

# **BAE Systems Applied Intelligence (International) Limited**

## **Annual Report and Financial Statements**

**31 December 2017**

Registered Number: 06815164



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## Strategic Report

### Review of business

#### Overview

Sales for the year amounted to £23,321k (2016: £10,809k) and the profit for the year before taxation amounted to £1,309k (2016: £574k).

The directors do not propose a dividend in respect of the year ended 31 December 2017 (2016: £nil).

The directors consider the results in the year to be encouraging and represents Applied Intelligence's increased investment in international markets. The Directors consider that the outlook for the Company is positive and expect the Company to perform well in the coming year.

#### Strategy Overview

BAE Systems Applied Intelligence business group ('Applied Intelligence'), of which this Company is part, exists to protect and enhance the connected world. It provides technology-based solutions which enable government and commercial customers to find and stop threats, manage risks and regulations and operate securely. Applied Intelligence's goal is to be a market leader in the financial crime, cyber security and national security domains. The strategy comprises five elements:

- Extend the strong position in national security in the UK and allied countries;
- Build on the strong position in financial services based on financial crime solutions;
- Pursue the significant, attractive market for cyber security operations and advisory services in commercial and government customers;
- Value people, enabling them to develop their capabilities and excel at their jobs; and
- Create a financially healthy and sustainable business.

#### Business Risks and Uncertainties

The significant high level risks identified by the Board have not changed substantially over the last 12 months and are as follows:

##### *Global economic climate*

As with all technology businesses, Applied Intelligence is exposed to any downturn in technology spending that may result from instability in the global economy caused, for example, by rising commodity prices, acts of terrorism or significant pressure on selected government spending programmes.

We believe that the diversified markets covered by the business and, in particular, Applied Intelligence's focus on the counter threat agenda and intellectual property led solutions to provide clients with greater value for money, provide some mitigation against this risk. In addition, staff base flexibility is maintained in order that resources can be moved to those sectors where demand is greatest.

##### *Recruitment market*

The current market sees a strong demand for the best people. This has been particularly the case for people with advanced technical skills and those with UK government clearances. The risk of a competitive recruitment market is addressed through a portfolio of measures, including a strengthened HR recruitment team, attractive staff reward schemes such as flexible benefits, and through new career development programmes.

##### *Pricing pressure*

Low-cost providers in off-shore locations continue to exert pressure on pricing in some sectors of the organisations markets. Applied Intelligence operate a UK delivery centre in Leeds, a similar centre in Poland and a larger global delivery centre in Malaysia to provide more efficient and cost-effective offerings to its clients. Some of Applied Intelligence's work is unsuitable for off-shore resourcing for security reasons, which is a constraint the organisation has sought to address by investing in secure facilities in our UK locations.

##### *Delivery risk*

Applied Intelligence has, over many years, built a track record of very strong project management and technical delivery of the most complex and business-critical programmes. Any failure to meet client expectations and/or Applied Intelligence's contractual obligations could damage Applied Intelligence's reputation in the marketplace. This risk is managed through rigorous bid approval controls, peer review of technical solutions and project plans and regular monitoring of high risk projects by project boards.

## Strategic Report *(continued)*

### Security

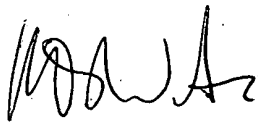
Much of Applied Intelligence's work relies on its reputation for strong security, in particular that for the national security community, where the Company is subject to particular rules applied by national governments. Security breaches could materially damage Applied Intelligence's business. Security matters are therefore carefully managed and are overseen by a director-level security committee, which ensures that the business systematically embeds rigorous security practice in its everyday operations. Applied Intelligence is investing to ensure its own security keeps pace with the evolving threat environment.

Each of the identified risks is regularly reviewed and actively managed by the Board.

### Key Performance Indicators

The directors consider revenue and operating profit/loss as the principal key performance indicators to assess progress towards achieving the Company's strategy. This information for the current and prior periods is set out in the Company's income statement on page 9.

### On behalf of the Board



M S Watson

Director

15 June 2018

## Directors' Report

### Company registration

BAE Systems Applied Intelligence (International) Limited (the 'Company') is a private company, limited by shares and registered in England and Wales with the registered number 06815164.

### Going concern

The Company has traded profitably in the year and the Directors believe that the company is well placed to manage its business risks. The Directors have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future. Thus they continue to adopt the going concern basis of accounting in preparing the annual financial statements.

### Indemnity insurance

The directors of the Company have been indemnified against liability in respect of proceedings brought by third parties, subject to the conditions set out in the Companies Act 2006. Such qualifying third party indemnity provision was in force during the period and continues to be in force as at the date of this Report. Directors and Officers' liability insurance has been purchased in order to minimise the potential impact of such proceedings.

### Financial instruments

The global nature of the Company's business means it is exposed to volatility in currency exchange rates. In order to protect itself against currency fluctuations, the Company's policy is to hedge all material firm transactional exposures.

### Overseas branch office

The Company has overseas branch offices in Singapore, Qatar and Jordan.

### Employees

Engaging and developing the workforce for current and future business is key to delivering our strategy successfully. We are, therefore, committed to attracting, selecting, developing and retaining the best people to deliver this.

We are committed to creating an inclusive work environment where a diverse range of talented people can work together to ensure business delivery. Diversity amongst our workforce is a significant force for innovation.

We focus on our goal of building a diverse workforce which reflects that of the populations we recruit from. A particular current focus is increasing female representation in the pipeline for senior roles.

Engaging our employees to help them make the fullest contribution to the business is important. Through a variety of media, we seek to listen to employees' views and opinions, and keep them informed about developments and prospects for the business. Regular internal communication, including e-enabled channels, leadership blogs, newsletters, management and team meetings, monthly team briefs and the intranet, keeps employees informed, involved and engaged.

The Company welcomes employees becoming shareholders in BAE Systems plc and offers a number of employee share plans to support this.

The Company is committed to giving full and fair consideration to applications for employment from disabled people who meet the requirements for the Company's roles, and making available training opportunities and appropriate accommodation to disabled people employed by the Company.

## **Directors' Report** *(continued)*

### **Directors and their interests**

The directors who served during the year and at the date of this Report were as follows:

A G Lazarus                      Resigned 22 May 2017

A D Leggetter

M S Watson                      Appointed 22 May 2017

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

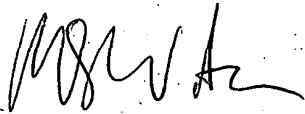
### **Disclosure of information to auditor**

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

### **Auditor**

Following an audit retender which concluded in 2017, Deloitte LLP was selected as auditor for the BAE Systems Group. Accordingly, it is intended that Deloitte LLP will be appointed to replace KPMG LLP as auditor for the year ending 31 December 2018.

### **On behalf of the Board**



M S Watson

Director

15 June 2018

Registered office:  
BAE Systems Applied Intelligence (International) Limited  
Priestley Road  
Surrey Research Park  
Guildford  
Surrey  
GU2 7YP  
England  
United Kingdom

## **Statement of Directors' Responsibilities in respect of the Strategic Report, Directors' Report and the Financial Statements**

The directors are responsible for preparing the Strategic Report, the Directors' 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;
- 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 BAE Systems Applied Intelligence (International) Limited**

### **Opinion**

We have audited the financial statements of BAE Systems Applied Intelligence (International) Limited for the year ended 31 December 2017 which comprise the Income Statement, Statement of Comprehensive Income, Balance Sheet, Statement of Changes in Equity and related notes, including the accounting policies in note 1.

In our opinion the financial statements:

- give a true and fair view of the state of the Company's affairs as at 31 December 2017 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**

We are required to report to you if we have concluded that the use of the going concern basis of accounting is inappropriate or there is an undisclosed material uncertainty that may cast significant doubt over the use of that basis for a period of at least twelve months from the date of approval of the financial statements. We have nothing to report in these respects.

### **Strategic Report and Directors' Report**

The directors are responsible for the Strategic Report and Directors' Report. Our opinion on the financial statements does not cover that Report and we do not express an audit opinion thereon.

Our responsibility is to read the Strategic Report and 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 6, 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.



## **Independent Auditor's Report to the Members of BAE Systems Applied Intelligence (International) Limited (continued)**

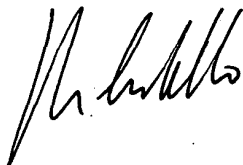
### **Auditor's responsibilities**

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](http://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.



John Costello (Senior Statutory Auditor)  
for and on behalf of KPMG LLP, Statutory Auditor  
Chartered Accountants

15 June 2018

KPMG LLP  
15 Canada Square  
E14 5GL

## Income Statement

for the year ended 31 December 2017

	Notes	2017 £'000	2016 £'000
Revenue		23,321	10,809
Operating costs	2	(21,980)	(10,235)
<b>Operating profit and profit before finance costs and taxation</b>		<b>1,341</b>	<b>574</b>
Finance income		-	18
Finance expenditure		(32)	(18)
<b>Profit before tax</b>		<b>1,309</b>	<b>574</b>
Tax income /(expense)	4	(7)	(23)
<b>Profit for the year</b>		<b>1,302</b>	<b>551</b>

## Statement of Comprehensive Income

for the year ended 31 December 2017

	2017 £'000	2016 £'000
<b>Profit for the year</b>	<b>1,302</b>	<b>551</b>
<b>Other comprehensive income</b>		
<b>Items that may be reclassified to the income statement:</b>		
Amounts credited to hedging reserve	176	-
Exchange differences on retranslation of foreign branches	(14)	97
<b>Total comprehensive income for the year</b>	<b>1,464</b>	<b>648</b>

The notes on pages 12 to 21 form part of the financial statements.

The results for 2017 and 2016 arise from continuing activities.

**Balance sheet**  
as at 31 December 2017

	Notes	2017 £'000	2016 £'000
<b>Non-current assets</b>			
Property, plant and equipment	6	460	617
Investments	7	1	1
		<b>461</b>	<b>618</b>
<b>Current assets</b>			
Inventories	8	-	49
Trade and other receivables	9	21,414	11,416
Other financial assets	12	188	-
Cash and cash equivalents		1,056	2,819
		<b>22,658</b>	<b>14,284</b>
<b>Total assets</b>		<b>23,119</b>	<b>14,902</b>
<b>Current liabilities</b>			
Trade and other payables	10	(13,738)	(14,200)
Other financial liabilities	12	(12)	-
Current tax		(14)	(15)
Provisions	11	(7,204)	-
<b>Total liabilities</b>		<b>(20,968)</b>	<b>(14,215)</b>
<b>Net assets</b>		<b>2,151</b>	<b>687</b>
<b>Capital and reserves</b>			
Issued share capital	13	-	-
Other reserves	13	176	-
Foreign translation reserve		(4)	10
Retained (deficit)/earnings		1,979	677
<b>Total (deficit)/equity</b>		<b>2,151</b>	<b>687</b>

The notes on pages 12 to 21 form part of the financial statements.

Approved by the Board on 15 June 2018 and signed on its behalf by:



M S Watson  
Director

Registered number: 06815164

**Statement of Changes in Equity**  
for the year ended 31 December 2017

	Issued share capital	Other reserves	Foreign translation reserve	Retained earnings	Total equity
	£'000	£'000	£'000	£'000	£'000
At 1 January 2016	-	-	2	2,237	2,239
Profit for the year	-	-	-	551	551
Retranslation of net assets of foreign branches	-	-	8	89	97
Dividend paid	-	-	-	(2,200)	(2,200)
At 31 December 2016	-	-	10	677	687
Profit for the year	-	-	-	1,302	1,302
Total other comprehensive income for the year	-	176	-	-	176
Retranslation of net assets of foreign branches	-	-	(14)	-	(14)
At 31 December 2017	-	176	(4)	1,979	2,151

The notes on pages 12 to 21 form part of the financial statements.

## Notes to the Financial Statements

### 1 Accounting policies

#### Basis of preparation

These financial statements were prepared in accordance with FRS 101 Reduced Disclosure Framework issued in September 2015. The amendments to FRS 101 (2015/16 cycle) issued in July 2016 and FRS 101 (2016/17 cycle) issued in July 2017 have no impact on the Company.

In preparing these financial statements, the Company applies the recognition, measurement and disclosure requirements of *International Financial Reporting Standards (IFRS)*, as adopted by the EU (EU-adopted IFRS), but makes amendments where necessary in order to comply with the Companies Act 2006 and has set out below where advantage of the FRS 101 disclosure exemptions has been taken:

- the requirements of paragraphs 45(b) and 46 to 52 of IFRS 2, Share-based Payment;
- the requirements of IFRS 7, Financial Instruments: Disclosures;
- the requirements of paragraphs 91 to 99 of IFRS 13, Fair Value Measurement;
- the requirement in paragraph 38 of IAS 1, Presentation of Financial Statements, to present comparative information in respect of: paragraph 79(a)(iv) of IAS 1; paragraph 73(e) of IAS 16, Property, Plant and Equipment; paragraph 118(e) of IAS 38, Intangible Assets; and paragraphs 76 and 79(d) of IAS 40, Investment Property;
- the requirements of paragraphs 10(d), 10(f), 16, 38A, 38B, 38C, 38D, 40A, 40B, 40C, 40D, 111 and 134 to 136 of IAS 1, Presentation of Financial Statements;
- the requirements of IAS 7, Statement of Cash Flows;
- the requirements of paragraphs 30 and 31 of IAS 8, Accounting Policies, Changes in Accounting Estimates and Errors;
- the requirements of paragraphs 17 and 18A of IAS 24, Related Party Disclosures;
- the requirements in IAS 24, Related Party Disclosures, to disclose related party transactions entered into between two or more members of a group, provided that any subsidiary which is a party to the transaction is wholly owned by such a member; and
- the requirements of paragraphs 130(f)(ii), 130(f)(iii), 134(d) to 134(f) and 135(c) to 135(e) of IAS 36, Impairment of Assets.

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

The following paragraphs summarise the main accounting policies of the Company and have, unless otherwise stated, been applied consistently to all periods presented in these financial statements.

The financial statements have been prepared under the historical cost convention, as modified by the revaluation of relevant financial assets and financial liabilities (including derivative instruments). The going concern basis has been applied in these accounts.

#### Future changes in accounting policies

IFRS 9, Financial Instruments, is effective from 1 January 2018. The standard covers recognition, classification, measurement and impairment of financial assets and financial liabilities, together with a new hedge accounting model.

IFRS 15, Revenue from Contracts with Customers, is effective from 1 January 2018. The standard requires the identification of performance obligations in contracts with customers and allocation of the total contractual value to each of the performance obligations identified. Revenue is recognised as each performance obligation is satisfied either at a point in time or over time. The standard will replace IAS 11, Construction Contracts, and IAS 18, Revenue.

#### Revenue and profit recognition

Revenue derived from professional fees billed to clients on a time and materials or fixed-price basis represents the value of work completed, including attributable profit, based on the stage of completion achieved on each project. For time and materials projects, revenue is recognised as services are performed. For fixed-price projects, revenue is recognised on completion of milestones as set out in our terms of engagement.

In accordance with paragraph 8 of IAS 18 Revenue, to the extent that the Company acts as principal in the transaction, revenue from recharging to clients the cost of specialist managed subcontractors, the purchase of software or hardware for client assignments and staff expenses incurred in the performance of client assignments, together with associated mark-up (if applicable), is recognised as these costs are incurred. Where the Company acts as agent in the transaction, only the commission is recognised as Company revenue.

## Notes to the Financial Statements (continued)

### 1 Accounting policies (continued)

Income is accrued where these revenue recognition policies result in the recognition of revenue before invoices are sent to clients.

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

#### Lease costs

Payments, including any incentives, made under operating leases are recognised in the income statement on a straight-line basis over the lease term.

#### Interest income

Interest income is recognised in the income statement in the period in which it is incurred.

#### Dividends

Dividends received and receivable are credited to the Company's income statement. Equity dividends paid on ordinary share capital are recognised as a liability in the period in which they are declared.

#### Foreign currencies

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

The assets and liabilities of foreign currency branches are translated at the exchange rates ruling at the balance sheet date. The income statements of these branches are translated at average rates of exchange during the year. All resulting exchange differences are recognised in the foreign translation reserve.

#### Property, plant and equipment

##### Cost

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

##### Depreciation

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

Leasehold improvements	- 10 years, or the lease term if shorter
Computers and ancillary equipment	- 20-33%
Office equipment	- 10%

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

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

##### Impairment

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

#### Investments

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

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

An impairment loss is recognised whenever the carrying amount of an asset exceeds its recoverable amount.

Impairment losses are recognised in the income statement.

## Notes to the Financial Statements *(continued)*

### 1 Accounting policies *(continued)*

#### Investments *(continued)*

An impairment loss is only reversed if the subsequent increase in recoverable amount can be related objectively to an event occurring after the impairment loss was recognised or if there has been a change in the estimate used to determine the recoverable amount.

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

#### Inventories

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

#### Trade and other receivables

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

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

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

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

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

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

#### Cash and cash equivalents

Cash and cash equivalents includes cash in hand, call and term deposits, and other short-term liquid investments with original maturities of three months or less and which are subject to an insignificant risk of change in value.

#### Trade and other payables

Trade and other payables are stated at their cost.

#### Financial instruments

##### *Derivative financial instruments and hedging activities*

The global nature of the Company's business means it is exposed to volatility in currency exchange rates. In order to protect itself against currency fluctuations, the Company's policy is to hedge all material firm transactional exposures. The Company aims to achieve hedge accounting treatment for all derivatives that hedge material foreign currency exposures.

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

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

## Notes to the Financial Statements (*continued*)

### 1 Accounting policies (*continued*)

#### Financial instruments (*continued*)

##### *Cash flow hedges*

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

##### *Fair value hedges*

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

#### **Tax**

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

##### *Current tax*

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

##### *Deferred tax*

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

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

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

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

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

#### **Retirement benefit obligations**

##### *Defined contribution pension schemes*

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

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



## Notes to the Financial Statements (continued)

### 2 Operating costs

Included within operating costs are the following expenses:

	2017 £'000	2016 £'000
Staff costs (note 3)	5,611	5,448
Depreciation, amortisation and impairment	153	111
Foreign exchange (gain)/loss	279	(563)
Intercompany operating expense <sup>1</sup>	(9,266)	631
Lease and sublease expense	530	686

<sup>1</sup> Relates to certain operating arrangements with fellow wholly owned subsidiaries.

The remuneration of the auditor for the year ended 31 December 2017 for statutory audit work was £53k (2016: £45k) and £nil (2016: £nil) in respect of non-audit work.

### 3 Employees

The average number of Company employees was as follows:

	2017	2016
	54	51

The aggregate staff costs of Company employees were as follows:

	2017 £'000	2016 £'000
Wages and salaries	5,431	5,109
Social security costs	17	134
Pension costs – defined contribution plans	163	205
	5,611	5,448

None of the directors received any emoluments from the Company during the year. All directors who served during the year were employed by other BAE Systems entities and were remunerated through those companies.

The directors did not provide any material qualifying services to the Company.

**Notes to the Financial Statements (continued)**

**4 Tax expense**

Tax expense	2017 £'000	2016 £'000
<b>Current tax</b>		
UK:		
Current tax	18	14
Double tax relief	(18)	(14)
Overseas:		
Current tax	18	22
Adjustments in respect of prior years	(11)	1
<b>Tax expense</b>	<b>(7)</b>	<b>23</b>

**Reconciliation of tax expense**

The following table reconciles the expected tax expense, using the UK corporation tax rate, to the reported tax expense.

	2017 £'000	2016 £'000
<b>Profit before tax</b>	<b>1,309</b>	<b>574</b>
UK corporation tax rate	19.25%	20%
Expected tax expense on profit	251	115
Expenses not tax effected	1	-
Property, plant and equipment	13	5
Provisions and accruals	(1)	222
Imputed interest income	(7)	(63)
Effect of tax rates in foreign jurisdictions	-	8
Losses (received from) group companies	(239)	(265)
Adjustment in respect of prior years	(11)	1
<b>Tax result</b>	<b>7</b>	<b>23</b>

**5 Deferred tax**

**Unrecognised deferred tax asset**

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

	2017 £'000	2016 £'000
Property, plant and equipment	37	29
Provisions and accruals	192	203
	<b>229</b>	<b>232</b>

The UK Corporation tax rate was reduced from 20% to 19% with effect from 1 April 2017, and will be reduced to 17% with effect from 1 April 2020. The rate applying to the unrecognised deferred tax asset is 17% (2016 – 18%).

Notes to the Financial Statements (continued)

6 Property, plant and equipment

	Leasehold improvements £'000	Computers and ancillary equipment £'000	Office equipment £'000	Total £'000
<b>Cost or valuation</b>				
At 1 January 2017	640	88	36	764
Additions	-	-	-	-
Transfers	-	-	-	-
Disposals	-	-	-	-
Foreign currency movement on translation of foreign branches	(8)	(1)	(1)	(10)
<b>At 31 December 2017</b>	<b>632</b>	<b>87</b>	<b>35</b>	<b>754</b>
<b>Depreciation and impairment</b>				
At 1 January 2017	93	47	7	147
Depreciation charge for the year	131	18	4	153
Disposals	-	-	-	-
Foreign currency movement on translation of foreign branches	(4)	(1)	(1)	(6)
<b>At 31 December 2017</b>	<b>220</b>	<b>64</b>	<b>10</b>	<b>294</b>
<b>Net book value</b>				
<b>At 31 December 2017</b>	<b>412</b>	<b>23</b>	<b>25</b>	<b>460</b>
At 31 December 2016	547	41	29	617

Operating lease commitments

The Company leases various offices under non-cancellable operating lease agreements. None of these agreements represent unusual arrangements or create material onerous or beneficial rights or obligations.

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

	2017 £'000	2016 £'000
<b>Payments due:</b>		
Not later than one year	520	554
Later than one year and not later than five years	1,023	1,469
	<b>1,543</b>	<b>2,023</b>

## Notes to the Financial Statements (continued)

### 7 Investments

Carrying value	£'000
At 1 January 2017 and at 31 December 2017	1

#### Subsidiary undertakings and participating interests at 31 December 2017

In accordance with Section 409 of the Companies Act 2006, a full list of subsidiary undertakings and significant holdings as at 31 December 2017 is disclosed below. Unless otherwise stated, all subsidiary undertakings and significant holdings are owned directly by BAE Systems Applied Intelligence (International) Limited and have a financial year end of 31 December.

Company name	Class of shares	Proportion of class (%)	Equity interest held (%)
BAE Systems Applied Intelligence (Japan) KK Ark Mori Building, 1-12-32 Akasaka, Minato-ku, Tokyo, 107-6024, Japan	Ordinary shares	100	100
BAE Systems Applied Intelligence (Malaysia) SDN BHD c/o RDL Corporate Services Sdn Bhd, 16th Floor, Wisma Sime Darby, Jalan Raja Laut, Kuala Lumpur, 50340, Malaysia	Ordinary shares	0.0001	0.0001

### 8 Inventories

	2017 £'000	2016 £'000
Short-term work in progress	-	49

### 9 Trade and other receivables

	2017 £'000	2016 £'000
<b>Current</b>		
Amounts due from customers for contract work	-	11
Trade receivables	7,887	8,244
Amounts owed by group subsidiaries	11,468	1,541
Other taxes and social security	21	2
Prepayments and accrued income	1,786	1,316
Other receivables	252	302
	<b>21,414</b>	<b>11,416</b>

### 10 Trade and other payables

	2017 £'000	2016 £'000
<b>Current</b>		
Trade payables	14	50
Amounts due to contract customers	4,009	747
Amounts owed to ultimate parent company	6,697	-
Amounts owed to group subsidiaries	261	11,039
Other taxes and social security costs	106	103
Accruals and deferred income	2,389	2,214
Other payables	262	47
	<b>13,738</b>	<b>14,200</b>

**Notes to the Financial Statements (continued)**

**11 Provisions**

	Reorganisation £'000	Contract loss £'000	Total £'000
At 1 January 2017	-	-	-
Created	4	7,200	7,204
<b>At 31 December 2017</b>	<b>4</b>	<b>7,200</b>	<b>7,204</b>
<b>Represented by:</b>			
Non-current	-	-	-
Current	4	7,200	7,204
	<b>4</b>	<b>7,200</b>	<b>7,204</b>

**Reorganisation**

It is anticipated that the reorganisation costs will be incurred within the next 12 months. There is limited volatility around the timing and amount of the ultimate outflows related to these provisions.

**Contract loss**

Although there are contract loss provisions, these are offset by the transfer pricing agreement with BAE Systems Applied Intelligence Limited. As such, this provision is ultimately passed to BAE Systems Applied Limited.

**12 Other financial assets**

	2017		2016	
	Assets £'000	Liabilities £'000	Assets £'000	Liabilities £'000
<b>Current</b>				
Cash flow hedges – foreign exchange contracts	188	(12)	-	-

**Cash flow hedges**

The net contractual cash flows on derivative financial instruments at the reporting date are £nil (2016: £nil).

**13 Share capital**

**Share capital**

	Ordinary shares £1	Nominal value £
<b>Issued and fully paid</b>		
At 1 January and 31 December 2017	2	2

**Equity dividends**

	2017 £'000	2016 £'000
Final dividend for ordinary shares paid in respect of the previous year	-	2,200

The directors do not propose a final dividend for the year ended 31 December 2017 (2016: £nil).

**Other reserves**

	Hedging reserve £'000	Total £'000
<b>At 1 January 2016</b>	-	-
Other comprehensive income	-	-
<b>At 31 December 2016</b>	-	-
Other comprehensive income	176	176
<b>At 31 December 2017</b>	<b>176</b>	<b>176</b>

**Notes to the Financial Statements** *(continued)*

**13 Share capital** *(continued)*

*Hedging reserve*

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

**14 Controlling parties**

The Company's immediate parent company is Detica Group Limited and the ultimate parent company is BAE Systems plc. Both companies are incorporated in Great Britain and registered in England and Wales. BAE Systems plc is the only parent company preparing group financial statements.

The consolidated Annual Report of BAE Systems plc is available to the public and may be obtained from:

6 Carlton Gardens  
London  
SW1Y 5AD

Website: [www.baesystems.com](http://www.baesystems.com)