



Diploma PLC

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# Annual Report & Accounts 2011

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Diploma PLC  
**Our business**

## **Our Sectors**

Diploma PLC is an international group of businesses supplying specialised technical products and services. We operate globally in three distinct sectors:

**Life Sciences** Suppliers of consumables, instrumentation and related services to the healthcare and environmental industries

**Seals** Suppliers of hydraulic seals, gaskets, cylinders, components and kits for heavy mobile machinery and industrial equipment

**Controls** Suppliers of specialised wiring, connectors, fasteners and control devices for technically demanding applications

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Sections 1–3 make up the Directors' Report in accordance with the Companies Act 2006

## Financial Highlights

# Continued strong performance

### Year ended 30 September 2011

	2011 £m	2010 £m	
Revenue	<b>230.6</b>	183.5	+26%
Adjusted operating profit <sup>1</sup>	<b>45.2</b>	32.1	+41%
Adjusted operating margin <sup>1</sup>	<b>19.6%</b>	17.5%	
Adjusted profit before tax <sup>1,2</sup>	<b>44.9</b>	32.2	+39%
Profit before tax	<b>39.2</b>	26.7	+47%
Profit for the year <sup>3</sup>	<b>27.6</b>	23.0	+20%
Free cash flow	<b>25.0</b>	29.8	-16%
	<b>Pence</b>	Pence	
Adjusted earnings per share <sup>1,2</sup>	<b>27.9</b>	18.9	+48%
Basic earnings per share	<b>24.0</b>	14.6	+64%
Total dividends per share	<b>12.0</b>	9.0	+33%
Free cash flow per share	<b>22.1</b>	26.3	-16%

1 Before acquisition related charges

2 Before fair value remeasurements

3 Profit for the year is stated after tax and includes the profit on sale of the discontinued businesses in the prior year. All other reported results relate to continuing businesses.

#### Note

Diploma PLC uses alternative performance measures as key financial indicators to assess the underlying performance of the Group. These include adjusted operating profit, adjusted profit before tax, adjusted earnings per share and free cash flow. The narrative in the Annual Review is based on these alternative measures and an explanation is set out in note 2 to the consolidated financial statements in the Annual Report & Accounts.

## Chairman's Statement

**John Rennocks**  
Chairman

As I enter my tenth year as a Director of the Company it is particularly encouraging to report another year of excellent progress at Diploma with key performance indicators all hitting record levels

These results continue to demonstrate the strength and resilience of the Group's business model which has enabled it to report consistent profitable growth over the past ten years. In July 2002 when I joined the Company the Group had recently emerged from a major restructuring programme, having divested a number of traditional core businesses and returned a large proportion of the cash proceeds (ca. £70m) to shareholders. The Group had just reported pre-tax profits of £10.0m on revenues of £66.3m in respect of its continuing businesses. At the same time the Group's market capitalisation was below £100m and total dividends were 2.6p per share.

Over the ten years since then, the Group has generated strong double digit compound growth in revenues through a combination of steady organic growth and value enhancing acquisitions. Profits and dividends over this period have increased by a factor of more than four times. The total shareholder return ("TSR") has also grown strongly relative to the FTSE mid-250 index (excluding investment trusts) ("FTSE 250") which we have always seen as a benchmark for our performance. This strong relative performance was recognised in October of this year when the Company achieved the important milestone of promotion to the FTSE 250.

Towards the end of this year, the Board approved proposals to further expand the activities in a number of key businesses by moving their existing activities to new enlarged facilities. These facilities will enable the momentum of growth to be sustained, within the constraints of an uncertain economic outlook. I remain confident that with its broader base of businesses, the resilience of its business model and its depth of resources, the Group is well placed to continue to make further progress in the next ten year period.

### 2011 Results

Group revenue increased by 26% to £230.6m (2010 £183.5m) with the businesses continuing to benefit from strong customer demand and with acquisitions completed over the past eighteen months contributing £17.2m to this year's Group result. The on-going focus on adding value to our delivery of product and services, together with the benefit of cost reductions carried out in 2009 has led to a further increase in adjusted operating margins to 19.6% (2010 17.5%). As a result there was a substantial increase in adjusted operating profit up by 41% to £45.2m (2010 £32.1m). Underlying Group revenues and adjusted operating profit increased by 17% and 31% respectively after adjusting for the contribution from acquisitions and from the impact of currency movements on the translation of overseas results.

Adjusted profit before tax increased by 39% to £44.9m (2010 £32.2m) and adjusted earnings per share which were boosted by the purchase of minority interests, increased by 48% to 27.9p (2010 18.9p).

Free cash flow of £25.0m was generated as the businesses took advantage of better supply of product to rebuild working capital from the exceptionally low level last year. Last year's free cash flow of £29.8m included £6.4m from the disposal of the Anachem businesses.

### Strong Balance Sheet

Given the current uncertainty in the global financial markets the Board continues to focus on ensuring that it has sufficient financial resources to take advantage of acquisition opportunities. An important part of this process was the securing of new bank facilities, earlier in the year, which can provide up to £40m of borrowings. These facilities, together with net cash of £12.2m held at 30 September 2011, ensure that the Group continues to maintain a strong balance sheet.

### Acquisitions

During the year the Group spent £28.2m on acquisitions principally in the Canadian Healthcare sector with the acquisition of Carsen Medical Inc ("CMI") in December 2010 and the purchase of the outstanding 25% minority shares in AMT. This latter acquisition of minorities facilitated the merger of AMT's endoscopy business with CMI with effect from 30 September 2011.

## Five year performance

EPS growth

**+19% p.a.**

Adjusted EPS in pence

TSR growth

**+21% p.a.**

TSR index, 2006 = 100

Dividend growth

**+21% p.a.**

Dividends in pence per share

It remains an important part of the Board's strategy to accelerate growth through carefully selected value enhancing acquisitions. A cornerstone of our acquisition programme has always been to target businesses where we see the opportunity for above average growth soon after the activities have been integrated into the Group.

We believe that the current stage of the business cycle provides a reasonably good environment for making such acquisitions. Good recent performance by target companies allows for sensible valuation discussions to be held with sellers, while the general economic uncertainty may encourage them to feel that the time may be right to sell their companies.

### Dividends

As a result of the excellent progress made by the Company during the year, the Board is recommending an increase in the final dividend of 37% to 8.5p per share (2010: 6.2p) which, subject to shareholder approval at the Annual General Meeting, will be paid on 25 January 2012, to shareholders on the register at 9 December 2011.

The total dividend per share for the year will be 12.0p which represents a 33% increase on 2010 and represents the twelfth successive year that the Company has reported an increase in dividends paid to shareholders.

### Governance

The importance of maintaining high standards of governance within the Company has been re-emphasised this year with the implementation of recommendations set out in the updated UK Corporate Governance Code. The development of strong governance is a continuous process and I will be working closely with my Board colleagues this year to ensure that the Company's governance standards and procedures are appropriate to meet the requirements of a FTSE 350 constituent member. These requirements are set out further in the Chairman's foreword to the statement on Corporate Governance set out on page 26 of the Annual Report & Accounts.

### Employees

Our employees are our most important asset and we continue to invest time and resources into developing strong management groups and committed staff teams. We encourage an entrepreneurial culture within our businesses so that our employees feel responsible for their own businesses while being able to draw on the resources of a larger group. I wish to thank all of our employees for their exceptional efforts in helping to deliver this year's very strong financial performance.

### Outlook

The financial performance of the Group this year has benefited from strong trading in its principal markets. While trading remains robust, underlying organic growth is expected to trend towards our target "GDP plus" levels when measured against increasingly demanding comparatives.

With a resilient business model, a good geographic spread of activities and supported by a strong balance sheet, the Group is well placed to withstand further shocks to the global economy. With this background, a combination of consistent organic growth, together with a favourable environment for acquisitions, provide the Board with confidence that further progress will be made in the new financial year.

### John Rennocks

Chairman  
21 November 2011

## Chief Executive's Review

**Bruce Thompson**  
Chief Executive Officer

### Principal corporate objectives

**Achieve double digit growth in adjusted EPS over the business cycle**

Adjusted earnings per share ("EPS") measured over the business cycle, provides an absolute benchmark of the Company's performance. Over the last five years, adjusted EPS has grown at a compound growth rate of 19% p a through a combination of steady organic growth and carefully targeted acquisitions

**Generate TSR growth in the upper quartile of the FTSE 250**

Total shareholder return ("TSR") is the growth in value of a share plus the value of dividends re-invested in the Company's shares on the day on which they are paid

This is measured against the TSR growth of the FTSE mid-250 index (excluding investment trusts) ("FTSE 250"). The last five years have seen a compound TSR growth for Diploma of 21% p a, which represents upper quartile performance as compared with the FTSE 250, where median TSR growth has been 3% p a

**Deliver progressive dividend growth with two times dividend cover**

Diploma follows a progressive dividend policy with a target cover of two times on an adjusted EPS basis. Over the last five years, dividends have steadily grown at the rate of 21% p a and this continues the trend of increasing dividends in each of the last 12 years

### Our business model

**Essential PRODUCTS**

We focus on businesses which supply essential products and services

- Funded by customers' operating rather than capital budgets
- Providing recurring income and stable revenue growth

**Essential SOLUTIONS**

We provide solutions to meet customer needs, combining

- Highly responsive customer service
- Deep technical knowledge and support
- Value adding activities

**Essential VALUES**

We encourage an entrepreneurial culture in our businesses

- Decentralised management model
- Ensures businesses are agile and responsive to change

“Our business model has delivered record performance in the year”

## Next level objectives

### Generate stable “GDP plus” organic revenue growth over the business cycle

The businesses target organic revenue growth, over the economic cycle, at a rate of 5–6% p a (“GDP plus” growth), with higher growth rates achieved at the Group level through carefully selected value enhancing acquisitions

### Maintain stable attractive margins

Operating margin is an important measure of the success of the businesses in achieving superior margins by offering strongly differentiated products and customer focused solutions, as well as by running efficient operations

### Accelerate growth through carefully selected value enhancing acquisitions

To complement the Group’s organic growth strategy the Group has an on-going acquisition programme, designed to accelerate growth and to facilitate entry into related strategic markets

### Generate consistently strong cash flow to fund growth strategy and dividends

Free cash flow is defined as the cash flow generated after tax, but before acquisitions and dividends. This measures the success of the Group and its businesses in turning profit into cash through the careful management of working capital and investments in fixed assets

### Create value by consistently exceeding 20% ROTCE

Return on trading capital employed (“ROTCE”) is defined as adjusted operating profit as a percentage of trading capital employed (“TCE”). TCE excludes net cash and non-operating assets and liabilities, but includes all goodwill and acquired intangible assets

## Key performance indicators

Total revenue growth % p a

**16% p.a.**  
compound

Underlying organic revenue growth % p a

**+6% p.a.**  
average

Operating margins % of revenue

**17-18%** average

Acquisition spend and ROI

**>20% ROI**

Free cashflow £m

**£22m p.a.**  
average

Working capital as % of revenue

**17%** average

ROTCE %

**23%** average

## Chief Executive's Review continued

### Business Model

The Group comprises a number of high quality, specialised businesses supplying technical products and services to customers in the Life Sciences, Seals and Controls industries. The Group's business model is designed to achieve the twin objectives of stable organic revenue growth and sustainable attractive margins. Growth is then accelerated through carefully selected, value-enhancing acquisitions which fit the Group's business model and offer entry into new strategic markets.

We aim to achieve these objectives by focusing on businesses which supply *essential products* and services which are funded by the customers' operating rather than their capital budgets, providing recurring income and stable revenue growth. Our businesses then design their individual business models to closely meet the requirements of their customers, offering a blend of high quality customer service, deep technical support and value adding activities. By supplying *essential solutions*, not just products, we build strong long-term relationships with our customers and suppliers, which support attractive and sustainable margins. Finally we encourage an entrepreneurial culture in our businesses through our decentralised management structure. We want our managers to feel that they have the freedom to run their own businesses, while being able to draw on the support and resources of a larger group. These *essential values* ensure that decisions are made close to the customer and that the businesses are agile and responsive to changes in the market and the competitive environment.

The Group's business model has been closely tested over the last three years. The businesses proved their resilience through the 2009 global downturn with Group revenues growing by 2% (albeit a decline on an underlying basis) and operating margins held at a creditable 16% of revenue. As markets have slowly recovered following the recession, the Group has moved forward strongly, posting seven quarters of growth in revenues and profits since the recovery started in early 2010 and outperforming economic and market benchmarks. This level of relative performance confirms that the operating businesses have succeeded in further penetrating their markets by maintaining high customer service levels and adding product lines through the downturn.

### Operating Performance

In 2011 revenues increased by 26% to £230.6m (2010 £183.5m) with underlying growth of 17% after adjusting for currency effects and acquisitions. As revenues have increased, the businesses have continued to manage costs carefully in view of continuing uncertainty over the sustainability of the recovery. With the resulting benefits of operational leverage, adjusted operating margins have increased to 19.6% of revenue (2010 17.5%).

The operating margins achieved this year are well above the three year average of ca. 18% of revenue. It is likely that over time operating margins will gradually trend back towards this average, as resources will need to be increased to support higher levels of revenue. In addition, there will be increased investment in fixed assets to ensure that the IT environment and the facilities in the businesses provide a robust foundation for further growth. This investment will result in higher operating costs and depreciation. In 2012, for example, three of the businesses will be moving into new facilities at a total cost of ca. £1m – the IS-Group in Swindon, RT Dygert in Minneapolis and Vantage Endoscopy in Toronto.

Free cash flow in 2011 has again been strong at £25.0m against a very strong prior year comparative (2010 £29.8m), which had been boosted by the proceeds from the sale of the Anachem businesses, as well as by a reduction in working capital across the Group. During 2010, working capital had fallen to the level of 15.4% of revenue as suppliers struggled to keep pace with increasing demand for their products. By the end of the 2011 financial year, working capital had moved back to a more normal level of 16.1% of revenue, with an additional investment of £7.4m.

During the year, £28.2m was invested in acquisitions, principally in the Canadian Healthcare business. Return on trading capital employed ("ROTCE") has increased to 25.4% (2010 22.1%) principally driven by the improved operating margins.

### Sector Developments

The Group's strategic objective is to build more substantial, broader based businesses in each of its chosen sectors through a combination of organic growth and acquisition. Good progress was made in the year in executing this strategy in each of the three sectors and the key developments this year are summarised below.

## Life Sciences

	2011 £m	2010 £m	
Revenue	74.4	55.4	+34%
Operating profit	17.1	11.9	+44%
Operating margin	23.0%	21.5%	

The Life Sciences businesses increased revenues in 2011 by 34% boosted by the contribution from the acquisition in December 2010 of CMI and also modest currency translation benefits. Underlying sector revenues increased by 12% after adjusting for the acquisition and currency effects. Operating margins increased by 150 basis points to 23.0% (2010 21.5%), mainly driven by improved profitability in the Environmental business.

The Group's *Healthcare* businesses in Canada and now Australia ("Diploma Healthcare Group" or "DHG"), account for almost 80% of the Life Sciences sector revenues. They operate in healthcare markets which are largely public sector funded and where the demand from growing, aging and well-educated patient populations drives a steady growth in funding (on average 6–7% p.a. growth over 15 years in Canada). Within these markets, the DHG businesses supply specialised products which are used in the pathology laboratories, operating rooms ("OR") and endoscopy suites of the hospitals as well as private clinics. During the recession there were initiatives to control costs including limits imposed on the number and cost of specific medical procedures and diagnostic tests and extended tender processes for capital equipment. However, overall Healthcare expenditure has continued to grow steadily in real terms and there has been some evidence of an easing of capital approvals.

The DHG business model is built on the supply, on an exclusive basis, of high quality manufacturer branded products secured by long-term distribution agreements. Strong customer relationships are forged through high levels of customer service, with highly qualified and experienced technical sales and product application staff working closely with the surgeons, OR nurses and laboratory technologists. A large proportion (over 60%) of DHG's revenues are secured under multi-year customer contracts.

During the year, DHG expanded its business in Canada through the acquisition of CMI, a supplier of medical devices, consumables and service to GI Endoscopy suites in hospitals and clinics across Canada. CMI shares a common customer base with the endoscopy business within our existing AMT company and the products are very complementary with few overlaps. With effect from the start of the new financial year, the businesses were combined under a single management team, with the new name of Vantage Endoscopy ("Vantage") and with plans to relocate to a new facility in the first half of the year. Vantage is now able to offer to its GI Endoscopy customers, the most complete range of products, including endoscopic imaging and reprocessing systems, therapeutic technologies and devices and other essential accessories and service support.

There are now three similar sized, growing DHG businesses in Canada: the Somagen clinical diagnostics business, AMT's core electrosurgery business and Vantage. Each of these businesses has good potential for further growth by continuing to penetrate core markets as well as by adding new product lines and suppliers. In Australia, BGS is a smaller version of AMT which was acquired towards the end of 2010. During the year investment was made to generate stronger growth by employing direct sales staff to replace sub-distributors in Victoria, Queensland, South Australia and New Zealand.

The remaining 20% of the sector revenues are generated by the a1-group of *Environmental* businesses in Europe which supply a range of products used in Environmental Testing and Health & Safety applications. The market demand is largely driven by regulation which ensures steady demand for the essential consumable products though customers do defer capital expenditure during economic downturns.

The a1-environmental group, following its restructuring in 2010, now has its principal operations in Germany and Switzerland with other Northern European markets served through sales and service staff. The benefits of the restructuring have been seen this year in the improvement in operating margins. The CBISS business in the UK has seen good growth in its sales of emissions monitoring systems, both in replacement systems for traditional power stations and new systems for alternative power plants (e.g. waste, biofuels, syngas). Demand for gas detection products has also been strong.

## Chief Executive's Review continued

### Seals

	2011 £m	2010 £m	
Revenue	80.0	60.1	+33%
Operating profit	14.9	8.9	+67%
Operating margin	18.6%	14.8%	

The Seals sector businesses increased revenues in 2011 by 33%, boosted by a full year contribution from All Seals acquired in September 2010, and despite modest currency translation losses. Underlying sector revenues increased by 26% after adjusting for the acquisition and currency effects. Operating margins increased by 380 basis points to 18.6% (2010: 14.8%), demonstrating the effects of operational leverage in this business, as increases in operating costs lagged the strong increase in revenue.

Currently just over 60% of Seals sector revenues are generated from the *Aftermarket* businesses of HFPG (Hercules, Bulldog and HKX) and FPE. Own brand sealing products, sourced from the same seal manufacturers who supply to the original equipment OEMs, are supplied to a broad range of mobile machinery applications in heavy construction, logging, mining, agriculture, material handling and refuse collection. The principal market drivers are therefore the growth in the general industrial economy and in particular heavy construction.

In the core *Aftermarket* business in North America, the key to success is the ability to provide a next day delivery service from inventory, for seals and seal kits used in a broad range of different manufacturers' machinery and different applications. Typically the first three years of equipment life is controlled by the OEMs through product warranty and lease terms. However, after the equipment is sold into the pre-used market or moves out of warranty, Hercules has a very compelling offering to customers by providing a responsive, next day delivery service for these time critical items.

The *Aftermarket* business was insulated from the worst of the 2009 recession, by its focus on customers' operational rather than capital budgets. As a result, it rebounded less strongly in 2010. In 2011, however, revenues increased by over 25% which suggests a significant increase in market share driven by the high level of customer service levels maintained during the downturn.

Outside North America, the main focus for development has been in Europe where good progress has been made in both direct sales in the UK and Benelux countries, as well as the appointment of sub-distributors to distribute Hercules seal kits in other mainland European countries. Initiatives are also being developed to increase penetration in other developing markets in Asia Pacific and South America.

The *Industrial OEM* business now represents close to 40% of sector revenues following the addition of All Seals to the RT Dygert and M Seals businesses. These companies supply seals, O-rings and custom moulded and machined parts to a range of specialised industrial OEM customers. Applications include spray painting guns, water filtration, wind power mills, hearing aids and medical devices. On a like-for-like basis, these businesses have increased revenues by 25% in 2011 and are experiencing demand well ahead of pre-recession levels.

The acquisition of All Seals has extended the Group's coverage in the US, with its strong position in California and the South Western States complementing RT Dygert's strength in the Mid-western States. M Seals has further penetrated its core Scandinavian markets from its operations in Denmark and Sweden and has established a wholly owned foreign enterprise ("WOFE") in Tianjin to trade directly with wind power customers in China.

### Controls

	2011 £m	2010 £m	
Revenue	76.2	68.0	+12%
Operating profit	13.2	11.3	+17%
Operating margin	17.3%	16.6%	

The Controls sector businesses increased revenues in 2011 by 12% in both UK sterling and constant currency terms. Operating margins increased by 70 basis points to 17.3% (2010: 16.6%).

The IS-Group (UK), Sommer and Filcon businesses supply high performance wiring, connectors, fasteners and control devices used in a range of technically demanding applications. The businesses offer high quality, manufacturer branded products sourced under the terms of long term exclusive distribution agreements. Strong customer relationships are based on ex-stock availability of product, responsiveness, technical advice on product applications and a range of value added services.

The largest end user sector is *Defence & Aerospace*. Here, the businesses do not typically supply to major platform OEMs and Tier 1 suppliers, who are mostly served direct by the manufacturers. Rather, the businesses supply into repair, refurbishment and upgrade programmes, as well as supplying to Tier 2 electronics customers, where ex-stock availability and responsiveness are important. The businesses therefore are less exposed to cutbacks and postponements in major defence programmes as a result of the Strategic Defence Reviews in the UK and Germany, though inevitably there will be some impact longer term at the sub-contractor and component supply level. In Commercial Aerospace, the businesses supply products principally for the initial installation and subsequent upgrades of aircraft interiors. After falling back in 2009, demand picked up in 2010 and as passenger numbers continue to recover, the sector appears to be returning to its long-term projected growth rate of ca. 5% p.a.

The businesses also supply to a range of specialised technical applications in the General Industrial market. The underlying market drivers are the growth of the industrial economies in Europe (in particular the UK and Germany), but demand tends to be more stable in the specialised sub-sectors in which we operate. In *Motorsport*, activity increased sharply with a successful F1 racing season and growth in the Indycar and Nascar series in the US, the DTM series in Germany and the World Rally Championship. *Medical Equipment* is another specialised market where demand has been stable and in *Energy*, there has been strong demand from the manufacturers of electrical generators and commercial batteries. The closure of the older nuclear plants in Germany will also require infrastructure investment in the power distribution network.

Hawco serves the *Commercial Refrigeration* market in the UK which continues to be buoyant, driven by investment by the major food retailers in new convenience stores and in energy saving technologies when refurbishing existing outlets.

#### Acquisition Activity

Over the last five years the Group has invested ca. £91m in acquisitions across the sectors and geographies – an average of ca. £18m p.a. The success in financial terms can be measured broadly by the profit return on the total investment which currently stands at over 20%. In 2011, a total of £28.2m was invested, mainly in the Canadian Healthcare business in the acquisition of CMI and the purchase of the 25% minority shareholdings in AMT.

While the time and effort invested in the acquisition programme is a sustained activity, the results can be more irregular. We find that most success tends to come at times when the business cycle is changing and creating uncertainty. For example, when markets are slowing down after an extended period of growth this may encourage owners to sell ahead of a market downturn. Alternatively, in the early stages of recovery, when confidence is building in future projections, owners who have delayed selling during a downturn may come back to the table. With the performance of many businesses having recovered since the 2009 recession, but uncertainty remaining as to the sustainability of the recovery, we believe that there will continue to be good opportunities for value adding acquisitions.

#### Summary and Outlook

The continued strong performance of the Group and the resilience shown over the last five years gives us confidence that we can maintain the "GDP plus" levels of underlying revenue growth over the business cycle. The Group is well diversified by geography and business area and the business model supports stable revenue growth and sustainable, attractive margins. Although general economic uncertainty over the strength of global markets continues to grow, we see good opportunities for future development, both organically and through acquisition.

**Bruce Thompson**  
Chief Executive Officer  
21 November 2011

## Sector Review

### Sector Performance

Life Sciences

**32%**

of revenues

#### Geography<sup>1</sup>

75% Canada  
20% Europe  
5% ROW

#### Customers

79% Clinical  
9% Utilities  
6% Industrial  
4% Chemical & Petrochemical  
2% Life Sciences Research

#### Products

68% Consumables  
23% Instrumentation  
9% Service

**223 employees worldwide**

<sup>1</sup> By destination

Seals

**35%**

of revenues

#### Geography<sup>1</sup>

70% North America  
15% Europe  
15% ROW

#### Customers

42% Heavy Construction  
33% Industrial OEMs  
16% General Industrial  
5% Dump & Refuse Trucks  
4% Logging & Agriculture

#### Products

62% Seals & Seal Kits  
15% O-rings  
10% Attachment Kits  
6% Gaskets  
7% Cylinders & Other

**432 employees worldwide**

Controls

**33%**

of revenues

#### Geography<sup>1</sup>

56% UK  
39% Continental Europe  
5% ROW

#### Customers

28% Defence & Aerospace  
28% General Industrial  
19% Commercial Refrigeration  
13% Motorsport  
7% Energy & Utilities  
5% Medical & Scientific

#### Products

39% Wire & Cable  
23% Connectors  
19% Equipment & Components  
11% Control Devices  
8% Fasteners

**245 employees worldwide**

### Geography<sup>1</sup>

Europe

**43%**

23% UK  
20% Continental Europe

<sup>1</sup> By destination

North America

**50%**

22% US  
28% Canada

Rest of World

**7%**

## Life Sciences

### Sector Definition and Scope

The Life Sciences sector businesses supply a range of consumables, instrumentation and related services to the healthcare and environmental industries

The Diploma Healthcare Group (“DHG”) in Canada comprises three principal operating businesses which supply to the 500–600 hospitals across the country as well as to private clinics. Somagen Diagnostics (“Somagen”) based in Edmonton, Alberta supplies a range of consumables and instruments used in the diagnostic testing of blood, tissue and other samples in hospital pathology laboratories. It is also a leading supplier to the growing assisted reproductive technology (“ART”) market. AMT Electrosurgery (“AMT”), based in Kitchener, Ontario, supplies specialised electrosurgery equipment and consumables for use in hospital operating rooms. Vantage Endoscopy (“Vantage”) supplies medical devices and related consumables and services to GI Endoscopy suites in hospitals and private clinics. Vantage combines the former AMT Endoscopy business with Carsen Medical Inc (“CMI”) acquired in December 2010.

DHG operates in Australia and New Zealand through Big Green Surgical (“BGS”), located near Sydney, Australia. BGS is a smaller, more narrowly focused version of the AMT business in Canada and shares a number of common suppliers.

The a1-group is a supplier to Environmental testing laboratories and to Health & Safety engineers. The a1-environmental business has locations in Dusseldorf in Germany and Basel in Switzerland and also has sales and service resources across Northern Europe. It supplies a range of specialised analysers for detecting and measuring specific elements in liquids, solids and gases and also supplies a range of containment enclosures for potent powder handling. The CBISS business, located in Tranmere in the UK, supplies equipment and services for the monitoring and control of environmental emissions, as well as a range of gas detection devices.

### Market Drivers

The DHG businesses in Canada supply into the *Healthcare* sector which is mostly public sector funded. The principal demand driver is therefore the level of healthcare spending by the Canadian Government.

C\$bn	2006	2007	2008	2009	2010
Public sector healthcare expenditure in Canada	105.8	113.2	121.1	128.6	135.1
Total healthcare expenditure in Canada	151.3	161.6	171.8	182.1	191.6
Total health expenditure as a % of GDP	na	na	10.7%	11.9%	11.7%

Source: Canadian Institute for Health Information

The Canadian Healthcare industry is a proven long-term growth environment for medical device distribution.

A growing, aging and well-educated population demands high standards of service delivery, helping to ensure on-going growing demand. Per capita healthcare spending in Canada is in the top 20% of OECD countries. The Canadian Health Act (“the Act”) ensures universal coverage for all insured persons for all medically necessary services provided by hospitals, physicians and other healthcare providers. The Provinces are responsible for the delivery of the healthcare services, but the Federal Government controls delivery through Federal-Provincial transfer payments, which represent the largest source of revenues for the Provinces.

The relative stability and consistency in funding by each of the Provinces, guaranteed through the Act, ensures that the market remains well funded through the economic cycle. Over many years, healthcare expenditure has grown steadily in the range 6–7% p.a. with annual variations mostly dependant on the periodic additional tranches of funding provided by individual Provinces. Healthcare continues to be the single largest budget category for Provincial governments and the improved delivery of healthcare services has a high profile in recent and current election campaigns.

Hospitals continue to represent the single largest component of public sector healthcare spending, accounting for over 40% of public healthcare spending. In 2010, hospital spending increased by 6.2% and the trend of hospital spending outpacing total healthcare spending is expected to continue, driven by the aging population.

The Healthcare market in Australia shares many of the same attractive characteristics as that of Canada. While privately funded healthcare is more prevalent, public sector healthcare funding is large and growing and supported by a stable, resource based economy. As with Canada, there is a large geography to be covered, low population density and purchasing processes that vary by State. These characteristics necessarily demand a significant investment by manufacturers in technical sales and service resource which makes the specialised distribution model very attractive as an efficient way to serve the market.

The a1-group supplies to customers in the *Environmental* industry across Europe. The market demand is largely driven by Environmental and Health & Safety regulations. Growth in recent years has been driven by the need to be compliant with a range of EU regulations including:

- legislation or regulatory obligations relating to the environment, pollutants or potentially hazardous contaminants,
- the growing importance to companies of protecting the workforce from contact with potentially hazardous materials, and
- greater use of new technologies in process control and integrated pollution control.

Since market demand is driven by regulation, this ensures reasonably steady demand for essential consumable products and service, though customers do defer capital expenditure during downturns in the economy.

## Sector Review continued

### Life Sciences continued

#### Sector Performance Life Sciences statistics

	2011	2010
Revenue	<b>£74.4m</b>	£55.4m
Adjusted Operating Profit	<b>£17.1m</b>	£11.9m
Operating Margin	<b>23.0%</b>	21.5%
Free Cash Flow	<b>£11.6m</b>	£10.1m
Trading Capital Employed	<b>£77.5m</b>	£49.7m
ROTCE	<b>23.1%</b>	24.0%

The Life Sciences businesses increased revenues in 2011 by 34% to £74.4m (2010: £55.4m). Sector revenues were boosted by the contribution from the CMI business in Canada, acquired in December 2010 and there were also modest benefits on translation from a stronger Canadian dollar relative to UK sterling. After adjusting for the acquisition and currency effects, underlying sector revenues increased by 12%.

Adjusted operating profits, which also benefited from the CMI acquisition and the stronger Canadian dollar, increased by 44% to £17.1m (2010: £11.9m). Adjusted operating margins increased to 23.0% (2010: 21.5%), with the increase driven mainly by improved profitability in the Environmental business following the prior year restructuring.

Capital expenditure in the sector was £0.8m, including £0.4m invested in field equipment for placement by the Canadian Healthcare businesses. The balance was invested in upgrading the IT environment for sales and back office functions. Free cash flow of £11.6m was generated in the sector (2010: £10.1m) reflecting the strong after tax cash flow from trading.

Revenues from the DHG businesses increased by 44% in UK sterling terms and by 41% in Canadian dollar terms. Revenues were boosted by the acquisition during the year of CMI and a full year contribution from BGS and by the recognition of revenues for an exceptional sale of face shields. After adjusting for these items, underlying revenues increased by 12% in Canadian dollars.

All of DHG's businesses in Canada experienced an easing of capital budgets, resulting in strong instrumentation sales from various public tenders by the hospitals. Somagen increased revenues by 7%, with good success in renewing longer term reagent rental contracts; the renewals were often linked to the sale or placement of innovative new instruments from our core suppliers. In addition, Somagen has achieved good growth in newer target markets including assisted reproductive technology ("ART") fecal occult blood testing to screen for colorectal cancer and non-clinical microbiology in the food and pharmaceutical industries.

AMT increased revenues in its electrosurgery and surgical products business by 19%, with underlying growth of 14%, before the exceptional face shield revenues. AMT experienced product shortages from a key supplier in the first half of the year but was able to manage the allocation of products to customers to ensure that no operating

procedures were affected. This inevitably impacted the resources that could be applied to other initiatives, but in spite of this AMT managed to achieve strong double digit growth in sales of its core electrosurgery and smoke evacuation products. BGS, a smaller version of AMT in Australia, increased revenues by more than 20% on a like-for-like basis. Since its acquisition, significant investment has been made in BGS to introduce direct sales resources to replace sub-distributors in Victoria, Queensland, South Australia and New Zealand.

In December 2010, the acquisition was completed of CMI, a leading distributor of medical devices, consumables and services supplied to GI Endoscopy suites in hospitals and private clinics across Canada. CMI shares a common customer base with AMT's Endoscopy business and the products are very complementary with few overlaps. The two businesses, operating individually during the year, performed strongly with aggregate revenues increasing by 21% on a like-for-like basis. With effect from the start of the new financial year, the businesses have been combined under a single management team, with the new name of Vantage Endoscopy and with plans to relocate to a new facility. Vantage Endoscopy now supplies a complete range of GI endoscopy products, including imaging and reprocessing systems, therapeutic technologies and devices and other related accessories and service support.

The a1-group increased revenues by 7%, with a1-environosciences revenues broadly similar to the prior year and CBISS revenues growing by 20%. In late 2010, the decision was taken to consolidate the UK operations of a1-environosciences into Germany and to exit from certain lower margin export sales activities. The reorganisation has been successful and has enabled a1-environosciences to return to solid profitability with a clear focus on higher margin opportunities. In Germany the demand for elemental analysers from the petrochemical and bulk chemical industries remained very positive throughout the year and in the UK, there were solid sales into the petrochemical and water testing sectors. In Switzerland, sales of high value, custom stainless steel laboratory enclosures remained positive and in Germany and France, sales of the standard acrylic enclosures delivered excellent growth.

CBISS experienced strong growth across its product range. The continuous emissions monitoring ("CEMS") business delivered significant growth as new power stations came on line and operators replaced outdated monitoring equipment in existing installations. The value of active prospects remained high throughout the year as funding became more readily available for alternative power plants (waste, biofuels, syngas) and concerted efforts were made to remove bottlenecks in the planning process. Service contract revenues also expanded as the installed CEMS base grew. In addition, CBISS had significant success, through highly focused marketing campaigns, with an expanded range of consumable and low-cost gas detection products.

## Seals

### Sector Definition and Scope

**The Seals sector businesses supply a range of hydraulic seals, gaskets, cylinders, components and kits used in heavy mobile machinery and specialised industrial equipment**

The *Hercules Fluid Power Group* ("HFPG") supplies to the Aftermarket through the Hercules Bulldog and HKX businesses and to Industrial OEM's ("Original Equipment Manufacturers") and equipment dealers through the RT Dygert and All Seals businesses

Hercules is the core Aftermarket business based in Clearwater, Florida and provides a next day delivery service throughout the US, for seals, seal kits and cylinders used in a range of heavy mobile machinery applications. Hercules in Canada offers the same range of products from its two branch operations located in the provinces of Ontario and Quebec. In Europe, Hercules has centred its operations in the Netherlands. Bulldog based in Reno, supplies a range of gasket and seal kits for heavy duty diesel engines, transmissions and hydraulic cylinders used in off road and marine applications. HKX is based near Seattle and supplies hydraulic kits used in the installation of attachments on excavators

The Industrial OEM businesses in North America comprise RT Dygert, with operations in Minneapolis and Chicago and All Seals, based in Santa Ana California. Both companies supply seals, O-rings and custom moulded and machined parts to a range of Industrial OEM customers, cylinder manufacturers and sub-distributors. Applications range from spray painting guns to water filtration to medical devices

*FPE* is based in the UK, with operations in Darlington and Doncaster, and supplies a range of seals, seal kits, cylinder parts and sealants to ram repairers, mobile and heavy plant operators, mechanical handling and process control companies

*M Seals* is a specialised distributor of O-rings, moulded parts, PTFE products and shaft seals, supplied to a range of specialised Industrial OEM customers. Products range from the finest precision seals for hearing aids to large heavy duty seals for wind power mills. *M Seals* has operations in Espergerde in Denmark, Halmstad in Sweden and Tianjin in China

### Market Drivers

The *Aftermarket* businesses supply sealing products to support a broad range of mobile machinery in applications including heavy construction, logging, mining, agriculture, material handling (lift trucks, fork lifts and dump trucks) and refuse collection. Products are generally used in the repair and maintenance of equipment after it has completed its initial warranty period or lease term, or has been sold on in the pre-used market. The main customers are machinery and cylinder repair shops, engine and transmission rebuilders and

tractor parts distributors. The principal market drivers are the growth in the general industrial economy and in particular, heavy construction

The customers of the *Industrial OEM* businesses are manufacturers of a wide range of specialised industrial (and some retail) products. The principal market driver in the OEM sector is therefore general growth in the industrial economy

	2006	2007	2008	2009	2010
US real GDP growth <sup>1</sup>	+2.7%	+1.9%	+0.0%	-2.6%	+2.2%
Annual US construction spending \$bn <sup>2</sup>	1,168	1,151	1,072	908	804
US mobile hydraulic shipments \$m <sup>3</sup>	2,766	2,626	2,913	1,669	2,515

#### Source

- 1 Bureau of Economic Analysis – US Department of Commerce
- 2 US Census Bureau
- 3 National Fluid Power Association

In the United States, the residential construction sector has continued to be subdued, as has spending on infrastructure construction. However, shipments of mobile hydraulic equipment, which among other items includes pumps, cylinders and seals, registered substantial increases to levels which suggest a substantial degree of re-stocking by customers in the US and increased exports driven again by re-stocking, but also by a relatively weak US dollar

In Canada, there was strong economic growth in 2010 resulting in a 3.4% increase in GDP. Although overall growth has slowed more recently, the overall environment remains favourable. In mainland Europe, activity levels were broadly maintained until the first quarter of 2011 when sovereign debt concerns appear to have put a halt to economic growth. Most European governments have been forced to implement austerity programs but they are also looking at ways to stimulate the economies. It is not yet clear how these programs will impact on future construction spending

In general, the *Aftermarket* businesses have experienced enhanced demand for products as repair and refitting of used equipment has continued well into 2011. The *Industrial OEM* businesses have continued to experience strong demand in an improved manufacturing environment

### Sector Performance

#### Seals statistics

	2011	2010
Revenue	£80.0m	£60.1m
Adjusted Operating Profit	£14.9m	£8.9m
Operating Margin	18.6%	14.8%
Free Cash Flow	£6.9m	£7.9m
Trading Capital Employed	£46.8m	£43.5m
ROTCF	31.6%	20.6%

## Sector Review continued

### Seals continued

The Seals businesses saw revenues increase in UK sterling terms by 33% to £80.0m (2010: £60.1m). The results benefited from a full twelve months contribution from All Seals, partly offset by currency translation losses. After adjusting for the All Seals acquisition and the impact of currency translation, underlying sector revenues increased by 26%. Adjusted operating profits increased by 67% to £14.9m (2010: £8.9m) and operating margins increased to 18.6% (2010: 14.8%), driven by operational leverage as increases in operating costs have lagged the strong increase in revenues.

Capital expenditure in the sector was £0.6m with the major elements being investment in two new custom seal making machines and further investment in completing the warehouse automation project in Clearwater. Free cash flow of £6.9m was generated in the year compared with £7.9m in 2010, as working capital returned to historic levels and tax payments increased sharply on higher profits.

*HFPG* underlying revenues, adjusted for the acquisition of All Seals, increased by 26% in US dollar terms. The Aftermarket businesses grew revenues by 27% and the Industrial OEM businesses by 22% on a like-for-like basis.

*Hercules US* the core Aftermarket seal business which services the US, Central and South America and other selected export markets, increased revenues by 19%. The recovery, which had gained momentum in the second half of 2010, continued to strengthen in 2011 and *Hercules US* made significant gains across all product categories and all geographies. The core seal products recorded the most significant overall gains, boosted by strong seal kits sales for construction equipment.

There was significant and sustained demand from the core equipment repair customers in the US, who continued to report heavy utilisation of their workshops. *Hercules US* also benefited from its superior stocking profile and purchasing power, during a year in which most seal manufacturers were either unable to satisfy demand or were quoting unacceptably long lead times. Although *Hercules US* itself had to manage supply shortages, the company was able to take end-user sales from competitors and to supply selected sub-distributors with product that would normally be purchased directly from manufacturers. The South American and other export business grew by 27% with good gains across all geographies, including the Far East.

*Hercules Canada*, *Hercules Europe* and *Bulldog* together increased revenues by 26%. *Hercules Canada* had another excellent year and delivered significant sales growth from a wide range of customers across all Provinces. *Hercules Europe* based in the Netherlands, continued to extend its reach into mainland European countries through the development of sub-distributors. *Bulldog* sells its products through a worldwide network of dealers that buy in relatively large quantities to take advantage of volume discounting and lower, consolidated, freight charges. *Bulldog* delivered a particularly strong performance in international markets

which account for ca. 80% of sales. In the earlier part of the year, orders from the Middle East were buoyant and in the second half there was significant activity from Malaysia, Australia and South Africa. *Bulldog*'s sales to the highly competitive US domestic market also grew steadily for the second consecutive year.

*HKX* had an exceptional year, growing revenues by over 60%. *HKX*'s traditional customers are the North American franchised dealers of the leading excavator manufacturers. Sales of new excavators collapsed in 2009 and *HKX* took action to extend its business model to target the retro-fit attachment sector and to expand internationally. Although still significantly below the historical peak, sales of new excavators grew strongly in 2011, boosted by new environmental legislation in the US. *HKX* was well positioned to resume its leading position in this sector as well as continuing to develop its extended offering to a generally more stable construction market.

In the Industrial OEM businesses, *RT Dygert* and *All Seals* both delivered strong performances with combined revenues growing by 22% on a like-for-like basis. The results were achieved despite product shortages in early 2011 caused by capacity constraints at key suppliers and raw material price and availability issues. During the year, *RT Dygert* continued to develop its sales reach and acquired new customers in its target industries, building on the recovery that began in the second half of 2010. The sales momentum in the general industrial sector continued throughout 2011 and further growth was added with the recovery of the Mid-Western hydraulic cylinder manufacturers.

*All Seals* was acquired in September 2010 and delivered good sales growth in 2011. The general industrial customers again provided positive sales momentum and the expanded sales team developed new opportunities in the large Californian market. Plans are under way to add additional sales support and technical resources to allow the business to build on its solid base and expand its reach in the Western United States.

The *FPE* and *M Seals* businesses in Europe both had excellent years with aggregate revenues growing by over 25%. In the UK, *FPE* made substantial gains in the sale of standard seals, cylinder parts and manufactured products and export sales were also very strong as sub-distributors continued to purchase in larger quantities. *M Seals* continued to build on the recovery that began in mid-2010 and delivered strong sales growth from its traditional industrial customers in Denmark and Sweden as confidence returned in both domestic and export markets. In particular, there were substantial increases in sales to the wind power market, where *M Seals* is a key supplier of large bearing seals to the industry-leading players in Western Europe and the US. During the year *M Seals* established a wholly owned foreign enterprise ("WFOE"), registered in Tianjin, China, in order to trade directly with the key companies in the developing Chinese wind power sector.

## Controls

### Sector Definition and Scope

**The Controls sector businesses supply specialised wiring, connectors, fasteners and control devices used in a range of technically demanding applications**

The IS-Group supplies high performance wiring, interconnect electro-mechanical and fastener products for use in a range of technically demanding applications in industries including Defence & Aerospace, Motorsport, Energy Medical and General Industrial. The IS-Group also supplies a range of its own manufactured products, including flexible braided products for earthing and lightning protection, power shunt connectors, and multi-core cables.

The IS-Rayfast Cabletec and Clarendon businesses are located in the UK in Swindon, Weston-Super-Mare and Leicester, respectively. The businesses serve the UK market, as well as supplying to other sub-distributors across Continental Europe. IS-Connect is located in Indianapolis to serve the Motorsport market in the US, as well as other specialised technical applications. A representative office has also been established in Beijing, China with an initial focus on Aftermarket requirements in the Commercial Aerospace and Industrial sectors.

The Sommer business is located in Stuttgart, Germany and also supplies high performance wiring and other interconnect products. A range of value adding activities enhances the customer offering including marking of protective sleeves, cut-to-length tubing kitting and prototype quantities of customised multi-core cables.

Filcon is located in Munich and supplies specialist connectors principally into the Defence & Aerospace markets in Germany. Filcon offers connector assembly as a value-added service. Hawco supplies a range of control devices used in the sensing, measurement and control of temperature and pressure. Applications range from chilled cabinets for supermarkets, bars and restaurants to fire detection systems. Hawco has its operations in Guildford and Bolton, in the UK.

### Market Drivers

The Controls sector businesses focus on specialised, technical applications in a range of industries including Defence & Aerospace, Motorsport Medical Equipment, Energy Commercial Refrigeration and General Industrial. The key market drivers in *Defence & Aerospace* are national defence budgets and commercial aerospace passenger activity.

	2006	2007	2008	2009	2010
<b>Defence equipment budgets</b>					
UK – £bn <sup>1</sup>	68	72	79	87	90
Germany – €bn <sup>2</sup>	82	86	95	103	104
<b>Commercial aerospace Market growth<sup>3</sup></b>	+5.2%	+7.2%	+1.6%	-2.0%	+7%

#### Sources

- 1 MOD UK Defence Statistics
- 2 Federal Ministry of Finance – Germany
- 3 Boeing and Airbus market outlook – revenue passenger kilometres

The Defence equipment budgets in the UK and Germany grew strongly until 2009 and, although growth slowed in 2010, spending remained at an historical high and growth over the five year period to 2010 averaged 7% p a in the UK and 6% p a in Germany. Moving forward, spending will inevitably be impacted by the Strategic Defence Reviews in the UK and Germany.

The IS-Group businesses in the UK and Sommer in Germany focus primarily on refurbishment, upgrade and maintenance programmes, as well as supplying to Tier 2 electronics suppliers. The businesses typically only supply to OEMs and the Tier 1 suppliers when ex-stock availability and responsiveness are important. They have therefore been less exposed to cutbacks and postponements in major defence programmes. Filcon has a greater involvement in the major capital projects through its supply of connectors. However, Filcon has its products designed-in to a broad range of air, sea and land applications and is not overexposed to individual projects.

In the Commercial Aerospace sector, the businesses supply products principally for the initial fit out of aircraft interiors and then their subsequent upgrade and refurbishment. The Commercial Aerospace market declined in 2009 as a result of the global economic downturn before recovering in 2010 and posting a healthy 7% growth. As passenger numbers continue to recover, the sector appears to be returning to its long-term projected growth rate of ca 5% p a.

The businesses also supply to a range of specialised technical applications in the *General Industrial* sector where the underlying market drivers are the growth of the industrial economies.

	2006	2007	2008	2009	2010
UK real GDP growth <sup>1</sup>	+2.8%	+2.7%	-0.1%	-4.9%	+1.3%
UK production index <sup>2</sup>	100.0	100.5	97.6	87.2	90.3
Germany real GDP growth <sup>1</sup>	+3.6%	+2.8%	+0.7%	-4.7%	+3.5%

#### Sources

- 1 Organisation for Economic Co-operation and Development (OECD)
- 2 The Office of National Statistics – Index of Production for Manufacturing

In the UK, manufacturing demand has remained relatively stable through 2010 and into the first half of 2011. In Germany, there was a sharp recovery in 2010 and into the first quarter of 2011 but growth has subsequently flattened out.

In *Motorsport*, activity increased sharply due to continued competitiveness within F1 across the grid, combined with greater financial stability in a number of teams. In the World Rally & DTM (Deutsche Tourenwagen Masters) competitions, changes to car specifications and new entrants such as Mini have stimulated interest in these series. The *Medical Equipment* market (particularly in Germany) remained stable and, in *Energy*, there was strong demand from the manufacturers of electrical generators and commercial batteries. In Germany, the

## Sector Review continued

### Controls continued

decision to close down eight of the older nuclear power plants will require changes to be made to the power distribution network and infrastructure spending may need to be increased in future years

The UK *Commercial Refrigeration* market continued to be boosted by the major retailers continuing to invest in new, convenience stores and in energy saving technologies when refurbishing existing outlets

#### Sector Performance

##### Controls statistics

	2011	2010
Revenue	<b>£76 2m</b>	£68 0m
Adjusted operating profit	<b>£13 2m</b>	£11.3m
Operating margin	<b>17 3%</b>	16 6%
Free cash flow	<b>£9 8m</b>	£9 9m
Trading capital employed	<b>£30 0m</b>	£29 3m
ROTCE	<b>44 0%</b>	38 6%

The Controls businesses increased revenues in 2011 by 12% to £76 2m (2010 £68 0m) on a UK sterling basis, with the same level of growth on a constant currency basis. Adjusted operating profits increased by 17% to £13 2m (2010 £11 3m) with operating margins increasing to 17 3% (2010 16 6%)

Capital expenditure in the sector was £0 3m mainly for the completion of a new ERP system in the Sommer operation. Free cash flow of £9 8m (2010 £9 9m) remained at a similar level to last year reflecting a small increase in both working capital and tax payments

The *IS-Group* increased revenues by 16% with the UK businesses growing by 18% and Sommer in Germany growing by 12%. In the UK, the *IS-Group's* sales to the Defence sector showed a modest decline from the historical high point achieved in the prior year but there was continuing demand from a wide range of customers that build or repair ground vehicles, large field guns and weapons systems. The military marine sector benefited from continuing work on Astute submarines and on torpedo systems, while military aerospace sales included components for the A340 landing gear and the Hawk jet trainer. Commercial Aerospace sales were positive as confidence returned to the sector and airlines commissioned the fit-out of new aircraft, in particular, there was good demand for parts for economy and premier class seating and for new galleys in new and refurbished aircraft

Sales of electrical harness components and aerospace grade fasteners to the Motorsport sector were exceptionally strong in the year. In a successful F1 racing season the *IS-Group* benefited from increased demand from the larger teams, boosted by the re-introduction of KERS (Kinetic Energy Recovery System) and increased sales of fastener products to the F1 teams based in mainland Europe. Sales to the two key US racing series, IndyCar and NASCAR, also showed excellent growth in the year

The General Industrial sector in the UK delivered strong growth with very positive demand across multiple sub-sectors including rail, specialist automotive, leisure marine, mining equipment and sub-sea activities. The Energy sector also delivered very significant sales growth for the *IS-Group* in 2011 with strong cabling and power shunt sales to generator manufacturers and significantly increased demand for components for batteries used in Uninterrupted Power Supply ("UPS") applications

In Germany Sommer was well positioned to take advantage of the sharp recovery in the General Industrial base and enjoyed a very strong first half in 2011 with buoyant sales to multiple segments including electronics, motors, valves, harnessing and specialist automotive. Motorsport sales were also very strong as confidence returned to the German auto industry and the key players invested in engines and cars for the F1, DTM and Le Mans series. Energy sales were buoyant and were boosted by the contribution from Fischer, the small acquisition made in August 2010. Defence sales remained subdued as concerns over the German defence budget caused uncertainty and spending slowed. Aerospace sales were on a par with the prior year with good sales to the satellite sector being mostly offset by a general slowdown in sales to the manufacturers of smaller aircraft. Medical sales were also at a similar level to the high point achieved in 2010

*Filcon* has a reasonably concentrated customer base for its high performance connector products with its core customers being the Tier 1 German Defence and Aerospace OEMs. The continuing review of German defence spending delayed the commencement of several projects and the quantity of components supplied by *Filcon* to the EFA programme continued to reduce as expected. Despite this background, *Filcon's* sales were only modestly lower than in the prior year as the company supplies to a wide range of individual applications including four separate helicopter projects and other projects in the specialist military radio sector. *Filcon* also supplies its specialised connectors to the Motorsport sector, where the buoyant F1 series ensured strong sales throughout the year

*Hawco* continued to build on its positioning as a specialist supplier of energy efficient components to the UK commercial refrigeration sector. A year of very solid growth was again driven primarily by the major food retailers opening new stores and refurbishing existing locations. *Hawco* also extended its reach into the attractive fast food retail sector by offering a range of both cooling and heating components to match the needs of individual franchises

## Finance Review

**Nigel Lingwood**  
Group Finance Director

### Continued Strong Performance

In 2011 Diploma achieved very strong growth in operating profits supported by robust cash generation as demand continued to remain buoyant in each of the Group's principal markets. Revenue increased by 26% to £230.6m (2010: £183.5m) and adjusted operating profit which is before acquisition related charges, increased by 41% to £45.2m (2010: £32.1m). The adjusted operating margin increased to a record 19.6% from 17.5% in the 2010 financial year, demonstrating the high degree of operational leverage in the Group's businesses and in the North American Seals businesses in particular. In the medium term, this level of operating margin is likely to fall back slightly as new investment is made in the businesses to add resource and upgrade the infrastructure to support future growth in the Group.

Adjusted operating profit in the second half of the year of £23.1m (2010: £17.5m) was 32% ahead of the comparable period last year and represented 51% of the full year's operating profit. This compared with an increase in operating profits of 51% in the first half of the year.

These results demonstrate that the recovery in 2010 following the 2009 recession, continued to be strong throughout much of 2011. Against increasingly demanding comparatives, the growth rates moderated slightly towards the end of the financial year.

### Substantial Increase in Underlying Operating Profits

Acquisitions completed during both 2010 and 2011 incrementally contributed £17.2m and £3.2m to revenues and adjusted operating profit respectively.

The net impact on the Group's results from the translation of the results of the overseas businesses to UK sterling was much smaller than in previous years. This year Group revenues and adjusted operating profits were reduced by £0.5m and £Nil respectively, as the impact of a weaker US dollar offset the benefit of a stronger Canadian dollar. On a transaction basis, a small gain to the gross margin of the UK businesses, from the volatility of the Euro during the year, was offset by a small net loss to gross margins in the Canadian Healthcare businesses from the effect of their US dollar hedging programme.

On an underlying basis, revenues and adjusted operating profit increased by 17% and 31% respectively, after adjusting for these items.

### Adjusted Profit, Earnings per Share and Dividends

Adjusted profit before tax increased 39% to £44.9m (2010: £32.2m), after net interest expense of £0.3m (2010: income of £0.1m). IFRS profit before tax, which is after acquisition related charges of £4.8m (2010: £3.5m) and fair value remeasurements of £0.9m (2010: £2.0m) was £39.2m (2010: £26.7m).

The Group's adjusted effective accounting tax charge represented 28.7% (2010: 29.2%) of adjusted profit before tax, which was also broadly consistent with the cash tax rate of 27.6%. This year's effective rate benefited from a reduction in the statutory corporate tax rates in both the UK and in Canada, although this was somewhat offset by the higher proportion of profits contributed by HFPG in the US, where the effective tax rate is ca. 38%.

Adjusted earnings per share increased by 48% to 27.9p, compared with 18.9p last year, which was much larger than the increase in adjusted profit. This larger increase reflected the impact of buying-out the 25% minority interest in AMT during the year. IFRS basic earnings per share increased to 24.0p (2010: 14.6p).

In light of the strong increase in earnings, the Directors have recommended an increase in the final dividend to 8.5p per share, this gives a total dividend for the year of 12.0p per share, which represents an increase of 33% on the prior year.

The dividend cover increases to 2.3 times, which is larger than previous years, but reflects a degree of caution, given the current uncertainty in the direction of global markets.

### Robust Free Cash Flow

The Group continued to generate strong free cash flow of £25.0m in 2011, despite the return of working capital to more normal levels. Last year's free cash flow was £29.8m, but this included £6.4m of proceeds from the sale of the Anachem businesses. Free cash flow is before expenditure on acquisitions or returns to shareholders.

## Finance Review continued

Operating cash flow increased to £40.3m (2010: £34.3m) after investing £7.4m (2010: £0.1m reduction) in working capital, mainly to rebuild inventories during the year to support the current level of trading activity. The ratio of working capital to revenues at 30 September 2011 was 16.1% (2010: 15.4%) which was still below the longer run average of ca. 17%.

Group tax payments increased to £12.4m (2010: £9.3m) in line with the increase in taxable profits and £1.6m (2010: £0.4m) was spent on funding the Employee Benefit Trust to allow it to purchase ordinary shares in the Company. Capital expenditure increased to £1.7m (2010: £1.3m) but remained below the £2.1m charge for depreciation. The Canadian Healthcare businesses spent £0.4m on acquiring field equipment in support of their customer contracts with Canadian hospitals. In Seals HFPG spent £0.3m on two new custom seal machines and a further £0.2m on completing the warehouse automation project in Clearwater. Other capital expenditure of £0.8m included enhancements to existing facilities and further investment in the IT infrastructure across the Group, including £0.2m on a new ERP system in Sommer.

The Group spent £28.2m (2010: £11.0m) of its cash resources on acquiring businesses, including minority interests, during the year and £14.8m (2010: £10.2m) on paying dividends to both Company and minority shareholders.

### Significant Reduction in Liabilities to Minority Shareholders

During the year the Group acquired the outstanding 25% minority shareholding in AMT, one of the Group's Healthcare businesses in Canada, for £12.5m. These shares were acquired through the exercise of put/call options, agreed at the time of acquisition in September 2007.

Following this transaction the liability retained by the Group to purchase the remaining minority shareholdings has fallen significantly to £2.0m (2010: £13.2m). This liability relates to minority shareholdings held in M Seals and BGS and in HPS which is a small subsidiary of the RT Dygert seals business, the majority of this liability will be payable in December 2012 to acquire the outstanding 10% minority shareholdings in M Seals. These liabilities arise under put/call options entered into at the time of acquisition and are based on the Directors' estimate of the Earnings Before Interest and Tax ("EBIT") of these businesses when the options crystallise.

Based on the expected performance of these businesses, the Directors have reassessed the potential liability at 30 September 2011 to acquire the remaining outstanding minority interests. The fair value remeasurement of these options has led to a financial charge of £0.9m (2010: £2.0m) being made in the consolidated Income Statement.

### Value Enhancing Acquisitions

The Group spent £28.2m on acquisitions during the year, including £12.5m on acquiring the outstanding 25% minority shares in AMT. Expenditure of £14.8m was paid during the year to acquire the Canadian healthcare business of CMI in December 2010. A provision of £1.1m has also been made at the year-end for deferred consideration relating to this acquisition. These acquisitions, including those made towards the end of the last financial year, have made a strong contribution to earnings this year. During the year deferred consideration of £0.9m was also paid in connection with three smaller acquisitions completed last year.

Acquisition intangible assets of £9.3m were recognised on completion of these acquisitions, as well as goodwill of £20.4m reflecting the amount paid in excess of the value of the net assets. The acquisition of the minority interest in AMT accounted for £13.1m of this goodwill and the balance of £7.3m comprised the value in CMI relating to both the prospects for sales growth in the future (from both new customers and new products) and from operating cost synergies.

### Excellent Return on Trading Capital and Strong Balance Sheet

The Group achieved an excellent return on trading capital employed ("ROTCE") of 25.4% in 2011 (2010: 22.1%). ROTCE is a pre-tax measure and includes all gross historic goodwill and intangible assets and represents an indication of the profitability of the Group. This improved return arose from a combination of the growth in profits and from strong management of working capital across the businesses.

In absolute terms, trading capital employed, which represents the amount of operational assets held by the businesses, increased by £30.6m to £152.9m (2010: £122.3m). The majority of this increase arose from the acquisition of intangible assets with the balance being contributed by investment in working capital to meet the stronger trading environment.

The Group recognises the importance of maintaining a strong balance sheet, particularly during this period of uncertainty in the global financial markets. At 30 September 2011 the Group held net cash funds of £12.2m with £17.8m of cash balances offset by £5.6m of borrowings. The cash funds are generally repatriated to the UK, unless they are required locally to meet certain commitments, including acquisitions.

The Group borrowings of £5.6m at the year-end were drawn from the Group's £20m revolving credit facility to help finance the purchase of the minority interests earlier during the year. The Group has an option to extend these bank facilities to £40m, subject to market pricing, and these facilities remain available until November 2013.

#### Land at Stamford

The Group continues to retain approximately 150 acres of farm and former quarry land in Stamford which relates to a former legacy business. This land is included in the balance sheet at £Nil and in the opinion of the Directors, it is unlikely to be worth more than £0.5m in its present condition. The Directors anticipate that this land will continue to be leased to a local farmer and there is no intention to dispose of this land in the foreseeable future.

#### Valuation of Merged Pension Scheme

The Group successfully completed the merger of its four small closed defined benefit pension schemes at 30 September 2010 and during 2011 finalised an actuarial funding valuation of the merged Scheme as at that date. The funding deficit in the newly merged Scheme was £2.7m representing a funding level of 87%. The Company has agreed with the Trustees to continue to pay £320,000 into the Scheme each year (increasing by 2% p.a.) with the objective of eliminating the deficit within ten years. With the scheme merger now completed, attention will be focused on exploring opportunities to reduce the Group's pension liability through the use of structured insurance products.

On an accounting basis, the net pension liability increased marginally at 30 September 2011 to £5.4m (2010: £5.3m). The higher accounting deficit reflects the accounting requirement to value the liabilities at a more conservative market discount rate, compared with the higher discount rate used in the funding valuation.

Both the funding and accounting valuations have benefited this year from HM Government's decision earlier in the year to use the Consumer Price Index ("CPI") instead of the Retail Price Index ("RPI") as the basis for statutory inflation increases in certain pension benefits. The benefit to the accounting valuation from the change to CPI is ca. £1.4m and this is included in the consolidated Statement of Comprehensive Income.

Pension benefits to existing employees, including the Executive Directors, are provided through defined contribution schemes at an aggregate cost in 2011 of £0.8m (2010: £0.7m).

#### Measuring Financial Performance

The Group continues to use a number of specific measures to assess the performance of the Group and these are referred to throughout this Annual Report in the discussion of the performance of the businesses. These measures are not defined in IFRS but are used by the Board to assess the underlying operational performance of the Group and its businesses. As such the Board believes these performance measures are important and should be considered alongside the IFRS measures. The alternative performance measures which have been used in this Annual Report, are described in note 2 to the consolidated financial statements.

Reported performance takes into account all the factors (including those which the Group cannot influence principally currency exchange rates) that have affected the results of the Group's business and which are reflected in the consolidated financial statements prepared in accordance with International Financial Reporting Standards ("IFRS"), as adopted by the European Union.

There have been no new accounting or disclosure requirements this year that have impacted the Group's consolidated financial statements.

## Principal Risks and Uncertainties

Risk assessment and evaluation is an integral part of the Group's annual planning cycle and market specific risks are evaluated as part of the annual budgeting process

Each operating business is required each year to identify and document the significant strategic, operational and financial and accounting risks facing the business. For each significant risk, a number of scenarios are mapped out and an assessment is made of the likelihood and impact of each risk scenario. Finally, plans and processes are established which are designed to control each risk and minimise its potential impact.

The risk assessments from each of the operating businesses are reviewed with the Executive Directors and a consolidated risk assessment is reviewed by the Board.

The principal risks and uncertainties which are currently judged to have the largest potential impact on the Group's long-term performance are set out below.

### Risk Strategic

#### Downturn in major markets

Adverse changes in the major markets in which the businesses operate can have a significant impact on performance. The effects will either be seen in terms of slowing revenue growth due to reduced or delayed demand for products and services, or pressure on margins due to increased competitive pressures.

A number of characteristics of the Group's businesses moderate the impact of economic and business cycles on the Group as a whole:

- The Group's businesses operate in three different sectors with different cyclical characteristics and across a number of geographic markets as set out on page 10.

- The businesses offer specialised products and services, this offers a degree of protection against customers quickly switching business to achieve a better price.
- A high proportion of the Group's sales comprise consumable products and service contracts which are purchased as part of customers' operating expenditure rather than through capital budgets.
- In the majority of cases the products are used in repair, maintenance and refurbishment applications, rather than original equipment manufacture.

#### Mitigation

The businesses identify key market drivers and monitor the trends and forecasts, as well as maintaining close relationships with key customers who may give an early

warning of slowing demand. Changes to cost levels and inventories can then be made in a measured way to mitigate the effects.

#### Loss of key supplier(s)

For manufacturer-branded products, there are risks to the business if a major supplier decides to cancel the distribution agreement or if the supplier is acquired by a company which has its own distribution channels in the relevant market. There is also the risk of a supplier taking away exclusivity and either setting up direct operations or establishing another distributor.

In times of rapid economic expansion in activity, such as after a global recession, the lead times to supply key product can become very long.

No supplier represents more than 15% of Group revenue and only five suppliers represent more than 2% each of Group revenue.

Relationships with suppliers have normally been built up over many years and a strong degree of interdependence has been established. The average length of the principal supplier relationships in each of the sectors is over ten years.

Strength of relationship with supplier and volume of activity generally ensures continuity of supply when there is shortage of product.

#### Mitigation

Actions to mitigate the risks include:

- Long term, multi-year exclusive contracts signed with suppliers with change of control clauses, where possible, included in contracts for protection or compensation in the event of acquisition.
- Collaborative projects and relationships maintained with individuals at many levels of the supplier organisation together with regular review meetings and adherence to contractual terms.

- Regular review of inventory levels.
- Bundling and kitting of products and provision of added value services.
- Periodic research of alternative suppliers as part of contingency planning.

**Risk Strategic continued**  
**Loss of major customer(s)**

The loss of one or more major customers can be a material risk	The nature of the Group's businesses is such that there is not a high level of dependence on any individual customers and no customer represents more than 5% of sector revenue or more than 2% of total Group revenue
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**Mitigation**

Specific large customers are important to individual operating businesses and a high level of effort is invested in ensuring that these customers are retained and encouraged not to switch to another supplier	In addition to providing high levels of customer service, close integration is established where possible with customers' systems and processes
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**Product liability**

There is a risk that products supplied by a Group business may fail in service, which could lead to a claim under product liability. The businesses, in their Terms and Conditions of sale with customers, will typically mirror the Terms and Conditions of sale from the suppliers. In this way the liability can be limited and subrogated to the supplier.	exposed to legal costs and potential damages if the claim succeeds and the supplier fails to meet its liabilities for whatever reason. Product liability insurance can be limited in terms of its scope of insurable events, such as product recall.
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However if a legal claim is made it will typically draw in our business as a party to the claim and the business may be	During 2011, the Group settled a small claim received from a customer in respect of product failure which it was unable to recover from the supplier. However, there have been no similar claims during the past ten years.
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**Mitigation**

Technically qualified personnel and control systems are in place to ensure products meet quality requirements. The Group has also established Group-wide product liability insurance which provides worldwide umbrella insurance cover of £10m in all sectors.	The Group's businesses may also elect not to supply products if they are not fully confident that the products will meet the demands of the operating environment.
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**Loss of key personnel**

The success of the Group is built upon strong self-standing management teams in the operating businesses, committed to the success of their respective businesses. As a result, the loss of key personnel can have a significant impact on performance, at least for a time.	Average age of our senior managers making up the self-standing management teams in the operating businesses is 43 with an average length of service of ten years.  As set out on page 43 the average length of service for all personnel in the Group is over five years.
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**Mitigation**

Contractual terms such as notice periods and non-compete clauses can mitigate the risk in the short term. However more successful initiatives focus on ensuring a challenging work environment with appropriate reward systems. The Group places very high importance on planning the development, motivation and reward for key managers in the operating businesses such as	<ul style="list-style-type: none"> <li>• Establishing management development programmes to ensure a broad base of talented managers</li> <li>• Offering a balanced and competitive compensation package with a combination of salary, annual bonus and long-term cash incentive plans targeted at the individual business level</li> <li>• Giving the freedom, encouragement, financial resources and strategic support for managers to pursue ambitious growth plans</li> </ul>
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## Principal Risks and Uncertainties continued

### Risk Operational

#### Major damage to premises

The Group's businesses mostly operate from combined office/warehouse facilities which are dedicated to each business and not shared with other Group businesses

However, the Group has not suffered any major damage to premises in recent years and in Clearwater, Florida there has been no significant hurricane activity for at least the last three years

Major damage to the facilities from fire, malicious damage or natural disaster would impact the businesses for a period until the damage is repaired or alternative facilities have been established

#### Mitigation

The business where the risk is greatest is Hercules in Clearwater Florida which is most at risk from an environmental disaster caused by a hurricane or tornado. The building structure has been designed to withstand 150mph winds and a specific disaster plan has been drawn up and is regularly reviewed

The other businesses have also developed plans to prevent incidents, including fire and security alarms and regular fire drills. Insurance policies are also in place including property, contents and business interruption cover which would mitigate the financial impact

This includes

- Backup power generator
- Materials on hand to secure the facility
- Communications reroute to other branches or interim locations
- IT recovery plan using backup server in separate location
- Regular building inspection and weather monitoring
- Plans to drop-ship product from suppliers direct to customers

However, the priority in such an event is to become operational as quickly as possible to minimise disruption to customers. Plans to ensure a quick and orderly recovery have been developed by the businesses and are periodically reviewed

#### Loss of Information Technology ("IT") systems

Computer systems are critical to the businesses since their success is built on high levels of customer service and quick response. A complete failure of IT systems,

with the loss of trading and other records, would be more damaging to the businesses than major physical damage to facilities

#### Mitigation

Business interruption insurance cover is held across the Group and contingency plans have been drawn up in all businesses. The recovery plans differ by individual business, but will include some or all of the following elements

- Full data backups as a matter of routine and backup tapes stored in a fireproof safe

- Backup servers identified and communication reroute options identified
- Service contracts with IT providers with access to replacement servers
- Uninterruptible power sources and backup generators where required
- Virus checkers and firewalls

### Risk Financial and Accounting

The Group's activities expose it to a variety of financial and accounting risks, including foreign currency liquidity, interest rate and credit. The policies for managing these financial risks, as well as the management of capital risks are set out in note 18 to the consolidated financial statements. The principal financial and accounting risks are summarised below. The Group's overall management of these risks is carried out by a central treasury team (Group treasury) under policies and

procedures which are reviewed and approved by the Board. Group treasury identifies, evaluates and where appropriate hedges financial risks in close co-operation with the Group's operating businesses. The Group treasury team does not undertake speculative foreign exchange dealings for which there is no underlying exposure.

#### Foreign currency risk – Translational exposure

Foreign currency risk is the risk that changes in currency rates will affect the Group's results. The Group operates internationally and is exposed to foreign exchange risk arising from various currency exposures, primarily with respect to the US dollar, the Euro and the Canadian dollar. The Group also has operations outside the UK whose net assets are also exposed to foreign currency translation risk.

During the year ended 30 September 2011, ca. 75% of the Group's revenue and operating profits were earned in currencies other than UK sterling. In comparison to the prior year, the net effect of currency translation was to increase revenue by £0.5m and to increase operating profit by £Nil. It is estimated that a strengthening of UK sterling by 10% against all the currencies in which the Group does business, would reduce operating profit

before acquisition related charges and tax, by approximately £3.4m (7.5%) due to currency translation.

Currency exposures also arise from the net assets of the Group's foreign operations. At 30 September 2011, the Group's non-UK sterling trading capital employed in overseas businesses was £130.9m (2010: £103.1m), which represented 86% of the Group's trading capital employed. It is estimated that a strengthening of UK sterling of 10% against all the non-UK sterling capital employed would reduce shareholders' funds by £12.6m.

Details of average exchange rates used in the translation of overseas earnings and of year end exchange rates, used in the translation of overseas balance sheets, for the principal currencies used by the Group, are shown in note 28 to the consolidated financial statements.

#### Mitigation

The Group does not hedge translational exposure.

#### Foreign currency risk – Transactional exposure

The Group's UK businesses are also exposed to foreign currency risk on purchases that are denominated in a currency other than their local currency, principally US dollars, Euro and Japanese yen. The Group's Canadian

and Australian businesses are also exposed to a similar risk as the majority of their purchases are denominated in US dollars.

#### Mitigation

The Group's businesses may hedge up to 80% of forecast (being a maximum of eighteen months) foreign currency exposures using forward foreign exchange

contracts. The Group classifies its forward foreign exchange contracts, hedging forecasted transactions, as cash flow hedges and states them at fair value.

### Risk Accounting

#### Inventory obsolescence

Working capital management is critical to success in specialised distribution businesses as this has a major impact on cash flow. The principal risk to working capital, is in inventory obsolescence and write-off.

The charge against operating profit in respect of old or surplus inventory is generally ca. £0.7m per year but inventories are generally not subject to technological obsolescence.

#### Mitigation

Inventory write-offs are controlled and minimised by active management of inventory levels based on sales forecasts and regular cycle counts. Where necessary

a provision is made to cover excess inventory and potential obsolescence.

## Board of Directors and Advisors

### John Rennocks (66)<sup>1, 2, 3</sup> Non-Executive Chairman

**Appointed** Joined the Board in July 2002 and appointed Chairman in January 2004

**Skills and experience** John is a Chartered Accountant with over 40 years of experience in commerce and industry, including nearly 20 years as the Finance Director of FTSE 100 companies. He has been a non-Executive Director of many companies in the past 17 years, including as Chairman of six other public or private companies across several industrial or support service sectors.

**External appointments** John is currently Chairman of Intelligent Energy PLC and the Senior Independent Director of Inmarsat PLC and Babcock International Group PLC.

### Bruce Thompson (56) Chief Executive Officer

**Appointed** Joined the Board in 1994 as a Group Director and appointed Chief Executive Officer in 1996.

**Skills and experience** Bruce started his career in the automotive industry, first as a design engineer and then in product marketing. He then spent three years in international marketing with a construction materials company developing new markets in Europe, the Middle East and North Africa. Prior to joining Diploma, he was a Director with Arthur D Little Inc the technology and management consulting firm, initially in the UK and then as Director of the firm's Technology Management Practice based in Cambridge, Massachusetts.

**External appointments** None.

### Nigel Lingwood (52) Group Finance Director and Company Secretary

**Appointed** Joined the Company in June 2001 and appointed Group Finance Director in July 2001.

**Skills and experience** Prior to joining the Company Nigel was the Group Financial controller at Unigate PLC where he gained experience of working in a large multi-national environment and on a number of large corporate transactions. Nigel qualified as a Chartered Accountant with Price Waterhouse London.

**External appointments** None.

Member of  
1 the Remuneration Committee  
2 the Audit Committee  
3 the Nomination Committee

**John Matthews (67)<sup>1,2,3</sup>**  
**Non-Executive Director**

**Appointed** Joined the Board in 2003

**Skills and experience** John is a Chartered Accountant and a former Managing Director and Head of Corporate Finance at County NatWest. Subsequent to this he was Deputy Chairman and Deputy Chief Executive at Beazer plc, an international civil engineering, construction, house building and aggregates group. He has also been Chairman of Crest Nicholson plc and Regus plc and a non-Executive Director of a number of listed and private companies.

**External appointments** John is currently a member of the Board of SDL plc and Aurelian Oil & Gas plc and a member of the Advisory Board of Alexander Proudfoot.

**Advisors**

**Investment Bankers**

Lazard  
 50 Stratton Street  
 London W1J 8LL

**Bankers**

Barclays Bank PLC  
 1 Churchill Place  
 London E14 5HP

**Ian Grice (58)<sup>1, 2,3</sup>**  
**Non-Executive Director**

**Appointed** Joined the Board in January 2007

**Skills and experience** A chartered engineer with over 35 years experience in the Support Services and Construction sectors, in the UK and International markets. Ian held senior roles in several industrial groups before joining the board of Alfred McAlpine plc in 1995 where he was Chief Executive Officer from 2003 to 2008.

**External appointments** Ian is currently a member of the Supervisory Board of Arcadis NV, and a non-Executive Director of three private companies.

**Auditor**

Deloitte LLP  
 2 New Street Square  
 London EC4A 3BZ

HSBC Bank plc  
 City Corporate Banking Centre  
 60 Queen Victoria Street  
 London EC4 4TR

**Iain Henderson (55)**  
**Chief Operating Officer**

**Appointed** Joined the Board as a Director in 1998 and appointed Chief Operating Officer in 2005.

**Skills and experience** Iain qualified as a chartered management accountant and began his career in the food industry, progressing to be an operations general manager with H J Heinz. Since 1988, Iain has specialised in the acquisition and development of small to medium sized enterprises ("SME") within group structures. This was firstly within the privately owned Bricom MBO, where he ran ANC Holdings and from 1994 in a public company environment as a Director of Glenchewton plc and then Diploma PLC.

**External appointments** None

**Corporate Stockbrokers**

Numis Securities  
 10 Paternoster Square  
 London EC4M 7LT

**Solicitors**

Ashurst  
 Broadwalk House  
 5 Appold Street  
 London EC2A 2HA

## Corporate Governance

**John Rennocks**  
Chairman

### Number of Board Meetings

Directors and attendance	2011
John Rennocks (Chairman)	6/6
John Matthews	6/6
Ian Grice	6/6
Bruce Thompson	6/6
Iain Henderson	6/6
Nigel Lingwood	6/6

This section of the Annual Report & Accounts sets out how the Board and its Committees discharge their duties and how we apply the principles of good governance set out in the new UK Corporate Governance Code

The Board has always been committed to the highest standards of corporate governance appropriate to a company of the size and complexity of Diploma PLC. The new Code which is applicable to the Company from 1 October 2010 has introduced a number of new obligations on larger companies, some of which have not yet been adopted in Diploma, as permitted by the Code

These obligations include the requirement that more than half the Board should comprise independent directors, that the directors should be subject to annual re-election and that the Board should have externally facilitated performance evaluations. As a smaller company, I have always considered that it was more important that the Board operated within the spirit of the principles of corporate governance, rather than necessarily following regimented rules

I firmly believe that good governance comes from a robust and effective Board which provides strong leadership to the Company and engages well with both management and shareholders. Throughout my tenure as Chairman, the Board has been made up of a good balance of Executive and non-Executive Directors whose skills have been carefully balanced and which has fostered an environment whereby constructive challenge and open debate is actively encouraged at all meetings

Over the ten years that I have been on the Board of Diploma, the Company has been very successful and has grown substantially to the point that the Company was recently promoted to the FTSE350. The Board recognises that with greater size comes greater accountability and I therefore intend with the support of the Board, to focus over the next eighteen months on developing the Board and its governance procedures so that it will be able to meet the higher standards set for large companies

With both myself and John Matthews having served on the Board for a number of years now, this process will include the addition of two further non-Executive Directors to the Board. A key element of our approach to Board structure has been and will be to seek to have a broad spread of skills blending together, so that we have a Board for which the overall strength is greater than "the sum of the parts". We will ensure that the process takes account of the findings of the Davies Report on Boardroom diversity and recent amendments to the Code by the FRC

Meanwhile I remain satisfied that the Board is well suited to our business and that the Board will continue to have the appropriate balance of skills, experience, independence and knowledge of the Company to enable the Directors to discharge their duties and responsibilities effectively

Finally I would like to encourage all shareholders to find the time to join us at our AGM on 18 January 2012 as it provides an excellent opportunity to meet all members of the Board

**John Rennocks**  
Chairman

### Compliance Statement

The Governance report on pages 26 to 41 is designed to provide shareholders with a clear summary of the Group's governance arrangements by reference to the UK Corporate Governance Code ("the Code"), published in June 2010 as it applied to the Company in 2011. Throughout the accounting period to which this report relates the Directors believe that the Company has complied with all of the relevant Provisions set out in Sections A to E of the Code

## Report on Corporate Governance

### Compliance with the UK Corporate Governance Code

As a UK-listed company Diploma PLC is required to state whether it has complied with the Main Principles of the UK Corporate Governance Code ("the Code") published by the Financial Reporting Council in June 2010 throughout the year in review and, where the provisions have not been complied with, to provide an explanation. Diploma PLC is also required to explain how it has applied the Main Principles of the Code and this is set out below.

### Leadership

The Company's governance structure is based on the leadership principles set out in the Code. The core activities of the Board and its Committees are planned on an annual basis and this forms the basic structure within which the Board operates. The Board has adopted formal terms of reference which reflect the principles contained in the Code, and cover the following:

- Strategy – reviewing and agreeing strategy
- Performance – monitoring the performance of the Group and also evaluating its own performance,
- Standards and values – setting standards and values to guide the affairs of the Group,
- Oversight – ensuring an effective system of internal controls is in place, ensuring that the Board receives timely and accurate information on the performance of the Group and the proper delegation of authority and
- People – ensuring the Group is managed by individuals with the necessary skills and experience and that appointments to the Board are managed effectively

The terms of reference also sets out the separate and distinct roles of the Chairman and the Chief Executive

The Board appoints the Chief Executive and monitors his performance in leading the Company and providing operational and performance management in delivering the agreed strategy. Specifically, he is responsible for developing, for the Board's approval, appropriate values and standards to guide all activities undertaken by the Company.

The approval of acquisitions for the most part is a matter reserved for the Board, save that it delegates to the Chief Executive the responsibility for such activities to a specified level of authority. Similarly, there are authority levels covering capital expenditure which can be exercised by the Chief Executive. Beyond these levels of authority, projects are referred to the Board for approval.

Other matters reserved to the Board include treasury policies, internal control, risk management and the appointment or removal of the Company Secretary. The Company maintains appropriate insurance cover with respect to legal action against its Directors.

To ensure that non-Executive Directors can constructively challenge and help proposals on strategy, the Board has adopted a process of reviewing and approving the agreed strategy for the Company on a two yearly basis. In 2010, the Board members undertook a formal strategy development review at the Group's business in Edmonton, Canada. The next strategy meeting will be held in 2012.

### Effectiveness

#### The Board

The Board comprises three non-Executive Directors including the Chairman, and three Executive Directors, providing an appropriate range of skill and experience. The biographical details of the Board members are set out on pages 24 and 25. The Board has six scheduled meetings each year and meets more frequently as required. It met on six occasions during the year under review and attendance at these meetings is set out in the chart opposite.

The non-Executive Directors are appointed for specified terms and the details of their respective appointments are set out in the Remuneration Report on page 41.

The non-Executive Directors are determined by the Board to be independent in character and judgement and there are no relationships or circumstances which could affect, or appear to affect, a Director's judgement. The Chairman, John Rennocks was considered independent by the Board both at the time of his appointment as Director on 12 July 2002 and as Chairman on 7 January 2004 and in accordance with the Code, the ongoing test of independence for the Chairman is not appropriate. John Matthews is the Senior Independent Director.

All non-Executive Directors are advised of the likely time commitments at appointment. The ability of individual Directors to allocate sufficient time to the discharge of their responsibilities is considered as part of the Directors' annual evaluation process overseen by the Chairman. Any issues concerning the Chairman's time commitment are dealt with by the Nominations Committee, chaired for this purpose by the Senior Independent Director.

Non-Executive Directors are required to inform the Board of any changes to their other appointments.

There are three standing Committees of the Board to which various matters are delegated. Membership of the Committees is set out on pages 24 and 25 and terms of reference of each the Committees are set out on the Company's website ([www.diplomapl.com](http://www.diplomapl.com)). In order to ensure that undue reliance is not placed on particular individuals, the Board has decided that all its independent non-Executive Directors should serve on all Committees.

## Corporate Governance continued

### Report on Corporate Governance continued

During the year the Chairman has also held meetings with the non-Executive Directors, without the Executive Directors present

#### Appointments to the Board

The Board has established a Nomination Committee which leads the process for Board appointments and makes recommendations to the Board. The members of the Nomination Committee are John Rennocks, who is the Chairman, and the two non-Executive Directors. The Committee would be chaired by the Senior Independent Director on any matter concerning the chairmanship of the Company. The Company Secretary is the Secretary to the Committee.

The Nomination Committee has written terms of reference which are available on the Company's website covering the authority delegated to it by the Board. In carrying out its duties, the Committee will

- Take responsibility for identifying and nominating, for the approval of the Board, candidates to fill Board vacancies as and when they arise
- Before making an appointment evaluate the balance of skills, knowledge and experience on the Board and in the light of this evaluation, prepare a description of the role and capabilities required for a particular appointment
- In identifying suitable candidates, consider candidates on merit and against objective criteria and will take care that appointees have enough time available to devote to the position
- Consider candidates from a range of backgrounds, both internally and externally and may use the services of external advisors to facilitate the search

The Nomination Committee met once during the year under review at which proposals for development of the Board were discussed.

#### Information and professional development

An induction programme is agreed for all new directors aimed at ensuring that they are able to develop an understanding and awareness of the Company's core processes, its people and businesses. This process includes visits to various operating businesses. In addition to the induction programme that all directors undertake on joining the Board, a programme of director awareness of the businesses has been developed through periodic visits to the principal business locations and presentations by senior management of the businesses to the Board.

The Chairman, with the assistance of the Chief Executive and Company Secretary, is responsible for ensuring that Directors are supplied with information in a timely manner that is in a form and of a quality appropriate to enable them to discharge their duties. In the normal course of business, the Chief Executive makes an oral report to the Board at each meeting and information is provided and reported through formal Board Reports that include information on operational matters and strategic developments. There are also reports on the performance of Group operations, financial performance relative to the Budget, business development and investor relations.

The training needs of the Directors are periodically discussed at meetings with briefings as necessary on various elements of corporate governance and regulatory issues.

The Company Secretary acts as an advisor to the Board on matters concerning governance and regulatory issues and ensures compliance with Board procedures. All Directors have access to his advice and a procedure also exists for Directors to take independent professional advice at the Company's expense. No such advice was sought during the year. The appointment and removal of the Company Secretary and his remuneration are matters for the Board as a whole.

Historically, because of the relatively small size of the Company and to limit its costs, the Board has decided that the role of the Company Secretary should be combined with that of the Group Finance Director. As the Group continues to grow in both size and complexity, this appointment will be reviewed again by the Board in the new financial year.

#### Board evaluation

The Board's annual evaluations of effectiveness are completed internally using specifically designed evaluation forms and under the direction of the Chairman. This exercise encompasses an evaluation of the performance of the Board as a whole, as well as of the Committees and individuals. Feedback on Board performance is presented to a meeting of the Board which agrees actions and objectives for the following year.

#### Re-election

All Directors to the Board are subject to election by the shareholders at the first Annual General Meeting following their appointment by the Board. The Board has decided to adopt the provision of the new UK Corporate Governance Code, whereby all Directors will be subject to re-election annually commencing from the Annual General Meeting on 18 January 2012.

### Remuneration

The Board has delegated to the Remuneration Committee responsibility for agreeing remuneration policy and the remuneration of the Executive Directors. The Committee is formed exclusively of independent non-Executive Directors and the Report of the Remuneration Committee is set out on pages 32 to 41.

### Accountability

The Board is committed to providing shareholders with a clear assessment of the Company's financial position and prospects. This is achieved through this Annual Report & Accounts and through other periodic financial statements and announcements.

The arrangements established by the Board for the application of risk management and internal control principles are set out on page 31. The Board has delegated to the Audit Committee oversight of the Group's corporate reporting, management of the relationship with the auditors and review of the Company's risk management and internal control procedures, further details of which can be found in the Audit Committee report on page 30.

### Relations with Shareholders

The Company has a well developed investor relations programme managed by the Chief Executive and Group Finance Director. Through this programme the Company maintains regular contact with major shareholders to communicate clearly the Group's objectives and monitors movements in significant shareholdings.

Most shareholder contact is with the Chief Executive Officer and Group Finance Director through presentations made twice a year on the operating and financial performance of the Group and its longer term strategy. The Chief Executive Officer and Group Finance Director generally deal with questions from individual shareholders.

All financial and trading announcements are published immediately on the Company's website [www.diplomapl.com](http://www.diplomapl.com), including copies of the presentations made to analysts and key shareholders.

The non-Executive Directors are given regular updates as to the views of institutional shareholders and an independent insight is sought through research carried out twice a year by the Company's advisors.

Through these processes, the Board is kept abreast of key issues and the opportunity for shareholders to meet the Chairman or Senior Independent Director, separately from the Executive Directors, is available on request.

Notice of the Annual General Meeting is sent to shareholders at least 20 working days prior to the meeting and includes a separate resolution on each substantially separate issue. All shareholders have the opportunity to put questions at the Company's Annual General Meeting when the Chairman and Chief Executive Officer give a statement on the Group's performance during the year, together with a statement on current trading conditions. The Chairman of the Board and of the Remuneration and Audit Committees will normally be available to answer questions at the meeting.

In the absence of a poll being called, proxy votes cast are declared after each resolution dealt with on a show of hands. The results of the AGM resolutions are published on the Company's website.

## Corporate Governance continued

### Audit Committee

#### Number of Committee Meetings

Directors and attendance	2011
John Matthews (Chairman)	7/7
John Rennocks	7/7
Ian Grice	7/7

**John Matthews**  
Chairman of the Audit Committee

The Audit Committee comprises John Matthews (Chairman), John Rennocks and Ian Grice. Both John Matthews and John Rennocks are chartered accountants who have recent and relevant financial experience as required by the Code.

The meetings of the Committee are normally attended by the Executive Directors and the external auditor. In addition, the Chairman of the Committee meets privately with the external auditor at least twice each year. The Secretary to the Committee is Nigel Lingwood.

#### Role of the Committee

The main roles and responsibilities of the Committee are set out in written terms of reference which are available on the Company's website ([www.diplomaplc.com](http://www.diplomaplc.com)). They are as follows:

- to monitor the integrity of the financial statements of the Group and any formal announcements relating to the Group's financial performance, reviewing significant financial judgements contained therein,
- to review the Group's internal controls systems and risk management procedures,
- to make recommendations to the Board, for it to put to shareholders for approval in general meeting, in relation to the appointment, re-appointment and removal of the external auditor and to approve the terms of engagement of the external auditor,
- to review and monitor the external auditor's independence and objectivity and the effectiveness of the audit process taking into consideration relevant UK professional and regulatory requirements,
- to develop and implement policy on the engagement of the external auditor to supply non-audit services, taking into account relevant guidance regarding the provision of non-audit services by the external auditor,
- to report to the Board, identifying any matters in respect of which it considers that action or improvement is needed and making recommendations as to the steps to be taken, and
- to consider annually whether there is a need for a formal internal audit function and make recommendation to the Board.

In addition, the Audit Committee has an important role to play through its responsibility for, and oversight of, the auditor relationship and auditor independence. The Committee reviewed the audit engagement in 2008 and following an audit tender process, recommended to the Board the appointment of Deloitte LLP as auditor to the Company and Group.

The Committee has also established a set of guidelines covering the type of non-audit work that can be assigned to the external auditor. These relate to further assurance services – where the auditor's detailed knowledge of the Group's affairs means that they may be best placed to carry out such work. This extends to, but is not restricted to, shareholder and other circulars, regulatory reports, and on occasions, work in connection with disposals. Work in connection with acquisitions, including due diligence reviews, is generally not provided by the auditor, but is placed with other firms.

Taxation services are generally not provided by the auditor, a separate firm is retained to provide tax advice, including any assistance with tax compliance matters generally, except in Canada and Denmark, where the auditor provides some assistance on the tax computations.

In other circumstances, proposed assignments are put out to tender and decisions to award work taken on the basis of demonstrable competence and cost effectiveness.

The Committee receives an annual report which provides details of any assignments and related fees carried out by the auditor in addition to their normal audit work, and these are reviewed against the above guidelines.

The Committee has also formally reviewed and approved the arrangements by which Company employees may, in confidence, raise concerns about possible irregularities in financial reporting or other matters (so called "whistleblowing" procedures).

### Activities During the Year

The Audit Committee assists the Board in assuring the integrity of the financial statements and related disclosures

During the current year the Committee carried out the following work

- at its meetings in May and November, the Committee reviewed the Interim Report and the Annual Report & Accounts respectively. On both occasions, the Committee received reports from the Group Finance Director and from the external auditor identifying any accounting or judgemental issues requiring its attention,
- in September the Committee met with the external auditor to discuss their audit plan process,
- in January and August the Committee met to approve formal Interim Management Statements which were released to the market, in accordance with the Disclosure and Transparency Rules, and
- the Committee met on two further occasions during the year to review Trading Updates which the Company issued to the market

During the meetings, the Committee reviewed the information included in the Annual Report & Accounts to ensure that the information provided a fair review of the Group's business. It also reviewed the external audit management letter and the procedures designed to ensure that the external auditor was aware of all "relevant audit information", as required by the Companies Act 2006

The Committee also assessed the effectiveness of the external audit process and the report on the external auditor's own quality control procedures. This assessment covers all aspects of the audit service provided by the Company's external auditor

### Risk Management and Internal Control

The Committee is responsible for reviewing the effectiveness of the Group's system of internal control. The system of internal control is designed to manage rather than eliminate the risk of failure to achieve business objectives and can only provide reasonable and not absolute assurance against material misstatement or loss

The Board has established a clear organisational structure with defined authority levels. The day to day running of the Group's business is delegated to the Executive Directors of the Company. The Executive Directors visit each operating unit on a regular basis and meet with both operational and finance management and staff

Key financial and operational measures are reported on a weekly and/or monthly basis and are measured against both budget and interim forecasts which have been approved and reviewed by the Board. On an annual basis, each business unit is required to prepare a risk

assessment process on the key strategic operational, financial and accounting risks to identify, evaluate and manage the significant risks to the Group's business. They include common definitions of risk and ensure, as far as practicable, that the policies and procedures established by the Board are appropriate to manage the perceived risks to the Group. These assessments are supplemented by a detailed evaluation of the key financial controls of the business units which are critically reviewed by the Group's internal auditor. The Committee will annually review the results of these assessments and identify the key strategic and operating risks of the Group. During the year, the risk assessment process revealed no significant risks of which the Board was not previously aware.

The risks and uncertainties which are currently judged to have the largest potential impact on the Group's long term performance are set out on pages 20 to 23

The Committee has reviewed the effectiveness of the Group's risk management and internal control systems. Taking into account the processes that have been designed and implemented for 2011, the Board, with the advice of the Committee, has reviewed the effectiveness of the risk management and internal control systems for the period from 1 October 2010 to the date of this report and is satisfied that the Group has in place effective risk management and internal control systems

### Internal Audit

The Group's finance department includes a full time internal auditor and a full programme of internal audit visits has been completed during the year. The scope of work carried out by internal audit generally focuses on the internal financial controls and risk management procedures operating within each business. Written reports are prepared on the results of each visit which sets out weaknesses identified during the work, together with recommendations to improve the control environment. These reports are reviewed and discussed with the Executive Directors

At the conclusion of the year the internal auditor reports to the Committee on the results of the audit work carried out in the year and agrees an audit plan for the following financial year. There were no significant weaknesses identified during these audits, but a number of recommendations were made to improve internal review processes and risk management procedures, particularly in businesses where the opportunity to segregate duties was limited

The Committee continues to keep under review the need for a fully independent internal audit function in the Group. The Committee remains satisfied that the Group's system of internal control is appropriate for a group of the size and nature of Diploma PLC and the Committee's current view is that a separate formal independent internal audit function is not necessary

## Corporate Governance continued

### Remuneration Report

#### Number of Committee Meetings

Directors and attendance	2011
Ian Grice (Chairman)	4/4
John Rennocks	4/4
John Matthews	4/4

**Ian Grice**  
Chairman of the Remuneration Committee

On behalf of the Board I am pleased to present the report on remuneration for 2011 for which the Board will be seeking approval from shareholders at the Annual General Meeting

Diploma PLC's remuneration policy continues to be focused on attracting, retaining and motivating the executive talent required for the delivery of the Group's growth strategy in a competitive international market, while ensuring that remuneration is linked to the long-term performance of the Group

The Committee pays attention to the evolution of best corporate governance practice in the design of its remuneration framework and believes that the Group's overall remuneration policy continues to be appropriate

There continues to be a strong emphasis on performance related awards and the Committee took the opportunity to enhance this element of remuneration in adopting replacement long-term incentive arrangements earlier this financial year

The Committee was satisfied that the previous Long Term Incentive Plan ("LTIP") which was due to expire in 2011, had been very effective in driving performance and that it provided an appropriate incentive for achieving upper quartile performance versus peers, however the Committee took the view that there should be some

tougher targets, but also an incentive to deliver performance beyond this level

The Committee, having taken advice from its independent advisers, Kepler Associates, decided to adopt a new Performance Share Plan ("PSP") with a structure similar to the previous LTIP, with performance measured against earnings per share ("EPS") and total shareholder return ("TSR") However it was felt appropriate to introduce tougher EPS targets and to link the TSR target to an absolute return above the median performance of the FTSE 250 Index

The Committee also decided to introduce a Share Matching Plan ("SMP") to expand the range of performance which is incentivised and to further align the interests of Executive Directors with those of shareholders by requiring Executive Directors to invest further in the Company's shares

Having consulted with shareholders on these proposals, the Committee was pleased to receive approval from shareholders for the new PSP and SMP collectively the "new LTIP", earlier this year at the Annual General Meeting

There have been no further changes made to the Company's remuneration policies during this current year

**Ian Grice**  
Chairman

#### Historical TSR performance

The graph opposite shows Diploma's TSR performance for the five year period ended 30 September 2011 (calculated in accordance with the Directors' Remuneration Report Regulations 2002 (the "Regulations")) against the FTSE 250 index

Growth in the value of a hypothetical £100 holding over five years

TSR is defined as the return on investment obtained from holding a company's shares over a period. It includes dividends paid, the change in the capital value of the shares and other payments to or by shareholders within the period

### Remuneration Committee

The Committee's principal responsibilities are

- setting, reviewing and recommending to the Board for approval the Group's overall remuneration policy and strategy
- setting, reviewing and approving individual remuneration arrangements for the Chief Executive and Executive Directors, including terms and conditions of employment and any changes,
- reviewing and monitoring remuneration arrangements for the senior managers of the operating businesses, including terms and conditions of employment and any policy changes, and
- approving the rules and launch of any Group share-based incentive plan, and the granting of awards under any such plan

The full terms of reference of the Committee can be found on the Diploma PLC website ([www.diplomaplc.com](http://www.diplomaplc.com)) and copies are available on request

Bruce Thompson, Chief Executive, attends meetings by the invitation of the committee to provide advice to the Committee to help it to make informed decisions. Nigel Lingwood, Company Secretary, attends meetings as Secretary to the Committee.

The Committee also holds meetings without management and receives information and independent executive remuneration advice from Kepler Associates, an external consultancy appointed by the Committee. During 2010, Kepler Associates provided advice to the Committee on incentive schemes and other remuneration issues. Kepler Associates does not advise the Group on any other issues.

Ashurst LLP also provides legal advice to the Committee on executive incentive schemes (as well as providing other legal services to the Group).

### Executive Directors

#### Remuneration policy

In defining the Group's remuneration policy the Committee takes into account advice received from external consultants and also the principles and best practice guidelines set by regulators and institutional shareholder bodies including the Association of British Issuers ("ABI"). The Committee has also followed the principles of Section D of the UK Corporate Governance Code that relate to remuneration.

The current intention is that the framework of this remuneration policy will apply for future years.

#### Performance based rewards

The Company has a well-developed Group-wide performance management system which ensures that senior managers are rewarded based on performance. For Executive Directors, the Company operated the following performance-related incentive arrangements in 2011:

- an Annual Performance Bonus Scheme – designed to focus executives on the business priorities of the financial year and to reinforce individual and Group performance objectives, and
- Long-Term Incentives – designed to reward and retain Executives over the longer term while also aligning their interests with those of the Company's shareholders. For awards made in January 2011, Executive Directors received grants of PSP and SMP awards. These awards aim to motivate participants to maximise Adjusted EPS and TSR as measured against the FTSE mid-250 Index, excluding Investment Trusts (the "FTSE 250 index").

The two incentive arrangements complement each other and enable the measurement and reward of both short and long-term performance. In particular, the Committee considers that these complementary incentive arrangements take appropriate account of business risk and align the reward arrangements of the Executive Directors with the delivery of sustained returns to shareholders. The Committee continues to consider that the three-year vesting period for its long-term incentives is appropriate.

The FTSE 250 index was chosen because this is a recognised broad equity market index of which the Company is now a member.

## Corporate Governance continued

### Remuneration Report continued

#### Shareholding guidelines

The Committee has adopted guidelines for Executive Directors, to encourage substantial long-term share ownership. These specify that, over a period of five years from the date of appointment, the Chief Executive should build up, and then retain, a holding of shares with a value equivalent to 200% of base salary. The guideline holding for other Executive Directors should be 100% of base salary. The guidelines also require that in relation to the long-term incentive awards, vested shares (net of tax) should be retained by the individual until the required shareholding level is reached.

Shareholdings at 30 September 2011 against guidelines

- Guideline holdings
- Actual holdings

The chart above sets out the percentage of base salary held in shares by each of the Executive Directors, as compared with the guidelines.

#### Components of remuneration

The table on page 35 summarises the components of reward for Executive Directors of Diploma PLC.

The current remuneration package for Executive Directors comprises fixed and variable components. The variable components are the incentive arrangements referred to above and the fixed components are base salary and benefits (including pensions entitlements).

The average proportion of total remuneration that was performance-related in 2011 is illustrated by the chart shown below. This shows that a significant proportion of each Executive Director's total remuneration is performance-related at the target performance level. For stretch performance, the proportion of total remuneration that is performance-related is higher still. In estimating the relative contribution of those elements of remuneration that are performance related and those that are not (as required by Regulations), a number of assumptions have had to be made about the Company's share price growth over the next three years and TSR performance relative to the FTSE 250 index.

Composition of remuneration package for Executive Directors  
As an average % of total remuneration at target and stretch performance

- Variable cash and share-based incentives
- Fixed base salary, benefits and pension

#### Senior executives below the Executive Directors

The policies and practices with regard to the remuneration of senior executives below the Executive Directors are generally treated consistently with the Executive Directors. These senior executives all have a significant portion of their reward package linked to performance. Annual bonuses are linked to short term financial targets which are similar to the targets for the Executive Directors. They also participate in cash based long-term incentive plans which are focused on the operating profit growth of their businesses over rolling three year periods. The Committee reviews and monitors the senior executive remuneration arrangements.

#### Executive Directors' base salaries

Executive Directors' salaries are reviewed each year, with any changes normally taking effect from 1 October. This review takes into account market competitiveness, individual performance and experience.

The base salary increases for the Executive Directors which took effect from 1 October 2010 are summarised in the table below. The salary increases awarded to the Executive Directors were in line with the average percentage base salary increases awarded across the Group.

Executive Director	Base salary at	Base salary at	% Increase
	30 Sep 2011	30 Sep 2010	
	£ 000	£ 000	
Bruce Thompson	360	345	4.3
Iain Henderson	220	210	4.8
Nigel Lngwood	230	220	4.5

The Committee has regard to reward levels and practices in the Company's businesses when determining remuneration levels for Executive Directors. In determining the annual base salary increases which applies from 1 October the Committee also considered the range of salary increases applying across the Group.

#### Annual performance bonus

The annual performance bonus is a cash based scheme designed to reward Executive Directors for meeting stretching shorter term performance targets. At the start of the year (1 October), the Board sets stretching financial performance targets relating to Adjusted EPS, operating margins, free cash flow and return on trading capital employed ("ROTCE"). Individual objectives are also set for the Chief Operating Officer and the Group Finance Director relating to factors including operational performance and business development activities.

At the end of the financial year, the Committee meets to assess the performance of each Executive Director against the financial and individual objectives. Bonuses are paid in cash in December.

## Components of Remuneration

### Summary of Reward components of Executive Directors

Component	Aim	Description	Further detail
Fixed Base Salary	<p>Attract and retain talent by ensuring that salaries are competitive</p> <p>Reflect the individual's experience and role within the Group</p>	Benchmarked against levels of pay awarded elsewhere in sector and FTSE index	<p>Paid monthly in cash</p> <p>Reviewed annually with increases taking effect from 1 October</p>
Benefits Core	Designed to be competitive within the market	Core benefits include pension contributions (or cash alternative) life assurance annual leave and medical insurance	Pension contributions paid at 20% (2010 20%) of base salary and paid directly into personal savings schemes or as cash alternative
Additional	–	These include cash in lieu of a company car and cash bonuses in lieu of dividends forgone on unexercised but vested 2004 LTIP awards	–
Variable Annual Performance Bonus	Designed to focus Executive Directors on achievement of the annual budget and other business priorities for the financial year	<p>Maximum 100% of salary for the Chief Executive Officer and 80% for other Executive Directors</p> <p>On target bonus is 60% for the Chief Executive Officer and 50% for the other Executive Directors</p>	<p>Dependent on specified financial metrics of the Group for the Chief Executive Officer</p> <p>For other Executive Directors 75% is based on the financial metrics of the Group with the remaining 25% subject to achievement of specific personal objectives</p>
Long Term Incentives – Share Awards	<p>Incentivise Executive Directors to achieve superior returns and long-term value growth</p> <p>Align the interests of the Executive Directors and shareholders through building a shareholding</p> <p>Performance assessed over rolling three-year performance periods</p>	<p>The final award under the 2004 LTIP was made on 18 November 2009. No further awards will be made under the 2004 LTIP</p> <p>The 2008 awards vested on 30 September 2011, as set out on page 39</p> <p>The outstanding 2004 LTIP awards will vest on 30 September 2012</p> <p>The 2004 LTIP was replaced by the new LTIP following approval by shareholders at the AGM on 12 January 2011. The first awards under the new LTIP will vest on 30 September 2013</p>	<p>Awards are discretionary</p> <p>Awards do not vest until the third anniversary of the date of grant</p> <p>If employment ceases during three-year vesting period, award will normally lapse</p>

## Corporate Governance continued

### Remuneration Report continued

#### Long-term incentive plans

The Company operates long term incentive arrangements for Executive Directors. These are designed to reward and retain Executive Directors over the longer term, while also aligning their interests with those of Diploma PLC shareholders.

The Diploma PLC LTIP ("2004 LTIP"), having been in operation over a number of years, expired in 2011. It was replaced by the new LTIP comprising two incentive schemes, the Diploma PLC 2011 Performance Share Plan ("PSP") and the Diploma PLC 2011 Share Matching Plan ("SMP"), following approval by the shareholders at the Company's annual general meeting on 12 January 2011.

The 2004 LTIP and the PSP which replaces it, operate in a similar way for Executive Directors of the Company. They both provide for a grant of conditional awards of a specified number of ordinary shares in the Company, or an option to acquire a specified number of shares at an exercise price determined by the Committee (which may be nil or a nominal amount). No payment is required for the grant of an award.

The SMP also operates for Executive Directors of the Company and again provides for a grant of conditional awards of a specified number of ordinary shares in the Company. In the case of the SMP however, an Executive Director must accept an invitation from the Committee to personally acquire or pledge shares for a period of three years. These acquired or pledged shares are held by a nominee for an Executive Director and will be released at the end of the three year performance period applying to the awards.

Awards, which are normally granted annually, must generally be made within 42 days after the announcement of the Company's annual results. When making the decision on the level of award, the Committee takes into consideration a number of factors, including the face value of the award and plan dilution limits.

The face value of an award is equal to the number of shares, or shares under option, multiplied by the relevant share price. The relevant share price will be the mid-market closing share price on the day before the award (however for the 2004 LTIP the share price was the average share price for the 30 days immediately preceding the award). A face value limit of 100% of base salary applies to each PSP or 2004 LTIP award to Executive Directors in normal circumstances. A face value limit of up to 100% of base salary is applied in respect of SMP awards.

All awards will normally vest three years after the date of grant. The vesting of awards is conditional on:

- continued employment,
- the Company's growth in Adjusted EPS over a three year performance period, and
- the Company's TSR performance over a three year performance period.

The latter two performance conditions apply to each award so that the vesting of 50% of the award is based on growth in Adjusted EPS and 50% of the award is based on the relative TSR performance. Each performance condition is measured over a three year period commencing on the first day of the financial year in which the award is made. There is no retesting of either performance metric.

The first performance condition is that the average annual compound growth in the Company's Adjusted EPS over the three consecutive financial years, following the year prior to the grant, must exceed the annual compound growth rate in the UK Retail Price Index ("RPI") over the same period as set out below.

Adjusted EPS growth (over 3 years)	% of awards vesting		
	New LTIP		2004 LTIP
	PSP	SMP	
RPI + 15% p a or above	100	200	100
RPI + 12% p a	100	100	100
RPI + 5% p a	45.5	45.5	100
RPI + 3% p a	30	30	30
Below RPI + 3% p a	NIL	NIL	NIL

Where the Company's Adjusted EPS performance is between these percentage bands, vesting of the award is on a straight line basis.

For the purposes of this condition, EPS will comprise adjusted EPS as defined in note 2 to the consolidated financial statements. The definition of adjusted EPS remains consistent with the definition of EPS approved by the Remuneration Committee in previous years.

The second performance condition compares the growth of the Company's TSR over a three year period to that of the companies in the FTSE 250 index as set out below.

TSR relative to FTSE 250 Index (over 3 years)	% of awards vesting		
	New LTIP		2004 LTIP
	PSP	SMP	
Median + 15% p a or greater	100	200	(a)
Median + 12% p a	100	100	(a)
Median	30	30	30
Below Median	NIL	NIL	NIL

(a) Under the 2004 LTIP the TSR condition is based on the ranking of the Company's performance in the comparator group, rather than on absolute performance. Where the Company's TSR performance ranks in the top quartile of the comparator group 100% of the awards will vest.

Where the Company's relative TSR performance is between the median and the maximum performance condition, vesting of the award is on a straight line basis.

At 30 September 2011, the award made under the 2004 LTIP on 17 December 2008 crystallised and 100% of the award vested as nil paid options. These options are exercisable by each individual at a price of £1 up until 17 December 2018. An award made under the 2004 LTIP on 18 November 2009 remains outstanding and will

crystallise at the end of the performance period at 30 September 2012. Awards under the PSP and SMP were made on 24 and 27 January 2011 respectively, to Bruce Thompson, Iain Henderson and Nigel Lingwood. The amount of shares that vest under these Awards will be determined at the completion of the three year performance period at 30 September 2013. Full details of all of these awards are set out on pages 38 and 39.

#### **Dilution**

In any ten-year period, the number of shares which may be issued or placed under option under any executive share plan established by the Company may not exceed 5% of the issued ordinary share capital of the Company from time to time. In any ten-year period, the aggregate number of shares which may be issued or placed under option, under all share plans established by the Company, may not exceed 10% of the issued ordinary share capital of the Company, from time to time.

#### **Change of control**

In the event of a change in control, vesting of award shares under the Company's long-term incentive plans is not automatic and would depend on the extent to which performance conditions had been met at that time. Time pro-rating will apply if the Committee considers it appropriate, given the circumstances of the change of control.

#### **Dividend accrual**

The Committee may decide, on or before the grant of an award, that on exercise of the award, the participant may receive, in addition to the shares to which he then becomes entitled, a payment equal in value to the aggregate amount of the dividends (excluding any tax credit) which would have been paid to the participant in respect of those shares between the date on which the award vests and the option period commences and the date on which the option is exercised, as if they had been beneficially owned by him over that period. The payment may be made in cash or in an equivalent number of shares.

#### **Pensions**

The pension arrangements for Executive Directors are set out on page 40.

#### **Service contracts**

The Executive Directors' service contracts, including arrangements for early termination, are carefully considered by the Committee and are designed to recruit, retain and motivate directors of the quality required to manage the Company. The Committee considers that a rolling contract with a notice period of one year is appropriate.

The Executive Directors' service contracts contain provisions for compensation in the event of early termination or change of control, equal to the value of salary and contractual benefits for the notice period.

However when calculating termination payments, the Committee takes into account a variety of factors, including individual and Company performance, the obligation for the Director to mitigate his or her own loss (for example, by gaining new employment) and the Director's length of service. Further details of the Executive Directors' service contracts can be found on page 40.

The Committee considers that these provisions assist with recruitment and retention and that their inclusion is therefore in the best interests of shareholders.

## Corporate Governance continued

### Remuneration Report continued

The following section of this Report provides details of the remuneration, service contracts or letters of appointment and share interests of all the Directors for the year ended 30 September 2011.

#### Executive Directors' remuneration

Individual remuneration for the year ended 30 September 2011

	Fixed emoluments		Performance	2011 Total £000	2010 Total £000
	Salary £000	Taxable benefits <sup>(a)</sup> £000	based bonus <sup>(b)</sup> £000		
Bruce Thompson	360	19	360	739	704
Iain Henderson	220	14	176	410	389
Nigel Lingwood	230	16	184	430	408

- (a) Taxable benefits include medical insurance, life assurance, cash allowance in lieu of a car and a dividend entitlement on 2004 LTIP shares which have vested.  
 (b) The performance based bonus represents amounts payable only in respect of the 2011 incentive year and will be paid in December 2011.

#### Executive Directors' interests in shares under the Diploma PLC 2011 Performance Share Plan

	Market price at date of award	Shares over which awards granted during the year	End of performance period	Vesting date	Shares over which awards held as at 30 Sep 2011
<b>Bruce Thompson</b> 24 January 2011	292.50p	123,077	30 Sep 2013	Nov 2013	123,077
<b>Iain Henderson</b> 24 January 2011	292.50p	75,214	30 Sep 2013	Nov 2013	75,214
<b>Nigel Lingwood</b> 24 January 2011	292.50p	78,632	30 Sep 2013	Nov 2013	78,632

- (a) Executive Directors received grants of Performance Share Plan awards in January 2011 in the form of nil-cost options. Under normal circumstances, the awards will not vest and the options will not become exercisable until after the end of the three-year vesting period which began on the first day of the financial year in which the award is made, following assessment of the performance conditions and provided the Director remains in employment. Options are exercisable until the tenth anniversary of the award date. The level of vesting is dependent on the achievement of specified performance criteria at the end of the three-year performance period. The performance conditions for the 2011 awards are set out on page 36.

#### Executive Directors' interests in shares under the Diploma PLC 2011 Share Matching Plan

	Market price at date of award	Pledged investment shares	Shares over which awards granted during the year	End of performance period	Vesting date	Shares over which awards held as at 30 Sep 2011
<b>Bruce Thompson</b> 27 January 2011	292.50p	30,154	123,077	30 Sep 2013	Nov 2013	123,077
<b>Iain Henderson</b> 27 January 2011	292.50p	18,427	75,214	30 Sep 2013	Nov 2013	75,214
<b>Nigel Lingwood</b> 27 January 2011	292.50p	19,265	78,632	30 Sep 2013	Nov 2013	78,632

- (a) Executive Directors received grants of Share Matching Plan awards in January 2011 in the form of nil-cost options. Under normal circumstances, the awards will not vest and the options will not become exercisable until after the end of the three-year vesting period which began on the first day of the financial year in which the award is made, following assessment of the performance conditions and provided the Director remains in employment. Options are exercisable until the tenth anniversary of the award date. The level of vesting is dependent on the achievement of specified performance criteria at the end of the three-year performance period. The performance conditions for the 2011 awards are set out on page 36.  
 (b) Under the Share Matching Plan, Executive Directors are required to pledge shares for a minimum period of three years. These shares are pledged on an after-tax basis; awards are made on a pre-tax basis.

### Executive Directors' interests in shares under the Diploma PLC 2004 Long Term Incentive Plan

	Market price at date of award	Shares over which awards held as at 1 Oct 2010	Shares in respect of which awards vested at 30 Sep 2011	End of performance period	Vesting date	Shares over which awards held as at 30 Sep 2011
<b>Bruce Thompson</b>						
17 December 2008	123 0p	276 423	<b>276,423</b>	30 Sep 2011	Nov 2011	–
18 November 2009	168 5p	204 748	–	30 Sep 2012	Nov 2012	<b>204,748</b>
<b>Iain Henderson</b>						
17 December 2008	123 0p	168 293	<b>168,293</b>	30 Sep 2011	Nov 2011	–
18 November 2009	168 5p	124 629	–	30 Sep 2012	Nov 2012	<b>124,629</b>
<b>Nigel Lingwood</b>						
17 December 2008	123 0p	168 293	<b>168,293</b>	30 Sep 2011	Nov 2011	–
18 November 2009	168 5p	130 564	–	30 Sep 2012	Nov 2012	<b>130,564</b>

- (a) Executive Directors were granted 2004 LTIP awards in December 2008 and November 2009 in the form of nil-cost options. Under normal circumstances the awards will not vest and the options will not become exercisable until after the end of the three-year vesting period which began on the first day of the financial year in which the award is made following assessment of the performance conditions and provided the Director remains in employment. Options are exercisable until the tenth anniversary of the Award provided the Director remains in employment. The level of vesting is dependent on the achievement of specified performance criteria at the end of the three-year performance period. The performance conditions for the 2008 and 2009 awards are set out on page 36.
- (b) The award which vested as at 30 September 2011 represented 100% of the LTIP award which was granted on 17 December 2008.
- Under the first performance condition the average annual compound growth rate in the Company's adjusted EPS (as defined on page 50) over the three year period ended 30 September 2011 was 20.4% pa this compares with an annual compound growth rate in RPI +5.0% over the same period of 7.9% pa. Accordingly 100% of the shares relating to this award (representing 50% of the total award) vested unconditionally.
  - Under the second performance condition the Company's TSR grew 139.1% over the three year period ended 30 September 2011 this growth gave the Company a ranking of 12 in the comparator group and put the Company in the 94 percentile. The median TSR was 61.7% and the lower threshold of the upper quartile was 96.6%. Accordingly 100% of the shares relating to this part of the award (representing 50% of the total award) vested unconditionally.
- (c) Awards vest in the form of nil paid options to acquire shares in the Company for aggregate consideration of £1. Set out in the table below are the number of options held by each Director which have not yet been exercised. The closing price of an ordinary share at 30 September 2011, which is the date the awards vested, was 319.0p.

### Executive Directors' interests in options over shares which have vested under the Diploma PLC 2004 Long Term Incentive Plan

	Options as at 1 Oct 2010	Exercised in year	Vested in year	Options as at 30 Sep 2011	Exercise price	Earliest normal exercise date	Expiry date
Bruce Thompson	178,225	(61,539) <sup>(a)</sup>	–	<b>116,686</b>	£1	Nov 2010	Nov 2017
	–	–	276 423	<b>276,423</b>	£1	Nov 2011	Dec 2018
Iain Henderson	106 715	(37 606) <sup>(b)</sup>	–	<b>69,109</b>	£1	Nov 2010	Nov 2017
	–	–	168 293	<b>168,293</b>	£1	Nov 2011	Dec 2018
Nigel Lingwood	106 715	(39 316) <sup>(c)</sup>	–	<b>67,399</b>	£1	Nov 2010	Nov 2017
	–	–	168 293	<b>168,293</b>	£1	Nov 2011	Dec 2018

- (a) The market price on 27 January 2011, the date of exercise, was 276.0p, the total gain before tax was £169,848.
- (b) The market price on 27 January 2011, the date of exercise, was 276.0p, the total gain before tax was £103,792.
- (c) The market price on 27 January 2011, the date of exercise, was 276.0p, the total gain before tax was £108,512.
- (d) The closing price of an ordinary share on 30 September 2011 was 319.0p (2010: 284.5p).
- (e) On 27 January 2011, a total of 70,615 shares which were subject to these exercises were sold to cover the tax liability (together with associated dealing costs) due on exercise. The market price at that time was 276.0p.

The closing price of an ordinary share on 30 September 2011 was 319.0p (2010: 284.5p). The range during the year was from 414.2p (high) to 259.2p (low). All market price figures are derived from the Daily Official List of the London Stock Exchange.

### Executive Directors' interests in ordinary shares

The Executive Directors' interests in ordinary shares of the Company at the start and end of the financial year were as follows:

	Interest in ordinary shares	
	As at 30 Sep 2011	As at 30 Sep 2010
Bruce Thompson	<b>1,155,154</b>	1,125,000
Iain Henderson	<b>470,031</b>	416,640
Nigel Lingwood	<b>194,265</b>	150,000

- (a) Interests include investment shares pledged under the Company's 2011 Share Matching Plan and shares held through personal saving vehicles.

As of 12 November 2011 there have been no changes to these interests in ordinary shares of the Company.

## Corporate Governance continued

### Remuneration Report continued

#### Pensions

The Executive Directors receive pension contributions from the Company which they may pay directly into personal savings vehicles or take as additional salary, subject to income tax

Pension contributions, which are equivalent to 20% (2010 20%) of base salary were as follows

	2011 £000	2010 £000
Bruce Thompson	72	69
Iain Henderson	44	42
Nigel Lingwood	46	44

No pension contributions were paid as additional salary during the year (2010 Nil)

In September 2010, the Company established an unregistered retirement benefits scheme known as the Diploma Holdings PLC Employer-Financed Retirement Benefits Scheme ("the Scheme"). The Scheme was established for Executive Directors and higher paid UK employees in the Group as an alternative to the employees' current pension arrangements and contains all the key features of a conventional registered pension plan. During the year, £111,000 of pension contributions received from the Company were paid into the Scheme relating to 2011 and earlier years. No contributions have been paid into the Scheme since 5 April 2011.

#### Executive Directors' service contracts

Details of the service contracts of the Executive Directors who served during the year are set out below

Executive Directors	Contract date	Unexpired term	Notice period	Compensation payable upon early termination
Bruce Thompson	13 July 2000	Rolling 1yr	1yr	1yr
Iain Henderson	1 August 2000	Rolling 1yr	1yr	1yr
Nigel Lingwood	3 July 2001	Rolling 1yr	1yr	1yr

#### Non-Executive Directors

The Board aims to recruit non-Executive Directors of a high calibre, with broad commercial, international or other relevant experience. Non-Executive Directors are appointed by the Board on the recommendation of the Nomination Committee. Their appointment is for an initial term of three years, subject to election by shareholders at the first general meeting following their appointment and commencing from 2011, subject to annual re-election thereafter. The terms of engagement of the non-Executive Directors are set out in a letter of appointment.

The basic annual fee paid in 2011 to non-Executive Directors is £35,000 (2010 £35,000). There are no additional fees payable for membership of, or chairing, a Committee of the Board or for acting as Senior Independent Director. The current remuneration policy for non-Executive Directors requires that fees are reviewed every two years by the Board, taking into account time commitment, competition for high-quality non-executive directors and market movements.

Non-Executive Directors are not eligible to participate in any of the Company's share schemes, incentive schemes or pension schemes.

#### Chairman

John Rennocks was appointed as a non-Executive Director of the Company with effect from 12 July 2002 and as Chairman with effect from 7 January 2004. He was re-appointed for a three-year term with effect from 14 January 2009, at which point his fee was increased to £70,000 per annum. In line with all Directors, John Rennocks' appointment will now be subject to annual re-election by shareholders at the annual general meeting. There is no notice period and no provision for payment in the event of early termination.

### Chairman and non-Executive Directors' letters of appointment

	Date of appointment or re-election	Expiry of term
John Rennocks	14 Jan 09	July 14
John Matthews	13 Jan 10	July 12
Ian Grice	12 Jan 11	Jan 13

The non-Executive Directors' letters of appointment do not contain any notice period or provision for compensation in the event of early termination of their appointment

### Non-Executive Directors' remuneration

Individual remuneration for the year to 30 September was as follows

	Salary/fees	
	2011 £000	2010 £000
John Rennocks	70	70
John Matthews	35	35
Ian Grice	35	35

### Non-Executive Directors' interests in ordinary shares

The non-Executive Directors' interests in ordinary shares of the Company at the start and at the end of the financial year were as follows

	Interests in ordinary shares	
	As at 30 Sep 2011	As at 1 Oct 2010
John Rennocks	103,766	73,776
John Matthews	12,420	-
Ian Grice	20,000	20,000

### Audit notes

In accordance with Section 421 of the Companies Act 2006 and the Regulations, the following sections of the report have been audited: Executive Directors' remuneration, Executive Directors' interests in the Diploma PLC 2011 Performance Share Plan, Executive Directors' interests in the Diploma PLC 2011 Share Matching Plan, Executive Directors' interests in the Diploma PLC 2004 Long Term Incentive Plan, Executive Directors' interests in options over shares which have vested under the Diploma PLC 2004 Long Term Incentive Plan, Executive Directors' interests in ordinary shares, non-Executive Directors' remuneration, non-Executive Directors' interests in ordinary shares, and the tables and notes in the Pensions section of the report. The remaining sections are not subject to audit.

By order of the Board

**Ian Grice**

Chairman of the Remuneration Committee  
21 November 2011

## Other Statutory Information

This section contains additional information which the Directors are required by law and regulation to include within the Annual Report & Accounts

### Shareholders

#### Incorporation and principal activity

Diploma PLC is domiciled in England and incorporated in England & Wales under Company Number 3899848. At the date of this Report there were 113,239,555 ordinary shares of 5p each in issue, all of which are fully paid up and quoted on the London Stock Exchange.

The principal activity of the Group is the supply of specialised technical products and services. A description and review of the activities of the Group during the financial year and an indication of future developments is set out on pages 4 to 23, the Review of Group Performance incorporates the requirements of the Companies Act.

#### Annual General Meeting

The Annual General Meeting will be held at midday on 18 January 2012 in the Brewers Hall, Aldermanbury Square, London EC2V 7HR. A Circular setting out the proposed resolutions, including a resolution to re-appoint Deloitte LLP as the auditor, will be set out in the Notice of the Annual General Meeting which is a separate document which will be sent to all Shareholders and published on the Group's website.

#### Substantial shareholdings

At 18 November 2011 the Company had been notified, pursuant to the Financial Service Authority's Disclosure and Transparency Rules, of the following notifiable voting rights in its ordinary share capital:

	Percentage of ordinary share capital
F&C Asset Management plc	8.27
Ameriprise Financial Inc	6.39
Mondrian Investment Partners Limited	6.02
IG International Management Limited	5.00
Newton Investment Management Limited	4.39
Legal & General Investment Management Limited	3.93

As far as the Directors are aware there were no other notifiable interests.

#### Share capital

The rights attaching to the Company's ordinary shares, as well as the powers of the Company's Directors, are set out in the Company's Articles of Association, copies of which can be obtained from the Company Secretary and are available on the Company's website at [www.diplomapl.com](http://www.diplomapl.com).

The Company is not aware of any agreements between shareholders that may result in restrictions on the transfers of securities and/or voting rights, other than those relating to the Company's Share Matching Plan described further below. No person holds securities in the Company carrying special rights with regard to

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

In accordance with the Listing Rules of the Financial Services Authority, all employees are required to seek approval of the Company before dealing in its shares.

#### Restrictions on transfer of shares

The Directors may refuse to register a transfer of a certificated share that is not fully paid, provided that the refusal does not prevent dealings in shares in the Company from taking place on an open and proper basis, or where the Company has a lien over that share. The Directors may also refuse to register a transfer of a certificated share unless the instrument of transfer is (i) lodged, duly stamped (if necessary), at the registered office of the Company or any other place as the Board may decide accompanied by the certificate for the share(s) to be transferred and/or such other evidence as the Directors may reasonably require to show the right of the transferor to make the transfer, (ii) in respect of only one class of shares, (iii) in favour of a person who is not a minor, infant, bankrupt or a person of unsound mind, or (iv) in favour of not more than four persons jointly.

Transfers of uncertificated shares must be carried out using CREST and the Directors can refuse to register a transfer of an uncertificated share in accordance with the regulations governing the operation of CREST.

Participants in the Company's Share Matching Plan pledge investment shares to a nominee for a period of three years, during which period these shares cannot be transferred. There are no other restrictions on the transfer of ordinary shares in the Company except certain restrictions which may from time to time be imposed by laws and regulations (for example insider trading laws) or where a shareholder with at least a 0.25% interest in the Company's certified shares has been served with a disclosure notice and has failed to provide with the Company with information concerning interests in those shares. Other than these shares held by participants of the Company's Share Matching Plan, the Directors are not aware of any agreements between holders of the Company's shares that may result in restrictions on the transfer of securities or on voting rights.

#### Shares held by the Diploma Employee Benefit Trust

Whilst ordinary shares are held within the Diploma Employee Benefit Trust, the voting rights in respect of those shares are exercisable by the trustees in accordance with their fiduciary duties. The Trustee of the Diploma Employee Benefit Trust also waives dividends on all shares held for the purposes of the Company's long-term incentive arrangements.

### Share allotment

A general allotment power and a limited power to allot shares in specific circumstances for cash otherwise than pro-rata to existing shareholders, were given to the Directors by resolutions approved at the Annual General Meeting of the Company held on 12 January 2011. These powers will expire at the conclusion of the 2012 Annual General Meeting and resolutions to renew the Directors' powers are therefore included within the Notice of the 2012 Annual General Meeting

### Authority to make market purchases of own shares

An authority to make market purchases of shares was given to the Directors by a special resolution at the Annual General Meeting of the Company held on 12 January 2011. In the year to 30 September 2011 the Company has not acquired any of its own shares. This authority will expire at the conclusion of the 2012 Annual General Meeting and a resolution to renew the authority is therefore included within the Notice of the 2012 Annual General Meeting

### Employees

#### Employees

Building and developing the skills, competencies, motivation and teamwork of employees is recognised by the Board as being key to achieving the Group's business objectives. The stability and commitment of the employees is demonstrated by the average length of service being 6.3 years (2010: 6.4 years) as shown in the chart below. In addition the number of working days lost to sickness is less than 1% a year (2010: 1%). These measures remain consistent across each of the Group's sectors

#### Key employee statistics

	2011	2010	2009
Number of employees	910	814	823
Females as % of total	32%	34%	34%
Length of service (years)	6.3	6.4	6.4
Average staff turnover	16.3%	15.0%	18.3%
Sick days lost per person	1.9	2.8	3.6

The Group values the commitment of its employees and recognises the importance of communication to good working relationships. The Group keeps employees informed on matters relating to their employment, on business developments and on financial and economic factors affecting the Group. This is achieved through management briefings, internal announcements, the Group's website and by the distribution of Preliminary and Interim Announcements and press releases. Copies of the Annual Review and Annual Report & Accounts are also made available in the operating businesses. This communication programme enables employees to gain a better understanding of the Group's business objectives and their roles in achieving them.

Both employment policy and practice in the Group are based on non-discrimination and equal opportunities. Ability and aptitude are the determining factors in the selection, training, career development and promotion of all employees. The Group remains supportive of the employment and advancement of disabled persons. Applications for employment by disabled persons are always fully considered, bearing in mind the respective aptitudes and abilities of the applicants concerned. If an employee is, or becomes disabled during their period of employment, the Group will, if necessary and to the extent possible, adapt the work environment to enable the employee to continue in their current position or retrain the employee for duties suited to their abilities following disablement. At 30 September 2011 the Group's employees included six who were disabled and two who were on long term sick leave.

Employment policies throughout the Group have been established to comply with relevant legislation and codes of practice relating to employment, health and safety and equal opportunities. The Group provides good quality working environments and facilities for employees and training and development appropriate to each of their roles.

#### Health and safety

The Group places a great deal of importance on the provision of clean, healthy and safe working conditions. In addition to compliance with all local regulations, the Group promotes working practices which protect the health and safety of its employees. Health and Safety matters are kept under regular review by local management who report on such matters to the Chief Operating Officer. During 2011, 16 employees (2010: 5) were reported as having suffered minor injuries at work, none of these injuries resulted in absence from work for more than three days. One employee (2010: 1) suffered a serious injury during the year and was absent from work for four days.

Health and safety training is part of the induction process for new employees. Specific training is given where relevant, for example regarding forklift truck operation and chemical handling, as well as general fire safety and first aid matters.

#### Environmental

The Group regards compliance with relevant environmental laws as an important part of its responsible approach to the environment and is committed to good environmental management practices throughout its operations. The Managing Directors, appointed by the Board, have responsibility for the environmental performance of their operating businesses and each subsidiary is required to implement initiatives to meet their responsibilities.

## Other Statutory Information continued

### Community

#### Relationships with suppliers, customers and other stakeholders

The Group recognises the obligation it has towards the parties with whom it has business dealings including customers, shareholders, employees, suppliers and advisors. Dealings with these groups depend upon the honesty and integrity of the Group's employees and every effort is made to ensure that a high standard of expertise and business principles is maintained in such dealings. Where appropriate, training is given to maintain and to raise standards.

The Group's policy towards suppliers is that each operating company is responsible for negotiating the terms and conditions under which they trade with their suppliers.

The Group does not have a formal code that it follows with regard to payments to suppliers. Group companies agree payment terms with their suppliers when they enter into binding purchasing contracts for the supply of goods and services.

Suppliers are, in that way, made aware of these terms. Group companies seek to abide by these payment terms when they are satisfied that the supplier has provided the goods or services in accordance with the agreed terms and conditions. At 30 September 2011 the amount of trade creditors shown in the Group balance sheet represents 51 days (2010: 51 days) of average purchases.

#### Community impact and involvement

The Group contributes to local worthwhile causes and charities and ensures that the Group's operations cause minimal negative impact within the community.

In common with all companies, the Group has limited resources and the amount of money available for charitable purposes varies over time.

The Group made donations for charitable purposes during the year which amounted to £26,050 (2010: £25,950). No political donations were made.

### Directors

#### Conflicts of interest

From 1 October 2008, the Directors became subject to a statutory duty under the Act to avoid a situation where they have, or could have, a direct or indirect interest that conflicts, or possibly could conflict, with the Company's interests. The Act allows directors of public companies to authorise conflicts and potential conflicts where appropriate, if the Articles of Association contain a provision to this effect. The Act also allows the Articles to contain other provisions for dealing with directors' conflicts of interest to avoid a breach of duty. At the 2009 AGM, revised Articles that contained such provisions were adopted.

#### Directors' and officers' liability insurance and indemnity

The Company has purchased insurance to cover its Directors and Officers against the costs of defending themselves in legal proceedings taken against them in that capacity and in respect of any damages resulting from those proceedings.

The Company also indemnifies its Directors and Officers to the extent permitted by law. Neither the insurance nor the indemnity provides cover where the Director or Officer has acted fraudulently or dishonestly.

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

Each of the Directors has reviewed this report and confirmed that so far as he is aware, there is no relevant audit information of which the Company's auditor is unaware and that he has taken all the steps that he ought to have taken as a Director in order to make himself aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

### Financial

#### Results and dividends

The profit for the financial year attributable to shareholders was £27.0m (2010: £21.5m). The Directors recommend a final dividend of 8.5p per ordinary share (2010: 6.2p), to be paid, if approved, on 25 January 2012. This, together with the interim dividend of 3.5p per ordinary share paid on 16 June 2011, amounts to 12.0p for the year (2010: 9.0p).

The results are shown more fully in the consolidated financial statement on pages 46 and 73 and summarised in the Financial Review on pages 17 to 19.

#### Directors' assessment of going concern

The Group's business activities, together with the factors likely to affect its future development, performance and position are set out in the section of the Report that deals with Group Performance on pages 4 to 23. The financial position of the Group, its cash flows, liquidity position and borrowing facilities are described in the Finance Review on page 18. In addition, pages 58 to 60 of the Annual Report & Accounts includes the Group's objectives, policies and processes for managing its capital, its financial risk management objectives, details of its financial instruments and hedging activities, and its exposures to credit risk and liquidity risk.

The Group has considerable financial resources together with a broad spread of customers and suppliers across different geographic areas and sectors, often secured with longer term agreements. As a consequence, the Directors believe that the Group is well placed to manage its business risks successfully, despite the current uncertain economic outlook.

After making enquiries, the Directors have a reasonable expectation that the Company and the Group 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 & Accounts.

#### Statement of Directors' responsibilities for preparing the financial statements

The Directors are responsible for preparing the Annual Report & Accounts, including the Group and Parent Company financial statements, in accordance with applicable law and regulations.

Company law requires the Directors to prepare Group and Parent Company financial statements for each financial year. Under that law the Directors are required to prepare Group financial statements in accordance with IFRSs as adopted by the European Union ("EU") and Article 4 of the IAS Regulations and have elected to prepare the Parent Company financial statements in accordance with United Kingdom Generally Accepted Accounting Standards (UK Accounting Standards).

The Group financial statements are required by law and IFRSs as adopted by the EU to present fairly the financial position and the performance of the Group, the Companies Act 2006 provides in relation to such financial statements, that references in the relevant part of that Act to financial statements giving a true and fair view are references to their achieving a fair presentation.

In preparing each of the Group and Company financial statements, the Directors are required to

- Select suitable accounting policies and then apply them consistently
- Make judgements and estimates that are reasonable and prudent
- For the Group financial statements state whether they have been prepared in accordance with IFRSs, as adopted by the EU
- For the Parent Company financial statements, state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the Parent Company financial statements
- Prepare the financial statements on the going concern basis, unless it is inappropriate to presume that the Group and the Parent Company will continue in business.

The Directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the Parent Company and enable them to ensure that its financial statements comply with the Companies Act 2006. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

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

#### Directors' Responsibility Statement

The Directors confirm that to the best of their knowledge

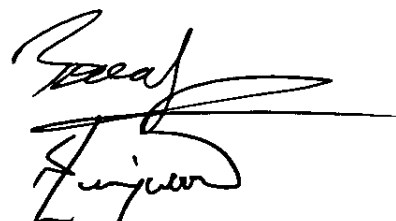
- the Group's consolidated financial statements, prepared in accordance with IFRSs as adopted by the EU and the Parent Company financial statements, prepared in accordance with UK Accounting Standards, give a true and fair view of the assets, liabilities, financial position and profit of the Group and Parent Company and the undertakings included in the consolidation taken as a whole and
- the Annual Report & Accounts 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 faced by the Group.

This responsibility statement was approved by the Board of Directors on 21 November 2011 and is signed on its behalf by

**BM Thompson**  
Chief Executive Officer

**NP Lingwood**  
Group Finance Director

Registered office  
12 Charterhouse Square  
London  
EC1M 6AX



## Consolidated Income Statement

For the year ended 30 September 2011

	Note	2011 £m	2010 £m
<b>Continuing businesses</b>			
Revenue	34	230.6	183.5
Cost of sales		(142.7)	(115.5)
<b>Gross profit</b>		<b>87.9</b>	<b>68.0</b>
Distribution costs		(5.5)	(4.4)
Administration costs		(42.0)	(35.0)
<b>Operating profit</b>	3	<b>40.4</b>	<b>28.6</b>
Financial expense net	6	(1.2)	(1.9)
<b>Profit before tax</b>		<b>39.2</b>	<b>26.7</b>
Tax expense	7	(11.6)	(8.8)
<b>Profit for the year from continuing businesses</b>		<b>27.6</b>	<b>17.9</b>
Profit from discontinued businesses		--	5.1
<b>Profit for the year</b>		<b>27.6</b>	<b>23.0</b>
Attributable to			
Shareholders of the Company		27.0	21.5
Minority interests	20	0.6	1.5
		27.6	23.0
<b>Earnings per share</b>			
	9		
Basic and diluted earnings – continuing		24.0p	14.6p
Basic and diluted earnings – discontinued		--	4.5p
Basic and diluted earnings – continuing and discontinued		24.0p	19.1p

## Alternative Performance Measures (note 2)

	Note	2011 £m	2010 £m
Operating profit		40.4	28.6
Add Acquisition related charges	11	4.8	3.5
<b>Adjusted operating profit</b>	34	<b>45.2</b>	<b>32.1</b>
(Deduct)/add Net interest (expense)/income	6	(0.3)	0.1
<b>Adjusted profit before tax</b>		<b>44.9</b>	<b>32.2</b>
<b>Adjusted earnings per share</b>	9	<b>27.9p</b>	<b>18.9p</b>

The notes on pages 50 to 73 form part of these financial statements

## Consolidated Statement of Comprehensive Income

For the year ended 30 September 2011

	Note	2011 £m	2010 £m
Profit for the year		276	230
Exchange rate adjustments on foreign currency net investments		(0.2)	1.9
Gains/(losses) on fair value of cash flow hedges		1.2	(0.4)
Actuarial losses on defined benefit pension schemes	25	(0.6)	(1.8)
Deferred tax on items recognised in equity	13	0.3	0.6
Other comprehensive income for the year		0.7	0.3
<b>Total comprehensive income for the year</b>		<b>28.3</b>	<b>23.3</b>
Attributable to			
Shareholders of the Company		27.7	21.8
Minority interests		0.6	1.5
		<b>28.3</b>	<b>23.3</b>

## Consolidated Statement of Changes in Shareholders' Equity

For the year ended 30 September 2011

	Note	Share capital £m	Translation reserve £m	Hedging reserve £m	Retained earnings £m	Total £m
<b>At 1 October 2009</b>		57	187	0.3	96.7	121.4
Total comprehensive income		-	1.9	(0.4)	20.3	21.8
Share-based payments	5	-	-	-	0.5	0.5
Purchase of minority interests	19	-	-	-	2.5	2.5
Future purchase minority interests	19	-	-	-	(0.6)	(0.6)
Purchase of own shares		-	-	-	(0.4)	(0.4)
Dividends	8	-	-	-	(9.1)	(9.1)
<b>At 30 September 2010</b>		<b>57</b>	<b>20.6</b>	<b>(0.1)</b>	<b>109.9</b>	<b>136.1</b>
Total comprehensive income		-	(0.2)	1.2	26.7	27.7
Share-based payments	5	-	-	-	0.7	0.7
Purchase of minority interests	19	-	-	-	12.1	12.1
Purchase of own shares		-	-	-	(1.6)	(1.6)
Dividends	8	-	-	-	(10.9)	(10.9)
<b>At 30 September 2011</b>		<b>57</b>	<b>20.4</b>	<b>1.1</b>	<b>136.9</b>	<b>164.1</b>

The notes on pages 50 to 73 form part of these financial statements

## Consolidated Statement of Financial Position

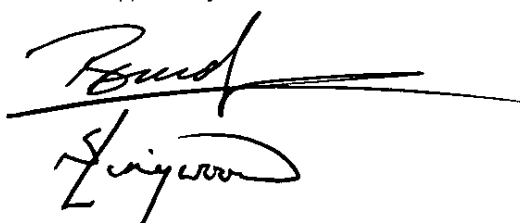
### As at 30 September 2011

	Note	2011 £m	2010 £m
<b>Non-current assets</b>			
Goodwill	10	871	673
Acquisition intangible assets	11	273	227
Other intangible assets	11	07	06
Property, plant and equipment	12	107	111
Deferred tax assets	13	28	24
		<b>1286</b>	<b>1041</b>
<b>Current assets</b>			
Inventories	14	384	320
Trade and other receivables	15	363	305
Cash and cash equivalents	17	178	301
		<b>925</b>	<b>926</b>
<b>Current liabilities</b>			
Trade and other payables	16	(352)	(323)
Current tax liabilities		(24)	(20)
Other liabilities	19	(08)	(130)
Borrowings	24	(56)	-
		<b>(440)</b>	<b>(473)</b>
<b>Net current assets</b>		<b>485</b>	<b>453</b>
<b>Total assets less current liabilities</b>		<b>1771</b>	<b>1494</b>
<b>Non-current liabilities</b>			
Retirement benefit obligations	25	(54)	(53)
Other liabilities	19	(23)	(12)
Deferred tax liabilities	13	(48)	(37)
<b>Net assets</b>		<b>1646</b>	<b>1392</b>
<b>Equity</b>			
Share capital		57	57
Translation reserve		204	206
Hedging reserve		11	(01)
Retained earnings		1369	1099
<b>Total shareholders' equity</b>		<b>1641</b>	<b>1361</b>
Minority interests	20	05	31
<b>Total equity</b>		<b>1646</b>	<b>1392</b>

The consolidated financial statements were approved by the Board of Directors on 21 November 2011 and signed on its behalf by

BM Thompson  
Chief Executive Officer

NP Lingwood  
Group Finance Director



The notes on pages 50 to 73 form part of these financial statements

## Consolidated Cash Flow Statement

For the year ended 30 September 2011

Continuing businesses	Note	2011 £m	2010 £m
<b>Cash flow from operating activities</b>			
Cash flow from operations	23	40.3	34.3
Interest (paid)/received net		(0.5)	0.1
Tax paid		(12.4)	(9.3)
<b>Net cash from operating activities</b>		<b>27.4</b>	<b>25.1</b>
<b>Cash flow from investing activities</b>			
Acquisition of subsidiaries (net of cash acquired)	21	(14.8)	(8.1)
Disposal of subsidiaries (net of cash disposed)	22	0.9	6.4
Deferred consideration paid	19	(0.9)	(0.4)
Purchase of property plant and equipment	12	(1.3)	(1.2)
Purchase of other intangible assets	11	(0.4)	(0.1)
<b>Net cash used in investing activities</b>		<b>(16.5)</b>	<b>(3.4)</b>
<b>Cash flow from financing activities</b>			
Acquisition of minority interests	20	(12.5)	(2.5)
Dividends paid to shareholders	8	(10.9)	(9.1)
Dividends paid to minority interests	20	(3.9)	(1.1)
Purchase of own shares		(1.6)	(0.4)
Proceeds from borrowings	24	5.4	–
<b>Net cash used in financing activities</b>		<b>(23.5)</b>	<b>(13.1)</b>
<b>Net cash used in discontinued businesses</b>		<b>–</b>	<b>(0.5)</b>
<b>Net (decrease)/increase in cash and cash equivalents</b>		<b>(12.6)</b>	<b>8.1</b>
Cash and cash equivalents at beginning of year		30.1	21.3
Effect of exchange rates on cash and cash equivalents		0.3	0.7
<b>Cash and cash equivalents at end of year</b>	17	<b>17.8</b>	<b>30.1</b>

## Alternative Performance Measures (note 2)

	2011 £m	2010 £m
<b>Free cash flow</b>		
Net (decrease)/increase in cash and cash equivalents	(12.6)	8.1
Add/(deduct) Dividends paid to shareholders	10.9	9.1
Dividends paid to minority interests	3.9	1.1
Acquisition of subsidiaries/minority interests	27.3	10.6
Deferred consideration paid	0.9	0.4
Proceeds from borrowings	(5.4)	–
<b>Free cash flow – continuing and discontinued businesses</b>	<b>25.0</b>	<b>29.3</b>
Add Free cash flow – discontinued businesses	–	0.5
<b>Free cash flow – continuing businesses</b>	<b>25.0</b>	<b>29.8</b>
<b>Net funds</b>		
Cash and cash equivalents	17.8	30.1
Borrowings	(5.6)	–
<b>Net funds</b>	<b>12.2</b>	<b>30.1</b>

The notes on pages 50 to 73 form part of these financial statements

# Notes to the Consolidated Financial Statements

## For the year ended 30 September 2011

### 1 General Information

Diploma PLC is a public limited company registered and domiciled in England and Wales and listed on the London Stock Exchange. The address of the registered office is 12 Charterhouse Square London EC1M 6AX. The consolidated financial statements comprise the Company and its subsidiaries (together referred to as the "Group") and were authorised by the Directors for publication on 21 November 2011. These statements are presented in UK sterling with all values rounded to the nearest one hundred thousand, except where otherwise indicated.

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as adopted by the European Union and in accordance with the Companies Act 2006 as applicable to companies reporting under IFRS. The financial statements of the Parent Company Diploma PLC have been prepared in accordance with "UK GAAP", and are set out in a separate section of the Annual Report & Accounts on pages 74 to 75.

### 2 Alternative Performance Measures

The Group uses a number of alternative (non-Generally Accepted Accounting Practice ("non-GAAP")) financial measures which are not defined within IFRS. The Directors use these measures in order to assess the underlying operational performance of the Group and as such these measures are important and should be considered alongside the IFRS measures. The following non-GAAP measures are referred to in this Annual Report & Accounts.

#### 2.1 Adjusted operating profit

At the foot of the consolidated income statement, "adjusted operating profit" is defined as operating profit before amortisation and impairment of acquisition intangible assets, acquisition expenses and adjustments to deferred consideration (collectively "acquisition related charges"). The Directors believe that adjusted operating profit is an important measure of the underlying operational performance of the Group.

#### 2.2 Adjusted profit before tax

At the foot of the consolidated income statement, "adjusted profit before tax" is separately disclosed being defined as profit before tax and before the costs of restructuring or rationalisation of operations, the profit or loss relating to the sale of property, fair value remeasurements under IAS 32 and IAS 39 in respect of future purchases of minority interests and acquisition related charges. The Directors believe that adjusted profit before tax is an important measure of the underlying performance of the Group.

#### 2.3 Adjusted earnings per share

"Adjusted earnings per share" is calculated as the total of adjusted profit less income tax costs but excluding the tax impact on the items included in the calculation of adjusted profit and the tax effects of goodwill in overseas jurisdictions less profit attributable to minority interests divided by the weighted average number of ordinary shares in issue during the year. The Directors believe that adjusted earnings per share provides an important measure of the underlying earning capacity of the Group.

#### 2.4 Free cash flow

At the foot of the consolidated cash flow statement "free cash flow" is reported being defined as net cash flow from operating activities after net capital expenditure on fixed assets and including proceeds received from business disposals but before expenditure on business combinations and dividends paid to both minority shareholders and the Company's shareholders. The Directors believe that free cash flow gives an important measure of the cash flow of the Group available for future investment.

#### 2.5 Trading capital employed

In the segment analysis in note 3 "trading capital employed" is reported being defined as net assets less cash and cash equivalents and after adding back retirement benefit obligations, deferred tax amounts in respect of future purchases of minority interests and adjusting for goodwill in respect of the recognition of deferred tax on acquisition intangible assets. Return on trading capital employed is defined as the adjusted operating profit divided by trading capital employed plus all historic goodwill and adjusted for the timing effect of major acquisitions and disposals. Return on trading capital employed at the sector level does not include historic goodwill. The Directors believe that return on trading capital employed is an important measure of the underlying performance of the Group.

### 3 Business Segment Analysis

For management reporting purposes the Group is organised into three main business segments: Life Sciences, Seals and Controls. These segments form the basis of the primary reporting format disclosures below. The principal activities of each of these segments is described in the review of Group Performance on pages 4 to 19. Segment revenue represents revenue from external customers, there is no inter-segment revenue. Segment results assets and liabilities include items directly attributable to a segment, as well as those that can be allocated on a reasonable basis.

	Life Sciences		Seals		Controls		Total	
	2011 £m	2010 £m	2011 £m	2010 £m	2011 £m	2010 £m	2011 £m	2010 £m
Revenue – existing businesses	65.4	55.4	80.0	60.1	76.2	68.0	221.6	183.5
– acquisitions	9.0	–	–	–	–	–	9.0	–
<b>Revenue</b>	<b>74.4</b>	<b>55.4</b>	<b>80.0</b>	<b>60.1</b>	<b>76.2</b>	<b>68.0</b>	<b>230.6</b>	<b>183.5</b>
Adjusted operating profit – existing businesses	15.1	11.9	14.9	8.9	13.2	11.3	43.2	32.1
– acquisitions	2.0	–	–	–	–	–	2.0	–
<b>Adjusted operating profit</b>	<b>17.1</b>	<b>11.9</b>	<b>14.9</b>	<b>8.9</b>	<b>13.2</b>	<b>11.3</b>	<b>45.2</b>	<b>32.1</b>
Acquisition related charges (note 11)	(2.7)	(1.6)	(1.7)	(1.5)	(0.4)	(0.4)	(4.8)	(3.5)
<b>Operating profit</b>	<b>14.4</b>	<b>10.3</b>	<b>13.2</b>	<b>7.4</b>	<b>12.8</b>	<b>10.9</b>	<b>40.4</b>	<b>28.6</b>

### 3 Business Segment Analysis continued

Segment assets exclude cash and cash equivalents, deferred tax assets and corporate assets that cannot be allocated on a reasonable basis to a business segment. Segment liabilities exclude retirement benefit obligations, deferred tax liabilities and corporate liabilities that cannot be allocated on a reasonable basis to a business segment. These items are shown collectively in the following analysis as "unallocated assets" and "unallocated liabilities" respectively.

	Life Sciences		Seals		Controls		Total	
	2011 £m	2010 £m	2011 £m	2010 £m	2011 £m	2010 £m	2011 £m	2010 £m
Operating assets	21.8	17.6	33.0	27.1	27.8	25.9	82.6	70.6
Goodwill	58.0	38.2	14.2	14.2	14.9	14.9	87.1	67.3
Acquisition intangible assets	16.6	9.9	9.8	11.5	0.9	1.3	27.3	22.7
	96.4	65.7	57.0	52.8	43.6	42.1	197.0	160.6
Unallocated assets								
– Deferred tax assets							2.8	2.4
– Cash and cash equivalents							17.8	30.1
– Corporate assets							3.5	3.6
<b>Total assets</b>							<b>221.1</b>	<b>196.7</b>
Operating liabilities	(11.9)	(11.3)	(8.9)	(8.0)	(13.0)	(12.2)	(33.8)	(31.5)
Unallocated liabilities								
– Deferred tax liabilities							(4.8)	(3.7)
– Retirement benefit obligations							(5.4)	(5.3)
– Future purchases of minority interests							(2.0)	(13.2)
– Borrowings							(5.6)	-
– Corporate liabilities							(4.9)	(3.8)
<b>Total liabilities</b>							<b>(56.5)</b>	<b>(57.5)</b>
<b>Net assets</b>							<b>164.6</b>	<b>139.2</b>
<b>Other segment information</b>								
Capital expenditure	0.8	0.7	0.6	0.5	0.3	0.1	1.7	1.3
Depreciation (including software)	1.0	0.8	0.8	0.9	0.3	0.4	2.1	2.1

### Alternative Performance Measures (note 2)

	Life Sciences		Seals		Controls		Total	
	2011 £m	2010 £m	2011 £m	2010 £m	2011 £m	2010 £m	2011 £m	2010 £m
<b>Net assets</b>							<b>164.6</b>	<b>139.2</b>
Add/(less)								
– Deferred tax, net							2.0	1.3
– Retirement benefit obligations							5.4	5.3
– Future purchases of minority interests							2.0	13.2
– Cash and cash equivalents							(17.8)	(30.1)
– Borrowings							5.6	-
– Adjustment to goodwill	(7.0)	(4.7)	(1.3)	(1.3)	(0.6)	(0.6)	(8.9)	(6.6)
<b>Group trading capital employed</b>							<b>152.9</b>	<b>122.3</b>
Corporate liabilities, net							1.4	0.2
<b>Segment trading capital employed</b>	<b>77.5</b>	<b>49.7</b>	<b>46.8</b>	<b>43.5</b>	<b>30.0</b>	<b>29.3</b>	<b>154.3</b>	<b>122.5</b>

### 4 Geographic Segment Analysis by Origin

	Revenue		Adjusted operating profit		Gross assets		Trading capital employed		Capital expenditure	
	2011 £m	2010 £m	2011 £m	2010 £m	2011 £m	2010 £m	2011 £m	2010 £m	2011 £m	2010 £m
United Kingdom	61.8	55.9	10.9	8.4	48.2	50.0	22.0	19.2	0.2	0.3
Rest of Europe	40.8	35.1	5.8	4.5	34.9	33.2	19.8	19.6	0.3	0.1
North America	128.0	92.5	28.5	19.2	138.0	113.5	111.1	83.5	1.2	0.9
	230.6	183.5	45.2	32.1	221.1	196.7	152.9	122.3	1.7	1.3

## Notes to the Consolidated Financial Statements continued

### For the year ended 30 September 2011

#### 5 Group Employee Costs

The key management of the Group are the Executive Directors who have authority and responsibility for planning and controlling all significant activities of the Group. The Directors' emoluments and interests in shares of the Company are given in the Remuneration Report on pages 32 to 41. The charge for share-based payments of £0.7m relate to the Group's share schemes described in the Remuneration Report. The fair value of services provided as consideration for part of the grant of the LTIP awards has been based on a predicted future value model and was £0.2m (2010: £0.2m).

Group staff costs including Directors' emoluments are as follows:

	2011 £m	2010 £m
Wages and salaries	38.3	32.1
Social security costs	3.4	2.9
Pension costs – defined contribution	0.8	0.7
Share-based payments	0.7	0.5
	<b>43.2</b>	<b>36.2</b>

The average number of employees including Executive Directors during the year were:

	2011 Number	2010 Number
Life Sciences	223	199
Seals	432	371
Controls	245	234
Corporate	10	10
<b>Number of employees – average</b>	<b>910</b>	<b>814</b>
<b>Number of employees – year end</b>	<b>954</b>	<b>847</b>

#### 6 Financial Expense, net

	2011 £m	2010 £m
<b>Interest and similar income</b>		
– interest receivable on short-term deposits	0.1	0.2
– net finance income from defined benefit pension scheme (note 25)	0.2	0.1
	<b>0.3</b>	<b>0.3</b>
<b>Interest expense and similar charges</b>		
– bank facility and commitment fees	(0.3)	(0.1)
– unwinding of discount on provisions	–	(0.1)
– interest payable on bank borrowings	(0.3)	–
	<b>(0.6)</b>	<b>(0.2)</b>
<b>Net interest (expense)/income</b>	<b>(0.3)</b>	<b>0.1</b>
– fair value remeasurement of put options (note 19)	(0.9)	(2.0)
<b>Financial expense, net</b>	<b>(1.2)</b>	<b>(1.9)</b>

The fair value remeasurement of £0.9m (2010: £2.0m) includes £0.1m (2010: £1.1m) which relates to the unwinding of the discount on the liability for future purchases of minority interests.

## 7 Tax Expense

	2011 £m	2010 £m
<b>Current tax</b>		
The tax charge is based on the profit for the year of the continuing businesses and comprises		
UK corporation tax	3.1	2.2
Overseas tax	9.7	7.0
	<b>12.8</b>	<b>9.2</b>
Adjustments in respect of prior year		
Overseas tax	–	(0.1)
	–	(0.1)
<b>Total current tax</b>	<b>12.8</b>	<b>9.1</b>
<b>Deferred tax</b>		
The deferred tax credit based on the origination and reversal of timing differences comprises		
United Kingdom	(0.2)	(0.1)
Overseas	(1.0)	(0.2)
<b>Total deferred tax</b>	<b>(1.2)</b>	<b>(0.3)</b>
<b>Total tax on profit for the year</b>	<b>11.6</b>	<b>8.8</b>

In addition to the above charge for deferred tax included in the consolidated Income Statement deferred tax relating to retirement benefit schemes and share-based payments of £0.3m (2010: £0.6m) was also charged directly to equity

### Factors affecting the tax charge for the year

The difference between the total tax charge shown above and the amount calculated by applying the standard rate of UK corporation tax to the profit before tax is as follows

	2011 £m	2010 £m
<b>Profit before tax</b>	<b>39.2</b>	<b>26.7</b>
Tax on profit at UK effective corporation tax rate of 27% (2010: 28%)	10.6	7.5
Effects of		
Higher tax rates on overseas earnings	0.6	1.0
Adjustments to tax charge in respect of previous years	–	(0.1)
Fair value remeasurements	0.2	0.6
Other permanent differences	0.2	(0.2)
<b>Total tax on profit for the year</b>	<b>11.6</b>	<b>8.8</b>

The Group earns its profits in the UK and overseas. The UK corporation tax rate reduced from 28% to 26% on 31 March 2011, however as the Group prepares its financial statements for the year to 30 September, the effective tax rate for UK corporation tax in respect of the year ended 30 September 2011 was 27% (2010: 28%) and this rate has been used for tax on profit in the above reconciliation. The Group's overseas tax rate is higher than that in the UK, primarily because the profits earned in North America are taxed at rates varying from 26% to 40%. The tax relating to the discontinued businesses is £Nil (2010: £0.2m credit) as set out in note 22.

## 8 Dividends

	2011 pence per share	2010 pence per share	2011 £m	2010 £m
Interim dividend paid in June	3.5	2.8	3.9	3.1
Final dividend of the prior year paid in January	6.2	5.3	7.0	6.0
	<b>9.7</b>	<b>8.1</b>	<b>10.9</b>	<b>9.1</b>

The Directors have proposed a final dividend in respect of the current year of 8.5p (2010: 6.2p) which will be paid on 25 January 2012, subject to approval of shareholders at the Annual General Meeting on 18 January 2012. The total dividend for the current year, subject to approval of the final dividend, will be 12.0p (2010: 9.0p).

The Diploma Employee Benefit Trust holds 1,094,512 (2010: 732,973) shares, which are not eligible for dividends.

## Notes to the Consolidated Financial Statements continued

### For the year ended 30 September 2011

#### 9 Earnings Per Share

##### Basic and diluted earnings per share

Basic and diluted earnings per ordinary 5p share are calculated on the basis of the weighted average number of ordinary shares in issue during the year of 112 423 842 (2010 112 577,283) and the profit for the year attributable to shareholders of £270m (2010 £21.5m). There were no potentially dilutive shares.

##### Adjusted earnings per share

Adjusted earnings per share, which is defined in note 2, is calculated as follows:

	2011 pence per share	2010 pence per share	2011 £m	2010 £m
<b>Profit before tax – continuing businesses</b>			<b>39.2</b>	<b>26.7</b>
Tax expense			<b>(11.6)</b>	<b>(8.8)</b>
Minority interests			<b>(0.6)</b>	<b>(1.5)</b>
	<b>24.0</b>	<b>14.6</b>	<b>270</b>	<b>164</b>
Profit from discontinued businesses	–	4.5	–	5.1
<b>Earnings for the year attributable to shareholders of the Company</b>	<b>24.0</b>	<b>19.1</b>	<b>270</b>	<b>21.5</b>
Acquisition related charges	<b>4.3</b>	<b>3.1</b>	<b>4.8</b>	<b>3.5</b>
Fair value remeasurements	<b>0.8</b>	<b>1.8</b>	<b>0.9</b>	<b>2.0</b>
Tax effects on goodwill, acquisition intangible assets and fair value remeasurements	<b>(1.2)</b>	<b>(0.6)</b>	<b>(1.3)</b>	<b>(0.6)</b>
Profit from discontinued businesses	–	(4.5)	–	(5.1)
<b>Adjusted earnings – continuing businesses</b>	<b>27.9</b>	<b>18.9</b>	<b>31.4</b>	<b>21.3</b>

#### 10 Goodwill

	Life Sciences £m	Seals £m	Controls £m	Total £m
At 1 October 2009	32.5	12.0	15.1	59.6
Acquisitions	3.7	2.5	–	6.2
Adjustment to prior year goodwill	–	(0.2)	–	(0.2)
Exchange adjustments	2.0	(0.1)	(0.2)	1.7
At 30 September 2010	38.2	14.2	14.9	67.3
Acquisitions (note 20 and 21)	20.4	–	–	20.4
Exchange adjustments	(0.6)	–	–	(0.6)
<b>At 30 September 2011</b>	<b>58.0</b>	<b>14.2</b>	<b>14.9</b>	<b>87.1</b>

The Directors carry out an impairment test on all goodwill generally twice a year. Goodwill is ascribed to a business which, for the purpose of these impairment tests, is referred to as a cash generating unit. The impairment test requires each cash generating unit to prepare "value in use" valuations from discounted cash flow forecasts. The cash flow forecasts are based on the annual budgets prepared by each business and by five year strategic plans prepared at a Group level.

The key assumptions used to prepare the cash flow forecasts relate to gross margin, growth rates and discount rates. The gross margins are assumed to remain sustainable, which is supported by historical experience. Growth rates generally approximate to the long-term average rates for the markets in which the business operate, unless there are particular factors relevant to a business, such as start-ups. The annual growth rates used in the cash flow forecasts in respect of the next five years vary between 2% and 5% in each of the sectors; these annual growth rates then trend down towards 2.0% over the longer term.

The cash flow forecasts are discounted to determine a current valuation, using a pre-tax discount rate of ca. 13% (2010 13%). This rate is based on the characteristics of lower risk, non-technically driven, distribution businesses with robust capital structures, which is broadly consistent with each of the Group's businesses.

Based on the criteria set out above, no impairment in the value of goodwill was identified.

The Directors have also carried out sensitivity analysis on the key assumptions to determine whether a "reasonably possible change" in any of these assumptions would result in an impairment of goodwill. This analysis indicates that a "reasonably possible change" in these key assumptions would be unlikely to give rise to an impairment charge to goodwill in any of the businesses in the Life Sciences or Seals segments. However, in the Controls sector a reduction of 2% in revenue growth in the medium term in some of the businesses in this sector would result in an impairment charge of up to £0.2m. The headroom in the cash flow valuation, before any sensitivities and based on the original assumptions in respect of these businesses in the Controls sector is £0.7m. In the prior year, the sensitivity analysis indicated that a reduction of 2% in revenue growth in the medium term in the Seals sector would have resulted in an impairment of £1.0m. The headroom, before sensitivities, in respect of these businesses in the Seals sector was £2.0m.

## 11 Acquisition and Other Intangible Assets

	Customer relationships £m	Supplier relationships £m	Trade names and databases £m	Total acquisition intangible assets £m	Other Intangible assets £m
<b>Cost</b>					
At 1 October 2009	163	100	26	289	21
Additions	–	–	–	–	01
Acquisitions	45	–	–	45	–
Exchange adjustments	01	03	–	04	–
At 30 September 2010	209	103	26	338	22
Additions	–	–	–	–	04
Acquisitions (note 21)	29	64	–	93	–
Exchange adjustments	–	(02)	–	(02)	–
<b>At 30 September 2011</b>	<b>238</b>	<b>165</b>	<b>26</b>	<b>429</b>	<b>26</b>
<b>Amortisation</b>					
At 1 October 2009	44	27	06	77	13
Charge for the year	19	11	03	33	03
Exchange adjustments	–	01	–	01	–
At 30 September 2010	63	39	09	111	16
Charge for the year	25	17	03	45	03
<b>At 30 September 2011</b>	<b>88</b>	<b>56</b>	<b>12</b>	<b>156</b>	<b>19</b>
<b>Net book value</b>					
<b>At 30 September 2011</b>	<b>150</b>	<b>109</b>	<b>14</b>	<b>273</b>	<b>07</b>
At 30 September 2010	146	64	17	227	06

Acquisition related charges are £4.8m (2010: £3.5m) and comprise £4.5m (2010: £3.3m) of amortisation of acquisition intangible assets and £0.3m (2010: £0.2m) of acquisition expenses.

Acquisition intangible assets relate to items acquired through business combinations which are amortised over their useful economic life.

	Economic life
Customer relationships	5–15 years
Supplier relationships	7–10 years
Databases and trade names	5–10 years

The amount in respect of customer relationships was valued using a discounted cash flow model, the databases were valued using a replacement cost model, the amount in respect of supplier relationships and trade names were valued on a relief from royalty method.

Other intangible assets comprise computer software that is separately identifiable from plant and equipment and includes software licences.

## Notes to the Consolidated Financial Statements continued

### For the year ended 30 September 2011

#### 12 Property, Plant and Equipment

	Freehold properties £m	Leasehold properties £m	Plant & equipment £m	Total £m
<b>Cost</b>				
At 1 October 2009	88	1.1	14.5	24.4
Additions	-	-	1.2	1.2
Disposals	-	-	(0.5)	(0.5)
Exchange adjustments	-	-	1.4	1.4
At 30 September 2010	88	1.1	16.6	26.5
Additions	-	0.1	1.2	1.3
Acquisitions	-	-	0.3	0.3
Disposals	-	(0.1)	(0.5)	(0.6)
<b>At 30 September 2011</b>	<b>88</b>	<b>1.1</b>	<b>17.6</b>	<b>27.5</b>
<b>Depreciation</b>				
At 1 October 2009	2.0	0.6	10.2	12.8
Charge for the year	0.1	0.1	1.6	1.8
Disposals	-	-	(0.5)	(0.5)
Exchange adjustments	-	-	1.3	1.3
At 30 September 2010	2.1	0.7	12.6	15.4
Charge for the year	0.1	0.1	1.6	1.8
Disposals	-	(0.1)	(0.3)	(0.4)
<b>At 30 September 2011</b>	<b>2.2</b>	<b>0.7</b>	<b>13.9</b>	<b>16.8</b>
<b>Net book value</b>				
<b>At 30 September 2011</b>	<b>6.6</b>	<b>0.4</b>	<b>3.7</b>	<b>10.7</b>
At 30 September 2010	6.7	0.4	4.0	11.1

Land included above but not depreciated, is £2.0m (2010: £2.0m). Capital commitments contracted but not provided were £Nil (2010: £Nil).

Freehold properties includes ca 150 acres of land at Stamford ("the Stamford land") which comprises mostly farm land and former quarry land. In the Directors' opinion the current value of this land is £0.5m (net book value: £Nil) (2010: £0.5m and £Nil, respectively).

#### 13 Deferred Tax

The movement on deferred tax is as follows:

	2011 £m	2010 £m
At 1 October	(1.3)	(2.0)
Credit for the year (note 7)	1.2	0.3
Acquisitions	(2.3)	-
Accounted for in equity	0.3	0.6
Exchange adjustments	0.1	(0.2)
<b>At 30 September</b>	<b>(2.0)</b>	<b>(1.3)</b>

Deferred tax assets and liabilities are only offset where there is a legally enforceable right of offset and there is an intention to settle the balances net.

	Assets		Liabilities		Net	
	2011 £m	2010 £m	2011 £m	2010 £m	2011 £m	2010 £m
Property, plant and equipment	0.4	0.3	(0.6)	(0.5)	(0.2)	(0.2)
Goodwill and intangible assets	-	-	(5.5)	(4.6)	(5.5)	(4.6)
Retirement benefit obligations	1.4	1.4	-	-	1.4	1.4
Inventories	0.8	0.7	-	-	0.8	0.7
Share-based payments	0.8	0.1	-	-	0.8	0.1
Other temporary differences	0.9	1.3	(0.2)	-	0.7	1.3
	4.3	3.8	(6.3)	(5.1)	(2.0)	(1.3)
Set off of deferred tax	(1.5)	(1.4)	1.5	1.4	-	-
	<b>2.8</b>	<b>2.4</b>	<b>(4.8)</b>	<b>(3.7)</b>	<b>(2.0)</b>	<b>(1.3)</b>

No deferred tax has been provided for unremitted earnings of overseas Group companies as the Group controls the dividend policies of its subsidiaries. Unremitted earnings may be liable to overseas taxation (after allowing for double taxation relief) if they were to be distributed as dividends. The aggregate amount for which deferred tax liabilities have not been recognised in respect of unremitted earnings was £1.2m (2010: £1.2m).

**14 Inventories**

	2011 £m	2010 £m
Finished goods and goods held for resale	38 4	32 0

Inventories are stated net of impairment provisions of £3.6m (2010: £3.6m). During the year £0.5m (2010: £1.0m) was recognised as an expense relating to the write-down of inventory to net realisable value.

**15 Trade and Other Receivables**

	2011 £m	2010 £m
Trade receivables	33 0	28 5
Less: impairment provision	(0 5)	(0 6)
	32 5	27 9
Other receivables	2 2	1 4
Prepayments and accrued income	1 6	1 2
	36 3	30 5

The maximum exposure to credit risk for trade receivables at the reporting date, by currency was:

	2011 £m	2010 £m
Sterling	10 4	10 0
US dollars	8 6	6 8
Canadian dollars	9 5	7 0
Euro	2 7	2 8
Other	1 8	1 9
	33 0	28 5

Trade receivables, before impairment provisions, are analysed as follows:

	2011 £m	2010 £m
Not past due	26 2	23 1
Past due, but not impaired	6 2	4 6
Past due, but partially impaired	0 6	0 8
	33 0	28 5

The ageing of trade receivables classed as past due, but not impaired, is as follows:

	2011 £m	2010 £m
Up to one month past due	4 7	3 5
Between one and two months past due	1 1	0 8
Between two and four months past due	0 3	0 2
Over four months past due	0 1	0 1
	6 2	4 6

The movement in the provision for impairment of trade receivables is as follows:

	2011 £m	2010 £m
At 1 October	0 6	0 5
Charged against profit, net	0 2	0 2
Utilised by write off	(0 3)	(0 1)
<b>At 30 September</b>	<b>0 5</b>	<b>0 6</b>

## Notes to the Consolidated Financial Statements continued

### For the year ended 30 September 2011

#### 16 Trade and Other Payables

	2011 £m	2010 £m
Trade payables	196	165
Other payables	23	28
Other taxes and social security	15	12
Accruals and deferred income	11.8	11.8
	<b>352</b>	<b>323</b>

The maximum exposure to foreign currency risk for trade payables at the reporting date, by currency was

	2011 £m	2010 £m
Sterling	54	56
US dollars	84	67
Canadian dollars	12	04
Euro	37	31
Other	09	07
	<b>196</b>	<b>165</b>

#### 17 Cash and Cash Equivalents

	Sterling £m	US\$ £m	C\$ £m	Euro £m	2011 Total £m	Sterling £m	US\$ £m	Can\$ £m	Euro £m	2010 Total £m
Cash at bank	27	33	38	32	130	27	35	15	14	91
Short-term deposits	37	–	–	11	48	77	–	12.2	1.1	21.0
	<b>64</b>	<b>33</b>	<b>38</b>	<b>43</b>	<b>178</b>	<b>104</b>	<b>35</b>	<b>13.7</b>	<b>25</b>	<b>301</b>

The short-term deposits and cash at bank are both interest bearing at rates linked to the UK Base Rate or equivalent rate

#### 18 Financial Instruments

The Group's principal financial instruments other than a limited number of forward foreign contracts comprise cash and short-term deposits, trade and other receivables and trade and other payables and other liabilities. Trade and other receivables and trade and other payables arise directly from the Group's day to day operations.

The financial risks to which the Group is exposed are those of credit, liquidity, foreign currency, interest rate and capital management. An explanation of each of these risks, how the Group manages these risks and an analysis of sensitivities is set out below or on page 23 within Principal Risks and Uncertainties which has been audited.

##### a) Credit risk

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations. This arises principally from the Group's trade and other receivables from customers and from cash balances (including deposits) held with financial institutions.

The Group is exposed to customers ranging from government backed agencies and large public and private wholesalers to small privately owned businesses and the underlying local economic risks vary throughout the world. Trade receivable exposures are managed locally in the operating units where they arise and credit limits are set as deemed appropriate for the customer.

The Group establishes an allowance for impairment that represents its estimate of incurred losses in respect of specific trade and other receivables where it is deemed that a receivable may not be recoverable. When the receivable is deemed irrecoverable, the allowance account is written off against the underlying receivable. The Group has not had any material irrecoverable trade receivables in the past five years, but the economic environment in some of the Group's principal markets has deteriorated during the current year.

Exposure to financial counterparty credit risk is controlled by the Group treasury team in establishing and monitoring counterparty limits. Centrally managed funds are invested entirely with counterparties whose credit rating is "AA" or better.

**18 Financial Instruments** continued

The Group's maximum exposure to credit risk was as follows

	Carrying amount	
	2011 £m	2010 £m
Trade receivables	32.5	27.9
Other receivables	2.2	1.4
Cash and cash equivalents	17.8	30.1
	<b>52.5</b>	<b>59.4</b>

There is no material difference between the carrying amount of the financial assets and their fair value at each reporting date. An analysis of the ageing and currency of trade receivables and the associated provision for impairment is set out in note 15. An analysis of cash and cash equivalents is set out in note 17.

**b) Liquidity risk**

Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. The Group continually monitors net funds and forecast cash flows to ensure that sufficient facilities are in place to meet the Group's requirements in the short, medium and long term and, in order to do so, arranges borrowings. Additionally, compliance with debt covenants are monitored and during 2011 all covenants have been fully complied with.

The Group is highly cash generative and uses monthly cash flow forecasts to monitor cash requirements and to optimise its return on investments. Typically, the Group ensures that it has sufficient cash on hand to meet foreseeable operational expenses, but the Group also has a committed £20m revolving bank facility which expires in November 2013, with an option to increase its facility to £40m, subject to market pricing. Interest on this facility is payable at between 150 and 195 bps over LIBOR, depending on the ratio of net debt to EBITDA. At 30 September 2011, £5.6m of the facility had been drawn down.

The undrawn committed facilities available at 30 September are as follows:

	2011 £m	2010 £m
Expiring within one year	–	20.0
Expiring after one year but within two years	14.4	–

The Group's financial liabilities are as follows:

	Carrying amount	
	2011 £m	2010 £m
Trade payables	19.6	16.5
Other payables	2.3	2.8
Other liabilities	3.1	14.2
Borrowings	5.6	–
	<b>30.6</b>	<b>33.5</b>
The maturities of the undiscounted financial liabilities are as follows:		
Less than one year	22.7	32.3
One-two years	7.7	–
Two-five years	0.6	1.4
	<b>31.0</b>	<b>33.7</b>
Less: Discount	(0.4)	(0.2)
	<b>30.6</b>	<b>33.5</b>

There is no material difference between the carrying amount of these financial liabilities and their fair value at each reporting date.

**c) Currency risk**

The Group's currency risk comprises translational and transactional risk from its exposure to movements in US dollars, Canadian dollars and Euros. The transactional exposure arises on trade receivables, trade payables and cash and cash equivalents and these balances are analysed by currency in notes 15, 16 and 17 respectively. Net foreign exchange gains of £0.1m (2010: £Nil) were recognised in profit for the year.

The Group holds forward foreign exchange contracts to hedge forecast transactional exposure in certain of the Group's businesses to movements in the US dollar and Euro. These forward foreign exchange contracts are classified as cash flow hedges and are stated at fair value. The net fair value of forward foreign exchange contracts used as hedges at 30 September 2011 was a £0.6m asset (2010: £0.7m liability). The amount removed from equity and taken to the consolidated Income Statement in cost of sales during the year was £1.0m credit (2010: £0.1m charge). The fair value of cash flow hedges taken to equity during the year was £1.2m credit (2010: £0.3m charge).

The currency risk arising from both translational and transactional risks are described further on page 23 within Principal Risks and Uncertainties.

## Notes to the Consolidated Financial Statements continued

### For the year ended 30 September 2011

#### 18 Financial Instruments continued

##### d) Interest rate risk

Interest rate risk is the risk that changes in interest rates will affect the Group's results. The Group's interest rate risk arises primarily from its cash funds and borrowings.

The Group does not undertake any hedging of interest rates. All cash deposits held in the UK and overseas are held on a short-term basis at floating rates or overnight rates based on the relevant UK Base Rate or equivalent rate.

Surplus funds are deposited with commercial banks that meet the credit criteria approved by the Board for periods of between one to six months at rates that are generally fixed by reference to the relevant UK Base Rate or equivalent rates. It is estimated that an increase of 1% in interest rates would increase the Group's profit before tax by a maximum of £0.1m.

An analysis of cash and cash equivalents at the reporting dates is set out in note 17.

##### e) Fair values

There are no material differences between the carrying value of financial assets and liabilities and their fair value. The basis for determining fair values are as follows:

##### Derivatives

Forward exchange contracts are valued at year end spot rates adjusted for the forward points to the contract's value date and gains and losses taken to equity. No contract's value date is greater than 24 months from the year end (Level 1 as defined by IFRS 7 Financial Instrument Disclosure).

##### Trade and other receivables/payables

As the majority of receivables/payables have a remaining life of less than one year, the nominal amount is deemed to reflect the fair value.

##### Other liabilities

The carrying amount represents a discounted value of the expected liability which is deemed to reflect the fair value.

##### f) Capital management risk

The Group's policy is to maintain a strong capital base so as to maintain investor, supplier and market confidence, provide strong returns to shareholders and to support the future development of the business. The capital structure of the Group consists of cash and cash equivalents, debt, which includes borrowings and equity attributable to equity holders of the parent, comprising issued share capital, reserves and retained earnings.

The Group is not subject to externally imposed capital requirements. There were no changes in the Group's approach to capital management during the year.

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 increase bank borrowings.

#### 19 Other Liabilities

	2011 £m	2010 £m
Future purchases of minority interests	20	13.2
Deferred consideration	11	1.0
	<b>31</b>	<b>14.2</b>
Analysed as		
Due within one year	0.8	13.0
Due after one year	2.3	1.2

The movement in the liability for future purchases of minority interests is as follows:

	2011 £m	2010 £m
At 1 October	13.2	13.1
Released to retained earnings on acquisition	(12.1)	(2.5)
Put options entered into during the year	–	0.6
Unwinding of discount	0.1	1.1
Fair value remeasurements	0.8	0.9
<b>At 30 September</b>	<b>2.0</b>	<b>13.2</b>

The Group retains put/call options to acquire the outstanding minority shareholdings. During the year, the Group acquired the outstanding 25% minority shares in AMT as explained in note 20. On acquisition of the minority interest shares, the liability of £12.1m recognised in the consolidated Statement of Financial Position at 30 September 2010 has been released to retained earnings. At 30 September 2011, the Group retains minority interests in BGS, HPS and M Seals and the put options to acquire these minority interests are exercisable between 1 October 2012 and 31 December 2017.

At 30 September 2011, the estimate of the financial liability to acquire the outstanding minority shareholdings was reassessed by the Directors based on their current estimate of the future performance of these businesses and to reflect foreign exchange rates at 30 September 2011. This led to a remeasurement of the fair value of these put options and the liability was increased by £0.8m (2010: £0.9m). The charge for the liability together with the charge from unwinding the discount on the liability was in aggregate £0.9m (2010: £2.0m) and has been charged to the consolidated Income Statement.

At 30 September 2011, deferred consideration of £1.1m is payable to the vendors of CMI. Deferred consideration of £0.7m was paid on 7 March 2011 to the vendors of All Seals in final settlement of their performance payment and on agreement of net assets acquired, £0.1m was paid on 19 October 2010 to the vendors of BGS on agreement of net assets acquired and £0.1m was paid to the vendors of Fischer.

**20 Minority Interests**

	£m
At 1 October 2009	2.7
Purchase of minority interest	(0.1)
Share of profit for the year	1.5
Dividends paid	(1.1)
Exchange adjustments	0.1
At 30 September 2010	3.1
Purchase of minority interests	0.7
Share of profit for the year	0.6
Dividends paid	(3.9)
<b>At 30 September 2011</b>	<b>0.5</b>

During the year the Group acquired the outstanding 25% share capital in AMT Vantage Group Inc ("AMT") held by the minority shareholders for consideration of £12.5m (C\$19.7m) including expenses pursuant to put/call option agreements entered into at the time of the original acquisition in August 2007. The consideration for this acquisition was paid in cash and met from the Group's existing cash and borrowing resources.

These shares were acquired in two tranches. 4% of the ordinary share capital of AMT was acquired on 7 January 2011 for £2.0m (C\$3.1m) and the remaining 21% was acquired on 28 February 2011 for £10.4m (C\$16.4m). Acquisition expenses of £0.1m (C\$0.2m) were incurred on this acquisition and were charged to the consolidated Income Statement. Goodwill of £13.1m arose on the acquisition of these minority interests which will not be allowable for a tax deduction in future years.

**21 Acquisition of Subsidiaries**

On 21 December 2010 the Group acquired 100% of Carsen Medical Inc ("CMI") for a maximum consideration of £16.5m (C\$25.9m) including expenses. The initial cash paid on acquisition was £14.3m (C\$22.5m) and a further £0.9m (C\$1.4m) of deferred consideration was paid during the year. The final tranche of deferred consideration of £1.1m (C\$1.8m) is payable in December 2011, depending principally on the operating profit of CMI in the year ending 30 September 2011. Acquisition expenses of £0.2m (C\$0.3m) were incurred on this acquisition and expensed to the consolidated Income Statement.

The consideration for this acquisition was paid in cash and met from the Group's existing cash and borrowing resources.

Set out below is an analysis of the net book value and fair value of the net assets acquired and the consideration payable in respect of this acquisition.

	Book value £m	Fair value £m
Acquisition intangible assets	0.3	9.3
Property, plant and equipment	0.4	0.4
Inventories	0.8	0.7
Trade and other receivables	2.4	2.3
Trade and other payables	(2.0)	(2.0)
Deferred tax	(0.1)	(2.3)
Net assets acquired	1.8	8.4
Goodwill		7.3
		<b>15.7</b>
<b>Satisfied by</b>		
Cash paid		15.2
Cash acquired		(0.6)
<b>Net cash paid, before acquisition expenses</b>		<b>14.6</b>
Provision for deferred consideration payable		1.1
<b>Total consideration</b>		<b>15.7</b>

Goodwill of £7.3m which arose on the acquisition of CMI represents the product know-how held by employees, prospects for sales growth from new customers and operating cost synergies. Goodwill and acquisition intangible assets relating to this acquisition of £16.6m will not be allowable for a tax deduction in future years.

From the date of acquisition to 30 September 2011, the newly acquired businesses of CMI contributed £9.0m to revenue and £2.0m to adjusted operating profit. If the acquisition of this business had been made at the beginning of this financial year, this business would have contributed £11.5m to revenue and £1.7m to profit after tax. Profit after tax should not be viewed as indicative of the results of this business that would have occurred, if this acquisition had been completed at the beginning of the year.

## Notes to the Consolidated Financial Statements continued

### For the year ended 30 September 2011

#### 22 Discontinued Businesses

In January 2010 the Group completed the disposal of the Manual Liquid Handling business of Anachem Limited for a maximum consideration of £8.5m before disposal costs. Initial cash proceeds of £7.7m were received of which £0.7m were held in escrow and up to a further £0.8m was receivable depending on the revenues for the year ended 31 December 2010. The revenues during the year ended 31 December 2010 were not sufficient to meet the criteria for the performance payment and as such no payment was received. During the year the Group received £0.7m on release of the escrow money.

The remainder of the business in Anachem Limited which comprised the Anachem Instruments division was transferred to a separate legal entity which was then sold in April 2010 for a maximum consideration of £0.4m before disposal costs. Initial proceeds of £0.2m were received with a further £0.2m received in January 2011 in final settlement.

Anachem Limited and Anachem Instruments Limited were both classified as discontinued businesses in the prior year and their results for that period until their disposal are set out below.

	2010 £m
<b>Revenue</b>	5.3
Cost of sales	(4.3)
<b>Gross profit</b>	1.0
Distribution costs	(0.2)
Administration costs	(1.4)
<b>Loss before tax</b>	(0.6)
Tax credit	0.2
<b>Loss after tax</b>	(0.4)
Profit on disposal	5.5
<b>Profit attributable to discontinued businesses</b>	5.1

#### 23 Reconciliation of Cash Flow from Operating Activities

	2011 £m	2010 £m
<b>Profit for the year from continuing businesses</b>	276	179
Depreciation/amortisation of tangible and other intangible assets	2.1	2.1
Acquisition related charges	4.8	3.5
Share-based payments expense	0.7	0.5
Financial expense net	1.2	1.9
Tax expense	11.6	8.8
<b>Operating cash flow before changes in working capital</b>	48.0	34.7
Increase in inventories	(5.5)	(3.2)
Increase in trade and other receivables	(3.3)	(4.0)
Increase in trade and other payables	1.4	7.3
Cash paid into defined benefit schemes (note 25)	(0.3)	(0.5)
<b>Cash flow from operating activities</b>	40.3	34.3

#### 24 Net Funds

The movement in net funds during the year is as follows:

	2011 £m	2010 £m
Net (decrease)/increase in cash and cash equivalents	(12.6)	8.1
Increase in borrowings	(5.4)	-
Effect of exchange rates	(18.0)	8.1
	0.1	0.7
<b>Movement in net funds</b>	(17.9)	8.8
Net funds at beginning of year	30.1	21.3
<b>Net funds at end of year</b>	12.2	30.1
<b>Comprising</b>		
Cash and cash equivalents	17.8	30.1
Borrowings	(5.6)	-
<b>Net funds at end of year</b>	12.2	30.1

The Group has a committed £20m revolving bank facility which expires on 18 November 2013. At 30 September 2011, the Group had utilised £5.6m of this facility. Interest on this facility is payable at between 150 and 175 bps over LIBOR depending on the ratio of net debt to EBITDA.

## 25 Retirement Benefit Obligations

The Group maintains several legacy defined benefit pension schemes in the UK which at 30 September 2010 were merged into a single scheme which was renamed Diploma Holdings PLC UK Pension Scheme ("the Scheme"). The Scheme is closed to future accrual and the assets of the Scheme are held in separate trustee administered funds. The Scheme is funded in accordance with rates recommended by an independent qualified actuary on the basis of triennial or shorter period reviews using the projected unit method.

Prior to the merger on 30 September 2010 the two principal defined benefit pension schemes were the Diploma Holdings PLC Permanent Staff Pension and Assurance Scheme and the Anachem Limited Retirement Benefits Scheme. The merger comprised these two schemes and two smaller legacy schemes. The two smaller schemes which at 30 September 2010 had aggregate assets of £2.5m and aggregate liabilities of £2.9m have in 2011 been included in the analysis set out below.

### Pension deficit included in the Consolidated Statement of Financial Position

	2011 £m	2010 £m
Market value of Scheme assets		
Equities	13.8	12.9
Bonds	4.2	3.4
Cash	0.2	-
	18.2	16.3
Present value of Scheme liabilities	(23.6)	(21.6)
	(5.4)	(5.3)

### Amounts credited to the Consolidated Income Statement in respect of defined benefit schemes

	2011 £m	2010 £m
Charged to operating profit	-	-
Interest cost	(1.2)	(1.0)
Expected return on Scheme assets	1.4	1.1
Credited to financial income (note 6)	0.2	0.1
	0.2	0.1

### Amounts recognised in the Consolidated Statement of Comprehensive Income

	2011 £m	2010 £m
Addition of two smaller schemes	(0.4)	-
Experience adjustments on Scheme assets	(1.8)	0.3
Changes in assumptions on Scheme liabilities	2.1	(2.2)
Experience adjustments on Scheme liabilities	(0.5)	0.1
<b>Actuarial loss on Scheme liabilities</b>	<b>(0.6)</b>	<b>(1.8)</b>

The changes in assumptions on the Schemes liabilities includes a reduction of £1.4m arising from the change in the inflation measure applied for the pension increases and revaluations, from RPI to CPI in accordance with legislation enacted in January 2011.

The cumulative amount of actuarial losses recognised in the consolidated Statement of Comprehensive Income since the transition to IFRS is £4.5m (2010: £3.9m).

### Analysis of movement in the pension deficit

	2011 £m	2010 £m
At 1 October	5.3	4.7
Addition of two smaller schemes	0.4	-
Amounts credited to Income Statement	(0.2)	(0.1)
Contributions paid by employer	(0.3)	(1.1)
Actuarial loss	0.2	1.8
<b>At 30 September</b>	<b>5.4</b>	<b>5.3</b>

### Analysis of the movements in the present value of the Scheme liabilities

	2011 £m	2010 £m
At 1 October	21.6	18.8
Addition of two smaller schemes	2.9	-
Interest cost	1.2	1.0
Actuarial loss/(gain)	0.5	(0.1)
(Gain)/loss on changes in assumptions	(2.1)	2.2
Benefits paid	(0.5)	(0.3)
<b>At 30 September</b>	<b>23.6</b>	<b>21.6</b>

## Notes to the Consolidated Financial Statements continued

### For the year ended 30 September 2011

#### 25 Retirement Benefit Obligations continued

##### Analysis of the movements in the present value of the Scheme assets

	2011 £m	2010 £m
At 1 October	163	141
Addition of two smaller schemes	25	–
Expected return on assets	14	1.1
Actuarial (loss)/gain	(1.8)	0.3
Contributions paid by employer	0.3	1.1
Benefits paid	(0.5)	(0.3)
<b>At 30 September</b>	<b>182</b>	<b>163</b>

The actual return on Scheme assets during the year was a £0.4m loss (2010 gain £1.4m)

##### Principal actuarial assumptions for the Schemes at balance sheet dates

	2011	2010	2009
Inflation rate – RPI	3.2%	3.2%	3.4%
– CPI	2.5%	–	–
Expected rate of pension increases – RPI	3.2%	3.2%	3.4%
– CPI	2.5%	–	–
Discount rate	5.1%	5.0%	5.5%
Number of years a current pensioner is expected to live beyond age 65			
Men	22.3	22.1	22.1
Women	24.6	25.0	25.0
Expected return on Scheme assets <sup>1</sup>			
Analysed as			
Equities	8.0%	8.0%	8.0%
Bonds	3.8%	5.0%	5.5%
Cash	1.0%	1.0%	2.0%

##### Demographic assumptions

Basic mortality table used	SINA
Year the mortality table was published	CMI 2010
Allowance for future improvements in longevity	Year of birth projections with a long-term improvement rate of 1.25%
Allowance made for members to take a cash lump sum on retirement	Members are assumed to take 100% of their maximum cash sum (based on current commutation factors)

##### Sensitivities

Sensitivity of 2011 pension liabilities to changes in assumptions are as follows

Assumption	Assumption	Impact on pension liabilities	
		Estimated increase %	Estimated increase £m
Discount rate	Decrease by 0.5%	9.3	2.2
Expected rate of pension increase	Increase by 0.5%	3.8	0.9
Life expectancy	Increase by 1 year	1.3	0.3

1. The expected return for each class of scheme assets is based on a combination of historical performance, current market yields and advice from investment managers.

## 25 Retirement Benefit Obligations continued

### Cash funding

Accounting costs do not impact on the incidence or amount of cash contributions for defined benefit plans. Future cash contributions are determined based upon triennial actuarial valuations.

Date of last formal funding valuation	30 September 2010
Deficit	£2,682 000
Funding level	87%
Funding approach	Assumes that Scheme assets will outperform Government 20 year fixed interest gilt yield by 2.90% pa pre-retirement and 0.80% pa post-retirement
Post retirement mortality table	S1NA
Post retirement mortality projections	CMI 2010 with long term improvement rate of 1.25% pa
Contributions per annum to remove the deficit	£320 000
Period over which the deficit is expected to be removed	1 October 2010 – 30 September 2021
Expected contributions during FY2012	£326 400
Current investment strategy	80% Equities/20% Bonds
Number of deferred members at date of actuarial valuation	344

### History of experience gains and losses

All experience adjustments are recognised directly in equity net of related tax

	2011	2010 <sup>1</sup>	2009 <sup>1</sup>	2008 <sup>1</sup>	2007 <sup>1</sup>
Experience adjustments arising on Scheme assets					
Amount (£m)	(0.4)	0.3	0.7	(3.4)	0.3
% of Scheme assets	2%	2%	5%	27%	2%
Changes in assumptions arising on present value of Scheme liabilities					
Amount (£m)	2.1	(2.2)	(3.8)	3.0	2.3
% of present value of Scheme liabilities	9%	10%	20%	21%	14%
Experience adjustments arising on present value of Scheme liabilities					
Amount (£m)	(0.5)	0.1	–	(0.1)	0.1
% of present value of Scheme liabilities	2%	–	–	1%	1%
Present value of Scheme liabilities	(23.6)	(21.6)	(18.8)	(14.2)	(16.4)
Market value of Scheme assets	18.2	16.3	14.1	12.5	14.8
Deficit	(5.4)	(5.3)	(4.7)	(1.7)	(1.6)

1 Amounts relate only to the two principal schemes

## 26 Commitments

At 30 September 2011 the Group has total lease payments under non-cancellable operating leases as follows

	Land and Buildings	
	2011 £m	2010 £m
Lease payments due		
Within one year	1.4	1.3
Within two to five years	2.3	2.3
After five years	0.6	–
Total payable at 30 September	4.3	3.6

Operating lease payments made in respect of land and buildings during the year were £1.4m (2010: £1.3m)

## Notes to the Consolidated Financial Statements continued

### For the year ended 30 September 2011

#### 27 Audit Fees

During the year the Group received the following services from the auditor

	2011 £ m	2010 £ m
Fees payable to the auditor for the audit of		
– the Company's annual report	0.1	0.1
– the Company's subsidiaries pursuant to legislation	0.2	0.1
<b>Total audit fees</b>	<b>0.3</b>	<b>0.2</b>

Non audit fees of £11,000 (2010: £7,000) for taxation advisory services provided in Canada and Denmark and £10,500 (2010: £10,000) in connection with the Half Year Announcement were paid to the Group's auditor

#### 28 Exchange Rates

The following exchange rates have been used to translate the results of the overseas businesses

	Average		Closing	
	2011	2010	2011	2010
US dollar	1.61	1.56	1.56	1.58
Canadian dollar	1.59	1.63	1.62	1.62
Euro	1.15	1.15	1.16	1.15

# Group Accounting Policies

## For the year ended 30 September 2011

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as endorsed by the European Union and in accordance with the Companies Act 2006 as applicable to companies reporting under IFRS. The accounting policies set out below have been consistently applied in 2011 and the comparative period. The following new standards, amendments and interpretations to existing standards have been published and have been endorsed by the EU, these are mandatory for the first time for the year ended 30 September 2011:

- Amendment to IFRS 2 "Share-based Payments" – cash settled share-based payment transactions
- Amendment to IAS 32 "Financial Instruments: Presentation" – classification of rights issues and
- Annual Improvements to IFRSs issued April 2009 and May 2010

The introduction of these amendments has had no impact on the results, financial position or presentation of the financial statements.

### 1 Group Accounting Policies

#### 1.1 Basis of preparation

The consolidated financial statements have been prepared under the historical cost convention, except for derivative financial instruments which are held at fair value. The consolidated financial statements have been prepared on a going concern basis, as discussed on page 44.

#### 1.2 Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company (its subsidiaries). Control exists when the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. The results of subsidiaries acquired or disposed of during the year are included in the consolidated Income Statement from the effective date of acquisition or up to the effective date of disposal, as appropriate.

Where necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with those detailed herein to ensure that the Group financial statements are prepared on a consistent basis. All intra-group transactions, balances, income and expenses are eliminated in preparing the consolidated financial statements.

Non-controlling interests, defined as minority interests in the net assets of consolidated subsidiaries, are identified separately from the Group's equity therein. Minority interests consist of the amount of those interests at the date of the original business combination and the minority's share of changes in equity since the date of the combination.

#### 1.3 Divestments

The results and cash flows of major lines of businesses that have been divested have been classified as discontinued businesses.

#### 1.4 Revenue recognition

Revenue is measured as the fair value of the consideration received or receivable for goods supplied and services rendered to customers, after deducting sales allowances and value added taxes. Revenue is recognised when the risk and rewards of ownership transfers to the customer, which depending on individual customer terms is at the time of despatch, delivery or upon formal customer acceptance. Provision is made for returns where appropriate. Service revenue received in advance is deferred and recognised over the period of the contract.

#### 1.5 Employee benefits

The Group operates a number of pension plans, both of the defined contribution and defined benefit type. The defined benefit schemes are closed to the accrual of future benefits.

- (a) Defined contribution pension plans: Contributions to the Group's defined contribution schemes are recognised as an employee benefit expense when they fall due.
- (b) Defined benefit pension plans: The deficit recognised in the balance sheet for the Group's defined benefit pension schemes is the present value of the defined benefit obligation at the balance sheet date less the fair value of the scheme assets. The defined benefit obligation is calculated by independent actuaries using the projected unit cost method and by discounting the estimated future cash flows using interest rates on high quality corporate bonds. The pension expense for the Group's defined benefit plans is recognised as follows:
  - (i) Within profit before tax:
    - Gains and losses arising on settlements and curtailments – where the item that gave rise to the settlement or curtailment is recognised in operating profit
    - Interest cost on the liabilities of the schemes – calculated by reference to the scheme liabilities and major assumptions, including the discount rate at the beginning of the year, and
    - Expected return on the assets of the schemes – calculated by reference to the scheme assets and long-term expected rate of return at the beginning of the year
  - (ii) Within the Statement of Comprehensive Income:
    - Actuarial gains and losses arising on the assets and liabilities of the schemes arising from actual experience and any changes in assumptions at the end of the year

The Group has adopted a policy of recognising all actuarial gains and losses for all of its defined benefit schemes in the period in which they occur, outside the Income Statement, in the consolidated Statement of Comprehensive Income.

## Group Accounting Policies continued

### For the year ended 30 September 2011

#### 1 Group Accounting Policies continued

##### (c) Share-based payments

The Executive Directors of the Group receive part of their remuneration in the form of share-based payment transactions whereby the Directors render services in exchange for shares in the Company or rights over shares ("equity-settled" transactions)

Equity-settled transactions are measured at fair value at the date of grant. The fair value determined at the grant date takes account of the effect of market based measures, such as the Total Shareholder Return ("TSR") targets upon which vesting of part of the award is conditional, and is expensed to the Income Statement on a straight line basis over the vesting period with a corresponding credit to equity. The cumulative expense recognised is adjusted to take account of shares forfeited by Executives who leave during the performance or vesting period and in the case of non-market related performance conditions where it becomes unlikely that shares will vest. For the market based measure the Directors have used a predicted future value model to determine fair value of the shares at the date of grant.

The Group operates an Employee Benefit Trust for the granting of shares to Executives. The cost of shares in the Company purchased by the Employee Benefit Trust are shown as a deduction from equity.

#### 1.6 Foreign currencies

The individual financial statements of each Group entity are prepared in their functional currency which is the currency of the primary economic environment in which that entity operates. For the purpose of the consolidated financial statements, the results and financial position of each entity are translated into UK sterling which is the presentational currency of the Group.

##### (a) Reporting foreign currency transactions in functional currency

Transactions in currencies other than the entity's functional currency (foreign currencies) are initially recorded at the rates of exchange prevailing on the dates of the transactions. At each subsequent balance sheet date:

- (i) Foreign currency monetary items are retranslated at the rates prevailing at the balance sheet date. Exchange differences arising on the settlement or retranslation of monetary items are recognised in the Income Statement,
- (ii) Non-monetary items measured at historical cost in a foreign currency are not retranslated and
- (iii) Non-monetary items measured at fair value in a foreign currency are retranslated using the exchange rates at the date the fair value was determined. Where a gain or loss on non-monetary items is recognised directly in equity, any exchange component of that gain or loss is also recognised directly in equity and conversely where a gain or loss on a non-monetary item is recognised in the Income Statement, any exchange component of that gain or loss is also recognised in the Income Statement.

##### (b) Translation from functional currency to presentational currency

When the functional currency of a Group entity is different from the Group's presentational currency its results and financial position are translated into the presentational currency as follows:

- (i) Assets and liabilities are translated using exchange rates prevailing at the balance sheet date
- (ii) Income and expense items are translated at average exchange rates for the year except where the use of such an average rate does not approximate the exchange rate at the date of the transaction in which case the transaction rate is used, and
- (iii) All resulting exchange differences are recognised in translation reserves as a separate component of equity. These cumulative exchange differences are recognised in the Income Statement in the period in which the foreign operation is disposed of.

##### (c) Net investment in foreign operations

Exchange differences arising on a monetary item that forms part of a reporting entity's net investment in a foreign operation are recognised in the Income Statement in the separate financial statements of the reporting entity or the foreign operation as appropriate. In the consolidated Group accounts such exchange differences are initially recognised in translation reserves as a separate component of equity and subsequently recognised in the Income Statement on disposal of the net investment.

#### 1.7 Taxation

The tax expense relates to the sum of current tax and deferred tax.

Current tax is based on taxable profit for the year which differs from profit before taxation as reported in the Income Statement. Taxable profit excludes items of income and expense that are taxable (or deductible) in other years and also excludes items that are never taxable or deductible. The Group's liability for current tax including UK corporation tax and overseas tax, is calculated using rates that have been enacted or substantively enacted at the balance sheet date.

Deferred tax is accounted for using the balance sheet liability method. Deferred tax is recognised on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. Temporary differences arise primarily from the recognition of the deficit on the Group's defined benefit pension schemes, the difference between accelerated capital allowances and depreciation and for short-term timing differences where a provision held against receivables or stock is not deductible for taxation purposes. However, deferred tax assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the tax profit nor the accounting profit.

### 1 Group Accounting Policies continued

Deferred tax liabilities are also recognised for taxable temporary differences arising on investments in subsidiaries except where the Group is able to control the reversal of the temporary difference and it is possible that the temporary difference will not reverse in the foreseeable future. No deferred tax is recognised on the unremitted earnings of overseas subsidiaries as the Group controls the dividend policies of its subsidiaries.

Deferred tax is calculated at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled. Deferred tax is charged or credited to the Income Statement, except when the item on which the tax or charged is credited or charged directly to equity in which case the deferred tax is also dealt with in equity. The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the assets to be recovered. Tax assets and liabilities are offset when there is a legally enforceable right to enforce current tax assets against current tax liabilities and when the deferred income tax relates to the same fiscal authority.

### 1.8 Property, plant and equipment

Freehold land is carried at cost less accumulated impairment losses. Other items of property, plant and equipment are carried at cost less accumulated depreciation and accumulated impairment losses. Cost comprises the purchase price plus costs directly incurred in bringing the asset into use, but excluding interest. All other repairs and maintenance expenditure is charged to the Income Statement in the period in which it is incurred.

Freehold land is not depreciated as it has an infinite life. Depreciation on other items of property, plant and equipment begins when the asset is available for use and is charged to the Income Statement on a straight-line basis so as to write off the cost less residual value of the asset over its estimated useful life as follows:

- Freehold property – between 20 and 50 years
- Leasehold property – term of the lease
- Plant and equipment – plant and machinery between 3 and 7 years
  - IT hardware between 3 and 5 years
  - fixtures and fittings between 5 and 15 years

The depreciation method used, residual values and estimated useful lives are reviewed and changed if appropriate at least at each financial year end. Assets held under finance leases are depreciated over their expected useful lives on the same basis as owned assets or where shorter over the term of the relevant lease. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. Gains and losses arising on disposals are determined by comparing sales proceeds with carrying amount and are recognised in the Income Statement.

### 1.9 Intangible assets

All intangible assets, excluding goodwill arising on a business combination, are stated at their amortised cost or fair value less any provision for impairment.

#### (a) Research and development costs

Research expenditure is written off as incurred. Development costs are written off as incurred until it can be demonstrated that the conditions for capitalisation as described in IAS 38 (Intangible Assets) are met. At which point further costs are capitalised as intangible assets up until the intangible asset is readily available for production and amortised on a straight-line basis over the asset's estimated useful life.

Costs are capitalised as intangible assets unless physical assets, such as tooling, exist when they are classified as property, plant and equipment.

#### (b) Computer software costs

Where computer software is not integral to an item of property, plant or equipment its costs are capitalised as other intangible assets. Amortisation is provided on a straight line basis over its useful economic life of between three and seven years.

#### (c) Acquired intangible assets – business combinations

Intangible assets that are acquired as a result of a business combination, including but not limited to customer lists, supplier lists, databases, technology and software and patents and that can be separately measured at fair value on a reliable basis, are separately recognised on acquisition at the fair value together with the associated deferred tax liability. Amortisation is charged on a straight line basis to the Income Statement over the expected useful economic lives.

#### (d) Goodwill – business combinations

Goodwill arising on the acquisition of a subsidiary represents the excess of the aggregate of the fair value of the consideration over the aggregate fair value of the identifiable intangible and tangible assets and net of the aggregate fair value of the liabilities (including contingent liabilities of businesses acquired at the date of acquisition). Goodwill is initially recognised as an asset at cost and is subsequently measured at cost less any accumulated impairment losses. Impairment testing is carried out annually or more frequently if events or changes in circumstances indicate that the carrying value may be impaired. Goodwill on acquisitions is not amortised.

## Group Accounting Policies continued

### For the year ended 30 September 2011

#### 1 Group Accounting Policies continued

##### 1.10 Impairment of tangible and intangible assets

An impairment loss is recognised to the extent that the carrying amount of an asset or cash generating unit exceeds its recoverable amount

The recoverable amount of an asset or cash-generating unit is the higher of (i) its fair value less costs to sell and (ii) its value in use. Its value in use is the present value of the future cash flows expected to be derived from the asset or cash-generating unit, discounted using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset or cash-generating unit. Impairment losses are recognised immediately in the Income Statement.

##### (a) Impairment of goodwill

Goodwill acquired in a business combination is allocated to a cash-generating unit. Cash-generating units for this purpose are the business entities which represent the lowest level within the Group at which the goodwill is monitored by the Group's Board of Directors for internal and management purposes. Cash-generating units to which goodwill has been allocated are tested for impairment annually, or more frequently when there is an indication that the unit may be impaired.

If the recoverable amount of the cash-generating unit is less than the carrying amount of the unit, the impairment loss is allocated first to reduce the goodwill attributable to the cash-generating unit.

An impairment loss recognised for goodwill is not reversed in a subsequent period.

##### (b) Impairment of other tangible and intangible assets

At each balance sheet date, the Group reviews the carrying amount of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent, if any, of the impairment loss. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash inflows. Where it is not possible to estimate the recoverable amount of an individual asset, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs.

Where an impairment loss subsequently reverses, the carrying amount of the asset or cash-generating unit is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset or cash-generating unit in prior years. A reversal of an impairment loss for tangible and intangible assets other than goodwill is recognised immediately in the Income Statement.

##### 1.11 Inventories

Inventories are stated at the lower of cost, (generally calculated on a weighted average cost basis) and net realisable value, after making due allowance for any obsolete or slow moving inventory. Cost comprises direct materials, duty and freight-in costs.

Net realisable value represents the estimated selling price less all estimated costs of completion and the estimated costs necessary to make the sale.

##### 1.12 Financial instruments

Financial assets and liabilities are recognised in the Group balance sheet when the Group becomes a party to the contractual provisions of the instrument.

##### (a) Trade receivables

Trade receivables are initially measured at fair value, do not carry any interest and are reduced by a charge for impairment for estimated irrecoverable amounts. Such impairment charges are recognised in the Income Statement.

##### (b) Trade payables

Trade payables are non-interest bearing and are initially measured at their fair value.

##### (c) Cash and cash equivalents

Cash and cash equivalents comprise cash in hand, interest bearing deposits, bank overdrafts and short-term highly liquid investments with original maturities of three months or less that are readily convertible to a known amount of cash and are subject to an insignificant risk of changes in value. Bank overdrafts are repayable on demand and can form an integral part of the Group's cash management system.

##### (d) Put options held by minority interests

On exercise of put options held by minority shareholders in the Group's subsidiaries, the purchase price of the shares is calculated by reference to the profitability of the relevant subsidiary at the time of exercise, using a multiple based formula. The net present value of the estimated future payments under these put options is shown as a financial liability. The corresponding entry is recognised in equity as a deduction against retained earnings. At the end of each year, the estimate of the financial liability is reassessed and any change in value is recognised in the Income Statement, as part of finance income or expense. Where the liability is in a foreign currency, any change in the value of the liability resulting from changes in exchange rates is recognised in the Income Statement.

## 1 Group Accounting Policies continued

### (e) Derivative financial instruments and hedge accounting

The Group uses derivative financial instruments in the form of forward foreign exchange contracts to manage the effects of its exposures to fluctuations in foreign exchange arising from operational and financial activities. In accordance with its treasury policy, the Group does not hold or issue derivative financial instruments for trading purposes. The fair value of forward foreign exchange contracts is their quoted market price at the balance sheet date.

Under IAS 39, hedging relationships are categorised by type and must meet strict criteria to qualify for hedge accounting. At the inception of the transaction, the Group documents the relationship between the hedging instrument and the hedged item. The Group also documents its assessment, both at hedge inception and on an ongoing basis, of whether the financial instruments that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items. The Group uses cash flow hedges (eg forward foreign exchange currency contracts) to hedge exposure to variability in cash flows of a highly probable forecast transaction.

In relation to cash flow hedges to hedge firm commitments which meet the conditions for hedge accounting, the portion of the gain or loss on the hedging instrument that is determined to be an effective hedge is recognised directly to equity and the ineffective portion is recognised in net profit or loss. For cash flow hedges that do not result in the recognition of an asset or a liability, the gains or losses that are recognised in equity are transferred to the Income Statement in the same year in which the hedged firm commitment affects the net profit and loss, for example when the future sale actually occurs.

Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated or exercised, or no longer qualifies for hedge accounting. At that point in time, any cumulative gain or loss on the hedging instrument recognised in equity is kept in equity until the hedged transaction occurs. If a hedged transaction is no longer expected to occur, the net cumulative gain or loss recognised in equity is transferred to net profit or loss for the year.

The Group does not use financial instruments to hedge the exposure to changes in the fair value of recognised assets or liabilities that are attributable to a particular risk and could affect profit or loss (fair value hedges). No financial instruments are used to hedge net investments in a foreign operation (net investment hedges).

### 1.13 Leases

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risk and rewards of ownership to the lessee. Leases include hire purchase contracts which have characteristics similar to finance or operating leases. All other leases are classified as operating leases.

#### (a) Finance leases

Assets held under finance leases are recognised as assets of the Group at their fair value at the inception of the lease or, if lower, at the present value of the minimum lease payments. The corresponding liability to the lessor is included in the balance sheet as a finance lease obligation. Lease payments are apportioned between finance charges and reduction of the lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged to the Income Statement.

#### (b) Operating leases

Rentals payable under operating leases are charged to the Income Statement on a straight-line basis over the term of the relevant lease. Benefits received and receivable as an incentive to enter into an operating lease are also spread on a straight-line basis over the expected lease term.

### 1.14 Other liabilities

Other liabilities are recognised when the Group has legal or constructive obligation as a result of a past event and it is possible that the Group will be required to settle that obligation. Other liabilities are measured at the Director's best estimate of the expenditure required to settle the obligation at the balance sheet date.

### 1.15 Dividends

The annual final dividend is not provided for until approved at the Annual General Meeting. Interim dividends are charged in the period they are paid.

### 1.16 Share capital and reserves

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of new shares are shown in equity as a deduction, net of tax, from the proceeds. The Group also maintains the following reserves:

- (a) Translation reserve – The translation reserve comprises all foreign exchange differences arising from the translation of the financial statements of foreign businesses.
- (b) Hedging reserve – The hedging reserve comprises the effective portion of the cumulative net change in the fair value of cash flow hedging instruments that are determined to be an effective hedge.
- (c) Retained earnings reserve – The retained earnings reserve comprises total recognised income and expense for the year attributable to shareholders. Bonus issues of share capital and dividends to shareholders are also charged directly to this reserve. On acquisition of minority interests, the liability held in the consolidated financial statements for the future purchases of those minority interests is released to the retained earnings reserve. In addition, the cost of acquiring shares in the Company and the liability to provide those shares to employees is accounted for in this reserve.

## Group Accounting Policies continued

### For the year ended 30 September 2011

#### 1 Group Accounting Policies continued

Where any Group company purchases the Company's equity share capital and holds that share either directly as treasury shares or indirectly within an ESOP trust the consideration paid including any directly attributable incremental costs (net of income taxes) is deducted from equity attributable to the Company's equity holders until the shares are cancelled, reissued or disposed of. Where such shares are subsequently sold or reissued, any consideration received, net of any directly attributable incremental transaction costs and the related income tax effects, is included in equity attributable to the Company's equity holders. These shares are used to satisfy share awards granted to Directors under the Group's share schemes. The trustee purchases the Company's shares on the open market using loans made by the Company or a subsidiary of the Company.

#### 1.17 Accounting standards, interpretations and amendments to published standards not yet effective

The following new standards, amendments and interpretations to existing standards have been published and have been endorsed by the EU that are mandatory for the Group's accounting periods beginning on or after 1 October 2011:

- IFRS 9 "Financial Instruments – Classification and Measurement"
- IFRS 10 "Consolidated Financial Statements",
- IFRS 11 "Joint Arrangements"
- IFRS 12 "Disclosure of Interests in Other Entities"
- IFRS 13 "Fair Value Measurement"
- IAS 19 "Employee Benefits"
- IAS 27 "Separate Financial Statements"
- IAS 28 "Investments in Associates and Joint Ventures"
- Amendment to IFRS 7 "Financial Instruments: Disclosures" enhancing disclosures about transfers of financial assets
- Amendment to IAS 1 "Presentation of Financial Statements", revision of presentation of comprehensive income
- Amendment to IAS 12 "Income Taxes" recovery of underlying assets
- Amendment to IAS 24 "Related Party Disclosures" revised definition of related parties and
- Annual Improvements to IFRSs issued May 2010

The Group has considered the impact of these new standards and interpretations in future periods and no significant impact is expected on reported profit or net assets.

The Group has chosen not to early adopt any of these new standards and interpretations.

#### 2 Critical Accounting Estimates and Judgements

In order to prepare these consolidated financial statements in accordance with the accounting policies set out in note 1 above, management has used estimates and judgements to establish the amounts at which certain items are recorded. Critical accounting estimates and judgements are those which have the greatest impact on the financial statements and require the most difficult and subjective judgements about matters that are inherently uncertain. Estimates are based on factors including historical experience and expectations of future events that management believe to be reasonable. However, given the judgemental nature of such estimates, actual results could be different from the assumptions used. The critical accounting estimates and judgements are set out below:

##### 2.1 Goodwill impairment

The Directors use their judgement to determine the extent to which goodwill has a value that will benefit the performance of the Group over future periods. To assist in making this judgement, the Directors undertake an assessment, at least annually, of the carrying value of the Group's capitalised goodwill, using discounted cash flow forecasts to derive the "value in use" to the Group of the capitalised goodwill. This calculation is usually based on projecting future cash flows over at least a five year period and using a terminal value to incorporate expectations of growth thereafter. A discount factor is applied to obtain a current value ("value in use"). The "fair value less costs to sell" of an asset is used if this results in an amount in excess of "value in use".

Estimated future cash flows for impairment calculations are based on management's expectations of future volumes and margins based on plans and best estimates of the productivity of the assets in their current condition. Future cash flows therefore exclude benefits from major expansion projects requiring future capital expenditure where that expenditure has not been approved at the balance sheet date.

Future cash flows are discounted using discount rates based on the Group's weighted average cost of capital, adjusted if appropriate for circumstances specific to the asset being tested. The weighted average cost of capital is impacted by estimates of interest rates, equity returns and market and country related risks. The Group's weighted average cost of capital is reviewed on an annual basis.

The projection period is, in the opinion of the Directors, an appropriate period over which to view the future results of the Group's businesses for this purpose. Changes to the assumptions and discount rates used in making these forecasts could significantly alter the Directors' assessment of the carrying value of goodwill.

##### 2.2 Retirement benefits

The Group's financial statements include the costs and obligations associated with the provision of pension retirement benefits to current and former employees. It is the Directors' responsibility to set the assumptions used in determining the key elements of the costs of meeting such future obligations. These assumptions are set after consultation with the Scheme's actuary and are consistent with those assumptions used to determine the financing elements related to the Scheme's assets and liabilities. Whilst the Directors believe that the assumptions used are appropriate, a change in the assumptions used would affect the Group profit and financial position. Details of these assumptions, which are based on advice from the Scheme's actuary, are set out in note 25.

## 2 Critical Accounting Estimates and Judgements continued

### 2.3 Taxation

The Group operates in a number of tax jurisdictions around the world. Tax regulations generally are complex and in some jurisdictions agreeing tax liabilities with local tax authorities can take several years. Consequently at the balance sheet date tax liabilities and assets are based on management's best estimate of the future amounts that will be settled. While the Group aims to ensure that the estimates recorded are accurate, the actual amounts could be different from those expected.

Deferred tax assets mainly represent timing differences that the Group expects to recover at some time in the future and by their nature, the amounts recorded are therefore dependent on management's judgement about future events. Account has also been taken of future forecasts of taxable profit in arriving at the values at which these deferred tax assets are recognised. If these forecast profits do not materialise or change, or there are changes in tax rates or to the period over which the timing difference might be recognised, then the value of the deferred tax asset will need to be revised in a future period.

### 2.4 Current assets

In the course of normal trading activities, judgement is used to establish the net realisable value of various elements of working capital, principally inventory and trade receivables. Impairment charges are made against obsolete or slow-moving inventories, bad or doubtful debts.

The decision to make an impairment charge is based on the facts available at the time the financial statements are approved and are also determined by using profiles based on past practice applied to certain aged inventory and trade receivables categories. In estimating the collectability of trade receivables, judgement is required in assessing their likely realisation, including the current creditworthiness of each customer and related ageing of the past due balances. Specific accounts are assessed in situations where a customer may not be able to meet its financial obligations due to deterioration of its financial condition, credit ratings or bankruptcy.

### 2.5 Property, plant and equipment

It is Group policy to depreciate its property, plant and equipment assets, except freehold land, on a straight-line basis over their estimated useful lives. This applies an appropriate matching of the revenue earned with the delivery of goods and services. A key element of this policy is the estimate of the useful life applied to each category of property, plant and equipment which, in turn, determines the annual depreciation charge. Variations in asset lives could impact Group profit through an increase or decrease in the depreciation charge.

### 2.6 Future purchases of minority interests

The Group's financial statements include a financial liability for the net present value of the expected amount that it will pay in future years to acquire the outstanding shares held by minority shareholders in the Group's subsidiaries. This amount is based on the Directors' estimate of the future profitability of the relevant subsidiary and on an assumption of the exchange rates prevailing at the time the payment is made. Any changes to the estimated profitability of the relevant business and/or changes to the assumption of the relevant exchange rate will change the estimate of this financial liability.


## Parent Company Balance Sheet

As at 30 September 2011

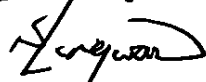
	Note	2011 £m	2010 £m
<b>Fixed assets</b>			
Investments	c	720	720
<b>Creditors amounts falling due within one year</b>			
Amounts owed to subsidiary undertakings		(42.2)	(42.3)
<b>Total assets less current liabilities</b>		<b>298</b>	<b>297</b>
<b>Capital and reserves</b>			
Called up equity share capital	d	57	57
Profit and loss account		241	240
		<b>298</b>	<b>297</b>

The financial statements of Diploma PLC, company number 3899848 were approved by the Board of Directors on 21 November 2011 and signed on its behalf by

BM Thompson  
Chief Executive Officer



NP Lingwood  
Group Finance Director



The notes on page 75 form part of these financial statements

## Reconciliation of Movements in Shareholders' Funds

For the year ended 30 September 2011

	Share capital £m	Profit and loss account £m	Total £m
<b>At 1 October 2010</b>	57	240	297
Retained profit for the year	–	1.3	1.3
Transfer of own shares net	–	(1.2)	(1.2)
<b>At 30 September 2011</b>	<b>57</b>	<b>241</b>	<b>298</b>

# Notes to the Parent Company Financial Statements

## For the year ended 30 September 2011

### a) Accounting Policies

#### a 1 Basis of accounting

These financial statements have been prepared on a going concern basis as discussed on page 44 under the historical cost convention in accordance with the Companies Act 2006 and applicable UK accounting standards. A summary of the accounting policies of the Parent company ("the Company") is set out below. As permitted by section 408 of the Companies Act 2006 no separate profit and loss account is presented for the Company.

#### a 2 Investments and dividends

Investments are stated at cost less provision for impairment. Dividend income is recognised when received. Dividend distributions are recognised in the Company's financial statements in the year in which the dividends are approved by the Company's shareholders. Interim dividends are recognised when paid.

#### a 3 Employment Benefit Trust and Employee Share Schemes

Shares held by the Diploma Employee Benefit Trust ("the Trust") are stated at cost and accounted for as a deduction from shareholders' funds in accordance with UITF 38. Shares that are held by the Trust are not eligible for dividends until such time as the awards have vested to the employees.

### b) Directors' Remuneration

No emoluments are paid directly by the Company. Information on the Directors' remuneration and interests in the share capital of the Company are set out in the Remuneration Report on pages 32 to 41.

### c) Investments

	£m
<b>Shares in Group undertakings</b>	
At 30 September 2011 and 1 October 2010	<b>72.0</b>

Details of the principal subsidiaries are set out on page 78.

### d) Share Capital

	2011 Number	2010 Number	2011 £m	2010 £m
<b>Allotted, issued and fully paid ordinary shares of 5p each</b>				
At 30 September	<b>113,239,555</b>	<b>113,239,555</b>	<b>5.7</b>	<b>5.7</b>

During the year 138,461 shares were transferred from the Diploma Employee Benefit Trust to participants in connection with vesting of awards under the Long Term Incentive Plan. During the year the Trust purchased a further 500,000 shares for an aggregate amount of £1.6m. In accordance with UITF 38 the purchase cost of own shares net of shares which have vested, are shown as a movement in shareholders' funds.

At 30 September 2011 the Trust held 1,094,512 (2010: 732,973) ordinary shares in the Company representing 1.0% of the called up share capital. The market value of the shares at 30 September 2011 was £3.5m (2010: £2.1m).

## Independent Auditor's Reports

### For the year ended 30 September 2011

#### Independent Auditor's Report on the Group financial statements to the Members of Diploma PLC

We have audited the Group financial statements of Diploma PLC for the year ended 30 September 2011 which comprise the consolidated income statement the consolidated statement of financial position, the consolidated cash flow statement the consolidated statement of comprehensive income the consolidated statement of changes in shareholders' equity the Group accounting policies and the related notes 1 to 28. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

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.

#### Respective responsibilities of directors and auditor

As explained more fully in the Statement of Directors' Responsibilities for preparing the Financial Statements, the directors are responsible for the preparation of the Group financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the Group financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's (APB's) Ethical Standards for Auditors.

#### Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of whether the accounting policies are appropriate to the Group's circumstances and have been consistently applied and adequately disclosed, the reasonableness of significant accounting estimates made by the directors, and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

#### Opinion on financial statements

In our opinion the Group financial statements

- give a true and fair view of the state of the Group's affairs as at 30 September 2011 and of its profit for the year then ended
- have been properly prepared in accordance with IFRSs as adopted by the European Union, and
- have been prepared in accordance with the requirements of the Companies Act 2006 and Article 4 of the IAS Regulation.

#### Opinion on other matter prescribed by the Companies Act 2006

In our opinion the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the Group financial statements.

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

We have nothing to report in respect of the following:

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- certain disclosures of directors' remuneration specified by law are not made, or
- we have not received all the information and explanations we require for our audit.

Under the Listing Rules we are required to review:

- the directors' statement contained within the Directors' Report in relation to going concern
- the part of the Corporate Governance Statement relating to the Company's compliance with the nine provisions of the UK Corporate Governance Code specified for our review, and
- certain elements of the report to shareholders by the Board on directors' remuneration.

#### Other matter

We have reported separately on the Parent company financial statements of Diploma PLC for the year ended 30 September 2011 and on the information in the Directors' Remuneration Report that is described as having been audited.

*Ian Waller*

Ian Waller (Senior Statutory Auditor)  
for and on behalf of Deloitte LLP  
Chartered Accountants and Statutory Auditor  
London  
21 November 2011

#### **Independent Auditor's Report on the Parent Company financial statements to the Members of Diploma PLC**

We have audited the Parent company financial statements of Diploma PLC for the year ended 30 September 2011 which comprise the Parent company balance sheet, the reconciliation of movements in shareholders' funds and the related notes a) to d). The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice)

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.

#### **Respective responsibilities of directors and auditor**

As explained more fully in the Statement of Directors' Responsibilities for preparing the Financial Statements, the directors are responsible for the preparation of the Parent company financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the Parent company financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's (APB's) Ethical Standards for Auditors.

#### **Scope of the audit of the financial statements**

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of whether the accounting policies are appropriate to the Parent company's circumstances and have been consistently applied and adequately disclosed, the reasonableness of significant accounting estimates made by the directors, and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

#### **Opinion on financial statements**

In our opinion the Parent company financial statements

- give a true and fair view of the state of the Parent company's affairs as at 30 September 2011
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice, and
- have been prepared in accordance with the requirements of the Companies Act 2006.

#### **Opinion 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, and
- the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the Parent company financial statements.

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

We have nothing to report in respect of the following matters where 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.

#### **Other matter**

We have reported separately on the Group financial statements of Diploma PLC for the year ended 30 September 2011.

*Ian Waller*

Ian Waller (Senior Statutory Auditor)  
for and on behalf of Deloitte LLP  
Chartered Accountants and Statutory Auditor  
London  
21 November 2011

## Principal Subsidiaries

	Group percentage of equity capital	Country of incorporation or registration
<b>Life Sciences</b>		
a1-envirosciences Limited	100%	England
a1-envirosciences GmbH	100%	Germany
a1-envirosciences AG (formerly a1-safetech AG)	100%	Switzerland
Somagen Diagnostics Inc	100%	Canada
AMT Electrosurgery Inc	100%	Canada
Vantage Endoscopy Inc (formerly Carsen Medical Inc)	100%	Canada
Big Green Surgical Company Pty Limited	80%	Australia
<b>Seals</b>		
Hercules Sealing Products Inc	100%	USA
RTD Seats Corp	100%	USA
All Seats Inc	100%	USA
HKX Inc	100%	USA
Hercules Europe BV	100%	Netherlands
M Seats A/S	90%	Denmark
FPE Limited	100%	England
<b>Controls</b>		
IS Rayfast Limited	100%	England
IS Motorport Inc	100%	USA
Clarendon Engineering Supplies Limited	100%	England
Cabletec Interconnect Components Systems Limited	100%	England
Sommer GmbH	100%	Germany
Filcon GmbH	100%	Germany
HA Wainwright (Group) Limited	100%	England
Hitek Limited	100%	England
<b>Other Companies</b>		
Diploma Holdings PLC	100%	England
Diploma Holdings Inc	100%	USA

A full list of subsidiaries will be annexed to the next Annual Return of Diploma PLC filed with the Registrar of Companies

## Financial Calendar and Shareholder Information

### Announcements (provisional dates)

Interim Management Statement released	18 January 2012
Interim Management Statement released	3 August 2012
Half Year Results announced	14 May 2012
Preliminary Results announced	19 November 2012
Annual Report posted to shareholders	3 December 2012
Annual General Meeting (2011)	18 January 2012
Annual General Meeting (2012)	16 January 2013
Dividends (provisional dates)	
Interim announced	14 May 2012
Paid	20 June 2012
Final announced	19 November 2012
Paid (if approved)	23 January 2013

### Annual Report

Copies can be obtained from the Company Secretary at the address shown below

### Share Registrar – Computershare Investor Services PLC

The Company's Registrar is Computershare Investor Services PLC PO Box 82 The Pavilions Bridgwater Road Bristol BS99 7NH Telephone 0870 7020010 Their website for shareholder enquiries is [www.computershare.co.uk](http://www.computershare.co.uk)

### Shareholders' enquiries

If you have any enquiry about the Company's business or about something affecting you as a shareholder (other than questions dealt with by Computershare Investor Services PLC) you are invited to contact the Company Secretary at the address shown below

### Secretary and Registered Office

N P Lingwood FCA 12 Charterhouse Square London EC1M 6AX Telephone 020 7549 5700 Fax 020 7549 5715  
Registered in England and Wales number 3899848

### Web site

Diploma's web site is [www.diplomapl.com](http://www.diplomapl.com)

## Five Year Record

Year ended 30 September	2011	2010	2009	2008	2007
Continuing businesses	£m	£m	£m	£m	£m
<b>Revenue</b>	<b>230 6</b>	<b>183 5</b>	<b>160 0</b>	<b>156 2</b>	<b>124 5</b>
<b>Adjusted operating profit</b>	<b>45 2</b>	<b>32 1</b>	<b>25 6</b>	<b>26 6</b>	<b>20 7</b>
Finance (expense)/income	(0 3)	0 1	(0 1)	0 2	1 2
<b>Adjusted profit before tax</b>	<b>44 9</b>	<b>32 2</b>	<b>25 5</b>	<b>26 8</b>	<b>21 9</b>
Acquisition related charges	(4 8)	(3 5)	(3 1)	(2 7)	(1 0)
Fair value remeasurements	(0 9)	(2 0)	(1 9)	(3 0)	–
<b>Profit before tax</b>	<b>39 2</b>	<b>26 7</b>	<b>20 5</b>	<b>21 1</b>	<b>20 9</b>
Tax expense	(11 6)	(8 8)	(7 1)	(7 2)	(7 1)
Profit for the year from continuing businesses	<b>27 6</b>	<b>17 9</b>	<b>13 4</b>	<b>13 9</b>	<b>13 8</b>
Profit from discontinued businesses	–	5 1	0 9	0 5	1 0
<b>Profit for the year</b>	<b>27 6</b>	<b>23 0</b>	<b>14 3</b>	<b>14 4</b>	<b>14 8</b>
<b>Capital structure</b>					
Equity shareholders funds	<b>164 1</b>	<b>136 1</b>	<b>121 4</b>	<b>108 1</b>	<b>90 7</b>
Minority interest	<b>0 5</b>	<b>3 1</b>	<b>2 7</b>	<b>1 9</b>	<b>1 8</b>
Add/(less) cash and cash equivalents	<b>(17 8)</b>	<b>(30 1)</b>	<b>(21 3)</b>	<b>(15 7)</b>	<b>(12 4)</b>
borrowings	<b>5 6</b>	<b>–</b>	<b>–</b>	<b>–</b>	<b>–</b>
retirement benefit obligations	<b>5 4</b>	<b>5 3</b>	<b>4 7</b>	<b>1 7</b>	<b>1 6</b>
future purchases of minority interests	<b>2 0</b>	<b>13 2</b>	<b>13 1</b>	<b>11 2</b>	<b>11 8</b>
deferred tax net	<b>2 0</b>	<b>1 3</b>	<b>2 0</b>	<b>3 3</b>	<b>3 6</b>
adjustment to goodwill in respect of deferred tax	<b>(8 9)</b>	<b>(6 6)</b>	<b>(6 5)</b>	<b>(6 0)</b>	<b>(5 6)</b>
<b>Trading capital employed</b>	<b>152 9</b>	<b>122 3</b>	<b>116 1</b>	<b>104 5</b>	<b>91 5</b>
Net (decrease)/increase in net funds	<b>(18 0)</b>	<b>8 6</b>	<b>2 2</b>	<b>2 0</b>	<b>(25 3)</b>
Add dividends paid	<b>14 8</b>	<b>10 2</b>	<b>9 1</b>	<b>7 8</b>	<b>5 7</b>
acquisition of businesses	<b>28 2</b>	<b>11 0</b>	<b>12 2</b>	<b>7 9</b>	<b>31 6</b>
<b>Free cash flow</b>	<b>25 0</b>	<b>29 8</b>	<b>23 5</b>	<b>17 7</b>	<b>12 0</b>
<b>Per ordinary share (pence)</b>					
Basic earnings	<b>24 0</b>	<b>14 6</b>	<b>10 8</b>	<b>11 4</b>	<b>11 8</b>
Adjusted earnings	<b>27 9</b>	<b>18 9</b>	<b>14 8</b>	<b>16 0</b>	<b>13 1</b>
Dividends	<b>12 0</b>	<b>9 0</b>	<b>7 8</b>	<b>7 5</b>	<b>5 4</b>
Total shareholders equity	<b>145</b>	<b>120</b>	<b>107</b>	<b>95</b>	<b>80</b>
Dividend cover	<b>2 3</b>	<b>2 1</b>	<b>1 9</b>	<b>2 1</b>	<b>2 4</b>
<b>Ratios</b>	<b>%</b>	<b>%</b>	<b>%</b>	<b>%</b>	<b>%</b>
Return on trading capital employed	<b>25 4</b>	<b>22 1</b>	<b>19 0</b>	<b>22 4</b>	<b>25 5</b>
Working capital revenue	<b>16 1</b>	<b>15 4</b>	<b>17 6</b>	<b>17 2</b>	<b>17 3</b>
Operating margin	<b>19 6</b>	<b>17 5</b>	<b>16 0</b>	<b>17 0</b>	<b>16 6</b>
<b>Continuing and discontinued businesses</b>	<b>£m</b>	<b>£m</b>	<b>£m</b>	<b>£m</b>	<b>£m</b>
Revenue	<b>230 6</b>	<b>188 8</b>	<b>175 7</b>	<b>172 3</b>	<b>140 7</b>
Adjusted profit before tax	<b>44 9</b>	<b>31 6</b>	<b>26 7</b>	<b>27 5</b>	<b>23 3</b>
Adjusted earnings per ordinary share (pence)	<b>27 9</b>	<b>18 5</b>	<b>15 6</b>	<b>16 4</b>	<b>14 0</b>

## Notes

- Return on trading capital employed represents operating profit, before acquisition related charges, as a percentage of trading capital employed (adjusted for the effect of the timing of major acquisitions and disposals). Trading capital employed is calculated as defined in note 2 to the consolidated financial statements.
- Adjusted earnings per share is calculated in accordance with note 9 to the consolidated financial statements.
- Total shareholders' equity per share have been calculated by dividing equity shareholders' funds by the number of ordinary shares in issue at the year end.
- Dividend cover is calculated on adjusted earnings as defined in note 2 to the consolidated financial statements.
- On 21 January 2008 the Company undertook a bonus issue of four new ordinary shares of 5 pence each for each ordinary share held by shareholders of the Company. The comparative amounts have been restated to reflect this bonus issue.
- Acquisition expenses have been charged against profit from 1 October 2009, prior to 1 October 2009 acquisition costs were included as part of the cost of investment.

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