees are entitled to participate in the QinetiQ Share Incentive Plan. The maximum opportunity available is based on the seniority and responsibility of the role. Participation in the PSP is available to Executive Directors; senior managers and selected employees throughout the organisation are also invited to participate. The Committee is advised of the general reward policy for other employees and of any significant changes proposed.

### Relative importance of spend on pay

The graph below shows actual spend on all employee remuneration, shareholder dividends and buybacks and any other significant use of profit and cash within the previous two financial years:



<sup>(a)</sup> For 2015 this figure relates to the share buyback resulting from sale of the US Services business.

### Implementation of Policy for the year ending 31 March 2016

#### Salary/fees

Non-executive Director fees were last increased on 1 August 2013, and the Chairman's fees were increased on 1 December 2013. Salaries and fees are reviewed in line with policy, although the Chairman requested no review of his fees on this occasion. The review of Non-executive Directors' fees resulted in an increase in base fees from £43,000 to £46,000 per annum, equivalent to an increase of 3% per annum since the last review. In March 2014, the Committee changed the Executive Directors' salary review date to 1 September in line with the rest of the employee population.

Steve Wadey, the new CEO, commenced his role on 27 April 2015. The agreed package is:

Base Salary	£560,000
Maximum Annual Bonus	225% of base salary
PSP	150%
Pension	20% allowance
Car Allowance	£19,000

Executive Directors are permitted to accept one external non-executive director position with the Board's approval. Any fees received in respect of these appointments may be retained by the Executive Director. The former CEO was a Non-executive Director of Betfair Group plc and Chairman of their Remuneration Committee. Non-executive Director fees, as reported in the Betfair Group plc Annual Report dated 30 April 2014, were £50,000 per annum plus £10,000 per annum for chairing a committee.

Neither the new CEO nor the CFO hold non-executive directorships in other companies.

Fees effective as at 1 April 2015	
Non-executive Chairman	£236,250
Accommodation allowance for Group Chairman	£75,000
Basic fee for UK Non-executive Director*	£43,000
Additional fee for chairing a Committee	£9,000
Additional fee to Deputy Chairman/Senior Independent Non-executive Director	£10,000
Additional fee for attendance at a Board meeting held in US by UK resident Non-executive Director	£2,500

\* From 1 July 2015 £46,000, being an equivalent to an increase of 3% per annum.

### Incentives for Executives

Below shows the measures and relative weighting for the 2016 Bonus Banking Plan for the CEO and CFO.

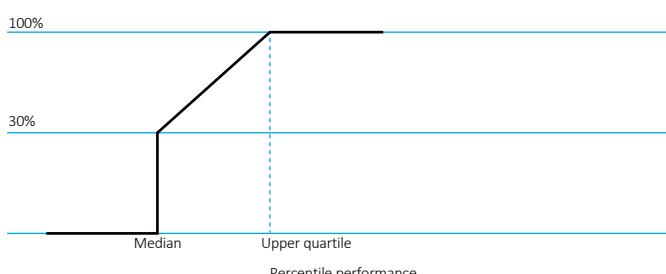
Performance Measure	Relative Weighting (%)
Group Underlying Operating Profit	30%
Bonus Banking Plan (target performance 112.5% of base salary, stretch performance 225% of base salary)	30%
Group Underlying Operating Cash Flow <sup>(a)</sup> (pre-customer capex)	20%
Group Underlying Profit After Tax	20%
Qualitative measures based on Company KPIs	20%

<sup>(a)</sup> Adjusted to exclude LTPA and MSCA capital expenditure.

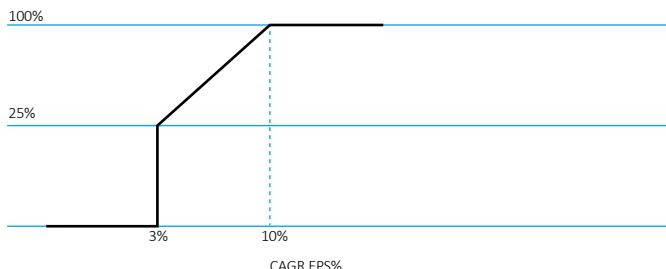
Details of specific performance targets for the Bonus Banking Plan have not been provided as they are deemed commercially sensitive. They will be disclosed retrospectively in next year's Annual Report on Remuneration.

In 2015 PSP awards to Executive Directors are equal to 150% of base salary. The graphs below show the targets against which the performance will be measured and the vesting mechanics:

#### TSR performance vs FTSE 250 (excl. investment trusts) – 50% of award



#### EPS performance – 50% of award



### Consideration by the Directors of matters relating to Directors' remuneration

Members of the Committee are appointed by the Board. The Committee comprises at least three members (not counting the Group Chairman of the Board), all of whom are independent Non-executive Directors. The Group Chairman of the Board also serves on the Committee as an additional member as he was considered independent on appointment as Chairman.

Only members of the Committee have the right to attend Committee meetings. However, other individuals such as the Chief Executive Officer, the Director of Capability, Group Reward Director and external advisors are invited to attend for all or part of any meeting, as and when appropriate.

The Board appoints the Committee Chairman who is an independent, Non-executive Director. In the absence of the Committee Chairman and/or an appointed deputy, the remaining members present shall elect one of themselves to chair the meeting who would qualify under these terms of reference to be appointed to that position by the Board. The Chairman of the Board is not permitted to be Chairman of the Committee.

The full terms of reference of the Committee can be found on the QinetiQ website ([www.QinetiQ.com](http://www.QinetiQ.com)).

The Committee has appointed PwC, an independent firm of remuneration consultants, to provide advice on market practice, corporate governance and institutional stakeholder views. Fees paid during the year for these services were £108,500 which included advice relating to the Bonus Banking Plan.

PwC provided the following additional services during the year:

- implementation support for the Company on executive reward plans;
- consultancy and advice to Group Tax, including tax support for the strategic review of the US Services division; and
- consultancy and advice in relation to Group Pensions.

The Committee is satisfied the scale and nature of this work does not impact on the objectivity and independence of the advice it receives from PwC.

The Group Chief Executive, Director of Capability and Group Reward Director also provided information and advice to the Committee.

The Chair of the Committee and the Chairman of the Board consult, from time to time, with key shareholders on significant remuneration matters. The shareholders' views are shared with the Committee to aid the Committee's decision making.

### Service contracts

Copies of Directors' service contracts and letters of appointment are available for inspection at the Company's registered office and at the AGM. Executive Directors' service agreements are of indefinite duration, terminable at any time by either party giving 12 months' prior notice.

Under each of the Executive Directors' service agreements, QinetiQ has the right to make a payment in lieu of notice of termination, being base salary and benefits that would have accrued to the Executive Director during the contractual notice period. In addition, the Committee reserves the right to allow continued participation in the annual bonus plan during the notice period provided that the individual is being required to work their notice period. It should be noted that the Company expects Executive Directors to mitigate.

Non-executives Directors' letters of appointment are renewed on a rolling 12-month basis subject to reappointment at the AGM. There are no provisions for compensation on early termination.

### Statement of voting

	Date of vote	For	%	Against	%	Abstained	% of issued share capital voted
Remuneration Policy	22 Jul 2014	422,740,088	84.66%	76,602,719	15.34%	4,877,598	76.68%
Remuneration Report from previous financial year	22 Jul 2014	498,994,031	99.42%	2,927,802	0.58%	2,298,572	77.08%

The Remuneration Report detailed on pages 72 to 85 was approved by the Board on 21 May 2015 and signed on its behalf by:

### Michael Harper

Remuneration Committee Chairman  
21 May 2015

**Statutory information contained elsewhere in the Annual Report**

Information required to be part of this Directors' report can be found elsewhere in the Annual Report as indicated in the table below and is incorporated into this report by reference:

Information	Location in Annual Report
Corporate Governance Statement	page 48
Directors' details	page 55
Directors' interests in shares	page 81
Employees	page 26
Financial instruments: Information on the Group's financial risk management objectives and policies, and its exposure to credit risk, liquidity risk, interest rate risk and foreign currency risk	page 120
Greenhouse gas emissions	page 29
Likely future developments in the business of the Company or its subsidiaries	pages 2 to 47
Results and dividends	page 45

**Management report**

The Strategic report on pages 2 to 47 and the Directors' report, as detailed on pages 86 to 89, including information which has been incorporated into those sections by reference, comprise the management report specified by rules 4.1.5R (2) and 4.1.8R of the FCA's Disclosure Rules and Transparency Rules.

**Research and development**

One of the Group's principal business streams is the provision of funded research and development (R&D) for customers. The Group also invests in the commercialisation of promising technologies across all areas of business.

The majority of R&D-related expenditure is incurred in respect of specific research contracts placed by customers. R&D costs are included within operating costs in the income statement and R&D income is reflected within revenue. In the financial year, the Group recorded £306.6m (2014: £314.6m) of total R&D-related expenditure, of which £285.8m (2014: £288.7m) was customer-funded work and £20.8m (2014: £25.9m) was internally funded (all comparative figures exclude discontinued operations). Additionally, £0.4m (2014: £2.1m) of late-stage development costs was capitalised and £0.6m (2014: £0.3m) of capitalised development costs was amortised in the year.

**Political donations**

QinetiQ does not make political donations to parties as that term would be commonly recognised. The legal definition of that term is, however, quite broad and may have the effect of covering a number of normal business activities that would not commonly be perceived to be political donations, such as sponsorship of events.

These may include legitimate interactions in making MPs and others in the political world aware of key industry issues and matters that affect QinetiQ, and that make an important contribution to their understanding of QinetiQ, the markets in which it operates and the work of their constituents.

**Branches**

The Company and its subsidiaries have established branches in a number of different countries in which they operate; their results are, however, not material to the Group's financial results.

**Share capital**

As at 31 March 2015, the Company had allotted and fully paid up share capital of 608,610,004 ordinary shares of 1p each with an aggregate nominal value of £6m (including shares held by employee share trusts) and one Special Share with a nominal value of £1.

Details of the shares in issue during the financial year are shown in note 28 on page 127.

**Share buyback**

At the general meeting of the Company held on 13 May 2014 relating to the sale of the US Services business, shareholder approval was given for the Directors to purchase ordinary shares up to 14.99% of the issued ordinary share capital. The Company resolved to use this authority to effect a £150 million return of capital to shareholders by way of an on-market share buyback, subject to prevailing equity market conditions, as this was considered to be a flexible distribution method which was simple to execute, easily understood by the market and provided shareholders with a choice as to whether to participate. During the financial year, the Company purchased 52,384,634 ordinary shares in the capital of the Company (representing 8.6% of the issued ordinary share capital as at 31 March 2015) at an average price of 203 pence per share. Since the year end, the buyback programme has continued and, as at 15 May 2015, a further 10,483,111 ordinary shares have been purchased (representing 1.72% of the issued share capital), at an average price of 202 pence per share. All of these shares have been cancelled. Subject to prevailing market conditions, it is intended that the buyback will remain ongoing until the £150 million return of capital has been achieved.

In the financial year, the impact of the share buyback has been to increase basic underlying earnings per share from 14.7p to 15.2p, for total shareholder return to remain unchanged and for net asset value to reduce by £107.1 million. In accordance with the Investment Association's guidelines, the effect of the share buyback has been neutralised in incentive schemes, such that for calculation purposes the number of shares in issue is regarded as the same at the end of the three-year performance period as at the beginning. Accordingly, no benefit has accrued under the incentive schemes as a consequence of the share buyback.

**Rights of ordinary shareholders**

The rights of ordinary shareholders are set out in the Articles of Association. The holders of ordinary shares are entitled to receive the Company's Reports and Accounts, to attend and speak at general meetings of the Company, to exercise voting rights in person or by appointing a proxy, and to receive a dividend where declared or paid out of profits available for that purpose.

**Rights of special shareholder**

The Special Share is held by HM Government through the Secretary of State for Defence (the Special Shareholder) and it may only be held by and transferred to HM Government. It confers certain rights which

are set out in the Articles of Association to protect UK defence and security interests. These include:

- the promotion and reinforcement of the MOD compliance principles which require QinetiQ to be an impartial, ethical and responsible contractor by avoiding conflicts of interest in its dealings with the MOD;
- the protection of defined strategic assets of the Group, such as certain testing facilities, by providing the Special Shareholder with an option to purchase those assets in certain circumstances;
- the right to require certain persons with a material interest in QinetiQ to dispose of some or all of their ordinary shares on the grounds of national security or conflict of interest; and
- nationality of directors provisions whereby at least the Chairman or Chief Executive must be a British citizen.

The Special Share carries no financial and economic value and the Special Shareholder is not entitled to vote at a general meeting of the Company. At any time the Special Shareholder may require QinetiQ to redeem the share at par and, if wound up, the Special Shareholder would be entitled to be repaid at its nominal value before other shareholders. Any variation of the rights attaching to the Special Share requires the written approval of the MOD. Further details can be found in note 28 on page 127.

#### Restrictions on the transfer of shares

As detailed above, the Special Share confers certain rights under the Company's Articles of Association to require certain persons with an interest in QinetiQ's shares that exceed certain prescribed thresholds to dispose of some or all of their ordinary shares on the grounds of national security or conflict of interest.

#### Employee share schemes

The QinetiQ Group plc Employee Benefit Trust (the Trust) holds shares in connection with QinetiQ's employee share schemes, excluding the Share Incentive Plan. As at 31 March 2015, the Trust held 5,139,557 ordinary shares of 1p each (the Trust Shares). The Trustees of the Trust have agreed to waive their entitlement to dividends payable on the Trust Shares. The Trust holds further ordinary shares in respect of deferred shares held on behalf of participants in the Company's Deferred Annual Bonus Plan. Dividends received by the Trust in respect of the deferred shares are paid direct to the plan participants on receipt and are not retained in the Trust.

Equiniti Share Plan Trustees Limited acts as Trustee in respect of all ordinary shares held by employees under the QinetiQ Group plc Share Incentive Plan (the Plan). As at 31 March 2015, 304,324 ordinary shares of 1p each were held in trust under the Plan. Equiniti Share Plan Trustees Limited will vote on all resolutions proposed at general meetings in accordance with voting instructions received from participants in the Plan.

#### Corporate sponsored nominee

In circumstances where ordinary shares are held by the corporate sponsored nominee service, Equiniti Corporate Nominees Limited will vote on all resolutions proposed at general meetings in accordance with voting instructions received from shareholders using such corporate nominee service.

#### Major shareholdings

The Company has been notified of the following interests of 3% or more in the issued ordinary share capital of the Company (being voting rights over such share capital) pursuant to Rule 5.1 of the Disclosure Rules and Transparency Rules:

Name of shareholder	At 31 March 2015 % of issued share capital*	At 15 May 2015* % of issued share capital*
Schroders	10.00%	11.08%
Ruane Cunniff & Goldfarb	9.71%	9.71%
Investec	5.02%	5.02%
Artisan Partners	5.01%	5.01%
Norges Bank	4.24%	3.93%

\* as notified by the shareholder.

\* being the latest practicable date prior to the issue of this report.

#### Directors' conflicts of interest

The Company requires Directors to disclose proposed outside business interests before they are entered into. This enables prior assessment of any conflict, or potential conflict, of interest and any impact on time commitment. An annual review of all external interests is carried out by the Board.

#### Directors' interests in contracts

At the date of this report, there is no contract or arrangement with the Company or any of its subsidiaries that is significant in relation to the business of the Group as a whole in which a Director of the Company is materially interested.

#### Indemnities

The Articles of Association of the Company entitle the Directors of the Company, to the extent permitted by law, to be indemnified out of the assets of the Company in the event that they suffer any expenses in connection with certain proceedings relating to the execution of their duties as Directors of the Company.

In addition, the Company purchases directors' and officers' liability insurance. Where it is not possible for directors and officers to be indemnified by the Company, such directors and officers of the Company benefit from the directors' and officers' liability insurance cover in respect of legal actions brought against them. This insurance protection is also provided to the Company and its subsidiaries where they have provided an indemnity.

The directors of QinetiQ Pension Scheme Trustee Limited, a Group company and the Trustee of the QinetiQ Pension Scheme (the Scheme), benefit from an indemnity contained in the rules of the Scheme. The indemnity would be provided out of the Scheme assets.

#### Articles of Association

Changes to the Articles must be submitted to shareholders for approval. Save in respect of the rights attaching to the Special Share, the Company has not adopted any special rules relating to the appointment and replacement of Directors or the amendment of the Company's Articles of Association, other than as provided under UK corporate law.

### Appointment and replacement of Directors

According to the Articles of Association, all Directors are subject to election by shareholders at the first annual general meeting following their appointment, and to re-election thereafter at intervals of no more than three years. In line with best practice reflected in the Code, however, the Company requires each serving member of the Board to be put forward for election or re-election on an annual basis at each annual general meeting.

### Powers of the Directors: allotment/purchase of own shares

As noted on page 86, at the general meeting of the Company held on 13 May 2014, shareholder approval was given for the Directors to purchase ordinary shares up to 14.99% of the issued ordinary share capital. The Company has used this authority to effect a £150m return of capital to shareholders by way of an on-market share buyback, subject to prevailing equity market conditions.

At the Company's Annual General Meeting held in July 2014, the shareholders passed resolutions which authorised the Directors to allot relevant securities up to an aggregate nominal value of £4,403,174 (£2,197,537 pursuant only to a rights issue) and to disapply pre-emption rights (up to 5% of the issued ordinary share capital).

Resolutions in respect of the allotment of relevant securities, the disapplication of pre-exemption rights and the purchase of own shares will be laid before the 2015 Annual General Meeting.

### Change of control – significant agreements

The following significant agreements contain provisions entitling the counterparties to require prior approval, exercise termination, alteration or other similar rights in the event of a change of control of the Company, or if the Company ceases to be a UK company:

- The Combined Aerial Target Service contract is a 20-year contract awarded to QinetiQ by the MOD on 14 December 2006. The terms of this contract require QinetiQ Limited to remain a UK company which is incorporated under the laws of any part of the UK, or an overseas company registered in the UK, and that at least 50% of the Board of Directors are UK nationals. The terms also contain change of control conditions and restricted share transfer conditions which require prior approval from HM Government if there is a material change in the ownership of QinetiQ Limited's share capital, unless the change relates to shares listed on a regulated market – 'material' is defined as being 10% or more of the share capital. In addition, there are restrictions on transfers of shares to persons from countries appearing on the restricted list as issued by HM Government.
- The Long Term Partnering Agreement (LTPA) is a 25-year contract, which QinetiQ Limited signed on 28 February 2003, to provide test, evaluation and training services to the MOD. This contract contains conditions under which the prior approval of HM Government is required if the contractor, QinetiQ Limited, ceases to be a subsidiary of the QinetiQ Group, except where such change in control is permitted under the shareholders Agreement to which the MOD is a party.

During the year under review, the Company re-financed its multi-currency revolving credit facility and entered into a new five-year facility, with a US\$100m tranche and a £166m tranche, provided by a consortium of banks, that expires on 29 August 2019. Under the terms of the facility, in the event of a change of control of the Company, any lender may give notice to cancel its commitment under the facility and require all outstanding amounts to be repaid.

The Directors' contracts contain no provisions for compensation for loss of office on a change of control of the Company.

### Annual General Meeting

The Company's Annual General Meeting will be held on Wednesday, 22 July 2015 at 11.00am, at Pennyhill Park Hotel, London Road, Bagshot, Surrey, GU19 5EU. Details of the business to be proposed and voted on at the meeting are contained in the Notice of Annual General Meeting, which is sent to all shareholders and is also published on the Company's website, [www.QinetiQ.com](http://www.QinetiQ.com) in the 'Investors' section.

### Auditor

KPMG LLP has expressed its willingness to continue in office as auditor and a resolution to re-appoint them will be proposed at the Annual General Meeting.

### Going concern

The Group's activities, combined with the factors that are likely to affect its future development and performance, are set out on pages 2 to 47. The Chief Financial Officer's review on pages 44 to 47 sets out details of the financial position of the Group, the cash flows, committed borrowing facilities, liquidity, and the Group's policies and processes for managing its capital and financial risks.

Note 26 on page 120 to the financial statements also provides details of the Group's hedging activities, financial instruments, and its exposure to liquidity and credit risk. The market conditions in which the Group operates have been, and are expected to continue to be, challenging as spending from the Group's key customers in its primary markets in the UK and the US remains under pressure. Despite these challenges, the Directors believe that the Group is well positioned to manage its overall business risks successfully. After making the appropriate enquiries, including a review of the latest two-year budget, the Directors have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. Consequently, the Annual Report and Accounts have been prepared on a going concern basis.

### Directors' responsibilities in respect of the Annual Report and 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 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 and applicable law (UK Generally Accepted Accounting Practice).

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 judgments 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; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group and the parent company will continue in business.

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 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.

#### **Statement of disclosure of information to the auditor**

The Directors who held office at the date of approval of this Directors' report have confirmed that, so far as the Directors are aware, there is no relevant audit information of which the Company's auditor is unaware; and the Directors have taken all the steps they reasonably should have taken as Directors to make themselves aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

#### **Responsibility statement of the Directors in respect of the Annual Report**

The Directors in office as at the date of this report confirm that to the best of their 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 Directors' report includes a fair review of the development and performance of the business, and the position of the Company and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

In addition, all Directors consider that the Annual Report, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Company's performance, business model and strategy. In this context, the coordination and review of the Group-wide input into the Annual Report is a vital part of the control process upon which the Directors rely and is an exercise which spans a period wider than the timetable for compiling the Annual Report itself. Critically these processes include the controls the business operates throughout the year to identify key financial and operational issues. Further details can be found in the report of the Audit Committee on pages 66 to 69 of the Corporate Governance Statement.

By order of the Board

#### **Jon Messent**

Company Secretary

Cody Technology Park  
Ively Road  
Farnborough  
Hampshire  
GU14 0LX

21 May 2015

## Opinions and conclusions arising from our audit

### 1. Our opinion on the financial statements is unmodified

We have audited the financial statements of QinetiQ Group plc for the year ended 31 March 2015 which comprise the Consolidated Income Statement, the Consolidated Statement of Comprehensive Income, the Consolidated Statement of Changes in Equity, the Consolidated Statement of Financial Position, the Consolidated Statement of Cash Flows, the parent company Balance Sheet and the related notes. 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 March 2015 and of the Group's profit 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 (IFRSs as adopted by the EU);
- the parent company financial statements have been properly prepared in accordance with UK Accounting Standards; 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.

### 2. Our assessment of risks of material misstatement

In arriving at our audit opinion above on the financial statements, the risks of material misstatement that had the greatest effect on our audit were as follows:

#### • Carrying value of US Global Products goodwill – £67.2 million

Refer to page 67 (Report of the Audit Committee), page 99 (accounting policy note) and page 112 (financial disclosures).

The risk: The carrying value of goodwill associated with the US Global Products business was written down to its recoverable amount in the year ended 31 March 2014 based on its discounted projected cash flows. As a result, any deterioration in these projections or an increase in the discount rate applied will result in a further write down being required. The carrying value of the US Global Products goodwill has been re-assessed in 2015 also based on the discounted projected cash flows of this business, which are inherently uncertain due to its lumpy revenue profile. In addition, there has been a reduction in demand for certain of this business' conflict related products and, whilst the projections anticipate that this will be offset partially by new revenue streams, the latter may not be realised in full or in the timeframe envisaged. This continues therefore to be an area of audit focus.

Our response: Our audit procedures included, among others, testing the principles and mathematical integrity of the Group's discounted cash flow model, comparing the Group's assumptions to externally derived data such as projected economic growth and discount rates, involving our own specialists as we considered appropriate and challenging the cash flow projections. We tested the sensitivity of the impairment calculation to changes in the judgments and assumptions used by the Directors. We also assessed whether the Group's disclosures about the sensitivity of the outcome of the impairment assessment to changes in key assumptions properly reflected the risks inherent in the valuation of goodwill.

#### • Recognition of revenues and profits on long-term contracts – £685.1 million

Refer to page 67 (Report of the Audit Committee), page 97 (accounting policy note) and page 103 (financial disclosures).

The risk: A significant proportion of the Group's revenues and profits are derived from long-term contracts. These contracts can include complex technological and commercial risks and often specify performance milestones to be achieved throughout the contract period. This results in estimates and assumptions having to be made to forecast the margin on each contract after making appropriate allowances for these technical and commercial risks related to performance milestones yet to be achieved. The risk of misstatement is that the accounting for the Group's significant contracts does not accurately reflect the status and the associated cost to complete of the relevant contract.

Our response: Our audit procedures included, amongst others, testing the design and operating effectiveness of controls in place to manage the commercial, technical and financial aspects of the Group's long-term contracts. For a sample of significant contracts, determined on the basis of technical and commercial complexity and profitability of the contract, we also obtained an understanding of the status of the contract through discussions with contract project teams and Directors at a Group and divisional level, attendance at project teams' contract review meetings, and examining externally available evidence, such as customer correspondence. We examined the assumptions behind estimated costs to complete, challenging the reasonableness of these in light of supporting evidence including past experience of the contracts and the extent of technical or commercial risk identified. We also assessed whether the Group's disclosures (see notes 2 and 32) in respect of the analysis of revenue and material contingent liabilities properly reflected the evidence obtained.

#### • Provisions and contingent liabilities – £25.4 million

Refer to page 67 (Report of the Audit Committee), page 100 (accounting policy note) and pages 117 and 135 (financial disclosures).

The risk: The Group operates in regulated environments and a failure to comply with particular regulations could result in fines and/or penalties. There is judgment required in determining the significance of any instances of potential non-compliance and, where appropriate, the extent of any potential liability. The Group holds provisions in respect of warranty claims and indemnities and environmental issues. The financial statements also disclose contingent liabilities in respect of legal claims and environmental issues which have not been provided for on the basis that they are not considered to qualify for recognition as provisions. This is one of our key areas of audit focus.

Our response: Our audit procedures included, among others, a critical assessment of the extent to which the Directors' estimates take into account a balanced assessment of the latest available information and the accuracy and reliability of the sources of that information. We corroborated the appropriateness of the assumptions by reference to third party confirmations and legal advice, where available, and considered whether our understanding of the business gained throughout the audit process corroborated the provisions recorded.

We considered the adequacy of the Group's disclosures in respect of provisions and contingent liabilities.

- **Tax liabilities – current tax payable £15.3 million, deferred tax asset £12.9 million**

Refer to page 67 (Report of the Audit Committee), page 98 (accounting policy note) and pages 109 and 115 (financial disclosures).

The risk: The Group is subject to income taxes in UK, USA and a number of other overseas jurisdictions. The level of current tax and deferred tax recognised requires judgments as to the likely outcome of decisions to be made by the tax authorities, including those related to specific tax allowances such as the UK Research and Development tax credit. There is a risk that the judgments on which the provisions are based do not take into account or do not properly reflect the latest available, reliable information or an appropriate application of relevant tax legislation, and are either under or overstated as a result. In addition, a deferred tax asset of £25 million in respect of brought forward un-utilised losses has been recognised in 2015. The timing of recognition of brought forward tax losses requires judgment in determining whether there will be sufficient future taxable profits against which they will be recoverable and there is a risk that the anticipated taxable profit will not be realised.

Our response: Our audit procedures included, among others, challenging the appropriateness of the Directors' assumptions and estimates in relation to tax assets and liabilities, by critically assessing the range of possible amounts that may be assessed under tax laws, likely settlements based on the latest correspondence with the relevant tax authorities and the complexity of the relevant tax legislation. We involved our tax specialist in analysing and challenging the assumptions used to determine tax provisions and the recoverability of tax assets based on our knowledge and experience of the application of the legislation by the relevant authorities and courts. We also assessed whether the Group's tax disclosures (see note 18) are appropriate and in accordance with relevant accounting standards.

- **Consolidation of US subsidiaries**

Refer to page 67 (Report of the Audit Committee) and page 97 (accounting policy note).

The risk: As detailed on page 65 concerning 'Management and control of US subsidiaries', the Group's holding of its US Global Products business (FMI) assets is regulated by a Proxy agreement, whose purpose is to insulate FMI from undue foreign ownership control or influence, the effects of which have to be considered when assessing whether it should be consolidated in accordance with the requirements of the relevant accounting standard. Judgment is required in assessing whether the Proxy agreement restricts the Group's ability to control FMI's operating and financial policies to an extent that it would be inappropriate to consolidate it and, if so, what the alternative accounting treatment should be.

Our response: Our audit procedures included, among others, challenging the appropriateness of the Directors' judgment, by critically assessing the available evidence as to the operation of the proxy agreement in the context of the relevant accounting standard. We reviewed the relevant documentation including the Proxy agreement to assess the respective rights of the QinetiQ and the Proxy Board's practical ability to direct the relevant activities of FMI's financial and operating policies. We also assessed whether the Group's disclosures are appropriate and in accordance with relevant accounting standards.

### 3. 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 £5.3 million, determined with reference to a benchmark of Group profit before taxation, normalised to exclude this year's specific adjusting items as disclosed in note 4, of £107.8 million, of which it represents 4.9%.

We report to the Audit Committee any corrected and uncorrected misstatements exceeding £0.3 million, in addition to other identified misstatements that warranted reporting on qualitative grounds.

For Group reporting purposes, we have performed an audit of QinetiQ Limited, the main UK trading company, and audits of account balances in respect of the US Global Products business including covering revenue, current assets and current liabilities. The components within the scope of our work accounted for the following percentages of the Group's results: 87% of total Group revenue; 93% of the total profits and losses that made up the Group's underlying profit before taxation; and 87% of total Group assets, of which the coverage attributable to QinetiQ Limited was 81%, 92% and 70% respectively. For the remaining components, we performed analysis at an aggregate Group level to re-examine our assessment that there were no significant risks of material misstatement within these.

The Group audit team instructed component auditors as to the significant areas to be covered, including the relevant risks detailed above and the information to be reported back. The Group audit team approved the component materialities, which ranged from £0.7 million to £4.3 million, having regard to the mix of size and risk profile of the Group across the components. The work on the US Global Products business was performed by component auditors and the rest by the Group audit team.

The Group audit team visited the US Global Products business, including to assess the audit risk and strategy. Telephone conference meetings were also held with the component auditor at this location. At this visit and in these meetings, the findings reported to the Group audit team were discussed in more detail, and any further work required by the Group audit team was then performed by the component auditor.

**4. Our opinion on other matters prescribed by the Companies Act 2006 is unmodified**

In our opinion:

- the part of the Directors' remuneration report to be audited has been properly prepared in accordance with the Companies Act 2006; and
- the information given in the Strategic report and Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

**5. We have nothing to report in respect of the matters on which we are required to report by exception**

Under ISAs (UK and Ireland) we are required to report to you if, based on the knowledge we acquired during our audit, we have identified other information in the Annual Report that contains a material inconsistency with either that knowledge or the financial statements, a material misstatement of fact, or that is otherwise misleading.

In particular, we are required to report to you if:

- we have identified material inconsistencies between the knowledge we acquired during our 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 performance, business model and strategy; or
- the Audit Committee Report does not appropriately address matters communicated by us to the Audit Committee

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.

Under the Listing Rules we are required to review:

- the Directors' statement, set out on page 88, in relation to going concern; and
- the part of the Corporate Governance Statement on pages 48 to 71 relating to the Company's compliance with the ten provisions of the 2012 UK Corporate Governance Code specified for our review.

We have nothing to report in respect of the above responsibilities.

**Scope of report and responsibilities**

As explained more fully in the Directors' Responsibilities Statement set out on pages 88 to 89, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. A description of the scope of an audit of accounts is provided on the Financial Reporting Council's website at [www.frc.org.uk/auditscopeukprivate](http://www.frc.org.uk/auditscopeukprivate). This report is made solely to the Company's members as a body and subject to important explanations and disclaimers regarding our responsibilities, published on our website at [www.kpmg.com/uk/auditscopeukco2014a](http://www.kpmg.com/uk/auditscopeukco2014a), which are incorporated into this report as if set out in full and should be read to provide an understanding of the purpose of this report, the work we have undertaken and the basis of our opinions.

**Anthony Sykes (Senior Statutory Auditor)**

for and on behalf of KPMG LLP, Statutory Auditor  
Chartered Accountants  
15 Canada Square  
London, E14 5GL

21 May 2015

# Consolidated income statement

for the year ended 31 March

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all figures in £ million	Note	2015			2014^		
		Underlying	Specific adjusting items*	Total	Underlying	Specific adjusting items*	Total
<b>Revenue</b>	2, 3	<b>763.8</b>	–	<b>763.8</b>	782.6	–	782.6
Operating costs excluding depreciation, amortisation and impairment		(636.9)	1.0	(635.9)	(653.4)	27.3	(626.1)
Other income	2	7.6	–	7.6	7.0	–	7.0
<b>EBITDA (earnings before interest, tax, depreciation and amortisation)</b>		<b>134.5</b>	<b>1.0</b>	<b>135.5</b>	136.2	27.3	163.5
Depreciation and impairment of property, plant and equipment	3, 16	(21.7)	–	(21.7)	(21.8)	1.4	(20.4)
Impairment of goodwill		–	–	–	–	(41.9)	(41.9)
Amortisation of intangible assets	3, 15	(1.5)	(2.8)	(4.3)	(0.7)	(3.4)	(4.1)
<b>Operating profit/(loss)</b>	3	<b>111.3</b>	<b>(1.8)</b>	<b>109.5</b>	113.7	(16.6)	97.1
Gain on business divestments	7	–	–	–	–	1.1	1.1
Finance income	8	1.3	–	1.3	1.9	–	1.9
Finance expense	8	(4.8)	(0.6)	(5.4)	(14.4)	(1.7)	(16.1)
<b>Profit/(loss) before tax</b>	4	<b>107.8</b>	<b>(2.4)</b>	<b>105.4</b>	101.2	(17.2)	84.0
Taxation (expense)/income	9	(11.8)	23.8	12.0	(11.4)	(4.6)	(16.0)
<b>Profit/(loss) for the year from continuing operations</b>		<b>96.0</b>	<b>21.4</b>	<b>117.4</b>	89.8	(21.8)	68.0
<b>Discontinued operations</b>							
Profit/(loss) before tax – discontinued operations		1.2	(13.7)	(12.5)	18.2	(98.1)	(79.9)
Tax in respect of discontinued operations		(0.5)	0.3	(0.2)	(4.0)	3.2	(0.8)
<b>Profit/(loss) for the year from discontinued operations</b>		<b>0.7</b>	<b>(13.4)</b>	<b>(12.7)</b>	14.2	(94.9)	(80.7)
<b>Profit/(loss) for the year attributable to equity shareholders</b>		<b>96.7</b>	<b>8.0</b>	<b>104.7</b>	104.0	(116.7)	(12.7)
<b>Earnings per share</b>							
Basic – continuing operations	13	15.2p		18.6p	13.8p		10.4p
Basic – total Group	13	15.3p		16.6p	16.0p		(1.9)p
Diluted – continuing operations	13			18.5p			10.4p
Diluted – total Group	13			16.5p			(1.9)p

\*For details of 'specific adjusting items' refer to note 4 to the financial statements.

^ Restated to reflect continuing/discontinued operations (see note 1).

## 94 | Consolidated statement of comprehensive income for the year ended 31 March

all figures in £ million	2015	2014
<b>Profit/(loss) for the year</b>	<b>104.7</b>	<b>(12.7)</b>
<i>Items that will not be reclassified to profit or loss:</i>		
Actuarial loss recognised in defined benefit pension schemes	(24.5)	(5.6)
Tax on items that will not be reclassified to profit and loss	5.1	1.3
<b>Total items that will not be reclassified to profit or loss</b>	<b>(19.4)</b>	<b>(4.3)</b>
<i>Items that may be reclassified to profit or loss:</i>		
Foreign currency translation differences for foreign operations	11.0	(21.2)
Recycling of currency translation differences to the income statement on disposal of foreign subsidiary	(40.9)	–
(Decrease)/increase in fair value of hedging derivatives	(0.1)	0.4
Reclassification of hedging derivatives to the income statement	0.1	(0.2)
Fair value gains on available-for-sale investments	0.2	0.9
Tax on items that may be reclassified to profit or loss	–	(0.1)
<b>Total items that may be reclassified to profit or loss</b>	<b>(29.7)</b>	<b>(20.2)</b>
<b>Other comprehensive expense for the year, net of tax</b>	<b>(49.1)</b>	<b>(24.5)</b>
<b>Total comprehensive income/(expense) for the year</b>	<b>55.6</b>	<b>(37.2)</b>

## Consolidated statement of changes in equity for the year ended 31 March

all figures in £ million	Issued share capital	Capital redemption reserve	Share premium	Hedge reserve	Translation reserve	Retained earnings	Total	Non-controlling interest	Total equity
<b>At 1 April 2014</b>	<b>6.6</b>	<b>39.9</b>	<b>147.6</b>	<b>0.1</b>	<b>23.1</b>	<b>160.7</b>	<b>378.0</b>	<b>0.1</b>	<b>378.1</b>
Profit for the year	–	–	–	–	–	104.7	104.7	–	104.7
Other comprehensive expense for the year, net of tax	–	–	–	–	(29.9)	(19.2)	(49.1)	–	(49.1)
Purchase of own shares	–	–	–	–	–	(0.6)	(0.6)	–	(0.6)
Purchase and cancellation of shares	(0.5)	0.5	–	–	–	(107.1)	(107.1)	–	(107.1)
Share-based payments settlement	–	–	–	–	–	0.6	0.6	–	0.6
Share-based payments	–	–	–	–	–	3.2	3.2	–	3.2
Dividends	–	–	–	–	–	(31.7)	(31.7)	–	(31.7)
<b>At 31 March 2015</b>	<b>6.1</b>	<b>40.4</b>	<b>147.6</b>	<b>0.1</b>	<b>(6.8)</b>	<b>110.6</b>	<b>298.0</b>	<b>0.1</b>	<b>298.1</b>
<b>At 1 April 2013</b>	<b>6.6</b>	<b>39.9</b>	<b>147.6</b>	<b>–</b>	<b>44.3</b>	<b>200.0</b>	<b>438.4</b>	<b>0.1</b>	<b>438.5</b>
Loss for the year	–	–	–	–	–	(12.7)	(12.7)	–	(12.7)
Other comprehensive income/(expense) for the year, net of tax	–	–	–	0.1	(21.2)	(3.4)	(24.5)	–	(24.5)
Purchase of own shares	–	–	–	–	–	(0.5)	(0.5)	–	(0.5)
Share-based payments settlement	–	–	–	–	–	0.9	0.9	–	0.9
Share-based payments	–	–	–	–	–	3.2	3.2	–	3.2
Dividends	–	–	–	–	–	(26.8)	(26.8)	–	(26.8)
<b>At 31 March 2014</b>	<b>6.6</b>	<b>39.9</b>	<b>147.6</b>	<b>0.1</b>	<b>23.1</b>	<b>160.7</b>	<b>378.0</b>	<b>0.1</b>	<b>378.1</b>

# Consolidated balance sheet

as at 31 March

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all figures in £ million	Note	2015	2014
<b>Non-current assets</b>			
Goodwill	14	107.2	141.3
Intangible assets	15	15.3	44.2
Property, plant and equipment	16	229.6	233.8
Other financial assets	24	0.9	1.5
Investments	17	0.4	0.5
Deferred tax	18	12.9	18.1
		<b>366.3</b>	<b>439.4</b>
<b>Current assets</b>			
Inventories	19	18.5	19.8
Other financial assets	24	12.3	3.1
Trade and other receivables	21	159.2	250.5
Investments	20	2.3	2.1
Cash and cash equivalents	24	184.3	322.2
		<b>376.6</b>	<b>597.7</b>
<b>Total assets</b>		<b>742.9</b>	<b>1,037.1</b>
<b>Current liabilities</b>			
Trade and other payables	22	(352.3)	(425.6)
Current tax		(15.3)	(4.6)
Provisions	23	(3.0)	(4.8)
Other financial liabilities	24	(1.9)	(2.2)
		<b>(372.5)</b>	<b>(437.2)</b>
<b>Non-current liabilities</b>			
Retirement benefit obligation	30	(39.4)	(22.2)
Deferred tax	18	-	(15.0)
Provisions	23	(22.4)	(19.3)
Other financial liabilities	24	(0.1)	(154.1)
Other payables	22	(10.4)	(11.2)
		<b>(72.3)</b>	<b>(221.8)</b>
<b>Total liabilities</b>		<b>(444.8)</b>	<b>(659.0)</b>
<b>Net assets</b>		<b>298.1</b>	<b>378.1</b>
<b>Capital and reserves</b>			
Ordinary shares	28	6.1	6.6
Capital redemption reserve		40.4	39.9
Share premium account		147.6	147.6
Hedging and translation reserve		(6.7)	23.2
Retained earnings		110.6	160.7
<b>Capital and reserves attributable to shareholders of the parent company</b>		<b>298.0</b>	<b>378.0</b>
Non-controlling interest		0.1	0.1
<b>Total shareholders' funds</b>		<b>298.1</b>	<b>378.1</b>

The financial statements were approved by the Board of Directors and authorised for issue on 21 May 2015 and were signed on its behalf by:

**Mark Elliott**  
Chairman

**Steve Wadey**  
Chief Executive Officer

**David Mellors**  
Chief Financial Officer

# 96 | Consolidated cash flow statement

## for the year ended 31 March

all figures in £ million	Note	2015	2014
<b>Net cash inflow from continuing operations before cash flows in respect of specific adjusting items<sup>^</sup></b>	27	<b>143.9</b>	<b>127.0</b>
Net cash outflow relating to restructuring		(0.6)	(10.3)
Disposal-related pension contribution		(6.0)	–
Cash generated from discontinued operations		1.8	30.3
Net cash outflow relating to pension scheme closure costs		–	(4.0)
<b>Cash inflow from operations</b>		<b>139.1</b>	<b>143.0</b>
Tax received		8.8	2.1
Interest received		1.0	1.0
Interest paid		(36.4)	(12.3)
<b>Net cash inflow from operating activities</b>		<b>112.5</b>	<b>133.8</b>
Purchases of intangible assets		(4.2)	(2.6)
Purchases of property, plant and equipment		(24.8)	(24.2)
Proceeds from sale of property, plant and equipment		–	6.0
Acquisition of business	6	(3.7)	–
Sale of investment in subsidiary		79.6	–
<b>Net cash inflow/(outflow) from investing activities</b>		<b>46.9</b>	<b>(20.8)</b>
Repayment of bank borrowings		(147.1)	–
Investment in available for sale investments		(10.0)	–
Payment of bank loan arrangement fee		(1.3)	–
Purchase of own shares		(106.8)	(0.5)
Dividends paid to shareholders		(31.7)	(26.8)
Capital element of finance lease rental payments		(2.8)	(2.8)
Capital element of finance lease rental receipts		3.0	3.0
<b>Net cash outflow from financing activities</b>		<b>(296.7)</b>	<b>(27.1)</b>
<b>(Decrease)/increase in cash and cash equivalents</b>		<b>(137.3)</b>	<b>85.9</b>
Effect of foreign exchange changes on cash and cash equivalents		0.4	(4.1)
Cash and cash equivalents at beginning of year		322.2	240.4
Cash and cash equivalents disposed		(1.0)	–
<b>Cash and cash equivalents at end of year</b>	24	<b>184.3</b>	<b>322.2</b>

<sup>^</sup> 2014 restated to reflect continuing/discontinued operations (see note 1)

## Reconciliation of movement in net cash

## for the year ended 31 March

all figures in £ million	Note	2015	2014
(Decrease)/increase in cash and cash equivalents in the year		(137.3)	85.9
Add back net cash flows not impacting net cash		158.2	(0.2)
<b>Change in net cash resulting from cash flows</b>	24	<b>20.9</b>	<b>85.7</b>
Cash and cash equivalents disposed		(1.0)	–
Other movements including foreign exchange	24	5.1	10.8
<b>Movement in net cash in the year</b>	24	<b>25.0</b>	<b>96.5</b>
Net cash at beginning of year	24	170.5	74.0
<b>Net cash at end of year</b>	24	<b>195.5</b>	<b>170.5</b>

## 1. Significant accounting policies

### Accounting policies

The following accounting policies have been applied consistently to all periods presented in dealing with items that are considered material in relation to the Group's financial statements. In the income statement, the Group presents specific adjusting items separately. In the judgment of the Directors, for the reader to obtain a proper understanding of the financial information, specific adjusting items need to be disclosed separately because of their size and nature.

Specific adjusting items include:

- amortisation of intangibles arising from acquisitions;
- pension gain on closure to future accrual and associated Scheme-closure mitigation costs;
- pension net finance expense;
- gains/losses on business divestments and disposal of investments;
- restructuring costs;
- impairment of property;
- impairment of goodwill and other intangible assets;
- tax on the above items; and
- tax credits on one-off recognition of deferred tax asset in respect of UK trade losses.

### Basis of preparation

The Group's financial statements, approved by the Directors, have been prepared on a going concern basis as discussed in the Directors' Report on page 88 and in accordance with International Financial Reporting Standards as adopted by the EU ('IFRS') and the Companies Act 2006 applicable to companies reporting under IFRS. The Company has elected to prepare its parent company financial statements in accordance with UK GAAP; these are presented on page 137. The financial statements have been prepared under the historical cost convention, as modified by the revaluation of available-for-sale financial assets and other relevant financial assets and liabilities. Non-current assets held for sale are held at the lower of carrying amount and fair value less costs to sell. The Group's reporting currency is sterling and unless otherwise stated the financial statements are rounded to the nearest £100,000.

The comparative income statement for the year ended 31 March 2014 has been re-presented for the sale of the US Services business, excluding Cyveillance®, which completed in May 2014. This disposal qualifies as a discontinued operation during the current year. Revenue as previously reported has been reduced by £408.8m and now reflects continuing operations only. Profit before tax, previously reported as a single figure of £4.1m, has been split into its component parts for continuing operations and discontinued operations. Further details of discontinued operations are presented within note 5.

### Basis of consolidation

The consolidated financial statements comprise the financial statements of the Company and its subsidiary undertakings to 31 March 2015. The purchase method of accounting has been adopted. Those subsidiary undertakings acquired or disposed of in the period are included in the consolidated income statement from the date control is obtained to the date that control is lost (usually on acquisition and disposal respectively). An investor controls an investee when it is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. This is the IFRS 10 definition of "control".

The Group comprises certain entities that are operated under the management of a Proxy Board. Details of the Proxy Board arrangements and the powers of the proxy holders and QinetiQ management are set out in the Corporate Governance section of this Annual Report. IFRS 10 is the accounting standard now applicable in respect of consolidation of entities. This does not specifically deal with proxy situations. However, having considered the terms of the Proxy agreement, the Directors consider that the Group meets the requirements of IFRS 10 in respect of control over such affected entities and, therefore, consolidates these entities in the consolidated accounts.

An associate is an undertaking over which the Group exercises significant influence, usually from 20%–50% of the equity voting rights, in respect of financial and operating policy. A joint venture is an undertaking over which the Group exercises joint control. Associates and joint ventures are accounted for using the equity method from the date of acquisition to the date of disposal. The Group's investments in associates and joint ventures are held at cost including goodwill on acquisition and any post-acquisition changes in the Group's share of the net assets of the associate less any impairment to the recoverable amount. Where an associate or joint venture has net liabilities, full provision is made for the Group's share of liabilities where there is a constructive or legal obligation to provide additional funding to the associate or joint venture.

The financial statements of subsidiaries, joint ventures and associates are adjusted where necessary to ensure compliance with Group accounting policies.

On consolidation, all intra-Group income, expenses and balances are eliminated.

### Revenue

Revenue represents the value of work performed for customers, and is measured net of value added taxes and other sales taxes on the following bases:

#### Service contracts

The Group's service contract arrangements are accounted for under IAS 18 'Revenue'. Revenue is recognised once the Group has obtained the right to consideration in exchange for its performance. No profit is recognised on contracts until the outcome of the contract can be reliably estimated. When the outcome of a contract can be reliably estimated, revenue and costs are recognised by reference to the stage of completion of the contract activity at the balance sheet date. This is normally measured by the proportion of contract costs incurred for work performed to date compared with the estimated total contract costs after making suitable allowances for technical and other risks.

## 1. Significant accounting policies continued

related to performance milestones yet to be achieved. When it is probable that total contract costs will exceed total contract revenue, the expected loss is recognised immediately as an expense. The Group generally does not undertake construction contracts.

### Goods sold

Sales of goods are recognised in the income statement on delivery of the product or when the significant risks and rewards of ownership have been transferred to the customer and revenue and costs can be reliably measured.

### Royalties and intellectual property

Royalty revenue is recognised over the period to which the royalty relates. Intellectual property revenue can be attributed either to perpetual licences or to limited licences. Limited licences are granted for a specified period and revenue is recognised over the period of the licence. Perpetual licences are granted for unlimited time frames and revenue is recognised when the risks and rewards of ownership are transferred to the customer.

### Segmental information

Segmental information is presented according to the Group's internal management reporting structure and the markets in which it operates. Segmental results represent the contribution of the different segments to the profit of the Group. Corporate expenses are allocated to the corresponding segments. Unallocated items mainly comprise specific adjusting items. Specific adjusting items are referred to in note 4. Eliminations represent inter-company trading between the different segments.

Segmental assets and liabilities information is not regularly provided to the chief operating decision maker.

### Research and development expenditure

R&D costs incurred in respect of specific contracts placed by customers are recognised within operating costs and revenue is recognised in respect of the R&D services performed. Internally funded development expenditure is capitalised in the balance sheet where there is a clearly defined project, the expenditures are separately identifiable, the project is technically and commercially feasible, all costs are recoverable by future revenue and the resources are committed to complete the project. Such capitalised costs are amortised over the forecast period of sales resulting from the development. All other R&D costs are expensed to the income statement in the period in which they are incurred. If the research phase cannot be clearly distinguished from the development phase, the respective project-related costs are treated as if they were incurred in the research phase only and expensed.

### Financing

Financing represents the financial expense on borrowings accounted for using the effective rate method and the financial income earned on funds invested. Exchange differences on financial assets and liabilities and the income or expense from interest hedging instruments that are recognised in the income statement are included within finance income and finance expense. Financing also includes the net finance expense in respect of defined benefit pension schemes.

### Taxation

The taxation charge is based on the taxable profit for the year and takes into account taxation deferred because of temporary differences between the treatment of certain items for taxation and accounting purposes. Current tax and deferred tax are charged or credited to the income statement, except where they relate to items charged or credited to equity, in which case the relevant tax is charged or credited to equity. Deferred taxation is the tax attributable to the temporary differences that appear when taxation authorities recognise and measure assets and liabilities with rules that differ from those of the consolidated financial statements. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using rates enacted or substantively enacted at the balance sheet date.

Any changes in the tax rates are recognised in the income statement unless related to items directly recognised in equity. Deferred tax liabilities are recognised on all taxable temporary differences excluding non-deductible goodwill. Deferred tax assets are recognised on all deductible temporary differences provided that it is probable that future taxable income will be available against which the asset can be utilised. Deferred tax assets and liabilities are offset only where there is a legally enforceable right to offset and there is an intention to settle balances on a net basis.

### Discontinued operation

A discontinued operation is a component of the Group's business, the operations and cash flows of which can be clearly distinguished from the rest of the Group and which:

- represents a separate major line of business or geographical area of operations;
- is part of a single coordinated plan to dispose of a separate major line of business or geographical area of operations; or
- is a subsidiary acquired exclusively with a view to re-sale.

Classification as a discontinued operation occurs at the earlier of disposal or when the operation meets the criteria to be classified as held for sale. When an operation is classified as a discontinued operation, the comparative statement of profit and loss and other comprehensive income is re-presented as if the operation had been discontinued from the start of the comparative year.

## Goodwill

Goodwill on acquisitions of subsidiaries is included in intangible assets. Goodwill on acquisitions of joint ventures and associates is included in the carrying value of equity accounted investments. Goodwill is tested annually for impairment and carried at cost less accumulated impairment losses. Gains and losses on the disposal of an entity include the carrying amount of goodwill related to the entity sold.

## Intangible assets

Intangible assets arising from business combinations are recognised at fair value and are amortised over their expected useful lives, typically between one and nine years. Internally generated intangible assets are recorded at cost, including labour, directly attributable costs and any third-party expenses. Purchased intangible assets are recognised at cost less amortisation. Intangible assets are amortised over their respective useful lives on a straight-line basis as follows:

Intellectual property rights	2–8 years
Development costs	1–4 years
Other	1–9 years

## Property, plant and equipment

Property, plant and equipment are stated at cost less depreciation. Freehold land is not depreciated. Other tangible non-current assets are depreciated on a straight-line basis over their useful economic lives to their estimated residual value as follows:

Freehold buildings	20–25 years
Leasehold land and buildings	Shorter of useful economic life and the period of the lease
Plant and machinery	3–10 years
Fixtures and fittings	5–10 years
Computers	3–5 years
Motor vehicles	3–5 years

Assets under construction are included in property, plant and equipment on the basis of expenditure incurred at the balance sheet date. In the case of assets constructed by the Group, the value includes the cost of own work completed, including directly attributable costs and interest.

The useful lives, depreciation methods and residual values applied to property, plant and equipment are reviewed annually and, if appropriate, adjusted accordingly.

## Impairment of tangible, goodwill, intangible and held for sale assets

At each reporting date the Group assesses whether there is an indication that an asset may be impaired. If the carrying amount of any asset exceeds its recoverable amount an impairment loss is recognised immediately in the income statement. In addition, goodwill is tested for impairment annually irrespective of any indication of impairment. If the carrying amount exceeds the recoverable amount, the respective asset or the assets in the cash-generating unit (CGU) are written down to their recoverable amounts. The recoverable amount of an asset or CGU is the higher of its fair value less costs to sell and its value in use. The value in use is the present value of the future cash flows expected to be derived from an asset or CGU calculated using an appropriate pre-tax discount rate. Impairment losses are expensed to the income statement.

## Investments in debt and equity securities

Investments held by the Group are classified as either a current asset or as a non-current asset and those classified as available for sale are stated at fair value, with any resultant gain or loss, other than impairment losses, being recognised directly in equity. When these investments are derecognised, the cumulative gain or loss previously recognised directly in equity is recognised in the income statement.

The fair value of quoted financial instruments is their bid price at the balance sheet date. The fair value of unquoted equity investments is based on the price of the most recent investment by the Group or a third party, if available, or derived from the present value of forecast future cash flows.

## Inventories

Inventory and work-in-progress are stated at the lower of cost and net realisable value. Work-in-progress and manufactured finished goods are valued at production cost. Production cost includes direct production costs and an appropriate proportion of production overheads. A provision is established when the net realisable value of any inventory item is lower than its cost.

## Bid costs

Costs incurred in bidding for work are normally expensed as incurred. In the case of large multi-year government contracts the bidding process typically involves a competitive bid process to determine a preferred bidder and then a further period to reach financial close with the customer. In these cases, the costs incurred after announcement of the Group achieving preferred bidder status are deferred to the balance sheet within work-in-progress. From the point financial close is reached, the costs are amortised over the life of the contract. If an opportunity for which the Group was awarded preferred bidder status fails to reach financial close, the costs deferred to that point will be expensed in the income statement immediately, when it becomes likely that financial close will not be achieved.

## 1. Significant accounting policies continued

### Trade and other receivables

Trade and other receivables are stated net of provisions for doubtful debts. Amounts recoverable on contracts are included in trade and other receivables and represent revenue recognised in excess of amounts invoiced. Payments received on account are included in trade and other payables and represent amounts invoiced in excess of revenue recognised.

### Cash and cash equivalents

Cash and cash equivalents comprise cash at bank and short-term deposits that are readily convertible into cash. In the cash flow statement overdraft balances are included in cash and equivalents.

### Current and non-current liabilities

Current liabilities include amounts due within the normal operating cycle of the Group. Interest-bearing current and non-current liabilities are initially recognised at fair value and then stated at amortised cost with any difference between the cost and redemption value being recognised in the income statement over the period of the borrowings on an effective interest rate basis. Costs associated with the arrangement of bank facilities or the issue of loans are held net of the associated liability presented in the balance sheet. Capitalised issue costs are released over the estimated life of the facility or instrument to which they relate using the effective interest rate method. If it becomes clear that the facility or instrument will be redeemed early, the amortisation of the issue costs will be accelerated.

### Provisions

A provision is recognised in the balance sheet when the Group has a present legal or constructive obligation as a result of a past event which can be reliably estimated, and it is probable that an outflow of economic benefits will be required to settle the obligation. Where appropriate, provisions are determined by discounting the expected cash flows at an appropriate discount rate reflecting the level of risk and the time value of money.

### Financial instruments

Financial assets and financial liabilities are recognised on the Group's balance sheet when the Group becomes a party to the contractual provisions of the instrument. The de-recognition of a financial instrument takes place when the Group no longer controls the contractual rights that comprise the financial instrument, when the instrument expires, or when the instrument is sold, terminated or exercised.

### Derivative financial instruments

Derivative financial instruments are initially recognised and thereafter held at fair value, being the market value for quoted instruments or valuation based on models and discounted cash flow calculations for unlisted instruments.

### Fair value hedging

Changes in the fair value of derivatives designated as fair value hedges of currency risk or interest rate risk are recognised in the income statement. The hedged item is held at fair value with respect to the hedged risk with any gain or loss recognised in the income statement.

### Cash flow hedging

Changes in the fair value of derivatives designated as a cash flow hedge that are regarded as highly effective are recognised in equity. The ineffective portion is recognised immediately in the income statement. Where a hedged item results in an asset or a liability, gains and losses previously recognised in equity are included in the cost of the asset or liability. Gains and losses previously recognised in equity are removed and recognised in the income statement at the same time as the hedged transaction.

### Leased assets

Leases are classified as finance leases when substantially all the risks and rewards of ownership are held by the lessee. Assets held under finance leases are capitalised and included in property, plant and equipment at the lower of the present value of minimum lease payments and fair value at the inception of the lease. Assets are then depreciated over the shorter of their useful economic lives or the lease term. Obligations relating to finance leases, net of finance charges arising in future periods, are included under financial liabilities.

Rentals payable under operating leases are charged to the income statement on a straight-line basis over the term of the lease.

### Foreign currencies

Transactions in foreign currencies are recorded using the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities in foreign currencies are translated at period-end rates. Any resulting exchange differences are taken to the income statement. Gains and losses on designated forward foreign exchange hedging contracts are matched against the foreign exchange movements on the underlying transaction.

The individual financial statements of each Group company are presented in its functional currency. On consolidation, assets and liabilities of overseas subsidiaries, associated undertakings and joint ventures, including any related goodwill, are translated to sterling at the rate of exchange at the balance sheet date. The results and cash flows of overseas subsidiaries, associated undertakings and joint ventures are translated to sterling using the average rates of exchange during the period. Exchange adjustments arising from the re-translation of the opening net investment and the results for the period to the period-end rate are taken directly to equity and reported in the statement of comprehensive income.

### Post-retirement benefits

The Group provides both defined contribution and defined benefit pension arrangements. The liabilities of the Group arising from defined benefit obligations, and the related current service cost, are determined using the projected unit credit method. Valuations for accounting purposes are carried out bi-annually. Actuarial advice is provided by external consultants. For the funded defined benefit

plans, the excess or deficit of the fair value of plan assets less the present value of the defined benefit obligation are recognised as an asset or a liability respectively.

For defined benefit plans, the cost charged to the income statement consists of administrative expenses and the net interest cost. There is no service cost due to the fact the plans are closed to future accrual. The finance element of the pension charge is shown in finance expense and the administration cost element is charged as a component of operating costs in the income statement. Actuarial gains and losses and re-measurement gains and losses are recognised immediately in full through the statement of comprehensive income. Contributions to defined contribution plans are charged to the income statement as incurred.

## Share-based payments

The Group operates share-based payment arrangements with employees. The fair value of equity-settled awards for share-based payments is determined on grant and expensed straight line over the period from grant to the date of earliest unconditional exercise. The fair value of cash-settled awards for share-based payments is determined each period end until they are exercised or lapse. The value is expensed straight line over the period from grant to the date of earliest unconditional exercise. The charges for both equity and cash-settled share-based payments are updated annually for non-market-based vesting conditions.

## Share capital

Ordinary share capital of the Company is recorded as the proceeds received, less issue costs. Company shares held by the employee benefit trusts are held at the consideration paid. They are classified as own shares within equity. Any gain or loss on the purchase, sale or issue of Company shares is recorded in equity.

## Recent accounting developments

### Developments adopted by the Group in 2015

The following EU-endorsed accounting standard was adopted for the first time in 2015:

**IFRS 10 'Consolidated Financial Statements'** – part of a new suite of standards on consolidation and related areas, replacing the existing accounting standards for subsidiaries and joint ventures (now joint arrangements) and making limited amendments in relation to associates. Refer to the 'Critical accounting estimates' section on page 102.

### Developments adopted by the Group in 2015 with no material impact on the financial statements

The following EU-endorsed amendments, improvements and interpretations of published standards are effective for accounting periods beginning on or after 1 April 2014 and have been adopted with no material impact on the Group's financial statements:

**IFRS 11 'Joint Arrangements'** – part of the same suite as IFRS 10;

**IFRS 12 'Disclosure of Interests in Other Entities'** – as above, contains the disclosure requirements for entities that have interest in subsidiaries, joint arrangements, associates and/or unconsolidated structure entities;

**IAS 27 'Separate Financial Statements'** – amended as part of the new suite of IFRSs as above;

**IAS 28 'Investments in Associates'** – reissued as IAS 28 'Investments in Associates and Joint Ventures'; it also forms part of the new suite of IFRSs 10-12;

**IFRS 10, 11, and 12** – amendments on transition guidance and on consolidation for investment entities;

**IAS 32 'Financial Instruments'** – amendment relating to asset and liability offsetting;

**IAS 39 'Financial Instruments: Recognition and measurement'** – amendment relating to the novation of derivatives and hedge accounting;

**IFRIC 21 'Levies'**.

### Developments expected in future periods of which the impact is being assessed

**Revenue from Contracts with Customers:** The final standard, IFRS 15, was published in May 2014. The IASB has tentatively decided to defer the effective date by one year and it is now expected that the standard will become effective, subject to EU endorsement, for annual reporting periods beginning on or after 1 January 2018, with earlier application permitted. The new standard introduces a five-step model to the principle of revenue recognition. Briefly, the framework includes identifying the contract with the customer, identifying the performance obligations in the contract, determining the transaction price, allocating the transaction price to the performance obligations in the contract and recognising revenue when (or as) the entity satisfies a performance obligation. QinetiQ is currently undertaking an assessment of the impact of the new standard. Typical issues to be analysed on a contract-by-contract basis include whether the current methodology for recognising revenue over time remains appropriate, the treatment of contract modifications, variable consideration, determination and distinction of performance obligations, collectability and licences (list not exhaustive). QinetiQ is also undertaking an analysis of the transitional guidance which allows for two different approaches, the retrospective method (with optional practical expedients) or the cumulative effect method.

**FRS 100, 101 and 102:** FRS 100, 101 and 102 all fall under the new UK GAAP regime. FRS 100 sets out the application of financial reporting requirements in the UK and Republic of Ireland and FRS 101, known as 'IFRS with reduced disclosures', outlines the reduced disclosure framework available for use by qualifying entities choosing to follow the principles of IFRS but under the umbrella of UK GAAP. FRS 102 is applicable in the UK and Republic of Ireland and is known as the 'new UK GAAP'. FRS 102 follows more closely the principles of existing UK GAAP with some exceptions. The mandatory effective date for the new framework of reporting is for accounting periods beginning on or after 1 January 2015. The Group can choose to apply either full IFRS, or a choice of either FRS 101 or FRS 102 to the Company and to its subsidiary entities. The two latter options both fall under UK GAAP and either may therefore be applied to Group companies on an entity by entity basis. If full IFRS is selected, this must be applied to all Group companies consistently. The Group will adopt the UK GAAP option with effect from 1 April 2015.

## 1. Significant accounting policies continued

**Leases:** A revised exposure draft was issued in May 2013 and following subsequent deliberations the IASB has decided upon the tentative adoption of a single right-of-use ("ROU") model. This approach eliminates off balance sheet accounting for lessees who will instead account for most leases on balance sheet as financing the purchase of an ROU asset. The ROU asset is a non-financial asset which would be accounted for consistently with other non-financial assets i.e. amortised. A corresponding liability would be recognised separately and accounted for at amortised cost, yielding an overall front-loaded expense profile, similar to existing finance leases. The IASB has tentatively agreed that no significant changes are needed to the current lessor model. The standard is expected to be published in 2015; the effective date is not yet known.

### Developments expected in future periods with no material impact on the Group's financial statements

The Directors anticipate that the adoption of the following new, revised, amended and improved published standards and interpretations, which were in issue at the date of authorisation of these financial statements, will have no material impact on the financial statements of the Group when they become applicable in future periods:

- IFRS 11 'Joint Arrangements'; IFRS 12 'Disclosure of Interests in Other Entities'; IFRS 14 'Regulatory Deferral Accounts';
- IAS 27 'Separate Financial Statements'; IAS 28 'Investments in Associates';
- Amendments to new standards IFRS 10, 11, 12 and 27; and
- Amendments to IAS 36 and 39.

## Critical accounting estimates and judgments in applying accounting policies

The following commentary is intended to highlight those policies that are critical to the business based on the level of management judgment required in their application, their complexity and their potential impact on the results and financial position reported for the Group. The level of management judgment required includes assumptions and estimates about future events that are uncertain and the actual outcome of which may result in a materially different outcome from that anticipated.

## Revenue and profit recognition

The estimation process required to evaluate the potential outcome of contracts and projects requires skill, knowledge and experience from a variety of sources within the business to assess the status of the contract, costs to complete, internal and external labour resources required and other factors. This process is carried out continuously throughout the business to ensure that project and contract assessments reflect the latest status of such work. No profit is recognised on a contract until the outcome can be reliably estimated.

## Business combinations and related goodwill

Intangible assets recognised on business combinations have been valued using established methods and models to determine estimated value and useful economic life, with input, where appropriate, from external valuation consultants. Such methods require the use of estimates which may produce results that are different from actual future outcomes.

The Group tests annually whether goodwill has suffered any impairment. This process relies on the use of estimates of the future profitability and cash flows of its CGUs which may differ from the actual results delivered. In addition, the Group reviews whether identified intangible assets have suffered any impairment. Further details on the sensitivity of the carrying value of goodwill to changes in the key assumptions are set out in note 14.

## Consolidation of US subsidiaries

As described on page 65, the Group and the US Department of Defense (DoD) have entered into a Proxy agreement that regulates the ownership, management and operation of certain Group subsidiaries. IFRS 10 is the accounting standard now applicable in respect of consolidation of entities. This does not specifically deal with proxy situations but the key principle of this new standard, effective for the year ended 31 March 2015, is that control exists, and consolidation is required, only if the investor (i) possesses power over the investee, (ii) has exposure to variable returns from its involvement with the investee and (iii) has the ability to use its power over the investee to affect its returns. Having considered the terms of the Proxy agreement, the Directors consider that the Group meets the requirements of IFRS 10 in respect of control over such affected entities and, therefore, consolidates the subsidiaries in the consolidated accounts.

## Tax

In determining the Group's provisions for income tax and deferred tax, it is necessary to assess the likelihood and timing of recovery of tax losses created, and to consider transactions in a small number of key tax jurisdictions for which the ultimate tax determination is uncertain. To the extent that the final outcome differs from the tax that has been provided, adjustments will be made to income tax and deferred tax provisions held in the period the determination is made. A key judgment made in the year to 31 March 2015 is that the utilisation of certain UK trade losses is now sufficiently probable in the foreseeable future that a deferred tax asset should be recognised in respect of those losses. As such, a deferred tax asset of £25.2m has been recognised at 31 March 2015.

## Post-retirement benefits

The Group's defined benefit pension obligations and net income statement costs are based on key assumptions, including discount rates, mortality and inflation. Management exercises its best judgment, in consultation with actuarial advisors, in selecting the values for these assumptions that are the most appropriate to the Group. Small changes in these assumptions at the balance sheet date, individually or collectively, may result in significant changes in the size of the deficit or the net income statement costs. Any change in these assumptions would have an impact on the retirement benefit obligation recognised. Further details of these assumptions are set out in note 30.

## 2. Revenue and other income

Revenue and other income is analysed as follows:

### Revenue by category – continuing operations

For the year ended 31 March

all figures in £ million	2015	2014 <sup>▲</sup>
Sales of goods	71.8	110.4
Services	685.1	665.8
Royalties and licences	6.9	6.4
<b>Revenue</b>	<b>763.8</b>	<b>782.6</b>
Share of joint ventures' and associates' (loss)/profit after tax	(0.1)	0.1
Other income	7.7	6.9
<b>Total other income</b>	<b>7.6</b>	<b>7.0</b>

Revenue and loss after tax of joint ventures and associates was £7.7m and £0.1m respectively (2014: revenue of £6.5m and profit before tax of £0.3m). The figures in the table above represent the Group share of this loss/profit after tax.

Other income is in respect of property rentals and the recovery of other related property costs.

### Revenue by customer geographic location – continuing operations

For the year ended 31 March

all figures in £ million	2015	2014 <sup>▲</sup>
United Kingdom	610.7	578.4
US	69.4	98.4
Other	83.7	105.8
<b>Total</b>	<b>763.8</b>	<b>782.6</b>

### Revenue by major customer type – continuing operations

For the year ended 31 March

all figures in £ million	2015	2014 <sup>▲</sup>
UK Government	537.6	503.9
US Government	51.2	72.9
Other	175.0	205.8
<b>Total</b>	<b>763.8</b>	<b>782.6</b>

Revenue from the UK Government was generated by the EMEA Services and Global Products operating segments. Revenue from the US Government was generated by the Global Products operating segment.

<sup>▲</sup> Restated for the reclassification of the US Services segment as a discontinued operation.

### 3. Segmental analysis

#### Operating segments

For the year ended 31 March

all figures in £ million

	Note	2015		2014^	
		Revenue	Operating profit	Revenue	Operating profit
EMEA Services		625.6	93.0	607.0	86.7
Global Products		138.2	18.3	175.6	27.0
<b>Total operating segments</b>		<b>763.8</b>	<b>111.3</b>	<b>782.6</b>	<b>113.7</b>
<b>Operating profit before specific adjusting items<sup>1</sup> – underlying operating profit</b>			<b>111.3</b>		<b>113.7</b>
Specific adjusting items:					
Restructuring			1.0		0.2
Pension scheme closure costs			–		27.1
Property impairment reversal			–		1.4
Impairment of goodwill			–		(41.9)
Amortisation of intangible assets arising from acquisitions			(2.8)		(3.4)
<b>Operating profit</b>			<b>109.5</b>		<b>97.1</b>
Gain on business divestments	7		–		1.1
Net finance expense	8		(4.1)		(14.2)
<b>Profit before tax</b>			<b>105.4</b>		<b>84.0</b>
Taxation income/(expense)	9		12.0		(16.0)
<b>Profit for the year from continuing operations</b>			<b>117.4</b>		<b>68.0</b>
<b>Discontinued operations</b>					
Loss from discontinued operations, net of tax	5		(12.7)		(80.7)
<b>Profit/(loss) for the period attributable to equity shareholders</b>			<b>104.7</b>		<b>(12.7)</b>

<sup>1</sup> The measure of profit presented to the chief operating decision maker is underlying operating profit (as defined in glossary on page 141).

No measure of segmental assets and liabilities has been disclosed as this information is not regularly provided to the chief operating decision maker.

<sup>^</sup> Restated for the reclassification of the US Services segment as a discontinued operation.

#### Depreciation and amortisation by business segment – excluding specific adjusting items

For the year ended 31 March 2015

all figures in £ million	EMEA Services	Global Products	Total continuing operations
Depreciation and impairment of property, plant and equipment	19.7	2.0	<b>21.7</b>
Amortisation of purchased or internally developed intangible assets	0.8	0.7	<b>1.5</b>
	<b>20.5</b>	<b>2.7</b>	<b>23.2</b>

For the year ended 31 March 2014

all figures in £ million	EMEA Services	Global Products	Total continuing operations
Depreciation of property, plant and equipment	19.7	2.1	21.8
Amortisation of purchased or internally developed intangible assets	0.6	0.1	0.7
	<b>20.3</b>	<b>2.2</b>	<b>22.5</b>

Excludes specific adjusting items not included within the measure of operating profit reported to the chief operating decision maker.

#### Non-current assets (excluding deferred tax) by geographic location

all figures in £ million	UK	Rest of World	Total
Year ended 31 March 2015	262.0	91.4	<b>353.4</b>
Year ended 31 March 2014	258.4	162.9	<b>421.3</b>

## 4. Profit/loss before tax

The following auditor's remuneration has been charged in arriving at profit/loss before tax:

	2015	2014
<b>Fees payable to the auditor and its associates:</b>		
Audit of the Group's annual accounts	0.4	0.6
Audit of the accounts of subsidiaries of the Company and its associated pension scheme	0.2	0.5
Audit-related assurance services	0.1	0.1
Other assurance services	—	0.2
Corporate finance services – due diligence support	—	1.3
All other non-audit services	0.1	—
<b>Total auditor's remuneration</b>	<b>0.8</b>	<b>2.7</b>

The fees payable to auditors were significantly lower in 2015 than 2014 due to the fact that in the prior year KPMG were engaged to perform work in connection with the strategic review and preparation for the proposed sale of the US Services division.

The following items have also been charged in arriving at profit/loss before tax for continuing operations:

	2015	2014 <sup>A</sup>
<b>Depreciation and impairment of property, plant and equipment:</b>		
Owned assets: depreciation	(20.7)	(21.8)
Owned assets: impairment (charge)/reversal	(1.0)	1.4
<b>Foreign exchange loss</b>	<b>(0.3)</b>	<b>(1.1)</b>
<b>Research and development expenditure – customer funded contracts</b>	<b>(285.8)</b>	<b>(288.7)</b>
<b>Research and development expenditure – Group funded</b>	<b>(20.8)</b>	<b>(25.9)</b>

In the income statement, the Group presents specific adjusting items separately. In the judgment of the Directors, for the reader to obtain a proper understanding of the financial information, specific adjusting items need to be disclosed separately because of their size and nature. The following specific adjusting items have been (charged)/credited in arriving at profit/loss before tax:

	Note	2015	2014 <sup>A</sup>
all figures in £ million			
Reversal of unutilised restructuring provisions		1.0	0.2
Reduction in pension liabilities on closure to future accrual		—	31.1
Pension scheme closure mitigation costs		—	(4.0)
<b>Specific adjusting items before amortisation, depreciation and impairment</b>		<b>1.0</b>	<b>27.3</b>
Impairment of goodwill		—	(41.9)
Property impairment reversal	16	—	1.4
Amortisation of intangible assets arising from acquisition	15	(2.8)	(3.4)
<b>Specific adjusting items operating loss</b>		<b>(1.8)</b>	<b>(16.6)</b>
Gain on business divestments	7	—	1.1
Defined benefit pension scheme net finance expense		(0.6)	(1.7)
<b>Specific adjusting items loss before tax – continuing operations</b>		<b>(2.4)</b>	<b>(17.2)</b>
Profit on disposal of subsidiary – before accelerated interest expense	5	15.9	—
Loss on disposal of subsidiary – accelerated interest expense	5	(28.8)	—
Loss on disposal of subsidiary	5	(12.9)	—
US Services pre-sale transaction costs		—	(6.0)
Impairment of goodwill		—	(84.0)
Amortisation of intangible assets arising from acquisition		(0.8)	(7.6)
Restructuring costs		—	(0.5)
<b>Specific adjusting items loss before tax – discontinued operations</b>		<b>(13.7)</b>	<b>(98.1)</b>
<b>Total specific adjusting items loss before tax</b>		<b>(16.1)</b>	<b>(115.3)</b>

<sup>A</sup> Restated for the reclassification of the US Services segment as a discontinued operation.

## 5. Discontinued operations

On 23 May 2014 the Group completed its sale of the US Services division, comprising QinetiQ North America Inc. and its subsidiaries. The Circular seeking shareholder approval for the sale of the US Services division specified that the proceeds would be applied in settling the remaining private placement ('PP') debt of \$248m which was put in place to finance the acquisitions of the US Services business. Accordingly, the penalty of £28.8m incurred on the early redemption of the PP is considered to be inextricably linked to the sale of that business and has, therefore, been disclosed as an adjustment to the loss on its sale rather than as a finance expense.

The initial cash consideration was \$165m prior to the standard working capital adjustments at completion. The mid-month completion of the deal resulted in the May month end payroll and creditor payments falling outside QinetiQ's period of ownership. This caused the closing balance sheet to have higher cash (to be retained by QinetiQ) and lower working capital than would have been the case at the month end. The working capital mechanism was designed to make such timing issues neutral. Hence working capital adjustments (and closing net-debt adjustments) of \$10.6m were required. Additional deferred consideration remains receivable. The earn-out is scheduled to be payable in the first half of the Group's next financial year on a sliding scale between zero and \$50m based on gross profit generated by the disposed business in the financial year to 31 March 2015. Actual gross profit delivered by the disposed business (still subject to audit) indicates that the deferred consideration receivable will be approximately \$9m in cash. The full impact of the disposal is given below:

### a) Results of discontinued operations

all figures in £ million	Note	2015	2014
Revenue		55.7	408.8
Operating costs excluding depreciation, amortisation and impairment		(54.2)	(387.3)
<b>EBITDA (earnings before interest, tax, depreciation and amortisation)</b>		<b>1.5</b>	<b>21.5</b>
Depreciation, amortisation and impairment of assets		(0.3)	(2.5)
<b>Underlying operating profit</b>		<b>1.2</b>	<b>19.0</b>
Impairment of goodwill		–	(84.0)
Amortisation of intangible assets arising from acquisitions		(0.8)	(7.6)
Other specific adjusting items	4	–	(6.5)
<b>Operating profit/(loss)</b>		<b>0.4</b>	<b>(79.1)</b>
Finance expense		–	(0.8)
<b>Profit/(loss) before tax</b>		<b>0.4</b>	<b>(79.9)</b>
Taxation expense		(0.2)	(0.8)
<b>Results from operating activities, net of tax</b>		<b>0.2</b>	<b>(80.7)</b>
Profit on sale of discontinued operations – before accelerated interest costs		15.9	–
Loss on sale of discontinued operations – accelerated interest costs		(28.8)	–
<b>Loss for the period</b>		<b>(12.7)</b>	<b>(80.7)</b>
Basic loss per share		(2.0)p	(12.4)p
Diluted loss per share		(2.0)p	(12.4)p
Underlying basic earnings per share		0.1p	2.2p

### b) Cash flows from discontinued operations

all figures in £ million	2015	2014
Net cash from operating activities	1.8	30.3
Net cash from investing activities	–	–
<b>Net cash inflow for the year</b>	<b>1.8</b>	<b>30.3</b>

### c) Effect of disposal on the financial position of the Group

all figures in £ million	2015
Goodwill	41.2
Intangible assets	32.6
Property, plant and equipment	5.9
Inventories	0.8
Trade and other receivables	71.7
Cash and cash equivalents	1.0
Deferred tax asset	9.6
Trade and other payables	(54.7)
<b>Net assets and liabilities</b>	<b>108.1</b>
Consideration received (net of transaction costs), satisfied in cash	79.6
Cash and cash equivalents disposed	(1.0)
<b>Net cash inflow in the year to 31 March 2015</b>	<b>78.6</b>

## 6. Business combinations

The Group made two acquisitions in the year to 31 March 2015. On 7 August 2014 the Group acquired the trade and assets of Redfern Integrated Optics Inc. from its founder management team and on 19 November 2014 the Group acquired the trade and assets of SR2020. Further information on each acquisition is given below.

### Redfern Integrated Optics Inc. ("RIO")

RIO is a US-based business that designs and manufactures highly coherent semiconductor lasers. QinetiQ's OptaSense® business uses the lasers within its core product range in the Distributed Acoustic Sensing market. RIO is the sole source supplier for this type of product and the acquisition was made to protect the supply to OptaSense® of the RIO laser product.

If the acquisition had been completed on the first day of the financial year, Group revenue for the period ended 31 March 2015 would have been £764.7m and the Group profit before tax would have been £105.4m.

Acquisition	Acquisition date	Expected cash consideration £million	Contribution post-acquisition	
			Revenue £million	Operating profit £million
Trade and assets of Redfern Integrated Optics Inc.	7 August 2014	3.8	1.8	–

Set out below are the allocations of purchase consideration, assets and liabilities of the acquisition made in the year and the adjustments required to the book values of the assets and liabilities in order to present the net assets of this business at fair value and in accordance with the Group accounting policies.

all figures in £ million	Book value	Fair value adjustment	Fair value at acquisition
Net assets acquired	1.8	(0.9)	0.9
Goodwill and intangibles	–	2.9	2.9
	1.8	2.0	3.8
Consideration satisfied by:			
Cash			3.3
Deferred consideration payable			0.5
<b>Total consideration</b>	<b>3.8</b>		

### SR2020 Inc.

SR2020 Inc. is a US-based leading provider of borehole seismic services who develop and use purpose written, proprietary software for borehole seismic imaging, micro-seismic monitoring and passive seismic monitoring. The business has extensive oil and gas industry experience and its expertise in processing and interpretation services will further enhance the Group's Optasense® product and services portfolio.

If the acquisition had been completed on the first day of the financial year, Group revenue for the period ended 31 March 2015 would have been £763.9m and the Group profit before tax would have been £104.6m.

Acquisition	Acquisition date	Expected cash consideration £million	Contribution post-acquisition	
			Revenue £million	Operating profit £million
Trade and assets of SR2020 Inc.	19 November 2014	0.4	0.1	(0.4)

Set out below are the allocations of purchase consideration, assets and liabilities of the acquisition made in the year and the adjustments required to the book values of the assets and liabilities in order to present the net assets of this business at fair value and in accordance with the Group accounting policies.

all figures in £ million	Book value	Fair value adjustment	Fair value at acquisition
Net assets acquired	0.3	(0.3)	–
Goodwill and intangibles	–	0.4	0.4
	0.3	0.1	0.4
Consideration satisfied by:			
Cash			0.4
Deferred consideration payable			–
<b>Total consideration</b>	<b>0.4</b>		

## 7. Gain on business divestments – continuing operations

For the year ended 31 March

all figures in £ million

	2015	2014
<b>Gain on business divestments</b>	–	1.1

The gain on business divestments relates to deferred consideration received in respect of the disposal of the Calibration business in 2009.

## 8. Finance income and expense – continuing operations

For the year ended 31 March

all figures in £ million

	2015	2014 <sup>a</sup>
Receivable on bank deposits	1.1	1.4
Finance lease income	0.2	0.5
<b>Finance income</b>	<b>1.3</b>	<b>1.9</b>
Amortisation of recapitalisation fee	(0.7)	(0.6)
Payable on bank loans and overdrafts	(0.9)	(1.4)
Payable on US dollar private placement debt	(2.6)	(11.3)
Finance lease expense	(0.2)	(0.4)
Unwinding of discount on financial liabilities	(0.4)	(0.7)
<b>Finance expense before specific adjusting items</b>	<b>(4.8)</b>	<b>(14.4)</b>
Specific adjusting items:		
Defined benefit pension scheme net finance expense	(0.6)	(1.7)
<b>Total finance expense</b>	<b>(5.4)</b>	<b>(16.1)</b>
<b>Net finance expense</b>	<b>(4.1)</b>	<b>(14.2)</b>

<sup>a</sup> Restated for the reclassification of the US Services segment as a discontinued operation.

The Circular seeking shareholder approval for the sale of the US Services division specified that the proceeds would be applied in settling the remaining private placement ('PP') debt of \$248m which was put in place to finance the acquisitions of the US Services business. Accordingly, the penalty of £28.8m incurred on the early redemption of the PP is considered to be inextricably linked to the sale of that business and has, therefore, been disclosed as an adjustment to the loss on its sale rather than as a finance expense. See note 5.

## 9. Taxation – continuing operations

all figures in £ million	2015			2014^		
	Before specific adjusting items*	Specific adjusting items*	Total	Before specific adjusting items*	Specific adjusting items*	Total
<b>Analysis of charge</b>						
Current UK tax expense/(income)	0.5	–	0.5	(4.2)	(0.9)	(5.1)
<b>Overseas corporation tax</b>						
Current year	1.4	(0.5)	0.9	(10.3)	(1.1)	(11.4)
Adjustment for prior year	(1.0)	0.6	(0.4)	–	–	–
<b>Current tax expense/(income)</b>	<b>0.9</b>	<b>0.1</b>	<b>1.0</b>	<b>(14.5)</b>	<b>(2.0)</b>	<b>(16.5)</b>
Deferred tax expense/(income)	11.3	(22.9)	(11.6)	25.0	7.8	32.8
Deferred tax impact of change in rates	(0.4)	–	(0.4)	0.9	–	0.9
Deferred tax in respect of prior years	–	(1.0)	(1.0)	–	(1.2)	(1.2)
<b>Deferred tax expense/(income)</b>	<b>10.9</b>	<b>(23.9)</b>	<b>(13.0)</b>	<b>25.9</b>	<b>6.6</b>	<b>32.5</b>
<b>Taxation expense/(income) – continuing operations</b>	<b>11.8</b>	<b>(23.8)</b>	<b>(12.0)</b>	<b>11.4</b>	<b>4.6</b>	<b>16.0</b>
<b>Factors affecting tax charge/(credit) in year</b>						
Principal factors reducing the Group's current year tax charge below the UK statutory rate are explained below:						
Profit/(loss) before tax	107.8	(2.4)	105.4	101.2	(23.2)	78.0
<b>Tax on profit/(loss) before tax at 21% (2014: 23%)</b>	<b>22.6</b>	<b>(0.5)</b>	<b>22.1</b>	<b>23.3</b>	<b>(5.3)</b>	<b>18.0</b>
Effect of:						
Expenses not deductible for tax purposes, research and development relief and non-taxable items	(18.6)	1.7	(16.9)	(9.9)	10.4	0.5
Recognition of deferred tax asset in respect of UK trading losses	–	(25.2)	(25.2)	–	–	–
Current tax losses for which no deferred tax asset was recognised	6.9	–	6.9	(1.0)	–	(1.0)
Deferred tax impact of change in rates	(0.4)	–	(0.4)	0.9	–	0.9
Deferred tax in respect of prior years	0.9	–	0.9	0.2	–	0.2
Effect of different rates in overseas jurisdictions	0.4	0.2	0.6	(2.1)	(0.5)	(2.6)
<b>Taxation expense/(income) – continuing operations</b>	<b>11.8</b>	<b>(23.8)</b>	<b>(12.0)</b>	<b>11.4</b>	<b>4.6</b>	<b>16.0</b>
<b>Effective tax rate</b>	<b>10.9%</b>		<b>(11.4%)</b>	<b>11.3%</b>		<b>20.5%</b>

\*Details of specific adjusting items can be found in note 4.

<sup>^</sup>Restated for the reclassification of the US Services segment as a discontinued operation.

Tax expense on continuing operations excludes the tax expense of the discontinued operation of £0.2m. This is included in 'profit/(loss) from discontinued operation, net of tax' (see note 5).

### Factors affecting future tax charges

The effective tax rate continues to be below the statutory rate in the UK, primarily as a result of the benefit of research and development tax relief in the UK. The effective tax rate is expected to remain below the UK statutory rate in the medium term, subject to the impact of any tax legislation changes and the geographic mix of profits and the assumption that the benefit of R&D tax relief remains in the tax line. The Finance Act 2013 allows the continued treatment of R&D tax relief as a super deduction until 1 April 2016, when R&D Expenditure Credit treatment becomes mandatory.

Deferred tax has been calculated at 20% being the enacted future statutory tax rate.

At 31 March 2015 the Group had unused tax losses of £291.6m (2014: £213.9m) which are available for offset against future profits. An asset of £25.2m has been recognised in respect of an element of these unused tax losses, relating to certain UK trading losses which are expected to be utilised in the foreseeable future. No deferred tax asset is recognised in respect of the other losses due to uncertainty over the timing and extent of their utilisation.

## 10. Dividends

An analysis of the dividends paid and proposed in respect of the years ended 31 March 2015 and 2014 is provided below:

	Pence per share	£m	Date paid/ payable
Interim 2015	1.8	11.1	Feb 2015
Final 2015 (proposed)	3.6	21.2	Sept 2015
<b>Total for the year ended 31 March 2015</b>	<b>5.4</b>	<b>32.3</b>	
Interim 2014	1.4	9.2	Feb 2014
Final 2014	3.2	20.6	Sept 2014
<b>Total for the year ended 31 March 2014</b>	<b>4.6</b>	<b>29.8</b>	

The Directors propose a final dividend of 3.6p (2014: 3.2p) per share. The dividend, which is subject to shareholder approval, will be paid on 4 September 2015. The ex-dividend date is 6 August 2015 and the record date is 7 August 2015.

## 11. Analysis of employee costs and numbers

The largest component of operating expenses is employee costs. The year-end and average monthly number of persons employed by the Group, including Executive Directors, analysed by business segment, were:

	As at 31 March		Monthly average	
	2015 Number	2014 Number	2015 Number	2014 Number
EMEA Services	5,576	5,399	5,521	5,292
Global Products	674	834	706	828
Continuing operations	6,250	6,233	6,227	6,120
US Services	-	2,704	227	3,014
<b>Total</b>	<b>6,250</b>	<b>8,937</b>	<b>6,454</b>	<b>9,134</b>

The aggregate payroll costs of these persons were as follows:

all figures in £ million	Note	2015	2014
Wages and salaries		284.0	450.3
Social security costs		27.6	38.3
Pension costs		35.1	40.8
Share-based payments costs	29	3.6	4.5
<b>Employee costs before UK pension closure mitigation costs</b>		<b>350.3</b>	<b>533.9</b>
UK pension scheme closure mitigation costs		—	4.0
<b>Total employee costs</b>		<b>350.3</b>	<b>537.9</b>

On closure of the UK defined benefit pension scheme to future accrual, affected employees were transferred to a defined contribution pension scheme. Additional one-off employer contribution payments were made by the Company into the new schemes during the prior year.

## 12. Directors and other senior management personnel

The Directors and other senior management personnel of the Group during the year to 31 March 2015 comprise the Board of Directors and the Operations Committee. The remuneration and benefits provided to Directors and the Operations Committee are summarised below:

all figures in £ million	2015	2014
Short-term employee remuneration including benefits	6.1	6.7
Post-employment benefits	0.1	0.2
Share-based payments costs	1.4	1.9
Termination benefits	0.1	0.8
<b>Total</b>	<b>7.7</b>	<b>9.6</b>

Short-term employee remuneration and benefits include salary, bonus and benefits. Post-employment benefits relate to pension amounts.

### 13. Earnings per share

Basic earnings per share is calculated by dividing the profit attributable to equity shareholders by the weighted average number of ordinary shares in issue during the year. The weighted average number of shares used excludes those shares bought by the Group and held as own shares (see note 28). For diluted earnings per share the weighted average number of shares in issue is adjusted to assume conversion of all potentially dilutive ordinary shares arising from unvested share-based awards including share options. Underlying basic earnings per share figures are presented below, in addition to the basic and diluted earnings per share, because the Directors consider this gives a more relevant indication of underlying business performance and reflects the adjustments to basic earnings per share for the impact of specific adjusting items (see note 4) and tax thereon.

For the year ended 31 March		2015	2014
<b>Underlying basic EPS – continuing operations</b>			
Profit attributable to equity shareholders	£ million	117.4	68.0
Remove (profit)/loss after tax in respect of specific adjusting items*	£ million	(21.4)	21.8
Underlying profit after taxation	£ million	96.0	89.8
Weighted average number of shares	Million	630.9	651.7
<b>Underlying basic EPS – continuing operations</b>	Pence	15.2	13.8

#### Underlying basic EPS – total Group

Profit/(loss) attributable to equity shareholders	£ million	104.7	(12.7)
Remove(profit)/loss after tax in respect of specific adjusting items*	£ million	(8.0)	116.7
Underlying profit after taxation	£ million	96.7	104.0
Weighted average number of shares	Million	630.9	651.7
<b>Underlying basic EPS – total Group</b>	Pence	15.3	16.0

For the year ended 31 March

2015	2014
<b>Basic EPS – continuing operations</b>	
Profit attributable to equity shareholders	£ million
Weighted average number of shares	Million
<b>Basic EPS – continuing operations</b>	Pence

#### Diluted EPS – continuing operations

Profit attributable to equity shareholders	£ million	117.4	68.0
Weighted average number of shares	Million	630.9	651.7
Effect of dilutive securities	Million	3.7	5.1
Diluted number of shares	Million	634.6	656.8
<b>Diluted EPS – continuing operations</b>	Pence	18.5	10.4

For the year ended 31 March

2015	2014
<b>Basic EPS – total Group</b>	
Profit/(loss) attributable to equity shareholders	£ million
Weighted average number of shares	Million
<b>Basic EPS – total Group</b>	Pence

#### Diluted EPS – total Group

Profit/(loss) attributable to equity shareholders	£ million	104.7	(12.7)
Weighted average number of shares	Million	630.9	651.7
Effect of dilutive securities <sup>1</sup>	Million	3.7	–
Diluted number of shares	Million	634.6	651.7
<b>Diluted EPS – total Group</b>	Pence	16.5	(1.9)

<sup>1</sup> The loss attributable to equity shareholders results in the effect of dilutive securities on the weighted average number of shares being nil in the prior year.

\*Details of specific adjusting items can be found in note 4.

## 14. Goodwill

all figures in £ million

	2015	2014
<b>Cost</b>		
At 1 April	541.4	593.0
Acquisitions	0.1	–
Disposals	(370.1)	–
Foreign exchange	11.9	(51.6)
<b>At 31 March</b>	<b>183.3</b>	<b>541.4</b>
<b>Impairment</b>		
At 1 April	(400.1)	(302.6)
Disposals	328.9	–
Impairment	–	(125.9)
Foreign exchange	(4.9)	28.4
<b>At 31 March</b>	<b>(76.1)</b>	<b>(400.1)</b>
<b>Net book value at 31 March</b>	<b>107.2</b>	<b>141.3</b>

Goodwill as at 31 March 2015 was allocated across various cash generating units (CGUs) in the following segments: EMEA Services (three) and Global Products (two). Goodwill previously allocated to the US Services CGU was written off in the year on disposal of that CGU.

Goodwill is attributable to the excess of consideration over the fair value of net assets acquired and includes expected synergies, future growth prospects and employee knowledge, expertise and security clearances. The Group tests each CGU for impairment annually, or more frequently if there are indications that goodwill might be impaired.

Impairment testing is dependent on management's estimates and judgments, particularly as they relate to the forecasting of future cash flows, the discount rates selected and expected long-term growth rates. Significant headroom exists in all CGUs with the exception of US Global Products, discussed below, and management considers that there are no likely variations in the key assumptions which would lead to an impairment being recognised in any of the other CGUs.

### Key assumptions

#### Cash flows

The value-in-use calculations generally use discounted future cash flows based on financial plans approved by the Board covering a two-year period. Discounted cash flows for the US Global Products CGU were based on a Board-approved three-year plan, reflecting increases in revenue from new product lines. Cash flows for periods beyond these periods are extrapolated based on the last year of the plans, with a terminal growth-rate assumption applied.

#### Terminal growth rates

The specific plans for each of the CGUs have been extrapolated using a terminal growth rate of 2.0% – 3.0% (2014: 2.0% – 3.0%). Growth rates are based on management's estimates which take into consideration the long-term nature of the industry in which the CGUs operate and external forecasts as to the likely growth of the industry in the longer term.

#### Discount rates

The Group's weighted average cost of capital was used as a basis in determining the discount rate to be applied adjusted for risks specific to the market characteristics of CGUs as appropriate on a pre-tax basis. This is considered to appropriately estimate a market participant discount rate. The pre-tax discount rates applied for the three EMEA Services CGUs were 10.6%, 13.2% and 17.0% and for the Global Products CGUs 10.0% and 10.5%.

Sensitivity analysis shows that the value of the terminal year cash flow, the discount rate and the terminal growth rates have a significant impact on the value of the discounted cash flow.

### Significant CGUs

The carrying value of the net operating assets of the US Global Products CGU was written down in the prior year. This brought the carrying value in line with the calculated value in use as at 31 March 2014. The carrying value of the goodwill for this CGU as at 31 March 2015 was £67.2m (2014: £60.0m). The value in use of this CGU as at 31 March 2015, calculated using the assumptions noted above, is marginally higher than the carrying value of net operating assets (of £78.0m) and no further impairment is required in the year to 31 March 2015. The key sensitivity impacting on the value in use calculations is the terminal year cash flows. These cash flows include certain assumptions about revenue and profit in respect of new product lines still to be launched. Applying a sensitivity to remove the new product contribution from the terminal year results in an impairment of £9.9m. An additional sensitivity to remove all expected growth in the terminal year (i.e. growth in existing products as well as new products) results in an impairment of £34.8m. Sensitivity analysis also shows that an increase of 1% in the discount rate assumption would result in an impairment of £9.5m. Sensitivity analysis also shows that a decrease of 1% in the terminal growth rate would result in an impairment of £8.2m.

The UK Global Products CGU and the three individual CGUs within EMEA Services all have significant headroom. An increase in the discount rate or a decrease in the terminal growth rate by 1% would not cause the net operating assets to exceed their recoverable amount. The carrying value of goodwill for the UK Global Products CGU as at 31 March 2015 was £5.2m (2014: £5.5m). The carrying values of goodwill for the three EMEA Services CGUs as at 31 March 2015 were £27.5m, £5.2m and £2.1m (2014: £27.5m, £4.6m and £2.3m). The Directors have not identified any other likely changes in other significant assumptions between 31 March 2015 and the signing of the financial statements that would cause the carrying value of the recognised goodwill to exceed its recoverable amount.

## 15. Intangible assets

Year ended 31 March 2015

all figures in £ million	Acquired intangible assets					Total
	Customer relationships	Intellectual property	Brand names	Development costs	Other intangible assets	
<b>Cost</b>						
At 1 April 2014	141.4	53.5	9.2	17.0	35.8	256.9
Additions – internally developed	–	–	–	0.4	1.3	1.7
Additions – purchased	–	–	–	–	2.5	2.5
Additions – recognised on acquisition	–	3.3	–	–	–	3.3
Divestments	(108.9)	(2.0)	(6.0)	(0.3)	(1.7)	(118.9)
Transfers	–	–	–	(0.1)	0.7	0.6
Foreign exchange	6.5	4.1	0.9	–	3.7	15.2
<b>At 31 March 2015</b>	<b>39.0</b>	<b>58.9</b>	<b>4.1</b>	<b>17.0</b>	<b>42.3</b>	<b>161.3</b>
<b>Amortisation and impairment</b>						
At 1 April 2014	105.5	49.9	8.1	14.5	34.7	212.7
Amortisation charge for year	1.4	2.1	0.1	0.6	0.9	5.1
Divestments	(79.0)	(1.0)	(5.9)	(0.1)	(0.3)	(86.3)
Transfers	–	–	–	–	(0.2)	(0.2)
Foreign exchange	5.1	6.8	0.3	–	2.5	14.7
<b>At 31 March 2015</b>	<b>33.0</b>	<b>57.8</b>	<b>2.6</b>	<b>15.0</b>	<b>37.6</b>	<b>146.0</b>
<b>Net book value at 31 March 2015</b>	<b>6.0</b>	<b>1.1</b>	<b>1.5</b>	<b>2.0</b>	<b>4.7</b>	<b>15.3</b>

The amortisation charge for the year of £5.1m includes £0.8m in respect of discontinued operations. Divestments are in respect of the disposal of the US Services division (see note 5).

Year ended 31 March 2014

all figures in £ million	Acquired intangible assets					Total
	Customer relationships	Intellectual property	Brand names	Development costs	Other intangible assets	
<b>Cost</b>						
At 1 April 2013	155.2	57.3	10.1	14.8	36.5	273.9
Additions – internally developed	–	–	–	2.1	–	2.1
Additions – purchased	–	–	–	–	0.5	0.5
Disposals	–	–	–	–	(1.0)	(1.0)
Transfers	–	–	–	0.1	0.2	0.3
Foreign exchange	(13.8)	(3.8)	(0.9)	–	(0.4)	(18.9)
<b>At 31 March 2014</b>	<b>141.4</b>	<b>53.5</b>	<b>9.2</b>	<b>17.0</b>	<b>35.8</b>	<b>256.9</b>
<b>Amortisation and impairment</b>						
At 1 April 2013	107.8	51.0	7.8	14.2	35.3	216.1
Amortisation charge for year	7.5	2.4	1.1	0.3	0.7	12.0
Disposals	–	–	–	–	(0.9)	(0.9)
Foreign exchange	(9.8)	(3.5)	(0.8)	–	(0.4)	(14.5)
<b>At 31 March 2014</b>	<b>105.5</b>	<b>49.9</b>	<b>8.1</b>	<b>14.5</b>	<b>34.7</b>	<b>212.7</b>
<b>Net book value at 31 March 2014</b>	<b>35.9</b>	<b>3.6</b>	<b>1.1</b>	<b>2.5</b>	<b>1.1</b>	<b>44.2</b>

## 16. Property, plant and equipment

Year ended 31 March 2015

all figures in £ million	Land and buildings	Plant, machinery and vehicles	Computers and office equipment	Assets under construction	Total
<b>Cost</b>					
At 1 April 2014	317.6	164.5	50.0	24.9	557.0
Additions – purchased	0.3	1.2	1.0	22.3	24.8
Additions – acquisition	–	0.3	0.1	–	0.4
Disposals	(0.8)	(0.5)	(0.2)	(1.2)	(2.7)
Divestments	(3.4)	(1.4)	(11.5)	–	(16.3)
Transfers	(1.9)	8.9	1.3	(8.9)	(0.6)
Foreign exchange	0.8	1.3	0.8	–	2.9
<b>At 31 March 2015</b>	<b>312.6</b>	<b>174.3</b>	<b>41.5</b>	<b>37.1</b>	<b>565.5</b>
<b>Depreciation</b>					
At 1 April 2014	145.9	137.5	39.8	–	323.2
Charge for year	9.7	8.5	2.8	–	21.0
Impairment	–	0.5	0.1	0.4	1.0
Disposals	(0.8)	(0.5)	(0.1)	–	(1.4)
Divestments	(1.9)	(1.0)	(7.5)	–	(10.4)
Transfers	(1.1)	1.1	0.2	–	0.2
Foreign exchange	0.5	0.9	0.9	–	2.3
<b>At 31 March 2015</b>	<b>152.3</b>	<b>147.0</b>	<b>36.2</b>	<b>0.4</b>	<b>335.9</b>
<b>Net book value at 31 March 2015</b>	<b>160.3</b>	<b>27.3</b>	<b>5.3</b>	<b>36.7</b>	<b>229.6</b>

Impairment of £1.0m (2014: reversal of £1.4m) expensed in the consolidated income statement relates to equipment which is no longer being utilised. The depreciation charge for the year of £21.0m includes £0.3m in respect of discontinued operations. Divestments are in respect of the disposal of the US Services division (see note 5).

Year ended 31 March 2014

all figures in £ million	Land and buildings	Plant, machinery and vehicles	Computers and office equipment	Assets under construction	Total
<b>Cost</b>					
At 1 April 2013	320.0	163.1	53.1	17.8	554.0
Additions	0.1	1.4	1.1	21.6	24.2
Disposals	(2.7)	(1.8)	(4.9)	(6.4)	(15.8)
Transfers	1.5	3.5	2.9	(8.1)	(0.2)
Foreign exchange	(1.3)	(1.7)	(2.2)	–	(5.2)
<b>At 31 March 2014</b>	<b>317.6</b>	<b>164.5</b>	<b>50.0</b>	<b>24.9</b>	<b>557.0</b>
<b>Depreciation</b>					
At 1 April 2013	140.5	130.8	41.3	–	312.6
Charge for year	9.8	9.8	4.4	–	24.0
Impairment reversal	(1.4)	–	–	–	(1.4)
Disposals	(2.2)	(1.7)	(4.5)	–	(8.4)
Foreign exchange	(0.8)	(1.4)	(1.4)	–	(3.6)
<b>At 31 March 2014</b>	<b>145.9</b>	<b>137.5</b>	<b>39.8</b>	<b>–</b>	<b>323.2</b>
<b>Net book value at 31 March 2014</b>	<b>171.7</b>	<b>27.0</b>	<b>10.2</b>	<b>24.9</b>	<b>233.8</b>

Under the terms of the Business Transfer Agreement with the MOD, certain restrictions have been placed on freehold land and buildings, and certain plant and machinery related to them. These restrictions are detailed in note 31.

## 17. Non-current investments

As at 31 March

	2015	2014	
	Joint venture and associates financial results	Group net share of joint ventures and associates	Joint venture and associates financial results
			Group net share of joint ventures and associates
all figures in £ million			
Non-current assets	0.3	0.1	0.3
Current assets	8.0	3.9	4.2
Current liabilities	8.3	4.0	4.5
Non-current liabilities	(7.6)	(3.7)	(3.4)
Net assets of joint ventures and associates	0.7	0.3	0.8
Other non-current investments		0.1	0.1
<b>Total</b>	<b>0.7</b>	<b>0.4</b>	<b>0.8</b>
			0.5

During the year ended 31 March 2015 there were sales to associates of £3.0m (2014: £3.3m). At the year end there were outstanding receivables from associates of £0.3m (2014: £0.1m).

## 18. Deferred tax

Deferred tax assets and liabilities are offset only where there is a legally enforceable right to do so and there is an intention to settle the balances net.

Movements in the deferred tax assets and liabilities are shown below:

Year ended 31 March 2015

### Deferred tax asset

all figures in £ million	Pension liability	Trading losses	Short-term timing differences	Total
At 1 April 2014	1.3	–	27.5	28.8
(Charged)/credited to income statement	(4.8)	25.2	(7.4)	13.0
Credited to other comprehensive income	5.1	–	–	5.1
Foreign exchange	–	–	1.9	1.9
Eliminated on disposal	–	–	(14.4)	(14.4)
<b>Gross deferred tax asset at 31 March 2015</b>	<b>1.6</b>	<b>25.2</b>	<b>7.6</b>	<b>34.4</b>
Less: liability available for offset				(21.5)
<b>Net deferred tax asset at 31 March 2015</b>				<b>12.9</b>

### Deferred tax liability

all figures in £ million	Accelerated capital allowances	Amortisation	Total
At 1 April 2014	(17.5)	(8.2)	(25.7)
(Charged)/credited to income statement	(1.3)	0.9	(0.4)
Eliminated on disposal	0.7	4.1	4.8
Foreign exchange	–	(0.6)	(0.6)
Deferred tax impact of change in rates	0.4	–	0.4
<b>Gross deferred tax liability at 31 March 2015</b>	<b>(17.7)</b>	<b>(3.8)</b>	<b>(21.5)</b>
Less: asset available for offset			21.5
<b>Net deferred tax liability at 31 March 2015</b>			–

At the balance sheet date the Group had unused tax losses of £291.6m (2014: £213.9m) potentially available for offset against future profits. An asset of £25.2m has been recognised in respect of an element of these unused losses, relating to certain UK trading losses which are expected to be utilised in the foreseeable future. No deferred tax asset is recognised in respect of the other losses due to uncertainty over the timing of their utilisation. These losses can be carried forward indefinitely. Balances eliminated on disposal are in respect of the disposal of the US Services division (see note 5).

## 18. Deferred tax continued

Year ended 31 March 2014

### Deferred tax asset

all figures in £ million	Pension liability	Short-term timing differences	Total
At 1 April 2013	13.7	29.9	43.6
(Charged)/credited to income statement	(13.0)	(4.7)	(17.7)
(Charged)/credited to other comprehensive income	1.2	(0.1)	1.1
Prior-year adjustment	0.1	1.4	1.5
Foreign exchange	–	(2.8)	(2.8)
Transfer to current tax	–	3.8	3.8
Deferred tax impact of change in rates	(0.7)	–	(0.7)
<b>Gross deferred tax asset at 31 March 2014</b>	<b>1.3</b>	<b>27.5</b>	<b>28.8</b>
Less: liability available for offset			(10.7)
<b>Net deferred tax asset at 31 March 2014</b>			<b>18.1</b>

### Deferred tax liability

all figures in £ million	Accelerated capital allowances	Amortisation	Total
At 1 April 2013	0.6	(11.8)	(11.2)
(Charged)/credited to income statement	(17.7)	2.6	(15.1)
Prior year adjustment	(0.3)	–	(0.3)
Foreign exchange	0.1	1.0	1.1
Deferred tax impact of change in rates	(0.2)	–	(0.2)
<b>Gross deferred tax liability at 31 March 2014</b>	<b>(17.5)</b>	<b>(8.2)</b>	<b>(25.7)</b>
Less: asset available for offset			10.7
<b>Net deferred tax liability at 31 March 2014</b>			<b>(15.0)</b>

## 19. Inventories

As at 31 March

all figures in £ million	2015	2014
Raw materials	9.6	11.4
Work in progress	3.3	4.8
Finished goods	5.6	3.6
	<b>18.5</b>	<b>19.8</b>

## 20. Current asset investments

As at 31 March

all figures in £ million	2015	2014
<b>Available-for-sale investment</b>	<b>2.3</b>	<b>2.1</b>

At 31 March 2015 the Group held a 4.9% shareholding in pSivida Limited (31 March 2014: 4.9%), a company listed on NASDAQ and the Australian and Frankfurt Stock Exchanges. The investment is held at fair value of £2.3m (2014: £2.1m) using the closing share price at 31 March 2015 of AUS\$5.08 per share (31 March 2014: AUS\$4.32 per share).

## 21. Trade and other receivables

As at 31 March

all figures in £ million	2015	2014
Trade receivables	82.0	136.3
Amounts recoverable under contracts	51.6	90.0
Other receivables	15.8	12.5
Prepayments	9.8	11.7
	<b>159.2</b>	<b>250.5</b>

In determining the recoverability of trade receivables, the Group considers any change in the credit quality of the trade receivable from the date credit was granted to the reporting date. Credit risk is limited as a result of the high percentage of revenue derived from UK and US government agencies. Accordingly, the Directors believe that no credit provision in excess of the allowance for doubtful debts is required. As at 31 March 2015 the Group carried a provision for doubtful debts of £3.3m (2014: £2.9m).

**Ageing of past due but not impaired receivables**

	2015	2014
Up to three months	13.0	43.7
Over three months	0.7	3.7
	<b>13.7</b>	<b>47.4</b>

**Movements in the doubtful debt provision**

	2015	2014
<b>At 1 April</b>	2.9	1.9
Created	1.8	1.9
Released	(0.5)	(0.9)
Divestments	(0.3)	–
Utilised	(0.6)	–
<b>At 31 March</b>	<b>3.3</b>	<b>2.9</b>

The maximum exposure to credit risk in relation to trade receivables at the reporting date is the fair value of trade receivables.

The Group does not hold any collateral as security. Divestments are in respect of the disposal of the US Services division (see note 5).

## 22. Trade and other payables

As at 31 March

	2015	2014
Trade payables	29.5	42.6
Other tax and social security	31.9	30.1
Other payables	5.6	11.8
Accruals and deferred income	285.3	341.1
<b>Total current trade and other payables</b>	<b>352.3</b>	<b>425.6</b>
Payments received on account	9.6	8.3
Other payables	0.8	2.9
<b>Total non-current trade and other payables</b>	<b>10.4</b>	<b>11.2</b>
<b>Total trade and other payables</b>	<b>362.7</b>	<b>436.8</b>

## 23. Provisions

Year ended 31 March 2015

	Restructuring	Property	Warranty and indemnities	Other	Total
At 1 April 2014	5.0	12.6	–	6.5	24.1
Created in year	–	2.9	5.9	0.9	9.7
Released in year	(1.4)	(0.3)	–	(1.5)	(3.2)
Unwind of discount	–	0.4	–	–	0.4
Utilised in year	(0.6)	(2.1)	–	(0.4)	(3.1)
Divestments	(3.0)	–	–	–	(3.0)
Foreign exchange	–	–	0.5	–	0.5
<b>At 31 March 2015</b>	<b>–</b>	<b>13.5</b>	<b>6.4</b>	<b>5.5</b>	<b>25.4</b>
Current liability	–	2.3	–	0.7	3.0
Non-current liability	–	11.2	6.4	4.8	22.4
<b>At 31 March 2015</b>	<b>–</b>	<b>13.5</b>	<b>6.4</b>	<b>5.5</b>	<b>25.4</b>

Restructuring provisions related to historic cost reduction initiatives in the US and included redundancy and vacant property provisions.

Property provisions, other than those relating to restructuring discussed above, relate to under-utilised properties in the UK. The extent of the provision is affected by the timing of when properties can be sub-let and the proportion of space that can be sub-let. Based on current assessment the provision will be utilised within 11 years.

Other provisions relate to environmental and other liabilities, the magnitude and timing of utilisation of which are determined by a variety of factors.

Divestments are in respect of the disposal of the US Services division (see note 5).

## 24. Net cash

As at 31 March

all figures in £ million	2015			2014		
	Assets	Liabilities	Net	Assets	Liabilities	Net
<b>Current financial assets/(liabilities)</b>						
Deferred financing costs	0.3	–	0.3	–	0.5	0.5
Borrowings	0.3	–	0.3	–	0.5	0.5
Available-for-sale investment	10.0	–	10.0	–	–	–
Derivative financial instruments	0.5	(0.5)	–	0.3	(0.1)	0.2
Finance lease debtor/(creditor)	1.5	(1.4)	0.1	2.8	(2.6)	0.2
<b>Total current financial assets/(liabilities)</b>	<b>12.3</b>	<b>(1.9)</b>	<b>10.4</b>	<b>3.1</b>	<b>(2.2)</b>	<b>0.9</b>
<b>Non-current assets/(liabilities)</b>						
US\$ private placement notes – 7.13%	–	–	–	–	(26.6)	(26.6)
US\$ private placement notes – 5.50%	–	–	–	–	(29.2)	(29.2)
US\$ private placement notes – 7.62%	–	–	–	–	(96.9)	(96.9)
Deferred financing costs	0.8	–	0.8	–	–	–
Borrowings	0.8	–	0.8	–	(152.7)	(152.7)
Derivative financial instruments	0.1	(0.1)	–	0.1	–	0.1
Finance lease debtor/(creditor)	–	–	–	1.4	(1.4)	–
<b>Total non-current financial assets/(liabilities)</b>	<b>0.9</b>	<b>(0.1)</b>	<b>0.8</b>	<b>1.5</b>	<b>(154.1)</b>	<b>(152.6)</b>
Cash	41.6	–	41.6	53.7	–	53.7
Cash equivalents	142.7	–	142.7	268.5	–	268.5
<b>Total cash and cash equivalents</b>	<b>184.3</b>	<b>–</b>	<b>184.3</b>	<b>322.2</b>	<b>–</b>	<b>322.2</b>
<b>Total net cash as defined by the Group</b>			<b>195.5</b>			<b>170.5</b>

At 31 March 2015 £1.3m (2014: £2.2m) of cash was held by the Group's captive insurance subsidiary, including £0.1m (2014: £0.1m) that was restricted in its use.

All US\$ private placement notes were repaid in the year. The Circular seeking shareholder approval for the sale of the US Services division specified that the proceeds would be applied in settling the remaining private placement debt of \$248m which was put in place to finance the acquisitions of the US Services business.

## Reconciliation of net cash flow to movement in net cash

all figures in £ million	2015	2014
(Decrease)/increase in cash and cash equivalents in the year	(137.3)	85.9
Repayment of US\$ private placement notes	147.1	–
Outflow in respect of available for sale investment	10.0	–
Payment of bank loan arrangement fee	1.3	–
Capital element of finance lease payments	2.8	2.8
Capital element of finance lease receipts	(3.0)	(3.0)
<b>Change in net cash resulting from cash flows</b>	<b>20.9</b>	<b>85.7</b>
Cash and cash equivalents disposed	(1.0)	–
Amortisation of deferred financing costs	(0.7)	(0.6)
Finance lease receivables	0.3	0.4
Finance lease payables	(0.2)	(0.4)
Foreign exchange and other non-cash movements	5.7	11.4
<b>Movement in net cash in year</b>	<b>25.0</b>	<b>96.5</b>
Net cash at beginning of year	170.5	74.0
<b>Net cash at 31 March</b>	<b>195.5</b>	<b>170.5</b>

## Finance leases

### Group as a lessor

The minimum lease receivables under finance leases fall as follows:

all figures in £ million	Minimum lease payments		Present value of minimum lease payments	
	2015	2014	2015	2014
<b>Amounts receivable under finance leases</b>				
Within one year	1.5	3.0	1.5	2.8
In the second to fifth years inclusive	—	1.5	—	1.4
	1.5	4.5	1.5	4.2
Less: unearned finance income	—	(0.3)	—	—
<b>Present value of minimum lease payments</b>	<b>1.5</b>	<b>4.2</b>	<b>1.5</b>	<b>4.2</b>

The Group leases out certain buildings under finance leases that expire in the year to 31 March 2016.

### Group as a lessee

The minimum lease payments under finance leases fall due as follows:

all figures in £ million	Minimum lease payments		Present value of minimum lease payments	
	2015	2014	2015	2014
<b>Amounts payable under finance leases</b>				
Within one year	1.4	2.8	1.4	2.6
In the second to fifth years inclusive	—	1.4	—	1.4
	1.4	4.2	1.4	4.0
Less future finance charges	—	(0.2)	—	—
<b>Present value of minimum lease payments</b>	<b>1.4</b>	<b>4.0</b>	<b>1.4</b>	<b>4.0</b>
<b>Classified as follows:</b>				
Financial liability – current			1.4	2.6
Financial liability – non-current			—	1.4
			1.4	4.0

The Group utilises certain buildings under finance leases that expire in the year to 31 March 2016.

## 25. Operating leases

### Group as a lessor

The Group receives rental income on certain properties. Primarily these are properties partially occupied by Group companies, with vacant space sub-let to third-party tenants. The Group had contracted with tenants for the following future minimum lease payments:

all figures in £ million	2015	2014
Within one year	7.3	8.3
In the second to fifth years inclusive	19.1	22.0
Greater than five years	10.9	6.6
	37.3	36.9

### Group as a lessee

all figures in £ million	2015	2014
Lease and sub-lease income statement expense – minimum lease payments	6.1	18.9

The Group had the following total future minimum lease payment commitments:

all figures in £ million	2015	2014
Within one year	5.0	17.8
In the second to fifth years inclusive	6.8	44.1
Greater than five years	1.2	18.2
	13.0	80.1

Operating lease payments represent rentals payable by the Group on certain property, plant and equipment. Principal operating leases are negotiated for a term of approximately ten years. The majority of the Group's operating lease expense in 2014 was in respect of leases held by the US Services division. This division was divested in the year resulting in a significant reduction in operating lease expense in the continuing operations.

## 26. Financial risk management

The Group's international operations expose it to financial risks that include the effects of changes in foreign exchange rates, interest rates, credit risks and liquidity risks.

Treasury and risk management policies, which are set by the Board, specify guidelines on financial risks and the use of financial instruments to manage risk. The instruments and techniques used to manage exposures include foreign currency derivatives and interest rate derivatives. Group treasury monitors financial risks and compliance with risk management policies. There have been no changes in any risk management policies since the year end.

### A) Fair values of financial instruments

The table below analyses financial instruments carried at fair value, by valuation method. The different levels have been defined as follows:

Level 1 – measured using quoted prices (unadjusted) in active markets for identical assets or liabilities;

Level 2 – measured using inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices). Level 2 derivatives comprise forward foreign exchange contracts which have been fair valued using forward exchange rates that are quoted in an active market; and

Level 3 – measured using inputs for the assets or liability that are not based on observable market data (i.e. unobservable inputs).

The following table presents the Group's assets and liabilities that are measured at fair value as at 31 March 2015:

all figures in £ million	Note	Level 1	Level 2	Level 3	Total
<b>Assets</b>					
Available for sale investments	24	10.0	–	–	10.0
Current other investments	20	2.3	–	–	2.3
Current derivative financial instruments	24	–	0.5	–	0.5
Non-current other investments	–	–	–	0.1	0.1
Non-current derivative financial instruments	24	–	0.1	–	0.1
<b>Liabilities</b>					
Current derivative financial instruments	24	–	(0.5)	–	(0.5)
Non-current derivative financial instruments	24	–	(0.1)	–	(0.1)
<b>Total</b>		<b>12.3</b>	<b>–</b>	<b>0.1</b>	<b>12.4</b>

The following table presents the Group's assets and liabilities that are measured at fair value as at 31 March 2014:

all figures in £ million	Note	Level 1	Level 2	Level 3	Total
<b>Assets</b>					
Current other investments	20	2.1	–	–	2.1
Current derivative financial instruments	24	–	0.3	–	0.3
Non-current other investments	–	–	–	0.1	0.1
Non-current derivative financial instruments	–	–	0.1	–	0.1
<b>Liabilities</b>					
Non-current derivative financial instruments	24	–	(0.1)	–	(0.1)
<b>Total</b>		<b>2.1</b>	<b>0.3</b>	<b>0.1</b>	<b>2.5</b>

For cash and cash equivalents, trade and other receivables and bank and current borrowings, the fair value of the financial instruments approximate to their carrying value as a result of the short maturity periods of these financial instruments. For trade and other receivables, allowances are made within the carrying value for credit risk. For other financial instruments, the fair value is based on market value, where available. Where market values are not available, the fair values have been calculated by discounting cash flows to net present value using prevailing market-based interest rates translated at the year end rates, except for unlisted fixed asset investments where fair value equals carrying value. There have been no transfers between levels.

All financial assets and liabilities have a fair value that is identical to book value at 31 March 2015 and 31 March 2014 except where noted below:

As at 31 March 2015

all figures in £ million	Note	Available for sale	Loans and receivables	Financial liabilities at amortised cost	Derivatives used as hedges	Total carrying value	Total fair value
<b>Financial assets</b>							
<b>Non-current</b>							
Derivative financial instruments	24	—	—	—	0.1	0.1	0.1
Other investments	17	0.1	—	—	—	0.1	0.1
<b>Current</b>							
Finance leases	24	—	1.5	—	—	1.5	1.5
Trade and other receivables	21	—	159.2	—	—	159.2	159.2
Derivative financial instruments	24	—	—	—	0.5	0.5	0.5
Current asset investments	20	2.3	—	—	—	2.3	2.3
Available for sale investment		10.0	—	—	—	10.0	10.0
Cash and cash equivalents	24	—	184.3	—	—	184.3	184.3
<b>Total financial assets</b>		<b>12.4</b>	<b>345.0</b>	—	<b>0.6</b>	<b>358.0</b>	<b>358.0</b>
<b>Financial liabilities</b>							
<b>Non-current</b>							
Trade and other payables	22	—	—	(10.4)	—	(10.4)	(10.4)
Deferred financing costs	24	—	—	0.8	—	0.8	0.8
Derivative financial instruments	24	—	—	—	(0.1)	(0.1)	(0.1)
<b>Current</b>							
Trade and other payables	22	—	—	(352.3)	—	(352.3)	(352.3)
Derivative financial instruments	24	—	—	—	(0.5)	(0.5)	(0.5)
Finance leases	24	—	—	(1.4)	—	(1.4)	(1.4)
Deferred financing costs	24	—	—	0.3	—	0.3	0.3
<b>Total financial liabilities</b>		<b>—</b>	<b>—</b>	<b>(363.0)</b>	<b>(0.6)</b>	<b>(363.6)</b>	<b>(363.6)</b>
<b>Total</b>		<b>12.4</b>	<b>345.0</b>	<b>(363.0)</b>	—	<b>(5.6)</b>	<b>(5.6)</b>

As at 31 March 2014

all figures in £ million	Note	Available for sale	Loans and receivables	Financial liabilities at amortised cost	Derivatives used as hedges	Total carrying value	Total fair value
<b>Financial assets</b>							
<b>Non-current</b>							
Finance leases	24	—	1.4	—	—	1.4	1.5
Derivative financial instruments	24	—	—	—	0.1	0.1	0.1
Other investments	17	0.1	—	—	—	0.1	0.1
<b>Current</b>							
Finance leases	24	—	2.8	—	—	2.8	2.9
Trade and other receivables	21	—	250.5	—	—	250.5	250.5
Derivative financial instruments	24	—	—	—	0.3	0.3	0.3
Current asset investments	20	2.1	—	—	—	2.1	2.1
Cash and cash equivalents	24	—	322.2	—	—	322.2	322.2
<b>Total financial assets</b>		<b>2.2</b>	<b>576.9</b>	—	<b>0.4</b>	<b>579.5</b>	<b>579.7</b>
<b>Financial liabilities</b>							
<b>Non-current</b>							
Trade and other payables	22	—	—	(11.2)	—	(11.2)	(11.2)
Bank and other borrowings	24	—	—	(152.7)	—	(152.7)	(175.5)
Finance leases	24	—	—	(1.4)	—	(1.4)	(1.4)
<b>Current</b>							
Trade and other payables	22	—	—	(425.6)	—	(425.6)	(425.6)
Derivative financial instruments	24	—	—	—	(0.1)	(0.1)	(0.1)
Finance leases	24	—	—	(2.6)	—	(2.6)	(2.8)
Deferred financing costs	24	—	—	0.5	—	0.5	0.5
<b>Total financial liabilities</b>		<b>—</b>	<b>—</b>	<b>(593.0)</b>	<b>(0.1)</b>	<b>(593.1)</b>	<b>(616.1)</b>
<b>Total</b>		<b>2.2</b>	<b>576.9</b>	<b>(593.0)</b>	<b>0.3</b>	<b>(13.6)</b>	<b>(36.4)</b>

## 26. Financial risk management continued

As at 31 March 2015 there are no financial assets or liabilities that have a fair value that is different from the carrying value.

The following table presents the fair value of the Group's assets and liabilities that have a fair value that is different from the carrying value as at 31 March 2014:

all figures in £ million	Level 1	Level 2	Level 3	Total
<b>Assets</b>				
Finance leases	–	4.4	–	4.4
<b>Liabilities</b>				
Finance leases	–	(4.2)	–	(4.2)
Non-current bank and other borrowings	–	(175.5)	–	(175.5)
<b>Total</b>	<b>–</b>	<b>(175.3)</b>	<b>–</b>	<b>(175.3)</b>

### B) Interest rate risk

The Group operates an interest rate policy designed to optimise interest costs and to reduce volatility in reported earnings. The Group's current policy is to require rates to be fixed for 30%–80% of the level of borrowings, which is achieved primarily through fixed-rate borrowings. Where there are significant changes in the level and/or structure of debt, policy permits borrowings to be 100% fixed, with regular Board reviews of the appropriateness of this fixed percentage. At 31 March 2015 100% (2014: 100%) of the Group's borrowings were at fixed rates with no adjustment for interest rate swaps.

#### Financial assets/(liabilities)

As at 31 March 2015

all figures in £ million	Financial asset			Financial liability		
	Fixed or capped	Floating	Non-interest bearing	Fixed or capped	Floating	Non-interest bearing
Sterling	1.5	163.9	10.6	(1.4)	–	(0.6)
US dollar	–	14.7	0.1	–	–	–
Euro	–	1.9	–	–	–	–
Australian dollar	–	3.0	2.3	–	–	–
Other	–	0.8	–	–	–	–
	<b>1.5</b>	<b>184.3</b>	<b>13.0</b>	<b>(1.4)</b>	<b>–</b>	<b>(0.6)</b>

As at 31 March 2014

all figures in £ million	Financial asset			Financial liability		
	Fixed or capped	Floating	Non-interest bearing	Fixed or capped	Floating	Non-interest bearing
Sterling	4.2	280.1	0.4	(4.0)	–	(0.1)
US dollar	–	30.5	0.1	(152.7)	–	–
Euro	–	2.3	–	–	–	–
Australian dollar	–	8.4	2.1	–	–	–
Other	–	0.9	–	–	–	–
	<b>4.2</b>	<b>322.2</b>	<b>2.6</b>	<b>(156.7)</b>	<b>–</b>	<b>(0.1)</b>

Floating-rate financial assets attract interest based on the relevant national LIBID equivalent. Floating-rate financial liabilities bear interest at the relevant national LIBOR equivalent. Trade and other receivables/payables and deferred finance costs are excluded from this analysis.

For the fixed or capped-rate financial assets and liabilities, the average interest rates (including the relevant marginal cost of borrowing) and the average period for which the rates are fixed are:

	2015			2014		
	Fixed or capped £m	Weighted average interest rate %	Weighted average years to maturity	Fixed or capped £m	Weighted average interest rate %	Weighted average years to maturity
Financial assets:						
Sterling	1.5	13.4	0.5	4.2	13.4	1.5
Financial liabilities:						
Sterling	(1.4)	12.1	0.5	(4.0)	12.1	1.5
US dollar	–	–	–	(152.7)	7.1	3.9
<b>Total financial liabilities</b>	<b>(1.4)</b>	<b>12.1</b>	<b>0.5</b>	<b>(156.7)</b>	<b>7.3</b>	<b>3.8</b>

Sterling assets and liabilities consist primarily of finance leases with the weighted average interest rate reflecting the internal rate of return of those leases.

### Interest rate risk management

The Group private placement borrowings were repaid during the year and were fixed-rate, while the revolving credit facility is floating-rate and undrawn as at 31 March 2015.

## C) Currency risk

### Transactional currency exposure

The Group is exposed to foreign currency risks arising from sales or purchases by businesses in currencies other than their functional currency. It is Group policy that when such a sale or purchase is certain, the net foreign exchange exposure is hedged using forward foreign exchange contracts. Hedge accounting documentation and effectiveness testing are undertaken for all the Group's transactional hedge contracts.

The table below shows the Group's currency exposures, being exposures on currency transactions that give rise to net currency gains and losses recognised in the income statement. Such exposures comprise the monetary assets and liabilities of the Group that are not denominated in the functional currency of the operating company involved.

#### Functional currency of the operating company

all figures in £ millions	Net foreign currency monetary assets/(liabilities)				
	US\$	Euro	AUS\$	Other	Total
<b>31 March 2015 – sterling</b>	<b>(5.9)</b>	<b>2.0</b>	<b>(0.1)</b>	<b>0.8</b>	<b>(3.2)</b>
31 March 2014 – sterling	(18.1)	(2.2)	2.1	0.6	(17.6)

The amounts shown in the table take into account the effect of the forward contracts entered into to manage these currency exposures.

The Group enters into forward foreign currency contracts to hedge the currency exposures that arise on sales and purchases denominated in foreign currencies, as the transaction occurs. The principal contract amounts of the outstanding forward currency contracts as at 31 March 2015 against sterling are net US dollars sold £24.3m (US\$36.0m) and net euros sold £1.1m (€1.5m).

### Translational currency exposure

The Group has significant investments in overseas operations, particularly in the US. As a result, the sterling value of the Group's balance sheet can be significantly affected by movement in exchange rates. The Group does not hedge against translational currency exposure to overseas net assets.

## D) Financial credit risk

The Group is exposed to credit-related losses in the event of non-performance by counterparties to financial instruments, but does not currently expect any counterparties to fail to meet their obligations. Credit risk is mitigated by a Board-approved policy of only selecting counterparties with a strong investment grade long-term credit rating for cash deposits. In the normal course of business the Group operates notional cash pooling systems, where a legal right of set-off applies.

The maximum credit-risk exposure in the event of other parties failing to perform their obligations under financial assets, excluding trade and other receivables, totals £198.8m (2014: £329.0m). The Group held cash and cash equivalents of £184.3m at 31 March 2015 (2014: £322.2m), which represents the maximum credit exposure on these assets. The cash and cash equivalents were held with different financial institutions which were rated single A or better, although £142.7m (2014: £218.5m) was invested in AAA-rated money funds at the year end and £50m was invested in deposits collateralised by security, where the security was gilts.

## 26. Financial risk management continued

### E) Liquidity risk

#### Borrowing facilities

As at 31 March 2015 the Group had a revolving credit facility (RCF) of US\$100m and £166m (2014: US\$250m and £118m).

The RCF is contracted until 2019 and is un-utilised as shown in the table below:

	Interest rate: LIBOR plus	Total £m	Drawn £m	Undrawn £m
Committed facilities 31 March 2015	0.65%	233.3	—	233.3
Freely available cash and cash equivalents				184.2
<b>Available funds 31 March 2015</b>				<b>417.5</b>
Committed facilities 31 March 2014	1.20%	267.9	—	267.9
Freely available cash and cash equivalents				322.1
<b>Available funds 31 March 2014</b>				<b>590.0</b>

#### Gross contractual cash flows for borrowings and other financial liabilities

The following are the contractual maturities of financial liabilities, including interest payments. The cash flows associated with derivatives that are cash flow hedges are expected to have an impact on profit or loss in the periods shown.

As at 31 March 2015

all figures in £ million	Book value	Contractual cash flows	1 year or less	1–2 years	2–5 years	More than 5 years
<b>Non-derivative financial liabilities</b>						
Trade and other payables	(362.7)	(362.7)	(352.3)	(10.4)	—	—
Recapitalisation fee	1.1	—	—	—	—	—
Finance leases	(1.4)	(1.4)	(1.4)	—	—	—
<b>Derivative financial liabilities</b>						
Forward foreign currency contracts – cash flow hedges	(0.6)	(0.6)	(0.5)	(0.1)	—	—
	<b>(363.6)</b>	<b>(364.7)</b>	<b>(354.2)</b>	<b>(10.5)</b>	<b>—</b>	<b>—</b>

As at 31 March 2014

all figures in £ million	Book value	Contractual cash flows	1 year or less	1–2 years	2–5 years	More than 5 years
<b>Non-derivative financial liabilities</b>						
Trade and other payables	(436.8)	(436.8)	(425.6)	(11.2)	—	—
US private placement debt	(152.7)	(195.8)	(10.6)	(37.0)	(148.2)	—
Recapitalisation fee	0.5	—	—	—	—	—
Finance leases	(4.0)	(4.2)	(2.8)	(1.4)	—	—
<b>Derivative financial liabilities</b>						
Forward foreign currency contracts – cash flow hedges	(0.1)	(0.1)	(0.1)	—	—	—
	<b>(593.1)</b>	<b>(636.9)</b>	<b>(439.1)</b>	<b>(49.6)</b>	<b>(148.2)</b>	<b>—</b>

## F) Derivative financial instruments

As at 31 March

all figures in £ million	2015			2014		
	Asset gains	Liability losses	Net	Asset gains	Liability losses	Net
Forward foreign currency contracts – cash flow hedges	0.6	(0.6)	–	0.4	(0.1)	0.3
<b>Derivative assets/(liabilities) at the end of the year</b>	<b>0.6</b>	<b>(0.6)</b>	<b>–</b>	<b>0.4</b>	<b>(0.1)</b>	<b>0.3</b>

As at 31 March

all figures in £ million	2015			2014		
	Asset gains	Liability losses	Net	Asset gains	Liability losses	Net
Expected to be recognised:						
In one year or less	0.5	(0.5)	–	0.3	(0.1)	0.2
Between one and two years	–	(0.1)	(0.1)	0.1	–	0.1
More than two years	0.1	–	0.1	–	–	–
<b>Derivative assets/(liabilities) at the end of the year</b>	<b>0.6</b>	<b>(0.6)</b>	<b>–</b>	<b>0.4</b>	<b>(0.1)</b>	<b>0.3</b>

## G) Maturity of financial liabilities

As at 31 March 2015

all figures in £ million	Trade and other payables	Bank borrowings and loan notes	Finance leases and derivative financial instruments	Total
Due in one year or less	352.3	(0.3)	1.9	353.9
Due in more than one year but not more than two years	10.4	(0.3)	0.1	10.2
Due in more than two years but not more than five years	–	(0.5)	–	(0.5)
Due in more than five years	–	–	–	–
	<b>362.7</b>	<b>(1.1)</b>	<b>2.0</b>	<b>363.6</b>

As at 31 March 2014

all figures in £ million	Trade and other payables	Bank borrowings and loan notes	Finance leases and derivative financial instruments	Total
Due in one year or less	425.6	(0.5)	2.7	427.8
Due in more than one year but not more than two years	11.2	26.6	1.4	39.2
Due in more than two years but not more than five years	–	126.1	–	126.1
Due in more than five years	–	–	–	–
	<b>436.8</b>	<b>152.2</b>	<b>4.1</b>	<b>593.1</b>

## H) Sensitivity analysis

The Group's sensitivity to changes in foreign exchange rates and interest rates on financial assets and liabilities as at 31 March 2015 is set out in the following table. The impact of a weakening in sterling on the Group's financial assets and liabilities would be more than offset in equity and income by its impact on the Group's overseas net assets and earnings respectively. Sensitivity on Group's assets other than financial assets and liabilities is not included in this analysis.

The amounts generated from the sensitivity analysis are forward-looking estimates of market risk assuming that certain market conditions occur. Actual results in the future may differ materially from those projected as a result of developments in the global financial markets that may cause fluctuations in interest and exchange rates to vary from the hypothetical amounts disclosed in the following table, which should not, therefore, be considered to be a projection of likely future events and losses.

The estimated changes for interest rate movements are based on an instantaneous decrease or increase of 1% (100 basis points) in the specific rate of interest applicable to each class of financial instruments from the levels effective at 31 March 2015, with all other variables remaining constant. The estimated changes for foreign exchange rates are based on an instantaneous 10% weakening or strengthening in sterling against all other currencies from the levels applicable at 31 March 2015, with all other variables remaining constant. Such analysis is for illustrative purposes only – in practice market rates rarely change in isolation.

The impact of transactional risk on the Group's monetary assets/liabilities that are not held in the functional currency of the entity holding those assets/liabilities is minimal. A 10% weakening in sterling would result in a £0.4m decrease in profit before tax.

## 26. Financial risk management continued

As at 31 March 2015

all figures in £ million	1% decrease in interest rates		10% weakening in sterling	
	Equity <sup>1</sup>	Profit before tax	Equity	Profit before tax
Sterling	–	(1.6)	–	–
US dollar	–	(0.1)	1.6	–
Other	–	(0.1)	0.9	–

all figures in £ million	1% increase in interest rates		10% strengthening in sterling	
	Equity <sup>1</sup>	Profit before tax	Equity	Profit before tax
Sterling	–	1.6	–	–
US dollar	–	0.1	(1.3)	–
Other	–	0.1	(0.7)	–

As at 31 March 2014

all figures in £ million	1% decrease in interest rates		10% weakening in sterling	
	Equity <sup>1</sup>	Profit before tax	Equity	Profit before tax
Sterling	–	(2.8)	–	–
US dollar	–	(0.3)	(13.6)	(1.2)
Other	–	(0.1)	1.5	–

all figures in £ million	1% increase in interest rates		10% strengthening in sterling	
	Equity <sup>1</sup>	Profit before tax	Equity	Profit before tax
Sterling	–	2.8	–	–
US dollar	–	0.3	11.1	1.0
Other	–	0.1	(1.3)	–

<sup>1</sup> This relates to the impact on items charged directly to equity and excludes the impact on profit/loss for the year flowing into equity.

## 27. Cash flows from operations

For the year ended 31 March

all figures in £ million	2015	2014
<b>Profit/(loss) after tax for the year</b>	<b>104.7</b>	<b>(12.7)</b>
Adjustments for:		
Taxation (income)/expense	(11.8)	16.8
Net finance costs	4.1	15.0
Loss on business divestments and disposal of investments	12.9	4.9
Reversal of unutilised restructuring provisions	(1.0)	–
Amortisation of purchased or internally developed intangible assets	1.5	1.0
Amortisation of intangible assets arising from acquisitions	3.6	11.0
Impairment of goodwill	–	125.9
Depreciation and impairment of property, plant and equipment	22.0	22.6
Loss on disposal of property, plant and equipment	1.2	1.4
Share of post-tax (loss)/profit of equity accounted entities	0.1	(0.1)
Share-based payments charge	3.6	4.5
Changes in retirement benefit obligations	(7.9)	(8.1)
Pension curtailment gain	–	(31.1)
Net movement in provisions	(1.6)	(10.5)
	131.4	140.6
Decrease in inventories	2.6	4.4
Decrease in receivables	27.3	21.7
Decrease in payables	(22.2)	(23.7)
<b>Changes in working capital</b>	<b>7.7</b>	<b>2.4</b>
<b>Cash generated from operations</b>	<b>139.1</b>	<b>143.0</b>
Add back: cash outflow relating to restructuring	0.6	10.3
Add back: disposal-related pension contribution	6.0	–
Less: cash generated from discontinued operations	(1.8)	(30.3)
Add back: cash outflow relating to pension scheme closure costs	–	4.0
<b>Net cash flow from operations before restructuring costs</b>	<b>143.9</b>	<b>127.0</b>

## 28. Share capital and other reserves

Shares allotted, called up and fully paid:

	Ordinary shares of 1p each (equity)		Special Share of £1 (non-equity)		Total	
	£	Number	£	Number	£	Number
At 1 April 2013	6,604,764	660,476,373	1	1	6,604,765	660,476,374
Issued in the year	—	—	—	—	—	—
At 31 March 2014	<b>6,604,764</b>	<b>660,476,373</b>	<b>1</b>	<b>1</b>	<b>6,604,765</b>	<b>660,476,374</b>
Issued in the year	—	—	—	—	—	—
Cancelled in the year	(518,664)	(51,866,369)	—	—	(518,664)	(51,866,369)
<b>At 31 March 2015</b>	<b>6,086,100</b>	<b>608,610,004</b>	<b>1</b>	<b>1</b>	<b>6,086,101</b>	<b>608,610,005</b>

Except as noted below all shares in issue at 31 March 2015 rank pari-passu in all respects.

In May 2014 the Company initiated a £150m capital return to shareholders by way of a share buyback. At 31 March 2015 £107m of this programme was complete.

### Rights attaching to the Special Share

QinetiQ carries out activities which are important to UK defence and security interests. To protect these interests in the context of the ongoing commercial relationship between the MOD and QinetiQ, and to promote and reinforce the Compliance Principles, the MOD holds a Special Share in QinetiQ. QinetiQ obtained MOD consent to changes in its Special Shareholder rights, which were approved by shareholders at the 2012 AGM. The changes to the Special Share were disclosed in the 2012 Annual Report. Subsequent to the changes approved at the 2012 AGM the Special Share confers certain rights on the holder:

- to require the Group to implement and maintain the Compliance System (as defined in the Articles of Association) so as to make at all times effective its and each member of QinetiQ Controlled Group's application of the Compliance Principles, in a manner acceptable to the Special Shareholder;
- to refer matters to the Board for its consideration in relation to the application of the Compliance Principles;
- to require the Board to obtain Special Shareholder's consent:
  - if at any time when the chairman is not a British Citizen, it is proposed to appoint any person to the office of chief executive, who is not a British Citizen; and
  - if at any time when the chief executive is not a British Citizen, it is proposed to appoint any person to the office of chairman, who is not a British Citizen;
- to require the Board to take action to rectify any omission in the application of the Compliance Principles, if the Special Shareholder is of the opinion that such steps are necessary to protect the defence or security interests of the United Kingdom; and
- to demand a poll at any of QinetiQ's meetings (even though it may have no voting rights except those specifically set out in the Articles).

The Special Shareholder has an option to purchase defined Strategic Assets of the Group in certain circumstances. The Special Shareholder has, inter alia, the right to purchase any Strategic Assets which the Group wishes to sell. Strategic Assets are normally testing and research facilities (see note 31 for further details).

The Special Share may only be issued to, held by and transferred to HM Government (or as it directs). At any time the Special Shareholder may require QinetiQ to redeem the Special Share at par. If QinetiQ is wound up the Special Shareholder will be entitled to be repaid the capital paid up on the Special Share before other shareholders receive any payment. The Special Shareholder has no other right to share in the capital or profits of QinetiQ.

The Special Shareholder must give consent to a general meeting held on short notice.

The Special Share entitles the Special Shareholder to require certain persons who hold (together with any person acting in concert with them) a material interest in QinetiQ to dispose of some or all of their ordinary shares in certain prescribed circumstances on the grounds of national security or conflict of interest.

The Directors must register any transfer of the Special Share within seven days.

### Other reserves

The translation reserve includes the cumulative foreign exchange difference arising on translation since the Group transitioned to IFRS. Movements on hedge instruments, where the hedge is effective, are recorded in the hedge reserve until the hedge ceases.

The capital redemption reserve, which was created following the redemption of preference share capital and the bonus issue of shares, cannot be distributed.

### Own shares

Own shares represent shares in the Company that are held by independent trusts and include treasury shares and shares held by the employee share ownership plan. Included in retained earnings at 31 March 2015 are 5,443,881 shares (2014: 7,811,861 shares).

## 29. Share-based payments

The Group operates a number of share-based payment plans for employees. The total share-based payment expense in the year was £3.6m, of which £3.4m related to equity-settled schemes and £0.2m related to cash-settled schemes (year to 31 March 2014: £4.5m, of which £3.4m related to equity-settled schemes and £1.1m to cash-settled schemes).

### 2003 Employee share option scheme (2003 ESOS)

Under the employee share option scheme all employees as at 25 July 2003 received share options which vested when the Group completed its IPO and which must be exercised within ten years of grant. The options are settled by shares.

	2015		2014	
	Number	Weighted average exercise price	Number	Weighted average exercise price
Outstanding at start of year	–	–	352,314	2.3p
Exercised during year	–	–	(335,294)	2.3p
Forfeited during year	–	–	(17,020)	2.3p
<b>Outstanding at end of year</b>	<b>–</b>	<b>–</b>	<b>–</b>	<b>–</b>

The 2003 ESOS are equity-settled awards. In respect of the share options exercised during the prior year, the average share price on the date of exercise was 189.7p.

### Performance Share Plan (PSP)

In the year, the Group made awards of conditional shares to certain UK senior employees under the PSP. The awards vest after three years with 50% of the awards subject to TSR conditions and 50% subject to EPS conditions as detailed in the Report of the Remuneration Committee.

	2015		2014
	Number of shares	Number of shares	Number of shares
Outstanding at start of year	8,090,260	7,351,207	
Granted during year	4,310,206	3,489,504	
Exercised during the year	(461,196)	(907,312)	
Forfeited/lapsed during year	(2,481,862)	(1,843,139)	
<b>Outstanding at end of year</b>	<b>9,457,408</b>	<b>8,090,260</b>	

PSP awards are equity-settled awards and those outstanding at 31 March 2015 had an average remaining life of 1.3 years (2014: 1.5 years). There is no exercise price for these PSP awards. Monte Carlo modelling was used to fair value the TSR element of the awards at grant date. Assumptions used in the models included 24% (2014: 28%) for the average share price volatility of the FTSE comparator group and 51% (2014: 52%) for the average correlation to the comparator group. The weighted average fair value of grants made during the year was £1.57 (2014: £1.88). The weighted average share price at date of exercise was £1.97 (2014: £1.84). Of the options outstanding at the end of the year nil were exercisable (2014: nil).

### Restricted Stock Units (RSU)

In prior years the Group granted RSU awards to certain senior US employees under the RSU plan. The awards vest over one, two, three and four years. Of the 2014 awards, and the awards granted before 2012, half are dependent on achieving QNA organic profit growth targets and half on a time-based criterion. The time-based criterion requires the employee to have been in continual service up to the date of vesting. QNA organic profit growth is measured over the most recent financial year compared with the previous financial year, with 125% of this element awarded at a QNA organic profit growth rate above 15%, 100% awarded at 12.5%, 75% awarded at 10% and 25% awarded at 5%. The 2012 grants are entirely dependent on achieving QNA organic profit growth targets. 67.5% of the 2013 grants are dependent on achieving QNA organic profit growth targets and 32.5% are dependent on a time-based criterion.

	2015		2014
	Number of shares	Number of shares	Number of shares
Outstanding at start of year	3,819,001	5,249,861	
Granted during year	–	2,500,000	
Exercised during year	(196,154)	(354,362)	
Forfeited/lapsed during year	(3,447,660)	(3,576,498)	
<b>Outstanding at end of year</b>	<b>175,187</b>	<b>3,819,001</b>	

RSUs are equity-settled awards; those outstanding at 31 March 2015 had an average remaining life of 1.1 years (2014: 1.1 years). There is no exercise price for these RSU awards. The weighted average share price at date of exercise was £2.09 (2014: £1.91). The weighted average fair value of grants made during the prior year was £1.88. Of the awards outstanding at the end of the year none were exercisable (2014: nil).

## Value Sharing Plan (VSP)

In 2012 and 2011, the Group granted VSP awards to certain senior UK employees under the VSP. The awards vest over a three-year performance period: 50% of the 2012 awards and 70% of the 2011 awards (which vested in 2014) are/were dependent on creating additional shareholder value, measured as net cash returns to investors and the increase in PBT over an 8.5% hurdle; 50% of the 2012 awards and 30% of the 2011 awards are/were dependent on TSR against a comparator group of FTSE 250 listed companies (less investment trusts) over a three-year performance period. Half the awards vest three years from the date of grant; the remaining half of the awards vest four years from the date of grant.

	2015 Number of shares	2014 Number of shares
Outstanding at start of year	5,018,288	10,850,040
Exercised during year	(1,210,650)	(979,853)
Forfeited/lapsed during year	(3,653,790)	(4,851,899)
<b>Outstanding at end of year</b>	<b>153,848</b>	<b>5,018,288</b>

VSP awards are equity-settled awards; those outstanding at 31 March 2015 had an average remaining life of 0.2 years (2014: 0.6 years). There is no exercise price for these VSP awards. The weighted average share price at date of exercise was £2.04 (2014: £1.92). Of the awards outstanding at the end of the year nil were exercisable (2014: nil).

## Group Share Incentive Plan (SIP)

Under the QinetiQ SIP the Group offers UK employees the opportunity of purchasing up to £150 worth of shares a month at the prevailing market rate. The Group will make a matching share award of a third of the employee's payment. The Group's matching shares may be forfeited if the employee ceases to be employed by QinetiQ within three years of the award of the shares. There is no exercise price for these SIP awards.

	2015 Number of matching shares	2014 Number of matching shares
Outstanding at start of year	725,904	1,009,663
Awarded during year	280,267	228,066
Exercised during year	(309,350)	(467,228)
Forfeited during year	(49,000)	(44,597)
<b>Outstanding at end of year</b>	<b>647,821</b>	<b>725,904</b>

SIP matching shares are equity-settled awards; those outstanding at 31 March 2015 had an average remaining life of 1.5 years (2014: 1.5 years). There is no exercise price for these SIP awards. Of the shares outstanding at the end of the year nil were exercisable (2014: nil).

## Group Deferred Annual Bonus Plan (DAB)

Under the QinetiQ DAB Plan the Group requires certain senior executives to defer part of their annual bonus as shares and be entitled to matching awards to a maximum of 1:1 based on EPS performance. The number that will vest is dependent on the growth of EPS over the measurement period of three years as detailed in the Report of the Remuneration Committee.

	2015 Number of matching shares	2014 Number of matching shares
Outstanding at start of year	1,162,896	914,621
Granted during year	303,639	502,060
Exercised during the year	(85,126)	–
Forfeited during year	(917,294)	(253,785)
<b>Outstanding at end of year</b>	<b>464,115</b>	<b>1,162,896</b>

DAB matching shares are equity-settled awards; those outstanding at 31 March 2015 had an average remaining life of 1.2 years (2014: 1.4 years). The weighted average fair value of grants made during the year was £2.08 (2014: £1.80). The weighted average share price at date of exercise was £2.08 (2014: n/a). There is no exercise price for these DAB awards. Of the shares outstanding at the end of the year nil were exercisable (2014: nil).

## 29. Share-based payments continued

### Cash Alternative Units (CAUs)

During the year, the Group granted CAU awards to certain employees in the UK and US.

	2015 Number of awards	2014 Number of awards
Outstanding at start of year	1,229,541	2,246,979
Awarded during year	94,894	—
Exercised during the year	(364,362)	(274,188)
Forfeited during year	(670,051)	(743,250)
<b>Outstanding at end of year</b>	<b>290,022</b>	<b>1,229,541</b>

CAUs are cash-settled awards which vest over one, two, three and four years from the date of grant. The CAUs have no performance criteria attached, other than the requirement that the employee remains in employment with the Group. Those awards outstanding at 31 March 2015 had an average remaining life of 0.8 years (2014: 1.8 years). There is no exercise price for these awards. The fair value of the grants at 31 March 2015 was £1.91 (2014: £2.26) being the Group's closing share price on that day. The weighted average share price on the date of exercise was £2.08 (2014: £1.90). The carrying amount of the liability of the grants at the balance sheet date was £0.3m (2014: £1.1m). Of the awards outstanding at the end of the year nil were exercisable.

## Bonus Banking Plan (BBP)

During the year, the Group granted BBP awards to certain senior executives in the UK.

	2015 Number of awards
Outstanding at start of year	—
Awarded during year	330,725
<b>Outstanding at end of year</b>	<b>330,725</b>

The BBP is a remuneration scheme that runs for four years with effect from 1 April 2014. Refer to the Directors' Remuneration Report for further details. Under the BBP a contribution will be made by the Company into the participant's plan account at the start of each plan year. 50% of the plan account balance for Executive Directors and 75% for all other participants will be paid in cash or shares (at the Company's discretion) at the end of each plan year. 100% of the balance in year 4 will be paid in shares to the participant. During the four-year plan period, 50% of the retained balance is at risk of forfeiture based on a minimum level of performance determined annually by the Audit Committee.

At 31 March 2015, the awards had an average remaining life of 1.7 years. There is no exercise price for these awards. The fair value of the awards at 31 March 2015 was £1.91 being the Group's closing share price on that day. Of the awards outstanding at the end of the year nil were exercisable.

## Share-based award pricing – other

Share-based awards that vest based on non-market performance conditions, including certain PSP, RSUs and DAB awards, have been valued at the share price at grant, less attrition.

## 30. Post-retirement benefits

### Defined contribution plans

In the UK the Group operates two defined contribution plans for the majority of its UK employees: a Group Personal Pension Plan (GPP) and a defined contribution section of the QinetiQ Pension Scheme. These are both defined contribution schemes managed by Zurich. A defined contribution plan is a pension plan under which the Group and employees pay fixed contributions to a third-party financial provider. The Group has no legal or constructive obligations to pay further contributions if the fund does not hold sufficient assets to pay all employees the benefits relating to employee service in the current and prior periods. The contributions are recognised as an employee benefit expense when they are due. Prepaid contributions are recognised as an asset to the extent that a cash refund or a reduction in the future payments is available.

#### Defined benefit pension plans

In the UK the Group operates the QinetiQ Pension Scheme (the 'Scheme') for a significant proportion of its UK employees. The Scheme closed to future accrual on 31 October 2013. After this date, defined benefit members transferred to a defined contribution scheme. On closure, the Group realised a reduction in scheme liabilities of £31.1m and a one-off cost of £4.0m arising from associated contributions to affected members' defined contribution plans following the closure of the scheme. The Scheme is a final salary plan, which provides benefits to members in the form of a guaranteed level of pension payable for life. The level of benefits provided depends on the members' length of service and their final pensionable earnings at closure to future accrual. In the Scheme, pensions in payment are generally updated in line with the Consumer Price Index (CPI). The benefit payments are made from Trustee-administered funds. Plan assets held in trusts are governed by UK regulations as is the nature of the relationship between the Group and the Trustees and their composition. Responsibility for the governance of the Scheme – including investment decisions and contribution schedules – lies jointly with the Company and the Board of Trustees. The Board of Trustees must be composed of representatives of the Company and plan participants in accordance with the Scheme's regulations.

The liability recognised in the balance sheet in respect of defined benefit pension plans is the present value of the defined benefit obligation at the end of the reporting period less the fair value of plan assets. The defined benefit obligation is calculated bi-annually by independent actuaries using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of high quality corporate bonds that are denominated in the currency in which the benefits will be paid, and that have terms to maturity approximating to the terms of the related pension obligation. In countries where there is no deep market in such bonds, the market rates on government bonds are used.

Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions are charged or credited to equity in other comprehensive income in the period in which they arise.

The expected employer cash contribution to the Scheme for the year ending 31 March 2016 is £13.0m. The Group has no further payment obligations once the contributions have been paid. Following the closure to future accrual, the income statement no longer includes an expense in respect of defined benefit pension service costs.

### Triennial funding valuation

The most recent completed full actuarial valuation of the Scheme was undertaken as at 30 June 2011 and resulted in an actuarially assessed deficit of £74.7m.

The latest triennial valuation of the Scheme is being completed as at 30 June 2014. It is expected that the agreed recovery plan will require £13m contributions per annum until 31 March 2018, the same annual funding level as previously. This includes £2.5m p.a. distributions to the Scheme, indexed by reference to CPI, from the Group's Pension Funding Partnership (see page 132).

## 30. Post-retirement benefits continued

### QinetiQ's Pension Funding Partnership structure

Following the 30 June 2011 valuation, a package of pension changes has been agreed with the Trustees to provide stability to the Scheme. As part of the package of proposals, on 26 March 2012 QinetiQ established the QinetiQ PFP Limited Partnership (the 'Partnership') with the Scheme. Under this arrangement, properties to the capitalised value of £32.3m were transferred to the Partnership. The transfers were affected through a 20-year sale and leaseback agreement. The Scheme's interest in the Partnership entitles it to an annual distribution of approximately £2.5m for 20 years, indexed with reference to CPI. These contributions replaced part of the regular contributions made under the past deficit recovery payments plan. The Scheme's interest in the Partnership will revert back to QinetiQ Limited in 2032.

The Partnership is controlled by QinetiQ and its results are consolidated by the Group. Under IAS 19, the interest held by the Scheme in the Partnership does not qualify as a plan asset for the purposes of the Group's consolidated financial statements and is, therefore, not included within the fair value of plan assets. As a result, the Group's consolidated financial statements are unchanged by the Partnership. In addition, the value of the property transferred to the Partnership and leased back to QinetiQ remains on the balance sheet. QinetiQ retains the operational flexibility to substitute properties of equivalent value within the Partnership and has the option to settle outstanding amounts due under the interest before 2032 if it so chooses.

### Other UK schemes

In the UK the Group has a small number of employees for whom benefits are secured through the Prudential Platinum Scheme. The net pension deficits of this scheme at 31 March 2015 amounted to £nil (2014: £nil). QinetiQ also offers employees access to a Group Self Invested Personal Pension Plan, but no Company contributions are paid to this arrangement.

### QinetiQ Pension Scheme net pension liability

The fair value of the QinetiQ Pension Scheme assets, which are not intended to be realised in the short term and may be subject to significant change before they are realised, and the present value of the Scheme's liabilities, which are derived from cash flow projections over long periods, and thus inherently uncertain, were:

all figures in £ million	2015	2014	2013	2012	2011
Equities	517.2	434.4	487.3	583.2	564.1
LDI investment*	323.4	273.6	205.9	—	—
Corporate bonds	311.4	279.9	276.8	194.6	158.7
Alternative bonds**	176.3	183.0	174.8	—	—
Government bonds	—	—	—	183.5	165.3
Property	113.4	94.0	81.3	82.4	78.0
Other	12.9	39.7	30.4	64.2	15.0
<b>Total market value of assets</b>	<b>1,454.6</b>	<b>1,304.6</b>	<b>1,256.5</b>	<b>1,107.9</b>	<b>981.1</b>
Present value of Scheme liabilities	(1,494.0)	(1,326.8)	(1,310.6)	(1,139.4)	(1,105.7)
<b>Net pension liability before deferred tax</b>	<b>(39.4)</b>	<b>(22.2)</b>	<b>(54.1)</b>	<b>(31.5)</b>	<b>(124.6)</b>
Deferred tax asset	1.6	1.3	13.7	13.3	32.4
<b>Net pension liability after deferred tax</b>	<b>(37.8)</b>	<b>(20.9)</b>	<b>(40.4)</b>	<b>(18.2)</b>	<b>(92.2)</b>

\* The Scheme has assets invested in a Liability Driven Investment portfolio. As at 31 March 2015 this hedges against approximately 20% of the interest rate and 45% of the inflation rate risk, as measured on the Trustees' gilt-funding basis.

\*\* Includes allocations to high-yield bonds, secured loans and emerging market debt.

## Changes to the fair value of Scheme assets

all figures in £ million	2015	2014
Opening fair value of Scheme assets	1,304.6	1,256.5
Interest income on Scheme assets	53.9	54.9
Re-measurement gain on Scheme assets	116.3	2.6
Contributions by the employer	9.2	20.6
Net benefits paid out and transfers	(28.1)	(28.8)
Administrative expenses	(1.3)	(1.2)
<b>Closing fair value of Scheme assets</b>	<b>1,454.6</b>	<b>1,304.6</b>

## Changes to the present value of the defined benefit obligation

all figures in £ million	2015	2014
Opening defined benefit obligation	(1,326.8)	(1,310.6)
Current service cost	–	(11.3)
Interest cost	(54.5)	(56.6)
<i>Actuarial (loss)/gain on Scheme liabilities based on:</i>		
Change in financial assumptions	(128.3)	(39.2)
Experience gains	7.8	31.0
Change in demographic assumptions	(20.3)	–
Curtailment gain	–	31.1
Net benefits paid out and transfers	28.1	28.8
<b>Closing defined benefit obligation</b>	<b>(1,494.0)</b>	<b>(1,326.8)</b>

## Changes to the net pension liability

all figures in £ million	2015	2014
Opening net pension liability	(22.2)	(54.1)
Current service cost	–	(11.3)
Net finance cost	(0.6)	(1.7)
Administrative expenses	(1.3)	(1.2)
Curtailment gain	–	31.1
Net actuarial loss	(24.5)	(5.6)
Contributions by the employer	9.2	20.6
<b>Closing net pension liability</b>	<b>(39.4)</b>	<b>(22.2)</b>

## Total income/expense recognised in the income statement

all figures in £ million	2015	2014
Current service cost	–	11.3
Past service gain (including curtailments)	–	(31.1)
Net interest on the net defined benefit liability	0.6	1.7
Administrative expenses	1.3	1.2
<b>Total expense/(income) recognised in the income statement (gross of deferred tax)</b>	<b>1.9</b>	<b>(16.9)</b>

## 30. Post-retirement benefits continued

### Assumptions

The major assumptions used in the IAS 19 valuation of the Scheme were:

	2015	2014
Discount rate applied to Scheme liabilities	3.2%	4.2%
CPI inflation assumption	2.1%	2.6%
Assumed life expectancies in years:		
Future male pensioners (currently aged 60)	88	88
Future female pensioners (currently aged 60)	91	90
Future male pensioners (currently aged 40)	91	90
Future female pensioners (currently aged 40)	93	92

The assumptions used by the actuary are the best estimates chosen from a range of possible actuarial assumptions which, because of the timescale covered, may not necessarily be borne out in practice. It is important to note that these assumptions are long term and, in the case of the discount rate and the inflation rate, are measured by external market indicators. The mortality assumptions as at 31 March 2015 were 90% of S2PMA for males and 90% of S2PFA for females, based on year of birth making allowance for improvements in mortality in line with CMI\_2013 Core Projections and a long-term rate of improvement of 1.5% per annum. These assumptions adopted at the previous year end were 90% of S1PMA for males and 90% of S1PFA for females, based on year of birth making allowance for improvements in mortality in line with CMI\_2011 Core Projections and a long-term rate of improvement of 1.25% per annum.

The balance sheet net pension liability is a snapshot view which can be significantly influenced by short-term market factors. The calculation of the surplus or deficit depends, therefore, on factors which are beyond the control of the Group – principally the value at the balance sheet date of equity shares (and other assets) in which the Scheme has invested and long-term interest rates which are used to discount future liabilities. The funding of the Scheme is based on long-term trends and assumptions relating to market growth, as advised by qualified actuaries and investment advisors.

The weighted average duration of the defined benefit obligation is approximately 20 years.

### Sensitivity analysis of the principal assumptions used to measure Scheme liabilities

Assumption	Change in assumption	Indicative impact on Scheme liabilities (before deferred tax)
Discount rate	Increase/decrease by 0.1%	Decrease/increase by £28m
Rate of inflation	Increase/decrease by 0.1%	Increase/decrease by £28m
Rate of mortality	Increase by one year	Increase by £37m

The above sensitivity analyses are based on a change in an assumption while holding all other assumptions constant. In practice, this is unlikely to occur, and changes in some of the assumptions may be correlated. When calculating the sensitivity of the defined benefit obligation to significant actuarial assumptions the same method (projected unit credit method) has been applied as when calculating the pension liability recognised within the statement of financial position. The methods and types of assumption did not change.

### Risks

Through its defined benefit pension plan, the Group is exposed to a number of risks, the most significant of which are detailed below:

Volatility in market conditions	Results under IAS 19 can change dramatically depending on market conditions. The defined benefit obligation is linked to yields on AA-rated corporate bonds, while many of the assets of the Scheme are invested in other assets. Changing markets in conjunction with discount rate volatility will lead to volatility in the net pension liability on the Group's balance sheet and in other comprehensive income. To a lesser extent this will also lead to volatility in the IAS 19 pension finance expense in the Group's income statement.
Choice of accounting assumptions	The calculation of the defined benefit obligation (DBO) involves projecting future cash flows from the Scheme many years into the future. This means that the assumptions used can have a material impact on the balance sheet position and profit and loss charge. In practice future experience within the Scheme may not be in line with the assumptions adopted. For example, members could live longer than foreseen or inflation could be higher or lower than allowed for in the DBO calculation.
Inflation rate risk	The majority of the Scheme's benefit obligations are linked to inflation, and higher inflation will lead to higher liabilities.

The accounting assumptions noted above are used to calculate the year end net pension liability in accordance with the relevant accounting standard, IAS 19 (revised) 'Employee benefits'. Changes in these assumptions have no impact on the Group's cash payments into the Scheme. The payments into the Scheme are reassessed after every triennial valuation.

The triennial valuations are calculated on a funding basis and use a different set of assumptions, as agreed with the pension Trustees. Given the current extremely low gilt yields, perhaps exacerbated by quantitative easing, a funding valuation of the Scheme would probably have resulted in a bigger deficit than the IAS 19 methodology if it had been performed at the year end.

## 31. Transactions with the MOD

The MOD continues to own its Special Share in QinetiQ which conveys certain rights as set out in note 28. Transactions between the Group and the MOD are disclosed as follows:

### Freehold land and buildings and surplus properties

Under the terms of the Group's acquisition of part of the business and certain assets of DERA from the MOD on 1 July 2001, the MOD retained certain rights in respect of the freehold land and buildings transferred.

#### Restrictions on transfer of title

The title deeds of those properties with strategic assets (see below) include a clause that prevents their transfer without the approval of the MOD. The MOD also has the right to purchase any strategic assets in certain circumstances.

### MOD's generic compliance regime

Adherence to the generic compliance system is monitored by the Risk & CSR Committee. Refer to the Committee's report within the Corporate governance statement on page 71.

### Strategic assets

Under the Principal Agreement with the MOD, the QinetiQ controlled Group is not permitted without the written consent of the MOD, to:

- i) dispose of or destroy all or any part of a strategic asset; or
- ii) voluntarily undertake any closure of, or cease to provide a strategic capability by means of, all or any part of a strategic asset.

The net book value of assets identified as being strategic assets as at 31 March 2015 was £7.5m (2014: £1.3m).

### Long Term Partnering Agreement

On 27 February 2003 QinetiQ Limited entered into a Long Term Partnering Agreement to provide Test and Evaluation (T&E) facilities and training support services to the MOD. This is a 25-year contract with a total revenue value of up to £5.6bn, dependent on the level of usage by the MOD, under which QinetiQ Limited is committed to providing T&E services with increasing efficiencies through cost saving and innovative service delivery.

## 32. Contingent liabilities and assets

Subsidiary undertakings within the Group have given unsecured guarantees of £36.2m at 31 March 2015 (2014: £40.3m) in the ordinary course of business.

The Company has on occasion been required to take legal action to protect its intellectual property rights, to enforce commercial contracts or otherwise and similarly to defend itself against proceedings brought by other parties. Provisions are made for the expected costs associated with such matters, based on past experience of similar items and other known factors, taking into account professional advice received, and represent management's best estimate of the likely outcome. The timing of utilisation of these provisions is uncertain pending the outcome of various court proceedings and negotiations. However, no provision is made for proceedings which have been or might be brought by other parties unless management, taking into account professional advice received, assesses that it is more likely than not that such proceedings may be successful. Contingent liabilities associated with such proceedings have been identified but the Directors are of the opinion that any associated claims that might be brought can be resisted successfully and therefore the possibility of any outflow in settlement is assessed as not probable.

The Group has not recognised contingent amounts receivable relating to the Chertsey property which was disposed of during 2004 or the Fort Halstead property disposed of in September 2005. Additional consideration is potentially due on the purchasers obtaining additional planning consents, with the quantum dependent on the scope of the consent achieved.

The Group has also not recognised contingent amounts receivable relating to property impairments in prior years that may potentially be recovered from the MOD. Recovery is subject to future negotiations. It is not considered practicable to calculate the value of this contingent asset.

### 33. Capital commitments

The Group had the following capital commitments for which no provision has been made:

Contracted	2015	2014
	30.8	38.7

Capital commitments at 31 March 2015 include £30.5m (2014: £37.8m) in relation to property, plant and equipment that will be wholly funded by a third-party customer under long-term contract arrangements.

### 34. Subsidiaries

The companies listed below are those which were part of the Group at 31 March 2015 and which, in the opinion of the Directors, significantly affected the Group's results and net assets during the year. The Directors consider that those companies not listed are not significant in relation to the Group as a whole. A comprehensive list of all subsidiaries will be disclosed as an appendix to the Group's annual return.

Name of company	Principal area of operation	Country of incorporation
<b>Subsidiaries<sup>1,2</sup></b>		
QinetiQ Group Holdings Limited	UK	England & Wales
QinetiQ Holdings Limited	UK	England & Wales
QinetiQ Limited	UK	England & Wales
QinetiQ Overseas Holdings Limited	UK	England & Wales
QinetiQ US Holdings, Inc.	US	US
Foster-Miller, Inc.	US	US

<sup>1</sup> Accounting reference date is 31 March. All principal subsidiary undertakings listed above have financial year ends of 31 March and 100% of the ordinary shares are owned by the Group.

<sup>2</sup> QinetiQ Group Holdings Limited is a direct subsidiary of QinetiQ Group plc. All other subsidiaries are held indirectly by other subsidiaries of QinetiQ Group plc.

# Company balance sheet

as at 31 March

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all figures in £ million	Note	2015	2014
<b>Fixed assets</b>			
Investments in subsidiary undertaking	2	458.2	454.8
		<b>458.2</b>	<b>454.8</b>
<b>Current assets</b>			
Debtors	3	81.6	79.5
		<b>81.6</b>	<b>79.5</b>
<b>Current liabilities</b>			
Creditors amounts falling due within one year	4	(205.5)	(64.6)
		<b>(205.5)</b>	<b>(64.6)</b>
<b>Net current (liabilities)/assets</b>		<b>(123.9)</b>	<b>14.9</b>
<b>Total assets less current liabilities</b>		<b>334.3</b>	<b>469.7</b>
<b>Net assets</b>		<b>334.3</b>	<b>469.7</b>
<b>Capital and reserves</b>			
Equity share capital	6	6.6	6.6
Capital redemption reserve	6	39.9	39.9
Share premium account	6	147.6	147.6
Profit and loss account	6	140.2	275.6
<b>Capital and reserves attributable to shareholders</b>		<b>334.3</b>	<b>469.7</b>

There are no other recognised gains and losses.

The financial statements of QinetiQ Group plc (company number 4586941) were approved by the Board of Directors and authorised for issue on 21 May 2015 and were signed on its behalf by:

**Mark Elliott**  
Chairman

**Steve Wadey**  
Chief Executive Officer

**David Mellors**  
Chief Financial Officer

## 1. Accounting policies

The following accounting policies have been applied consistently in dealing with items which are considered material in relation to the Company's financial statements.

### Basis of preparation

The financial statements have been prepared under the historical cost convention and in accordance with applicable UK Accounting Standards. As permitted by section 408(4) of the Companies Act 2006, a separate profit and loss account dealing with the results of the Company has not been presented.

### Investments

In the Company's financial statements, investments in subsidiary undertakings are stated at cost less any impairment in value.

### Share-based payments

The fair value of equity-settled awards for share-based payments is determined on grant and expensed straight line over the period from grant to the date of earliest unconditional exercise. The fair value of cash-settled awards for share-based payments is determined at each period end until they are exercised or lapse. The value is expensed straight line over the period from grant to the date of earliest unconditional exercise. The charges for both equity and cash-settled share-based payments are updated annually for non-market-based vesting conditions. Further details of the Group's share-based payment charge are disclosed in note 29 to the Group financial statements. The cost of share-based payments is charged to subsidiary undertakings.

## 2. Investment in subsidiary undertaking

As at 31 March

all figures in £ million

	2015	2014
Subsidiary undertaking – 100% of ordinary share capital of QinetiQ Group Holdings Limited	424.3	424.3
Capital contributions arising from share-based payments to employees of subsidiaries	33.9	30.5
	<b>458.2</b>	<b>454.8</b>

A list of all principal subsidiary undertakings of QinetiQ Group plc is disclosed in note 34 to the Group financial statements.

## 3. Debtors

As at 31 March

all figures in £ million

Amounts owed by Group undertakings	2015	2014
	<b>81.6</b>	<b>79.5</b>

## 4. Creditors

As at 31 March

all figures in £ million

Amounts owed to Group undertakings	2015	2014
	<b>205.5</b>	<b>64.6</b>

## 5. Share capital

The Company's share capital is disclosed in note 28 to the Group financial statements.

## 6. Reserves

all figures in £ million	Issued share capital	Capital redemption reserve	Share premium	Profit and loss	Total equity
At 1 April 2014	6.6	39.9	147.6	275.6	469.7
Profit for the year	—	—	—	0.2	0.2
Purchase of own shares	—	—	—	(0.6)	(0.6)
Purchase and cancellation of shares	(0.5)	0.5	—	(107.1)	(107.1)
Share-based payments – settlement	—	—	—	0.6	0.6
Dividend paid	—	—	—	(31.7)	(31.7)
Share-based payments	—	—	—	3.2	3.2
<b>At 31 March 2015</b>	<b>6.1</b>	<b>40.4</b>	<b>147.6</b>	<b>140.2</b>	<b>334.3</b>
At 1 April 2013	6.6	39.9	147.6	194.9	389.0
Profit for the year	—	—	—	103.7	103.7
Purchase of own shares	—	—	—	(0.5)	(0.5)
Share-based payments – settlement	—	—	—	0.9	0.9
Dividend paid	—	—	—	(26.8)	(26.8)
Share-based payments	—	—	—	3.4	3.4
<b>At 31 March 2014</b>	<b>6.6</b>	<b>39.9</b>	<b>147.6</b>	<b>275.6</b>	<b>469.7</b>

The capital redemption reserve is not distributable and was created following redemption of preference share capital.

## 7. Share-based payments

The Company's share-based payment arrangements are set out in note 29 to the Group financial statements.

## 8. Other information

Directors' emoluments, excluding Company pension contributions, were £2.9m (2014: £3.1m). These emoluments were all in relation to services provided on behalf of the QinetiQ Group with no amount specifically relating to their work for the Company. Details of the Directors' emoluments, share schemes and entitlements under money purchase pension schemes are disclosed in the Remuneration Report.

The remuneration of the Company's auditor for the year to 31 March 2015 was £178,000 (2014: £146,000), which was for audit of the Group's annual accounts and audit related assurance services. No other services were provided by the auditor to the Company.

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for the years ended 31 March (unaudited)

		2015	2014	2013 <sup>4</sup>	2012 <sup>3</sup>	2011 <sup>2,3</sup>
EMEA Services (formerly UK Services)	£m	625.6	607.0	594.6	620.9	663.7
Global Products	£m	138.2	175.6	269.4	325.0	442.6
<b>Revenue – continuing operations</b>	£m	763.8	782.6	864.0	945.9	1,106.3
Discontinued operations (US Services)	£m	55.7	408.8	463.8	523.7	596.3
<b>Revenue – total Group</b>	£m	819.5	1,191.4	1,327.8	1,469.6	1,702.6
EMEA Services (formerly UK Services)	£m	93.0	86.7	84.8	56.3	45.8
Global Products	£m	18.3	27.0	60.2	66.2	52.1
<b>Underlying operating profit<sup>1</sup> – continuing operations</b>	£m	111.3	113.7	145.0	127.5	97.9
Discontinued operations (US Services)	£m	1.2	19.0	23.7	37.1	45.8
<b>Underlying operating profit<sup>1</sup> – total Group</b>	£m	112.5	132.7	168.7	159.6	143.7
Profit/(loss) before tax	£m	105.4	4.1	(137.0)	316.3	7.9
Profit/(loss) attributable to equity shareholders	£m	104.7	(12.7)	(133.2)	246.3	(8.8)
Underlying basic EPS <sup>1</sup>	Pence	15.3	16.0	18.9	13.6	13.0
Basic EPS	Pence	16.6	(1.9)	(20.5)	37.9	(1.3)
Diluted EPS	Pence	16.5	(1.9)	(20.5)	37.6	(1.3)
Dividend per share	Pence	5.4	4.6	3.8	2.9	1.6
Underlying net cash from operations						
(post capex) <sup>1</sup>	£m	116.7	136.5	175.9	235.4	265.8
Net cash/(debt)	£m	195.5	170.5	74.0	(122.2)	(260.9)
Average number of employees		6,454	9,134	9,772	10,637	12,033
<b>Continuing operations:</b>						
Orders	£m	613.6	596.9	626.1	706.8	1,417.2
Underlying operating margin <sup>1</sup>	%	14.6	14.5	16.8	13.0	8.8
Underlying profit before tax <sup>1</sup>	£m	107.8	101.2	128.4	73.1	58.0
Profit/(loss) before tax	£m	105.4	84.0	103.7	288.3	(29.9)
Profit/(loss) after tax	£m	117.4	68.0	89.9	233.9	(29.6)
Underlying basic EPS <sup>1</sup>	Pence	15.2	13.8	16.6	10.5	7.9
Basic EPS	Pence	18.6	10.4	13.9	36.0	(4.5)
Underlying net cash from operations						
(post capex) <sup>1</sup>	£m	114.9	106.2	137.7	217.3	214.5

<sup>1</sup> Underlying measures are stated before specific adjusting items. Definitions of underlying measures of performance are in the glossary on page 141. Underlying financial measures are presented because the Board believes these provide a better representation of the Group's long-term performance trend. For details of specific adjusting items refer to Note 4 of the financial statements.

<sup>2</sup> The 2011 figures have been restated to reflect the transfer of businesses from Global Products to UK Services and US Services at the beginning of the 2012 financial year.

<sup>3</sup> IAS 19 (revised) 'Employee Benefits' was adopted for 2013 and the 2012 and 2011 comparatives have been restated accordingly.

<sup>4</sup> The 2013 figures have been restated to reflect the reclassification of product sales from UK Services to Global Products and the reclassification of Cyveillance® from US Services to EMEA Services. 2012 and 2011 have also been restated to reflect the reclassification of Cyveillance® from US Services to EMEA Services.

<b>AGM</b>	Annual General Meeting	<b>PBT</b>	Profit before tax
<b>CAGR</b>	Compound Annual Growth Rate	<b>PSP</b>	Performance Share Plan
<b>C4ISR</b>	Command, control, communications, computers, intelligence, surveillance and reconnaissance	<b>QNA</b>	QinetiQ North America
<b>CPI</b>	Consumer Price Index	<b>QSOS</b>	QinetiQ Share Option Scheme
<b>CR</b>	Corporate Responsibility	<b>R&amp;D</b>	Research and development
<b>CSR</b>	Corporate Social Responsibility	<b>RSU</b>	Restricted Stock Unit
<b>DAB</b>	Deferred Annual Bonus	<b>Specific adjusting items</b>	Amortisation of intangible assets arising from acquisitions; net restructuring charges/recoveries; net pension finance expense; net pension gain on closure to future accrual; impairment of property; impairment of goodwill and intangible assets; gain/loss on business combinations and divestments; gain/loss on disposal of investments; tax on the preceding items; and tax credits on one-off recognition of deferred tax asset in respect of UK trade losses
<b>DE&amp;S</b>	MOD's Defence, Equipment and Support organisation	<b>SDSR</b>	Strategic Defence and Security Review
<b>DHS</b>	US Department of Homeland Security	<b>SSRO</b>	Single Source Regulations Office
<b>DoD</b>	US Department of Defense	<b>TSR</b>	Total shareholder return
<b>EBITDA</b>	Earnings before interest, tax, depreciation and amortisation	<b>UK Corporate Governance Code</b>	Guidelines of the Financial Reporting Council to address the principal aspects of corporate governance
<b>EMEA</b>	Europe, Middle East and Australasia	<b>UK GAAP</b>	UK Generally Accepted Accounting Practice
<b>EPS</b>	Earnings per share	<b>Underlying basic earnings per share</b>	Basic earnings per share as adjusted to exclude 'specific adjusting items'
<b>FMI</b>	Foster-Miller, Inc. – the legal entity through which the US Products division operates	<b>Underlying effective tax rate</b>	The tax charge for the year excluding the tax impact of 'specific adjusting items' expressed as a percentage of underlying profit before tax
<b>Funded backlog</b>	The expected future value of revenue from contractually committed and funded customer orders (excluding the £998m third-term re-pricing of the LTPA contract)	<b>Underlying net cash from operations (post capex)</b>	Net cash inflow from operations before cash flows of specific adjusting items, less net cash outflow on purchase/sale of intangible assets and property, plant and equipment
<b>Gearing ratio</b>	This is the ratio of net debt to adjusted EBITDA in accordance with the Group's credit-facility ratios. EBITDA is adjusted to exclude charges for share-based payments. Net debt is adjusted to reflect the same exchange rates as used for EBITDA and to reflect other requirements of the debt-holders' covenant calculations	<b>Underlying net finance costs</b>	Net finance costs excluding net pension finance costs
<b>IAS</b>	International Accounting Standards	<b>Underlying operating cash conversion</b>	The ratio of underlying net cash from operations (post capex) to underlying operating profit excluding share of post-tax result of equity-accounted joint ventures and associates
<b>IFRS</b>	International Financial Reporting Standards	<b>Underlying operating margin</b>	Underlying operating profit expressed as a percentage of revenue
<b>KPI</b>	Key Performance Indicator	<b>Underlying operating profit</b>	Operating profit as adjusted to exclude 'specific adjusting items'
<b>LIBID</b>	London inter-bank bid rate	<b>Underlying profit before tax</b>	Profit before tax as adjusted to exclude 'specific adjusting items'
<b>LIBOR</b>	London inter-bank offered rate	<b>VSP</b>	Value Sharing Plan
<b>LTPA</b>	Long Term Partnering Agreement – 25-year contract established in 2003 to manage the MOD's test and evaluation ranges	<b>Yellow Book</b>	Single-source pricing regulations used by MOD up to 2015. Now replaced by the Orange Book
<b>MOD</b>	UK Ministry of Defence		
<b>MSCA</b>	Maritime Strategic Capability Agreement		
<b>OHSAS</b>	Occupational Health and Safety Advisory Services		
<b>Orange book</b>	Single-source pricing regulations used by UK Government from 1 April 2015. Replaces the Yellow Book regulations		
<b>Organic growth</b>	The level of year-on-year growth, expressed as a percentage, calculated at constant foreign exchange rates, adjusting comparatives to incorporate the results of acquired entities but excluding the results for any disposals or discontinued operations for the same duration of ownership as the current period		

### Shareholding enquiries

The Company's registrar is Equiniti. Enquiries regarding your shareholding, including the following administrative matters, should be addressed to Equiniti:

- Change of personal details such as change of name or address.
- Lost share certificates.
- Dividend payment enquiries.
- Direct dividend payments. You can have your dividends paid directly into a UK bank or building society account by completing a dividend mandate form. The associated tax voucher will still be sent to your registered address. If you live outside the UK, Equiniti offers a global payments service which is available in certain countries and could enable you to receive your dividends direct into your bank account in your local currency.
- Tax voucher enquiries. Tax vouchers are sent to a shareholder's registered address. Shareholders who have dividends paid direct into a bank or building society account receive a consolidated tax voucher which details all dividends paid for the year. Shareholders who prefer to continue receiving a tax voucher with each dividend payment, rather than a consolidated tax voucher, can contact Equiniti to request this.

### Contact details for registrar

#### By post:

Equiniti Limited, Aspect House, Spencer Road, Lancing, West Sussex BN99 6DA

#### By telephone:

0871 384 2021\* for UK calls

+44 (0)121 415 7576 for calls from outside the UK

\* Lines are open 8.30am to 5.30pm, Monday to Friday, excluding bank holidays. Calls to 0871 numbers are charged at 8p per minute plus network extras.

#### By email:

You can send an email enquiry securely from Equiniti's website, at <https://help.shareview.co.uk>.

#### Online:

Equiniti's website at <https://help.shareview.co.uk> (Shareview) includes answers to frequently asked questions and provides key forms for download. Shareview also offers online access to your shareholding where you can manage your account, register for electronic communications, see details of balance movements and complete certain amendments online, such as changes to dividend mandate instructions. You can register at [www.shareview.co.uk](https://www.shareview.co.uk), click on 'Register' and follow the steps.

### Electronic communications

The Company offers shareholders the option to receive documentation and communications electronically, via the Company's website.

The wider use of electronic communications enables fast receipt of documents, reduces the Company's printing, paper and postal costs and reduces the Company's environmental impact. Shareholders can register for electronic communications at [www.shareview.co.uk](https://www.shareview.co.uk) and may also cast their vote for the 2015 Annual General Meeting online quickly and easily using the Sharevote service by visiting [www.sharevote.co.uk](https://www.sharevote.co.uk).

### Donating shares to charity – ShareGift

Small parcels of shares, which may be uneconomic to sell on their own, can be donated to ShareGift, the share donation charity (registered charity no. 1052686). ShareGift transfers these holdings into their name, aggregates them, and uses the proceeds to support a wide range of UK charities based on donor suggestion. If you would like further details about ShareGift, please visit [www.sharegift.org](http://www.sharegift.org), email [help@sharegift.org](mailto:help@sharegift.org) or telephone them on 020 7930 3737.

### Share price

Details of current and historical share prices can be found on the Company's website at [www.QinetiQ.com/investors](http://www.QinetiQ.com/investors). The graph below shows the share price trend during the year ended 31 March 2015:



The share prices used in the graph above are the mid-market prices as derived from the London Stock Exchange Daily Official List.

### Analysis of Share Register at 31 March 2015

By type of holder	Number of holdings	% of total holdings	Shares held	% of share capital
Individuals	5,923	87.22%	6,171,964	1.01%
Institutions and others	868	12.78%	602,438,040	98.99%
<b>Total</b>	<b>6,791</b>	<b>100.00%</b>	<b>608,610,004</b>	<b>100.00%</b>
<b>By size of holding</b>				
1–500	4,385	64.57%	890,912	0.15%
501–1,000	617	9.09%	498,216	0.08%
1,001–5,000	1,135	16.71%	2,783,820	0.46%
5,001–10,000	195	2.87%	1,455,210	0.24%
10,001–100,000	239	3.52%	8,159,016	1.34%
Over 100,000	220	3.24%	594,822,830	97.73%
<b>Total</b>	<b>6,791</b>	<b>100.00%</b>	<b>608,610,004</b>	<b>100.00%</b>

**Beware of share fraud**

Fraudsters use persuasive and high-pressure tactics to lure investors into scams. They may offer to sell shares that turn out to be worthless or non-existent, or to buy shares at an inflated price in return for an upfront payment. While high profits are promised, if you buy or sell shares in this way you will probably lose your money.

**How to avoid share fraud**

1. Keep in mind that firms authorised by the FCA are unlikely to contact you out of the blue with an offer to buy or sell shares.
2. Do not get into a conversation, note the name of the person and firm contacting you and then end the call.
3. Check the Financial Services Register from [www.fca.org.uk](http://www.fca.org.uk) to see if the person and firm contacting you is authorised by the FCA.
4. Beware of fraudsters claiming to be from an authorised firm, copying its website or giving you false contact details.
5. Use the firm's contact details listed on the Register if you want to call it back.
6. Call the FCA on 0800 111 6768 if the firm does not have contact details on the Register or you are told they are out of date.
7. Search the list of unauthorised firms to avoid at [www.fca.org.uk/scams](http://www.fca.org.uk/scams).
8. Consider that if you buy or sell shares from an unauthorised firm you will not have access to the Financial Ombudsman Service or Financial Services Compensation Scheme.
9. Think about getting independent financial and professional advice before you hand over any money.
10. Remember: if it sounds too good to be true, it probably is!

**Report a scam**

- If you are approached by fraudsters please tell the FCA using the share fraud reporting form at [www.fca.org.uk/scams](http://www.fca.org.uk/scams), where you can find out more about investment scams.
- You can also call the FCA Consumer Helpline on **0800 111 6768**.
- If you have already paid money to share fraudsters you should contact Action Fraud on **0300 123 2040**.

**Key dates**

22 July 2015	Interim management statement
22 July 2015	Annual General Meeting
6 August 2015	Ordinary shares marked ex-dividend
7 August 2015	Final 2015 dividend record date
4 September 2015	Final 2015 dividend payment date
30 September 2015	Half-year financial period end
19 November 2015	Half-year results announcement
February 2016	Interim management statement (provisional date)
31 March 2016	Financial year end
May 2016	Preliminary results announcement (provisional date)

**Cautionary statement**

All statements other than statements of historical fact included in this Annual Report, including, without limitation, those regarding the financial condition, results, operations and businesses of QinetiQ and its strategy, plans and objectives and the markets and economies in which it operates, are forward-looking statements. Such forward-looking statements, which reflect management's assumptions made on the basis of information available to it at this time, involve known and unknown risks, uncertainties and other important factors which could cause the actual results, performance or achievements of QinetiQ or the markets and economies in which QinetiQ operates to be materially different from future results, performance or achievements expressed or implied by such forward-looking statements. Nothing in this Annual Report should be regarded as a profit forecast.

This Annual Report is intended to provide information to shareholders and is not designed to be relied upon by any other party. The Company and its Directors accept no liability to any other person other than under English law.

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