

# Financial statements

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### Group accounting policies

Accounting policies are included within the relevant note to the Group accounts.



## Group accounts

### Preparation

#### Basis of preparation

The consolidated financial statements of BAE Systems plc have been prepared on a going concern basis, as discussed in the Corporate governance report on page 64, and in accordance with EU-endorsed International Financial Reporting Standards (IFRS) and the Companies Act 2006 applicable to companies reporting under IFRS.

The consolidated financial statements are presented in pounds sterling and, unless stated otherwise, rounded to the nearest million. They have been prepared under the historical cost convention, as modified by the revaluation of available-for-sale financial assets, and other relevant financial assets and financial liabilities (including derivative instruments).

Transactions in foreign currencies are translated at the exchange rates ruling at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are retranslated at the exchange rates ruling at the balance sheet date. These exchange differences are recognised in the income statement.

#### Significant accounting policies

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

Certain of the Group'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 consolidated financial statements. The critical accounting policies are listed below and explained in more detail in the relevant notes to the Group accounts:

Critical accounting policy	Description	Notes
<b>Revenue and profit recognition</b>		1
– The recognition of revenue and profit on long-term contracts.	<p>The majority of long-term contracts are accounted for under IAS 11, Construction Contracts. Revenue on long-term contracts is recognised when performance milestones have been completed.</p> <p>The ultimate profitability of long-term contracts is estimated based on estimates of revenue and costs, including allowances for technical and other risks, which are reliant on the knowledge and experience of the Group's project managers, engineers, and finance and commercial professionals. Material changes in these estimates could affect the profitability of individual contracts.</p> <p>Revenue and cost estimates are reviewed and updated at least quarterly, and more frequently as determined by events or circumstances.</p> <p>Profit is recognised progressively as risks have been mitigated or retired.</p>	
<b>Carrying value of intangible assets</b>		8
– The valuation of acquired intangible assets; and	<p>Acquired intangible assets, excluding goodwill, are valued in line with internationally used models, which require the use of estimates that may differ from actual outcomes. These assets are amortised over their estimated useful lives. Future results are impacted by the amortisation periods adopted and, potentially, any differences between estimated and actual circumstances related to individual intangible assets.</p>	
– the determination of assumptions underpinning goodwill impairment testing.	<p>Goodwill is not amortised, but is tested annually for impairment and carried at cost less accumulated impairment losses. For the purposes of impairment testing, goodwill is allocated to Cash-Generating Units on a consistent basis. The impairment review calculations require the use of estimates related to the future profitability and cash-generating ability of the acquired businesses and the pre-tax discount rate used in discounting these projected cash flows.</p>	
<b>Valuation of retirement benefit obligations</b>		20
– The determination of assumptions underpinning the valuation of retirement benefit obligations for defined benefit pension schemes; and	<p>Pension scheme accounting valuations are prepared by independent actuaries. For each of the actuarial assumptions used to measure the Group's pension scheme liabilities, there is a range of possible values and management exercises judgement in deciding the point within that range that most appropriately reflects the Group's circumstances. Small changes in these assumptions can have a significant impact on the size of the deficit.</p>	
– the determination of the share of the pension deficit allocated to the Group's equity accounted investments and other participating employers.	<p>With the exception of the allocation of the BAE Systems Pension Scheme (Main Scheme) deficit to Airbus, the deficit allocation method for other employers of the Main Scheme and for all other schemes is based on the relative payroll contributions of active members, which is consistent with prior years and is intended to reflect a reasonable approximation of the share of the deficit.</p> <p>In December 2015, BAE Systems, Airbus and the scheme trustees agreed to work towards the creation of a separate Airbus section of the Main Scheme in 2016 with the allocation of the deficit to the BAE Systems and Airbus sections based on each member's last employer. This allocation methodology is considered to represent a better estimate of the deficit allocation and has been reflected in the allocation of the IAS 19 pension deficit in the Main Scheme at 31 December 2015.</p>	

**Preparation** continued**Tax provisions**

In addition to the critical accounting policies, the directors exercise judgement to determine the amount of tax provisions. Provision is made for known issues based on interpretation of country-specific legislation and the likely outcome of negotiations or litigation. Included within the Consolidated balance sheet as at 31 December 2015 are current tax liabilities of £315m, which comprise a provision of £353m and other tax creditors of £35m, offset by a debtor of £73m in respect of research and development expenditure credits. The provision of £353m is in respect of known tax issues, of which £287m relates to non-UK jurisdictions. The resolution of tax positions taken by the Group can take a considerable period of time to conclude and, in some cases, it is difficult to predict the outcome. The directors believe that adequate provision is made for each known tax risk.

**Changes in accounting policies**

IFRS 9, Financial Instruments, issued in July 2014 with an effective date of 1 January 2018, is not yet EU endorsed. It is not expected to have a material impact on the Group.

IFRS 15, Revenue from Contracts with Customers, issued in May 2014 with an effective date of 1 January 2018, is not yet EU endorsed. Management is in the process of reviewing the impact that this will have on the Group.

IFRS 16, Leases, issued in January 2016 with an effective date of 1 January 2019, is not yet EU endorsed.

**Consolidation**

The financial statements of the Group consolidate the results of the Company and its subsidiary entities, and include its share of its joint ventures' results accounted for under the equity method.

A subsidiary is an entity controlled by the Group. The Group controls a subsidiary when it is exposed, or has the rights, to variable returns from its involvement with the subsidiary and has the ability to affect those returns through its power over the subsidiary.

The results of subsidiaries are included in the income statement from the date of acquisition.

Intra-group balances and transactions, and any unrealised income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements.

Joint ventures are accounted for under the equity method where the Consolidated income statement includes the Group's share of their profits and losses, and the Consolidated balance sheet includes its share of their net assets within equity accounted investments.

The assets and liabilities of overseas subsidiaries and equity accounted investments are translated at the exchange rates ruling at the balance sheet date. The income statements of such entities are translated at average rates of exchange during the year. All resulting exchange differences are recognised directly in a separate component of equity.

Translation differences that arose before the transition date to IFRS (1 January 2004) are presented in equity, but not as a separate component. When a foreign operation is sold, the cumulative exchange differences recognised in equity since 1 January 2004 are recognised in the income statement as part of the profit or loss on sale.

## Consolidated income statement for the year ended 31 December

	Notes	2015		2014	
		£m	Total £m	£m	Total £m
<b>Continuing operations</b>					
<b>Combined sales of Group and share of equity accounted investments</b>	1		<b>17,904</b>		16,637
Less: share of sales of equity accounted investments	1		<b>(1,117)</b>		(1,207)
<b>Revenue</b>	1		<b>16,787</b>		15,430
Operating costs	2		<b>(15,622)</b>		(14,387)
Other income	4		<b>227</b>		174
<b>Group operating profit</b>			<b>1,392</b>		1,217
Share of results of equity accounted investments	1		<b>110</b>		83
<i>Underlying EBITA<sup>1</sup></i>	1	<b>1,683</b>		1,702	
<i>Non-recurring items</i>	1	<b>26</b>		–	
<i>EBITA</i>		<b>1,709</b>		1,702	
<i>Amortisation of intangible assets</i>	1	<b>(108)</b>		(184)	
<i>Impairment of intangible assets</i>	1	<b>(78)</b>		(170)	
<i>Financial income/(expense) of equity accounted investments</i>	5	<b>3</b>		(30)	
<i>Taxation expense of equity accounted investments</i>		<b>(24)</b>		(18)	
<b>Operating profit</b>	1		<b>1,502</b>		1,300
<i>Financial income</i>		<b>241</b>		241	
<i>Financial expense</i>		<b>(653)</b>		(659)	
<b>Finance costs</b>	5		<b>(412)</b>		(418)
<b>Profit before taxation</b>			<b>1,090</b>		882
Taxation expense	6		<b>(147)</b>		(130)
<b>Profit for the year</b>			<b>943</b>		752
<b>Attributable to:</b>					
Equity shareholders			<b>918</b>		740
Non-controlling interests			<b>25</b>		12
			<b>943</b>		752
<b>Earnings per share</b>					
	7				
Basic earnings per share			<b>29.0p</b>		23.4p
Diluted earnings per share			<b>28.9p</b>		23.3p

1. Earnings before amortisation and impairment of intangible assets, finance costs and taxation expense (EBITA) excluding non-recurring items.

## Consolidated statement of comprehensive income for the year ended 31 December

	Notes	2015			2014		
		Other reserves <sup>1</sup> £m	Retained earnings £m	Total £m	Other reserves <sup>1</sup> £m	Retained earnings £m	Total £m
<b>Profit for the year</b>		–	<b>943</b>	<b>943</b>	–	752	752
<b>Other comprehensive income</b>							
<b>Items that will not be reclassified to the income statement:</b>							
Remeasurements on retirement benefit schemes:							
Subsidiaries		–	<b>864</b>	<b>864</b>	–	(2,023)	(2,023)
Equity accounted investments		–	<b>21</b>	<b>21</b>	–	(73)	(73)
Tax on items that will not be reclassified to the income statement	6	–	<b>(261)</b>	<b>(261)</b>	–	503	503
<b>Items that may be reclassified to the income statement:</b>							
Currency translation on foreign currency net investments:							
Subsidiaries		<b>260</b>	–	<b>260</b>	277 <sup>2</sup>	–	277 <sup>2</sup>
Equity accounted investments		<b>(45)</b>	–	<b>(45)</b>	(13) <sup>2</sup>	–	(13) <sup>2</sup>
Reclassification of cumulative currency translation reserve on disposal	25	<b>20</b>	–	<b>20</b>	–	–	–
Fair value (loss)/gain on available-for-sale financial assets		–	<b>(1)</b>	<b>(1)</b>	–	4	4
Amounts credited/(charged) to hedging reserve:	13						
Subsidiaries		<b>11</b>	–	<b>11</b>	(92)	–	(92)
Equity accounted investments		<b>(36)</b>	–	<b>(36)</b>	–	–	–
Tax on items that may be reclassified to the income statement	6	<b>5</b>	–	<b>5</b>	19	–	19
<b>Total other comprehensive income for the year (net of tax)</b>		<b>215</b>	<b>623</b>	<b>838</b>	191	(1,589)	(1,398)
<b>Total comprehensive income for the year</b>		<b>215</b>	<b>1,566</b>	<b>1,781</b>	191	(837)	(646)
<b>Attributable to:</b>							
Equity shareholders		<b>216</b>	<b>1,541</b>	<b>1,757</b>	191	(849)	(658)
Non-controlling interests		<b>(1)</b>	<b>25</b>	<b>24</b>	–	12	12
		<b>215</b>	<b>1,566</b>	<b>1,781</b>	191	(837)	(646)

1. An analysis of other reserves is provided in note 22.  
2. Restated.

## Consolidated statement of changes in equity for the year ended 31 December

	Attributable to equity holders of the parent						Non-controlling interests £m	Total equity £m
	Issued share capital £m	Share premium £m	Other reserves <sup>1</sup> £m	Retained earnings £m	Total £m			
At 1 January 2015	87	1,249	5,061	(4,555)	1,842	35	1,877	
Profit for the year	–	–	–	918	918	25	943	
Total other comprehensive income for the year	–	–	216	623	839	(1)	838	
Share-based payments	–	–	–	44	44	–	44	
Net sale of own shares	–	–	–	1	1	–	1	
Ordinary share dividends	–	–	–	(655)	(655)	(40)	(695)	
Disposal of non-controlling interest	–	–	–	–	–	(6)	(6)	
<b>At 31 December 2015</b>	<b>87</b>	<b>1,249</b>	<b>5,277</b>	<b>(3,624)</b>	<b>2,989</b>	<b>13</b>	<b>3,002</b>	
At 1 January 2014	89	1,249	4,868	(2,825)	3,381	37	3,418	
Profit for the year	–	–	–	740	740	12	752	
Total other comprehensive income for the year	–	–	191	(1,589)	(1,398)	–	(1,398)	
Share-based payments	–	–	–	42	42	–	42	
Net purchase of own shares	(2)	–	2	(281)	(281)	–	(281)	
Ordinary share dividends	–	–	–	(642)	(642)	(14)	(656)	
At 31 December 2014	87	1,249	5,061	(4,555)	1,842	35	1,877	

1. An analysis of other reserves is provided in note 22.

## Consolidated balance sheet as at 31 December

	Notes	2015 £m	2014 £m
<b>Non-current assets</b>			
Intangible assets	8	10,117	9,983
Property, plant and equipment	9	1,698	1,589
Investment property	10	120	129
Equity accounted investments	11	250	229
Other investments		6	7
Other receivables	12	275	347
Retirement benefit surpluses	20	193	162
Other financial assets	13	107	38
Deferred tax assets	14	985	1,327
		<b>13,751</b>	<b>13,811</b>
<b>Current assets</b>			
Inventories	15	726	690
Trade and other receivables including amounts due from customers for contract work	12	2,940	2,850
Current tax		4	7
Other financial assets	13	105	46
Cash and cash equivalents	16	2,537	2,308
Assets held for sale		20	76
		<b>6,332</b>	<b>5,977</b>
<b>Total assets</b>	17	<b>20,083</b>	<b>19,788</b>
<b>Non-current liabilities</b>			
Loans	18	(3,775)	(2,868)
Other payables	19	(1,020)	(932)
Retirement benefit obligations	20	(4,694)	(5,530)
Other financial liabilities	13	(72)	(79)
Deferred tax liabilities	14	(13)	(21)
Provisions	21	(354)	(436)
		<b>(9,928)</b>	<b>(9,866)</b>
<b>Current liabilities</b>			
Loans and overdrafts	18	(237)	(482)
Trade and other payables	19	(6,162)	(6,670)
Other financial liabilities	13	(130)	(107)
Current tax		(315)	(448)
Provisions	21	(301)	(315)
Liabilities held for sale		(8)	(23)
		<b>(7,153)</b>	<b>(8,045)</b>
<b>Total liabilities</b>		<b>(17,081)</b>	<b>(17,911)</b>
<b>Net assets</b>		<b>3,002</b>	<b>1,877</b>
<b>Capital and reserves</b>			
Issued share capital	22	87	87
Share premium		1,249	1,249
Other reserves	22	5,277	5,061
Retained earnings – deficit		(3,624)	(4,555)
<b>Total equity attributable to equity holders of the parent</b>		<b>2,989</b>	<b>1,842</b>
<b>Non-controlling interests</b>		<b>13</b>	<b>35</b>
<b>Total equity</b>		<b>3,002</b>	<b>1,877</b>

Approved by the Board on 17 February 2016 and signed on its behalf by:

**I G King**  
Chief Executive

**P J Lynas**  
Group Finance Director

# Consolidated cash flow statement

## for the year ended 31 December

	Notes	2015 £m	2014 £m
<b>Profit for the year</b>		<b>943</b>	752
Taxation expense	6	147	130
Research and development expenditure credits		(65)	–
Share of results of equity accounted investments	1	(110)	(83)
Finance costs	5	412	418
Depreciation, amortisation and impairment	2	460	657
Profit on disposal of property, plant and equipment	2,4	(28)	(20)
Profit on disposal of investment property	2,4	(41)	(12)
Profit on disposal of non-current other investments		(1)	–
Loss on disposal of businesses	2	24	–
Fair value gain	4	–	(47)
Cost of equity-settled employee share schemes		44	42
Movements in provisions		(139)	(153)
Decrease in liabilities for retirement benefit obligations		(234)	(345)
(Increase)/decrease in working capital:			
Inventories		(6)	(1)
Trade and other receivables		60	197
Trade and other payables		(542)	(622)
<b>Cash inflow from operating activities</b>		<b>924</b>	913
Interest paid		(180)	(152)
Taxation paid		(116)	(92)
<b>Net cash inflow from operating activities</b>		<b>628</b>	669
Dividends received from equity accounted investments	11	41	63
Interest received		7	7
Purchase of property, plant and equipment, and investment property		(359)	(263)
Purchase of intangible assets		(54)	(59)
Proceeds from sale of property, plant and equipment, and investment property		136	539
Proceeds from sale of non-current other investments		1	–
Purchase of subsidiary undertakings	23	(5)	(233)
Cash and cash equivalents acquired from purchase of subsidiary undertakings	23	–	3
Equity accounted investment funding	11	(8)	(2)
Proceeds from sale of subsidiary undertakings	23	34	–
Cash and cash equivalents disposed of with subsidiary undertakings	23	(13)	–
<b>Net cash (outflow)/inflow from investing activities</b>		<b>(220)</b>	55
Net sale/(purchase) of own shares		1	(281)
Equity dividends paid	22	(655)	(642)
Dividends paid to non-controlling interests		(40)	(14)
Cash inflow from matured derivative financial instruments		12	8
Cash inflow from movement in cash collateral		3	10
Cash inflow from loans		1,625	679
Cash outflow from repayment of loans		(1,135)	(398)
<b>Net cash outflow from financing activities</b>		<b>(189)</b>	(638)
<b>Net increase in cash and cash equivalents</b>		<b>219</b>	86
Cash and cash equivalents at 1 January		2,313	2,222
Effect of foreign exchange rate changes on cash and cash equivalents		5	5
<b>Cash and cash equivalents at 31 December</b>		<b>2,537</b>	2,313
Comprising:			
Cash and cash equivalents	16	2,537	2,308
Cash and cash equivalents (included within assets held for sale)		–	6
Overdrafts	18	–	(1)
<b>Cash and cash equivalents at 31 December</b>		<b>2,537</b>	2,313

# Notes to the Group accounts

## 1. Segmental analysis

### Revenue and profit recognition

Sales include the Group's share of sales of equity accounted investments. Revenue represents sales made by the Company and its subsidiary undertakings, excluding the Group's share of sales of equity accounted investments.

### Long-term contracts

The majority of the Group's long-term contract arrangements are accounted for under IAS 11, Construction Contracts. Sales are recognised when the Group has obtained the right to consideration in exchange for its performance. This is usually when title passes or a separately identifiable phase (milestone) of a contract or development has been completed.

No profit is recognised on contracts until the outcome of the contract can be reliably estimated. Profit is calculated by reference to reliable estimates of contract revenue and forecast costs after making suitable allowances for technical and other risks related to performance milestones yet to be achieved. Profit is recognised progressively as risks have been mitigated or retired.

When it is probable that total contract costs will exceed total contract revenue, the expected loss is recognised immediately as an expense.

### Goods sold and services rendered

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

Revenue from the sale of goods not under a long-term contract is recognised in the income statement when the significant risks and rewards of ownership have been transferred to the buyer, recovery of the consideration is probable, there is no continuing management involvement with the goods, and the amount of revenue and costs can be measured reliably. Profit is recognised at the time of sale.

Revenue from the provision of services not under a long-term contract is recognised in the income statement in proportion to the stage of completion of the contract at the reporting date. The stage of completion is measured on the basis of direct expenses incurred as a percentage of total expenses to be incurred for material contracts and labour hours delivered as a percentage of total labour hours to be delivered for time contracts.

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

### Research and development

The Group undertakes research and development activities either on its own behalf or on behalf of customers.

Where the research and development activity is performed on behalf of customers, the revenue arising is recognised in the income statement in accordance with the Group's revenue recognition policy.

### Key Performance Indicator – Underlying EBITA

Management uses an underlying profit measure to monitor the year-on-year profitability of the Group, which is defined as earnings before amortisation and impairment of intangible assets, finance costs and taxation expense (EBITA) excluding non-recurring items (defined as items that are relevant to an understanding of the Group's performance with reference to their materiality and nature). This definition is referred to as underlying EBITA. Underlying EBITA is the measure of profit on which segmental performance is monitored by management. As such, underlying EBITA is disclosed on page 115 on a segmental basis and reconciled to the reporting segment result and operating profit in the consolidated financial statements.

### Non-recurring items

In 2015, the Group completed the sale of its 75% holding in BAE Systems Land Systems South Africa (Pty) Limited, resulting in a loss on disposal of businesses of £24m.

In 2013, UK legislation changed so that UK government credits for research and development spend are now accounted for as part of operating profit rather than as part of taxation expense. This treatment was optional for the first three years. During 2015, the Group exercised that option, effective from 2013, and has reflected this change in the 2015 accounts. The credits relating to 2013 and 2014, totalling £50m, are included in non-recurring items in 2015.

In 2014, there were two equal and opposite non-recurring items, a fair value gain (see note 4) and an impairment loss (see note 9).



# Notes to the Group accounts

## continued

### 1. Segmental analysis continued

#### Sales and revenue by customer location

	Sales		Revenue	
	2015 £m	2014 £m	2015 £m	2014 £m
UK	4,006	3,703	3,812	3,518
Rest of Europe <sup>1</sup>	2,506	2,215	1,971	1,514
US	6,380	5,979	6,377	5,978
Canada	74	51	74	51
Saudi Arabia	3,839	3,320	3,653	3,153
Rest of Middle East	102	154	63	124
Australia	559	682	558	680
Rest of Asia and Pacific	347	420	234	326
Africa, and Central and South America	91	113	45	86
	<b>17,904</b>	<b>16,637</b>	<b>16,787</b>	<b>15,430</b>

#### Revenue by category

	2015 £m	2014 £m
Long-term contracts	9,420	8,687
Sale of goods	3,647	3,211
Provision of services	3,715	3,518
Royalty income	5	14
	<b>16,787</b>	<b>15,430</b>

#### Revenue by major customer

Revenue from the Group's three principal customers, which individually represent over 10% of total revenue, is as follows:

	2015 £m	2014 £m
UK Ministry of Defence <sup>1</sup>	4,838	4,230
US Department of Defense	3,838	3,655
Kingdom of Saudi Arabia Ministry of Defence and Aviation	3,582	3,124

1. Includes £1.4bn (2014 £1.1bn) generated under the Typhoon work share agreement with Eurofighter Jagdflugzeug GmbH.

Revenue from the UK Ministry of Defence and the US Department of Defense was generated by the five principal reporting segments. Revenue from the Kingdom of Saudi Arabia Ministry of Defence and Aviation was generated by the Platforms & Services (UK) and Platforms & Services (International) reporting segments.

## 1. Segmental analysis continued

### Reporting segment result

	Underlying EBITA <sup>1</sup>		Non-recurring items <sup>2</sup>		Amortisation of intangible assets <sup>3</sup>		Impairment of intangible assets <sup>4</sup>		Reporting segment result	
	2015 £m	2014 <sup>5</sup> £m	2015 £m	2014 £m	2015 £m	2014 <sup>5</sup> £m	2015 £m	2014 <sup>5</sup> £m	2015 £m	2014 <sup>5</sup> £m
Electronic Systems	396	373	–	–	(18)	(14)	–	(1)	378	358
Cyber & Intelligence	145	153	–	–	(57)	(61)	(78)	(4)	10	88
Platforms & Services (US)	177	117	(24)	–	(13)	(15)	–	(165)	140	(63)
Platforms & Services (UK)	721	772	50	–	(11)	(84)	–	–	760	688
Platforms & Services (International)	335	366	–	–	(9)	(10)	–	–	326	356
HQ <sup>6</sup>	(91)	(79)	–	–	–	–	–	–	(91)	(79)
	<b>1,683</b>	<b>1,702</b>	<b>26</b>	<b>–</b>	<b>(108)</b>	<b>(184)</b>	<b>(78)</b>	<b>(170)</b>	<b>1,523</b>	<b>1,348</b>
Financial income/(expense) of equity accounted investments									3	(30)
Taxation expense of equity accounted investments									(24)	(18)
<b>Operating profit</b>									<b>1,502</b>	<b>1,300</b>
Finance costs									(412)	(418)
<b>Profit before taxation</b>									<b>1,090</b>	<b>882</b>
Taxation expense									(147)	(130)
<b>Profit for the year</b>									<b>943</b>	<b>752</b>

### Share of results of equity accounted investments within reporting segments

	2015 £m	2014 £m
Underlying EBITA <sup>1</sup> :		
Electronic Systems	7	2
Platforms & Services (US)	12	12
Platforms & Services (UK)	15	21
Platforms & Services (International)	96	70
HQ	5	31
	<b>135</b>	<b>136</b>
Amortisation of intangible assets	(4)	(5)
Financial income/(expense)	3	(30)
Taxation expense	(24)	(18)
	<b>110</b>	<b>83</b>

1. Earnings before amortisation and impairment of intangible assets, finance costs and taxation expense (EBITA) excluding non-recurring items.

2. In 2015, Platforms & Services (US) comprises a loss on the sale of the Group's 75% holding in BAE Systems Land Systems South Africa (Pty) Limited and Platforms & Services (UK) includes research and development expenditure credits relating to 2013 and 2014 (see page 112).

3. The reduction in amortisation of intangible assets primarily reflects acquired intangible assets fully amortising in 2014 in the Group's Maritime business within Platforms & Services (UK).

4. See note 8.

5. Re-presented for the reallocation of the Integrated Electronics & Warfare Systems activities from Platforms & Services (US) to Cyber & Intelligence.

6. In 2014, HQ included a £30m benefit from re-assessment of a long-term liability.

# Notes to the Group accounts

## continued

### 2. Operating costs

<b>Leases</b>
Payments, including any incentives, made under operating leases are recognised in the income statement on a straight-line basis over the lease term. Lease incentives granted are charged to the income statement over the term of the lease.
<b>Research and development</b>
The Group undertakes research and development activities either on its own behalf or on behalf of customers.
Group-funded expenditure on both research and development activities not meeting the conditions for capitalisation is written off as incurred and charged to the income statement.
Customer-funded expenditure on research and development activities is held in long-term contract balances as a contract cost within trade and other receivables and recognised in the income statement in accordance with the Group's revenue recognition policy.

	2015 £m	2014 £m
Raw materials, subcontracts and other bought-in items	6,030	6,114
Change in inventories of finished goods and work-in-progress	1,027	8
Cost of inventories expensed	7,057	6,122
Staff costs (note 3)	5,052	4,827
Depreciation, amortisation and impairment	460	657
Loss on disposal of property, plant and equipment, and investment property	4	1
Loss on disposal of businesses	24	–
Other operating charges	3,025	2,780
<b>Operating costs</b>	<b>15,622</b>	<b>14,387</b>

Included within the analysis of operating costs are the following expenses:

Lease and sublease expense	257	242
Research and development expense including amounts funded under contract	1,263	1,343

#### Fees payable to the Company's auditor and its associates included in operating costs

	2015			2014		
	UK £'000	Overseas £'000	Total £'000	UK <sup>1</sup> £'000	Overseas <sup>1</sup> £'000	Total <sup>1</sup> £'000
<b>Fees payable to the Company's auditor for the audit of the Company's annual accounts*</b>	1,759	–	1,759	1,669	–	1,669
<b>Fees payable to the Company's auditor and its associates for other services pursuant to legislation:</b>						
The audit of the Company's subsidiaries*	2,612	3,659	6,271	2,687	3,425	6,112
Interim review*	490	–	490	485	–	485
Other	164	19	183	200	2	202
<b>Audit-related assurance services:</b>						
Advice on accounting matters	–	6	6	9	2	11
<b>Tax compliance services</b>	22	457	479	7	637	644
<b>Tax advisory services</b>	30	125	155	59	141	200
<b>Corporate finance services:</b>						
M&A	–	1,806	1,806	–	–	–
<b>Other assurance services:</b>						
Due diligence	–	–	–	–	134	134
IT advisory	–	–	–	123	–	123
<b>Other non-audit services:</b>						
Investor relations	220	–	220	200	3	203
Other	184	47	231	315	16	331
<b>Total fees payable to the Company's auditor and its associates</b>	<b>5,481</b>	<b>6,119</b>	<b>11,600</b>	<b>5,754</b>	<b>4,360</b>	<b>10,114</b>
*Total fees payable to the Company's auditor and its associates for audit services and interim review			<b>8,520</b>			<b>8,266</b>
<b>Fees in respect of BAE Systems pension schemes:</b>						
Audit	140	241	381	139	214	353
Tax compliance	–	4	4	44	–	44
Tax advisory	19	–	19	–	–	–
	<b>159</b>	<b>245</b>	<b>404</b>	<b>183</b>	<b>214</b>	<b>397</b>

1. Restated.

### 3. Employees

The weekly average and year-end numbers of employees, excluding those in equity accounted investments, were as follows:

	Weekly average		At year end	
	2015 Number '000	2014 <sup>1</sup> Number '000	2015 Number '000	2014 <sup>1</sup> Number '000
Electronic Systems	12	12	12	12
Cyber & Intelligence	13	13	13	13
Platforms & Services (US)	11	12	11	11
Platforms & Services (UK)	29	29	29	29
Platforms & Services (International)	10	10	9	10
HQ	1	1	1	1
	<b>76</b>	<b>77</b>	<b>75</b>	<b>76</b>

1. Re-presented for the reallocation of the Integrated Electronics & Warfare Systems activities from Platforms & Services (US) to Cyber & Intelligence.

The aggregate staff costs of Group employees, excluding employees of equity accounted investments, were as follows:

	2015 £m	2014 £m
Wages and salaries	4,367	4,184
Social security costs	333	334
Share-based payments (note 28)	16	14
Pension costs – defined contribution plans (note 20)	140	125
Pension costs – defined benefit plans (note 20)	194	169
US healthcare costs (note 20)	2	1
	<b>5,052</b>	<b>4,827</b>

### 4. Other income

#### Rental income

Rental income is recognised in other income on a straight-line basis over the term of the relevant lease.

	2015 £m	2014 £m
Research and development expenditure credits <sup>1</sup>	65	–
Rental income from operating leases – investment property	23	21
Rental income from operating leases – other	19	20
Profit on disposal of property, plant and equipment	28	21
Profit on disposal of investment property	45	12
Profit on disposal of non-current other investments	1	–
Fair value gain <sup>2</sup>	–	47
Management recharges to equity accounted investments (note 29)	17	17
Other <sup>3</sup>	29	36
<b>Other income</b>	<b>227</b>	<b>174</b>

1. In 2013, UK legislation changed so that UK government credits for research and development spend are now accounted for as part of operating profit rather than as part of taxation expense. This treatment was optional for the first three years. During 2015, the Group exercised that option, effective from 2013, and has reflected this change in the 2015 accounts. The credits relating to 2013 and 2014, totalling £50m, are included in non-recurring items in 2015.

2. Fair value gain on the Group's existing 40% shareholding in Saudi Development and Training Company upon acquisition of an additional 59% and control of the company in 2014.

3. There are no individual amounts in excess of £10m.

# Notes to the Group accounts

## continued

### 5. Finance costs

<b>Interest income and borrowing costs</b>		
Interest income and borrowing costs are recognised in the income statement in the period in which they are incurred.		
	2015 £m	2014 £m
Interest income	17	28
Gain on remeasurement of financial instruments at fair value through profit or loss	167	99
Foreign exchange gains	57	114
<b>Financial income</b>	<b>241</b>	<b>241</b>
Interest expense on bonds and other financial instruments	(175)	(177)
Facility fees	(4)	(4)
Net present value adjustments	(29)	(48)
Net interest expense on retirement benefit obligations (note 20)	(192)	(147)
Loss on remeasurement of financial instruments at fair value through profit or loss	(72)	(75)
Foreign exchange losses	(181)	(208)
<b>Financial expense</b>	<b>(653)</b>	<b>(659)</b>
<b>Finance costs</b>	<b>(412)</b>	<b>(418)</b>
<b>Additional analysis</b>		
	2015 £m	2014 £m
Finance costs:		
Group	(412)	(418)
Share of equity accounted investments	3	(30)
	<b>(409)</b>	<b>(448)</b>
Analysed as:		
Underlying interest expense:		
Group	(191)	(201)
Share of equity accounted investments	(3)	(3)
	<b>(194)</b>	<b>(204)</b>
Other:		
Group:		
Net interest expense on retirement benefit obligations	(192)	(147)
Fair value and foreign exchange adjustments on financial instruments and investments	(29)	(70)
Share of equity accounted investments:		
Net interest expense on retirement benefit obligations	(8)	(8)
Fair value and foreign exchange adjustments on financial instruments and investments	14	(19)
	<b>(409)</b>	<b>(448)</b>

## 6. Taxation expense

Income 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 or substantively 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.

Taxation expense	2015 £m	2014 £m
<b>Current taxation</b>		
UK:		
Current tax	(109)	(90)
Double tax relief	–	1
Adjustments in respect of prior years <sup>1</sup>	17	24
	(92)	(65)
Overseas:		
Current year	(105)	(56)
Adjustments in respect of prior years <sup>2</sup>	99	20
	(6)	(36)
	(98)	(101)
<b>Deferred taxation</b>		
UK:		
Origination and reversal of temporary differences	8	21
Adjustments in respect of prior years	8	8
Tax rate adjustment <sup>3</sup>	(5)	–
	11	29
Overseas:		
Origination and reversal of temporary differences	(51)	(67)
Adjustments in respect of prior years	(9)	9
	(60)	(58)
	(49)	(29)
<b>Taxation expense</b>	<b>(147)</b>	<b>(130)</b>
UK	(81)	(36)
Overseas	(66)	(94)
<b>Taxation expense</b>	<b>(147)</b>	<b>(130)</b>

1. 2015 includes a £52m credit in respect of the adjustment of certain UK tax provisions in the light of clarification received.

2. 2015 includes an £82m credit in respect of the adjustment of certain overseas tax provisions in the light of rulings received. 2014 included a £51m credit in respect of the re-assessment of existing tax provisions where information received in the year enabled the estimate to be updated.

3. The UK current tax rate was reduced from 21% to 20% with effect from 1 April 2015, and will be reduced to 19% with effect from 1 April 2017 and to 18% with effect from 1 April 2020. In line with this change, the rate applying to UK deferred tax assets and liabilities has been reduced from 20% to 18%, creating a rate adjustment in 2015, which is partly reflected in the Consolidated income statement and partly in the Consolidated statement of comprehensive income.

# Notes to the Group accounts

## continued

### 6. Taxation expense continued

#### Reconciliation of taxation expense

The following table reconciles the theoretical income tax expense, using the UK corporation tax rate, to the reported tax expense. The reconciling items represent, besides the impact of tax rate differentials and changes, non-taxable benefits or non-deductible expenses arising from differences between the local tax base and the reported financial statements.

	2015 £m	2014 £m
<b>Profit before taxation</b>	<b>1,090</b>	882
UK corporation tax rate	20.25%	21.5%
Expected income tax expense	(221)	(190)
Effect of tax rates in foreign jurisdictions, including US state taxes	(69)	(46) <sup>1</sup>
Effect of intra-group financing	13	13 <sup>1</sup>
Expenses not tax effected	(13)	(12)
Income not subject to tax	41	32 <sup>1</sup>
Research and development tax credits and patent box benefits	7	29
Non-deductible goodwill impairment	(15)	(35)
Chargeable gains and non-taxable gains/non-deductible losses on disposal of businesses	(7)	–
Utilisation of previously unrecognised tax losses	4	3
Adjustments in respect of prior years <sup>2</sup>	115	61
Adjustments in respect of equity accounted investments	22	18
Tax rate adjustment	(5)	–
Other	(19)	(3)
<b>Taxation expense</b>	<b>(147)</b>	(130)

#### Calculation of the underlying effective tax rate

	2015 £m	2014 £m
Profit before taxation	1,090	882
Add back:		
Taxation expense of equity accounted investments (note 1)	24	18
Loss on disposal of businesses (note 1)	24	–
Goodwill impairment (note 8)	75	161
<b>Adjusted profit before taxation</b>	<b>1,213</b>	1,061
Taxation expense	(147)	(130)
Taxation expense of equity accounted investments (note 1)	(24)	(18)
Exclude: Re-assessment of existing tax provisions <sup>2</sup>	–	(51)
<b>Adjusted taxation expense (including equity accounted investments)</b>	<b>(171)</b>	(199)
<b>Underlying effective tax rate</b>	<b>14%</b>	19%
Adjusted profit before taxation (above)	1,213	1,061
Exclude: Research and development expenditure credits <sup>3</sup>	(77)	–
	<b>1,136</b>	1,061
Adjusted taxation expense (including equity accounted investments) (above)	(171)	(199)
Exclude: Adjustments relating to research and development expenditure credits <sup>3</sup>	68	–
Exclude: Adjustment of tax provisions <sup>2</sup>	(134)	–
	<b>(237)</b>	(199)
<b>Underlying effective tax rate, excluding research and development expenditure credits<sup>3</sup> and adjustment of tax provisions<sup>2</sup></b>	<b>21%</b>	19%

1. Re-presented.

2. 2015 includes credits totalling £134m in respect of the adjustment of certain UK and overseas tax provisions in the light of clarification and rulings received. 2014 included a £51m credit in respect of the re-assessment of existing tax provisions where information received in the year enabled the estimate to be updated, which was excluded from the calculation of the underlying effective tax rate.

3. In 2013, UK legislation changed so that UK government credits for research and development spend are now accounted for as part of operating profit rather than as part of taxation expense. This treatment was optional for the first three years. During 2015, the Group exercised that option, effective from 2013, and has reflected this change in the 2015 accounts. The adjustment reverses this treatment to show an underlying effective tax rate that is comparable with the prior year. The £77m excluded from profit before taxation comprises £50m included in non-recurring items relating to 2013 and 2014 (see note 1) and £27m included in underlying EBITA relating to 2015, of which £12m relates to the Group's share of equity accounted investments. The £68m includes £45m relating to the £50m included in non-recurring items.

**6. Taxation expense** continued**Tax recognised in other comprehensive income**

	2015			2014		
	Before tax £m	Tax (expense)/ benefit £m	Net of tax £m	Before tax £m	Tax (expense)/ benefit £m	Net of tax £m
<b>Items that will not be reclassified to the income statement:</b>						
Remeasurements on retirement benefit schemes:						
Subsidiaries	864	(173)	691	(2,023)	482	(1,541)
Equity accounted investments	21	(3)	18	(73)	16	(57)
Share-based payments	–	(3)	(3)	–	4	4
Other	–	(8)	(8)	–	1	1
Tax rate adjustment <sup>1</sup>	–	(74)	(74)	–	–	–
<b>Items that may be reclassified to the income statement:</b>						
Currency translation on foreign currency net investments:						
Subsidiaries	260	–	260	277 <sup>2</sup>	–	277 <sup>2</sup>
Equity accounted investments	(45)	–	(45)	(13) <sup>2</sup>	–	(13) <sup>2</sup>
Reclassification of cumulative currency translation reserve on disposal	20	–	20	–	–	–
Fair value (loss)/gain on available-for-sale financial assets	(1)	–	(1)	4	–	4
Amounts credited/(charged) to hedging reserve:						
Subsidiaries	11	(2)	9	(92)	19	(73)
Equity accounted investments	(36)	7	(29)	–	–	–
	<b>1,094</b>	<b>(256)</b>	<b>838</b>	<b>(1,920)</b>	<b>522</b>	<b>(1,398)</b>

	2015			2014		
	Other reserves £m	Retained earnings £m	Total £m	Other reserves £m	Retained earnings £m	Total £m
<b>Current tax</b>						
Pensions	–	42	42	–	59	59
Other	–	(8)	(8)	–	1	1
	–	34	34	–	60	60
<b>Deferred tax</b>						
Subsidiaries	(2)	(218)	(220)	19	427	446
Tax rate adjustment <sup>1</sup>	–	(74)	(74)	–	–	–
Equity accounted investments	7	(3)	4	–	16	16
	5	(295)	(290)	19	443	462
<b>Tax on other comprehensive income</b>	<b>5</b>	<b>(261)</b>	<b>(256)</b>	<b>19</b>	<b>503</b>	<b>522</b>

- The UK current tax rate was reduced from 21% to 20% with effect from 1 April 2015, and will be reduced to 19% with effect from 1 April 2017 and to 18% with effect from 1 April 2020. In line with this change, the rate applying to UK deferred tax assets and liabilities has been reduced from 20% to 18%, creating a rate adjustment in 2015, which is partly reflected in the Consolidated income statement and partly in the Consolidated statement of comprehensive income.
- Restated.

# Notes to the Group accounts

## continued

### 7. Earnings per share

#### Key Performance Indicator – Underlying earnings per share

Underlying earnings per share is presented in addition to that required by IAS 33, Earnings per Share, to align the adjusted earnings measure with the performance measure reviewed by the directors. The directors consider that this gives a more appropriate indication of underlying performance.

	2015			2014		
	£m	Basic pence per share	Diluted pence per share	£m	Basic pence per share	Diluted pence per share
Profit for the year attributable to equity shareholders	918	29.0	28.9	740	23.4	23.3
(Deduct)/add back:						
Re-assessment of existing tax provisions	–			(51)		
Non-recurring items, post tax	19			–		
Net interest expense on retirement benefit obligations, post tax <sup>1</sup>	158			126		
Fair value and foreign exchange adjustments on financial instruments and investments, post tax <sup>1</sup>	12			72		
Amortisation and impairment of intangible assets, post tax <sup>1</sup>	88			156		
Impairment of goodwill	75			161		
<b>Underlying earnings, post tax</b>	<b>1,270</b>	<b>40.2</b>	<b>40.1</b>	<b>1,204</b>	<b>38.0</b>	<b>37.9</b>
		Millions	Millions		Millions	Millions
Weighted average number of shares used in calculating basic earnings per share		3,161	3,161		3,165	3,165
Incremental shares in respect of employee share schemes			10			10
Weighted average number of shares used in calculating diluted earnings per share			3,171			3,175

1. The tax impact is calculated using the underlying effective tax rate, excluding research and development expenditure credits and adjustment of tax provisions, of 21% (2014 19%).

## 8. Intangible assets

Intangible assets are carried at cost or valuation, less accumulated amortisation and impairment losses.

### Cost or valuation

Intangible assets arising from a business combination are recognised at fair value, amortised over their estimated useful lives and subject to impairment testing. The Group's accounting policy on business combinations is included in note 25.

### Goodwill

Goodwill on acquisitions of subsidiaries is included in intangible assets. Goodwill on acquisitions of joint ventures and associates is included in the carrying value of equity accounted investments. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

### Programme and customer-related

The most significant intangible assets recognised by the Group are in relation to ongoing programmes within businesses acquired, mainly in respect of customer relationships and order backlog.

### Other intangible assets

Other intangible assets include:

- **Computer software licences acquired** for use within the Group are capitalised as an intangible asset on the basis of the costs incurred to acquire and bring to use the specific software;
- **Software development costs** that are directly associated with the production of identifiable and unique software products controlled by the Group, and that will probably generate economic benefits exceeding costs beyond one year, are recognised as intangible assets. Group-funded expenditure associated with enhancing or maintaining computer software programs for sale is recognised as an expense as incurred;
- **Research and development expenditure** funded by the Group on development activities applied to a plan or design for the production of new or substantially improved products is capitalised as an internally generated intangible asset if certain conditions are met. The expenditure capitalised includes the cost of materials, direct labour and related overheads; and
- **Patents, trademarks and licences.**

### Amortisation

Amortisation is charged to the income statement on a straight-line basis over the estimated useful lives of the intangible assets.

For programme-related intangibles, amortisation is set on a programme-by-programme basis over the life of the individual programme. Amortisation for customer-related intangibles is also set on an individual basis.

The estimated useful lives are as follows:

<b>Programme and customer-related</b>	up to 15 years
<b>Other intangible assets:</b>	
Computer software licences acquired	2 to 5 years
Software development costs	2 to 5 years
Research and development expenditure	up to 10 years
Patents, trademarks and licences	up to 20 years
Other intangibles	up to 10 years

The Group has no indefinite-life intangible assets other than goodwill.

### Impairment of intangible assets, property, plant and equipment, investment property and equity accounted investments

The carrying amounts of the Group's intangible assets, property, plant and equipment, investment property and equity accounted 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. For intangible assets that are not yet available for use, impairment testing is performed annually.

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 goodwill is not reversed.

An impairment loss in respect of other intangible assets, property, plant and equipment, investment property and equity accounted investments 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.

# Notes to the Group accounts

## continued

### 8. Intangible assets continued

	Goodwill £m	Programme and customer- related £m	Other £m	Total £m
<b>Cost or valuation</b>				
At 1 January 2014	13,180	1,729	504	15,413
Additions:				
Acquired separately	–	–	33	33
Internally developed	–	–	23	23
Business acquisitions	208	51	30	289
Disposals <sup>1</sup>	–	(1,061)	(77)	(1,138)
Transfer to held for sale	(19)	–	(3)	(22)
Transfer from property, plant and equipment	–	–	9	9
Transfer from inventories	–	–	4	4
Foreign exchange adjustments	339	20	10	369
At 31 December 2014	13,708	739	533	14,980
Additions:				
Acquired separately	–	–	42	42
Internally developed	–	–	12	12
Disposals <sup>1</sup>	–	(147)	(33)	(180)
Transfer from property, plant and equipment	–	–	5	5
Foreign exchange adjustments	333	12	8	353
<b>At 31 December 2015</b>	<b>14,041</b>	<b>604</b>	<b>567</b>	<b>15,212</b>
<b>Amortisation and impairment</b>				
At 1 January 2014	3,799	1,502	377	5,678
Amortisation charge	–	142	37	179
Impairment charge	161	8	1	170
Disposals <sup>1</sup>	–	(1,061)	(77)	(1,138)
Transfer to held for sale	–	–	(3)	(3)
Foreign exchange adjustments	84	18	9	111
At 31 December 2014	4,044	609	344	4,997
Amortisation charge	–	61	43	104
Impairment charge	75	3	–	78
Disposals <sup>1</sup>	–	(147)	(33)	(180)
Foreign exchange adjustments	82	8	6	96
<b>At 31 December 2015</b>	<b>4,201</b>	<b>534</b>	<b>360</b>	<b>5,095</b>
<b>Net book value</b>				
<b>At 31 December 2015</b>	<b>9,840</b>	<b>70</b>	<b>207</b>	<b>10,117</b>
At 31 December 2014	9,664	130	189	9,983
At 1 January 2014	9,381	227	127	9,735

1. Includes intangible assets with nil net book value no longer used by the Group.

#### Impairment testing

In order to calculate the recoverable amount of the Group's goodwill, all goodwill balances have been considered with regard to value-in-use calculations.

The value-in-use calculations use risk-adjusted future cash flow projections based on the Group's five-year Integrated Business Plan (IBP) and include a terminal value based on the projections for the final year of that plan, with growth rate assumptions applied. The IBP process includes the use of historic experience, available government spending data and the Group's order backlog. Pre-tax discount rates, derived from the Group's post-tax weighted average cost of capital of 7.47% (2014 7.12%) (adjusted for risks specific to the market in which the Cash-Generating Unit (CGU) operates), have been used in discounting these projected risk-adjusted cash flows.

The final year growth rate assumption in the value-in-use calculations is in the range 0% to 2%.

## 8. Intangible assets continued

### Significant CGUs

Goodwill allocated to CGUs, which are largely dependent on US government spending on defence, aerospace and security, represents £7.4bn (2014 £7.3bn) of the Group's total goodwill balance. The Group monitors changes in defence budgets on an ongoing basis.

Cash-Generating Unit	Key assumptions	Allocated goodwill		Pre-tax discount rate	
		2015 £bn	2014 <sup>1</sup> £bn	2015 %	2014 <sup>1</sup> %
Electronic Systems	Continued demand from the US government for electronic warfare systems (where the business has a leadership position), other technology-based solutions and growth in the commercial avionics market	3.2	3.2	10	9
Intelligence & Security (within Cyber & Intelligence)	Continued demand in the US for the Group's services in the areas of homeland security, law enforcement and counter-intelligence	1.1	1.1	10	9
Platforms & Services (US)	Continued demand in the Group's principal markets for existing and successor military tracked vehicles, naval guns, missile launchers, artillery systems, munitions, upgrade programmes and support, and in the US for complex infrastructure, maritime and aviation services	3.1	3.0	10	9

The headroom, calculated as the difference between net assets including allocated goodwill as at 31 December 2015 and the value-in-use calculations, for the CGUs listed above, is shown below. The table also shows the headroom assuming a 1% reduction in the terminal value growth rate assumption and a 1% increase in the discount rate used in the value-in-use calculations.

Cash-Generating Unit	Headroom as at 31 December		Headroom assuming a 1% reduction in the terminal value growth rate assumption		Headroom assuming a 1% increase in the discount rate	
	2015 £bn	2014 <sup>1</sup> £bn	2015 £bn	2014 <sup>1</sup> £bn	2015 £bn	2014 <sup>1</sup> £bn
Electronic Systems	1.7	1.6	1.0	0.8	0.8	0.6
Intelligence & Security	–	0.2	(0.1)	(0.1)	(0.1)	(0.1)
Platforms & Services (US)	0.4	0.5	(0.1)	(0.1)	(0.3)	(0.2)

1. Re-presented for the reallocation of the Integrated Electronics & Warfare Systems activities from Platforms & Services (US) to Cyber & Intelligence.

### Other CGUs

The remaining goodwill balance of £2.4bn (2014 £2.4bn) is allocated across multiple CGUs, including £0.6bn (2014 £0.5bn) in the Applied Intelligence CGU, with no individual CGU exceeding 10% of the Group's total goodwill balance. The majority of the projected cash flows within these CGUs are underpinned by expected levels of primarily UK government spending on defence, aerospace and security, and the Group's ability to capture a broadly consistent market share. In the case of Applied Intelligence, the future cash flow projections are based on the expectation of growth in cyber and intelligence, in the UK and overseas government markets, together with increasing demand for products and services in commercial markets.

### Impairment – goodwill

In 2015, the impairment charge of £75m in the Intelligence & Security CGU reflects lower growth assumptions.

In 2014, the impairment charge of £161m comprised the Platforms & Services (US) CGU, reflecting performance issues at the US commercial shipbuilding business (£87m) and the agreement to sell the Group's 75% holding in BAE Systems Land Systems South Africa (Pty) Limited at a price below its total carrying value (£74m).

### Impairment – intangible assets

In 2015, the impairment charge of £3m relates to the Cyber & Intelligence reporting segment.

In 2014, the impairment charge of £9m related to the Electronic Systems (£1m), Cyber & Intelligence (£4m) and Platforms & Services (US) (£4m) reporting segments.

## Notes to the Group accounts continued

### 9. 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. The cost of demonstration assets is written off as incurred.

Assets held for leasing out under operating leases are included in property, plant and equipment at cost less accumulated depreciation and impairment losses.

#### 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:

<b>Buildings</b>	up to 50 years, or the lease term if shorter
<b>Plant and machinery:</b>	
Computing equipment and motor vehicles	4 to 5 years
Other equipment	10 to 20 years, or the project life if shorter

For certain items of plant and equipment in the Group's US businesses, depreciation is normally provided on a basis consistent with cost reimbursement profiles under US government contracts. Typically, this provides for a faster rate of depreciation than would otherwise arise on a straight-line basis.

No depreciation is provided on freehold land and assets in the course of construction.

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 Group's property, plant and equipment are reviewed at each balance sheet date to determine whether there is any indication of impairment in accordance with the policy shown in note 8.

**9. Property, plant and equipment** continued

	Land and buildings £m	Plant and machinery £m	Total £m
<b>Cost</b>			
At 1 January 2014	2,103	2,735	4,838
Additions	55	208	263
Business acquisitions	–	7	7
Transfer from long-term contract balances	–	21	21
Transfer to other intangible assets	–	(9)	(9)
Transfer to held for sale	(11)	(24)	(35)
Disposals	(463)	(244)	(707)
Foreign exchange adjustments	38	59	97
At 31 December 2014	1,722	2,753	4,475
Additions <sup>1</sup>	108	284	392
Transfer to other intangible assets	–	(5)	(5)
Reclassification between categories	17	(17)	–
Disposals	(113)	(266)	(379)
Foreign exchange adjustments	36	57	93
<b>At 31 December 2015</b>	<b>1,770</b>	<b>2,806</b>	<b>4,576</b>
<b>Depreciation and impairment</b>			
At 1 January 2014	946	1,956	2,902
Depreciation charge for the year	91	157	248
Impairment charge for the year	48	8	56
Transfer from provisions	10	–	10
Transfer to held for sale	(6)	(20)	(26)
Disposals	(145)	(220)	(365)
Foreign exchange adjustments	19	42	61
At 31 December 2014	963	1,923	2,886
Depreciation charge for the year	80	163	243
Impairment charge for the year	21	8	29
Reclassification between categories	2	(2)	–
Disposals	(80)	(261)	(341)
Foreign exchange adjustments	19	42	61
<b>At 31 December 2015</b>	<b>1,005</b>	<b>1,873</b>	<b>2,878</b>
<b>Net book value</b>			
<b>At 31 December 2015</b>	<b>765</b>	<b>933</b>	<b>1,698</b>
At 31 December 2014	759	830	1,589
At 1 January 2014	1,157	779	1,936
<b>Net book value</b>			
	Land and buildings £m	Plant and machinery £m	Total £m
Freehold property	612	–	612
Long leasehold property	17	–	17
Short leasehold property	136	–	136
Plant and machinery	–	811	811
Fixtures, fittings and equipment	–	122	122
<b>At 31 December 2015</b>	<b>765</b>	<b>933</b>	<b>1,698</b>

1. Includes £44m of land and buildings, and £5m of plant and machinery at Barrow-in-Furness, UK, relating to the Successor submarine programme funded by the UK government.

## Notes to the Group accounts continued

### 9. Property, plant and equipment continued

#### Impairment

	2015 £m	2014 £m
Cyber & Intelligence	1	–
Platforms & Services (US)	2	1
Platforms & Services (UK)	1	4
Platforms & Services (International)	25	51
	<b>29</b>	<b>56</b>

#### 2015

The viability of the Williamstown shipyard in Australia remains uncertain with no near-term prospect of work beyond the Landing Helicopter Dock and Air Warfare Destroyer programmes. The impairment in Platforms & Services (International) includes a £24m charge against the carrying value of the Williamstown facility.

#### 2014

The impairment in Platforms & Services (International) included the £47m charge against the carrying value of Aircraft Accessories and Components Company upon classification of the business as held for sale.

#### Assets in the course of construction

	Land and buildings <sup>1</sup> £m	Plant and machinery £m	Total £m
<b>At 31 December 2015</b>	<b>98</b>	<b>194</b>	<b>292</b>
At 31 December 2014	36	154	190

1. Includes £42m (2014 £nil) at Barrow-in-Furness, UK, relating to the Successor submarine programme funded by the UK government.

#### Operating leases

The future aggregate minimum lease income from the non-cancellable elements of operating leases for assets capitalised (including investment property – see note 10) are as follows:

	2015 £m	2014 £m
Receipts due:		
Not later than one year	25	23
Later than one year and not later than five years	93	84
Later than five years	94	99
	<b>212</b>	<b>206</b>

Under the terms of the lease agreements, no contingent rents are receivable. The leases have varying terms including escalation clauses and renewal rights. None of these terms represent unusual arrangements or create material onerous or beneficial rights or obligations.

## 10. Investment property

### Cost

Land and buildings that are leased to non-Group entities are classified as investment property. The Group 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 Group's investment property are reviewed at each balance sheet date to determine whether there is any indication of impairment in accordance with the policy shown in note 8.

	£m
<b>Cost</b>	
At 1 January 2014	199
Additions	8
Disposals	(21)
At 31 December 2014	186
Additions	13
Disposals	(23)
<b>At 31 December 2015</b>	<b>176</b>
<b>Depreciation and impairment</b>	
At 1 January 2014	64
Depreciation charge for the year	4
Disposals	(11)
At 31 December 2014	57
Depreciation charge for the year	4
Impairment charge for the year	2
Disposals	(7)
<b>At 31 December 2015</b>	<b>56</b>
<b>Net book value</b>	
<b>At 31 December 2015</b>	<b>120</b>
At 31 December 2014	129
At 1 January 2014	135
<b>Fair value</b>	
<b>At 31 December 2015</b>	<b>178</b>
At 31 December 2014	226

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 Group accounts

## continued

### 11. Equity accounted investments

A joint venture is a joint arrangement whereby the parties that have joint control have rights to the net assets of the arrangement.

#### Carrying value

The carrying value of an equity accounted investment comprises the Group's share of net assets and purchased goodwill, and is assessed for impairment as a single asset. The carrying amounts of the Group's equity accounted investments are reviewed at each balance sheet date to determine whether there is any indication of impairment in accordance with the policy shown in note 8.

#### Principal equity accounted investments

Joint venture	Principal activities	Shareholding	Principally operates in
Eurofighter Jagdflugzeug	Management and control of the European Typhoon programme	33%	Germany
MBDA	Development and manufacture of guided weapons	37.5%	Europe
Air Astana	Carriage by air of passengers and cargo	49%	Kazakhstan

The following tables summarise the financial information of the Group's principal equity accounted investments included in their own financial statements, as adjusted for fair value adjustments at acquisition and differences in accounting policies, and reconcile this to the Group's interest in those equity accounted investments.

	2015			2014		
	Eurofighter Jagdflugzeug £m	MBDA £m	Air Astana £m	Eurofighter Jagdflugzeug £m	MBDA £m	Air Astana £m
<b>Revenue (100%)</b>	<b>4,239</b>	<b>2,087</b>	<b>484</b>	3,281	1,929	570
EBITA <sup>1</sup> excluding depreciation	24	282	41	46	215	91
Depreciation and amortisation	–	(60)	(30)	–	(54)	(28)
Financial income	2	59	37	2	68	–
Financial expense	(1)	(70)	(12)	(1)	(79)	(44)
Taxation expense	(7)	(53)	(7)	(13)	(19)	(6)
<b>Profit for the year (100%)</b>	<b>18</b>	<b>158</b>	<b>29</b>	34	131	13
Remeasurements on retirement benefit schemes, net of tax	–	47	–	–	(151)	–
Amounts charged to hedging reserve, net of tax	–	–	(58)	–	–	–
Foreign exchange adjustments	–	1	(89)	–	(6)	(29)
<b>Total comprehensive income for the year (100%)</b>	<b>18</b>	<b>206</b>	<b>(118)</b>	34	(26)	(16)
Group's share of total comprehensive income for the year before elimination of unrealised profit	6	77	(58)	11	(10)	(8)
Elimination of unrealised profit	–	–	–	–	(4)	–
<b>Group's share of total comprehensive income for the year</b>	<b>6</b>	<b>77</b>	<b>(58)</b>	11	(14)	(8)
Non-current assets	9	1,498	219	9	1,507	358
Cash and cash equivalents	4	1,047	143	6	1,182	16
Current assets excluding cash and cash equivalents	1,048	2,921	56	1,102	2,940	194
Current assets	1,052	3,968	199	1,108	4,122	210
Non-current financial liabilities excluding trade and other payables, and provisions	–	(7)	(255)	–	(10)	(267)
Other non-current liabilities	(19)	(742)	–	(18)	(903)	–
Non-current liabilities	(19)	(749)	(255)	(18)	(913)	(267)
Current financial liabilities excluding trade and other payables, and provisions	–	–	(28)	(4)	(20)	(26)
Other current liabilities	(1,011)	(4,421)	(82)	(1,062)	(4,580)	(103)
Current liabilities	(1,011)	(4,421)	(110)	(1,066)	(4,600)	(129)
<b>Net assets (100%)</b>	<b>31</b>	<b>296</b>	<b>53</b>	33	116	172

1. Earnings before amortisation and impairment of intangible assets, finance costs and taxation expense (EBITA) excluding non-recurring items.

**11. Equity accounted investments** continued

	2015				2014			
	Eurofighter Jagdflugzeug £m	MBDA £m	Air Astana £m	Total £m	Eurofighter Jagdflugzeug £m	MBDA £m	Air Astana £m	Total £m
Group's share of net assets	10	111	26	147	11	43	84	138
Elimination of unrealised profit	–	(4)	–	(4)	–	(4)	–	(4)
Goodwill	–	4	–	4	–	15	–	15
<b>Carrying value</b>	<b>10</b>	<b>111</b>	<b>26</b>	<b>147</b>	<b>11</b>	<b>54</b>	<b>84</b>	<b>149</b>

	2015				2014			
	Eurofighter Jagdflugzeug £m	MBDA £m	Air Astana £m	Total £m	Eurofighter Jagdflugzeug £m	MBDA £m	Air Astana £m	Total £m
<b>Dividends received</b>	<b>6</b>	<b>17</b>	<b>3</b>	<b>26</b>	<b>6</b>	<b>44</b>	<b>3</b>	<b>53</b>

**Group summary**

The Group also has a number of individually immaterial joint ventures. The following table shows a reconciliation of opening to closing carrying value for both the Group's principal and immaterial joint ventures in aggregate.

	Principal equity accounted investments £m	Other £m	Total £m
At 1 January 2014	214	69	283
<i>Group's share of profit for the year</i>	67	16	83
<i>Group's share of remeasurements on retirement benefit schemes</i>	(73)	–	(73)
<i>Tax on items that will not be reclassified to the income statement</i>	16	–	16
<i>Foreign exchange adjustments</i>	(17)	1	(16)
<i>Elimination of unrealised profit</i>	(4)	–	(4)
Group's share of total comprehensive income for the year	(11)	17	6
Equity accounted investment funding	–	2	2
Dividends received from equity accounted investments	(53)	(10)	(63)
Business disposals	–	(2)	(2)
Foreign exchange adjustments	(1)	4	3
At 31 December 2014	149	80	229
<i>Group's share of profit for the year</i>	79	31	110
<i>Group's share of remeasurements on retirement benefit schemes</i>	21	–	21
<i>Tax on items that will not be reclassified to the income statement</i>	(3)	–	(3)
<i>Foreign exchange adjustments</i>	(42)	(1)	(43)
<i>Amounts charged to hedging reserve</i>	(36)	–	(36)
<i>Tax on items that may be reclassified to the income statement</i>	7	–	7
Group's share of total comprehensive income for the year	26	30	56
Equity accounted investment funding	–	8	8
Dividends received from equity accounted investments	(26)	(15)	(41)
Foreign exchange adjustments	(2)	–	(2)
<b>At 31 December 2015</b>	<b>147</b>	<b>103</b>	<b>250</b>

**Contingent liabilities**

The Group is not aware of any material contingent liabilities in respect of its equity accounted investments.

## Notes to the Group accounts

### continued

#### 12. Trade and other receivables

Trade and other receivables are stated at their cost less provision for bad debts. A provision for bad debt is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of the receivables. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganisation, and default or delinquency in payments are considered indicators that the trade receivable is impaired. Receivables with a short-term duration are not discounted.

A loss on provision for bad debt is reversed if the subsequent increase in recoverable amount can be related objectively to an event occurring after the impairment loss was recognised.

Amounts due from customers for contract work includes long-term contract balances and amounts due from contract customers, less attributable progress payments.

Long-term contract balances are stated at cost less provision for any anticipated losses. Provisions for losses on contracts are recorded when it becomes probable that total estimated contract costs will exceed total contract revenues. Such provisions are recorded as write downs of long-term contract balances for that portion of the work which has already been completed, and the remainder is included as amounts due to long-term contract customers within trade and other payables. Losses are determined on the basis of estimated results on completion of contracts and are updated regularly.

Progress payments are amounts received from customers in accordance with the terms of contracts which specify payments in advance of delivery and are credited, as progress payments, against any expenditure incurred for the particular contract. Any unexpended balance in respect of progress payments is held in trade and other payables as customer stage payments or, if the amounts are subject to advance payment guarantees unrelated to Group performance, as cash received on customers' account.

Amounts due from contract customers represent unbilled income and are stated at cost, plus attributable profit.

	2015 £m	2014 £m
<b>Non-current</b>		
Prepayments and accrued income	23	85
US deferred compensation plan assets	234	238
Other receivables	18	24
	<b>275</b>	<b>347</b>
<b>Current</b>		
Long-term contract balances	4,407	5,413 <sup>1</sup>
Less: Attributable progress payments	(3,762)	(4,571) <sup>1</sup>
Amounts due from contract customers	413	476
Amounts due from customers for contract work	1,058	1,318
Trade receivables	1,284	935
Amounts owed by equity accounted investments (note 29)	75	92
Prepayments and accrued income	254	251
Other receivables	269	254
	<b>2,940</b>	<b>2,850</b>

1. Restated.

The aggregate amount of costs incurred and recognised profits (less recognised losses) to date in respect of contracts in progress at 31 December 2015 is estimated to be £26.4bn (2014 £30.2bn).

Trade receivables are disclosed net of a provision for bad debts. Disclosures relating to the ageing of trade receivables and movements in the provision for bad debts are provided in note 27.

### 13. Other financial assets and liabilities

#### Derivative financial instruments and hedging activities

The global nature of the Group's business means it is exposed to volatility in currency exchange rates. In order to protect itself against currency fluctuations, the Group's policy is to hedge all material firm transactional exposures. The Group also uses interest rate derivative instruments to manage the Group's exposure to interest rate fluctuations on its borrowings and deposits by varying the proportion of fixed rate debt relative to floating rate debt over the forward time horizon. The Group aims to achieve hedge accounting treatment for all derivatives that hedge material foreign currency exposures and those interest rate exposures where hedge accounting can be achieved.

In accordance with its treasury policy, the Group does not hold derivative financial instruments for trading purposes.

Derivative financial instruments are recognised initially at fair value. Subsequent to initial recognition, such instruments are stated at fair value at the balance sheet date. Gains and losses on derivative financial instruments that do not qualify for hedge accounting are recognised in the income statement for the period.

#### Cash flow hedges

Where a derivative financial instrument is designated as a hedge of cash flows relating to a highly probable forecast transaction (income or expense), the effective portion of any change in the fair value of the instrument is recognised in other comprehensive income and presented in the hedging reserve in equity. Amounts recognised in equity are reclassified from reserves into the cost of the underlying transaction and recognised in the income statement when the underlying transaction affects profit or loss. The ineffective portion of any change in the fair value of the instrument is recognised in the income statement immediately.

#### Fair value hedges

Where a derivative financial instrument is designated as a fair value hedge, changes in the fair value of the underlying asset or liability attributable to the hedged risk, and gains and losses on the derivative instrument, are recognised in the income statement for the period.

	2015		2014	
	Assets £m	Liabilities £m	Assets £m	Liabilities £m
<b>Non-current</b>				
Cash flow hedges – foreign exchange contracts	52	(72)	28	(79)
Other foreign exchange/interest rate contracts	2	–	–	–
Debt-related derivative financial instruments – assets <sup>1</sup>	53	–	10	–
	<b>107</b>	<b>(72)</b>	<b>38</b>	<b>(79)</b>
<b>Current</b>				
Cash flow hedges – foreign exchange contracts	47	(123)	41	(97)
Other foreign exchange/interest rate contracts	58	(7)	5	(10)
	<b>105</b>	<b>(130)</b>	<b>46</b>	<b>(107)</b>

1. Includes fair value hedges of £7m (2014 £4m).

The debt-related derivative financial liabilities are presented as a component of loans and overdrafts (see note 18).

#### Cash flow hedges

The hedged, highly probable forecast transactions denominated in foreign currency are predominantly expected to occur at various stages during the next 12 months. The majority of those extending beyond 12 months are expected to have been transacted within five years of the balance sheet date.

Amounts charged to the hedging reserve in respect of cash flow hedges were £25m (2014 £92m), including a £54m (2014 £1m) credit on reclassification to profit and loss on maturity and a £79m (2014 £93m) charge on contracts held at 31 December 2015.

#### Fair value hedges

The gain arising in the income statement on fair value hedging instruments was £3m (2014 loss £2m). The loss arising in the income statement on the fair value of the underlying hedged items was £2m (2014 £1m). The ineffective portion recognised in the income statement arising from fair value hedges was £1m (2014 £3m).

## Notes to the Group accounts continued

### 14. Deferred tax

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 Group's pension/retirement schemes (see below). 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 contributions are paid to the pension/retirement 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 which run until 2026. In other words, these temporary differences are largely expected to reverse over the next ten years.

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 on the same taxable entity, or on different taxable entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realised simultaneously.

#### Deferred tax assets/(liabilities)

	Deferred tax assets		Deferred tax liabilities		Net balance at 31 December	
	2015 £m	2014 £m	2015 £m	2014 £m	2015 £m	2014 £m
Property, plant and equipment	16	15	(101)	(93)	(85)	(78)
Intangible assets	13	4	(30)	(39)	(17)	(35)
Provisions and accruals	299	287	–	–	299	287
Goodwill	–	–	(326)	(273)	(326)	(273)
Pension/retirement schemes:						
Deficits	908	1,154	–	–	908	1,154
Additional contributions and other <sup>1</sup>	112	121	–	–	112	121
Share-based payments	15	21	–	–	15	21
Financial instruments	16	26	(6)	(5)	10	21
Other items	35	66	–	–	35	66
Rolled over capital gains	–	–	(12)	(13)	(12)	(13)
Capital losses carried forward	12	13	–	–	12	13
Trading losses carried forward	21	22	–	–	21	22
<b>Deferred tax assets/(liabilities)</b>	<b>1,447</b>	<b>1,729</b>	<b>(475)</b>	<b>(423)</b>	<b>972</b>	<b>1,306</b>
Set off of tax	(462)	(402)	462	402	–	–
<b>Net deferred tax assets/(liabilities)</b>	<b>985</b>	<b>1,327</b>	<b>(13)</b>	<b>(21)</b>	<b>972</b>	<b>1,306</b>

1. Includes deferred tax assets on US deferred compensation plans.

**14. Deferred tax** continued**Movement in temporary differences during the year**

	At 1 January 2015 £m	Foreign exchange adjustments £m	Acquisitions and disposals £m	Recognised in income £m	Recognised in equity £m	At 31 December 2015 £m
Property, plant and equipment	(78)	(6)	–	(1)	–	<b>(85)</b>
Intangible assets	(35)	(1)	–	19	–	<b>(17)</b>
Provisions and accruals	287	13	–	(1)	–	<b>299</b>
Goodwill	(273)	(17)	–	(36)	–	<b>(326)</b>
Pension/retirement schemes:						
Deficits	1,154	14	–	15	(275)	<b>908</b>
Additional contributions and other <sup>1</sup>	121	6	–	(3)	(12)	<b>112</b>
Share-based payments	21	–	–	(2)	(4)	<b>15</b>
Financial instruments	21	–	–	(8)	(3)	<b>10</b>
Other items	66	(1)	–	(30)	–	<b>35</b>
Rolled over capital gains	(13)	–	–	1	–	<b>(12)</b>
Capital losses carried forward	13	–	–	(1)	–	<b>12</b>
Trading losses carried forward	22	1	–	(2)	–	<b>21</b>
	<b>1,306</b>	<b>9</b>	<b>–</b>	<b>(49)</b>	<b>(294)</b>	<b>972</b>

	At 1 January 2014 £m	Foreign exchange adjustments £m	Acquisitions and disposals <sup>2</sup> £m	Recognised in income £m	Recognised in equity £m	At 31 December 2014 £m
Property, plant and equipment	(62)	(6)	–	(10)	–	(78)
Intangible assets	(45)	1	(29)	38	–	(35)
Provisions and accruals	308	13	(2)	(32)	–	287
Goodwill	(221)	(15)	–	(37)	–	(273)
Pension/retirement schemes:						
Deficits	692	15	–	12	435	1,154
Additional contributions and other <sup>1</sup>	124	7	–	2	(12)	121
Share-based payments	19	–	–	(2)	4	21
Financial instruments	1	–	–	1	19	21
Other items	59	(3)	–	10	–	66
Rolled over capital gains	(13)	–	–	–	–	(13)
Capital losses carried forward	13	–	–	–	–	13
Trading losses carried forward	19	1	13	(11)	–	22
	<b>894</b>	<b>13</b>	<b>(18)</b>	<b>(29)</b>	<b>446</b>	<b>1,306</b>

1. Includes deferred tax assets on US deferred compensation plans.

2. In 2014, included net deferred tax liabilities on acquisition of subsidiaries (£17m) and the transfer of net deferred tax assets to held for sale (£1m).

**Unrecognised deferred tax assets**

Deferred tax assets have not been recognised in respect of the following items:

	2015 £m	2014 £m
Deductible temporary differences, including tax credits	<b>1</b>	2
Capital losses carried forward	<b>31</b>	38
Trading and other losses carried forward	<b>38</b>	62
	<b>70</b>	102

These assets have not been recognised as the incidence of future profits in the relevant countries and legal entities cannot be accurately predicted at this time.

**Future changes in tax rates**

Under the Finance Act 2013, the UK current tax rate reduced from 21% to 20% with effect from 1 April 2015. Under the Finance (No. 2) Act 2015, the UK current tax rate will reduce to 19% with effect from 1 April 2017 and to 18% with effect from 1 April 2020. This will reduce future UK current tax charges accordingly.

The reduction to 18% was substantively enacted before 31 December 2015. In line with this change, the rate applying to UK deferred tax assets and liabilities has been reduced from 20% to 18%, creating a rate adjustment in 2015, which is partly reflected in the Consolidated income statement and partly in the Consolidated statement of comprehensive income. Accordingly, both recognised and unrecognised UK deferred tax balances as at 31 December 2015 have been calculated at 18%.

## Notes to the Group accounts continued

### 15. Inventories

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

	2015 £m	2014 £m
Short-term work-in-progress	455	439
Raw materials and consumables	197	189
Finished goods and goods for resale	74	62
	<b>726</b>	<b>690</b>

The Group recognised £16m (2014 £4m) as a write down of inventories to net realisable value.

### 16. Cash and cash equivalents

Cash and cash equivalents includes cash in hand, call and term deposits, and other short-term liquid investments with original maturities of three months or less and which are subject to an insignificant risk of change in value. For the purpose of the cash flow statement, cash and cash equivalents also includes bank overdrafts that are repayable on demand.

	2015 £m	2014 £m
Cash	536	537
Short-term deposits	2,001	1,777
	<b>2,537</b>	<b>2,314</b>
Less: Cash and cash equivalents (included within assets held for sale)	–	(6)
	<b>2,537</b>	<b>2,308</b>

### 17. Geographical analysis of assets

#### Analysis of non-current assets by geographical location

Asset location	Notes	2015 £m	2014 £m
UK		2,537	2,505
Rest of Europe		538	546
US		8,635	8,444
Saudi Arabia		349	316
Australia		406	469
Rest of Asia and Pacific		1	2
Africa, and Central and South America		–	2
<b>Non-current segment assets</b>		<b>12,466</b>	<b>12,284</b>
Retirement benefit surpluses	20	193	162
Other financial assets	13	159	74
Tax		989	1,334
Inventories	15	726	690
Current trade and other receivables	12	2,940	2,850
Cash (as defined by the Group) <sup>1</sup>	24	2,590	2,318
Assets held for sale		20	76
<b>Consolidated total assets</b>		<b>20,083</b>	<b>19,788</b>

1. Includes cash and cash equivalents (note 16) and debt-related derivative financial instrument assets (note 13).

## 18. Loans and overdrafts

Loans and overdrafts are recognised initially at fair value, less attributable transaction costs. Subsequent to initial recognition, loans and overdrafts are stated at either amortised cost or, where hedge accounting has been adopted, fair value in respect of the hedged risk. Any difference between the amount initially recognised and the redemption value is recognised in the income statement over the period of the borrowings.

	2015 £m	2014 £m
<b>Non-current</b>		
US\$350m 3.5% bond, repayable 2016	–	224
Albertville Hangar bond, repayable 2018	6	6
US\$1bn 6.375% bond, repayable 2019	680	642
US\$500m 2.85% bond, repayable 2020	337	–
US\$500m 4.75% bond, repayable 2021	339	320
£400m 4.125% bond, repayable 2022	398	398
US\$800m 3.8% bond, repayable 2024	546	514
US\$750m 3.85% bond, repayable 2025	501	–
US\$500m 7.5% bond, repayable 2027	337	319
US\$400m 5.8% bond, repayable 2041	268	254
US\$550m 4.75% bond, repayable 2044 (2014 US\$300m)	363	190
Debt-related derivative financial instruments – liabilities	–	1
	<b>3,775</b>	<b>2,868</b>
<b>Current</b>		
US\$750m 5.2% bond, repayable 2015	–	481
US\$350m 3.5% bond, repayable 2016	237	–
Overdrafts	–	1
	<b>237</b>	<b>482</b>

US\$500m of the US\$1bn 6.375% bond, repayable 2019, has been converted to a floating rate bond by utilising interest rate swaps that mature in June 2019 and give an effective rate during 2015 of 5.8%.

US\$500m of the US\$800m 3.8% bond, repayable 2024, has been converted to a floating rate bond by utilising interest rate swaps that mature in October 2019 and give an effective rate during 2015 of 2.9%. US\$500m of the US\$800m bond is measured at fair value.

The US\$500m 7.5% bond, repayable 2027, was converted at issue to a sterling fixed rate bond by utilising cross-currency swaps and has an effective interest rate of 7.7%.

The debt-related derivative financial instruments represent the fair value of interest rate and cross-currency derivatives relating to the US\$500m 7.5% bond, repayable 2027, and the US\$800m 3.8% bond, repayable 2024. These derivatives have been entered into specifically to manage the Group's exposure to foreign exchange or interest rate risk. Debt-related derivative financial liabilities are presented within loans and overdrafts above and debt-related derivative financial assets are presented within other financial assets (see note 13).

## Notes to the Group accounts continued

### 19. Trade and other payables

Trade and other payables are stated at their cost.

	2015 £m	2014 £m
<b>Non-current</b>		
Amounts due to long-term contract customers	456	404
Amounts owed to equity accounted investments (note 29)	32	40
Accruals and deferred income <sup>1</sup>	121	45
US deferred compensation plan liabilities	264	262
Other payables	147	181
	<b>1,020</b>	<b>932</b>
<b>Current</b>		
Amounts due to long-term contract customers	3,119	3,713
Amounts due to other customers	204	285
Trade payables	690	599
Amounts owed to equity accounted investments (note 29)	414	454
Other taxes and social security costs	155	76
Accruals and deferred income	1,371	1,181
Other payables	209	362
	<b>6,162</b>	<b>6,670</b>
Included above:		
Amounts due to long-term contract customers, including contract losses	3,575	4,117
Advances from long-term contract customers	3,416	3,935

1. Includes £46m (2014 £nil) of funding received from the UK government for property, plant and equipment at Barrow-in-Furness, UK, relating to the Successor submarine programme.

## 20. Retirement benefit obligations

### Pension schemes

#### Defined contribution

Obligations for contributions are recognised as an expense in the income statement as incurred.

#### Defined benefit

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 Consolidated 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.

The retirement benefit obligation recognised in the Group's balance sheet represents the present value of the defined benefit obligations calculated using a number of actuarial assumptions as set out on page 142 reduced by the fair value of scheme assets. 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.

Certain of the Group's equity accounted investments participate in the Group's defined benefit schemes as well as Airbus SAS (Airbus), the Group's share of which was disposed of in 2006. As these schemes are multi-employer schemes, the Group has allocated a share of the IAS 19 pension deficit to its equity accounted investments and other participating employers.

In December 2015, BAE Systems, Airbus and the scheme trustees agreed to work towards the creation of a separate Airbus section of the BAE Systems Pension Scheme (Main Scheme) in 2016 with the allocation of the deficit to the BAE Systems and Airbus sections based on each member's last employer. This allocation methodology is considered to represent a better estimate of the deficit allocation than the relative payroll contributions of active members and has been reflected in the allocation of the IAS 19 pension deficit in the Main Scheme at 31 December 2015. The impact of this change on the amounts allocated at 31 December 2015 is an increase of £187m (£153m post-tax) in the Group's share of the reported IAS 19 deficit. Currently, in the event that an employer who participates in the Group'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 Group considers the likelihood of this event arising as remote. However, following the creation of an Airbus section of the Main Scheme, the Group's obligation in respect of Airbus is expected to be removed.

With the exception of the allocation of the Main Scheme deficit to Airbus, the deficit allocation method for other employers of the Main Scheme and for all other schemes is based on the relative payroll contributions of active members, which is consistent with prior years and is intended to reflect a reasonable approximation of the share of the deficit.

The Group's share of the IAS 19 pension deficit allocated to the equity accounted investments is included in the balance sheet within equity accounted investments.

### Pension schemes

#### Background

BAE Systems plc operates pension schemes for the Group's qualifying employees in the UK, US and other countries. The principal schemes in the UK and US are funded defined benefit schemes, and the assets are held in separate trustee-administered funds. The two largest funded defined benefit schemes are the Main Scheme and the BAE Systems 2000 Pension Plan (2000 Plan) which, in aggregate, represent 71% (2014 71%) of the total IAS 19 defined benefit obligation at 31 December 2015. The schemes in other countries are primarily defined contribution schemes.

At 31 December 2015, the weighted average durations of the UK and US defined benefit pension obligations were 18 years (2014 19 years) and 12 years (2014 12 years), respectively.

The split of the defined benefit pension liability on a funding basis between active, deferred and pensioner members for the Main Scheme, 2000 Plan and US schemes in aggregate is set out below:

	Active %	Deferred %	Pensioner %
Main Scheme <sup>1</sup>	32	19	49
2000 Plan <sup>2</sup>	14	29	57
US schemes <sup>3</sup>	34	18	48

1. Source: Main Scheme actuarial valuation report as at 31 March 2014.

2. Source: 2000 Plan actuarial valuation report as at 31 March 2014.

3. Source: Annual updates of the US schemes as at 1 January 2015.

# Notes to the Group accounts

## continued

### 20. Retirement benefit obligations continued

#### 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 the Group.

The funded US schemes are tax-qualified pension schemes regulated by the Pension Protection Act 2006 and insured by the Pension Benefit Guarantee Corporation (PBGC) up to certain limits. These schemes were established under and are governed by the US Employee Retirement Income Security Act 1974 and the BAE Systems Administrative Committee is a named fiduciary with the authority to manage their operation.

#### 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 and 2000 Plan 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: [baesystemspensions.com](http://baesystemspensions.com).

The US defined benefit schemes ceased to be final salary schemes in January 2013. The benefits accrued based on the final salaries of members at that point will become payable on retirement. The Normal Retirement Age for the largest scheme in the US is 65.

#### Funding

The majority of the UK and US defined benefit pension schemes are funded by the Group's subsidiaries, equity accounted investments and other participating employers. 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, whilst the liabilities are determined based on prudent assumptions set by the trustees following consultation with scheme actuaries.

The separate actuarial valuations for funding purposes include assumptions which differ from the actuarial assumptions used for IAS 19 accounting purposes shown on page 142. The latest valuations of the Main Scheme and 2000 Plan were performed as at 31 March 2014 and showed a funding deficit of £2.6bn. The total net funding deficit in respect of all of the UK schemes was £2.7bn. Deficit recovery plans agreed with the trustees of the relevant schemes run until 2026.

The results of future triennial valuations and associated funding requirements will be impacted by the future performance of investment markets, and interest and inflation rates.

The total Group contributions made to the defined benefit schemes in the year ended 31 December 2015 were £438m (2014 £548m) excluding those amounts allocated to equity accounted investments and participating employers of £98m (2014 £92m). This includes additional contributions of £33m into the UK schemes relating to the share buyback programme (2014 £108m).

In 2016, the Group expects to make contributions at a similar level to the recurring contributions and deficit funding as made in 2015.

The Group incurred a charge of £140m (2014 £125m) in relation to defined contribution schemes for employees.

## 20. Retirement benefit obligations continued

### Risk management

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

Risk	Mitigation
<p><b>Market (investment) risk</b></p> <p>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 provide reasonable assurance that no single security or type of security could have a materially adverse impact on the total portfolio. 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 48% (2014 46%) of the Group's 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 Group's pension schemes use derivative financial instruments as part of their investment strategy to manage the level of market risk. In August 2013, the Main Scheme implemented a long-dated equity option strategy protecting £1.4bn of assets against a significant fall in equity markets.</p>
<p><b>Interest rate risk</b></p> <p>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 principal 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.</p>
<p><b>Inflation risk</b></p> <p>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.</p> <p>Effective 1 May 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><b>Longevity risk</b></p> <p>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 February 2013, with the agreement of the Company, the trustees of the 2000 Plan entered into an arrangement with Legal &amp; General to insure against longevity risk for the current pensioner population, covering £2.7bn of pension scheme liabilities. In December 2013, similar arrangements were entered into, with Legal &amp; General, by the trustees of the Royal Ordnance Pension Scheme and Shipbuilding Industries Pension Scheme, covering £0.9bn and £0.8bn of pension scheme liabilities, respectively. These arrangements reduce the funding volatility relating to increasing life expectancy.</p>

# Notes to the Group accounts

## continued

### 20. Retirement benefit obligations continued

#### 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.

	UK			US		
	2015	2014	2013	2015	2014	2013
<b>Financial assumptions</b>						
Discount rate (%)	3.9	3.6	4.5	4.5	4.1	4.9
Inflation (%)	3.2	3.2	3.4	n/a	n/a	n/a
Rate of increase in salaries (%)	3.2	3.2	3.4	n/a	n/a	n/a
Rate of increase in deferred pensions (%)	2.3/3.2	2.3/3.2	2.5/3.4	n/a	n/a	n/a
Rate of increase in pensions in payment (%)	1.8 – 3.6	1.8 – 3.6	1.9 – 3.7	n/a	n/a	n/a
<b>Demographic assumptions</b>						
Life expectancy of a male currently aged 65 (years)	87 – 89	87 – 89	87 – 89	87	87	84
Life expectancy of a female currently aged 65 (years)	89 – 90	89 – 90	89 – 90	89	89	86
Life expectancy of a male currently aged 45 (years)	89 – 91	89 – 91	88 – 90	87	87	84
Life expectancy of a female currently aged 45 (years)	91 – 92	91 – 92	91 – 92	89	89	86

#### Discount rate

Discount rate assumptions are based on third-party AA corporate bond indices and yields that reflect the maturity profile of the expected benefit payments.

#### Inflation

In the UK, 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. In the US, inflation assumptions are not significant as the Group's US pension schemes are not indexed with inflation.

#### Rate of increase in salaries

The rate of increase in salaries for the UK schemes is assumed to be Retail Prices Index (RPI) inflation of 3.2% (2014 RPI inflation of 3.2%), plus a promotional scale. From 1 January 2013, employees in the US schemes no longer accrue salary-related benefits.

#### Rate of increase in deferred pensions

The rate of increase in deferred pensions for the UK schemes is based on Consumer Prices Index (CPI) inflation of 2.3% (2014 CPI inflation of 2.3%), with the exception of the 2000 Plan, which is based on RPI inflation of 3.2% (2014 RPI inflation of 3.2%). 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 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

For its UK pension schemes, the Group has used the Self-Administered Pension Schemes S2 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. In addition, to allow for future improvements in longevity, the Continuous Mortality Investigation 2013 tables (published by the Institute of Actuaries) have been used, with an assumed long-term rate of future annual mortality improvements of 1.25% (2014 1.25%), for both pensioner and non-pensioner members.

In October 2015, the Society of Actuaries in the US released updated mortality assumptions reflecting the results of its comprehensive mortality study. For the majority of the US schemes, the mortality tables used at 31 December 2015 are a blend of the fully generational RP-2014 Aggregate table and the RP-2014 White Collar table, both projected using Scale MP-2015. The mortality table changes resulted in a small reduction in the US defined benefit obligations. IRS approval of the mortality tables is expected in 2017, following which the tables are expected to be adopted for funding valuation purposes.

## 20. Retirement benefit obligations continued

### Retirement benefits other than pensions

#### Background

The Group operates a number of non-pension retirement benefit schemes, under which certain employees are eligible to receive benefits after retirement, the majority of which relate to the provision of medical benefits to retired employees of the Group's subsidiaries in the US. The latest valuations of the principal schemes, covering retiree medical and life insurance schemes in certain US subsidiaries, were performed by independent actuaries as at 1 January 2015. These valuations were rolled forward to reflect the information at 31 December 2015. The method of accounting for these is similar to that used for defined benefit pension schemes.

#### Principal actuarial assumptions

The assumption for long-term healthcare cost increases is 4.8% (2014 5.3%) based on the assumptions that the increases are 7.3% in 2016 reducing to 4.5% by 2024 and 4.5% each year thereafter for pre-retirement, and 8% in 2016 reducing to 4.5% by 2024 and 4.5% each year thereafter for post-retirement.

The disclosures below relate to post-retirement benefit schemes in the UK, US and other countries which are accounted for as defined benefit schemes in accordance with IAS 19.

#### Summary of movements in retirement benefit obligations

	UK £m	US and other £m	Total £m
Total IAS 19 deficit at 1 January 2015	(6,066)	(746)	(6,812)
Actual return on assets excluding amounts included in interest expense	(335)	(198)	(533)
Decrease in liabilities due to changes in financial assumptions	1,348	202	1,550
Decrease in liabilities due to changes in demographic assumptions	–	29	29
Experience gains/(losses)	224	(4)	220
Additional contributions in excess of service cost	177	–	177
Recurring contributions in excess of service cost	44	53	97
Past service cost – plan amendments	(10)	–	(10)
Settlements	–	4	4
Net interest expense	(206)	(32)	(238)
Foreign exchange adjustments	–	(40)	(40)
Movement in US healthcare schemes	–	2	2
<b>Total IAS 19 deficit at 31 December 2015</b>	<b>(4,824)</b>	<b>(730)</b>	<b>(5,554)</b>
Allocated to equity accounted investments and other participating employers	1,053	–	1,053
<b>Group's share of IAS 19 deficit excluding Group's share of amounts allocated to equity accounted investments and other participating employers at 31 December 2015</b>	<b>(3,771)</b>	<b>(730)</b>	<b>(4,501)</b>

## Notes to the Group accounts

### continued

#### 20. Retirement benefit obligations continued

##### Amounts recognised on the balance sheet

The table below shows a reconciliation between the gross assets and liabilities of the Group's UK, US and other post-retirement benefit schemes and the amounts recognised on the Group's balance sheet after allocation to equity accounted investments and other participating employers.

	2015				2014			
	UK defined benefit pension schemes £m	US and other pension schemes £m	US healthcare schemes £m	Total £m	UK defined benefit pension schemes £m	US and other pension schemes £m	US healthcare schemes £m	Total £m
Present value of unfunded obligations	(59)	(131)	–	(190)	(41)	(138)	–	(179)
Present value of funded obligations	(24,974)	(4,072)	(145)	(29,191)	(26,195)	(4,132)	(146)	(30,473)
Fair value of scheme assets	20,209	3,452	166	23,827	20,170	3,505	165	23,840
Total IAS 19 (deficit)/surplus, net	(4,824)	(751)	21	(5,554)	(6,066)	(765)	19	(6,812)
Allocated to equity accounted investments and other participating employers	1,053	–	–	1,053	1,444	–	–	1,444
<b>Group's share of IAS 19 (deficit)/surplus, net</b>	<b>(3,771)</b>	<b>(751)</b>	<b>21</b>	<b>(4,501)</b>	<b>(4,622)</b>	<b>(765)</b>	<b>19</b>	<b>(5,368)</b>
Represented by:								
Retirement benefit surpluses	120	41	32	193	89	41	32	162
Retirement benefit obligations	(3,891)	(792)	(11)	(4,694)	(4,711)	(806)	(13)	(5,530)
	(3,771)	(751)	21	(4,501)	(4,622)	(765)	19	(5,368)
<b>Group's share of IAS 19 deficit of equity accounted investments</b>	<b>(139)</b>	<b>–</b>	<b>–</b>	<b>(139)</b>	<b>(165)</b>	<b>–</b>	<b>–</b>	<b>(165)</b>

Total cumulative actuarial losses recognised in equity since the transition to IFRS are £5.2bn (2014 £6.0bn).

**20. Retirement benefit obligations** continued**Changes in the fair value of scheme assets before allocation to equity accounted investments and other participating employers**

	UK defined benefit pension schemes £m	US and other pension schemes £m	US healthcare schemes £m	Total £m
Value of scheme assets at 1 January 2014	18,331	3,043	148	21,522
<i>Interest income</i>	820	146	7	973
<i>Actual return on assets excluding amounts included in interest income</i>	1,240	208	5	1,453
Actual return on assets	2,060	354	12	2,426
<i>Contributions by employer</i>	554	86	1	641
<i>Contributions by employer in respect of employee salary sacrifice arrangements</i>	105	–	–	105
Total contributions by employer	659	86	1	746
Members' contributions	12	–	–	12
Administrative expenses	(31)	(9)	(1)	(41)
Foreign exchange translation	–	201	10	211
Benefits paid	(861)	(170)	(5)	(1,036)
Value of scheme assets at 31 December 2014	20,170	3,505	165	23,840
<i>Interest income</i>	720	142	7	869
<i>Actual return on assets excluding amounts included in interest income</i>	(335)	(198)	(9)	(542)
Actual return on assets	385	(56)	(2)	327
<i>Contributions by employer</i>	460	76	2	538
<i>Contributions by employer in respect of employee salary sacrifice arrangements</i>	103	–	–	103
Total contributions by employer	563	76	2	641
Members' contributions	11	–	–	11
Administrative expenses	–	(12)	(1)	(13)
Settlements	–	(64)	–	(64)
Foreign exchange translation	–	190	9	199
Benefits paid	(920)	(187)	(7)	(1,114)
<b>Value of scheme assets at 31 December 2015</b>	<b>20,209</b>	<b>3,452</b>	<b>166</b>	<b>23,827</b>

# Notes to the Group accounts

## continued

### 20. Retirement benefit obligations continued

#### Assets of defined benefit pension schemes

	2015								
	UK			US and other			Total		
	Quoted £m	Unquoted £m	Total £m	Quoted £m	Unquoted £m	Total £m	Quoted £m	Unquoted £m	Total £m
Equities:									
UK <sup>1</sup>	4,133	–	4,133	–	–	–	4,133	–	4,133
Overseas	2,883	–	2,883	602	–	602	3,485	–	3,485
Pooled investment vehicles <sup>2</sup>	3,254	–	3,254	480	–	480	3,734	–	3,734
Fixed interest securities:									
UK gilts	2,103	–	2,103	–	–	–	2,103	–	2,103
UK corporates	2,771	–	2,771	–	–	–	2,771	–	2,771
Overseas government	–	–	–	111	–	111	111	–	111
Overseas corporates	389	–	389	2,084	–	2,084	2,473	–	2,473
Index-linked securities:									
UK gilts	1,754	–	1,754	–	–	–	1,754	–	1,754
UK corporates	1,678	–	1,678	–	–	–	1,678	–	1,678
Property <sup>3</sup>	1,280	153	1,433	–	146	146	1,280	299	1,579
Derivatives	–	(678)	(678)	–	–	–	–	(678)	(678)
Cash:									
Sterling	253	–	253	–	–	–	253	–	253
Foreign currency	57	–	57	23	–	23	80	–	80
Other	–	179	179	–	6	6	–	185	185
<b>Total</b>	<b>20,555</b>	<b>(346)</b>	<b>20,209</b>	<b>3,300</b>	<b>152</b>	<b>3,452</b>	<b>23,855</b>	<b>(194)</b>	<b>23,661</b>

  

	2014								
	UK			US and other			Total		
	Quoted £m	Unquoted £m	Total £m	Quoted £m	Unquoted £m	Total £m	Quoted £m	Unquoted £m	Total £m
Equities:									
UK <sup>1</sup>	4,183	–	4,183	–	–	–	4,183	–	4,183
Overseas	2,920	–	2,920	640	–	640	3,560	–	3,560
Pooled investment vehicles <sup>2</sup>	2,487	270	2,757	454	–	454	2,941	270	3,211
Fixed interest securities:									
UK gilts	2,332	–	2,332	–	–	–	2,332	–	2,332
UK corporates	2,464	–	2,464	–	–	–	2,464	–	2,464
Overseas government	–	–	–	158	–	158	158	–	158
Overseas corporates	377	–	377	2,044	–	2,044	2,421	–	2,421
Index-linked securities:									
UK gilts	2,198	–	2,198	–	–	–	2,198	–	2,198
UK corporates	1,508	–	1,508	–	–	–	1,508	–	1,508
Property <sup>3</sup>	1,176	159	1,335	–	165	165	1,176	324	1,500
Derivatives	–	(509)	(509)	–	–	–	–	(509)	(509)
Cash:									
Sterling	288	–	288	–	–	–	288	–	288
Foreign currency	172	–	172	36	–	36	208	–	208
Other	–	145	145	–	8	8	–	153	153
<b>Total</b>	<b>20,105</b>	<b>65</b>	<b>20,170</b>	<b>3,332</b>	<b>173</b>	<b>3,505</b>	<b>23,437</b>	<b>238</b>	<b>23,675</b>

1. Includes £31m (2014 £14m) of the Company's own ordinary shares.

2. Primarily comprises equities.

3. Includes £257m (2014 £282m) of property occupied by Group companies.

**20. Retirement benefit obligations** continued**Changes in the present value of the defined benefit obligations before allocation to equity accounted investments and other participating employers**

	UK defined benefit pension schemes £m	US and other pension schemes £m	US healthcare schemes £m	Total £m
Defined benefit obligations at 1 January 2014	(22,603)	(3,340)	(117)	(26,060)
<i>Current service cost</i>	(200)	(9)	(1)	(210)
<i>Contributions by employer in respect of employee salary sacrifice arrangements</i>	(105)	–	–	(105)
Total current service cost	(305)	(9)	(1)	(315)
Members' contributions	(12)	–	–	(12)
Past service cost – plan amendments	(3)	(1)	–	(4)
Actuarial loss due to changes in financial assumptions	(3,273)	(405)	(10)	(3,688)
Actuarial loss due to changes in demographic assumptions	(341)	(283)	(6)	(630)
Experience gains/(losses)	435	(6)	(3)	426
Interest expense	(995)	(160)	(5)	(1,160)
Foreign exchange translation	–	(236)	(9)	(245)
Benefits paid	861	170	5	1,036
Defined benefit obligations at 31 December 2014	(26,236)	(4,270)	(146)	(30,652)
<i>Current service cost</i>	(239)	(11)	(2)	(252)
<i>Contributions by employer in respect of employee salary sacrifice arrangements</i>	(103)	–	–	(103)
Total current service cost	(342)	(11)	(2)	(355)
Members' contributions	(11)	–	–	(11)
Past service cost – plan amendments	(10)	–	–	(10)
Settlements	–	68	–	68
Actuarial gain due to changes in financial assumptions	1,348	202	7	1,557
Actuarial gain due to changes in demographic assumptions	–	29	2	31
Experience gains/(losses)	224	(4)	1	221
Interest expense	(926)	(174)	(6)	(1,106)
Foreign exchange translation	–	(230)	(8)	(238)
Benefits paid	920	187	7	1,114
<b>Defined benefit obligations at 31 December 2015</b>	<b>(25,033)</b>	<b>(4,203)</b>	<b>(145)</b>	<b>(29,381)</b>

**Amounts recognised in the income statement after allocation to equity accounted investments and other participating employers**

	2015				2014			
	UK defined benefit pension schemes £m	US and other pension schemes £m	US healthcare schemes £m	Total £m	UK defined benefit pension schemes £m	US and other pension schemes £m	US healthcare schemes £m	Total £m
<b>Included in operating costs:</b>								
Current service cost	(177)	(11)	(2)	(190)	(156)	(9)	(1)	(166)
Past service cost – plan amendments	(10)	–	–	(10)	(3)	(1)	–	(4)
Settlements	–	4	–	4	–	–	–	–
	(187)	(7)	(2)	(196)	(159)	(10)	(1)	(170)
Administrative expenses	–	(12)	(1)	(13)	(25)	(9)	(1)	(35)
	(187)	(19)	(3)	(209)	(184)	(19)	(2)	(205)
<b>Included in finance costs:</b>								
Net interest (expense)/income on retirement benefit obligations	(161)	(32)	1	(192)	(135)	(14)	2	(147)
<b>Included in share of results of equity accounted investments:</b>								
Group's share of equity accounted investments' operating costs	(10)	–	–	(10)	(8)	–	–	(8)
Group's share of equity accounted investments' finance costs	(6)	–	–	(6)	(5)	–	–	(5)

# Notes to the Group accounts

## continued

### 20. Retirement benefit obligations continued

#### Sensitivity analysis

The sensitivity information has been derived using scenario analysis from the actuarial assumptions as at 31 December 2015 and keeping all other assumptions as set out on page 142.

#### Financial assumptions

Changes in the following financial assumptions would have the following effect on the defined benefit pension obligation before allocation to equity accounted investments and other participating employers:

	(Increase)/decrease £bn
<b>Discount rate:</b>	
0.1 percentage point increase	0.5
0.1 percentage point decrease	(0.5)
<b>Inflation:</b>	
0.1 percentage point increase	(0.5)
0.1 percentage point decrease	0.5

The sensitivity analysis does not allow for the impact of the Group's risk management activities in respect of interest rate and inflation risk (see page 141) on the valuation of the assets. Across all of its pension schemes, the Group is hedged against approximately 35% and 40% of interest rate and inflation risk, respectively, measured relative to the funding liabilities. The Group's US schemes are not indexed with inflation.

The sensitivity of the valuation of the liabilities to changes in the inflation assumption presented above assumes that a 0.1 percentage point change to expectations of future inflation results in a 0.1 percentage point change to all inflation-related assumptions (rate of increase in salaries, rate of increase in deferred pensions and rate of increase in pensions in payment) used to value the liabilities. However, upper and lower limits exist on the majority of inflation-related benefits such that a change in expectations of future inflation may not have the same impact on the inflation-related benefits, and hence will result in a smaller change to the valuation of the liabilities. Accordingly, extrapolation of the above results beyond the specific sensitivity figures shown may not be appropriate. To illustrate this, the (increase)/decrease in the defined benefit pension obligation resulting from larger changes in the inflation assumption would be as follows:

	(Increase)/decrease £bn
<b>Inflation:</b>	
0.5 percentage point increase	(1.6)
0.5 percentage point decrease	1.6
1.0 percentage point increase	(3.2)
1.0 percentage point decrease	3.0

#### Demographic assumptions

Changes in the life expectancy assumption, including the benefit of longevity swap arrangements (see longevity risk on page 141), would have the following effect on the total IAS 19 deficit:

	(Increase)/decrease £bn
<b>Life expectancy:</b>	
One-year increase	(0.9)
One-year decrease	0.9

## 21. Provisions

A provision is recognised in the balance sheet when the Group has a present legal or constructive obligation as a result of a past event, 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.

### Warranties and after-sales service

Warranties and after-sales service are provided in the normal course of business with provisions for associated costs being made based on an assessment of future claims with reference to past experience. A provision for warranties is recognised when the underlying products and services are sold. The provision is based on historical warranty data and a weighting of possible outcomes against their associated probabilities.

### Reorganisations

A provision for restructuring is recognised when the Group has approved a detailed and formal restructuring plan, and the restructuring has either commenced or has been publicly announced. The costs associated with the reorganisation programmes are supported by detailed plans and based on previous experience as well as other known factors. Future operating costs are not provided for.

### Legal, contractual and environmental

The Group holds provisions for expected legal, contractual and environmental costs that it expects to incur over an extended period. These costs are based on past experience of similar items and other known factors and represent management's best estimate of the likely outcome.

### Other

Other provisions include provisions for onerous contracts, which are recognised when the expected benefits to be derived by the Group from a contract are lower than the unavoidable cost of meeting its obligations under the contract.

	Warranties and after-sales service £m	Reorganisations £m	Legal, contractual and environmental £m	Other £m	Total £m
Non-current	50	46	281	59	436
Current	30	91	135	59	315
At 1 January 2015	80	137	416	118	751
Created	43	52	69	24	188
Utilised	(30)	(95)	(52)	(24)	(201)
Released	(10)	(29)	(41)	(34)	(114)
Reclassification between categories	–	–	14	(14)	–
Net present value adjustments	–	–	14	3	17
Foreign exchange adjustments	2	–	9	3	14
<b>At 31 December 2015</b>	<b>85</b>	<b>65</b>	<b>429</b>	<b>76</b>	<b>655</b>
Represented by:					
Non-current	48	–	278	28	354
Current	37	65	151	48	301
	<b>85</b>	<b>65</b>	<b>429</b>	<b>76</b>	<b>655</b>

### Warranties and after-sales service

Warranty and after-sales service costs are generally incurred within three years post-delivery. Whilst actual events could result in potentially significant differences to the quantum, but not the timing, of the outflows in relation to the provisions, management has reflected current knowledge in assessing the provision levels.

### Reorganisations

Reorganisation costs are generally incurred within one to three years. There is limited volatility around the timing and amount of the ultimate outflows related to these provisions.

### Legal, contractual and environmental

Reflecting the inherent uncertainty within many legal proceedings, the timing and amount of the outflows could differ significantly from the amount provided.

### Other

There are no individually significant provisions included within other provisions.

# Notes to the Group accounts

## continued

### 22. Share capital and other reserves

#### Share capital

	Equity		Non-equity		Total
	Ordinary shares of 2.5p each		Special Share of £1		Nominal value £m
	Number of shares m	Nominal value £m	Number of shares	Nominal value £	
<b>Issued and fully paid</b>					
At 1 January 2014	3,536	89	1	1	89
Repurchased and cancelled	(67)	(2)	–	–	(2)
At 31 December 2014	3,469	87	1	1	87
Repurchased and cancelled	(2)	–	–	–	–
<b>At 31 December 2015</b>	<b>3,467</b>	<b>87</b>	<b>1</b>	<b>1</b>	<b>87</b>

#### Special Share

One Special Share of £1 in the Company is held on behalf of the Secretary of State for Business, Innovation and Skills (the Special Shareholder). Certain provisions of the Company's Articles of Association cannot be amended without the consent of the Special Shareholder. These provisions include the requirement that no foreign person, or foreign persons acting in concert, can have more than a 15% voting interest in the Company, the requirement that the majority of the directors are British, and the requirement that the Chief Executive and any executive Chairman are British citizens. The effect of these requirements can also be amended by regulations made by the directors and approved by the Special Shareholder.

The Special Shareholder may require the Company at any time to redeem the Special Share at par or to convert the Special Share into one ordinary voting share. The Special Shareholder is entitled to receive notice of and to attend general meetings and class meetings of the Company's shareholders, but has no voting right, nor other rights, other than to speak in relation to any business in respect of the Special Share.

#### Share buyback

In 2015, 1,450,000 (2014 67,417,000) ordinary shares of 2.5p were repurchased under the three-year buyback programme announced in February 2013 and such repurchased shares have been cancelled.

#### Treasury shares

As at 31 December 2015, 301,808,103 (2014 315,826,614) ordinary shares of 2.5p each with an aggregate nominal value of £7,545,203 (2014 £7,895,665) were held in treasury. During 2015, 14,018,511 (2014 11,818,338) treasury shares were used to satisfy awards and options under the Share Incentive Plan, International Share Incentive Plan, Restricted Share Plan and Executive Share Option Plan.

#### Own shares held

Own shares held, including treasury shares and shares held by BAE Systems Employee Share Option Plan (ESOP) Trust, are recognised as a deduction from retained earnings.

#### BAE Systems ESOP Trust

The Group has an ESOP discretionary trust to administer the share plans and to acquire Company shares, using funds loaned by the Group, to meet commitments to Group employees. Dividend waivers were in operation for shares within the ESOP Trust, other than those owned beneficially by the participants, for the dividends paid in June and November 2015.

At 31 December 2015, the ESOP held 897,873 (2014 1,509,844) ordinary shares of 2.5p each, with a market value of £4m (2014 £7m). The shares held by the ESOP are recorded at cost and deducted from retained earnings until such time as the shares vest unconditionally to employees.

A dividend waiver was also in operation for the dividends paid in June and November 2015 over shares within the Company's Share Incentive Plan Trust other than those shares owned beneficially by the participants.

#### Equity dividends

Equity dividends on ordinary share capital are recognised as a liability in the period in which they are declared. The interim dividend is recognised when it has been approved by the Board and the final dividend is recognised when it has been approved by the shareholders at the Annual General Meeting.

	2015 £m	2014 £m
Prior year final 12.3p dividend per ordinary share paid in the year (2014 12.1p)	389	383
Interim 8.4p dividend per ordinary share paid in the year (2014 8.2p)	266	259
	<b>655</b>	<b>642</b>

After the balance sheet date, the directors proposed a final dividend of 12.5p per ordinary share. The dividend, which is subject to shareholder approval, will be paid on 1 June 2016 to shareholders registered on 22 April 2016. The ex-dividend date is 21 April 2016.

Shareholders who do not at present participate in the Company's Dividend Reinvestment Plan and wish to receive the final dividend in shares rather than cash should complete a mandate form for the Dividend Reinvestment Plan and return it to the registrars no later than 10 May 2016.

## 22. Share capital and other reserves continued

### Other reserves

	Merger reserve £m	Statutory reserve £m	Revaluation reserve £m	Capital redemption reserve £m	Hedging reserve £m	Translation reserve £m	Total £m
At 1 January 2014	4,589	202	10	1	31	35	4,868
Currency translation on foreign currency net investments:							
Subsidiaries	–	–	–	–	–	277 <sup>1</sup>	277 <sup>1</sup>
Equity accounted investments	–	–	–	–	–	(13) <sup>1</sup>	(13) <sup>1</sup>
Amounts charged to hedging reserve	–	–	–	–	(92)	–	(92)
Tax on other comprehensive income	–	–	–	–	19	–	19
Net purchase of own shares	–	–	–	2	–	–	2
At 31 December 2014	4,589	202	10	3	(42)	299	5,061
Currency translation on foreign currency net investments:							
Subsidiaries	–	–	–	–	–	261	261
Equity accounted investments	–	–	–	–	–	(45)	(45)
Reclassification of cumulative currency translation reserve on disposal	–	–	–	–	–	20	20
Amounts charged to hedging reserve	–	–	–	–	(25)	–	(25)
Tax on other comprehensive income	–	–	–	–	5	–	5
<b>At 31 December 2015</b>	<b>4,589</b>	<b>202</b>	<b>10</b>	<b>3</b>	<b>(62)</b>	<b>535</b>	<b>5,277</b>

1. Restated.

### Merger reserve

The merger reserve arose on the acquisition of the Marconi Electronic Systems (MES) business by British Aerospace in 1999 to form BAE Systems, and represents the amount by which the fair value of the shares issued by British Aerospace as consideration exceeded their nominal value.

### Statutory reserve

Under Section 4 of the British Aerospace Act 1980, this reserve may only be applied in paying up unissued shares of the Company to be allotted to members of the Company as fully paid bonus shares.

### Revaluation reserve

The revaluation reserve relates to the revaluation at fair value of the net assets of the BVT joint venture previously held as an equity accounted investment on the acquisition of the remaining 45% interest in 2009.

### Capital redemption reserve

The capital redemption reserve represents the cumulative nominal value of the Company's ordinary shares repurchased and subsequently cancelled. During the year ended 31 December 2015, 1,450,000 (2014 67,417,000) ordinary shares with a nominal value of £nil (2014 £2m) were repurchased and have been subsequently cancelled.

### Hedging reserve

The hedging reserve comprises the effective portion of the cumulative net change in the fair value of cash flow hedging instruments related to hedged transactions that have not yet occurred.

### Translation reserve

The translation reserve comprises all foreign currency differences arising from the translation of the financial statements of foreign operations.

### Capital

The Group funds its operations through a mixture of equity funding and debt financing, including bank and capital market borrowings.

At 31 December 2015, the Group's capital was £3,064m (2014 £1,919m), which comprises total equity of £3,002m (2014 £1,877m), excluding amounts accumulated in equity relating to cash flow hedges of £62m (2014 £42m). Net debt (as defined by the Group) was £1,422m (2014 £1,032m).

The capital structure of the Group reflects the judgement of the directors of an appropriate balance of funding required. The Group's policy is to maintain an investment grade credit rating and ensure operating flexibility, whilst:

- meeting its pension obligations;
- continuing to pursue organic investment opportunities;
- paying dividends in line with the Group's policy of long-term sustainable cover of around two times underlying earnings (see note 7);
- making accelerated returns of capital to shareholders when the balance sheet allows and only when the return from doing so is in excess of the Group's Weighted Average Cost of Capital; and
- investing in value-enhancing acquisitions, where market conditions are right and where they deliver on the Group's strategy.

# Notes to the Group accounts

## continued

### 23. Cash flow analysis

#### Operating business cash flow

	2015 £m	2014 £m
Cash inflow from operating activities	924	913
Purchase of property, plant and equipment, and investment property	(359)	(263)
Purchase of intangible assets	(54)	(59)
Proceeds from sale of property, plant and equipment, and investment property	136	539
Proceeds from sale of non-current other investments	1	–
Equity accounted investment funding	(8)	(2)
Dividends received from equity accounted investments	41	63
<b>Operating business cash flow</b>	<b>681</b>	<b>1,191</b>

	2015 £m	2014 <sup>1</sup> £m
Electronic Systems	323	246
Cyber & Intelligence	93	125
Platforms & Services (US)	100	147
Platforms & Services (UK)	220	173
Platforms & Services (International)	164	881
HQ	(219)	(381)
<b>Operating business cash flow</b>	<b>681</b>	<b>1,191</b>

1. Re-presented for the reallocation of the Integrated Electronics & Warfare Systems activities from Platforms & Services (US) to Cyber & Intelligence.

#### Cash flows from acquisitions and disposals

	2015 £m	2014 £m
Proceeds from sale of subsidiary undertakings	34	–
Cash and cash equivalents disposed of with subsidiary undertakings	(13)	–
<b>Proceeds from sale of subsidiary undertakings (net of cash disposed)</b>	<b>21</b>	<b>–</b>
Purchase of subsidiary undertakings	(5)	(233)
Cash and cash equivalents acquired from purchase of subsidiary undertakings	–	3
<b>Acquisitions and disposals</b>	<b>16</b>	<b>(230)</b>

## 24. Net (debt)/cash (as defined by the Group)

### Key Performance Indicator – Net (debt)/cash

Net (debt)/cash comprises cash and cash equivalents, less loans and overdrafts (including debt-related derivative financial instruments) and cash received on customers' account<sup>1</sup>.

### Movement in net (debt)/cash (as defined by the Group)

	Notes	2015 £m	2014 £m
Operating business cash flow	23	681	1,191
Interest		(173)	(145)
Taxation		(116)	(92)
Free cash inflow		392	954
Acquisitions and disposals	23	16	(230)
Net sale/(purchase) of own shares		1	(281)
Equity dividends paid		(655)	(642)
Dividends paid to non-controlling interests		(40)	(14)
Cash inflow from matured derivative financial instruments		12	8
Cash inflow from movement in cash collateral		3	10
Cash inflow from loans		1,625	679
Cash outflow from repayment of loans		(1,135)	(398)
Net increase in cash and cash equivalents		219	86
Foreign exchange adjustments		(165)	(146)
Other non-cash movements		46	13
Less: Cash classified as held for sale		–	(6)
Less: Movement in cash received on customers' account <sup>1</sup>		–	1
Less: Cash inflow from loans		(1,625)	(679)
Less: Cash outflow from repayment of loans		1,135	398
Movement in net debt (as defined by the Group)		(390)	(333)
Opening net debt (as defined by the Group)		(1,032)	(699)
<b>Closing net debt (as defined by the Group)</b>		<b>(1,422)</b>	<b>(1,032)</b>

### Components of net (debt)/cash (as defined by the Group)

	Notes	2015 £m	2014 £m
Debt-related derivative financial instrument assets – non-current	13	53	10
Cash and cash equivalents	16	2,537	2,314
Less: Cash classified as held for sale		–	(6)
<b>Cash (as defined by the Group)</b>	17	<b>2,590</b>	<b>2,318</b>
Loans – non-current	18	(3,775)	(2,868)
Loans and overdrafts – current	18	(237)	(482)
<b>Debt (as defined by the Group)</b>		<b>(4,012)</b>	<b>(3,350)</b>
<b>Net debt (as defined by the Group)</b>		<b>(1,422)</b>	<b>(1,032)</b>

1. Cash received on customers' account is the unexpended cash received from customers in advance of delivery which is subject to advance payment guarantees unrelated to Group performance.

## Notes to the Group accounts continued

### 25. Acquisition and disposal of subsidiaries

Business combinations are accounted for using the acquisition method as at the acquisition date, which is the date on which control is transferred to the Group. The Group measures goodwill as the acquisition-date fair value of the consideration transferred, including the amount of any non-controlling interest in the acquiree, less the net of the acquisition-date fair values of the identifiable assets acquired and liabilities assumed, including contingent liabilities as required by IFRS 3, Business Combinations.

Consideration transferred includes the fair values of assets transferred, liabilities incurred by the Group to the previous owners of the acquiree, equity interests issued by the Group, contingent consideration, and share-based payment awards of the acquiree that are replaced in the business combination. Any contingent consideration payable is recognised at fair value at the acquisition date. Subsequent changes to the fair value of contingent consideration that is not classified as equity are recognised in the income statement.

Transaction costs that the Group incurs in connection with a business combination, such as finder's fees, legal fees, due diligence fees, and other professional and consulting fees, are expensed as incurred.

#### Subsidiaries acquired during 2015

In June, the Group completed the acquisition of Eclipse Electronic Systems, Inc., a provider of advanced Intelligence, Surveillance and Reconnaissance products and services, for cash consideration of \$8m (£5m).

#### Subsidiaries disposed of during 2015

In April, the Group completed the sale of its 75% holding in BAE Systems Land Systems South Africa (Pty) Limited for cash consideration of 655 million Rand (£36m).

	£m	£m
Cash consideration		36
Transaction costs paid		(2)
<b>Cash proceeds</b>		<b>34</b>
<b>Net assets disposed:</b>		
Intangible assets	(19)	
Property, plant and equipment	(9)	
Inventories	(7)	
Trade and other receivables	(9)	
Deferred tax assets	(3)	
Cash and cash equivalents	(13)	
Trade and other payables	8	
Deferred tax liabilities	2	
Provisions	6	
		<b>(44)</b>
Non-controlling interest disposed		6
Cumulative currency translation loss		(20)
<b>Loss on disposal of businesses</b>		<b>(24)</b>

#### Subsidiaries acquired during 2014

In 2014, the Group acquired Perimeter Internetworking Corp., trading as SilverSky; an additional 59% shareholding in Saudi Development and Training Company; and Signal Innovations Group, Inc. For all acquisitions made during 2014, there were no adjustments made in 2015 to the provisional fair values.

## 26. Fair value measurement

### Fair value of financial instruments

Certain of the Group's financial instruments are held at fair value.

The fair value of a financial instrument is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the balance sheet date.

The fair values of financial instruments held at fair value have been determined based on available market information at the balance sheet date, and the valuation methodologies listed below:

- the fair values of forward foreign exchange contracts are calculated by discounting the contracted forward values and translating at the appropriate balance sheet rates;
- the fair values of both interest rate and cross-currency swaps are calculated by discounting expected future principal and interest cash flows and translating at the appropriate balance sheet rates; and
- the fair values of loans and overdrafts have been estimated by discounting the future cash flows to net present values using appropriate market-based interest rates prevailing at 31 December.

Due to the variability of the valuation factors, the fair values presented at 31 December may not be indicative of the amounts the Group would expect to realise in the current market environment.

### Fair value hierarchy

The fair value measurement hierarchy is as follows:

- Level 1 – Quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2 – Inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3 – Inputs for the asset or liability that are not based on observable market data (i.e. unobservable inputs).

### Carrying amounts and fair values of certain financial instruments

	Notes	2015		2014	
		Carrying amount £m	Fair value £m	Carrying amount £m	Fair value £m
<b>Financial instruments measured at fair value:</b>					
<b>Non-current</b>					
Available-for-sale financial assets		6	6	7	7
Other receivables <sup>1</sup>	12	234	234	238	238
Other financial assets	13	107	107	38	38
Other financial liabilities	13	(72)	(72)	(79)	(79)
Loans	18	(346)	(346)	(325)	(325)
Trade and other payables <sup>1</sup>	19	(264)	(264)	(262)	(262)
<b>Current</b>					
Other financial assets	13	105	105	46	46
Other financial liabilities	13	(130)	(130)	(107)	(107)
<b>Financial instruments not measured at fair value:</b>					
<b>Non-current</b>					
Loans	18	(3,429)	(3,704)	(2,543)	(2,900)
<b>Current</b>					
Cash and cash equivalents	16	2,537	2,537	2,308	2,308
Loans and overdrafts	18	(237)	(241)	(482)	(494)

1. Represents US deferred compensation plan assets and liabilities.

All of the financial assets and liabilities measured at fair value are classified as level 2 using the fair value hierarchy. There were no transfers between levels during the year.

Financial assets and liabilities in the Group's consolidated balance sheet are either held at fair value or their carrying value approximates to fair value, with the exception of loans, most of which are held at amortised cost.

The fair value of total loans and overdrafts estimated using market prices at 31 December 2015 is £4,291m (2014 £3,719m).

# Notes to the Group accounts

## continued

### 27. Financial risk management

#### Interest rate risk

The Group's objective is to manage its exposure to interest rate fluctuations on borrowings through varying the proportion of fixed rate debt relative to floating rate debt with derivative instruments, including interest rate and cross-currency swaps.

The Group's interest rate management policy is that a minimum of 50% (2014 50%) and a maximum of 90% (2014 90%) of gross debt is maintained at fixed interest rates. At 31 December 2015, the Group had 83% (2014 81%) of fixed rate debt and 17% (2014 19%) of floating rate debt based on a gross debt of £4.0bn, including debt-related derivative financial assets (2014 £3.3bn).

Based on contracted maturities and/or repricing dates, the following amounts are exposed to interest rate risk over the future as shown below:

	Less than one year £m	Between one and two years £m	More than two years £m
Cash and cash equivalents	2,537	–	–
Loans and overdrafts	(681)	(681)	(681)

The floating rate debt has been predominantly achieved by entering into interest rate swaps which swap the fixed rate US dollar interest payable on debt into either floating rate sterling or US dollars. At the end of 2015, the Group had a total of \$1.0bn (2014 \$1.0bn) of this type of swap outstanding with a weighted average duration of 3.6 years (2014 4.6 years). In respect of the fixed rate debt, the weighted average period in respect of which interest is fixed was 11.5 years (2014 10.1 years).

Given the level of short-term interest rates during the year, the average cost of the floating rate debt was 3.5% (2014 4.1%) on US dollars. The cost of the fixed rate debt was 4.9% (2014 5.4%).

A change of 100 basis points in short-term rates applied to the average fixed/floating mix and level of borrowings would vary the interest cost to the Group by £7m (2014 £6m).

In respect of cash deposits, given the fluctuation in the Group's working capital requirements, cash is generally invested for short-term periods based at floating interest rates. A change of 100 basis points in the average interest rates during the year applied to the average cash deposits would vary the interest receivable by £7m (2014 £9m).

#### Liquidity risk

##### Contractual cash flows on financial liabilities

The contracted cash flows on loans and overdrafts, and derivative financial instruments at the reporting date are shown below, classified by maturity. The cash flows are shown on a gross basis, are not discounted and include estimated interest payments where applicable.

	31 December 2015					31 December 2014				
	Carrying amount £m	Contracted cash flow				Carrying amount £m	Contracted cash flow			
		Less than one year £m	Between one and five years £m	More than five years £m	Total £m		Less than one year £m	Between one and five years £m	More than five years £m	Total £m
<b>Loans and overdrafts</b>	<b>(4,012)</b>	<b>(431)</b>	<b>(1,698)</b>	<b>(3,939)</b>	<b>(6,068)</b>	(3,350)	(655)	(1,420)	(2,926)	(5,001)
(Sale)/purchase contracts:										
US dollar		(299)	(217)	50	(466)		(39)	(41)	71	(9)
Euro		814	238	27	1,079		707	761	47	1,515
Sterling		(555)	(89)	(77)	(721)		(696)	(696)	(118)	(1,510)
Other		35	55	–	90		24	(27)	–	(3)
<b>Cash flow hedges – foreign exchange contracts</b>	<b>(96)</b>	<b>(5)</b>	<b>(13)</b>	<b>–</b>	<b>(18)</b>	(107)	(4)	(3)	–	(7)
Purchase/(sale) contracts:										
US dollar		2,133	(4)	–	2,129		1,399	(9)	–	1,390
Euro		441	–	–	441		507	–	–	507
Sterling		(2,672)	4	–	(2,668)		(2,044)	9	–	(2,035)
Other		98	–	–	98		138	–	–	138
Interest rate contracts		3	(1)	–	2		4	(4)	–	–
<b>Other foreign exchange/interest rate contracts</b>	<b>53</b>	<b>3</b>	<b>(1)</b>	<b>–</b>	<b>2</b>	(5)	4	(4)	–	–
<b>Debt-related derivative financial instruments</b>	<b>53</b>	<b>6</b>	<b>11</b>	<b>55</b>	<b>72</b>	10	6	2	23	31
<b>Other financial assets and liabilities</b>	<b>10</b>	<b>4</b>	<b>(3)</b>	<b>55</b>	<b>56</b>	(102)	6	(5)	23	24

Contractual cash flows in respect of all other financial liabilities are equal to the balance sheet carrying amount. Current contractual amounts relating to other financial liabilities, such as trade payables, are settled within the normal operating cycle of the business.

## 27. Financial risk management continued

### Borrowing facilities

The Group's objective is to maintain adequate undrawn committed borrowing facilities.

At 31 December 2015, the Group had a committed Revolving Credit Facility (RCF) of £2bn (2014 £2bn). The RCF is contracted until 2018 at £2bn and from 2018 to 2020 at £1.9bn. The RCF was undrawn throughout the year. The RCF also acts as a back stop to Commercial Paper issued by the Group. At 31 December 2015, the Group had no Commercial Paper in issue (2014 £nil).

### Cash management

Cash flow forecasting is performed by the businesses on a monthly basis. The Group monitors a rolling forecast of its liquidity requirements to ensure that there is sufficient cash to meet operational needs and maintain adequate headroom.

Surplus cash held by the businesses over and above balances required for working capital management is loaned to the Group's centralised treasury department. Surplus cash is invested in interest bearing current accounts, term deposits, money market deposits and marketable securities, choosing instruments with appropriate maturities or sufficient liquidity to provide sufficient headroom as determined by cash forecasts.

The Group's objective is to monitor and control counterparty credit risk and credit limit utilisation. The Group adopts a conservative approach to the investment of its surplus cash. It is deposited with financial institutions with the strongest credit ratings for short periods. The cash and cash equivalents balance at 31 December 2015 of £2,537m (2014 £2,308m) was invested with 35 (2014 30) financial institutions. A credit limit is allocated to each institution taking account of its market capitalisation, credit rating and credit default swap price.

The cash and cash equivalents of the Group are invested in non-speculative financial instruments which are usually highly liquid, such as short-term deposits. The Group, therefore, believes it has reduced its exposure to counterparty credit risk through this process.

### Currency risk

The Group's objective is to reduce its exposure to transactional volatility in earnings and cash flows from movements in foreign currency exchange rates, mainly the US dollar, Euro, Saudi Riyal and Australian dollar.

The Group is exposed to movements in foreign currency exchange rates in respect of foreign currency denominated transactions. All material firm transactional exposures are hedged and the Group aims, where possible, to apply hedge accounting to these transactions.

The Group is exposed to movements in foreign currency exchange rates in respect of the translation of net assets and income statements of foreign subsidiaries and equity accounted investments. The Group does not hedge the translation effect of exchange rate movements on the income statements or balance sheets of foreign subsidiaries and equity accounted investments it regards as long-term investments.

### Credit risk

The Group has material receivables due from the UK, US and Saudi Arabian governments where credit risk is not considered an issue. For the remaining trade receivables, a provision for bad debts has been calculated taking into account individual assessments based on past credit history and prior knowledge of debtor insolvency or other credit risk, and no one counterparty constitutes more than 12% of the balance (2014 7%).

The ageing of trade receivables is detailed below:

	2015			2014		
	Gross £m	Provision £m	Net £m	Gross £m	Provision £m	Net £m
Not past due and not impaired	807	–	807	611	–	611
Up to 180 days overdue and not impaired	376	–	376	266	–	266
Past 180 days overdue and not impaired	101	–	101	58	–	58
Past 180 days overdue and impaired	25	(25)	–	28	(28)	–
	<b>1,309</b>	<b>(25)</b>	<b>1,284</b>	963	(28)	935

Movements on the provision for bad debts are as follows:

	2015 £m	2014 £m
At 1 January	28	27
Created	8	15
Utilised	(3)	(4)
Released	(9)	(11)
Foreign exchange adjustments	1	1
<b>At 31 December</b>	<b>25</b>	<b>28</b>

# Notes to the Group accounts

## continued

### 28. Share-based payments

The Group has granted equity-settled share options and Long-Term Incentive Plan (LTIP) arrangements, and cash-settled share appreciation rights to employees.

Equity-settled share options and LTIP 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 Group's estimate of the number of shares that will actually vest.

Cash-settled share options are measured at fair value at the balance sheet date. The Group recognises a liability at the balance sheet date based on these fair values, and taking into account the estimated number that will actually vest and the relative completion of the vesting period. Changes in the value of this liability are recognised in the income statement for the year.

Details of the terms and conditions of each share-based payment plan are given in the Annual remuneration report on pages 73 to 86.

#### Expense in year

	2015	2014
	Equity-settled £m	Equity-settled £m
Executive Share Option Plan	6	4
Performance Share Plan	6	5
Restricted Share Plan	4	5
	<b>16</b>	<b>14</b>

The Group also incurred a charge of £28m (2014 £28m) in respect of the equity-settled all-employee free shares and matching Partnership Shares elements of the Share Incentive Plan.

#### Executive Share Option Plan

	2015		2014	
	Number of shares '000	Weighted average exercise price £	Number of shares '000	Weighted average exercise price £
<b>Equity-settled options</b>				
Outstanding at the beginning of the year	35,594	3.70	30,959	3.52
Granted during the year	9,349	5.25	10,578	4.12
Exercised during the year	(9,838)	3.38	(1,644)	3.07
Expired during the year	(2,940)	3.52	(4,299)	3.71
Outstanding at the end of the year	32,165	4.26	35,594	3.70
Exercisable at the end of the year	4,307	3.30	3,633	4.30
<b>Cash-settled share appreciation rights</b>				
Outstanding at the beginning of the year	694	2.69	1,802	2.38
Exercised during the year	(678)	2.69	(1,078)	2.19
Expired during the year	(16)	2.71	(30)	2.07
Outstanding at the end of the year	–	–	694	2.69
Exercisable at the end of the year	–	–	694	2.69

	2015		2014	
	Equity-settled	Cash-settled	Equity-settled	Cash-settled
Range of exercise price of outstanding options (£)	3.01 – 5.43	–	2.64 – 4.79	2.64 – 3.56
Weighted average remaining contracted life (years)	8	–	8	–
Weighted average fair value of options granted (£)	0.76	–	0.64	–

**28. Share-based payments** continued**Performance Share Plan, Share Matching Plan and Restricted Share Plan**

	Performance Share Plan		Share Matching Plan		Restricted Share Plan	
	2015 Number of shares '000	2014 Number of shares '000	2015 Number of shares '000	2014 Number of shares '000	2015 Number of shares '000	2014 Number of shares '000
Outstanding at the beginning of the year	18,868	21,693	5,618	11,201	3,760	6,070
Granted during the year	7,167	8,678	–	–	1,218	1,205
Exercised during the year	(335)	(637)	–	–	(1,876)	(2,872)
Expired during the year	(6,038)	(10,866)	(3,366)	(5,583)	(255)	(643)
Outstanding at the end of the year	19,662	18,868	2,252	5,618	2,847	3,760
Exercisable at the end of the year	204	266	–	–	–	–
	2015	2014	2015	2014	2015	2014
Weighted average remaining contracted life (years)	5	5	–	1	5	5
Weighted average fair value of awards granted (£)	4.49	3.01	–	–	5.12	4.12

All awards are equity-settled.

The exercise price for the Performance Share Plan and Restricted Share Plan is £nil (2014 £nil).

**Details of options/awards granted in the year**

The fair value of equity-settled options/awards granted in the year has been measured using the weighted average inputs below and the following valuation models:

- Executive Share Option Plan – Binomial model
- Performance Share Plan – Monte Carlo
- Restricted Share Plan – Dividend valuation model

	2015	2014
Range of share price at date of grant (£)	4.38 – 5.43	4.12 – 4.51
Expected option/award life (years)	3 – 10	3 – 10
Volatility (%)	20 – 21	21 – 24
Risk free interest rate (%)	0.5 – 0.9	1.0 – 1.2

Volatility was calculated with reference to the Group's weekly share price volatility, after allowing for dividends and stock splits, for the greater of 30 weeks or for the period until vest date.

The average share price in the year was £4.87 (2014 £4.33).

# Notes to the Group accounts

## continued

### 29. Related party transactions

The Group has a related party relationship with its directors and key management personnel (see below), equity accounted investments (note 11) and pension schemes (note 20).

Transactions occur with the equity accounted investments in the normal course of business, are priced on an arm's-length basis and settled on normal trade terms. The more significant transactions are disclosed below:

Related party	Sales to related party		Purchases from related party		Amounts owed by related party		Amounts owed to related party <sup>1</sup>		Management recharges <sup>1</sup>	
	2015 £m	2014 £m	2015 £m	2014 £m	2015 £m	2014 £m	2015 £m	2014 £m	2015 £m	2014 £m
Advanced Electronics Company Limited	22	9	46	56	–	–	–	–	–	–
CTA International SAS	15	3	–	–	11	2	–	–	–	–
Eurofighter Jagdflugzeug GmbH	1,417	1,087	–	11	37	64	65	77	–	–
FADEC International LLC	72	74	–	–	–	–	–	–	–	–
Gripen International KB	–	–	–	–	19	15	14	14	–	–
MBDA SAS	23	22	286	90	6	6	367	403	17	17
Panavia Aircraft GmbH	53	34	47	44	2	5	–	–	–	–
Saudi Development and Training Company Limited (SDT) <sup>2</sup>	n/a	–	n/a	8	n/a	n/a	n/a	n/a	n/a	–
	<b>1,602</b>	<b>1,229</b>	<b>379</b>	<b>209</b>	<b>75</b>	<b>92</b>	<b>446</b>	<b>494</b>	<b>17</b>	<b>17</b>

1. Also relates to disclosures under IAS 24, Related Party Disclosures, for the parent company, BAE Systems plc. At 31 December 2015, £405m (2014 £453m) was owed by BAE Systems plc and £41m (2014 £41m) by other Group subsidiaries.
2. For the period from 1 January 2014 to 15 September 2014 when the Group accounted for its share of the results of SDT under the equity method, in accordance with IAS 28, Investments in Associates and Joint Ventures (revised 2011).

The Group considers key management personnel as defined under IAS 24, Related Party Disclosures, to be the members of the Group's Executive Committee and the Company's non-executive directors. Fuller disclosures on directors' remuneration are set out in the Annual remuneration report on pages 73 to 86. Total emoluments for directors and key management personnel charged to the Consolidated income statement were:

	2015 £'000	2014 £'000
Short-term employee benefits	14,831	14,383
Post-employment benefits	2,021	1,678
Termination benefits	–	1,702
Share-based payments	4,144	3,320
	<b>20,996</b>	<b>21,083</b>

### 30. Contingent liabilities and commitments

#### Guarantees and performance bonds

The Group has entered into a number of guarantee and performance bond arrangements in the normal course of business and regards these as insurance contracts. Provision is made for any amounts that the directors consider may become payable under such arrangements.

#### Operating lease commitments – where the Group is the lessee

The Group leases various offices, factories and shipyards under non-cancellable operating lease agreements. 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.

The future aggregate minimum lease payments under non-cancellable operating leases and associated future minimum sublease income are as follows:

	2015 £m	2014 £m
Payments due:		
Not later than one year	222	213
Later than one year and not later than five years	710	678
Later than five years	779	810
	<b>1,711</b>	<b>1,701</b>
Total of future minimum sublease income under non-cancellable subleases	<b>139</b>	<b>159</b>

#### Capital commitments

Capital expenditure contracted for but not provided for in the accounts is as follows:

	2015 £m	2014 £m
Property, plant and equipment <sup>1</sup>	264	142
Intangible assets	8	3
	<b>272</b>	<b>145</b>

1. Includes £99m (2014 £nil) at Barrow-in-Furness, UK, relating to the Successor submarine programme funded by the UK government.

# Notes to the Group accounts

## continued

### 31. Information about related undertakings

In accordance with Section 409 of the Companies Act 2006, a full list of subsidiaries and equity accounted investments as at 31 December 2015 is disclosed below. Unless otherwise stated, the Group's shareholding represents ordinary shares held indirectly by BAE Systems plc, the year end is 31 December and the address of the registered office is Warwick House, PO Box 87, Farnborough Aerospace Centre, Farnborough, Hampshire GU14 6YU, United Kingdom. No subsidiary undertakings have been excluded from the consolidation.

#### Subsidiaries – wholly-owned

4219 Lafayette, LLC <sup>21</sup> 4219-120 Lafayette Center Drive, Chantilly VA 20151, United States	BAE Systems (Moose Jaw) Inc. <sup>15</sup> LeBlanc Nichols, The Chambers, 1000-300 Terry Fox Drive, Ottawa ON K2K 0E3, Canada	BAE Systems Applied Intelligence France SAS 112 Avenue Kleber, 75016, Paris, France
Aerosystems International Limited Lupin Way, Alvington, Yeovil, Somerset BA22 8UZ, United Kingdom	BAE Systems (Nominees) Limited <sup>1</sup>	BAE Systems Applied Intelligence Limited Surrey Research Park, Guildford, Surrey GU2 7YP, United Kingdom
Alabama Dry Dock and Shipbuilding, LLC <sup>21</sup> PO Box 3202, Main Gate, Dunlap Drive, Mobile AL 36652, United States	BAE Systems (Oman) Limited	BAE Systems Applied Intelligence LLC <sup>21</sup> 8200 Greensboro Drive, 9th Floor, McLean VA 22102, United States
Alvis Pension Scheme Trustees Limited	BAE Systems (Operations) Limited <sup>10</sup>	BAE Systems Applied Intelligence New Zealand Limited c/o Russell McVeagh, Vero Centre, 48 Shortland Street, Auckland Central, 1140, New Zealand
Alvis Limited	BAE Systems (Operations) Singapore Pte Limited One Marina Boulevard #28-00, Singapore 018989, Singapore	BAE Systems Applied Intelligence Pty Limited Level 12, 16-20 Bridge Street, Sydney NSW 2000, Australia
Alvis Vickers Limited	BAE Systems (Overseas Holdings) Limited	BAE Systems Applied Intelligence US Corp <sup>5</sup> 440 Wheelers Farms Road, Suite 202, Milford CT 06461, United States
Armor Holdings Inc. <sup>6</sup> 2000 North 15th Street, 11th Floor, Arlington VA 22201, United States	BAE Systems (Poland) Sp. z o.o. ul. Abp. A. Baraniaka 88, 61-131 Poznan, Poland	BAE Systems Australia Datagate Pty Limited Evans Building, Taranaki Road, Edinburgh Parks, Edinburgh SA 5111, Australia
Armstrong Whitworth Aircraft Limited <sup>1</sup>	BAE Systems (Projects) Limited	BAE Systems Australia Defence Holdings Pty Limited Evans Building, Taranaki Road, Edinburgh Parks, Edinburgh SA 5111, Australia
Atlantic-Alabama Holding Company, LLC <sup>21</sup> PO Box 3202, Main Gate, Dunlap Drive, Mobile AL 36652, United States	BAE Systems (Property Investments) Limited	BAE Systems Australia Defence Pty Limited <sup>14</sup> Evans Building, Taranaki Road, Edinburgh Parks, Edinburgh SA 5111, Australia
Australian Marine Engineering Corporation (Finance) Pty Limited Evans Building, Taranaki Road, Edinburgh Parks, Edinburgh SA 5111, Australia	BAE Systems (Stanmore) Limited <sup>15</sup> 15 Canada Square, London E14 5GL, United Kingdom	BAE Systems Australia (Electronic Systems) Pty Limited Evans Building, Taranaki Road, Edinburgh Parks, Edinburgh SA 5111, Australia
Avro International Aerospace Limited <sup>1</sup>	BAE Systems (Sweden) AB <sup>16</sup> c/o Advokatfirman DLA Nordic KB, Box 7315, SE-103 90 Stockholm, Sweden	BAE Systems Australia (NSW) Holdings Pty Limited Evans Building, Taranaki Road, Edinburgh Parks, Edinburgh SA 5111, Australia
BAE Systems (Aberdeen) Limited <sup>13,15</sup> Saltire Court, 20 Castle Terrace, Edinburgh EH1 2EG, United Kingdom	BAE Systems (Vehicles and Equipment) Limited	BAE Systems Australia (NSW) Pty Limited Evans Building, Taranaki Road, Edinburgh Parks, Edinburgh SA 5111, Australia
BAE Systems (AI Diriyah C4i) Limited <sup>1</sup>	BAE Systems 2000 Pension Plan Trustees Limited <sup>1</sup>	BAE Systems Australia (Singapore) Pte Limited <sup>19</sup> c/o Koh Choo Services Pte Ltd, 150 Cecil Street #15-01, Singapore 069543, Singapore
BAE Systems (Aviation Services) Limited	BAE Systems AB <sup>13</sup> Box 5676, SE-114 86 Stockholm, Sweden	BAE Systems Australia Holdings Limited <sup>1</sup> Evans Building, Taranaki Road, Edinburgh Parks, Edinburgh SA 5111, Australia
BAE Systems (Bristol House) Limited <sup>1,11,15</sup> 15 Canada Square, London E14 5GL, United Kingdom	BAE Systems AI Diriyah Programme Limited <sup>1</sup>	BAE Systems Australia Limited Evans Building, Taranaki Road, Edinburgh Parks, Edinburgh SA 5111, Australia
BAE Systems (Canada) Inc. 220 Laurier Avenue West, Suite 1200, Ottawa ON K1P 5Z9, Canada	BAE Systems Applied Intelligence (Asia Pacific) Pte Limited United Square, 101 Thomson Road, #25-03/04, 307591, Singapore	BAE Systems Australia Logistics Pty Limited <sup>10</sup> Evans Building, Taranaki Road, Edinburgh Parks, Edinburgh SA 5111, Australia
BAE Systems (Combat and Radar Systems) Limited PO Box 727, St. Paul's Gate, New Street, St. Helier JE4 8ZB, Jersey	BAE Systems Applied Intelligence (Australia) Pty Limited Level 12, 16-20 Bridge Street, Sydney NSW 2000, Australia	BAE Systems Australia Sea Sentinel Project Pty Limited Evans Building, Taranaki Road, Edinburgh Parks, Edinburgh SA 5111, Australia
BAE Systems (Consultancy Services) Limited	BAE Systems Applied Intelligence (Belgium) NV Geldenaaksebaan 329, B-3001, Heverlee, Leuven, Belgium	BAE Systems Avionics Overseas Limited <sup>15</sup> 15 Canada Square, London E14 5GL, United Kingdom
BAE Systems (Corporate Air Travel) Limited	BAE Systems Applied Intelligence Canada Inc. 1959 Upper Water Street, Suite 900, Halifax NS B3J 2X2, Canada	BAE Systems Avionics Singapore Pte Limited One Marina Boulevard, #28-00, Singapore 018989, Singapore
BAE Systems (CS&SI – Qatar) Limited <sup>1</sup>	BAE Systems Applied Intelligence (Connect) A/S Bouet Mollevej 3-5, 9400 Norresundby, Denmark	BAE Systems Bofors AB SE-691 80 Karlskoga, Sweden
BAE Systems (Defence Systems) Limited	BAE Systems Applied Intelligence Inc. <sup>5</sup> 5th Floor, Suite 1920, 256 Franklin Street, Boston MA 02110, United States	BAE Systems Bofors Holdings Sdn Bhd Level 21, Suite 21.01, The Gardens South Tower, Mid Valley City, Lingkaran Syed Putra, 59200 Kuala Lumpur, Malaysia
BAE Systems (Dynamics) Limited	BAE Systems Applied Intelligence GCS Inc. <sup>6</sup> 1676 International Drive, 10th Floor, Suite 1000, McLean VA 22102, United States	BAE Systems Capital Limited <sup>1</sup> PO Box 727, St. Paul's Gate, New Street, St. Helier JE4 8ZB, Jersey
BAE Systems (Farnborough 1) Limited	BAE Systems Applied Intelligence (GCS) Limited Surrey Research Park, Guildford, Surrey GU2 7YP, United Kingdom	BAE Systems China (Exports) Limited
BAE Systems (Farnborough 2) Limited	BAE Systems Applied Intelligence (Integration) Limited Surrey Research Park, Guildford, Surrey GU2 7YP, United Kingdom	BAE Systems C-ITS AB Box 5676, SE-114 86 Stockholm, Sweden
BAE Systems (Farnborough 3) Limited	BAE Systems Applied Intelligence (International) Limited Priestley Road, Surrey Research Park, Guildford, Surrey GU2 7YP, United Kingdom	BAE Systems Command and Control Limited <sup>10,15</sup> 15 Canada Square, London E14 5GL, United Kingdom
BAE Systems (Finance) Limited	BAE Systems Applied Intelligence (Ireland) Limited Level 5, Block 4, Dundrum Town Centre, Sandyford Road, Dundrum, Dublin 16, D16 A4W6, Ireland	BAE Systems Communications Limited <sup>1</sup>
BAE Systems (Funding Two) Limited	BAE Systems Applied Intelligence (Luxembourg) SARL 1 Boulevard de la Foire, L-1528 Luxembourg, Luxembourg	BAE Systems Communications Solutions, LLC <sup>21</sup> PO Box 111, Knowledge Oasis Muscat, Building 4, 2nd Floor, Muscat, Oman
BAE Systems (Funding Three) Limited	BAE Systems Applied Intelligence (Malaysia) Sdn Bhd 16th Floor, Wisma Sime Darby, Jalan Raja Laut, 50350 Kuala Lumpur, Malaysia	
BAE Systems (Gripen Overseas) Limited	BAE Systems Applied Intelligence (Spain) S.A. Paseo de la Castellana, 141, Cuzco IV, 28046 Madrid, Spain	
BAE Systems (Hawk Synthetic Training) Limited	BAE Systems Applied Intelligence (UK) Limited	
BAE Systems (Holdings) Limited <sup>1</sup>	BAE Systems Applied Intelligence A/S Bouet Mollevej 3, 9400 Norresundby, Denmark	
BAE Systems (Insurance) Limited		
BAE Systems (International) Limited		
BAE Systems (Jersey) Limited <sup>1</sup> PO Box 727, St. Paul's Gate, New Street, St. Helier JE4 8ZB, Jersey		
BAE Systems (Kazakhstan) Limited		
BAE Systems (Land and Sea Systems) Limited <sup>11</sup>		
BAE Systems (Malaysia) Sdn Bhd 16th Floor, Wisma Sime Darby, Jalan Raja Laut, 50350 Kuala Lumpur, Malaysia		
BAE Systems (MEH) Limited		
BAE Systems (Military Air) Overseas Limited		

## 31. Information about related undertakings continued

### Subsidiaries – wholly-owned continued

BAE Systems Controls Inc. <sup>5</sup> 1098 Clark Street, Endicott NY 13760, United States	BAE Systems InFlight Systems (Overseas) Limited <sup>15</sup> 15 Canada Square, London E14 5GL, United Kingdom	BAE Systems Protection Systems Inc. <sup>7</sup> 7822 South 46th Street, Phoenix AZ 85044, United States
BAE Systems Creole Inc. <sup>7</sup> 3701 Outlet Ctr. Drive, Suite 15, Sealy TX 77474-4904, United States	BAE Systems Information and Electronic Systems Integration Inc. <sup>6</sup> 65 Spit Brook Road, Nashua NH 03061, United States	BAE Systems Quest Limited <sup>1</sup>
BAE Systems Datagate Limited	BAE Systems Information Solutions Inc. <sup>6</sup> 8201 Greensboro Drive, McLean VA 22102, United States	BAE Systems Regional Aircraft (Japan) KK <sup>6</sup> Minami Azabu T&F Building 8th Floor, 4-11-22 Minami Azabu, Minato-ku, Tokyo, Japan
BAE Systems Datagate Holdings Limited	BAE Systems (Isle of Man) Limited Tower House, Loch Promenade, Douglas, IM1 2LZ, Isle of Man, United Kingdom	BAE Systems Regional Aircraft Colombia SAS c/o Brigard & Urrutia, Calle 70 A No. 4-41, Bogota, Colombia
BAE Systems Defence Limited <sup>1</sup>	BAE Systems Insyte Limited <sup>15</sup> 15 Canada Square, London E14 5GL, United Kingdom	BAE Systems Resolution Inc. <sup>7</sup> 3701 Outlet Ctr. Drive, Suite 15, Sealy TX 77474-4904, United States
BAE Systems Deployed Systems Limited <sup>2</sup>	BAE Systems Integrated System Technologies (KSA) Limited	BAE Systems RO Defense Inc. <sup>6</sup> 1801 Electronics Drive, Anniston AL 36207, United States
BAE Systems Detica GmbH Pfungstweidstrasse 3, 60316 Frankfurt am Main, Germany	BAE Systems Integrated System Technologies (Overseas) Limited	BAE Systems Rokar International Limited PO Box 45059, 11 Hartom Street, Mount Hotzvim, 91450 Jerusalem, Israel
BAE Systems Display Technologies Limited	BAE Systems Integrated System Technologies GmbH Hans-StieBberger-Str. 2b, 85540 Haar, Germany	BAE Systems S&S Holdings Inc. <sup>7</sup> 3701 Outlet Ctr. Drive, Suite 15, Sealy TX 77474-4904, United States
BAE Systems do Brasil Ltda SCN Quadra 5 Bloco A, Ed. Brasilia Shopping, Torre Norte, Sala 426, Brasilia, DF CEP:70715-900, Brazil	BAE Systems Integrated System Technologies Limited	BAE Systems S&S Operations Inc. <sup>6</sup> 3701 Outlet Ctr. Drive, Suite 15, Sealy TX 77474-4904, United States
BAE Systems Electronic Systems (Overseas) Limited	BAE Systems International Inc. <sup>5</sup> 1101 Wilson Blvd, Ste 2000, Arlington VA 22209, United States	BAE Systems San Diego Ship Repair Inc. <sup>6</sup> 2205 East Belt Street, Foot of Sampson Street, San Diego CA 92113, United States
BAE Systems Electronics Limited	BAE Systems Land & Armaments Holdings Inc. <sup>6</sup> 2000 North 15th Street, 11th Floor, Arlington VA 22201, United States	BAE Systems San Francisco Ship Repair Inc. <sup>6</sup> Foot of 20th Street at Illinois Street, San Francisco CA 94107-7644, United States
BAE Systems Enterprises Limited	BAE Systems Land & Armaments Inc. <sup>6</sup> 2000 North 15th Street, 11th Floor, Arlington VA 22201, United States	BAE Systems Saudi Limited PO Box 1732, Riyadh 11441, Saudi Arabia
BAE Systems Executive Pension Scheme Trustees Limited <sup>1</sup>	BAE Systems Land & Armaments L.P. <sup>21</sup> 2000 North 15th Street, 11th Floor, Arlington VA 22201, United States	BAE Systems Saudi Arabia (Maintenance and Equipment Services) Limited PO Box 1732, Riyadh 11441, Saudi Arabia
BAE Systems Finance (Ireland) <sup>22</sup> Level 5, Block 4, Dundrum Town Centre, Sandyford Road, Dundrum, Dublin 16, D16 A4W6, Ireland	BAE Systems Land Systems ATF Limited	BAE Systems Saudi Arabia (Vehicles and Equipment Holdings) Limited <sup>1</sup>
BAE Systems Finance B.V. c/o SGG Netherlands N.V., Hoogoorddreef 15, 1101 BA Amsterdam, Netherlands	BAE Systems Land Systems (Finance) Limited	BAE Systems Saudi Arabia (Vehicles and Equipment Nominees) Limited <sup>1</sup>
BAE Systems Finance Inc. <sup>6</sup> 45479 Holiday Drive, Sterling VA 20166, United States	BAE Systems Land Systems FMTV International Inc. <sup>7</sup> 1101 Wilson Blvd, Ste 2000, Arlington VA 22209, United States	BAE Systems Shared Services Inc. <sup>6</sup> 11215 Rushmore Drive, Charlotte NC 28277, United States
BAE Systems Flight Training (Australia) Pty Limited <sup>10</sup> Evans Building, Taranaki Road, Edinburgh Parks, Edinburgh SA 5111, Australia	BAE Systems Land Systems (Investments AVG) Limited <sup>15</sup> 15 Canada Square, London E14 5GL, United Kingdom	BAE Systems Shared Services (Overseas) Limited
BAE Systems Funds Management <sup>1,22</sup>	BAE Systems Land Systems (Investments South Africa) Limited	BAE Systems Share Plans Trustee Limited <sup>1</sup>
BAE Systems Global Combat Systems Bridging Limited	BAE Systems Land Systems (Investments) Limited	BAE Systems Ship Repair Inc. <sup>6</sup> 750 West Berkley Ave., Norfolk VA 23523, United States
BAE Systems Global Combat Systems Limited	BAE Systems Land Systems (Logistics) Limited	BAE Systems Southeast Shipyards Alabama LLC <sup>21</sup> PO Box 3202, Main Gate, Dunlap Drive, Mobile AL 36652, United States
BAE Systems Global Combat Systems Munitions Limited	BAE Systems Land Systems (Pinzgauer) Limited	BAE Systems Southeast Shipyards AMHC Inc. <sup>6,21</sup> 8500 Heckscher Drive, Jacksonville FL 32226, United States
BAE Systems Global Mobility LLC <sup>21</sup> 1300 Wilson Blvd., Arlington VA 22209, United States	BAE Systems Land Systems (Pinzgauer (Holdings) Limited	BAE Systems Southeast Shipyards Jacksonville LLC <sup>21</sup> 8500 Heckscher Drive, Jacksonville FL 32226, United States
BAE Systems Global Tactical Systems LLC <sup>21</sup> 3701 Outlet Ctr. Drive, Suite 15, Sealy TX 77474-4904, United States	BAE Systems Land Systems (Ranges) Limited	BAE Systems Southeast Shipyards Mayport LLC <sup>21</sup> 8500 Heckscher Drive, Jacksonville FL 32226, United States
BAE Systems Högglunds AB SE-691 80, Karlskoga, Sweden	BAE Systems Land Systems (Singapore Investments) Limited	BAE Systems SSY Alabama Property Holdings LLC <sup>21</sup> PO Box 3202, Main Gate, Dunlap Drive, Mobile AL 36652, United States
BAE Systems Hawaii Shipyards Inc. <sup>6</sup> 3049 Ualena Street, Suite 915, Honolulu HI 96819, United States	BAE Systems Logistica Ltda SCN Quadra 5 Bloco A, Ed. Brasilia Shopping, Torre Norte, Sala 426, Brasilia, DF CEP:70715-900, Brazil	BAE Systems SSY Floating Dry Dock Holdings LLC <sup>21</sup> 8500 Heckscher Drive, Jacksonville FL 32226, United States
BAE Systems Holdings (South Africa) (Pty) Limited Central Office Park No. 5, 257 Jean Avenue, Centurion, Gauteng, 0157, South Africa	BAE Systems Marine (Holdings) Limited	BAE Systems SSY Florida Property Holdings LLC <sup>21</sup> 8500 Heckscher Drive, Jacksonville FL 32226, United States
BAE Systems Holdings B.V. c/o SGG Netherlands N.V., Hoogoorddreef 15, 1101 BA Amsterdam, Netherlands	BAE Systems Marine (YSL) Limited	BAE Systems Surface Ships (Holdings) Limited
BAE Systems Holdings Germany GmbH <sup>7</sup> c/o Heuking Kühn Lüer Wojtek, Neuer Wall 63, 20354 Hamburg, Germany	BAE Systems Marine Limited	BAE Systems Surface Ships Limited
BAE Systems Holding GmbH Hauptstrasse 48, 82433 Bad Kohlgrub, Germany	BAE Systems Maritime Engineering & Services Inc. <sup>6</sup> 7330 Engineer Road, Suite A, San Diego CA 92111, United States	BAE Systems Surface Ships (Projects) Limited
BAE Systems Holdings Inc. <sup>5</sup> 1101 Wilson Blvd, Ste 2000, Arlington VA 22209, United States	BAE Systems Norfolk Ship Repair Inc. <sup>6</sup> 750 West Berkley Avenue, Norfolk VA 23523, United States	BAE Systems Surface Ships Intermediate Holdings Limited
BAE Systems Holdings International LLC <sup>21</sup> 1101 Wilson Blvd, Ste 2000, Arlington VA 22209, United States	BAE Systems Oman LLC <sup>21</sup> PO Box 74, Postal Code 111, Seeb, Oman	BAE Systems Surface Ships Integrated Support Limited
BAE Systems Imaging Solutions Inc. <sup>5</sup> 1841 Zanker Road, Suite 50, San Jose CA 95112, United States	BAE Systems Ordnance Systems Inc. <sup>6</sup> 4509 West Stone Drive, Kingsport TN 37660-9982, United States	BAE Systems Surface Ships International Limited <sup>13</sup>
BAE Systems, Inc. <sup>6</sup> 1101 Wilson Blvd, Ste 2000, Arlington VA 22209, United States	BAE Systems Overseas Inc. <sup>6</sup> 1101 Wilson Blvd, Ste 2000, Arlington VA 22209, United States	BAE Systems Surface Ships Maritime Limited
BAE Systems India (Services) Private Limited <sup>17</sup> 2nd Floor, Hotel Le-Meridien Commercial Tower, Raisina Road, New Delhi 110001, India	BAE Systems PAMCO Services International Inc. <sup>7</sup> 3701 Outlet Ctr. Drive, Suite 15, Sealy TX 77474-4904, United States	BAE Systems Surface Ships Portsmouth Limited <sup>13</sup>
BAE Systems India (Homeland Security) Private Limited <sup>17</sup> 2nd Floor, Hotel Le-Meridien Commercial Tower, Raisina Road, New Delhi 110001, India	BAE Systems Pension Funds CIF Trustees Limited <sup>1</sup>	BAE Systems Surface Ships Projects (Malaysia) Sdn Bhd Level 14, West Block, Wisma Selangor Dredging, 142-C, Jalan Ampang, 50450 Kuala Lumpur, Malaysia
BAE Systems India (Technology) Private Limited <sup>17</sup> 2nd Floor, Hotel Le-Meridien Commercial Tower, Raisina Road, New Delhi 110001, India	BAE Systems Pension Funds Investment Management Limited <sup>1,18</sup>	BAE Systems Surface Ships Property Services Limited
BAE Systems India (Ventures) Private Limited <sup>17</sup> 2nd Floor, Hotel Le-Meridien Commercial Tower, Raisina Road, New Delhi 110001, India	BAE Systems Pension Funds Trustees Limited <sup>1</sup>	BAE Systems Surface Ships Support Limited <sup>10</sup>
	BAE Systems Project Services Limited	BAE Systems Surface Ships Hellas A.E. <sup>16</sup> 3 Strategiou Tombra Street, Aghia Paraskevi, GR 153 42 Athens, Greece
	BAE Systems Projects (Canada) Limited	
	BAE Systems Properties Limited	



### 31. Information about related undertakings continued

#### Equity accounted investments<sup>23</sup>

**Advanced Electronics Company Limited (50%)**  
PO Box 90916, Riyadh 11623, Saudi Arabia

**Air Astana (49%)<sup>5</sup>**  
Zakarpatskaya Str 4A, 050039 Almaty, Kazakhstan

**AMSH B.V. (50%)<sup>9</sup>**  
Weena 210-212, 3012 NJ Rotterdam, Netherlands

**BAeHAL Software Limited (40%)<sup>1,17</sup>**  
Airport Lane, HAL Estate, Bangalore 560010, India

**BHIC Bofors Defense Asia Sdn Bhd (49%)**  
Suite B, Menara Maxis, Kuala Lumpur City Centre, 50088 Kuala Lumpur, Malaysia

**BAE (Consultancy Services) Malaysia Sdn Bhd (49%)**  
Tkt.11, Wisma Damansara, Damansara Heights, 50490 Kuala Lumpur, Malaysia

**CTA International SAS (50%)**  
13 Route De La Minière, 78000 Versailles, France

**Data Link Solutions L.L.C. (50%)<sup>20,21</sup>**  
400 Collins Ave, Cedar Rapids IA 52498, United States

**Eurofighter Aircraft Management GmbH (33%)<sup>1</sup>**  
Am Soldnermoos 17, 85399 Hallbergmoos, Germany

**Eurofighter International Limited (33%)<sup>1,9</sup>**

**Eurofighter Jagdflugzeug GmbH (33%)<sup>1</sup>**  
Am Soldnermoos 17, 85399 Hallbergmoos, Germany

**European Aerosystems Limited (50%)<sup>1,8</sup>**

**FADEC International LLC (50%)<sup>21</sup>**  
1098 Clark Street, Endicott NY 13760, United States

**FAST Holdings Limited (50%)<sup>8,17</sup>**

**FAST Training Services Limited (50%)<sup>17</sup>**

**FBV Designs Limited (50%)<sup>8,17</sup>**  
33 Wigmore Street, London W1U 1QX, United Kingdom

**FNSS Savunma Sistemleri A.S (49%)<sup>8</sup>**  
PK 37, Golbasi 06830, Ankara, Turkey

**Gripen International KB (50%)<sup>21</sup>**  
SE-581 88 Linköping, Sweden

**MBDA Holdings SAS (25%)**  
1 Avenue Réaumur, 92350 Le Plessis-Robinson, France

**Nobel Business Support AB (34%)**  
SE-691 80 Karlskoga, Sweden

**Nurol BAE Systems Hava Sistemleri Anonim Şirketi (49%)<sup>9</sup>**  
Arjantin Cad. No: 7 06700, Gaziosmanpaşa, Ankara, Turkey

**Panavia Aircraft GmbH (42.5%)<sup>1</sup>**  
Am Soldnermoos 17, 85399 Hallbergmoos, Germany

**Patria Hägglunds Oy (50%)**  
Naulakatu 3, FI-33100 Tampere, Finland

**Saab-BAE Systems Gripen AB (50%)<sup>1</sup>**  
SE-581 88 Linköping, Sweden

**Saab Bofors Test Center AB (30%)**  
SE-691 80 Karlskoga, Sweden

**Sandstone Integrated Operations, LLC (20%)<sup>21</sup>**  
2016 Mt. Athos Road, Lynchburg VA 24504, United States

**Seele-Alvis Fenestration Limited (43.5%)<sup>8,19</sup>**  
Unit A33, Jack's Place, 6 Corbett Place, London E1 6NN, United Kingdom

**SIKA International Limited (50%)<sup>8</sup>**

**Spectrum Technologies Public Limited Company (20%)<sup>1,17</sup>**  
Western Avenue, Bridgend Industrial Estate, Bridgend, Mid Glamorgan CF31 3RT, United Kingdom

**Tirs Mateen & Co LLC (50%)<sup>21</sup>**  
PO Box 3369, Postal Code 111, Seeb, Oman

**Winner Developments Limited (33.3%)**

#### Notes

1. Directly owned by BAE Systems plc.
2. 40% owned by BAE Systems plc.
3. 1% owned by BAE Systems plc.
4. 33.3% owned by BAE Systems plc.
5. Ownership held in common stock.
6. Ownership held in common shares.
7. Ownership held in authorized shares.
8. Ownership held in class of A shares.
9. Ownership held in class of B shares.
10. Ownership held in class of A shares and B shares.
11. Ownership held in class of A shares, B shares and preference shares.
12. Ownership held in ordinary shares and class of A shares.
13. Ownership held in ordinary shares and preference shares.
14. Ownership held in ordinary shares and redeemable preference shares.
15. In members' voluntary liquidation.
16. In liquidation.
17. Year end 31 March.
18. Year end 5 April.
19. Year end 30 June.
20. Year end 30 September.
21. Unincorporated entity for which the address given is the principal place of business.
22. Unlimited company.
23. For companies incorporated outside of the United Kingdom, the country of incorporation is shown in the address.

## Company statement of comprehensive income for the year ended 31 December

	2015 £m	2014 <sup>1</sup> £m
<b>Profit for the year</b>	<b>94</b>	1,193
<b>Other comprehensive income</b>		
<b>Items that will not be reclassified to the income statement:</b>		
Remeasurements on retirement benefit schemes	14	(59)
<b>Items that may be reclassified to the income statement:</b>		
Amounts credited to hedging reserve	7	10
<b>Total other comprehensive income for the year (net of tax)</b>	<b>21</b>	(49)
<b>Total comprehensive income for the year</b>	<b>115</b>	1,144

1. Restated on adoption of Financial Reporting Standard (FRS) 101, Reduced Disclosure Framework.

## Company statement of changes in equity for the year ended 31 December

	Issued share capital £m	Share premium £m	Other reserves £m	Retained earnings <sup>1</sup> £m	Total equity £m
At 1 January 2014 (as previously reported) <sup>2</sup>	89	1,249	290	2,360	3,988
Effect of transition to FRS 101 (note 12)	–	–	(24)	(179)	(203)
At 1 January 2014 (restated on adoption of FRS 101)	89	1,249	266	2,181	3,785
Profit for the year	–	–	–	1,193	1,193
Total other comprehensive income for the year	–	–	10	(59)	(49)
Share-based payments	–	–	–	37	37
Net purchase of own shares	(2)	–	2	(281)	(281)
Ordinary share dividends	–	–	–	(642)	(642)
At 31 December 2014 (restated on adoption of FRS 101)	87	1,249	278	2,429	4,043
Profit for the year	–	–	–	94	94
Total other comprehensive income for the year	–	–	7	14	21
Share-based payments	–	–	–	39	39
Net sale of own shares	–	–	–	1	1
Ordinary share dividends	–	–	–	(655)	(655)
Non-distributable reserve transfer	–	–	(67)	67	–
<b>At 31 December 2015</b>	<b>87</b>	<b>1,249</b>	<b>218</b>	<b>1,989</b>	<b>3,543</b>

1. The non-distributable portion of retained earnings is £255m (2014 £196m).

2. Restated for a correction to amounts due to other Group companies, a net increase of £81m to retained earnings.

# Company balance sheet

## as at 31 December

	Notes	2015 £m	2014 <sup>1</sup> £m
<b>Non-current assets</b>			
Intangible assets		31	11
Property, plant and equipment		20	8
Investments in subsidiary undertakings and participating interests	2	8,138	8,169
Other receivables		5	9
Retirement benefit surpluses	8	6	5
Other financial assets	4	151	105
		<b>8,351</b>	<b>8,307</b>
<b>Current assets</b>			
Trade and other receivables	3	3,221	3,225
Current tax		14	32
Other financial assets	4	212	128
Cash and cash equivalents		2,061	1,792
		<b>5,508</b>	<b>5,177</b>
<b>Total assets</b>		<b>13,859</b>	<b>13,484</b>
<b>Non-current liabilities</b>			
Loans	5	(1,005)	(1,197)
Other payables		(5)	(12)
Retirement benefit obligations	8	(259)	(270)
Other financial liabilities	4	(98)	(98)
Provisions	7	(105)	(109)
		<b>(1,472)</b>	<b>(1,686)</b>
<b>Current liabilities</b>			
Loans and overdrafts	5	(237)	(1)
Trade and other payables	6	(8,430)	(7,609)
Other financial liabilities	4	(165)	(134)
Provisions	7	(12)	(11)
		<b>(8,844)</b>	<b>(7,755)</b>
<b>Total liabilities</b>		<b>(10,316)</b>	<b>(9,441)</b>
<b>Net assets</b>		<b>3,543</b>	<b>4,043</b>
<b>Capital and reserves</b>			
Issued share capital		87	87
Share premium		1,249	1,249
Other reserves	9	218	278
Retained earnings		1,989	2,429
<b>Total equity</b>		<b>3,543</b>	<b>4,043</b>

1. Restated on adoption of FRS 101 and for a correction to amounts due to other Group companies.

Approved by the Board on 17 February 2016 and signed on its behalf by:

**I G King**  
Chief Executive

**P J Lynas**  
Group Finance Director

Registered number: 1470151

# Notes to the Company accounts

## 1. Preparation

### Basis of preparation

These financial statements were prepared in accordance with Financial Reporting Standard (FRS) 101, Reduced Disclosure Framework. Amendments to FRS 101 (2013/14 Cycle), issued in July 2014 and effective for periods beginning on or after 1 January 2015, has been applied. Amendments to FRS 101 (2014/15 cycle and other minor amendments), issued in July 2015 and effective for periods beginning on or after 1 January 2016, has been early adopted and applied.

In preparing these financial statements, the Company applies the recognition, measurement and disclosure requirements of International Financial Reporting Standards (IFRS) as adopted by the EU (EU-adopted IFRS), 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 requirements of paragraphs 62, B64(d), B64(e), B64(g), B64(h), B64(j), to B64(m), B64(n)(ii), B64(o)(ii), B64(p), B64(q)(ii), B66 and B67 of IFRS 3, Business Combinations;
- the requirements of paragraph 33(c) of IFRS 5, Non-current Assets Held for Sale and Discontinued Operations;
- the requirements of IFRS 7, Financial Instruments: Disclosures;
- the requirements of paragraphs 91 to 99 of IFRS 13, Fair Value Measurement;
- 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; 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 paragraphs 17 and 18A of IAS 24, Related Party Disclosures;
- the requirements in IAS 24, Related Party Disclosures, to disclose related party transactions entered into between two or more members of a group, provided that any subsidiary which is a party to the transaction is wholly owned by such a member; and
- the requirements of paragraphs 130(f)(ii), 130(f)(iii), 134(d) to 134(f) and 135(c) to 135(e) of IAS 36, Impairment of Assets.

In its transition to FRS 101, the Company has applied IFRS 1, whilst ensuring that its assets and liabilities are measured in compliance with FRS 101. An explanation of how the transition to FRS 101 has affected the Company's reported financial performance and position is provided in note 12 to the Company accounts.

The Company intends to continue to prepare its financial statements in accordance with FRS 101.

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 Group accounts on pages 106 to 165. Accordingly, these financial statements present information about the Company as an individual undertaking and not as a group.

In accordance with Section 408(3) of the Companies Act 2006, the Company is exempt from the requirement to present its own income statement. The amount of profit for the year of the Company is disclosed in the Company statement of comprehensive income.

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).

### Significant accounting policies

The significant accounting policies applied in the preparation of these individual financial statements are set out below. These policies have been applied consistently to all the years presented, unless otherwise stated.

### Investments in subsidiary undertakings and participating interests

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

### Other significant accounting policies

Other significant accounting policies are consistent with the Group accounts and the table below references where they are disclosed.

Significant accounting policy	Page
Loans and overdrafts	137
Pension schemes	139
Provisions	149

## 2. Investments in subsidiary undertakings and participating interests

	£m
<b>Cost</b>	
At 1 January 2015	8,183
Additions	8
Disposals	(39)
<b>At 31 December 2015</b>	<b>8,152</b>
<b>Impairment provisions</b>	
<b>At 1 January and 31 December 2015</b>	<b>14</b>
<b>Net carrying value</b>	
<b>At 31 December 2015</b>	<b>8,138</b>
At 31 December 2014	8,169

## 3. Trade and other receivables

	2015 £m	2014 £m
<b>Current</b>		
Amounts owed by subsidiary undertakings	<b>3,159</b>	3,182
Amounts owed by Group joint ventures	<b>5</b>	5
Prepayments and accrued income	<b>45</b>	23
Other receivables	<b>12</b>	15
	<b>3,221</b>	3,225

## 4. Other financial assets and liabilities

	2015		2014	
	Assets £m	Liabilities £m	Assets £m	Liabilities £m
<b>Non-current</b>				
Cash flow hedges – foreign exchange contracts	<b>8</b>	–	4	–
Other foreign exchange/interest rate contracts	<b>97</b>	<b>(98)</b>	95	(98)
Debt-related derivative financial instruments – assets <sup>1</sup>	<b>46</b>	–	6	–
	<b>151</b>	<b>(98)</b>	105	(98)
<b>Current</b>				
Cash flow hedges – foreign exchange contracts	<b>5</b>	–	2	–
Other foreign exchange/interest rate contracts	<b>207</b>	<b>(165)</b>	126	(134)
	<b>212</b>	<b>(165)</b>	128	(134)

1. Debt-related derivative financial instrument assets are presented as other financial assets. Debt-related derivative financial instrument liabilities are presented as a component of loans and overdrafts (see note 5).

The contractual cash flows on derivative financial instruments at the reporting date are shown below, classified by maturity.

	2015 £m	2014 £m
Less than one year	<b>2</b>	1
Between one and five years	<b>9</b>	3
More than five years	<b>55</b>	23
	<b>66</b>	27

Full disclosures relating to the Group's other financial assets and liabilities, and financial risk management strategies are given in notes 13, 26 and 27 to the Group accounts.

## Notes to the Company accounts continued

### 5. Loans and overdrafts

	2015 £m	2014 £m
<b>Non-current</b>		
US\$350m 3.5% bond, repayable 2016	–	224
US\$500m 4.75% bond, repayable 2021	339	320
£400m 4.125% bond, repayable 2022	398	398
US\$400m 5.8% bond, repayable 2041	268	254
Debt-related derivative financial instruments – liabilities	–	1
	<b>1,005</b>	<b>1,197</b>
<b>Current</b>		
US\$350m 3.5% bond, repayable 2016	237	–
Overdrafts	–	1
	<b>237</b>	<b>1</b>

### 6. Trade and other payables

	2015 £m	2014 <sup>1</sup> £m
<b>Current</b>		
Amounts owed to subsidiary undertakings	7,824	6,978
Amounts owed to Group joint ventures	405	453
Accruals and deferred income	100	46
Other payables	101	132
	<b>8,430</b>	<b>7,609</b>

1. Restated for a correction to amounts due to other Group companies.

### 7. Provisions

	Contracts and other £m
Non-current	109
Current	11
At 1 January 2015	120
Created	2
Utilised	(11)
Net present value adjustments	6
<b>At 31 December 2015</b>	<b>117</b>
Represented by:	
Non-current	105
Current	12
	<b>117</b>

The Company holds provisions for contractual costs that it expects to incur over an extended period. These costs are based on past experience of similar items and represent management's best estimate of the likely outcome.

## 8. Retirement benefit obligations

The Company participates in all of the Group's UK pension schemes. Full disclosures relating to these schemes are given in note 20 to the Group accounts.

### Amounts recognised on the balance sheet

The table below shows a reconciliation between the gross assets and liabilities of the Group's UK pension schemes and the amounts recognised on the Company's balance sheet after allocation to other participating employers.

	2015 £m	2014 £m
Present value of unfunded obligations	(59)	(41)
Present value of funded obligations	(24,974)	(26,195)
Fair value of scheme assets	20,209	20,170
Total IAS 19 deficit, net	(4,824)	(6,066)
Allocated to other participating employers	4,571	5,801
<b>Company's share of IAS 19 deficit, net</b>	<b>(253)</b>	<b>(265)</b>
Represented by:		
Retirement benefit surpluses	6	5
Retirement benefit obligations	(259)	(270)
	<b>(253)</b>	<b>(265)</b>

## 9. Share capital and other reserves

### Share capital

Disclosures in respect of the Company's share capital are provided in note 22 to the Group accounts.

### Other reserves

	Capital reserve £m	Non- distributable reserve £m	Statutory reserve £m	Capital redemption reserve £m	Hedging reserve £m	Total £m
At 1 January 2014 (as previously reported)	24	67	202	1	(4)	290
Effect of transition to FRS 101 (note 12)	(24)	–	–	–	–	(24)
At 1 January 2014 (restated on adoption of FRS 101)	–	67	202	1	(4)	266
Amounts credited to hedging reserve	–	–	–	–	10	10
Net purchase of own shares	–	–	–	2	–	2
At 31 December 2014 (restated on adoption of FRS 101)	–	67	202	3	6	278
Amounts credited to hedging reserve	–	–	–	–	7	7
Transfer to retained earnings	–	(67)	–	–	–	(67)
<b>At 31 December 2015</b>	<b>–</b>	<b>–</b>	<b>202</b>	<b>3</b>	<b>13</b>	<b>218</b>

### Statutory reserve

Under Section 4 of the British Aerospace Act 1980, this reserve may only be applied in paying up unissued shares of the Company to be allotted to members of the Company as fully paid bonus shares.

### Capital redemption reserve

The capital redemption reserve represents the cumulative nominal value of the Company's ordinary shares repurchased and subsequently cancelled. During the year ended 31 December 2015, 1,450,000 (2014 67,417,000) ordinary shares with a nominal value of £nil (2014 £2m) were repurchased and have been subsequently cancelled.

### Hedging reserve

The hedging reserve comprises the effective portion of the cumulative net change in the fair value of cash flow hedging instruments related to hedged transactions that have not yet occurred.

## Notes to the Company accounts continued

### 10. Share-based payments

Options over shares of the Company have been granted to employees of the Company under various plans. Details of the terms and conditions of each share-based payment plan are given in the Annual remuneration report on pages 73 to 86.

	2015		2014	
	Range of exercise price of outstanding options (£)	Weighted average remaining contracted life (years)	Range of exercise price of outstanding options (£)	Weighted average remaining contracted life (years)
Executive Share Option Plan	3.01 – 5.43	8	2.64 – 4.79	7
Performance Share Plan	–	5	–	5
Share Matching Plan	–	–	–	1
Restricted Share Plan	–	5	–	5

The average share price in the year was £4.87 (2014 £4.33).

### 11. Other information

#### Company audit fee

Fees payable to the Company's auditor for the audit of the Company's annual accounts totalled £1,759,000 (2014 £1,669,000).

#### Employees

The total number of employees of the Company at 31 December 2015 was 1,030 (2014 1,189). Total staff costs, excluding charges for share-based payments, were £98m (2014 £111m).

#### Related party transactions

Disclosures in respect of related party transactions are provided in note 29 to the Group accounts.

The Company also has a related party relationship with its directors and key management personnel, and pension schemes.

#### Directors' emoluments

Under Schedule 5 of the Large and Medium-Sized Companies and Groups (Accounts and Reports) Regulations 2008 (Schedule 5), total directors' emoluments, excluding Company pension contributions, were £6,949,237 (2014 £6,601,189); these amounts are calculated on a different basis to emoluments in the Annual remuneration report which are calculated under Schedule 8 of the Large and Medium-Sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013 (Schedule 8 (2013)). These emoluments were paid for their services on behalf of the BAE Systems Group. No emoluments related specifically to their work for the Company. Under Schedule 5, the aggregate gains made by the directors from the exercise of share options in 2015 as at the date of exercise was £992,252 (2014 £739,401) and the net aggregate value of assets received by directors in 2015 from Long-Term Incentive Plans as calculated at the date of vesting was £nil (2014 £nil); these amounts are calculated on a different basis from the valuation of share plan benefits under Schedule 8 (2013) in the Annual remuneration report. Retirement benefits are accruing to two directors in respect of defined benefit schemes and to one director in respect of defined contribution schemes.

#### Company guaranteed borrowings

Borrowings by subsidiary undertakings totalling £2,764m (2014 £2,146m), which are included in the Group's borrowings, have been guaranteed by the Company.

#### Information about related undertakings

In accordance with Section 409 of the Companies Act 2006, a full list of the Company's subsidiaries and significant holdings is included in note 31 to the Group accounts.

## 12. Explanation of transition to FRS 101

As stated in note 1, these are the Company's first financial statements prepared in accordance with FRS 101.

The accounting policies set out in note 1 have been applied in preparing the financial statements for the year ended 31 December 2015, the comparative information for the year ended 31 December 2014 and the opening FRS 101 balance sheet at 1 January 2014 (the Company's date of transition).

In preparing its FRS 101 balance sheets, the Company has adjusted amounts reported in financial statements prepared in prior years in accordance with its previous basis of accounting. An explanation of how the transition to FRS 101 has affected the Company's reported financial performance and position is set out in the following tables.

### Impact of transition to FRS 101 on the Company statement of comprehensive income

	Year ended 31 December 2014		
	As previously reported £m	Pension schemes adjustment <sup>1</sup> £m	FRS 101 £m
<b>Profit for the year</b>	1,183	10	<b>1,193</b>
<b>Other comprehensive income</b>			
<b>Items that will not be reclassified to the income statement:</b>			
Remeasurements on retirement benefit schemes	–	(59)	<b>(59)</b>
<b>Items that may be reclassified to the income statement:</b>			
Amounts credited to hedging reserve	10	–	<b>10</b>
<b>Total other comprehensive income for the year (net of tax)</b>	10	(59)	<b>(49)</b>
<b>Total comprehensive income for the year</b>	1,193	(49)	<b>1,144</b>

1. It had been the Company's policy to account for the UK defined benefit pension schemes in which it participates as defined contribution schemes as permitted by FRS 17, Retirement Benefits. Upon transition to FRS 101, the Company has been allocated a share of the assets and liabilities of the Group's UK defined benefit pension schemes using an allocation method intended to reflect a reasonable approximation of its share of the deficit.

# Notes to the Company accounts

## continued

### 12. Explanation of transition to FRS 101 continued

#### Impact of transition to FRS 101 on the Company balance sheet

	1 January 2014 (the Company's date of transition)			
	As previously reported <sup>1</sup> £m	Pension schemes adjustment <sup>2</sup> £m	Other transition adjustments £m	FRS 101 £m
<b>Non-current assets</b>				
Intangible assets	–	–	1	<b>1</b>
Property, plant and equipment	10	–	(1)	<b>9</b>
Investments in subsidiary undertakings and participating interests	8,057	–	–	<b>8,057</b>
Other receivables	22	–	–	<b>22</b>
Other financial assets	80	–	–	<b>80</b>
	8,169	–	–	<b>8,169</b>
<b>Current assets</b>				
Trade and other receivables	3,630	–	–	<b>3,630</b>
Current tax	32	–	–	<b>32</b>
Other financial assets	126	–	–	<b>126</b>
Cash and cash equivalents	1,732	–	–	<b>1,732</b>
	5,520	–	–	<b>5,520</b>
<b>Total assets</b>	13,689	–	–	<b>13,689</b>
<b>Non-current liabilities</b>				
Loans	(1,159)	–	–	<b>(1,159)</b>
Other payables	(21)	11	–	<b>(10)</b>
Retirement benefit obligations	–	(214)	–	<b>(214)</b>
Other financial liabilities	(86)	–	–	<b>(86)</b>
Provisions	(36)	–	–	<b>(36)</b>
	(1,302)	(203)	–	<b>(1,505)</b>
<b>Current liabilities</b>				
Loans and overdrafts	(100)	–	–	<b>(100)</b>
Trade and other payables	(8,142)	–	–	<b>(8,142)</b>
Other financial liabilities	(141)	–	–	<b>(141)</b>
Provisions	(16)	–	–	<b>(16)</b>
	(8,399)	–	–	<b>(8,399)</b>
<b>Total liabilities</b>	(9,701)	(203)	–	<b>(9,904)</b>
<b>Net assets</b>	3,988	(203)	–	<b>3,785</b>
<b>Capital and reserves</b>				
Issued share capital	89	–	–	<b>89</b>
Share premium	1,249	–	–	<b>1,249</b>
Other reserves	290	–	(24)	<b>266</b>
Retained earnings	2,360	(203)	24	<b>2,181</b>
<b>Total equity</b>	3,988	(203)	–	<b>3,785</b>

1. Restated for a correction to amounts due to other Group companies.

2. It had been the Company's policy to account for the UK defined benefit pension schemes in which it participates as defined contribution schemes as permitted by FRS 17, Retirement Benefits. Upon transition to FRS 101, the Company has been allocated a share of the assets and liabilities of the Group's UK defined benefit pension schemes using an allocation method intended to reflect a reasonable approximation of its share of the deficit.

## 12. Explanation of transition to FRS 101 continued

	31 December 2014			FRS 101 £m
	As previously reported <sup>1</sup> £m	Pension schemes adjustment <sup>2</sup> £m	Other transition adjustments £m	
<b>Non-current assets</b>				
Intangible assets	10	–	1	<b>11</b>
Property, plant and equipment	9	–	(1)	<b>8</b>
Investments in subsidiary undertakings and participating interests	8,169	–	–	<b>8,169</b>
Other receivables	9	–	–	<b>9</b>
Retirement benefit surpluses	–	5	–	<b>5</b>
Other financial assets	105	–	–	<b>105</b>
	<b>8,302</b>	<b>5</b>	<b>–</b>	<b>8,307</b>
<b>Current assets</b>				
Trade and other receivables	3,225	–	–	<b>3,225</b>
Current tax	32	–	–	<b>32</b>
Other financial assets	128	–	–	<b>128</b>
Cash and cash equivalents	1,792	–	–	<b>1,792</b>
	<b>5,177</b>	<b>–</b>	<b>–</b>	<b>5,177</b>
<b>Total assets</b>	<b>13,479</b>	<b>5</b>	<b>–</b>	<b>13,484</b>
<b>Non-current liabilities</b>				
Loans	(1,197)	–	–	<b>(1,197)</b>
Other payables	(25)	13	–	<b>(12)</b>
Retirement benefit obligations	–	(270)	–	<b>(270)</b>
Other financial liabilities	(98)	–	–	<b>(98)</b>
Provisions	(109)	–	–	<b>(109)</b>
	<b>(1,429)</b>	<b>(257)</b>	<b>–</b>	<b>(1,686)</b>
<b>Current liabilities</b>				
Loans and overdrafts	(1)	–	–	<b>(1)</b>
Trade and other payables	(7,609)	–	–	<b>(7,609)</b>
Other financial liabilities	(134)	–	–	<b>(134)</b>
Provisions	(11)	–	–	<b>(11)</b>
	<b>(7,755)</b>	<b>–</b>	<b>–</b>	<b>(7,755)</b>
<b>Total liabilities</b>	<b>(9,184)</b>	<b>(257)</b>	<b>–</b>	<b>(9,441)</b>
<b>Net assets</b>	<b>4,295</b>	<b>(252)</b>	<b>–</b>	<b>4,043</b>
<b>Capital and reserves</b>				
Issued share capital	87	–	–	<b>87</b>
Share premium	1,249	–	–	<b>1,249</b>
Other reserves	302	–	(24)	<b>278</b>
Retained earnings	2,657	(252)	24	<b>2,429</b>
<b>Total equity</b>	<b>4,295</b>	<b>(252)</b>	<b>–</b>	<b>4,043</b>

1. Restated for a correction to amounts due to other Group companies.

2. It had been the Company's policy to account for the UK defined benefit pension schemes in which it participates as defined contribution schemes as permitted by FRS 17, Retirement Benefits. Upon transition to FRS 101, the Company has been allocated a share of the assets and liabilities of the Group's UK defined benefit pension schemes using an allocation method intended to reflect a reasonable approximation of its share of the deficit.