

MEARS

Partners for purpose

Mears Group PLC
Annual Report and Accounts 2020



Secure.
Responsible.
Innovative.

Mears today

Mears is one of the UK's leading and most trusted providers of a wide range of specialist Housing services to Local and Central Government.



Specialists in housing solutions

Our purpose

Working together to help people and communities thrive. This is the guiding principle that defines our brand and drives our activities. It is what makes Mears distinctive and is the starting point for all of our activities.

Our vision

To be the leading provider of housing services and solutions to the affordable housing market in the UK.

Our values

We value our customers and communities, putting their needs at the heart of everything we do.

We value teamwork, supporting each other, sharing ideas and never excluding others.

We value personal responsibility, setting consistently high standards for our work and holding ourselves accountable for achieving them.

We value innovation, being inventive in our approach and empowering people to take reasonable action without fear or discrimination.

Our business at a glance

Where we operate

We operate across the UK through a range of local branches and facilities with a national coverage. A sample of our branches and recent contract wins is given below.

1. Awarded a £2 million contract for kitchens and bathrooms with A2Dominion on top of its current contract **London & South East**
2. Won Crawley contract valued at £167 million over 10 years **Crawley**
3. Signed our new Rotherham R&M contract which went live in April 2020 transitioning a new service at the commencement of the first national lock down **Rotherham**
4. Won 30 year partnership contract in Cornwall to deliver extra care homes in Hayle, St Austell, Newquay, Falmouth and Liskeard **Cornwall**
5. Renewed repairs response and void refurbishment contract to the London Borough of Hammersmith and Fulham **West London**
6. Won repairs contract for Accent Housing's Eastern region **East of England**
7. Retained our £40 million contract with Islington Council for a range of planned works **Central London**
8. Awarded a repairs contract with Longhurst **Midlands and East of England**
9. Contract Extension with Leeds City Council **Leeds**
10. Contract Extension with East Kent Housing **Kent**
11. Contract Extension with Home Group North East **Newcastle**
12. Contract Extension with Milton Keynes **Milton Keynes**
13. MPS Contract Extension with Wrexham Council **Wrexham**
14. Appointed to be Exeter City Council's partner to deliver the new Integrated Asset Management contract **Exeter**
15. Environmental Works win contract with Astar Group **South West**
16. The third year of our contract within Aberdeenshire Council sees a significant increase in volume to the first two years due to great service. The change in profile will see our revenues double from the current year to circa £13 million **Aberdeenshire**



Introduction

What we do

Mears has a single minded focus on the housing market and delivering services to the residents of these homes. We operate within the affordable housing sector, which is an area that will see continued investment given the significant housing shortage and the rising number of people who are regarded as statutorily homeless.

Our services

Our core services are in the maintenance and management of homes. Increasingly we operate an intelligent approach to maintenance, using technology and experience to operate preventative maintenance programmes that reduce levels of emergency repairs. As regards management, we collect rent and ensure homes are managed and maintained to a decent standard, whilst often providing other welfare services to the tenants. Our particular focus is on providing sustainable alternatives to homelessness, helping reduce the rising problems created by the housing shortage in the UK.

Our customers

We work predominantly with Central Government and Local Government, in the delivery of housing services. These are typically through long term contracts. We equally consider that the residents of the homes that we manage and/or maintain, to be our customers, and we take pride in the high levels of customer satisfaction that we achieve.

Long-term drivers

The shortage of housing in the UK has made investment in housing both a political and an economic priority. More recently, the Social Housing White Paper and the Grenfell tragedy have put greater focus on tenant engagement and safety. Long-term UK carbon reduction targets will also mean that significant further investment in housing is needed, including the replacement of gas boilers.

As such, we anticipate rising investment in our markets and a greater attention to the quality of delivery.

Demographic change is also a key long-term driver, given the growing and ageing population of the UK. This will create opportunity for more specialist housing, where management and maintenance services can be effectively combined through a single partner.

Revenue £m

Maintenance-led contracts

2020	536.9
2019	660.7

Management-led contracts

2020	253.8
2019	181.3

Development

2020	15.1
2019	39.5



Highlights

Financial highlights

Group revenue*

£805.8m

(2019: £881.5m)

Adjusted loss before tax**

£3.4m

(2019: profit £32.4m)

Reported loss before tax*

£15.2m

(2019: profit £20.3m)

Order book

£2.6bn

(2019: £2.5 bn)

Net debt (inclusive of lease obligations)

£152.2m

(2019: £256.2m)

Adjusted net cash (exclusive of lease obligations)

£56.9m

(2019: net debt £51.0m)

EBITDA to cash conversion***

185%

(2019: 113%)

Accident frequency rate

0.15

(2019: 0.23)

Contents

Strategic report

- 01 Highlights
- 02 2020 accreditations
- 04 Chairman's letter
- 08 Chief Executive Officer's review
- 16 Financial review
- 28 Providing homes and supporting communities
- 30 Meeting the extra care needs in Cornwall
- 32 Listening to our stakeholders
- 36 S172 Statement
- 38 Market drivers
- 40 Business model
- 42 Our strategy
- 44 Key performance indicators
- 48 Our approach to ESG
- 60 Why invest
- 62 Risk management
- 66 Principal risks and uncertainties
- 68 Business planning and financial viability

Corporate governance

- 71 Chairman's introduction
- 72 Board of Directors
- 74 Corporate governance framework
- 75 Key board activities in 2020
- 76 Promoting the success of the Company
- 77 Stakeholder engagement
- 79 Roles and responsibilities
- 81 Board composition
- 82 Report of the Nomination Committee
- 84 Report of the Audit Committee
- 92 Report of the Remuneration Committee
- 101 Annual report on remuneration
- 109 Report of the Directors
- 112 Statement of Directors' responsibilities

Financial statements

- 113 Independent auditor's report
- 124 Consolidated statement of profit or loss
- 125 Consolidated statement of comprehensive income
- 126 Consolidated balance sheet
- 127 Consolidated cash flow statement
- 128 Consolidated statement of changes in equity
- 129 Notes to the financial statements – Group
- 179 Parent Company balance sheet
- 180 Parent Company statement of changes in equity
- 181 Notes to the financial statements – Company

Shareholder information

- 191 Five-year record (unaudited)
- 192 Shareholder and corporate information

Strategic highlights

During a year which has seen unprecedented challenges, the Group made strong progress against all of its key strategic objectives as detailed below:

- ▶ Completed the exit from standalone Domiciliary Care
- ▶ Completed the disposal of its planning solutions business ('Terraquest'), generating an upfront cash inflow of £56.9m
- ▶ Continued to make progress in managing the controlled closure of the Development activities, to unlock working capital absorbed in that area
- ▶ Significant reduction in its indebtedness, reporting net cash at the year together with a reduction in the daily net debt

Reconciliations between the statutory figures and the alternative performance measures are reconciled on pages 16 to 18 of the Finance Review. The Financial review also provides detailed analysis of the financial impact from the discontinued operations.

Strategic report

2020 accreditations

Measuring our success

We want to drive continuous improvement in everything we do. That's why we seek accreditation from some of the most prestigious organisations who recognise how to drive improvement.

Our awards and accreditations show that we place safety, our colleagues and our customers at the heart of everything we do.



An organisation that champions Social Mobility

Social Mobility Compact

Department for Business, Innovation and Skills (BIS) introduced the champion tier of the compact in 2014. As a social mobility champion, Mears have made a public commitment to lead the way on improving social mobility.

Social Mobility Index

Mears is listed as a top Social Mobility Employer in the Social Mobility Index. The Index is an important bench-marking initiative that ranks Britain's employers on the actions they are taking to ensure they are open to accessing and progressing talent from all backgrounds and it showcases progress towards improving social mobility.



Delivering excellent customer service

ICS ServiceMark

Mears aims to put customers at the heart of everything we do. The Institute of Customer Service (ICS) Service Mark helps organisations understand how effective their customer service strategy is, and identifies areas for improvement.



Read more about the award and criteria at www.instituteofcustomerservice.com



An organisation that delivers quality

Customer Service Excellence

Mears aims to put customers at the heart of everything we do. The Customer Service Excellence accreditation is a practical tool for driving customer-focused change.



Colleagues receive best in class training

ICS TrainingMark

The Institute of Customer Service's TrainingMark demonstrates that our Customer Excellence Training (Making a Positive Difference) programs meet national standards for customer service, as independently recognised by the ICS.



An organisation that engages with customers

TPAS Contractor Accreditation

Mears has continuously held the TPAS Contractor accreditation since 2015. It is an independent evidence-based accreditation scheme that assesses and recognises resident engagement arrangements.



An organisation that actively promotes support to Armed Forces Veterans

Armed Forces Covenant – Gold Award

Mears Group has been awarded the prestigious Gold Award in the Defence Employer Recognition Scheme (ERS), for actively demonstrating our support and contribution towards the armed forces community.



Read more about the award and criteria at www.rospa.com



An organisation that believes good people make a great business

Investors in People

Mears is proud to have long held the Investors in People standard. Investors in People is the industry standard for people management.



A socially responsible business

FTSE 4 Good

Mears Group is placed in the top 9% of the UK's most socially responsible businesses in the FTSE4Good Index which recognizes excellent environmental, social and governance practices.



A great employer

Best Companies

Mears was named once more in 2020 as one of the Top 25 large businesses to work for in the Sunday Times Best Companies to work for list. Best Companies recognises businesses who take workplace engagement seriously in order to build a happier, healthier workforce.



Read more about the award and criteria at www.b.co.uk



A diverse and inclusive business

Diversity Network Accreditation (DNA)

Achieving DNA is recognition from the Housing Diversity Network, the leading specialist body in the sector, that an organisation has effective leadership and processes in place around Diversity and Inclusion and that they are achieving positive outcomes for employees and customers.



Read more www.ftse4good.com



An organisation that promotes a safe working environment

Royal Society for the Prevention of Accidents

Health and safety is paramount to our business. Mears has been recognized by RoSPA with an Order of Distinction for achieving 15 consecutive Gold awards.



Strategic report continued

Chairman's letter



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The scale of disruption from Covid-19 to our normal ways of working has been immense but I can report that the Group, particularly its people, have risen magnificently to the challenges and continue to do so”

Kieran Murphy
Chairman

Introduction

As with all businesses in the UK, the past year at Mears has been dominated by the Covid-19 pandemic and our response to the complex operational and financial challenges it presented to our business, our staff and our customers. The scale of disruption to our normal ways of working has been immense and there will be no-one within the group who has been unaffected. I can report that your company, particularly its people, have risen magnificently to the challenges and continue to do so.

The prior investment in client relationships, our people and infrastructure within Mears over many years has been much in evidence in the past 12 months. The quality of our relationships with our clients has ensured that almost all of them have continued to support the company financially through the pandemic, ensuring that our infrastructure has remained intact and our financial future has not at any time been in question. Similarly, the focus which we have placed on employee welfare, safety and training has been repaid by immense hard work from our staff and, on many occasions, extraordinary efforts by team members. Our past investment in our IT systems

has allowed our teams to move the company efficiently and effectively onto a remote working footing with effective controls and functionality.

That spirit of support has also been in evidence among our stakeholders. In the spring, our lending banks put in place additional facilities and later accepted revised financing covenants to ensure that the group had the financial flexibility to weather a reduced trading performance. Similarly, our shareholders have accepted that the company could not make any dividend distributions to them during the course of the year.

All that said, and despite the difficulties, the company made very significant strategic progress this year. We have completed our transition to a low capital-intensity housing specialist. We have significantly strengthened the balance sheet, the order book remains robust and high quality and we are in the process of identifying new areas for future growth. As the political roadmap out of lockdown unfolds, we can look forward to the future with confidence.

£805.8m

(2019: £881.5m) – Continuing revenue

£56.9m

(2019: net debt £51.0m) –
Net cash at 31 December

People

I said in my letter last year that it was the culture of our business and the quality and commitment of our staff which has enabled Mears to quickly, responsibly and effectively respond to the Covid crisis. Twelve months on, I can add the quality of resilience. Both for those who have been able to work throughout the year and for those who spent some time on furlough (at one point over 2,200 or c.40% of our colleagues) it has been a difficult year and required personal sacrifices and resolve. I hope that by the time this report is published we will have brought all staff back from furlough and that we will be reverting to more or less normal working patterns across the UK.

I have now seen many notes of thanks from grateful recipients of the services which Mears provide. They illustrate how so many members of the Mears workforce are not just professional and committed but are prepared to go that extra mile to provide something outstanding to the people whose lives we support.

On behalf of the Board, I offer my respect, admiration and gratitude for all that has been achieved by our staff during the course of this difficult year.

One of the pleasures of my role during my first year in office in 2019 was being able to visit teams up and down the country and talk to them about their work. Clearly, that has been impossible these past 12 months. I would very much hope to resume those visits after the summer, all being well.

Results

The financial results for the year were inevitably impacted by the pandemic but the strengths of our business model have underpinned our response. Maintenance-led work volumes were reduced by lockdown restrictions, and we agreed with most clients to defer non-emergency works in people's homes and deliver a service more focused on emergency works. In the majority of cases, our long-term relationships with our clients facilitated a swift transition to interim trading arrangements, reflecting these reduced activity levels, which broadly allowed us to recover direct labour and local overhead costs, but typically not central overhead or a profit contribution. These arrangements were in line with

government guidance to support public sector supply chains. This eliminated the risk of significant loss in this part of our business and also allowed us to retain our operational infrastructure for the recovery in work volumes which we expect this year. By contrast, our central government contracts, including AASC and Key Worker, saw increasing numbers of users and service requirements during the pandemic and have performed strongly.

Taken together, on a continuing basis, full year revenue fell by 9% to £806m (2019: £881m) and the Group recorded a small normalised loss¹ before tax of £(3.4)m (2019: £32.4m profit). However, this loss was concentrated in the first half of the year. The second half of the year showed a profit from continuing operations of £4.8m. This more robust performance is continuing into 2021. The business is well-placed to return to its pre-Covid financial metrics once all operating restrictions are eased. The statutory loss on continuing activities before tax after deducting amortisation of acquired intangibles and exceptional items was £15.2m (2019: £20.3m profit). The statutory profit, including discontinued operations, on the same basis was £41.7m (2019: loss £62.0m).

The Group ended 2020 with a strong net cash balance of £56.9m (2019: £51.0m net debt). This number was driven in large part by disposal proceeds and by lower than usual working capital demands from a maintenance business where activity was reduced. It was also flattered by a number of Covid-19 related deferrals and payments received on account which will unwind in the first half of FY2021. Adjusting for all of these, our underlying average net debt position for the year is in the region of £65m (Q4 2019: £126.1m). This represents a material strengthening of the position relative to the end of 2019. The Board expects further debt reduction progress to be made in 2021, despite the fact that some of the one-off effects discussed above will unwind or not be repeated.

The adoption in 2019 of IFRS 16, the new standard for leases accounting, was complex and challenging given the number of leases held by the Group. During the year, the Group revisited the assessments made in the previous year when initially recognising a right of use asset and the associated lease obligations.

This has resulted in a reduction in both the asset and liability and a restatement to the prior year. This is detailed further within the Financial Review and the supporting notes to the Financial Statements. Reported profit before tax and earnings are not impacted by this change.

Strategy

Despite the difficult market conditions created by the pandemic, we made excellent progress during the year in pursuing and, in large measure, achieving the strategic objectives which we set ourselves back in 2019. These were to refocus on housing activities, significantly to reduce indebtedness and to improve the returns which we obtain on our invested capital.

The sale in two tranches of our domiciliary care businesses was a key step. It allowed us to exit a business which we had improved operationally but which had underperformed financially for a number of years and was likely to continue to do so. It also significantly reduced the operational scale and complexity of the group, allowing us to streamline our central functions. The terms on which we did so ensured that service users' interests were preserved throughout the process. We will continue to develop our 'housing with care' solutions for clients and were pleased to have been selected by Cornwall Council to be its partner for a number of such projects over the coming years.

We have continued to run down our housing development activities, selling properties where we can do so for value and strictly limiting the build-up of working capital in the division. There remains some £25m of working capital to be released from this activity over the course of the next couple of years. As the properties are gradually converted to cash, that will contribute to our continuing objective of reducing the indebtedness of the Group.

The disposal of Terraquest, which was completed shortly before the year end, also significantly contributed to the achievement of our strategic objectives. Mears is to be congratulated for having nurtured the development of Terraquest from a small start-up to a thriving profitable enterprise. But it became increasingly clear that this business was very different in kind from our other activities and that its continuing prosperity might be optimised by a different owner. We decided that we should run a structured process to find such a buyer and were

¹ Adjusted profit/(loss) before tax stated on continuing activities before exceptional items and before the amortisation of acquired intangibles. See Financial Review for reconciliation of alternative performance measure.

Strategic report continued

Chairman's letter continued

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From its creation in 1988, Mears has sought to differentiate itself with a consistent and long-term focus on the wider societal value, as well as financial value, which it can and should generate.”

pleased to conclude a transaction with Apse Capital. The Ministry of Housing and Local Government, who have been our partners in Terraquest since the start, will remain partners in the business for the future. The terms of the transaction provide for Mears to have a continuing modest economic interest but the disposal was substantially satisfied in cash, £52.5m of which was received in 2020 (net of transaction costs). Those cash proceeds were used to reduce our indebtedness, thus making substantial inroads into our debt reduction target.

The pandemic required us to institute widespread changes in our trading terms. These are discussed in the Chief Executive Officer's Review and Financial Review but were only possible because of the close and effective working relationships built up with many clients over a number of years, and the constructive approach which those clients took to the need for Mears to retain its operating infrastructure for the future. The changes nevertheless resulted in a reduction in our profitability in 2020. We took the opportunity during the course of the year to exit certain contractual arrangements which were providing a drag on our financial performance. By contrast, the pandemic resulted in a significant increase in the number of service users in our asylum contracts. We had to make some difficult operational decisions and dealt with a serious incident in Glasgow which resulted in a fatality. We did so with a clear focus on staff and service user safety and this approach will guide us in the future. We look forward to moving to more normal trading arrangements and with a more optimised portfolio of contracts.

Much work has been done in the last six months on Mears' growth strategy for the next few years. We will remain focused on providing a range of housing solutions, mostly to public sector clients, which are capital-light and address key societal issues where demand can be expected to continue into the medium term. There remains a significant shortage of decent affordable housing in the UK and the developing green agenda will require very significant investment in the existing stock if the country is to achieve its overall carbon reduction targets. Mears is well placed to continue to develop the range of its services, growing its revenue line through new business wins in its core business, expanding the range of its capabilities in housing management and responding to clients' needs for solutions for homelessness and new ways of heating homes. There are opportunities for growth in both the Local Authority and Housing Association segments as well as with Central Government. The business will continue to work to improve operating efficiencies, and deliver an increasing operating margin over time.

From a financial perspective, Mears will continue to use cash generated from operations, as well as from the unwind of development, to make significant further reductions in its indebtedness. Some investment may be required in the business to mobilise new business wins and to develop new activities in homelessness and the greening of social housing, but the objective will remain that new activities be light

in capital intensity and fundamentally cash generative. The board is also conscious that shareholders have not received a dividend for over a year and will seek to return to the dividend list once it is prudent to do so. Taken together, and with a return toward more normal day to day trading, the Board would expect all these developments to drive significant shareholder returns.

Board developments

The pandemic changed the manner in which the Board worked, especially during the central part of the year. From March 2020 onwards, all meetings were (and they remain) virtual and for a period during the spring and early summer, meetings took place at weekly intervals so as to ensure that the Board was abreast of the developing situation caused by the pandemic and could effectively oversee the work of the executive team. I am grateful to all of my Board colleagues both for their willingness to make time available to participate in all of those discussions and for the constructive way in which they contributed their advice and counsel during that period.

During 2020 and early 2021, much work has been done on succession planning by the management team, at Nominations Committee and Board level, addressing both the senior executive team and the non-executive directors. There is a succession plan in place for all of the posts in the senior executive team.

As foreshadowed in my report last year, Jason Burt stood down from the Board in March 2020 and took up a new role in the Group coordinating and advising on health and safety and environmental matters. In that role, he continues to attend the Audit Committee by invitation and participates in Board discussions from time to time.

As a result of the disposal of our domiciliary care business, we needed to recruit a new Employee Director this year. A process was run to encourage applicants from within the Group and two candidates were shortlisted and interviewed by non-executive Board directors. We were pleased to appoint Claire Gibbard with effect from 28 July 2020. This position is an important part of how the Board interacts with the workforce and we wish Claire well in helping us to improve the quality of our decision making.

Roy Irwin and Geraint Davies have indicated their intention to retire from the Board and will not offer themselves for re-election at the 2021 AGM.

Roy joined the Board in 2017, bringing over 30 years of experience gained in a variety of senior roles in public sector housing. Geraint joined the Board in 2015, having been in professional practice as a chartered accountant for over 25 years. Both have offered their considerable knowledge and wisdom which has been invaluable at the Board table and also in many other discussions within the company.

Geraint has chaired the audit committee since appointment while Roy has served on the Remuneration Committee, and for the last two years has been its chairman. Much Board-level work is now done at committee level and both Roy and Geraint have provided exceptional service to the company in these roles during their tenure. I take this opportunity to thank them on behalf of the company for all of their work and input to the company over the last four and six years respectively.

Post the AGM, Jim Clarke, having been a member of the Audit Committee since his appointment to the Board in July 2019, will become its chairman. Julia Unwin will become a member of that committee. Chris Loughlin, who has been a member of the Remuneration Committee since his appointment to the board in September 2019, will become its chairman. Jim Clarke will become a member of that committee. Julia Unwin has indicated her wish to stand down as Senior Independent Director after three years in the role and Chris Loughlin has also agreed to take on that responsibility. The Board would like to thank Julia for her work as SID over the last three years.

In line with the overall streamlining of the Group which has occurred over the last couple of years, these decisions collectively provide an opportunity to modestly reduce the overall size of the Board, keeping in mind the need to remain compliant with the Code. Accordingly, it is intended to add one new non-executive director to the Board and a search will be commenced shortly to identify to identify a suitable candidate.

Relationships with shareholders

I maintained contact with shareholders throughout 2020, although face-to-face meetings were not possible, and have continued dialogue into 2021, including with a number of new holders who have joined the register in the last 12 months. It remains my view that, while the executive team should lead dialogue with shareholders about company performance, the chairman should be available to hear their views. I intend to continue dialogue into the year.

ESG

From its creation in 1988, Mears has sought to differentiate itself with a consistent and long-term focus on the wider societal value, as well as financial value, which it can and should generate. This is reflected by a commitment which can be seen throughout the Group to the lives of the people we support and the communities in which they live, the quality of the staff experience itself and, increasingly, a commitment to change in the environmental agenda. This is a core purpose for the company and, accordingly, for those who work within it.

The strength of the commitment is evidence by the company's continued success over many years in a number of areas, whether it be the FTSE4Good accreditation programme, the Sunday Times' Top 25 Best Big companies to work for or the Royal Society for the Prevention of Accidents Order of Distinction Award. In 2020, we have refocused the work of the Mears Foundation, our staff charity based on give-as-you-earn with employer matching, where we now have an independent chair and, for the first time, a General Manager. Similarly, the Mears Customer Scrutiny board, chaired by Terrie Alafat, has started its work to help us to improve the way we work with tenants to help them receive the best service from us. The ESG section of the Strategic Report later in this document gives more details of the very wide range of initiatives which the company has in place to generate value.

During 2020, we appointed our first Head of Carbon Reduction. This individual will help to develop our efforts in two areas. First, as discussed above and in the Strategic Report, the Company believes that the country's need to change the way in which we heat residential housing will open up revenue generating opportunities for us. But, in addition, Mears must make its own contribution to the country's net zero target and it will be a priority for the Board this year to develop a programme to 'green' Mears.

Summary

2020 was a challenging year, and for many of our people a difficult one. The success of the vaccination programme is opening up hope that the economy, Mears' position within it and our lives generally, can progressively move back towards normality. The actions which the Company has taken during the pandemic will stand it in very good stead for the recovery. I would like to give my thanks to the senior management team for the unstinting efforts which they have made during 2020 and subsequently which have left the company in a much better condition than it was at the start of last year. Finally, I would like to thank again the Mears workforce whose commitment to the company and the people who we serve is such an important reason why the Group will continue to prosper into 2021 and beyond.

K Murphy
Chairman

kieran.murphy@mearsgroup.co.uk

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I would like to thank again the Mears workforce whose commitment to the company and the people who we serve is such an important reason why the Group will continue to prosper into 2021 and beyond."

Strategic report continued

Chief Executive Officer's review



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Notwithstanding the operational challenges brought by Covid-19, it is pleasing that the Group made such strong progress against all of its key strategic objectives

David Miles
Chief Executive Officer

£2.6bn

(2019: 2.5bn) – Secured order book

53%

(2019: 39%) – New bid conversion rate
(by value)

0.15

(2019: 0.23) – Accident Frequency rate

Introduction

I am extremely proud of the resilience shown by the Group during a year which has seen unprecedented challenges.

Notwithstanding the fact that much of the energy and focus in 2020 was expended in reacting to the operational challenges brought by Covid-19, it is pleasing that the Group made such strong progress against all of its key strategic objectives as detailed below:

- Having already been included within the Sunday Times list of top 25 Best Big Companies to work for, the staff survey carried out in June 2020 saw our scores reach a new high, reflecting the efforts made on communication and keeping all staff safe, involved and supported. In addition, we saw positive progress on our key workforce measurements in respect of staff retention and diversity.

- The Group completed its exit from standalone Domiciliary Care with the disposal of its England and Wales Domiciliary Care business in January 2020 followed by the disposal of the Scotland business in September 2020. Recognising the sensitivity of completing the sale of a Care business during a pandemic, the Board delayed the completion of the second transaction until the end of the third quarter, whilst providing transitional support to the buyer for an extended period to ensure no negative impact upon service users as a result of this transaction.

- ▶ The Group completed the disposal of its planning solutions business ('Terraquest') in November 2020, generating an upfront cash inflow of £52.5m (after transaction costs) and a profit on disposal of £52.8m. Following a strategic review, the Board considered the business activities of Terraquest to be different from the core activities of the Group, and that the prospects of Terraquest would be optimised under new ownership. The disposal contributed to the Board's stated objective of reducing indebtedness of the Group and hence strengthening its balance sheet. A deal arrangement including contingent consideration and continued equity participation provides Mears' shareholders an opportunity to benefit further from future upside
- ▶ Despite significant market disruption, the Company has continued to make progress in managing the unwind of the Development part of the business. The working capital absorbed in this area of c.£25.0m was maintained at a similar level to the prior year. Unit sales picked up in the second half and have continued into the new year. Given the relatively low number of outstanding units, and the advanced stage of completion of the two active sites, the risk associated with this area of the business has been much reduced over the last 12-months.
- ▶ The Group has reported a significant reduction in its indebtedness, reporting an adjusted net cash at 31 December 2020 of £56.9m (2019: net debt: £51.0m). Importantly, the Group has reported a quarter-on-quarter improvement in its average daily net debt, which for the full year was £97.3m (2019: £114.4m). Restating this average on a pro-forma basis for the impact of the Terraquest disposal and for temporary improvements flowing from Covid-19, gives an adjusted average daily net debt for the year of £66.8m.

COVID-19

Given the year that has been experienced globally, which has impacted all employees and stakeholders, it is inevitable that Covid-19 is a theme running consistently throughout this year-end statement and it has had a significant impact across all the Group's key performance measures. I will initially address this upfront from a Group perspective, whilst leaving the finer detail to be addressed below.

Mears' response to Covid-19 was swift and decisive. Positively, service levels have remained at their traditionally high levels, with many clients directly complimenting the exceptional performance and dedication of the Mears workforce. The Group's IT systems enabled a swift transfer to remote working for many staff. The Group's ability to adapt so quickly to the new methods required for managing the business benefited from the investment made in the core systems over many years, and the customer-centric ethos which has consistently been core to Mears' values. As detailed below, the Group received tremendous support from its clients throughout this period, which would not have been forthcoming without the strong client relationships built over many years. Accordingly, we have been able to retain our key people, infrastructure, clients and capabilities through the pandemic and are well-positioned to make a full recovery once normality returns. The demand for the services the Group provides is undiminished by Covid-19 and a back-log of lower priority maintenance-led jobs now requires swift resolution. The health inequalities that the pandemic has so cruelly exposed, will only add further political pressure to increase and upgrade the affordable and social housing stock in the UK.

In adapting to new ways of working, the primary focus has always been the safety and well-being of our staff and of the individual customers to whom services are provided. As with many of our peers, access to PPE was difficult at times but the established procurement routes, together with the support of many clients, helped to keep staff fully protected.

The Group's success depended upon the commitment and engagement of its workforce. Significant extra effort has been put into workforce management and the Group is pleased to put on record its recognition of the dedication and commitment shown by all our staff and our appreciation for the fundamental role they played.

Financial performance Group

This review focusses upon the performance of the Group's continuing operations. A detailed analysis of the Group's discontinued operations is included within the Financial review.

The challenges of Covid-19 had a significant impact on the Group's trading results, particularly in the Maintenance-led activities in the first half of the financial year, which were restricted to the delivery of essential and priority services only. However, in the second half, as lockdown restrictions eased our clients and service users adapted to the changing environment and the Group experienced a lesser impact on work volumes, even in subsequent lockdowns. Accordingly, financial performance recovered strongly in the second half, with all areas of our maintenance-led and management-led activities returning to profitability in this period.

Following the disposal of the Group's Domiciliary Care and Planning Solution activities, Mears is a smaller and simpler business with a single strategic focus; to be a leading provider of housing solutions. This single Housing segment reported revenues in the period of £805.8m (2019: £881.5m) and adjusted operating profits (pre IFRS-16) of £0.6m (2019: £37.6m).

The Group's Housing activities have historically been categorised between maintenance-led, management-led and Development. This categorisation remains relevant particularly with respect to Development, but following these disposals, the significant proportion of the contracts allocated between maintenance-led and management-led are similar in nature, being predominantly non-discretionary housing and accommodation services with a public sector customer, enjoying similar risk sharing mechanics, margin structure and contract lengths. From an internal perspective, these two categories are treated as one when it comes to allocating resources and managing performance. It is also important to recognise that our management-led contracts require the delivery of maintenance as part of the service offering, and similarly our maintenance-led contracts include a significant level of tenancy management.

Strategic report continued

Chief Executive Officer's review continued

Continuing activities	H1 2020 £m	H2 2020 £m	FY 2020 £m	2019 £m
Revenue				
Maintenance-led	266.9	270.0	536.9	660.7
Management-led	121.2	132.6	253.8	181.3
Development	8.6	6.5	15.1	39.5
Total	396.7	409.1	805.8	881.5
Operating profit measures				
Statutory operating (loss)/profit	(8.8)	2.5	(6.3)	28.1
Adjusted operating (loss)/profit (post-IFRS16) ³	(3.1)	9.7	6.6	41.1
Adjusted operating (loss)/profit (pre-IFRS16) ⁴	(5.9)	6.5	0.6	37.6
Profit before tax measures				
Statutory (Loss)/profit before tax	(13.9)	(1.3)	(15.2)	20.3
Adjusted (loss)/profit before tax ⁵	(8.2)	4.8	(3.4)	32.4

While disclosure of revenue trends between these 'Management-led' and 'Maintenance-led' contracts remains of relevance, the disposal of the Domiciliary Care and Planning Solutions, together with the withdrawal from Development, makes the split of operating margin against each category of limited value. The Group has a single support function servicing all continuing activities and applying an arbitrary allocation of central overheads against each revenue stream is not reflective of the commercial reality. The continuing maintenance-led and management-led activities are priced to achieve similar operating margins.

The Group reported a statutory loss before tax on continuing activities of £15.2m (2019: profit before tax £20.3m). At the adjusted PBT level the Group returned to profitability in the second half posting a profit of £4.8m (H1 2020: £(8.2m)). The Group's adjusted loss before tax for the full year was therefore (£3.4m) (2019: adjusted profit £32.4m). This outturn for the full year represents a very resilient financial performance given the impact of the pandemic and was in line with the Board's expectations set at the half year of 2020. The disposal of Terraquest in late in 2020 resulted in the Terraquest profit contribution being included within discontinued activities and accordingly continuing adjusted PBT moved to the small loss stated above.

As described in detail below, the Group adapted quickly at the start of the first national lockdown to agree interim operating and financial arrangements with its maintenance-led clients. In the majority of cases, this limited maintenance-led activity in people's homes to an emergency-only service and provided new payment mechanisms which (at a minimum) were sufficient to cover direct costs and local site overheads. These arrangements varied by client, but typically these new arrangement fell short of covering central support costs and a profit margin, in line with central government guidance. This was the principle factor in the significant reduction in profitability in 2020. A small number of maintenance-led clients failed to provide any financial support and those contracts account disproportionately towards the operating loss in the first half.

Positively, notwithstanding the operational challenges, the management-led activities delivered an operating profit which was in line with management expectations at the start of the year.

In respect of the services delivered under the maintenance-led category, the Group saw a significant reduction in work volumes as the UK entered the first national lockdown. Generally, a consistent position was taken across all our Local Authority and Housing Association clients, with activity levels reducing to cover only

emergency and priority works which was typically 15-20% of the normal level of activity. The primary focus was ensuring the safety of our workforce and our vulnerable service users. The primary focus was ensuring the safety of our workforce and our vulnerable service users.

The pricing mechanisms attached to the Group's maintenance-led contracts can broadly be split into two types which brought different financial challenges and required different negotiated solutions with clients:

- ▶ a lump sum mechanism where Mears receives a fixed amount, irrespective of work volumes. Whilst revenues have been recognised against these works, the pandemic has resulted in some order backlog and costs have been accrued to protect against the unwinding of this backlog when normality returns. In a normal year, around 25% of the Group's maintenance-led revenues fall into this lump sum category.
- ▶ a volume linked pricing mechanism where the revenues generated are directly linked to the activities delivered. In a period that saw such a sharp drop in activity, but required the continued provision of emergency cover, these volume-linked mechanisms represented a significant financial risk to the Group. Positively, in most cases, the Group secured interim arrangements with its clients to address these risks and ensure the recovery of direct labour and local overheads ("cost reimbursement models"). Whilst these interim arrangements removed much of the downside financial risk, such arrangements typically provided reduced recovery of central overheads and a limited profit contribution. Around 75% of the Group's maintenance-led contracts fall into this volume linked category.

Whilst the Group's clients took a consistent stance on entering the first national lockdown, there was less consistency in the approach and speed over which lower-priority works started to return. The picture was further complicated by the regional nature of further restrictions through the second half and ultimately the return to national lockdown in November and

³ Adjusted operating (loss)/profit (post-IFRS16) stated on continuing activities before exceptional items, the amortisation of acquired intangibles and the application of IFRS 16 and inclusive of share of profit from associates.

⁴ Adjusted operating (loss)/profit (pre-IFRS16) stated on continuing activities before exceptional items, the amortisation of acquired intangibles and the application of IFRS 16 and inclusive of share of profit from associates.

⁵ Adjusted profit/(loss) before tax stated on continuing activities before exceptional items and before the amortisation of acquired intangibles. See Financial Review for reconciliation of alternative performance measure.

December. In addition, the Group recognised early in the pandemic that normality was unlikely to return quickly, and that there remained a risk of further lockdowns; in doing so, the Group chose to take a more conservative approach in managing the return to normality. Whilst it was disappointing to see a second and third national lockdown spanning the year end, it highlighted that the Group's approach has been the right one. Prudently, the Group had retained the majority of its cost reimbursement mechanisms with clients, thereby protecting the Group from further downside risk as work volumes again saw some volatility through the second and third national lockdowns, albeit not the same extremes as the first lockdown.

The Group utilised the job retention scheme ('furlough'), taking guidance from its clients before adopting an approach on a contract by contract basis. Where clients agreed interim arrangements with the Group, the impact of the cost reduction generated from furlough was incorporated into those mechanisms, and ultimately any open book reconciliation will ensure all savings are passed on to clients, within the spirit of the scheme. The Group also utilised furlough in respect of its central support functions to further mitigate financial downside and more importantly the ability to retain exceptional staff. I am pleased to note the Group has also elected to repay its furlough rebate in respect of the first quarter of 2021 amounting to around £1.5m, recognising the improving performance of the Group and reduced uncertainty surrounding Covid-19.

The maintenance-led activities reported revenues of £536.9m (2019: £660.7m), a reduction by 19%. A revenue reduction is inevitable given the impact of Covid-19, although the percentage reduction in revenues in the second-quarter by around 50%, is significantly less than the reduction in work volumes which, during the first national lockdown, non-emergency works reduced by up to 80%. As detailed above, where the Group delivered maintenance-led services under a volume linked pricing mechanism, a significant proportion of those contracts saw temporary arrangements, adopting a short-term cost reimbursement mechanism. Accordingly, there is less of a defined correlation between work volumes, revenues and profitability in this year than in prior years.

Revenue by quarter

2020 Revenue by quarter

	Q1 £m	Q2 £m	Q3 £m	Q4 £m	Total £m
Maintenance-led	173.9	93.0	131.6	138.4	536.9
	Q1 £m	Q2 £m	Q3 £m	Q4 £m	Total £m
Management-led	61.5	59.7	65.0	67.6	253.8
	Q1 £m	Q2 £m	Q3 £m	Q4 £m	Total £m
Development	7.1	1.5	3.2	3.3	15.1

As disclosed previously, in the early part of 2020 and prior to the impact of Covid-19, the Group saw the expiry of a small number of contracts with annual revenues amounting to circa £45m where the Group did not participate in a retender. In addition, the Group had taken action to exit contracts with annual revenues of circa £20m, where the Group identified certain contracts as not fitting the criteria of the Mears way of working. In addition, the Group also terminated several customer relationships, with an annual revenue of £30m, where the Group could not sufficiently mitigate the short-term risk, and the longer-term payback was not sufficiently visible.

In respect of the services delivered under the management-led category, the Group saw increasing demand during the year. This is because the large numbers of key workers and vulnerable service users whose accommodation and other service needs provided by Mears were undiminished (if not increased) by the pandemic. Accordingly, the challenge in this category was not financial but the operational challenge of continuing to support such vulnerable service users whilst adhering to the social distancing and other Covid-19 restrictions. The management activities reported revenues of £253.8m (2019: £181.3m), an increase of 40%. Much of this increase is due to the full year impact of the Asylum Accommodation and Support Contract ('AASC') which mobilised in September 2019.

The Group saw an increase in AASC volumes across the entire process over the course of the year, with new service users entering the system and few exiting. The requirement for additional accommodation was operationally challenging. Covid-19 presented a challenge for those people new to the UK with many lacking language skills and the knowledge to access basic supplies and necessities. In agreement with the relevant public authorities, it was decided that the safest environment for new service users was to locate them in good quality hotels.

That ensured their protection from Covid-19 infection, the ability to self-isolate if required and that they had access to food and other essentials. Despite recognising that few people want to be in a hotel for an extended period it was agreed that this was absolutely the right approach. It remains the intention to support moving these people into dispersed accommodation as soon as it is safe to do so. Mears' priority throughout and going forward, will be the safety of staff and the service users.

When excluding growth from the AASC contract, the pre-existing Management-led business has reported a revenue reduction. This is in line with management expectations, as the Group reduces its focus on emergency homelessness solutions. The Group's Key Worker housing management contract with the Defence Infrastructure Organisation has performed well through the year, with all major performance KPIs being met. This contract is in re-bid with the result expected shortly. Mears has been shortlisted with one other party.

The 2019 comparative figures for the management-led revenue category have been adjusted to remove the Group's planning solutions activity ('Terraquest'). The figure includes revenues generated by the Group's Extra Care and Supported Living activities

Strategic report continued

Chief Executive Officer's review continued

Development plots

	units
Completed units as at 1 January 2020	29
Units completed during period	43
Units sold during period	(23)
Completed units at 31 December	49*
Building in progress at 31 December (in addition to completed units)	43
Net Working Capital absorbed (average month-end)	£25.0m (2019: £24.7m)

* Of the 92 total units (completed and live) at year end; 10 units have been sold since year end and 22 units are subject to reservation

('Housing with Care') and which continues to represent an important value generating opportunity for the future.

The Group made a clear strategic decision in 2019 to reduce its exposure to Development activity and exit from those new build activities which utilised significant amounts of the Group's working capital. These new build sites were developed in conjunction with a number of the Group's existing clients and the Group continues to honour its commitments to deliver and sell-through on the remaining active projects. During the Covid-19 outbreak, the remaining two active building sites were mothballed, and action was taken immediately to reduce the fixed cost base. These sites have subsequently been reopened but the activity maintained at a low level to ensure that working capital cash flows are tightly controlled.

The sales activity in 2020 was restricted to predominantly four remaining sites, and the units completed and sold are detailed above. The Board is taking active steps to accelerate the unwind of the working capital absorbed in this area, and maintain a sensible balance between liquidity and maximising value.

Strategy

We are leaders in the affordable housing market, for which the future demand profile remains positive, given the fundamental shortage and poor quality of affordable housing in the UK. With the non-core disposal programme completed during the year, the Board conducted a strategic review, together with external consultants to refine and enhance the Group's strategy to be the most respected housing specialist outsourced service provider in the UK.

Work is continuing, but the fundamental attractions of our existing business and the

key drivers of its future growth are already clear. After a period of strategic transition and Covid-19 disruption, Mears has a number of simple market, growth and margin drivers across its Housing solutions businesses:

Market drivers

- ▶ Increased government investment in the affordable housing sector given expanding social housing waiting lists and renewed political focus on housing post-Covid
- ▶ Social Housing white paper and Government policy towards higher standards for safety and customer engagement
- ▶ The commitment to raise the carbon efficiency of all social housing stock by one EPC band by 2030, presents significant investment requirements
- ▶ Increasing Local Authority spend on long-term, cost-effective Homelessness solutions
- ▶ On-going demographic pressure on the UK housing shortage particularly in Mears core competencies of affordable rental and specialist retirement living

Mears growth drivers

- ▶ Leverage our market leading position in housing maintenance to better cross-sell/ upsell our broader housing services through more effective client planning
- ▶ Continue to evolve our affordable rental, temporary accommodation, and integrated housing offer to meet increasing market demands
- ▶ Participation in larger, integrated housing contracts, across Local and Central Government
- ▶ Assist new and existing clients to meet their targets for the de-carbonisation of housing stock

Margin drivers

- ▶ Fully restore normal charging mechanisms, overhead recovery and operating profit margins as interim Covid restrictions ease and volumes return
- ▶ Drive greater operational efficiencies through more centralised administrative and support services such as our regional Hub network
- ▶ Continued digital innovation to increase agility of frontline operations whilst continuing to drive improvements to the customers experience
- ▶ Operational consistency across the Group and contract rationalisation to improve underperforming contracts

Even with the potential post-Covid economic challenges, Housing is a sector that will be invested in to support economic recovery and indeed to meet longer term challenges, such as those posed by climate change. There is clear opportunity to grow both our maintenance-led and management-led work and indeed we see an increasing number of opportunities that will integrate all of our services. The responsible approach that we have taken to business through Covid and indeed from the start of Mears, has left us really well placed to benefit from these opportunities.

Current trading and guidance

The Board is pleased with the resilient trading and liquidity performance of the Group during the first quarter of FY2021 and is confident of a full recovery as lockdown restrictions are lifted. Accordingly, profitability for the full year is expected to be H2 weighted. Cash and working capital management has remained in-line with expectations in Q1, with average daily net debt of £17.0m.

The Group is confident to re-instate the following guidance:

	Key measures	Guidance FY21
Revenue growth	Annual revenue growth	► FY 21 Revenues: £770m-£820m
Profit before tax	Profit before tax before exceptional items and amortisation of acquired intangibles	► FY 21 Profit before tax: £21.3m-25.5m
Cash conversion	Operating cash inflow as a % of EBITDA	<ul style="list-style-type: none"> ► 100% conversion on the combined 2020/2021 results; taking the two year measure removes the short-term Covid related impacts such as the VAT deferral and client payments received on account ► £25m of Development working capital unwind over 2 years
Capex		<ul style="list-style-type: none"> ► c.1.25% of revenue
Capital allocation	Investment	<ul style="list-style-type: none"> ► Not material in FY21 (or FY22)
	Capital structure (adjusted net debt (pre-IFRS-16) / EBITDA (pre-IFRS-16))	<ul style="list-style-type: none"> ► Continued average net debt reduction
	Shareholder distributions	<ul style="list-style-type: none"> ► Return to dividend list as soon as prudent

Strategic report continued

Chief Executive Officer's review continued

Orderbook and bid pipeline

The order book stands at £2.6bn (2019: £2.5bn), a consistent level over the last twelve months reflecting a number of contract extensions. The Group secured maintenance-led contracts in 2020 valued at over £150m with a win rate (by value) of 53%. The key orders secured are detailed below:

	Base term (years)	Extension option (years)	Annual value £m	Base contract value £m	New/ Retention
Contracts awarded in 2020					
Exeter City Council; repairs and maintenance	10	5	8.5	85.0	Retention
London Borough of Hammersmith and Fulham; repairs and maintenance	5	2	4.2	21.0	Retention
Islington Council; cyclical works	4	6	10.0	40.0	Retention
Sub-total; secured in 2020			22.7	146.0	
London Borough of Redbridge; repairs and maintenance	7	7	5.2	36.4	Retention
Angus Council	3	2	2.3	6.9	New
Leeds City Council; repairs and maintenance	5	–	12.8	64.0	Retention
Sub-total; secured in 2021 to date			20.3	107.3	

In addition, Mears was delighted to secure a three-year contract extension with Milton Keynes Council, which will see Mears continue to provide services, with an annual value of around £40m per annum, until at least April 2024. This contract, which mobilised in April 2016, has delivered excellence in respect of service delivery and employee engagement, and it was pleasing to see the efforts of our local team recognised and rewarded with this extension.

Mears has also been confirmed as the preferred bidder by Cornwall Council, to be a strategic partner to deliver to the Council up to 750 new extra care units across the County over the next 7-10 years. As Strategic Partner, and using Council owned land, Mears will

deliver the end to end solution to identify funders, and to design, build, manage and maintain the units over a period of up to 30 years. Mears is not required to commit significant working capital. The contract value attached to this contract may be significant but at this stage no value has been assigned to the order book in respect of this opportunity.

The Group has an active bid pipeline. Given the bidding delays across the market as a result of Covid-19, 2020 was a relatively quiet year for bid activity. However, we are now entering a period of increased bid activity. This includes a c.£25m annual revenue contract for the national accommodation management services under the Future Defence Infrastructure Services programme.

There are also a number of existing contracts which are active live tenders, with a combined annual revenue of circa £100m. These are important clients to the Group, and we remain confident that we will retain these key customer relationships. This re-bid activity includes the work we do with the Defence Infrastructure Organisation providing housing management and relocation services to key workers nationally. This contract is worth £60m of revenue per annum. Mears is short-listed in the final two candidates and an outcome is expected shortly.

David Miles
Chief Executive Officer

An interview with the Chief Executive Officer

Q How has Covid 19 changed your business?

A I would say that whilst it has been extremely disruptive for all businesses, we have taken the lessons learnt from 2020 to create a much more streamlined and focused business. Our response from staff has been outstanding and some of the individual stories and team stories of how Mears has supported communities, will live long in the memory. We were able to adapt immediately to the challenges of remote working, given our leading technology platforms and we have managed covid health risks for staff and customers very well. Sadly of course, some of our elderly service users, particularly on the care business, did lose their lives as a result of covid. Our heartfelt commiserations go out to every family impacted.

Our housing maintenance business did see significant volume reductions during the peak lockdown period but this largely recovered by the end of 2020. This meant we did have to use Furlough to protect staff. Our housing management business grew, given the pressures on the Asylum system, which Mears has done everything it can to support.

At the start of 2021 I am proud to report that we have a simple, focussed and resilient business with lots of opportunities for growth.

Q Has Mears engaged with Central Government during the Pandemic?

A Yes, and we are lucky to have the support of our Crown Representative in the Cabinet Office which has enabled us to raise issues of concern direct to the Government – a good example being the supply of PPE to our key workers, where Mears were one of the first organisations to appeal for better support to the care sector and we are obviously pleased to see that there is greater awareness now amongst the public, of the important work that care staff do. Even after the sale of our domiciliary care services, we still have 1000 people employed providing care within Extra Care and Supported Living environments.

Q Do you think you have handled the Asylum contract responsibly?

A Seeing the hard work which goes on to house and care for asylum seekers behind the scenes has made me very proud. This contract has been especially challenging during a pandemic and a national lockdown and we saw the sad event in Glasgow which led to injury of colleagues, police officers and asylum seekers and the loss of life of the perpetrator.

I am confident that beyond this extremely upsetting event we have acted with the care and welfare of our customers as our first thought. We have managed our facilities in such a way which ensured that we were able to provide direct access to healthcare and support and all other amenities.

2021 will see further increases in housing stock which will be managed and maintained to our extremely high standards.

Q How have you helped staff during a very difficult period?

A During a very uncertain year for everyone we knew that as an employer we had a duty to support our workforce, whether financially or by ensuring our welfare offer was right for them. We took the decision to pay 100% of furloughed colleagues pay for those on £20,000 or below and we paid 80% of those salaries above £20,000 without the Government cap. We introduced a hardship fund for colleagues who were struggling and created a new awards programme to celebrate the achievements of those who went above and beyond during lockdown.

As an employer we knew that we had a responsibility to ensure that we were supporting people's mental health and wellbeing and as such we have reviewed and relaunched our wellbeing policy and instituted mental health first aiders as a first point of contact and have begun training managers to support mental health. The Mears policy over this difficult time has and continues to be "Let's keep talking".

Q Are there plans to sell any other parts of the business?

A No. In 2020 we saw the planned disposal of our domiciliary care businesses in England & Wales and Scotland and of Terraquest. These sales were planned and announced in our last annual report to enable us to focus in on what we have always been known for – as a provider of repairs and housing solutions. We remain active in the Supported Living and Extra Care sectors.

Q Do you see the Government continuing to invest in housing?

A Absolutely. The affordable housing sector will form a key plank in the Government's efforts to reduce our national carbon emissions and Mears stands ready to help the Government in this work. The national housing stock works on a constant cycle of repair and maintenance which will continue. We hope that post pandemic we will see Government commit to a new Decent Homes Standard, but I believe the future of housing investment remains very positive.

Q What will happen to Mears given Brexit?

A Mears has limited exposure to Brexit risk, given we do not export to the EU and most of our supplies come from the Far East. We remain ready to act on Government advice as the Brexit process goes on, but I remain very positive about the core affordable housing market in the UK.

Q What does the next 5 years hold for Mears?

A Mears has undertaken a strategy review looking at our markets and possible returns in the next 5 years. We find that we remain the dominant force in repairs and maintenance – and the national leader in reactive works. There is a huge opportunity to help to fulfil the UK's carbon targets and we have ensured that we have the right expertise in place.

We are a large private provider of temporary accommodation in the UK and there is a massive market where we have the opportunity to grow.

Mears has continued to retain and win contracts throughout the pandemic and we have a number of large opportunities in 2021.



Strategic report continued

Financial review

This section provides further key information in respect of the financial performance and financial position of the Group to the extent not already covered in detail within the Chief Executive Officer's Review.

Alternative performance measures ('APM')

The Strategic Report includes both statutory and adjusted performance measures, the latter of which is considered to be useful to stakeholders in projecting a basis for measuring the underlying performance of the business and excludes items which could distort the understanding of performance in the year and between periods, and when comparing the financial outputs to those of our peers. The APMs have been set considering the requirements and views of the Group's investors and debt funders amongst other stakeholders. The APMs and KPIs are aligned to the Group's strategy and also form the basis of the performance measures for remuneration.

These APMs should not be considered to be a substitute for or superior to IFRS measures, and the Board has endeavoured to report both statutory and alternative measures with equal prominence throughout the Strategic Report and Financial Statements.

The APMs used by the Group are detailed below and an explanation as to why management considers the APM to be useful in helping understanding as to the Group's underlying performance. A reconciliation is also provided to map each non-IFRS measure to its IFRS equivalent.

The Group defines normalised results as excluding the amortisation of acquisition intangibles and before other normalisation adjustments which management believe are infrequent in nature and are considered not to be part of underlying trading. The normalised results are further adjusted to reflect an 19% corporation tax charge. The Directors believe this aids consistency when comparing to historical results, and provides less incentive for the Group to participate in schemes where the primary intention is to reduce the tax charge. The Group's normalised results typically focus on continuing activities, however for completeness are also reported to include discontinued activities.

A reconciliation between the statutory profit measures and the normalised result for both 2020 and 2019 is detailed below. This is analysed between both continuing and discontinued activities together with the aggregate result for the Group.

	Note	2020 £'000	2019 £'000
Continuing activities			
(Loss)/profit before tax	Statutory	(15,218)	20,253
Amortisation of acquisition intangibles	Note 4	9,525	10,122
Non-underlying item: restructure costs	Note 8	779	–
Non-underlying item: fixed asset impairment	Note 8, 15	1,500	–
Non-underlying item: litigation costs	Note 8	–	2,018
Normalised (loss)/profit before tax	APM	(3,414)	32,393
Net Finance costs	Note 5	9,998	8,731
Normalised operating (loss)/profit	APM	6,584	41,125
Discontinued activities			
Profit/(loss) for the year before tax	Statutory	56,933	(82,223)
Non-underlying item: profit on disposal of business activities	Note 10	(54,074)	–
Non-underlying item: litigation costs	Note 10	1,206	–
Non-underlying item impairment of intangibles	Note 10	–	80,562
Normalised profit/(loss) before tax	APM	4,065	(1,661)
Net Finance income	Note 10	4	191
Normalised operating (loss)/profit	APM	4,069	(1,470)
All activities			
Profit for the year before tax	Statutory	41,715	(61,970)
Normalised profit for the year before tax	APM	651	30,732
Normalised operating profit for the year	APM	10,653	39,655

In addition, the Group also provides an APM which reports results before the impact of lease accounting under IFRS 16. Management have provided this alternative measure at the request of a number of shareholders and market analysts to allow those stakeholders to properly assess the results of the Group over-time. The Group adopted IFRS 16 from 1 January 2019 and the results prior to this date have not been re-stated resulting in a distortion of the results compared over time. In addition, the Group's banking covenants utilise adjustment profit measurements which are reported before IFRS 16 and stakeholders require better visibility of the Group's adjusted profit for that purpose.

A reconciliation between the statutory measure for EBITDA and the same measurement before the impact of IFRS 16 for 2020 and 2019 is detailed below:

	Note	2020 £'000	2019 £'000
Continuing activities			
(Loss)/profit before tax	Statutory	(15,218)	20,253
Removal of IFRS 16 profit impact	See below	1,118	2,223
Finance costs (non-IFRS 16)	Note 5	2,875	2,971
Amortisation of acquired intangibles	Note 4	9,526	10,122
Non-underlying items	Note 8	2,279	2,018
Operating profit pre-IFRS-16 before non-underlying items and amortisation of acquired intangibles	APM	580	37,587
Amortisation of software intangibles	Note 4	2,211	2,109
Depreciation and loss on disposal (non IFRS 16)	Note 4	5,677	5,955
EBITDA pre-IFRS 16 and before non-underlying items	APM	8,467	45,652
IFRS 16 profit impact		(1,118)	(2,223)
Finance costs (IFRS 16)	Note 5	7,123	5,760
Depreciation and loss on disposal (IFRS 16)	Note 4	42,242	29,908
EBITDA post-IFRS-16 before non-underlying items and amortisation of acquired intangibles	APM	56,714	79,096
Amortisation of software intangibles		(2,211)	(2,109)
Depreciation and loss on disposal (IFRS 16)	Note 4	(42,242)	(29,908)
Depreciation and loss on disposal (non-IFRS 16)	Note 4	(5,677)	(5,955)
Operating profit post IFRS 16 and before non-underlying items	APM	6,585	41,124
		2020 £'000	2019 £'000
Charge to income statement on a post-IFRS 16 basis		(49,365)	(35,668)
Charge to Income Statement on a pre-IFRS 16 basis		(48,247)	(33,445)
Profit impact from the adoption of IFRS 16		(1,118)	(2,223)

For the purposes of assessing the Group's compliance with its banking covenants, the Group utilises an adjusted measure based on EBITDA before the impact of IFRS 16 and before non-underlying items which are termed as 'exceptional items' within the Group's bank facility agreement.

A reconciliation between the statutory measure for Profit (loss) for the year attributable to shareholders before and after adjustments for both basic and diluted EPS is:

	Normalised (continuing)		Normalised (discontinued)		Normalised (continuing and discontinued)	
	2020 £'000	2019 £'000	2020 £'000	2019 £'000	2020 £'000	2019 £'000
Profit/(loss) attributable to shareholders:	(11,781)	17,367	56,242	(83,755)	44,461	(66,388)
Amortisation of acquisition intangibles	9,525	10,122	—	—	9,525	10,122
Full tax adjustment	(2,125)	(2,757)	(10,696)	1,360	(12,821)	(1,397)
Exceptional costs	1,846	1,634	(42,823)	65,255	(40,977)	66,889
Normalised earnings	(2,535)	26,366	2,723	(17,140)	188	9,226

Strategic report continued

Financial review continued

Net cash/(debt)

The Group excludes the financial impact from IFRS 16 from its adjusted net debt measure. This adjusted net debt measure has been introduced to align with the borrowings measurement which is defined for the Group's banking covenants, which are required to be stated before the impact of IFRS 16. The Group utilises leases as part of its day to day business providing around 10,000 residential properties to vulnerable service users and key workers. A significant proportion of these leases have break provisions and the lease terms are aligned to the Group's customer contracts to mitigate risk. The Group does not recognise these lease obligations as traditional debt instruments given the Group's ability to break these leases and in so doing cancel the associated lease obligation. A reconciliation between the reported net cash/(debt) and the adjusted measure is detailed below:

	Note	2020 £'000	2019 £'000
Cash and cash equivalents		96,220	73,061
Long-term borrowings and overdrafts		(39,353)	(124,047)
Adjusted net cash/(debt)	APM	56,867	(50,986)
Lease liabilities (current)	Note 24	(42,888)	(39,175)
Lease liabilities (non-current)	Note 24	(166,183)	(166,000)
Total	Statutory	(152,204)	(256,161)
Less: Lease Obligations (IFRS 16)	Note 24	209,071	205,175
Adjusted net cash/(debt)		56,867	(50,986)

COVID-19

The business faced significant challenges in mitigating the risks of Covid-19, reacting quickly to the fast-changing environment and maintaining traditionally high service levels, albeit often at lower levels of activity as the business focussed on emergency and high priority works.

It is inevitable that the financial outputs delivered in 2020 have been significantly impacted by these events and this is covered in detail throughout the Annual Report. From a financial perspective, I would highlight two key messages:

- ▶ Firstly, the support that we received from our clients was fantastic and we do not take this for granted. However, this level of support should also be recognised as payback for our strong customer-centric approach which has underpinned the culture of the Group from its inception. Mears' investment in social value and community engagement underpins those strong local relationships and was fundamental in being able to put in place interim arrangements so quickly, giving stability and protecting the Group's liquidity
- ▶ Secondly, the investment that we have made in our core IT systems was critical in the Group being able to adapt so quickly to new methods of working, maintaining strong service delivery and liquidity during a period where much of the business was carried out remotely.

As described in detail within the Chief Executive Officer's review, the Group adapted quickly at the start of the first national lockdown to agree interim arrangements with maintenance-led clients that ensured in the majority of cases, a new pricing mechanism which was typically sufficient to cover direct costs and local site overheads. However, this often fell short of covering central support costs and a profit margin. This was the most significant factor in the loss reported for 2020.

In adapting to new ways of working, the primary focus has always been the safety and well-being of our staff and of the individual customers and ensuring that they were kept fully protected although access to PPE was difficult at times. The Group's saw its PPE expenditure increase by £1.7m in the year, with further PPE provided by clients, free of charge.

To mitigate losses flowing from Covid-19, and the impact of a significant reduction in work volumes, the Group participated in the Government's Job Retention Scheme. The number of people furloughed peaked at around 2,200 employees in May 2020 and there remained a small number of people on furlough at the year end. Under this scheme, individuals were put on an extended period of leave during which time HMRC reimbursed Mears for 80% of their pay, up to £30,000. Mears applied top-up payments to ensure the lowest paid saw no reduction in pay, and those higher paid employees received no less than 80% of their normal pay. Total top-up payments made to people on furlough amounted to £3.0m. Total payments made to those on furlough amounted to £19.1m and the total recovery was £16.1m.

Whilst the cost of PPE and Furlough combined amounts to around £4.7m, the Directors concluded that it would be inappropriate to treat this as an exceptional item and it is not adjusted within the Group's APM. The Group was able to recover a proportion of this additional cost through its contract relationships which mitigated part of this loss. In addition, an element of the PPE was incurred in relation to the Group's discontinued Domiciliary Care activities, and therefore does not impact on the Group's headline performance measures which look to the continuing activities only.

Restatement of Prior Year – Reassessment of Lease Accounting

During the year, the Group revisited the assumptions made at the time of the adoption of IFRS 16, and its assessment of the right of use assets and lease obligations as at transition and at 31 December 2019. The Directors have concluded that in the prior year, the right of use asset and associated lease obligation were overstated and as such, the Consolidated Statement of Profit or Loss, Consolidated Balance Sheet and Consolidated Cash Flow Statement have been restated to correct this error. In respect of the Statements of Profit or Loss and Cash Flow, the adjustments to the prior year have no impact upon their respective bottom lines. The restatements to the Balance Sheet are significant and reduces retained earnings by £0.7m. The accounting for residential leases is covered in detail below and the line level adjustments together with additional explanation is included within note 33 to the financial statements.

Non-underlying items

Non-underlying items are items which are considered outside normal operations. They are material to the results of the Group either through their size or nature. These items have been disclosed separately on the face of the Income Statement to provide a better understanding as to the underlying performance of the Group.

	2020 £'000	2019 £'000
Restructure costs	779	–
Impairment of assets in the course of construction	1,500	–
Exceptional legal costs	–	2,018
	2,279	2,018

(i) Restructuring costs

The Group incurred restructuring costs in 2020 of £3.2m (2019: £1.7m) of which £0.8m (2019: £nil) has been categorised within non-underlying items. In choosing how to report and disclose the impact of this expense, management has focussed on distinguishing between the different types of restructuring cost incurred. Restructuring costs are included within the statutory operating profit measures to the extent that they arise from Group-wide initiatives to reduce the ongoing cost base and improve efficiency in the business or where they relate to local initiatives at a branch level which will typically be supported by a business case which shows a positive financial impact to the Group over the longer-term. This is not considered exceptional as they are recurring in nature and reflect the normal day to day stewardship of the business. However, restructuring costs are excluded from the adjusted operating profit to the extent they arise from initiatives which are significant in scope and impact but will not form part of recurring operational activities in the future; in this case this included redundancy costs associated with the Development activities and the terminations of a number of maintenance-led contracts.

(ii) Impairment of assets in the course of construction

In 2018, Mears commenced the construction of a modular homes scheme which has, over the previous two financial years, been disclosed as an asset in the course of construction. The off-site construction is complete, however the impact of Covid-19 has meant that a significant part of the on-site installation remains outstanding. The original agreement was that upon completion, Mears would lease these units to a Local Authority client for a period of 15 years and the lease payments would fund the construction cost. Given the Board's stated objective to reduce the Group's indebtedness, the Group agreed to a contract variation which has removed Mears entirely from this arrangement, in return for a fixed payment of £6.4 million, payable on completion of the installation. As at 31 December 2020, Mears had incurred capital expenditure of £5.8m. Following an assessment of the costs incurred to date, and the costs required to complete the on-site installation, an impairment has been recognised on the asset in the course of construction by £1.5m. Following the reduction in the carrying value, the asset has been re-categorised as a contract asset. The impairment charge applied against this asset is considered to be an exceptional item. It is abnormal in size and nature and relates to an activity which is not part of the continuing activities of the Group.

Amortisation of acquisition intangibles

	2020 £'000	2019 £'000
Amortisation charge	9,525	10,122

A charge for amortisation of acquisition intangibles arose in the year of £9.5m (2019: £10.1m). The majority of the remaining carrying value of acquired intangible of £10.3m will be amortised during 2021. As detailed above, the Group adjusts for this charge within the Group's alternative profit measure. This amortisation charge is very material in size and can vary significantly based upon the Directors' assessment of useful economic life. The Group's shareholders and market analysts typically add back this item in their analysis and the Group's alternative performance measure is aligned to that. Management believe that through reporting profit figures that excludes this item can help the reader to more easily understand the underlying performance of the business, without any distortion as a result of this charge.

Strategic report continued

Financial review continued

Discontinued activities

The Chairman's Statement and Chief Executive Officer's review focuses upon the results relating to the continuing activities of the Group. However, 2020 was a particularly active year in refocussing Mears on housing activities, with the Group completing its exit from standalone Domiciliary Care and the sale of its planning solutions business ('Terraquest'). Both transactions are covered in greater detail below, and the trading results for the period leading up to disposal are included with additional granularity, whilst aggregated into a single line on the face of the Income Statement. The other category comprises litigation costs relating to a business sold in 2013.

	2020				2019		
	Planning solutions £'000	Domiciliary Care £'000	Other £'000	Total £'000	2019 £'000	2020 £'000	2019 £'000
Sales revenue	16,282	19,106	–	35,388	20,879	77,521	98,400
Cost of sales	(6,403)	(14,384)	–	(20,787)	(9,029)	(61,411)	(70,440)
Gross profit	9,880	4,722	–	14,602	11,850	16,110	27,960
Administrative expenses	(5,101)	(5,436)	–	(10,532)	(6,788)	(22,642)	(29,430)
Finance (costs)/income	–	(4)	–	(4)	(114)	(77)	(191)
Profit/(loss) for the year before tax before exceptional items	4,779	(714)	–	4,066	4,948	(6,609)	(1,661)
Exceptional items	52,798	1,054	(984)	52,868	–	(80,562)	(80,562)
Profit/(loss) for the year before tax and before exceptional items	57,577	340	(984)	56,933	4,948	73,953	(82,223)
Tax	(121)	–	–	(121)	(961)	(100)	(1,061)
Profit/(loss) for the year after tax	57,456	340	(984)	56,812	3,987	73,853	(83,284)

(i) Domiciliary care disposal

In January 2020, the Group completed the disposal of the England and Wales Domiciliary Care business to Cera Care Operations Holdings Limited ('Cera Care') for cash consideration of £4.0m payable on completion, and a further £1.0m of deferred consideration was received over the following twelve months. The transaction was completed on a debt free basis, and with a normal level of working capital. A completion balance sheet mechanism resulted in the Group making a subsequent payment to the buyer of £0.1m in respect of a working capital shortfall.

In September 2020, the Group completed its exit from standalone domiciliary care with the disposal of the Scotland Domiciliary Care business, once again to Cera Care for a cash consideration of £2.0m payable on completion, and a further £0.5m of deferred consideration receivable twelve months from completion and which is due to be settled in September 2021. The contract mechanics for the Scotland sale were identical to the first transaction and a working capital top-up payment was subsequently made of £0.1m.

	Domiciliary Care (England and Wales) £'000	Domiciliary Care (Scotland) £'000	Domiciliary Care (All regions) £'000
Initial consideration	4,000	2,000	6,000
Deferred consideration	1,000	500	1,500
Working capital top-up	(102)	(91)	(193)
Total consideration	4,898	2,409	7,307
Less: Net assets and goodwill	(3,947)	(1,571)	(5,518)
Less: Transaction costs	(519)	(216)	(735)
Profit on disposal	432	622	1,054

(ii) Planning solutions disposal ('terraquest')

In November 2020, the Group announced its intention to sell its entire share capital in its Planning Solutions business ('Terraquest') for a headline enterprise value of £72m. Following a strategic review, the Board considered the business activities of Terraquest to be different from the core activities of the Group, and that the prospects of Terraquest would be optimised under new ownership. The Disposal constituted a Class 1 transaction requiring shareholder approval which was subsequently received on 25 November 2020 with over 99% of votes cast voting in favour of the transaction. For the purposes of accounting for the disposal, this date was taken as the point that the risks and rewards of ownership, together with control, was lost. The transaction was legally completed on 9 December 2020.

The Buyer was a newly formed company controlled by funds advised by Apse Capital ('the Buyer'). The Buyer and the Group entered into the Disposal Agreement on 5 November 2020 to sell the entire issued share capital of Terraquest. The consideration payable to the Company pursuant to the terms of the Disposal Agreement is structured as follows:

- ▶ £56.9 million payable in cash at Completion
- ▶ the issue by the Buyer to the Company of Consideration Loan Notes with an aggregate nominal value of £3.16 million, accruing an interest rate of 10 per cent. per annum payable on redemption
- ▶ the issue by the Buyer to the Company of £0.06m of Ordinary Shares in the Buyer, representing 6.16 per cent of the entire issued share capital
- ▶ a maximum amount of £10 million of deferred consideration payable in cash conditional upon the Terraquest Group achieving an aggregate EBITDA of £9.5 million in the financial year ending on 31 December 2021. A base figure of £5 million is guaranteed.

	Terraquest £'000
Initial consideration	56,869
Deferred consideration	5,395
Equity and loan notes	3,225
Total consideration	65,489
Less: Net assets and goodwill	(8,297)
Less: Transaction costs	(4,394)
Profit on disposal	52,798

The Directors have estimated deferred consideration of £6.0m based upon Terraquest generating an EBITDA of £8.5m during the earn-out period. Given that £5.0m of the deferred consideration has been guaranteed by the buyer, the element which can be considered at risk is only the additional £1.0m above this base figure. Deferred consideration has been fair valued at £5.4m. The deferred consideration is payable in April 2022.

The gain on disposal is not subject to Corporation Tax due to the substantial shareholding exemption.

As part of the Disposal, the Continuing Group has agreed to provide certain transitional services already being provided by it to the Terraquest for a limited period following Completion.

Taxation

Tax strategy

Mears does not engage in artificial tax planning arrangements but takes advantage of available tax reliefs. The tax position in any transaction is aligned with the commercial reality and any tax planning is consistent with the spirit as well as the letter of tax law. Mears has a low appetite for risk and when making decisions regarding tax; reputational and commercial as well as financial risks are considered. Given the Group's activities are largely involved in servicing public sector clients, the risk of reputational damage flowing from a tax compliance failure is higher than in other sectors. This leads the Group to take a risk averse approach if there is an element of uncertainty regarding a particular treatment.

The Group 'normalises' its headline Earnings per Share ('EPS') measure to reflect a full tax charge. In so doing, the Board has removed from its primary performance measure any potentially positive impact that could be achieved through reducing the Group's corporation tax charge.

Taxes paid

Further detail in respect of the taxes paid during 2020 are detailed below:

	For the year ended 31 December 2020		
	Taxes borne £m	Tax collected £m	Total £m
Corporation Tax	–	–	–
VAT & IPT	2.2	62.0	64.2
Construction industry tax	–	12.4	12.4
Income taxes	–	28.6	28.6
National insurance	19.5	18.2	37.7
Total	21.7	121.2	142.9

As detailed above, the Group participated in the Government's Job Retention Scheme ('Furlough'). Total payments made to those on furlough amounted to £19.1m resulting in a tax recovery of £16.1m. This tax rebate is not included within the table above.

Strategic report continued

Financial review continued

In addition, the Group accepted the short-term relief to defer the payment of its March 2020 VAT liability. This sum of £16.0m is included within the figures detailed above and was settled in full since the year end. The Group has also elected to repay its furlough rebate received and relating to the first quarter of 2021 amounting to £2.1m, recognising that much of the uncertainty surrounding Covid-19 has now been resolved, and following the disposal of Terraquest, Mears should no longer utilize further Government support.

Balance sheet

	Note	2020 £'000	2019 £'000
Goodwill, acquisition intangibles and investments		135,044	152,382
Property, plant and equipment		23,600	26,326
Right of use asset	1	200,041	198,384
Inventories	2	31,258	36,045
Trade receivables	2	139,884	164,091
Trade payables	2	(221,373)	(202,366)
Net cash/(debt)		56,867	(51,138)
Lease obligations	1	(209,071)	(205,175)
Net pension	3	(7,880)	2,088
Taxation		3,678	(2,231)
Receivables relating to disposal of Terraquest	4	8,591	–
Net assets held for resale		–	5,293
Other payables		(4,588)	(5,362)
Net assets		156,051	118,337

1 Detailed explanation provided in IFRS16 section below

2 Working capital balances include trade receivables, trade payables and inventories; further explanation is provided within the working capital management section below

3 Net pension is detailed within the pension section below and comprises pension assets of £7.1m (2019: £6.9m), pension guarantee assets of £30.7m (2019: £23.8m) less pension obligations of £45.7m (2019: £28.6m)

4 Receivables relating to the disposal of Terraquest comprises deferred consideration of £5.4m and loan notes of £3.1m as detailed within the Discontinued activities section above

Overall, the Group reported an increase in net assets driven by the profit generated on the disposal on the sale of Terraquest and the Domiciliary Care businesses. The key elements which are addressed in greater detail below is the reduction in working capital balances (together with the positive cash flows flowing from this), the significant impact to the business of the IFRS 16 lease accounting and the balances relating to pensions and how the Group seeks to manage those risks.

Cash flow and working capital management

	2020 £'000	2019 £'000
EBITDA on continuing operations	55,935	77,078
Cash inflow from operating activities of continuing operations before taxes paid	103,223	86,918
Cash conversion %	185%	113%
Average daily net debt	97,300	114,400
Adjusted net cash/ (debt) at 31 December	56,867	50,986

The Group reported a net cash position at the year-end of £56.9m (2019: net debt £51.0m). The key drivers for this improvement was the consideration received in respect of the Terraquest and Domiciliary Care disposals amounting to £63.9m (before transaction costs of £5.1m), and a significant operating cash inflow from operating activities of £102.7m, resulting in a cash conversion of 185% (2019: 113%) when taken as a proportion of EBITDA. Importantly, the strong year end performance is also mirrored in the average daily net debt for the year at £97.3m (2019: £114.4m).

Whilst this reflects excellent working capital management and highlights the Group's ability to adapt quickly to changing payment mechanisms, the impact of Covid-19 resulted in certain cashflows which are non-recurring and will unwind over time, which is detailed below. The components which are considered temporary and are expected to unwind over the course of 2021 are primarily:

- ▶ the £16.0m deferral of the Group's March 2020 VAT liability which is now been settled in full
- ▶ contract payments received on account of £23.0m relating to client receipts in respect of the Covid-19 interim arrangements
- ▶ amounts received in respect of lump sum arrangement where the associated cost had not been incurred. This amounts to £0.7m at the year end, having been around £4.0m as the Group exited the first national lockdown

The average month end trade receivable and trade payable balance split by Housing category reflects strong working capital management during a period where liquidity was paramount. The Group is grateful also for the additional support which the majority of clients showed throughout the course of the pandemic; their commitment to settle payments, often ahead of their due date, provided stability and allowed the Group to similarly support its own supply chain.

	2020			2019		
	Receivables £m	Payables £m	Net working capital £m	Receivables £m	Payables £m	Net working capital £m
			£m			£m
Maintenance-led	138.5	(125.7)	12.8	159.3	(126.2)	33.1
Management-led	32.4	(25.5)	6.9	29.8	(24.3)	5.5
Development	31.0	(6.0)	25.0	33.4	(8.7)	24.7
	201.9	(157.2)	44.7	222.5	(159.2)	63.3

The core activities of Maintenance and Management have historically absorbed a relatively low level of working capital when compared to the size of the business and the profit generated. As detailed above, the Maintenance-led activities delivered a reduction in working capital utilisation, reducing from £33.1m to £12.8m; after adjusting for the benefit from the VAT deferral and the increase in payments received on account, this reduction is broadly in line with the reduction in revenue.

The average working capital absorbed in Management increased from £5.5m to £6.9m which outperformed management expectations. It was previously indicated that the full year impact from the Asylum contract was likely to absorb a further £6.0m of working capital in 2020 given the averaging methodology reflected only a part-year impact in 2019 for this newly mobilised contract. The underlying movement in working capital absorbed in Management-led activities is broadly in line with the increase in revenue.

The working capital absorbed within the Development activity was maintained at a similar level to the prior year at £25.0m (2019: £24.7m). The remaining two active sites were mothballed during the period but have subsequently been reopened, but activity has been maintained at a low level to closely manage the working capital cash flows. Management expect to see the unwind of the working capital absorbed in this area over the course of the next 2-years.

Strategic report continued

Financial review continued

A summary of the consolidated cash flow is detailed below together with explanations in respect of the major movements.

	Note	2020		2019	
		Reported £'000	Before the impact of IFRS 16 £'000	Reported £'000	Before the impact of IFRS 16 £'000
(Loss)/profit before tax		(15,218)	(14,100)	20,253	22,475
Net finance costs		9,998	2,875	8,731	2,971
Amortisation of acquisition intangibles		9,525	9,525	10,122	10,122
Depreciation and amortisation		51,630	9,388	37,972	8,064
EBITDA		55,935	7,688	77,078	43,633
Other adjustments		1,608	1,608	(5)	(5)
Change in inventories		4,787	4,787	(6,357)	(6,357)
Change in operating receivables		17,975	17,975	2,680	2,680
Change in operating payables		22,418	24,075	13,523	12,848
Operating cash flow		103,223	56,633	86,918	52,798
EBITDA to operating cash conversion		185%	737%	113%	121%
Taxes paid		41	41	(3,377)	(3,377)
Cash inflow from discontinued operations	1	2,528	2,528	4,904	4,904
Capital expenditure		(6,765)	(6,765)	(12,318)	(12,318)
Cash flows relating to property acquisition activity	2	4,618	4,618	(7,176)	(7,176)
Acquisitions and Disposals	3	54,612	54,612	(1,300)	(1,300)
Dividends	4	—	—	(13,811)	(13,811)
Financing costs		(10,447)	(3,324)	(9,744)	(3,984)
Discharge of lease liability		(39,958)	(491)	(29,179)	(819)
Change in net debt		107,853	107,853	14,918	14,918
Opening net debt		(50,986)	(50,986)	(65,904)	(65,904)
Closing net debt	5	56,867	56,867	(50,986)	(50,986)

- As detailed above, the Domiciliary Care and Planning Solutions activities have been reported as discontinued in the results for the year
- The Group cancelled its property acquisition facility. The final asset sold in 2019 included an element of deferred consideration of £4.6m which was settled in September 2020.
- As reported earlier, the disposal of Domiciliary Care and Planning Solutions resulted in a combined cash inflow after acquisition costs of £57.8m. Netted off this figure is a balance of £3.5m reflecting the acquisition of a minority interest in equity and loan notes in the buyer of the planning solutions business. Within the consolidated cash flow statement these entries are not netted off and are reported individually.
- Following the uncertainties surrounding Covid-19, the Board did not believe it appropriate to declare a dividend for 2020. The dividend for 2019 comprises the final dividend for 2018 of 8.85p and an interim dividend for 2019 of 3.65p, resulting in a total in-year outflow of £13.8m
- The statutory cash flow statement reports a cash balance at 31 December 2020 of £96.2m (2019: £73.1m). Whilst this disclosure complies with accounting standards, it is not a fair reflection of the Group's funding arrangement. The Group has a revolving credit facility to the value of £125m. The Group makes drawdowns against that facility, meaning the cash balance and loan balance are inextricably linked. The closing net debt at 31 December 2020 of £56.9m (2019: £51.0m) comprises a cash balance of £96.2m (£73.1m) reduced by an associated drawdown of £39.4m (2019: £124.0m).

Accounting for residential leases and IFRS 16

Leasing properties for rental to tenants is a core business activity for Mears. As a result, Mears currently holds around 10,425 residential property leases and this number can be expected to increase over time. The Group's management of the operational and financial risks and rewards of leasing is thus a key element of the value which the Group generates for stakeholders. This section describes in brief the main different classes of residential lease assets held by Mears, their key contractual obligations, the associated risk and reward and the accounting treatment. (Mears also has over 3,500 office property and vehicle leases, but the risk and reward and accounting treatment of these is straightforward and not considered further here).

Accounting for residential leases is a complex area. A number of key judgements must be made, as follows:

- Identifying whether a given contractual arrangement is a lease
- Assessing whether Mears or another party has the right to direct the use of the lease asset to obtain economic benefit
- Determining the term of the lease
- Assessing the value of future lease payments, including variable and fixed elements

Only once this has been done is it possible to conclude whether any given lease should be accounted for under IFRS 16 or not. Broadly speaking, a lease should be accounted for under IFRS 16 only if Mears has the right to direct its use which, through its decision-making rights, can affect the economic benefit derived from that asset. In addition, a practical expedient offered under IFRS 16 allows those leases with a term of less than 12-months to be expensed. Of Mears' portfolio of some 10,425 residential leases, over 60% do not fall under the criteria for recognising on the Balance Sheet, mostly because they are either short term in nature or they have two-way break clauses with short notice periods or because Mears does not in practice have the right to control the use of the asset. IFRS 16 focuses upon a 'right of use asset', and to complete the book-keeping, recognises a corresponding lease obligation. Given the focus of the standard is on the right of use asset, the lease obligation is not entirely consistent with the historical definition of a liability; accordingly, the lease obligation is not a typical debt instrument.

The table below splits the Group's residential property leases across several lease categories. It highlights the operational risks and contractual obligations that need to be managed and the key factors which are considered to assess the correct accounting treatment, in particular whether the arrangements fall under the definition of a lease as laid down by IFRS 16.

Lease category	Number of leases	Lease term	Annual lease payment	IFRS 16 lease obligation	Key considerations for assessing the accounting treatment under IFRS 16, together with risk management considerations
Category A	2,480	3–5 years	£16.3m	£32.4m	This lease type contains a one-way no-fault break in Mears' favour. Whilst the Group could exit all arrangements within 30 days, the Group is deemed to control the asset, and the arrangement meets the definition of a lease under IFRS 16. Notwithstanding the break clause, the Group measures the obligation based on the Group's best estimate of its future intentions, which has been modelled on 3 years. Notwithstanding the reported lease obligation, the unavoidable debt obligation to the Group is one-twelfth of the annual lease payment, being £1.7m.
Category B	380	7–10 years	£3.8m	£23.7m	This lease category meets the definition of a lease under IFRS 16. The Group has no ability to terminate these leases early. Positively, the lease term is aligned to the underlying contract, and Mears would have the right to novate these leases to a new provider if the customer contract was to be terminated early. There remains a relatively low number of this lease type but it is an area where the Group anticipates an increasing number to secure an optimal mix of lease terms to provide best value whilst retaining the flexibility to react to changes in the volume of service users.
Category C	635	3–20 years	£9.3m	£85.0m	This lease category meets the definition of a lease under IFRS 16. The Group has no ability to terminate these leases early but enjoys nomination agreements with Local Authority clients which ensures that a property is either occupied, or that Mears is compensated if the property is empty.
Category D	400	20 years	£3.5m	£42.4m	This lease category meets the definition of a lease under IFRS 16. The Group does not enjoy an ability to terminate these leases early. Positively, these properties have been secured at rental levels below market rent and in areas where demand is expected to remain high. Whilst the Group considers this asset type to be low risk, it does carry a higher bad debt and void risk than the Group's other lease categories.
Category E	660	10 years	£4.2m	£nil as treated as short term	These leases have been procured through Housing Associations and typically enjoy a no-fault two-way break with a 2-month notice period. These leases are not considered to be legally enforceable beyond 2 months and are therefore considered to be short-life leases within the rules of IFRS 16. These leases can be considered low risk from a financial standpoint given the ability to break at short notice. However, this represents an operational risk and Mears endeavours to ensure its portfolio has a mix of tenures and break clauses as the financial costs of running short of suitable properties is equally as severe as carrying surplus bed spaces.
Category F	1,065	7–10 years	£9.3m	£nil as not a lease under IFRS 16	These leases represent a long-term commitment to lease properties. However, the lessor has a right of substitution meaning that the lessor can swap one property for another without Mears approval. As such, under the rules of IFRS 16, Mears does not control an identifiable asset, and there is no right of use asset or lease obligation. Notwithstanding this, the Board believes that stakeholders should be aware of this annual lease payment which represents a long-term financial commitment. Positively, the lease term is aligned to the underlying contract, and Mears holds the right to terminate these leases early if the customer contract was terminated.
Category G	500	20 years	£4.6m	£nil as not a lease under IFRS 16	Under the terms of these leases, Mears has no right to direct the use of the asset. The Group's Local Authority partner has the right to operate the asset in a manner that it determines, and Mears participation is restricted to delivering tenancy management and maintenance services. Mears enjoys a rent guarantee and certain void protections meaning its income is secure and that Mears carries limited risk associated with the lease.

Strategic report continued

Financial review continued

Lease category	Number of leases	Lease term	Annual lease payment	IFRS 16 lease obligation	Key considerations for assessing the accounting treatment under IFRS 16, together with risk management considerations
Category H	4,005	<1year	£47.9m	£nil as treated as short term	These leases are procured for a period of less than 12 months or the underlying asset is continuing to be used after the expiry of the original lease term. Under the rules of IFRS 16, these are termed as short-life leases and there is no recognition of either a right of use asset or lease obligation. Given their short duration, these leases represent minimal financial risk but this can be a negative from an operational standpoint, given we are required under the customer contract to provide accommodation at short notice, in locations where there is a scarcity of suitable properties.
Category I	300	3 years	£3.0m	£nil as no variable lease payment is estimated	This lease type typically contains a one-way no-fault break in Mears' favour. Whilst Mears direct the use of the asset, the lease obligation to the landlord is based on a pass-through arrangement. Mears only make lease payments to the owner to the extent that the property is occupied and to the extent that rents are received from the tenant, in an environment where credit risk is high. As such, Mears recognises no fixed lease payments associated with these leases and as a result, no right of use asset or lease obligation is recognised. Importantly, these leases carry no financial risk.
Total	10,425		£101.9m	£183.5m	

Where a contract is identified as a lease under the rules of IFRS 16, the Group recognises its right to use a leased asset and a lease liability representing its obligation to make lease payments. The depreciation cost of the newly recognised 'right of use' lease asset is charged to profit within cost of sales or administrative costs, whilst the interest cost of the newly recognised lease liability is charged to finance costs.

On the basis that depreciation is required to be charged on a straight-line basis, whilst the interest element is charged on a reducing balance basis, this results in a higher charge being applied to the income statement in the early years of a lease, with this impact reversing over the later years.

Pensions

The Group participates in two principal Group pension schemes (2019: two) together with a further 20 (2018: 28) individual defined benefit schemes where the Group has received Admitted Body status in a Local Government Pension Scheme (LGPS). The accounting treatment for these schemes follows the guidelines set for defined benefit schemes. This treatment does not present the commercial reality for a number of these LGPS arrangements, where the Group holds back-to-back indemnities from its clients in respect of both its exposure to changes in pension contribution rates and to future deficit risk.

The pension disclosure is split on the face of the Balance Sheet between non-current assets and non-current liabilities. In addition, the pension guarantee assets are reported separately from their associated liabilities which complies with accounting standards but is not reflective of the contractual nature. The table below provides an alternative categorisation to assist stakeholders in better understanding the Group's pension risks. Where the Group enjoys a back to back indemnity with its Local Authority and Housing Association clients, it is classed within 'limited-risk'. For other LGPS arrangements, whilst the Group does not benefit from an indemnity, the risks associated with these schemes matches the time horizon of the underlying contract which, whilst not removing all risks, does reduce the period over which a deficit can arise. This second category has been identified in the table below as 'medium-term risk'. The Group schemes are standard defined benefit arrangements where the Group will continue to continue to hold a long-term obligation regardless of whether the underlying works contract to which the members were working is still being performed by the Group. The Group actively participates in running these schemes and meets with the Trustees regularly. This last category has been classified as 'long-term risk'.

	Non-contract specific (no indemnity) long-term risk	Contract specific (no indemnity) medium-term risk	Contract specific (indemnified) limited risk	Total
Number of schemes	2	12	8	22
Scheme assets £'000	185,436	63,317	225,174	473,927
Scheme liabilities £'000	(181,184)	(74,279)	(245,907)	(501,370)
Funded status £'000	4,252	(10,962)	(20,733)	(27,443)
Surpluses not recognised £'000	–	(870)	(10,272)	(11,142)
Guarantee asset £'000	–	–	30,705	30,705
Net surplus/(deficit) £'000	4,252	(11,832)	(300)	(7,880)

Banking and financial covenants

The Company is party to a £120m Revolving Credit Facility ('RCF') and is grateful for the tremendous support that has been provided to the Group by its three banking partners, Barclay, HSBC and Bank of Ireland. At the time that the UK entered the first national lockdown, the Group held total commitments of £170m and given the level of uncertainty at that time, quickly secured additional short-term funding, increasing the Group's debt facilities to £192.7m. The Group has delivered strong cash performance and positively the additional funding line has not been drawn down. Following the disposal of Terraquest, the Group cancelled this short-term facility together with voluntarily reducing total commitments from £170.0m to £145.0m prior to the year end. Since the year end, the Board have further reduced the total commitment by a further £25.0m, reducing the RCF facility to £120.0m.

In order to mitigate the Covid-related risks on the Group's banking covenants, and in support of the Terraquest disposal, the Group agreed amendments to its banking covenants. The new financial covenants removed the existing leverage and interest cover covenants tested at December 2020 and June 2021 and introduced two new covenants requiring a minimum level of Covenant EBITDA and a maximum level of adjusted net debt at those two testing dates only. In setting these amended covenants, the Company was required to prepare projections on the basis of what was considered by the Board to be a reasonable worst scenario. The covenants applicable from December 2020 up to the expiry of the existing debt facility in November 2022 are detailed below:

	Previous	December 2020	June 2021	December 2021	June 2022
Leverage	3.00x	n/a	n/a	3.50x	3.00x
Interest cover	3.50x	n/a	n/a	3.50x	3.50x
Minimum adjusted EBITDA	n/a	(£9.0m)	£3.8m	n/a	n/a
Maximum net borrowings	n/a	£63.0m	£95.0m	n/a	n/a

The covenant calculations are tested every six months using figures derived on a rolling 12-month basis. EBITDA and Net Borrowings are calculated on a pre-IFRS 16 basis. The key items included within the covenant calculation are detailed below as:

	2020 £'000	2019 £'000
(Loss)/profit before tax on continuing operations	(15,220)	20,253
Add back: depreciation (non-IFRS 16)	5,677	5,955
Add back: profit impact of IFRS 16	1,118	2,223
Add back: amortisation	11,736	12,231
Add back: finance costs (non-IFRS 16)	2,875	2,971
Add back: share based payments	993	400
Add back: non-underlying item	2,279	2,018
Covenant EBITDA	9,458	46,052
Net finance costs	9,998	8,731
Deduct: net interest received on pension obligations	102	432
Deduct: credit on unwind of discount	36	–
Deduct: finance costs (IFRS 16)	(7,123)	(5,760)
Covenant net finance costs	3,013	3,403
Adjusted net debt (or £nil if cash)	–	50,986
Leverage covenant (Adjusted net debt/Covenant EBITDA)	n/a	1.1
Interest cover covenant (Covenant net finance costs/Covenant EBITDA)	3.1	12.8

Andrew Smith
Chief Financial Officer

Strategic report continued

Case study

Providing Homes and Supporting Communities: Rotherham Council contract retention

Rotherham Metropolitan Borough Council ('Rotherham Council') reappointed Mears as the main contractor to provide £150m repairs and maintenance during a ten-year contract period from April 2020.

The team provides repairs, make empty properties ready to be re-let, provide caretaking services and make adaptations to approximately 22,000 homes.

Our journey

Mears Group has been running the contracts since late 2012 and delivered excellent customer service until it came to an end in March 2020. Mears Group successfully tendered for the new contract of 5 years + 5 years extension and this was mobilised during a national lockdown in April 2020.

This contract in Rotherham is a true testament to our excellent relationship with Rotherham Council, where both partners have worked hard to deliver great outcomes.

We currently have 116 colleagues working on the contract with our longest serving colleague clocking up over 47 years continuous service. A large proportion of our operational staff started their careers on this contract as apprentices, providing a wealth of skills and local knowledge.

Investing in our community

Over the life of our contract, we have provided a total of 49 apprenticeship opportunities. This commitment will continue with a total of 100 apprenticeship opportunities to be made available to local residents over the next 10 years.

We have strong links with local stakeholders through our social value offering with key projects with Age UK Rotherham and the local secondary schools.

Our Christmas delivery to Age UK service users and our first virtual employment event for local students and jobseekers in partnership with Rotherham Council and Job Centre Plus harnessed the spirit of the partnership in the midst of the pandemic.

Mears have a strong presence within the town of that is marked by our presence on a number of strategic groups such as the Rotherham Together Partnership, Rotherham Pioneers and the Business Growth Board's Employment & Skills Group.

These groups are a collaboration between local government, key stakeholders and local businesses who work together in the best interests of the town and community.



£150m

over 10 years

22,000

tonnes

Strategic report continued

Case study

Meeting the Extra Care needs in Cornwall



Mears provides specialist housing with care solutions. Under Mears' Extra Care and Support Living programmes, we manage the build, management, maintenance and provision of care to specially-adapted homes for elderly and disabled people to help them live independently for longer.

This is exemplified by our recent contract award to be the Strategic Partner to Cornwall Council for the provision of additional specialist housing, called Extra Care, to meet much needed demand across the County.

The aim of the scheme is to allow older people and those with disabilities to live independently in their own homes and have access to range of support, such as care and community events.

Under a 30-year arrangement and 14-year care contract, Mears will source third-party funding and contractors and organise the build of housing for elderly people and those with special needs with access to care services. The partnership will provide 750 self contained dwellings in an extra care environment over seven years and will be a mixture of affordable rented and shared ownership options. The Mears' Registered Provider will take on the management of the schemes once built.

Priority will be given to residents who already live near the schemes, the first sites have been proposed for construction in Hayle, St Austell, Newquay and Falmouth.

The deal worth £300m will create around 700 jobs for people across Cornwall that pays the Living Wages Foundation rate to those delivering care and support. The partnership will also incorporate a £90m spent on local supply chain and will support small and medium enterprises.

The Elderly Accommodation Counsel (EAC) estimates that there are approximately 520,000 units of retirement housing (including some degree of support or care) in England. EAC estimates a substantial shortfall in housing and care provision by 2035 of nearly 400,000 units of purpose-built housing for older people in England.

In Cornwall 25% of the population is over 65 and it is expected to rise to 29% over the next two years.

The most significant rise will be in the 75 to 84 age group and many will need care and support to live. To try to ease the pressure Cornwall council identified the need to team up with a strategic partner to provide hundreds of new extra care houses across the county.

Mears has commissioned independent research which showed that extra care living can prevent people from having to go to hospital due to on-site care and due to the benefits of living in specially adapted accommodation which is designed for their specific needs.

We look forward to working with Cornwall Council to create well designed homes with a focus on health and wellbeing for our over 55's communities.

Contract value up to

£300m

750

extra care dwellings

Strategic report continued

Listening to our stakeholders

Stakeholder engagement is central to our strategy. We are focused on delivering positive outcomes for all our stakeholders

Drivers

How we engage

Stakeholder expectations



Clients

Our clients are from Central and local Government and housing associations. Our model has always been based on establishing long-term partnerships that address the significant housing challenges and solutions to help our clients. Transparency and responsibility are at the heart of our approach and we focus on solutions that establish sustainable solutions, rather than quick fixes.

Our clients expect a trusted partner that can contribute to wider sector and strategic thinking as well as deliver innovative operational solutions that improve service and lower long-term cost. Partners now look beyond the contract and rightly demand good governance, a responsible financial position and high levels of social responsibility to be at the heart of what we do.



Tenants and customers

Our "Your Voice" programme is now engaging tenants via our independent and resident-led scrutiny board, our customer forums and our online customer network.

We have strengthened our tenant engagement to ensure that we go above and beyond requirements suggested in the Government White Paper. At a local level we have a system to engage customers as soon as they interact with Mears, should they wish to do so. This enables us to create a network of our customers via feedback and online forums which can feed into our scrutiny board to create a genuinely resident designed service.

How we engage our Board

The Your Voice independent scrutiny board reports directly into our PLC Board to ensure that its findings are reported at the highest level of our organisation.

Our tenants and service users expect to be part of developing solutions rather than to be simply a recipient. Expectations from tenants is rightly rising and they should be seen not merely as service users but as consumers who have the right to levels of service. The greater requirements for complaint handling and reporting emerging from the Government White Paper is something we have already gone above and beyond. Mears welcomes any further regulation from Government in this area.



Communities

All of our branches develop their own local specific social value plans which demonstrates where we will add value to the community, often over and above any contract commitments. Our normal social value activity has been refocussed in 2020 to help support communities through the impact of Covid and lockdown. Examples include supporting local food banks and helping to build Covid testing centres. The detail of our work is shown in the Social value section of this report

How we engage our Board

An Executive board member sits on our independent Social and Diversity Impact Board which is led by independent experts and helps us to drive our social value resources to achieve meaningful community outcomes. The independent board reports directly into the PLC Board.

Stakeholders expect, given their long-term commitment, that we contribute positively to the communities in which they live. They want us to help local people into work, to upskill people and to work with them to address local issues where we can. This will all become more important as companies like Mears remain as large-scale local employers despite the economic effect of 2020.

Relevance to business model and strategy
Key issues
Action we are taking

We operate as a trusted long-term partner to the public sector. As partners we have to demonstrate that our values complement their own. We are not like many other outsource organisations, in that both the focused nature of our services and the cultural fit with our clients continues to position us to win major new contracts, such as with the Home Office, and to retain long-standing contracts in the way that we do. We also try to lead the sector in good practice, as demonstrated by our thorough independent scrutiny arrangements which take the best of public sector scrutiny.

Clients want us to demonstrate a strong set of financial, cultural and community-led values. Outsourcers need to go back to the beginning and focus on bringing private sector innovation in areas such as technology and access to institutional finance whilst maintaining the spirit of public service delivery and transparency whilst putting customers at the heart of what they do.

- ▶ We worked closely with clients through the pandemic to deliver a sector leading approach to customer safety through our Partners in Safety approach, mixed with new technology to improve the customer journey.

As an organisation with a clear objective to be the leader in terms of customer service, wherever we operate, this cannot be done without good engagement. Our outstanding customer service performance is a testament to our success.

Increased regulation is coming in 2021 and we have spent the last year preparing to go above and beyond. Our customer forum has hosted the Housing Ombudsman to test whether the Mears approach is working and to ensure that we are leading the sector rather than responding to future legislation.

- ▶ Created the Your Voice scrutiny approach with customers involved at every level
- ▶ Provided a direct line from the Your Voice board to the PLC Board – our resident board members can speak to our non-executive and executive board members directly.
- ▶ Engaged with the Housing Ombudsman to ensure our processes are already in place before legislation is passed
- ▶ Innovated with our repairs platform MCM Live which gives tenants more information about when their repair is due and enables them to change the time/date without having to call us

Being a socially responsible organisation with a firm commitment to supporting communities is essential to being a valued partner to our clients. Establishing strong community links also helps us attract the right people into our workforce and to establish links with other community-based organisations, which can contribute to our service offer.

Severe economic downturn in the communities we serve. Opportunities to address our sector skills gap as a large employer. Government have indicated in the CSR that the public sector will be a key driver in addressing the net zero carbon challenge and have allocated funding for retrofitting.

- ▶ Providing free learning provision to our colleagues, clients and communities we work in.
- ▶ Ensuring we have the right local skills in place through our apprenticeship programmes.
- ▶ Focusing our social value capabilities towards supporting communities through the pandemic. In 2021 we will closely align all social value activity to support community recovery.
- ▶ Continuing to bid for contracts with a high premium placed on the social value we deliver, rather than paying lip service.
- ▶ Lobbying Government for a more transparent measure of social value for all bidders in a contract.

Strategic report continued

Listening to our stakeholders continued

Drivers	How we engage	Stakeholder expectations
 <p>Colleagues</p>	<p>We are proud to be on the list of the Sunday Times 25 Best Big Companies to Work For, and on the Social Mobility Index of the top 75 employers in the UK for our commitment to social mobility. We have a national Workforce Group that is responsible for setting the approach to staff engagement and each local branch has a People plan, which sets out what it will do in each year. We have an Employee Director who sits on the Mears Group Board, which also helps ensure that the views of the workforce are listened to and actioned.</p> <p>Our SWYS survey is now aligned with the Sunday Times Best Companies portal providing independent and anonymous feedback.</p> <p>We have improved our internal communications offer with a direct link from the Executive Board to every single employee for feedback.</p>	<p>All workplaces have been through a concerning time and we as an employer strive to do everything we can to show support. Our regular surveying shows that our colleagues want transparent and regular communication from the business about how we stand financially and an honesty in our approach to any business changes.</p> <p>Our staff want to work for an organisation that values them and the communities in which they live. They want an organisation that treats people fairly and gives them the opportunity for personal development.</p>
 <p>Suppliers</p>	<p>We work in partnership with clients and we reflect this way of working with our suppliers. We focus on keeping our promises to them, be that how we pay them or the commitments we make in terms of helping them grow their business. This has been especially important in 2020. We challenge them to operate to the same social value approaches that we do and have a clear supplier charter that sets out our expectations from them. We recognise that all suppliers cannot be at the same level as ourselves but will support them where we can to improve. As you would expect, we set appropriate controls to ensure work quality and compliance standards are delivered to our expectations. We also have an established approach to setting up new supplier arrangements, to ensure that both parties are clear on responsibilities and risks.</p>	<p>The most important thing for our suppliers is that we keep the promises that we make to them. This means that we set out clearly what is expected in conjunction with our supply partners and that we keep our part of the arrangement in a fair and transparent way</p>
 <p>Investors and Bankers</p>	<p>The Company is committed to maintaining good communications with investors and other providers of capital. There is an active programme of communication with existing and potential shareholders. We have appointed a Head of Investor Relations to support senior management and Board interactions with the market. There is a full programme of senior management meetings with institutional investors following the publication of final and interim results. The Company has also looked to hold additional shareholder days during the year to provide greater detail on current operations, market developments and future strategy. The Group regularly receives and responds to questions raised by small private shareholders through the investor enquiry portal on the Group's website. The Chairman, CEO and CFO regularly make themselves available to meet with existing and potential new investors to understand their views on the business, its strategy, governance and performance. The Group holds regular meetings with its funding partners.</p>	<p>Our shareholders and bankers expect the Group to communicate clearly, concisely and consistently with all market participants and keep the market updated on all material operational, financial and strategic developments at the Company. In addition, our investors and bankers expect to see a full range of financial and non-financial disclosures and KPIs upon which to assess the financial and operational performance of the business.</p>

Relevance to business model and strategy
Key issues
Action we are taking

Our workforce engagement is built around the Mears 'Red Thread' model, which works to establish the type and culture of workforce that we know will lead to both customer and financial success.

Security in the workplace during a time of financial fluctuation. A focus on mental health, wellbeing, and encouraging hard to reach groups into our workforce. Creating a more diverse workforce.

A renewed need for better communication and performance management.

- ▶ We have worked with independent experts, through our Social and Diversity Impact Board and colleague engagement to look at where our sector needs to improve in recruiting, promoting and retaining colleagues from backgrounds who suffer from discrimination. This has formed our new proactive policies to which we will be held account.
- ▶ We have placed a primary focus on performance management to ensure that our workforce is appraised and able to develop in the best way for each individual.
- ▶ Our mental health steering group has worked throughout the pandemic to review our mental health and wellbeing strategy with a focus on trained colleagues available in all of our branches and wider company support for rewards and support.
- ▶ Our internal communication focuses on honesty and transparency. Our Executive Board hold monthly briefing sessions for 300 managers who are expected to cascade those messages down to every single colleague.

All information is shared, no matter how difficult.

Our supply chain is fundamental to the success of our business, both in the provision of materials and in the delivery of services under our leadership.

Meeting payment promises, partnership working, good communication and governance.

- ▶ We apply partnership working principles to our suppliers and have robust processes to ensure that we select the right suppliers for our business and that they are managed in a fair and appropriate manner. We have reviewed our approach with large and smaller suppliers, in line with Government thinking on payment arrangements.

Our business model is refined through continuous feedback from our shareholders. We have been in regular consultation with our leading shareholders in recent years as we have re-focussed the Group on its core Housing services, with the aim to be the leading provider of housing services and solutions to the resilient and growing affordable housing market in the UK.

The particular operational and financial stresses placed on the business by the Coronavirus pandemic, required more regular and more detailed communication with all shareholders.

Our shareholders have helped shape our views on capital allocation and appropriate levels of debt.

It is with reference to shareholder views that the Board seeks to strike the appropriate balance between pursuing growth and maintaining our core operational focus, discipline and financial returns.

- ▶ Our new Head of Investor Relations will help senior management enhance the Group's communications with our shareholders.
- ▶ We will continue into 2021 our programme of regular trading and operational updates to keep shareholders informed of the impact of Covid-19 on the business and its financial performance.
- ▶ Our sale of Terraquest has enabled us to reduce company debt significantly and reduce the Company's financial risk profile.
- ▶ Our sale of domiciliary care and Terraquest Solutions has enabled us to return to our core business function – to provide housing solutions to Central and Local Government.
- ▶ The Board will seek to return to the dividend list once it is prudent to do so.

Strategic report continued

S172 statement

Statement by the directors in performance of their statutory duties in accordance with s172(1) Companies Act 2006

The Board of directors of Mears Group PLC consider, both individually and together, that they have acted in the way they consider, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole in the decisions taken during the year ended 31 December 2020.



Further information on the board is available here:

Examples of some of the key decisions taken by the Board in 2020 is detailed in the Corporate Governance report on page 76 showing how the Directors considered the impact of these decisions across a range of stakeholders.

The Board recognises a wide range of stakeholder interests and seeks to create a culture whereby decisions are made with consideration to the wider impact upon the organisation as well as financial performance and strategic objectives. The Company's Directors recognise their legal duties under section 172(1) of the Companies Act 2006, to act in the way that is most likely to promote the success of the Company for the benefit of its members as a whole whilst also having regard for the interests of employees, the success of their relationships with suppliers and customers, the impact of our operations on the community and the environment, whilst maintaining a reputation for high standards of business conduct.

This has never been more important than during the Covid-19 pandemic where the Mears' business has acted with a great sense of responsibility and professionalism. The Group's primary focus has been and remains the safety and well-being of customers and staff. Our people performed valiantly in the most challenging of circumstances. Service quality levels to our local and central government clients, and to our many vulnerable service users, remained at high levels throughout the period.

Our employees are fundamental to meeting our strategic priorities. We recognise that we are in an increasingly competitive environment as regards attracting skilled staff and we have taken a consistent approach across the Group to ensure that we are an attractive organisation to join and to develop a successful career with.

We aim to be a responsible employer in our approach to the pay and benefits that our employees receive and have implemented strong governance to ensure a fair approach is taken across the Group. Whilst during the pandemic it was necessary to place some staff into the Government's job retention scheme ('furlough'), top-up payments were made to support the lowest paid and a staff hardship fund was created to provide additional relief.

The Group's success depends upon the commitment and engagement of its workforce. Given the challenges encountered in 2020, significant extra effort was applied to workforce management, including amongst those staff that have been furloughed. Mears was already in the Sunday Times list of top 25 Big Companies to work for, but in a staff survey carried out in June 2020, our scores reached a new high, reflecting the efforts made on communication and keeping staff safe.

In addition, we saw positive progress on our key workforce measurements in respect of staff retention and diversity.

The Company is one of a small number of companies in the UK to appoint an Employee Director, clearly underlining the Company's commitment to progressive business practice and corporate governance. We recognise the importance of diversity and inclusion and benchmark ourselves against others. We have placed emphasis on programmes to attract women into the Trades and into management positions.

During the year, the Board completed its withdrawal from delivering stand-alone Domiciliary Care. The Care market has been difficult in recent years with low levels of profitability and return on capital employed, and a challenging backdrop of poor staff retention and the reputational and operational risks associated with this sector. Over several challenging years, the Board of Directors are extremely proud of the achievements made in terms of driving improvements in service delivery and workforce pay and conditions, but it has not proved possible to generate an adequate financial return. The Group completed its exit from standalone Domiciliary Care with the disposal of its England and Wales Domiciliary Care business in January 2020 followed by the disposal of the Scotland business in September 2020. Recognising the sensitivity of completing the sale of the Care business during a pandemic, the Board delayed the completion of the second transaction until the end of the third quarter, whilst providing transitional support to the buyer for an extended period to ensure no negative impact upon service users as a result of this transaction.

The Board regularly reviews the Group's dividend policy to provide a fair return to shareholders whilst looking to maintain a prudent capital structure and retaining the ability to invest in growth. Given the uncertainty surrounding the Covid-19 pandemic, the Board reacted decisively, making no dividend payments during 2020 which included the final dividend for 2019. The Board is grateful for the support which shareholders provided the Board throughout this challenging period. The Board is also mindful that the Group took advantage of reliefs made available by Central Government, notably placing staff on furlough

where appropriate and enjoying the benefit of the deferral of its VAT liability for the March 2020 quarter. The Board remains mindful that it would be inappropriate to pay dividends during a period where it has taken such reliefs. It remains the Board's intention to return to a progressive dividend policy once it is confident that activity and working practices have returned to normal and that it would be prudent financially to do so.

The Board is mindful of the views of our shareholders, debt funders and our wider stakeholders and has a desire to see average net debt reduce. The Group has reported a significant reduction in its indebtedness during the year, recognising that a debt reduction is to the benefit of all stakeholders.

The health, safety and well-being of our employees is our primary consideration in the way we do business. Health, safety and environmental risks are fully embedded in the governance structures of the Group. The emphasis that the Board places on this area is evidenced by the Compliance Committee, which plays an active role in monitoring Group activities, and reports into both Audit Committee and the Board. The Covid-19 pandemic brought new and unique challenges however the Group adapted quickly to the new methods of working to ensure the well-being of our employees and service users. Whilst access to PPE was difficult at times, the established procurement routes, together with the support of many clients, ensured staff were protected.

As the Board of Directors, our intention is to behave responsibly and ensure that management operate the business in a responsible manner, operating within the high standards of business conduct and good governance. This expectation is cascaded throughout the business. Employee reward and recognition is directed towards delivering high service levels, in a safe and responsible environment.

We have been recognised as an organisation which is delivering strongly on the social responsibility agenda. The Group take a strategic approach to corporate social responsibility and embed it into every area of our business. This is evidenced by our newly appointed Social and Diversity Impact Board.

Our Social and Diversity Impact statement within the Strategic Report demonstrates our clear ambition towards improving people's lives and building strong, sustainable communities.

We aim to act responsibly in how we engage with our suppliers. We expect our suppliers to acknowledge the significance of social, environmental and ethical matters in their conduct and demonstrate compliance with legislation. We have a commitment with our customers to increase the number of local SME subcontractors working within our supply chain, ensuring that a significant proportion of the contract spend remains within the local economy. The Board of Directors acknowledges the importance of good payment practices and is committed to ensuring that suppliers are paid to on a timely basis to agreed terms.

Our Non-financial statement on pages 54 and 55 of the Strategic Report details how the Board decisions impact upon on our employees and the communities we serve.

As the Board of Directors, we endeavour to behave responsibly toward our shareholders and treat them fairly and equally, so that they will benefit from the Group meeting its strategic objectives. The Directors regularly make themselves available for dialogue with shareholders.

Strategic report continued

Market drivers

Housing Market

The Affordable housing will be an attractive place to play for the longer term, given the UK housing shortage, long social housing waiting lists, cycles of outsourcing, policy changes encouraging more social house building and broader resilience of demand.

Market Position



A leading provider of affordable housing solutions in the UK



A large provider of repairs to the affordable housing sector



Provider of affordable rental management solutions



A private registered provider of housing sites within Group



Leading partner to both Central and Local Government



Political and economic landscape

- ▶ Stable majority Government but heavily focussed on Covid 19 through 2020. It is hoped this will start to change in 2021 fuelled by the Social Housing White Paper published in November 2020.
- ▶ Budgetary pressures but significant protection from ring-fenced Housing Revenue Account (HRA).
- ▶ The Homelessness reduction Act has expanded the duties of local authorities from applicants with "priority" status to all households.
- ▶ UK commitment to carbon reduction.
- ▶ Potential for devolution.



Rising levels of homelessness

- ▶ UK faces a housing shortage, and the supply of social housing has not kept up with overall housing growth, with long waiting lists (1.3m households waiting for social housing).
- ▶ Number of people in temporary accommodation grew by over 40% between 2014 and 2019.

Opportunities and Risks

- ▶ Many decisions postponed in 2020, so there is a backlog both on tenders and work within maintenance.
- ▶ Infrastructure and especially housing based investment is likely to remain a priority for Government although investment timings may be impacted.
- ▶ Significant opportunity to meet the increasing homelessness challenge that is likely to increase further given Covid 19.
- ▶ Investment to achieve carbon reduction targets is likely and emphasised in the Social Housing White paper but timings unclear.
- ▶ We believe there is little direct impact from Brexit to Mears although some material supplies may be impacted in the short term.

Ensure that we continue to have strong, local tailored approaches across England, Northern Ireland, Scotland and Wales.

Opportunities and Risks

- ▶ Given the rising numbers of homelessness, this will create opportunities for quality housing, that provides more secure tenancies at affordable rent levels.
- ▶ There is always the risk that Government policy around housing benefit and LHA levels will change.

The availability of housing stock will also be driven by economic factors.

Mears' Response

- ▶ Excellent response to Covid 19 challenges has positioned us well for the future with clients.
- ▶ Reductions in debt levels to ensure a resilient balance sheet.
- ▶ Improving our expertise as a carbon reduction partner to clients.
- ▶ We have planned ahead on material supply considering the Brexit risk posed to each key item.
- ▶ Ensure that we have a localised response in Scotland meeting the specific requirements of Scottish Government.

Mears' Response

- ▶ We are established as the leading private housing provider of temporary housing solutions,
- ▶ We have our own not-for-profit RSL in England and are seeking registration in Scotland.
- ▶ We are creating new sustainable models to better manage balance sheet risk.



Demographic change

- We continue to see an ageing population that will drive the need both for more affordable housing and more end of life housing.

Opportunities and Risks

- There is opportunity to help provide against in particular the shortage of end of life housing in the UK.
- We need to ensure that our employee proposition is strong enough to attract young people into the Group.

Mears' Response

- Mears has become the strategic partner to Cornwall Council with the aim of creating a material change in the number of end of life housing units in the County. This will lead to a 30 year relationship with the County.
- Mears will continue to support the expansion of end of life and supported living accommodation across the UK.
- Mears has become a great employer with a strong sense of social responsibility.



Pace of technological development

- We are excited by the opportunity that technological change brings to enhance both our service and our employee experience.

Opportunities and Risks

- Covid has created a likely permanent change in the mix between office and home working.
- Consumer expectations have risen given the advantages created by everything from smart phone technology to home delivery services.
- The Cyber threat is likely to continue to grow.

Mears' Response

- Mears has already adjusted to enable its workforce to work from home wherever possible. We see opportunity in reducing our office estate over time.
- Mears has fully enabled mobile working technology across its business units.
- We continue to invest in advancing security of our systems, indeed our contracts in particular with Central Government already set very high standards.
- We will monitor closely developments in smart home technology and seek opportunity to improve our service accordingly.



Rising customer expectations

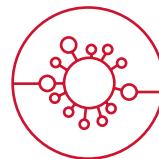
- People expect faster and more responsive approaches, driven by changes in other markets.
- Post-Grenfell focus on social value and high compliance across the market.
- Government focus on 'levelling up' and a commitment to renewal of democracy so people's voices can be heard.

Opportunities and Risks

- We need to be able to provide "live" information and responses to our consumer base.
- We see opportunity as the demands on building safety increase, as highlighted in the 2020 White Paper on Social Housing but we equally need to be more vigilant ourselves.
- We must ensure the customer voice is heard within the organisation and acted on.

Mears' Response

- Our Housing systems have been improved to provide real time information on repair status.
- We are increasing our expertise across all areas of building safety including fire compliance.
- We have established an independent Customer Scrutiny Board, that reports directly to the Mears Group Board.



COVID-19

- Covid 19 brings both short term and long term change, which we are well prepared for.

Opportunities and Risks

- While vaccination programmes will take away a lot of the risk here, we need to recognise the lasting impact on customer and employee expectations.
- Covid has also created a back log of work that will continue into 2021/2.
- Given the specific challenges to the Asylum contract, a review of the whole asylum system seems likely.

Mears' Response

- Mears will ensure that many of the positive new approaches developed through Covid are maintained e.g. levels of communication, infection control procedures.
- We will work with clients to catch up on properties that have suffered from reduced repair activity in 2020.
- Our focus on Asylum will be to provide continued good service and to work with the Home Office to ensure there is sufficient supply of initial and dispersed accommodation.
- Our workforce model has adapted quickly and effectively to the changing environment.

Strategic report continued

Business model

Long-term outcomes and positive social, economic and environmental impact

Key resources and relationships

Outstanding partnerships:

Firmly rooted in Local Government and Housing Associations, we are now seen as an important partner for Central Government. Our end service users are the recipients of housing services and extra care living.

A Responsible approach:

Creating social value is a key part of our business strategy, as this enables us to be seen as a trusted partner by our clients and is an essential part of building stronger relationships. Our response during Covid was helped by the engrained culture of service to clients and communities.

Exceptional people:

Proud to be in the Sunday Times Top 25 Big Companies to work for. We recognise our staff as our greatest asset. Mears employees are skilled in delivering an excellent service whilst showing a strong customer service ethos and an empathy for our service users.

Market-leading technology:

Our performance is built on a bedrock of first class IT platforms giving market-leading capability and driving innovation and resident engagement.

Supply chain partners:

We choose suppliers who share our values and meet our standards. We work closely with suppliers to develop innovative services and integrate them with our core systems.

Financial strategy:

We are funded from a combination of shareholder funds, retained profits and moderate levels of bank debt. Our underlying business has good forward visibility, stable margins, strong cash conversion and limited capital requirements. Accordingly, free cash flow can predominantly be used to pay down balance sheet debt and provide returns to capital providers.

Innovation:

The challenge of delivering service improvements at lower cost requires innovative thinking and the use of technology. We create and lead best practice in our markets.

Our role and services

Housing management

- ▶ Procure, manage and maintain portfolios of affordable housing stock

Housing maintenance

- ▶ Regenerate, refurbish and re-purpose stock Intelligent maintenance
- ▶ Intelligent maintenance

Supporting people in these homes

- ▶ Tenancy management
- ▶ Tenant welfare and support

Outcomes

Community outcomes



Create better places to live



Reduced homelessness



Reduce pressures on the NHS and the public purse



Improve life chances for people

Financial outcomes

How we generate revenue

Mears' revenue is generated from payments from Government, Local Authority and Housing Association clients in respect of its Housing services. Whilst the end service users are at the centre of our business model, they do not pay for the service directly. These payments are made under long term contracts (avg. 7 years).

The value we share



Shareholders

Given the public health emergency, and given the over-riding importance of cash management, the Board considered it would be imprudent to declare a dividend during 2020. This will be the first time, in the 25 years since the Group's flotation, that the dividend has not been increased. Given the reduced financial leverage within the business and its strong underlying cash generation characteristics, the Board intend to return to the dividend list as soon as prudent to do so.



Government

As detailed in the Financial Review, in 2020 we paid an aggregate sum in direct and indirect taxes of £142.9m. In addition, through the services we provide to the public sector, we are delivering significant cost savings and better value to Central Government, Local Authorities and the NHS.



Customers

We maintain over 600,000 homes in the UK, undertaking around 6,000 repairs per day. Mears has extended its activities to provide solutions to resolve the challenges of homelessness, asylum housing and MOD accommodation.



Communities

At the heart of Mears lies a strong sense of responsibility towards improving people's lives. We create opportunities and enable people to develop new skills within some of the most disadvantaged and marginalised communities in the UK. Every branch of Mears makes a social value pledge, which focuses on specific activities to improve its local community in at least one of our social value priorities.



Employees

Mears is committed to training. We employ over 180 apprentices and provide a number of alternative training solutions for upskilling employees and for the professional development of Mears managers. We are proud to be rated as one of the best 25 large companies in the UK to work for by the Sunday Times.

Stable margins and good cash conversion

We have a long standing record of stable profit margins on contracts (once mobilised) and converting profit into cash, utilising strong financial management combined with good relationships with clients and the supply chain.

Strategic report continued

Our strategy

Strategic priorities



Deepening client relationships

What we achieved

- ▶ We had a number of contracts ending in 2020. We achieved an excellent contract retention rate as well as securing a number of new customer contracts.

2021 priorities

- ▶ Maintain our progress on retaining or extending all sustainable contacts
- ▶ Retain our existing key worker contact and secure a new contract with this same client
- ▶ Develop our service offering to meet the Carbon Reduction agenda

How we measure success

- ▶ Extending services with existing clients. Retaining contracts at sustainable pricing.
- ▶ Winning work with new clients who share our values.
- ▶ Being seen as a trusted, responsible and ethical provider to Central Government

Risks

- ▶ Competitor difficulties have led to reduced confidence in outsourcing



Focus on our core Housing services activities

What we achieved

- ▶ Completed the disposal of our Domiciliary Care businesses in England and Wales in January and our Scottish equivalent business in September 2020
- ▶ Despite the market dislocation from Covid-19 secured an excellent exit valuation for our Terraquest business, with c.£53m of initial cash proceeds received in December 2020

2021 priorities

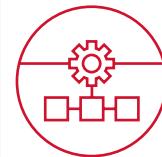
- ▶ After a period of significant strategic change and operational complexity (Covid-19), management will be solely focused on driving forward our core Housing services businesses
- ▶ Continue with the orderly sell-down of houses from our development portfolio

How we measure success

- ▶ Continued working capital releases from the sell-down of the development portfolio
- ▶ Improved win rate/retention rates and margin enhancement in our core Housing services business

Risks

- ▶ Deterioration in the market for new homes
- ▶ Contract losses in our core Housing services
- ▶ Covid-19 and associated lockdown restrictions continue to impact on the operational and financial performance of the Housing business



Increasing quality leadership

What we achieved

- ▶ Through the Covid period, we maintained our already excellent service scores.
- ▶ We have established our new independent Customer Scrutiny Board, who have written their first review in this document

2021 priorities

- ▶ Establish our new independent Customer Scrutiny Board at the heart of the business.

How we measure success

- ▶ Service user and client feedback.

Risks

- ▶ Rising customer expectation requiring ever more individual responses



Growing and improving our business

What we achieved

- ▶ Business wins/rebids
- ▶ Selective exits from unprofitable contracts
- ▶ Managing significant growth in numbers in Asylum
- ▶ We have significantly reduced our debt, given the sales of Terraquest and Domiciliary Care

2021 priorities

- ▶ Significant rebids in maintenance
- ▶ Returning maintenance contract arrangements to business as usual
- ▶ Extending work for MOD
- ▶ Effectively returning Asylum contracts to more normal operations
- ▶ Maintain a tight control of debt, focussing on contracts with low working capital requirements and strong operating cashflows
- ▶ Existing remaining Housing Development work

How we measure success

- ▶ Growth in revenue and profit from 2020 levels
- ▶ Continued free cash flow generation and debt reduction
- ▶ Further decreasing level of net debt

Risks

- ▶ Covid delays to returning to business as usual
- ▶ Rebids failure
- ▶ The failure to develop Affordable Rent solutions without the financial constraints placed on the Group by IFRS 16



Developing our people

What we achieved

- ▶ We have retained our position in the Sunday Times Top 25 best big companies list.
- ▶ Staff satisfaction and has reached a record high
- ▶ Staff turnover has reached a record low
- ▶ We have provided a wide range of tools to assist with mental health and well being

2021 priorities

- ▶ Maintain our Sunday Times Best Companies position
- ▶ Continue to increase the diversity of our workforce at all levels
- ▶ Maintain focus on employee engagement and helping tackle the challenges of Well being and mental health

How we measure success

- ▶ Staff retention level.
- ▶ Benchmarking other organisations.
- ▶ Margin improvements and cost reduction resulting from better recruitment and retention

Risks

- ▶ The importance of diversity and inclusion has never been clearer.



Continue to innovate and transform our business responsibly

What we achieved

- ▶ We have retained our high position within FTSE4Good
- ▶ We swiftly enabled around a third of our workforce to move from office to home working

2021 priorities

- ▶ Help raise the understanding and importance of ethical outsourcing
- ▶ Develop new partnership models that enable more temporary housing units to be sourced

How we measure success

- ▶ Winning new business based on our values
- ▶ A happier, healthier and more engaged workforce based on Best Companies survey results and mental health and wellbeing working group policies

Risks

- ▶ Rising expectations across different stakeholder groups

Strategic report continued

KPIs**Non-financial****Customer satisfaction**

In order for customers to recommend us, we must deliver excellent service. The Group completed over 2 million repairs in 2020 and we subsequently post inspect around 10% of works orders and encourage tenants to provide feed back so we can deliver further service improvements.

Results from the year**91%**

We are delighted that our service delivery has remained at a high level. Strong performance will ensure competitiveness as we continue to be ranked above our peers. Whilst the target is against customer satisfaction, we aspire to achieve an excellent service rating. The performance for prior years was measured based on PDA surveys. The Group has changed to a new survey methodology during 2020 where the Group has increased response rates using text and e-mail for securing feedback. This was expected to reduce the measure but importantly provides a more accurate measure. For 2020, the Group achieved customer satisfaction of 91% and importantly 86% of customers rated the service as excellent. Our target for 2021 recognises that the impact of the third national lockdown, and a subsequent order backlog, will impact on service ratings.

How we performed

2020 target

90%

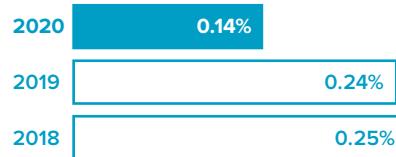
2021 target

>85%

Outperformance

Customer complaints

Incidents resulting from poor service result in a complaint. We are committed to dealing with all complaints on an individual basis.

Results from the year**0.14%**

We are committed to providing our colleagues with the skills and equipment to deliver great service. We seek to identify trends in order to improve our overall service quality. A complaint measure of 0.14% represents excellent performance and well ahead of target. We have seen complaint levels rise during the second half of the year, reflecting the impact of Covid-19 and an increase in the number of overdue works orders. The Group is working hard to resolve any backlogs although the third national lockdown has delayed progress. Inevitably this order backlog has meant that complaint levels did increase during the last quarter of 2020.

How we performed

2020 target

<0.24%

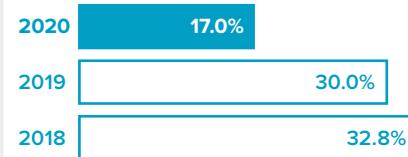
2021 target

<0.22%

Outperformance

Employee turnover

Our employees are fundamental to meeting our strategic priorities. We recognise the importance in attracting and retaining skilled staff and we have taken a consistent approach across the Group to ensure that we are an attractive organisation with which to develop a successful career with. The staff churn figure is calculated as the total number of leavers during the year as a proportion of the average headcount.

Results from the year**17%**

The Group monitors a suite of Workforce related measures, including those focused on gender equality and social value. The Group was nominated by the Sunday Times 'Best Big Companies' and we achieved our best result in the mid-year pulse survey. We significantly outperformed the employee turnover target, but the Group would recognise that unique events in respect of Covid-19 will have reduced staff turnover and the strong performance in 2020 should not be taken in isolation. We are placing increasing focus on performance management and succession planning.

How we performed

2020 target

28%

2021 target

26%

Outperformance

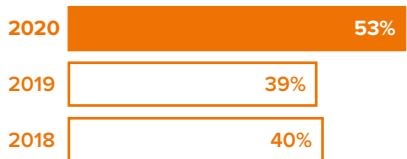
Business development

New contract success

Contract success is measured by the total revenues secured as a proportion of the total value of tenders submitted. We typically tender around £1bn of new opportunities each year. The average contract length is around six years. In order to achieve our organic growth forecasts, it is important that we secure around one in three, by value.

Results from the year

53%



The Group's new bid conversion rate was above target; however, the impact of the pandemic meant that many of the new contract opportunities were delayed, although positively this meant that several of the Group's existing contracts enjoyed short extensions with the new contract award deferred to 2021. The Group tendered new contracts to the value of £280m which is significantly lower than a typical year but the conversion rate was very pleasing.

How we performed

2020 target



2021 target

33%

Order book

Our order book provides us good visibility of those revenues secured for future periods. It is helpful that we have long-term contracts that allow us to plan with confidence, in the knowledge that we have significant revenues already contracted. It is also positive for all our stakeholders, providing stability to our supply chain, funders and, most importantly, for recruiting and motivating our workforce.

Results from the year

£2.6bn



The Group originally entered 2020 with the target to maintain the order book at a similar level to 2019, being £2.5bn. However, the emergence of the COVID-19 and the realisation that new contract bidding was likely to be lower, meant the Group reduced this target to £2.1bn. A number of existing contract extensions meant that this target was exceeded.

The order book does not stand still – there is a continuous inflow of new orders adding to the secured value, and a daily outflow as services are delivered to our customers which reduces the order book. The Group is forecasting revenues of in excess of £800m in 2021, and new orders must be secured of a similar value for the value to be maintained. The Group has an active pipeline of new bidding opportunities however it is likely that a number of these will fall into 2022. The Group has set a target for 2021 which reflects this.

How we performed

2020 target



2021 target

£2.1bn **£2.4bn**

Outperformance

Strategic report continued

KPIs continued

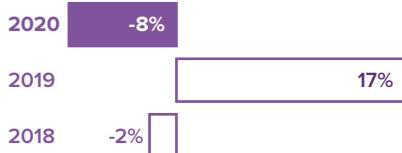
Financial performance

Revenue growth (continuing activities)

Revenue represents the amounts due for services provided during the year. Our KPI target relates to total revenue, although it is important to also identify the split between organic growth and growth that has been delivered through acquisitions. We believe that organic growth gives a better indication of business performance, as it is a purer aggregation of market growth, success in new contract bidding and contract retention.

Results from the year

-8%



As detailed within the Business Review, the Group's revenues for 2020 were severely impacted by the pandemic and the actions that the Board took to de-risk the contract portfolio. The maintenance-led revenues reported a reduction by 18% however this was mitigated in part by a 40% increase in management-led revenues. Whilst the Group secured 53% of contracts bid (by value), a number of these are renewals and will not result in growth. The Group is targeting 2% growth in 2021.

How we performed

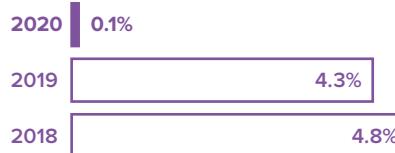
2020 target	2021 target
—	2%

Adjusted operating margin (continuing activities)

Operating margin is the KPI used to measure and understand the profitability of our activities. The Operating profit measure is taken before exceptional costs and the amortisation of acquisition intangibles. The measure is stated on a pre IFRS 16 basis, being the measure that is utilised within the business and understood by our investors and bankers.

Results from the year

0.1%



As detailed with the Business Review, the operating result was impacted by Covid-19 and the Group delivered an adjusted operating loss for the year. The Group expects trading in 2021 to return to normality during the second quarter and is setting a margin target which reflects this.

How we performed

2020 target	2021 target
—	3.7%

Average net debt (excluding lease obligations)

Good working capital management remains a cornerstone of the business. The Group's IT systems are designed to deal with the challenges of high volume and low value activities. The Board has a stated strategy to reduce debt to around 1x EBITDA on a pre-IFRS 16 basis.

Results from the year

£97m



With the on-set of Covid-19, the Group increased its original target for 2020 from £110m to £140m. The Group significantly outperformed both these targets. The Group reported a significant operating cash inflow reflecting excellent working capital management and also certain Covid-related cashflows which are non-recurring and will unwind over the course of 2021. The target for 2021 is £60m reflecting the consideration received following the disposal of Terraquest, the proceeds of which we used to pay down indebtedness.

How we performed

2020 target	2021 target
—	£60m

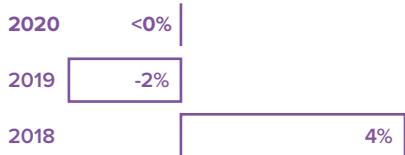
Health and safety

Growth in normalised diluted EPS

Normalised earnings are stated before exceptional costs and exclude the amortisation of acquisition intangibles together with an adjustment to reflect a full tax charge.

Results from the year

<0%



Given the adjusted loss on continuing activities reported in 2020, and the unique circumstances of a global pandemic, the Group will not focus on an EPS growth target, but rather an absolute measure. The consensus forecast of market analysts for normalised diluted EPS is between 16.0p and 18.0p per share which is in line with the Board's own expectations.

Accident frequency rate

The health, safety and well-being of our employees is our primary consideration in the way we do business. Health, safety and environmental risks are fully embedded in the governance structures of the Group. Providing our employees with a safe working environment remains paramount. Our accident frequency rate (AFR) is calculated as the number of reportable incidents (by both employees, service users and third parties) divided by the number of hours worked, multiplied by 100,000.

Results from the year

0.15



We are proud of our record in this area and we continue to invest in our health and safety training. We place emphasis upon all accidents and near misses, however trivial, being reported. The performance in 2020 has been affected as a result the pandemic with reduced work activities and a reduced number of reportable incidents. We will continue to strive to deliver further improvements to this critical area.

How we performed

2020 target



2021 target

18.0p

How we performed

2020 target

<0.25

2021 target

<0.24

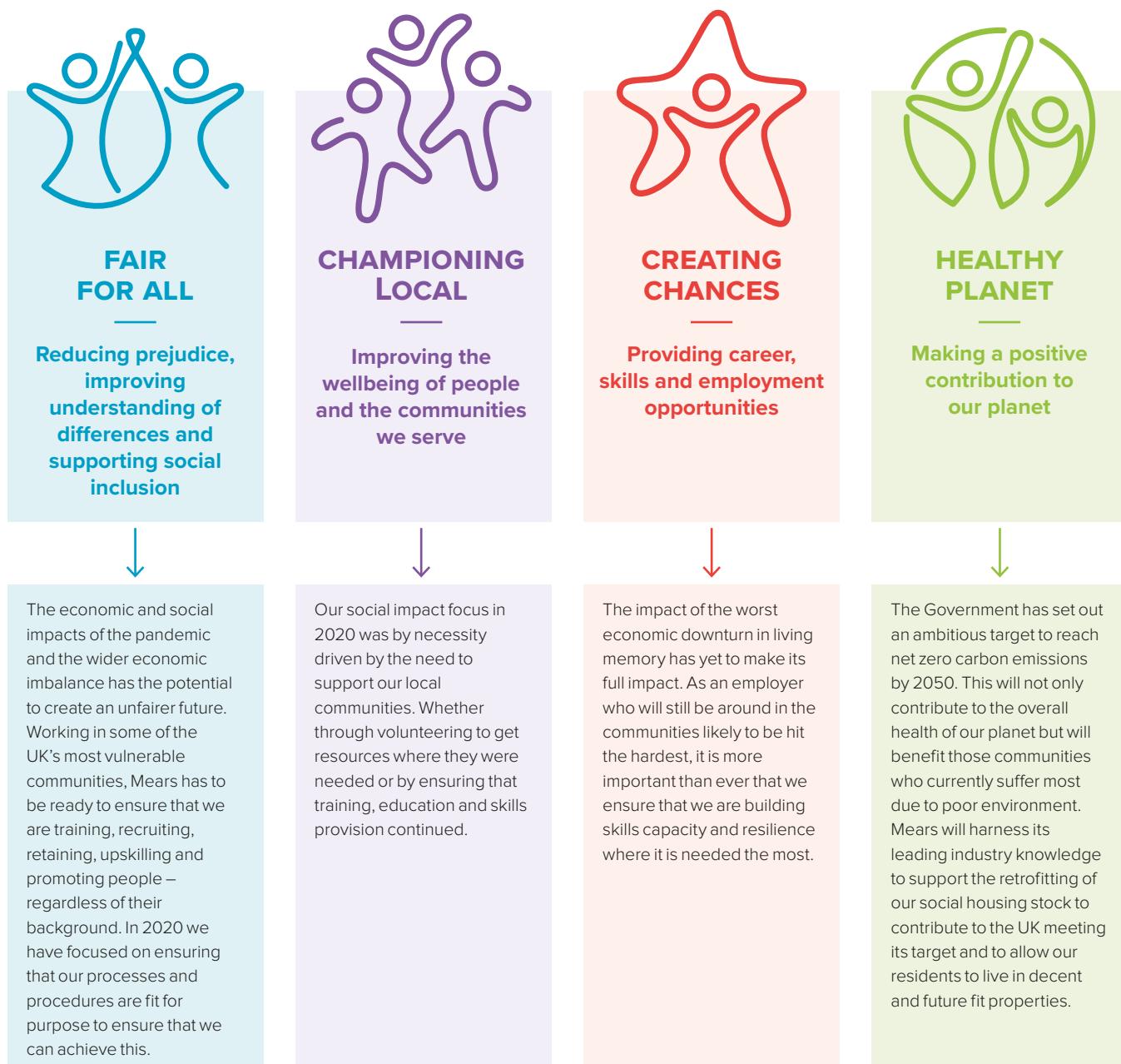


Outperformance

Strategic report continued

Our approach to Environment, Social and Governance (ESG)

Mears are not new to ESG. In fact, it has always been at the heart of what we do. We structure our ESG approach through our four priorities – Fair for All, Championing Local, Creating Chances and Healthy Planet. Each of these is driven by an understanding that a company of our size can make an impact on the communities we work in and on the wider world. We set our standards extremely high and have a robust set of governance structures in place with independent scrutiny to ensure that we don't just pay lip service to our beliefs. Mears believes that despite the challenges presented by 2020, there is an opportunity for companies to play a major role in levelling up our economy, creating a more resilient national skills base, and being the vanguards to achieve net zero by 2050. If this wasn't enough, we firmly believe that getting ESG right will secure competitive advantage for those companies. By building on our reputation as a socially responsible business, enabling our customers and communities to positively benefit from the positive social, diverse and environmental impact we create.





Wellbeing at Mears

The pandemic has been hard on all of us. But it has also provided a timely reminder to companies of their obligations to their employees and ensuring that they play a role in everyone's well-being and prioritising the mental and physical health of our colleagues. Looking after ourselves and each other has never been more important.

Work is a big part of anyone's life and we truly believe it is one place where people can turn to when they need help. At Mears we are constantly evaluating our contribution in the following areas:

Having a good work/life balance

Ensuring that we are providing the opportunities for the Group's employees to work as flexibly as possible and to fully support colleagues to maintain the best possible balance.

Helping people at home as well as at work

Many of our colleagues are working from home more often – we need to ensure that this doesn't alienate people and they have the right structures and support.

Having a positive, safe working culture for all

A safe and positive culture should be the basis of everything we do. A company where we can come to work without fear of illness or injury and one which has a caring culture which values all colleagues.

Opportunities for career development

Through appraisals, feedback and training opportunities Mears should be letting our workforce know how we value their contribution and provide positive feedback and encouragement for their future within the company and beyond.

Going above and beyond for our workforce during the pandemic

We have always tried to do things differently at Mears. We want to be a workplace that brings people on and stands by them when things are tough. At the start of the pandemic we immediately agreed to pay sick pay from day 1, which went against Government guidelines that stated that it should be paid from day 4. That was just the beginning.

We took an early decision to create the Mears hardship fund which has a ring-fenced budget for colleagues to apply to. For those who were furloughed we removed the Government cap of £2,500 (which would have affected anyone earning over £30k p.a.) and supported our lowest paid by paying 100% to those earning under £20k p.a.

We created a central Covid management group to receive and process new guidance from the Government and to ensure that the guidance was quickly turned into new policy for Mears and communicated and understood, amongst our workforce.

During the pandemic we reviewed and amended our mental health and wellbeing policy to ensure that it stood up to the greatest crisis of our working lifetimes. Our Mental Health Steering Group ran awareness campaigns and from our Executive Board down our daily slogan to every single one of our colleagues was "Let's keep talking."

Mears have a huge package of commitments, including training over 1,000 members of staff on how to support people's mental health and wellbeing.

We created a new awards process – #mearsamazingpeople – which relies on our colleagues nominating one another for going above and beyond the call of duty. By the end of 2020 we had received over 1,000 nominations.

We want everyone who works for us to be the best they can be, to develop, train and learn and to feel supported when times are tough.

Strategic report continued

Our approach to Environment, Social and Governance (ESG) continued

Oversight: how we ensure we continue to do the right things

Social and diversity impact board

To drive social and diversity impact throughout the business, we continue to operate our externally appointed Social and Diversity Impact Board. This ensures that we take a strategic approach to corporate social responsibility and embed it into every area of our business. The Board is endorsed by three external experts whose role is to challenge us to drive forward our social and diversity agenda and to hold us to account. The Board's work with external partners has been crucial in developing our approach to diversity and inclusion policy in 2020 and a full review of how we recruit, retain and develop people from backgrounds who suffer from discrimination.

Mears foundation

In 2020 we launched a full review of the Mears Foundation – the charitable trust which independently underpins our social impact work. The pandemic will have a lasting impact on our communities, and we wanted to ensure that the Trust had the necessary organisation and resources to achieve meaningful impact. We appointed Christine Losecaat MBE as our Independent Chair and have also appointed the Foundation's first ever General Manager.

The Foundation aims to help improve the lives of young people, vulnerable groups, the elderly and those with significant health issues, through practical help, support and intervention. The Foundation provides support through volunteering and hands on help for nominated causes, not just financial support. We look forward to focusing the Foundation's work in 2021 to stand by our communities who will bear the impact of the pandemic in both economic, health and social terms.

Mears Your Voice Scrutiny Board

Launched in 2020, Your Voice is part of our new Customer involvement Strategy and aims to drive action and advance service standards for Mears customers (whoever they are, wherever they live and whatever their circumstances), through customer-led scrutiny, challenge and support of Mears' performance in these areas.

Your Voice sets the highest standards of customer involvement and engagement across the Group, leading the way nationally and delivering real benefits to all our customer groups – clients, colleagues, customers and local communities.

The learnings from the Scrutiny Panel and associated groups also promotes best practice and shared learning across the Group through insights, challenges and innovation.

Your Voice is made up of three component parts:

1. Mears Customer Scrutiny Board

Independently chaired by former CIH Chief Executive Terrie Alafat and made up of a panel of tenants and residents working alongside the PLC Board and providing oversight, challenge and support to Mears. It is supported and its independence assured by the Centre for Public Scrutiny.

2. Mears Customer Champions Forum

Made up of our own Branch based customer engagement leads plus other key stakeholders such as client scrutiny board chairs, resident association leads, community activists. This forum creates a link between the Scrutiny Board and our local involvement groups and scrutiny structures.

3. Mears Online Customer Network

A virtual network of residents from around the country, who opt into providing feedback on our services – provide insight into what's important and what's not – offer opinion and suggestions – validate and endorse our thinking/new initiatives.

The forum is Chaired by TPAS

the tenant engagement experts, and alongside residents we have heard directly from the Housing Ombudsman on the new code of conduct and MHCLG on the Housing White Paper. By drawing experts together with residents we hope that we can use this resource to improve national standards and legislation.

£2,540

of social value, delivered per employee



Delivering solutions to the carbon challenge in Aberdeenshire

As a provider of housing management and maintenance services, Mears is a source of positive influence in our sector with landlords, tenants and supply chain partners. The UK has set ambitious targets around carbon reduction and housing is at the forefront of this. Social Housing stock specifically has to achieve a stepped change in its energy efficiency by 2030.

The implications for local authorities and housing associations, sees a requirement to retrofit existing social housing stock to ensure it meets new carbon reduction standards.

Most local authorities and housing associations see this as an important long-term challenge and are in the early stages of this journey.

Mears is already helping design and implement a number of carbon reduction schemes and will expand its capability and resource to help clients achieve this important ambition.

In Aberdeenshire we are delivering for the Housing Improvement Programme (HIP) which is part of the Council's 30-year business plan for improving council houses and flats. Mears is fast approaching the close of Year 2 activities. Year 3 activity sees a strategic shift in focus and a doubling of the

in-year revenues to circa £14m with over 75% of the work now focussed on energy saving measures. This theme will continue into Year 4 and beyond into the follow-on HIP 2 project.

The change in strategy is to deliver on Scotland's ambitious EESSH standards and will see us install Photovoltaic systems (PV systems) on around 900 roofs, along with External Wall Insulation, energy efficient electric heating systems and high specification window and door replacements.

From Year 4 the Council intends to move away from Gas Heating installations and renewals in favour of more sustainable alternatives.

Mears will integrate our expertise with our ongoing maintenance activities across all contracts to ensure changes are made efficiently and will provide advice and guidance to tenants to help ensure the most benefits can be gained. In 2021 our focus will be on developing our offer to help accessing funding, to design and implementation.

We stand ready to support our local partners to deliver on their ambitious plans and bring them to fruition.

Strategic report continued

Our approach to Environment, Social and Governance (ESG) continued

Applying ESG through our business model



Standing with our communities

Clients

Throughout the lockdown we worked alongside our clients to identify where we could pool our resources to direct our efforts to supporting the most vulnerable.

Tenants and customers

We will harness the support of the Mears Foundation to direct resources where communities need it the most.

Our social impact will continue to be directed at developing local skills and encouraging harder to reach groups to enter a trade such as our Women in Maintenance Programme.

Communities

We have supported local charities through our branch targets for social impact.

Colleagues

The creation of a hardship fund for all of our colleagues recognised that we are part of a wider community.

We actively support the employment of veterans, young and old.

Investors

We know that our investors support our long-held maintenance contracts and the positive cycle of providing social impact in these communities which leads to longer term partnerships with our clients.



Diversity and Social Impact

Clients

Our clients are diverse and expect their partners to also draw on the benefits of diversity. We are accredited by Housing Diversity Network, who also accredit many of our clients. Going forward we intend to set a higher benchmark for our activities.

Tenants and customers

Our new Strategic Approach to Social and Diversity Impact will ensure that our local teams reflect the communities they serve and encourage people from those communities to join us and learn a trade for life.

Communities

Our Social value approach directly supports inclusion. We work with many charities and through our own Foundation to help build the resilience of local communities.

Colleagues

We will create a diverse, engaged and highly skilled workforce at every level that fully represents the communities we work with.

This commitment is reflected in Mears' Strategic Approach to Social and Diversity Impact (2020-2022) an overarching document that brings together all relevant plans and procedures.

Investors

The future will see challenges to secure the workforce needed to meet our growth ambition. By recruiting and retaining staff from all backgrounds, we will be better placed than most to support our growth.



Leading Governance and Scrutiny

Clients

We have maintained and grown external recognition and accreditation for our approach to social and diversity impact.

Tenants and customers

The creation of our Your Voice Scrutiny Board, independently chaired and resident led.

Communities

To drive social and diversity impact throughout the business, we continue to operate our externally appointed Social and Diversity Impact Board.

Colleagues

Our new approach to performance management is designed to bring out the best in all of our employees and to ensure that we are harnessing their skills.

Investors

Our Your Voice Scrutiny Board will publish an independent and public annual report which will assess current performance and detail future recommendations for improvement.



Leading on Net Zero

Clients

We are already working with a number of clients to support their longer term ambition around carbon reduction. These pilot projects will bring the experience needed to make a material difference as funding streams develop.

Tenants and customers

We have appointed a Head of Carbon Reduction to support our customers in meeting net zero targets through retrofitting – this is a key component in the Government's plans to reach environmental targets.

Communities

We actively seek to incorporate environmental standards into all contracts we agree with landlords in our delivery of PRS schemes for key workers, military personnel, homeless people and asylum seekers.

Colleagues

We will develop our own carbon neutral plans in 2021. We already recycle well over 90% of our waste.

Investors

We have maintained our place on the FTSE 4 Good – showing our commitment to be a genuinely ethical investment. We will continue to use this benchmark to see our progress.



Engaging our staff

Clients

We see a direct correlation between employee satisfaction and customer satisfaction. That's why we are proud to be one of the top 25 big companies to work for according to the Sunday Times list.

Tenants and customers

The commitment of our staff was seen at its best during lockdown, as our staff went the extra mile to support tenants and service users. This was seen in the very high level of compliments received.

Communities

Our policy has always been to recruit, wherever possible, directly from the communities where we work. This we believe brings both local knowledge and commitment.

Colleagues

The Mears Workforce Group, which reports to the Main Board, leads on our workforce engagement programme. Our communication, recognition, performance management and inclusion approaches are now amongst the best, as demonstrated by the Sunday Times survey.

Investors

We have appointed an employee Director for the second time – one of the few listed companies in the UK to do so and further demonstrating our commitment to ESG to our shareholders.

Strategic report continued

Our approach to Environment, Social and Governance (ESG) continued

ESG Performance Targets

Main policies and standards

Community and social matters

We have a clear Social Value plan with four Strategic priorities: 1. Fair for all: Reducing prejudice, improving understanding of differences, supporting social inclusion 2. Championing local: Improving the wellbeing of people and the communities we serve 3. Creating chances: Providing career, skills and employment opportunities 4. Healthy planet: Making a positive contribution to our planet.

Target

For each employee on average to deliver £2500 per FTE of social value per annum

What we have achieved

Our branches provided an exceptional response to the covid outbreak right from the start.

In 2020 Mears delivered over £12m in social value, exceeding our target of £2500 per FTE, despite the difficulties Covid created in carrying out many of our traditional support activities.

 [Read more about our Social and Diversity Impact Board on page 50](#)

Health & Safety

Mears aims to be the industry leader for creating a safe working environment for everyone. We operate a full health and safety training programme. We fully monitor accident frequency rates and we have a proud record on safety within our workplaces and across all of our contracts. Our strategy includes:

Target

An accident frequency rate (AFR) of below 0.25.

AFR is calculated as the number of reportable incidents (by both employees, service users and third parties) divided by the number of hours worked, multiplied by 100,000.

Mears achieved its 18th consecutive RoSPA 'Gold' Award. Such awards are only issued to those organisations which have "achieved a very high level of performance, demonstrating well developed occupational health and safety management systems and culture, outstanding control of risk and very low levels of error, harm or loss".

Mears was again presented with RoSPA's 'Order of Distinction', reserved for those organisations who have "achieved a minimum of 15 consecutive 'Gold' Awards".

Mears successfully retained its certification to ISO 9001 (Organisational Quality Management System) and ISO 45001 (Management System of Occupational Health & Safety).

Mears delivered in excess of 17,000 hours of SHE training to ensure we continued our commitment of improving the skills and awareness of all employees.

We had an accident frequency rate of 0.15, significantly out performing our target.

Environment and Waste Recycling

Mears will work with its clients to help address the challenges of climate change. We will also ensure our own operations see ongoing improvements.

Our targets

To ensure that we divert over 90% of our waste from landfill

To become Carbon Neutral as an organisation

Mears successfully retained ISO 14001 (Environmental Management System).

Mears exceeded its target for annual diversion of waste from landfill of over 95%.

Mears has invested in its internal capability to reduce our own carbon footprint and to support our clients ambitions to address carbon reduction within their housing stock.

Customer Satisfaction

Our ambition for customers to see our service is excellent rather than satisfactory.

Target

75% of customers rating our service as Excellent (scoring Mears as 9 or 10 out of 10 on a 10 point scale)

In 2020, over 80% of customers rated our service as "Excellent".

Our new Independent Customer Scrutiny Board is chaired independently by Terrie Alafat and is made up of residents and tenants from across our services. The Board will publish its first open and independent report in 2021.

Main policies and standards**Human rights, anti-corruption and anti-bribery**

We set the highest standards here.

Our policies include:

- ▶ Prevention of modern slavery and human trafficking
- ▶ Preventing engagement of child labour
- ▶ Whistleblowing policy
- ▶ Family Friendly policy

What we have achieved

We have fully upheld our standards in 2020.

Mears is proud of its Social Mobility Index status, again scoring in the Top 75 nationally, creating opportunities and enabling people to develop new skills in some of the most disadvantaged and marginalised communities in the UK.

Measures taken by Mears to improve social mobility included:

- ▶ 67 Management Qualifications
- ▶ Over 250 employees completing apprenticeships
- ▶ 142 NVQ level 2 and 3 qualifications
- ▶ Selecting an employee director to sit on our board

Workforce

We want to be a great place to work and to place our colleagues at the very heart of what we do. Our policies include:

- ▶ Whistleblowing
- ▶ Family Friendly
- ▶ Safeguarding
- ▶ Equality, Diversity and Inclusion
- ▶ Approach to Labour Standards compliance

We have been accredited once more as one of the top 25 Best Big Companies to work for in the UK. This is underpinned by a clear improvement in colleague engagement.

Our Best Companies Index Score is a recognised standard for employee engagement. It is calculated by combining the responses to eight workplace factors. For employee engagement Mears has improved our score and now has a 'very good level of workplace engagement'

We are accredited as an Investor in People and have been awarded Diversity Network Accreditation. In addition, this year we were listed in the Top 75 Social Mobility Index and Social Mobility Best Practice organisation. Our employees are at the heart of our business and we provide extensive employee benefits; a commitment to a transparent pay policy and a commitment to training and development.

Red thread Wearing the Mears badge carries a lot of responsibility. All Mears colleagues are bound by a common set of behaviours. We call this the Red Thread. It's in our DNA and it helps us achieve more as individuals, as a team, and as a Company.

Motivation: There are no limits; we can all reach our personal goals and aspirations. Individually and collectively we can deliver the services our customers expect a little bit better every day.

Empowerment: Great leaders aren't born, they grow. We urge you to take the initiative, take ownership and take responsibility, and support you every step of the way.

Customer focus: It's very simple; we're here to serve. The success of Mears is built on 360-degree service and appreciating that the needs of clients and customers are complex and multi-dimensional.

Role models: Everyone who represents the Company is expected to lead by example, whether you're looking after vulnerable people or making sure the homes of elderly tenants are properly maintained.

High standards: We set industry-wide standards and encourage everyone to work hard, present themselves well and keep raising the bar. If we do, success is guaranteed.

Target

To remain in the Best Companies list of the best 25 large companies to work for in the UK

 Read more about how we apply ESG through our business model on pages 48 to 51.

Strategic report continued

Our approach to Environment, Social and Governance (ESG) continued

Our ESG initiatives in action

FTSE 4 Good Accreditation

Mears successfully retained its FTSE 4 Good accreditation for 2020, thus securing a place once again in the top 40% of companies for displaying strong corporate social responsibility.

FTSE 4 Good is an initiative ran by FTSE to provide an independent measure the Environmental, Social and Governance practices of companies on its Global index. It is the leading ESG accreditation across all market sectors. It was set up to cater for a growing number of investors who want access to a list of companies recognised for being involved in socially responsible investment.

Organisations hoping to be included on the list must supply robust evidence for how they fulfil the index's key indices which focus on three areas: the environment, human rights and stakeholder relations.

Our performance was strong in all areas, when compared to the organisations in our sub-sector of support services and industry averages, which now places the Group within the top 45% of businesses. We aim to improve our position here over the next decade and to feature in the top 10% of organisations.

Executive Director Alan Long said:

"As we see a shift to companies highlighting their work on ESG, it is pleasing to evidence that Mears has been working in this space for a long time. Year on year we have improved our scores across many of the criteria areas, which is great news. Mears scored particularly highly on Labour standards and Human Rights and Community which make us very proud and demonstrates the hard work which goes in to ESG."

Creating a level playing field for social impact

In 2020 Mears commissioned the think tank Localis to review the Social Value Act and to recommend ways in which we can level the playing field when commissioning social value. Mears are convinced that this is a golden opportunity to get things right now so that our most vulnerable communities can harness the support of the private sector in a genuinely meaningful way and achieve the Government's ambition to level up our economy.

The public sector procurement community is bracing itself for an onslaught of tender responses to normal services as well as a glut of

Covid-19 recovery contracts. Commissioners will be keen to ensure that their own actions deliver not just economic efficiency and long-honoured 'value for money' but also promote community resilience and social wellbeing that has the potential to deliver and embed real social value in the recovery process. This report offers a clear route map for realising the promise of social value.

The report finds:

- ▶ The lives of residents must measurably improve as a result of how councils commission and provide local public services.
- ▶ It calls for a standardised approach to evaluating social value which would give communities a greater say in the benefits received in the commissioning of local public services from commercial suppliers.
- ▶ The report calls for the public sector to adopt a Community Value Charter as a standard framework for setting place-sensitive local outcomes that build on inherent strengths such as social and natural capital
- ▶ We call for a greater sense of human values, trust and relationship in how we generate value for our communities from the commissioning process.
- ▶ Providers must be accountable to residents, tenants and local people for both the services they deliver, and the benefits agreed to when business contracts are signed.
- ▶ These must be explained in a clear way – not through complex targets and opaque mechanisms. We must see strong actual proof in how effectively local services are provided as something which is reflected in the improved lived experience of people in our communities.

We will continue to press Government and the sector to accept a more consistent procurement system and work to get everyone working to the same ends.

Solutions for the Planet

Mears have once again supported the Big Ideas Programme in Scotland, the North East and Yorkshire in a project providing business mentors to schools.

The Big Ideas Programme is an annual event run by Solutions for the Planet to provide mentors to school children with a focus on STEM subjects and has an emphasis on sustainability and entrepreneurship. It is delivered in partnership with local companies, who support teams of pupils (in KS3) to generate solutions or 'Big Ideas' to sustainability issues. These Big Ideas are submitted to the competition with the finals at the Houses of Parliament.

We sat in on the national finals of the Big Ideas Programme and were incredibly impressed with the creativity and innovation demonstrated by some brilliant young people to solve incredibly important sustainability issues.

The National Final welcomed 12 teams from schools across the UK who had to provide innovative ideas to solve their chosen sustainability issue.

The winning team was the Bannockburn High School, Stirling with the concept of 'Food for All'. Their idea is to tackle food waste and poverty with a café that re-distributes food to people in need, and a campaign to educate people about healthy eating.

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As we see a shift to companies highlighting their work on ESG, it is pleasing to evidence that Mears has been working in this space for a long time. Year on year we have improved our scores across many of the criteria areas, which is great news."

Alan Long
Executive Director

Other entries included; the Priory School in Portsmouth with their concept of a mobile refilling station for health, hygiene and beauty product and the Colton Hills Community School with their ideas for reducing plastic pollution in the oceans.

We look forward to welcoming 20 mentors for 2021 programme.

Social Mobility Index

Mears has once again been ranked as one of the top employers in the Social Mobility Employer Index, the leading authority on employer best practice, demonstrating our commitment to social mobility in the wake of the Covid-19 pandemic.

Employers have a huge part to play in the levelling up agenda, and the Index demonstrates what is possible if organisations commit to supporting young people from all backgrounds.

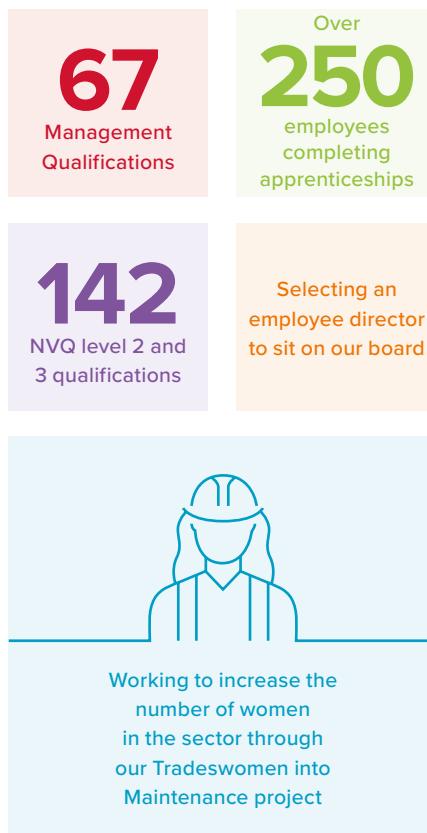
The Index was created by the Social Mobility Foundation in 2017 and ranks UK's employers on the action they take to ensure they are open to and progressing talent from all backgrounds. It highlights the employers who are doing the most to change how they find, recruit, and advance talented employees from different social class backgrounds.

Now in its fourth year, the Employer Index is the definitive benchmark of organisations committed to improving social mobility in the workplace.

Employers are assessed across seven key areas, these include their work with young people, routes into the company, how they attract talent, recruitment and selection, data collection, progression, experienced hires, and advocacy. This year, 119 employers from 17 sectors, who collectively employ almost one million in the UK, answered around 100 questions across seven different areas. Over 14,000 employees also took part in a voluntary employee survey.

Mears has been ranked in the listed Top 75 employers in the Index for the work we have done to tackle this issue, ensuring we enable those from lower socio-economic backgrounds to succeed. Being the only organisation representing the housing sector in this multi-sector accreditation, Mears has been recognised and ranked in the 45th position on the index for leading the way in removing the barriers which are holding back the best and brightest candidates in our communities.

Measures taken by Mears to improve social mobility included:



Board



2019: Male: 9, female: 2

Senior Management



2019: Male: 25, female: 6

Employees



2019: Male: 4,714 , female: 4,047

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Marketing and Communications Executive, Lisa Mcilree was a Mears mentor this year. She said,

I am so incredibly proud to be a part of this programme. The competition was fierce this year and I wish all the teams' success in continuing to develop and implement their ideas. It feels great to be part of something that helps not just encourage students to bring out their creativity and ideas, but also demonstrates what we could do to make a better planet. These ideas will help forge a better future for all of us."

Strategic report continued

Our approach to Environment, Social and Governance (ESG) continued

Last year, Mears began working with the Social Mobility Pledge led by former Cabinet Minister Justine Greening.

As a mark of our commitment, Mears signed the pledge alongside 24 major UK businesses, including 12 of the FTSE100 and 15 Universities to create a network of employers committed to social mobility.

In October, Justine delivered the outcome of our work in Rotherham – to celebrate not just what we have achieved but to publicly say to communities like Rotherham – we are still here and we will still offer anyone the path to an amazing skillset and career.

We are proud to be recognised as one of the top employers that are committed to improving people's lives. As a business, we are literally rooted in the communities where we work. Whether that's by interacting with people as customers or by being large community employers.

AASC Scotland: Mears Team Supports Glasgow's Baby and Family Support Service

The staff in our Glasgow asylum team have been praised for their support to fund and distribute goods and services worth more than £430,000 to Glasgow's Number One Baby and Family Support Service.

More than 160 children from the Glasgow asylum seeker community and many others, were beneficiaries of special Christmas stockings filled with toys and warm clothes over the festive season.

The team have been helping the charity which has generated goods to the value of £2.7m in just over 4 years since it was launched.

As well as donating funding, they have also provided help with packaging and distribution while company staff in Glasgow have given donations and their own time to assist during the pre-Christmas rush to make sure gifts reached children in time.

Our partnership manager Anne Kinghorn who has helped oversee the company's staff involvement said every week housing and welfare managers from Mears request additional items of clothing for children, babies and adults along with requests for household goods or specialised pieces of equipment and clothing which can range from swimming floats to bicycles.

Anne said the charity exists to support people who are in financial hardship and struggling to make ends meet and added: "We are especially proud of our staff who have become deeply involved and many Mears employees also use their volunteering days as part of the company's social value aims."

Audrey Dempsey who runs the charity took time out from packing gifts to publicly acknowledge the work Mears and its staff have carried out and said: "The Mears staff are an absolute godsend to us. The work they do is absolutely fabulous. Their help allows us to focus on others in need and they also involve themselves in packing and the delivery of goods. Mears have organised a rota where staff have been drafted in to assist in packing, distribution and delivery of presents."

"The Mears Foundation also helped us with a grant which has been a great help and support."

Barnsley Home Schooling Project

Mears was delighted to be successful in winning contracts for Asylum Accommodation and Support Contracts (AASC). The UK Government has a duty to provide Asylum for people fleeing persecution and in danger in their homeland. Whilst considering the asylum application, the Home Office must provide accommodation and support. Mears is responsible for over 18,000 people seeking asylum.

Those seeking asylum can be singles (30%) or families (70%), we are responsible in providing housing and crucially we are responsible for their wellbeing and welfare. One of the areas around wellbeing is ensuring they are integrated into their communities and that the children of families attend regular schooling. Mears dedicated colleagues work very hard to ensure this happens.

The pandemic created many challenges for the Mears AASC contracts. Following lockdown, we saw an immediate increase in migrant numbers, as those not already registered in the asylum system sort shelter and care. It also brought challenges to families with schools closed and teaching being moved on-line.

Asylum service users do not have laptops or tablets, which took them immediately out of formal learning. Families have the potential to stay permanently in the UK, depending on Home Office decisions, and not being able to get an education or learn English could create huge problems further down the line and could create future integration problems.

Our AASC Partnership Managers have worked since the start of the pandemic with partners, such as the City of Sanctuary, the Refugee Council and Barnsley Council. These charities and local authorities recognised that children were being put at huge disadvantage. They donated funding to obtain recycled laptops, and retailers were asked for donations to ensure as many families as possible would have access to Barnsley's Home-Schooling service. Mears helped to distribute the technology and to ensure that the most vulnerable families received them first. This also required guides in their own language so they could access and use them. The feedback from the families was very humbling, it put smile on children's faces at a time where they could have become very isolated and disconnected from society.

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We take our responsibility to social mobility very seriously and hope that wherever we work we contribute to that society as an employer, as a local partner and as a driver of opportunity."

Leeds Food Bank

Our colleagues in Leeds came to the aid of Leeds South and East Foodbank during the early days of the COVID-19 Pandemic.

The team donated transport to help deliver food to the people who desperately need it the most during these difficult times.

According to Leeds South and East Foodbank, many more people in the local area have called upon their services for the first time. From March 2020 to mid-July 2020 the foodbank fed 3,138 people including 1,282 children, which was a 45% increase in comparative to figures from last year.

Due to COVID-19, parcels are now delivered to people's homes by volunteer drivers. Mears helped foodbank staff and volunteers to travel across South and East Leeds to deliver food to a temporary mini-warehouse, pick up food donations and distribute emergency food to the most vulnerable in society, during this pandemic and in the future.

Garry Jamieson, Head of Operations at Leeds, said:

People at Mears give their heart and soul to help their communities. We have seen fantastic examples of how colleagues across the business have gone above and beyond to help people during these challenging times.

"A special thank you to our staff who volunteered to work with the food bank despite being on furlough.

"Mears works in some of the most marginalised communities in the UK and these are difficult times for all of us. We must all do our part to help the most vulnerable people in the community. Because of COVID-19, children have been out of school for much longer than anyone anticipated and families who were depending on free school meals have been left trying to make already tight budgets stretch further and many have needed assistance from the foodbank just to feed their children.

"No one in our communities should have to face going hungry and we are glad that our van will help make a positive difference to their lives."



Championing Equality and Diversity

The Black Lives Matter protests in 2020 rightly highlighted the need for companies across the world to demonstrate that they are taking real action to recruit, retain, encourage and promote people from backgrounds where they might suffer from discrimination.

We deliberately waited to say anything about this until we had taken the opportunity to understand how the impact of our current working practices affects encouraging diversity and appropriate representation across all areas of our workforce. We felt that to say anything on this important matter before we understood the current status would be to pay lip service and to jump on the bandwagon.

As part of our review, we commissioned the EW Group who are experts in equality, diversity and inclusion to review what we can do as a company. We have also engaged with Black Lives Matter and provided full access to our policies which they have commented on positively. We believe this is fundamental to our business model given the diversity of our customer base and the need to ensure we have the strongest possible workforce for the future. This is not a one off project but one that will continue for the foreseeable future and be embedded to all our policies and procedures. We have a wide range of ambitions here including:

- ▶ Better recruitment and retention of staff
- ▶ Continuing to see greater diversity at every level of the organisation
- ▶ Increase customer and employee satisfaction
- ▶ Improve our contract win rate by demonstrating that we understand the needs of all our customers.

Mears has always tried to ensure we treat all of our workforce with dignity and respect and to ensure if this is not happening appropriate action is taken. We have worked hard to achieve accreditation from the Diversity Network, we pride ourselves on being a company who believes that anyone, from any background can go on to lead our company. We also run our regular Women in Maintenance programme to ensure that we have the best people in our business – all of this is about having the most skilled people working with us regardless of where they come from or who they are.

We hope that by asking our colleagues and clients for their experiences, we have been able to build awareness and policy change to create genuine social mobility in our company. By adjusting our policies, a story telling culture for those who suffer from discrimination to feel that they are able to seek advice, support, and encouragement from our family at Mears.

Strategic report continued

Why invest

Mears is the UK's leading and most trusted provider of a wide range of specialist Housing services to Local and Central Government.



Market leading housing specialist

- ▶ No. 1 outsourced provider of responsive repair services to the social housing sector in the UK
- ▶ Trusted client relationships with local and central government and 30+ year reputation for quality, customer service, operational excellence and innovation



Large, stable markets underpinned by legislation

- ▶ Our range of essential housing services and solutions help our public sector clients address the chronic shortage of decent, affordable housing in the UK
- ▶ Our services are non-discretionary, required by legislation with funding often coming from 'ring-fenced' sources



Revenue visibility from £2.5bn orderbook

- ▶ Low risk, high quality contract portfolio with > 60 local and central government clients
- ▶ Highly disciplined and successful tender process delivering contract strong extension and retention rates. Focus on quality measures as well as price, thereby maintaining strong embedded margin





Contract portfolio delivers stable revenues and margins

- ▶ Once mobilised our contracts tend to deliver stable, dependable revenues and margins
- ▶ Average contract length is 7 years (+ extension options) and typically include a balance of lump-sum and volume-based mechanisms, indexation, ancillary growth opportunities and mobilisation payments



Good cash conversion and disciplined capital allocation

- ▶ Post mobilisation, our contracts have low working capital requirements delivering strong operating cashflow and returns on capital
- ▶ The Group has low capex requirements and a strengthened balance sheet. The Group has a 23-year progressive dividend history and intends to return to the dividend list post-pandemic



Good growth prospects

- ▶ Market leading delivery confers competitive advantage in contract bidding
- ▶ Scope to extend range of services offered to core Housing clients, especially following green agenda
- ▶ Opportunities to extend offer to Central Government and private sector



mearsgroup.co.uk



INVESTORS
IN PEOPLE

Strategic report continued

Risk management

Effective management of risks and opportunities is essential to the delivery of the Group's strategic objectives, the achievement of sustainable shareholder value and maintaining good standards of corporate governance

Risk management process



The Board

The Board has overall responsibility for determining the nature and extent of risk it is willing to accept within the agreed strategy and ensuring that risks are managed effectively across the Group.

Risk is a regular agenda item at Board meetings and is closely aligned to strategy review.

The Board also reviews reports on the effectiveness of the systems and processes of risk management and internal control.

The Senior Management Team

The Senior Management Team reviews and identifies the key risks which may impact upon the achievement of the Group's strategic goals and will consider how these risks are developing with changes in the operations, markets and the regulatory environment.

The nature of the risk is reviewed, including the possible triggering events and the aggregated impacts, before setting appropriate mitigation strategies directed at the causes and consequences of each risk. The risk is assessed in relation to the likelihood of occurrence and the potential impact of the risk upon the business and assessed against a matrix scoring system which is then used to escalate risks within the Group as appropriate. The Senior Management Team has responsibility for managing the Group's key risks.

The Audit Committee

The Audit Committee monitors the Group's key risks identified by the risk assessment processes and reports its findings to the Board. It also has delegated responsibility for reviewing in detail the effectiveness of the Group's system of internal control policies and procedures for the identification, assessment and reporting of risk.

Compliance Committee

The Audit Committee has a very active sub-committee, being the Compliance Committee. This reflects the significant focus that the Group gives to dealing with health, safety and environmental risks. The extent to which the full integration of health, safety and environmental risks is now embedded in the governance structures of the Group is highlighted by the members of the Compliance Committee who include the Group's Chief Executive Officer, Health and Safety Director and internal Health and Safety legal adviser.

Risk management function

The Group risk function is headed by the CEO and CFO. The Group has a functional risk register and there is a good understanding of the risks that could impact the Group, and their severity. The Group has a positive risk culture, with a clear tone-at-the-top being set by the Senior Management Team. The control environment is underpinned by a detailed scheme of delegated responsibilities that defines processes and procedures for the approval process in respect of decision making. This ensures that decisions within the organisation are made by the appropriate level of management.

The Group has engaged KPMG as an outsourced provider of internal audit services. KPMG assists the internal Group risk function to set the Internal Audit plan. This is a dynamic programme set on a three-year time horizon and ensures certain risks and themes are prioritised and appropriate resource and skills applied to those areas.

Risk management approach

The Group's approach to risk management is targeted towards early identification of risks and mitigation of those risks to reduce their likelihood and impact.

The Group is committed to protection of its assets through an effective risk management process, supported by insurance where appropriate. Examples of assets within scope include human, intellectual, physical property and financial resources.

Reporting within the Group is structured so that key issues can be escalated rapidly through the management team to the Board where appropriate. Risks are continually monitored, contingency plans are provided and this information is reported through established procedures. There is extensive fieldwork undertaken by risk auditors incorporating systems review, branch visits and cross-business surveillance.

The internal control approach is designed to manage rather than eliminate the risk of failure and thus can only provide a reasonable, rather than absolute, assurance against material misstatement or loss.

Internal audit approach

Our internal audit plan is devised by understanding the strategy, objectives and risk profile of the Group and considering the other forms of management and independent assurance before agreeing what internal audit work is required. This enables us to ensure that our internal audit resources target the key areas and it also enables us to be efficient by not duplicating other assurance activities.

We take a different approach to each risk type:

Strategic: We take a high-level view or a deep dive into areas of specific risk or investment. We link our work to the Group's strategic priorities and principal risks, to the extent the Board does not receive other assurance.

Operational: At the heart of our plan, we consider whether core controls are working effectively across the Group, again taking account of other assurance activities.

Strategic report continued

Risk management continued

Setting our internal audit priorities



Risk management process

The responsibility for risk identification, analysis, evaluation and mitigation rests with the line management of the businesses. They are also responsible for reporting and monitoring key risks in accordance with established processes under the Group operational policies.

Identified risks are documented in risk registers showing: the risks that have been identified; characteristics of the risks; consequences of the risks; the basis for determining the mitigation strategy; and what reviews and monitoring are necessary. The person(s) accountable for assessing and monitoring each risk is noted.

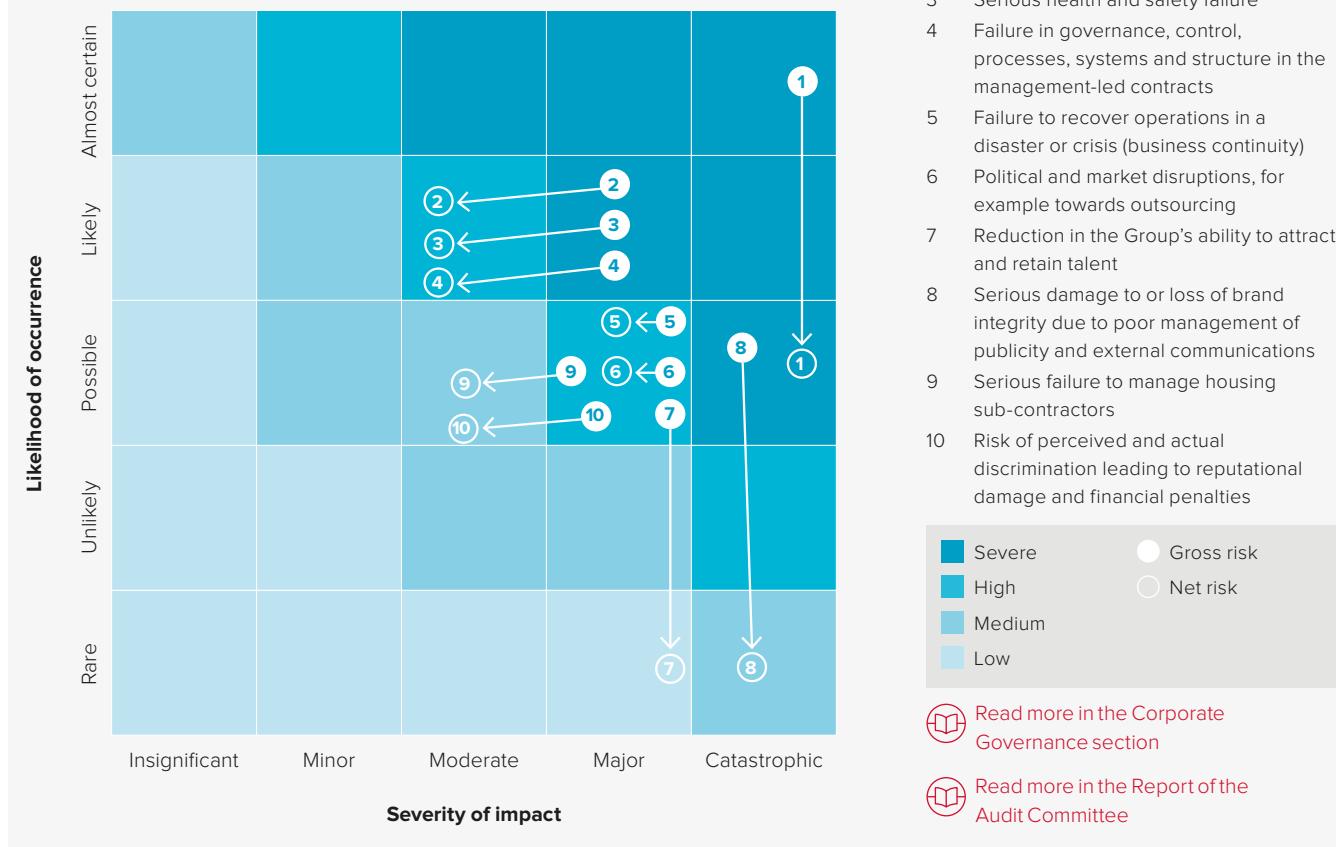
We continue to drive improvements in our risk management process. We also review our business model, core markets and business processes to ensure that we have properly identified all risks. We continually review our mitigating actions to ensure that they are sufficient to minimise our residual risk. Key financial and non-financial risks identified by the business from the risk assessment processes are collated and reviewed by the Audit Committee. The financial and non-financial risk registers are reviewed to monitor the status and progression of mitigation plans; the key risks are reported to the Board on a regular basis.

Principal risks

The Board has carried out a robust assessment of the principal risks facing the Group, including those that threaten the business model, strategy, future performance, solvency and liquidity. Risks have been identified as 'principal' based on the likelihood of occurrence and the severity of the impact on the Group and have been identified through the application of policies and processes previously outlined. The Board is keen to simplify the reporting of risks, to ensure the risks disclosed to shareholders are those that are considered as business critical or potentially catastrophic. Therefore no additional risks have been disclosed in this Annual Report. These business-as-usual risks are monitored by divisional management.

Principal Risk Heat Map: year end

The Group's risk register rates risks on a matrix scoring system based on their likelihood and impact, i.e. potential severity. This severity can be measured using life and limb, financial, customer service, growth, regulatory compliance and reputational criteria. Therefore, Mears measures more than simply the financial impact of the risk. These scores are used to escalate risks and to drive the mitigation plans.



Emerging risks

The Board have considered the following areas and their risk to the company:

Covid-19: Short-term	The risk that the Group fails to successfully recover from short term impact of Covid-19. Areas of concern are increased Health & Safety risks to the Group's staff and its service users, adapting to remote working and mental health and wellbeing.
Covid-19: Long-term risks	Covid-19 has long-term implications for the Group that could result in financial losses and limitations on future growth. Possible scenarios include reduction in government spending, increased taxation, and potential future claims from staff and service users in relation to the medical condition 'Long Covid'.
Environmental, Social and Corporate Governance (ESG)	ESG presents risks and opportunities for the Group. There is a risk that Mears does not identify and manage the risks associated with changes in environmental legislation relating to housing, transportation and corporate reporting requirements. There is also a risk that the Group does not maximise opportunities presented by ESG related changes in its business environment.
Succession planning at Executive level	Failure to adequately plan for changes at executive level resulting in business disruption and barriers to deliver strategic objectives.
Legislative changes	Changes to building and fire safety legislation that result in higher cost to comply with requirements and increased scrutiny from regulators.
Maintaining and developing competitive advantage	Mears has made significant investment in IT systems over many years. There is a risk that competitive advantage deteriorates in the Housing Maintenance division as a result.

Prioritising our risks

The Group's risk register rates risks on a matrix scoring system based on their likelihood and impact, i.e. potential severity. This severity can be measured using life and limb, financial, customer service, growth, regulatory compliance and reputational criteria. Therefore, Mears measures more than simply the financial impact of the risk. These scores are used to escalate risks and to drive the mitigation plans.

Strategic report continued

Principal risks and uncertainties

Risks are identified as 'principal' based on the likelihood of occurrence and the potential impact on the Group. The Group's principal risks are identified below, together with how we mitigate those risks.

Key risk movements

Each principal risk is considered in the context of how it relates to the achievement of the Group's strategic objectives. The risk discussion includes assessment of gross risk and net risk. Gross risk reflects the exposure and risk landscape before considering the mitigations in place, with net risk being the residual risk after mitigations. The gross risk movement from the prior year for each principal risk has been assessed and is presented below.

Mitigations in place supporting the management of the risk to a net risk position are also described for each principal risk.

Reputation

Increased gross risk exposure

Definition	Mitigation	
<p>We recognise the significant commercial value attributable to the Mears brand. Our success in securing larger and more complex contracts, such as the new Asylum contract, increases the risk of reputational damage in the event of failure. Poor service delivery would damage our reputation. Both our Housing and Care markets are close-knit communities where examples of poor performance are quickly communicated widely.</p> <p>In the environment of caring for vulnerable people, there is a risk of isolated incidents of abuse and neglect, which rightly receive significant press coverage with the inevitable reputational damage.</p>	<ul style="list-style-type: none"> ▶ In-house IT system developed to provide operational management with a real-time dashboard of service delivery indicators. ▶ Internal auditing of KPI reporting including 'mystery shoppers'. ▶ Strict process in place for vetting and approval of subcontractors. ▶ We drive a culture of putting our customers first; this is continually reinforced through internal communications. 	<ul style="list-style-type: none"> ▶ Well-communicated policy for dealing with press enquiries and incident management. ▶ Care risk plans for dealing with vulnerable customers. ▶ Compliance management of bribery and corruption legislation and whistleblowing policy. ▶ We induct and train all new starters. This induction ensures that all employees understand our values and it reinforces the Group's culture. ▶ We ensure that staff are properly trained for their roles. We ensure that we deliver relevant training and implement best practice.
<p>KPIs associated with risk:</p> <ul style="list-style-type: none"> ▶ 'Excellent' service rating ▶ Customer complaints ▶ Staff churn 		

People

Reduction in risk exposure 

Definition	Mitigation
<p>The Group employs around 6,000 people who are critical to the success of our contract performance. Attracting and maintaining good relations with employees and investment in their training and development are essential to the efficiency and sustainability of the Group's operations. Delivery of strategic objectives increases our ability to attract, motivate and retain talent.</p> <p>KPIs associated with risk:</p> <ul style="list-style-type: none"> ▶ 'Excellent' service rating ▶ Customer complaints ▶ Staff churn 	<ul style="list-style-type: none"> ▶ We induct and train all new starters. This induction ensures that all new employees understand our strategy, vision and values. All Care staff have access to NVQ training. ▶ We regularly review and benchmark our remuneration packages to ensure that they remain competitive. In Care, we are investing in an innovative recruitment process to ensure an increase in the volume and quality of carers. Local Care branches are targeted on a monthly basis in the areas of recruitment and retention. ▶ At the senior end of the business, we have increased our focus on succession planning and increased our investment in senior management development. Our senior leadership programme has identified a cross-section of the Group's brightest talent that we would envisage will play central roles in our future business. ▶ Expansion of apprenticeships.

Health and safety

No change in risk exposure 

Definition	Mitigation
<p>Prevention of injury or loss of life for both employees and customers is of utmost importance. In addition, it is vital to maintain the confidence our customers and clients have in our business.</p> <p>KPIs associated with risk:</p> <ul style="list-style-type: none"> ▶ Accident frequency rates ▶ Customer complaints ▶ 'Excellent' service rating 	<ul style="list-style-type: none"> ▶ Significant investment in the centralised health, safety and environment (HSE) function to maintain consistency and quality. ▶ We have comprehensive safe systems of work which are well communicated through a robust and coordinated internal training regime. ▶ We have robust processes for inducting new staff to ensure the importance of health and safety is emphasised together with detailed method statements for working safely. ▶ Compliance Committee to monitor and oversee health and safety strategy and performance, regulatory compliance and risk management.

IT and data

No change in risk exposure 

Definition	Mitigation
<p>A major incident or catastrophic event could impact on the Group's ability to trade. In addition, it is essential that the security of customer, employee and Company confidential data is maintained.</p> <p>A major breach of information security could have a major negative financial and reputational impact on the business. The risk landscape of IT and data is constantly increasing with deliberate acts of cyber-crime becoming more sophisticated and frequent across all markets.</p>	<ul style="list-style-type: none"> ▶ The Business Continuity Plan is regularly reviewed and tested to ensure it is fit for purpose. ▶ Business continuity and IT disaster recovery management resource is convened at short notice to manage the response and any associated risk to the Group. ▶ General Data Protection Regulation (GDPR) steering group.

Strategic report continued

Business planning and financial viability

This latest Viability review is being completed immediately following a period that has seen the unprecedented event of a worldwide pandemic. The Covid-19 outbreak brought significant short-term challenges where the Group was required to adapt quickly to deliver services in a secure and safe environment to protect both our employees and service users. The Group's maintenance activities saw a reduction by around 80% at the peak of the first lock-down. Whilst a large proportion of the Group's customers were supportive during this period, putting in place interim arrangements to support the recovery of local contract costs, the loss of revenues naturally resulted in a significant under-recovery of central overheads. Whilst the Group also adapted quickly to find new ways of working, the alternative methods of working reduced productivity and brought incremental costs such as PPE. However the Board takes significant comfort from the fact that during this period, where the Group was required to react to an event that was more severe than any scenario that was modelled in previous periods, the Group delivered services safely, maintained high levels of customer satisfaction and improved employee engagement, whilst from a financial perspective, delivered both a small profit and improved liquidity without recourse to shareholders. Whilst this viability review looks to the future, the performance of the business in the recent past in the most challenging of circumstances provides the Board additional confidence as to the resilience of the Group.

In accordance with C.2.2 of The UK Corporate Governance Code 2014, the Directors are required to assess the viability of the Group over a five-year period. A period of five years has been chosen as it reflects broadly the average contract length, being a blend of an average contract length of five years excluding extension options. Whilst the Group holds contracts which extend beyond this time horizon, a period of greater than five years is considered too long, given the inherent uncertainties involved.

The Board considered its key risks. The principal risks are set out on pages 66 to 77 and the most relevant of these risks on viability were considered to be:

- ▶ A service delivery failure, possibly resulting in the death or harm of a service user, with significant negative publicity and long-term reputation damage.

- ▶ A Health and Safety failure resulting in serious personal injury or death of an employee or service user, leading to both significant financial penalties and significant reputational damage.
- ▶ A failure in our IT systems impacting upon our ability to deliver our services. We provide services to vulnerable people and even a short period of downtime could cause severe reputation damage. A serious system failure could have significant impact to invoicing our customers and collecting cash.

A financial model has been built on a contract by contract basis for the next twelve months and extended for the following four years. The five-year plan considers cash flows as well as financial covenants. The forecast for 2021 is based on the existing customer relationships only, and assumes no revenue growth, and a business that is generating contract margins that are in-line with the historic run-rate. Some impact from Covid-19 is built into the forecast for the first quarter of 2021, at which point a return to normality is assumed. The services delivered by the Group are non-discretionary, and management believe that any reduction in revenues from Covid-19, while potentially significant, are temporary. The base case model forecasts a result for 2025, being year 5 of the model, with revenues and PBT of £747.3m and £33.9m respectively, and an average net cash at the end of that period of £41.1m. Given this modelling excludes the Group securing work with new customers, and reflects some revenue reduction from existing clients where it is forecast that there will be no further opportunity upon expiry of the current contract, the base case model should be considered to be conservative and below the Board's expectations.

Sensitivity analysis was undertaken to stress-test the resilience of the Group and its business model to the potential impact of the Group's principal risks, or a combination of those risks. The Board overlaid the potential impact of the principal risks which could affect solvency or liquidity in "severe but plausible" scenarios. The Group considered modelling a fourth Covid-19 lock-down within this viability review, however management felt that the scenarios modelled were likely to have a more negative impact on profitability and liquidity than that of a further lockdown. Management also recognised that the financial covenants for June 2021 had already been adjusted to accommodate a down-side scenario reflecting a further national

lockdown, and therefore any short-term risk has already been substantially addressed.

Three scenarios were modelled:

Scenario 1

This scenario assumes a negative outcome in respect of Housing maintenance contract renewals. Given the average contract length of 5 years, several key contracts will come up for renewal over this review period. The Group has a good track-record of re-securing work on re-bid. However, for the purposes of this viability review, management has assumed a significant deterioration in the Group's performance in this area, possibly following a significant event which has impacted negatively on the Group's reputation in the sector. The Group has modelled a downside scenario where it fails to re-secure any material contracts that come up for re-bid during the period 2021 to 2024. The impact upon revenue of this assumption is detailed below:

Contract	Annual value £m	Expiry date
Contract A	£18m	2021
Contract B	£12m	2022
Contract C	£20m	2022
Contract D	£18m	2023
Contract E	£20m	2023
Contract F	£40m	2024
Total annual value in 2025	£128m	

This loss of revenue results in a reduction in contract operating margins and an under-recovery in central support overhead, resulting in a reduction in revenue from £747.3m to £618.5m and in PBT from £33.9m to £18.6m in year 5 of the model.

Scenario 2

This scenario assumes a significant deterioration in the cash collection measurements, being an increase in the time period between the completion of works (which typically matches the point in time which sees a working capital outflow), and the receipt of cash from the Group's clients (which follows a process where works are valued and invoiced by the Group before being approved and settled by clients). The Group has made significant investment in its operational systems which are key in respect of capturing all costs against individual orders, ensuring that the work delivered is identified and invoiced correctly, and

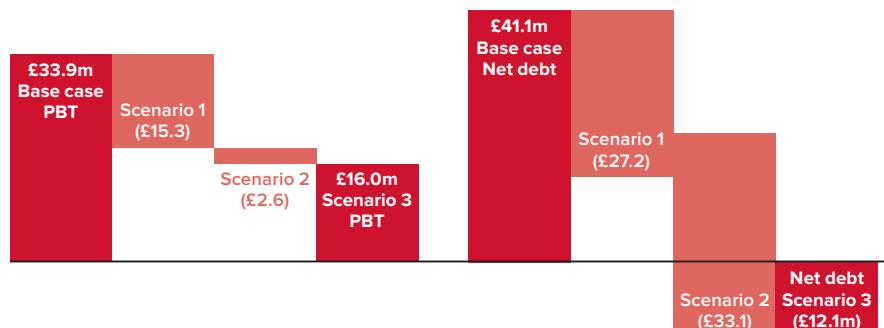
maximising the operating margin). The Group has an excellent track-record in managing the working capital absorbed within its Maintenance activities. In this second scenario, a significant increase in the time taken to receive monies in respect of works completed across multiple clients, would be reflective of a system failure, impacting on the Group's ability to invoice accurately; on time and in a format which can be easily uploaded onto the clients own finance system. Management was mindful when modelling this scenario to consider both the temporary impact of a system failure on the timing of working capital cashflows, and of even greater concern, a system failure impacting on the Group's ability to properly value its revenue which could in some circumstances result in a permanent loss of value. For the purpose of this scenario, management has modelled an operating margin reduction of 2% for a single duration of 3-months at any point during the 5-year review period. In addition, this scenario modelled a 3-week deterioration in respect of the maintenance contract asset collection period, increasing from 55 to 76 days. The working capital cycle is impacted for a six-month period, reflecting the fact that given the high volume and low value nature of the maintenance activities, an invoicing backlog resulting from a system failure takes several months to resolve. This impact of scenario 2 results in a reduction in profit of around £2.6m and a temporary deterioration in net debt by circa £33m.

Scenario 3

A combination of both scenario 1 and 2. The combination of both a significant loss in revenue together with some reduction in operating margin from scenario 1, and both a reduced margin and an impact on liquidity in the event of scenario 2. The impact on both PBT and net debt in 2025 based on this combined scenario is detailed below:

All scenarios showed that the Group would remain viable even in the event of a severe business failure over an extended period. No mitigating actions were included within either scenario which was considered conservative but not entirely realistic. Whilst the Group's operations are entirely based in the UK, the large network of branches reduces the risk of serious business interruption through a single failure. In addition, the Group has a broad spread of customers – the largest single client is now 15% of Group revenues, being the Asylum contract. While significant, the loss of a major client would not impact on the Group's wider viability.

PBT impact on 2025

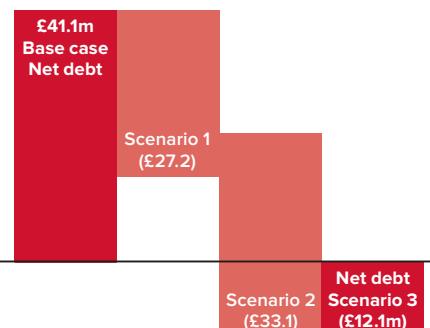


The Group's existing debt facilities run to November 2022. The future viability review extends beyond this date and therefore assumes that there will be enough appetite from our existing or new funders to provide the required level of funding on similar terms. The Group's pro-forma average daily net debt in 2020 was £42m when adjusting for the full year impact from the disposal of Terraquest. The future viability review indicates a net debt at the point of renewal, to be around £14.4m, £16.0m, £46.2m and £46.8m across the base case, scenario 1, scenario 2 and scenario 3 respectively. Therefore in all four cases, it is forecast that the Group would have delivered a reduction in its debt level at renewal compared to the balance today, and management expect to be in a position to seek a reduction in the facilities required at renewal.

In addition to the three scenarios, the Board tested the sensitivity of the business to increasing the severity of the assumptions detailed in each case, to measure the trigger points at which the viability of the Group, in the absence of further mitigations, could be impacted.

- ▶ Scenario 1 already assumes that all revenue is lost on re-bid and in isolation this would not impact on the viability of the business. Were the Group to see existing contracts terminated before their time, this could impact upon covenants and funding levels, and could inevitably impact upon viability.
- ▶ Scenario 2, for each 0.1% reduction in operating margin results in PBT reducing by around £0.15m. In addition, for each day increase in the collection period on contract assets results in a deterioration in net debt by circa £1.5m.

Net debt impact on 2025



The viability statement also highlighted the increasing risk that fines can be levied upon companies for non-compliance in areas such as health and safety and data protection. Fines are discretionary based on the nature, gravity and culpability of the company but fines are applied based upon a percentage of Group revenue. In a low margin business such as Mears, any single fine could have a significant and is proportionate impact upon retained profits. Whilst such an event could be damaging, it would not be expected to ultimately impact on the long-term viability of the Group. Both health and safety and IT and data feature high on the Group's risk register and we continually review our mitigating actions to ensure that we minimise our residual risk.

The viability statement highlighted that there is naturally uncertainty within any forecast and this uncertainty increases as the projections cover a five-year period. The conclusion attached to the viability review was that there was a reasonable expectation that the Group will continue in operation and would be able to continue to meet liabilities as they fall due over the five-year period of business planning.

This Strategic Report was approved by the Board on 12 May 2021

D Miles
Chief Executive Officer
david.miles@mearsgroup.co.uk

Corporate Governance

Our Corporate Governance Compliance Statement

An effective culture of governance

The Board believes that the Company has complied with the principles and provisions of UK Corporate Governance Code 2018 (the '2018 Code) throughout the financial year ended 31 December 2020. The 2018 code is available on the FRC website (www.frc.org.uk)

The table below assists stakeholders to assess how the Company has applied the principles of the 2018 Code and where this is detailed within this Corporate Governance Report.

Introduction to Corporate Governance

Chairman's introduction	Page 71
-------------------------	---------

Board leadership and company purpose

Board of Directors	Page 72
--------------------	---------

Corporate governance framework	Page 74
--------------------------------	---------

Key board activities in 2020	Page 75
------------------------------	---------

Promoting the success of the Company	Page 76
--------------------------------------	---------

Stakeholder engagement	Page 77
------------------------	---------

Division of Responsibilities

Roles and responsibilities	Page 79
----------------------------	---------

Composition, succession and evaluation

Board composition	Page 81
-------------------	---------

Report of the Nomination Committee	Page 82
------------------------------------	---------

Audit, risk and internal controls

Report of the Audit Committee	Page 84
-------------------------------	---------

Remuneration

Report of the Remuneration Committee	Page 92
--------------------------------------	---------

Annual report on remuneration	Page 101
-------------------------------	----------

Report of the Directors	Page 112
-------------------------	----------

Statement of Directors' responsibilities	Page 115
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Further information on how we have applied the principles and complied with the provisions of the 2018 Code available [here](#):

Nomination Committee Report
pages 82 to 83

Audit and Compliance Committee Report
pages 84 to 91

Report of the Remuneration Committee
pages 101 to 111

Introduction to Corporate Governance

Chairman's introduction

Dear shareholder,

On behalf of the Board, I am pleased to introduce the Corporate Governance Report for 2020. This report looks to update you on what the Board and its committees have focussed on in 2020, with details about the effective governance systems throughout the Group which supports the long-term success of our business. During the year ended 31 December 2020, we have been compliant with the provisions and principles of good governance, as set down within the UK Corporate Governance Code 2018 (the 'Code').

We believe that Mears has a strong corporate culture which values people and encourages continuous improvement. This is evidenced in our positive staff engagement responses. Our teams are hardworking, passionate and adaptable. This has been especially evidenced by the commitment delivered across the business during the Covid-19 crisis. Our culture and governance systems have supported the business and provided it with the ability to adapt and respond to the fast-changing situation and communicate effectively to employees and other stakeholders.

Board activities

Later in this report, shareholders will find a summary of the matters which the Board discussed during 2020. These include regular reports on operations and financial performance, but also specific strategic questions and developments in relation to the disposal of non-core activities, workforce engagement and dialogue with end customers of the Group. The Board was required to be flexible this year, as the fast moving events linked to Covid-19 and the associated risks meant that, in addition to the scheduled monthly Board meetings, the Board held regular weekly updates for a

period to ensure that the Board was fully involved in understanding and managing the challenges and emerging risks. I am very grateful to my Board colleagues for the extra commitment which they showed to the Company during the course of the year.

Board composition

The composition and size of the Board will continue to be under review. We believe that our Board has a good mix of sector experience, business acumen, knowledge and independence in order to support and challenge the management team and discharge its duties and responsibilities effectively.

Jason Burt stood down from the Board as a Non-Executive Director, in March 2020. Following Jason's resignation from the Board, he confirmed that he did not have any concerns about the operations of the Board or the management of the Group.

Our Employee Director, Amanda Hillerby, left the Board early in 2020 to be replaced by Claire Gibbard. The Board firmly believes that better employee representation can improve the quality of decision making.

Our nominations committee, of which all Non-Executive Directors are members, has been developing succession plans for the Board and senior management. More details can be found in the Nominations Committee report.

Committee governance

Within this annual report, stakeholders will find reports from the chairman of each of the main Board Committees, respectively audit, nomination and remuneration. Committee meetings have taken place throughout the year. I would like to thank the Committee chairs for their work during the year, but also my fellow Non-Executive Directors for their commitment to the work which is increasingly undertaken at Committee level rather than at the main Board. The Committee chairs have remained available to shareholders throughout the year.

Stakeholder engagement

Engagement with the Company's stakeholders, including its workforce, customers, service users, suppliers, Government, regulators, debt funders and investors, is key to enabling the Board to understand what is important to stakeholders, and to assist the Board in making better decisions. This Strategic report and Corporate Governance reports detail how we engage with our key stakeholders, and the wider impact upon the organisation of decisions that are made.

K Murphy**Chairman**

kieran.murphy@mearsgroup.co.uk
12 May 2021

66

Mears must be equipped with a Board that can provide a wide range of views, skills and experience to work with and challenge the management team."



Board leadership and company purpose

Board of Directors

The right mix of skills and experience
to deliver our strategy



1 Kieran Murphy Independent Non-Executive Chairman

Age: 62

Tenure: 2 years

Skills and experience: Kieran is a very experienced non-executive director and chairman. He spent much of his executive career working in finance, holding senior positions. At Kleinwort Benson, he built a market-leading corporate finance advisory business in the building and construction sector and became a member of the bank's Investment Bank Management Committee. More recently, at Gleacher Shacklock, Kieran extended his advisory work into the business services sector.

Principal external appointments: Aliaxis SA., Ordnance Survey, University of London

2 David J Miles Chief Executive Officer

Age: 55

Tenure: 24 years (14 years on the Board)

Skills and experience: David joined Mears in 1996 and, prior to his appointment to the Board in January 2007, was Managing Director of the Mears Social Housing division. Prior to joining Mears, David held a senior position with the Mitie Group. His background is in electrical engineering.

Principal external appointments: None

3 Andrew C M Smith Finance Director

Age: 48

Tenure: 21 years (14 years on the Board)

Skills and experience: Andrew joined Mears in 1999 and, prior to his appointment to the Board, was Finance Director covering the Group's subsidiaries. Andrew qualified as a Chartered Accountant in 1994 and worked in professional practice prior to joining Mears.

Principal external appointments: None

4 Roy Irwin Independent Non-Executive Deputy Chairman and Chair of the Remuneration Committee

Age: 66

Tenure: 4 years

Skills and experience: Roy has significant experience in the social housing sector, having lately been Chief Inspector of the Audit Commission following a career of over 30 years in public sector housing. Since 2013, Roy has held the position of Non-Executive Chairman of Plexus and Omega Housing, being Mears' Registered Providers of social housing with the Regulator of Social Housing.

Principal external appointments: None

5 Dame Julia Unwin Independent Non-Executive Director and Senior Independent Director

Age: 64

Tenure: 5 years

Skills and experience: Julia is former Chief Executive of the Joseph Rowntree Foundation and the Joseph Rowntree Housing Trust. She has significant experience in the housing and care sectors, having been a member of the Housing Corporation Board for ten years. She was appointed Dame Commander of the order of the British Empire in January 2020 for service to civil society.

Principal external appointments: Yorkshire Water Services Limited, Financial Reporting Council, York St John University

6 Alan Long Executive Director

Age: 58

Tenure: 15 years (11 years on the Board)

Skills and experience: Alan joined Mears in 2005 and, prior to his appointment to the Board in August 2009, was Managing Director of the Group's Care division, having previously held the position of Group Sales and Marketing Director. Prior to joining Mears, Alan held senior roles at Britannia Building Society, Mars and Smith & Nephew.

Principal external appointments: None

7 Geraint Davies CBE Independent Non-Executive Director and Chair of the Audit Committee

Age: 66

Tenure: 5 years

Skills and experience: Geraint is a Fellow of the Institute of Chartered Accountants in England and Wales. He was a partner for a leading professional practice for over 25 years. His commercial experience includes working with Registered Social Landlords and a number of organisations in the healthcare sector.

Principal external appointments: Cardiff International Airport Limited

8 Jim Clarke Independent Non-Executive Director

Age: 61

Tenure: 1 year

Skills and experience: Jim is a very experienced listed company Finance Director. He qualified as a Chartered Accountant in 1984. He has spent much of his career in senior finance roles in consumer facing industries, having been Finance Director at David Lloyd Leisure, JD Wetherspoon and Countrywide.

Principal external appointments: None

9 Chris Loughlin Independent Non-Executive Director

Age: 68

Tenure: 1 year

Skills and experience: Chris' is a very experienced CEO. His last executive role, prior to his retirement in 2020, was Chief Executive Officer of Pennon Group plc, the listed company which owned South West Water and the waste business Viridor. He was previously also CEO of South West Water and before that held roles at Lloyds Register, British Nuclear Fuels Plc and Magnox.

Principal external appointments: British Water, Water UK, Reall

10 Claire Gibbard Employee Nominated Non-Executive Director

Age: 33

Tenure: 6 months

Skills and experience: Claire joined the Group in 2018, following the acquisition of Mitie's maintenance business. Prior to this, Claire worked for a Local Authority as well as previously working at Mears for 7 years in various roles. Claire is currently working as a Business Support Manager in the Group's Housing division and has worked across a range of Housing contracts across a wide range of branches and central support.

Principal external appointments: None

11 Ben Westran Company Secretary

Age: 44

Tenure: 17 years (6 years as Company Secretary)

Skills and experience: Ben is a Chartered Accountant and, prior to his appointment as Company Secretary, was Group Financial Controller and Director of a number of the Group's subsidiaries. Ben joined the Group in 2004 having previously worked in professional practice.

Principal external appointments: None

Board leadership and company purpose continued

Corporate governance framework

Our governance framework supports the development of good governance practices throughout the Group. No one individual has unfettered powers of decision. The Board works closely with the Executive team which ensures that the Board and its culture are effectively communicated and embedded within the Group. Regular updates are received from the Executive Directors in order to keep the Non-Executive Board members informed of how the business is progressing.

 Documents available at www.mearsgroup.co.uk

[Articles of Association](#)

[Matters reserved for the Board](#)

[Committee Terms of Reference](#)

[Remuneration Policy \(approved at 2020 AGM\)](#)

The Board

The Board leads and provides strategic direction to the Group and carries ultimate responsibility for management of the Group's activities and financial performance within a framework of internal controls, reviewing its principal and emerging risks. The Board acknowledges accountability to shareholders for proper conduct of the business and responsibility for the long-term success of the Group, while taking into account the interests of a range of stakeholders.

 [Read the Biographies on page 73](#)

 [Read the Board Activities on page 75](#)

 [Read the Roles and Responsibilities on page 79](#)



The Board delegates certain matters to its principal committees which report to the board at every meeting

Audit and Compliance Committee

Assists the Board in discharging its responsibilities for effective corporate governance in respect of financial reporting, agreeing the scope and effectiveness of the external audit, reviewing the effectiveness of the Group's system of internal controls, risk management and internal audit processes.

 [Read the Report of the Audit Committee](#)

Remuneration Committee

Determines the Company's framework and policy on remuneration of Executive Directors and senior management and also reviewing workforce policies and practices.

 [Read the Report of the Remuneration Committee](#)

Nomination Committee

Reviews the structure, size, composition and effectiveness of the Board and its Committees. The Committee also assists the Board on issues of succession planning for the Board and senior management.

 [Read the Report of the Nomination Committee](#)

The Chief Executive Officer and the senior operational leadership team

Responsibility for the development and implementation of the Group's strategy and overall commercial objectives rest with the Chief Executive Officer, supported by the senior leadership team

 [Read the Roles and Responsibilities of Executive Directors on page 79](#)

 [Read the Chief Executive Officer's review](#)

Key Board activities in 2020

Section 172 matters

- Long-term consequences of a decision
- Interests of company's employees
- Fostering relationships with suppliers, customers and others

- Impact on community and environment
- Maintaining a reputation for high standards of business conduct
- Acting fairly between members

Strategy and operations

- ▶ Commenced an in-depth review of the Group's 2021 to 2024 strategy
- ▶ Reviewed and approved the disposal of the Group's Domiciliary Care activities
- ▶ Completed a strategic review of the Group's land referencing and planning activities and subsequently approved the transaction documentation in respect of the disposal of Terraquest
- ▶ Continued to monitor the downsizing of the Housing Development division and opportunities to accelerate the reduction in working capital invested in this activity
- ▶ Received regular updates in respect of the Group's Asylum Accommodation and Support Contract, with a particular focus on the health and safety risks and reputational impact associated with a high-profile contract
- ▶ Received reports on bidding activity for new contract opportunities together with contract renewals
- ▶ Received presentations from divisional management on performance against budget, and their key priorities and plans



COVID-19

- ▶ The Board received roughly weekly updates on progress and stakeholder impacts as the disease first progressed and Mears' operation adjusted to the consequences
- ▶ Early in 2020, a £22.7m 365-day loan to provide additional funding as a precaution at a time of uncertainty



Financial performance

- ▶ Approved the Group's Annual Report and Accounts and half year statement
- ▶ Reviewed and approved the annual budget for 2021
- ▶ Reviewed and approved the viability statement for the Annual Report
- ▶ Approved amendment to the Group's Revolving Credit Facility and significant easing in financial covenants
- ▶ Reviewed the Audit Committee's advice on internal audit planning, progress and reviews
- ▶ Reviewed the Audit Committee's advice on making the 'fair, balanced and understandable' statement in the Annual Report
- ▶ Approved the Group's Tax Strategy



Risk management

- ▶ Reviewed health and safety reports at each Board meeting assessing accidents and other issues affecting Group employees, subcontractors and, where relevant, end customers
- ▶ Received reports from the Chair of Audit and Compliance Committee
- ▶ Reviewed and approved the Group's risk register
- ▶ Reviewed and validated the effectiveness of the Group's system of internal controls
- ▶ Reviewed the creation of the new Customer Scrutiny Board and agreed that, in the first instance, the chair be the link between the two Boards



Leadership and people

- ▶ Reviewed the results of the Group's annual 'say what you see' survey and monitored progress against improvement measures in poorly performing branches
- ▶ Reviewed the Group's report on gender pay and options for improvement
- ▶ Selected the new Employee Director
- ▶ Received reports from the Chair of the Remuneration Committee on its activities and recommendations, with particular focus on finalising the Group's Remuneration Policy for approval at the 2020 AGM
- ▶ Approved grant of Save As You Earn option scheme to all employees



Stakeholder engagement

- ▶ Debated the Group's investor relations plan and the market's assessment of the Company's position and principals
- ▶ Review of operational performance measures through 'voice of customer' initiative
- ▶ Reviewed feedback from major shareholders following release of final results for 2019 and interim results for 2020
- ▶ Approval of the creation of a new and independently chaired Customer Scrutiny Board to seek to raise service standards



Board leadership and company purpose continued

Promoting the success of the Company

The Board recognises a wide range of stakeholder interests and seeks to create a culture whereby decisions are made with consideration to the wider impact upon the organisation as well as financial performance and strategic objectives. The Company's Directors recognise their legal duties under section 172(1) of the Companies Act 2006, to act in the way that is most likely to promote the success of the Company for the benefit of its members as a whole whilst also having regard for the interests of employees, the success of their relationships with suppliers and customers, the impact of our operations on the community and the environment, whilst maintaining a reputation for high standards of business conduct.

Examples of some of the key decisions taken by the Board in 2020 are detailed below, and in each case an explanation provided as to how the Directors recognised the impact of these decisions across a range of stakeholders and how the decision was delivered for the long-term success of Mears, whilst being sensitive to the impact upon stakeholder group and looking to mitigate negative impacts where this can be easily achieved.

Stakeholder groups

S Service Users **E** Employees **I** Investors **C** Community **D** Debt Funders **C** Customers

Key decision	Directors consideration of impact upon stakeholders	Stakeholder group
Disposal of Domiciliary Care activities	<ul style="list-style-type: none"> The Board recognised that the continued underfunding of social care made it impossible to develop a sustainable Care business which could deliver a high-quality service while maintaining a stable workforce Underfunding of social care, with consequent poor returns, made disposal of the Group's Domiciliary Care activities a sensible course of action supported by a number of the Group's largest shareholders The Board agreed a transitional service arrangement where IT and Accounting support was maintained for a period following completion. The disposal of the Scotland Domiciliary Care business was delayed until September 2020 to ensure that the Group's service users and employees were not impacted during the Covid lockdown The business was sold with a normal level of working capital, ensuring there were no financial constraints following completion The Group continued to allow the buyer to utilise the Group's PPE stock for a period of 2 months following the sale of the Scotland business, to ensure continuity of service and the safety of former employees and service users 	S E C I E E C E S E C
Amendment to bank facility in respect of increased liquidity and adjustment to financial covenants	<ul style="list-style-type: none"> The additional commitment agreed with funders in April 2020, put in place as a precaution, provided reassurance to investors, employees, clients, suppliers and Government. The decision to utilise debt rather than equity, ensured that investors did not experience long-term dilution, especially given the backdrop where investors had already supported the decision not to declare a final dividend for 2019 During Q4, the Board approved amendment to the financial covenants which ensured that the Group would be compliant, even in the event of a reasonable worst case. Once again, this decision was taken to provide reassurance to all stakeholder groups 	S E I C D C I S E I C D C
Covid-19 crisis management	<ul style="list-style-type: none"> Daily communications throughout lockdown Decision taken to furlough circa 2,200 colleagues, however top-up mechanism introduced to ensure lowest paid staff were not financially disadvantaged Hardship fund introduced for staff in financial difficulty Rapid provision of additional mobile technology to enable people to work from home Topping up salaries of staff required to self-isolate Putting health and safety first at all times, including agreeing with clients to focus on emergency and essential works only Rapid response to PPE shortage enabling Mears to secure stocks when many others did not Cancellation of final dividend for 2019 	E I D E E E E E C S E C C D

Stakeholder engagement

Board engagement with key stakeholders

Within the Strategic Report, we detail how we engage with our key stakeholders, and explain how each stakeholder group impacts upon our business model and our ability to deliver against our strategic priorities. The Board recognises that engagement with key stakeholder groups strengthens our relationships and is an ongoing part of the operational management of the Group. This includes employee surveys, assessments of customer satisfaction and ongoing conversations with regulators and non-governmental organisations. The Board receives regular updates from senior management on insights and feedback from stakeholders, which allows the Board to understand and consider the perspectives of key stakeholders in decision-making.

The table below sets out the different stakeholders with whom we engage and how the Board monitors these important relationships.

Description	How the Board is kept informed	Read more
 Clients	<ul style="list-style-type: none"> Executive team have daily contact with key clients Regular discussion of key issues at each Board meeting Access to external press and news flow 	 Link to page 32
 Tenants and customers	<ul style="list-style-type: none"> Monthly customer performance statistics, including satisfaction, complaints and compliments Executive Director attendance at tenant panel meetings Customer Scrutiny Board 	 Link to page 32
 Communities	<ul style="list-style-type: none"> Monthly Social Value measures Social Value Annual Report 	 Link to page 32
 Colleagues	<ul style="list-style-type: none"> Close monitoring of staff surveys Monthly People KPIs Employee Director 	 Link to page 34
 Suppliers	<ul style="list-style-type: none"> Engagement with supply chain 	 Link to page 34
 Shareholders and debt funders	<ul style="list-style-type: none"> Investor roadshows and investor briefings Shareholder feedback gathered bi-annually Analyst research notes Regular dialogue with shareholders and funding banks 	 Link to page 34

The Company is committed to maintaining good communication with investors

Investor meetings

Investor meetings are predominantly attended by the Group CEO, CFO and Head of Investor Relations, although other senior Executives may attend. There is an active programme of communication with existing and potential shareholders, with 'City Days' scheduled on a monthly basis (outside of closed periods) which provides any shareholder an opportunity for a meeting with management. There is increased dialogue following the publication of final and interim results, which is facilitated through a series of formal presentations and management allocate a full week at those times to ensure all shareholders can be accommodated. The Chairman is also available for discussions with shareholders as and when they so wish and a number of such discussions took place during the year.

Board leadership and company purpose continued

Stakeholder engagement continued

The Covid-19 crisis required increased communication with our shareholders, but at a time where physical meetings were not considered safe or within Government guidelines. Regular updates were released to investors throughout 2020 to ensure that they had a full understanding of the challenges faced by the Group and how these were being addressed. The Board, and in particular the CEO and CFO made themselves available to shareholders, outside the normal investor relations schedule, via telephone and video conferencing platforms, to provide regular business updates.

The Chair regularly engages with major shareholders to canvass their views on governance and performance against strategy. Committee Chairs will engage with shareholders where a particular matter relates to their area of responsibility.

Annual General Meeting

Shareholder participation at each AGM is usually encouraged. Given the restrictions caused by the Covid-19 pandemic, special measures meant that no shareholders were able to attend the 2020 AGM in these unique circumstances. Full details of the 2021 AGM will be set out in the Notice of Meeting. In normal circumstances, all shareholders are invited to attend the Company's AGM at which point they have the opportunity to meet the Board and raise questions. Shareholders who are unable to attend are invited to e-mail questions in advance to company.secretary@mearsgroup.co.uk

Capital market days

The Company also held additional investor days during the year to ensure that they are better informed of market and Company developments. A Capital Markets Day in January 2020 provided an update on the

Asylum Accommodation and Support Services Contract (AASC). The event was well attended, and the management team delivered a detailed presentation followed by an opportunity for shareholders to ask questions.

Annual Report and other communications

The Board maintains regular contact through the provision of the Annual Report, regular Interim Reports and regular trading updates. This information can be found on the Group's website (www.mearsgroup.co.uk).

Corporate website

The Group website has a dedicated investor section which provides an overview of Mears, whilst also providing access to historic Annual reports and shareholder presentations. The Group regularly receives and responds to questions raised by small private shareholders through the investor enquiry portal within the Group's website.

The Group also has regular dialogue with its banking partners, valuing the close relationship with Barclays, HSBC and Bank of Ireland.



	Holding at April 2021	Holding at February 2020
	% IC	% IC
Shareholders holding over 2% of issued share capital		
● PrimeStone Capital	12.3%	13.1%
● Artemis Investment Management	11.3%	9.3%
● Fidelity Management & Research	10.0%	6.7%
● Shareholder Value Management	9.8%	10.6%
● Majedie Asset Management	8.2%	8.2%
● LOYS	5.1%	—
● Columbia Threadneedle Investments	5.1%	5.8%
● Heronbridge Investment Management	5.0%	6.5%
● Dimensional Fund Advisors	4.1%	4.4%
● Huntington Partners	3.3%	—

2020 investor relations programme:

January

- ▶ Trading update
- ▶ Capital Markets Day covering AASC contract

February

- ▶ Close period

March

- ▶ Covid-19 update released followed by investor calls with all major shareholders

April

- ▶ Shareholder calls upon request

May

- ▶ Covid-19 update released in early May followed by investor calls with all major shareholders
- ▶ 2019 finals released; roadshow, but no face to face meetings

June

- ▶ AGM under Covid-19 rules

July

- ▶ Trading update released but closed period reduced dialogue

August

- ▶ Half-year 2020 results released with full roadshow but no face to face meetings

September

- ▶ Announced disposal of Scotland Domiciliary Care; investor calls upon request

October

- ▶ Update calls with existing and prospective shareholders upon request

November

- ▶ Announce offer for Terraquest; shareholder conference call held – one-to-one calls upon request

December

- ▶ Trading update; shareholder calls available upon request

Division of responsibilities

Roles and responsibilities

Role	Responsibilities include:
Chairman Kieran Murphy	<ul style="list-style-type: none"> ▶ Promoting a culture of challenge, debate, openness, support and mutual respect. ▶ Leadership of the Board, setting its agenda and ensuring its effectiveness through effective information flow and time management. ▶ Ensuring that Directors contribute effectively and allocate sufficient time to the Company to do so. ▶ Ensuring that the Board listens to the views of shareholders, workforce, customers and other stakeholders. ▶ Ensuring that the Board demonstrates culture, values and behaviours of the Group. ▶ Ensuring that the Board determines the nature and extent of risk and reward in strategy execution. ▶ Ensuring effective Board evaluation.
Senior independent director Julia Unwin	<ul style="list-style-type: none"> ▶ Leading the annual performance evaluation of the Chairman. ▶ Providing a sounding board for the Chairman. ▶ Available to shareholders as a channel for them to raise Board level issues.
Independent non-executive directors Roy Irwin Geraint Davies Jim Clarke Chris Loughlin	<ul style="list-style-type: none"> ▶ Promoting the highest standards of integrity, probity and corporate governance throughout the Group. ▶ Constructively challenging decisions proposed by the Executive Directors. ▶ Assisting in developing proposals on strategy. ▶ Contributing to the performance evaluation of the Chairman. ▶ Briefing the Board on decisions made and key issues from each Committee Chair.
Employee director Claire Gibbard Amanda Hillerby	<ul style="list-style-type: none"> ▶ Promoting the highest standards of integrity and probity. ▶ Assisting in developing proposals on strategy. ▶ Assisting the Board to receive full, open and honest insight and views from its workforce on how strategic initiatives are being implemented. ▶ Helping to provide the wider workforce with a better understanding of how the Board operates.
Executive directors David Miles Chief Executive Officer	<ul style="list-style-type: none"> ▶ Managing the day-to-day running of the business in line with the strategy and objectives set by the Board. ▶ Ensuring the Board is supplied with sufficient and appropriate information on a timely basis. ▶ Leading the business within the scope set by the Board. ▶ Developing strategy and setting objectives to meet the Group strategy approved by the Board. ▶ Managing the Group's operations to ensure they meet the risk appetite set by the Board.
Andrew Smith Chief Finance Officer	<ul style="list-style-type: none"> ▶ Supporting the Chief Executive Officer in developing strategy and meeting objectives. ▶ Establishing strong control processes. ▶ Managing the treasury activities in accordance with the credit risk appetite set by the Board. ▶ Supporting the Chief Executive Officer with investor relations. ▶ Leading the development of talent within the finance function.
Alan Long Executive Director	<ul style="list-style-type: none"> ▶ Supporting the Chief Executive Officer in developing strategy and meeting objectives. ▶ Supporting the Chief Executive Officer in managing external communications and investor relations. ▶ Setting the Group social value policies and procedures. ▶ Leading the operational leadership and development function of the Group.

Division of responsibilities continued

Roles and responsibilities continued

Attendance

Name	Board Meeting*	Nominations Committee	Audit and Risk Committee	Remuneration Committee
Kieran Murphy	10/10	3/3	–	5/5
Julia Unwin	10/10	3/3	–	5/5
Roy Irwin	10/10	3/3	–	5/5
Geraint Davies	9/10	3/3	8/8	–
Jim Clarke	10/10	2/2	8/8	–
Chris Loughlin	10/10	2/2	8/8	5/5
Claire Gibbard	4/4	–	–	–
David Miles	10/10	–	–	–
Andrew Smith	10/10	–	–	–
Alan Long	10/10	–	–	–

* In addition to the scheduled full Board meetings, a further 17 meetings were held, predominantly relating to Covid-19, with particular focus upon better understanding the operational challenges and liquidity. These meetings were typically arranged at short notice but attendance was high, reflecting the additional input required at that time.

Independence and conflicts of interest

The Board reviews the independence of its Non-Executive Directors as part of the annual evaluation process. The Nominations Committee also considers this as part of its ongoing review of the board composition. The Board considered all Non-Executive Directors to be independent.

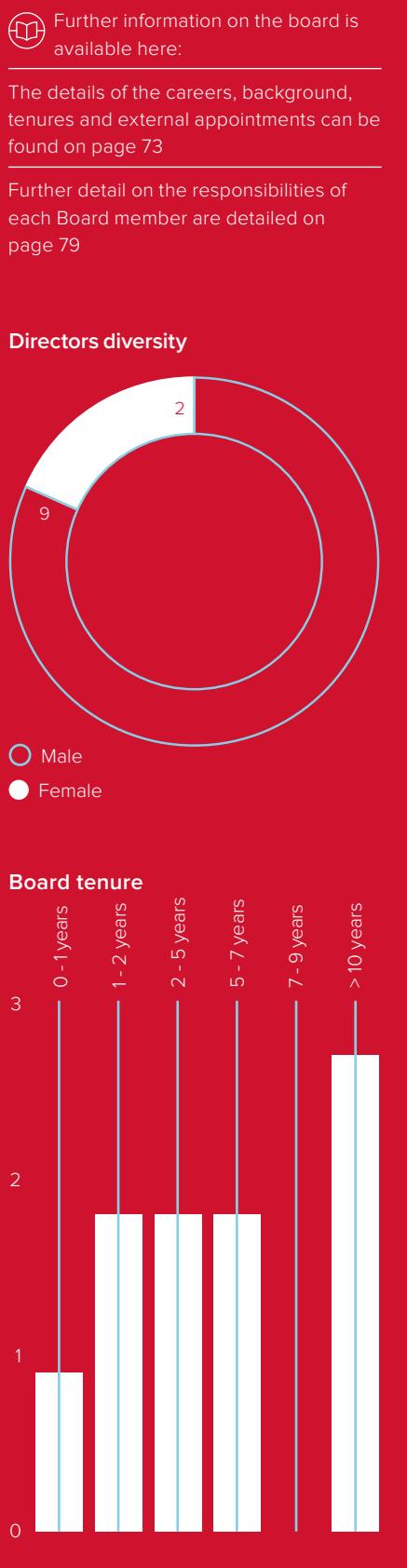
The Board operates a policy to identify and manage situations declared by Directors in which they or their connected persons have, or may have, an actual or potential conflict of interest with the Company. No Director conflict situation currently exists or existed at any time during the year.

Indemnifications of Directors

In accordance with our Articles of Association and to the extent permitted by the laws of England and Wales, Directors are granted an indemnity from the Company in respect of liabilities incurred as a result of their position in office. However, our indemnity does not cover Directors or officers in the event of being proven of acting dishonestly or fraudulently.

Composition, succession and evaluation

Board composition



Our Board is comprised of:

- ▶ the Chairman
- ▶ five independent Non-Executive Directors
- ▶ one non-independent Employee Nominated Director
- ▶ three Executive Directors

The Board adopts the principles of the Code regarding tenure of the Board. In accordance with Code requirements, each of the Directors offer themselves for re-election annually. The Board considers that each of the Non-Executive Directors continues to be effective and that they are considered to demonstrate appropriate commitment to the role.

Directors skills and experiences

An effective Board requires a wide range of views, skills and experience in order to work with and provide challenges to the management. Each Director should have demonstrable experience, skills and knowledge which enhance Board effectiveness and will complement those of other members. The balance of capabilities within the Board is kept under review to ensure that the Board is equipped to provide effective leadership. In addition, each Director should demonstrate a familiarity and respect for the Group's core values.

The Board and Nominations Committee have considered Board succession during the course of the year and into 2021. The outcome of their deliberation is set out within the Nominations Committee report.

Board performance evaluation

The Chairman regularly discusses with each Non-Executive Director their contribution to the Company's overall success. The Senior Independent Director provides feedback to the Chairman on his performance, having canvassed opinion from the other Directors and more widely. It was the intention of the Chairman to undertake an externally facilitated review in 2020 given that the last independent review was carried out in 2017 and, since that time, the Board composition has changed considerably. However, given the short-term Covid-19 challenges which diverted the attention of the Board, the external review has been rescheduled to 2021.

All Directors have access to the Company Secretary, who is responsible for all Board compliance requirements, to ensure they are updated on all legislative developments. In addition to this, the Company Secretary ensures that the Board agenda and papers are provided usually at least three days in advance of the meeting. Minutes and actions from previous meetings are distributed on a timely basis. As per the Board policies and procedures, any Non-Executive Director may, on request through the Company Secretary or the Chairman, meet with any member of staff in the Group. Non-Executive Directors are able to request the support of an independent adviser from the Company Secretary.

Directors' commitment is reviewed as part of the Board and director evaluation process and the Nominations Committee keeps this under close review. The Non-Executive Directors are expected to devote as much time and skills as are reasonably required for the performance of their duties. The Board remains satisfied that all of the Directors devote sufficient time. This has been especially demonstrated during the Covid-19 crisis where each Non-Executive Director made themselves available at short notice. Between mid-March and mid-July 2020, the Board met 13 times, with full attendance.

If a Non-Executive Director wishes to take an additional external appointment, they are required to seek permission of the Board. The Board will take into consideration the time commitment required by the Non-Executive Director in giving any permission.

K Murphy

Chairman

12 May 2021

Composition, succession and evaluation continued

Report of the Nomination Committee

Kieran Murphy
Nomination Committee
Chairman



Meeting attendance

K Murphy	3/3
J Unwin	3/3
R Irwin	3/3
G Davies	3/3
J Clarke	2/2
C Loughlin	2/2

This report sets out the key matters which were addressed by the Committee in 2020.

The main focus of the Committee in 2020 was to complete the process of rebalancing and rightsizing the Board which began in 2019. Having introduced two new non-executive directors with extensive private sector experience in financial and general management respectively, it was necessary to reduce the overall size of the non-executive director group and focus on skills and expertise required at board level. Liz Corrado left the Board at the very end of 2019. Jason Burt stood down from the Board with effect from the end of March 2020. The Board is grateful to both for their contribution while directors. In the case of Jason Burt, the company was pleased to retain him in a new role where he is advising on health, safety and environmental matters. In that role, he is invited to attend certain Audit and Risk Committee meetings. He will also be invited to attend Board meetings from time to time to ensure that the Board is able directly to assess the Group's development in these areas.

Amanda Hillerby, the Company's first employee Director, left the Group consequent on the disposal of the England and Wales domiciliary care business and accordingly stood down from the Board. The Company ran an internal process to seek applicants to succeed her and two individuals, both female, were selected to be interviewed by a panel consisting of the Chairman and two members of the nominations committee. That panel recommended that Claire Gibbard be asked to join the Board as the new Employee Director and she took her place in July 2021. Claire has since undergone an induction process to familiarise herself with Board processes. From 2021, Claire will also be invited to attend (not as a member) meetings of the audit and risk and the remuneration committees so that she can acquire a full understanding of the work of the Board and its committees.

During the summer, the committee was strengthened by the appointment of both Jim Clarke and Chris Loughlin to serve on it alongside the existing membership.

At the start of 2020, it was the committee's intention to put in place a formal and independent evaluation of the effectiveness the Board and its various committees during the course of the year. In the light of the Covid 19 outbreak and the substantially increased frequency of Board meetings during the spring and summer, it was decided to delay this process. This will be an area of focus for the Committee in 2021.

During the latter part of 2020 and into 2021, the Committee has given careful consideration to succession planning for the Board and senior management. There is a succession plan in place for all of the posts in the senior executive team.

Roy Irwin and Geraint Davies have indicated their intention to retire from the Board as non-executive directors and will not offer themselves for re-election at the AGM. Both colleagues have given exemplary service to the Board and the company over a number of years. They have also served with distinction as chairmen respectively of the remuneration and audit committees.

The retirement of Roy and Geraint necessitates a number of changes in non-executive responsibilities. Chris Loughlin will become the chairman of the Remuneration Committee, on which he has served since his appointment to the Board in September 2019. Jim Clarke will become chairman of the Audit Committee, on which he has served since his appointment to the Board in July 2019. Jim will join the Remuneration Committee as a member while Julia Unwin will join the Audit Committee as a member. Julian Unwin has indicated her wish to stand down as Senior Independent Director after three years in the role and Chris Loughlin has agreed to take on that responsibility.

During the last 18 months, the company has taken a number of steps to simplify and streamline its activities. Against that background, the Committee considered that there was a good case for reducing the overall size of the Board, keeping in mind the need to remain compliant with the Code. Accordingly, it is intended to appoint one new independent non-executive director and a search will be commenced shortly to identify a suitable candidate.

Role of the Committee

The Nomination Committee's responsibilities include:

- ▶ keeping under review the composition of the Board and succession to it, and succession planning for senior management positions within the Group;
- ▶ making recommendations to the Board concerning appointments to the Board, whether of Executive or Non-Executive Directors, having regard to the balance of skills, knowledge, experience and diversity of the Board;
- ▶ reviewing the length of service of Non-Executive Directors to ensure a progressive refreshing of the Board, whilst retaining the correct level of experience;
- ▶ making recommendations to the Board concerning the re-appointment of any Non-Executive Director at the conclusion of his/her specified term and the re-election of any Director by shareholders under the retirement provisions of the Company's Articles of Association;
- ▶ managing a formal, rigorous and transparent procedure for any appointments of new Directors to the Board;
- ▶ prior to the appointment of a Director, requiring that the proposed appointee discloses any other business interests that may result in a conflict of interest and reports any future business interests that could result in a conflict of interest; and
- ▶ ensuring that, on appointment to the Board, Non-Executive Directors receive a formal letter of appointment setting out clearly what is expected of them in terms of time commitment, Committee service and involvement outside Board meetings.

Activities during the year

- ▶ Considered succession issues within the Board structure
- ▶ Continued dialogue with major shareholders, including their views on the Board
- ▶ Carried out a rigorous appointment process to appoint a new Employee Director

The terms and conditions of each of the non-executive directors are made available on request of the Company Secretary, and are available for inspection at the AGM.

K Murphy

Nomination Committee Chairman

12 May 2021

Audit, risk and internal controls

Report of the Audit Committee

G Davies
Audit Committee
Chairman



Meeting attendance

G Davies	8/8
J Clarke	8/8
C Loughlin	8/8

This report sets out how the Committee has fulfilled its responsibilities during the year and in relation to financial reporting matters, the significant issues that were considered and how they were addressed.

As Chairman of the Audit Committee, I am pleased to present the summary of the work of the Committee over the last twelve months.

As detailed later within this report, the Committee tendered the external auditor engagement following a competitive tender process and appointed Ernst & Young LLP ("EY") as the new external auditor. The Committee has overseen the transition from Grant Thornton to EY, placing emphasis on ensuring a seamless handover and ensuring that additional management time was allowed to ensure EY could quickly increase its understanding of the Group. The Committee has been pleased with the first year of the new auditor, and recognises that it has brought fresh challenge to the business.

The Committee has reviewed the significant financial reporting matters and judgements identified by the management team and EY through the audit process, and the approach to addressing these is detailed on pages 116 to 120 of this report.

With the advent of the Covid-19 pandemic, and its impact on the Group, the Committee was very mindful that a very detailed assessment was required to assure the Board that the Group maintained sufficient liquidity and remained in compliance with the Group's financial covenants. The Committee reviewed a range of forecasts produced by management and reviewed the detailed assumptions behind the most severe downside scenario. The Committee also considered the impact of instigated and proposed mitigating actions. The Executive Directors continued to prepare a revised assessment over the course of the year and the Committee monitored this closely throughout both the first and second lockdowns and as part of the Reporting Accountant requirements in support of the Class 1 disposal of the Terraquest Group.

The last year has seen a number of challenges for the Compliance Committee, most notably the need to maintain the safety of our people, customers and contractors by ensuring Covid-19 secure places of work and systems of operation were introduced and maintained

across the Group's various activities. The developing nature of the pandemic and the rapidly expanding range of safety guidance issued in response required close monitoring and careful consideration regarding its implementation, particularly in relation to our higher risk services, such as Extra Care and asylum support.

In relation to risk management and internal controls, the Board and Audit Committee are mindful of the importance of improving both control and output in this area. During 2019, the Board took the decision to strengthen the Internal Audit Function by co-sourcing with a major provider, KPMG. The work carried out during 2020 is detailed within this report. The co-sourcing between the internal Mears team and KPMG has delivered a high-quality output and excellent value, allowing KPMG to bring on ad hoc basis specialists rather than adding full time employment for what are mainly 'task and finish' projects. The overall lead for our internal audit work continues to sit with KPMG.

Our regular programme of meetings and discussions, supported by our interactions with the Company's management, external auditors and internal auditors, and the quality of the reports and information provided to us, enable the Committee members to effectively discharge their duties and responsibilities.

How the audit committee operates

The Committee provides independent review and monitoring of the risk management and control procedures within the Group. Each Committee member is independent and has broad commercial experience. Geraint Davies is a Chartered Accountant and previously Audit partner at Grant Thornton UK. Jim Clarke is a Chartered Accountant and has significant recent and relevant financial experience, most recently at Countrywide as Group CFO. The final committee member, Chris Loughlin has held a number of CEO and COO roles within large quoted entities and brings broader, more operationally focussed commercial expertise.

During the year, the Committee held eleven meetings. With the exception of the Audit Meeting held in relation to the new external auditor appointment, these meetings were also attended by the Group Chief Executive Officer, the Chief Finance Officer and the Chairman. The internal and external auditors were invited to all meetings. The Company Secretary acts as secretary to the Committee.

The Audit Committee Chairman meets with the external auditor and lead Internal auditor regularly throughout the year.

Compliance committee

In addition, the Audit Committee has a very active sub-committee, being the Compliance Committee. This reflects the significant focus that the Group gives to dealing with health, safety and environmental risks. The Compliance Committee is a sub-committee of the Audit Committee and is chaired by Jason Burt, the Group Director of Health, Safety and Compliance, a former specialist health and safety lawyer. He has an extensive detailed working knowledge of the issues which can adversely impact the efficiency of health, safety and compliance governance systems and cause and drive regulatory prosecutions and employers' and public liability claims. The extent to which the full integration of health, safety and environmental risks is now embedded in the governance structures of the Group is highlighted by the members of the Compliance Committee who include the Group's Chief Executive Officer, Health and Safety Director and internal Health and Safety legal adviser. Others are called upon to attend as required.

The Committee's terms of reference are available on the Company's website and on request from the Company Secretary.

Financial performance

- ▶ Reviewed the basis of preparation of the financial Statements as a Going Concern and the long-term viability statement
- ▶ Reviewed and discussed reports from the CFO on the Financial Statements and considered the significant accounting judgements or where there is estimation uncertainty. Considered reports from the External Auditor in respect of the suitability of the accounting policies and the integrity of the financial reporting.
- ▶ Reviewed the 2020 Annual Report and Accounts and provided a recommendation to the Board that, as a whole, they complied with the 2018 Code principle to be fair, balanced and understandable and provide the information necessary for shareholders to assess the Company's position, performance, business model and strategy

Risk management

- ▶ Received reports from the Chair of Compliance Committee
- ▶ Reviewed and approved the Group's risk register
- ▶ Reviewed and validated the effectiveness of the Group's system of internal controls
- ▶ Monitored fraud reporting and incidents of whistleblowing
- ▶ Oversight and monitoring of the Group's compliance with the Bribery Act

Main activities of the Committee during the year

Internal audit

- ▶ Reviewed and monitored progress against 2020 Internal audit plan
- ▶ Reviewed the quality and effectiveness of the outsourced arrangement
- ▶ Reviewed the Internal audit Plan for 2021

External auditor

- ▶ External audit engagement tender process
- ▶ Agreed the audit fee for the year ended 31 December 2020
- ▶ Reviewed the proposed audit plan for the 2020 statutory audit

Audit, risk and internal controls continued

Report of the Audit Committee continued

We considered the aspects of the financial statements that required significant accounting judgements or where there is estimation uncertainty. These are explained in greater detail within the notes to the Financial Statements. The Audit Committee received detailed reports from the CFO and the External Auditor on these areas and other matters which they believed should be drawn to the attention of the Committee.

The Committee discussed the range of possible treatments both with management and with the External Auditor, confirming that the judgements made by the management were robust and supportable. For all the significant issues detailed below, it was concluded that the treatment adopted was the most appropriate.

Significant issue	Read more as to how this key issue was addressed in the financial statements
Lease accounting	<p>IFRS 16 was adopted with effect from 1 January 2019 and as detailed in last years' report, has proved a difficult standard to implement and one which has required significant changes to the systems and day to day processes.</p> <p>Under IFRS 16, a lessee will recognise its right to use a leased asset along with a lease liability representing its obligation to make lease payments. On inception of a new lease, a right of use asset and lease obligation is measured at the present value of the future lease payments discounted using the Group's incremental borrowing rate. The depreciation cost of the newly recognised 'right of use asset' will be charged to the profit within cost of sales or administrative costs, whilst the interest cost of the newly recognised liability will be charged to net finance costs. On the basis that depreciation is required to be charged on a straight line basis, whilst interest is charged on a reducing balance basis, this results in a higher overall charge being applied to the income statement in the early years of a lease with this impact reversing over the later years. The profit impact over the life of a lease is neutral and IFRS 16 has no impact on pre-tax cashflows.</p> <p>Lease accounting is critical to Mears given the Group holds more than 15,000 leases across its portfolio of residential properties, offices, and vehicles. The most significant and complex category relates to the Group's portfolio of residential properties which comprises approximately 10,500 leases; whilst the Group endeavours to standardise the form of leases, operational demands dictate that many leases have specific wording to address the specific operational need and also to manage the associated operational and financial risks. The Group's suppliers of residential properties, being the property owners, will similarly have their own requirements. As such, each residential property leases requires individual assessment and the Group is required to make key judgements which include:</p> <ul style="list-style-type: none"> ▶ the identification of a lease ▶ assessing the right to direct the use of the asset ▶ determining the lease term ▶ the assessment as to the level of future lease payments including variable and fixed elements <p>The Committee challenged management in respect of the processes and controls that were in place throughout the year in order to ensure the completeness of the right of use asset and lease obligations. The Committee recognised this to be a high- risk area given the high number of new leases being inceptioned and the complexities of IFRS 16.</p> <p>The Committee has reviewed the assumptions and key judgements provided by Management, including the additional detail provided, resulting from the extensive review and reassessment of the process in respect of lease identification.</p> <p>The committee recognise that Lease accounting is very significant to Mears and is a key area for stakeholders to fully understand. Detailed analysis has been included within the Finance Review section of the Strategic Report, providing additional granularity in respect of the Group's residential property leases, highlighting the operational risks and contractual obligations that need to be managed and the key factors which are considered to assess the correct accounting treatment, in particular whether the arrangements fall under the definition of a lease as laid down by IFRS 16.</p> <p>The committee took comfort from the external expert report in arriving at the pro-forma credit rating and yield curves. The Committee reviewed the methodology for assessing the Group's incremental borrowing rate across a range of maturities.</p> <p>The completeness of the lease obligation is identified as a key audit area and EY have provided further detail as to how this matter was addressed during their audit work on page 116.</p>

Significant issue	Read more as to how this key issue was addressed in the financial statements	
Lease accounting (continued)	<p>The most typical challenges encountered, and which form the key judgements are:</p> <ul style="list-style-type: none"> ▶ where the lessor has a right of substitution meaning that the lessor can swap one property for another without Mears approval. Under the rules of IFRS 16, Mears does not control an identifiable asset, and there is no right of use asset or lease obligation ▶ where the lease contains a one-way no-fault break in Mears' favour, the Group measures the obligation based on the Group's best estimate of its future intentions ▶ where Mears does not in practice have the right to control the use of the asset and the key decision-making rights are retained by the supplier ▶ where a wider agreement for a supply of services includes a lease component which meets the definition of a lease under IFRS 16 ▶ the assessment of the fixed lease payments where the lease obligation to the landlord is based on a pass-through arrangement where Mears only make lease payments to the owner to the extent that the property is occupied and to the extent that rents are received from the tenant ▶ the calculation of the appropriate discount rate utilising yield curve at the mid-point between BBB and BB rated GBP corporate bond yields for a range of maturities 	
Prior year adjustment	<p>During the year, the Group revisited the assumptions made at the time of the adoption of IFRS 16, and its assessment of the right of use asset and lease obligations as at transition and at 31 December 2019. The work previously carried out at transition was significant and this was impacted further through the mobilisation of the AASC contract during the final quarter of 2019 which resulted in an additional 5,000 leases.</p> <p>Several errors and omissions were identified by management and EY impacting on the carrying values reported within the 2019 comparatives. These errors demonstrate a significant deficiency in the IFRS 16 control environment. Procedures are now in place to ensure that the finance team has appropriate support and resource to improve the control environment in this area. One particularly significant lease type which results in a significant reduction in the right of use asset and lease obligation reported in 2019 relates to the Group's 'More Homes' homelessness solution whereby the Group and its Local Authority partner acquire properties and utilising a leasing arrangement make these properties available to service users nominated by the Local Authority partner. Mears has no right to direct the use of the asset and the Local Authority partner operates the asset in a manner that it determines. Mears participation is restricted to delivering tenancy management and maintenance services. During 2019, this leasing arrangement was incorrectly identified as a lease within the definition of IFRS 16. This treatment has been reassessed during 2020, and the Directors recognise that the previous treatment was incorrect.</p>	<p>The Committee has reviewed the assumptions and key judgements provided by Management, including the additional detail provided, resulting from the extensive review and reassessment of the process in respect of lease identification.</p> <p>The Committee challenged management in respect of the processes and controls that were in place throughout the year in order to ensure the completeness of the right of use asset and lease obligations. The Committee recognised this to be a high-risk area given the high number of new leases being inceptioned and the complexities of IFRS 16.</p> <p>The Committee took additional comfort from the work of the external auditors which undertook detailed testing of the assumptions and the complex models supporting the carrying values reported in the Balance Sheet as at December 2020, December 2019 and at 1 January 2019, being the date of transition.</p> <p>The completeness of the lease obligation is identified as a key audit area and EY have provided further detail as to how this matter was addressed during their audit work on page 116.</p> <p>Further explanation as to the impact of the Prior Year Adjustment is detailed in note 33 to the Financial Statements.</p>

Audit, risk and internal controls continued

Report of the Audit Committee continued

Significant issue	Read more as to how this key issue was addressed in the financial statements	
Determination of the amount of the Group's retirement benefit obligations	<p>At 31 December 2020, the Group reported a net retirement benefit obligation of £8m, being the difference between the fair value of the scheme assets less the present value of the benefits expected to be paid to members of the schemes. This assessment requires an assumption to be made in respect of mortality rates and future inflation rates which will result in an increase in future benefits received by members. This also requires an appropriate discount rate in order to calculate the present value of these future obligations for the future payments. Where the Group has a contractual right to recover the costs of making good any deficit pension scheme, the fair value of that asset has been recognised and disclosed.</p>	<p>The Committee reviewed the key assumptions proposed by management, notably assumptions in respect of discount rate, RPI, CPI and future salary increases which are detailed in note 29 of the financial statements.</p>
Goodwill impairment	<p>At 31 December 2020, the Group reported goodwill with a carrying value of £119m. For the purposes of assessing impairment, management identified two separately identifiable cash flows which are termed as cash-generating units (CGUs). The two CGUs identified is the continuing Care activities (referred to as 'Housing with Care') and the Group's other Housing activities. Determining whether goodwill is impaired requires an estimate of the value in use of each of the CGUs to which goodwill has been allocated. The value-in-use calculation involves an estimate of the future cash flows of the CGU using the current one-year budget, extrapolated for five years to December 2025, requiring a medium term growth assumption and a general terminal growth rate, and an assessment of an appropriate discount rate to calculate present values. Whilst the Committee took comfort from the fact that there was significant headroom when reviewing any impairment in the prior year, the Committee were mindful of the impact of Covid-19 on carrying values.</p>	<p>The key assumptions, and a discussion of how they are established, as well as the sensitivity analysis are described in note 13 to the consolidated financial statements.</p>
Revenue Recognition	<p>Revenue is recognised in accordance with IFRS 15 'Revenue from Contracts with Customers'. IFRS 15 provides a single, principles-based, five-step model to be applied to all sales contracts. It is based on the transfer of control of goods and services to customers. The accounting policy within note 2 sets out the principal types of contract and how the revenue is recognised in accordance with IFRS 15.</p> <p>Determining future contract profitability requires estimates of future revenues, costs to complete, stage of completion of certain contracts and the recovery of work in progress, mobilisation costs and contract assets. Each contract is treated on its merits and subject to a regular review of the revenue and costs to complete that contract. In making these assessments there is a degree of inherent uncertainty. The Group utilises the appropriate expertise in determining these estimates and has well-established internal controls to assess and review the expected outcome.</p>	<p>The Audit Committee addressed this area of judgement in the following ways:</p> <ul style="list-style-type: none"> ▶ The Committee reviewed the key judgements report prepared by management which provided a detailed explanation in respect of the valuation of unbilled works and the recognition of revenues. ▶ The Committee took comfort from the contract management system which is central in generating the valuation of works (both billed and unbilled) and the integrated process that follows to ensure an accurate cut-off so that revenue is appropriately matched to cost. EY carried out substantive testing of the amounts recoverable on contracts, adopting a blend of risk-based and random sampling approaches to testing, and provided detailed feedback to the Committee in this area.

Significant issue	Read more as to how this key issue was addressed in the financial statements
Disposal accounting – assessment of the fair value of contingent consideration	<p>During the year, the Group completed the disposal of its Planning Solutions business, with completion in December 2020. The disposal of the planning solutions business ('the TerraQuest group') was completed in December 2020. The proceeds from this disposal were £56.9m in cash, £3.2m in loan notes, £0.1m of shares, representing a 6.16% holding in the disposed business and a maximum of £10.0m of contingent consideration payable in April 2022. The fair value of the contingent consideration was estimated as £5.4m based on the terms of the sale agreement, the expected future profitability of the TerraQuest Group on which the consideration will be calculated, and adjusted to reflect the time value of money.</p>
	<p>The Committee reviewed the terms of the sale agreement and the expected future profitability of the TerraQuest group which was underpinned by the business plan prepared prior to the commencement of the sales process and updated for subsequent events. Given the materiality of the Terraquest transaction to the Group, all Committee members already held a high level of understanding given the significant involvement of all Board members throughout the sales process.</p> <p>The Committee utilised financial measures provided by an external valuation expert in support of the Group's goodwill impairment as a reasonable proxy for the discount rate to be applied to the fair value of the contingent consideration.</p>
Compliance Committee activities	<p>The primary focus of the Compliance Committee during 2020 was directed towards:</p>
<ul style="list-style-type: none"> ▶ Monitoring and review of the Group's policies in relation to health, safety and environmental (HSE) matters; ▶ Review of HSE risks and risk assessments on the Group risk register and mitigation actions and controls related thereto, including subcontractor controls and related procurement; ▶ Providing an operational focal point and report for KPMG, the Group's independent internal auditors; ▶ Considering any other significant HSE matters including emerging risks and unforeseen risks as they arose. 	<p>The Group responded and performed very well, with reports of positive cases linked to our activities being relatively low.</p> <p>The Compliance Committee also focussed upon the activities of Mears Living, the Group's Registered Provider, overseeing the development and implementation of an enhanced system of safety and compliance management to enable it to meet the challenges posed by forthcoming changes in legislation.</p> <p>The Group's Asylum Accommodation and Support Contract was under significant pressure, and the Committee assisted the frontline teams to maintain compliance and implement enhanced governance systems linked to property securement and maintenance, in response to higher than expected levels of services users.</p>
<p>The Committee also provides the Board with the assurance that the risk management and internal controls systems as a whole, including strategic, financial, operational, and compliance controls, are sufficiently robust to mitigate the principal and emerging risks that may impact the Company.</p>	<p>The system of internal controls is designed to manage rather than eliminate the risk of failure to achieve business objectives and can only provide reasonable, but not absolute, assurance against material misstatement or loss. It includes all controls including financial, operational and compliance controls and risk management procedures. These include health and safety, people, legal compliance, quality assurance, insurance and security, and reputational, social, ethical and environmental risks.</p>
<p>The last year has seen a number of challenges for the Compliance Committee, most notably the need to maintain the safety of our people, customers and contractors by ensuring Covid-19 secure places of work and systems of operation were introduced and maintained across the Group's various activities. The developing nature of the pandemic and the rapidly expanding range of safety guidance issued in response required close monitoring and careful consideration regarding its implementation, particularly in relation to our higher risk services, such as care and asylum support.</p>	<p>Internal control and risk management</p> <p>The Board is responsible for establishing the Group's overall risk appetite and ensuring that the Group has in place an adequate system of internal controls. However, in accordance with the requirements of the Financial Reporting Council's Guidance on Risk Management, Internal Control and Related Financial and Business Reporting, the responsibility of monitoring and reviewing the integrity and effectiveness of the Group's overall systems of internal controls and risk management has been delegated to the Committee.</p>

Audit, risk and internal controls continued

Report of the Audit Committee continued

The Group's principal risk report captures and assesses the principal risks facing the Group. This forms part of the Group's framework for determining risk and risk appetite. This document is updated regularly and is considered at both Committee and Board level throughout the year. Further details are included within the Strategic report on pages 62 to 67.

The internal audit function carries out work across the Group, providing independent assurance, advice and insight to help the organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluating and improving the effectiveness of risk management, control and governance processes. In December 2019, the Audit and Risk Committee agreed the FY20 audit plan to be undertaken by the internal audit team. The audit plan coverage is based on risk, strategic priorities and consideration of the strength of the control environment. The internal audit function prepares audit reports and recommendations following each audit, and appropriate measures are then taken to ensure that all recommendations are implemented. Significant issues, if any, are raised at once. There were no such issues in 2020.

The Board has reviewed these procedures and considers them appropriate given the nature of the Group's operations. During the year a decision was taken to strengthen the review of internal controls by co-sourcing the internal audit provision with KPMG who were initially tasked to review the Group's risk management framework and mitigations in place. KPMG are now extending this piece of work to embedding the risk management framework and provide further assurance in respect of fraud risk management and the core controls in respect of the scheme of delegated authority. The Committee is pleased with the additional support provided by KPMG and has concluded that the system of internal controls and risk management is embedded into the operations of the Group and the actions taken to mitigate any weaknesses are carefully monitored.

The Board has adopted a scheme of delegated authority, defining financial and other authorisation limits and setting procedures for approving capital and investment expenditure. The Board also approves detailed annual budgets. It subsequently reviews performance against targets set forth in these plans and budgets.

Throughout the year, the Group's principal risks have been regularly reviewed by management to provide assurance on the robustness, integrity and effectiveness of the systems in place, including those that could threaten its business model, operations, future performance, solvency and liquidity.

The Board also seeks to ensure that a sound system of internal controls, based on the Group's policies, standards and procedures, is in place in all material associate and joint arrangement entities. Our systems of internal controls and risk management are designed to identify, mitigate and manage rather than eliminate business risk and can only ever provide reasonable, and not absolute, assurance against material financial misstatement or fraud.

The system of internal controls encompasses the culture, behaviours, organisation design, policies, standards, procedures, systems that, taken together, facilitate its effective and efficient operation. These internal controls are based on the 'three lines of defence' principles as detailed on pages 62 and 63 of the Strategic report.

The Company's risk-based internal audit programme for 2020 was considered and approved by the Committee in April 2020. This programme was developed further during the year to take into account the Company's principal risks and to identify where they primarily occur in the business; through discussions with the Committee and senior management; by recognising changes within the Group and the external environment; and with consideration to prior audit coverage. In approving the 2020 audit programme, the Committee considered the coverage of the principal risks by the proposed audits. It was agreed that primary focus for 2020 should be cover the following areas:

► **Risk Management:**

- Refresh of Principal risks, mitigating actions, and assurance review
- Fraud Risk register facilitation

► **Core Controls**

- Core controls spot checks
- Scheme of Delegated authority ('SODA')

► **Specific risk areas**

- Serious incident response
- Branch spot visits including business continuity and subcontractor management
- Information security

It has been a challenging year for the Group, not least in managing the impact of Covid-19. In addition, Management time has been taken up with corporate transactions in relation to Care and Terraquest. However pleasingly there has been good sponsorship of internal audit from Management and it is pleasing to observe the positive tone at the top in terms of openness to discussion of issues, agreement of action plans and a commitment to doing the right thing.

From a risk management perspective, 2020 has been a year for managing risks in the moment however, the improvements recommended to the risk management framework are being owned by the Compliance Committee, whose taking on an oversight role is enhancing the Group's governance and management of risk. A fraud risk register has been established this year which will assist in future oversight of this area of risk.

From the core controls work completed to date, no high priority gaps were identified however in a number of areas there is a need to ensure that processes are being followed and for control activity to be formally documented and evidenced. This is also important within the wider regulatory context where there are emerging requirements for public interest entities to have a documented control framework and in due course an articulated Audit & Assurance Policy. This will have focus during 2021.

There is a culture across the Group of active monitoring by the executive and senior management. Our focus this year was on management's oversight of branches. The challenging environment in 2020 meant that only two branch audits were completed and the themes identified during those audits will be developed further as more branch visits are completed and reported during 2021.

The 2021 programme was considered and approved by the Committee in December 2020 and performance against this plan will be reported in next years' Annual Report.

The Company has in place internal control and risk management systems in relation to the Company's financial reporting process and the Group's process for the preparation of the consolidated financial statements which are produced by the Group finance function, which is responsible for the review and compilation of reports and financial results from each of the operating subsidiaries in accordance with the Group reporting procedures. The consolidated financial statements are supported by detailed working papers. The Audit Committee is responsible for overseeing and monitoring these processes, which are designed to ensure that the Company complies with relevant regulatory reporting and filing requirements. As at the end of the period covered by this report, the Audit Committee, with the participation of the Chief Executive Officer and the Finance Director, evaluated the effectiveness of the design and operation of disclosure controls and procedures designed to ensure that information required to be disclosed in financial reports is recorded, processed, summarised and reported within specified time periods.

We have conducted an annual review of the effectiveness of our risk management system and internal control systems in accordance with the UK Corporate Governance Code. Part of this review involves regular review of our financial, operational and compliance controls, following which we report back to the Board on our work and findings as described above. This allowed us to provide positive assurance to the Board to assist it in making the statements that our risk management and internal control systems are effective, as required by the UK Corporate Governance Code.

External auditors

Following the AGM in June 2020 Grant Thornton confirmed that following a client portfolio review they would resign as auditor. The Committee then tendered the external audit engagement and after a detailed review of the independence of a number of possible candidates. The Committee identified and short-listed two new firms to tender. Each firm was provided meetings with key Executive and Non-Executive Directors and other key employees. Further information was provided in response to requests received and provided to both firms involved in the tender. Presentations were made to a panel comprising the Audit Committee. The proposals received were assessed against pre-determined criteria including audit approach, understanding of key audit issues, quality assurance, experience of the audit team, engagement with executive, transition planning, strength in depth in the firm and technological capability. The fee submission was not scored but an acceptable fee range had been set by the Committee prior to receipt of tenders and both bidders fell within that range. Following careful consideration, the Committee agreed that, across the criteria as a whole, EY had delivered the best proposal and therefore the Audit Committee recommended to the Board that EY be appointed as Auditor. The Board is proposing a resolution to the AGM to reappoint EY as external auditor for the year ending 31 December 2021.

The Senior Statutory Auditor, Paul Mapleston, is required to rotate after a maximum of five years, the year ending December 2024 being his last possible financial year.

The Committee expects that the next tender date will be no later than 2030 in accordance with the current regulation that requires a tender every 10 years.

Annually, the Committee reviews the external Auditor's audit plan and reviews and assesses information provided by them confirming their independence and objectivity within the context of applicable regulatory requirements and professional standards.

The Committee also reviews their effectiveness, which involves assessment of the Auditor by the Committee and key Executives; and confirmation that the Auditor meets minimum standards of qualification, independence, expertise, effectiveness and communication. These assessments are carried out prior to the Committee recommending to the Board that the external Auditor be proposed for reappointment at the Company's AGM.

External auditor independence and non-audit services

The Company has adopted a strict policy of prohibiting the external auditor from carrying out non-audit services, in order to safeguard audit objectivity and independence. The Committee is responsible for approval of all non-audit services provided by EY; however, this is considered to be in exceptional circumstances only. In such an exceptional event, the Audit Committee would approve only where the Company would be disadvantaged by engaging an alternative provider, for instance where EY possesses a detailed knowledge of the structure of the business or an understanding of the markets within which the Group operates. No non-audit services were provided by EY during 2020.

G Davies

Audit Committee Chairman

geraint.davies@mearsgroup.co.uk

12 May 2021

Remuneration

Report of the Remuneration Committee

R Irwin
Remuneration
Committee Chairman



Dear shareholders

I am pleased to present the Directors' Remuneration Report for the year ended 31 December 2020.

This report is made up of three parts:

- ▶ This Annual Statement where I set out details of the key decisions of the Remuneration Committee and the business context within which they were taken.
- ▶ An abridged version of the Director's Remuneration Policy which was approved by shareholders in June 2020.
- ▶ The Annual Report on Remuneration which sets out details of (i) remuneration earned by Directors and the link between company performance and pay in the year ended 31 December 2020 and (ii) how we intend to implement the Directors' Remuneration Policy in 2021.

There will be an advisory shareholder vote on the Annual Statement and the Annual Report on Remuneration at the 2021 AGM. Shareholders approved the current Directors' Remuneration Policy at the 2020 AGM and this is intended to apply for a three-year period up to the 2023 AGM.

Business Context

Earlier in this report you will have seen the outputs and outcomes for a year that no-one will forget as Government, businesses, communities and families have had to try and come to terms with the most virulent pandemic faced by the United Kingdom, and arguably the world, for a century.

Despite two nationwide lockdowns and an ongoing range of ever changing national and regional tiered restrictions the Group has performed admirably. In so doing positive relationships with clients have been maintained and the day-to-day safe delivery of essential services to customers, many of them vulnerable, has continued. Despite the obvious additional challenges this has brought to the business the health, safety and well-being of our workforce and our customers has remained paramount.

Against the backdrop of a rapidly changing situation, the Group took swift and prudent actions to ensure the safety and well-being of our staff.

The Group also acted quickly to protect cash flow and liquidity which included a cancellation of the final dividend and detailed consideration of whether or not there would be the need for taking advantage of central Government reliefs including the furlough scheme.

Meeting attendance

R Irwin	5/5
J Unwin	5/5
K Murphy	5/5
C Loughlin	5/5

Mears position within UK listed companies is unusual. Its client base is made up of local authorities, housing associations and Government departments. Almost all of its income comes from the public sector or entities close to it. In March 2020 Government issued advice through the Cabinet Office to all our clients (local authorities, housing associations and the Government itself) collectively termed "contracting authorities", under the national procurement framework advocating the maintenance of payment arrangements through the pandemic to reduce the demand for Furlough support from Government. Many, but not all, of the Group's clients adhered to this advice. Where clients, for various local reasons, did not maintain payments at the appropriate level the Group appropriately drew on the Furlough scheme – in effect substituting a public pound from one source for the absence of that pound, despite advice to the contrary, from another public service body.

Following on from decisions made in 2019 the Board has, despite the impact of COVID-19, continued to implement its strategic plans. The Group successfully exited the domiciliary care market in England and Wales in January 2020, as planned, followed by the exit from the Scottish domiciliary market, again as planned, in October 2020. Housing development activity has been re-focused to provide a contracting service to long-standing clients with the ongoing sale of developed assets.

In addition to these significant strategic actions we also sold a small but profitable Planning Solutions business ('Terraquest') during the second lockdown for a headline enterprise value of £72 million. This class one transaction – supported overwhelmingly by shareholders – has contributed to a significant reduction in the Group's average net debt going forward – a key and ongoing goal for the Group.

The implementation of these actions has re-enforced the Board's intention to be the UK's most respected and trusted provider of Housing solutions. This singular objective is the overarching focus of our strategic review which the Board is currently working to finalise.

Outcomes for 2020

Background

The variable pay outcomes for the previous financial year, 2019, were based on performance under the previous EIP scheme which formed part of the previous Directors' Remuneration Policy approved by shareholders in 2017. Under that policy and scheme, the EIP outcome for 2019 performance, as disclosed in last year's report, was 58% of the maximum, reflecting strong performance in ROCE, cash conversion, customer service and health and safety.

The Remuneration Committee was due to approve the EIP outcome in early 2020, but as a result of the onset of COVID-19, like many other companies, the publication of the Group's 2019 results was delayed beyond the original expected announcement date in late March 2020.

While excellent progress was made in mitigating the immediate financial impact of the operational changes to the business as a result of the pandemic, following the delay to the results publication the Remuneration Committee no longer felt it was appropriate to pay the 2019 EIP outcome, which was worth 58% of salary. The payout was therefore reduced from 58% of salary to zero for each executive director. As stated in last year's report, the Executive Team agreed with this decision.

This decision was in contrast to the large majority of December year end companies which did not reduce bonuses for the year ended 31 December 2019 on the basis that the performance year preceded the onset of the pandemic and due to most of these

companies determining bonuses and reporting these before the full impact of the pandemic became clear.

Annual bonus outcome

As set out in the business context section above, the Group made excellent progress in taking the necessary steps to address the challenges faced because of the pandemic. The Group also made strong progress against its key strategic objectives which were to refocus on core housing activities and significantly reduce indebtedness.

The 2020 annual bonus was based 40% on group operating profit, 30% on average daily net debt and 30% on strategic objectives relating to customers, employees and the generation of social value. These targets were set early in the year and were not adjusted at any point thereafter. The achievements against the targets were as follows:

► **Operating profit (40%)**

- the Group delivered an operating profit of £62.3m which was ahead of the maximum target of £58.4m

► **Average daily net debt (30%)**

- the average for the year of £97.3m meant the target was achieved as debt was lower than the maximum target

► **Employee engagement, customer and social value generated (30%)**

- the employee engagement measure was met in full while customer and social value generated metrics were partially achieved

Overall, the strong performance over the year resulted in a formulaic bonus outcome of 86.6% of the maximum. On balance, and taking into consideration the negative discretion applied by the Committee in respect of the 2019 annual bonus, the Committee considered all the outcomes carefully and concluded that reducing the bonus to zero for a second year in the circumstances did not represent a fair outcome.

The Committee has a history of exercising negative discretion, as evidenced by, for example, the reductions (to zero) made in each of the previous three performance years (2017-2019), despite a number of targets being met in respect of each of those years.

	Bonus targets achieved?	Negative Discretion applied?
2019	Yes, significantly	Yes, from 58% down to nil
2018	Yes, partial	Yes, down to nil
2017	Yes, partial	Yes, down to nil

The Committee has reviewed carefully the appropriateness of the outcomes for each of the respective measures and targets given the exogenous nature of the pandemic and its long-lasting impact on society and on our business. Specifically the Committee considered the sale of Terraquest and the impact of this significant and positive transaction had on the financial elements of the bonus.

On balance, we decided to reduce the operating profit outcome of the bonus from 40% of salary to nil. This reflects the one-off nature of Terraquest on profit and the impact of the pandemic on our various stakeholders.

The Terraquest transaction, which completed in December 2020 did not impact the outcome of the average daily net debt measure.

Therefore, the Remuneration Committee has determined that the formulaic bonus outcome for 2020 should be reduced from 86.6% to 46.6% of salary. The Remuneration Committee believes the resulting bonus is a fair outcome and recognises the resilient operational and financial performance of the business, the delivery of strategic goals in 2020 and the negative discretion applied by the Committee in respect of the 2019 bonus. In arriving at this conclusion, the Committee also took into account the following factors:

Support for Employees

- Enhanced the statutory furlough scheme to provide better financial support, particularly for lower paid staff. An enhanced sick pay scheme was introduced for those with COVID-related absence who previously only had a contractual entitlement to Statutory Sick Pay. Concerned that these measures did not cover all aspects of the impact of the pandemic a Hardship Scheme was also implemented.
- Recognised the outstanding efforts by staff to support colleagues and customers by introducing the "Mears Amazing People" and "Mears Amazing Manager" schemes to give full recognition of those going above and beyond.

Remuneration continued

Report of the Remuneration Committee continued

- ▶ Quickly supported remote working utilising our agile IT to swiftly embed new and safe approaches into daily practice. Training on Mental Health Awareness for Managers was stepped up as was the number of Mental Health First Aiders as staff felt the strain of different and often difficult times. Improved access to the Employee Assistance Programme was also granted.
- ▶ The early acquisition of Personal Protective Equipment (PPE) supplies ensured all front-line staff have had the appropriate protective gear. Throughout the pandemic the Group has been diligent in the recording of incidences of COVID, testing results and vaccines.
- ▶ Maintained high levels of Health and Safety for staff and customers.

Response to Clients and Customers

- ▶ Implemented new and more exacting measures for Customer Satisfaction backed up by the establishment of the Your Voice Independent Scrutiny Board which reports to the PLC Board.
- ▶ Achieved a very good level of customer satisfaction during an often challenging and sometimes confusing time..
- ▶ Kept the essential services of heating, hot water, electricity, gas safety and security as well as other emergency and essential repairs working for our clients and customers throughout the pandemic.
- ▶ Despite the practical difficulties kept our commitment to the generation of social value providing additional support to the Communities in which we work.

In accordance with the agreed policy one third of the bonus will be deferred in shares and the remainder, which should be paid in cash, will be withheld by the Company and released at an appropriate time in 2021, taking into account business recovery and the impact on our shareholders.

LTIP outcome

There were no long-term incentive awards capable of vesting for performance ending in 2020 under the EIP plan we previously operated. In addition, no long-term incentive awards were granted during the year and the first awards under the LTIP we adopted as part of the new Directors' Remuneration Policy at the 2020 AGM will be made in 2021.

Applying the Policy in 2021

Base salaries

The Committee has agreed that the Executive Team will have a 2% uplift in base salaries, in line with the workforce, from 1 April 2021. The Committee intends to review base salary positioning later in the year with any proposed increases disclosed in next year's report and applying from 1 April 2022.

Annual bonus 2021

Following on from the above the Committee have considered both the measures and targets for 2021. We have decided that all but one of the measures should remain the same for 2021 as was the case in 2020 with Operating Profit being replaced by Profit before Tax. The reason for this change is due to the introduction of IFRS 16 which distorts Operating Profit with Profit before Tax not affected to the same degree and therefore will be better understood by shareholders. Profit before Tax will represent 40% of the weighting within the bonus calculation for 2021.

As in 2020 the measures of Average Daily Net Debt (30%), Customer satisfaction (10%) Employee Engagement (10%) and the generation of Social Value (10%) will remain. The specific targets for each of these measures have also been set to reflect the achievements in 2020 and our goals for 2021 and will be reported in 2022.

LTIP 2021

The first awards under the LTIP adopted as part of the Directors' Remuneration Policy approved at the 2020 AGM will be made in 2021 at a level of 100% of salary to each of the executive directors. Following a comprehensive shareholder consultation with our largest shareholders and Investor Advice agencies the Committee concluded that the LTIP should consist of two measures these being Earnings per Share (EPS) growth and Total Shareholder Return (TSR) measured relative to the FTSE SmallCap (excluding investment trusts, financial services and natural resource companies). A soft ROCE underpin will apply to the EPS component and the Committee has the ability to reduce the vesting outcome in the event of windfall gains.

Pension

Pension contributions for the current executive directors for 2021 will be 15% of salary. This contribution level will reduce from 15% of salary to a level aligned with the workforce by 1 January 2023. The contribution level for any new executive director hires will be aligned with the workforce immediately on joining.

Sharesave 2021

The Board was delighted to support the grant of share options under the Save As You Earn plan which saw 850 employees apply to participate in the scheme, being around 15% of employees. This was a terrific opportunity to thank all our colleagues for their commitment, professionalism and exceptional performance in the most challenging circumstances, whilst also aligning their interests to those of our shareholders.

Conclusion

It has been a difficult and complicated year that has challenged us all and I am very grateful for the endeavour, respect and patience exercised by all of my colleagues in getting through such a turbulent time. The Group has performed well in the unforeseen emergency that is still with us today. The protection of our staff, of our customers, and our shareholders and other stakeholders, while re-shaping the business, have been our priorities.

I believe the Committee has put its mind to the matter of Executive Pay matters in a serious and thorough way and has been faithful to the policy that we consulted with our shareholders on in preparation for its adoption this time last year.

I am happy to receive feedback from the company's shareholders. Please get in touch with me direct, or via the Company Secretary, Ben Westran.

R Irwin

Remuneration Committee Chairman

roy.irwin@mearsgroup.co.uk

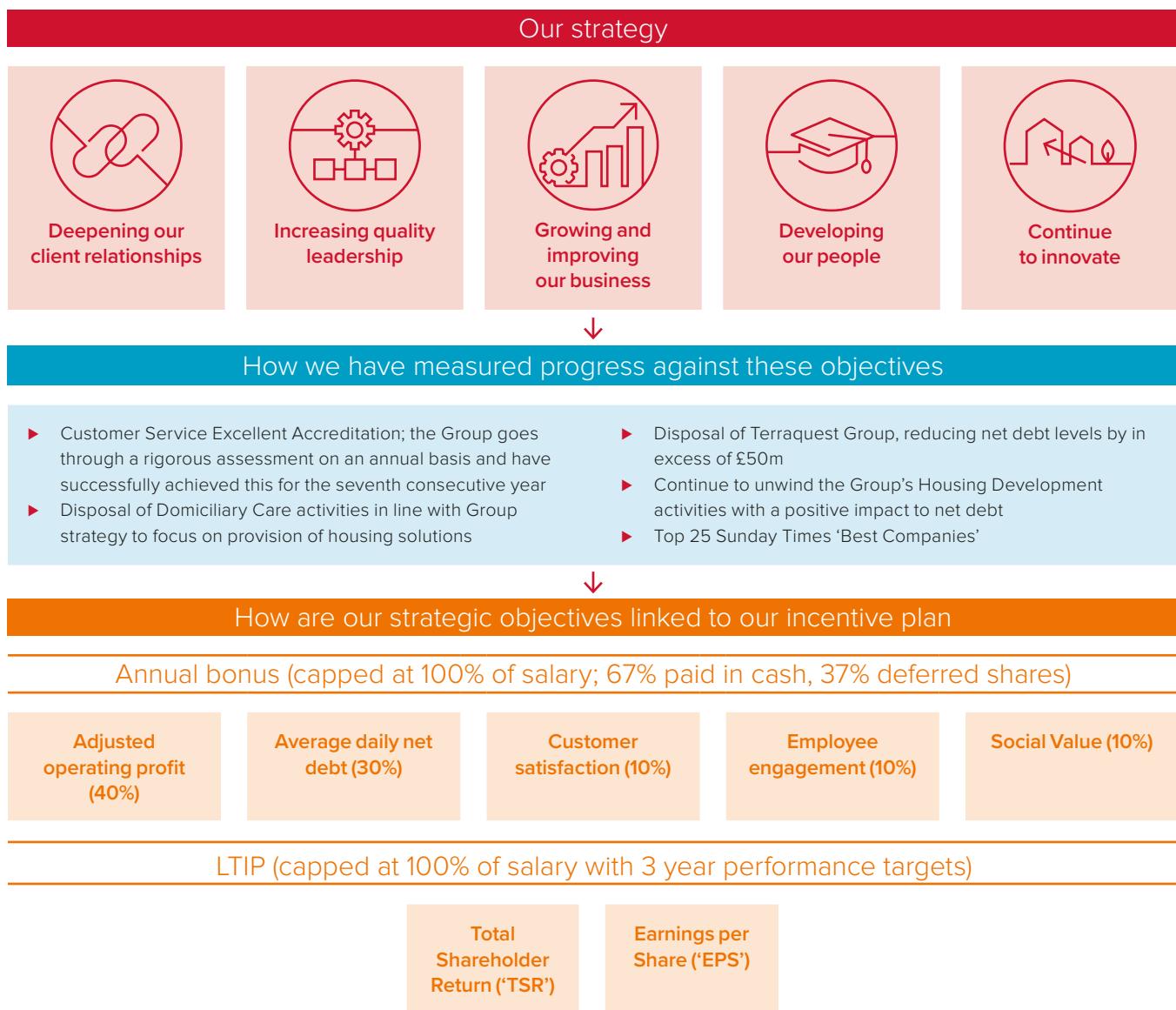
12 May 2021

Remuneration framework – at a glance

The following section sets out our remuneration framework, a summary of how our policy was applied in 2020 in the context of our business performance, and from page 106 details of how the Committee intends to implement the policy in 2021.

Strategic alignment of remuneration

The Committee believes it is important that, for Executive Directors and senior management, a significant proportion of the remuneration package should be performance-related, and the performance conditions applying to incentive arrangements should support the delivery of the Company's strategy. The following table sets out how the annual bonus scheme and LTIP reflect the Group's strategic priorities:



Remuneration continued

Report of the Remuneration Committee continued

Taking account of the UK Corporate Governance Code

In implementing our Policy during the course of 2020 and in planning for its implementation in 2021, we have been careful to take full account of the provisions of the Code and it will continue to be a key touchstone for the Committee. In summary, with regard to how we have sought to comply with the six factors outlined in Provision 40 of the Code, we believe the following are worthy of particular note:

- ▶ **Clarity** – the policy is well understood by our Directors and has been clearly articulated to shareholders and proxy voting agencies.
- ▶ **Simplicity** – the remuneration structure is simple and transparent and we have purposefully avoided any complex structures which have the potential to deliver unintended outcomes.
- ▶ **Risk** – our Policy and approach to target setting seek to discourage any inappropriate risk-taking. A balanced scorecard of financial and non-financial objectives applies to the annual bonus scheme and the targets are appropriately stretching, to mitigate the risk of inappropriate actions being taken. Malus and claw back provisions apply.
- ▶ **Predictability** – executives' incentive arrangements are subject to individual participation caps. An indication of the range of values in packages is provided in the reward scenario charts on page 99. Deferred bonus and LTIP awards provide alignment with the share price and their values will depend on share price at the time of vesting.
- ▶ **Proportionality** – there is a clear link between individual awards, delivery of strategy and our long-term performance.
- ▶ **Alignment to culture** – pay and policies cascade down the organisation and are fully aligned to Mears' culture.

Directors' remuneration policy – a summary

The Directors' Remuneration Policy was approved by shareholders at the 2020 Annual General Meeting and is intended to apply for a period of three years including the 2021 financial year. An abridged version of the Policy which sets out the key aspects is set out below (to include updated charts illustrating the application of remuneration policy in 2021) and the full original policy can be found in the 2019 annual report and on the company website.

Remuneration policy table

The table below sets out the key elements of the Policy for Executive Directors:

Objective and link to strategy	Operation	Maximum opportunity	Performance measures and assessment
Base salary The purpose of the base salary is to: <ul style="list-style-type: none"> ▶ help recruit and retain individuals of the necessary calibre to execute the business strategy; ▶ reflect the individual's experience, role and contribution within the Group; and ▶ ensure fair reward for 'doing the job'. 	<p>Salaries will be eligible for increases during the three-year period that the Remuneration Policy operates. The Committee reviews base salaries annually with any change typically effective from 1 April.</p> <p>The Committee will retain the discretion to increase an individual's salary where there is a significant difference between current levels and a market competitive rate. When determining base salaries and whether to increase levels the Committee will take the following into consideration:</p> <ul style="list-style-type: none"> ▶ the performance of the individual Executive Director; ▶ the individual Executive Director's experience and responsibilities; ▶ the impact on fixed costs of any increase; ▶ pay and conditions throughout the Group; and ▶ the economic environment. <p>When setting the salary levels for the Executive Directors, in addition to the factors summarised above, salary levels paid by companies of a similar size and complexity to Mears are taken into account.</p>	<p>The Committee is guided by the general increase for the broader employee population but may decide to award a lower increase for Executive Directors or indeed exceed this to recognise, for example, an increase in the scale, scope or responsibility of the role and/or to take into account relevant market movements.</p>	Not applicable.

Objective and link to strategy	Operation	Maximum opportunity	Performance measures and assessment
Pension	<p>The Company may contribute directly into an occupational pension scheme (an Executive Director's personal pension) or pay a salary supplement in lieu of pension. If appropriate, a salary sacrifice arrangement can apply. Only the base salary is pensionable.</p>	<p>The current Executive Directors receive a contribution of up to 15% of salary.</p> <p>Any new Executive Director appointments to the Board after 1 January 2020 will receive a pension contribution (in percentage of salary terms) in line with the prevailing contribution for the majority of the Mears workforce.</p>	Not applicable.
Annual bonus	<p>Bonus measures and targets are reviewed annually and any pay out is determined by the Committee after the end of the financial year, based on performance against targets set for the one-year financial period.</p> <p>Up to 67% of any bonus that becomes payable is paid in cash with the remainder deferred into shares for three years.</p> <p>Deferred bonus share awards typically vest subject to continued employment.</p> <p>Individuals may be able to receive a dividend equivalent payment on deferred bonus shares at the time of vesting equal to the value of dividends which would have accrued during the vesting period. The dividend equivalent payment may assume the reinvestment of dividends on a cumulative basis.</p> <p>In the event that there was (i) a material misstatement of the Company's results; (ii) a miscalculation or an assessment of any performance conditions that was based on incorrect information; (iii) misconduct on behalf of an individual; (iv) the occurrence of an insolvency or administration event; (v) reputational damage; or (vi) serious health and safety events; malus and/or clawback provisions may apply for three years from the date of payment of any bonus or the grant of any deferred bonus share award.</p>	<p>Maximum bonus potential is capped at 100% of salary for Executive Directors.</p>	<p>Bonus performance measures are set annually and will be predominantly based on challenging financial targets set in line with the Group's strategic priorities and tailored to each individual role as appropriate; for example, targets relating to adjusted earnings. For a minority of the bonus, strategic or operational objectives may operate.</p> <p>The Committee has the discretion to vary the performance measures used from year to year depending on the strategic priorities at the start of each year. Details of the performance measures for the relevant financial year will be provided in the Annual Report on Remuneration and actual targets will be disclosed retrospectively.</p> <p>For financial targets, and where practicable in respect of operational or strategic targets, bonus starts to accrue once the threshold target is met (up to 20% payable) rising on a graduated scale to 100% for stretch performance.</p> <p>The Committee may adjust bonus outcomes, based on the application of the bonus formula set at the start of the relevant year, if it considers the quantum to be inconsistent with the performance of the Company, business or individual during the year. For the avoidance of doubt this can be to zero and bonuses may not exceed the maximum levels detailed above. Any use of such discretion would be detailed in the Annual Report on Remuneration.</p>

Remuneration continued

Report of the Remuneration Committee continued

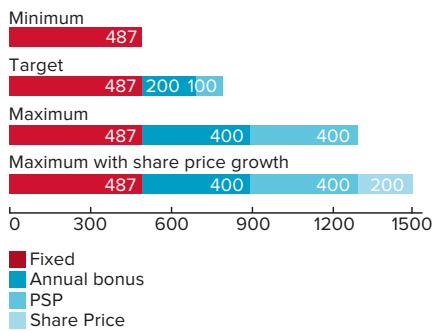
Objective and link to strategy	Operation	Maximum opportunity	Performance measures and assessment
Benefits To provide benefits that are valued by the recipient and are appropriately competitive.	The Executive Directors may receive benefits including a Company-provided car or an allowance in lieu, life assurance and private medical insurance. Other additional benefits may be provided where appropriate. Benefits in kind are not pensionable.	Benefit values vary year on year depending on premiums and the maximum potential value is the cost of these provisions.	Not applicable.
Long-Term Incentive Plan Its purpose is to incentivise and reward the delivery of strategic priorities and sustained performance over the longer term. To provide greater alignment with shareholders' interests.	<p>The LTIP provides for awards of free shares (i.e. either conditional shares or nil or nominal cost options) normally on an annual basis which are eligible to vest after three years subject to continued service and the achievement of challenging performance conditions. It is anticipated that the first award under this scheme for current Directors will be made in 2021.</p> <p>Vested awards are subject to a two-year post-vesting holding period. In exceptional circumstances such as due to regulatory or legal reasons, vested awards may also be settled in cash.</p> <p>Dividend equivalent payments may be made on vested LTIP awards and may assume the reinvestment of dividends, on a cumulative basis.</p> <p>In the event that there was (i) a material misstatement of the Company's results; (ii) a miscalculation or an assessment of any performance conditions based on incorrect information; (iii) misconduct on behalf of an individual; (iv) the occurrence of an insolvency or administration event; (v) reputational damage; or (vi) serious health and safety events, malus and/or clawback provisions may apply for three years from an award becoming eligible to vest.</p>	<p>In any financial year, performance shares with a face value of up to 100% of salary (or 150% of salary on an exceptional basis, such as in recruitment cases) may be granted to an Executive Director.</p> <p>The actual grant level will take into account the share price performance of the Group and the number of awards made in previous years.</p>	<p>The Committee may set such performance conditions on LTIP awards as it considers appropriate reflecting the medium-term priorities of the Group. The choice of measures and their weightings will be determined prior to each grant.</p> <p>Up to 25% of awards will vest for threshold performance with full vesting taking place for equalising, or exceeding, the maximum performance targets. No awards vest for performance below threshold. A graduated vesting scale operates between threshold and maximum performance levels.</p> <p>The Committee may adjust LTIP vesting outcomes, based on the result of testing the performance condition, if it considers the quantum to be inconsistent with the performance of the Company, business or individual during the three-year performance period. For the avoidance of doubt this can be to zero. Any use of such discretion would be detailed in the Annual Report on Remuneration.</p>
Shareholding requirement Secures a long-term locked-in alignment between the Executive Directors and shareholders, ensuring that they build up and maintain a minimum level of shareholding throughout their employment with the Company.	<p>The shareholding requirement will operate in the following manner:</p> <ul style="list-style-type: none"> ▶ shares unconditionally owned by the Executive Director will count towards the requirement; and ▶ unvested deferred bonus shares or vested LTIP shares which are subject to a holding period may count towards the guideline on a net of tax basis. <p>All vested deferred bonus and LTIP awards must be retained until the guideline has been achieved. It is expected that the shareholding is built up over a five-year period from implementation of this policy.</p>	<p>Minimum shareholding requirement is 400% of salary for the current Directors (in place at 1 January 2020) and 200% of salary for new Director appointments.</p> <p>Any vested share deferred bonus and LTIP shares must be retained on a net of tax basis until the guideline has been achieved.</p>	Not applicable.

Objective and link to strategy	Operation	Maximum opportunity	Performance measures and assessment
All-employee share plans Encourages employees to own shares in order to increase alignment over the longer term.	<p>All employees are eligible to participate in the Company's Share Incentive Plan (SIP) and Share save Plan (Save As You Earn).</p> <p>Under the terms of the Share save Plan, all employees can apply for three or five-year options to acquire the Company's shares priced at a discount of up to 20%.</p> <p>Under the terms of the SIP, the Company can choose to offer free shares, partnership shares, matching shares (up to two for one on any partnership shares purchased) and/or dividend shares.</p> <p>In addition, the Company operates a discretionary unapproved share plan and a Company Share Option Plan (CSOP). No awards to Executive Directors are proposed under these plans.</p>	<p>Under the SIP, Share save Plan and CSOP, the maximum amount is equal to the HMRC limits set from time to time.</p>	Not applicable.

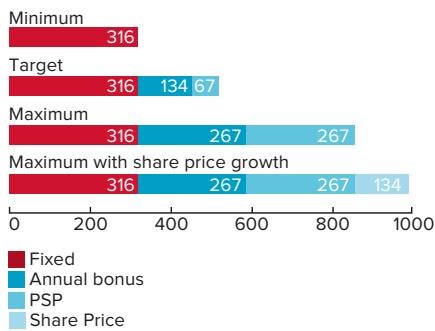
Illustrations of application of remuneration policy

The Company's Remuneration Policy results in a significant proportion of remuneration received by Executive Directors being dependent on Company performance. The composition and total value of the Executive Directors' remuneration packages for minimum, on-target and maximum performance scenarios, along with a maximum performance scenario with a share price growth assumption included, are set out in the charts below.

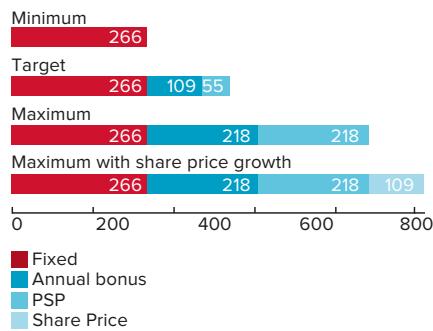
CEO
Salary from 1 April 2021



CFO
Salary from 1 April 2021



Other
Salary from 1 April 2021



Assumptions:

- ▶ Minimum performance includes only fixed pay (base salary for 2021, the value of 2020 benefits as per the single figure of remuneration table and a 15% of salary pension contribution).
- ▶ On-target performance includes fixed pay and assumes an annual bonus payout of 50% of maximum and 25% vesting of a 100% of salary grant of LTIP awards.
- ▶ Maximum performance includes fixed pay and assumes full bonus and 100% LTIP vesting.
- ▶ Maximum performance with share price growth as per maximum but with 50% share price growth assumed on LTIP awards.

Remuneration continued

Report of the Remuneration Committee continued

The Board as a whole is responsible for setting the remuneration of the Non-Executive Directors, other than the Chairman, whose remuneration is determined by the Committee and recommended to the Board.

The table below sets out the key elements of the policy for the Chairman and Non-Executive Directors.

Objective and link to strategy	Operation	Maximum opportunity	Performance measures and assessment
To provide compensation that attracts individuals with appropriate knowledge and experience.	<p>Fee levels are reviewed periodically taking into account independent advice and the time commitment required of Non-Executive Directors.</p> <p>The fees paid to the Chairman and the fees of the other Non-Executive Directors aim to be competitive with other listed companies which the Committee (in the case of the Chairman) and the Board (in respect of the Non-Executive Directors) consider to be of equivalent size and complexity.</p> <p>Non-Executive Directors receive a base fee and additional responsibility fees for undertaking the role of Senior Independent Director or for membership and/or chairmanship of certain Committees.</p> <p>In exceptional circumstances, if there is a temporary yet material increase in the time commitment for Non-Executive Directors, the Board may pay extra fees on a pro-rata basis to recognise the additional workload involved.</p> <p>The Chairman receives a single fee and does not receive any additional fees for membership and/or chairmanship of Committees.</p> <p>Non-Executive Directors also receive reimbursement of reasonable expenses (and any tax thereon) incurred through undertaking their duties and/or Company business.</p>	<p>Any increase in Non-Executive Director base fees or additional responsibility fees may be above the level awarded to other employees, given that they may only be reviewed periodically and may need to reflect any changes to time commitments or responsibilities.</p> <p>The Company will pay reasonable expenses incurred by Non-Executive Directors.</p> <p>Current fee levels are set out in the Statement of implementation on page 106.</p>	<p>Non-Executive Director fees are not performance related.</p> <p>Non-Executive Directors do not receive any variable remuneration element.</p>

Annual report on remuneration

This section of the Directors' Remuneration report contains details of how the Company's Directors' Remuneration Policy was implemented during the financial year ended 31 December 2020 and how it will be implemented for the following year.

Single total figure of remuneration (audited)

Executive Directors

The remuneration of Executive Directors showing the breakdown between elements and comparative figures is set out below. Figures provided have been calculated in accordance with the regulations.

Executive Director (£'000)	Year	Salary ¹	Taxable benefits ¹	Pension ²	Fixed pay and benefits sub-total	Annual bonus ³	Long-term incentives	Variable pay sub-total	Total remuneration
D J Miles	2020	393	26	59	477	123	—	123	600
	2019	387	24	58	469	—	—	—	469
A C M Smith	2020	262	9	39	310	82	—	82	392
	2019	258	13	39	310	—	—	—	310
A Long	2020	214	15	32	261	67	—	67	328
	2019	211	13	32	256	—	—	—	256

1 Benefits included a company-provided car or an allowance in lieu, life assurance and private medical insurance.

2 Executive Directors received a cash allowance in lieu of pension.

3 Full details of the annual bonus outcomes are set out in the section below.

Additional details in respect of single total figure of remuneration table (audited)

The performance measures and targets for the annual bonus for the year ended 31 December 2020 are detailed below.

The annual bonus measures chosen for 2020 were dependent upon achievement of a number of targets detailed below; 70% of the annual bonus was linked to financial measures with the remaining 30% based on strategic objectives relating to customer satisfaction, employee engagement and monetary social value generated. The actual performance achieved in respect of the annual bonus for 2020 is also summarised below against each target.

Measure	Weighting (% of salary)	Threshold (% of maximum payable)	Maximum (% of maximum payable)	Threshold target for 2020	Maximum for 2020	Actual performance for 2020	Bonus outcome (% of salary)
Adjusted Group operating profit ⁽ⁱ⁾	40%	20%	100%	£48.7m	£58.4m	£62.3m	40.0%
Average daily net debt ^{(ii) & (iii)}	30%	20%	100%	£110m (FY measure)	n/a (FY measure), £51.9m (Q4)	£97.3m	30.0%
Customer satisfaction ^(iv)	10%	20%	100%	90%	94%	91.1%	4.2%
Employee engagement ^{(v) (v)}	5%	20%	100%	50%	60%	>60%	5.0%
Employee engagement ^{(2) (vi)}	5%	n/a	100%	n/a	Re-accreditation	Re-accreditation	5.0%
Social value ^(vii)	10%	20%	100%	£2,520	£2,880	£2,540	2.4%

(i) Adjusted Group Operating profit is stated before the amortisation of acquisition intangibles

(ii) Average daily net debt (derived from statement balances)

(iii) Quarter four target £57.4m, actual £51.9m

(iv) Customer Satisfaction is based on percentage of customers that rate the Mears' service at 7 out of 10 or above with methodology signed off by independent Customer Scrutiny Panel

(v) The first employee engagement measure is set against the 'Say What You See' staff survey and the proportion of employees rating the Group as a 'Great place to work'

(vi) The second employee engagement measure is applied against the successful retention of The Sunday Times best employer status

(vii) Social Value is independently assessed utilising a Social Value measurement tool and is expressed as an amount generated per employee

Remuneration continued

Annual report on remuneration continued

As set out in the Annual Statement on pages 101 to 111, the Remuneration Committee, having considered all relevant matters, applied negative discretion to reduce the Operating profit element from 40% to 0% and therefore the Annual Bonus award for 2020 was reduced from 86.6% to 46.6% of salary.

The annual bonus mechanism, after applying the negative discretion, resulted in an aggregate bonus entitlement across the three Executive Directors of £0.4m. Two thirds of this entitlement is paid in cash, and is included within the single total figure of remuneration. One-third of the bonus entitlement will be deferred in shares for a period of three years. The cash element will be withheld by the Committee and released at an appropriate time in 2021, taking into account business recovery and the impact on our shareholders.

Non-Executive Directors

The remuneration of Non-Executive Directors showing the breakdown between elements and comparative figures is shown below. Figures provided have been calculated in accordance with the regulations.

Chairman and Non-Executive Director (£'000)	Year	Salary/fees ⁷	Taxable benefits	Pension	Fixed pay sub-total	Annual bonus	Long-term incentives	Variable pay sub-total	Total remuneration
K Murphy	2020	147	—	—	147	—	—	—	147
	2019	159	—	—	159	—	—	—	159
G Davies	2020	69	—	—	69	—	—	—	69
	2019	74	—	—	74	—	—	—	74
J Unwin	2020	55	—	—	55	—	—	—	55
	2019	63	—	—	63	—	—	—	63
R Irwin	2020	78	—	—	78	—	—	—	78
	2019	84	—	—	84	—	—	—	84
J Burt ¹	2020	18	—	—	18	—	—	—	18
	2019	70	—	—	70	—	—	—	70
E Corrado ²	2020	—	—	—	—	—	—	—	—
	2019	55	—	—	55	—	—	—	55
C Loughlin ³	2020	56	—	—	56	—	—	—	56
	2019	16			16				16
J Clarke ⁴	2020	52	—	—	52	—	—	—	52
	2019	27			27				27
A Hillerby ⁵	2020	1	—	—	1	—	—	—	1
	2019	28	5	—	33	—	—	—	33
C Gibbard ⁶	2020	23	—	—	23	—	—	—	23
	2019	—	—	—	—	—	—	—	—

Variations between the figures above and the approved fee rates relate to the part-year impact for changes in the Committee membership. To reflect the challenges the business encountered during the COVID-19 lockdown, the Non-Executive Directors elected to take a 20% reduction in fees between April and October 2020.

1 J Burt stepped down from the Board on 31 March 2020.

2 E Corrado stepped down from the Board on 31 December 2019. A payment in lieu of notice of £14,000 has been paid in addition to the figures reported above.

3 C Loughlin was appointed to the Board on 17 September 2019.

4 J Clarke was appointed to the Board on 2 July 2019.

5 A Hillerby stepped down from the Board on 12 February 2020.

6 C Gibbard was appointed to the Board on 28 July 2020.

7 To reflect the challenges the business encountered during the COVID-19 lockdown, the Non-Executive Directors elected to take a 20% reduction in fees between April and October 2020.

Statement of Directors' shareholding and share interests (audited)

Directors' share interests as at 31 December 2020 are set out below:

Director	Share interests		
	Number of beneficially owned shares	Vested but unexercised options	Total interests held at year end
D J Miles	336,769	—	336,769
A C M Smith	199,333	—	199,333
A Long	92,957	—	92,957
G Davies	2,500	—	2,500

There were no changes to the holdings set out above from the period 31 December 2020 to date of sign off.

Except as detailed above in respect of G Davies, no other Non-Executive Director holds an interest in shares.

The current Executive Directors each have a shareholding requirement of 400% of salary. As at 31 December 2020, D J Miles, A C M Smith and A Long had met 128%, 114% and 65% of their requirement respectively (based on a share price of £1.50).

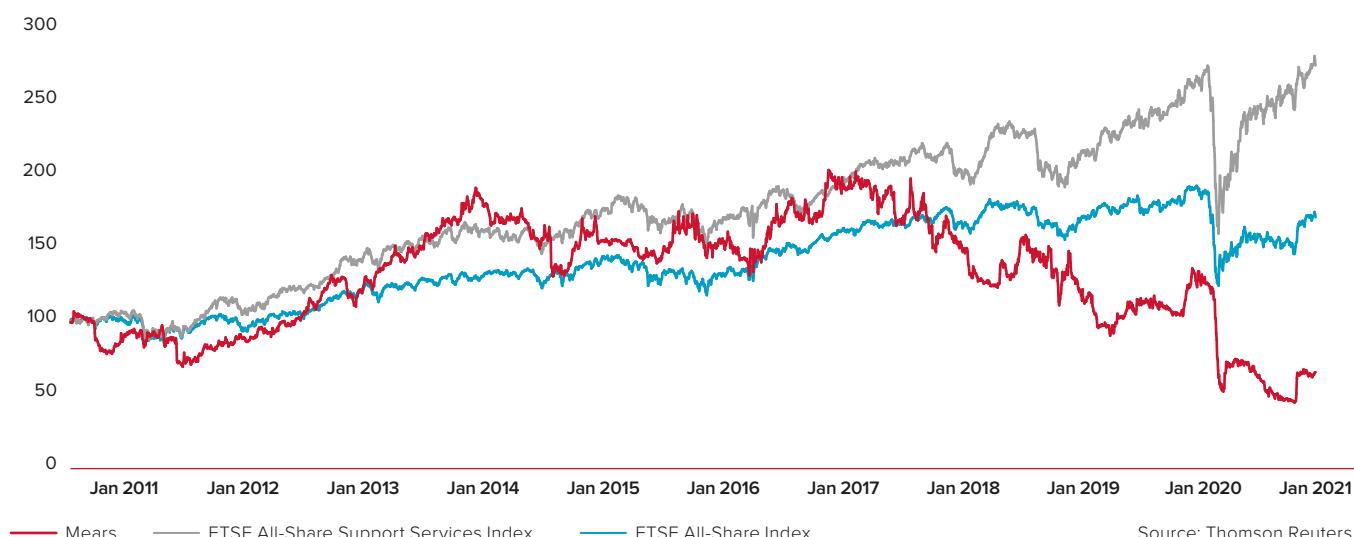
Shareholder dilution

In accordance with the Investment Association's guidelines, the Company can issue a maximum of 10% of its issued share capital in a rolling ten-year period to employees under all its share plans. In addition, of this 10% the Company can issue 5% to satisfy awards under discretionary or Executive plans. The Company operates all its share plans within these guidelines.

Performance graph and table (unaudited)

The graph below shows the Group's performance, measured by TSR, compared with the constituents of the FTSE All-Share Index and the FTSE All-Share Support Services Index over the past ten years. The Company is a constituent of both indices and these peer groups are considered to provide relevant comparisons.

Total shareholder return



Remuneration continued

Annual report on remuneration continued

The table below shows the Chief Executive Officer's remuneration package over the past ten years, together with incentive payout/vesting as compared to the maximum opportunity.

Year	Name	Single figure of total remuneration (£'000)	Bonus payout (as % maximum opportunity)	Long-term incentive vesting (as % maximum opportunity)
2020	D J Miles	600	47%	—
2019	D J Miles	469	—	—
2018	D J Miles	455	—	—
2017	D J Miles	443	—	—
2016	D J Miles	436	—	—
2015	D J Miles	436	—	20%
2014	D J Miles	412	—	35%
2013	D J Miles	825	—	100%
2012	D J Miles	409	—	—
2011	D J Miles	384	—	—
2010	D J Miles	270	—	—

Percentage change in Remuneration of Directors Compared with other employees (unaudited)

The table below compares the percentage change in the salary of the directors with that of the wider employee population.

	Remuneration		
	Salary/fee	Benefits	Bonus/incentives
D J Miles	2.0%	—	—
A C M Smith	2.0%	—	—
A Long	2.0%	—	—
K Murphy	—	—	—
G Davies	—	—	—
J Unwin	—	—	—
R Irwin	—	—	—
J Burt ¹	—	—	—
C Loughlin ²	—	—	—
J Clarke ³	—	—	—
A Hillerby ⁴	—	—	—
C Gibbard ⁵	—	—	—
All employee's salaries	2.0%	—	—

¹ J Burt stepped down from the Board on 31 March 2020. Percentage change calculation includes part-year remuneration in 2020.

² C Loughlin was appointed to the Board on 17 September 2019. Percentage change calculation includes part-year remuneration in 2019.

³ J Clarke was appointed to the Board on 2 July 2019. Percentage change calculation includes part-year remuneration in 2019.

⁴ A Hillerby stepped down from the Board on 12 February 2020. Percentage change calculation includes part-year remuneration in 2020.

⁵ C Gibbard was appointed to the Board on 28 July 2020. No prior year comparison available.

CEO to employee pay ratio (unaudited)

The table below sets out the ratio between the total pay of the CEO and the total pay of the employees at the 25th, 50th (median) and 75th percentiles of the workforce.

Year	Method	25th percentile	Median	75th percentile
2020	B	23:1	21:1	19:1
2019	B	24:1	23:1	16:1

The 25th, 50th and 75th percentile ranked individuals have been identified using the gender pay gap survey data for 2020, i.e. as allowed for under method B of the UK reporting requirements. This was deemed to be the most reasonable and practical approach to identifying the relevant individuals for the purposes of this disclosure. The day by reference to which the 25th, 50th and 75th percentile employees were determined was 30 April 2021. The CEO pay figure is the total remuneration figure as set out in the single figure table on page 101 and equivalent figures (on a full-time equivalent basis) have been calculated for the relevant 25th, 50th and 75th percentile employees. The Remuneration Committee is comfortable that the resulting calculations are representative of pay levels at the respective quartiles.

The total pay and benefits figures used to calculate the ratios for each of the 25th percentile, median and 75th percentile employees are £25,548, £29,117 and £31,209 respectively. The salary element for each of these figures are £25,037, £28,450 and £31,015 respectively.

Relative importance of spend on pay (unaudited)

The table below sets out the relative importance of spend on pay in the financial year and previous financial year compared with other disbursements from profit.

Significant distributions	Disbursements from profit in financial year 2020 £'000	Disbursements from profit in previous financial year 2019 £'000	% change	
			2019 £'000	% change
Total Directors' pay	1,819	1,629		12%
Profit distributed by way of dividend	—	13,811		(100%)
Operating profit before non-underlying items (continuing activities)	6,585	41,124		(84%)

The profit distributed by way of dividend relates to dividends paid during the previous year. Following the uncertainty surrounding COVID-19, the Board proposed that no dividend be paid in respect of the 2020 financial year.

Details of service contracts and letters of appointment

Director	Date of contract/letter of appointment	Notice period by Company or Director
Executive		
D J Miles	June 2008	Twelve months
A C M Smith	June 2008	Twelve months
A Long	August 2009	Twelve months
Chairman/Non-Executive		
K Murphy	January 2019	Six months
G Davies	October 2015	Six months
J Unwin	January 2016	Six months
R Irwin	February 2017	Six months
J Clarke	July 2019	Six months
C Loughlin	September 2019	Six months
C Gibbard	September 2020	Three months

Remuneration continued

Annual report on remuneration continued

Payments to past Directors and Payments for Loss of Office (Audited)

There were no payments for loss of office or to past Directors during the year.

Statement of implementation of remuneration policy in the following financial year

Executive Directors

Salary

The salary entitlements for the forthcoming year are set out below:

Executive Director	2021 £	2020 £	% change
D J Miles	400,471	392,619	2%
A C M Smith	267,017	261,781	2%
A Long	218,468	214,184	2%

The salary increase for 2021 is effective from 1 April 2021 and matches the general workforce inflationary increase of 2% applied on 1 January 2021.

Pension

Details of pension contributions for the year ended 31 December 2020 are set out below:

Executive Director	Pension
D J Miles	15%
A C M Smith	15%
A Long	15%

The current executive directors' pension contribution rates will be reduced to the majority workforce rate from 1 January 2023. New directors appointed to the Board will have a contribution no higher than the workforce rate on joining.

Annual bonus 2021

The maximum bonus potential will be 100% of salary and will be dependent upon the following performance measures:

- ▶ Profit before Tax (40%)
- ▶ Net debt (30%)
- ▶ Strategic objectives (30%) relating to customer satisfaction (10%), employee engagement (10%) and monetary social value generated (10%)

These strategic objectives, which will be built around the Group's strategy for customer success and supported by our independently chaired Customer Scrutiny Board, reflect the Group's commitment to serving our clients and customers; to further developing our Social Value offer to add value in the Communities we serve; and to securing high levels of positive employee engagement through net promoter scores and validation by external accreditation.

In addition, health and safety will apply as a discretionary underpin and before any bonus becomes payable, the Committee will consider health and safety performance over the year and will have the power to reduce the bonus outcome if standards are below expectations.

Any bonus payable will be delivered in a mix of cash (67%) and deferred share awards (33%) which will vest after three years from grant.

LTIP for 2021

The first LTIP award under the new plan adopted as part of the Directors' Remuneration Policy at the 2020 AGM will be made in 2021. It is intended that awards will be made at 100% of salary to each of the executive directors. The measures and targets will be as follows:

Description	Weighting	Calculation	Targets
Total shareholder Return ('TSR')	50%	Relative TSR target against the constituents of the FTSE SmallCap (excluding Investment Trusts, Financial Services and Natural Resources companies) measured over a three-year performance period.	Threshold: Median (25% vests) Maximum: Upper Quartile (100% vests)
Earnings per Share ('EPS')	50%	Adjusted Earnings per Share (EPS) target relating to the 2023 financial year i.e. the third year of the three-year performance period. The Committee will consider ROCE performance over the performance period and may reduce the EPS vesting outcome if the Committee is not satisfied that the level of EPS vesting is not justified on account of the Group's ROCE over the Performance Period.	Threshold: 20 pence (25% vests) Maximum: 25 pence (100% vests)

The Remuneration Committee believes the use of TSR and EPS provides an appropriate balance between focusing on share price recovery and delivering financial returns.

Vesting will be on a pro-rata basis between the threshold and maximum vesting figures. In addition, the Committee retains discretion to reduce the overall LTIP vesting level if it considers that the underlying business performance of the Company does not justify vesting (taking into consideration a range of factors, including, for example, ROCE performance). If the Committee is not satisfied that the formulaic vesting outcome is aligned with underlying Group performance then it may reduce (potentially to zero) the vesting outcome.

Any shares which vest from this award will be subject to a two-year post-vesting holding period.

Non-Executive Directors

The following table sets out the fee rates for the Non-Executive Directors:

	2021	2020	% change
Chairman fee	160,000	160,000	—
Base fee	50,000	50,000	—
Committee Chairman fee	15,000	15,000	—
Committee membership fee	5,000	5,000	—

Role of The Committee and Activities

The Committee determines the total individual remuneration packages of each Executive Director of the Group and certain other senior employees (and any exit terms) and recommends to the Board the framework and broad policies of the Group in relation to Senior Executive remuneration. The Committee determines the targets for all of the Group's performance-related remuneration and exercises the Board's powers in relation to all of the Group's share and incentive plans. The terms of reference of the Committee are available on the Company's website.

There is a formal and transparent procedure for developing policy on Executive remuneration and for determining the remuneration of individual Directors.

The Remuneration Committee is responsible for:

- ▶ determining and agreeing with the Board the broad remuneration policy for:
 - the Chairman, the Executive Directors and senior management; and
 - the Executive Directors' remuneration and other benefits and terms of employment, including performance related bonuses and share options; and
- ▶ approving the service agreements of each Executive Director, including termination arrangements.

No Director is involved in determining his/her own remuneration.

Remuneration continued

Annual report on remuneration continued

During the year the Committee addressed the following main topics:

- ▶ Undertook a comprehensive review of executive directors' remuneration which culminated in the preparation of a revised remuneration policy which was put to shareholders for approval at the 2020 AGM;
- ▶ Reviewed the pension contributions of the executive directors to align the contributions to the workforce level by 1 January 2023;
- ▶ Sought the views of our major shareholders and the main voting agencies as part of a comprehensive investor consultation exercise to inform the design process for the revised policy which was approved at the 2020 AGM;
- ▶ Reviewed guidance from investor bodies and institutional shareholders;
- ▶ Assessed whether our remuneration framework is appropriately aligned with our culture and values and motivates our leaders to achieve the Group's strategic objectives;
- ▶ Reviewed and approved the remuneration packages for our current executive directors;
- ▶ Formulated the basis for consultation with leading shareholders on the LTIP for 2021 and reviewed all responses, and
- ▶ Finalised the annual bonus payments for the 2019 financial year to the executive directors (which included the exercise of negative discretion to reduce the formulaic outcome from 58% of maximum to zero) and the annual bonus plan for the 2020 financial year.

Composition of the Remuneration Committee

The members of the Committee during the year were Roy Irwin (Chair), Julia Unwin, Kieran Murphy and Chris Loughlin.

Support to the Remuneration Committee

By invitation of the Committee, meetings are also attended by the Company Secretary (who acts as secretary to the Committee) and the HR Director, who are consulted on matters discussed by the Committee, unless those matters relate to their own remuneration. The Committee is authorised to take such internal and external advice as it considers appropriate in connection with carrying out its duties, including the appointment of its own external remuneration advisers. During the year, the Committee was assisted in its work by FIT Remuneration Consultants LLP. FIT was appointed in 2019 following a tender process and has provided advice in 2020 in relation to general remuneration matters and the review of the remuneration policy. Fees paid to FIT in relation to advice to the Committee in 2020 were £25,000 (excluding VAT). FIT did not provide any other services to the Company. FIT is a member of the Remuneration Consultants Group and, as such, voluntarily operates under the Code of Conduct in relation to executive remuneration consulting in the UK. The Committee is satisfied that the advice they received from FIT is objective and independent.

Statement of voting at general meeting

The table below shows the voting outcome in respect of the remuneration-related resolutions at the 2020 AGM.

Item	Votes for	%	Votes against	%	Votes withheld
To approve the Remuneration policy	58,127,776	69%	26,079,580	31%	383,371
To approve the Remuneration report	62,521,479	78%	17,237,114	22%	4,715,289
To approve the Long-Term Incentive Plan	66,618,893	79%	17,964,291	21%	7,543

The significant vote against the Annual Report on Remuneration at the 2020 AGM was primarily as a result of the dissatisfaction with the performance of the Company – at that time – of a small number of significant shareholders. The Remuneration Committee has consulted extensively with our major shareholders, as well as the leading proxy voting agencies, during the course of 2020 and early 2021 in order to understand how we may, from a remuneration perspective, be able to optimise our arrangements going forward. This consultation process has been constructive and the feedback we received has been crucial in informing our approach to designing the revised Policy for which we will be seeking approval at the 2021 AGM.

Report of the Directors

The Directors present their report together with the consolidated financial statements for the year ended 31 December 2020.

Principal activities

The principal activities of the Group are the provision of a range of outsourced services to the public and private sectors. The principal activity of the Company is to act as a holding company.

Business review

The Company is required to set out a fair review of the business of the Group during the reporting period. The information that fulfils this requirement can be found in the Strategic Report, Review of Operations and Financial Review. The results of the Group can be found within the consolidated income statement. Information required to be disclosed in respect of emissions and future developments is included within the Strategic Report.

Dividend

No dividend has been declared in respect of 2020. Following the impact on the business from the Covid-19 pandemic, the Board took steps to protect its liquidity and is grateful for the strong support of the majority of shareholders for the actions taken by the Directors during this period of uncertainty. As detailed in the Strategic Report, the Group has reported a significant reduction in its indebtedness, with the Terraquest disposal being a major single factor behind this improvement. It remains the Board's intention to continue to adopt a progressive dividend policy once it is confident that activity and working practices have returned to normal and that it would be prudent to do so.

Corporate governance

Details of the Group's corporate governance are set out on pages 70 to 108.

Key performance indicators (KPIs)

We focus on a range of key indicators to assess our performance. Our performance indicators are both financial and non-financial and ensure that the Group targets its resources around its customers, employees, operations and finance. Collectively they form an integral part of the way that we manage the business to deliver our strategic goals. Our primary performance indicators are detailed on pages 44 to 47.

Directors

The present membership of the Board is set out with the biographical detail on page 73.

In line with current practice, all of the Directors will retire and, being eligible, offer themselves for re-election at the AGM in June 2021. Roy Irwin and Geraint Davies have announced their intention to retire and will not offer themselves for re-election at the AGM. Any person appointed by the Directors must retire at the next AGM but will be eligible for re-election at that meeting.

The beneficial interests of the Directors in the shares of the Company at 31 December 2020 are detailed within the Remuneration Report on page 104.

The process governing the appointment and replacement of Directors is detailed within the Report of the Nomination Committee.

Amendment to articles of association

The Company's Articles of Association can be amended only by a special resolution of the members, requiring a majority of not less than 75% of such members voting in person or by proxy.

Report of the Directors continued

Share capital authorisations

The 2020 Annual General Meeting (AGM) held in June 2020 authorised:

- ▶ the Directors to allot shares within defined limits. The Companies Act 2006 requires directors to seek this authority and, following changes to Financial Services Authority (FSA) rules and institutional guidelines, the authority was limited to one third of the issued share capital, a total of £368,343 plus an additional one third of issued share capital of £368,343 that can only be used for a rights issue or similar fundraising;
- ▶ the Directors to issue shares for cash on a non-preemptive basis. This authority was limited to 5% of the issued share capital of £55,251 and is required to facilitate technical matters such as dealing with fractional entitlements or possibly a small placing; and
- ▶ the convening of general meetings (other than an AGM) on 14 days' notice. Section 307A of the Companies Act 2006 provides that listed companies must hold general meetings (other than annual general meetings) on 21 days' notice unless the members of that company pass a special resolution agreeing to a shorter notice period which cannot be any less than 14 clear days. It is therefore necessary for the Company to pass this resolution allowing the Company to continue to hold general meetings (other than annual general meetings) on not less than 14 clear days' notice.

Further details of these authorisations are available in the notes to the 2020 Notice of AGM. Shareholders are also referred to the 2021 Notice of AGM, which contains similar provisions in respect of the Company's equity share capital.

AGM

The 2021 AGM will be held on 29 June 2021 at 11:00am. A formal Notice of Meeting and Form of Proxy will be issued in advance. The ordinary business to be conducted will include the reappointment of all Directors.

Principal risks and uncertainties

Risk is an accepted part of doing business. The Group's financial risk management is based on sound economic objectives and good corporate practice. The Board has overall responsibility for risk management and internal controls within the context of achieving the Group's objectives. Our process for identifying and managing risks is set out in more detail within the Corporate Governance Statement. The key risks and mitigating factors are set out on pages 66 and 67. Details of financial risk management and exposure to price risk, credit risk and liquidity risk are given in note 24 to the financial statements.

Contracts of significance

The Group is party to significant contracts. The Directors do not consider that any one of those contracts is essential in its own right to the continuation of the Group's activities. As detailed within the Strategic Report on pages 68 to 69, the Directors completed a long-term assessment of the Group's financial viability and the loss of a number of key contracts was modelled as one possible downside scenario but the Group remained viable in such an event.

Payment policy

The Company acts purely as a holding company and as such is non-trading. Accordingly, no payment policy has been defined. However, the policy for Group trading companies is to set the terms of payment with suppliers when entering into a transaction and to ensure suppliers are aware of these terms. Group trade creditors during the year amounted to 59 days (2019: 55 days) of average supplies for the year.

Capital structure

The Group is financed through both equity share capital and debt. Details of changes to the Company's share capital are given in note 26 to the financial statements. The Company has a single class of shares – ordinary 1p shares – with no right to any fixed income and with each share carrying the right to one vote at the general meetings of the Company. Under the Company's Articles of Association, holders of ordinary shares are entitled to participate in any dividends pro-rata to their holding. The Board may propose and pay interim dividends and recommend a final dividend for approval by the shareholders at the AGM. A final dividend may be declared by the shareholders in a general meeting by ordinary resolution but such dividend cannot exceed the amount recommended by the Board.

Substantial shareholdings

As at 9 April 2021 the Company has been notified of, or is aware of, the shareholders holding 2% or more of the issued share capital of the Company. These shareholders are detailed on page 78.

Disabled employees

Applications for employment by disabled persons are always fully considered, bearing in mind the aptitudes of the applicant concerned. In the event of members of staff becoming disabled, every effort is made to ensure that their employment with the Group continues and that appropriate training is arranged. It is the policy of the Group that the training, career development and promotion of disabled persons should, as far as possible, be identical to that of other employees.

GHG emissions

The Group's carbon emissions data for the year is provided below. Mears continues to be committed to implementing the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD). We recognise climate change as one of the biggest threats the world faces, and one which could pose challenges and opportunities to our business including our supply chain and operations. We believe that disclosing these climate related risks is an important step in demonstrating our understanding of them and assists in our efforts to mitigate them. During 2020 we appointed our first Head of Carbon Reduction, and it will be a priority for 2021 to continue to develop our programme to reduce carbon emissions.

Both Scope 1 and Scope 2 emissions have risen significantly in the year, this is a result of the provision of energy for accommodation utilised in our Asylum Accommodation and Support Contract which mobilised in September 2019. The supply of gas and electricity for these properties is included within the emissions reported below.

These figures have been generated from independently provided reports of carbon emissions or energy usage from a variety of sources and, where necessary, energy usage has been converted into carbon emissions using the 2020 dataset provided by the Department for Environment, Food & Rural Affairs.

Scope	Units	2020	2019
Scope 1 – UK	Tonnes CO ₂ e	34,370	19,728
Scope 2 – UK location-based	Tonnes CO ₂ e	7,376	2,714
Scope 1 and 2		2020	2019
Intensity tonnes CO ₂ e/£m revenue		49.63	22.82
Energy consumption	MWh	189,074	92,598

Our reporting follows the Greenhouse Gas Protocol Corporate Accounting and Reporting Standard, applying the "Financial Control" approach (organisational boundary).

Our policy is to restate Carbon and energy figures in consideration of changes in methodologies, improvements in the accuracy, or discovery of errors in previous years' data. No restatement has been made this year.

Our gross carbon emissions have been classified in the following way:

Scope 1 – Direct emissions from: vehicle use (owned and leased); heating fuels used in buildings.

Scope 2 – Indirect emissions from: electricity used in our buildings. We report location-based emissions (taking into account the UK grid average).

Scope 3 – Indirect emissions from business travel by air and taxi; hotel stays; water supply; and waste recycling and disposal.

Out of Scope – Indirect emissions from: biofuel usage from all divisions in line with DEFRA reporting guidelines.

Employee information and consultation

The Group has received recognition under the 'Investors in People' award. The Group continues to involve its staff in the future development of the business. Information is provided to employees through a daily news email, a quarterly newsletter posted out to all staff, the Group website and the intranet to ensure that employees are kept well informed of the performance and objectives of the Group.

CREST

CREST is the computerised system for the settlement of share dealings on the London Stock Exchange. CREST reduces the amount of documentation required and also makes the trading of shares faster and more secure. CREST enables shares to be held in an electronic form instead of the traditional share certificates. CREST is voluntary and shareholders can keep their share certificates if they wish. This may be preferable for shareholders who do not trade in shares on a frequent basis.

Auditor

Ernst & Young LLP offers itself for reappointment as auditor in accordance with Section 489 of the Companies Act 2006.

By order of the Board

B Westran

Company Secretary

ben.westran@mearsgroup.co.uk

12 May 2021

Statement of Directors' responsibilities

The Directors are required to prepare the financial statements for the Company and the Group at the end of each financial year in accordance with all applicable laws and regulations. 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 and profit or loss of the Group and the Company for that period. In preparing these financial statements, the Directors are required to:

- ▶ select suitable accounting policies and apply them consistently;
- ▶ make judgements and accounting estimates that are reasonable;
- ▶ state whether the Consolidated Financial Statements have been prepared in accordance with International Financial Reporting Standards ('IFRSs') adopted pursuant to Regulation (EC) No 1606/2002 as it applies in the European Union and with international accounting standards in conformity with the Companies Act 2006;
- ▶ state for the Company Financial Statements whether United Kingdom Accounting Standards and applicable law, including Financial Reporting Standard 101 Reduced Disclosure Framework ("FRS 101") have been followed; and
- ▶ prepare the Financial Statements on the going concern basis unless it is inappropriate to presume that the Company and the Group will continue in business.

The Directors are responsible for ensuring that the Group keeps proper accounting records which disclose with reasonable accuracy the financial position of the Group and the Company to enable them to ensure that the Financial Statements comply with the Companies Act 2006 and, as regards the Consolidated Financial Statements, IFRSs adopted pursuant to Regulation (EC) No 1606/2002 as it applies in the European Union. The Directors are also responsible for the system of internal control, for safeguarding the assets of the Group and the Company, and taking reasonable steps 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.

The Directors confirm that:

- ▶ so far as each Director is aware there is no relevant audit information of which the Company's auditor is unaware; and
- ▶ the Directors have taken all the steps that they ought to have taken as Directors in order to make themselves aware of any relevant audit information and to establish that the auditor is aware of that information.

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

The Board confirms that to the best of its knowledge:

- ▶ that 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 Group and the undertakings included in the consolidation taken as a whole; and
- ▶ that the Annual Report includes a fair review of the development and performance of the business and the position of the Group and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

The Directors are responsible for preparing the Annual Report in accordance with applicable law and regulations. The Board considers the Annual Report and Accounts, taken as a whole, is fair, balanced and understandable and that it provides the information necessary for shareholders to assess the Group's performance, business model and strategy.

Going Concern

We principally operate in robust defensive markets where spend is largely non-discretionary and our contracts tend to be long-term partnerships. The Group reported net cash of £56.9m at 31 December 2020. The core debt required to satisfy the day-to-day requirements of the business is in the region of £70m. This represents significant headroom against the £120m unsecured revolving credit facility, with an additional accordion mechanism allowing the facility to be increased to a maximum of £200m, maturing in November 2022.

After reviewing the Group's and Company's budget for the next financial year and longer-term plans, the Directors consider that, as at the date of approving the financial statements, it is appropriate to adopt the going concern basis in preparing the financial statements.

On behalf of the Board

A C M Smith

Chief Financial Officer

andrew.smith@mearsgroup.co.uk

12 May 2021

Financial statements

Independent auditor's report

to the members of Mears Group PLC

Opinion

In our opinion:

- ▶ Mears Group plc's group financial statements and parent company financial statements (the "financial statements") give a true and fair view of the state of the Group's and of the parent company's affairs as at 31 December 2020 and of the group's profit for the year then ended;
- ▶ the Group financial statements have been properly prepared in accordance with International Accounting Standards in conformity with the requirements of the Companies Act 2006 and International Financial Reporting Standards adopted pursuant to Regulation (EC) No.1606/2002 as it applies in the European Union;
- ▶ the parent company financial statements have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- ▶ the financial statements have been prepared in accordance with the requirements of the Companies Act 2006.

We have audited the financial statements of Mears Group plc (the 'parent company') and its subsidiaries (the 'Group') for the year ended 31 December 2020 which comprise:

Group	Parent company
Consolidated statement of profit or loss for the year then ended	Balance sheet as at 31 December 2020
Consolidated statement of comprehensive income for the year then ended	Statement of changes in equity for the year then ended
Consolidated balance sheet as at 31 December 2020	Related notes 1 to 17 to the financial statements, including a summary of significant accounting policies
Consolidated cash flow statement for the year then ended	
Consolidated statement of changes in equity for the year then ended	
Related notes 1 to 33 to the financial statements, including a summary of significant accounting policies	

The financial reporting framework that has been applied in the preparation of the Group financial statements is applicable law and International Accounting Standards in conformity with the requirements of the Companies Act 2006 and International Financial Reporting Standards adopted pursuant to Regulation (EC) No. 1606/2002 as it applies in the European Union. The financial reporting framework that has been applied in the preparation of the parent company financial statements is applicable law and United Kingdom Accounting Standards, including FRS 101 "Reduced Disclosure Framework" (United Kingdom Generally Accepted Accounting Practice).

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of our report. We are independent of the group and company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the FRC's Ethical Standard as applied to listed public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Conclusions relating to going concern

In auditing the financial statements, we have concluded that the directors' use of the going concern basis of accounting in the preparation of the financial statements is appropriate. Our evaluation of the directors' assessment of the Group and parent company's ability to continue to adopt the going concern basis of accounting included:

- ▶ testing the clerical accuracy of the model and obtaining management's going concern paper used to prepare the Group's going concern assessment;
- ▶ assessing the reasonableness of the cashflow forecast by analysing management's historical forecasting accuracy as well as reviewing the contracted order book and margins. We evaluated the key assumptions underpinning the group's forecasts (such as contract renewals and margins) by proposing alternatives such as a greater loss rate, as well as considering the uncertainties arising from COVID-19 (eg, the extent to which the Group's activities can continue to be performed due to restrictions), and challenging management's position by modelling our own scenarios;
- ▶ assessing whether the group's forecasts in the going concern assessment were consistent with other forecasts used by the Group in its accounting estimates, including goodwill impairment;
- ▶ challenging, based on our own independent analysis, whether the severe downside cases prepared by management could lead either to a loss of liquidity or a covenant breach and whether these scenarios were plausible. Our assessment included consideration of the impact and likelihood of:
 - the loss of significant customer contracts;

Financial statements continued

Independent auditor's report continued

to the members of Mears Group PLC

- ongoing COVID-19 restrictions;
- a significant health and safety event which leading to significant reputational damage to the Group;
- ▶ considering the mitigating actions such as cost optimisation programmes and reduced fixed asset spend that management could undertake in a severe but plausible downside scenario;
- ▶ considering, independently, a “reverse stress-test” scenario that would lead to either a loss of liquidity or a covenant breach and concluding that such a scenario would be implausible based on evidence obtained and our understanding of the business; and
- ▶ we also confirmed the availability of debt facilities through to November 2022, and considered their underlying terms, including covenants, by examination of executed documentation.

We observed that whilst the Group revenue for the year ended 31 December 2020 decreased by 9% in total compared to the prior year, the Group's cash and cash equivalents (net of the revolving credit facility) is £56.9 million at 31 December 2020 (2019: negative of £51.0 million), refer to the going concern section of the accounting policies.

Based on the work we have performed, we have not identified any material uncertainties relating to events or conditions that, individually or collectively, may cast significant doubt on the Group and parent company's ability to continue as a going concern for the period to 30 June 2022.

In relation to the Group and parent company's reporting on how they have applied the UK Corporate Governance Code, we have nothing material to add or draw attention to in relation to the directors' statement in the financial statements about whether the directors considered it appropriate to adopt the going concern basis of accounting.

Our responsibilities and the responsibilities of the directors with respect to going concern are described in the relevant sections of this report. However, because not all future events or conditions can be predicted, this statement is not a guarantee as to the Group's ability to continue as a going concern.

Overview of our audit approach

Group

Audit scope	<ul style="list-style-type: none"> ▶ We performed an audit of the complete financial information of seven components and audit procedures on specific balances for a further five components. ▶ The components where we performed full or specific audit procedures accounted for 100% of profit before tax from continuing and discontinued operations, 99% of revenue and 91% of total assets.
Key audit matters	<ul style="list-style-type: none"> ▶ Appropriateness of lease accounting under IFRS 16. ▶ Valuation of the Group and parent's defined benefit pension obligation. ▶ Appropriateness of revenue recognition including contract accounting, contract assets, and contract accruals. ▶ Management override of controls focusing on manual journal entries, top-side consolidation adjustments, judgemental provisions and accruals. ▶ Disposal accounting including recognition of profit on disposal and contingent consideration. ▶ <u>First year audit transition including assessment of opening balances.</u>
Materiality	<ul style="list-style-type: none"> ▶ Overall Group materiality of £1.1m which represents 4.75% of normalized profit before tax from continuing operations. We used professional judgment to determine materiality given the impact of Covid-19 on the Group's relevant materiality measures.

An overview of the scope of the parent company and Group audits

Tailoring the scope

Our assessment of audit risk, our evaluation of materiality and our allocation of performance materiality determine our audit scope for each company within the Group. Taken together, this enables us to form an opinion on the consolidated financial statements. We take into account size, risk profile, the organisation of the group and effectiveness of group-wide controls, changes in the business environment and other factors when assessing the level of work to be performed at each company.

The Group's operations are entirely based within the United Kingdom, and all are accounted for within the United Kingdom. There was no change in our scoping as a result of the prior year adjustments identified given the overall coverage of components in scope, consideration of the nature of the adjustments and the coverage over the account balances affected.

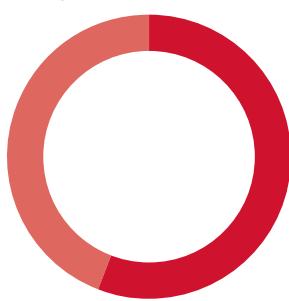
Of the 20 components selected, we performed an audit of the complete financial information of seven components (“full scope components”) which were selected based on their size or risk characteristics. For five components (“specific scope components”), we performed audit procedures on specific accounts within that component that we considered had the potential for the greatest impact on the significant accounts in the financial statements either because of the size of these accounts or their risk profile.

The reporting components where we performed audit procedures accounted for more than 100% of the Group's profit before tax from continuing and discontinued operations (as a result of some loss making operations on which other procedures were performed), 99% of the Group's revenue and 91% of the group's total assets. For the current year, the full scope components contributed 56% of the Group's profit before tax from continuing and discontinued operations, 88% of the group's revenue and 87% of the Group's total assets. The specific scope components contributed 49% of the Group's profit before tax from continuing and discontinued operations, 11% of the Group's revenue and 4% of the Group's total assets. The audit scope of these components may not have included testing of all significant accounts of the specific component but will have contributed to the coverage of significant accounts tested for the Group.

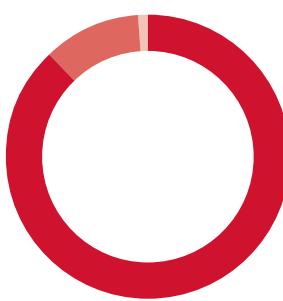
Of the remaining eight components that together represent less than 1% of the Group's normalized profit before tax from continuing operations none individually represent more than 5% of the Group's normalized profit before tax from continuing operations. For these components, we performed other procedures, including analytical review, testing of consolidation journals and intercompany eliminations to respond to any potential risks of material misstatement to the Group financial statements.

The charts below illustrate the coverage obtained from the work performed by our audit teams.

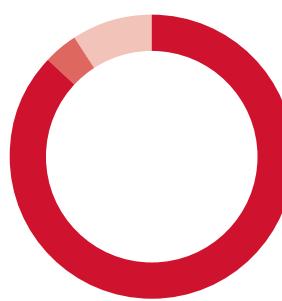
**Profit before tax
(or adjusted PBT measure used)**



Revenue



Total assets



Involvement with component teams

All audit work performed for the purposes of the audit was undertaken by the Group audit team.

Impact of the Covid-19 pandemic

As a result of the Covid-19 outbreak and resulting lockdown restrictions we have performed the majority of our planning, pre year-end, and year-end audit remotely. We were able to physically attend an on-site planning meeting with management in September 2020 and physically attend on-site meetings at the closing stages of the audit during April 2021, we physically attended six stock counts at various dates in December 2020 and January 2021, and four development site inspections were physically attended by the Senior Statutory Auditor in February 2021.

We have engaged virtually with a very wide range of Group personnel, including those outside the finance function, throughout the period of remote working using frequent video calls, share-screen functionality, secure encrypted document exchanges and data downloads to avoid any limitation on the audit evidence required. This approach was supported through use of bespoke EY software collaboration platforms for the secure and timely delivery of requested audit evidence. All audit evidence was recorded in electronic form on our audit systems. We performed virtual site visits, also attended by the Chief Executive Officer as part of our understanding of the business. We held additional calls with branch management accountants, members of the group's commercial team and quantity surveyors to understand, assess, and challenge accounting positions on sampled transactions selected for testing.

We held regular calls, including video calls, throughout the audit with management, including the group Finance Director and Audit Committee Chair to monitor progress, discuss evidence provided, and understand accounting judgements.

Key audit matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) that we identified. These matters included those which had the greatest effect on: the overall audit strategy; the allocation of resources in the audit, and directing the efforts of the engagement team. These matters were addressed in the context of our audit of the financial statements as a whole, and in our opinion thereon, and we do not provide a separate opinion on these matters.

Financial statements continued

Independent auditor's report continued

to the members of Mears Group PLC

Risk	Our response to the risk	Key observations communicated to the Audit Committee
Appropriateness of lease accounting under IFRS 16 (right of use assets Group 2020 £200.0m, Group 2019 £200.0m, lease liabilities Group 2020 £209.1, Group 2019 £205.2)*	<p>Scoping: We performed audit procedures over this risk area which covered 100% of the risk amount.</p> <p>Our procedures included:</p> <p>Assessing management's process: We gained an understanding through a walkthrough of the process and controls management have in place over the implementation and completeness of IFRS 16.</p> <p>Assessing management's expert: We have assessed the independence, objectivity and competence of the Group's external specialist engaged to compute an appropriate discount rate, which included understanding the scope of services being provided and considering the appropriateness of the qualifications of the external specialist. With the support of our Corporate Treasury specialists we have assessed the appropriateness of the IBR by reviewing managements methodology and reperforming the calculations and validating with reference to observable market rates.</p> <p>Key judgments: We challenged the key judgements and assumptions used by management in relation to assessing whether leasing arrangements fall within the scope of IFRS 16 and in determining the appropriate lease term at the inception of the lease where leased assets are subject to extension or termination options. Further, the Group has a high volume of leases, some of which are complex in nature, and the group uses the manual bespoke excel modelling templates to derive the ROU asset and lease liability values.</p> <p>Due to the significant financial statement impact of IFRS 16, as well as the high level of estimation and judgment required in determining the appropriate accounting treatment, and the manual modelling of the impact, we therefore identified IFRS 16 as a significant risk, which was one of the most significant assessed risks of material misstatement.</p> <p>*after restatement</p>	<p>As at 31 December 2019:</p> <ul style="list-style-type: none"> ▶ The IFRS 16 accounting policy applied on transition to IFRS 16 and to be applied from 1 January 2019 disclosed in the 2019 Annual Report and Accounts had not been followed. Specifically: lease liabilities and right of use assets were recognised for leases for which the lease term ended within 12 months of the date of initial application; IFRS 16 was applied to leases for which the underlying asset was of low value; and IFRS 16 was applied to short term leases. ▶ 577 properties held under two contractual arrangements were found to contain no lease contract. ▶ Certain lease arrangements had been incorrectly treated, with the underlying lease data used to calculate the transitional and initial year of implementation impact being incomplete and/or inaccurate. ▶ The IFRS 16 implementation and initial year adoption modelling failed to correctly account for property leases with specified fixed stepped lease payment increases over the lease term.

Risk	Our response to the risk	Key observations communicated to the Audit Committee
Valuation of the Group and parent's defined benefit pension obligation (Group 2020: net deficit £39.5m, Group 2019: net deficit £21.7m, Parent 2020: net deficit £3.0m, Parent 2019: net deficit £1.4m)	Scoping: We performed audit procedures over this risk area which covered 100% of the risk amount.	We conclude that management's actuarial assumptions are appropriate and fall within a central range or have been assessed and set on an appropriate basis.
<i>Refer to the Audit Committee Report (page 88); Accounting policies (page 169); and Note 29 of the Consolidated Financial Statements (page 169).</i> <i>The Group operates a number of defined benefit pension schemes ('Group schemes') and is an admitted body of other defined benefit pension schemes ('LGPS').</i>	Our procedures included: Assessing management's process: We have understood management's process and methodology for calculating the pension liability for each scheme, including discussions with management's external actuaries, walkthrough of the processes, understanding the key inputs and the design and implementation of key controls. We performed a fully substantive audit approach rather than testing the operating effectiveness of key controls.	We have noted below, for the assumptions that are assessed against a specific range, our ranges compared to management's assessment: Discount rate: 1.15%-1.55% (Mears rate: 1.35%) RPI inflation: 2.60%-3.25% (Mears rate: 2.85%).
Subjective valuation using complex actuarial assumptions: A gross defined benefit pension liability of £501.4m was held at 31 December 2020 in respect of all defined benefit pension schemes. Small changes in the assumptions and estimates used to value the Group's and parent's pension obligation (before deducting scheme assets) would have a significant effect on the carrying value of those pension obligations.	Assessing management's experts: We have assessed the independence, objectivity and competence of the Group's external actuaries, which included understanding the scope of services being provided and considering the appropriateness of the qualifications of the external actuary.	We conclude that Group scheme assets were under-valued based on external confirmations received. Management made adjustments to increase the Group scheme asset values by £0.9 to reflect this. Our testing did not identify any other material misstatements.
The effect of these matters is that, as part of our risk assessment, we determined that the Group's and parent company's pension obligation has a high degree of estimation uncertainty, with a potential range of reasonable outcomes greater than our materiality for the financial statements as a whole. The financial statements (note 29) discloses the estimation uncertainty identified by the Group and parent company.	Assessing source data: We tested a sample of the membership data used by the actuaries to the Group's records. We directly confirmed the existence and valuation of pension scheme assets with asset managers and custodians for Group Schemes and analysed the movements on assets for LGPS. We obtained the asset manager control assurance reports to provide assurance as to the reliability of their valuations. With the support of our valuation and actuarial specialists we independently challenged the valuation of scheme assets by performing detailed testing on a sample of assets across all asset categories.	We are satisfied with the adequacy of disclosure within the financial statements.
Valuation of defined benefit pension assets: The fair value of the defined pension scheme assets as at 31 December 2020 was £473.0m. Judgement is applied in valuing the more complex Group schemes' assets, while the LGPS assets are estimated by rolling forward the published asset position from the previous year using market index returns over the period.	Benchmarking assumptions: With the support of our pension actuarial specialists, we assessed and challenged the appropriateness of the assumptions adopted by the Directors by comparing them to the expectations of our pension actuarial specialists which they had derived from broader market data.	
The effect of these matters is that, as part of our risk assessment, we identified that the Group's and parent company's pension assets was one of the most significant assessed risks of material misstatement.	Disclosure: We considered the adequacy of IAS 19 disclosures, including sensitivity of the obligation to the key assumptions. All audit work in relation to this key audit matter was undertaken by the Group engagement team with assistance from our actuarial and valuation specialists.	

Financial statements continued

Independent auditor's report continued

to the members of Mears Group PLC

Risk	Our response to the risk	Key observations communicated to the Audit Committee
<p>Appropriateness of revenue recognition including contract accounting, contract assets and contract accruals (Group revenue 2020: £805.9m, Group revenue 2019: £881.5m)*</p> <p><i>Refer to the Audit Committee Report (page 88); Accounting policies (page 132); and Note 2 of the Consolidated Financial Statements (page 132)</i></p> <p>Mears has several different key revenue streams, which are aligned with the relevant revenue accounting policy. Determining the amount of revenue to be recognised requires management to make significant judgements and estimates in the application of IFRS 15, the stage of completion of certain contracts and the recoverability of WIP, mobilisation costs and contract assets.</p> <p>There is considered to be a risk of material error and management override in making this assessment.</p>	<p>Scoping: We performed audit procedures over this risk area which covered 100% of the risk amount.</p> <p>Our procedures included: Our response to the assessed risk included but was not limited to: We performed walkthroughs of the revenue recognition process for all material revenue streams to assess the design and implementation of key controls. We used data analysis tools on 100% of revenue transactions in the year to test the correlation between revenue, trade debtors and cash receipts to verify the occurrence of revenue. We tested non-correlating entries with detailed testing of a sample of revenue transactions to ensure that revenue had been appropriately recognised. We obtained the schedule of contract assets and selected a sample of contracts using the lower range of our testing threshold to include an element of unpredictability. We investigated the recoverability of contract assets balances by reference to post balance sheet cash collection, obtained the evidence from the work certified by the customer's or Group's internal or independent quantity surveyor. For revenue recognised but not certified by the customer's or Group's internal or independent quantity surveyor, we inquired the reason for non-certification and challenged the recognition of contract assets and related revenue. We challenged the estimated contract cost to complete including obtaining evidence to support our independent conclusions where relevant (eg verifying the work orders issued to sub-contractors and challenging the estimation basis of overheads). We held meetings with the in-house legal counsel and reviewed the board meeting minutes to identify and assess the impact of any ongoing disputes in relation to the recoverability of the contract assets balance and challenged the management on the recoverability of such contract assets where they had been recognised. For a sample of contracts, where the forecasted margin is low, we challenged management on the appropriateness of their onerous contracts provision. For a sample of customers, we obtained direct confirmations to verify their contract trade terms with Mears. We have obtained the deferred income schedule and ensured that revenue is recognised in accordance with IFRS 15. We selected a sample of revenue transactions recorded before and after year end to verify that the revenue had been recorded in the appropriate period. We selected a sample of credit notes issued after year-end and obtained documentation to verify that revenue adjustments at year end had been recorded appropriately.</p> <p>Disclosure: We assessed the adequacy of Group's disclosures in accordance with the requirements of IFRS 15, and whether management accounted for revenue in accordance with the accounting policies. All audit work in relation to this key audit matter was undertaken by the Group engagement team</p>	<p>For the year to 31 December 2019 certain contractual arrangements were accounted for under IFRS15 with a Mears group company incorrectly determined to be the principal rather than the agent. The prior year income statement has been restated to correct this error.</p>

Risk	Our response to the risk	Key observations communicated to the Audit Committee
Management override of controls focusing on manual journal entries, top-side consolidation adjustments, judgemental provisions and accruals	<p>Scoping: We performed audit procedures over this risk area centrally, covering both full and specific scope components.</p> <p>Our procedures included: We walked through the consolidation process to assess the design and implementation of key controls. We independently verified the results and balances of the consolidated entities by agreeing the results and balances included in the consolidation directly to the audited results and balances for all full and specific scope components. We obtained an understanding of all consolidation journal entries posted and specifically tested a sample of the journals to supporting evidence. We have tested journal entries throughout the audit process using our data analytics general ledger analyser tools to tag unusual journal entries based on their size and /or description. We identified 6 journal source types that in our judgement may be more susceptible to management override. We tested all journal entries greater than £100,000 impacting the income statement in December 2020 as we felt there was greater risk of management override close to the year end date. We tested journal entries in January 2021 for reversing entries to understand the adjusting impact on the 2020 financial statements. We understood the nature and appropriateness of material round sum amounts in accruals and provisions at the year end by challenging all round sum accruals greater than £40,000. We ensured we understood the reason for significant movements in provisions and accruals from the prior year and challenged management where there had been no movement. All audit work in relation to this key audit matter was undertaken by the Group engagement team.</p>	<p>We conclude that based on the audit procedures performed, manual journal entries, top-side consolidation adjustments, judgemental provisions and accruals are appropriate.</p>
<p><i>Accounting policies (page 131); set out in Note 1 of the Consolidated Financial Statements (page 129).</i></p> <p>There is a level of complexity within the business which necessitates high volumes of manual journal entries, and top-side adjustments in preparing the consolidated financial statements. This increases the risk that management will post an erroneous journal that will materially affect the Annual Report & Accounts.</p> <p>There are also a number of provisions and accruals at year end that are based on management judgement.</p>		<p>Our procedures did not identify any instances of management override of controls.</p>
Disposal accounting including recognition of profit on disposal and contingent consideration	<p>Scoping: We tested each disposal transaction fully substantively.</p> <p>Our procedures included: We confirmed that the disposal groups met the criterion to be classified as "held for sale" at the opening balance sheet date in accordance with IFRS5. We reperformed the calculation of the gains on disposal based on the carrying value of the assets held at date of disposal and sale proceeds received, including any estimated contingent consideration. We independently assessed the reasonableness of contingent consideration, most specifically in respect of the Terraquest disposal. We tested the completeness of transaction costs and consideration of warranties and indemnities in the context of provision requirements and/or contingent liability disclosures. We verified the disposal proceeds by checking to bank statements. We considered the accuracy of the disclosure of discontinued operations in the Annual Report and Accounts. All audit work in relation to this key audit matter was undertaken by the Group engagement team.</p>	<p>We conclude that based on the audit procedures performed, the disposal transactions have been accounted for appropriately.</p>

Financial statements continued

Independent auditor's report continued

to the members of Mears Group PLC

Risk	Our response to the risk	Key observations communicated to the Audit Committee
First year audit transition including assessment of opening balances	<p>Refer to the Audit Committee Report (page 91)</p> <p>The year ended 31 December 2020 is our first as auditor of the Group. We commenced our audit planning procedures subsequent to us being formally appointed by Mears Group plc on 9 September 2020. From the procedures performed during our review of the predecessor auditors working papers we noted several unadjusted differences that were immaterial individually and in aggregate. In response to the unadjusted differences we designed our initial audit procedures to cover both opening balance sheet procedures and year end audit requirements. Accordingly, we amended our planned audit approach, including the refinement of our risk assessment and redesign of audit procedures. Given the refinements made to our initial planned audit approach, we consider this to be a Key Audit Matter.</p> <p>Scoping: We performed audit procedures over this risk area centrally, covering both full and specific scope components.</p> <p>We have performed procedures since our appointment covering initial transition activities, opening balance sheet procedures and the year end audit requirements for the components within the Group.</p> <p>Our transition activities included:</p> <ul style="list-style-type: none"> ▶ Establishing independence from Mears Group plc by considering non-audit services which may impair or be perceived to impair our independence. We identified no such services; ▶ Establishing an appropriately resourced and skilled audit team, including specialists; ▶ Holding introductory meetings with Mears Group plc management; ▶ Establishing an audit approach, with specific amendment of key risks and audit focus based on interim conclusions and resulting prior year adjustments; and ▶ Establishing an IT approach and subsequent refinements after obtaining an initial understanding and performing walkthroughs of the IT General Controls. <p>Our opening balance sheet procedures included, but were not limited to:</p> <ul style="list-style-type: none"> ▶ Reviewing the previous auditor's 2019 audit files and holding discussions with the previous audit team; ▶ Holding a planning meeting in September 2020 at Mears' Head Office in Gloucester at which members of Mears Group plc management briefed senior members of our Group audit on Mears Group plc's organisation; ▶ Identifying significant risk and other audit matters to direct our specific testing of opening balances. This testing involved challenging key assumptions and estimations and reviewing the appropriateness of management's prior year conclusions; ▶ Understanding accounting policies and historic accounting judgments by reviewing accounting policy papers prepared by management on specific accounting topics; and ▶ Performing detailed walkthroughs of key processes. <p>As a result of the procedures performed, we identified prior year adjustments at 31 December 2019 relating to the implementation of IFRS16 (as set out in the IFRS16 KAM above) We reassessed our audit approach to reflect these errors, which included:</p> <ul style="list-style-type: none"> ▶ We considered the root cause of the prior year adjustments and the impact on our reliance on the opening balance sheet. ▶ We increased focus on the areas in which prior year errors had been identified, including increased level of senior team involvement and we reported all outcomes on these areas to the Audit Committee. ▶ We set our performance materiality at 50% of planning materiality to reflect our first year of audit involvement, the number of errors identified in the prior year and to address the risk of undetected material misstatements ▶ Full details of the adjustments are disclosed in Note 33 to the accounts <p>All audit testing was performed by the Group engagement team.</p>	<p>We conclude that, based on the procedures performed, the opening balances are fairly stated, following adjustment to correctly account for IFRS16 as described in the KAM above.</p>

Our application of materiality

We apply the concept of materiality in planning and performing the audit, in evaluating the effect of identified misstatements on the audit and in forming our audit opinion. Any prior year reference relates to the assessment used by Grant Thornton UK LLP.

Materiality

The magnitude of an omission or misstatement that, individually or in the aggregate, could reasonably be expected to influence the economic decisions of the users of the financial statements. Materiality provides a basis for determining the nature and extent of our audit procedures.

We determined materiality for the Group to be £1.1million (2019: £1.3 million), which represents our professional judgement based on the relevant metrics used by investors and other users of the financial statements and represents 4.75% of normalised profit before tax from continuing operations (2019: 4.75% of the Group's continuing profit before exceptional items and taxation). Materiality in 2020 was based on our judgement of normalised earnings of the group from continuing operations. To form the basis of this assessment we have considered the average profit from continuing operations before tax for financial years 2018 and 2019, and the forecast profit before tax for financial year 2021, reduced by 12.5% to allow for the impact of further Covid-19 restrictions in the first quarter of 2021.

We capped our materiality for the Parent Company at the Group materiality of £1.1 million (2019: £0.8 million), which is 1% (2019: 1%) of net assets.

During the course of our audit, we reassessed initial materiality to reflect the continuing impact of Covid-19 on Mears Group plc. We concluded that no change is required to our final materiality.

Performance materiality

The application of materiality at the individual account or balance level. It is set at an amount to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds materiality.

On the basis of our risk assessments, together with our assessment of the Group's overall control environment, our judgement was that performance materiality was 50% (2019: 70%) of our planning materiality, namely £550,000 (2019: £910,000). We have set performance materiality at this percentage due to differences identified relating to both the current year and prior year adjustments.

Audit work at component locations for the purpose of obtaining audit coverage over significant financial statement accounts is undertaken based on a percentage of total performance materiality. The performance materiality set for each component is based on the relative scale and risk of the component to the Group as a whole and our assessment of the risk of misstatement at that component. In the current year, the range of performance materiality allocated to components was £75,000 to £500,000.

Reporting threshold

An amount below which identified misstatements are considered as being clearly trivial.

We agreed with the Audit Committee that we would report to them all uncorrected audit differences in excess of £55,000 (2019: £65,000), which is set at 5% of planning materiality, as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds.

We evaluate any uncorrected misstatements against both the quantitative measures of materiality discussed above and in light of other relevant qualitative considerations in forming our opinion.

Other information

The other information comprises the information included in the annual report set out on pages 1 to 112, including the Strategic Report, set out on pages 1 to 69, Corporate Governance, set out on pages 71 to 112, and Shareholder information, set out on pages 191 and 192, other than the financial statements and our auditor's report thereon. The directors are responsible for the other information contained within the annual report.

Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in this report, we do not express any form of assurance conclusion thereon.

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

We have nothing to report in this regard.

Financial statements continued

Independent auditor's report continued to the members of Mears Group PLC

Opinions on other matters prescribed by the Companies Act 2006

In our opinion, the part of the directors' remuneration report to be audited has been properly prepared in accordance with the Companies Act 2006.

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

- ▶ the information given in the strategic report and the directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- ▶ the strategic report and the directors' report have been prepared in accordance with applicable legal requirements.

Matters on which we are required to report by exception

In the light of the knowledge and understanding of the group and the parent company and its environment obtained in the course of the audit, we have not identified material misstatements in the strategic report or the directors' report.

We have nothing to report in respect of the following matters in relation to which the Companies Act 2006 requires us 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

Corporate Governance Statement

The Listing Rules require us to review the directors' statement in relation to going concern, longer-term viability and that part of the Corporate Governance Statement relating to the group and company's compliance with the provisions of the UK Corporate Governance Code specified for our review.

Based on the work undertaken as part of our audit, we have concluded that each of the following elements of the Corporate Governance Statement is materially consistent with the financial statements or our knowledge obtained during the audit:

- ▶ Directors' statement with regards to the appropriateness of adopting the going concern basis of accounting and any material uncertainties identified set out on page 130;
- ▶ Directors' explanation as to its assessment of the company's prospects, the period this assessment covers and why the period is appropriate set out on page 68;
- ▶ Directors' statement on fair, balanced and understandable set out on page 85;
- ▶ Board's confirmation that it has carried out a robust assessment of the emerging and principal risks set out on page 65 to 67;
- ▶ The section of the annual report that describes the review of effectiveness of risk management and internal control systems set out on page 89; and;
- ▶ The section describing the work of the audit committee set out on page 84.

Responsibilities of directors

As explained more fully in the directors' responsibilities statement set out on page 112, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the group and parent company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the group or the parent company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

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

Explanation as to what extent the audit was considered capable of detecting irregularities, including fraud

Irregularities, including fraud, are instances of non-compliance with laws and regulations. We design procedures in line with our responsibilities, outlined above, to detect irregularities, including fraud. The risk of not detecting a material misstatement due to fraud is higher than the risk of not detecting one resulting from error, as fraud may involve deliberate concealment by, for example, forgery or intentional misrepresentations, or through collusion. The extent to which our procedures are capable of detecting irregularities, including fraud is detailed below.

However, the primary responsibility for the prevention and detection of fraud rests with both those charged with governance of the company and management.

- ▶ We obtained an understanding of the legal and regulatory frameworks that are applicable to the group and determined that the most significant are those that relate to the reporting framework (IFRS, FRS101 and the Companies Act 2006, then Financial Reporting Council (FRC) and the UK Corporate Governance Code) and the relevant tax compliance regulations in the UK.
- ▶ We understood how Mears Group plc is complying with those frameworks by reading internal policies and assessing the entity level control environment, including the level of oversight of those charged with governance. We made enquiries of the Chair of the Audit Committee, the group's legal counsel and internal audit of any known instances of non-compliance or suspected non-compliance with laws and regulations. We corroborated our enquiries through review of correspondence with regulatory bodies. We designed our audit procedures to identify non-compliance with such laws and regulations identified in the paragraph above.
- ▶ We assessed the susceptibility of the group's financial statements to material misstatement, including how fraud might occur by considering the programs and controls that the group has established to address risks identified by the entity, or that otherwise prevent, deter and detect fraud, how senior management monitor those programs and controls, evaluating conditions in the context of incentive and/or pressure to commit fraud, considering the opportunity to commit fraud and the potential rationalisation of the fraudulent act.
- ▶ Based on this understanding we designed our audit procedures to identify non-compliance with such laws and regulations. Our procedures involved making enquiries of senior management, including the Group Finance Director, Company Secretary and Chair of the Audit Committee. As well as attendance and enquiry at meetings, our procedures involved a review of board meetings, internal audit reports, and other committee minutes to identify any non-compliance with laws and regulations. We planned our audit procedures to identify risks of management override, tested higher risk journal entries and performed audit procedures to address the potential for management bias, particularly over areas involving significant estimation. Further detail of our approach to address the identified risks of management override are set out in the key audit matters section of our report.

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website at <https://www.frc.org.uk/auditorsresponsibilities>. This description forms part of our auditor's report.

Other matters we are required to address

- ▶ Following the recommendation from the audit committee, we were appointed as auditors by the Board of Directors of Mears Group plc and signed an engagement letter on 9 September 2020, to audit the financial statements for the year ending 31 December 2020, and subsequent periods. The period of total uninterrupted engagement including previous renewals and reappointments is one year, covering the years ending 31 December 2020.
- ▶ The non-audit services prohibited by the FRC's Ethical Standard were not provided to the group or the parent company and we remain independent of the group and the parent company in conducting the audit.
- ▶ The audit opinion is consistent with the additional report to the audit committee.

Use of our report

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

Paul Mapleston (Senior statutory auditor)
for and on behalf of Ernst & Young LLP, Statutory Auditor
 Bristol
 12 May 2021

Financial statements continued

Consolidated statement of profit or loss

For the year ended 31 December 2020

	Note	2020 £'000	2019 (restated*) £'000
Continuing operations			
Sales revenue	2	805,817	881,457
Cost of sales		(649,530)	(675,348)
Gross profit		156,287	206,109
Other administrative expenses		(150,759)	(165,880)
Exceptional costs	8	(2,279)	(2,018)
Amortisation of acquisition intangibles	14	(9,525)	(10,122)
Total administrative costs		(162,563)	(178,020)
Operating profit before exceptional costs and amortisation of acquisition intangibles		5,528	40,229
Operating (loss)/profit		(6,276)	28,089
Share of profits of associates	17	1,056	895
Finance income	5	293	849
Finance costs	5	(10,291)	(9,580)
(Loss)/profit for the year before tax, exceptional costs and amortisation of acquisition intangibles		(3,414)	32,393
(Loss)/profit for the year before tax		(15,218)	20,253
Tax credit/(expense)	9	3,207	(3,015)
(Loss)/profit for the year from continuing operations		(12,011)	17,238
Discontinued operations			
Profit/(loss) from discontinued operations	10	56,933	(82,223)
Tax charge on discontinued operations	9	(121)	(1,061)
Profit/(loss) for the year after tax from discontinued operations		56,812	(83,284)
Profit/(loss) for the year from continuing and discontinued operations		44,801	(66,046)
Attributable to:			
Owners of Mears Group PLC		44,519	(66,388)
Non-controlling interest		282	342
Profit/(loss) for the year		44,801	(66,046)
Earnings per share – from continuing operations			
Basic	12	(10.66)p	15.72p
Diluted	12	(10.66)p	15.64p
Earnings per share – from continuing and discontinued operations			
Basic	12	40.21p	(60.09)p
Diluted	12	40.21p	(59.77)p

* Note 33 contains details of the restatement of the prior year figures.

The accompanying accounting policies and notes form an integral part of these financial statements.

Consolidated statement of comprehensive income

For the year ended 31 December 2020

	Note	2020 £'000	2019 (restated*) £'000
Profit/(loss) for the year		44,801	(66,046)
Other comprehensive expense:			
Which will be subsequently reclassified to the Consolidated Statement of Profit or Loss:			
Cash flow hedges:			
▶ losses arising in the year	24	(1,139)	(145)
▶ reclassification to the Consolidated Statement of Profit or Loss	24	354	49
Increase in deferred tax asset in respect of cash flow hedges	25	149	18
Which will not be subsequently reclassified to the Consolidated Statement of Profit or Loss:			
Actuarial loss on defined benefit pension scheme	29	(19,114)	(15,519)
Pension guarantee asset movements in respect of actuarial loss	29	10,024	4,231
Increase in deferred tax asset in respect of defined benefit pension schemes	25	1,727	2,145
Other comprehensive expense for the year		(7,999)	(9,221)
Total comprehensive income/(expense) for the year		36,802	(75,267)
Attributable to:			
Owners of Mears Group PLC		36,520	(75,609)
Non-controlling interest		282	342
Total comprehensive income/(expense) for the year		36,802	(75,267)
Total comprehensive income/(expense) for the year attributable to owners of Mears Group PLC arises from:			
Continuing operations		(19,721)	8,146
Discontinued operations		56,241	(83,755)
Total comprehensive income/(expense) for the year attributable to owners of Mears Group PLC		36,520	(75,609)

* Note 33 contains details of the restatement of the prior year figures.

The accompanying accounting policies and notes form an integral part of these financial statements.

Financial statements continued

Consolidated balance sheet

As at 31 December 2020

	Note	2020 £'000	2019 (restated*) £'000
Assets			
Non-current			
Goodwill	13	118,873	123,204
Intangible assets	14	15,205	28,642
Property, plant and equipment	15	23,600	26,326
Right of use assets	16	200,041	198,384
Investments	17	966	536
Loan notes	24	3,160	—
Contingent consideration	24	5,431	—
Pension and other employee benefits	29	7,068	8,249
Pension guarantee assets	29	30,705	23,810
Deferred tax asset	25	3,320	—
		408,369	409,151
Current			
Assets classified as held for sale	10	—	11,185
Inventories	18	31,258	36,045
Trade and other receivables	19	139,884	164,091
Current tax assets		358	—
Cash and cash equivalents	24	96,220	72,909
		267,720	284,230
Total assets		676,089	693,381
Equity			
Equity attributable to the shareholders of Mears Group PLC			
Called up share capital	26	1,109	1,105
Share premium account		82,225	82,224
Share-based payment reserve		1,312	2,421
Hedging reserve	24	(760)	(124)
Merger reserve		7,971	12,956
Retained earnings		63,536	19,840
Total equity attributable to the shareholders of Mears Group PLC		155,393	118,422
Non-controlling interest		658	(85)
Total equity		156,051	118,337
Liabilities			
Non-current			
Long-term borrowing and overdrafts	24	39,353	124,047
Pension and other employee benefits	29	45,653	29,971
Deferred tax liabilities	25	—	1,572
Interest rate swaps	24	462	39
Lease liabilities	21	166,183	166,000
Other payables	23	3,667	4,700
		255,318	326,329
Current			
Trade and other payables	20	221,029	202,366
Interest rate swaps	24	459	119
Lease liabilities	21	42,888	39,175
Provisions	22	344	504
Current tax liabilities		—	659
Liabilities related to assets classified as held for sale	10	—	5,892
Current liabilities		264,720	248,715
Total liabilities		520,038	575,044
Total equity and liabilities		676,089	693,381

* Note 33 contains details of the restatement of the prior year figures.

The financial statements were approved and authorised for issue by the Board of Directors and were signed on its behalf on 12 May 2021.

D J Miles
Director

A C M Smith
Director

Company number: 03232863

The accompanying accounting policies and notes form an integral part of these financial statements

Consolidated cash flow statement

For the year ended 31 December 2020

	Note	2020 £'000	2019 (restated*) £'000
Operating activities			
Result for the year before tax	27	(15,218)	20,253
Adjustments		72,761	56,819
Change in inventories		4,787	(6,357)
Change in trade and other receivables		18,475	2,680
Change in trade, other payables and provisions		22,418	13,523
Cash inflow from operating activities of continuing operations before taxation		103,223	86,918
Taxes paid		41	(3,377)
Net cash inflow from operating activities of continuing operations		103,264	83,541
Net cash outflow from operating activities of discontinued operations		2,527	4,904
Net cash inflow from operating activities		105,791	88,445
Investing activities			
Additions to property, plant and equipment		(5,065)	(8,377)
Additions to other intangible assets		(1,717)	(1,679)
Proceeds from disposals of property, plant and equipment		17	46
Cash inflow in respect of property for resale	28	4,618	7,824
Payments on acquisitions, net of cash acquired		–	(1,300)
Loans repaid by/(made to) other entities (non-controlled)		10	(48)
Interest received		86	363
Net cash outflow from investing activities of continuing operations		(2,051)	(3,171)
Net cash inflow/(outflow) from investing activities of discontinued operations		54,612	(2,309)
Net cash inflow/(outflow) from investing activities		52,561	(5,480)
Financing activities			
Proceeds from share issue		4	1
Repayment of borrowings related to assets classified as held for sale	27	–	(15,000)
Net movement in revolving credit facility		(84,694)	30,267
Discharge of lease liabilities		(39,958)	(29,179)
Interest paid		(10,056)	(9,446)
Dividends paid – Mears Group shareholders		–	(13,811)
Net cash outflow from financing activities of continuing operations		(134,704)	(37,168)
Net cash outflow from financing activities of discontinued operations		(489)	(612)
Net cash outflow from financing activities		(135,193)	(37,780)
Cash and cash equivalents, beginning of year		73,061	27,876
Net increase in cash and cash equivalents		23,159	45,185
Cash and cash equivalents, end of year (including discontinued)		96,220	73,061
The Group considers its revolving credit facility to be an integral part of its cash management:			
► Cash and cash equivalents		96,220	73,061
► Revolving credit facility		(39,353)	(124,047)
Cash and cash equivalents, including revolving credit facility		56,867	(50,986)

* Note 33 contains details of the restatement of the prior year figures.

The accompanying accounting policies and notes form an integral part of these financial statements.

Financial statements continued

Consolidated statement of changes in equity

For the year ended 31 December 2020

	Attributable to equity shareholders of the Company							
	Share capital £'000	Share premium account £'000	Share-based payment reserve £'000	Hedging reserve £'000	Merger reserve £'000	Retained earnings £'000	Non-controlling interest £'000	Total equity £'000
At 1 January 2019	1,105	82,224	2,021	(46)	46,214	79,189	(427)	210,280
Impact of change in accounting policies (restated*)	–	–	–	–	–	(3,074)	–	(3,074)
Adjusted balance at 1 January 2019 (restated*)	1,105	82,224	2,021	(46)	46,214	76,115	(427)	207,206
Net result for the year (restated*)	–	–	–	–	–	(66,388)	342	(66,046)
Other comprehensive income	–	–	–	(78)	–	(9,143)	–	(9,221)
Total comprehensive income for the year (restated*)	–	–	–	(78)	–	(75,531)	342	(75,267)
Deferred tax on share-based payments	–	–	–	–	–	(191)	–	(191)
Share options – value of employee services	–	–	400	–	–	–	–	400
Transfer of realised profits	–	–	–	–	(33,258)	33,258	–	–
Dividends	–	–	–	–	–	(13,811)	–	(13,811)
At 1 January 2020	1,105	82,224	2,421	(124)	12,956	19,840	(85)	118,337
Net result for the year	–	–	–	–	–	44,519	282	44,801
Other comprehensive income	–	–	–	(636)	–	(7,363)	–	(7,999)
Total comprehensive income for the year	–	–	–	(636)	–	37,156	282	36,802
Deferred tax on share-based payments	–	–	–	–	–	10	–	10
Issue of shares	4	1	–	–	–	–	–	5
Share options – value of employee services	–	–	1,029	–	–	–	–	1,029
Share options – exercised or lapsed	–	–	(2,138)	–	–	2,138	–	–
Non-controlling interest eliminated on disposal of subsidiary	–	–	–	–	–	–	(132)	(132)
Transactions with non-controlling interests	–	–	–	–	–	(593)	593	–
Transfer of realised profits	–	–	–	–	(4,985)	4,985	–	–
At 31 December 2020	1,109	82,225	1,312	(760)	7,971	63,536	658	156,051

* Note 33 contains details of the restatement of the prior year figures.

The accompanying accounting policies and notes form an integral part of these financial statements.

Notes to the financial statements – Group

For the year ended 31 December 2020

1. Accounting policies

Accounting policies are detailed in their respective notes, where relevant. Policies that are not specific to a particular note are detailed below.

Basis of preparation

The consolidated financial statements of the Group have been prepared in accordance with International Accounting Standards in conformity with the requirements of the Companies Act 2006 and International Financial Reporting Standards (IFRS) adopted pursuant to Regulation (EC) No. 1606/2002 as it applies in the European Union and as issued by the International Accounting Standards Board (IASB). The financial statements are prepared under the historical cost convention as modified by the revaluation of derivative financial instruments and share-based payments. They are presented in Sterling and all values are rounded to the nearest thousand (£'000).

The accounting policies remain unchanged from the previous year except for the modification of a number of standards with effect from 1 January 2020. Changes include Amendments to IFRS 3 (Definition of a Business); IAS 1 and IAS 8 (Definition of Material) and IFRS 9, IAS 39 and IFRS 7 (Interest Rate Benchmark Reform). The adoption of these amendments had no material effect on the Group's financial statements.

The preparation of financial statements in conformity with IFRS requires the use of estimates and judgements that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the year. Although these estimates are based on management's best knowledge of the amounts, actual results may ultimately differ from those estimates. The most significant estimates made by management in these financial statements are set out in the accounting policies to which they relate.

Mears Group PLC is incorporated and domiciled in England and Wales (registration number 03232863). Its registered office and principal place of business is 1390 Montpellier Court, Gloucester Business Park, Brockworth, Gloucester GL3 4AH. Mears Group PLC's shares are listed on the London Stock Exchange.

Basis of consolidation

The Consolidated Balance Sheet includes the assets and liabilities of the Company and its subsidiaries and is made up to 31 December 2020. Entities for which the Group has the ability to exercise control over financial and operating policies are accounted for as subsidiaries. Control is achieved where the Company has existing rights that give it the current ability to direct the activities that affect the Company's returns and exposure or rights to variable returns from the entity. Interests acquired in entities are consolidated from the effective date of acquisition and interests sold are consolidated up to the date of disposal.

All significant intercompany transactions and balances between Group enterprises, including unrealised profits arising from intra-group transactions, are eliminated on consolidation; no profit is taken on sales between Group companies.

Non-controlling interests in the net assets of consolidated subsidiaries are identified separately from the Group's equity therein. Non-controlling interests consist of the amount of those interests at the date of the original business combination and the non-controlling shareholders' share of changes in equity since the date of the combination. Total comprehensive income is attributed to non-controlling interests even if this results in the non-controlling interest having a deficit balance.

A joint venture is a joint arrangement whereby the parties that have joint control have the rights to the net assets of the arrangement. Associates are entities over which the Group does not have control, but has significant influence. Investments in joint ventures and associates are accounted for using the equity method of accounting. Under this method, the Group's share of post-acquisition profits or losses is recognised in the Consolidated Statement of Profit or Loss; the cost of the investment in a given joint venture or associate, together with the Group's share of that entity's post-acquisition changes to shareholders' funds, is included in investments within the Consolidated Balance Sheet.

Financial statements continued

Notes to the financial statements – Group continued

For the year ended 31 December 2020

1. Accounting policies continued

Going concern

The Directors consider that, as at the date of approving the financial statements, there is a reasonable expectation that the Group and Company have adequate resources to continue in operational existence for the period to at least 30 June 2022. When making this assessment, management considers whether the Group will be able to maintain adequate liquidity headroom above the level of its borrowing facilities and to operate within the financial covenants applicable to those facilities which will be measured at 30 June 2021, 31 December 2021 and 30 June 2022. At 31 December 2020, the Group had £145m of committed borrowing facilities, maturing in November 2022. Since the year end, the Directors have voluntarily cancelled £25m of facilities, with the total commitments available reduced to £120m at the date of signing. The principal borrowing facilities are subject to covenants as detailed within the Finance Review section of the Strategic Report. The Strategic Report also details the principal risks and uncertainties and how the Group manages its risks. Note 24 to the financial statements sets out more information on the Group's objectives, policies and processes for managing its capital, its financial risk management objectives, details of its financial instruments and hedging activities, and its exposures to credit and liquidity risk. During the year, certain covenants were renegotiated due to the initial effects of the COVID-19 pandemic resulting in a very significant headroom at 31 December 2020. The covenants will return to the previous measures from 31 December 2021 and the Group has modelled its cash flow outlook for the period to 30 June 2022 and the forecasts indicate significant liquidity headroom will be maintained above the Group's borrowing facilities and that financial covenants will be met throughout the period, including the covenant tests at 30 June 2021 and 31 December 2021. The Group's existing debt facilities run to November 2022. The Group considers that there will be enough appetite from its existing or new funders to provide the required level of funding on similar terms, as supported by evidence from the facility amendments during 2020, the positive trading outlook and the time available to renegotiate as necessary.

The Group has carried out stress tests against the base case to determine the performance levels that would result in a breach of covenants or a reduction of headroom against its borrowing facilities to £nil. The Group's average contract length is broadly five years and the Group has a good track record of re-securing work on re-bid but it has modelled a significant deterioration whereby it fails to re-secure any material contracts during the going concern period to 30 June 2022. Additionally, the Group has also modelled an operating margin reduction of 2% for a single duration of 3 months within the going concern period. Combining these scenarios shows that the Group would remain viable even in the event of a severe business failure over an extended period. Consequently, the Directors consider any scenario which would cause the business to be no longer a going concern to be implausible. The Group has continued to trade profitably during the latest lockdown and is confident in its ability to return to more normalised activity levels during the remainder of 2021. The Group also has several mitigating actions under its control including minimising capital expenditure to critical requirements, reducing levels of discretionary spend, rationalising its overhead base and curtailing future dividend payments which, should they be required, could be implemented in order to be able to meet the covenant tests and to continue to operate within borrowing facility limits. Further detail regarding the Group's stress testing is provided in the Business planning and financial viability section on pages 68 and 69. After making these assessments, the Directors have a reasonable expectation that the Company and its subsidiaries have adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the Annual Report and Accounts.

Business combinations

Business combinations are accounted for using the acquisition method. The acquisition method involves the recognition at fair value of all identifiable assets and liabilities, including contingent liabilities of the subsidiary at the acquisition date, regardless of whether or not they were recorded in the financial statements of the subsidiary prior to acquisition. On initial recognition, the assets and liabilities of the subsidiary are included in the Consolidated Balance Sheet at their fair values, which are also used as the bases for subsequent measurement in accordance with the Group accounting policies. Goodwill is stated after separating out identifiable intangible assets. Goodwill represents the excess of acquisition cost over the fair value of the Group's share of the identifiable net assets of the acquired subsidiary at the date of acquisition.

Where applicable, the consideration for an acquisition includes any assets or liabilities arising from a contingent consideration arrangement, measured at fair value at the acquisition date. Subsequent changes in such fair values are adjusted against the cost of acquisition where they result from additional information obtained up to one year from the acquisition date about facts and circumstances that existed at the acquisition date. All other subsequent changes in the fair value of contingent consideration classified as an asset or liability are recognised in accordance with IFRS 9 in the Consolidated Statement of Profit or Loss.

For transactions with non-controlling parties that do not result in a change of control, the difference between the fair value of the consideration paid and the amount by which the non-controlling interest is adjusted is recognised in equity.

Any business combinations prior to 1 January 2010 were accounted for in accordance with the standards in place at the time, which differ in the following respects: transaction costs directly attributable to the acquisition formed part of the acquisition costs; contingent consideration was recognised if, and only if, the Group had a present obligation, the economic outflow was more likely than not and a reliable estimate was determinable; and subsequent adjustments to the contingent consideration were recognised as part of goodwill.

1. Accounting policies continued

Fair value

The Group measures certain assets and liabilities at fair value on a recurring basis, including its interest rate swaps, contingent consideration and assets in the Group's defined benefit pension schemes.

Trade and other receivables, trade and other payables and other loans are initially measured at fair value and are subsequently held at amortised cost. Other assets are measured at fair value when they are assessed for impairment or on classification as held for sale.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The Group uses valuation techniques that maximise the use of relevant observable inputs using the following valuation hierarchy, ordered from highest to lowest priority:

Level 1 – Quoted prices in active markets for identical assets or liabilities.

Level 2 – Inputs other than quoted prices included in Level 1 that are observable either directly or indirectly.

Level 3 – Unobservable inputs, typically derived from the Group's own information with any necessary adjustments to eliminate factors specific to the Group.

For assets and liabilities measured at fair value on a recurring basis, the Group determines whether transfers have occurred between levels in the hierarchy by assessing the lowest level input that is significant to the most recent measurement.

Details of the particular valuation techniques used by the Group are provided in the relevant notes for each type of asset or liability measured at fair value.

Use of judgements and estimates

The preparation of financial statements requires management to make estimates and judgements that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of income and expenditure during the reported period. The estimates and associated judgements are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making judgements about carrying values of assets and liabilities that are not readily apparent from other sources.

The estimates and underlying judgements are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

In the preparation of these consolidated financial statements, key estimates and judgements have been made by management concerning provisions necessary for certain liabilities, the discount rates used and other judgements when recognising right of use assets for lease accounting, the timing of revenue recognition, the recoverability of contract assets and work in progress, actuarial estimates in respect of defined benefit pension schemes, the fair value of contingent consideration in respect of disposed entities and other similar evaluations. Actual amounts could differ from those estimates. Further details of key estimates and judgements are provided in the appropriate notes.

The impact of COVID-19 has been considered when making the estimates and judgements above. The global and local effects of the pandemic have primarily affected the discount rates used for lease accounting as well as the assumptions of discount rate and inflation rate used in calculating the Group's liabilities in respect of defined benefit pension schemes.

New standards and interpretations not yet applied

A number of standards have been modified with effect for accounting periods commencing on or after 1 January 2021. These include 'Interest Rate Benchmark Reform – Phase 2 – Amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16', 'IAS 37 – Cost of Fulfilling a Contract', 'IAS 16 – Proceeds Before Intended Use' and other existing standards arising from the Annual Improvements to IFRSs 2018-2020 cycle. None of these amendments are expected to have a material effect on the Group's financial statements.

Financial statements continued

Notes to the financial statements – Group continued

For the year ended 31 December 2020

2. Revenue

Accounting policy

Revenue is recognised in accordance with IFRS 15 'Revenue from Contracts with Customers'. IFRS 15 provides a single, principles-based, five-step model to be applied to all sales contracts. It is based on the transfer of control of goods and services to customers. The detail below sets out the principal types of contract and how the revenue is recognised in accordance with IFRS 15.

Repair and maintenance contracts

For contracts in this category, the customer raises orders on demand, for example to carry out responsive repairs. Revenue is derived from a mixture of lump-sum periodic payments and task-based payments depending on the terms of the individual contract.

Where a lump-sum payment is in place it may cover the administrative element of the contract or may cover the majority of the tasks undertaken within that contract with exclusions to this being charged in addition to the lump-sum charge. For the works covered by the lump-sum payment, the performance obligation is being available to deliver the goods and services in the scope of the contract, not the performance of the individual works orders themselves. Revenue is recognised on a straight-line basis as performance obligations are being met over time.

For works orders not covered by a lump-sum payment, each works order represents a distinct performance obligation and, as the customer controls the asset being enhanced through the works, the performance obligation is satisfied over time. Each works order can be broken down into one or more distinct tasks which are either complete or not complete. The stage of completion of the works order is assessed by looking at which tasks are complete. The transaction price for partly completed works orders is recognised as cost plus expected margin. The transaction price for completed works orders is the invoice value, which is typically determined by a pricing schedule referred to as a Schedule of Rates that provides a transaction price for each particular task.

Some contracts may include an element of variable revenue based on certain key performance indicators (KPIs). These are recognised either at a point in time or over time, depending on the nature of the KPI and the contractual agreement in which it is contained. Where there is uncertainty in the measurement of variable consideration, at both the start of the contract and subsequently, management will consider the facts and circumstances of the contract in determining either the most likely amount of variable consideration when the outcome is binary, or the expected value based on a range of possible considerations. Included within this assessment will be the extent to which there is a high probability that a significant reversal in variable consideration revenues will not occur once the uncertainty is subsequently resolved. This assessment will include consideration of the following factors: the total amount of the variable consideration; the proportion of consideration susceptible to judgements of customers or third parties, for example KPIs; the length of time expected before resolution of the uncertainty; and the Group's previous experience of similar contracts.

2. Revenue continued

Property income

Where the Group is acting as principal, lessor operating lease revenue is recognised in revenue on a straight-line basis over the tenancy.

Where the Group is providing a management service, Mears recognises revenue as an agent (the net management fee) on a straight-line basis. Where significant initial costs are required to make good the housing to perform Housing Management activities, the costs directly attributable to the initial upgrade will be recognised as costs incurred to fulfil a contract and held within current assets, to the extent that it is determined that costs are recoverable.

Where the Group is providing an accommodation and support service, revenue is recognised at a point in time for each night that the accommodation is occupied.

Some contracts may include an element of variable revenue based on certain KPIs. This is recognised on the same basis as above.

Where the Group enters into arrangements with customers for the provision of housing, an assessment is made as to whether this income is recognised under IFRS 15 or IFRS 16. The contract between the Group and the customer is deemed to contain a lease where the contract conveys the right to control an identified asset for a period of time in exchange for consideration. In this instance, the rental income is recognised on a straight-line basis over the life of the lease. All such sub-leased residential property leases are classified as operating leases. Revenue in respect of sub-leased residential property is disclosed separately.

Professional services

Revenue represents amounts recoverable from clients for professional services provided during the year. Revenue is recognised either at a point in time, where the performance obligation is completed instantaneously such as processing a planning application, or over time, where the services are delivered over time. For this latter category, revenue is recognised by reference to the time expended to date as a proportion of the total time expected to be required to complete the performance obligation.

Care services

The standalone selling prices for providing care are overtly stated in the contract, and the method of application of the rate of charge is on a unit of time basis, usually expressed as a rate per visit. Revenue will be recognised in respect of this single performance obligation, by reference to the chargeable rate and time for completed care visits in the period.

From time to time, care contracts with customers include a fixed fee per period for performing a consistent scope of care services. For these contract types, the revenue recognition is consistent with lump-sum payments included in repair and maintenance contracts, as described above.

Other

From time to time, the Group receives revenue that does not fall within any of the categories above but is not individually significant enough to require a specific policy. In these cases, the revenue is considered separately and recognised in accordance with IFRS 15.

Mobilisation

Across all revenue types, where a contract includes a mobilisation element, consideration is initially given to whether the mobilisation element contains any discrete performance obligations. If this is the case, an element of the total contract price is allocated to those performance obligations and recognised either at a point in time or over time, depending on the nature of the performance obligation. Mobilisation income is included in the revenue category to which the contract relates.

Where amounts are received for mobilisation elements that are not performance obligations, these amounts are allocated to the performance obligations in the contract to which they relate.

No revenue was recognised during 2020 in respect of mobilisation performance obligations.

Contracting projects

For contracting projects, the contract states the scope and specification of the construction works to be carried out, for a fixed price. Mears is continuously satisfying this single performance obligation as cost is incurred, determining progress against the performance obligation on an input basis. The customer controls the site or output as the work is being performed on it and therefore revenue is recognised over time where there is an enforceable right to payment for works completed to date and the work completed does not create an asset with an alternative use to the Group. An assessment is made of costs incurred to date and the costs required to complete the project. If a project is not deemed to be profitable, the unavoidable costs of fulfilling the contract are provided for immediately. This category also includes construction contracts where an end customer has not yet been identified and the revenue is recognised at the point of sale of the property, rather than over time.

Financial statements continued

Notes to the financial statements – Group continued

For the year ended 31 December 2020

2. Revenue continued**Key sources of estimation uncertainty****Contract recoverability**

Determining future contract profitability requires estimates of future revenues and costs to complete. In making these assessments there is a degree of inherent uncertainty. The Group utilises the appropriate expertise in determining these estimates and has well-established internal controls to assess and review the expected outcome.

Critical judgements in applying the Group's accounting policies**Revenue recognition**

The estimation techniques used for revenue and profit recognition in respect of contracting and variable consideration contracts require judgements to be made about the stage of completion of certain contracts and the recovery of work in progress, mobilisation costs and contract assets. Each contract is treated on its merits and subject to a regular review of the revenue and costs to complete that contract.

The Group's revenue disaggregated by pattern of revenue recognition is as follows:

	2020 £'000	2019 (restated) £'000
Revenue from contracts with customers		
Repairs and maintenance	449,974	562,181
Contracting	103,643	171,097
Property income	199,718	99,119
Professional services	47	645
Care services	19,825	19,237
Other	62	581
	773,269	852,860
Lease income	32,548	28,597
	805,817	881,457

All of the above categories fall exclusively within the Housing segment. In addition to the restatement detailed in note 33, revenue for 2019 has been re-presented in order to aid comparability with the 2020 disaggregation.

A total of £2.1m of revenue was recognised in respect of the balance of contract liabilities at the start of the year (2019: £1.9m).

Repairs and maintenance and care service revenue is typically invoiced between one and 30 days from completion of the performance obligation. Contracting revenue is typically invoiced based on the stage of completion of the overall contract. Property income is typically invoiced monthly in advance. Professional services revenue is typically invoiced monthly in arrears. Payment terms for revenue invoiced are typically 30 to 60 days from the date of invoice.

A maturity analysis of future minimum lessor income as at 31 December is shown in the table below:

	2020 £'000	2019 £'000
Less than 1 year	7,963	7,001
Between 1 and 2 years	2,938	2,314
Between 2 and 3 years	2,385	1,484
Between 3 and 4 years	2,087	1,484
Between 4 and 5 years	1,683	1,488
Over 5 years	2,296	3,767
	19,352	17,538

3. Segment reporting

Accounting policy

Segment information is presented in respect of the Group's operating segments based on the format that the Group reports to its chief operating decision maker.

The Group considers that the chief operating decision maker comprises the Executive Directors of the business.

The Group had one continuing operating segment during the year:

- Housing – following the disposal of the Group's domiciliary care operations, all services provided by the Group fall within this segment. This includes housing repairs and maintenance services, a full housing management service and Care services directly related to housing provision.

All of the Group's activities are carried out within the United Kingdom and the Group's principal reporting to its chief operating decision maker is not segmented by geography.

The principal financial measures used by the chief operating decision maker to review the performance of the Group are those of revenue growth and operating margin. The operating result utilised within the key performance measures is stated before amortisation of acquisition intangibles and costs relating to the long-term incentive plans. Whilst the Strategic Report includes reference to a number of sub-categories of activities, this has been included to assist stakeholders in understanding the Group's business model. The key decision around the allocation of resources is made at the full continuing Group level.

The disclosures below also include information in respect of the discontinued activities of the business, which comprise Care and Planning Solutions activities.

	2020		2019 (restated)	
	Housing (continuing) £'000	Care and Planning Solutions (discontinued) £'000	Housing (continuing) £'000	Care and Planning Solutions (discontinued) £'000
Operating segments				
Revenue	805,817	35,388	881,457	98,400
Operating result, including share of profits of associates, before exceptional costs, amortisation of acquisition intangibles and long-term incentive plans	7,577	4,105	41,524	(1,470)
Operating margin, including share of profits of associates, before exceptional costs amortisation of acquisition intangibles and long-term incentive plans	0.94%	11.60%	4.71%	(1.49%)
Long-term incentive plans	(993)	(36)	(400)	–
Operating result, including share of profits of associates, before exceptional costs and amortisation of acquisition intangibles	6,584	4,069	41,124	(1,470)
Exceptional (costs)/income	(2,279)	–	(2,018)	–
Impairment of assets to fair value less costs to sell	–	–	–	(80,562)
Profit on disposal of discontinued business	–	52,868	–	–
Amortisation of acquisition intangibles	(9,525)	–	(10,122)	–
Operating (loss)/profit including share of profits of associates	(5,220)	56,937	28,984	(82,032)
Net finance (costs)/income	(9,998)	(4)	(8,731)	(191)
Tax credit/(expense)	3,207	(121)	(3,015)	(1,061)
(Loss)/profit for the year	(12,011)	56,812	17,238	(83,284)

All revenue and all non-current assets arise within the United Kingdom. All of the revenue reported is external to the Group. No revenue in respect of a single customer comprises more than 8% of the total revenue reported.

Financial statements continued

Notes to the financial statements – Group continued

For the year ended 31 December 2020

4. Operating costs

Operating costs, relating to continuing activities, include the following:

	2020 £'000	2019 (restated) £'000
Share-based payments	993	400
Depreciation	47,688	35,187
Impairment of fixed assets	1,500	–
Amortisation of acquisition intangibles	9,525	10,122
Amortisation of other intangibles	2,211	2,109
Loss on disposal of property, plant and equipment	231	178

Fees payable for audit and non-audit services during the year were as follows:

	2020 £'000	2019 £'000
In respect of continuing activities:		
Fees payable to the auditor for the audit of the Group's financial statements	130	71
Other fees payable to the auditor in respect of:		
▶ auditing of accounts of subsidiary undertakings pursuant to legislation	485	265
▶ other audit related fees	–	9
Fees payable to the auditor in respect of discontinued activities	70	50
Total auditor's remuneration	685	395

5. Finance income and finance costs

	2020 £'000	2019 (restated) £'000
Interest charge on overdrafts and loans	(2,663)	(3,541)
Interest charge on hedged items (effective hedges)	(354)	(49)
Interest on lease obligations	(7,123)	(5,760)
Other interest	(19)	(122)
Finance costs on bank loans, overdrafts and finance leases	(10,159)	(9,472)
Interest charge on defined benefit obligation	(132)	(108)
Total finance costs	(10,291)	(9,580)
Interest income resulting from short-term bank deposits	6	48
Interest income resulting from defined benefit asset	234	540
Other interest income	53	261
Finance income	293	849
Net finance charge	(9,998)	(8,731)
Gains and losses on hedged items recognised in other comprehensive income		
Losses arising in the year	(1,139)	(145)
Reclassification to the Consolidated Statement of Profit or Loss	354	49
Changes in mark-to-market of interest rate swaps (effective hedges)	(785)	(96)

6. Employees

Accounting policy

Government grants are recognised where there is reasonable assurance that the grant will be received, and all attached conditions will be complied with. When the grant relates to an expense item, it is recognised as income on a systematic basis over the periods that the related costs, for which it is intended to compensate, are expensed.

During the period, the Group benefited from receipts from the UK Government under the Coronavirus Job Retention Scheme (CJRS). In accordance with IAS 20, amounts received were presented as a deduction to the employment costs upon which CJRS claims had been based.

Staff costs during the year were as follows:

	2020 £'000	2019 £'000
Wages and salaries	161,128	203,576
Social security costs	17,380	20,123
Other pension costs	9,454	9,120
	187,962	232,819

Wages and salaries are presented net of Coronavirus Job Retention Scheme receipts of £15.7m (2019: £nil).

The average number of employees of the Group during the year was:

	2020 £'000	2019 £'000
Site workers	3,474	3,796
Carers	703	724
Office and management	2,150	2,370
	6,327	6,890

7. Share-based employee remuneration

Accounting policy

All share-based payment arrangements are recognised in the consolidated financial statements in accordance with IFRS 2.

The Group operates equity-settled share-based remuneration plans for its employees. All employee services received in exchange for the grant of any share-based remuneration are measured at their fair values. These are indirectly determined by reference to the fair value (excluding the effect of non-market-based vesting conditions) of the share options awarded. Their value is determined at the date of grant and is not subsequently remeasured unless the conditions on which the award was granted are modified. The fair value at the date of the grant is calculated using the Black Scholes option pricing model and the cost is recognised on a straight-line basis over the vesting period. Adjustments are made to reflect expected and actual forfeitures during the vesting period. For Save As You Earn (SAYE) plans, employees are required to contribute towards the plan. This non-vesting condition is taken into account in calculating the fair value of the option at the grant date.

All share-based remuneration is ultimately recognised as an expense in the Consolidated Statement of Profit or Loss. For equity-settled share-based payments there is a corresponding credit to the share-based payment reserve.

Upon exercise of share options, the proceeds received net of any directly attributable transaction costs up to the nominal value of the shares issued are allocated to share capital, with any excess being recorded as share premium.

As at 31 December 2020 the Group maintained four active share-based payment schemes for employee remuneration.

Financial statements continued

Notes to the financial statements – Group continued

For the year ended 31 December 2020

7. Share-based employee remuneration continued

Details of the share options outstanding and movement during the year are as follows:

	2020		2019	
	Number '000	Weighted average exercise price p	Number '000	Weighted average exercise price p
Operating segments				
Outstanding at 1 January	3,325	217	2,752	265
Granted	4,004	93	1,704	216
Forfeited or lapsed	(1,647)	240	(1,128)	333
Exercised	(390)	7	(3)	26
Outstanding at 31 December	5,292	131	3,325	217

The weighted average share price at the date of exercise for share options exercised during the period was 129p. At 31 December 2020, 0.4m options had vested and were still exercisable at prices between 1p and 429p. These options had a weighted average exercise price of 314p and a weighted average remaining contractual life of 3.0 years.

The fair values of options granted were determined using the Black Scholes option pricing model. Significant inputs into the calculation include the market price at the date of grant, the exercise price and share price volatility. Furthermore, the calculation incorporates an estimate of the future dividend yield and the risk-free interest rate. The share price volatility was determined from the daily log normal distributions of the Company share price over a period commensurate with the expected life as calculated back from the date of grant. The risk-free interest rate utilised the zero-coupon bond yield derived from UK Government bonds as at the date of calculation for a life commensurate with the expected life. Adjustments are made to reflect expected and actual forfeitures during the vesting period due to failure to satisfy service conditions.

There were 4.0m options granted during the year and 1.6m options that lapsed during the year. The market price at 31 December 2020 was 154p and the range during 2020 was 106p to 320p.

All share-based employee remuneration will be settled in equity. The Group has no legal obligation to repurchase or settle the options.

The Group recognised the following expenses related to share-based payments:

	2020 £'000	2019 £'000
Giving rise to share-based payment reserve:		
▶ SAYE	682	93
▶ Share plan	347	307
	1,029	400

The Group is currently running four active schemes, detailed below:

Share Incentive Plan (SIP)

All employees are eligible to participate in the Company's Share Incentive Plan. Under the terms of the plan, all employees can apply for three or five-year options to acquire the Company's shares priced at a discount of up to 20%. Under the terms of the SIP, the Company can choose to offer free shares, partnership shares, matching shares (up to two for one on any partnership shares purchased) and/or dividend shares.

To date, no awards have been granted under this plan.

Options are exercisable at a price equal to the average quoted market price of the Company's shares on the three dealing days prior to the date of grant. The vesting period is three years. If the options remain unexercised after a period of 10 years from the date of grant, the options expire. Options are forfeited if the employee leaves Mears Group before the options vest.

Share save plan (Save As You Earn (SAYE))

Options are available to all employees. Options are granted for a period of three years. Options are exercisable at a price based on the quoted market price of the Company's shares at the time of invitation, discounted by up to 20%. Options are forfeited if the employee leaves Mears Group before the options vest, which impacts on the number of options expected to vest. If an employee stops saving but continues in employment, this is treated as a cancellation, which results in an acceleration of the share-based payment charge.

7. Share-based employee remuneration continued

Company Share Option Plan (CSOP)

The Company operates a discretionary unapproved share plan and a Company Share Option Plan. Options are exercisable at a price below market value at the date of grant and often at nominal value. The vesting period is three years. If the options remain unexercised after a period of 10 years from the date of grant, the options expire. Options are forfeited if the employee leaves Mears Group before the options vest. No awards to Executive Directors are proposed under these plans.

Long-Term Incentive Plans (LTIP)

The LTIP provides for awards of free shares (i.e. either conditional shares or nil or nominal cost options) normally on an annual basis which are eligible to vest after three years subject to continued service and the achievement of challenging performance conditions. It is anticipated that the first award under this scheme will be made in 2021. Options are granted under this scheme to key senior management subject to performance conditions as detailed on page 103 of the Remuneration Report.

The Group has managed the run-off from a number of legacy plans and any remaining options granted under those plans vested prior to 2020. No further issues will be made under these plans and during 2020 the final options under those arrangements were either exercised or expired.

8. Exceptional costs

Accounting policy

Exceptional items are transactions that are outside normal operations and are material to the results of the Group, either by virtue of size or nature. As such, the items set out below require separate disclosure on the face of the Consolidated Statement of Profit or Loss to assist with the understanding of the underlying performance of the Group.

	2020 £'000	2019 £'000
Costs of restructure	779	–
Impairment of fixed assets	1,500	–
Exceptional legal costs	–	2,018
	2,279	2,018

The Group incurred restructuring costs in 2020 of £3.2m (2019: £1.7m) of which £0.8m (2019: £nil) has been categorised within exceptional items. In assessing how to report and disclose the costs of restructure, management has focused on distinguishing between the underlying drivers for the cost incurred. Restructure costs are not considered exceptional where they are recurring in nature or where they form part of a wider plan to deliver operational and financial improvements to the business to the benefit of future periods. Management considers such expenditure to be a normal trading item. However, where an expense arises in respect of a permanent exit from a contract or from a type of activity which management considers will not form part of recurring operational activities in the future, then such expenditure is categorised as an exceptional item. This was the case for £0.8m of the cost incurred, which related to the redundancy costs incurred in respect of the termination of a number of maintenance-led contracts, together with the acceleration of the exit from the Group's development activities.

In 2018, Mears commenced the construction of a modular homes scheme which has, over the previous two financial years, been disclosed as an asset in the course of construction. The off-site construction is complete; however the impact of the COVID-19 pandemic has meant that a significant part of the on-site installation remains outstanding. The original agreement was that upon completion, Mears would lease these units to a Local Authority client for a period of 15 years and the lease payments would fund the construction cost. Given the Board's stated objective to reduce the Group's indebtedness, the Group agreed to a contract variation which has removed Mears entirely from this arrangement, in return for a fixed payment of £6.4m, payable on completion of the installation. As at 31 December 2020, Mears had incurred capital expenditure of £5.8m. Following an assessment of the costs incurred to date, and the costs required to complete the on-site installation, an impairment has been recognised on the asset in the course of construction by £1.5m. Following the reduction in the carrying value, the asset has been reclassified as a contract asset. The impairment charge applied against this asset is considered to be an exceptional item. It is abnormal in size and nature and relates to an activity which is not part of the continuing activities of the Group.

Exceptional legal costs were incurred during 2019 in respect of a property lease. Given the size of this item and unique circumstance of the dispute, management believes this should be treated as an exceptional item to better reflect the underlying financial performance. No further costs are anticipated in respect of this dispute and no further costs were incurred during 2020.

Financial statements continued

Notes to the financial statements – Group continued

For the year ended 31 December 2020

9. Tax expense**Accounting policy**

Current tax assets and/or liabilities comprise those obligations to, or claims from, fiscal authorities that are unpaid at the balance sheet date. They are calculated according to the tax rates and tax laws applicable to the accounting periods to which they relate, based on the taxable profit for the year.

Where an item of income or expense is recognised in the Consolidated Statement of Profit or Loss, any related tax generated is recognised as a component of tax expense in the Consolidated Statement of Profit or Loss. Where an item is recognised directly to equity or presented within the Consolidated Statement of Comprehensive Income, any related tax generated is treated similarly.

Deferred taxation is the tax expected to be repayable or recoverable on differences between the carrying amounts of assets and liabilities in the financial statements and corresponding tax bases used in the computation of taxable profit and is accounted for using the balance sheet liability method.

Deferred taxation liabilities are generally recognised on all taxable temporary differences in full with no discounting. Deferred taxation assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. However, deferred tax is not provided on the initial recognition of goodwill, nor on the initial recognition of an asset or liability, unless the related transaction is a business combination or affects tax or accounting profit.

Deferred taxation is calculated using the tax rates and laws that are expected to apply in the period when the liability is settled or the asset is realised, provided they are enacted or substantively enacted at the balance sheet date. The carrying value of deferred taxation assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available against which taxable temporary differences can be utilised. Deferred tax is charged or credited to either the Consolidated Statement of Profit or Loss, the Consolidated Statement of Comprehensive Income or equity to the extent that it relates to items charged or credited. Deferred tax relating to items charged or credited directly to equity is also credited or charged to equity.

Tax recognised in the Consolidated Statement of Profit or Loss:

	2020 £'000	2019 (restated) £'000
United Kingdom corporation tax	(785)	3,248
Adjustment in respect of previous periods	674	71
<u>Total current tax (credit)/charge recognised in Consolidated Statement of Profit or Loss</u>	<u>(111)</u>	<u>3,319</u>
Deferred taxation charge:		
▶ on defined benefit pension obligations	(167)	(40)
▶ on share-based payments	101	46
▶ on accelerated capital allowances	(26)	228
▶ on amortisation of acquisition intangibles	(1,553)	(1,882)
▶ on short-term temporary timing differences	144	(52)
▶ on corporate tax losses	(324)	1,770
▶ other timing differences	43	53
Adjustment in respect of previous periods	(1,314)	(427)
<u>Total deferred taxation recognised in Consolidated Statement of Profit or Loss</u>	<u>(3,096)</u>	<u>(304)</u>
Total tax (credit)/charge recognised in Consolidated Statement of Profit or Loss on continuing operations	(3,207)	3,015
Total tax charge recognised in Consolidated Statement of Profit or Loss on discontinued operations	121	1,061
<u>Total tax (credit)/charge recognised in Consolidated Statement of Profit or Loss</u>	<u>(3,086)</u>	<u>4,076</u>

9. Tax expense continued

The charge for the year can be reconciled to the result for the year as follows:

	2020 £'000	2019 (restated) £'000
(Loss)/profit for the year on continuing operations before tax	(15,218)	20,253
Profit/(loss) for the year on discontinued operations before tax	56,933	(82,223)
Result for the year before tax	41,715	(61,970)
Result for the year multiplied by standard rate of corporation tax in the United Kingdom for the period of 19.0% (2019: 19.0%)	7,926	(11,774)
Effect of:		
► expenses not deductible for tax purposes	142	496
► goodwill impairment	—	15,658
► fixed asset impairment	285	—
► net proceeds of disposals of subsidiaries not subject to tax	(9,760)	—
► income not subject to tax	(248)	(135)
► tax impact of employee share schemes	201	120
► temporary timing differences not recognised in deferred tax	—	67
► tax losses not previously recognised in deferred tax	(35)	—
► adjustment in respect of prior periods	(1,597)	(356)
Actual tax expense	(3,086)	4,076

Deferred tax is recognised on both temporary differences between the treatment of items for tax and accounting purposes. Deferred tax on the amortisation of acquisition intangibles is a temporary difference and arises because no tax relief is due on this kind of amortisation.

Tax losses generated in previous years which are expected to be utilised against future profits are recognised as a deferred tax asset and a subsequent charge arises as those losses are utilised. No deferred tax asset is recognised in respect of losses of £29.0m (2019: £28.9m) across several entities in the Group as it is not expected that they will be eligible to be utilised against profits in the future.

Deferred tax is also recognised on short-term temporary timing differences, primarily relating to provisions. These differences are expected to reverse in the following year and arise because tax relief is only available when the costs are incurred.

Capital allowances represent tax relief on the acquisition of property, plant and equipment and are spread over several years at rates set by legislation. These differ from depreciation, which is an estimate of the use of an item of property, plant and equipment over its useful life.

Deferred tax is recognised on the difference between the remaining value of such an asset for tax purposes and its carrying value in the accounts.

The UK Budget 2021 announcements on 3 March 2021 included measures to support economic recovery as a result of the ongoing COVID-19 pandemic. These included an increase to the UK's main corporation tax rate to 25%, which is due to be effective from 1 April 2023. These changes were not substantively enacted at the balance sheet date and hence have not been reflected in the measurement of deferred tax balances at the period end. If the Group's deferred tax balances at the period end were remeasured at 25% this would result in a deferred tax credit of £1.0m.

The following tax has been charged to other comprehensive income or equity during the year:

	2020 £'000	2019 (restated) £'000
Deferred tax credit recognised in other comprehensive income		
► on defined benefit pension obligations	(1,727)	(2,145)
► on cash flow hedges	(149)	(18)
Total deferred tax credit recognised in other comprehensive income	(1,876)	(2,163)
Deferred tax recognised directly in equity		
Deferred tax (credit)/charge:		
► on share-based payments	(10)	191
Total deferred tax recognised in equity	(10)	191
Total tax		
Total current tax	10	4,275
Total deferred tax	(4,982)	(2,171)

Financial statements continued

Notes to the financial statements – Group continued

For the year ended 31 December 2020

10. Discontinued activities

During the year, the Group completed the disposal of its Domiciliary Care business with the disposal of the England and Wales element in January and the Scotland business in September. These businesses had been classified as held for sale in 2019 as their disposal was anticipated during 2020.

In addition, the Group disposed of its Planning Solutions business, with completion in December 2020. This comprised of two trading subsidiaries: Terraquest Solutions Limited and Portalplanquest Limited.

The results of all disposed businesses prior to their disposal are presented within discontinued operations in the Consolidated Statement of Profit or Loss.

The results of the operations which have been included in the consolidated financial statements are as follows:

	2020 £'000	2019 (restated) £'000
Revenue and profits		
Sales revenue	35,388	98,400
Cost of sales	(20,787)	(70,440)
Administrative expenses	(11,738)	(29,430)
Impairment of intangibles	—	(80,562)
Profit on disposal	54,074	—
Finance costs	(4)	(191)
Profit/(loss) for the year before tax on discontinued operations	56,933	(82,223)
Tax on discontinued operations	(121)	(1,061)
Profit/(loss) for the year after tax on discontinued operations	56,812	(83,284)

The results of all disposed businesses prior to their disposal are presented within discontinued cash flows in the Consolidated Cash Flow Statement.

The results of the operations which have been included in the Consolidated Cash Flow Statement are as follows:

	2020 £'000	2019 (restated) £'000
Operating activities		
Result for the year before tax	56,933	(82,223)
Net finance costs	4	191
Share based payments	36	—
Depreciation and amortisation	1,004	3,721
Impairment of goodwill	—	80,562
Net loss/(profit) on disposal of investments	(58,993)	—
Change in operating receivables	586	6,198
Change in operating payables	2,962	(3,930)
Net cash inflow from operating activities before taxation	2,532	4,519
Taxes paid	(5)	385
Net cash inflow from operating activities	2,527	4,904
Investing activities		
Additions to property, plant and equipment	(305)	(977)
Additions to other intangible assets	(3,141)	(1,332)
Proceeds from disposal of subsidiaries	63,676	—
Net cash disposed of with subsidiaries	(5,618)	—
Net cash inflow/(outflow) from investing activities	54,612	(2,309)
Financing activities		
Discharge of lease liabilities	(485)	(421)
Interest paid	(4)	(191)
Net cash outflow from financing activities	(489)	(612)
Net increase in cash and cash equivalents	56,650	1,983

10. Discontinued activities continued

	2020 £'000	2019 £'000
Statement of Financial Position		
Assets of disposal group	–	11,185
Liabilities related to assets classified as held for sale	–	(5,892)
Net assets of disposal group	–	5,293

The major classes of assets and liabilities classified as held for sale at 31 December 2019 are as follows:

	£'000
Property, plant and equipment	2,824
Pension guarantee assets	57
Deferred tax asset	280
Trade and other receivables	7,872
Cash and cash equivalents	152
Trade and other payables	(3,756)
Pension and other employee benefits	(57)
Lease liabilities	(2,064)
Current tax liabilities	(15)
Net assets held for sale	5,293

Net assets held for sale are held at the lower of their carrying amount and fair value less costs to sell. Management assessed the fair value less costs to sell of the disposal group as at 31 December 2019. There were no observable inputs to the valuation of the disposal group, so the assessment was based on level 3 inputs.

The Group had commenced a sales process during 2019 and a number of offers had been received from potential buyers at that time. At 31 December 2019, the expected sales valuation was estimated to be in the region of £6.0m, valued on a debt-free basis, with a normal level of working capital, and an assumption that the England & Wales and Scotland Domiciliary Care businesses would be sold to two separate buyers. Legal and advisory costs were estimated to be £0.7m, resulting in a net recoverable amount of £5.3m which supported the carrying value of the net assets held, as detailed above.

11. Dividends

Accounting policy

Dividend distributions payable to equity shareholders are included in 'Current financial liabilities' when the dividends are approved in a general meeting prior to the balance sheet date.

The following dividends were paid on ordinary shares in the year:

	2020 £'000	2019 £'000
Final 2019 dividend of 0p (2019: final 2018 dividend of 8.55p) per share	–	9,778
Interim 2020 dividend of 0p (2019: interim 2019 dividend of 3.65p) per share	–	4,033
	–	13,811

Given the impact of the COVID-19 pandemic, and the loss for the year from continuing operations, the Board does not intend to declare a dividend for 2020. The Board will seek to return to the dividend list once it is prudent to do so.

Financial statements continued

Notes to the financial statements – Group continued

For the year ended 31 December 2020

12. Earnings per share

	Basic (continuing)		Basic (discontinued)		Basic (continuing and discontinued)	
	2019		2019		2019	
	2020	(restated)	2020	(restated)	2020	(restated)
Earnings per share	(10.66)	15.72	50.87	(75.80)	40.21	(60.09)
Effect of amortisation of acquisition intangibles	8.62	9.16	–	–	8.62	9.16
Effect of full tax adjustment	(1.92)	(2.50)	(9.68)	1.23	(11.60)	(1.26)
Effect of exceptional costs	1.67	1.48	(38.73)	59.06	(37.06)	60.54
Normalised earnings per share	(2.29)	23.86	2.46	(15.51)	0.17	8.35

	Diluted (continuing)		Diluted (discontinued)		Diluted (continuing and discontinued)	
	2019		2019		2019	
	2020	(restated)	2020	(restated)	2020	(restated)
Earnings per share	(10.66)	15.64	50.87	(75.41)	40.21	(59.77)
Effect of amortisation of acquisition intangibles	8.62	9.11	–	–	8.62	9.11
Effect of full tax adjustment	(1.92)	(2.48)	(9.68)	1.22	(11.60)	(1.26)
Effect of exceptional costs	1.67	1.47	(38.73)	58.75	(37.06)	60.22
Normalised earnings per share	(2.29)	23.74	2.46	(15.44)	0.17	8.30

A normalised earnings per share (EPS) is disclosed in order to show performance undistorted by the amortisation of acquisition intangibles and exceptional costs. The Group defines normalised earnings as excluding the amortisation of acquisition intangibles and exceptional costs and adjusted to reflect a full tax charge. The profit attributable to shareholders before and after adjustments for both basic and diluted EPS is:

	Normalised (continuing)		Normalised (discontinued)		Normalised (continuing and discontinued)	
	2019		2019		2019	
	2020	(restated)	2020	(restated)	2020	(restated)
(Loss)/profit attributable to shareholders:	(11,781)	17,367	56,242	(83,755)	44,461	(66,388)
► Amortisation of acquisition intangibles	9,525	10,122	–	–	9,525	10,122
► Full tax adjustment	(2,125)	(2,757)	(10,696)	1,360	(12,821)	(1,397)
► Exceptional costs	1,846	1,634	(42,823)	65,255	(40,977)	66,889
Normalised earnings	(2,535)	26,366	2,723	(17,140)	188	9,226

The calculation of EPS is based on a weighted average of ordinary shares in issue during the year. The diluted EPS is based on a weighted average of ordinary shares calculated in accordance with IAS 33 'Earnings per Share', which assumes that all dilutive options will be exercised. IAS 33 defines dilutive options as those whose exercise would decrease earnings per share or increase loss per share from continuing operations. The additional normalised basic and diluted EPS use the same weighted average number of shares as the basic and diluted EPS.

	2020 Million	2019 Million
Weighted average number of shares in issue:	110.56	110.49
► Dilutive effect of share options	–	0.58
Weighted average number of shares for calculating diluted earnings per share	110.56	111.07

As the Group made a loss from continuing operations during 2020, there were no dilutive options during this period. The number of antidilutive potential shares not included in the above table for 2020 was 0.39 million (2019: none).

13. Goodwill

Accounting policy

Goodwill arises on the acquisition of subsidiaries and represents any excess of the cost of the acquired entity over the Group's interest in the fair value of the entity's identifiable assets and liabilities acquired and is capitalised as a separate item. Goodwill is recognised as an intangible asset.

Under the business combinations exemption of IFRS 1, goodwill previously written off directly to reserves under UK GAAP is not recycled to the Consolidated Statement of Profit or Loss on calculating a gain or loss on disposal.

Impairment

For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows: cash-generating units (CGUs). As a result, some assets are tested individually for impairment and some are tested at CGU level. Goodwill is allocated to those CGUs that are expected to benefit from synergies of the related business combination and represent the lowest level within the Group at which management monitors the related cash flows.

Goodwill or CGUs that include goodwill and those intangible assets not yet available for use are tested for impairment at least annually. All other individual assets or CGUs are tested for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

An impairment loss is recognised in the Consolidated Statement of Profit or Loss for the amount by which the asset's or CGU's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of fair value, reflecting market conditions less costs to sell, and value in use based on an internal discounted cash flow evaluation. Impairment losses recognised for CGUs, to which goodwill has been allocated, are credited initially to the carrying amount of goodwill. Any remaining impairment loss is charged pro-rata to the other assets in the CGU. With the exception of goodwill, all assets are subsequently reassessed for indications that an impairment loss previously recognised may no longer exist.

For the partial disposal of a CGU, goodwill is allocated proportionately to the branches acquired based on operating profit.

Key sources of estimation uncertainty

The determination of whether goodwill is impaired has been a key source of estimation uncertainty in the past, given the size of the carrying value, combined with the challenging environment of domiciliary care. Following the disposal of this business, the remaining goodwill is attached to the Group's Housing business, which has a higher level of headroom between the carrying value and the value in use. Whilst management will continue to carry out regular assessments of the carrying value, this area is no longer considered a key source of estimation uncertainty.

	Goodwill arising on consolidation £'000	Purchased goodwill £'000	Total £'000
Gross carrying amount			
At 1 January 2019	195,516	8,250	203,766
Assets classified as held for sale	(80,562)	–	(80,562)
At 1 January 2020	114,954	8,250	123,204
Reclassification	4,208	(4,208)	–
Disposal of subsidiary	(4,331)	–	(4,331)
At 31 December 2020	114,831	4,042	118,873
Accumulated impairment losses			
At 1 January 2019, at 1 January 2020 and at 31 December 2020	–	–	–
Carrying amount			
At 31 December 2020	114,831	4,042	118,873
At 31 December 2019	114,954	8,250	123,204

Financial statements continued

Notes to the financial statements – Group continued

For the year ended 31 December 2020

13. Goodwill continued

Goodwill on consolidation arises on the excess of cost of acquisition over the fair value of the net assets acquired on purchase of a company.

Purchased goodwill arises on the excess of cost of acquisition over the fair value of the net assets acquired on the purchase of the trade and assets of a business by the Group.

Goodwill is not amortised but is reviewed for impairment on an annual basis or more frequently if there are any indications that goodwill may be impaired. Goodwill acquired in a business combination is allocated to groups of CGUs according to the level at which management monitors that goodwill. Goodwill is carried at cost less accumulated impairment losses.

The sale of the Terraquest Group during the year resulted in the disposal of £4.3m of goodwill arising on consolidation.

The carrying value of goodwill is allocated to the following CGUs:

	Goodwill arising on consolidation £'000	Purchased goodwill £'000	Total £'000
Housing	95,742	4,042	99,784
Housing with Care	19,089	–	19,089
	114,831	4,042	118,873

An asset is impaired if its carrying value exceeds the CGUs recoverable amount, which is based on value in use. At 31 December 2020 impairment reviews were performed by comparing the carrying value with the value in use for the CGUs to which goodwill has been allocated.

The Housing CGU's value in use is calculated from the Board-approved one-year budgeted cash flows and extrapolated cash flows for the next four years discounted at a post-tax discount rate of 8.0% over a five-year period with a terminal value. The impairment reviews incorporated a terminal growth assumption of 1.0%, which is conservative when compared with the UK long-term growth rate.

The Housing with Care CGU's value in use is calculated from a detailed business plan deriving cash flows over a five-year review period, discounted at a post-tax discount rate of 8.0% over a five-year period with a terminal value. The impairment review incorporated a terminal growth assumption of 1.7%, which is in line with the UK long-term growth rate of 1.7% and is supported by the underlying demographics underpinning strong organic growth in adult social care.

The estimated growth rates are based on knowledge of the individual CGU's sector and market and represent management's base level expectations for future growth. Changes to revenue and direct costs are based on past experience and expectation of future changes within the markets of the CGUs. All CGUs have the same access to the Group's treasury function and borrowing arrangements to finance their operations.

Management considers that reasonably possible changes in these assumptions would not cause a CGU's carrying amount to exceed its recoverable amount.

The rates used were as follows:

	Post-tax discount rate	Pre-tax discount rate	Volume growth rate (years 1–5)	Terminal growth rate
Housing	8.00%	9.20%	1.00%	1.00%
Housing with Care	8.00%	9.45%	2.00%	1.70%

14. Other intangible assets

Accounting policy

In accordance with IFRS 3 (Revised) 'Business Combinations', an intangible asset acquired in a business combination is deemed to have a cost to the Group of its fair value at the acquisition date. The fair value of the intangible asset reflects market expectations about the probability that the future economic benefits embodied in the asset will flow to the Group. Where an intangible asset might be separable, but only together with a related tangible or intangible asset, the group of assets is recognised as a single asset separately from goodwill where the individual fair values of the assets in the Group are not reliably measurable. Where the individual fair values of the complementary assets are reliably measurable, the Group recognises them as a single asset provided the individual assets have similar useful lives. Intangible assets are amortised over the useful economic life of those assets.

Development costs incurred on software development are capitalised when all the following conditions are satisfied:

- ▶ Completion of the software module is technically feasible so that it will be available for use.
- ▶ The Group intends to complete the development of the module and use it.
- ▶ The software will be used in generating probable future economic benefits.
- ▶ There are adequate technical, financial and other resources to complete the development and to use the software.
- ▶ The expenditure attributable to the software during its development can be measured reliably.

Costs incurred making intellectual property available for use (including any associated borrowing costs) are capitalised when all of the following conditions are satisfied:

- ▶ Completion of the data set is technically feasible so that it will be available for use.
- ▶ The Group intends to complete the preparation of the data and use it.
- ▶ The data will be used in generating probable future economic benefits.
- ▶ There are adequate technical, financial and other resources to complete the data set and to use it.
- ▶ The expenditure attributable to the intellectual property during its development can be measured reliably.

Development costs not meeting the criteria for capitalisation are expensed as incurred. Careful judgement by management is applied when deciding whether the recognition requirements for development costs have been met. This is necessary as the economic success of any development is uncertain and may be subject to future technical problems at the time of recognition. Judgements are based on the information available at each balance sheet date. In addition, all internal activities related to the research and development of new software are continually monitored by management.

The cost of an internally generated intangible asset comprises all directly attributable costs necessary to create, produce and prepare the asset to be capable of operating in the manner intended by management. Directly attributable costs include employee costs incurred on software development.

Amortisation commences upon completion of the asset and is shown within other administrative expenses. Until the asset is available for use on completion of the project, the assets are subject to impairment testing only. Development expenditure is amortised over the period expected to benefit.

The identifiable intangible assets and associated periods of amortisation are as follows:

Order book	– over the period of the order book, typically three years
Client relationships	– over the period expected to benefit, typically five years
Supplier relationships	– over the period expected to benefit, typically two years
Development expenditure	– over four to five years, straight line
Intellectual property	– over the period of usefulness of the intellectual property, typically five years
Software	– 25% p.a., reducing balance

The useful economic lives of intangible assets are reviewed annually and amended if appropriate.

Financial statements continued

Notes to the financial statements – Group continued

For the year ended 31 December 2020

14. Other intangible assets continued

	Acquisition intangibles				Other intangibles			
	Client relationships £'000	Order book £'000	Supplier relationships £'000	Total acquisition intangibles £'000	Development expenditure £'000	Intellectual property £'000	Total other intangibles £'000	Total intangibles £'000
Gross carrying amount								
At 1 January 2019	83,438	40,626	–	124,064	19,976	224	20,200	144,264
Additions	–	–	1,300	1,300	3,022	–	3,022	4,322
Reclassification	(460)	(412)	872	–	–	–	–	–
Disposals	–	–	–	–	–	(224)	(224)	(224)
Assets classified as held for sale	(16,991)	(22,444)	–	(39,435)	–	–	–	(39,435)
At 1 January 2020	65,987	17,770	2,172	85,929	22,998	–	22,998	108,927
Additions	–	–	–	–	4,858	–	4,858	4,858
Disposals of subsidiaries	–	–	–	–	(7,896)	–	(7,896)	(7,896)
At 31 December 2020	65,987	17,770	2,172	85,929	19,960	–	19,960	105,889
Accumulated amortisation								
At 1 January 2019	66,991	28,422	–	95,413	11,615	224	11,839	107,252
Amortisation charge for period	1,891	8,014	217	10,122	2,570	–	2,570	12,692
Reclassification	(460)	(412)	872	–	–	–	–	–
Disposals	–	–	–	–	–	(224)	(224)	(224)
Assets classified as held for sale	(16,991)	(22,444)	–	(39,435)	–	–	–	(39,435)
At 1 January 2020	51,431	13,580	1,089	66,100	14,185	–	14,185	80,285
Amortisation charge for period	8,351	525	650	9,526	2,625	–	2,625	12,151
Disposal of subsidiaries	–	–	–	–	(1,752)	–	(1,752)	(1,752)
At 31 December 2020	59,782	14,105	1,739	75,626	15,058	–	15,058	90,684
Carrying amount								
At 31 December 2020	6,205	3,665	433	10,303	4,902	–	4,902	15,205
At 31 December 2019	14,556	4,190	1,083	19,829	8,813	–	8,813	28,642

Development expenditure is an internally developed intangible asset and relates largely to the development of the Group's Housing job management system. Development expenditure is amortised over its useful economic life of 5.0 years. The weighted average remaining economic life of the asset is 3.1 years (2019: 3.4 years).

Amortisation of development expenditure is included within other administrative expenses. Amortisation of acquisition intangibles is presented separately.

15. Property, plant and equipment

Accounting policy

Items of property, plant and equipment are stated at historical cost, net of depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items. Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow into the Group and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the Consolidated Statement of Profit or Loss during the financial period in which they are incurred.

Freehold land is not depreciated. Depreciation on other assets is calculated to write down the cost less estimated residual value over their estimated useful economic lives. The rates generally applicable are:

Freehold buildings	– 2% p.a., straight line
Leasehold improvements	– over the period of the lease, straight line
Plant and machinery	– 25% p.a., reducing balance
Equipment	– 25% p.a., reducing balance
Fixtures and fittings	– 50% p.a., straight line
Motor vehicles	– 25% p.a., reducing balance

During the year management reassessed the depreciation methodology for fixtures and fittings from 25% reducing balance to 50% straight line. This reassessment was made as a result of a change in the types of assets included in this category. Typically, these are now assets for residential accommodation which are now considered to have a shorter useful economic life.

Residual values are reviewed annually and updated if appropriate. The carrying value is reviewed for impairment in the period if events or changes in circumstances indicate the carrying value may not be recoverable. An asset's carrying value is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognised within administrative expenses in the Consolidated Statement of Profit or Loss.

Identifying whether there are indicators of impairment in respect of property, plant and equipment involves some judgement and a good understanding of the drivers of value behind the asset. At each reporting period an assessment is performed in order to determine whether there are any such indicators, which involves considering the performance at both a contract and business level, and any significant changes to the markets in which we operate. This is not considered to be a critical judgement or an area of significant uncertainty.

Financial statements continued

Notes to the financial statements – Group continued

For the year ended 31 December 2020

15. Property, plant and equipment continued

	Freehold property £'000	Leasehold improvements £'000	Plant and machinery £'000	Fixtures, fittings and equipment £'000	Motor vehicles £'000	Assets under construction £'000	Total £'000
Gross carrying amount							
At 1 January 2019	932	18,424	3,105	50,549	1,001	3,593	77,604
Additions	–	5,050	253	2,962	16	1,133	9,414
Disposals	–	(383)	(425)	(5,091)	(9)	–	(5,908)
Transferred to disposal group	(110)	(594)	–	(980)	–	–	(1,684)
At 1 January 2020	822	22,497	2,933	47,440	1,008	4,726	79,426
Additions	–	2,969	28	846	–	1,113	4,956
Disposals	(6)	(6,080)	(151)	(10,755)	(24)	–	(17,016)
Reclassification	–	(104)	–	104	–	–	–
Disposal of subsidiaries	–	(241)	(761)	(2,005)	–	–	(3,007)
Transferred from disposal group	110	129	–	17	–	–	256
At 31 December 2020	926	19,170	2,049	35,647	984	5,839	64,615
Depreciation							
At 1 January 2019	27	11,235	2,264	38,134	988	–	52,648
Provided in the year	19	2,077	222	4,683	3	–	7,004
Eliminated on disposals	–	(353)	(373)	(4,959)	(9)	–	(5,694)
Transferred to disposal group	–	(135)	–	(723)	–	–	(858)
At 1 January 2020	46	12,824	2,113	37,135	982	–	53,100
Provided in the year	28	2,226	214	3,205	7	–	5,680
Eliminated on disposals	(6)	(6,080)	(135)	(10,496)	(23)	–	(16,740)
Impairment	–	–	–	–	–	1,500	1,500
Reclassification	–	2	–	(2)	–	–	–
Disposal of subsidiaries	–	(102)	(641)	(1,808)	–	–	(2,551)
Transferred from disposal group	–	18	–	8	–	–	26
At 31 December 2020	68	8,888	1,551	28,042	966	1,500	41,015
Carrying amount							
At 31 December 2020	858	10,282	498	7,605	18	4,339	23,600
At 31 December 2019	776	9,673	820	10,305	26	4,726	26,326

16. Right of use asset

Accounting policy

Where an asset is subject to a lease, the Group recognises a right of use asset and a lease liability on the balance sheet. The right of use asset is measured at cost, which matches the initial measurement of the lease liability and any costs expected at the end of the lease, and then depreciated on a straight-line basis over the lease term.

The lease liability is measured at the present value of the future lease payments discounted using the Group's incremental borrowing rate. Lease payments include fixed payments, variable payments based on an index and payments arising from options reasonably certain to be exercised.

The Group has elected to account for short-term leases and leases of low-value assets using the practical expedients. Instead of recognising a right of use asset and a lease liability, the payments in relation to these are recognised as an expense in profit or loss on a straight-line basis over the lease term.

On the statement of financial position, right of use assets and lease liabilities are presented separately.

Critical judgements in applying the Group's accounting policies

The Group holds more than 15,000 leases across its portfolio of residential properties, offices and vehicles. Whilst the Group endeavours to standardise the form of leases, operational demands dictate that many leases have specific wording to address particular operational needs and also to manage the associated operational and financial risks. As such, each lease requires individual assessment and the Group is required to make key judgements which include:

- ▶ the identification of a lease;
- ▶ assessing the right to direct the use of the underlying asset;
- ▶ determining the lease term; and
- ▶ the assessment as to the level of future lease payments, including fixed and variable payments.

The most typical challenges encountered and which form the key judgements are:

- ▶ where the lease contains a one-way no-fault break in Mears' favour, the Group measures the obligation based on the Group's best estimate of its future intentions;
- ▶ where a unilateral break is in place, assessing whether the lease can be terminated with no more than an insignificant penalty;
- ▶ where the lessor has a right of substitution meaning that the lessor can swap one property for another without Mears' approval;
- ▶ where Mears does not in practice have the right to control the use of the asset and the key decision-making rights are retained by the supplier;
- ▶ where a wider agreement for a supply of services includes a lease component which meets the definition of a lease under IFRS 16; and
- ▶ the assessment of the fixed lease payments where the lease obligation to the landlord is based on a pass-through arrangement in which Mears only makes lease payments to the owner to the extent that the property is occupied and to the extent that rents are received from the tenant.

Key sources of estimation uncertainty

Estimation is required in calculating the appropriate discount rate to use when recognising the present value of future lease payments as a lease obligation. The Group undertook a synthetic credit rating exercise which determined a credit rating of BB+ for Mears Group PLC. Given the cross-guarantees in place across the Group, it was considered appropriate to use a single credit rating across all Group entities. Using the Thomson Reuters Eikon database, a yield curve was built that can be used to determine appropriate incremental borrowing rates for the varying lease tenors. In order to build an appropriate yield curve, we have calculated a proxy GBP BB+ yield curve for a range of maturities by interpolating yields at the mid-point between BBB and BB rated GBP corporate bond yields.

The sensitivity of the lease liability to the assumptions used in these estimations is indicated in note 21.

Investment property

Included within right of use assets are certain properties classified as investment properties in accordance with IAS 40. These properties are held primarily in order to earn rentals. The Group has chosen to apply the cost model to all investment property and therefore measurement is in line with IFRS 16 as described in the Leased assets accounting policy.

Properties that generate rentals but are primarily held for the provision of social benefits are not considered to meet the definition of investment property.

Financial statements continued

Notes to the financial statements – Group continued

For the year ended 31 December 2020

16. Right of use asset continued

	Assets that are sub-leased to customers		Assets that are used directly within the business			Total £'000
	Investment property £'000	Residential property £'000	Residential property £'000	Offices £'000	Motor vehicles £'000	
Gross carrying amount						
At 1 January 2019	–	–	–	–	–	–
Recognised on transition to IFRS 16 (restated)	27,052	104,673	–	11,088	21,179	163,992
Additions (restated)*	–	10,983	42,455	3,454	11,124	68,016
Disposals (restated)	–	(64)	(103)	–	–	(167)
Transferred to disposal group	–	–	–	(2,581)	(194)	(2,775)
At 1 January 2020	27,052	115,592	42,352	11,961	32,109	229,066
Additions*	476	2,999	33,462	1,479	8,187	46,603
Disposals	–	(6,552)	(507)	(1,105)	(2,390)	(10,554)
Disposal of subsidiaries	–	–	–	(1,259)	–	(1,259)
At 31 December 2020	27,528	112,039	75,307	11,076	37,906	263,856
Depreciation						
At 1 January 2019	–	–	–	–	–	–
Provided in the year (restated)	1,509	11,878	3,463	3,503	10,652	31,005
Eliminated on disposals (restated)	–	(4)	(3)	–	–	(7)
Impairment	–	–	–	463	–	463
Transferred to disposal group	–	–	–	(684)	(95)	(779)
At 1 January 2020	1,509	11,874	3,460	3,282	10,557	30,682
Provided in the year	1,521	10,832	16,292	2,753	11,112	42,510
Eliminated on disposals	–	(5,555)	(140)	(1,063)	(2,215)	(8,973)
Disposal of subsidiaries	–	–	–	(404)	–	(404)
At 31 December 2020	3,030	17,151	19,612	4,568	19,454	63,815
Carrying amount						
At 31 December 2020	24,498	94,888	55,695	6,508	18,452	200,041
At 31 December 2019 (restated)	25,543	103,718	38,892	8,679	21,552	198,384

* Additions includes both new underlying assets and remeasurement of the right of use asset for changes in the lease terms.

Investment property included above represents properties held by the Group primarily to earn rentals, rather than for use in the Group's other activities. The amount included in lease income in note 2 in respect of these properties is £2.9m (2019: £3.0m). Direct operating expenses arising from investment property that generated rental income during the period was £3.4m (2019: £3.2m). The carrying value of the right of use asset in respect of investment property is considered to be approximately equal to its fair value.

17. Investments

Accounting policy

Investments include those over which the Group has significant influence but which it does not control. These are categorised as associates. It is presumed that the Group has significant influence where it has between 20% and 50% of the voting rights in the investee unless indicated otherwise. The Group also holds investments in joint ventures where the Group and other parties have joint control over their activities.

The basis by which associates and joint ventures are consolidated in the Group financial statements is through the equity method, as outlined in the basis of consolidation.

In addition to associates and joint ventures, the Group holds investments in entities over which it does not exert significant influence. These are accounted for at fair value through profit or loss.

17. Investments continued

	Associates £'000	Joint ventures £'000	Other investments £'000	Total £'000
At 1 January 2019	—	—	—	—
Share of profit	895	—	—	895
Distributions received	(359)	—	—	(359)
At 1 January 2020	536	—	—	536
Share of profit	1,056	—	—	1,056
Distributions received	(691)	—	—	(691)
Acquisition	—	—	65	65
At 31 December 2020	901	—	65	966

On 9 December 2020, as part of the disposal of the Group's planning solutions business, the Group acquired 6.16% of the ordinary share capital of Mason Topco Limited, the new owner of the disposed business. This investment is presented in Other investments and is mandatorily held at fair value through profit or loss. There were no changes in the fair value of the investment following initial acquisition.

The Group has an interest in one active joint venture, as described below. This entity has retained losses and therefore the carrying value of the investment recognised at 31 December 2020 was £nil (2019: £nil).

Joint ventures and associates

Set out below are the investments in joint ventures and associates as at 31 December 2020, which in management's opinion are significant to the Group:

	Nature of relationship		Country of registration	Carrying value	
				2020 £'000	2019 £'000
Pyramid Plus South LLP	Associate	30%	England and Wales	901	536
YourMK LLP	Joint venture	50%	England and Wales	—	—

Pyramid Plus South LLP is a repairs and maintenance service provider that is central to one of the Group's contracts. YourMK LLP is a joint venture with Milton Keynes Council and manages the delivery of regeneration and maintenance.

During the year, the Group received distributions of £0.7m (2019: £0.9m) from Pyramid Plus South LLP. Summarised financial information for Pyramid Plus South LLP for the year is shown below:

	2020 £'000	2019 (restated) £'000
Revenue and profits		
Revenue	18,413	15,047
Expenses	(14,895)	(12,064)
Profit for the year	3,518	2,983
Other comprehensive income	—	—
Total comprehensive income	3,518	2,983
Share of profit at 30%	1,056	895
Net assets		
Non-current assets	—	—
Current assets	6,275	3,485
Current liabilities	(3,257)	(1,681)
Non-current liabilities	(4)	(4)
Total assets less total liabilities	3,014	1,800

Cash and cash equivalents of £0.9m (2019: £0.7m) were included in current assets above.

Financial statements continued

Notes to the financial statements – Group continued

For the year ended 31 December 2020

17. Investments continued

The Group's unrecognised share of losses in YourMK LLP for 2020 is £0.3m (2019 share of profit: £0.1m). The Group's unrecognised share of the cumulative losses in YourMK LLP as at 31 December 2020 is £0.3m (2019: £nil).

The subsidiary undertakings within the Group at 31 December 2020 are shown below:

	Proportion held	Country of registration	Nature of business
3c Asset Management Limited	100%	England and Wales	Dormant
Careforce Group PLC	100%	England and Wales	Dormant
Coulter Estates Limited	100%	Scotland	Dormant
Evolve Housing Limited	50%	England and Wales	Dormant
Helcim Group Limited	100%	England and Wales	Dormant
Helcim Homes Limited	100%	England and Wales	Dormant
ILS Group Limited	100%	Scotland	Dormant
ILS Trustees Limited	100%	Scotland	Dormant
Jackson Lloyd Limited	100%	England and Wales	Dormant
Laidlaw Scott Limited	100%	Scotland	Dormant
Let to Birmingham Limited	100%	England and Wales	Housing management services
Manchester Working Limited	80%	England and Wales	Maintenance services
Mears Direct Limited	80%	England and Wales	Dormant
Mears Energy Limited	100%	England and Wales	Dormant
Mears Estates Limited	100%	England and Wales	Grounds maintenance
Mears Extra Care Limited	100%	England and Wales	Provision of care
Mears Facility Management Limited	100%	England and Wales	Dormant
Mears Home Improvement Limited	100%	England and Wales	Maintenance services
Mears Homecare Limited	100%	England and Wales	Provision of care
Mears Homes Limited	100%	England and Wales	Dormant
Mears Housing Management Limited	100%	England and Wales	Housing management services
Mears Housing Management (Holdings) Limited	100%	England and Wales	Intermediate holding company
Mears Housing Portfolio (Holdings) Limited	100%	England and Wales	Intermediate holding company
Mears Housing Portfolio (London) Limited	100%	England and Wales	Dormant
Mears Housing Portfolio 1 Limited	100%	England and Wales	Dormant
Mears Housing Portfolio 3 Limited	100%	England and Wales	Dormant
Mears Housing Portfolio 4 Limited	100%	England and Wales	Property acquisition
Mears Insurance Company Limited	99.99%	Guernsey	Insurance services
Mears Learning Limited	90%	England and Wales	Dormant
Mears Limited	100%	England and Wales	Maintenance services
Mears Modular Homes Limited	100%	England and Wales	Dormant
Mears New Homes Limited	100%	England and Wales	House building
Mears Scotland (Housing) Limited	100%	Scotland	Dormant
Mears Scotland (Services) Limited	66.67%	Scotland	Dormant
Mears Scotland LLP	66.67%	Scotland	Maintenance services
Mears Social Housing Limited	100%	England and Wales	Dormant
Mears Supported Living Limited	100%	Scotland	Provision of care
Mears Wales Limited	100%	England and Wales	Dormant
MHM Property Services Limited	100%	England and Wales	Maintenance services
Morrison Facilities Services Limited	100%	Scotland	Maintenance services
MPM Housing Limited	100%	England and Wales	Dormant
MPS Housing Limited	100%	England and Wales	Maintenance services
O&T Developments Limited	100%	England and Wales	Housing management services
Omega Housing Limited	100%	England and Wales	Housing registered provider
Plexus UK (First Project) Limited	100%	England and Wales	Housing registered provider
PS Business Services Limited	100%	Scotland	Dormant
Scion Group Limited	100%	England and Wales	Dormant
Scion Property Services Limited	100%	England and Wales	Dormant
Scion Technical Services Limited	100%	England and Wales	Maintenance services
Supporta Limited	100%	England and Wales	Dormant
Tando Homes Limited	100%	England and Wales	Housing management services
Tando Property Services Limited	100%	England and Wales	Housing management services

17. Investments continued

All subsidiary undertakings with the exception of Evolve Housing Limited, Manchester Working Limited and MPM Housing Limited prepare accounts to 31 December. Evolve Housing Limited prepares accounts to 30 June in line with its historical accounting reference date. Manchester Working Limited and MPM Housing Limited prepare accounts to 30 September.

The Group includes the following three trading subsidiaries with non-controlling interests: Manchester Working Limited, Mears Learning Limited and Mears Scotland LLP. The table below sets out selected financial information in respect of those subsidiaries:

	2020 £'000	2019 £'000
Revenue and profits		
Revenue	46,586	63,987
Expenses and taxation	(47,685)	(63,816)
Profit for the year	(1,099)	171
Other comprehensive expense	—	—
Total comprehensive income	(1,099)	171
(Loss)/profit for the year allocated to non-controlling interests	(68)	255
Total comprehensive expense allocated to non-controlling interests	—	—
Net assets		
Non-current assets	305	380
Current assets	17,538	19,978
Current liabilities	(12,899)	(14,120)
Non-current liabilities	(1,421)	(1,773)
Total assets less total liabilities	3,523	4,465
Equity shareholders' funds	2,865	3,681
Non-controlling interests	658	784
Total equity	3,523	4,465

The following UK subsidiaries will take advantage of the audit exemption set out within Section 479A of the Companies Act 2006 for the year ended 31 December 2020, except MPM Housing Limited, which will take the same exemption for the period ended 30 September 2021:

	Registration number
Careforce Group PLC	05201238
Let to Birmingham Limited	08757503
Mears Estates Limited	03720903
Mears Home Improvement Limited	03716517
Mears Housing Management (Holdings) Limited	04726480
Mears Housing Portfolio (Holdings) Limited	10908305
Mears Housing Portfolio 4 Limited	10952906
MHM Property Services Limited	07448134
MPM Housing Limited	03528320
O&T Developments Limited	05692853
Scion Group Limited	03905442
Scion Technical Services Limited	03671450
Tando Homes Limited	09260353
Tando Property Services Limited	07405761

Financial statements continued

Notes to the financial statements – Group continued

For the year ended 31 December 2020

18. Inventories

Accounting policy

Inventories are stated at the lower of cost and net realisable value. Cost is the actual purchase price of materials.

Work in progress is included in inventories after deducting any foreseeable losses and payments on account not matched with revenue.

Work in progress represents costs incurred on speculative construction projects where a customer has not yet been identified. Work in progress is stated at the lower of cost and net realisable value. Cost comprises materials, direct labour and any subcontracted work that has been incurred in bringing the inventories and work in progress to their present location and condition.

	2020 £'000	2019 £'000
Materials and consumables	3,558	7,068
Work in progress	27,700	28,977
	31,258	36,045

The Group consumed inventories totalling £163.3m during the year (2019: £168.9m). No items are being carried at fair value less costs to sell (2019: £nil).

19. Trade and other receivables

Accounting policy

Trade receivables represent amounts due from customers in respect of invoices raised. They are initially measured at their transaction price and subsequently remeasured at amortised cost.

Retention assets represent amounts held by customers for a period following payment of invoices, to cover any potential defects in the work. Retention assets are included in trade receivables and are therefore initially measured at their transaction price.

Contract assets represent revenue recognised in excess of the total of payments on account and amounts invoiced.

Critical judgements and key sources of estimation uncertainty

The estimation techniques used for revenue in respect of contracting require judgements to be made about the stage of completion of certain contracts and the recovery of contract assets. Each contract is treated on its merits and subject to a regular review of the revenue and costs to complete that contract. Contract assets represent revenue recognised in excess of the total of payments on account and amounts invoiced.

However, due to the estimation uncertainty across numerous contracts each with different characteristics, it is not practical to provide a quantitative analysis of the aggregated judgements that are applied, and management does not believe that disclosing a potential range of outcomes on a consolidated basis would provide meaningful information to a reader of the accounts.

There is a small sub-set of the contract asset balance where the contract asset being carried is the subject of a crystallised contractual dispute and litigation. Additional analysis is provided within the note to provide stakeholders with an understanding as to the quantum and the range of possible outcomes. Management has engaged third party legal advisers and other quantum experts in assessing each judgement.

	2020 £'000	2019 (restated) £'000
Current assets:		
Trade receivables	39,831	36,749
Contract assets	88,594	110,263
Contract fulfilment costs	1,408	1,253
Prepayments and accrued income	6,517	6,111
Deferred consideration	500	4,618
Other debtors	3,034	5,097
Total trade and other receivables	139,884	164,091

19. Trade and other receivables continued

Included in trade receivables is £4.7m (2019: £3.7m) in respect of retention payments due in more than one year.

Trade receivables are normally due within 30 to 60 days and do not bear any effective interest rate. All trade receivables and accrued income are subject to credit risk exposure.

The maximum exposure to credit risk in relation to trade receivables and accrued income at the balance sheet date is the fair value of trade receivables and accrued income. The Group's customers are primarily a mix of Local and Central Government and Housing Associations where credit risk is minimal. The Group's customer base is large and unrelated and, accordingly, the Group does not have a significant concentration of credit risk with any one counterparty.

The amounts presented in the balance sheet in relation to the Group's trade receivables and accrued income balances are presented net of loss allowances. The Group measures loss allowances at an amount equal to lifetime expected credit losses using both quantitative and qualitative information and analysis based on the Group's historical experience, and forward-looking information.

The ageing analysis of trade receivables is as follows:

	2020			2019		
	Gross amount due £'000	Expected credit loss £'000	Carrying value £'000	Gross amount due £'000	Expected credit loss £'000	Carrying value £'000
Not past due	33,279	(722)	32,557	31,548	(1,184)	30,364
Less than three months past due	5,496	(479)	5,017	4,784	(547)	4,237
More than three months past due	9,221	(6,964)	2,257	7,539	(5,391)	2,148
Total trade receivables	47,996	(8,165)	39,831	43,871	(7,122)	36,749

For expected credit losses with large organisations, such as Government bodies or Housing Associations, expected credit losses are calculated on an individual basis, taking account of all the relevant factors applicable to the amount outstanding. The Group has no history of defaults with these types of customers, so expected credit losses relate to specific disputed balances.

For individual tenant customers, expected credit losses are calculated based on the Group's historical experience of default by applying a percentage based on the age of the customer's balance.

The movement in expected credit loss during the period is shown below:

	2020 £'000	2019 £'000
As at 1 January	7,122	6,347
Changes in amounts provided	2,958	1,031
Amounts utilised	(1,915)	(256)
As at 31 December	8,165	7,122

The movement in contract assets during the period is shown below:

	2020 £'000	2019 £'000
As at 1 January	110,263	94,801
Recognised on completion of performance obligations	773,269	852,860
Invoiced during the year	(794,938)	(837,398)
As at 31 December	88,594	110,263

Contract assets includes a sub-set of contracts where the balance being carried is the subject of a crystallised contractual dispute and litigation. The combined carrying value of the contracts in dispute at 31 December 2020 is £1.2m (2019: £3.1m) against a total claim value of £3.2m. (2019: £3.2m). Management believes that the carrying value represents the mid-point in the range of likely outcomes, whilst recognising that all claims carry litigation risk.

Deferred consideration of £0.5m (2019: £4.6m) is consideration receivable in respect of the disposal of subsidiaries. The 2020 balance is in respect of the disposal of the Group's Domiciliary Care business as detailed in note 28. The 2019 balance was in respect of the disposal of Mears Housing Portfolio 2 Limited in 2019 and was received in full during 2020.

Financial statements continued

Notes to the financial statements – Group continued

For the year ended 31 December 2020

20. Trade and other payables

	2020 £'000	2019 £'000
Trade payables	114,711	125,054
Accruals	42,797	46,470
Social security and other taxes	34,983	21,989
Contract liabilities	25,330	2,112
Other creditors	3,208	6,741
	221,029	202,366

Due to the short duration of trade payables, management considers the carrying amounts recognised in the Consolidated Balance Sheet to be a reasonable approximation of their fair value.

The movement in contract liabilities during the period is shown below:

	2020 £'000	2019 £'000
As at 1 January	2,112	1,814
Revenue recognised in respect of contract liabilities	(2,112)	(1,814)
Payments received in advance of performance obligations being completed	25,330	2,112
As at 31 December	25,330	2,112

Contract liabilities relate to payments received from the customer on the contract, and/or amounts invoiced to the customer in advance of the Group performing its obligations on contracts where revenue is recognised either over time or at a point in time. These amounts are expected to be recognised within revenue within one year of the balance sheet date.

21. Lease liabilities

Lease liabilities are separately presented on the face of the Consolidated Statement of Financial Position as shown below:

	2020 £'000	2019 (restated) £'000
Current	42,888	39,175
Non-current	166,183	166,000
	209,071	205,175

The Group had not committed to any leases which had not commenced at 31 December 2020. The majority of the Group's property leases contain variable lease payments that vary annually either by reference to an index, such as the Consumer Prices Index (CPI), or based on market conditions each year. The potential impact of this variation depends on future events and therefore cannot be quantified but the Group would typically expect commensurate adjustments to income derived from these properties.

A smaller number of property leases contain termination or extension options. Management has assessed whether it is reasonably certain that the longer term will apply. In some cases, a portfolio of leases with similar lease terms is considered together and, where a rolling notice period is available to the Group, an average expected lease life may be applied.

The Group has elected not to recognise a lease liability for short-term leases and leases of low value. Payments made under such leases are expensed on a straight-line basis. Certain leases incorporate variable lease payments that are not included in the measurement of lease liabilities in accordance with IFRS 16. The expense relating to payments not included in the measurement of the lease liability is as follows:

	2020 £'000	2019 (restated) £'000
Short-term leases	45,846	51,035
Low-value leases	839	812
Variable lease payments	2,737	3,479

The portfolio of short-term leases to which the Group is committed at the end of the reporting period is not dissimilar to the portfolio to which the above disclosure relates.

21. Lease liabilities continue

Other disclosures relating to lease liabilities are provided in the table below:

	Note	2020 £'000	2019 (restated) £'000
Depreciation of right of use assets during the year	16	42,510	31,005
Additions during the year	16	46,603	68,016
Carrying value at the year end	16	200,041	198,384
Interest on lease liabilities during the year – continuing activities	5	7,123	5,760
Total cash outflow in respect of leases during the year	27	47,470	35,434

The Group's lease liabilities are subject to changes in certain key assumptions in estimating the incremental borrowing rates (IBRs) used to calculate the liabilities. The impact of an increase in all IBRs applied during 2020 by 0.1% is a £0.8m reduction in the lease liability and a £0.1m reduction in profit before tax.

22. Provisions

A summary of the movement in provisions during the year is shown below:

	Onerous contract provisions £'000	Other provisions £'000	Total £'000
At 1 January 2020	320	184	504
Reclassified from accruals	737	–	737
Adjusted balance as at 1 January 2020	1,057	184	1,241
Utilised during the year	(713)	(184)	(897)
At 31 December 2020	344	–	344

A provision of £0.7m for costs in respect of offices related to the discontinued care business was reclassified from accruals to onerous contract provision on 1 January 2020. The balance of this provision of £0.3m as at 31 December 2020 is expected to be utilised within one year.

All prior year provisions arose as a result of the acquisition of MPS Housing Limited on 30 November 2018 and related to contracts where a future loss was anticipated as a result of contractual obligations entered into by MPS Housing Limited and provisions for dilapidations of leased offices. The utilisation of provisions in the year resulted from the expected liabilities being settled.

23. Long-term other liabilities

Accounting policy

The Group self-insures certain fleet and liability risks. A provision for claims incurred but not received is recognised in respect of these potential claims. The value of this provision is estimated based on past experience of claims.

	2020 £'000	2019 £'000
Other creditors	3,667	4,700

Long-term other creditors represent self-insured claims incurred but not yet reported.

Financial statements continued

Notes to the financial statements – Group continued

For the year ended 31 December 2020

24. Financial instruments

Accounting policy

The Group uses a limited number of financial instruments comprising cash and liquid resources, borrowings, interest rate swaps and various items such as trade receivables and trade payables that arise directly from its operations. The main purpose of these financial instruments is to finance the Group's operations. The Group seeks to finance its operations through a combination of retained earnings and borrowings and investing surplus cash on deposit. The Group uses financial instruments to manage the interest rate risks arising from its operations and sources of finance but has no interests in the trade of financial instruments.

Financial assets and liabilities are recognised in the Consolidated Balance Sheet when the Group becomes party to the contractual provisions of the instrument. The principal financial assets and liabilities of the Group are as follows:

Financial assets

Investments in unlisted equities that do not convey control or significant influence over the underlying entity are recognised at fair value. They are subsequently remeasured at fair value with any changes being recognised in the Consolidated Statement of Profit or Loss.

Contingent consideration is held by the Group in order to collect the associated cash flows but until the amount is determined, these are not solely payments of principal and interest and therefore these assets are measured both initially and subsequently at fair value, with any changes being recognised in the Consolidated Statement of Profit or Loss.

Loan notes are held by the Group in order to collect the associated cash flows and not for trading. They are therefore initially recognised at fair value and subsequently measured at amortised cost, less any provision for impairment.

Financial assets generated from goods or services transferred to customers are presented as either trade receivables or contract assets. All of the Group's trade receivables are short-term in nature, with payments typically due within 60 days of the works being performed. The Group's contracts with its customers therefore contain no significant financing component.

Mears recognises a loss allowance for expected credit losses on financial assets subsequently measured at amortised cost using the 'simplified approach'. Individually significant balances are reviewed separately for impairment based on the credit terms agreed with the customer. Other balances are grouped into credit risk categories and reviewed in aggregate.

Trade receivables and cash at bank and in hand are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Trade receivables are initially recorded at fair value net of transaction costs, being invoiced value less any provisional estimate for impairment should this be necessary due to a loss event. Trade receivables are subsequently remeasured at invoiced value, less an updated provision for impairment. Any change in their value through impairment or reversal of impairment is recognised in the Consolidated Statement of Profit or Loss.

Cash and cash equivalents include cash at bank and in hand and bank deposits available with no notice or less than three months' notice from inception that are subject to an insignificant risk of changes in value. Bank overdrafts are presented as current liabilities to the extent that there is no right of offset with cash balances. The Group considers its revolving credit facility to be an integral part of its cash management.

Following initial recognition, financial assets are subsequently remeasured at amortised cost using the effective interest rate method.

Financial liabilities

The Group's financial liabilities are overdrafts, trade and other payables and interest rate swaps. They are included in the Consolidated Balance Sheet line items 'Long-term borrowings and overdrafts', 'Trade and other payables', 'Interest rate swaps' and 'Other payables'.

All interest related charges are recognised as an expense in 'Finance costs' in the Consolidated Statement of Profit or Loss with the exception of those that are directly attributable to the construction of a qualifying asset, which are capitalised as part of that asset.

Bank and other borrowings are initially recognised at fair value net of transaction costs. Gains and losses arising on the repurchase, settlement or cancellation of liabilities are recognised respectively in finance income and finance costs. Borrowing costs are recognised as an expense in the period in which they are incurred with the exception of those which are directly attributable to the construction of a qualifying asset, which are capitalised as part of that asset.

Trade payables on normal terms are not interest bearing and are stated at their fair value on initial recognition and subsequently at amortised cost.

24. Financial instruments continued

Derivative financial instruments

The Group uses derivative financial instruments to hedge its exposure to interest rate risks arising from operational and financing activities.

Derivative financial instruments are recognised initially and subsequently at fair value, with mark-to-market movements recognised in the Consolidated Statement of Profit or Loss except where cash flow hedge accounting is applied.

The fair value of interest rate swaps is the estimated amount that the Group would receive or pay to terminate the swap at the balance sheet date, taking into account current interest rates and the current creditworthiness of the swap counterparties.

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

Hedge accounting for interest rate swaps

Where an interest rate swap is designated as a hedge of the variability in cash flows of an existing or highly probable forecast loan interest payment, the effective part of any valuation gain or loss on the swap instrument is recognised in other comprehensive income in the hedging reserve. The cumulative gain or loss is removed from equity and recognised in the Consolidated Statement of Profit or Loss at the same time as the hedged transaction. The ineffective part of any gain or loss is recognised in the Consolidated Statement of Profit or Loss immediately.

When a hedging instrument or hedge relationship is terminated but the hedged transaction is still expected to occur, the cumulative gain or loss at that point remains in equity and is recognised in accordance with the above policy when the transaction occurs. If the hedged transaction is no longer probable, the cumulative unrealised gain or loss recognised in equity is recognised in the Consolidated Statement of Profit or Loss immediately.

Categories of financial instruments

	2020 £'000	2019 (restated) £'000
Non-current assets		
Fair value (level 3)		
Investments – other investments	65	–
Contingent consideration	5,431	–
	5,496	–
Amortised cost		
Loan notes	3,160	–
Current assets		
Amortised cost		
Trade receivables	39,831	36,749
Deferred consideration	500	4,618
Other debtors	3,034	5,097
Cash at bank and in hand	96,220	72,909
	139,585	119,373
Non-current liabilities		
Fair value (level 2)		
Interest rate swaps – effective	(479)	(39)
Interest rate swaps – ineffective	17	–
Interest rate swaps	(462)	(39)
Amortised cost		
Long-term borrowing and overdrafts	(39,353)	(124,047)
Lease liabilities	(166,183)	(166,000)
Other payables	(3,667)	(4,700)
	(209,203)	(294,747)
Current liabilities		
Fair value (level 2)		
Interest rate swaps – effective	(484)	(119)
Interest rate swaps – ineffective	25	–
Interest rate swaps	(459)	(119)
Amortised cost		
Trade payables	(114,711)	(125,054)
Lease liabilities	(42,888)	(39,175)
Other creditors	(3,208)	(6,741)
	(160,807)	(170,970)
	(222,690)	(346,502)

Financial statements continued

Notes to the financial statements – Group continued

For the year ended 31 December 2020

24. Financial instruments continued

The amount recognised as an allowance for expected credit losses on trade receivables during 2020 was £3.0m (2019: £1.0m).

The IFRS 13 hierarchy level categorisation relates to the extent the fair value can be determined by reference to comparable market values. The classifications range from level 1, where instruments are quoted on an active market, through to level 3, where the assumptions used to arrive at fair value do not have comparable market data.

The fair values of interest rate swaps have been calculated by a third party expert discounting estimated future cash flows on the basis of market expectations of future interest rates (level 2).

The amount of contingent consideration receivable is typically determined by future expected profits of the sold businesses. The fair values of contingent consideration have been calculated by management by reference to expected future income and expenditure of the disposed business and the terms of the sale (level 3). Where appropriate, the fair value of contingent consideration is discounted at the Group's weighted average cost of capital.

The increase in the fair value of contingent consideration of £0.04m between the date of disposal and the year end was recognised in the Consolidated Statement of Profit or Loss.

The fair values of investments in unlisted equity instruments are determined by reference to an assessment of the fair value of the entity to which they relate. This is typically based on a multiple of earnings of the underlying business.

There have been no transfers between levels during the year.

Fair value information

The fair value of the Group's financial assets and liabilities is as disclosed above and approximates to the book value.

Financial risk management

The Group's activities expose it to a variety of financial risks: market risk (including interest rate risk and price risk); credit risk; and liquidity risk. The main risks faced by the Group relate to the availability of funds to meet business needs and the risk of credit default by customers. The Group's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Group's financial performance.

Risk management is carried out under policies and guidelines approved by the Board of Directors.

Borrowing facilities

The Group's borrowing facilities are drawn on as required to manage its cash needs. Banking facilities are reviewed regularly and extended and replaced in advance of their expiry.

The Group had total borrowing facilities of £145.0m with Barclays Bank PLC, HSBC Bank PLC and the Bank of Ireland, of which £40.0m was utilised at 31 December 2020.

The facilities comprise a committed four-year £135.0m revolving credit facility and an unsecured overdraft facility of £10.0m. The undrawn amounts at 31 December 2020 were a £95.0m revolving credit facility and an overdraft facility of £10.0m.

Details of the Group's banking covenants are provided on page 27.

Interest rate risk management

The Group finances its operations through a mixture of retained profits and bank borrowings from major banking institutions at floating rates of interest based on LIBOR. The Group's exposure to interest rate fluctuations on borrowings is managed through the use of interest rate swaps; hence the fixed rate borrowings relate to floating rate loans where the interest rate has been fixed by a hedging arrangement. Publication of LIBOR is expected to cease before the end of 2021, after which floating interest rates currently linked to LIBOR will be transitioned to an appropriate alternative reference rate.

The fair value of interest rate exposure on financial liabilities of the Group as at 31 December 2020 was:

	Interest rate			
	Fixed £'000	Floating £'000	Zero £'000	Total £'000
Financial liabilities – 2020	40,000	–	–	40,000
Financial liabilities – 2019	70,000	55,000	–	125,000

24. Financial instruments continued

The Group's policy is to accept a degree of interest rate risk, provided the effects of the various potential changes in rates remain within certain prescribed parameters.

Accordingly, at 31 December 2020 the Group had hedged part of the £145.0m total borrowing facilities by entering into interest rate swap arrangements with Barclays Bank PLC and Bank of Ireland. In addition, the Group had entered into interest rate swap arrangements with forward start dates with HSBC Bank PLC.

The arrangement with Barclays Bank PLC consists of two £15.0m swap contracts expiring in August 2021. The arrangement with Bank of Ireland consists of one £15.0m swap contract expiring in June 2023. The arrangement with HSBC Bank PLC consists of three swap contracts totalling £45.0m expiring in January 2024. All arrangements have quarterly maturity, matching the underlying facility.

The maturity of the interest rate swap contracts is as follows:

	2020		2019	
	Nominal amount hedged £'000	Average applicable interest rates %	Nominal amount hedged £'000	Average applicable interest rates %
Within one year	30,000	0.96%	40,000	0.84%
One to two years	–	–	30,000	0.96%
Two to five years	60,000	0.45%	–	–
More than five years	–	–	–	–

Effective interest rates

Interest rate swaps with fair value liabilities of £0.9m (2019: £0.2m) and average remaining lives of two years and two months have been accounted for in financial liabilities.

The Group's overall average cost of debt, including effective interest rate swaps, is 2.4% as at 31 December 2020 (2019: 2.6%). Excluding these swaps, the average is 2.1% (2019: 2.6%).

Cash flow hedging reserve

The cash flow hedging reserve comprises all gains and losses arising from the valuation of interest swap contracts which are effective hedges and mature after the year end. These are valued on a mark-to-market basis, accounted for through the Consolidated Statement of Comprehensive Income and recycled through the Consolidated Statement of Profit or Loss when the hedged item affects the Consolidated Statement of Profit or Loss.

Movements during the year were:

	£'000
At 1 January 2019	(46)
Amounts transferred to the Consolidated Statement of Profit or Loss	49
Revaluations during the year	(145)
Deferred tax movement	18
At 1 January 2020	(124)
Amounts transferred to the Consolidated Statement of Profit or Loss	354
Revaluations during the year	(1,139)
Deferred tax movement	149
At 31 December 2020	(760)

At 31 December 2020 the Group had minimal exposure to movements in interest rates as the remaining interest rate risk was offset by the Group's cash and short-term deposits.

If the interest rates had been 0.5% higher or lower and all other variables were held constant, the Group's profit before taxation for the year ended 31 December 2020 and reserves would decrease or increase, respectively, by £0.6m (2019: £0.4m).

Liquidity risk management

The Group seeks to manage liquidity risk by ensuring sufficient liquidity is available to meet foreseeable needs and to invest cash assets safely and profitably.

Financial statements continued

Notes to the financial statements – Group continued

For the year ended 31 December 2020

24. Financial instruments continued

Management monitors rolling forecasts of the Group's liquidity reserve (comprising undrawn borrowing facilities and cash and cash equivalents) on the basis of expected cash flows. This is generally carried out at a local level in the operating companies of the Group in accordance with the practice and limits set by the Group. These limits vary by location and take into account the liquidity and nature of the market in which the entity operates.

The quantum of committed borrowing facilities of the Group is regularly reviewed and is designed to exceed forecast peak gross debt levels. For short-term working capital purposes, the Group utilises bank overdrafts as required. These facilities are regularly reviewed and are renegotiated ahead of their expiry date.

The table below shows the maturity profile of the Group's financial liabilities:

	Within 1 year £'000	1–2 years £'000	2–5 years £'000	Over 5 years £'000	Total £'000
2020					
Non-derivative financial liabilities					
Bank borrowings	–	39,353	–	–	39,353
Trade and other payables	117,919	3,667	–	–	121,586
Lease liabilities	55,237	33,777	54,774	121,603	265,391
Derivative financial liabilities					
Interest rate swaps – effective	459	246	216	–	921
2019					
Non-derivative financial liabilities					
Bank borrowings	54,047	–	70,000	–	124,047
Trade and other payables	131,795	4,700	–	–	136,495
Lease liabilities (restated)	41,383	32,499	53,499	126,455	253,836
Derivative financial liabilities					
Interest rate swaps – effective	119	39	–	–	158

The Group has disclosed core bank borrowings of £39.4m as due in two to five years. Whilst the amounts borrowed could be repaid each quarter, the Group's intention is to align core bank borrowings with its interest rate swaps.

Credit risk management

The Group's credit risk is primarily attributable to its trade receivables, contract assets and work in progress.

Trade receivables are normally due within 30 to 60 days. Trade and other receivables included in the Consolidated Balance Sheet are stated net of a bad debt provision which has been estimated by management following a review of individual receivable accounts. There is no Group-wide rate of provision and provision made for debts that are overdue is based on prior default experience and known factors at the balance sheet date. Receivables are written off against the bad debt provision when management considers that the debt is no longer recoverable.

Housing customers are typically Local and Central Government and Housing Associations. The nature of these customers means that credit risk is minimal. Other trade receivables contain no specific concentration of credit risk as the amounts recognised represent a large number of receivables from various customers.

The Group continually monitors the position of major customers and incorporates this information into its credit risk controls. External credit ratings are obtained where appropriate.

Details of the ageing of trade receivables are shown in note 19.

Loan notes receivable

The loan notes included within non-current assets were received as part of the disposal of the TerraQuest Group. They are repayable in December 2028 and accrue interest at 10% per annum.

24. Financial instruments continued

Deferred and contingent consideration

The table below shows the movements in deferred consideration receivable:

	Deferred £'000	Contingent £'000	Total £'000
At 1 January 2019	–	–	–
Increase due to disposals in the year	4,618	–	4,618
At 1 January 2020	4,618	–	4,618
Increase due to disposal of Domiciliary Care businesses	1,500	–	1,500
Fair value of contingent consideration on disposal of Planning Solutions business	–	5,395	5,395
Movement in fair value of contingent consideration	–	36	36
Received during the year	(5,618)	–	(5,618)
At 31 December 2020	500	5,431	5,931

The balance of deferred consideration is expected to be received within one year. The balance of contingent consideration is expected to be received in March 2022.

Capital management

The Group's objectives when managing capital are:

- ▶ to safeguard the Group's ability to continue as a going concern, so that it can continue to provide returns for shareholders and benefits for other stakeholders;
- ▶ to provide an adequate return to shareholders by pricing products and services commensurately with the level of risk; and
- ▶ to maintain an optimal capital structure to reduce the cost of capital.

The Group sets the amount of capital in proportion to risk. The Group manages the capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets. In order to maintain or adjust the capital structure, the Group may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares or sell assets to reduce debt.

The capital structure of the Group consists of net debt as disclosed below and equity as disclosed in the Consolidated Statement of Changes in Equity.

	2020 £'000	2019 £'000
The Group considers its revolving credit facility to be an integral part of its cash management:		
▶ Cash at bank and in hand	96,220	73,061
▶ Revolving credit facility	(39,353)	(124,047)
Cash and cash equivalents, including revolving credit facility	56,867	(50,986)

Financial statements continued

Notes to the financial statements – Group continued

For the year ended 31 December 2020

25. Deferred taxation

Deferred tax is calculated on temporary differences under the liability method.

Deferred tax assets

The following deferred tax assets were recognised by the Group as at 31 December 2020:

	Pension scheme £'000	Share-based payments £'000	Cash flow hedges £'000	Tax losses £'000	Other temporary differences (restated) £'000	Total £'000
At 1 January 2019	723	607	11	1,407	1,752	4,500
Impact of change in accounting policies (restated)	–	–	–	–	646	646
<u>Adjusted balance at 1 January 2019 (restated)</u>	<u>723</u>	<u>607</u>	<u>11</u>	<u>1,407</u>	<u>2,398</u>	<u>5,146</u>
Credit/(debit) to Consolidated Statement of Profit or Loss	92	(45)	–	(1,343)	(330)	(1,626)
Debit to Consolidated Statement of Changes in Equity	–	(191)	–	–	–	(191)
Credit to Consolidated Statement of Comprehensive Income	356	–	18	–	–	374
Assets classified as held for sale	–	–	–	–	(280)	(280)
At 1 January 2020	1,171	371	29	64	1,788	3,423
Credit/(debit) to Consolidated Statement of Profit or Loss	145	(100)	–	1,215	264	1,524
Credit to Consolidated Statement of Changes in Equity	–	10	–	–	–	10
Credit to Consolidated Statement of Comprehensive Income	1,524	–	149	–	–	1,673
Disposal of subsidiary	–	–	–	–	(92)	(92)
At 31 December 2020	2,840	281	178	1,279	1,960	6,538

In accordance with IFRS 2 'Share-based Payment', the Group has recognised an expense for the consumption of employee services received as consideration for share options granted. A tax deduction will not arise until the options are exercised. The tax deduction in future periods is dependent on the Company's share price at the date of exercise. The estimated future tax deduction is based on the options' intrinsic value at the balance sheet date.

The cumulative amount credited to the Consolidated Statement of Profit or Loss is limited to the tax effect of the associated cumulative share-based payment expense. The excess has been credited directly to equity. This is presented in the Consolidated Statement of Comprehensive Income.

In addition to those recognised, unused tax losses totalling £29.0m (2019: £28.9m) have not been recognised as management does not consider that it is probable that they will be recovered.

Deferred tax liabilities

The following deferred tax liabilities were recognised by the Group as at 31 December 2020:

	Pension scheme £'000	Acquisition intangibles £'000	Total £'000
At 1 January 2019	3,300	5,310	8,610
Debit/(credit) to Consolidated Statement of Profit or Loss	56	(1,882)	(1,826)
Credit to Consolidated Statement of Comprehensive Income	(1,789)	–	(1,789)
At 1 January 2020	1,567	3,428	4,995
Credit to Consolidated Statement of Profit or Loss	(22)	(1,553)	(1,575)
Credit to Consolidated Statement of Comprehensive Income	(202)	–	(202)
At 31 December 2020	1,343	1,875	3,218

Intangible assets acquired as part of a business combination are capitalised at fair value at the date of the acquisition and amortised over their useful economic lives. The UK tax regime calculates tax using the individual financial statements of the members of the Group and not the consolidated accounts. Hence, the tax base of acquisition intangible assets arising on consolidation is £nil. Furthermore, no UK tax relief is available on the majority of acquisition intangibles within individual entities, so the tax base of these assets is also £nil. The estimated tax effect of this £nil tax base is accounted for as a deferred tax liability which is released over the period of amortisation of the associated acquisition intangible asset.

26. Share capital and reserves

Classes of reserves

Share capital represents the nominal value of shares that have been issued.

Share premium represents the difference between the nominal value of shares issued and the total consideration received.

Share-based payment reserve represents employee remuneration which is credited to the share-based payment reserve until the related share options are exercised. Upon exercise the share-based payment reserve is transferred to retained earnings.

The cash flow hedging reserve comprises all gains and losses arising from the valuation of interest swap contracts which are effective hedges and mature after the year end. These are valued on a mark-to-market basis, accounted for through the Consolidated Statement of Comprehensive Income and recycled through the Consolidated Statement of Profit or Loss when the hedged item affects the Consolidated Statement of Profit or Loss.

The merger reserve relates to the difference between the nominal value and total consideration in respect of acquisitions, where the Company was entitled to the merger relief offered by the Companies Act 2006. During the year, £5.0m (2019: £33.3m) of this reserve was transferred to retained earnings following the disposal of a subsidiary (2019: following the impairment of the goodwill associated with the original merger reserve).

Share capital

	2020 £'000	2019 £'000
Allotted, called up and fully paid		
At 1 January 110,490,459 (2019: 110,487,586) ordinary shares of 1p each	1,105	1,105
Issue of 391,438 (2019: 2,873) shares on exercise of share options	4	–
At 31 December 110,881,897 (2019: 110,490,459) ordinary shares of 1p each	1,109	1,105

During the year 391,438 (2019: 2,873) ordinary 1p shares were issued in respect of share options exercised.

27. Notes to the Consolidated Cash Flow Statement

The following non-operating cash flow adjustments have been made to the result for the year before tax:

	2020 £'000	2019 (restated) £'000
Depreciation	47,688	35,187
Impairment of fixed assets	1,500	–
Loss on disposal of property, plant and equipment	231	178
Amortisation	11,736	12,231
Share-based payments	993	400
IAS 19 pension movement	878	190
Equity accounted income from investments	(365)	(536)
Finance income	(86)	(362)
Finance cost	10,186	9,531
Total	72,761	56,819

Financial statements continued

Notes to the financial statements – Group continued

For the year ended 31 December 2020

27. Notes to the Consolidated Cash Flow Statement continued

Movements in financing liabilities during the year are as follows:

	Revolving credit facility £'000	Borrowings relating to assets held for resale £'000	Lease liabilities £'000	Total £'000
At 1 January 2019	93,780	15,000	1,268	110,048
Impact of change in accounting policies	–	–	167,713	167,713
Adjusted balance at 1 January 2019	93,780	15,000	168,981	277,761
Inception of new leases	–	–	68,016	68,016
Termination of leases	–	–	(138)	(138)
Interest	3,157	335	5,814	9,306
Arrangement fees expensed during the year	531	–	–	531
Transferred to assets held for sale	–	–	(2,064)	(2,064)
Cash inflows/(outflows)	26,579	(15,335)	(35,434)	(24,190)
At 1 January 2020	124,047	–	205,175	329,222
Inception of new leases	–	–	46,603	46,603
Termination of leases	–	–	(1,611)	(1,611)
Interest	2,711	–	7,254	9,965
Arrangement fees expensed during the year	515	–	–	515
Disposal of subsidiaries	–	–	(880)	(880)
Cash outflows	(87,920)	–	(47,470)	(135,390)
At 31 December 2020	39,353	–	209,071	248,424

The movement on the borrowings relating to assets held for resale represents the repayment of the remainder of the property acquisition facility introduced during 2017 to enable the Group to acquire and build portfolios of properties prior to disposal to a long-term funding partner.

28. Acquisitions and disposals

The Group made three disposals during the year: its England and Wales Domiciliary Care business in the form of Mears Care Limited, its Scotland Domiciliary Care business in the form of Mears Care (Scotland) Limited and its Planning Solutions business in the form of Terraquest Solutions Limited and Portalplanquest Limited.

Both Domiciliary Care businesses were classified as available for sale in the year ended 31 December 2019. Mears Care Limited was sold on 31 January 2020 for £4.0m in cash and £1.0m in deferred consideration, all of which had been received at 31 December 2020. Mears Care (Scotland) Limited was sold on 25 September 2020 for £2.0m in cash and £0.5m in deferred consideration, with the deferred consideration due during 2021. These disposals completed the Group's planned exit from the Domiciliary Care market. The Group made a profit on disposal of £0.4m and £0.6m respectively for the sales of Mears Care Limited and Mears Care (Scotland) Limited.

The disposal of the Planning Solutions business (the 'Terraquest group') was completed on 9 December 2020. The proceeds from this disposal were £56.9m in cash, £3.2m in loan notes, £0.1m of shares, representing a 6.16% holding in the disposed business and a maximum of £10.0m of contingent consideration. The fair value of the contingent consideration was estimated as £5.4m based on the terms of the sale agreement and the expected future profitability of the Terraquest group, on which the consideration will be calculated. Portalplanquest Limited was a 75% owned subsidiary prior to the sale and therefore the non-controlling interest was eliminated at the point of disposal, resulting in a decrease in equity of £0.1m. The Group made a profit on disposal of £53.0m from the sale of the Terraquest group. Further details of the terms of the sale can be found in the Financial Review on page 20.

During the year, the Group also acquired the remaining 10% of the share capital of Mears New Homes Limited, a subsidiary in which there had previously been a non-controlling interest. These shares were acquired for nominal consideration and resulted in the elimination of the non-controlling interest in the net liabilities of the subsidiary of £0.5m as presented in the Consolidated Statement of Changes in Equity.

During 2019, the Group disposed of Mears Housing Portfolio 2 Limited (MHP 2), a subsidiary that had been part of the Group's property acquisition business. The company was sold for £6.9m of cash plus £4.6m of deferred consideration. The amount received on sale of £6.9m is included in 'cash inflow in respect of property for resale' in the Consolidated cash flow statement for 2019. The deferred consideration was received in September 2020 as described in note 19.

29. Pensions

Accounting policy

Retirement benefit obligations

The Group operates both defined benefit and defined contribution pension schemes as follows:

Defined contribution pensions

A defined contribution plan is a pension plan under which the Group pays fixed contributions to an independent entity. The Group has no legal obligations to pay further contributions after payment of the fixed contribution.

The contributions recognised in respect of defined contribution plans are expensed as they fall due. Liabilities and assets may be recognised if underpayment or prepayment has occurred and are included in current liabilities or current assets as they are normally of a short-term nature.

The assets of the schemes are held separately from those of the Group in an independently administered fund.

Defined benefit pensions

The Group contributes to defined benefit schemes which require contributions to be made to separately administered funds.

A defined benefit plan is a pension plan that defines an amount of pension benefit that an employee will receive on retirement, usually dependent on one or more factors such as age, years of service and salary. The legal obligations for any benefits from this kind of pension plan remain with the Group, even if plan assets for funding the defined benefit plan have been set aside.

Scheme liabilities are measured using the projected unit funding method, applying the principal actuarial assumptions at the balance sheet date. Assets are measured at market value. In accordance with IFRIC 14, the asset that is recognised is restricted to the amount by which the IAS 19 service cost is expected, over the lifetime of the scheme, to exceed funding contributions payable in respect of accruing benefits.

Where the Group has a contractual obligation to make good any deficit in its share of a Local Government Pension Scheme (LGPS) but also has the right to recover the costs of making good any deficit from the Group's client, the fair value of that guarantee asset has been recognised and disclosed. Movements in the guarantee asset are taken to the Consolidated Statement of Profit or Loss and to the Consolidated Statement of Comprehensive Income to match the movement in pension assets and liabilities.

The Group recognises the pension liability and guarantee assets separately on the face of the Consolidated Balance Sheet.

Actuarial gains and losses are taken to the Consolidated Statement of Comprehensive Income as incurred. For this purpose, actuarial gains and losses comprise both the effects of changes in actuarial assumptions and experience adjustments arising because of differences between the previous actuarial assumptions and what has actually occurred.

Other movements in the net surplus or deficit are recognised in the Consolidated Statement of Profit or Loss, including the current service cost, any past service cost and the effect of curtailments or settlements. The net interest cost is also charged to the Consolidated Statement of Profit or Loss. The amount charged to the Consolidated Statement of Profit or Loss in respect of these plans is included within operating costs.

When the Group ceases its participation in a defined benefit pension scheme, the difference between the carrying value of the scheme as calculated on an IAS 19 basis and any deficit payment or surplus receipt due are recognised in the Consolidated Statement of Profit or Loss as a settlement.

The Group's contributions to the scheme are paid in accordance with the rules of the scheme and the recommendations of the scheme actuary.

Defined benefit assets

Scheme assets for LGPS have been estimated by rolling forward the published asset position from the previous year using market index returns over the period. This is considered to provide a good estimate of the fair value of the scheme assets and the values will be updated to actuals each time a triennial valuation takes place.

Financial statements continued

Notes to the financial statements – Group continued

For the year ended 31 December 2020

29. Pensions continued

Defined benefit liabilities

A number of key estimates have been made, which are given below, and which are largely dependent on factors outside the control of the Group:

- ▶ inflation rates;
- ▶ mortality;
- ▶ discount rate; and
- ▶ salary and pension increases.

Details of the particular estimates used are included in this note. Sensitivity analysis for these key estimates is included below.

Where the Group has a contractual obligation to make good any deficit in its share of an LGPS but also has the right to recover the costs of making good any deficit from the Group's client, the fair value of that asset has been recognised and disclosed. The right to recover costs is limited to exclude situations where the Group causes the scheme to incur service costs in excess of those which would have been incurred were the members employed within Local Government. Management has made judgements in respect of whether any of the deficit is as a result of such situations.

The right to recover costs is also limited to situations where the cap on employer contributions to be suffered by the Group is not set so as to contribute to reducing the deficit in the scheme. Management, in conjunction with the scheme actuaries, has made judgements in respect of the predicted future service cost and contributions to the scheme to reflect this in the fair value of the asset recognised.

Key sources of estimation uncertainty

The net position on defined benefit pension schemes is a key source of estimation uncertainty. Given the importance of this area and to ensure appropriate estimates are made based on the most relevant information available, management has continued to engage with third party advisors in assessing each of the underlying assumptions. The discount rate is derived from the return on corporate bond yields, and whilst this is largely observable, any change in discount rates in the future could have a material impact on the carrying value of the defined benefit obligation. Similarly, inflation rates and mortality assumptions impact the defined benefit obligation as they are used to model future salary increases and the duration of pension payments. Whilst current assumptions use projected future inflation rates and the most up to date information available on expected mortality, if these estimates change, the defined benefit obligation could also change materially in future periods.

Defined contribution schemes

The Group operates a defined contribution Group personal pension scheme for the benefit of certain employees. The Group contributes to personal pension schemes of certain Directors and senior employees. The Group operates a stakeholder pension plan available to all employees. During the year, the Group contributed £6.0m (2019: £5.7m) to these schemes.

Defined benefit schemes

The Group contributed to 23 (2019: 30) principal defined benefit schemes on behalf of a number of employees which require contributions to be made to separately administered funds.

These pension schemes are operated on behalf of Mears Limited, Morrison Facilities Services Limited and their subsidiary undertakings. The assets of the schemes are administered by trustees in funds independent from the assets of the Group.

The Group schemes are no longer open to new members and have no particular concentration of investments, so expose the Group only to typical risks associated with defined benefit pension schemes including the risk that investments underperform compared with movements in the scheme liabilities.

In certain cases, the Group will participate under Admitted Body status in the LGPS. The Group will contribute for a finite period up until the end of the particular contract. The Group is required to pay regular contributions as detailed in the scheme's schedule of contributions. In some cases, these contributions are capped and any excess can be recovered from the body from which the employees originally transferred. Where the Group has a contractual right to recover the costs of making good any deficit in the scheme from the Group's client, the fair value of that asset has been recognised as a separate pension guarantee asset. Certain judgements around the value of this asset have been made and are discussed in the judgements and estimates disclosure within the accounting policies.

The disclosures in respect of the two (2019: two) Group defined benefit schemes and the 21 (2019: 28) other defined benefit schemes in this note have been aggregated. Details of movements in pension guarantee assets are presented in a separate table and the disclosures for 2019 have been re-presented in the same way in order to aid comparability.

29. Pensions continued

Costs and liabilities of the schemes are based on actuarial valuations. The latest full actuarial valuations for the schemes were updated to 31 December 2020 by qualified independent actuaries using the projected unit funding method.

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

	2020	2019
Rate of increase of salaries – first year	2.85%	2.90%
Rate of increase of salaries – second year	2.85%	2.90%
Rate of increase of salaries – long term	2.85%	2.90%
Rate of increase for pensions in payment – based on CPI with a cap of 5%	2.45%	1.95%
Rate of increase for pensions in payment – based on RPI with a cap of 5%	2.80%	2.85%
Rate of increase for pensions in payment – based on CPI with a cap of 3%	2.10%	1.75%
Rate of increase for pensions in payment – based on RPI with a cap of 3%	2.30%	2.35%
Discount rate	1.35%	2.10%
Retail prices inflation	2.85%	2.90%
Consumer prices inflation	2.45%	1.90%
Life expectancy for a 65-year-old male	21.8 years	22.4 years
Life expectancy for a 65-year-old female	24.0 years	24.6 years

The amounts recognised in the Consolidated Balance Sheet and major categories of plan assets are:

	2020			2019		
	Group schemes £'000	Other schemes £'000	Total £'000	Group schemes £'000	Other schemes £'000	Total £'000
Quoted assets						
Equities	–	180,791	180,791	–	178,526	178,526
Bonds	92,356	66,618	158,974	86,567	65,003	151,570
Property	4,325	29,857	34,182	4,341	7,934	12,275
Pooled investment vehicles						
Multi-asset funds	82,147	–	82,147	69,507	–	69,507
Alternative asset funds	10,604	–	10,604	9,291	–	9,291
Return seeking funds	2,089	–	2,089	1,449	–	1,449
Other assets						
Equities	–	–	–	–	14,924	14,924
Bonds	–	–	–	–	1,836	1,836
Property	–	361	361	–	6,853	6,853
Derivatives	2,284	–	2,284	15,046	–	15,046
Cash and other	3,823	10,864	14,687	2,263	28,388	30,651
Investment liabilities						
Derivatives	(12,192)	–	(12,192)	(25,214)	–	(25,214)
Group's estimated asset share	185,436	288,491	473,927	163,250	303,464	466,714
Present value of funded scheme liabilities	(181,184)	(320,186)	(501,370)	(156,379)	(327,460)	(483,839)
Funded status	4,252	(31,695)	(27,443)	6,871	(23,996)	(17,125)
Scheme surpluses not recognised as assets	–	(11,142)	(11,142)	–	(4,597)	(4,597)
Pension asset/(liability)	4,252	(42,837)	(38,585)	6,871	(28,593)	(21,722)
Pension guarantee assets	–	30,705	30,705	–	23,810	23,810

As noted above, there are two Group schemes, one of which had a recognised surplus at 31 December 2020 of £7.1m (2019: £8.2m) while the other had a deficit of £2.8m (2019: £1.4m). The scheme in deficit is aggregated with the other schemes in deficit on the face of the Consolidated Balance Sheet.

Financial statements continued

Notes to the financial statements – Group continued

For the year ended 31 December 2020

29. Pensions continued

The amounts recognised in the Consolidated Statement of Profit or Loss are as follows:

	2020			2019		
	Group schemes £'000	Other schemes £'000	Total £'000	Group schemes £'000	Other schemes £'000	Total £'000
Current service cost	2,029	4,244	6,273	1,989	4,595	6,584
Past service cost	–	–	–	–	150	150
Settlement and curtailment	–	(22)	(22)	–	–	–
Administration costs	375	–	375	277	–	277
Total operating charge	2,404	4,222	6,626	2,266	4,745	7,011
Net interest	(206)	466	260	(512)	481	(31)
Effects of limitation of recognisable surplus related to net interest	–	56	56	–	119	119
Total charged to the result for the year	2,198	4,744	6,942	1,754	5,345	7,099

Past service cost above includes a charge of £nil (2019: £150,000) in respect of the Group's estimate of the impact on LGPSs of the 'McCloud' judgement in respect of historical age discrimination.

Cumulative actuarial gains and losses recognised in other comprehensive income (OCI) are as follows:

	2020			2019		
	Group schemes £'000	Other schemes £'000	Total £'000	Group schemes £'000	Other schemes £'000	Total £'000
Return on plan assets in excess of that recorded in net interest	21,081	20,766	41,847	8,623	33,851	42,474
Actuarial gain arising from changes in demographic assumptions	1,693	8,364	10,057	717	–	717
Actuarial loss arising from changes in financial assumptions	(25,060)	(62,337)	(87,397)	(18,481)	(40,664)	(59,145)
Actuarial (loss)/gain arising from liability experience	(350)	25,300	24,950	(957)	(1)	(958)
On scheme transfer	–	(157)	(157)	–	–	–
Effects of limitation of recognisable surplus related to OCI movements	–	(8,414)	(8,414)	–	1,393	1,393
Total gains and losses recognised in OCI	(2,636)	(16,478)	(19,114)	(10,098)	(5,421)	(15,519)

Changes in the present value of the defined benefit obligations are as follows:

	2020			2019		
	Group schemes £'000	Other schemes £'000	Total £'000	Group schemes £'000	Other schemes £'000	Total £'000
Present value of obligations at 1 January	156,379	327,460	483,839	136,548	282,368	418,916
Liabilities related to assets classified as held for sale	–	–	–	–	(3,105)	(3,105)
Current service cost	2,029	4,244	6,273	1,989	2,391	4,380
Past service cost	–	–	–	–	150	150
Interest on obligations	3,241	5,974	9,215	3,958	7,812	11,770
Plan participants' contributions	264	763	1,027	301	894	1,195
Benefits paid	(4,446)	(4,189)	(8,635)	(5,138)	(5,505)	(10,643)
Contract transfer	–	(42,595)	(42,595)	–	(79)	(79)
Settlements	–	(144)	(144)	–	–	–
Actuarial gain arising from changes in demographic assumptions	(1,693)	(8,364)	(10,057)	(717)	–	(717)
Actuarial loss arising from changes in financial assumptions	25,060	62,337	87,397	18,481	42,533	61,014
Actuarial loss/(gain) arising from liability experience	350	(25,300)	(24,950)	957	1	958
Present value of obligations at 31 December	181,184	320,186	501,370	156,379	327,460	483,839

29. Pensions continued

Changes in the fair value of the plan assets are as follows:

	2020			2019		
	Group schemes £'000	Other schemes £'000	Total £'000	Group schemes £'000	Other schemes £'000	Total £'000
Fair value of plan assets at 1 January	163,250	303,464	466,714	152,872	268,774	421,646
Assets classified as held for sale	–	–	–	–	(3,079)	(3,079)
Expected return on plan assets	3,447	5,508	8,955	4,470	7,331	11,801
Employer's contributions	2,215	1,805	4,020	2,399	1,767	4,166
Plan participants' contributions	264	763	1,027	301	894	1,195
Benefits paid	(4,446)	(4,189)	(8,635)	(5,138)	(5,505)	(10,643)
Scheme administration costs	(375)	–	(375)	(277)	–	(277)
Contract transfer	–	(39,836)	(39,836)	–	(253)	(253)
Settlements	–	(122)	(122)	–	–	–
Return on plan assets above/(below) that recorded in net interest	21,081	21,098	42,179	8,623	33,535	42,158
Fair value of plan assets at 31 December	185,436	288,491	473,927	163,250	303,464	466,714

Changes in the fair value of guarantee assets are as follows:

	2020 £'000	2019 £'000
Fair value of guarantee assets at 1 January	23,810	16,947
Assets classified as held for sale	–	(92)
Transferred out on scheme exit	(5,173)	–
Recognised in the Consolidated Statement of Profit or Loss		
Guarantee asset movement in respect of service cost	1,626	2,204
Guarantee asset movement in respect of net interest	418	520
Recognised in other comprehensive income		
Guarantee asset movement in respect of actuarial losses	10,024	4,231
Fair value of guarantee assets at 31 December	30,705	23,810

Financial statements continued

Notes to the financial statements – Group continued

For the year ended 31 December 2020

29. Pensions continued

History of experience gains and losses is as follows:

	Group schemes				
	2020 £'000	2019 £'000	2018 £'000	2017 £'000	2016 £'000
Fair value of scheme assets	185,436	163,250	152,872	157,325	149,529
Net present value of defined benefit obligations	(181,184)	(156,379)	(136,548)	(132,591)	(137,721)
Net surplus	4,252	6,871	16,324	24,734	11,808
Experience adjustments arising on scheme assets					
Amount	21,081	8,623	(7,270)	3,942	27,129
Percentage of scheme assets	11.4%	5.3%	(4.8%)	2.5%	18.1%
Experience adjustments arising on scheme liabilities					
Amount	350	957	3,967	28	(1,000)
Percentage of scheme liabilities	0.2%	0.6%	2.9%	0.0%	(0.7%)
Other schemes					
	2020 £'000	2019 £'000	2018 £'000	2017 £'000	2016 £'000
Fair value of scheme assets	288,491	303,464	268,774	345,527	404,104
Pension guarantee assets	30,705	23,810	16,947	7,026	18,587
Net present value of defined benefit obligations	(320,186)	(327,460)	(282,368)	(324,920)	(410,258)
Net (deficit)/surplus	(990)	(186)	3,353	27,633	12,433
Asset value not recognised as surplus	(11,142)	(4,597)	(6,111)	(30,025)	(15,747)
Net deficit	(12,132)	(4,783)	(2,758)	(2,392)	(3,314)
Experience adjustments arising on scheme assets					
Amount	21,098	33,535	(17,467)	(4,314)	59,020
Percentage of scheme assets	7.3%	11.1%	(6.5%)	(1.2%)	14.6%
Experience adjustments arising on scheme liabilities					
Amount	(25,300)	1	676	(31,447)	(1,714)
Percentage of scheme liabilities	(7.9%)	0.0%	0.2%	(9.7%)	(0.4%)

Funding arrangements are agreed for each of the Group's defined benefit pension schemes with their respective trustees. The employer's contributions expected to be paid during the financial year ending 31 December 2021 amount to £3.3m.

Each of the schemes manages risks through a variety of methods and strategies to limit downside in falls in equity markets, movement in inflation and movement in interest rates.

The Group's defined benefit obligation is sensitive to changes in certain key assumptions. The sensitivity analysis below shows how a reasonably possible increase or decrease in a particular assumption, in isolation, results in an increase or decrease in the present value of the defined benefit obligation as at 31 December 2020.

	Decrease £'000	Increase £'000
Rate of inflation – decrease/increase by 0.1%	(8,795)	8,689
Rate of increase in salaries – decrease/increase by 0.1%	(3,755)	3,744
Discount rate – decrease/increase by 0.1%	9,157	(9,051)
Life expectancy – decrease/increase by 1 year	(18,816)	18,816

30. Capital commitments

The Group had no capital commitments at 31 December 2020 or at 31 December 2019.

31. Contingent liabilities

The Group has guaranteed that it will complete certain Group contracts that it has commenced. At 31 December 2020 these guarantees amounted to £14.7m (2019: £19.3m).

The Group had no other contingent liabilities at 31 December 2020 or at 31 December 2019.

32. Related party transactions

Identity of related parties

The Group has a related party relationship with its pension schemes, its subsidiaries and its Directors.

Pension schemes

Details of contributions to pension schemes are set out in note 29.

Subsidiaries

The Group has a central treasury arrangement in which all subsidiaries participate. Management does not consider it meaningful to set out details of transfers made in respect of this treasury arrangement between companies, nor does it consider it meaningful to set out details of interest or dividend payments made within the Group.

Transactions with key management personnel

The Group has identified key management personnel as the Directors of Mears Group PLC.

Key management personnel held the following percentage of voting shares in Mears Group PLC:

	2020 %	2019 %
Directors	0.6	0.3

Key management personnel's compensation is as follows:

	2020 £'000	2019 £'000
Salaries including social security costs	2,063	1,634
Contributions to defined contribution pension schemes	131	130
Share-based payments	340	—
	2,534	1,764

Further details of Directors' remuneration are disclosed within the Remuneration Report.

No dividends were paid to Directors during the year (2019: £0.04m).

Transactions with other related parties

During the year the Group made an additional short-term loan to YourMK LLP, an entity in which the Group is a 50% member, totalling £0.2m (2019: £0.1m). This loan was repaid during the period. At 31 December 2020, the Group was owed £0.5m (2019: £0.5m) by YourMK LLP.

During the year the Group provided maintenance services to Pyramid Plus South LLP, an entity in which the Group is a 30% member, totalling £7.9m (2019: £6.5m). At 31 December 2020, £0.9m (2019: £0.8m) was due to the Group in respect of these transactions. Pyramid Plus South LLP also made recharges of certain staff costs to the Group totalling £0.1m (2019: £nil). There were no amounts outstanding at 31 December 2020 in respect of these recharges (2019: £nil).

Financial statements continued

Notes to the financial statements – Group continued

For the year ended 31 December 2020

33. Restatement of prior year

Discontinued activities

The Consolidated statement of Profit or Loss has been restated to reflect the disposal of the Group's Planning Solutions business which was the subject of a disposal in December 2020, as detailed in note 10.

Deferred tax reclassification

A reclassification adjustment has been made to deferred tax and relates to the netting off of the deferred tax asset against the deferred tax liability, where the asset and liability were previously reported separately.

Reassessment of lease accounting

During the year, the Group revisited the assumptions made at the time of the adoption of IFRS 16, and its assessment of the right of use assets and lease obligations as at transition and at 31 December 2019. As detailed below, the Directors have concluded that in the prior year, the right of use asset and associated lease obligation were overstated and as such, the Consolidated Statement of Profit or Loss, Consolidated Balance Sheet and Consolidated Cash Flow Statement have been restated to correct this error.

The Group holds more than 15,000 leases across its portfolio of residential properties, offices and vehicles. The most significant and complex category relates to the Group's portfolio of residential properties which comprises approximately 10,500 leases; whilst the Group endeavours to standardise the form of leases, operational demands dictate that many leases have specific wording to address particular operational needs and also to manage the associated operational and financial risks. The Group's suppliers of residential properties, being the property owners, will similarly have their own requirements. As such, each residential property lease requires individual assessment and the Group is required to make key judgements which include:

- ▶ the identification of a lease;
- ▶ assessing the right to direct the use of the asset;
- ▶ determining the lease term; and
- ▶ the assessment as to the level of future lease payments, including fixed and variable payments.

The most typical challenges encountered, and which form the key judgements, are:

- ▶ where the lease contains a one-way no-fault break in Mears' favour, the Group measures the obligation based on the Group's best estimate of its future intentions;
- ▶ where a unilateral break is in place, assessing whether the lease can be terminated with no more than insignificant penalty;
- ▶ where the lessor has a right of substitution meaning that the lessor can swap one property for another without Mears approval;
- ▶ where Mears does not in practice have the right to control the use of the asset and the key decision-making rights are retained by the supplier;
- ▶ where a wider agreement for a supply of services includes a lease component which meets the definition of a lease under IFRS 16; and
- ▶ the assessment of the fixed lease payments where the lease obligation to the landlord is based on a pass-through arrangement in which Mears only makes lease payments to the owner to the extent that the property is occupied and to the extent that rents are received from the tenant.

Several errors and omissions impacting on the carrying values reported within the 2019 comparatives were identified; one particularly significant reassessment resulted in a significant reduction in the right of use asset and lease obligation reported in 2019. This reassessment related to the Group's 'More Homes' homelessness solution, through which the Group and its Local Authority partner acquire properties and, utilising a leasing arrangement, make these properties available to service users nominated by the Local Authority partner. Mears has no right to direct the use of the properties and the Local Authority partner operates the asset in a manner that it determines. Mears' participation is restricted to delivering tenancy management and maintenance services, and therefore the associated revenue has been restated to reflect Mears as the agent.

In the prior year, this arrangement was incorrectly identified as a lease within the definition of IFRS 16. This treatment has been reassessed during 2020, and management recognises that the previous treatment was incorrect.

The comparative figures have therefore been restated to reflect the correctly calculated figures as shown in the tables below:

33. Restatement of prior year continued

The comparative figures have therefore been restated to reflect the correctly calculated figures as shown in the tables below:

	Previously reported £'000	Discontinued activities £'000	Reassessment of lease accounting £'000	Restated £'000
Consolidated Statement of Profit or Loss				
Continuing operations				
Sales revenue	905,084	(20,880)	(2,747)	881,457
Cost of sales	(686,874)	9,030	2,496	(675,348)
Gross profit	218,210	(11,850)	(251)	206,109
Other administrative expenses	(172,632)	6,788	(36)	(165,880)
Exceptional costs	(2,018)	–	–	(2,018)
Amortisation of acquisition intangibles	(10,122)	–	–	(10,122)
Total administrative costs	(184,772)	6,788	(36)	(178,020)
Operating profit/(loss)	33,438	(5,062)	(287)	28,089
Share of profits of associates	895	–	–	895
Finance income	849	–	–	849
Finance costs	(9,981)	114	287	(9,580)
Profit/(loss) for the year before tax	25,201	(4,948)	–	20,253
Tax (expense)/credit	(3,976)	961	–	(3,015)
Profit/(loss) for the year from continuing operations	21,225	(3,987)	–	17,238

The adjustment for discontinued activities removes the trading result from the Group's Planning Solutions business in accordance with IFRS 5.

The adjustment for the reassessment of lease accounting in the Consolidated Statement of Profit or Loss reflects Mears as agent in the arrangement with More Homes referred to above and the net impact of removing the depreciation charge to reflect the reduction in the right of use asset, replacing this with the lease payments associated with the assets no longer falling under IFRS 16. Similarly, the reduction in the interest charge reflects the reduction in the lease obligation.

	Previously reported £'000	Reclassification £'000	Reassessment of lease accounting £'000	Restated £'000
Consolidated Balance Sheet – restated lines				
Non-current assets				
Right of use assets	264,576	–	(66,192)	198,384
Deferred tax asset	3,310	(3,310)	–	–
Current assets				
Trade and other receivables	162,838	–	1,253	164,091
Equity				
Retained earnings	20,496	–	(656)	19,840
Non-current liabilities				
Deferred tax liabilities	4,995	(3,310)	(113)	1,572
Lease liabilities	228,588	–	(62,588)	166,000
Current liabilities				
Lease liabilities	40,757	–	(1,582)	39,175

The reclassification adjustment relates to the netting off of the deferred tax asset against the deferred tax liability where the asset and liability were previously reported separately.

The adjustment for the reassessment of lease accounting in the Consolidated Statement of Profit or Loss reflects Mears as agent in the arrangement with More Homes referred to above and the net impact of removing the depreciation charge to reflect the reduction in the right of use asset, replacing this with the lease payments associated with the assets no longer falling under IFRS 16. Similarly, the reduction in the interest charge reflects the reduction in the lease obligation.

Financial statements continued

Notes to the financial statements – Group continued

For the year ended 31 December 2020

33. Restatement of prior year continued

	Previously reported £'000	Discontinued activities £'000	Reassessment of lease accounting £'000	Restated £'000
Consolidated Cash Flow Statement – restated lines				
Operating activities				
Result for the year before tax	25,201	(4,948)	–	20,253
Adjustments	64,032	(1,607)	(5,606)	56,819
Change in inventories	(6,294)	(63)	–	(6,357)
Change in trade and other receivables	4,971	(1,038)	(1,253)	2,680
Change in trade, other payables and provisions	12,340	1,195	(12)	13,523
Cash inflow from operating activities of continuing operations before taxation	100,250	(6,461)	(6,871)	86,918
Taxes paid	(2,991)	(386)	–	(3,377)
Net cash inflow from operating activities of continuing operations	97,259	(6,847)	(6,871)	83,541
Net cash outflow from operating activities of discontinued operations	(1,943)	6,847	–	4,904
Net cash inflow from operating activities	95,316	–	(6,871)	88,445
Investing activities				
Additions to property, plant and equipment	(8,513)	136	–	(8,377)
Additions to other intangible assets	(3,011)	1,332	–	(1,679)
Proceeds from disposals of property, plant and equipment	46	–	–	46
Cash inflow in respect of property for resale	7,824	–	–	7,824
Payments on acquisitions, net of cash acquired	(1,300)	–	–	(1,300)
Loans made to other entities (non-controlled)	(48)	–	–	(48)
Interest received	363	–	–	363
Net cash (outflow)/inflow from investing activities of continuing operations	(4,639)	1,468	–	(3,171)
Net cash (outflow)/inflow from investing activities of discontinued operations	(841)	(1,468)	–	(2,309)
Net cash outflow from investing activities	(5,480)	–	–	(5,480)
Financing activities				
Proceeds from share issue	1	–	–	1
(Repayment of)/receipts from borrowings related to assets classified as held for sale	(15,000)	–	–	(15,000)
Net movement in revolving credit facility	30,267	–	–	30,267
Discharge of lease liabilities	(35,411)	(351)	6,583	(29,179)
Interest paid	(9,843)	109	288	(9,446)
Dividends paid – Mears Group shareholders	(13,811)	–	–	(13,811)
Net cash outflow from financing activities of continuing operations	(43,797)	(242)	6,871	(37,168)
Net cash outflow from financing activities of discontinued operations	(854)	242	–	(612)
Net cash outflow from financing activities	(44,651)	–	6,871	(37,780)
Cash and cash equivalents, beginning of year	27,876	–	–	27,876
Net increase in cash and cash equivalents	45,185	–	–	45,185
Cash and cash equivalents, end of year (including discontinued)	73,061	–	–	73,061

The adjustment for discontinued activities removes the cash flows from the Group's Planning Solutions business which are aggregated and included within the discontinued operations.

The adjustment for the reassessment of lease accounting reflects the changing focus from IFRS 16 (which is seen as financing activities) to IFRS 15 (which is seen as operating cash flows). IFRS 16 has no impact on pre-tax cash flows and as such there is no cash impact from this restatement of the prior year.

Parent Company balance sheet

As at 31 December 2020

	Note	2020 £'000	2019 (restated) £'000
Non-current assets			
Intangible assets: goodwill		—	—
Right of use assets	6	19,146	22,448
Investments	7	139,398	39,583
Deferred tax asset		713	319
		159,257	62,350
Current assets			
Debtors	8	40,772	189,096
Cash at bank and in hand		21,461	21,597
		62,233	210,693
Creditors: amounts falling due within one year	9	(30,194)	(27,590)
Net current assets		32,039	183,103
Total assets less current liabilities		191,296	245,453
Creditors: amounts falling due after more than one year	10	(49,919)	(135,575)
Provisions for liabilities			
Pension liability	15	(2,816)	(1,378)
		138,561	108,500
Capital and reserves			
Called up share capital	12	1,109	1,105
Share premium account		82,225	82,224
Share-based payment reserve		1,312	2,421
Hedging reserve		(760)	(124)
Profit and loss account		54,675	22,874
Shareholders' funds		138,561	108,500

The Parent Company has taken advantage of Section 408 of the Companies Act 2006 and has not included its own profit and loss account in these financial statements. The Group loss (2019: profit) for the year includes a profit of £42.2m (2019: loss of £11.7m) which is dealt with in the financial statements of the Company.

The financial statements were approved by the Board of Directors on 12 May 2021.

D J Miles **A C M Smith**
Director **Director**
 Company number: 03232863

*Note 17 contains details of the restatement of the prior year figures.

The accompanying accounting policies and notes form an integral part of these financial statements.

Financial statements continued

Parent Company statement of changes in equity

For the year ended 31 December 2020

	Share capital £'000	Share premium account £'000	Share- based payment reserve £'000	Hedging reserve (restated) £'000	Retained earnings (restated) £'000	Total equity £'000
At 1 January 2019	1,105	82,224	2,021	(46)	48,435	133,739
Impact of change in accounting policies	–	–	–	–	(69)	(69)
Adjusted balance at 1 January 2019	1,105	82,224	2,021	(46)	48,366	133,670
Net result for the year	–	–	–	–	(11,128)	(11,128)
Other comprehensive expense	–	–	–	(78)	(553)	(631)
Total comprehensive expense for the year	–	–	–	(78)	(11,681)	(11,759)
Share option charges	–	–	400	–	–	400
Dividends	–	–	–	–	(13,811)	(13,811)
At 1 January 2020	1,105	82,224	2,421	(124)	22,874	108,500
Net result for the year	–	–	–	–	30,936	30,936
Other comprehensive expense	–	–	–	(636)	(1,273)	(1,909)
Total comprehensive (expense)/income for the year	–	–	–	(636)	29,663	29,027
Issue of shares	4	1	–	–	–	5
Share options – value of employee services	–	–	1,029	–	–	1,029
Share options – exercised, cancelled or lapsed	–	–	(2,138)	–	2,138	–
At 31 December 2020	1,109	82,225	1,312	(760)	54,675	138,561

* Note 17 contains details of the restatement of the prior year figures.

The accompanying accounting policies and notes form an integral part of these financial statements.

Notes to the financial statements – Company

For the year ended 31 December 2020

1. Accounting policies

Accounting policies are detailed in their respective notes, where relevant. Policies that are not specific to a particular note are detailed below.

Statement of compliance

Mears Group PLC is a public limited company incorporated in England and Wales. Its registered office is 1390 Montpellier Court, Gloucester Business Park, Brockworth, Gloucester GL3 4AH.

Basis of preparation

The financial statements have been prepared in accordance with applicable United Kingdom accounting standards, including FRS 101 and the Companies Act 2006. The financial statements have been prepared on the historical cost basis except for the modification to a fair value basis for certain financial instruments specified in the accounting policies below. The financial statements are presented in Sterling.

The Company has taken advantage of the exemption in Section 408 of the Companies Act 2006 from disclosing its individual profit and loss account.

The Company has taken advantage of the reduced disclosures for subsidiaries and the ultimate parent provided for in FRS 101 and has therefore not provided a cash flow statement or certain disclosures in respect of share-based payments.

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

Government grants

Government grants are recognised where there is reasonable assurance that the grant will be received, and all attached conditions will be complied with. When the grant relates to an expense item, it is recognised as income on a systematic basis over the periods that the related costs, for which it is intended to compensate, are expensed.

During the period, the Group benefited from receipts from the UK Government under the Coronavirus Job Retention Scheme (CJRS). In accordance with FRS 101, amounts received were presented as other income.

Deferred taxation

Deferred tax is recognised on all timing differences where the transactions or events that give the Company an obligation to pay more tax in the future, or a right to pay less tax in the future, have occurred by the balance sheet date. Deferred tax assets are recognised where it is more likely than not that they will be recovered. Deferred tax is measured using rates of tax and laws that have been enacted or substantively enacted by the balance sheet date.

Critical judgements and key sources of estimation uncertainty

Critical judgements in applying the Company's accounting policies and key sources of estimation uncertainty are disclosed in the Group's accounting policies.

2. Result for the financial year

This result for the year is stated after charging auditor's remuneration of £130,000 (2019: £71,000) relating to audit services.

3. Directors and employees

Employee benefits expense:

	2020 £'000	2019 £'000
Wages and salaries	13,189	13,469
Social security costs	1,665	1,826
Other pension costs	412	282
	15,266	15,577

A Coronavirus Job Retention Scheme grant of £0.6m was recognised as other income.

Financial statements continued

Notes to the financial statements – Company continued

For the year ended 31 December 2020

3. Directors and employees continued

The average number of employees of the Company during the year was:

	2020 Number	2019 Number
Management	308	335
	2020 £'000	2019 £'000
Emoluments	1,821	1,499
Pension contributions to personal pension schemes	131	130
Gains on exercise of options	340	–
	2,292	1,629

During the year contributions were paid to personal pension schemes for three Directors (2019: three).

During the year three Directors (2019: none) exercised share options.

4. Share-based employee remuneration

Accounting policy

All share-based payment arrangements that were granted after 7 November 2002 are recognised in the financial statements.

The Group operates equity-settled and cash-settled share-based remuneration plans for its employees. All employee services received in exchange for the grant of any share-based remuneration are measured at their fair value. These are indirectly determined by reference to the fair value of the share options awarded. Their value is determined at the date of grant and is not subsequently remeasured unless the conditions on which the award was granted are modified. The fair value at the date of the grant is calculated using the Black Scholes option pricing model and the cost is recognised on a straight-line basis over the vesting period. Adjustments are made to reflect expected and actual forfeitures during the vesting period.

Share-based remuneration in respect of employees of the Company is ultimately recognised as an expense in the profit and loss account. For equity-settled share-based payments there is a corresponding credit to the share-based payment reserve; for cash-settled share-based payments the Company recognises a liability at the balance sheet date. The Company operates share-based remuneration plans for employees of subsidiaries using the Company's equity instruments. The fair value of the compensation given in respect of these share-based compensation plans less payments received from subsidiaries in respect of those share-based payments is recognised as a capital contribution.

Upon exercise of share options, the proceeds received, net of any directly attributable transaction costs up to the nominal value of the shares issued, are allocated to share capital with any excess being recorded as share premium.

As at 31 December 2020 the Group maintained four share-based payment schemes for employee remuneration. The details of each scheme are included within note 7 to the consolidated financial statements.

All share-based employee remuneration will be settled in equity. The Group has no legal obligation to repurchase or settle the options.

5. Dividends

The following dividends were paid on ordinary shares in the year:

	2020 £'000	2019 £'000
Final 2019 dividend of 0p (2019: final 2018 dividend of 8.55p) per share	–	9,778
Interim 2020 dividend of 0p (2019: interim 2019 dividend of 3.65p) per share	–	4,033
	–	13,811

Given the impact of the COVID-19 pandemic, and the loss for the year from continuing operations, the Board does not intend to declare a dividend for 2020. The Board will seek to return to the dividend list once it is prudent to do so.

6. Right of use assets

Accounting policy

Where an asset is subject to a lease, the Company recognises a right of use asset and a lease liability on the balance sheet. The right of use asset is measured at cost, which matches the initial measurement of the lease liability and any costs expected at the end of the lease, and then depreciated on a straight-line basis over the lease term.

The lease liability is measured at the present value of the future lease payments discounted using the Group's incremental borrowing rate. Lease payments include fixed payments, variable payments based on an index and payments arising from options reasonably certain to be exercised.

The Group has elected to account for short-term leases and leases of low-value assets using the practical expedients. Instead of recognising a right of use asset and a lease liability, the payments in relation to these are recognised as an expense in profit or loss on a straight-line basis over the lease term.

On the statement of financial position, right of use assets and lease liabilities are presented separately.

	Offices £'000	Motor vehicles £'000	Total £'000
Gross carrying amount			
At 1 January 2019	—	—	—
Recognised on transition to IFRS 16 (restated)	1,115	20,985	22,100
Additions (restated)*	—	11,124	11,124
At 1 January 2020	1,115	32,109	33,224
Additions*	12	8,187	8,199
Disposals	(18)	(2,390)	(2,408)
At 31 December 2020	1,109	37,906	39,015
Depreciation			
At 1 January 2019	—	—	—
Provided in the year (restated)	219	10,557	10,776
At 1 January 2020	219	10,557	10,776
Provided in the year	214	11,112	11,326
Eliminated on disposals	(18)	(2,215)	(2,233)
At 31 December 2020	415	19,454	19,869
Carrying amount			
At 31 December 2020	694	18,452	19,146
At 31 December 2019 (restated)	895	21,552	22,448

* Additions includes both new underlying assets and remeasurement of the right of use asset for changes in the lease terms.

7. Fixed asset investments

Accounting policy

Investments in equity shares which are not publicly traded and where fair value cannot be measured reliably are measured at deemed cost less impairment. Dividends on equity securities are recognised in income when receivable.

	Investment in subsidiary undertakings £'000
At 1 January 2019	58,123
Impairment	(18,540)
At 1 January 2020	39,583
Capitalisation of loans with subsidiaries	110,000
Disposal of subsidiary	(10,250)
Retention of holding in disposed subsidiary	65
At 31 December 2020	139,398

Details of the subsidiary undertakings of the Company are shown in note 17 to the consolidated financial statements.

The impairment during 2019 represents a write-down of the Company's investment in its Domiciliary Care business to its fair value less costs of disposal following the decision to dispose of this business.

Financial statements continued

Notes to the financial statements – Company continued

For the year ended 31 December 2020

8. Debtors

	2020 £'000	2019 £'000
Amounts owed by Group undertakings	31,724	188,060
Other receivables	9,048	1,036
	40,772	189,096

Amounts owed by Group undertakings are repayable on demand. Expected credit losses are assessed on an individual basis taking into account all the relevant factors in respect of the counterparty.

9. Creditors: amounts falling due within one year

	2020 £'000	2019 (restated) £'000
Trade creditors	15,478	15,607
Amounts owed to Group undertakings	4,123	–
Interest rate swaps	459	119
Accruals	751	191
Corporation tax	579	395
Lease obligations	8,768	11,258
Other payables	36	20
	30,194	27,590

10. Creditors: amounts falling due in more than one year

	2020 £'000	2019 (restated) £'000
Bank borrowings	39,344	124,047
Lease obligations	10,113	11,490
Interest rate swaps	462	38
	49,919	135,575

The Company considers core bank borrowings of £40.0m as due in one to two years. Whilst the amounts borrowed could be repaid each quarter, the Company's intention is to align core bank borrowings with its interest rate swaps.

11. Financial instruments

Accounting policy

Financial assets and liabilities are recognised in the Consolidated Balance Sheet when the Company becomes party to the contractual provisions of the instrument. The principal financial assets and liabilities of the Company are as follows:

Financial assets

Basic financial assets, including trade and other receivables, amounts due to Group companies and cash and cash equivalents, are initially recognised at transaction price, unless the arrangement constitutes a financing transaction, where the transaction is measured at the present value of the future receipts discounted at a market rate of interest.

Such assets are subsequently carried at amortised cost using the effective interest rate method.

At the end of each reporting period financial assets measured at amortised cost are assessed for objective evidence of impairment. If an asset is impaired the impairment loss is the difference between the carrying amount and the present value of the estimated cash flows discounted at the asset's original effective interest rate. The impairment loss is recognised in profit or loss.

Financial assets are derecognised when (a) the contractual rights to the cash flows from the asset expire or are settled; (b) substantially all the risks and rewards of the ownership of the asset are transferred to another party; or (c) despite having retained some significant risks and rewards of ownership, control of the asset has been transferred to another party which has the practical ability to unilaterally sell the asset to an unrelated third party without imposing additional restrictions.

Cash and cash equivalents include cash at bank and in hand and bank deposits available with no notice or less than three months' notice from inception that are subject to an insignificant risk of changes in value. Bank overdrafts are presented as current liabilities to the extent that there is no right of offset with cash balances.

Financial liabilities

Basic financial liabilities, including trade and other payables, and amounts payable to Group companies that are classified as debt, are initially recognised at transaction price, unless the arrangement constitutes a financing transaction, where the debt instrument is measured at the present value of the future receipts discounted at a market rate of interest.

Bank borrowings are non-basic financial liabilities and are initially recognised at fair value, being the present value of future payments discounted at a market rate of interest. Bank borrowings are remeasured at fair value.

Derivatives, including interest rate swaps, are not basic financial instruments.

Derivatives are initially recognised at fair value on the date a derivative contract is entered into and are subsequently remeasured at their fair value. Changes in the fair value of derivatives are recognised in profit or loss in finance costs or finance income as appropriate, unless they are included in a hedging arrangement.

Financial liabilities are derecognised when the liability is extinguished, that is when the contractual obligation is discharged or cancelled or expires.

Offsetting

Financial assets and liabilities are offset and the net amounts presented in the financial statements when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis or to realise the asset and settle the liability simultaneously.

Hedge accounting for interest rate swaps

The Company applies hedge accounting for transactions entered into to manage the cash flow exposures of borrowings. Interest rate swaps are held to manage the interest rate exposures and are designated as cash flow hedges of floating rate borrowings.

Changes in the fair values of derivatives designated as cash flow hedges, and which are effective, are recognised directly in equity. Any ineffectiveness in the hedging relationship (being the excess of the cumulative change in fair value of the hedging instrument since inception of the hedge over the cumulative change in the fair value of the hedged item since inception of the hedge) is recognised in the Consolidated Statement of Profit or Loss.

The gain or loss recognised in other comprehensive income is reclassified to the Consolidated Statement of Profit or Loss when the hedge relationship ends. Hedge accounting is discontinued when the hedging instrument expires or no longer meets the hedging criteria, the forecast transaction is no longer highly probable, the hedged debt instrument is derecognised or the hedging instrument is terminated.

Financial statements continued

Notes to the financial statements – Company continued

For the year ended 31 December 2020

11. Financial instruments continued

The Company has the following financial instruments:

	2020 £'000	2019 £'000
Financial assets that are debt instruments measured at amortised cost:		
▶ Amounts owed by Group undertakings	44,224	188,060
▶ Other receivables	9,048	1,036
Financial liabilities that are measured at fair value through other comprehensive income:		
▶ Interest rate swaps	(921)	(158)
Financial liabilities that are measured at amortised cost:		
▶ Bank borrowings	(39,344)	(124,047)
▶ Lease obligations	(18,881)	(22,748)
▶ Other payables	(36)	(20)
	(5,910)	42,123

There have been no changes during the period or cumulatively in the fair value of bank borrowings attributable to changes in the credit risk of the instrument. The change attributable to changes in own credit risk is not material due to the short life of individual draw-downs within bank borrowings. The difference between the carrying amount and the amount expected to be paid at maturity is not material due to the short life of individual draw-downs within bank borrowings.

During the year the Company recognised an expected credit loss of £7.6m (2019: £4.3m) in respect of its loan to Mears New Homes Limited. During the period year the Company also recognised an expected credit loss of £23.0m in respect of its loan to Mears Care Limited.

The Company pays a margin over and above LIBOR on bank borrowings. The margin is based on the ratio of Group consolidated net borrowings to Group consolidated adjusted EBITDA and could have varied between 1.35% and 2.2% during the year.

The Company has entered into interest rate swaps to receive interest at LIBOR and pay interest at fixed rates. At 31 December 2020, these consist of two £15.0m swap contracts expiring in August 2021 with a fixed interest rate of 0.96%, one £15.0m swap contract expiring in June 2023 with a fixed interest rate of 0.52% and three £15.0m swap contracts commencing in January 2021 and expiring in January 2024 with fixed interest rates of 0.43%. The swaps have quarterly maturity matching the underlying debt.

These instruments are used to mitigate the Company's exposure to any interest rate movements. The fair value of the interest rate swaps is a liability of £0.9m (2019: £0.2m).

During 2020, a hedging loss of £1.1m (2019: £0.1m) was recognised in other comprehensive income for changes in the fair value of the interest rate swap and £0.4m (2019: £nil) was reclassified from the hedge reserve to profit and loss.

The Company seeks to manage liquidity risk by ensuring sufficient liquidity is available to meet foreseeable needs and to invest cash assets safely and profitably.

Management monitors rolling forecasts of the Group and Company's liquidity reserve (comprising undrawn borrowing facilities and cash and cash equivalents) on the basis of expected cash flows. The quantum of committed borrowing facilities of the Group and Company is regularly reviewed and is designed to exceed forecast peak gross debt levels. For short-term working capital purposes, the Group and Company utilise bank overdrafts as required. These facilities are regularly reviewed and are renegotiated ahead of their expiry date.

12. Share capital and reserves

	2020 £'000	2019 £'000
Allotted, called up and fully paid		
At 1 January 110,490,459 (2019: 110,487,586) ordinary shares of 1p each	1,105	1,105
Issue of 391,438 (2019: 2,873) shares on exercise of share options	4	–
At 31 December 110,881,897 (2019: 110,490,459) ordinary shares of 1p each	1,109	1,105

During the year 391,438 (2019: 2,873) ordinary 1p shares were issued in respect of share options exercised.

12. Share capital and reserves continued

Classes of reserves

Share capital represents the nominal value of shares that have been issued.

Share premium represents the difference between the nominal value of shares issued and the total consideration received.

Share-based payment reserve represents employee remuneration which is credited to the share-based payment reserve until the related share options are exercised. Upon exercise the share-based payment reserve is transferred to retained earnings.

The cash flow hedging reserve comprises all gains and losses arising from the valuation of interest swap contracts which are effective hedges and mature after the year end. These are valued on a mark-to-market basis, accounted for through the Consolidated Statement of Comprehensive Income and recycled through the Consolidated Statement of Profit or Loss when the hedged item affects the Consolidated Statement of Profit or Loss.

13. Capital commitments

The Company had no capital commitments at 31 December 2020 or at 31 December 2019.

14. Contingent liabilities

The Company has guaranteed that it will complete certain Group contracts that its subsidiaries have commenced. At 31 December 2020 these guarantees amounted to £14.7m (2019: £19.3m).

The Company had no other contingent liabilities at 31 December 2020 or at 31 December 2019.

15. Pensions

Accounting policy

Defined contribution pension scheme

The pension costs charged against profits are the contributions payable to individual policies in respect of the accounting period.

Defined benefit pensions

The Company contributes to defined benefit schemes which require contributions to be made to separately administered funds.

A defined benefit plan is a pension plan that defines an amount of pension benefit that an employee will receive on retirement, usually dependent on one or more factors such as age, years of service and salary. The legal obligations for any benefits from this kind of pension plan remain with the Group, even if plan assets for funding the defined benefit plan have been set aside.

Scheme liabilities are measured using the projected unit funding method, applying the principal actuarial assumptions at the balance sheet date. Assets are measured at market value. The asset that is recognised is restricted to the amount by which the service cost is expected, over the lifetime of the scheme, to exceed funding contributions payable in respect of accruing benefits.

Actuarial gains and losses are taken to the Consolidated Statement of Comprehensive Income as incurred. For this purpose, actuarial gains and losses comprise both the effects of changes in actuarial assumptions and experience adjustments arising because of differences between the previous actuarial assumptions and what has actually occurred.

Other movements in the net surplus or deficit are recognised in the profit and loss account, including the current service cost, any past service cost and the effect of curtailments or settlements. The interest costs less the expected return on assets are also charged to the Consolidated Statement of Profit or Loss. The amount charged to the Consolidated Statement of Profit or Loss in respect of these plans is included within operating costs.

The Company's contributions to the schemes are paid in accordance with the rules of the schemes and the recommendations of the actuary.

Defined contribution schemes

The Company contributes to the personal pension schemes of certain employees.

Financial statements continued

Notes to the financial statements – Company continued

For the year ended 31 December 2020

15. Pensions continued**Defined benefit scheme**

The Company operates a defined benefit pension scheme for the benefit of certain employees of its subsidiary companies. The assets of the schemes are administered by trustees in a fund independent from the assets of the Company.

Costs and liabilities of the scheme are based on actuarial valuations. The actuarial valuations were reviewed and updated to 31 December 2020 by a qualified independent actuary using the projected unit funding method.

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

	2020	2019
Rate of increase of salaries – first year	2.85%	2.90%
Rate of increase of salaries – second year	2.85%	2.90%
Rate of increase of salaries – long term	2.85%	2.90%
Rate of increase for pensions in payment – based on RPI with a cap of 5%	2.85%	2.85%
Rate of increase for pensions in payment – based on RPI with a cap of 3%	2.35%	2.35%
Discount rate	1.35%	2.10%
Retail prices inflation	2.85%	2.90%
Consumer prices inflation	2.45%	1.90%
Life expectancy for a 65-year-old male	21.1 years	20.7 years
Life expectancy for a 65-year-old female	24.0 years	23.8 years

The amounts recognised in the Parent Company Balance Sheet and major categories of plan assets as a percentage of total plan assets are:

	2020 £'000	2019 £'000
Quoted assets		
Bonds	3,865	5,190
Other assets		
Multi-asset funds	17,813	15,107
Derivatives	733	154
Cash and other	275	334
Investment liabilities		
Derivatives	(194)	(314)
Group's estimated asset share	23,050	20,972
Present value of funded scheme liabilities	(25,866)	(22,350)
Funded status	(2,816)	(1,378)
Related deferred tax asset	535	262
Pension liability	(2,281)	(1,116)

The amounts recognised in the profit and loss account are as follows:

	2020 £'000	2019 £'000
Current service cost	13	26
Administration costs	77	–
Total operating charge	90	26
Net interest	28	25
Total charged to the result for the year	118	51

15. Pensions continued

	2020 £'000	2019 £'000
Present value of obligations at 1 January	22,350	19,987
Current service cost	13	26
Interest on obligations	463	582
Plan participants' contributions	2	5
Benefits paid	(624)	(518)
Actuarial loss/(gain) arising from changes in demographic assumptions	216	(99)
Actuarial loss arising from changes in financial assumptions	3,613	2,437
Actuarial gain arising from liability experience	(167)	(70)
Present value of obligations at 31 December	25,866	22,350

Changes in the fair value of the plan assets are as follows:

	2020 £'000	2019 £'000
Fair value of plan assets at 1 January	20,972	18,943
Expected return on plan assets	435	557
Employer's contributions	252	399
Plan participants' contributions	2	5
Benefits paid	(624)	(518)
Administration costs	(77)	–
Return on plan assets above that recorded in net interest	2,090	1,586
Fair value of plan assets at 31 December	23,050	20,972

The movements in the net pension liability and the amount recognised in the Parent Company Balance Sheet are as follows:

	2020 £'000	2019 £'000
Deficit in schemes at 1 January	(1,378)	(1,044)
Current service cost	(13)	(26)
Administration costs	(77)	–
Contributions	252	399
Other finance cost	(28)	(25)
Actuarial (loss)/gain arising from changes in demographic assumptions	(216)	99
Actuarial loss arising from changes in financial assumptions	(3,613)	(2,437)
Actuarial gain arising from liability experience	167	70
Return on plan assets above that recorded in net interest	2,090	1,586
Deficit in schemes at 31 December	(2,816)	(1,378)

The employer's contributions expected to be paid during the financial year ending 31 December 2021 amount to £0.05m.

Financial statements continued

Notes to the financial statements – Company continued

For the year ended 31 December 2020

16. Related party transactions

Identity of related parties

The Group has a related party relationship with its pension schemes, its subsidiaries and its Directors.

Pension schemes

Details of contributions to pension schemes are set out in note 15 to the financial statements.

Subsidiaries

The Group has a central treasury arrangement in which all subsidiaries participate. Management does not consider it meaningful to set out details of transfers made in respect of this treasury arrangement between companies, nor does it consider it meaningful to set out details of interest or dividend payments made within the Group.

Transactions with key management personnel

The Group has identified key management personnel as the Directors of Mears Group PLC. Details of transactions are disclosed in note 32 to the consolidated financial statements.

17. Restatement of prior year

As detailed in note 33 to the consolidated financial statements, the Group revisited the assumptions made at the time of the adoption of IFRS 16 and concluded that certain leases had been treated incorrectly.

The More Homes 'homelessness' solution detailed in note 33 has no impact on the parent company. However, while of no impact to the Group as a whole, it was concluded that certain vehicle leases that had been recognised in subsidiary entities of the Group should have been recognised in Mears Group PLC itself. The prior year figures have therefore been restated to correct these errors:

	Previously reported £'000	Reassessment of lease accounting £'000	Restated £'000
Parent Company Balance Sheet – restated lines			
Right of use assets	1,360	21,088	22,448
Deferred tax asset	333	(14)	319
Creditors: amounts falling due within one year	(16,799)	(10,791)	(27,590)
Creditors: amounts falling due after more than one year	(125,059)	(10,516)	(135,575)
Profit and loss account	23,107	(233)	22,874

Shareholder information

Five-year record (unaudited)

Consolidated Statement of Profit or Loss (continuing activities)

	2020 (continuing) £'000	2019 (continuing) £'000	2018 (continuing) £'000	2017 (all activities) £'000	2016 (all activities) £'000
Revenue by business segment					
Housing	805,817	881,457	771,861	766,121	787,530
Care	—	—	—	134,063	152,570
Continuing activities	805,817	881,457	771,861	900,184	940,100
Gross profit	156,287	206,109	184,928	223,702	244,894
Operating profit before acquisition intangible amortisation and exceptional costs	5,528	40,229	39,093	39,151	41,850
Exceptional items	(2,279)	(2,018)	(5,657)	—	—
Operating (loss)/profit	(6,276)	28,089	29,698	28,513	31,160
(Loss)/profit for the year before tax	(15,218)	20,253	27,377	26,484	29,372
Profit before taxation before acquisition intangible amortisation and exceptional costs	(3,414)	32,393	36,772	37,122	40,062
Earnings per share					
Basic	(10.66)p	15.72p	21.91p	20.28p	23.54p
Diluted	(10.66)p	15.64p	21.78p	20.10p	23.41p
Normalised	(2.29)p	23.74p	27.70p	28.05p	30.36p
Dividends per share	0.0p	3.65p	12.40p	12.00p	11.70p

Consolidated Balance Sheet

	2020 (continuing) £'000	2019 (continuing) £'000	2018 (continuing) £'000	2017 (all activities) £'000	2016 (all activities) £'000
Non-current assets	408,369	409,151	304,549	264,567	262,263
Current assets	267,720	284,230	244,272	211,439	222,158
Current liabilities	(255,318)	(326,329)	(222,909)	(198,678)	(194,567)
Non-current liabilities	(264,720)	(248,715)	(115,632)	(67,738)	(91,180)
Total equity	156,051	118,337	210,280	209,590	198,674
Cash and cash equivalents, end of year	56,867	(50,986)	(65,904)	(25,789)	(12,374)

Shareholder information continued

Shareholder and corporate information

Financial calendar

Annual General Meeting
29 June 2021

Registered office

1390 Montpellier Court
Gloucester Business Park
Brockworth
Gloucester GL3 4AH

Tel: 01452 634600
www.mearsgroup.co.uk

Company registration number

03232863

Company Secretary

Ben Westran
1390 Montpellier Court
Gloucester Business Park
Brockworth
Gloucester GL3 4AH

Tel: 01452 634600

Bankers

Barclays Bank PLC
Wales and South West
Corporate Banking
4th Floor, Bridgewater House
Counterslip
Finzels Reach
Bristol BS1 6BX

Tel: 0800 285 1152

HSBC Bank PLC

West & Wales
Corporate Banking Centre
3 Rivergate
Temple Quay
Bristol BS1 6ER

Tel: 0845 583 9796

Bank of Ireland

Bow Bells House
1 Bread Street
London EC4M 9BE

Tel: 0845 583 9796

Solicitors

Travers Smith
10 Snow Hill
London EC1A 2AL

Tel: 020 7295 3000

Auditor

Ernst & Young LLP
Registered Auditor
Chartered Accountants
The Paragon
Counterslip
Bristol BS1 6BX

Tel: 0117 981 2050

Financial adviser

Investec Bank PLC
2 Gresham Street
London EC2V 7QP

Tel: 020 7597 2000

Registrar

Neville Registrars Ltd
Neville House
Steelpark Road
Halesowen
West Midlands B62 8HD

Tel: 0121 585 1131

Corporate brokers

Peel Hunt
Moor House
20 London Wall
London EC2Y 5ET

Tel: 020 7418 8900

Internet

The Group operates a website which can be found at www.mearsgroup.co.uk. This site is regularly updated to provide information about the Group. In particular all of the Group's press releases and announcements can be found on the site.

Registrar

Any enquiries concerning your shareholding should be addressed to the Company's registrar. The registrar should be notified promptly of any change in a shareholder's address or other details.

Investor relations

Requests for further copies of the Annual Report and Accounts, or other investor relations enquiries, should be addressed to the registered office.

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Mears Group PLC

1390 Montpellier Court
Gloucester Business Park
Brockworth
Gloucester GL3 4AH

Tel: 01452 634 600

www.mearsgroup.co.uk