

General Dynamics United Kingdom Limited

Annual report and financial statements

Registered number 1911653

31 December 2021

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Strategic Report

Business Review

General Dynamics United Kingdom Limited (“GDUK” or “the Company”) operates in the defence sector offering a broad portfolio of products and service with customers including the United Kingdom Ministry of Defence (UK MoD). Throughout 2021, the Company has focused on its key strategies of customer first, delivering on order book, whilst positioning for key pursuit wins for the future through investment in research and new product development. 2021 saw a number of highlights on some key programmes including:

- The AJAX programme has continued to make progress in the face of significant delays resulting from technical concerns raised by the UK MoD and, to a lesser extent, the residual pressures of Covid-19. In particular, safety notices issued by the customer in 2021 have impeded progress in many areas. Nevertheless, the design baseline for the full AJAX capability has been released into trials and production. Trials activity resulted in a 100% increase in requirements acceptance over the last reporting period. Training systems, training courseware, support equipment and services have continued to be provided to ensure availability of the delivered vehicles and training systems. In areas such as Production and Reliability Growth Trials this progress was significantly slower than planned, with Reliability Growth Trials in particular experiencing delay. Following the success of the Noise and Vibration User Validation Trials in October 2022 and positive user feedback on the overall AJAX capability there is evidence of user confidence in the technical baseline that underpins the programme path forward. Significant effort to ensure programme delivery has been expended by the Company, UK MoD (DE&S) and the British Army resulting in a jointly developed revised schedule that embodies full resolution of the technical concerns including a production schedule that will ensure delivery of the full AJAX capability to the British Army. The Company continues to progress the programme to the extent reasonably practicable in anticipation that the safety notices will be relaxed and in reliance upon the customer’s actions in support of the revised schedule.

In a public statement released on 22-Dec-22 by the UK MoD and Secretary Of State for Defence, Ben Wallace, it was highlighted that Ajax User Validation Trials were recognised as completing successfully and that the government has reaffirmed its commitment to the Ajax contract.

Whilst payment from the UK MoD was not received during 2022 the parties continue to engage at senior levels to recommence normal program activities, including payment.

- MORPHEUS Evolve to Open (EvO) is the UK MoD programme to transition from the in-service Bowman tactical communications system to a future system. The Company is contracted for the first phase of this programme and continues to work on the artefacts required for the EvO system design whilst the customer progresses its wider MORPHEUS procurement and approvals cycle. UK MoD is currently assessing alternative procurement strategies and timelines for the broader MORPHEUS programme beyond EvO, which could impact upon the contract currently being delivered by the Company.
- Since 2016, the in-service Bowman Tactical Communications System has been going through a series of programme updates to the software and hardware overcoming obsolescence challenges and delivering capability enhancements where appropriate. Following the successful fielding of the 5.6 Bowman Tactical Communications system to the Army’s fleet of vehicles, the system continues to receive positive feedback from the user community and is delivering key capability on operational deployments continuously. Throughout 2021 and 2022 the system has been updated with the fielding of Capability Uplift 2 and will continue to be supported as a system through the capability uplift improvement programme on an annual basis.

The year ended 31 December 2021 saw revenues fall by 18% on 2020 to £604m. Operating profit reduced by 80.5% to £15.1m. The reduction in revenue was driven by changes on the AJAX and EvO contracts. Costs in 2021 did not reduce at the same rate as sales due to the business planning activities in order to realign its cost base following a reduction in revenues, thus impacting operating profit. In addition the company saw a reduction in the profit rate on two of its key contracts (AJAX and EvO) reducing in year profit by the cumulative impact of this change. The reduction in profit rate for the AJAX programme was primarily due to the significant delays referenced above and the resultant increased programme costs as the programme extends. Reductions in profit on the EvO programme are as a result of the discussions between the Company and UK MoD during 2021 on the programme.

Strategic Report *(continued)*

Similar to 2020, the Company did not receive the anticipated cash receipts nor raise anticipated invoices pending contractual discussions with the customer. This timing change has been modelled by the Company as part of its going concern assessment.

Net current assets decreased to £360m in 2021 compared to £453m in 2020. This was principally caused by a lower increase in current assets compared to current liabilities: The increase in Current Liabilities of £423m was primarily due to:

1. An increase in the amounts owed by the company to related party entities. This is due to additional working capital support from the wider group while contractual discussions with the customer continued.

The increase in Current Assets of £329m was primarily due to:

1. A reduction of £195m in the debtor balance following the receipt of a cash deposit on a contract in late 2020 which increased the amounts owed to GDUK under the GD Group Cash Pooling arrangement.
2. An increase in the contract assets balance by £513m in 2021 primarily driven by delays in gaining approval to invoice customers on the AJAX and EvO contracts.
3. The remainder is primarily due to a reduction in the fair value of cash flow hedges in 2021 as several of the hedges outstanding at the end of 2020 for AJAX ended in 2021 so were no longer outstanding.

Business performance is assessed using several performance indicators above the traditional financial measures and programme Key Performance Indicators. These are focused on delivery performance in development and production contracts, staff turnover, the success rate of new business pursuits, employee engagement and the measurement of cost effectiveness and productivity. The company experienced a larger amount of voluntary staff attrition in 2021 than it has seen through previous years. This is aligned to what the wider market has experienced in terms of the well published Great Resignation. In addition, the company embarked on a period of restructuring which is often followed by higher levels of voluntary staff attrition. The company continues to focus on employee engagement activities in addition to running regular employee briefing sessions.

Principal Risks and Uncertainties

Individual programme and business segment level risk reviews are undertaken regularly. Whilst the Coronavirus impact has diminished, the Company continues to operate in a hybrid environment, ensuring business continuity and the ability to react to changing circumstances.

As the wider economy experiences higher inflation and also as the Ukraine conflict impacts the cost and availability of key supplies, the organisation continues to monitor and mitigate the supply chain and financial risks associated with these.

As discussed, the Company has been in discussions with the UK MoD on two of its contracts. These discussions are ongoing and, until fully agreed, a degree of uncertainty exists as to the final terms of the contract amendment. The Company continues to monitor this risk closely.

Regulatory Matters

Some of the Company's contracts are Qualifying Defence Contracts, as defined by the UK Defence Reform Act 2014. The Company is an active member of the Single Source Regulator's Operational Working Groups and reports into the regulator on contract performance quarterly and annually.

Financial Risk Management

Foreign Exchange Rate Risk: Change in foreign exchange rates are dealt with by the Company as follows:

- To the extent possible, the foreign currency exchange rate risk relating to receipts from customers, payments to suppliers and inter-company transactions denominated in foreign currencies are sought to be mitigated via the terms and conditions within contracts.
- The Company will also seek to reduce the impact of foreign exchange risk by concluding transactions in the Company's functional currency or naturally hedging income and expenses in a foreign currency.

Strategic Report (continued)

- Alternatively, the Company will enter into derivative instruments, principally foreign currency forward purchase and sale contracts, designed to offset and minimise risk. The Company does not use derivatives for trading or speculative purposes.

Credit Risk: Credit risk is considered to be low given that the majority of sales are to the UK Government.

Liquidity and Cash-flow Risk: The Company's liquidity is ensured by means of regular group-wide monitoring and planning of liquidity coordinated by the Group's centralised treasury department. In order to facilitate cash management activities, the Company has entered into a cash pool agreement with other General Dynamics companies within Europe. The cash pooling arrangement and regular forecasting of cash needs by the cash pool members significantly reduces any cash flow risk to the Company.

Section 172 (1) Statement

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

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

Decision Making

The business units within GDUK reports into two of the five operating segments within the General Dynamics Corporation; Mission Systems into the Technologies segment and Land Systems into the Land Systems segment. The GD Corporate team sets the overall strategy for each operating segment being responsible for the execution of its own strategy and operational performance, whilst also adhering to GDUK's robust policies and processes. Decisions taken affecting each business unit are taken in line with the Company Delegation of Authority and GDUK's policies and processes.

As part of its operational performance, the business units produce a strategic plan alongside a 5-year financial projection. This is produced annually and reviewed for the subsequent 18 months every quarter, and this includes the development and review of risks and opportunities to this strategy and the financial projections. In conducting this process, regard is given for the business, its stakeholders and the long-term implications of the decisions that they are undertaking.

Employees

Employee engagement is a key focus for the Directors and Management of the Company to ensure it is connecting employees to the Company's strategy and empowering them to contribute to operational performance. In addition to the employee engagement described within the Director's report, the Company utilises an internal employee engagement platform where employees can share news and ideas with colleagues. The Company encourages participation and involvement in matters, which affect their interests as employees. Encouragement is given to employees to provide feedback using organisation wide questionnaires with the aim of achieving a common awareness on all aspects affecting the performance of the Company. The Employee Consultation Group provides a safe forum for elected employee representatives to openly discuss business and employment matters with senior management. The Company's implemented policies and processes also provide a means to give employees their views and feedback. Through the implementation by the Company of these policies and processes, the Directors and Management have regard to the interests of the Company's employees.

Fostering business relationships with suppliers, customers and other

The Board of Directors and Management of the Company believe that the prime value of the Company is generated from its employees, supply chain and customer relationships. Fostering business relationships with key stakeholders, such as customers and suppliers is considered as essential to the Company's success.

Strategic Report *(continued)*

The Senior Management and Supply Chain team within the Company meet with key suppliers in order to develop and enhance strategic relationships with them. The Company also works closely with its supply chain through several forums and continues to pledge support to the UK Government's Small- Medium Sized enterprise agenda.

In 2019, the Company signed up to the Prompt Payment Code (PPC) and through 2021 paid 94% of the volume of its invoices within 60 days (2020: 98%). The Directors recognise the importance of paying suppliers promptly and actively monitors and reviews the Company's payment practices.

The EDGE UK® is a concept developed by GD, which provides Small and Medium Sized Enterprises, academia and customers with access to virtual and physical collaboration environments. This enables Small and Medium Sized Enterprises with a route to market and provides customers with potential solutions to complex engineering problems.

The Company also continues to focus on building collaborative relationships with customers and external stakeholders. The Directors and their delegates sit on a number of UK Government Defence supplier groups and work directly with its customer base to build strong relationships. The Company obtained the ISO 44001 Collaborative Business Relationship Management accreditation in 2019 and continues to utilise across its programmes.

The community and the environment

The Directors recognise and agree the importance of leading a Company that not only generates value for the shareholders but also contributes to the wider community. The Company is committed to the Armed Forces Covenant and to maintaining its Employer Recognition Scheme Gold Award. The Company has formed and continued to promote an Armed Forces Network for employees meeting each quarter as an open forum to discuss ways to further support the armed forces community.

In addition, the Company regularly supports Armed Forces charities. Charitable donations and community involvement are encouraged across all sites and employees are supported by well-developed policies and practices.

Corporate Sustainability is rooted in the Company ethos. Climate change is a concern to the Directors who are committed to reducing global environmental impact and striving to be a leader in improving environmental quality. The Company refers more to its commitment to the environment in the Directors Report.

Maintaining a reputation for a high standard of conduct

The Directors and the Management of the Company promote the GD Corporate policy of Ethos, which demonstrates distinguishing moral nature. The Company prides itself on values of Honesty, Transparency, Trust and Alignment throughout its workforce and operations. These values drive how the Company operates its business, governs how to interact with each other including customers, partners and suppliers, guide the way employees are treated and determines how to connect with the community.

The Company has a Standards of Business Ethics and Conduct Handbook that applies to all employees. This ethics programme also includes periodic training on ethics and compliance topics for all employees and a 24-hour ethics helpline, which employees can access via telephone or online to communicate any business-related ethics concerns. The Company has implemented an Ethics code specifically applicable to the Board of Directors, which embodies the commitment to manage the business in accordance with the highest standards of ethical conduct.

The Directors periodically review and approve frameworks such as its Modern Slavery Statements, to ensure that its high standards are maintained both internally and within external business.

The tax strategy is developed by General Dynamics Corporation and is applicable to General Dynamics United Kingdom Ltd for which General Dynamics Corporation (GDC) has ultimate control. The tax strategy is publically available on the website of the Company to enable external stakeholders to understand the Group's approach to tax.

Environmental

Corporate Sustainability is rooted in the Company ethos. Climate change is a concern to the Directors who are committed to reducing global environmental impact and striving to be a leader in improving environmental quality.

In the period covered by the report, GDUK completed its upgrades to one of its facilities Building Energy Management Systems. This delivered improved controls over the heating, ventilation and cooling (HVAC) system, enabling energy management efficiencies with a reduction of 65,761 kWh in electricity consumption.

The company's formal reporting environmental disclosure is as follows:

Strategic Report *(continued)*

Quantification and Reporting Methodology

The company has followed the 2019 UK Government Environmental Reporting Guidelines and used the 2021 UK Government's Conversion Factors for Company Reporting.

Organisational boundary

The company has used the financial control approach.

Operational scopes

The company has measured its scope 1, 2 and employee car business travel scope 3 emissions.

Intensity Measurement:

The company has chosen the metric gross scope 1 and 2 emissions in tonnes of CO₂e per tonne of Full Time Equivalent as the most relevant business metric for the industry sector.

Base Year

The company has a fixed base year of 2020. The base year recalculation policy is to recalculate the base year and the prior year emissions for relevant significant changes which meet the significance threshold of 5% of base year emissions.

Targets


GDUK published its first Carbon Reduction Plan in September 2021, using a base year of 2020 data to commit to work towards achieving net zero emissions by 2050. As part of the GDUK roadmap to net zero, the company is also working towards 100% renewable energy from 2025. During the reporting period GDUK contracted with Carbon Footprint Ltd to initiate an independent SME carbon appraisal, review of its full value chain and provide support to model further reduction targets and meet the company's goal of net zero by 2050. The Company has chosen the metric "Gross scope 1 and 2 emissions in tonnes of CO₂e per tonne of Full Time Equivalent" as the most relevant business metric for our industry sector. These metrics are presented below:

Strategic Report *(continued)*

Energy consumption used to calculate emissions: 9,156,638 kWh	Current Reporting Year 2021 UK (no offshore activity)	% of activity data that is estimated	Comparison Reporting Year 2020 UK (no offshore activity)
SCOPE 1 tCO₂e Emissions from activities for which the company own or control including combustion of fuel & operation of facilities		No data estimated	
Gas Consumption	556		527
Process emissions	250		3
Fugitive emissions	81		138
Total Scope 1	888		668
SCOPE 2 tCO₂e Emissions from purchase of electricity purchased for own use (location-based factors)	1,181		1,393
Total gross Scope 1 & Scope 2 emissions tCO₂e	2,069		2,061
Company's chosen intensity ratio (scope 1&2) tCO₂e per Full Time Equivalent	1.46		1.55
SCOPE 3 tCO₂e Emissions from employee business travel for which the company does not own or control. Business travel activities included: rental, personal and company cars	213		221
Total Gross Scope 1, Scope 2 (location) & Scope 3 emissions tCO₂e	2,282		2,282

2021 Summary

The Company continued to deliver on its programmes in 2021 but experienced reductions in revenue and profit due to changes in two of its key contracts. Programmes execution, delivery and customer satisfaction continue to be a priority for the business, coupled with ongoing investment activities to position the Company well for future opportunities. Employees, customers and suppliers continue to be at the forefront of the Company's prime value generation and the ongoing focus on these key relationships will ensure a vibrant future for the Company.


Lieutenant General A C Figgures
Director

Date. 26 Jan 23

21 Holborn Viaduct
London
EC1A 2DY

Directors' Report

The Directors present their annual report and the audited financial statements for the year ended 31 December 2021.

Principal Activities

GDUK has two business units

1. **Mission Systems**, which specialises primarily in the design, delivery and through-life support of solutions in the Command, Control, Communications, Computing and Information (C4I) domain.
2. **Land Systems**, which designs, manufactures and sustains land combat platforms; most notably the AJAX armoured fighting vehicle.

C4I is the delivery of vital information via the integration of technology and networks. This information is used to observe and act decisively in the field of battlespace management. In 2004 the Company delivered Bowman, one of the world's most advanced battlefield communication systems, to the UK MoD. In 2017, the Company was awarded the first phase of the MORPHEUS contract, known as Evolve to Open (EvO), which aims to modernise the UK's communications and command and control systems by evolving the Bowman network into a more open system, able to maintain pace with ever-advancing technology. The Company has also been successful in providing a Tactical Communications System for the Dutch Marines.

The Company is contracted for the Demonstration, Production and Extended Support Phases of the AJAX programme for the UK Army. The AJAX armoured fighting vehicle, a next generation medium weight tracked combat vehicle, offers advanced electronic architecture and proven technology for an unparalleled balance of survivability, lethality and mobility along with high reliability for a vehicle in its weight class.

Work on the AJAX programme is soon to transition from engineering to test and then full production. Completion of all 589 vehicles in six different variants is anticipated in 2027 based on current delivery schedule and solutions agreed with the customer.

The Company also provides a range of best-in-class avionics products including tactical processors, tactical data links, weapon management computer systems and secure data recorders. This wealth of experience in the avionics business has made the Company a key supplier to programmes such as Typhoon and Wildcat.

Research and development

To foster innovation, product development and evolution, the Company has a policy of targeted investment in the design and development of new technologies and capabilities that support business growth and the pursuits that the business is planning to win in future periods.

Major areas of interest include the development of new products for future MORPHEUS competitions and export versions of the core EvO products.

Further areas of focus in the Land sector are joint AJAX capability growth experimentation with the UK Army (including so-called Manned/Unmanned Teaming or MUM-T), AFV sustainment related technologies such as Health and Usage Monitoring Systems (HUMS), ensuring vehicle electronic architectures are aligned with MORPHEUS and helping develop the Land Environment's latest ISTAR thinking.

In the air sector, the Company is investing in the Typhoon mid-life update as well as future unmanned combat air platforms, such as TEMPEST.

Financial Instruments risk, policy and exposure

The Company is subject to foreign exchange rate risk, which is detailed in the Strategic Report. Where receipts and disbursements cannot be denominated in the functional currency or offset by an equal amount with identical timing to create a natural hedge, it is Company practice to enter into hedge contracts that reduce the impact of currency movements over a period of time.

Foreign exchange exposure is reviewed on a monthly basis and explanation provided for any unhedged transactions greater than \$1m. Responsibility for monitoring and review is delegated to senior management who are responsible for the day to day financial operations and a foreign exchange exposure report is prepared and reviewed on a quarterly basis to capture this detail. As a result, the Company's exposure to foreign exchange risk is considered low.

Directors' Report *(continued)*

Results and proposed dividend

Profit after taxation for the year ended 31 December 2021 was £10.4m compared to £67m for the year ended 31 December 2020. The directors paid a dividend in the year of £80.5m to its wholly owned parent, General Dynamics Limited, which it is understood has been retained within the ultimate UK parent company, General Dynamics Global Holdings Ltd (2020: £nil). This is the first dividend that has been paid by the Company since 2016.

Directors

The directors who held office during the year and to the date of this report were as follows:

Non-Executive Directors:

Lieutenant General Andrew Collingwood Figgures

Steven Edward Rowbotham (Appointed Non-Executive Director January 2021)

Executive Directors:

Danny Deep

Directors' indemnities

The Company has maintained liability insurance for Directors and officers and its subsidiaries. Neither the insurance nor the indemnity provides cover where a Director acts fraudulently or dishonestly. The Company has made qualifying third-party indemnity provisions for the benefit of the Directors which were made during the year and remain in force at the date of this report.

Corporate Responsibility

During 2020, the Company continued to build on its solid progress and actively ensured delivery of stakeholder commitments. The Company website explains to stakeholders the Company policies, strategies and business progress and is updated on a regular basis. Employees receive frequent updates on progress and the latest Company initiatives through a weekly e-newsletter. In addition, the Company has introduced a new social media communication platform that enables employees to connect and share information about the latest news and activities across the business.

The Company strives to maintain the highest standards of ethical conduct and corporate responsibility. Employees receive annual training on this subject, and support mechanisms are in place for employees through an information telephone line, which is operational 24 hours a day, 365 days of the year. By operating proactive policies, the Company manages its customer and supplier relationships responsibly.

The Company is committed to the Armed Forces Covenant, and to maintaining its Employer Recognition Scheme Gold Award. The Company has formed an Armed Forces Network for employees meeting each quarter as an open forum to encourage employee engagement with the covenant and to discuss ways to further support the armed forces community. Service leavers are supported by attending Transition Fairs designed to promote employment opportunities, contribute to military thought leadership and support existing employees undertaking Reserve service and cadet instructors with a period of paid leave.

The single greatest contribution to the communities in which the Company operates is the sustained wealth created by providing hundreds of highly skilled jobs. Charitable donations and community involvement are encouraged across all our sites and employees are supported by well-developed policies and practices.

Employees

Employees are considered by the Company as the key part to the success of the business. Employee engagement is assessed through regular formal survey's in addition to regular one to one sessions between Employees and Management. Employee Communication is considered a key attribute to enhanced employee engagement and the Company's approach to this is laid out in the Section 172 disclosure within the Strategic Report.

The Company is committed to promoting diversity and creating a fully inclusive working environment, where every employee can fulfil their potential. The Company recognises that diversity of experience, perspectives and capabilities is good for the team, wider stakeholders and it is critical to future success. The Company has a commitment to a

Directors' Report *(continued)*

comprehensive inclusion and diversity strategy; a working group has been established across the UK and is investing in areas that foster an inclusive, diverse and transparent working environment for all colleagues.

During 2021, the Company continued to support the Women in Defence charter. In addition, the company continued to support initiatives run by Chwrae Teg to promote inclusion and diversity.

On December 31, 2021, the Company employed 1,229 employees across its sites in Oakdale in South Wales, Merthyr Tydfil in South Wales, Hastings in East Sussex, Chippenham in Wiltshire and Bristol. Of these employees 83 are represented by a Union.

Political

The Company made no political contributions during the year (2020: nil).

Going Concern Assessment

Following assessment and review, the Directors have a reasonable expectation that the Company has sufficient resources to continue to operate for at least the next 12 months from the date of approval of these financial statements. Further detail on the going concern assessment is disclosed in note 1.


Disclosure of information to auditor

The directors who held office at the date of approval of this directors' report confirm that, so far as they are each aware, there is no relevant audit information of which the Company auditor is unaware; and each director has taken all the steps that he ought to have taken as a director to make himself aware of any relevant audit information and to establish that the Company auditor is aware of that information.

Auditor

Pursuant to Section 487 of the Companies Act 2006, the auditor will be deemed to be reappointed and KPMG LLP will therefore continue in office.

By Order of the Board



Lieutenant General A C Figgures
Director

21 Holborn Viaduct
London
EC1A 2DY

Date

26 Jan 23

STATEMENT OF DIRECTORS' RESPONSIBILITIES IN RESPECT OF THE ANNUAL REPORT AND THE FINANCIAL STATEMENTS

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

Company law requires the directors to prepare financial statements for each financial year. Under that law they have elected to prepare the financial statements in accordance with UK accounting standards and applicable law (UK Generally Accepted Accounting Practice), including FRS 101 *Reduced Disclosure Framework*.

Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period. In preparing these financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable UK accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements;
- assess the company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and
- use the going concern basis of accounting unless they either intend to liquidate the company or to cease operations, or have no realistic alternative but to do so.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 2006. They are responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error, and have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the company and to prevent and detect fraud and other irregularities.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF GENERAL DYNAMICS UNITED KINGDOM LIMITED

Opinion

We have audited the financial statements of General Dynamics United Kingdom Limited ("the Company") for the year ended 31 December 2021 which comprise the Income statement, Other Comprehensive Income, Balance Sheet and Statement of Changes in Equity and related notes, including the accounting policies in note.

In our opinion the financial statements:

- give a true and fair view of the state of the Company's affairs as at 31 December 2021 and of its profit for the year then ended;
- have been properly prepared in accordance with UK accounting standards, including FRS 101 *Reduced Disclosure Framework*; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities are described below. We have fulfilled our ethical responsibilities under, and are independent of the Company in accordance with, UK ethical requirements including the FRC Ethical Standard. We believe that the audit evidence we have obtained is a sufficient and appropriate basis for our opinion.

Going concern

The directors have prepared the financial statements on the going concern basis as they do not intend to liquidate the Company or to cease its operations, and as they have concluded that the Company's financial position means that this is realistic. They have also concluded that there are no material uncertainties that could have cast significant doubt over its ability to continue as a going concern for at least a year from the date of approval of the financial statements ("the going concern period").

In our evaluation of the directors' conclusions, we considered the inherent risks to the Company's business model and analysed how those risks might affect the Company's financial resources or ability to continue operations over the going concern period.

Our conclusions based on this work:

- we consider that the directors' use of the going concern basis of accounting in the preparation of the financial statements is appropriate;
- we have not identified, and concur with the directors' assessment that there is not, a material uncertainty related to events or conditions that, individually or collectively, may cast significant doubt on the Company's ability to continue as a going concern for the going concern period.

However, as we cannot predict all future events or conditions and as subsequent events may result in outcomes that are inconsistent with judgements that were reasonable at the time they were made, the above conclusions are not a guarantee that the Company will continue in operation.

Fraud and breaches of laws and regulations – ability to detect

Identifying and responding to risks of material misstatement due to fraud

To identify risks of material misstatement due to fraud ("fraud risks") we assessed events or conditions that could indicate an incentive or pressure to commit fraud or provide an opportunity to commit fraud. Our risk assessment procedures included:

- Enquiring of directors and inspection of policy documentation as to the Company's high-level policies and procedures to prevent and detect fraud, including the Company's channel for "whistleblowing", as well as whether they have knowledge of any actual, suspected or alleged fraud.
- Reading Board minutes.
- Considering remuneration incentive schemes and performance targets for management.
- Using analytical procedures to identify any unusual or unexpected relationships.

We communicated identified fraud risks throughout the audit team and remained alert to any indications of fraud throughout the audit.

As required by auditing standards, and taking into account possible pressures to meet profit targets and our overall knowledge of the control environment, we perform procedures to address the risk of management override of controls and the risk of fraudulent revenue recognition, in particular:

- the risk that management may be in a position to make inappropriate accounting entries;
- the risk of bias in accounting estimates including those related to revenue. The amount of revenue recognised in a year is based on the assessment of the percentage of completion of long-term contracts and the forecast cost profile of each contract. The estimated outturn requires significant judgement to be applied in estimating total costs to deliver the contract. The nature of these estimates means their continual refinement can have impacts on revenue which can be significant.

We did not identify any additional fraud risks.

We performed procedures including:

- Identifying journal entries and other adjustments to test based on risk criteria and comparing the identified entries to supporting documentation. These those posted by individuals who are not authorised to do so or who do not frequently post journal entries, those posted to unusual accounts or account combinations, and those which are for round sum amounts.
- Assessing significant accounting estimates for bias including estimates linked to long-term contract revenue.

Identifying and responding to risks of material misstatement due to non-compliance with laws and regulations

We identified areas of laws and regulations that could reasonably be expected to have a material effect on the financial statements from our general commercial and sector experience, through discussion with the directors and other management (as required by auditing standards), and discussed with the directors and other management the policies and procedures regarding compliance with laws and regulations.

We communicated identified laws and regulations throughout our team and remained alert to any indications of non-compliance throughout the audit.

The potential effect of these laws and regulations on the financial statements varies considerably.

Firstly, the Company is subject to laws and regulations that directly affect the financial statements including financial reporting legislation (including related companies legislation), distributable profits legislation, pensions legislation and taxation legislation. and we assessed the extent of compliance with these laws and regulations as part of our procedures on the related financial statement items.

Secondly, the Company is subject to many other laws and regulations where the consequences of non-compliance could have a material effect on amounts or disclosures in the financial statements, for instance through the imposition of fines or litigation. We identified the following areas as those most likely to have such an effect: health and safety, anti-bribery, data protection laws, employment law and contracts legislation (including government contracts), recognising the nature of the Company's activities. Auditing standards limit the required audit procedures to identify non-compliance with these laws and regulations to enquiry of the directors and other management and inspection of regulatory and legal correspondence, if any. Therefore if a breach of operational regulations is not disclosed to us or evident from relevant correspondence, an audit will not detect that breach.

Context of the ability of the audit to detect fraud or breaches of law or regulation

Owing to the inherent limitations of an audit, there is an unavoidable risk that we may not have detected some material misstatements in the financial statements, even though we have properly planned and performed our audit in accordance with auditing standards. For example, the further removed non-compliance with laws and regulations is from the events and transactions reflected in the financial statements, the less likely the inherently limited procedures required by auditing standards would identify it.

Strategic report and directors' report

The directors are responsible for the strategic report and the directors' report. Our opinion on the financial statements does not cover those reports and we do not express an audit opinion thereon.

Our responsibility is to read the strategic report and the directors' report and, in doing so, consider whether, based on our financial statements audit work, the information therein is materially misstated or inconsistent with the financial statements or our audit knowledge. Based solely on that work:

- we have not identified material misstatements in the strategic report and the directors' report;
- in our opinion the information given in those reports for the financial year is consistent with the financial statements; and
- in our opinion those reports have been prepared in accordance with the Companies Act 2006.

Matters on which we are required to report by exception

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

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

We have nothing to report in these respects.

Directors' responsibilities

As explained more fully in their statement set out on page 10, the directors are responsible for: the preparation of the financial statements and for being satisfied that they give a true and fair view; such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and using the going concern basis of accounting unless they either intend to liquidate the Company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities

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

A fuller description of our responsibilities is provided on the FRC's website at www.frc.org.uk/auditorsresponsibilities.

The purpose of our audit work and to whom we owe our responsibilities

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



Huw Brown (Senior Statutory Auditor)
for and on behalf of KPMG LLP, Statutory Auditor
Chartered Accountants
66 Queen Square
Bristol
BS1 4BE

26 January 2023

Income statement
for the year ended 31 December 2021

	<i>Note</i>	2021 £000	2020 £000
Turnover	2	604,373	734,833
Cost of sales		(557,634)	(626,065)
Gross profit		46,739	108,768
Administrative expenses		(31,680)	(31,229)
Operating profit		15,059	77,539
Interest receivable and similar income	5	152	160
Interest payable and similar expenses	6	(1,740)	(3,144)
Other (losses) / gains	7	(28)	771
Profit before taxation	8	13,443	75,326
Tax on profit	10	(3,077)	(8,362)
Profit for the financial year		10,366	66,964

The profit for the year and the preceding year arises entirely from continuing operations.

The notes on pages 17 to 52 form part of these financial statements.

Other Comprehensive Income

		2021 £000	2020 £000
Profit for the financial year		10,366	66,964
Items that will not be reclassified subsequently to profit and loss:			
Actuarial gain / (loss) on the pension scheme (net of deferred tax)	24	518	(1,196)
Items that will be reclassified subsequently to profit or loss:			
Change in fair value of cash flow hedges (net of deferred tax)	21	(13,453)	9,449
Total comprehensive (expense) / income for the year		(2,569)	75,217

Balance sheet
At 31 December 2021

	<i>Note</i>	2021 £000	2020 £000
Fixed assets			
Intangible assets	<i>11</i>	556	576
Tangible assets	<i>12</i>	39,155	39,008
		39,711	39,584
Current assets			
Stock and work in progress	<i>13</i>	404	531
Debtors	<i>14</i>	1,084,621	747,620
Other financial assets	<i>17</i>	1,670	9,122
Cash at bank		-	57
		1,086,695	757,330
Creditors: amounts falling due within one year	<i>15</i>	(727,057)	(303,956)
Net current assets		359,638	453,374
Total assets less current liabilities		399,349	492,958
Creditors: amounts falling due after more than one year	<i>16</i>	(7,876)	(8,993)
Provisions for liabilities and charges	<i>19</i>	(16,874)	(25,010)
Net assets		374,599	458,955
Capital and reserves			
Called up share capital	<i>20</i>	9,262	9,262
Capital redemption reserve		88	88
Other reserves		1	1
Cashflow hedge reserve	<i>21</i>	(3,183)	10,270
Profit and loss account		368,431	439,334
Shareholders' funds		374,599	458,955

These financial statements were approved by the board of directors on January 26th 2023 and were signed on its behalf by:


Lieutenant General A C Figgures
Director

The notes on pages 17 to 52 form part of these financial statements.

Statement of Changes in Equity

	Called up Share capital £000	Capital redemption reserve £000	Other reserves £000	Cash flow hedge reserve £000	Profit and loss account £000	Total £000
Balance at 1 January 2021	9,262	88	1	10,270	439,334	458,955
Other Comprehensive income for the year	-	-	-	(13,453)	10,884	(2,569)
Dividend paid	-	-	-	-	(80,498)	(80,498)
IFRS 2 share based payment charges	-	-	-	-	(1,289)	(1,289)
At 31 December 2021	9,262	88	1	(3,183)	368,431	374,599

	Called up Share capital £000	Capital redemption reserve £000	Other reserves £000	Cash flow hedge reserve £000	Profit and loss account £000	Total £000
Balance at 1 January 2020	9,262	88	1	821	372,792	382,964
Other Comprehensive income for the year	-	-	-	9,449	65,768	75,217
IFRS 2 share based payment charges	-	-	-	-	774	774
At 31 December 2020	9,262	88	1	10,270	439,334	458,955

Notes

(forming part of the financial statements)

1 Accounting policies

General Dynamics United Kingdom Limited (the “Company”) is a private company incorporated, domiciled and registered in England and Wales. The registered number is 1911653 and the registered address is 21 Holborn Viaduct, London, EC1A 2DY.

Basis of Preparation

These financial statements were prepared in accordance with Financial Reporting Standard 101 Reduced Disclosure Framework (“FRS 101”). In preparing these financial statements, the Company applies the recognition, measurement and disclosure requirements of international accounting standards in conformity with the requirements of the Companies Act 2006 (“Adopted IFRSs”), but makes amendments where necessary in order to comply with Companies Act 2006 and has set out below where advantage of the FRS 101 disclosure exemptions has been taken.

As the Company’s ultimate parent undertaking, General Dynamics Corporation, includes the Company in its consolidated financial statements, which are intended to give a true and fair view of the assets, liabilities, financial position, and profit and loss, the Company qualifies for the preparation of accounts using FRS101 with reduced disclosures. The consolidated financial statements of General Dynamics Corporation are prepared in accordance with US GAAP and are available to the public and may be obtained from 11011 Sunset Hills Road, Reston, VA 20190.

In these financial statements, the Company has applied the exemptions available under FRS 101 in respect of the following disclosures:

- Cash Flow Statement and related notes;
- Disclosures in respect of capital management;
- Disclosures in respect of the compensation of Key Management Personnel;
- Disclosures in respect comparatives of Fixed Assets; and Intangibles.

As the consolidated financial statements of General Dynamics Corporation include the equivalent disclosures, the Company has also taken the exemptions under FRS 101 available in respect of the following disclosures:

- IFRS 2 Share Based Payments in respect of group settled share based payments, excluding the Save As You Earn scheme where equivalent disclosures are not included in the consolidated financial statements;
- Certain disclosures required by IAS 36 Impairment of assets in respect of the impairment of goodwill and indefinite life intangible assets; and
- Certain disclosures required by IFRS 13 Fair Value Measurement and the disclosures required by IFRS 7 Financial Instrument Disclosures.

The Company proposes to continue to adopt the reduced disclosure framework of FRS 101 in its next financial statements.

The accounting policies set out below have, unless otherwise stated, been applied consistently to all periods presented in these financial statements.

Measurement Convention

The financial statements are prepared on the historic cost basis except for derivatives which are stated at fair value.

The financial statements are presented in round thousands.

Going Concern

The Directors have prepared cash flow forecasts for a period of 12 months from the date of approval of these financial statements which indicate that, taking account of reasonably possible downsides on its operations and its financial resources, the Company will have sufficient funds, through funding from its ultimate parent company, General Dynamics Corporation, to meet its liabilities for that period.

Notes (continued)

1 Accounting policies (continued)

Going Concern (continued)

In preparing the forecasts, the Directors have considered reasonably possible downside scenarios.

Specifically, they have considered the following factors:

- The Company's contracts contain defined payment plans under which the Company receives cash through the life of the contract to fund activities on those contracts. The Company remains in negotiation with the UK MoD in relation to two of its significant contracts (AJAX and MORPHEUS). The Company has modelled the completion of these negotiations at two different points in the downside scenario planning.
- Separately, the Company has also considered the impact of milestone payment delays on other key contracts within its portfolio.
- The significant majority of the Company's trade is with the UK MoD. During the reporting period, the Company has seen a deterioration in payments from UK MoD, in particular the non-receipt of any payments from the UK MoD during 2022 on its AJAX contract. Whilst it is anticipated that payment will be received in the first quarter of 2023 and regular payments will recommence thereafter, the downside modelled includes a scenario in which no payments are received from the MOD in 2023. In this downside scenario parental support would be available.
- Contracts with customers other than the UK MoD have not seen a deterioration in the timeliness of receivables settlements noting that while they are with third parties, substantially all relate to either government bodies or are related to underlying contracts with government bodies (both UK and International).
- The Company continues to manage its supply chain closely to ensure continuity of supply in support of contract delivery

The Company finances its activities through its cash balances. These cash balances are held in a cash pool operated by its intermediate parent company General Dynamics European Finance Limited ("GDEF"). Under the terms of the cash pooling agreement with GDEF the Company and any other member of the cash pool may drawdown funds from GDEF. The agreement does not restrict the cash pool members to drawing down only those funds already deposited but allows cash pool members to borrow further funds from the cash pool up to GDEF's external borrowing limits. In the downside scenario described above, the Company would need to borrow from the cash pool in excess of the cash balances deposited during the forecast period. The directors are not able to assess whether GDEF would be able to provide the extent of funding which the Company requires given they cannot assess the borrowing requirements of the other cash pool members. In the event the Company cannot borrow the amounts required from the GDEF cash pool, it would instead need to rely on the support of General Dynamics Corporation, the Company's ultimate parent undertaking ("the parent").

Therefore, those forecasts are dependent on the parent not seeking repayment of amounts due to the group, which at 31 December 2021 amounted to £20.9M, and providing additional financial support during that period.

The parent has indicated its intention to continue to make available such funds as are needed by the Company, and that it does not intend to seek repayment of the amounts due at the balance sheet date, for the period covered by the forecasts.

Having made enquiries of the directors of the parent and assessed the financial position of the parent the directors are satisfied the parent has the ability, intent and economic rationale to continue to support the Company. As with any company placing reliance on other group entities for financial support, the directors acknowledge that there can be no certainty that this support will continue although, at the date of approval of these financial statements, they have no reason to believe that it will not do so. Consequently, the directors are confident that the Company will have sufficient funds to continue to meet its liabilities as they fall due for at least 12 months from the date of approval of the financial statements and therefore have prepared the financial statements on a going concern basis.

Notes (continued)

1 Accounting policies (continued)

Intangible assets

(i) Goodwill

Goodwill represents the future economic benefits arising from assets acquired in a business combination that are not individually identified and separately recognised. Such benefits include future synergies expected from the combination and intangible assets not meeting the criteria for separate recognition. Goodwill is carried at cost less accumulated impairment losses. Goodwill is not amortised and is tested annually for impairment at country level, representing the lowest level at which it is monitored for internal management purposes, by assessing the recoverable amount of each cash generating unit or groups of cash generating units to which the goodwill relates. The recoverable amount is assessed by reference to the net present value of expected future pre-tax cash flows ('value-in-use') or fair value less costs to sell if higher. When the recoverable amount of the goodwill is less than its carrying amount, an impairment loss is recognised immediately in the income statement which cannot be subsequently reversed. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold. Goodwill had been fully impaired prior to 1 January 2021.

(ii) Customer relationships

Customer relationships represent the future economic benefits arising from specific supplier or customer lists, or are party to supplier or customer relationships that are valuable. Customer relationships are held at cost less any provisions for impairment, with impairment reviews being performed annually. Amortisation commences when the Customer Relationship assets are available and is over the estimated useful life of 8 years. Customer relationships were fully amortised / impaired prior to 1 January 2021.

(iii) Other Intangibles

The other intangibles are a royalty-free licence for relief from royalty. Royalty-free licence relief is held at cost less any provisions for impairment, with impairment reviews being performed annually. Amortisation commences when the royalty-free licence relief is available and is over the estimated useful life of 8 years. Other intangibles were fully amortised / impaired prior to 1 January 2021.

(iv) Computer software

Where software is not an integral part of a related item of computer hardware, it is classified as an intangible asset. Costs that are directly associated with the acquisition or production of identifiable software products controlled by the Group, which are expected to generate economic benefits exceeding costs beyond one year, are recognised as intangible assets. Capitalised costs include those of software licences and development, including costs of employees, and consultants. Costs that are not directly attributable such as identifying, sourcing, evaluating or maintaining computer software, training and overheads are recognised as an expense as incurred. Software under development is held at cost less any provisions for impairment, with impairment reviews being performed annually. Amortisation commences when the software assets are available for use and is over their estimated useful lives of 3 to 4 years.

Tangible fixed assets and depreciation

Tangible fixed assets are stated at cost less accumulated depreciation and accumulated impairment losses. Where parts of an item of tangible fixed assets have different useful lives, they are accounted for as separate items of tangible fixed assets.

The Company recognises a right-of-use asset and a lease liability at the lease commencement date (or transition date for leases existing on the implementation of IFRS16 on 1 January 2019). At inception of a contract, the Company assesses whether a contract is, or contains, a lease. A contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. To assess whether a contract conveys the right to control the use of an identified asset, the Company uses the definition of a lease in IFRS16.

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date / transition date. The future lease payments are discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, the Company's incremental borrowing rate ('IBR'). Generally, the Company uses its incremental borrowing rate as the discount rate.

Notes (continued)

1 Accounting policies (continued)

Tangible fixed assets and depreciation (continued)

The Company determines its incremental borrowing rate by adopting the rates utilised at the corporate level. The Treasury function is managed at the European Treasury level. This function exists to provide expediency and convenience for foreign operations; however, any action including additional borrowing, requires Corporate Treasury approval. As such, European Treasury functions are not autonomous, cannot borrow funds independently and are extensions of the Corporate Treasury function. Since all funding is managed by the Corporate Treasury function, all leases of a similar term have similar risk characteristics from the lessor's perspective, regardless of the business unit. Additional funding is obtained through the Corporate Treasury function regardless of the functional currency of the lease. As such, risk is based on the consolidated treasury function and rates would remain uniform. It is considered that use of the corporate borrowing rate is appropriate due to the centralised nature of the treasury function.

The IBR is based on the NSS (Nelson, Sigel, Svensson) yield curve obtained from Bloomberg. The NSS curve is a specialised yield curve with five components that account for the shapes found in yield curves and most accurately reflects the cost of borrowing. Varying rates are applied for varying lease terms with rates published monthly. The weighted average IBR applied is 3.6506%.

Lease payments included in the measurement of the lease liability comprise the following:

- Fixed payments
- Extensions only where the contract contains an option to extend and it is reasonably certain to be exercised.
- Where variable lease payments may be possible due to the contractual existence of lease pricing reviews, the payments have been assumed to remain at their current fixed amount over the lease term given the uncertainty of future changes.

Right of use assets are measured at an amount equal to the lease liability, adjusted by the amount of any prepaid or accrued lease payments. The asset is depreciated using the straight-line method from the commencement date / remaining lease term following the transition date, to the end of the lease term.

The Company has elected not to recognise right-of-use assets and lease liabilities for leases of low-value assets and short-term leases. An asset is considered to be low-value where it has a value of less than \$5k when new. Short-term leases are those with a lease term of 12 months or less.

The Company leases several assets including property, motor vehicles and IT equipment.

The right-of-use asset is subsequently depreciated using the straight-line method from the commencement date / remaining lease term following the transition date, to the end of the lease term.

Depreciation is charged to the profit and loss account on a straight-line basis over the estimated useful lives of each part of an item of tangible fixed assets. Leased assets are depreciated over the shorter of the lease term and their useful lives. Land is not depreciated. The estimated useful lives are as follows:

Freehold Buildings:	50 years
Right-of-use assets	Life span of lease
Plant, Machinery and Motor Vehicles:	4-8 years

Depreciation methods, useful lives and residual values are reviewed at each balance sheet date.

Fixed asset investments

Investments in subsidiaries are carried at cost less provision for impairment (if any).

Notes (continued)

1 Accounting policies (continued)

Taxation

Tax on the profit or loss for the year comprises current and deferred tax. Tax is recognised in the profit and loss account except to the extent that it relates to items recognised directly in equity or other comprehensive income, in which case it is recognised directly in equity or other comprehensive income. Current tax is the expected tax payable or receivable on the taxable income or loss for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided on temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The following temporary differences are not provided for: the initial recognition of goodwill; the initial recognition of assets or liabilities that affect neither accounting nor taxable Current tax is the expected tax payable or receivable on the profit other than in a business combination, and differences relating to investments in subsidiaries to the extent that they will probably not reverse in the foreseeable future. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date. A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the temporary difference can be utilised.

Deferred taxation at 35% is applied to UK pension surplus, being the rate applicable to refunds from a scheme.

Stocks and work in progress

Stocks are stated at the lower of cost and net realisable value. Cost is based on the first-in first-out principle and includes expenditure incurred in acquiring the stocks, production or conversion costs and other costs in bringing them to their existing location and condition.

Foreign Currencies

Transactions in foreign currencies are translated to the Company's functional currencies at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are retranslated to the functional currency at the foreign exchange rate ruling at that date. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are retranslated to the functional currency at foreign exchange rates ruling at the dates the fair value was determined. Foreign exchange differences arising on translation are recognised in the profit and loss account, except for differences arising on the retranslation of qualifying cash flow hedges, which are recognised in other comprehensive income.

Research and Development

Expenditure on research activities is recognised in the profit and loss account as an expense as incurred. Expenditure on development activities is capitalised if the product or process is technically and commercially feasible and the Company intends and has the technical ability and sufficient resources to complete development, future economic benefits are probable and if the Company can measure reliably the expenditure attributable to the intangible asset during its development. Development activities involve a plan or design for the production of new or substantially improved products or processes. The expenditure capitalised includes the cost of materials, direct labour and an appropriate proportion of overheads and capitalised borrowing costs. Other development expenditure is recognised in the profit and loss account as an expense as incurred. Capitalised development expenditure is stated at cost less accumulated amortisation and less accumulated impairment losses.

Employee Benefits

Defined contribution plans

A defined contribution plan is a post-employment benefit plan under which the Company pays fixed contributions into a separate entity and will have no legal or constructive obligation to pay further amounts. Obligations for contributions to defined contribution pension plans are recognised as an expense in the profit and loss account in the periods during which employees render services.

Notes (continued)

1 Accounting policies (continued)

Employee benefits (continued)

Where members retire during the year and the value of their money purchase funds did not cover their defined benefit underpin benefits, the net shortfall would be recognised as a liability whilst they are deferred members.

Upon retirement, the money purchase funds are transferred to the defined benefit assets and the full liability for these members is recognised.

Defined benefit plans

A defined benefit plan is a post-employment benefit plan other than a defined contribution plan. The Company's net obligation in respect of defined benefit pension plans and other post-employment benefits is calculated separately for each plan by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods; that benefit is discounted to determine its present value, and the fair value of any plan assets (at bid price) are deducted. The Company determines the net interest on the net defined benefit liability/(asset) for the period by applying the discount rate used to measure the defined benefit obligation at the beginning of the annual period to the net defined benefit liability/(asset).

The discount rate is the yield at the reporting date on bonds that have a credit rating of at least AA that have maturity dates approximating the terms of the Company's obligations and that are denominated in the currency in which the benefits are expected to be paid.

Re-measurements arising from defined benefit plans comprise actuarial gains and losses, the return on plan assets (excluding interest) and the effect of the asset ceiling (if any, excluding interest). The Company recognises them immediately in other comprehensive income and all other expenses related to defined benefit plans in employee benefit expenses in profit or loss.

The calculation of the defined benefit obligations is performed by a qualified actuary using the projected unit credit method. When the calculation results in a benefit to the Company, the recognised asset is limited to the present value of benefits available in the form of any future refunds from the plan or reductions in future contributions and takes into account the adverse effect of any minimum funding requirements.

General Dynamics Retirement and Death Benefit Scheme (the Scheme)

The Company sponsors a hybrid arrangement that includes both a defined contribution section and a defined benefit section. The defined benefit section was closed from 6th April 1997, at which time members ceased to accrue benefits on a defined benefit basis. The assets of the scheme are held separately from the assets of the Company.

The defined benefit section costs and obligations depend on several assumptions and estimates. The key assumptions include mortality and interest rates used to discount estimated future liabilities. The Company determines the long-term expected rate of return on cash by reference to bank base rates, the long-term return on bonds by reference to UK long dated government and corporate bond yields, and the long-term rate of return on equities based on the rate of return on bonds allowing for forward-looking returns.

These retirement scheme estimates are based on our best judgement, including consideration of current and future market conditions. In the event any of the assumptions change, pension and post-retirement benefit cost could increase or decrease. In line with the requirements of the Scheme regulator, any shortfalls in asset value in the actuarial valuation for the defined benefit section are met by the Company over an agreed period. For additional information on the Pension Scheme, see note 24 of the Annual report and financial statements.

Paragraph 11(b) of IFRIC 14 states that if the entity's right to a refund of a surplus depends on the occurrence or non-occurrence of one or more uncertain future events not wholly within its control, the entity does not have an unconditional right and shall not recognise an asset. The Company does have an unconditional right to a refund and the pension surplus has been recognised as an asset on the balance sheet.

The Trustees of the pension fund are required by law to act in the best interests of the plan participants and during 2019 entered into a binding agreement with Legal and General to insure the liabilities of the scheme known as a buy-in. The Company is committed to convert to a buy-out.

Notes (continued)

1 Accounting policies (continued)

Employee benefits (continued)

Short-term benefits

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided. A liability is recognised for the amount expected to be paid under short-term cash bonus or profit-sharing plans if the Company has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

Termination benefits

Termination benefits are recognised as an expense when the Company is demonstrably committed, without realistic possibility of withdrawal, to a formal detailed plan to either terminate employment before the normal retirement date, or to provide termination benefits as a result of an offer made to encourage voluntary redundancy. Termination benefits for voluntary redundancies are recognised as an expense if the Company has made an offer of voluntary redundancy, it is probable that the offer will be accepted, and the number of acceptances can be estimated reliably. If benefits are payable more than 12 months after the reporting date, then they are discounted to their present value.

Employee share schemes

The share option programme allows employees to acquire shares in the Company's ultimate parent. The fair value of options granted after 7 November 2002 and those not yet vested as at the effective date of IFRS 2, is recognised as an employee expense with a corresponding increase in equity. The fair value is measured at grant date and spread over the period during which the employees become unconditionally entitled to the options. The fair value of the options granted is measured using a Black - Scholes option pricing model, taking into account the terms and conditions upon which the options were granted. The amount recognised as an expense is adjusted to reflect the actual number of share options that vest except where variations are due only to share prices not achieving the threshold for vesting.

For cash settled share based payment transactions, the fair value of the amount payable to the employee is recognised as an expense with a corresponding increase in liabilities. The fair value is initially measured at grant date and spread over the period during which the employees become unconditionally entitled to payment. The fair value is measured based on an option pricing model taking into account the terms and conditions upon which the instruments were granted. The liability is revalued at each balance sheet date and settlement date with any changes to fair value being recognised in the profit and loss account.

Financial Instruments

Recognition and initial measurement

Trade receivables and debt securities are initially recognised when they are originated. All other financial assets and financial liabilities are initially recognised when the Company becomes a party to the contractual provisions of the instrument.

A financial asset (unless it is a trade receivable without a significant financing component) or financial liability is initially measured at fair value plus, for an item not at 'fair value through profit or loss' (FVTPL), transaction costs that are directly attributable to its acquisition or issue. A trade receivable without a significant financing component is initially measured at the transaction price.

Classification and subsequent measurement

Financial assets

Classification

On initial recognition, a financial asset is classified as measured at amortised cost; Fair Value through OCI ('FVOCI') or FVTPL.

Financial assets are not reclassified subsequent to their initial recognition unless the Company changes its business model for managing financial assets in which case all affected financial assets are reclassified on the first day of the first reporting period following the change in the business model.

A financial asset is measured at amortised cost if it meets both of the following conditions:

Notes (continued)

1 Accounting policies (continued)

Financial Instruments (continued)

- It is held within a business model whose objective is to hold assets to collect contractual cash flows; and
- Its contractual terms give rise on specified dates to cash flows that are solely principal and interest on the principal amount outstanding.

A debt instrument is measured at fair value through other comprehensive income (FVOCI) if it meets both of the following conditions:

- It is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets; and
- Its contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

On initial recognition of an equity investment that is not held for trading, the Company may irrevocably elect to present subsequent changes in the investment's fair value in OCI. This investment is made on an investment-by-investment basis.

All financial assets not classified as measured at amortised cost or FVOCI as described above are measured at FVTPL. This includes all derivative financial assets.

Investments in joint ventures are carried at cost less impairment.

Subsequent measurement of gains and losses

Financial assets at FVTPL – these assets (other than derivatives designated as hedging instruments) are subsequently measured at fair value. Net gains and losses, including any interest or dividend income, are recognised in profit or loss.

Financial assets at amortised cost – these assets are subsequently measured at amortised cost using the effective interest method. The amortised cost is reduced by impairment losses. Interest income, foreign exchange gains and losses and impairment are recognised in profit or loss. Any gain or loss on de-recognition is recognised in profit or loss.

Debt instruments at FVOCI – these assets are subsequently measured at fair value. Interest income calculated using the effective interest method, foreign exchange gains and losses and impairment are recognised in profit or loss. Other net gains and losses are recognised in OCI. On de-recognition, gains and losses accumulated in OCI are reclassified to profit or loss.

Equity investments at FVOCI – these assets are subsequently measured at fair value. Dividends are recognised as income in profit or loss unless the dividend clearly represents a recovery of part of the cost of the investment. Other net gains and losses are recognised in OCI and are never reclassified to profit or loss.

De-recognition of financial assets

The Company recognises a financial asset only when the contractual rights to the cash flows from the asset expire, or when it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity.

Financial liabilities and equity

Classification

Financial instruments issued by the Company are treated as equity only to the extent that they meet the following two conditions:

- They include no contractual obligations upon the Company to deliver cash or other financial assets or to exchange financial assets or financial liabilities with another party under conditions that are potentially unfavourable to the Company; and

Notes (continued)

1 Accounting policies (continued)

Financial liabilities and equity (continued)

- Where the instrument will or may be settled in the Company's own equity instruments, it is either a non-derivative that includes no obligation to deliver a variable number of the Company's own equity instruments or is a derivative that will be settled by the Company exchanging a fixed amount of cash or other financial assets for a fixed number of its own equity instruments.

To the extent that this definition is not met, the proceeds of issue are classified as a financial liability. Where the instrument so classified takes the legal form of the Company's own shares, the amounts presented in these financial statements for called up share capital and share premium account exclude amounts in relation to those shares.

Financial liabilities are classified as measured at amortised cost or FVTPL. A financial liability is classified as at FVTPL if it is classified as held-for-trading, it is a derivative or it is designated as such on initial recognition. Financial liabilities at FVTPL are measured at fair value and net gains and losses, including interest expense, are recognised in profit or loss. Other financial liabilities are subsequently measured at amortised cost using the effective interest method. Interest expense and foreign exchange gains and losses are recognised in profit or loss. Any gain or loss on de-recognition is also recognised in profit or loss.

De-recognition of financial liabilities

The Company derecognises financial liabilities when the Company's obligations are discharged, cancelled or they expire.

Effective Interest Method

The effective interest method is a method of calculating the amortised cost of a debt instrument and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts through the expected life of the debt instrument, or, where appropriate, a shortened period, to the net carrying amount on initial recognition.

Income is recognised on an effective interest basis for debt instruments other than those financial assets classified as at FVTPL.

Derivative financial instruments and hedging

Derivative financial instruments

The Company enters into forward contracts as derivative financial instruments to manage its exposure to foreign exchange rate risk.

Derivatives are initially recognised at fair value at the date a derivative contract is entered into and are subsequently re-measured to their fair value at each balance sheet date. The resulting gain or loss is recognised in profit or loss immediately unless the derivative is designated and effective as a hedging instrument, in which event the timing of the recognition in profit or loss depends on the nature of the hedge relationship.

Hedge accounting

The Company designates certain hedging instruments in respect of foreign currency risk as cash flow hedges where the hedges are of foreign exchange risk on firm commitments.

At the inception of the hedge relationship, the entity documents the relationship between the hedging instrument and the hedged item, along with its risk management objectives and its strategy for undertaking various hedge transactions. Furthermore, at the inception of the hedge and on an ongoing basis, the Company documents whether the hedging instrument is highly effective in offsetting changes in cash flows of the hedged item.

Cash flow hedges

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges are recognised in other comprehensive income. The gain or loss relating to the ineffective portion is recognised in profit or loss, and is included in the 'other gains and losses' line item.

Notes (continued)

1 Accounting policies (continued)

Derivative financial instruments (continued)

Amounts previously recognised in other comprehensive income and accumulated in equity are reclassified to profit or loss in the periods when the hedged item is recognised in profit or loss, in the same line of the income statement as the recognised hedged item. However, when the forecast transaction that is hedged results in the recognition of a non-financial asset or a non-financial liability, the gains and losses previously accumulated in equity are transferred from equity and included in the initial measurement of the cost of the non-financial asset or non-financial liability.

Hedge accounting is discontinued when the Company revokes the hedging relationship, the hedging instrument expires or is sold, terminated, or exercised, or no longer qualifies for hedge accounting. Any gain or loss recognised in other comprehensive income at that time is accumulated in equity and is recognised when the forecast transaction is no longer expected to occur. The gain or loss accumulated in equity is recognised immediately in profit or loss.

Certain ineffectiveness can arise during the hedging process. The main sources of hedge ineffectiveness are considered to be timing differences between entering into the hedged items and into the hedging instruments and differences between the maturity profile of the hedged items and the hedging instruments.

Impairment

Financial assets, other than those at FVTPL, are assessed for indicators of impairment at each balance sheet date. Financial assets are impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows have been affected.

When determining whether credit risk of a financial asset has increased significantly since initial recognition and when estimating Expected Credit Losses (ECL), the Company considers reasonable and supportable information which is relevant and available without undue cost of effort. This includes both quantitative and qualitative information and analysis, based on the Company's historical experience and informed credit assessment, including forward looking information.

Objective evidence of impairment could include:

- Significant financial difficulty of the issuer or counterparty; or
- Default or delinquency in interest or principal payments; or
- It becoming probable that the borrower will enter bankruptcy or financial re-organisation.

Loss allowances for trade receivables and contract assets (as defined in IFRS 15) are always measured at an amount equal to lifetime ECL. Lifetime ECLs are the ECLs that result from all possible default events over the expected life of a financial instrument. 12-month ECLs are the portion of ECLs that result from default events that are possible within the 12 months after the reporting date (or a short period if the expected life of the instrument is less than 12 months). The maximum period considered when estimating ECLs is the maximum contractual period over which the Company is exposed to credit risk.

For financial assets carried at amortised cost, the amount of the impairment is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the financial asset's effective interest rate.

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade receivables, where the carrying amount is reduced through the use of an allowance account. When a trade receivable is considered uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognised in profit or loss.

In a subsequent period, if the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed through profit or loss to the extent that the carrying amount of the investment at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised.

Measurement of ECLs

ECLs are probability-weighted estimates of credit losses. Credit losses are measured as the present value of all cash shortfalls (i.e. the difference between cash flows due to the entity in accordance with the contract and the cash flows the Company expects to receive). ECLs are discounted at the effective interest rate of the financial asset.

Notes (continued)

1 Accounting policies (continued)

Impairment (continued)

Credit-impaired financial assets

At each reporting date, the Company assesses whether financial assets carried at amortised cost and debt securities at FVOCI are credit-impaired. A financial asset is 'credit-impaired' when one or more events that have a detrimental impact on the estimated future cash flows of the financial asset have occurred.

Write-offs

The gross carrying amount of a financial asset is written off to the extent that there is no realistic prospect of recovery.

2 Turnover

Turnover has been wholly derived from the operation of design, production and support of armoured vehicles, avionic, communications and associated electronic equipment, which originates in the United Kingdom. The analysis of turnover by geographical destination is as follows:

	2021 £000	2020 £000
United Kingdom	591,020	723,465
Rest of Europe	1,015	5,560
North America	9,102	974
Rest of the World	3,236	4,834
	<u>604,373</u>	<u>734,833</u>

3 Staff numbers and costs

The average number of persons employed by the Company (including directors) during the year, analysed by category, was as follows:

	Number of employees	
	2021	2020
Administration	266	313
Production	1,001	1,019
	<u>1,267</u>	<u>1,332</u>

The aggregate payroll costs of these persons were as follows:

	2021 £000	2020 £000
Wages and salaries	68,159	70,789
Social security costs	6,699	7,046
Other pension costs (see note 24)	9,850	10,375
	<u>84,708</u>	<u>88,210</u>

Wages and salaries includes severance of £879k (2020: £1.062k). Wages and salary in 2020 were exclusive of severance.

Notes (continued)

4 Leases

The Company leases commercial property for its operations. The leases typically run for a period of 5 years with no option to renew. One lease is for the land on which a Company owned commercial building is located. This lease does contain an option to renew and runs for 125 years. The lease payments on the land are negotiated every 10 years to reflect market rentals and were last agreed on 1 January 2015. The value recognised in the accounts assumes that lease payments are fixed as it is not possible to accurately forecast changes in value as a result of future inflationary adjustments.

Other leases that represent right-of-use-assets include vehicles, IT equipment and property utilised by certain business travellers. The Company has elected not to recognise right-of-use assets and lease liabilities for leases of low value or term (where the lease is for a period of less than 1 year).

Calculation of the incremental borrowing rate is detailed in note 1. The weighted average applied is 3.6506%.

The Company presents right-of-use assets as tangible assets with lease liabilities split between creditors due within one year and in more than one year accordingly on the balance sheet.

Right-of-use assets

	Long leasehold Land & buildings £000	Short leasehold Land & buildings £000	Vehicles £000	IT Equipment £000	Total £000
Balance at 1 January 2021	1,243	5,445	152	984	7,824
Additions to right-of-use assets	-	1,230	119	1,555	2,904
Disposals of right-of-use assets	-	(207)	-	(1,092)	(1,299)
Depreciation of right-of-use assets	(14)	(1,533)	(128)	(568)	(2,243)
Depreciation on disposal		166		550	716
Balance at 31 December 2021	1,229	5,101	143	1,429	7,902

Amounts recognised in profit and loss

Leases under IFRS16

	2021 £000	2020 £000
Interest on lease liabilities	215	262
Expenses relating to short term leases	100	205
Expenses relating to leases of low value assets	131	148
Depreciation of leased assets	2,243	2,440
	2,689	3,055

Expenses relating to short term leases are shown in the profit and loss account within the expense category associated with the nature of the expense.

5 Other interest receivable and similar income

	2021 £000	2020 £000
Bank interest	69	82
Pension interest	35	78
Gain on foreign exchange	48	-
	152	160

Notes (continued)

6 Interest payable and similar charges

	2021 £000	2020 £000
Other interest payable	(1,525)	(324)
Loss on foreign exchange	-	(2,558)
Interest on lease liabilities	(215)	(262)
	<u>(1,740)</u>	<u>(3,144)</u>

7 Other gains and losses

	2021 £000	2020 £000
(Loss) / gain recognised on ineffective hedge	(28)	771
	<u>(28)</u>	<u>771</u>

8 Profit on ordinary activities before taxation

	2021 £000	2020 £000
The profit on ordinary activities before taxation is stated after charging/(crediting):		
Short-term Leases/Operating leases		
- Land and buildings	90	138
- Motor vehicles and office equipment	141	215
Research and development	3,975	3,570
Profit on disposal of leased assets	37	26
Depreciation of owned fixed assets	2,407	2,140
Depreciation of leased assets	2,243	2,440
Intangible amortisation	146	487
IFRS 2 share based payment charges	(1,289)	774
)	
Restructuring (reversal) / charge	(134)	596
Auditor's Remuneration		
Audit of these Financial Statements	383	349
Taxation compliance services	100	100
Non audit financial services	32	-

The restructuring credit in the profit and loss account has arisen following the reversal of an over accrual in 2020.

Notes (continued)

9 Directors' remuneration

	2021 £000	2020 £000
Directors' emoluments	302	502
Company contributions to money purchase pension schemes	6	43

Two Directors exercised share options in the ultimate parent company in the year (2020: two). The above amounts do not include any gains made on the exercise of share options. Gains made on the exercise of share options by these Directors were £0.3m (2020:£1.9m). These shares had an average market price of £116.34 (2020:£134.53). One of the Directors' emoluments represent the intercompany recharge of their salary for time spent on affairs of the Company.

Pensions

The number of Directors who were members of pension schemes was as follows:

	2021 Number	2020 Number
Hybrid pension	1	2

Highest paid director

The above amounts for remuneration include the following in respect of the highest paid Director:

	2021 £000	2020 £000
Directors' emoluments	147	381
Company contributions to pension schemes	-	-

No Director had a direct or indirect interest in any transaction, arrangement or agreement, which in the opinion of the other Directors requires disclosure under the provisions of the Companies Act 2006.

Notes (continued)

10 Taxation

	2021 £000	2020 £000
UK deferred tax (see note 19)	866	(173)
UK current tax	2,126	10,071
Adjustments in respect of prior periods	85	(1,536)
	<hr/>	<hr/>
Income statement	3,077	8,362
	<hr/>	<hr/>
	2021	2020
	£000	£000
Reconciliation of effective tax rate		
<i>Profit for year</i>	10,366	66,964
Total tax expense	3,077	8,362
	<hr/>	<hr/>
Profit excluding taxation	13,443	75,326
<i>Tax using the Corporate tax rate of 19% (2020: 19%)</i>	2,554	14,312
Non-deductible expenses	148	(3,781)
Tax exempt revenues	(89)	(221)
Capital allowances for year in excess of depreciation	(487)	(138)
Under/(over) provided in prior years	85	(1,536)
Group relief claimed	-	(101)
Deferred tax	866	(173)
	<hr/>	<hr/>
Total tax expense	3,077	8,362
	<hr/>	<hr/>
Income tax recognised in other comprehensive income		
Deferred tax		
Net gain/ (loss) on revaluation of cash flow hedges	(3,156)	2,241
	<hr/>	<hr/>
Total income tax recognised in other comprehensive income	(3,156)	2,241
	<hr/>	<hr/>

An increase in the UK corporation tax rate from 19% to 25% (effective 1 April 2023) was substantively enacted on 24 May 2021. The deferred tax liability as at 31 December 2021 has been calculated at 25% (2020:19%) resulting in a deferred tax liability approximately £540k greater than if a rate of 19% had continued.

Notes (continued)

11 Intangible assets

	Goodwill	Customer relationships	Other	Software	Total
	£000	£000	£000	£000	£000
Cost					
At 1 January 2021	17,141	14,200	1,820	6,956	40,117
Additions	-	-	-	126	126
At 31 December 2021	17,141	14,200	1,820	7,082	40,243
Accumulated amortisation and impairment					
Accumulated impairment	17,141	14,200	1,820	6,380	39,541
Amortisation charge for the year	-	-	-	146	146
Amortisation and impairment	17,141	14,200	1,820	6,526	39,687
Net book value	-	-	-	556	556
At 31 December 2021					
Net book value	-	-	-	576	576
At 31 December 2020					

Investments

Investment entity	Holding company	Share capital	Proportion held	Loss in year £000
General Dynamics Information Systems and Technology Arabia Company, Olaya Area, Al-Munajem Building, PO Box 30505, Riyadh 11361	General Dynamics UK Ltd	SAR12,000,000	49%	-

All investments have been written down to zero in prior years.

Notes (continued)

12 Tangible fixed assets

	Premises land and buildings £000	Long leasehold land and Buildings £000	Short leasehold land and buildings £000	Plant machinery and vehicles £000	Leased plant machinery and vehicles £000	Total £000
Cost						
At 1 January 2021	29,220	2,933	11,845	40,829	2,485	87,312
Adjustment to opening balance	-	11	-	57	-	68
Additions (excluding IFRS16)	-	26	-	2,382	-	2,408
IFRS16 additions	-	-	1,230	-	1,674	2,904
Disposals	-	-	(207)	-	(1,092)	(1,299)
At 31 December 2021	29,220	2,970	12,868	43,268	3,067	91,393
Depreciation						
At 1 January 2021	5,750	1,708	6,388	33,109	1,349	48,304
Charge for year (excluding IFRS16)	555	103	-	1,749	-	2,407
IFRS16 charge for year	-	14	1,533	-	696	2,243
Disposals	-	-	(166)	-	(550)	(716)
At 31 December 2021	6,305	1,825	7,755	34,858	1,495	52,238
Net book value						
At 31 December 2021	22,915	1,145	5,113	8,410	1,572	39,155
At 31 December 2020	23,470	1,225	5,457	7,720	1,136	39,008

Land not depreciated was valued at £2,204k (2020: £2,204k).

13 Stocks and work in progress

	2021 £000	2020 £000
Raw materials and consumables	404	531

Given the nature of the contracts, contract stock is booked to cost of sales as utilised in the year. Immaterial amounts are expensed to the income statement. There was no write-down of stock to net realisable value nor reversal of write-downs.

Notes (continued)

14 Debtors

	2021 £000	2020 £000
Amounts falling due within one year:		
Amounts owed by related parties	4,515	199,915
Amounts recoverable on contracts	1,008,310	494,989
Taxation and social security	24,534	-
Trade debtors	12,100	11,344
Prepayments and other debtors	15,925	14,422
Total amounts falling due within one year	1,065,384	720,670
Debtor amounts greater than one year		
Trade debtor	15,678	15,678
Amounts recoverable on contracts	500	1,000
Pension surplus (see note 24)	3,005	2,626
Foreign exchange hedge asset (see note 17)	54	7,646
Total debtors	1,084,621	747,620

Debtors falling due within one year are all expected to be recoverable within one year. The trade debtor greater than one year relates to the award of a default judgement against the State of Libya in favour of the Company. Substantial work is being undertaken to recover the debt and recovery is not expected within one year. Amounts owed by related parties comprise the following: The Amounts recoverable on contracts of £1,008,310, (2020 £494,989) has increased in line with the retention of payments by the UK MoD as a path forward is agreed.

Amounts owed by related parties comprise the following:

	2021 £000
General Dynamics Land Systems Canada Corporation	613
General Dynamics European Finance Ltd	23
General Dynamics Ltd	24
General Dynamics Mission Systems International Ltd	35
General Dynamics Swiss Financial Management Ltd	4
General Dynamics Global Holdings Ltd	70
GPS Source Inc	6
General Dynamics Mission Systems Inc	3,365
General Dynamics Mission Systems Italy SRL	375
	4,515

Payment terms are as determined by the related party and / or in accordance with agreed milestone payment plans. The balance owed by General Dynamics European Finance Ltd is the result of the sweeping of principal accounts to manage the collective cash needs of the cash pool member companies. This balance is deemed repayable on demand with interest calculated at LIBOR.

Notes (continued)

15 Creditors: amounts falling due within one year

	<u>2021</u>	<u>2020</u>
	<u>£000</u>	<u>£000</u>
Obligations under right of use assets (see note 18)	2,417	2,399
Payments on account on long term contracts	65,844	26,513
Trade creditors	99,567	223,145
Taxation and social security	-	26,596
Accruals	22,309	18,798
Deferred tax liability (see note 19)	-	4,842
Amounts owed to related undertakings	530,148	375
Welsh Development Agency grant	1,084	1,084
Foreign exchange hedge liability (see note 17)	5,561	204
Cash	127	-
	<u>727,057</u>	<u>303,956</u>

16 Creditors: amounts falling due after more than one year

	2021	2020
	£000	£000
Foreign exchange hedge liability (see note 17)	41	134
Obligations under right of use assets (see note 18)	5,668	5,592
Welsh Development Agency grant	2,167	3,267
	<u>7,876</u>	<u>8,993</u>

The £7.7m Welsh Development Grant was received in 2016 in order to help fund the development of the Merthyr Tydfil site. The grant is repayable in equal instalments over 7 years.

Amounts owed to related undertakings comprise the following:

	2021
	£000
GD Santa Barbara Sistemas S.A	84,004
General Dynamics Corporation	1,037
General Dynamics Land Systems Inc	431
General Dynamics Land Systems Canada Corporation	824
General Dynamics Mission Systems Inc	6,562
Jet Aviation Management AG	43
General Dynamics Information Technology Inc	14
General Dynamics Global Holdings Ltd	329
General Dynamics European Finance Ltd	436,904
	<u>530,148</u>

Payment terms are as determined by the related party and / or in accordance with agreed milestone payment plans. Invoices processed and approved for payment are generally settled in the month. The balance owed to General Dynamics European Finance Ltd is the result of the sweeping of principal accounts to manage the collective cash needs of the cash pool member companies. This balance is deemed repayable on demand with interest calculated at LIBOR + 80bps.

Notes (continued)

17 Other financial asset and liabilities

	2021	2020
	Assets	Assets
	£000	£000
Current		
Gross cash flow hedges held at fair value – foreign exchange asset	1,670	9,122
Gross cash flow hedges held at fair value – foreign exchange liability (see note 15)	(5,561)	(204)
Non-current		
Gross cash flow hedges held at fair value – foreign exchange asset (see note 14)	54	7,646
Gross cash flow hedges held at fair value – foreign exchange liability (see note 16)	(41)	(134)
	<u>(3,878)</u>	<u>16,430</u>

During the year, gains of £80k on non-qualifying hedges were credited to the income statement (2020: 2,980k)

Financial risk management Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates, interest rates and equity prices will affect the Company's income or the value of its holdings of financial instruments.

The foreign currency exchange rate risk relates to receipts from customers, payments to suppliers and inter-company transactions denominated in foreign currencies. To the extent possible, the Company include terms in its contracts that are designed to protect it from this risk. The Company will also seek to reduce the impact of foreign exchange risk by concluding transactions in the Company's functional currency or naturally hedging income and expenses in a foreign currency. Otherwise, it enters into derivatives, principally foreign currency forward purchase and sale contracts, designed to offset and minimise its risk. The Company does not use derivatives for trading or speculative purposes.

To further reduce market price risk resulting from changes in price, the Company enters into fixed price contracts with customers and suppliers.

Credit risk

Credit risk is the risk of financial loss to the Company if a customer fails to meet its contractual obligations and arises principally from the Company's receivables from customers.

Credit risk is considered low given that the majority of sales are to UK and overseas governments.

Liquidity risk and cash flow risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. Cash flow risk is the risk that the Company's available cash will not be sufficient to meet its financial obligations.

The Company's liquidity is ensured by means of regular group-wide monitoring and planning of liquidity coordinated by the Group's centralised treasury department. The Group consists of the members of the European cash pool agreement.

In order to facilitate cash management activities, the Company has entered into a cash pool agreement for which General Dynamics European Finance Ltd operates as the cash pool leader. The zero balancing cash pool consists of four underlying pools of different currencies (Euro, Swiss Francs, USD and GBP). Cash pool members pool their accounts to obtain a reduction in external financing costs and can obtain more favourable credit and debit interest rates due to economies of scale. The cash pooling arrangement and regular forecasting of cash needs by the cash pool members significantly reduces any cash flow risk to the Company. As a cash pool member, the Company has requested that General Dynamics Worldwide Holdings Inc. (the guarantor) guarantees potential claims for payment of funds to General Dynamics European Finance Ltd in accordance with the terms of the cash pool agreement. As such, the guarantor unconditionally, absolutely and irrevocably guarantees the payment obligations of the Company arising from the cash pool.

Notes (continued)

18 Obligations under right of use assets

The maturity of obligations under right of use assets is as follows:

	2021 £000	2020 £000
Within one year	2,417	2,399
In the second to fifth years	4,644	4,539
Later than five years	1,023	1,053
	<u>8,084</u>	<u>7,991</u>

19 Provisions for liabilities and charges

	01-Jan-21 £'000	Recognised in income £'000	Recognised in equity £'000	31-Dec-21 £'000
Deferred tax	4,842	866	(3,156)	2,552
Warranty provision charge / (release)	25,010	(10,688)	-	14,322
	<u>29,852</u>	<u>(9,822)</u>	<u>(3,156)</u>	<u>16,874</u>

Deferred tax was previously disclosed within creditors: amounts falling due within one year on the balance sheet and has been moved to provisions for the year ended 31 December 2021. The prior year deferred tax comparative included as a creditor in 2020 is £4.8m.

The warranty provision has been re-profiled in recognition of the additional development and refinements to the vehicles which will now be embedded as part of the revised delivery schedules. It also now encompasses information that has been gained from the further testing and use of the vehicles and is better aligned to the group wide experience on similar programmes.

Deferred tax assets and liabilities

	01-Jan-21 £'000	Recognised in income £'000	Recognised in equity £'000	31-Dec-21 £'000
Tangible fixed assets	1,531	1,269	-	2,800
Share-based payments	(17)	(535)	-	(552)
Pension	919	132	-	1,051
Hedge Loss	2,409	-	(3,156)	(747)
	<u>4,842</u>	<u>866</u>	<u>(3,156)</u>	<u>2,552</u>

The deferred tax on the pension scheme surplus was calculated at a rate of 35% which reflects the rate of tax payable on any return of the defined benefit pension surplus rather than the 25%. A rate of 19% has been used for calculation of deferred tax on the hedge loss as it is expected to unwind within 1 year.

Notes (continued)

19 Provisions for liabilities and charges (continued)

The elements of deferred taxation are as follows:

	2021 £000	2020 £000
Deferred tax on pension scheme surplus	1,051	919
Income Statement		
Difference between accumulated depreciation and capital allowances	2,800	1,531
Other timing differences	(552)	(17)
Other Comprehensive income		
Other timing differences	(747)	2,409
	<hr/>	<hr/>
Deferred tax liability	2,552	4,842
	<hr/>	<hr/>

20 Share capital

The share capital of the Company comprises ordinary shares of 50p each.

	Number of Shares	2021 £000	Number of Shares	2020 £000
Allotted, called-up and fully paid	18,523,150	9,262	18,523,150	9,262

21 Hedging reserve

	2021 £000	2020 £000
Opening balance	10,270	821
Effect of change in tax rate	-	(20)
Gain / loss recognised on cash flow hedges		
Foreign currency forward contracts	(14,228)	12,649
Income tax related to losses recognised in other comprehensive income	752	(2,556)
Transfer to income statement:		
Foreign currency forward contract ineffectiveness	28	(771)
Income tax related to gains / (losses) transferred to income	(5)	147
	<hr/>	<hr/>
Closing balance	(3,183)	10,270
	<hr/>	<hr/>

The fair value of foreign currency forward contracts is estimated by discounting the difference between the contractual forward price and the current forward price for the residual maturity in the contract using a risk-free interest rate.

The hedging reserve represents the cumulative amount of gains and losses on hedging instruments deemed effective in cash flow hedges. The cumulative deferred gain or loss on the hedging instrument is recognised in income statement when the hedge transaction impacts the income statement. The gain or loss relating to the ineffective portion is recognised in the income statement and is included in the 'other gains and losses' line item. A loss of £1.032k was recycled to the income statement on maturity of the qualifying hedges.

Notes (continued)

21 Hedging reserve (continued)

The ineffectiveness relates to differences in the forecast cash flows for which a foreign currency forward contract was entered to in order to mitigate foreign currency exposure. These forecast cash flows were based on management's best judgement at the time the hedges were put in place as this preceded the signing of the subcontract agreement with the supplier in December 2020 in connection with the AJAX contract. Following the signing of the subcontract, additional hedges were arranged in 2021 to align with the subcontract.

Where identification of hedged items are performed by reference to time buckets and a hedge transaction occurs outside of that time bucket, it cannot be considered to be the same hedged item. If there are no cash flows within a time bucket, then there can be no hedged item. To the extent that insufficient cash flow can be allocated against a hedge instrument within the "time bucket," hedge ineffectiveness is recognised on the remaining deficit with the corresponding gain / loss moved from reserves to the profit and loss account.

Implementation Guidance in the previous IAS39 suggests that a 3-month layering approach for the designation of highly probable forecast transactions designated in cash flow hedging relationships may be appropriate. In the absence of specific implementation guidance in IFRS9, consideration has also been given to commercial considerations and a desire to settle invoices within 30 days. As a result, a time bucket of 30 days prior to hedge maturity and 30 days after hedge maturity has been adopted.

22 Financial commitments

(a) Capital commitments at the end of the financial year, for which no provision has been made, are as follows:

	2021 £000	2020 £000
Contracted	264	173
Authorised but not contracted	1,507	7
	<u>1,771</u>	<u>180</u>

(b) Aggregate commitments for low value and short-term leases are as follows:

	2021		2020	
	Land and buildings £000	Other £000	Land and buildings £000	Other £000
Non right-of-use assets which expire:				
Within one year	33	78	23	110
In the second to fifth years inclusive	-	64	-	23
	<u>33</u>	<u>142</u>	<u>23</u>	<u>133</u>

Notes (continued)

23 Contingent liabilities

	2021	2020
	£000	£000
Offset bond expressed in AED	AED 4,195k	AED 4,195k
- expressed in GBP	£851k	£835k

The offset bond was a requirement of a contract that the Company held in the United Arab Emirates where as part of the terms and conditions of the contract, the Company is required to provide in country services such as knowledge transfer or invest in local product development activity. If the Company were unsuccessful with these activities, the bond would be retained. The value has been converted into GBP at a spot rate at the Balance Sheet date of 0.203.

24 Pension scheme

The Company sponsors the General Dynamics Retirement and Death Benefit Scheme ('the Scheme'). The Scheme is a hybrid arrangement, which includes both a defined contribution section and a defined benefit section comprising of current and deferred pensioners. The defined benefit section of the Scheme was closed from 6 April 1997, at which time members ceased to accrue benefits on a defined benefit basis and were given the option to transfer their benefits to the defined contribution section of the Scheme. The assets of the Scheme are held separately from those of the Company, being invested with an external fund manager. The expenses of the Scheme are borne by the Company.

The defined benefit pension scheme of General Dynamics Information Technology Ltd (GDIT: a related party) was transferred to the Company in 2019 following the cessation of trade of GDIT and remains an entirely separate scheme to that of General Dynamics United Kingdom Ltd. A binding agreement was entered into with Legal and General to insure the liabilities of the GDIT scheme known as a buy-in with the full intention to convert to a buy-out. The detail contained in this note excludes the GDIT scheme due to immateriality other than where certain financial disclosures are required to reconcile to the financial statements. Where GDIT disclosures have been included, the notes reflect the consolidated position for both schemes. The IAS19 2019 accounting disclosures allowed for the impact of the buy in by extinguishing the value of the liabilities and corresponding assets, leaving a surplus of £25,000. Since there has been no further action on the scheme during 2021 and, given the immateriality of the scheme, it was not considered necessary to prepare full IAS19 disclosures for the GDIT scheme in 2021 and therefore the financial statements continue to recognise a surplus of £25,000.

Defined contribution element

The pension cost for the year was £9,849,582 (2020: £10,250,179) being contributions to the defined contribution plan and £175,000 of expenses paid out of planned assets in respect of the defined benefit plan. There were no outstanding or prepaid contributions at 31 December 2021 (2020: £nil).

Defined Benefit Section

A full actuarial valuation of this scheme was carried out by a qualified independent actuary at 5 April 2021. This has been updated on an approximate basis to 31 December 2021.

During 2019, the trustees purchased an insurance policy that covers all the retirement benefit obligations within the scheme, thereby removing exposure to the significant risks within the scheme. The impact of this buy-in was accounted for as a settlement in the 31 December 2019 financial statements. There have been no other plan amendments, curtailments or settlements in the year ended 31 December 2021.

The scheme's insurer is responsible for ensuring that there are sufficient assets to meet all future pension obligations, and is subject to EU solvency regulations. There is no volatility associated with the insurance policy asset as under IAS19 its value is deemed to match the scheme liabilities. Asset volatility is limited only to the assets remaining in the scheme which are expected to meet additional costs with any balance returned to the Company on wind-up of the scheme. Additional assets invested with Legal & General remain within the scheme. These assets represent the balance from the premium paid to complete the buy-in and will be used to meet the cost of any potential GMP equalisation adjustment required to the insured members and expenses. Tax of 35% has been recognised on the remaining surplus which is payable on any amount returned to the Company on the winding-up. The value of insured assets are matched against the value of liabilities with the remaining invested assets (£2m net of deferred tax) included within plan assets and recognised on the balance sheet. No contributions have been made in the year.

Notes (continued)

24 Pension scheme (continued)

Assumptions

The inflation risk premium has been set based on the Gilt Inflation Curve (2020: Gilt Inflation Curve less 0.1% p.a. each term)) For CPI, the long term gap between RPI and CPI has been reduced from 0.7% to 0.6% until 2030 reflecting the belief that the market has largely adjusted to changes to RPI with an RPI/CPI gap from 2030 of nil.

In line with IAS19, mortality assumptions are based on the CMI 2020 model.

The mortality assumptions adopted at 31 December 2021 imply the following life expectancies:

Male retiring in 2021	22.1
Female retiring in 2021	23.9
Male retiring in 2041	23.4
Female retiring in 2041	25.4

Expected long term rates of return

The long-term expected rate of return on cash is determined by reference to bank base rates at the balance sheet dates. The long-term expected return on bonds is determined by reference to UK long dated government and corporate bond yields at the balance sheet date. The long-term expected rate of return on equities is based on the rate of return on bonds with an allowance for out-performance.

The expected long-term rates of return applicable for each period are as follows:

	Period commencing 01/01/2022 % per annum	Period commencing 01/01/2021 % per annum
Buy-in policy	1.20%	0.70%
Equity	-	-
Bonds	-	-
Gilts	1.20%	0.70%
Property	-	-
Multi Asset Fund	5.2%	4.7%
Cash	2.0%	1.45%
Overall for scheme	1.33%	0.82%

The assets of the scheme have been taken at market value and the liabilities have been calculated using the following principal actuarial assumptions:

	2021	2020	2019
Revaluation rate for deferred pensioners	3.03%	2.64%	2.18%
Rate of increase in pensions in payment and deferred pensions	3.03%	2.64%	2.18%
Discount rate applied to scheme liabilities	1.77%	1.45%	2.09%
Inflation assumption	3.43%	3.04%	2.88%

In valuing the liabilities of the pension fund at 31 December 2021, mortality assumptions have been made as indicated above. If life expectancy had been changed to assume that all members of the fund lived for one year longer, the value of the reported liabilities at 31 December 2021 would have increased by £1,045k before deferred tax. The value of the reported assets will also increase by this same amount due to the insurance policy on buy-in.

The table below sets out the fair value of assets, a breakdown of the assets into the main asset classes, the present value of the IAS 19 liabilities and the surplus of assets below the IAS 19 liabilities (which equals the gross pension asset). While there remains considerable uncertainty over movements in financial markets, given the nature of the assets (the majority being annuities which match liabilities held) we would not expect there to be a material impact since the balance sheet date compared to that shown in the report.

Notes (continued)

24 Pension scheme (continued)

Scheme assets

None of the fair values of the assets shown below include any direct investments in the Company's own financial instruments or any property occupied by, or other assets used by, the Company. All of the scheme assets have a quoted market price in an active market with the exception of the Trustee's bank account balance. There are no additional assets pledged, and no additional arrangements agreed between the Company and trustees to secure members' benefits under the plan.

	2021 £000	2020 £000
Fair value of plan assets	26,846	29,588
Present value of funded deferred benefit obligations	(23,895)	(27,015)
Historic contribution adjustment	53	53
Surplus	3,004	2,626
Deferred tax at 35%	(1,051)	(919)
Net pension asset	1,953	1,707

Following a review of the pension scheme and in accordance with IFRIC 14, the pension surplus is deemed recoverable and the gross pension debtor has been recognised in the 2021 accounts together with deferred tax of 35%. Reconciliation of opening and closing balances of the present value of the scheme liabilities.

	2021 £000	2020 £000
Scheme liabilities at start of year - GDUK	25,106	21,870
Scheme liabilities at start of year - GDIT	1,909	1,909
Interest cost	354	452
Actuarial gains	(2,056)	3,311
Benefits paid, death in service insurance premiums and expenses	(1,418)	(810)
Past service costs	-	125
Impact of Defined Benefits underpin member retirements	-	158
Defined benefit obligation at end of period	23,895	27,015

Notes (continued)

24 Pension scheme (continued)

Reconciliation of opening and closing balances of the fair value of scheme assets.

	2021 £000	2020 £000
Fair value of scheme assets at start of year - GDUK	27,654	25,661
Fair value of scheme assets at start of year - GDIT	1,934	1,934
Interest income	389	530
Actuarial gains/(Loss)	(1,538)	2,115
Benefits paid	(1,418)	(810)
Impact of Defined Benefits underpin member retirements	-	158
Administrative Expenses	(175)	-
Fair value of scheme assets at end of year	26,846	29,588

Movement in the surplus during the year

	2021 £000	2020 £000
Surplus in the Scheme at 1 January - GDUK	2,601	3,844
Surplus in the Scheme at 1 January - GDIT	25	25
Other finance expense	35	78
Administrative expenses from plan assets	(175)	-
Past Service Cost	-	(125)
Actuarial (losses)/Gain	518	(1,196)
Surplus in the Scheme at 31 December	3,004	2,626

Analysis of amounts included in income statement:

	2021 £000	2020 £000
Past service cost	-	(125)
Interest income	389	530
Interest on pension scheme liabilities	(354)	(452)
Administrative Expenses	(175)	-
	(140)	(47)

Notes (continued)

24 Pension scheme (continued)

Analysis of amount recognised in Other Comprehensive Income:

	2021 £000	2020 £000
Return on plan assets (excluding amounts included in net interest cost)	(1,538)	2,115
Experience gains arising on Scheme liabilities	1,145	682
Changes in assumptions underlying the present value of Scheme liabilities	911	(3,993)
	<u>518</u>	<u>(1,196)</u>

The fair value of plan assets and return on those assets were as follows:

	2021 £000	2020 £000
Gilts	2,305	2,294
Cash	1,130	821
Insured assets	23,411	26,473
	<u>26,846</u>	<u>29,588</u>
Total	<u>26,846</u>	<u>29,588</u>
Actual return on plan assets (loss) / gain	<u>(1,538)</u>	<u>2,115</u>

The expected contribution to be paid to the scheme in the next financial year is nil (2021: nil).

The total amount recognised in the other comprehensive income in respect of actuarial gains and losses is a gain of £0.5m (2020: £1.2m loss).

Notes (continued)

25 Related party disclosures

The Company is controlled by its immediate parent undertaking General Dynamics Ltd. The ultimate controlling party is General Dynamics Corporation (See note 28). The table below summarises the intercompany transactions arising during the year ended 31 December 2021.

Year ended 31 December 2022				
Purchase/Sale	Contracting party	Country	Type of Transaction	Value (£)
Sale	GD Mission Systems Canada	Canada	Inventory	44,360
Sale	GD Mission Systems Italy	Italy	Service	377,484
Sale	GDIT Inc.	USA	Service	343,605
Sale	GD MS Inc.	USA	Service	220,046
Sale	GD Land Systems Canada	Canada	Service	176,378
Sale	GPS	USA	Service	107,589
Sale	GD Global Holdings Limited	UK	Service	289,317
Sale	GD Swiss Financial Management Limited	UK	Service	3,775
Sale	GD Missions Systems International Limited	UK	Service	35,075
Sale	GD Land Systems	USA	Service	13,850
Sale	GD European Finance Limited	UK	Service	88,335
Sale	GD Mission Systems Canada	Canada	Service	1,260,437
Purchase	SBS	Spain	Inventory	188,748,464
Purchase	GD Mission Systems Canada	Canada	Inventory	51,744
Purchase	GD Mission Systems Italy	Italy	Service	172,833
Purchase	GD Land Systems	USA	Service	3,780,400
Purchase	General Dynamics Land Systems - Canadian Services Limited	Canada	Service	198,573
Purchase	GD Land Systems Canada	Canada	Service	5,644,118
Purchase	GD Global Holdings Limited	UK	Service	461,001
Purchase	GD European Finance Limited	UK	Service	61,727
Purchase	CHQ	USA	Service	669,803
Purchase	GD Mission Systems Canada	Canada	Service	4,453,514
Purchase	GD Mission Systems	USA	Service	3,473,776
Loan Interest Receivable	GD European Finance Limited	UK	Loan Interest Receivable	3,494
Loan Interest Payable	GD European Finance Limited	UK	Loan Interest Payable	1,525,042

Notes (continued)

26 Employee benefits

Share based payments

The Save As You Earn (SAYE) scheme is offered to all employees of General Dynamics United Kingdom Ltd (GDUK) once a year and employees have the option of entering either a 3 year or 5 year scheme.

There was no 2021 SAYE award granted by the parent.

The terms and conditions of grants are as follows:

Grant date/ Employees entitled/ nature of scheme	Number of instruments	Vesting conditions	Contractual life of options
2016 Cash-settled 5 year SAYE award to employees. Granted by parent on 30/11/16.	GDUK 2,710	5 years from start of contract	2022
2017 Cash-settled 3 year SAYE award to employees. Granted by parent on 30/11/17.	GDUK 15,278	3 years from start of contract	2021
2017 Cash-settled 5 year SAYE award to employees. Granted by parent on 30/11/17.	GDUK 2,801	5 years from start of contract	2023
2018 Cash-settled 3 year SAYE award to employees. Granted by parent on 27/11/18.	GDUK 22,285	3 years from start of contract	2022
2018 Cash-settled 5 year SAYE award to employees. Granted by parent on 27/11/18.	GDUK 4,227	5 years from start of contract	2024
2019 Cash-settled 3 year SAYE award to employees. Granted by parent on 29/11/19.	GDUK 18,980	3 years from start of contract	2023
2019 Cash-settled 5 year SAYE award to employees. Granted by parent on 29/11/19.	GDUK 1,960	5 years from start of contract	2025
2020 Cash-settled 3 year SAYE award to employees. Granted by parent on 30/11/20.	GDUK 44,388	3 years from start of contract	2024
2020 Cash-settled 5 year SAYE award to employees. Granted by parent on 30/11/20.	GDUK 9,052	5 years from start of contract	2026

The number and weighted average exercise prices of SAYE share options are as follows:

	2021 Weighted Average option price £	2021 Number of options	2020 Weighted Average option price £	2020 Number of options
Outstanding at the beginning of the year	102.16	98,390	115.08	77,250
Forfeited during the year	111.06	(19,340)	117.85	(19,166)
Exercised during the year	108.02	(5,044)	102.53	(15,032)
Granted during the year	82.40	15	89.66	55,338
Lapsed during the year	-	-	-	-
Outstanding at the end of the year	99.43	74,021	102.16	98,390
Exercisable at the end of the year	97.99	188	125.46	420

Notes (continued)

26 Employee benefits (continued)

Share based payments (continued)

The weighted average share price at the date of exercise of share options exercised during the period was £130.04 (2020: £135.97).

The options outstanding at the year-end have an exercise price in the range of £89.33 to £127.66 and a weighted average remaining contractual life of 2.13 years.

The fair value of services received in return for share options granted are measured by reference to the fair value of share options granted. The estimate of the fair value of the services received is measured based on a Black Scholes model. Measurement inputs and assumptions are as follows:

	SAYE 3 year		SAYE 5 year	
	2021	2020	2021	2020
Fair value at grant date	-	29.7303	-	28.7041
Weighted average share price	-	89.3258	-	89.3258
Exercise price	-	89.3258	-	89.3258
Expected volatility (expressed as % used in the modelling under Black Scholes model)	-	30.788%	-	26.498%
Option life (expressed as weighted average life used in the modelling under Black Scholes model)	-	39 months	-	63 months
Expected dividends	-	2.4%	-	2.4%
Risk-free interest rate (based on national government bonds)	-	0.235%	-	0.410%

The total expenses recognised for the year arising from share based payments are as follows:

	2021	2020
	£000	£000
Equity settled share based payments (Restricted Stock and EC options for which the Company has applied the exemption)	148	51
Cash settled share based payments (SAYE)	680	(214)
Total carrying amount of liabilities (SAYE)	2,096	90

Notes (continued)

27 Financial Instruments

Fair value of financial instruments

At 31 December, the Company held the following instruments to hedge exposures to changes in foreign currency.

	0-6 months £000	6-12 months £000	>12 months £000	Total £000
<i>Foreign currency risk</i>				
<i>Forward exchange contracts</i>				
Net exposure	142,162	34,785	2,589	179,536
Average GBP-USD forward contract rate	1.3264	-	-	
Average GBP-EUR forward contract rate	0.8621	0.8672	-	
Average GBP-CAD forward contract rate	1.7505	1.7584	1.7641	

With the exception of the trade debtor greater than one year, where it is not considered that the carrying value and book value are materially different, the carrying value of the following current financial instruments approximates fair value because of the short period to maturity:

- Cash and cash equivalents
- Trade receivables
- Prepayments & other debtors
- Trade payables
- Accruals and deferred income

The fair value measurement of some derivatives requires assumptions and management's assessment of certain market parameters. Where a market price is not available, a valuation model which takes into consideration discounted cash flows is used with consideration for the special characteristics of the underlying asset. The fair value of foreign currency forward contracts is estimated by discounting the difference between the contractual forward price and the current forward price for the residual maturity in the contract using a risk-free interest rate.

Carrying amount and fair value of each class of financial assets and liabilities are presented in the table below:

As at 31 December 2021	Financial assets measured at fair value through Other Comprehensive Income (£000)	Financial assets measured at amortised cost (£000)	Financial assets measured at fair value through profit or loss (£000)	Financial liabilities measured at amortised cost (£000)	Total carrying amount (£000)	Fair value (£000)
Trade debtors within 1 year ¹	-	1,025,425	-	-	1,025,425	1,025,425
Prepayments and other debtors	-	40,459	-	-	40,459	40,459
Gross derivative financial assets	1,621	-	103	-	1,724	1,724
Trade debtor greater than 1 year	-	16,178	-	-	16,178	16,178
Total assets	1,621	1,082,062	103	-	1,083,786	1,083,786
Cash pooling ²		436,842			436,842	436,842
Trade creditors ³	-	-	-	261,968	261,968	261,968
Cash	-	-	-	-	127	127
Gross derivative financial liabilities	5,579	-	23	-	5,602	5,602
Accruals & deferred income	-	-	-	22,309	22,309	22,309
Total liabilities	5,579	436,842	23	284,277	726,848	726,848

¹ Trade debtors includes amounts recoverable on contracts and intercompany receivables.

² Cash pooling represents amounts owed to a related party under the cash pooling arrangements.

³ Trade creditors includes amounts owing to a related party, loan and payments on account on long term contracts.

Notes (continued)

28 Ultimate parent company

The Company is a 100% owned subsidiary undertaking of General Dynamics Limited, a company incorporated in Great Britain. General Dynamics Corporation is the ultimate parent company incorporated in the USA.

The largest and smallest group in which the results of the Company are consolidated is that headed by General Dynamics Corporation, incorporated in the USA. The consolidated accounts of the group are available to the public and may be obtained from 11011 Sunset Hills Road, Reston, VA 20190.

29 Accounting Estimates and Judgements

The preparation of the consolidated financial statements in conformity with FRS101 requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. The reported amounts and note disclosures reflect management's best estimate of the most probable set of economic conditions and planned course of actions. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

Significant areas of estimation uncertainty and critical judgments in applying accounting policies that have the most significant effect on the amounts recognised in these consolidated financial statements include:

Provisions for liabilities and charges

The Company has made a legal claim in connection with a debt owed by the State of Libya. The Company was successful in being awarded a default judgement and substantial work is being undertaken to recover the £16m debt. Management has made judgements as to the likelihood of recovery of the debt owed and, as a result, the full debtor is recognised within debtors greater than one year. The time for concluding the legal claim and recovery of money owed is uncertain. Despite the debt being deemed recoverable in more than 1 year, management do not consider the carrying value and book value to be materially different and have not discounted the expected future cash flow.

Revenue IFRS 15

Long Term Contracts

The majority of the Company's projects are long-term development or support contracts spanning multiple financial years. Revenue on long-term contracts is recognised over time as work progresses using costs incurred to date relative to total estimated costs at completion to measure progress towards satisfying performance obligations. Incurred cost represents work performed which corresponds with and thereby best depicts the transfer of control to the customer. Contract costs include labour, material, subcontractor costs and G&A expenses. The revenue recognised by the Company at a point in time relates to the Bowman equipment contract. Revenue on this contracts is recognised when the customer obtains control of the asset, which is upon delivery and acceptance of the equipment.

The Company estimates the profit on a contract as the difference between the total estimated revenue and expected costs to complete a contract and recognise that profit over the life of the contract. Contract estimates are based on various assumptions to project the outcome of future events that often span several years. These assumptions include labour productivity and availability, the complexity of the work to be performed, the cost and availability of materials, the performance of subcontractors and the availability and timing of funding from the customer.

Notes (continued)

29 Accounting Estimates and Judgements (continued)

Revenue IFRS 15 (continued)

As a significant change in one or more of these assumptions could affect the profitability of contracts, the Company reviews and updates its contract-related estimates regularly. The Company recognises adjustments in estimated profit on contracts under the cumulative catch-up method. Under this method, the impact of the adjustment on profit recorded to date on a contract is recognised in the period the adjustment is identified. Revenue and profit in future periods of contract performance are recognised using the adjusted estimate. If at any time the estimate of contract profitability indicates an anticipated loss on the contract, the Company recognises the total loss in the period it is identified.

The majority of revenue is derived from long-term contracts and programmes that can span several years. Revenue is accounted for in accordance with IFRS15.

Performance Obligations

An assessment is conducted on contract inception to identify the number of performance obligations pertaining to the contract award using the 5-step methodology defined in IFRS15. A number of contracts have multiple performance obligations, most commonly due to the contract covering multiple phases of the product lifecycle (development, production, maintenance and support). For contracts with multiple performance obligations, the contract's transaction price is allocated to each performance obligation using the best estimate of the standalone-selling price of each distinct good or service in the contract. The primary method used to estimate standalone selling price is the expected cost plus a margin approach for that distinct goods or service performance obligation. The transaction price is allocated to each distinct performance obligation and recognised as revenue as, the performance obligation is satisfied.

The nature of the Company's contracts gives rise to some types of variable consideration, including positive incentive adjustments and final contract pricing adjustments. Positive incentive adjustments are included within the estimated transaction price when there is a basis to reasonably estimate the amount of the recovery and there is no significant risk of reversal. These estimates are based on experience, anticipated performance and best judgment at the time of reviewing the contract financials. Variable considerations are re-assessed on significant contracts at least every six months.

Performance obligations are satisfied over time as work progresses or at a point in time. Revenue from products and services transferred to customers over time accounted for 96.6% of revenue in 2021 (2020: 96.5%). Substantially all of the revenue is recognised over time, because control is transferred continuously to customers. The majority of revenue recognised at a point in time is for sales of specialised product. Revenue on these contracts is recognised when the customer receives the product and a billing is raised.

Warranty obligations are accounted for within the contract estimates at completion and the basis of assumptions reviewed quarterly. As programme costs are incurred, an accrual is made based upon the assumptions within the estimate at completion and held on the balance sheet until warranty returns are received.

At 31st December 2021, the Company had £1.1Bn of remaining performance obligations, which is also referred to as total backlog, the majority of which relates to the AJAX contract. At 31st December 2021, the Company expects to recognise approximately 44.5% of the remaining performance obligations as revenue in 2022, a further 30.6% by the end of 2023 and the balance thereafter.

The impact of adjustments in contract estimates on operating earnings can be reflected in either operating costs and expenses or revenue. The aggregate impact of adjustments in contract estimates decreased revenue and operating profit as follows (£m):

Year Ended December 31	2021	2020
Revenue	(41)	(8)
Operating Profit	(41)	(8)

Notes (continued)

29 Accounting Estimates and Judgements (continued)

Revenue IFRS 15 (continued)

Revenue by Category

The portfolio of products and services consists of 354 active profit centres compared to 267 at the end of 2020. The following series of tables presents revenue disaggregated by several categories.

Revenue by major products and services was as follows (£m):

Year Ended December 31	2021	2020
C4	70	165
Avionics	31	28
LS	503	542
Total	<u>604</u>	<u>735</u>

Revenue by contract type was as follows (£m):

Year Ended December 31, 2021	C4	Avionics	LS	Total Revenue
Firm Fixed-Price	70	31	503	604
<i>Firm Fixed Price 2020</i>	<i>165</i>	<i>28</i>	<i>542</i>	<i>735</i>
Time and Materials	0	0	0	0
<i>Time and Materials 2020</i>	<i>0</i>	<i>0</i>	<i>0</i>	<i>0</i>
Other	0	0	0	0
Total revenue	70	31	503	604
<i>Total revenue 2020</i>	<i>165</i>	<i>28</i>	<i>542</i>	<i>735</i>

Each of these contract types presents advantages and disadvantages. Typically, more risk is assumed with fixed-price contracts. However, these types of contracts offer additional profits when work is completed for less than originally estimated. Time and Material contracts generally are lower risk. Accordingly, the associated base fees are usually lower than fees earned on fixed-price contracts.

Revenue by customer was as follows (£m):

	C4/ Avionics	LS	Total Revenue
UK Government	68	493	561
Non-UK Government	33	10	43
Total revenue	101	503	604

Notes (continued)

29 Accounting Estimates and Judgements (continued)

Revenue IFRS 15 (continued)

Contract Modifications

Contract modifications are routine in the performance of contracts. Contracts are often modified to account for changes in contract specifications or requirements. In most instances, contract modifications are for goods or services that are not distinct and therefore, are accounted for as part of the existing contract on a cumulative catch up basis. An assessment is conducted for every contract modification to determine if the amendment results in a separate performance obligation or if the modification results in the combining of performance obligations.

During the year, the Company signed a Heads of Terms Agreement with UK MoD on its MORPHEUS contract. The purpose of the Heads of Terms was to capture the terms of contract discussions which governed the approach to the documentation of a proposed Formal Agreement for the MORPHEUS Contract. Under IFRS15, the Heads of Terms agreement was deemed a modification to the existing contract.

The revenue traded in 2021 is primarily related to contracts that were awarded pre 1 January 2021. £584m of the revenue recognised in the current period relates to performance obligations, which have been fully or partially satisfied in previous periods.

Contract Balances

Contract Assets

The timing of revenue recognition, billings and cash collections results in billed accounts receivable, unbilled receivables (Debtors Less than 1 year), and customer advances and deposits (Creditors less than 1 year) on the Balance Sheet. Amounts are billed as work progresses in accordance with agreed-upon contractual terms, either at periodic intervals or upon achievement of contractual milestones. Generally, billing occurs subsequent to revenue recognition, resulting in contract assets. At 31 December 2021 the Company held £1Bn of contract assets compared to £495m in 2020. The contracts contributing to this contract asset value are AJAX and MORPHEUS.

Contract Liabilities

Sometimes advances or deposits from customers can be received before revenue is recognised, resulting in contract liabilities. These liabilities are reported on the Balance Sheet at the end of each reporting period. At 31 December 2020, the Company held £30.4m of contract liabilities. During 2021, £11.9m of this was traded as revenue, primarily related to the Bowman & Typhoon contracts. At the close of 2021, the Company held £26.8m of contract liabilities primarily relating to the Typhoon, NIMCIS and Bowman programmes.