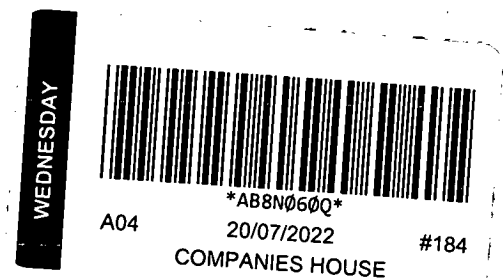


BAE Systems Properties Limited

Annual Report and Financial Statements

31 December 2021

Registered number: 02863702



Contents

	Page
Strategic Report	1 - 4
Directors' Report	5 - 4
Directors' Responsibilities Statement	7
Independent Auditor's Report to the Members of BAE Systems Properties Limited	8 - 11
Income Statement	12
Statement of Comprehensive Income	12
Balance Sheet	13 - 14
Statement of Changes in Equity	15
Notes to the Financial Statements	16 - 46

Strategic Report
for the year ended 31 December 2021

Review of business and principal activities

BAE Systems Properties Limited (the "Company") is a member of the BAE Systems plc Group ("BAE Systems Group or Group") of companies. The Company has made a profit during 2021 of £5,080k (2020: profit £4,538k), which is in line with expectations and has net liabilities of £42,694k (2020: £54,093k). The movement in net liabilities is largely the result of a remeasurement on the retirement benefit schemes.

During 2021 the Company continued to manage its ongoing businesses of Disposals, Programmes, Real Estate Management and Work Place Services. These services enabled the Company to maintain key operational sites on behalf of BAE Systems plc and other BAE Systems Group companies managing surplus property, site remediation, waste, water and power on behalf of the Group. The Company is working with Energy Suppliers to identify opportunities to help reduce energy consumption and carbon footprint.

Key performance indicators (KPIs)

The Company is part of the BAE Systems Group and the key performance indicators used to monitor and review the business are set by the Group and discussed in more detail in the BAE Systems plc annual report 2021 (available at: baesystems.com/investors). The directors do not consider it necessary to provide additional key performance indicators at a company level for an understanding of the development, performance or position of the business.

Principal risks and uncertainties

The key business risks and uncertainties affecting the Company are listed below:

Environmental warranties

The Company maintains insurance to cover any Environmental Warranties issued to support land remediation contracts. Warranted land remediation work is carried out to agreed contractual and regulatory requirements & standards, including conditions imposed by Grants of Planning Permission. The Company ISO9001 certification covers the planning and delivery of land remediation, supported by a programme of 1st, 2nd & 3rd party auditing.

Property Dilapidations

As the Company's properties age, increased maintenance charges are likely. The directors of the Company follow a five year maintenance plan to mitigate this risk.

Health & Safety

Those managing health, safety and the environment ("SHE") risks have the appropriate level of SHE competence, training and experience. A SHE governance structure and SHE resource is in place to support all areas of the business and the Company has a number of formal processes in place to identify and manage our legal and statutory obligations. Effectiveness of control measures are continually assessed through a programme of 1st, 2nd & 3rd party assurance audits and assessments; the Company is covered by the BAE Systems Shared Services ISO45001 certification.

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

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

Many people have contracted the disease across the world and many deaths have occurred as a result of the COVID-19 pandemic. Although there has been an effective roll-out of vaccination programmes in certain countries, it is still not clear how long this pandemic will last or how enduring its long-term impact will be, or the further measures that will be taken by governments and others to seek to control this pandemic and its impact. The uncertainties surrounding the development of this pandemic make it difficult to predict the extent to which the Company may be affected.

Areas of the Company's business that could be impacted include the requirement for the Company to close sites, the inability of the Company to meet its contractual requirements on time, and the inability to adequately staff and manage the business. Any of the above could have a material adverse effect on the Company's business, financial condition and results of operations.

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

Section 172(1) statement

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

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

Decision making

The Operational Framework provides a stable foundation from which to deliver our strategy, improve our Company performance and continue to develop our culture. It is an important part of our governance structure, underpinning the operational excellence that is critical to our ongoing success. The Operational Framework sets out the principles of good governance to which Group subsidiaries are required to adhere, together with Group's values, policies and processes. Decisions affecting a subsidiary are required to be taken in line with the Operational Framework, including in accordance with applicable delegations of authority. Decision making is also informed by requirements of ISO standard certifications held by the Company covering quality, environmental and health and safety management, as well as the regulatory frameworks applicable to the Company's operations.

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

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

Employees

Employee engagement is a primary focus for the directors of the Company – connecting employees to the Company's and the Group's strategy and purpose, empowering them to contribute to improving business performance and creating an environment in which everyone can fulfil their potential.

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

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

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

Through the implementation by the Company of the processes and policies, the directors have regard to the interests of the employees.

Health & Safety

The Company is committed to the management of health, safety and environment risks.

Fostering business relationships with suppliers, customers and others

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

The Company's business is focused on meeting the property needs of the BAE Systems Group companies. Strong and collaborative relationships with Group companies help to identify customer requirements and to help position the Company as a trusted provider. The relevant directors are in regular contact with the customers of the Company and carry out customer surveys to ensure the Company delivers as a trusted partner.

The Company's real estate and work place services teams work with suppliers and their supply chains to provide services that meet customer requirements. The Company's property transactions tend to be long term due to the length of the product life cycles of Group companies' customers and the directors meet with key suppliers to develop deep long-term relationships.

The community and the environment

The directors recognise the importance of leading a company that not only generates value for shareholders but also contributes to wider society. Through the Operational Framework the Company implements the requirements of the BAE Systems Group's Community Investment Policy, which looks to ensure that we build and nurture mutually beneficial relationships between our business, our people and local stakeholders.

The Company is supporting the Group's target of achieving net zero greenhouse emissions across the Group's operations (scope 1 and 2) by 2030 and its target of working towards a net zero value chain by 2050.

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

Our employees regularly support fundraising events organised by BAE Systems businesses in line with the Group's Community Investment Policy. These activities form part of the Company's implementation of the BAE Systems Group-wide community and environment processes and policies and the Group's impacts thereon which are described in the Environment and Social sections (pages 38-47 and pages 58-63 respectively) of BAE Systems plc's Annual Report 2021 (available at www.baesystems.com/investors).

Maintaining a reputation for high standards of business conduct

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

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

Approved by the Board and signed on its behalf by:



D A Green
Director

Date: 20 June 2022

Directors' Report

Company registration

BAE Systems Properties Limited is a private company, limited by shares and registered in England and Wales with the registered number 02863702.

Results and dividends

The Company's profit for the financial year is £5,080k (2020: £4,538k profit). The directors do not propose a dividend for 2021 (2020: £nil).

Looking forward

The Company seeks to develop its Work Place Services offering, to provide operational facilities management to internal Group customers and manage vacant space. It also plans to continue its Programmes business providing remediation and infrastructure services to internal Group customers.

Going concern

The financial statements have been prepared on the going concern basis, notwithstanding net current liabilities of £561,161k, which the directors believe to be appropriate for the following reasons. The Company is dependent for its working capital on funds provided to it by BAE Systems plc, the Company's ultimate parent. BAE Systems plc has indicated in writing that, for at least 12 months from the date of approval of these financial statements, it will continue to make available funds as are needed by the Company to meet its liabilities as they fall due and in particular will not seek repayment of amounts currently made available.

Credit risk and liquidity

The applicable financial risk management policies and exposure to financial risks including price, credit, liquidity and cash flow risks are discussed in detail within the BAE Systems plc Group accounts (available at: www.baesystems.com/investors).

Energy and carbon reporting exemption

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

Directors and their interests

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

D A Green
A-L Holding
D S Parkes
M A Reason

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

Directors' Report (continued)

Disclosure of information to auditor

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

Auditor

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

Approved by the Board and signed on its behalf by:



D A Green
Director

Date: *20 June 2022*

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

Directors' Responsibilities Statement

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

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law), including Financial Reporting Standard 101 ("FRS 101") Reduced Disclosure Framework.

Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period.

In preparing these financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

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

Independent Auditor's Report to the Members of BAE Systems Properties Limited

Report on the audit of the financial statements

Opinion

In our opinion the financial statements of BAE Systems Properties Limited (the "Company"):

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

We have audited the financial statements which comprise:

- the Income Statement;
- the Statement of Comprehensive Income;
- the Balance Sheet;
- the Statement of Changes in Equity;
- the Statement of Accounting Policies; and
- the related notes 1 to 20.

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

Basis for opinion

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

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

Conclusions relating to going concern

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

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

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

Other information

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

Independent Auditor's Report to the Members of BAE Systems Properties Limited (continued)

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

We have nothing to report in this regard.

Responsibilities of directors

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

In preparing the financial statements, the directors are responsible for assessing the company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

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

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

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

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

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

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

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

Independent Auditor's Report to the Members of BAE Systems Properties Limited (continued)

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

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

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

Report on other legal and regulatory requirements

Opinions on other matters prescribed by the Companies Act 2006

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

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

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

Matters on which we are required to report by exception

Under the Companies Act 2006 we are required to report in respect of the following matters if, in our opinion:

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

We have nothing to report in respect of these matters.

Independent Auditor's Report to the Members of BAE Systems Properties Limited (continued)

Use of our report

This report is made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.



Peter McDermott FCA (Senior Statutory Auditor)

for and on behalf of Deloitte LLP
1 New Street Square
London
EC4A 3HQ

Date: 20 June 2022

Income Statement
for the year ended 31 December 2021

	Note	2021 £000	2020 £000
Revenue	3	34,514	22,802
Operating costs	4	(36,531)	(24,168)
Other income	7	7,204	6,011
Operating profit		5,187	4,645
Financial expense	8	(107)	(107)
Profit before tax		5,080	4,538
Tax expense	9	-	-
Profit for the financial year		5,080	4,538

Statement of Comprehensive Income
for the year ended 31 December 2021

		2021 £000	2020 £000
Profit for the financial year		5,080	4,538
Other comprehensive income:			
Items that will not be classified to the Income Statement :			
Remeasurements on retirement benefit schemes	17	6,200	(3,400)
Total comprehensive income for the year		11,280	1,138

The notes on pages 16 to 46 form part of these financial statements.

The results for 2021 and 2020 arise from continuing activities.

BAE Systems Properties Limited
Annual Report and Financial Statements
31 December 2021

Balance Sheet
as at 31 December 2021

	Note	2021 £000	2020 £000
Non-current assets			
Property, plant and equipment	11	202	270
Investment property	10	59	149
Right-of-use assets	16	406	334
Investments	12	-	-
Trade and other receivables	13	518,796	518,796
Retirement benefit surpluses	17	4,600	4,300
		<u>524,063</u>	<u>523,849</u>
Current assets			
Inventories	14	26	114
Trade and other receivables	13	349,484	92,262
		<u>349,510</u>	<u>92,376</u>
Total assets		<u><u>873,573</u></u>	<u><u>616,225</u></u>

BAE Systems Properties Limited
Annual Report and Financial Statements
31 December 2021

Balance Sheet (continued)
as at 31 December 2021

	Note	2021 £000	2020 £000
Non-current liabilities			
Lease liabilities	16	(183)	(165)
Retirement benefit obligations	17	(5,400)	(11,300)
Provisions	18	(13)	(8)
		<u>(5,596)</u>	<u>(11,473)</u>
Current liabilities			
Trade and other payables	15	(910,236)	(658,437)
Lease liabilities	16	(216)	(164)
Provisions	18	(219)	(244)
		<u>(910,671)</u>	<u>(658,845)</u>
Total liabilities		<u>(916,267)</u>	<u>(670,318)</u>
Net liabilities		<u>(42,694)</u>	<u>(54,093)</u>
Capital and reserves			
Issued share capital	19	50,000	50,000
Retained deficit		(92,694)	(104,093)
Total equity		<u>(42,694)</u>	<u>(54,093)</u>

Approved by the Board on 20 June 2022 and signed on its behalf by:



D A Green
Director

Registered number: 02863702

The notes on pages 16 to 46 form part of these financial statements.

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

	Issued share capital	Retained deficit	Total equity
	£000	£000	£000
At 1 January 2020	50,000	(105,357)	(55,357)
Profit for the year	-	4,538	4,538
Other comprehensive income	-	(3,400)	(3,400)
Share-based payments	-	126	126
At 31 December 2020	<u>50,000</u>	<u>(104,093)</u>	<u>(54,093)</u>
Profit for the year	-	5,080	5,080
Other comprehensive income	-	6,200	6,200
Share-based payments	-	119	119
At 31 December 2021	<u><u>50,000</u></u>	<u><u>(92,694)</u></u>	<u><u>(42,694)</u></u>

The notes on pages 16 to 46 form part of these financial statements.

Notes to the Financial Statements

1. General information

BAE Systems Properties Limited is a private company, limited by shares, and registered in England and Wales and incorporated in the United Kingdom. Its ultimate controlling party is disclosed in note 20. The address of the Company's registered office is shown on page 6.

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

2. Accounting policies

2.1 Basis of preparation

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

- the requirements of paragraphs 45(b) and 46 to 52 of IFRS 2 Share-based Payment;
- the requirement in paragraph 38 of IAS 1 Presentation of Financial Statements to present comparative information in respect of:
 - paragraph 79(a)(iv) of IAS 1 Presentation of Financial Statements;
 - paragraph 73(e) of IAS 16 Property, Plant and Equipment;
 - paragraph 118(e) of IAS 38 Intangible Assets; and
 - paragraphs 76 and 79(d) of IAS 40 Investment Property.
- the requirements of paragraphs 10(d), 10(f), 16, 38A, 38B, 38C, 38D, 40A, 40B, 40C, 40D, 111 and 134 to 136 of IAS 1 Presentation of Financial Statements;
- the requirements of IAS 7 Statement of Cash Flows;
- the requirements of paragraphs 30 and 31 of IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors;
- the requirements of paragraph 17 and 18A of IAS 24 Related Party Disclosures; and
- the requirements of paragraphs 130(f)(ii), 130(f)(iii), 134(d)-134(f) and 135(c)-135(e) of IAS 36 Impairment of Assets.

The Company intends to continue to prepare its financial statements in accordance with FRS 101 and on a going concern basis.

The Company is exempt under Section 400 of the Companies Act 2006 from the requirement to prepare consolidated financial statements as it and its subsidiary undertakings are included by full consolidation in the consolidated financial statements of its ultimate parent, BAE Systems plc, a Company registered in England and Wales. Accordingly, these financial statements present information about the Company as an individual undertaking and not as a group.

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

Notes to the Financial Statements

2. Accounting policies (continued)

2.1 Basis of preparation (continued)

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

Critical accounting policies

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

Critical accounting policy	Description
Valuation of retirement benefit obligations	Defined benefit pension scheme accounting valuations are prepared by independent actuaries. The liabilities of the pension schemes are valued based on a number of actuarial assumptions. For each of the actuarial assumptions used there is a range of possible values and management estimates the point within that range that most appropriately reflect the Company's circumstances. Small changes in these assumptions can have a significant impact on the size of the deficit. See note 17.

Judgements made in applying accounting policies

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

Key sources of estimation uncertainty

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

Post-employment benefit obligations - the Company's share of the net IAS 19 post-employment scheme deficit £800k (at 31 December 2021). See note 17 and critical accounting policies above.

Changes in accounting policies

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

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

The following amendments to existing standards have been issued and became effective in the year as a response to the COVID-19 pandemic, but did not have a material impact on the Company:

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

Notes to the Financial Statements

2. Accounting policies (continued)

2.1 Basis of preparation (continued)

Significant accounting policies

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

2.2 Leases

The Company as lessee

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

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

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

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

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

The Company as lessor

Leases in which the Company is lessor are classified as finance leases or operating leases. If the lease transfers substantially all of the risks and rewards of ownership to the lessee, the lease is classified as a finance lease. All other leases are classified as operating leases.

Lease income under operating leases is recognised in the Income Statement on a straight-line basis over the lease term.

Amounts due from lessees under finance leases are recognised as a receivable discounted at the interest rate implicit in the lease. Finance lease income is recognised in the Income Statement over the lease term to produce a constant periodic rate of interest on the receivable.

Notes to the Financial Statements

2. Accounting policies (continued)

2.3 Revenue and profit recognition

Revenue represents income derived from the provision of property leasing and management services by the Company.

Revenue is measured at the fair value of the consideration received or receivable, net of returns, rebates and other similar allowances.

Revenue and profits on intercompany trading are determined on an arm's length basis.

2.4 Interest income and borrowing costs

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

2.5 Property, plant and equipment

Cost

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

Depreciation

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

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

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

Impairment

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

Notes to the Financial Statements

2. Accounting policies (continued)

2.6 Investment property

Cost

Land and buildings that are leased to BAE Systems plc Group or non-BAE Systems plc Group entities are classified as investment property. The Company measures investment property at its cost less accumulated depreciation and impairment losses.

Depreciation

Depreciation is provided, on a straight-line basis, to write off the cost of investment property over its estimated useful life of up to 50 years.

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

Impairment

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

2.7 Investments

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

The carrying amounts of the Company's investments are reviewed at each Balance Sheet date to determine whether there is any indication of impairment as required by IAS 36 Impairment of Assets. If any such indication exists, the asset's recoverable amount is estimated.

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

The recoverable amount is the greater of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using an appropriate pre-tax discount rate. For an asset that does not generate largely independent cash flows, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

Impairment losses are recognised in the Income Statement.

An impairment loss in respect of property, plant and equipment, investment property, investments and right-of-use assets is reversed if the subsequent increase in recoverable amount can be related objectively to an event occurring after the impairment loss was recognised or if there has been a change in the estimate used to determine the recoverable amount.

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

2.8 Inventories

Inventories are stated at the lower of cost, including all relevant overhead expenditure, and net realisable value.

Notes to the Financial Statements

2. Accounting policies (continued)

2.9 Trade and other receivables

Trade and other receivables are stated at amortised cost.

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

2.10 Trade and other payables

Trade and other payables are stated at amortised cost.

2.11 Provisions

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

Legal, contractual and environmental

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

2.12 Tax

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

Current tax

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

Deferred tax

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

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

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

Notes to the Financial Statements

2. Accounting policies (continued)

2.12 Tax (continued)

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

The most significant recognised deferred tax assets relate to the deficits on the Company's pension/retirement benefit schemes. This is because retirement benefit costs are deducted in determining accounting profit as service is provided by employees, but deducted in determining taxable profit either when the contributions are paid to the pension/retirement benefit schemes or when retirement benefits are paid. In reviewing the probability that taxable profits will be available in the future against which such contributions/payments can be deducted, account has been taken of the deficit recovery plans agreed with the trustees of the relevant schemes under which the deficits are expected to be cleared between 2021 and 2026.

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

2.13 Share-based payments

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

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

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

2.14 Retirement benefit obligations

Defined contribution pension schemes

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

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

Defined benefit pension schemes

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

Notes to the Financial Statements

2. Accounting policies (continued)

2.14 Retirement benefit obligations (continued)

The retirement benefit surpluses and obligations recognised in the Company's Balance Sheet represents the fair value of scheme assets, less the present value of the defined benefit obligations calculated using a number of actuarial assumptions as set out on page 39. The bid values of scheme assets are not intended to be realised in the short term and may be subject to significant change before they are realised. The present values of scheme liabilities are derived from cash flow projections over long periods and are, therefore, inherently uncertain.

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

The Company participates in a number of group and multi-employer schemes administered by its ultimate parent company, BAE Systems plc. A share of the IAS 19 Employee Benefits pension deficit has been allocated to all participating employers. This allocation is based on the relative payroll contributions of active members, which is consistent with prior years. Whilst this methodology is intended to reflect a reasonable estimate of the share of the deficit, it may not accurately reflect the obligations of the participating employers. Gains and losses resulting from changes to the relative payroll contributions of active members year on year are included within actual return on assets and actuarial gains and losses for the disclosures in respect of changes in the fair value of scheme assets and changes in the present value of defined benefit obligations, respectively.

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

Notes to the Financial Statements

3. Revenue

Revenue by reporting segment

	2021 £000	2020 £000
Programmes	34,514	22,802

Revenue by customer location

	2021 £000	2020 £000
United Kingdom	34,514	22,802

Revenue by category

	2021 £000	2020 £000
Provision of services	34,514	22,802

4. Operating costs

	2021 £000	2020 £000
Raw materials, subcontracts and other bought-in items used	26,465	14,224
Staff costs (note 5)	8,086	7,710
Depreciation, amortisation and impairment	355	356
Other operating charges	1,625	1,878
	36,531	24,168

The remuneration of the auditor for the year ended 31 December 2021 for auditing of the financial statements was £70k (2020: £53k) and £nil (2020: £nil) in respect of non-audit work.

Notes to the Financial Statements

5. Employees

The monthly average number of Company employees was 101 (2020: 110). The aggregate staff costs of Company employees were as follows:

	2021 £000	2020 £000
Wages and salaries	6,356	5,942
Social security costs	697	744
Cost of defined benefit pension scheme (note 17)	700	682
Cost of defined contribution pension scheme (note 17)	214	216
Share-based payments	119	126
	<u>8,086</u>	<u>7,710</u>

One of the directors received emoluments from the Company during the year. All other directors who served during the year were employed by BAE Systems plc, and were remunerated through that company.

6. Directors' remuneration

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

	2021 £000	2020 £000
Directors' remuneration	203	191
Company contributions to defined benefit pension schemes	31	43
	<u>234</u>	<u>234</u>

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

	2021 Number of directors	2020 Number of directors
Defined benefit schemes	<u>2</u>	<u>2</u>
	2	2
Number of directors who exercised share options	2	2
Number of directors in respect of whose qualifying services shares were received or receivable under long-term incentive schemes	<u>2</u>	<u>2</u>

Notes to the Financial Statements

6. Directors' remuneration (continued)

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

	2021 £000	2020 £000
Remuneration and amounts receivable under long-term incentive schemes	179	168
Company contributions to defined benefit pension schemes	26	38
	205	206
	205	206

The highest paid director's defined benefit accrued pension and accrued lump sum at 31 December 2021 were £113,733 (2020: £107,828) and £nil (2020: £nil), respectively.

During the year, the highest paid director received shares under a long-term incentive scheme.

7. Other income

	2021 £000	2020 £000
Operating lease income (note 16)	5	11
Profit on disposal of investment property	115	205
Management recharges	7,030	4,364
Intercompany provision release	54	1,431
	7,204	6,011
	7,204	6,011

8. Financial expense

	2021 £000	2020 £000
Net interest expense on retirement benefit obligations (note 17)	100	100
Interest expense on lease liabilities (note 16)	7	7
	107	107
	107	107

9. Tax

The Company has not provided for current tax for the year as any taxable profits will be covered by the surrender of losses from fellow group companies, in respect of which no payment will be made.

Notes to the Financial Statements

9. Tax (continued)

Reconciliation of tax expense

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

	2021	2020
	£000	£000
Profit before tax	5,080	4,538
UK corporation tax rate	19.00%	19.00%
Expected tax (expense) on profit	(965)	(862)
Expenses not tax effected	(50)	101
Income not subject to tax	22	38
Property, plant and equipment	(4)	(3)
Provisions and accruals	(12)	10
Imputed interest expense	164	117
Losses received from fellow group companies	845	599
Tax result	-	-

The deferred tax asset which has not been recognised in the accounts is made up as follows:

	2021	2020
	£000	£000
Property, plant and equipment	79	75
Provisions and accruals	28	15
Retirement benefit schemes: deficits	200	1,330
Retirement benefit schemes: additional contributions	332	445
Deferred tax asset	639	1,865

The deferred tax asset has not been recognised because there is insufficient evidence of future taxable profits to support its recoverability.

In 2021, the Government announced that with effect from 1 April 2021, the UK corporation tax rate would remain at 19% rather than reducing to the previously enacted rate of 17%.

On 3 March 2021, the Government announced that the UK corporation tax rate would be increased from 19% to 25% with effect from 1 April 2023. The unprovided deferred tax asset has therefore been calculated at the tax rates, enacted at each Balance Sheet date, expected to apply to the temporary differences when they reverse.

Notes to the Financial Statements

10. Investment property

	£000
Cost	
At 1 January 2021	273
Transfers intra group	120
Disposals	(274)
At 31 December 2021	119
Depreciation and impairment	
At 1 January 2021	124
Transfers intra group	56
Disposals	(120)
At 31 December 2021	60
Net book value	
At 31 December 2021	59
At 31 December 2020	149
Fair Value	
At 31 December 2021	125
At 31 December 2020	270

The fair values above are based on and reflect current market values as prepared by in-house professionals who have the appropriate professional qualifications and recent experience of valuing properties in the location and of the type being valued.

Notes to the Financial Statements

11. Property, plant and equipment

	Plant and machinery £000
Cost or valuation	
At 1 January 2021	1,087
Additions	55
At 31 December 2021	1,142
Depreciation	
At 1 January 2021	817
Depreciation charge for the year	123
At 31 December 2021	940
Net book value	
At 31 December 2021	202
At 31 December 2020	270

Capital commitments

Capital expenditure contracted for but not provided for in full in the financial statements is £nil (2020: £nil).

Notes to the Financial Statements

12. Investments

	£000
Cost	
At 1 January 2021	59,560
Dissolved subsidiaries	(15,219)
At 31 December 2021	44,341
Impairment	
At 1 January 2021	59,560
Dissolved subsidiaries	(15,219)
At 31 December 2021	44,341
Net book value	
At 31 December 2021	-
At 31 December 2020	-

Impairment testing

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

Subsidiary undertakings and participating interests at 31 December 2021

In accordance with Section 409 of the Companies Act 2006, a full list of subsidiary undertakings and significant holdings as at 31 December 2021 is disclosed below. Unless otherwise stated, all subsidiary undertakings and significant holdings are owned directly by the Company and have a financial year end of 31 December. The registered office address is Warwick House, PO Box 87, Farnborough Aerospace Centre, Farnborough, Hampshire, GU14 6YU.

Company name	Class of shares held	Proportion of class (%)
Lemacrown Limited	Ordinary shares	100
Lemacrown Limited	Ordinary A shares	100
Newcombe Properties Limited	Ordinary shares	100
Winner Developments Limited	Ordinary shares	33.33

During the year under review the following subsidiary undertakings were dissolved: Buckfield Properties Limited, Hertfordshire Estates Limited and The Leeds Partnership Limited.

Notes to the Financial Statements

13. Trade and other receivables

	2021 £000	2020 £000
Due after more than one year		
Amounts owed by BAE Systems plc	518,796	518,796
	<u>518,796</u>	<u>518,796</u>
Due within one year		
Trade receivables	456	1,738
Amounts owed by BAE Systems plc and its subsidiaries	335,802	76,796
Other receivables	7,274	9,072
Prepayments	2,150	1,865
Accrued income	3,802	2,791
	<u>349,484</u>	<u>92,262</u>

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

14. Inventories

	2021 £000	2020 £000
Work in progress	26	114
	<u>26</u>	<u>114</u>

Notes to the Financial Statements

15. Trade and other payables

	2021 £000	2020 £000
Current		
Trade payables	2,588	2,792
Amounts owed to BAE Systems plc and its subsidiaries	902,244	649,020
Other payables	129	1,773
Deferred income	2,595	2,706
Accruals	2,680	2,146
	<u>910,236</u>	<u>658,437</u>

Amounts owed to BAE Systems plc and its subsidiaries are payable on demand. No interest is applied to amounts owed.

Notes to the Financial Statements

16. Leases

The Company leases land, buildings, vehicles and equipment under non-cancellable lease arrangements. The leases have varying terms, including escalation clauses, renewal rights and purchase options. None of these terms represent unusual arrangements or create material onerous or beneficial rights or obligations.

Right-of-use assets

	<u>31 December 2021</u>			<u>31 December 2020</u>		
	Land and buildings £000	Plant and machinery £000	Total £000	Land and buildings £000	Plant and machinery £000	Total £000
Additions during the year	5	299	304	-	102	102
Depreciation expense for the year	82	150	232	71	158	229
Lease modifications	-	-	-	4	-	4
Net book value	<u>94</u>	<u>312</u>	<u>406</u>	<u>171</u>	<u>163</u>	<u>334</u>

Lease liabilities

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

	2021	2020
	£000	£000
Payments due:		
Within one year	221	169
Between one and five years	185	168
	<u>406</u>	<u>337</u>
Reconciliation to Balance Sheet:		
Undiscounted lease liability	406	337
Impact of discounting	(7)	(8)
Total discounted lease liability	<u>399</u>	<u>329</u>

The total cash outflow for leases recognised on the Balance Sheet in the year ended 31 December 2021, amounted to £222k (2020: £232k).

Notes to the Financial Statements

16. Leases (continued)

Amounts recognised in the Income Statement

	2021	2020
	£000	£000
Included in operating costs:		
Depreciation on right-of-use assets	232	229
Short-term lease expense	122	160
	<u>354</u>	<u>389</u>
Included in other income:		
Operating lease income from subleasing right-of-use assets	5	11
	<u>5</u>	<u>11</u>
Included in net finance costs:		
Interest expense on lease liabilities	7	7
	<u>7</u>	<u>7</u>

Notes to the Financial Statements

17. Retirement benefit obligations

Background

BAE Systems plc operates pension schemes for qualifying employees in the UK, US and other countries. The principal schemes in the UK are funded defined benefit schemes and the assets are held in separate trustee-administered funds. The allocation of each Company's share of the pension deficit is based on the relative payroll contributions of active members, as outlined on page 22.

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

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

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

	Active %	Deferred %	Pensioner %
Main Scheme (merged) ¹	31	21	48

¹Source: 31 October 2019 actuarial valuation reports.

Regulatory framework

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

Benefits

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

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

Funding

Introduction

Disclosures in respect of pension funding provided below reflect the pension schemes as a whole. Disclosures in respect of pension accounting under IAS 19 are provided on pages 39 - 44.

Notes to the Financial Statements

17. Retirement benefit obligations (continued)

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

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

The funding valuations are performed by professional qualified independent actuaries and include assumptions which differ from the actuarial assumptions used for IAS 19 accounting purposes shown on page 39. The purpose of the funding valuations is to design funding plans which ensure that the schemes have sufficient funds available to meet future benefit payments.

Valuations

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

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

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

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

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

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

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

Notes to the Financial Statements

17. Retirement benefit obligations (continued)

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

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

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

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

Contributions

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

The total Company contributions made to the defined benefit schemes in the year ended 31 December 2021 were £1.0m (2020 £4.9m).

Notes to the Financial Statements

17. Retirement benefit obligations (continued)

Risk management

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

Risk	Mitigation
<p>Market (investment) risk Asset returns may not move in line with the liabilities and may be subject to volatility.</p>	<p>The investment portfolios are highly diversified, investing in a wide range of assets, in order to reduce the exposure of the total portfolio to a materially adverse impact from a single security or type of security. To reduce volatility, certain assets are held in a matching portfolio, which largely consists of index-linked bonds, gilts and swaps, designed to mirror movements in corresponding liabilities.</p> <p>Some 43% (2020 37%) of the UK pension scheme assets are held in equities and pooled investment vehicles due to the higher expected level of return over the long term.</p> <p>Some of the pension schemes use derivative financial instruments as part of their investment strategy to manage the level of market risk. The Main Scheme has an equity option strategy protecting £2.9bn of assets against a significant fall in equity markets, in line with the prior year. The strategy also caps the upside if equity markets increase more than an agreed percentage.</p>
<p>Interest rate risk Liabilities are sensitive to movements in interest rates, with lower interest rates leading to an increase in the valuation of liabilities.</p>	<p>In addition to investing in bonds as part of the matching portfolio, the UK schemes invest in interest rate swaps to reduce the exposure to movements in interest rates. The swaps are held with several banks to reduce counterparty risk. The current level of interest rate protection is expressed as a hedge ratio of 79.0% (2020 72.4%).</p> <p>The discount rate assumptions set as part of the UK funding valuations directly reflect the expected returns on assets held by the schemes and provide a natural hedge against interest rate risk. The planned investment strategy, which is reflected in the discount rate and liability calculation, is for the schemes to increase their investments in bonds or other assets which match the liabilities as the schemes mature. Under the UK funding valuations, the Company expects the schemes to be fully hedged against interest rate movements following a five-year transition period to the planned investment strategy.</p>
<p>Inflation risk Liabilities are sensitive to movements in inflation, with higher inflation leading to an increase in the valuation of liabilities.</p>	<p>In addition to investing in index-linked bonds as part of the matching portfolio, the principal UK schemes invest in long-term inflation swaps to reduce the exposure to movements in inflation. The swaps are held with several banks to reduce counterparty risk. The current level of inflation protection is expressed as a hedge ratio of 107.8% (2020 100.2%).</p> <p>The UK funding valuations provide a natural hedge against inflation movements within the discount rate. The Company is already fully hedged against inflation movements and, under the planned investment strategy, aims to maintain a fully hedged position.</p> <p>In 2014, the Main Scheme implemented a pension increase exchange to allow retired members to elect for a higher current pension in exchange for foregoing certain rights to future pension increases.</p>
<p>Longevity risk Liabilities are sensitive to life expectancy, with increases in life expectancies leading to an increase in the valuation of liabilities.</p>	<p>Longevity adjustment factors are used in the majority of the UK pension schemes in order to adjust the pension benefits payable so as to share the cost of people living longer with employees.</p> <p>In 2013, with the agreement of BAE Systems plc, the trustees of the 2000 Plan, Royal Ordnance Pension Scheme and Shipbuilding Industries Pension Scheme (SIPS) entered into arrangements with Legal & General to insure against longevity risk for the current pensioner population, covering a total of £4.4bn of pension scheme liabilities. These arrangements reduce the funding volatility relating to increasing life expectancy. This longevity risk cover with Legal & General remains in place following the merger of the 2000 Plan and SIPS into the Main Scheme.</p>

Notes to the Financial Statements

17. Retirement benefit obligations (continued)

IAS 19 Accounting

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

Principal actuarial assumptions

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

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

Discount rate

The discount rate assumptions are derived through discounting the projected benefit payments of the principal schemes using a third-party AA corporate bond yield curve to produce a single equivalent discount rate. This inherently captures the maturity profile of the expected benefit payments. The discount rate used for future service differs from that used for past service as it only uses the cash flows relating to active members, which have a different duration. Further information on the duration of the schemes is detailed on page 35.

Retail Prices Index (RPI) inflation

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

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

Rate of increase in salaries

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

Notes to the Financial Statements

17. Retirement benefit obligations (continued)

Rate of increase in deferred pensions

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

Rate of increase in pensions in payment

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

Life expectancy

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

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

The disclosures below are in respect of the Company's share of the IAS 19 deficit using the allocation methodology outlined on page 22.

Summary of movements in retirement benefit obligations

	£m
Company's share of IAS 19 deficit at 1 January 2021	(7.0)
Actual return on assets excluding amounts included in interest expense	2.1
Decrease in liabilities due to changes in assumptions and experience	4.1
Contributions in excess of service cost	0.1
Net interest expense	(0.1)
Company's share of IAS 19 deficit at 31 December 2021	(0.8)

Notes to the Financial Statements

17. Retirement benefit obligations (continued)

Amounts recognised in the Balance Sheet

	2021 £m	2020 £m
Present value of funded obligations	(94.3)	(100.0)
Fair value of scheme assets	93.5	93.0
Company's share of IAS 19 deficit, net	(0.8)	(7.0)
Represented by:		
Retirement benefit surpluses	4.6	4.3
Retirement benefit obligations	(5.4)	(11.3)
	(0.8)	(7.0)

Changes in the fair value of scheme assets

	£m
Company's share of the value of scheme assets at 1 January 2020	84.2
Interest income	1.8
Actual return on assets excluding amounts included in interest income	6.0
Actual return on assets	7.8
Contributions by employer	4.7
Contributions by employer in respect of employee salary sacrifice arrangements	0.2
Total contributions by employer	4.9
Members' contributions	-
Administrative expenses	(0.1)
Benefits paid	(3.8)
Company's share of the value of scheme assets at 31 December 2020	93.0
Interest income	1.2
Actual return on assets excluding amounts included in interest income	2.1
Actual return on assets	3.3
Contributions by employer	0.8
Contributions by employer in respect of employee salary sacrifice arrangements	0.2
Total contributions by employer	1.0
Members' contributions	-
Administrative expenses	-
Benefits paid	(3.8)
Company's share of the value of scheme assets at 31 December 2021	93.5

Notes to the Financial Statements

17. Retirement benefit obligations (continued)

Assets of defined benefit pension schemes

	2021			2020		
	Quoted £m	Unquoted £m	Total £m	Quoted £m	Unquoted £m	Total £m
Equities:						
UK	3.2	-	3.2	2.8	-	2.8
Overseas	10.7	-	10.7	7.5	-	7.5
Pooled investment vehicles ¹	0.7	25.4	26.1	2.2	21.7	23.9
Fixed interest securities:						
UK gilts	10.5	-	10.5	14.1	-	14.1
UK corporates	10.0	8.4	18.4	12.7	8.4	21.1
Overseas government	0.2	-	0.2	0.1	-	0.1
Overseas corporates	5.1	0.1	5.2	7.3	-	7.3
Index-linked securities:						
UK gilts	18.2	-	18.2	17.4	1.2	18.6
UK corporates	-	3.2	3.2	-	2.7	2.7
Property ²	-	5.2	5.2	-	5.0	5.0
Derivatives ³	-	(11.7)	(11.7)	-	(13.5)	(13.5)
Cash:						
Sterling	2.5	1.4	3.9	2.1	0.6	2.7
Foreign currency	-	0.1	0.1	0.1	0.1	0.2
Other	0.1	0.2	0.3	-	0.5	0.5
Company total	61.2	32.3	93.5	66.3	26.7	93.0

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

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

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

Longevity swap

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

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

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

Notes to the Financial Statements

17. Retirement benefit obligations (continued)

Changes in the present value of the defined benefit obligations

	£m
Company's share of the defined benefit obligations at 1 January 2020	(91.7)
Current service cost	(0.6)
Contributions by employer in respect of employee salary sacrifice arrangements	(0.2)
Total current service cost	(0.8)
Members' contributions	-
Past service cost – plan amendments	-
Actuarial loss due to changes in assumptions and experience	(9.4)
Interest expense	(1.9)
Benefits paid	3.8
Company's share of the defined benefit obligations at 31 December 2020	(100.0)
Current service cost	(0.7)
Contributions by employer in respect of employee salary sacrifice arrangements	(0.2)
Total current service cost	(0.9)
Members' contributions	-
Past service cost – plan amendments	-
Actuarial gain due to changes in assumptions and experience	4.1
Interest expense	(1.3)
Benefits paid	3.8
Company's share of the defined benefit obligations at 31 December 2021	(94.3)

Amounts recognised in the Income Statement

	2021 £m	2020 £m
Included in operating costs:		
Current service cost	(0.7)	(0.6)
Administrative expenses	-	(0.1)
	(0.7)	(0.7)
Included in finance costs:		
Net interest expense on retirement benefit obligations	(0.1)	(0.1)

The Company incurred a charge of £0.2m (2020 £0.2m) in relation to defined contribution schemes for employees.

Sensitivity analysis

The sensitivity information has been derived using scenario analysis from the actuarial assumptions as at 31 December 2021 and keeping all other assumptions as set out on page 39.

The pension schemes hold a number of unquoted pooled investment vehicles, which are investments in private markets. These are valued based on latest available valuation reports, and as noted on page 38, these valuations are subject to estimation uncertainty as their valuation techniques incorporate a number of assumptions, including those associated with the COVID-19 pandemic and the impact of climate change.

Notes to the Financial Statements

17. Retirement benefit obligations (continued)

Financial assumptions

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

	(Increase)/ decrease in pension obligation £m	Increase/ (decrease) in scheme assets £m
Discount rate:		
0.1 percentage point increase	2	(1)
0.1 percentage point decrease	(2)	1
0.5 percentage point increase	7	(5)
0.5 percentage point decrease	(8)	5
Inflation:		
0.1 percentage point increase	(2)	1
0.1 percentage point decrease	2	(1)
0.5 percentage point increase	(5)	4
0.5 percentage point decrease	5	(4)
1.0 percentage point increase	(10)	9
1.0 percentage point decrease	9	(7)

Demographic assumptions

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

	(Increase)/ decrease in net deficit £m
Life expectancy:	
One-year increase	(4)
One-year decrease	4

Notes to the Financial Statements

18. Provisions

	Legal, contractual and environmental £000
Non-current	8
Current	244
	252
At 1 January 2021	252
Created	17
Utilised in year	(37)
	232
At 31 December 2021	232
Represented by:	
Non-current	13
Current	219
	232
	232

Legal, contractual and environmental

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

19. Share capital

	£1 Ordinary shares	Nominal value £000
Issued and fully paid		
At 1 January 2020, 31 December 2020 and 31 December 2021	50,000,000	50,000

Notes to the Financial Statements

20. Controlling parties

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

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

6 Carlton Gardens
London
SW1Y 5AD

Website: www.baesystems.com