

Notes to the Accounts

For the year ended 31 December 2002

1 Accounting policies

These Accounts have been prepared in accordance with applicable UK accounting standards, and the particular accounting policies adopted are detailed below. These have all been applied consistently with the exception of bid costs which is explained in the restatement below.

Accounting convention

These Accounts have been prepared under the historical cost convention.

Basis of consolidation

The Group Accounts consolidate the Accounts of the Company and its subsidiaries, and equity accounts for its share of joint ventures made up to 31 December of each year, for the periods they are owned by Serco Group plc.

Restatement

The 2001 Accounts have been restated to reflect the impact of the Urgent Issues Task Force Abstract 34 ("UITF 34") – Pre-Contract Costs; eliminating £1,193,000 of bid costs, previously disclosed within debtors, and the associated tax effect of £387,000. The impact of this adjustment in the 2002 Accounts is a reduction in amortisation of bid costs of £400,000.

The Profit and Loss Account has been restated to reclassify 'Other operating costs relating to joint ventures' within 'Other administrative expenses'.

Accounting for PFI Contracts

Within Public Private Partnership ("PPP") projects (including Private Finance Initiative ("PFI") projects), where the concession agreement transfers limited risks and rewards associated with ownership to the contractor, the costs incurred during the period of initial asset construction, as a direct consequence of financing, designing and constructing the asset, are shown as 'assets in the course of construction' within current assets. On completion of the asset construction phase the asset is transferred to debtors as 'amounts receivable under PPP contracts'.

Revenues received from the customer are apportioned between capital repayments and operating revenue. The 'finance income' element of the capital repayment is shown within interest receivable.

Serco has one Special Purpose Company – Traffic Information Services (TIS) Limited, where the results are fully consolidated. All other SPCs are classified as joint ventures and accounted for using the gross equity method.

Pension costs: Defined benefit schemes

Retirement benefits to employees of Group companies, except in Germany, are funded by contributions from Group companies and employees. Payments are made to trust funds which are financially separate from the Group in accordance with periodic calculations by consulting actuaries. The expected cost to the Group of providing defined benefit pensions is charged to the Profit and Loss Account so as to spread the cost of pensions over the average service lives of employees in the schemes, in such a way that the cost is a substantially level percentage of payroll cost, with experience surpluses and deficits being amortised on a straight-line basis.

In Germany retirement benefits to employees are accrued for by Serco GmbH & Co.KG. The expected cost to the Company for providing defined benefit pensions is calculated in accordance with periodic valuations by consulting actuaries.

1 Accounting policies (continued)**Pension costs: Defined contribution schemes**

Contributions for the year in respect of defined contribution schemes are charged to the Profit and Loss Account. Differences between charges accruing during the year and cash payments are included as either accruals or prepayments in the Balance Sheet.

The Group has adopted the transitional disclosure requirements of Financial Reporting Standard 17 ("FRS 17") – Retirement Benefits. For further information see Note 31.

Turnover

Turnover represents net sales of goods and services to third parties together with investment related income.

Goodwill

Goodwill arising on acquisitions is capitalised in the Consolidated Balance Sheet in accordance with Financial Reporting Standard 10 ("FRS 10") – Goodwill and Intangible Assets. Amortisation of goodwill is provided on a straight-line basis over a period of 20 years, which, in the opinion of the Directors is a period not exceeding the economic useful life of the asset.

Current Tax

Current tax, including UK Corporation Tax and foreign tax, is provided at amounts expected to be paid (or recovered) using the tax rates and laws that have been enacted or substantially enacted at the Balance Sheet date.

Fixed asset investments: Subsidiaries

Investments held as fixed assets are stated at cost less provision for any impairment in value.

Fixed asset investments: Joint ventures

In the consolidated Accounts, investments in joint ventures are accounted for using the gross equity method of accounting in accordance with Financial Reporting Standard 9 ("FRS 9") – Associates and Joint Ventures.

The Group Consolidated Profit and Loss Account includes the Group's share of joint ventures' operating profits and interest, and the attributable taxation. In the Consolidated Balance Sheet, the Group's share of the net assets of its joint ventures, which includes several PFIs, is included under the heading 'investments in joint ventures'. The share of net assets is split between gross assets and gross liabilities.

Fixed asset investment: Own shares

Investment in own shares represents shares in Serco Group plc held by the Serco Group plc 1998 Employee Share Ownership Trust (the "Trust"). The dividends on these shares have been waived. Investment in own shares is stated at cost less provision for impairment.

The Trust is a discretionary trust for the benefit of the employees, and shares are held to satisfy the Group's liabilities to employees for share options and long term incentive plans. The net cost to the Group of these schemes is charged to the Profit and Loss Account over the performance period during which the benefits are earned by employees.

Leases

Assets obtained under finance leases are capitalised at their fair value on acquisition and depreciated over the shorter of their estimated useful lives or lease term. The finance charges are allocated over the period of the lease in proportion to the capital element outstanding. Rentals on assets under operating leases are charged to the Profit and Loss Account in equal annual amounts.

1 Accounting policies (continued)

Depreciation

Depreciation is provided on a straight-line basis at rates which, in the opinion of the Directors, reduce the assets to their residual value over their estimated useful lives.

The principal annual rates used are:

Freehold buildings	2.5%
Short leasehold building improvements	The higher of 10% or rate produced by lease term
Machinery	15% – 20%
Motor vehicles	18% – 50%
Furniture	10%
Office equipment	20% – 33%
Leased equipment	The higher of the rate produced by either lease term or useful life

Stocks

Stocks are stated at the lower of cost and net realisable value. Cost includes an appropriate proportion of direct material and labour.

Long term contracts

Long term contract balances represent costs incurred on specific contracts, net of amounts transferred to cost of sales in respect of work recorded as turnover by reference to the value of the work carried out to date. No profit is recognised until the contract has advanced to a stage where the total profit can be assessed with reasonable certainty. Advance payments are included in creditors to the extent that they exceed the related work in progress.

Pre-contract costs

All bid costs are expensed through the Profit and Loss Account up to the point where contract award is virtually certain in accordance with UITF 34. Bid costs incurred after this point are then capitalised within debtors. On contract award these bid costs are amortised through the Profit and Loss Account on a straight-line basis over the contract period.

Deferred taxation

The charge for taxation takes account of taxation deferred because of differences between the timing of recognition of certain items for taxation purposes and for accounting purposes. Deferred tax is recognised in respect of all timing differences that have originated but not reversed at the Balance Sheet date where the transactions or events that give rise to an obligation to pay more or less tax in the future have occurred by the Balance Sheet date. A deferred tax asset is recognised only when it is considered more likely than not that it will be recovered.

Deferred tax is recognised on a non-discounted basis using tax rates in force at the Balance Sheet date. Financial Reporting Standard 19 ("FRS 19") – Deferred Tax has been adopted for the first time in these financial statements and there is no material effect on the comparative figures.

Basis of translation of foreign currencies

Transactions of UK companies denominated in foreign currencies are translated into Sterling at the rate ruling at the date of the transaction. Amounts receivable and payable in foreign currencies at the Balance Sheet date are translated at the rates ruling at that date and any differences arising are taken to the Profit and Loss Account.

The Accounts of overseas subsidiary companies and associated undertakings are translated into Sterling at the closing rates of exchange at the Balance Sheet date and any difference arising from the translation of the opening net investment and matched long term foreign currency borrowings is taken directly to reserves. The Profit and Loss Account is translated using average exchange rates.

2 Segmental Report

Classes of Business 2002	Group £'000	Joint Ventures £'000	Total £'000
TURNOVER			
Civil Government	267,127	89,220	356,347
Defence	228,579	134,654	363,233
Transport	347,815	4,796	352,611
Science	115,603	–	115,603
Private sector	138,154	–	138,154
TOTAL	1,097,278	228,670	1,325,948
PROFIT BEFORE TAXATION AND OTHER COSTS			
Civil Government	17,796	5,287	23,083
Defence	13,259	15,956	29,215
Transport	15,126	640	15,766
Science	9,845	–	9,845
Private sector	6,909	–	6,909
TOTAL	62,935	21,883	84,818
OTHER COSTS			
Common costs			(25,734)
Amortisation of intangible assets			(8,098)
Net interest – Group			(4,064)
Net interest – Joint ventures			2,019
PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION			48,941
NET ASSETS			
Civil Government			43,269
Defence			53,400
Transport			45,716
Science			69,771
Private sector			31,679
TOTAL			243,835
Unallocated assets			24,022
TOTAL			267,857

2 Segmental Report (continued)

Classes of Business 2001	Group £'000	Joint Ventures £'000	Restated Total £'000
TURNOVER			
Civil Government	202,605	107,917	310,522
Defence	218,001	115,349	333,350
Transport	275,888	4,244	280,132
Science	87,404	–	87,404
Private sector	129,795	–	129,795
TOTAL	913,693	227,510	1,141,203
PROFIT BEFORE TAXATION AND OTHER COSTS			
Civil Government	13,271	5,169	18,440
Defence	11,312	11,996	23,308
Transport	14,179	209	14,388
Science	4,907	–	4,907
Private sector	6,778	–	6,778
TOTAL	50,447	17,374	67,821
OTHER COSTS			
Common costs			(24,070)
Exceptional item: Cost of unsuccessful NATS acquisition			(10,187)
Exceptional item: GSR refinancing			15,356
Amortisation of intangible assets			(5,123)
Net interest: Group			(5,092)
Net interest: Joint ventures			1,334
PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION			40,039
NET ASSETS			
Civil Government			33,517
Defence			36,282
Transport			27,044
Science			903
Private sector			14,246
TOTAL			111,992
Unallocated assets			17,079
TOTAL			129,071

2 Segmental Report (continued)

Geographical segments	Group £'000	Joint Ventures £'000	Total £'000
2002			
TURNOVER			
United Kingdom	752,247	178,207	930,454
Rest of Europe and Middle East	163,218	7,341	170,559
Asia Pacific	116,671	38,406	155,077
North America	65,142	4,716	69,858
TOTAL	1,097,278	228,670	1,325,948
PROFIT BEFORE TAXATION AND OTHER COSTS			
United Kingdom	35,065	19,029	54,094
Rest of Europe and Middle East	12,895	625	13,520
Asia Pacific	9,503	1,750	11,253
North America	5,472	479	5,951
TOTAL	62,935	21,883	84,818
OTHER COSTS			
Common costs			(25,734)
Amortisation of intangible assets			(8,098)
Net interest: Group			(4,064)
Net interest: Joint ventures			2,019
PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION			48,941
NET ASSETS			
United Kingdom			142,821
Rest of Europe and Middle East			43,951
Asia Pacific			40,057
North America			17,006
TOTAL			243,835
Unallocated assets			24,022
TOTAL			267,857

Note: Turnover is shown by geographical origin. Turnover analysed by geographical destination is not materially different.

2 Segmental Report (continued)

Geographical segments			
2001	Group £'000	Joint Ventures £'000	Restated Total £'000
TURNOVER			
United Kingdom	618,559	175,641	794,200
Rest of Europe and Middle East	130,608	8,876	139,484
Asia Pacific	103,414	38,588	142,002
North America	61,112	4,405	65,517
TOTAL	913,693	227,510	1,141,203
PROFIT BEFORE TAXATION AND OTHER COSTS			
United Kingdom	26,988	14,068	41,056
Rest of Europe and Middle East	10,041	720	10,761
Asia Pacific	8,597	1,871	10,468
North America	4,821	715	5,536
TOTAL	50,447	17,374	67,821
OTHER COSTS			
Common costs			(24,070)
Exceptional item: Cost of unsuccessful NATS acquisition			(10,187)
Exceptional item: GSR refinancing			15,356
Amortisation of intangible assets			(5,123)
Net interest: Group			(5,092)
Net interest: Joint ventures			1,334
PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION			40,039
NET ASSETS			
United Kingdom			64,563
Rest of Europe and Middle East			9,278
Asia Pacific			30,919
North America			7,232
TOTAL			111,992
Unallocated assets			17,079
TOTAL			129,071

Note: Turnover is shown by geographical origin. Turnover analysed by geographical destination is not materially different.

3 Information regarding Directors and Employees

	2002 £'000	2001 £'000
a) Directors' remuneration:		
Fees as Directors	97	83
Other emoluments	1,730	1,319
Total remuneration excluding pensions	1,827	1,402

The prior year comparative includes Directors who did not serve in 2002.

	2002 £'000	2001 £'000
b) Employee costs including Directors:		
Wages and salaries	444,693	399,447
Social security costs	36,713	36,376
Other pension costs (Note 31)	29,096	19,544
Long Term Incentive Scheme costs	776	661
	511,278	456,028

	2002	2001
c) Number of persons employed by Serco Group plc and its subsidiaries		
Average number of persons employed in the provision of services:		
Civil Government	7,138	6,738
Defence	6,251	6,491
Transport	4,442	4,653
Science	1,665	1,460
Private sector	2,999	2,445
Non-specific	202	116
	22,697	21,903

4 Interest receivable

	2002 £'000	2001 £'000
Short term deposits	818	1,484
Loans to joint ventures	604	723
Total Group	1,422	2,207
Share of joint venture interest	16,894	17,102
	18,316	19,309

5 Interest payable and similar charges

	2002 £'000	2001 £'000
Bank loans and overdrafts	5,486	7,299
Share of joint venture interest	14,875	15,768
	20,361	23,067

6 Profit on ordinary activities before taxation

	2002 £'000	2001 £'000
Profit on ordinary activities before taxation is after charging:		
Rentals under operating leases:		
Land and buildings	12,599	11,790
Plant and machinery	20,686	17,586
Depreciation on tangible assets:		
Owned	12,307	10,861
Held under finance leases	3,227	2,299
Finance lease interest on operational assets	721	454
Amortisation of goodwill and intangible assets	8,098	5,123
Auditors' remuneration:		
Deloitte & Touche	514	444
Other auditors	175	125
Other fees paid to Deloitte & Touche:		
Bid support	1,170	659
Tax	490	544
Other	595	432
Other fees paid to other accountancy firms:		
Internal audit	152	183
Other	555	391

7 Taxation on profit on ordinary activities

	2002 £'000	Restated 2001 £'000
The taxation charge on the profit for the year is made up as follows:		
United Kingdom Corporation Tax	1,654	3,010
Double tax relief	–	(349)
Overseas taxation:		
Operating income	1,950	2,777
Exceptional item: GSR refinancing	–	1,219
Deferred taxation	4,120	(504)
Adjustment in respect of prior years:		
United Kingdom Corporation Tax	(750)	292
Overseas taxation	(37)	–
Deferred taxation	2,375	501
Share of joint ventures' taxation charge	7,327	6,066
	16,639	13,012

The current tax recognised for the year is higher than the United Kingdom corporation tax rate of 30%. The main reasons for this are set out below:

	2002 £'000	Restated 2001 £'000
Profit on ordinary activities before taxation multiplied by the UK Corporation Tax rate of 30%	14,682	12,012
Effect on the reported tax charge of:		
Expenses not deductible for tax purposes (primarily goodwill amortisation)	3,463	4,450
Tax allowances in excess of depreciation	(1,828)	(2,610)
Other short term timing differences	(1,953)	(2,109)
Unrelieved tax losses and higher tax rates on overseas earnings	255	2,458
Tax exempt income and the effect of the use of unrecognised tax losses	(634)	(519)
Tax incentives including Tonnage Tax and Research & Development Tax Credits	(3,054)	(959)
Current tax charge for the year	10,931	12,723
Deferred tax	6,495	(3)
Adjustment in respect of prior years	(787)	292
Taxation on profit on ordinary activities	16,639	13,012

8 Dividends

	2002 £'000	2001 £'000
Interim dividend of 0.64p per share on 429,260,960 Ordinary Shares (2001 – 0.57p on 392,551,903 Ordinary Shares) of 2p each fully paid – paid 11 October 2002	2,747	2,238
Proposed final dividend of 1.44p per share on 429,448,207 Ordinary Shares (2001 – 1.29p on 389,613,782 Ordinary Shares) of 2p each fully paid – proposed payment on 13 May 2003	6,184	5,026
	8,931	7,264
2001 final dividend of 1.29p on 39,547,465 shares issued between 31 December 2001 and 13 March 2002 (record date)	510	–
2000 final dividend of 1.13p on 50,212 shares relating to shares issued between 31 December 2000 and 6 April 2001 (record date)	–	1
	9,441	7,265

A dividend waiver is effective for those shares held on behalf of the Company by its Employee Share Ownership Trust.

9 Earnings per Ordinary Share

Basic and diluted earnings per Ordinary Share after goodwill have been calculated in accordance with Financial Reporting Standard 14 ("FRS 14") – Earnings Per Share. Earnings per share is shown both before and after goodwill to assist in the understanding of the impact of FRS 10 on the Group Accounts.

The calculation of basic earnings per Ordinary Share after goodwill is based on profits of £32,302,000 for the year ended 31 December 2002 (2001 restated – £27,027,000) and the weighted average number of 421,813,107 (2001 – 389,552,980) Ordinary Shares of 2p each in issue during the year.

The calculation of basic earnings per Ordinary Share before goodwill is based on profits of £40,400,000 (adjusted for the effect of goodwill amortisation of £8,098,000) for the year ended 31 December 2002 (2001 restated – £32,150,000 adjusted for the effect of goodwill amortisation of £5,123,000) and the weighted average number of 421,813,107 (2001 – 389,552,980) Ordinary Shares of 2p each in issue during the year.

The calculation of diluted earnings per Ordinary Share after goodwill is based on profits of £32,302,000 for the year ended 31 December 2002 (2001 restated – £27,027,000) and the weighted average number of 423,288,423 (2001 – 391,115,673) Ordinary Shares of 2p each assuming that the options are all exercised.

The calculation of diluted earnings per Ordinary Share before goodwill is based on profits of £40,400,000 (adjusted for the effect of goodwill amortisation of £8,098,000) for the year ended 31 December 2002 (2001 restated – £32,150,000 adjusted for the effect of goodwill amortisation of £5,123,000) and the weighted average number of 423,288,423 (2001 – 391,115,673) Ordinary Shares of 2p each assuming that the options are all exercised.

10 Intangible assets

	Goodwill £'000	Other £'000	Group Total £'000
Cost:			
At 1 January 2002	152,889	–	152,889
Additions during the year	13,029	1,775	14,804
Adjustments to goodwill capitalised on acquisitions prior to 1 January 2002	(403)	–	(403)
AT 31 DECEMBER 2002	165,515	1,775	167,290
Accumulated amortisation:			
At 1 January 2002	11,719	–	11,719
Charge for the year	7,777	321	8,098
AT 31 DECEMBER 2002	19,496	321	19,817
Net book value:			
AT 31 DECEMBER 2002	146,019	1,454	147,473
At 31 December 2001	141,170	–	141,170

Other intangible assets comprise a £1,775,000 premium for the acquisition of two, five-year, licences and are amortised over the licence life.

11 Tangible assets

Group	Freehold land and buildings £'000	Short leasehold building improvements £'000	Machinery, motor vehicles, furniture and equipment £'000	Total £'000
Cost:				
At 1 January 2002	7,567	10,128	97,846	115,541
Subsidiaries acquired	–	–	838	838
Transfer from asset held for resale	5,532	–	–	5,532
Capital expenditure	63	3,749	25,619	29,431
Disposals	(5,535)	(214)	(5,799)	(11,548)
Foreign exchange differences	405	73	1,916	2,394
AT 31 DECEMBER 2002	8,032	13,736	120,420	142,188
Accumulated depreciation:				
At 1 January 2002	2,234	4,074	60,509	66,817
Subsidiaries acquired	–	–	483	483
Provided during the year	181	1,153	14,200	15,534
Disposals	–	(175)	(4,458)	(4,633)
Foreign exchange differences	143	17	1,348	1,508
AT 31 DECEMBER 2002	2,558	5,069	72,082	79,709
Net book value:				
AT 31 DECEMBER 2002	5,474	8,667	48,338	62,479
At 31 December 2001	5,333	6,054	37,337	48,724

The cost of assets held by the Group under finance leases at 31 December 2002 was £24,977,000 (2001 – £18,905,000). The accumulated depreciation provided for those assets at 31 December 2002 was £9,168,000 (2001 – £6,903,000).

11 Tangible assets (continued)

Company	Short leasehold building improvements £'000	Machinery, motor vehicles, furniture and equipment £'000	Total £'000
Cost:			
At 1 January 2002	1,117	2,624	3,741
Transfers from subsidiary undertakings	1,161	2,329	3,490
Transfers to subsidiary undertakings	(1,049)	(1,897)	(2,946)
Capital expenditure	36	1,054	1,090
Disposals	-	(27)	(27)
AT 31 DECEMBER 2002	1,265	4,083	5,348
Accumulated depreciation:			
At 1 January 2002	355	1,704	2,059
Transfers from subsidiary undertakings	365	1,398	1,763
Transfers to subsidiary undertakings	(323)	(1,160)	(1,483)
Provided during the year	151	566	717
Disposals	-	(17)	(17)
AT 31 DECEMBER 2002	548	2,491	3,039
Net book value:			
AT 31 DECEMBER 2002	717	1,592	2,309
At 31 December 2001	762	920	1,682

The cost of assets held by the Company under finance leases at 31 December 2002 was £872,000 (2001 – £Nil). The accumulated depreciation provided for those assets at 31 December 2002 was £71,307 (2001 – £Nil).

12 Investments held as fixed assets

	Company £'000
a) Shares in subsidiary companies at cost:	
At 1 January 2002	35,598
Transfer of investments from Group companies	115,890
Transfer of investments to Group companies	(29,437)
Equity subscriptions for shares in Group companies	22,908
Redemption of Serco Australia Pty Ltd preference shares	(3,541)
AT 31 DECEMBER 2002	141,418

12 Investments held as fixed assets (continued)

	Group £'000
b) Group investments in joint ventures:	
At 1 January 2002	30,510
Dividends receivable	(11,095)
Acquisitions	370
Disposals	(139)
Foreign exchange translation difference	(338)
Share of profits after tax	16,575
AT 31 DECEMBER 2002	35,883
	Group £'000
c) Investment in own shares:	
At 1 January 2002	18,983
Amortisation	(776)
AT 31 DECEMBER 2002	18,207

Investment in own shares represents 5,414,630 (2001 – 5,557,033) shares in Serco Group plc held by the Employee Share Ownership Trust (the "Trust") equal to 1.25% of current allotted share capital (2001 – 1.4%). The market value of shares held by the Trust at 31 December 2002 was £8,284,384 (2001 – £20,283,170). 142,403 shares were allotted during the year, all of which were at nil value (2001 – 52,308, of which 9,864 were allotted at £4.26 and 42,444 at nil value).

d) Joint ventures:

The Group's share of its joint ventures is summarised as follows:

	AWE* £'000	PCG† £'000	Other £'000	2002 Total £'000	2001 Total £'000
Turnover	91,386	52,504	84,780	228,670	227,510
Profit before tax	7,801	4,993	11,108	23,902	18,708
Tax	(1,832)	(2,070)	(3,425)	(7,327)	(6,066)
Fixed assets	–	2,288	31,278	33,566	54,147
Current assets	21,861	124,266	138,138	284,265	268,191
	21,861	126,554	169,416	317,831	322,338
Liabilities due within one year	17,660	17,518	27,313	62,491	62,817
Liabilities due after more than one year	1,066	94,446	123,945	219,457	229,011
	18,726	111,964	151,258	281,948	291,828
Net assets	3,135	14,590	18,158	35,883	30,510

* Atomic Weapons Establishment Management Ltd

† Premier Custodial Group Ltd

Adjustments have been made to joint venture results to ensure they are consistent with Group accounting policies.

12 Investments held as fixed assets (continued)

- e) A list of the principal undertakings of Serco Group plc is shown in Note 32. All the subsidiaries of the Group have been consolidated.
- f) At 31 December 2002, Group companies had branches in Abu Dhabi, Bahrain, Chile, Dubai, Korea, Ras Al Khaimah, Saudi Arabia, Sharjah and Switzerland.
- g) The subsidiaries of Serco Group plc and its joint venture undertakings are primarily engaged in the provision of services with the exception of Serco Investments Limited and certain other holding companies, which manage equity investments.
- h) Acquisitions:

All acquisitions made during the year have been accounted for using the acquisition method of accounting. The goodwill arising on all acquisitions made in the year is being amortised over a period of 20 years.

i) CCM Software Services Limited

All the issued share capital of CCM Software Services Limited was acquired by Serco International Limited on 3 December 2002 for cash consideration of £8,647,000 and deferred cash consideration, contingent on achievement of certain financial targets post acquisition, valued at £2,068,000. Acquisition costs of £515,000 were incurred.

The fair value of net assets acquired was £631,000 after taking account of adjustments of £448,000 required to recognise obligations for which no liability had been booked at the date of acquisition.

The goodwill arising on consolidation is £10,599,000.

ii) Other acquisitions

The issued share capital of Euromedic Ltd and the assets and liabilities of SDC, a partnership, were acquired by Serco Holdings Ltd on 13 March 2002 and 31 May 2002 respectively for a total cash consideration of £2,088,000 and deferred cash consideration, contingent on achievement of certain financial targets post acquisition, valued at £223,000. Acquisition costs of £103,000 were incurred.

The fair values of assets and liabilities acquired are considered to be the same as their book values. The total goodwill arising on consolidation is £2,430,000.

13 Stocks

	Group 2002 £'000	Group 2001 £'000
Service spares	10,065	10,093
Long term contract balances	28,679	25,745
	38,744	35,838

14 Debtors

	Group 2002 £'000	Restated Group 2001 £'000	Company 2002 £'000	Company 2001 £'000
a) Amounts due within one year:				
Amounts recoverable on contracts	168,820	150,342	–	–
Other debtors	18,425	21,224	21,089	14,747
Prepayments and accrued income	30,131	19,148	580	73
Amounts owed by joint ventures	2,666	4,257	–	–
Building held for re-sale	–	4,734	–	–
	220,042	199,705	21,669	14,820

	Group 2002 £'000	Restated Group 2001 £'000	Company 2002 £'000	Company 2001 £'000
b) Amounts due after more than one year:				
Amounts recoverable on contracts	18,412	11,847	–	–
Other debtors	16,297	14,131	1,297	–
Pensions prepayment (Note 31)	28,350	26,460	–	–
Amounts owed by joint ventures	12,033	9,567	–	–
PFI asset in the course of construction*	33,840	14,100	–	–
	108,932	76,105	1,297	–
TOTAL DEBTORS	328,974	275,810	22,966	14,820

Included in amounts recoverable on contracts is £7,978,000 (2001 – £14,710,000) in respect of items procured on behalf of customers. This is offset by an amount of £8,792,000 (2001 – £12,038,000) in trade creditors and an amount of £945,000 (2001 – £1,611,000) in accruals.

* The impact on the Group Accounts of the PFI asset in the course of construction in relation to the Traffic Control Centre contract is summarised as follows:

	Balance at 1 January 2002 £'000	Movement during the year £'000	Balance at 31 December 2002 £'000
Balances in relation to asset in course of construction:			
PFI asset in the course of construction excluding capitalised interest	13,733	18,355	32,088
Interest included in PFI asset in the course of construction	367	1,385	1,752
Total PFI asset in the course of construction	14,100	19,740	33,840
Cash	–	270	270
Other debtors	–	1,447	1,447
Accruals and deferred income	–	(4,852)	(4,852)
	14,100	16,605	30,705
Funded by:			
Non-recourse loan	(14,100)	(15,600)	(29,700)
Profits retained within Special Purpose Company	–	(1,005)	(1,005)
	(14,100)	(16,605)	(30,705)

15 Other creditors including taxation and social security

	Group 2002 £'000	Group 2001 £'000	Company 2002 £'000	Company 2001 £'000
Obligations under finance leases	4,836	2,557	267	–
Corporation Tax	2,195	4,418	–	–
Other taxes and social security costs	31,432	30,464	304	631
Other creditors	38,034	47,689	117	446
Amounts owed to joint ventures	16,974	14,864	–	–
Other loans	372	629	–	–
	93,843	100,621	688	1,077

16 Creditors: Amounts falling due after more than one year

	Group 2002 £'000	Group 2001 £'000	Company 2002 £'000	Company 2001 £'000
a) Bank loans and overdrafts	2,386	70,647	–	30,245
Obligations under finance leases	15,291	11,385	792	–
Other loans	77,505	60,371	43,259	41,420
Total loans	95,182	142,403	44,051	71,665
Less: amounts included in creditors falling due within one year	7,594	73,833	267	30,245
Amounts falling due after more than one year	87,588	68,570	43,784	41,420

	Group 2002 £'000	Group 2001 £'000	Company 2002 £'000	Company 2001 £'000
b) Analysis of loan repayments due:				
Bank loans and overdrafts:				
Within one year or on demand	2,386	70,647	–	30,245
Obligations under finance leases:				
Within one year or on demand	4,836	2,557	267	–
Between one and two years	4,667	2,543	525	–
Between two and five years	4,291	3,826	–	–
After five years	1,497	2,459	–	–
Other loans:				
Within one year or on demand	372	629	–	–
Between one and two years	1,687	1,618	–	–
Between two and five years	70,735	14,681	43,259	–
Non-recourse debt to fund PFI asset	25,200	14,100	–	–
Other	45,535	581	43,259	–
After five years	4,711	43,443	–	41,420
Non-recourse debt to fund PFI asset	4,500	–	–	–
Other	211	43,443	–	41,420
	95,182	142,403	44,051	71,665

c) Finance lease obligations are secured by retention of title to the relevant assets.

17 Treasury policies and risk management

The principal risks arising from the Group's financing activities are interest rate risk and foreign currency risk. Treasury operations are conducted within a framework of policies set and reviewed by the Board. There has been no material change during the year or since the year end to the major financial risks faced by the Group or the Group's approach to the management of these risks.

As permitted by Financial Reporting Standard 13 ("FRS 13") – Derivatives and other Financial Instruments: Disclosures short term debtors and non interest bearing short term creditors and loans from joint ventures have been excluded from the following disclosures other than the disclosure of the currency profile of financial assets and liabilities.

The fundamental purpose of interest rate and foreign currency financial instruments entered into is to hedge monetary assets and liabilities, the details of which are set out below.

Interest rate risk

The Group borrows at both fixed and floating rates of interest. The Group's exposure to interest rate fluctuations on its long term borrowings is managed by using interest rate swaps and forward rate agreements. At 31 December 2002, after taking account of interest rate swaps, the proportion of the Group's fixed rate borrowings was 66.6% (2001 – 33.3%).

Foreign currency risk

The Group's policy is not to hedge the net assets of overseas subsidiaries as they represent a small proportion of the market value of the Group and because exchange rate fluctuations thereon are unlikely to have a material effect on the consolidated net asset value of the Group.

Business units are required to hedge their material trading transactions (sales and purchases in currencies other than their functional currency) by using forward contracts. There were no material debtors or creditors as at 31 December 2002 with unhedged transactional exposure.

Financial assets and liabilities

i) Assets

	Sterling £'000	Euro £'000	Australian Dollar £'000	US Dollar £'000	Other currencies £'000	Total £'000
31 December 2002						
Cash and short term deposits	43,024	13,468	2,009	2,868	10,405	71,774
Long term interest-bearing loans to joint ventures	8,009	–	4,024	–	–	12,033
Other long term debtors	87,918	7,285	1,696	–	–	96,899
TOTAL LONG TERM ASSETS	95,927	7,285	5,720	–	–	108,932
31 December 2001						
Cash and short term deposits	12,782	11,282	2,450	5,670	2,628	34,812
Long term interest-bearing loans to joint ventures	8,817	–	750	–	–	9,567
Other long term debtors	64,564	–	1,363	611	–	66,538
Total long term assets	73,381	–	2,113	611	–	76,105

Included in the above is £4,095,000 (2001 – £4,117,000) of loans to joint ventures which carry a fixed interest rate of 13.0% for a weighted average period of 13 years (2001 – 14 years). All other interest-bearing assets are held at floating rates of interest. Of total short term debtors 79% (2001 – 93%) is denominated in Sterling.

17 Treasury policies and risk management (continued)

ii) Liabilities

31 December 2002	Total liabilities £'000	Floating rate liabilities £'000	Fixed rate liabilities £'000	Fixed Rate Liabilities	
				Weighted average interest rate %	Weighted average time for which rate is fixed Years
Sterling	44,586	14,886	29,700	5.46	3
Australian Dollar	3,075	3,075	–	–	–
US Dollar	46,885	13,182	33,703	7.33	5
Euro	636	636	–	–	–
TOTAL	95,182	31,779	63,403		

31 December 2001	Total liabilities £'000	Floating rate liabilities £'000	Fixed rate liabilities £'000	Fixed Rate Liabilities	
				Weighted average interest rate %	Weighted average time for which rate is fixed Years
Sterling	98,077	83,977	14,100	5.46	3
Australian Dollar	2,451	2,451	–	–	–
US Dollar	41,420	8,038	33,382	7.34	6
Euro	455	455	–	–	–
Total	142,403	94,921	47,482		

Of total short term creditors 80% (2001 – 81%) is denominated in Sterling.

The maturity of the Group's financial liabilities at 31 December 2002 and 31 December 2001:

31 December 2002	Maturing within one year £'000	Maturing between one and two years £'000	Maturing between two and five years £'000	Maturing after more than five years £'000	Total £'000
Sterling	4,105	3,884	30,677	5,920	44,586
Australian Dollar	768	1,255	829	223	3,075
US Dollar	2,085	1,215	43,520	65	46,885
Euro	636	–	–	–	636
TOTAL	7,594	6,354	75,026	6,208	95,182

31 December 2001	Maturing within one year £'000	Maturing between one and two years £'000	Maturing between two and five years £'000	Maturing after more than five years £'000	Total £'000
Sterling	72,677	3,216	17,777	4,407	98,077
Australian Dollar	701	945	730	75	2,451
US Dollar	–	–	–	41,420	41,420
Euro	455	–	–	–	455
Total	73,833	4,161	18,507	45,902	142,403

17 Treasury policies and risk management (continued)

iii) Fair Values

The book value and fair value of the Group's financial assets and liabilities at 31 December 2002 and 31 December 2001 were:

	2002 Book value £'000	2002 Fair value £'000	2001 Book value £'000	2001 Fair value £'000
ASSETS				
Cash and short term deposits	71,774	71,774	34,812	34,812
Long term loans to joint ventures	12,033	12,033	9,567	9,567
Other long term debtors	96,899	96,899	66,538	66,538
Derivatives held to manage currency and interest rate risk	–	1,716	–	4,492
TOTAL	108,932	110,648	76,105	80,597
LIABILITIES				
Long term borrowing:				
Sterling	40,481	40,481	25,400	25,400
Australian Dollar	2,307	2,307	1,750	1,750
US Dollar	44,800	49,091	41,420	48,991
TOTAL	87,588	91,879	68,570	76,141
Short term borrowing:				
Sterling	4,105	4,105	72,677	72,677
Australian Dollar	768	768	701	701
US Dollar	2,085	2,085	–	–
Euro	636	636	455	455
TOTAL	7,594	7,594	73,833	73,833

Foreign currency assets which are hedged using forward foreign exchange contracts are translated at the contracted rates.

The fair value of other foreign currency contracts, interest rate swaps, and the US\$70,000,000 loan notes, have been determined by reference to prices available from the markets on which the instruments involved are traded.

Gains and losses on hedges

Changes in the fair value of financial instruments used as hedges are not recognised until the hedged position matures. There was an unrecognised gain of £1,716,000 (2001 – gain of £4,492,000) on hedges as at 31 December 2002. The unrecognised gain is not expected to be recognised in the Profit and Loss Account in the next period.

Borrowing facilities

The Group had committed bank credit facilities of £50,000,000 at 31 December 2002. The Group also had annually renewable uncommitted bank facilities totalling £111,000,000, all of which were undrawn at 31 December 2002.

18 Provisions for liabilities and charges

Group	Restated Balance 1 January 2002 £'000	Utilised £'000	Charged to the profit and loss account £'000	Foreign exchange differences £'000	Balance 31 December 2002 £'000
Pensions provision	23,003	(463)	1,663	1,605	25,808
Deferred taxation	2,246	–	6,495	(16)	8,725
	25,249	(463)	8,158	1,589	34,533

Company	Balance 1 January 2002 £'000	Utilised £'000	Charged to the profit and loss account £'000	Foreign exchange differences £'000	Balance 31 December 2002 £'000
Deferred tax	–	–	335	–	335

19 Deferred taxation

	Group 2002 £'000	Restated Group 2001 £'000	Company 2002 £'000	Company 2001 £'000
The amounts of deferred taxation provided in the accounts are:				
Tax allowances in excess of depreciation	2,650	332	(77)	–
Overseas timing differences	1,967	692	–	–
Other timing differences	4,108	1,222	412	–
	8,725	2,246	335	–
Potential amounts of deferred taxation for which no credit has been taken:				
Overseas timing differences	(2,767)	(3,224)	–	–
	(2,767)	(3,224)	–	–

20 Reconciliation of movements in shareholders' funds

	2002 £'000	Restated 2001 £'000
Profit on ordinary activities after taxation	32,302	27,027
Dividends	(9,441)	(7,265)
	22,861	19,762
Currency translation differences on foreign currency net investments	(1,911)	(1,917)
New capital subscribed	117,929	3,561
Exercise of share scheme options	(93)	(1,260)
Net increase in shareholders' funds	138,786	20,146
Opening shareholders' funds as previously stated	129,877	108,925
Prior year adjustment	(806)	–
Opening shareholders' funds as restated	129,071	108,925
Closing shareholders' funds as restated	267,857	129,071

21 Called up share capital

	2002 £'000	2001 £'000
a) Authorised 550,000,000 (2001 – 550,000,000) Ordinary Shares of 2p each	11,000	11,000
b) Called up, allotted and fully paid: 434,862,837 (2001 – 395,170,815) Ordinary Shares of 2p each	8,697	7,903

c) Ordinary Shares of 2p each allotted in the year:

During the year 289,581 Ordinary Shares of 2p each were allotted to the holders of options or their personal representatives.

Of these, 147,178 were allotted using newly issued shares, 2,628 were allotted at £2.0208*, 104,796 at £2.175, 38,706 at £2.45*, and 1,048 at £3.81.

The remaining 142,403 were allotted at nil value using shares purchased in the market and held in trust.

In addition to the above, 39,500,000 Ordinary Shares of 2p each were allotted under a share placement on 12 March 2002 at £3.05. 44,844 Ordinary Shares of 2p each were also allotted on 19 December 2002 as deferred consideration relating to the acquisition of Serco QAA (formerly Quality Assurance Associates Limited) made in December 2000.

*Restated to reflect the capitalisation issue on 5 April 2000.

d) Options in respect of Ordinary Shares of 2p each:

- i) In January 1996, 1,210,392 options in respect of Ordinary Shares of 2p each were granted in accordance with the rules of the 'Serco Group plc 1996 Long Term Incentive Scheme'. At 31 December 2002 no options remain.
- ii) In January 1997, 1,439,622 options in respect of Ordinary Shares of 2p each were granted in accordance with the rules of the 'Serco Group plc 1996 Long Term Incentive Scheme'. At 31 December 2002 there remained 54,000 options which are exercisable at nil value in accordance with the rules of the Scheme.
- iii) 3,341,346 options in respect of Ordinary Shares of 2p each were granted in May and September 1998 in accordance with the rules of the 'Serco Group plc 1998 Executive Option Plan'. At 31 December 2002 there remained 1,606,259 options which are exercisable at a price of £2.175 each and 10,830 at £2.0208* each in accordance with the rules of the Scheme.
- iv) On 1 April 1999, 3,461,664 options in respect of Ordinary Shares of 2p each were granted in accordance with the rules of the 'Serco Group plc 1998 Executive Option Plan'. At 31 December 2002 there remained 2,385,474 options which are exercisable at a price of £2.45 each in accordance with the rules of the Scheme.
- v) On 31 March 2000, 4,511,988 options in respect of Ordinary Shares of 2p each were granted as part of the 1996 Sharesave Scheme. 2,577,092 options were held by employees on 31 December 2002. The options are exercisable at any time between 1 May 2003 and 31 October 2003 at a price of £3.81 each in accordance with the rules of the Scheme.
- vi) On 5 April 2000, 2,524,836 options in respect of Ordinary Shares of 2p each were granted in accordance with the rules of the 'Serco Group plc 1998 Executive Option Plan'. At 31 December 2002 there remained 2,368,224 options which are exercisable at a price of £4.2542* each in accordance with the rules of the Scheme.

21 Called up share capital (continued)

d) Options in respect of Ordinary Shares of 2p each: (continued)

- vii) On 5 April 2000, 219,900 options in respect of Ordinary Shares of 2p each were granted in accordance with the rules of the '1996 Serco Group plc Long Term Incentive Scheme as amended by the Company on 5 April 2000'. At 31 December 2002 there remained 148,236 options which are exercisable at a nil value in accordance with the rules of the Scheme.
- viii) 37,677 options in respect of Ordinary Shares of 2p each were granted in August and November 2000, in accordance with the rules of the 'Serco Group plc 1998 Executive Option Plan'. As at 31 December 2002 there remained 26,268 options which are exercisable at a price of £5.825 and 8,878 options which are exercisable at a price of £4.90 each in accordance with the rules of the scheme.
- ix) On 24 November 2000, 259,351 options in respect of Ordinary Shares of 2p each were granted in accordance with the rules of the '1996 Serco Group plc Long Term Incentive Scheme as amended by the Company on 5 April 2000'. At 31 December 2002 there remained 188,169 options which are exercisable at nil value in accordance with the rules of the Scheme.
- x) On 20 March 2001, 2,851,962 options in respect of Ordinary Shares of 2p each were granted in accordance with the rules of the 'Serco Group plc 1998 Executive Option Plan'. As at 31 December 2002 there remained 2,700,200 options which are exercisable at a price of £4.07 each in accordance with the rules of the Scheme.
- xi) On 27 March 2001, 603,144 options in respect of Ordinary Shares of 2p each were granted in accordance with the rules of the 'Serco Group plc 1998 Executive Option Plan'. As at 31 December 2002 there remained 600,838 options which are exercisable at a price of £4.35 each in accordance with the rules of the Scheme.
- xii) On 16 November 2001, 248,374 options in respect of Ordinary Shares of 2p each were granted in accordance with the rules of the '1996 Serco Group plc Long Term Incentive Scheme as amended by the Company on 5 April 2000'. At 31 December 2002 there remained 200,202 options which are exercisable at nil value in accordance with the rules of the Scheme.
- xiii) On 3 May 2002, 5,986,743 options in respect of Ordinary Shares of 2p each were granted in accordance with the rules of the 'Serco Group plc 1998 Executive Option Plan'. As at 31 December 2002 there remained 5,914,886 options which are exercisable at a price of £2.64 each in accordance with the rules of the Scheme.
- xiv) On 3 May 2002, 55,600 options in respect of Ordinary Shares of 2p each were granted in accordance with the rules of the '1996 Serco Group plc Long Term Incentive Scheme as amended by the Company on 5 April 2000'. At 31 December 2002 no options had been exercised or lapsed. These options have been granted in respect of a three year performance period starting 1 January 2002 and are exercisable at a nil value in accordance with the rules of the Scheme.
- xv) On 6 September 2002, 5,428,691 options in respect of Ordinary Shares of 2p each were granted in accordance with the rules of the 'Serco Group plc 1998 Executive Option Plan'. As at 31 December 2002 there remained 5,327,309 options which are exercisable at a price of £1.645 each in accordance with the rules of the Scheme.

*Restated to reflect the capitalisation issue on 5 April 2000.

- e) The market price of Serco Group plc Ordinary Shares of 2p each as at 31 December 2002 was £1.53. The market prices of these shares ranged from £4.00 to £1.325 during the year.

22 Share premium account

Group and Company	£'000
Balance at 1 January 2002	73,656
Deferred consideration relating to the acquisition of Serco QAA Limited	69
Share premium on issue of shares upon exercise of options	422
Share placement (net of £3,041,000 expenses)	116,644
BALANCE AT 31 DECEMBER 2002	190,791

23 Profit and loss account

	£'000
Group	
At 31 December as previously stated	48,175
Prior year adjustment	(806)
Balance at 1 January 2002 as restated	47,369
Retained profit transferred to reserves	22,861
Currency translation differences on foreign currency net investments	(1,911)
Exercise of share option schemes	(93)
BALANCE AT 31 DECEMBER 2002	68,226

The Profit and Loss Account includes a goodwill charge of £41,578,000 under the accounting policy applicable prior to the implementation of FRS 10.

Company

As permitted by Section 230 of the Companies Act 1985, the Profit and Loss Account of the Parent Company is not presented as part of these accounts. The consolidated profit for the financial year includes the Parent Company profit of £14,219,000, which includes dividends of £24,874,000 received from subsidiary companies.

A final ordinary dividend of £6,184,000 is proposed, which together with the interim dividend of £2,747,000 and the payment in relation to the 2001 final dividend caused by the movement in the number of shares in issue of £510,000, leaves a profit of £4,778,000 which has been added to reserves brought forward of £34,958,000. This, along with a foreign exchange charge of £1,947,000, results in reserves carried forward of £37,789,000.

24 Reconciliation of operating profit to net cash inflow from operating activities

	2002 £'000	Restated 2001 £'000
Operating profit before cost of unsuccessful NATS acquisition	29,103	21,254
Exceptional item: Cost of unsuccessful NATS acquisition	–	(10,187)
Operating profit	29,103	11,067
Depreciation	15,534	13,160
Amortisation of goodwill and intangible fixed assets	8,098	5,123
Profit on sale of tangible fixed assets	(1,948)	(1,236)
Increase in stocks	(2,906)	(8,932)
Increase in debtors	(41,870)	(56,223)
Increase in creditors	30,795	53,578
Increase/(decrease) in provisions	2,805	(1,053)
One off pension fund contribution	(15,500)	–
NET CASH INFLOW FROM OPERATING ACTIVITIES BEFORE PFI ASSET EXPENDITURE	24,111	15,484
Expenditure on PFI asset in the course of construction	(14,950)	(13,733)
Net cash inflow from operating activities after PFI asset expenditure	9,161	1,751

25 Analysis of net debt

	Balance 1 January 2002 £'000	Cash flow £'000	Other non-cash changes £'000	Balance 31 December 2002 £'000
Cash at bank and in hand	34,812	36,962	–	71,774
Overdrafts	(70,647)	68,261	–	(2,386)
Cash net of overdrafts	(35,835)	105,223	–	69,388
Other loans due after more than one year	(45,642)	(24)	(1,767)	(47,433)
Other loans due within one year	(629)	300	(43)	(372)
Finance leases	(11,385)	3,594	(7,500)	(15,291)
Recourse net cash	(93,491)	109,093	(9,310)	6,292
Non-recourse debt to fund PFI asset	(14,100)	(15,600)	–	(29,700)
Net debt	(107,591)	93,493	(9,310)	(23,408)

26 Reconciliation of increase/(decrease) in cash to movement in net debt

	2002 £'000	2001 £'000
Increase/(decrease) in cash	105,223	(81,332)
Cash inflow from non-recourse debt financing PFI asset	(15,600)	(14,100)
Cash outflow from debt and lease financing	3,870	1,935
Change in net debt resulting from cash flows	93,493	(93,497)
Non cash changes from other debt and lease financing	(9,310)	(10,089)
Movement in net debt in the year	84,183	(103,586)
Net debt at 1 January	(107,591)	(4,005)
Net debt at 31 December	(23,408)	(107,591)

27 Major non-cash transactions

During the year the Group entered into finance lease arrangements in respect of assets with a total capital value at the inception of the leases of £7,610,000 (2001 – £10,089,000).

During the year £93,000 (2001 – £1,260,000) has been charged to the profit and loss reserve in respect of shares issued under employee share incentive schemes.

Other non-cash movements with respect to other loans relate to foreign exchange.

28 Contingent liabilities

The Group has given indemnities in respect of overseas credit facilities and lease payments amounting to £7,426,000 (2001 – £7,590,000).

In addition to this, the Group has given indemnities in respect of performance guarantees, letters of credit and import duty guarantees issued on its behalf in the ordinary course of business, which are not expected to result in any material financial loss.

29 Capital and other commitments

	Group 2002 £'000	Group 2001 £'000	Company 2002 £'000	Company 2001 £'000
Capital expenditure contracted but not provided	8,595	1,244	–	–

There is a commitment of £30 million in relation to the Traffic Control Centre PFI asset under construction, which will be funded by non-recourse bank debt.

During the year ending 31 December 2003 the Group is to make the following payments in respect of operating leases:

	Land and buildings £'000	Other £'000
Leases which expire:		
Within one year	1,965	4,199
Between one and five years	7,015	16,690
After five years	4,464	4,264
	13,444	25,153

30 Related parties

Directors

The Directors of Serco Group plc had no material transactions with the Group during the year other than service contracts and Directors' liability insurance.

Joint ventures

The following material transactions took place between the Group and its joint ventures during 2002:

	2002 £'000	2001 £'000
Net loans during the year	1,797	2,131
Net trading	1,800	2,671
Royalties and management fees receivable	2,302	2,448
Dividends receivable	11,095	9,645
	16,994	16,895

The following receivable balances relating to joint ventures were included in the Group Balance Sheet:

	2002 £'000	2001 £'000
Amounts due within one year:		
Loans	2,140	–
Trading balance	287	342
Royalties and management fees	239	3,915
	2,666	4,257
Amounts due after more than one year:		
Loans	12,033	9,567
	12,033	9,567

The following payable balances relating to joint ventures were included in the Group Balance Sheet:

	2002 £'000	2001 £'000
Amounts payable within one year:		
Loans	16,974	14,165
Trading balance	–	699
	16,974	14,864

Details of Group investments in joint ventures and other principal undertakings are given in Note 32.

31 Pension schemes

The Group has continued to account for pensions in accordance with SSAP 24. Full adoption of the requirements of FRS 17 - Retirement Benefits will not be mandatory for the Group until the year ended 31 December 2005. The transitional disclosures required by FRS 17 are set out in Part (B) of this note which shows the Group's pension deficit in accordance with FRS 17 at 31 December 2002 was £73.6 million (2001 - £3.6 million) on an asset base of £294.4 million (2001 - £298.4 million).

A) SSAP 24 Disclosure

The net pension charge in accordance with SSAP 24 for the year ended 31 December 2002 was £29,096,000 (2001 - £19,544,000). The Group operates or is a member of a number of pension schemes as follows:

a) Serco Pension and Life Assurance Scheme ("SPLAS")

This is a pre-funded defined benefit scheme.

The funding policy is to contribute such variable amounts, on the advice of the actuary, as will achieve 100% funding on a projected salary basis.

The latest formal valuation of the scheme was carried out as at 6 April 1999. The figures included in the accounts are based on a formal valuation, which is currently being carried out as at 6 April 2002. During 2002 there has been a fall in general stock market values and a bulk transfer was received from the AEA Technology Pension Scheme. The figures in the Profit and Loss Account and the Balance Sheet prepayment have been determined in accordance with the requirements of SSAP 24. The average contribution rate is currently 18% for the scheme.

The projected unit method was adopted for the actuarial valuation of the Scheme for accounting purposes. The main actuarial assumptions used to value liabilities are:

Investment yield	7.0% p.a. (5.5% post retirement)
Salary growth	3.75% p.a.
Price inflation	2.5% p.a.
Pension increases	2.5% p.a.

The Scheme is assessed to be fully funded on a current funding level basis based on a market value of assets of £145,881,000 at 6 April 1999. Liabilities for this purpose are calculated using the basis for determining individual cash equivalents for active members and deferred pensioners and by estimating the cost of purchasing annuity policies for pensioners.

The actuarial value of the assets represented 81% of the ongoing liabilities of the Scheme. Variations from the normal costs are amortised for accounting purposes over a fifteen year period as a constant monetary amount.

Employer pension contributions paid into the Scheme during the year were £12,300,000 (2001 - £9,760,000), of which £500,000 related to special contributions in respect of a discretionary increase to pensions in payment awarded during the year (2001 - £652,000) and £600,000 of contributions in respect of augmentations (2001 - £810,000). A £15,000,000 contribution which was included in accruals and prepayments at 31 December 2001 was paid in February 2002.

At 31 December 2002 a prepayment of £17,450,000 (2001 - £17,360,000) in respect of the Scheme was included in the Balance Sheet. £12,210,000 was charged to the Profit and Loss Account in respect of the Scheme (2001 - £8,950,000).

31 Pension schemes (continued)

A) SSAP 24 Disclosure (continued)

b) The Serco-IAL Pension Scheme

This is a pre-funded defined benefit scheme.

The funding policy is to contribute such variable amounts, on the advice of the actuary, as will achieve 100% funding on a projected salary basis.

Actuarial assessments covering expenses and contributions are carried out by independent qualified actuaries, with the last such review being carried out as at 31 March 2001. On the assumptions adopted for accounting purposes and based on a market value of assets of £104,037,000 at 31 March 2001, the actuarial value of the assets represented 110% of the ongoing past service liabilities of the Scheme as at that date. The current contribution rate is 17.8% for the Scheme.

For accounting purposes, the projected unit method has been adopted and the main actuarial assumptions used to value liabilities are:

Investment return	6.0% p.a.
Salary growth (excluding salary scale)	4.5% p.a.
Pension increases	2.5% p.a.

The past service surplus in excess of the prepayment as at 31 March 2001 is being amortised for accounting purposes over a nine year period at a constant monetary amount.

Employer pension contributions paid into the Scheme during the year were £2,125,000 (2001 – £1,738,000).

An amount of £325,000 (2001 – £300,000) has been charged to the 2002 Profit and Loss Account in respect of the Scheme and a prepayment of £10,900,000 (2001 – £9,100,000) has been included in the Balance Sheet as at 31 December 2002.

c) Serco GmbH & Co.KG Pension arrangement

The German pension arrangement comprises two elements; an unfunded defined benefit arrangement and an unfunded hybrid scheme.

Actuarial assessments covering liabilities are carried out by independent qualified actuaries, with the last such review being carried out as at 23 December 1999 and updated as at 31 December 2002 by a qualified independent actuary.

The projected unit method was adopted for the actuarial valuation of the arrangement. The main actuarial assumptions used in the valuation for accounting purposes were:

Discount rate	6.0% p.a.
Salary growth	3.0% p.a.
Price inflation	1.0% p.a.

The Profit and Loss charge for the year was £1,663,000 (2001 – £130,000) and a provision of £25,808,000 (2001 – £23,003,000) has been included in the Balance Sheet as at 31 December 2002 of which £20,271,000 (2001 – £17,466,000) relates to the hybrid element of the Scheme and £5,537,000 to the defined benefit element of the Scheme.

31 Pension schemes (continued)**A) SSAP 24 Disclosure (continued)**

d) Serco Superannuation Fund

The defined benefit element of the Scheme was established in Australia on 1 April 1993 to provide equivalent benefits for members transferring from the AWA Defence Industries Superannuation Fund, a defined benefit scheme.

Actuarial assessments covering expenses and contributions relating to the defined benefit element of the Scheme are carried out by independent qualified actuaries, with the last such valuation being carried out as at 31 December 2000. The attained age method was used for the actuarial valuation of the Scheme as at 31 December 2000. This method was chosen to produce a level employer contribution rate as a proportion of members' salaries over the expected future working lives of the existing members, as the defined benefit element of the Scheme was closed to new members with effect from 1 April 1993.

The main actuarial assumptions used in the actuarial valuation for accounting purposes were:

Average long term interest rate (net of investments and administration expenses and investment tax)	8.0% p.a.
Average long term allowance for salary increases	5.5% p.a.

The defined benefit element of the Scheme was assessed to be fully funded on a current funding level based on a market value of assets of £1,385,000 (A\$3,938,000) at 31 December 2000 with a ratio of market value of assets to current funding level liabilities of 107%.

The actuarial value of assets of the defined benefit element of the Scheme represented 115% of its ongoing liabilities at 31 December 2000. The pension cost calculated under the attained age method will amortise the above surplus over the expected future working lives of the existing members which have an average value of 11 years.

Employer pension contributions paid into the Scheme and charged to the 2002 Profit and Loss Account relating to the defined benefit element of the Scheme were £257,000 (2001 – £104,000).

e) The NPL Management Limited Pension Scheme

This is a pre-funded defined benefit scheme. The Company accounts for this scheme as a defined contribution scheme since at re-bid any surplus or deficit would transfer to the next contractor. Cash contributions are recognised as pension costs and no asset or liability is shown on the Balance Sheet.

Actuarial assessments covering expenses and contributions are carried out by independent qualified actuaries, with the last such review being carried out as at 5 April 2001. The funding policy is to contribute such variable amounts as will achieve 100% funding on a projected unit basis.

The average contribution rate is currently 20.8% for the scheme.

The main actuarial assumptions proposed in the valuation were:

Investment return	6.50% p.a. (5.0% for current pensioners)
Salary growth	4.25% p.a. (plus promotional scale)
Price inflation	2.25% p.a.
Pension increases	2.25% p.a.

The market value of assets represented 93% of the ongoing liabilities of the Scheme.

Employer pension contributions charged to the 2002 Profit and Loss Account were £1,903,000 (2001 – £1,634,000).

31 Pension schemes (continued)

A) SSAP 24 Disclosure (continued)

f) The Serco Shared Cost Section of the Railways Pension Scheme

This is a pre-funded defined benefit scheme. The Company accounts for this scheme as a defined contribution scheme since at re-bid any surplus or deficit would transfer to the next contractor. Cash contributions are recognised as pension costs and no asset or liability is shown on the Balance Sheet.

Actuarial assessments covering expenses and contributions are carried out by independent qualified actuaries, the last such review being carried out as at 31 December 2001. The funding policy is to contribute such variable amounts as will achieve 100% funding on a projected unit basis.

The main actuarial assumptions used in the valuation were:

Investment return	6.3% p.a.
Salary growth	4.0% p.a. (plus promotional scale)
Price inflation	2.5% p.a.
Pension increases	2.5% p.a.

The actuarial value of assets represented 117% of the ongoing liabilities of the Scheme. The current contribution rate is 7.5%.

Employer pension contributions charged to the 2002 Profit and Loss Account during the year were £715,000 (2001 – £634,000).

g) Serco Metrolink Pension Scheme

This is a pre-funded defined benefit scheme. The Company accounts for this scheme as a defined contribution scheme as at re-bid any surplus or deficit would transfer to the next contractor. Cash contributions are recognised as pension costs and no asset or liability is shown on the Balance Sheet.

Actuarial assessments covering expenses and contributions are carried out by independent qualified actuaries, the last such review being carried out as at 31 August 2001. The funding policy is to contribute such variable amounts as will achieve 100% funding on a projected unit basis.

The main actuarial assumptions used in the valuation were:

Investment return	6.5% p.a.
Salary growth	4.4% p.a.
Price inflation	2.4% p.a.
Pension increases	2.4% p.a.

The actuarial value of assets represented 82% of the ongoing liabilities of the Scheme. The current contribution rate is 8.2%.

Employer pension contributions charged to the 2002 Profit and Loss Account were £244,000 (2001 – £225,000).

31 Pension schemes (continued)**A) SSAP 24 Disclosure (continued)**

h) Docklands Light Railway Pension Scheme

This is a pre-funded defined benefit scheme with Docklands Light Railway Limited being the principal employer. Serco accounts for this scheme as a defined contribution scheme, since at re-bid any surplus or deficit would transfer to the next contractor. Cash contributions are recognised as pension costs and no asset or liability is shown on the Balance Sheet.

Actuarial assessments covering expenses and contributions are carried out by independent qualified actuaries, with the last such review being carried out at 1 April 2001. The funding policy is to contribute such variable amounts as will achieve 100% funding on a projected unit basis. The main actuarial assumptions used in the valuation this year were:

Investment return	7.0% p.a.
Salary growth	5.0% p.a. (including promotional scale)
Pension increases	3.0% p.a.
Dividend yield	2.75% p.a.

The actuarial value of assets represented 96% of the ongoing liabilities of the Scheme. The current contribution rate is 15.2%.

Employer pension contributions charged to the 2002 Profit and Loss Account were £1,378,000 (2001 – £1,181,000).

i) Other defined contribution schemes

The Group paid employer contributions of £10,401,000 (2001 – £6,386,000) into UK and Australian defined contribution schemes and foreign state pension schemes.

B) FRS 17 Disclosure

The disclosures required under the transitional arrangements within FRS 17 have been based on the most recent full actuarial valuations of the Serco Pension and Life Assurance Scheme as at 6 April 1999 and the Serco-IAL Scheme as at 31 March 2001, updated to 31 December 2002 by independent qualified actuaries.

If the amounts had been recognised in the financial statements the net assets and the Profit and Loss Account would be as follows:

	2002 £'000	Restated 2001 £'000
Net assets excluding net, SSAP 24, pension assets	248,012	110,549
Net pension liability under FRS 17	(73,601)	(3,614)
Net assets including pension liabilities under FRS 17	174,411	106,935
	2002 £'000	Restated 2001 £'000
Profit and loss reserve	68,226	47,369
Reversal of SSAP 24 prepayments, net of deferred taxation	(19,845)	(18,522)
	48,381	28,847
(Deficit) in relation to SPLAS scheme, net of deferred taxation	(62,427)	(5,740)
(Deficit)/surplus in relation to Serco-IAL scheme, net of deferred taxation	(11,174)	2,126
Total pension deficit	(73,601)	(3,614)
Profit and loss reserve adjusted	(25,220)	25,233

31 Pension schemes (continued)**B) FRS 17 Disclosure (continued)**

a) Serco Pension and Life Assurance Scheme ("SPLAS")

The financial assumptions used were:

	2002 % p.a.	2001 % p.a.
Rate of increase in salaries	3.85	4.00
Rate of increase in deferred pensions	2.25	2.25
Rate of increase in pensions in payment	2.25	2.25
Discount rate	5.47	5.83
Inflation assumption	2.35	2.50

The Scheme's assets and the expected rates of return as at 31 December 2002 were:

	2002 % p.a.	2002 £'000	2001 % p.a.	2001 £'000
Equities	7.00	134,319	7.25	119,600
AA corporate bonds	5.47	17,252	5.83	15,500
Gilts	4.50	28,264	5.00	21,000
Cash and other	4.00	–	4.00	15,800
Total market value of assets		179,835		171,900
Present value of scheme liabilities		(269,017)		(180,100)
Deficit in the Scheme		(89,182)		(8,200)
Related deferred tax asset		26,755		2,460
Net pension liability		(62,427)		(5,740)

The amount chargeable under FRS 17 to operating profit for the year ended 31 December 2002 would have been:

	£'000
Service cost	11,391
Past service cost	1,100
Total operating charge	12,491

Analysis of the net return on the pension scheme for the year ended 31 December 2002:

	£'000
Expected return on pension scheme assets	12,872
Interest on pension liabilities	(12,664)
Net return	208

31 Pension schemes (continued)**B) FRS 17 Disclosure (continued)**

a) Serco Pension and Life Assurance Scheme ("SPLAS") (continued)

Analysis of amount recognisable in Statement of Total Recognised Gains and Losses ("STRGL") for the year ended 31 December 2002:

	£'000
Actual return less expected return on assets	(56,996)
Experience gains and losses on liabilities	(20,013)
Changes in assumptions	(3,990)
Actuarial loss recognised in STRGL	(80,999)

Movement in deficit during the year:

	£'000
Deficit in scheme at 31 December 2001	(8,200)
Movement in year:	
Current service cost	(11,391)
Contributions	12,300
Past service costs	(1,100)
Net return on assets	208
Actuarial loss	(80,999)
Deficit in scheme at 31 December 2002	(89,182)

History of experience gains and losses:

	2002 £'000
Difference between expected and actual return on scheme assets	(56,996)
Percentage of scheme assets	31.7%
Experience gains and losses on scheme liabilities	(20,013)
Percentage of scheme liabilities	7.4%
Total amount recognised in STRGL	(80,999)
Percentage of scheme liabilities	30.1%

31 Pension schemes (continued)**B) FRS 17 Disclosure (continued)**

b) The Serco-IAL Pension Scheme

The financial assumptions used were:

	2002 % p.a.	2001 % p.a.
Rate of increase in salaries	3.85	4.00
Rate of increase in pensions		
– RPI	2.35	2.50
– LPI	2.25	2.25
– discretionary	2.25	2.25
Discount rate	5.47	5.83
Inflation assumption	2.35	2.50

The Scheme's assets and the expected rates of return as at 31 December 2002 were:

	2002 % p.a.	2002 £'000	2001 % p.a.	2001 £'000
Equities	7.00	49,483	7.25	59,694
UK bonds	4.82	28,758	5.18	31,336
Property	6.24	7,690	6.54	7,329
Cash and other assets	4.50	908	4.00	78
Annuity policies	5.47	27,798	5.83	28,100
Total market value of assets		114,637		126,537
Present value of scheme liabilities		(130,600)		(123,500)
(Deficit)/surplus in the Scheme		(15,963)		3,037
Related deferred tax asset/(liability)		4,789		(911)
Net pension (liability)/asset		(11,174)		2,126

The amount chargeable under FRS 17 to operating profit for the year ended 31 December 2002 would have been:

	£'000
Service cost	2,300
Past service cost	–
Total operating charge	2,300

Analysis of the net return on the pension scheme for the year ended 31 December 2002:

	£'000
Expected return on pension scheme assets	7,900
Interest on pension liabilities	(7,000)
Net return	900

31 Pension schemes (continued)**B) FRS 17 Disclosure (continued)**

b) The Serco-IAL Pension Scheme (continued)

Analysis of amount recognisable in STRGL for the year ended 31 December 2002:

	£'000
Actual return less expected return on assets	(16,100)
Experience gains and losses on liabilities	700
Changes in assumptions	(4,300)
Actuarial loss recognised in STRGL	(19,700)

Movement in surplus during the year:

	£'000
Surplus in scheme at 31 December 2001	3,037
Movement in year:	
Current service cost	(2,300)
Contributions	2,100
Past service costs	-
Net return on assets	900
Actuarial loss	(19,700)
Deficit in scheme at 31 December 2002	(15,963)

History of experience gains and losses:

	2002 £'000
Difference between expected and actual return on scheme assets	(16,100)
Percentage of scheme assets	14.0%
Experience gains and losses on scheme liabilities	700
Percentage of scheme liabilities	0.5%
Total amount recognised in STRGL	(19,700)
Percentage of scheme liabilities	15.1%

c) The Balance Sheet position for all of the other Group Pension Schemes is materially the same in accordance with FRS 17 as for SSAP 24.

32 List of principal undertakings

The companies listed below are, in the opinion of the Directors, the principal undertakings of Serco Group plc. The percentage of equity capital directly or indirectly held by Serco Group plc is shown. The voting rights are the same as the percentage holding. The companies are incorporated and principally operate in the countries stated below.

Principal subsidiaries

United Kingdom	Serco Limited	100%
	Serco-Denholm Limited	90%
	Serco Europe Limited	100%
	Serco-IAL Limited	100%
	Serco Railtest Limited	100%
	Serco Systems Limited	100%
	NPL Management Limited	100%
	Serco Docklands Limited	100%
	Rakmulti Technology Limited	100%
	Serco QAA Limited	100%
	Traffic Information Services (TIS) Limited	100%
Rest of Europe		
Belgium	Serco Belgium S.A.	100%
Denmark	Metro Service A/S	67%
France	Serco France Sarl	100%
Germany	Serco International GmbH	100%
	Serco Services GmbH	100%
Ireland	Serco Services Ireland Limited	100%
	CCM Software Services Ltd	100%
Italy	Serco s.r.l	100%
Guernsey	Serco Insurance Company Limited	100%
Luxembourg	Serco Facilities Management S.A.	100%
The Netherlands	Serco Facilities Management BV	100%
Spain	Serco Gestion de Negocias SL	100%
Sweden	Serco Sverige AB	100%
Switzerland	Serco Facilities Management S.A.	100%
Asia Pacific		
Australia	Serco Group Pty Limited	100%
	Serco Australia Pty Limited	100%
	Great Southern Railway Limited	100%
New Zealand	Serco Group NZ Limited	100%
Hong Kong	Serco Group (Hong Kong) Limited	100%
Other		
Canada	Serco Facilities Management, Inc.	100%
USA	Serco Group, Inc.	100%
	Serco, Inc.	100%
	Serco Management Services, Inc. (Delaware)	100%
	Barton ATC, Inc.	100%
	Serco Management Services, Inc. (Tennessee)	100%
	JL Associates, Inc.	100%

32 List of principal undertakings (continued)**Joint venture undertakings**

United Kingdom		
	Premier Custodial Group Limited	50%
	Kilmarnock Prison Services Limited	50%
	Lowdham Grange Prison Services Limited	50%
	Medomsley Holdings Limited	50%
	Pucklechurch Custodial Services Limited	50%
	Moreton Prison Services Limited	50%
	Serco Gulf Engineering Limited	50%
	Defence Management Watchfield Limited	50%
	Laser (Teddington) II Limited	50%
	Altram (Manchester) Limited	26%
	Serco-Denholm Shipping Company Limited	50%
	AWE Management Limited	33%
Asia Pacific		
Australia		
	Defence Maritime Services Pty Limited	50%
	Serco Sodexho Defence Services Pty Limited	50%
New Zealand		
	Serco Sodexho Defence Services Limited	50%
Other		
USA		
	Serco – SKE	50%
Bahrain		
	Aeradio Technical Services WLL	49%
Bermuda		
	BAS-Serco Limited	40%
Cyprus		
	Serco Kalisperas	50%
Dubai		
	International Aeradio (Emirates) LLC	49%
Saudi Arabia		
	Key Communications Development Co Limited	49%
Singapore		
	Serco Guthrie Pte Ltd	50%
Turkey		
	Elektronik Sistemier Destek Sanavi ve Ticaret AS	51%

Full details of related undertakings will be attached to the Company's Annual Return to be filed with the Registrar of Companies.